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

Form 10-K

(Mark One)

☑ ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the fiscal year ended December 31, 2005

or

☐ TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the transition period from to

Commission file number 1-8787

American International Group, Inc.

(Exact name of registrant as specified in its charter)

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

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

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

Title of each class	Name of each exchange on which registered
Common Stock, Par Value $2.50 Per Share	New York Stock Exchange, Inc.

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

Title of each class
None

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

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

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

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

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of "accelerated filer and large accelerated filer" in Rule 12b-2 of the Exchange Act. (Check one):

Large Accelerated Filer ☑ Accelerated Filer ☐ Non-Accelerated Filer ☐

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes ☐ No ☑

The aggregate market value of the voting and nonvoting common equity held by nonaffiliates of the registrant computed by reference to the price at which the common equity was last sold as of June 30, 2005 (the last business day of the registrant's most recently completed second fiscal quarter), was approximately $127,330,500,000.

As of January 31, 2006, there were outstanding 2,596,987,248 shares of Common Stock, $2.50 par value per share, of the registrant.

Documents Incorporated by Reference:

The registrant's definitive proxy statement filed or to be filed with the Securities and Exchange Commission pursuant to Regulation 14A involving the election of Directors at the Annual Meeting of Shareholders of the registrant scheduled to be held on May 17, 2006 is incorporated by reference in Part III of this Form 10-K.

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Part I

ITEM 1.
Business

American International Group, Inc. (AIG), a Delaware corporation, is a holding company which, through its subsidiaries, is engaged in a broad range of insurance and insurance-related activities in the United States and abroad. AIG's primary activities include both General Insurance and Life Insurance & Retirement Services operations. Other significant activities include Financial Services and Asset Management. The principal General Insurance company subsidiaries are American Home Assurance Company (American Home), National Union Fire Insurance Company of Pittsburgh, Pa. (National Union), New Hampshire Insurance Company (New Hampshire), Lexington Insurance Company (Lexington), The Hartford Steam Boiler Inspection and Insurance Company (HSB), Transatlantic Reinsurance Company, American International Underwriters Overseas, Ltd. (AIUO) and United Guaranty Residential Insurance Company. Significant Life Insurance & Retirement Services operations include those conducted through American Life Insurance Company (ALICO), American International Reinsurance Company, Ltd. (AIRCO), American International Assurance Company, Limited together with American International Assurance Company (Bermuda) Limited (AIA), Nan Shan Life Insurance Company, Ltd. (Nan Shan), The Philippine American Life and General Insurance Company (Philamlife), AIG Star Life Insurance Co., Ltd. (AIG Star Life), AIG Edison Life Insurance Company (AIG Edison Life), AIG Annuity Insurance Company (AIG Annuity), the AIG American General Life Companies (AIG American General), American General Life and Accident Insurance Company (AGLA), The United States Life Insurance Company in the City of New York (USLIFE), The Variable Annuity Life Insurance Company (VALIC), SunAmerica Life Insurance Company (SunAmerica Life) and AIG SunAmerica Life Assurance Company. AIG's Financial Services operations are conducted primarily through International Lease Finance Corporation (ILFC), AIG Financial Products Corp. and AIG Trading Group Inc. (AIGTG) and their respective subsidiaries (collectively referred to as AIGFP), and American General Finance, Inc. and its subsidiaries (AGF). AIG's Asset Management operations include AIG SunAmerica Asset Management Corp. (SAAMCo) and AIG Global Asset Management Holdings Corp. (formerly known as AIG Global Investment Group, Inc.) and its subsidiaries and affiliated companies (AIG Global Investment Group). For information on AIG's business segments, see Note 2 of Notes to Consolidated Financial Statements.

At December 31, 2005, AIG and its subsidiaries had approximately 97,000 employees.

AIG's Internet address for its corporate website is *www.aigcorporate.com*. AIG makes available free of charge, through the Investor Information section of AIG's corporate website, Annual Reports on Form 10-K, Quarterly Reports on Form 10-Q and Current Reports on Form 8-K and amendments to those reports filed or furnished pursuant to Section 13(a) or 15(d) of the Securities Exchange Act of 1934 (the Exchange Act) as soon as reasonably practicable after such materials are electronically filed with, or furnished to, the Securities and Exchange Commission (SEC). AIG also makes available on its corporate website copies of its charters for its Audit, Nominating and Corporate Governance and Compensation Committees, as well as its Corporate Governance Guidelines (which includes Director Independence Standards) and Director, Executive Officer and Senior Financial Officer Code of Business Conduct and Ethics.

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

The Restatements

AIG has completed two restatements of its financial statements (the Restatements). In connection with the first restatement (the First Restatement), AIG restated its consolidated financial statements and financial statement schedules for the years ended December 31, 2003, 2002, 2001 and 2000, the quarters ended March 31, June 30 and September 30, 2004 and 2003 and the quarter ended December 31, 2003. In the second restatement (the Second Restatement), AIG restated its consolidated financial statements and financial statement schedules for the years ended December 31, 2004, 2003 and 2002, along with 2001 and 2000 for purposes of preparation of the Consolidated Financial Data for 2001 and 2000, the quarterly financial information for 2004 and 2003 and the first three quarters of 2005. AIG, however, did not amend its quarterly report on Form 10-Q for the quarter ended September 30, 2005 because the adjustments to the financial statements included therein were not material to those financial statements. All financial information included in this Annual Report on Form 10-K reflects the Restatements.

The following table shows the general development of the business of AIG on a consolidated basis, the contributions made to AIG's consolidated revenues and operating income and the assets held, in the periods indicated, by its General Insurance, Life Insurance & Retirement Services, Financial Services and Asset Management operations and other realized capital gains (losses). For additional information, see Selected Financial Data, Management's Discussion and Analysis of Financial Condition and Results of Operations and Notes 1 and 2 of Notes to Consolidated Financial Statements.

Years Ended December 31, *(in millions)*	**2005**	2004	2003	2002	2001
General Insurance operations:					
Gross premiums written	**$ 52,725**	$ 52,046	$ 46,938	$ 36,678	$ 28,341
Net premiums written	**41,872**	40,623	35,031	26,718	19,793
Net premiums earned	**40,809**	38,537	31,306	23,595	18,661
Underwriting profit (loss)[a]	**(2,050)**	(247)	1,975	(1,082)[c]	(777)[d]
Net investment income	**4,031**	3,196	2,566	2,350	2,551
Realized capital gains (losses)	**334**	228	(39)	(345)	(189)
Operating income	**2,315**	3,177	4,502	923[c]	1,585[d]
Identifiable assets	**150,667**	131,658	117,511	105,891	88,250
Loss ratio	**81.1**	78.8	73.1	83.1	79.3
Expense ratio	**23.6**	21.5	19.6	21.8	24.3
Combined ratio[b]	**104.7**	100.3	92.7	104.9[c]	103.6[d]
Life Insurance & Retirement Services operations:					
GAAP premiums	**29,400**	28,088	23,496	20,694	19,600
Net investment income	**18,134**	15,269	12,942	11,243	10,451
Realized capital gains (losses)[e]	**(218)**	43	240	(372)	(400)
Operating income	**8,844**	7,923	6,807	5,181	4,633[f]
Identifiable assets	**480,622**	447,841	372,126	289,914	256,767
Insurance in-force at end of year[g]	**1,852,833**	1,858,094	1,583,031	1,298,592	1,228,501
Financial Services operations:					
Interest, lease and finance charges[h]	**10,525**	7,495	6,242	6,822	6,321
Operating income[g]	**4,276**	2,180	1,182	2,125	1,769
Identifiable assets	**166,488**	165,995	141,667	128,104	107,719
Asset Management operations:					
Advisory and management fees and net investment income from GICs	**5,325**	4,714	3,651	3,467	3,565
Operating income	**2,253**	2,125	1,316	1,125	1,019
Identifiable assets	**81,080**	80,075	64,047	53,732	42,961
Other realized capital gains (losses)	**225**	(227)	(643)	(936)	(321)
Revenues[i]	**108,905**	97,666	79,421	66,171	59,958
Total operating income[j]	**15,213**	14,845	11,907	7,808	5,917
Total assets	**853,370**	801,145	675,602	561,598	490,614

(a) Underwriting profit (loss), a Generally Accepted Accounting Principles (GAAP) measure, is statutory underwriting profit (loss) adjusted primarily for changes in the deferral of policy acquisition costs. This adjustment is necessary to present the financial statements in accordance with GAAP.

(b) Calculated on a statutory basis, includes catastrophe losses of $2.63 billion, $1.05 billion, $83 million, $61 million and $867 million (including World Trade Center and related losses (WTC losses) of $769 million) in 2005, 2004, 2003, 2002 and 2001, respectively.

(c) In the fourth quarter of 2002, after completion of its annual review of General Insurance loss and loss adjustment expense reserves, AIG increased its net loss reserves relating to accident years 1997 through 2001 by $2.1 billion.

(d) Includes $867 million of catastrophe losses.

(e) Includes the effect of hedging activities that do not qualify for hedge accounting treatment under FAS 133 and the application of FAS 52. For 2005, 2004, 2003, 2002, and 2001, respectively, the amounts included are $(437) million, $(140) million, $78 million, $(91) million and $(219) million.

(f) Includes $100 million in WTC losses.

(g) 2005 includes the effect of the non-renewal of a single large group life case of $36 billion. Also, the foreign in-force is translated to U.S. dollars at the appropriate balance sheet exchange rate in each period.

(h) Includes the effect of hedging activities that do not qualify for hedge accounting treatment under FAS 133, including the related foreign exchange gains and losses. For 2005, 2004, 2003, 2002 and 2001, respectively, the amounts included in interest, lease and finance charges are $2.01 billion, $(122) million, $(1.01) billion, $220 million and $56 million, and the amounts included in Financial Services operating income are $1.98 billion, $(149) million, $(964) million, $240 million and $75 million.

(i) Represents the sum of General Insurance net premiums earned, Life Insurance & Retirement Services GAAP premiums, net investment income, Financial Services interest, lease and finance charges, Asset Management advisory and management fees and net investment income from Guaranteed Investment Contracts (GICs), and realized capital gains (losses).

(j) Represents income before income taxes, minority interest and cumulative effect of accounting changes. Includes segment operating income and other realized capital gains (losses) presented above, as well as AIG Parent and other operations of $(2.70) billion, $(333) million, $(1.26) billion, $(610) million and $(751) million in 2005, 2004, 2003, 2002 and 2001, respectively, and acquisition, restructuring and related charges of $(2.02) billion in 2001.

General Insurance Operations

AIG's General Insurance subsidiaries are multiple line companies writing substantially all lines of property and casualty insurance both domestically and abroad. Domestic General Insurance operations are comprised of the Domestic Brokerage Group (DBG), which includes the operations of HSB; Transatlantic Holdings, Inc. (Transatlantic); Personal Lines, including 21st Century Insurance Group (21st Century); and United Guaranty Corporation (UGC).

AIG's primary domestic division is DBG. DBG's business in the United States and Canada is conducted through its General Insurance subsidiaries including American Home, National Union, Lexington and certain other General Insurance company subsidiaries of AIG.

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

In addition to writing substantially all classes of business insurance, including large commercial or industrial property insurance, excess liability, inland marine, environmental, workers compensation and excess and umbrella coverages, DBG offers many specialized forms of insurance such as aviation, accident and health, equipment breakdown, directors and officers liability (D&O), difference-in-conditions, kidnap-ransom, export credit and political risk, and various types of professional errors and omissions coverages. The AIG Risk Management operation provides insurance and risk management programs for large corporate customers. The AIG Risk Finance operation is a leading provider of customized structured insurance products. Also included in DBG are the operations of AIG Environmental, which focuses specifically on providing specialty products to clients with environmental exposures. Lexington writes surplus lines, those risks for which conventional insurance companies do not readily provide insurance coverage, either because of complexity or because the coverage does not lend itself to conventional contracts.

Certain of the products of the DBG companies include funding components or have been structured in a manner such that little or no insurance risk is actually transferred. Funds received in connection with these products are recorded as deposits, included in other liabilities, rather than premiums and incurred losses.

The AIG Worldsource Division introduces and coordinates AIG's products and services to U.S.-based multinational clients and foreign corporations doing business in the U.S.

Transatlantic subsidiaries offer reinsurance capacity on both a treaty and facultative basis both in the U.S. and abroad. Transatlantic structures programs for a full range of property and casualty products with an emphasis on specialty risk.

AIG's Personal Lines operations provide automobile insurance through AIG Direct, the mass marketing operation of AIG, Agency Auto Division and 21st Century, as well as a broad range of coverages for high net-worth individuals through the AIG Private Client Group.

The main business of the UGC subsidiaries is the issuance of residential mortgage guaranty insurance on conventional first lien mortgages for the purchase or refinance of 1-4 family residences. This type of insurance protects lenders in both domestic and international markets against loss if borrowers default. Other UGC subsidiaries write second lien and private student loan guaranty insurance. The second lien coverage protects lenders against loss from default on home equity and closed-end second mortgages used to finance home improvements, repairs or other expenses not directly related to the purchase of a borrower's home. Private student loan guaranty insurance protects lenders against loss if the student, or in many cases the student's parent, defaults on their education loan. UGC had approximately $23 billion of guaranty risk in force at December 31, 2005.

AIG's Foreign General Insurance group accepts risks primarily underwritten through American International Underwriters (AIU), a marketing unit consisting of wholly owned agencies and insurance companies. The Foreign General Insurance group also includes business written by AIG's foreign-based insurance subsidiaries. The Foreign General group uses various marketing methods and multiple distribution channels to write both commercial and consumer lines insurance with certain refinements for local laws, customs and needs. AIU operates in Asia, the Pacific Rim, the United Kingdom, Europe, Africa, the Middle East and Latin America. See also Note 2 of Notes to Consolidated Financial Statements.

During 2005, DBG and the Foreign General Insurance group accounted for 55 percent and 24 percent, respectively, of AIG's General Insurance net premiums written.

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

Certain of DBG's commercial insurance is reinsured on a quota share basis by AIRCO. Various AIG profit centers, including AIU, AIG Reinsurance Advisors, Inc. and AIG Risk Finance, use AIRCO as a reinsurer for certain of their businesses, and AIRCO also receives premiums from offshore fronting arrangements for clients of AIG subsidiaries. In accordance with permitted accounting practices in Bermuda, AIRCO discounts reserves attributable to certain classes of business assumed from other AIG subsidiaries. See Management's Discussion and Analysis of Financial Condition and Results of Operations – "Operating Review – Reserve for Losses and Loss Expenses."

The utilization of reinsurance is closely monitored by senior management and AIG's Credit Risk Committee. AIG believes that no exposure to a single reinsurer represents an inappropriate concentration of risk to AIG, nor is AIG's business substantially dependent upon any reinsurance contract. See also Management's Discussion and Analysis of Financial Condition and Results of Operations and Note 5 of Notes to Consolidated Financial Statements.

AIG is diversified both in terms of classes of business and geographic locations. In General Insurance, approximately 15 percent of net premiums written for the year ended December 31, 2005 represented workers compensation business. During 2005, of the direct General Insurance premiums written (gross premiums less return premiums and cancellations, excluding reinsurance assumed and before deducting reinsurance ceded), 11 percent and 7 percent were written in California and New York, respectively. No other state accounted for more than five percent of such premiums.

The majority of AIG's General Insurance business is in the casualty classes, which tend to involve longer periods of time for the reporting and settling of claims. This may increase the risk and uncertainty with respect to AIG's loss reserve development. See also the Discussion and Analysis of Consolidated Net Losses and Loss Expense Reserve Development in this Item 1. Business and Management's Discussion and Analysis of Financial Condition and Results of Operations.

A significant portion of AIG's General Insurance operating revenue is derived from AIG's insurance investment operations. For a table summarizing the investment results of General Insurance see "Insurance Investments Operations" below. See also Management's Discussion and Analysis of Financial Conditions and Results of Operations and Notes 1, 2 and 8 of Notes to Consolidated Financial Statements.

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

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

Loss reserves established with respect to foreign business are set and monitored in terms of the respective local or functional currency. Therefore, no assumption is included for changes in currency rates. See also Note 1(bb) of Notes to Consolidated Financial Statements.

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

The "Analysis of Consolidated Net Losses and Loss Expense Reserve Development" table presents the development of net losses and loss expense reserves for calendar years 1995 through 2005. Immediately following this table is a second table that presents all data on a basis that excludes asbestos and environmental net losses and loss expense reserve development. The opening reserves held are shown at the top of the table for each year end date. The amount of loss reserve discount included in the opening reserve at each date is shown immediately below the reserves held for each year. The undiscounted reserve at each date is thus the sum of the discount and the reserve held. The upper half of the table shows the cumulative amounts paid during successive years related to the undiscounted opening loss reserves. For example, in the table that excludes asbestos and environmental losses, with respect to the net losses and loss expense reserve of $24.55 billion as of December 31, 1998, by the end of 2005 (seven years later) $24.75 billion had actually been paid in settlement of these net loss reserves. In addition, as reflected in the lower section of the table, the original reserve of $25.45 billion was reestimated to be $30.64 billion at December 31, 2005. This increase from the original estimate would generally result from a combination of a number of factors, including reserves being settled for larger amounts than originally estimated. The original estimates will also be increased or decreased as more information becomes known about the individual claims and overall claim frequency and severity patterns. The redundancy (deficiency) depicted in the table, for any particular calendar year, shows the aggregate change in estimates over the period of years subsequent to the calendar year reflected at the top of the respective column heading. For example, the deficiency of $3.75 billion at December 31, 2005 related to December 31, 2004 net losses and loss expense reserves of $47.30 billion represents the cumulative amount by which reserves for 2004 and prior years have developed deficiently during 2005. The deficiency that has emerged in the last year can be attributed primarily to the excess casualty, excess workers compensation, and D&O and related management liability classes of business. These classes in total produced approximately $4 billion of adverse development in 2005, primarily related to claims from accident years 2002 and prior. For most other classes, accident years 2002 and prior generally produced adverse development in 2005, whereas accident year 2004 generally produced favorable development. In total, the favorable development for all classes of business for accident year 2004 was approximately $3.85 billion. The accident year emergence can be seen by comparing the respective development in 2005 for each column's loss reserve in the table that follows. Loss development patterns utilized to test the reserves generally rely on the actual historical loss development patterns of prior accident years for each class of business. See also Management's Discussion and Analysis of Financial Condition and Results of Operations for further discussion of loss development in 2005.

The bottom of each table below shows the remaining undiscounted and discounted net loss reserve for each year. For example, in the table that excludes asbestos and environmental losses, for the 2000 year-end, the remaining undiscounted reserves held as of December 31, 2005 are $10.01 billion, with a corresponding discounted net reserve of $9.32 billion.

The reserves for net losses and loss expenses with respect to Transatlantic and 21st Century are included only in consolidated net losses and loss expenses commencing with the year ended December 31, 1998, the year they were first consolidated in AIG's financial statements. Reserve development for these operations is included only for 1998 and subsequent periods. Thus, the presentation for 1997 and prior year ends is not fully comparable to that for 1998 and subsequent years in the tables below.

Analysis of Consolidated Losses and Loss Expense Reserve Development

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

(in millions)	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004	**2005**
Net Reserves Held	$19,755	$20,496	$20,901	$25,418	$25,636	$25,684	$26,005	$29,347	$36,228	$47,254	**$57,476**
Discount (in Reserves Held)	217	393	619	897	1,075	1,287	1,423	1,499	1,516	1,553	**2,110**
Net Reserves Held (Undiscounted)	19,972	20,889	21,520	26,315	26,711	26,971	27,428	30,846	37,744	48,807	**59,586**
Paid (Cumulative) as of:											
One year later	5,416	5,712	5,607	7,205	8,266	9,709	11,007	10,775	12,163	14,910	
Two years later	8,982	9,244	9,754	12,382	14,640	17,149	18,091	18,589	21,773		
Three years later	11,363	11,943	12,939	16,599	19,901	21,930	23,881	25,513			
Four years later	13,108	14,152	15,484	20,263	23,074	26,090	28,717				
Five years later	14,667	16,077	17,637	22,303	25,829	29,473					
Six years later	16,120	17,551	18,806	24,114	28,165						
Seven years later	17,212	18,415	19,919	25,770							
Eight years later	17,792	19,200	21,089								
Nine years later	18,379	20,105									
Ten years later	19,155										

(in millions)	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004	**2005**
Net Reserves Held (undiscounted)	$19,972	$20,889	$21,520	$26,315	$26,711	$26,971	$27,428	$30,846	$37,744	$48,807	**$59,586**
Undiscounted Liability as of:											
One year later	19,782	20,795	21,563	25,897	26,358	26,979	31,112	32,913	40,931	53,486	
Two years later	19,866	20,877	21,500	25,638	27,023	30,696	33,363	37,583	49,463		
Three years later	19,865	20,994	21,264	26,169	29,994	32,732	37,964	46,179			
Four years later	20,143	20,776	21,485	28,021	31,192	36,210	45,203				
Five years later	19,991	20,917	22,405	28,607	33,910	41,699					
Six years later	19,950	21,469	22,720	30,632	38,087						
Seven years later	20,335	21,671	24,209	33,861							
Eight years later	20,558	22,986	26,747								
Nine years later	21,736	25,264									
Ten years later	23,878										
Net Redundancy/(Deficiency)	(3,906)	(4,375)	(5,227)	(7,546)	(11,376)	(14,728)	(17,775)	(15,333)	(11,719)	(4,679)	
Remaining Reserves (Undiscounted)	4,724	5,158	5,658	8,091	9,922	12,226	16,486	20,666	27,690	38,576	
Remaining Discount	252	299	358	459	568	690	846	999	1,212	1,568	
Remaining Reserves	4,472	4,859	5,300	7,632	9,354	11,536	15,640	19,667	26,478	37,008	

The table below shows the gross liability (before discount), reinsurance recoverable and net liability recorded at each year-end and the reestimation of these amounts as of December 31, 2005.

(in millions)	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004	**2005**
Gross Liability, End of Year	$32,298	$32,605	$32,049	$36,973	$37,278	$39,222	$42,629	$48,173	$53,387	$63,431	**$79,279**
Reinsurance Recoverable, End of Year	12,326	11,716	10,529	10,658	10,567	12,251	15,201	17,327	15,643	14,624	**19,693**
Net Liability, End of Year	19,972	20,889	21,520	26,315	26,711	26,971	27,428	30,846	37,744	48,807	**59,586**
Reestimated Gross Liability	40,012	40,817	42,937	51,847	56,864	61,991	65,704	66,398	66,967	69,327	
Reestimated Reinsurance Recoverable	16,134	15,553	16,190	17,986	18,777	20,292	20,501	20,219	17,504	15,841	
Reestimated Net Liability	23,878	25,264	26,747	33,861	38,087	41,699	45,203	46,179	49,463	53,486	
Cumulative Gross Redundancy/(Deficiency)	(7,713)	(8,212)	(10,888)	(14,874)	(19,586)	(22,769)	(23,075)	(18,225)	(13,580)	(5,896)	

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

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

(in millions)	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004	**2005**
Net Reserves Held	$19,247	$19,753	$20,113	$24,554	$24,745	$24,829	$25,286	$28,650	$35,559	$45,742	**$55,227**
Discount (in Reserves Held)	217	393	619	897	1,075	1,287	1,423	1,499	1,516	1,553	**2,110**
Net Reserves Held (Undiscounted)	19,464	20,146	20,732	25,451	25,820	26,116	26,709	30,149	37,075	47,295	**57,336**
Paid (Cumulative) as of:											
One year later	5,309	5,603	5,467	7,084	8,195	9,515	10,861	10,632	11,999	14,718	
Two years later	8,771	8,996	9,500	12,190	14,376	16,808	17,801	18,283	21,419		
Three years later	11,013	11,582	12,618	16,214	19,490	21,447	23,430	25,021			
Four years later	12,645	13,724	14,972	19,732	22,521	25,445	28,080				
Five years later	14,139	15,460	16,983	21,630	25,116	28,643					
Six years later	15,404	16,792	18,014	23,282	27,266						
Seven years later	16,355	17,519	18,972	24,753							
Eight years later	16,798	18,149	19,960								
Nine years later	17,230	18,873									
Ten years later	17,826										

(in millions)	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004	**2005**
Net Reserves Held (undiscounted)	$19,464	$20,146	$20,732	$25,451	$25,820	$26,116	$26,709	$30,149	$37,075	$47,295	**$57,336**
Undiscounted Liability as of:											
One year later	18,937	19,904	20,576	24,890	25,437	26,071	30,274	32,129	39,261	51,048	
Two years later	18,883	19,788	20,385	24,602	26,053	29,670	32,438	35,803	46,865		
Three years later	18,680	19,777	20,120	25,084	28,902	31,619	36,043	43,467			
Four years later	18,830	19,530	20,301	26,813	30,014	34,102	42,348				
Five years later	18,651	19,633	21,104	27,314	31,738	38,655					
Six years later	18,574	20,070	21,336	28,345	34,978						
Seven years later	18,844	20,188	21,836	30,636							
Eight years later	18,984	20,515	23,441								
Nine years later	19,173	21,858									
Ten years later	20,379										
Net Redundancy/(Deficiency)	(915)	(1,712)	(2,709)	(5,185)	(9,158)	(12,539)	(15,639)	(13,318)	(9,790)	(3,753)	
Remaining Reserves (undiscounted)	2,553	2,985	3,482	5,883	7,712	10,012	14,269	18,446	25,447	36,330	
Remaining Discount	252	299	358	459	568	690	846	999	1,212	1,568	
Remaining Reserves	2,301	2,686	3,124	5,424	7,144	9,322	13,423	17,447	24,235	34,762	

The table below shows the gross liability (before discount), reinsurance recoverable and net liability recorded at each year-end and the reestimation of these amounts as of December 31, 2005.

(in millions)	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004	**2005**
Gross Liability, End of Year	$30,356	$30,302	$29,740	$34,474	$34,666	$36,777	$40,400	$46,036	$51,363	$59,897	**$73,912**
Reinsurance Recoverable, End of Year	10,892	10,156	9,008	9,023	8,846	10,661	13,691	15,887	14,288	12,602	**16,576**
Net Liability, End of Year	19,464	20,146	20,732	25,451	25,820	26,116	26,709	30,149	37,075	47,295	**57,336**
Reestimated Gross Liability	30,452	31,660	34,226	43,461	48,886	54,534	58,776	59,813	60,788	63,544	
Reestimated Reinsurance Recoverable	10,073	9,802	10,785	12,825	13,908	15,879	16,428	16,346	13,923	12,496	
Reestimated Net Liability	20,379	21,858	23,441	30,636	34,978	38,655	42,348	43,467	46,865	51,048	
Cumulative Gross Redundancy/(Deficiency)	(96)	(1,358)	(4,486)	(8,987)	(14,220)	(17,757)	(18,376)	(13,777)	(9,425)	(3,647)	

Reconciliation of Net Reserves for Losses and Loss Expenses

(in millions)	**2005**	2004	2003
Net reserve for losses and loss expenses at beginning of year	**$47,254**	$36,228	$29,347
Foreign exchange effect	**(628)**	524	580
Acquisition	**–**	–	391[a]
Losses and loss expenses incurred:			
Current year	**28,426**	26,793	20,509
Prior years[b]	**4,665**	3,564	2,363
	33,091	30,357	22,872
Losses and loss expenses paid:			
Current year	**7,331**	7,692	6,187
Prior years	**14,910**	12,163	10,775
	22,241	19,855	16,962
Net reserve for losses and loss expenses at end of year[c]	**$57,476**	$47,254	$36,228

(a) Reflects the opening balances with respect to the GE U.S.-based auto and home insurance business acquired in 2003.

(b) Includes accretion of discount of $(15) million in 2005, including an increase of $375 million in the discount recorded in 2005; $377 million in 2004 and $296 million in 2003. Additionally, includes $269 million in 2005, $317 million in 2004 and $323 million in 2003 for the general reinsurance operations of Transatlantic, and $197 million of additional losses incurred in 2005 resulting from increased labor and material costs related to the 2004 Florida hurricanes.

(c) See also Note 6(a) of Notes to Consolidated Financial Statements.

The reserve for losses and loss expenses as reported in AIG's Consolidated Balance Sheet at December 31, 2005 differs from the total reserve reported in the Annual Statements filed with state insurance departments and, where appropriate, with foreign regulatory authorities. The differences at December 31, 2005 relate primarily to reserves for certain foreign operations not required to be reported in the United States for statutory reporting purposes.

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

For further discussion regarding net reserves for losses and loss expenses, see Management's Discussion and Analysis of Financial Condition and Results of Operations.

Life Insurance & Retirement Services Operations

AIG's Life Insurance & Retirement Services subsidiaries offer a wide range of insurance and retirement savings products both domestically and abroad. Insurance-oriented products consist of individual and group life, payout annuities, endowment and accident and health policies. Retirement savings products consist generally of fixed and variable annuities. See also Management's Discussion and Analysis of Financial Condition and Results of Operations.

Life Insurance & Retirement Services operations in foreign countries comprised 78 percent of Life Insurance & Retirement Services GAAP premiums and 59 percent of Life Insurance & Retirement Services operating income in 2005. AIG operates overseas principally through ALICO, AIA, Nan Shan, Philamlife, AIG Star Life, and AIG Edison Life. ALICO is incorporated in Delaware and all of its business is written outside of the United States. ALICO has operations either directly or through subsidiaries in Europe, Latin America, the Caribbean, the Middle East, South Asia and the Far East, with Japan being the largest territory. AIG added significantly to its presence in Japan with the acquisition of GE Edison Life Insurance Company (now AIG Edison Life), which was consolidated beginning with the fourth quarter of 2003. AIA operates primarily in China (including Hong Kong), Singapore, Malaysia, Thailand, Korea, Australia, New Zealand, Vietnam, and India. The operations in India are conducted through a joint venture, Tata AIG Life Insurance Company Limited. Nan Shan operates in Taiwan. Philamlife is the largest life insurer in the Philippines. AIG Star Life operates in Japan. See also Note 2 of Notes to Consolidated Financial Statements.

AIRCO acts primarily as an internal reinsurance company for AIG's foreign life operations. This facilitates insurance risk management (retention, volatility, concentrations) and capital planning locally (branch and subsidiary). It also allows AIG to pool its insurance risks and purchase reinsurance more efficiently at a consolidated level, manage global counterparty risk and relationships and manage global life catastrophe risks.

AIG's principal domestic Life Insurance & Retirement Services operations include AGLA, AIG American General, AIG Annuity, USLIFE, VALIC and SunAmerica Life. These companies utilize multiple distribution channels including independent producers, brokerage, career agents and banks to offer life insurance, annuity and accident and health products and services, as well as financial and other investment products. The domestic Life Insurance & Retirement Services operations comprised 22 percent of total Life Insurance & Retirement Services GAAP premiums and 41 percent of Life Insurance & Retirement Services operating income in 2005.

There was no significant adverse effect on AIG's Life Insurance & Retirement Services results of operations from

economic conditions in any one state, country or geographic region for the year ended December 31, 2005. See also Management's Discussion and Analysis of Financial Condition and Results of Operations.

Life insurance products such as whole life and endowment continue to be significant in the overseas companies, especially in Southeast Asia, while a mixture of life insurance, accident and health and retirement services products are sold in Japan.

In addition to the above, AIG also has subsidiary operations in Canada, Egypt, Mexico, Poland, Switzerland and Puerto Rico, and conducts life insurance business through a joint venture in Brazil and through an AIUO subsidiary company in Russia, and in certain countries in Central and South America.

The Foreign Life Insurance & Retirement Services companies have over 270,000 full and part-time agents, as well as independent producers, and sell their products largely to indigenous persons in local and foreign currencies. In addition to the agency outlets, these companies also distribute their products through direct marketing channels, such as mass marketing, and through brokers and other distribution outlets, such as financial institutions.

Insurance Investment Operations

A significant portion of AIG's General Insurance and Life Insurance & Retirement Services operating revenues are derived from AIG's insurance investment operations. See also Management's Discussion and Analysis of Financial Condition and Results of Operations and Notes 1, 2 and 8 of Notes to Consolidated Financial Statements.

The following table summarizes the investment results of the General Insurance operations. See also Management's Discussion and Analysis of Financial Condition and Results of Operations and Note 8 of Notes to Consolidated Financial Statements.

	Annual Average Cash and Invested Assets				
Years Ended December 31, *(in millions)*	Cash (including short-term investments)	Invested Assets[a]	Total	Return on Average Cash and Assets[b]	Return on Average Assets[c]
2005	**$ 2,450**	**$ 86,211**	**$ 88,661**	**4.5%**	**4.7%**
2004	2,012	73,338	75,350	4.2	4.4
2003	1,818	59,855	61,673	4.2	4.3
2002	1,537	47,477	49,014	4.8	5.0
2001	1,338	41,481	42,819	6.0	6.2

(a) Including investment income due and accrued, and real estate.

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

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

The following table summarizes the investment results of the Life Insurance & Retirement Services operations. See also Management's Discussion and Analysis of Financial Condition and Results of Operations and Note 8 of Notes to Consolidated Financial Statements.

	Annual Average Cash and Invested Assets				
Years Ended December 31, *(in millions)*	Cash (including short-term investments)	Invested Assets[a]	Total	Return on Average Cash and Assets[b]	Return on Average Assets[c]
2005	**$ 6,180**	**$ 352,250**	**$ 358,430**	**5.1%**	**5.1%**
2004	5,089	307,659	312,748	4.9	5.0
2003	4,680	247,608	252,288	5.1	5.2
2002	3,919	199,750	203,669	5.5	5.6
2001	3,615	162,708	166,323	6.3	6.4

(a) Including investment income due and accrued, and real estate.

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

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

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

Financial Services Operations

AIG's Financial Services subsidiaries engage in diversified activities including aircraft and equipment leasing, capital markets transactions, consumer finance and insurance premium financing.

AIG's Aircraft Finance operations represent the operations of ILFC, which generates its revenues primarily from leasing new and used commercial jet aircraft to domestic and foreign airlines. Revenues also result from the remarketing of commercial jets for its own account, for airlines and for financial institutions. See also Note 2 of Notes to Consolidated Financial Statements.

The Capital Markets operations of AIG are conducted primarily through AIGFP, which engages as principal in standard and customized interest rate, currency, equity, commodity, energy and credit products with top-tier corporations, financial institutions, governments, agencies, institutional investors, and high-net-worth individuals throughout the world. AIGFP also raises funds through municipal reinvestment contracts and other private and public security offerings, investing the proceeds in a diversified portfolio of high grade securities and derivative transactions. See also Note 2 of Notes to Consolidated Financial Statements.

Consumer Finance operations include AGF as well as AIG Consumer Finance Group, Inc. (AIGCFG). AGF provides a wide variety of consumer finance products, including real estate mortgages, consumer loans, retail sales finance and credit-related insurance to customers in the United States. AIGCFG, through its subsidiaries, is engaged in developing a multi-product consumer finance business with an emphasis on emerging markets. See also Note 2 of Notes to Consolidated Financial Statements.

Together, the Aircraft Finance, Capital Markets and Consumer Finance operations generate the vast majority of the revenues produced by AIG's consolidated Financial Services operations.

Imperial A.I. Credit Companies also contribute to Financial Services income. This operation engages principally in insurance premium financing for both AIG's customers and those of other insurers. See Note 1 of Notes to Consolidated Financial Statements.

Asset Management Operations

AIG's Asset Management operations comprise a wide variety of investment-related services and investment products, including institutional and retail asset management, broker dealer services and spread-based investment business from the sale of guaranteed investment contracts, also known as funding agreements (GICs). Such products and services are offered to individuals and institutions both domestically and overseas.

AIG's principal Asset Management operations are conducted through certain subsidiaries of AIG Retirement Services, Inc. (AIG SunAmerica), including SAAMCo and the AIG Advisor Group broker dealers and AIG Global Investment Group. AIG SunAmerica sells and manages mutual funds and provides financial advisory services through independent-contractor registered representatives. AIG Global Investment Group manages invested assets on a global basis for third-party institutional, retail, private equity and real estate investment funds, provides securities lending and custodial services and organizes and manages the invested assets of institutional private equity investment funds. Each of these subsidiary operations receives fees for investment products and services provided. See also Management's Discussion and Analysis of Financial Condition and Results of Operations and Note 2 of Notes to Consolidated Financial Statements.

Other Operations

Certain other AIG subsidiaries provide insurance-related services such as adjusting claims and marketing specialized products. Several wholly owned foreign subsidiaries of AIG operating in countries or jurisdictions such as Ireland, Bermuda, Barbados and Gibraltar provide insurance and related administrative and back office services to a variety of insurance and reinsurance companies. These companies include captive insurance companies unaffiliated with AIG, subsidiaries of AIG and the subsidiaries of holding companies in which AIG holds an interest, such as IPC Holdings, Ltd (IPC) and Allied World Assurance Holdings, Ltd. (AWAC). AIG also has several other subsidiaries which engage in various businesses. Mt. Mansfield Company, Inc. owns and operates the ski slopes, lifts, school and an inn located at Stowe, Vermont. Also included in other operations are unallocated corporate expenses, including the settlement costs more fully described in Item 3. Legal Proceedings and Note 12(i) of Notes to Consolidated Financial Statements.

Additional Investments

AIG holds a 24.3 percent interest in IPC, a reinsurance holding company, a 23.4 percent interest in AWAC, a property-casualty insurance holding company, and a 24.5 percent interest in The Fuji Fire and Marine Insurance Co., Ltd., a general insurance company. See also Note 1(s) of Notes to Consolidated Financial Statements.

Locations of Certain Assets

As of December 31, 2005, approximately 34 percent of the consolidated assets of AIG were located in foreign countries (other than Canada), including $4.4 billion of cash and securities on deposit with foreign regulatory authorities. Foreign operations and assets held abroad may be adversely affected by political developments in foreign countries, including such possibilities as tax changes, nationalization, and changes in regulatory policy, as well as by consequence of hostilities and unrest. The risks of such occurrences and their overall effect upon AIG vary from country to country and cannot easily be predicted. If expropriation or nationalization does occur, AIG's policy is to take all appropriate measures to seek recovery of such assets. Certain of the countries in which AIG's business is conducted have currency restrictions which generally cause a delay in a company's ability to repatriate assets and profits. See also Notes 1 and 2 of Notes to Consolidated Financial Statements and "Risk Factors — Foreign Operations" in Item 1A. Risk Factors.

Regulation

AIG's operations around the world are subject to regulation by many different types of regulatory authorities, including insurance, securities, investment advisory, banking and thrift regulators in the United States and abroad. The regulatory environment can have a significant effect on AIG and its business. AIG's operations have become more diverse and consumer-oriented, increasing the scope of regulatory supervision and the possibility of intervention. In addition, the investigations into financial accounting practices that led to the Restatements of AIG's financial statements have heightened regulatory scrutiny of AIG worldwide.

Certain states require registration and periodic reporting by insurance companies that are licensed in such states and are controlled by other corporations. Applicable legislation typically requires periodic disclosure concerning the corporation that controls the registered insurer and the other companies in the holding company system and prior approval of intercorporate services and transfers of assets (including in some instances payment of dividends by the insurance subsidiary) within the holding company system. AIG's subsidiaries are registered under such legislation in those states that have such requirements. See also Note 11 of Notes to Consolidated Financial Statements.

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

In connection with the Restatements, AIG undertook to examine and evaluate each of the items that have been restated or adjusted in its consolidated GAAP financial statements to determine whether restatement of the previously filed statutory financial statements of its insurance company subsidiaries would be required. AIG completed its 2004 audited statutory financial statements for all of the Domestic General Insurance companies in late 2005. The statutory accounting treatment of the various items requiring adjustment or restatement were reviewed and agreed to with the relevant state insurance regulators in advance of the filings. Adjustments necessary to reflect the cumulative effect on statutory surplus of adjustments relating to years prior to 2004 were made to 2004 opening surplus, and 2004 statutory net income was restated accordingly. Previously reported General Insurance statutory surplus at December 31, 2004 was reduced by approximately $3.5 billion to approximately $20.6 billion.

AIG also recently completed its 2005 unaudited statutory financial statements for all of the Domestic General Insurance companies, again after reviewing and agreeing with the relevant state insurance regulators the statutory accounting treatment of various items. The state regulators have permitted the Domestic General Insurance companies to record a $724 million reduction to opening statutory surplus as of January 1, 2005, to reflect the effects of the Second Restatement. See also Management's Discussion and Analysis of Financial Condition and Results of Operations — "Capital Resources — Regulation and Supervision" herein.

AIG has taken various steps to enhance the capital positions of the Domestic General Insurance companies. AIG entered into capital maintenance agreements with the Domestic General Insurance companies that set forth procedures through which AIG will provide ongoing capital support. Dividends from the Domestic General Insurance companies were suspended in the fourth quarter of 2005. AIG contributed an additional $750 million of capital into American Home effective September 30, 2005, and contributed a further $2.25 billion of capital in February 2006 for a total of approximately $3 billion of capital into Domestic General Insurance subsidiaries effective December 31, 2005. Furthermore, in order to allow the Domestic General Insurance companies to record as an admitted asset at December 31, 2005 certain reinsurance ceded to non-U.S. reinsurers (which has the effect of increasing the statutory surplus of such Domestic General Insurance companies), AIG has obtained, and entered into reimbursement agreements for $1.5 billion of letters of credit issued by several commercial banks in favor of certain Domestic General Insurance companies.

AIG's insurance operations are currently under review by various state regulatory agencies. See Item 3. Legal Proceedings for a further description of these investigations and see "Risk Factors – Regulatory Investigations" in Item 1A. Risk Factors for more information on their application to AIG's insurance businesses.

Risk-Based Capital (RBC) is designed to measure the adequacy of an insurer's statutory surplus in relation to the risks inherent in its business. Thus, inadequately capitalized general and life insurance companies may be identified.

The RBC formula develops a risk adjusted target level of statutory surplus by applying certain factors to various asset, premium and reserve items. Higher factors are applied to more risky items and lower factors are applied to less risky items. Thus, the target level of statutory surplus varies not only as a result of the insurer's size, but also on the risk profile of the insurer's operations.

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

corrective action to placing the insurer under regulatory control.

The statutory surplus of each of AIG's domestic general and life insurance subsidiaries exceeded their RBC standards as of December 31, 2005.

To the extent that any of AIG's insurance entities would fall below prescribed levels of surplus, it would be AIG's intention to infuse necessary capital to support that entity.

A substantial portion of AIG's General Insurance business and a majority of its Life Insurance business is carried on in foreign countries. The degree of regulation and supervision in foreign jurisdictions varies. Generally, AIG, as well as the underwriting companies operating in such jurisdictions, must satisfy local regulatory requirements. Licenses issued by foreign authorities to AIG subsidiaries are subject to modification or revocation by such authorities, and AIU or other AIG subsidiaries could be prevented from conducting business in certain of the jurisdictions where they currently operate. In the past, AIU has been allowed to modify its operations to conform with new licensing requirements in most jurisdictions.

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

In 1999, AIG became a unitary thrift holding company when the Office of Thrift Supervision (OTS) granted AIG approval to organize AIG Federal Savings Bank. Annually, the OTS conducts an examination of AIG. The OTS examination involves assessing the organization's overall risk profile.

Competition

AIG's Insurance, Financial Services and Asset Management businesses operate in a highly competitive environment, both domestically and overseas. Principal sources of competition are insurance companies, banks, investment banks and other non-bank financial institutions.

The insurance industry in particular is highly competitive. Within the United States, AIG's General Insurance subsidiaries compete with approximately 3,100 other stock companies, specialty insurance organizations, mutual companies and other underwriting organizations. AIG's subsidiaries offering Life Insurance and Retirement Services compete in the United States with approximately 2,000 life insurance companies and other participants in related financial services fields. Overseas, AIG subsidiaries compete for business with foreign insurance operations of the larger U.S. insurers, global insurance groups, and local companies in particular areas in which they are active.

AIG's strong ratings have historically provided a competitive advantage. The effect on the business of AIG of recent regulatory investigations, the Restatements, and subsequent ratings actions is currently unknown, but these developments may adversely affect the competitive position of AIG and its subsidiaries. See "Risk Factors — AIG Credit Ratings" in Item 1A. Risk Factors.

ITEM 1A.
Risk Factors

AIG's Credit Ratings

The downgrades in AIG's credit ratings will increase AIG's borrowing costs, may lessen AIG's ability to compete in certain businesses and will require AIG to post additional collateral.

From March through June of 2005, the major rating agencies downgraded AIG's ratings in a series of actions. Standard & Poor's, a division of The McGraw-Hill Companies, Inc. (S&P), lowered the long-term senior debt and counterparty ratings of AIG from 'AAA' to 'AA' and changed the rating outlook to negative. Moody's Investors Service (Moody's) lowered AIG's long-term senior debt rating from 'Aaa' to 'Aa2' and changed the outlook to stable. Fitch Ratings (Fitch) downgraded the long-term senior debt ratings of AIG from 'AAA' to 'AA' and placed the ratings on Rating Watch Negative.

The agencies also took rating actions on AIG's insurance subsidiaries. S&P and Fitch lowered to 'AA+' the insurance financial strength ratings of most of AIG's insurance companies. Moody's lowered the insurance financial strength ratings generally to either 'Aa1' or 'Aa2'. A.M. Best downgraded the financial strength ratings for most of AIG's insurance subsidiaries from 'A++' to 'A+' and the issuer credit ratings from 'aa+' to 'aa–'. Many of these companies' ratings remain on a negative watch.

In addition, S&P changed the outlook on ILFC's 'AA–' long-term senior debt rating to negative. Moody's affirmed ILFC's long-term and short-term senior debt ratings ('A1'/'P-1'). Fitch downgraded ILFC's long-term senior debt rating from 'AA–' to 'A+' and placed the rating on Rating Watch Negative and downgraded ILFC's short-term debt rating from 'F1+' to 'F1'. Fitch also placed the 'A+' long-term senior debt ratings of American General Finance Corporation and American General Finance, Inc. on Rating Watch Negative. S&P and Moody's affirmed the long-term and short-term senior debt ratings of American General Finance Corporation at 'A+'/'A-1' and 'A1'/'P-1', respectively.

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

These ratings actions have affected and will continue to affect AIG's business and results of operations in a number of ways.

- **Downgrades in AIG's debt ratings will adversely affect AIG's results of operations.** AIG relies on external sources of financing to fund several of its operations. The cost and availability of unsecured financing are generally dependent on the issuer's long-term and short-term debt ratings. These downgrades and any future downgrades in AIG's debt ratings may adversely affect AIG's borrowing costs and therefore adversely affect AIG's results of operations.
- **The downgrade in AIG's long-term senior debt ratings will adversely affect AIGFP's ability to compete for certain businesses.** Credit ratings are very important to the ability of financial institutions to compete in the derivative and structured transaction marketplaces. Historically, AIG's triple-A ratings provided AIGFP a competitive advantage. The downgrades have reduced this advantage and, for specialized financial transactions that generally are conducted only by triple-A rated financial institutions, counterparties may be unwilling to transact business with AIGFP except on a secured basis. This could require AIGFP to post more collateral to counterparties in the future. See below for a further discussion of the effect that posting collateral may have on AIG's liquidity.
- **Although the financial strength ratings of AIG's insurance company subsidiaries remain high compared to many of their competitors, the downgrades have reduced the previous ratings differential.** The competitive advantage of the ratings to AIG's insurance company subsidiaries may be lessened accordingly.
- **As a result of the downgrades of AIG's long-term senior debt ratings, AIG was required to post approximately $1.16 billion of collateral with counterparties to municipal guaranteed investment contracts and financial derivatives transactions.** In the event of a further downgrade, AIG will be required to post additional collateral. It is estimated that, as of the close of business on February 28, 2006 based on AIG's outstanding municipal guaranteed investment agreements and financial derivatives transactions as of such date, a further downgrade of AIG's long-term senior debt ratings to 'Aa3' by Moody's or 'AA–' by S&P would permit counterparties to call for approximately $962 million of additional collateral. Further, additional downgrades could result in requirements for substantial additional collateral, which could have a material effect on how AIG manages its liquidity. The actual amount of additional collateral that AIG would be required to post to counterparties in the event of such downgrades depends on market conditions, the market value of the outstanding affected transactions and other factors prevailing at the time of the downgrade. Any additional obligations to post collateral will increase the demand on AIG's liquidity.

Regulatory Investigations

Significant legal proceedings have adversely affected AIG's results of operations for 2005. As a result of the settlements discussed below under Item 3. Legal Proceedings, AIG recorded an after-tax charge of approximately $1.15 billion in the fourth quarter of 2005. AIG is party to numerous other legal proceedings and regulatory investigations. It is possible that the effect of the unresolved matters could be material to AIG's consolidated results of operations for an individual reporting period. For a discussion of these unresolved matters, see Item 3. Legal Proceedings.

Significant investigations into AIG's business are continuing and the commencement of additional investigations is possible. Broad-ranging investigations into AIG's business practices continue. These investigations are being conducted by a number of regulators, and related actions by regulators both within and outside the United States may be undertaken in response. The review of large amounts of information by various regulatory authorities may result in the commencement of new areas of inquiry and, possibly, new significant legal proceedings.

The Relationships Between AIG and Starr and SICO

The relationships between AIG and Starr and SICO may take an extended period of time to unwind and/or resolve, and the consequences of such resolution are uncertain. Although AIG is currently working on unwinding and resolving its relationships with C.V. Starr & Co, Inc. (Starr) and Starr International Company, Inc. (SICO), AIG cannot predict what its future relationship with Starr and SICO will be. AIG subsidiaries are in the process of terminating their agency relationships with the Starr agencies and are beginning to write the business previously produced by those agencies on a direct basis. AIG also continues to address the issues posed by compensation plans and programs previously provided to AIG executives by Starr and SICO, as AIG is providing compensation programs that recognize those plans and programs. In January 2006, Starr announced that it had completed its tender offers to purchase interests in Starr and that all eligible shareholders had tendered their shares. As a result of completion of the tender offers, no AIG executive currently holds any Starr interest. AIG has entered into agreements pursuant to which AIG agrees, subject to certain conditions, to assure AIG's current employees that all payments are made under a series of two-year Deferred Compensation Profit Participation Plans provided by SICO (SICO Plans). See Note 12(f) and Note 16 of Notes to Consolidated Financial Statements. Nevertheless, there can be no assurance that AIG will be able to effectively address the consequences for its executives of the unwinding of their participation in the Starr and SICO plans and programs. Nor can there be any assurance that AIG will compete successfully for the business previously produced by the Starr agencies.

Finally, litigation between AIG and Starr and SICO remains pending, and the timing and terms of any resolution cannot currently be predicted. As a result of the foregoing, there can be no assurance that the ultimate resolution of AIG's relationships with Starr and SICO will not be adverse to AIG. For further information about litigation between AIG and Starr and SICO, see Item 3. Legal Proceedings.

Certain Material Weaknesses

Management identified three remaining material weaknesses in AIG's internal control over financial reporting. Remediation of these material weaknesses is ongoing. Until these weaknesses are remediated, the weaknesses could affect the accuracy or timing of future filings with the SEC and other regulatory authorities. A discussion of these material weaknesses and AIG's remediation efforts can be found in Item 9A of Part II of this Annual Report on Form 10-K.

Access to Capital Markets

AIG's access to the U.S. public capital markets may be delayed by the SEC registration process. Although AIG is able to access the Rule 144A and Euro markets, AIG will be unable to access the U.S. public securities markets until it has filed and the SEC has declared effective a new registration statement under the Securities Act of 1933. Depending upon the SEC's review of these filings, this process may take several months or more.

Unless relief is granted by the SEC, AIG will not be able to avail itself of certain favorable provisions of the Securities Act. AIG will not, for a period of three years, be a "well-known seasoned issuer". During this period, AIG's ability to communicate with respect to new product offerings and to structure client products will be more limited than they otherwise would. In addition, during this period, AIG will not be able to avail itself of provisions that allow for an automatically effective shelf registration statement or rely on the "forward-looking statements" safe harbor under the securities laws in providing forward-looking information to investors.

Foreign Operations

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

The degree of regulation and supervision in foreign jurisdictions varies. Generally, AIG, as well as the underwriting companies operating in such jurisdictions, must satisfy local regulatory requirements. Licenses issued by foreign authorities to AIG subsidiaries are subject to modification and revocation. Thus, AIG's insurance subsidiaries could be prevented from conducting future business in certain of the jurisdictions where they currently operate. AIG's international operations include operations in various developing nations. Both current and future foreign operations could be adversely affected by unfavorable political developments including tax changes, regulatory restrictions and nationalization of AIG's operations without compensation. Adverse affects resulting from any one country may affect AIG's results of operations, liquidity and financial condition depending on the magnitude of the event and AIG's net financial exposure at that time in that country.

Liquidity

Payments from subsidiaries may be limited by regulators. AIG depends on dividends, distributions and other payments from AIG's subsidiaries to fund dividend payments and to fund payments on AIG's obligations, including debt obligations. Regulatory and other legal restrictions may limit AIG's ability to transfer funds freely, either to or from AIG's subsidiaries. In particular, many of AIG's subsidiaries, including AIG's insurance subsidiaries, are subject to laws and regulations that authorize regulatory bodies to block or reduce the flow of funds to the parent holding company, or that prohibit such transfer altogether in certain circumstances. These laws and regulations may hinder AIG's ability to access funds that AIG may need to make payments on AIG's obligations.

Regulation

AIG is subject to extensive regulation in the jurisdictions in which it conducts its businesses. AIG's operations around the world are subject to regulation by different types of regulatory authorities, including insurance, securities, investment advisory, banking and thrift regulators in the United States and abroad. AIG's operations have become more diverse and consumer-oriented, increasing the scope of regulatory supervision and the possibility of intervention. In particular, AIG's consumer lending business is subject to a broad array of laws and regulations governing lending practices and permissible loan terms, and AIG would expect increased regulatory oversight relating to this business.

The regulatory environment could have a significant effect on AIG and its businesses. Among other things, AIG could be fined, prohibited from engaging in some of its business activities or subject to limitations or conditions on its business activities. Significant regulatory action against AIG could have material adverse financial effects, cause significant reputational harm, or harm business prospects. New laws or regulations or changes in the enforcement of existing laws or regulations applicable to clients may also adversely affect AIG and its businesses. See Item 1. Business — "Regulation."

Casualty Insurance Underwriting and Reserves

Casualty insurance liabilities are difficult to predict and may exceed the related reserves for losses and loss expenses. Although AIG annually reviews the adequacy of the established reserve for losses and loss expenses, there can be no assurance that AIG's ultimate loss reserves will not develop adversely and materially exceed AIG's current loss reserves. Estimation of ultimate net losses, loss expenses and loss reserves is a complex process for long-tail casualty lines of business, which include excess and umbrella liability, D&O, professional liability, medical malpractice, workers compensation, general liability, products liability and related classes, as well as for asbestos and environmental exposures. Generally, actual historical loss development factors are used to project future loss development. However, there can be no assurance that future loss development patterns will be the same as in the past. Moreover, any deviation in loss cost trends or in loss development factors might not be discernible for an extended period of time subsequent to the recording of the initial loss reserve estimates for any accident year. Thus, there is the potential for reserves with respect to a number of years to be significantly affected by changes in loss cost trends or loss development factors that were relied upon in setting the reserves. These changes in loss trends or loss development factors could be attributable to changes in inflation in labor and material costs or in the judicial environment, or in other social or economic phenomena affecting claims. See "Management's Discussion and Analysis of Financial Condition and Results of Operations — Operating Review — Reserve for Losses and Loss Expenses."

Natural Disasters and Pandemic Diseases

Natural disasters and pandemic disease could adversely affect AIG's operating results. Natural disasters such as hurricanes, earthquakes and other catastrophes have the potential to adversely affect AIG's operating results. Other risks, such as an outbreak of a pandemic disease, such as the Avian Influenza A Virus (H5N1), could adversely affect AIG's business and operating results to an extent that may be only minimally offset by reinsurance programs.

While to date outbreaks of the Avian Flu continue to occur among poultry or wild birds in a number of countries in Asia, parts of Europe, and recently in Africa, transmission to humans has been rare. If the virus mutates to a form that can be transmitted from human to human, it has the potential to spread rapidly worldwide. If such an outbreak were to take place, early quarantine and vaccination could be critical to containment.

Both the contagion and mortality rate of any mutated H5N1 virus that can be transmitted from human to human are highly speculative. AIG continues to monitor the developing facts. A significant global outbreak could have a material adverse effect on AIG's life insurance business operating results and liquidity from increased mortality and morbidity rates.

ITEM 1B.
Unresolved Staff Comments

There are no material unresolved written comments that were received from the SEC staff 180 days or more before the end of AIG's fiscal year relating to AIG's periodic or current reports under the Securities Exchange Act of 1934 (Exchange Act).

ITEM 2.
Properties

AIG and its subsidiaries operate from approximately 2,200 offices in the United States, 8 offices in Canada and numerous offices in approximately 100 foreign countries. The offices in Montgomery, Alabama; Greensboro, North Carolina; Springfield, Illinois; Amarillo, Ft. Worth and Houston, Texas; Wilmington, Delaware; San Juan, Puerto Rico; Tampa, Florida; Livingston, New Jersey; Evansville, Indiana; Nashville, Tennessee; 70 Pine Street, 72 Wall Street and 175 Water Street in New York City; and offices in more than 30 foreign countries and jurisdictions including Bermuda, Chile, Hong Kong, the Philippines, Japan, United Kingdom, Singapore, Switzerland, Taiwan and Thailand are located in buildings owned by AIG and its subsidiaries. The remainder of the office space utilized by AIG subsidiaries is leased.

ITEM 3.
Legal Proceedings

General

AIG and its subsidiaries, in common with the insurance industry in general, are subject to litigation, including claims for punitive damages, in the normal course of their business. See Notes 12(d), 12(g), 12(h) and 12(i) of Notes to Consolidated Financial Statements, as well as the Discussion and Analysis of Consolidated Net Losses and Loss Expense Reserve Development and Management's Discussion and Analysis of Financial Condition and Results of Operations.

2006 Regulatory Settlements

In February 2006, AIG reached a final settlement with the SEC, the United States Department of Justice (DOJ), the Office of the New York Attorney General (NYAG) and the New York State Department of Insurance (DOI). The settlements resolved outstanding litigation filed by the SEC, NYAG and DOI against AIG and concluded negotiations with these authorities and the DOJ in connection with the accounting, financial reporting and insurance brokerage practices of AIG and its subsidiaries, as well as claims relating to the underpayment of certain workers compensation premium taxes and other assessments. The 2005 financial statements included in this Annual Report on Form 10-K include a fourth quarter after-tax charge of $1.15 billion recording the settlements.

As part of the settlement with the SEC, the SEC filed a civil complaint, alleging that from 2000 until 2005, AIG materially falsified its financial statements through a variety of transactions and entities in order to strengthen the appearance of its financial results to analysts and investors.

AIG, without admitting or denying the allegations in the SEC complaint, consented to the issuance of a final judgment on February 9, 2006: (a) permanently restraining and enjoining AIG from violating Section 17(a) of the Securities Act of 1933 (Securities Act) and Sections 10(b), 13(a), 13(b)(2) and 13(b)(5) and Rules 10b-5, 12b-20, 13a-1, 13a-13 and 13b2-1 of the Exchange Act; (b) ordering AIG to pay disgorgement in the amount of $700 million; and (c) ordering AIG to pay a civil penalty in the amount of $100 million. These amounts have been paid into a fund under the supervision of the SEC to be available to resolve claims asserted in various civil proceedings, including shareholder lawsuits.

In February 2006, AIG and the DOJ entered into a letter agreement. In the letter agreement, the DOJ notified AIG that in its view, AIG, acting through some of its employees, violated federal criminal law in connection with misstatements in periodic financial reports that AIG filed with the SEC between 2000 and 2004 relating to certain transactions. The settlement with the DOJ consists of, among other things, AIG's cooperating with the DOJ in the DOJ's ongoing criminal investigation, accepting responsibility for certain of its actions and those of its employees relating to these transactions and paying $25 million.

Effective February 9, 2006, AIG entered into agreements with the NYAG and the DOI, settling claims under New York's Martin Act and insurance laws, among other provisions, which were originally brought by the NYAG and the DOI in a civil complaint filed on May 26, 2005. Under the agreements, $375 million was paid into a fund under the supervision of the NYAG and the DOI to be available principally to pay certain AIG insureds who purchased excess casualty policies through Marsh & McLennan Companies, Inc. or Marsh Inc. In addition, approximately $343 million will be used to compensate participating state funds in connection with the underpayment of certain workers compensation premium taxes and other assessments. In addition, AIG paid $100 million as a fine to the State of New York.

As part of these settlements, AIG has agreed to retain for a period of three years an independent consultant who will conduct a review that will include the adequacy of AIG's internal controls over financial reporting and the remediation plan that AIG has implemented as a result of its own internal review.

PNC Settlement

In November 2004, AIG and AIGFP reached a final settlement with the SEC, the Fraud Section of the DOJ and the United States Attorney for the Southern District of Indiana with respect to issues arising from certain structured transactions entered into with Brightpoint, Inc. and The PNC Financial Services Group, Inc. (PNC), the marketing of transactions similar to the PNC transactions and related matters.

As part of the settlement, the SEC filed against AIG a civil complaint, based on the conduct of AIG primarily through AIGFP, alleging violations of certain antifraud provisions of the federal securities laws and for aiding and abetting violations of reporting and record keeping provisions of those laws. AIG, without admitting or denying the allegations in the SEC complaint, consented to the issuance of a final judgment permanently enjoining it and its employees and related persons from violating certain provisions of the Exchange Act, Exchange Act Rules and the Securities Act, ordering disgorgement of fees it received in the PNC transactions and providing for AIG to establish a transaction review committee to review the appropriateness of certain future transactions and to retain an independent consultant to examine certain transactions entered into between 2000 and 2004 and review the policies and procedures of the transaction review committee. The independent consultant has a broad mandate to review transactions entered into by AIG during this period. The review of the independent consultant is now ongoing and AIG cannot at this time predict the outcome of this review.

The DOJ filed against AIGFP PAGIC Equity Holding Corp. (AIGFP PAGIC), a wholly-owned subsidiary of AIGFP, a criminal complaint alleging that AIGFP PAGIC violated federal securities laws by aiding and abetting securities law violations by PNC, in connection with a transaction entered into in 2001 with PNC that was intended to enable PNC to remove certain assets from its balance sheet.

The settlement with the DOJ consists of separate agreements with AIG and AIGFP and a complaint filed against, and deferred prosecution agreement with, AIGFP PAGIC. Under the terms of the settlement, AIGFP paid a monetary penalty of $80 million. On January 17, 2006, the court approved an order dismissing the complaint with prejudice. The obligations of AIG, AIGFP and AIGFP PAGIC under the DOJ agreements relate principally to cooperating with the DOJ and other federal agencies in connection with their related investigations.

Investigations of Insurance Practices

Regulators from several states have commenced investigations into insurance brokerage practices related to contingent commissions and other broker-related conduct, such as alleged bid rigging. Various parties, including insureds and shareholders, have also asserted putative class action and other claims against AIG or its subsidiaries alleging, among other things, violations of the antitrust and federal securities laws, and AIG expects that additional claims may be made. Pursuant to the settlements with the NYAG and the DOI, $375 million was paid into a fund under the supervision of the NYAG and the DOI to be available principally to pay certain AIG insureds who purchased excess casualty policies through Marsh Inc. In addition, approximately $343 million will be used to compensate participating states in connection with the underpayment of certain workers compensation premium taxes and other assessments. It is likely that many of the claims arising from state investigations, as well as claims made by insureds, will be settled using these funds.

Various federal and state regulatory agencies are reviewing certain other transactions and practices of AIG and its subsidiaries in connection with industry-wide and other inquiries. AIG has cooperated, and will continue to cooperate, with all these investigations, including by producing documents and other information in response to the subpoenas.

Pending Litigation

A number of lawsuits have been filed regarding the subject matter of the investigations of insurance brokerage practices, including derivative actions, individual actions and class actions under the federal securities laws, Racketeering Influenced and Corrupt Organizations Act (RICO), Employee Retirement Income Security Act (ERISA) and state common and corporate laws in both federal and state courts, including the federal district court in the United States District Court for the Southern District of New York (Southern District of New York), in the Commonwealth of Massachusetts Superior Court and in the Delaware Chancery Court. All of these actions generally allege that AIG and its subsidiaries violated the law by allegedly concealing a scheme to "rig bids" and "steer" business between insurance companies and insurance brokers.

Since October 19, 2004, AIG or its subsidiaries have been named as a defendant in fifteen complaints that were filed in federal court and two that were originally filed in state court (Massachusetts and Florida) and removed to federal court. These cases generally allege that AIG and its subsidiaries violated federal and various state antitrust laws, as well as federal RICO laws, various state deceptive and unfair practice laws and certain state laws governing fiduciary duties. The alleged basis of these claims is that there was a conspiracy between insurance companies and insurance brokers with regard to the use of contingent commission agreements, bidding practices, and other broker-related conduct concerning coverage in certain sectors of the insurance industry. The Judicial Panel on Multidistrict Litigation entered an order on February 17, 2005, consolidating most of these cases and transferring them to the United States District Court for the District of New Jersey (District of New Jersey). The remainder of these cases have been transferred to the District of New Jersey. On August 15, 2005, the plaintiffs in the multidistrict litigation filed a Corrected First Consolidated Amended Commercial Class Action Complaint, which, in addition to the previously named AIG defendants, names new AIG subsidiaries as defendants. Also on August 15, 2005, AIG and two subsidiaries were named as defendants in a Corrected First Consolidated Amended Employee Benefits Class Action Complaint filed in the District Court of New Jersey, which asserts similar claims with respect to employee benefits insurance and a claim under ERISA on behalf of putative classes of employers and employees. On November 29, 2005, the AIG defendants, along with other insurer defendants and the broker defendants filed motions to dismiss both the Commercial and Employee Benefits Complaints. Plaintiffs have filed a motion for class certification in the consolidated action. In addition, complaints were filed against AIG and several of its subsidiaries in Massachusetts and Florida state courts, which have both been stayed. In the Florida action, the plaintiff has filed a petition for a writ of certiorari with the District Court of Appeals of the State of Florida, Fourth District with respect to the stay order. On February 9, 2006, a complaint against AIG and several of its subsidiaries was filed in Texas state court, making claims similar to those in the federal cases above.

In April and May 2005, amended complaints were filed in the consolidated derivative and securities cases, as well as in one of the ERISA lawsuits, pending in the Southern District of New York adding allegations concerning AIG's accounting treatment for non-traditional insurance products. In September 2005, a second amended complaint was filed in the consolidated securities cases adding allegations concerning AIG's First Restatement. Also in September 2005, a new securities action complaint was filed in the Southern District of New York, asserting claims premised on the same allegations made in the consolidated cases. Motions to dismiss have been filed in the securities actions. In September 2005, a consolidated complaint was filed in the ERISA case pending in the Southern District of New York. Motions to dismiss have been filed in that ERISA case. Also in April 2005, new derivative actions were filed in the Delaware Chancery Court, and in July and August 2005, two new derivative actions were filed in the Southern District of New York asserting claims duplicative of the claims made in the consolidated derivative action.

In July 2005, a second amended complaint was filed in the consolidated derivative case in the Southern District of New York, expanding upon accounting-related allegations based upon AIG's First Restatement and, in August 2005, an amended consolidated complaint was filed. In June 2005, the derivative cases in Delaware were consolidated. AIG's Board of Directors has appointed a special committee of independent directors to review the matters asserted in the derivative complaints. The courts have approved agreements staying the derivative cases pending in the Southern District of New York and in the Delaware Chancery Court while the special committee of independent directors performs its work. In September 2005, a shareholder filed suit in Delaware Chancery Court seeking documents relating to some of the allegations made in the derivative suits. AIG filed a motion to dismiss in October 2005.

In late 2002, a derivative action was filed in the Delaware Chancery Court in connection with AIG's transactions with certain entities affiliated with Starr and SICO. In May 2005, the plaintiff filed an amended complaint which adds additional claims premised on allegations relating to insurance brokerage practices and AIG's non-traditional insurance products. Plaintiffs in that case have agreed to dismiss newly added allegations unrelated to transactions with entities affiliated with Starr and SICO without prejudice to pursuit of these claims in the separate derivative actions described above. On February 16, 2006, the Delaware Chancery Court entered an order dismissing the litigation with prejudice with respect to AIG's outside directors and dismissing the claims against the remaining AIG defendants without prejudice.

On July 8, 2005, SICO filed a complaint against AIG in the Southern District of New York. The complaint alleges that AIG is in the possession of items, including artwork, which SICO claims it owns, and seeks an order causing AIG to release those items as well as actual, consequential, punitive and exemplary damages. On September 27, 2005, AIG filed its answer to SICO's complaint denying SICO's allegations and asserting counter-claims for breach of contract, unjust enrichment, conversion and breach of fiduciary duty relating to

SICO's breach of its commitment to use its AIG shares for the benefit of AIG and its employees. On October 17, 2005, SICO replied to AIG's counter-claims and additionally sought a judgment declaring that SICO is neither a control person nor an affiliate of AIG for the purposes of Schedule 13D under the Exchange Act, and Rule 144 under the Securities Act, respectively. AIG responded to the SICO claims on November 7, 2005.

Effect on AIG

In the opinion of AIG management, AIG's ultimate liability for the unresolved matters referred to above is not likely to have a material adverse effect on AIG's consolidated financial condition, although it is possible that the effect would be material to AIG's consolidated results of operations for an individual reporting period.

ITEM 4.
Submission of Matters to a Vote of Security Holders

There were no matters submitted to a vote of security holders during the fourth quarter of 2005.

Directors and Executive Officers of the Registrant

Set forth below is information concerning the directors and executive officers of AIG. All directors are elected for one-year terms at the annual meeting of shareholders. All officers serve at the pleasure of the Board of Directors, but subject to the foregoing, are elected to one-year terms.

Except as hereinafter noted, each of the executive officers has, for more than five years, occupied an executive position with AIG or companies that are now its subsidiaries. There are no other arrangements or understandings between any officer and any other person pursuant to which the officer was elected to such position. From January 2000 until joining AIG in May 2004, Mr. Frenkel served as Chairman of Merrill Lynch International, Inc. Between 1991 and 2001, Mr. Frenkel served for two consecutive terms as the Governor of the Bank of Israel. Prior to joining AIG in September 2002, Mr. Bensinger was Executive Vice President and Chief Financial Officer of Combined Specialty Group, Inc. (a division of Aon Corporation) commencing in March 2002, and served as Executive Vice President of Trenwick Group, Ltd. from October 1999 through December 2001. Prior to joining AIG in February 2005, Mr. Winans was a Vice President at Lehman Brothers Equity Research covering property-casualty insurers. Prior to joining Lehman Brothers in June 2003, he held a similar position at Williams Capital, following three years as an equity analyst covering the property-casualty sector at Morgan Stanley and previously at Paine Webber, which he joined in late 1999. From May 1985 until joining AIG, Mr. Roemer was employed by JPMorgan Chase, most recently as Senior Vice President – Internal Audit.

Name	Title	Age	Served as Director or Officer Since
M. Bernard Aidinoff	Director	77	1984
Pei-yuan Chia	Director	67	1996
Marshall A. Cohen	Director	70	1992
William S. Cohen	Director	65	2004
Martin S. Feldstein	Director	66	1987
Ellen V. Futter	Director	56	1999
Stephen L. Hammerman	Director	67	2005
Carla A. Hills	Director	72	1993
Richard C. Holbrooke	Director	64	2001
Fred H. Langhammer	Director	62	2006
George L. Miles, Jr.	Director	64	2005
Morris W. Offit	Director	69	2005
Martin J. Sullivan	Director, President and Chief Executive Officer	51	2002
Michael H. Sutton	Director	65	2005
Edmund S. W. Tse	Director, Senior Vice Chairman – Life Insurance	68	1996
Robert B. Willumstad	Director	60	2006
Frank G. Zarb	Director and Chairman	71	2001
Thomas R. Tizzio	Senior Vice Chairman – General Insurance	68	1982
Jacob A. Frenkel	Vice Chairman – Global Economic Strategies	62	2004
Frank G. Wisner	Vice Chairman – External Affairs	67	1997
Steven J. Bensinger	Executive Vice President and Chief Financial Officer	51	2002
Rodney O. Martin, Jr.	Executive Vice President – Life Insurance	53	2002
Kristian P. Moor	Executive Vice President – Domestic General Insurance	46	1998
Win J. Neuger	Executive Vice President and Chief Investment Officer	56	1995
R. Kendall Nottingham	Executive Vice President – Life Insurance	67	1998
Robert M. Sandler	Executive Vice President – Domestic Personal Lines	63	1980
Nicholas C. Walsh	Executive Vice President – Foreign General Insurance	55	2005
Jay S. Wintrob	Executive Vice President – Retirement Services	48	1999
William N. Dooley	Senior Vice President – Financial Services	53	1992
Axel I. Freudmann	Senior Vice President – Human Resources	59	1986
David L. Herzog	Senior Vice President and Comptroller	46	2005
Robert E. Lewis	Senior Vice President and Chief Risk Officer	54	1993
Ernest T. Patrikis	Senior Vice President and General Counsel	61	1998
Michael E. Roemer	Senior Vice President and Director of Internal Audit	43	2005
Brian T. Schreiber	Senior Vice President – Strategic Planning	40	2002
Richard W. Scott	Senior Vice President – Investments	52	2002
Kathleen E. Shannon	Senior Vice President and Secretary	56	1986
Keith L. Duckett	Vice President – Administration	45	2001
Robert A. Gender	Vice President and Treasurer	48	2005
Charlene M. Hamrah	Vice President and Director of Investor Relations	58	2004

Name	Title	Age	Served as Director or Officer Since
Peter K. Lathrop	Vice President and Director of Taxes	63	2001
Eric N. Litzky	Vice President – Corporate Governance	44	2005
Christopher D. Winans	Vice President – Media Relations	55	2005

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

(a) AIG's common stock is listed in the U.S. on the New York Stock Exchange, as well as the stock exchanges in London, Paris, Switzerland and Tokyo.

The table below shows the high and low closing sales prices per share of AIG's common stock on the New York Stock Exchange Composite Tape, for each quarter of 2005 and 2004.

	2005		2004	
	High	Low	High	Low
First quarter	**$73.46**	**$54.18**	$75.12	$66.79
Second quarter	**58.94**	**49.91**	76.77	69.39
Third quarter	**63.73**	**56.00**	72.66	66.48
Fourth quarter	**64.40**	**60.43**	68.72	54.70

(b) In 2005, AIG paid a quarterly dividend of 12.5 cents in March and June and 15.0 cents in September and December for a total cash payment of 55.0 cents per share of common stock. In 2004, AIG paid a quarterly dividend of 6.5 cents in March and June and 7.5 cents in September and December for a total cash payment of 28.0 cents per share of common stock. Subject to the dividend preference of any of AIG's serial preferred stock which may be outstanding, the holders of shares of common stock are entitled to receive such dividends as may be declared by the Board of Directors from funds legally available therefor.

See Note 11(a) of Notes to Financial Consolidated Statements for a discussion of certain restrictions on the payment of dividends to AIG by some of its insurance subsidiaries.

(c) The approximate number of holders of common stock as of January 31, 2006, based upon the number of record holders, was 56,000.

(d) The following table summarizes AIG's stock repurchases for the three month period ended December 31, 2005:

Period	Total Number of Shares Purchased*(a)(b)*	Average Price Paid per Share	Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs	Maximum Number of Shares that May Yet Be Purchased Under the Plans or Programs at End of Month*(b)*
October 1 - 31, 2005	–	$ –	–	36,542,700
November 1 - 30, 2005	–	–	–	36,542,700
December 1 - 31, 2005	–	–	–	36,542,700
Total	–	$ –	–	

(a) Does not include 76,829 shares delivered or attested to in satisfaction of the exercise price by holders of AIG employee stock options exercised during the three months ended December 31, 2005.

(b) On July 19, 2002, AIG announced that its Board of Directors had authorized the open market purchase of up to 10 million shares of common stock. On February 13, 2003, AIG announced that the Board had expanded the existing program through the authorization of an additional 50 million shares. The purchase program has no set expiration or termination date.

ITEM 6.
Selected Financial Data

AMERICAN INTERNATIONAL GROUP, INC. AND SUBSIDIARIES
SELECTED CONSOLIDATED FINANCIAL DATA

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

Years Ended December 31, *(in millions, except per share data)*	**2005**	2004	2003	2002	2001
Revenues[a]:					
Premiums and other considerations	**$ 70,209**	$ 66,625	$ 54,802	$ 44,289	$ 38,261
Net investment income	**22,165**	18,465	15,508	13,593	13,002
Realized capital gains (losses)	**341**	44	(442)	(1,653)	(910)
Other revenues[b]	**16,190**	12,532	9,553	9,942	9,605
Total revenues	**108,905**	97,666	79,421	66,171	59,958
Benefits and expenses:					
Incurred policy losses and benefits	**63,711**	58,360	46,034	40,005	33,984
Insurance acquisition and other operating expenses	**29,981**	24,461	21,480	18,358	18,040
Acquisition, restructuring and related charges	**–**	–	–	–	2,017
Total benefits and expenses	**93,692**	82,821	67,514	58,363	54,041
Income before income taxes, minority interest and cumulative effect of accounting changes[c]	**15,213**	14,845	11,907	7,808	5,917
Income taxes	**4,258**	4,407	3,556	1,919	1,594
Income before minority interest and cumulative effect of accounting changes	**10,955**	10,438	8,351	5,889	4,323
Minority interest	**(478)**	(455)	(252)	(160)	(101)
Income before cumulative effect of accounting changes	**10,477**	9,983	8,099	5,729	4,222
Cumulative effect of accounting changes, net of tax	**–**	(144)	9	–	(136)
Net income	**10,477**	9,839	8,108	5,729	4,086
Earnings per common share:					
Basic					
Income before cumulative effect of accounting changes	**4.03**	3.83	3.10	2.20	1.61
Cumulative effect of accounting changes, net of tax	**–**	(0.06)	–	–	(0.05)
Net income	**4.03**	3.77	3.10	2.20	1.56
Diluted[d]					
Income before cumulative effect of accounting changes	**3.99**	3.79	3.07	2.17	1.59
Cumulative effect of accounting changes, net of tax	**–**	(0.06)	–	–	(0.05)
Net income	**3.99**	3.73	3.07	2.17	1.54
Dividends per common share[e]	**0.63**	0.29	0.24	0.18	0.16
Total assets	**853,370**	801,145	675,602	561,598	490,614
Long-term debt and commercial paper[f]					
Guaranteed by AIG	**10,425**	8,498	7,469	7,144	8,141
Liabilities connected to trust preferred stock	**1,391**	1,489	1,682	–	–
Matched/not guaranteed by AIG	**98,033**	86,912	71,198	63,866	56,073
Total Liabilities[g]	**766,867**	721,273	606,180	501,163	438,551
Shareholders' equity	**$ 86,317**	$ 79,673	$ 69,230	$ 58,303	$ 49,881

(a) Represents the sum of General Insurance net premiums earned, Life Insurance & Retirement Services GAAP premiums, net investment income, Financial Services interest, lease and finance charges, Asset Management advisory and management fees and net investment income from guaranteed investment contracts, and realized capital gains (losses).

(b) Includes the effect of hedging activities that do not qualify for hedge accounting treatment under FAS 133, including the related foreign exchange gains and losses. For 2005, 2004, 2003, 2002 and 2001, respectively, the amounts included are $2.01 billion, $(122) million, $(1.01) billion, $220 million and $56 million.

(c) Includes catastrophe losses of $3.28 billion in 2005, $1.16 billion in 2004, $83 million in 2003, $61 million in 2002 and World Trade Center losses of $900 million in 2001.

(d) Assumes conversion of contingently convertible bonds due to the adoption of EITF Issue No. 04-8 "Accounting Issues Related to Certain Features of Contingently Convertible Debt and the Effect on Diluted Earnings per Share."

(e) Dividends have not been restated to reflect dividends paid by AGC which was acquired by AIG on August 29, 2001.

(f) Including that portion of long-term debt maturing in less than one year. See also Note 9 of Notes to Consolidated Financial Statements.

(g) Includes $2.1 billion and $2.2 billion for the years ended 2002 and 2001, respectively, of other liabilities connected to the consolidation of the Muni Tender Option Bond Program trusts.

Management's Discussion and Analysis of Financial Condition and Results of Operations

ITEM 7.

Management's Discussion and Analysis of Financial Condition and Results of Operations

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

Management's Discussion and Analysis of Financial Condition and Results of Operations

Management's Discussion and Analysis of Financial Condition and Results of Operations is designed to provide the reader a narrative with respect to AIG's operations, financial condition and liquidity and certain other significant matters.

Cautionary Statement Regarding Projections and Other Information About Future Events

This Annual Report on Form 10-K and other publicly available documents may include, and AIG's officers and representatives may from time to time make, projections concerning financial information and statements concerning future economic performance and events, plans and objectives relating to management, operations, products and services, and assumptions underlying these projections and statements. These projections and statements are not historical facts but instead represent only AIG's belief regarding future events, many of which, by their nature, are inherently uncertain and outside AIG's control. These projections and statements may address, among other things, the status and potential future outcome of the current regulatory and civil proceedings against AIG and their potential effect on AIG's businesses, financial position, results of operations, cash flows and liquidity, the effect of the credit rating downgrades on AIG's businesses and competitive position, the unwinding and resolving of various relationships between AIG and Starr and SICO and AIG's strategy for growth, product development, market position, financial results and reserves. It is possible that AIG's actual results and financial condition may differ, possibly materially, from the anticipated results and financial condition indicated in these projections and statements. Factors that could cause AIG's actual results to differ, possibly materially, from those in the specific projections and statements are discussed throughout this Management's Discussion and Analysis of Financial Condition and Results of Operations and in "Risk Factors" in Item 1A, Part I of this Annual Report on Form 10-K. AIG is not under any obligation (and expressly disclaims any such obligations) to update or alter any projection or other statement, whether written or oral, that may be made from time to time, whether as a result of new information, future events or otherwise.

Overview of Operations and Business Results

In 2003 and prior years, AIG's operations were conducted by its subsidiaries principally through four operating segments: General Insurance, Life Insurance, Financial Services and Retirement Services & Asset Management. Beginning with the first quarter of 2004, AIG reports Retirement Services results in the same segment as Life Insurance, reflecting the convergence of protective financial and retirement products and AIG's current management of these operations. All financial information herein gives effect to the Restatements described in "The Restatements" under Item 1. Business. Information for years prior to 2005 included herein has been reclassified to show AIG's results of operations and financial position on a comparable basis with the 2005 presentation.

Through these segments, AIG provides insurance and investment products and services to both businesses and individuals in more than 130 countries and jurisdictions. This geographic, product and service diversification is one of AIG's major strengths and sets it apart from its competitors. The importance of this diversification was especially evident in 2005, when record catastrophe losses, settlements of legal proceedings and charges for increases in reserves for loss and loss expenses, were more than offset by profitability in other segments and product lines. Although regional economic downturns or political upheaval could negatively affect parts of AIG's operations, AIG believes that its diversification makes it unlikely that regional difficulties would have a material effect on its operating results, financial condition or liquidity.

AIG's subsidiaries serve commercial, institutional and individual customers through an extensive property-casualty and life insurance and retirement services network. In the United States, AIG companies are the largest underwriters of commercial and industrial insurance and one of the largest life insurance and retirement services operations as well. AIG's Financial Services businesses include commercial aircraft and equipment leasing, capital markets operations and consumer finance, both in the United States and abroad. AIG also provides asset management services and offers guaranteed investment contracts (GICs) to institutions and individuals.

A primary goal of AIG in managing its General Insurance operations is to achieve an underwriting profit. To achieve this goal, AIG must be disciplined in its risk selection and premiums must be adequate and terms and conditions appropriate to cover the risk accepted. AIG believes in strict control of expenses.

AIG's 2005 operating performance reflects continuing implementation of various long-term strategies in its various operating segments.

A central focus of AIG operations in recent years is the development and expansion of new distribution channels. In 2005, AIG continued to expand its distribution channels in many Asian countries, which now include banks, credit card companies and television-media home shopping. In late 2003, AIG entered into an agreement with PICC Property and Casualty Company, Limited (PICC), which will enable the marketing of accident and health products throughout China through PICC's branch networks and agency system. AIG participates in the underwriting results through a reinsurance agreement and also holds a 9.9 percent ownership interest in PICC. Other examples of new distribution channels used both domestically and overseas include banks, affinity groups, direct response and e-commerce.

AIG patiently builds relationships in markets around the world where it sees long-term growth opportunities. For example, the fact that AIG has the only wholly-owned foreign life insurance operations in eight cities in China is the result of relationships developed over nearly 30 years. AIG's more recent expansion of operations into India, Vietnam, Russia and other emerging markets reflect the same growth strategy. Moreover, AIG believes in investing in the economies and infrastructures of these countries and growing with them. When AIG companies enter a new jurisdiction, they typically offer both basic protection and savings products. As the economies evolve, AIG's products evolve with them, to more complex and investment-oriented models.

Growth for AIG may be generated both internally and through acquisitions which both fulfill strategic goals and offer adequate return on investment. In recent years, the acquisitions of AIG Star Life and AIG Edison Life have broadened AIG's penetration of the Japanese market through new distribution channels and will result in operating efficiencies as they are integrated into AIG's previously existing companies operating in Japan.

AIG provides leadership on issues of concern to the global and local economies as well as the insurance and financial services industries. In recent years, efforts to reform the tort system and class action litigation procedures, legislation to deal with the asbestos problem and the renewal of the Terrorism Risk Insurance Act have been key issues, while in prior years trade legislation and Superfund had been issues of concern.

The following table summarizes AIG's revenues, income before income taxes, minority interest and cumulative effect of accounting changes and net income for the twelve months ended December 31, 2005, 2004 and 2003:

Years Ended December 31, *(in millions)*	**2005**	2004	2003
Total revenues	**$108,905**	$97,666	$79,421
Income before income taxes, minority interest and cumulative effect of accounting changes	**15,213**	14,845	11,907
Net income	**$ 10,477**	$ 9,839	$ 8,108

Consolidated Results

The 12 percent growth in revenues in 2005 and 23 percent growth in revenues in 2004 were primarily attributable to the growth in net premiums earned from global General Insurance operations as well as growth in both General Insurance and Life Insurance & Retirement Services net investment income and Life Insurance & Retirement Services GAAP premiums. An additional factor was the capital gains realized in 2004 rather than the capital losses realized in 2003.

AIG's income before income taxes, minority interest and cumulative effect of accounting changes increased 2 percent in 2005 when compared to 2004 and 25 percent in 2004 when compared to 2003. Life Insurance & Retirement Services, Financial Services and Asset Management operating income gains accounted for the increase over 2004 and 2003 in both pretax income and net income. Somewhat offsetting these gains in 2005 was the effect of the charges related to regulatory settlements, as described in Item 3. Legal Proceedings.

The following table summarizes the net effect of catastrophe losses for December 31, 2005, 2004 and 2003.

(in millions)	**2005**	2004	2003
Pretax(*)	**$ 3,280**	$ 1,155	$ 83
Net of tax and minority interest	**2,109**	729	53

(*) Includes $312 million and $96 million in catastrophe losses from partially owned companies in 2005 and 2004, respectively.

The following table summarizes the operations of each principal segment for the twelve months ended December 31, 2005, 2004 and 2003. See also Note 2 of Notes to Consolidated Financial Statements.

(in millions)	**2005**	2004	2003
Revenues[a]:			
General Insurance[b]	**$ 45,174**	$41,961	$33,833
Life Insurance & Retirement Services[c]	**47,316**	43,400	36,678
Financial Services[d]	**10,525**	7,495	6,242
Asset Management[e]	**5,325**	4,714	3,651
Other	**565**	96	(983)
Total	**$108,905**	$97,666	$79,421
Operating Income[a][f][g]:			
General Insurance	**$ 2,315**	$ 3,177	$ 4,502
Life Insurance & Retirement Services	**8,844**	7,923	6,807
Financial Services	**4,276**	2,180	1,182
Asset Management	**2,253**	2,125	1,316
Other[h][i]	**(2,475)**	(560)	(1,900)
Total	**$ 15,213**	$14,845	$11,907

(a) Includes the effect of hedging activities that do not qualify for hedge accounting treatment under FAS 133, including the related foreign exchange gains and losses. For 2005, 2004 and 2003, the effect was $(34) million, $(27) million and $49 million, respectively, in operating income for Aircraft Finance and $2.01 billion, $(122) million and $(1.01) billion in revenues and operating income, respectively, for Capital Markets (AIGFP).

(b) Represents the sum of General Insurance net premiums earned, net investment income and realized capital gains (losses).

(c) Represents the sum of Life Insurance & Retirement Services GAAP premiums, net investment income and realized capital gains (losses). Included in realized capital gains (losses) is the effect of hedging activities that do not qualify for hedge accounting treatment under FAS 133 and the application of FAS 52 of $(437) million, $(140) million and $78 million.

(d) Represents interest, lease and finance charges.

(e) Represents management and advisory fees, and net investment income with respect to GICs.

(f) Represents income before income taxes, minority interest, and cumulative effect of accounting changes.

(g) Catastrophe losses were $3.28 billion, $1.16 billion and $83 million in 2005, 2004 and 2003, respectively.

(h) Represents unallocated corporate expenses and other realized capital gains (losses) and includes the NYAG, DOI, SEC and DOJ settlement costs in 2005.

(i) Includes $312 million and $96 million in catastrophe related losses from partially owned companies in 2005 and 2004, respectively, and approximately $1.6 billion of regulatory settlement charges in 2005.

General Insurance

AIG's General Insurance operations provide property and casualty products and services throughout the world. The decrease in General Insurance operating income in 2005 compared to 2004 was primarily attributable to catastrophe related losses, increases in the reserve for losses and loss expenses and changes in estimates related to the remediation of AIG's material weakness in control over certain balance sheet reconciliations, partially offset by profitable growth in Foreign General's underwriting results and DBG's and Foreign General's net investment income. In addition, realized capital gains increased in 2005 compared to 2004. General Insurance operating income includes $2.89 billion, $1.05 billion and $83 million in catastrophe related losses in 2005, 2004 and 2003, respectively. DBG's operating income included $197 million of additional losses in 2005 resulting from increased labor and material costs related to the 2004 Florida hurricanes.

Life Insurance & Retirement Services

AIG's Life Insurance & Retirement Services operations provide insurance, financial and investment products throughout the world. Foreign operations provided approximately 59 percent and 61 percent of AIG's Life Insurance & Retirement Services operating income in 2005 and 2004, respectively.

Life Insurance & Retirement Services operating income increased 12 percent in 2005 and 16 percent in 2004 when compared to 2003. Foreign Life Insurance & Retirement Services operating income grew 8 percent in 2005. Realized capital gains included in operating income was $84 million in 2005 compared to $372 million in 2004 and $486 million in 2003. The decline in realized capital gains in 2005 includes the effect of hedging activities that do not qualify for hedge accounting under FAS 133, including the related foreign exchange gains and losses under FAS 52. For 2005, the foreign Life & Retirement Service segment also incurred higher policy benefit costs for contributions to the participating policyholder fund in Singapore, totaling $137 million related to the settlement of a long disputed local tax issue. The domestic Life Insurance & Retirement Services segment operating income grew by 17 percent in 2005. Realized capital losses included in operating income was $(302) million in 2005 compared to $(329) million in 2004 and $(246) million in 2003. The 2004 results include increased policy benefits of $178 million associated with the workers compensation arbitration with Superior National. The domestic Life Insurance & Retirement

Services segment also includes $12 million and $5 million in catastrophe related losses in 2005 and 2004, respectively.

Financial Services

AIG's Financial Services subsidiaries engage in diversified activities including aircraft and equipment leasing, capital markets transactions, consumer finance and insurance premium financing.

Financial Services operating income increased significantly in 2005 compared to 2004 and in 2004 compared to 2003, primarily due to the fluctuation in earnings resulting from not qualifying for hedge accounting treatment under FAS 133. Offsetting this increase in 2004 when compared to 2003 is the effect of ILFC's disposition of approximately $2 billion in aircraft through securitizations in the third quarter of 2003 and the first quarter of 2004. Fluctuations in revenues and operating income from quarter to quarter are not unusual because of the transaction-oriented nature of Capital Markets operations and the effect of not qualifying for hedge accounting treatment under FAS 133 for hedges on securities available for sale and borrowings. The increase in 2005 when compared to 2004 was partially offset by $62 million in catastrophe related losses in the Consumer Finance operations in 2005. The charge relating to the PNC settlement, see Item 3. Legal Proceedings, had a significant negative effect on results in 2004. Consumer Finance operations increased revenues and operating income, both domestically and internationally.

Asset Management

AIG's Asset Management operations include institutional and retail asset management and broker dealer services and spread-based investment business from the sale of GICs. These products and services are offered to individuals and institutions, both domestically and overseas.

Asset Management operating income increased 6 percent in 2005 when compared to 2004 as a result of the upturn in worldwide financial markets and a strong global product portfolio; operating income also increased 61 percent in 2004 when compared to 2003 as a result of the same factors.

Capital Resources

At December 31, 2005, AIG had total consolidated shareholders' equity of $86.32 billion and total consolidated borrowings of $109.85 billion. At that date, $99.42 billion of such borrowings were either not guaranteed by AIG or were matched borrowings under obligations of guaranteed investment agreements (GIAs), liabilities connected to trust preferred stock, or matched notes and bonds payable.

During 2005, AIG repurchased in the open market 2,477,100 shares of its common stock.

Liquidity

At December 31, 2005, AIG's consolidated invested assets included $17.24 billion in cash and short-term investments. Consolidated net cash provided from operating activities in 2005 amounted to $25.14 billion. AIG believes that its liquid assets, cash provided by operations and access to short term funding through commercial paper and bank credit facilities will enable it to meet any anticipated cash requirements.

Outlook

From March through June of 2005, the major rating agencies downgraded AIG's ratings in a series of actions. S&P lowered the long-term senior debt and counterparty ratings of AIG from 'AAA' to 'AA' and changed the rating outlook to negative. Moody's lowered AIG's long-term senior debt rating from 'Aaa' to 'Aa2' and changed the outlook to stable. Fitch downgraded the long-term senior debt ratings of AIG from 'AAA' to 'AA' and placed the ratings on Rating Watch Negative.

The agencies also took rating actions on AIG's insurance subsidiaries. S&P and Fitch lowered to 'AA+' the insurance financial strength ratings of most of AIG's insurance companies. Moody's lowered the insurance financial strength ratings generally to either 'Aa1' or 'Aa2'. A.M. Best downgraded the financial strength ratings for most of AIG's insurance subsidiaries from 'A++' to 'A+' and the issuer credit ratings from 'aa+' to 'aa–'. Many of these companies' ratings remain on a negative watch.

In addition, S&P changed the outlook on ILFC's 'AA–' long-term senior debt rating to negative. Moody's affirmed ILFC's long-term and short-term senior debt ratings ('A1'/'P-1'). Fitch downgraded ILFC's long-term senior debt rating from 'AA–' to 'A+' and placed the rating on Rating Watch Negative and downgraded ILFC's short-term debt rating from 'F1+' to 'F1'. Fitch also placed the 'A+' long-term senior debt ratings of American General Finance Corporation and American General Finance, Inc. on Rating Watch Negative. S&P and Moody's affirmed the long-term and short-term senior debt ratings of American General Finance Corporation at 'A+'/'A-1' and 'A1'/'P-1', respectively.

These debt and financial strength ratings are current opinions of the rating agencies. As such, they may be changed, suspended or withdrawn at any time by the rating agencies as a result of changes in, or unavailability of, information or based on other circumstances. Ratings may also be withdrawn at AIG management's request. This discussion of ratings is not a complete list of ratings of AIG and its subsidiaries. For a discussion of the effect of these ratings downgrades on AIG's businesses, see "Risk Factors — AIG's Credit Ratings" in Item 1A. Risk Factors.

Despite industry price erosion in some classes of general insurance, AIG expects to continue to identify profitable opportunities and build attractive new General Insurance businesses as a result of AIG's broad product line and extensive distribution networks. In December 2005, AIUO received a license from the government of Vietnam to operate a wholly owned general insurance company in Vietnam. This license, the first general insurance license granted by Vietnam to a U.S.-based insurance organization, permits AIG to operate a general insurance company throughout Vietnam. In early 2006, AIG announced plans to acquire a leading general insurance company in Taiwan.

In China, AIG has wholly-owned life insurance operations in eight cities. These operations should benefit from China's rapid rate of economic growth and growing middle class, a segment that is a prime market for life insurance. AIG believes that it may also have opportunities in the future to grow by entering the group insurance business. However, in March 2005 it withdrew its application to serve the group insurance market until certain regulatory issues are resolved. Among the regulatory issues to be addressed is the response to AIG's acknowledgment that certain of its Hong Kong based agents sold life insurance to customers on the Chinese mainland in contravention of applicable regulations.

AIG Edison Life, acquired in August 2003, adds to the current agency force in Japan, and provides alternative distribution channels including banks, financial advisers, and corporate and government employee relationships. In January 2005, AIG Star Life entered into an agreement with the Bank of Tokyo Mitsubishi, one of Japan's largest banks, to market a multi-currency fixed annuity. Through ALICO, AIG Star Life and AIG Edison, AIG has developed a leadership position in the distribution of annuities through banks. AIG is also a leader in the direct marketing of insurance products through sponsors and in the broad market. AIG also expects continued growth in India, Korea and Vietnam.

Domestically, AIG anticipates continued operating growth in 2006 as distribution channels are expanded and new products are introduced. The home service operation has not met business objectives, although its cash flow has been strong, and domestic group life/health continues to be weak. The home service operation is expected to be a slow growth business. AIG American General's current ratings remain equal to or higher than many of its principal competitors. AIG American General competes with a variety of companies based on services and products, in addition to ratings. The recent rating actions appear to be having no negative long term effect on independent producer relationships or customer surrender activity.

In the airline industry, changes in market conditions are not immediately apparent in operating results. Lease rates have firmed considerably, as a result of strong demand spurred by the recovering global commercial aviation market, especially in Asia. Sales have begun to increase, and AIG expects an increasing level of interest from a variety of purchasers. AIG also expects increased contributions to Financial Services revenues and income from its consumer finance operations overseas. However, the downgrades of AIG's credit ratings may adversely affect funding costs for AIG and its subsidiaries and AIGFP's ability to engage in derivative transactions and certain structured products. See "Risk Factors – AIG's Credit Ratings" in Item 1A. Risk Factors.

GICs, which are sold domestically and abroad to both institutions and individuals, are written on an opportunistic basis when market conditions are favorable. In September 2005, AIG launched a $10 billion matched investment program in the Euromarkets under which AIG debt securities will be issued. AIG also expects to launch a matched investment program in the domestic market which, along with the Euro program, will become AIG's principal spread-based investment activity. However, the timing of the launch of the domestic program is uncertain. Because AIG's credit spreads in the capital markets have widened following the ratings declines, there may be a reduction in the earnings on new business in AIG's spread based funding businesses.

AIG has many promising growth initiatives underway around the world. Cooperative agreements such as those with PICC and various banks in the U.S., Japan and Korea are expected to expand distribution networks for AIG's products and provide models for future growth.

For a description of the risk factors that may affect these operations and initiatives, see Item 1A. Risk Factors.

Critical Accounting Estimates

AIG considers its most critical accounting estimates those with respect to reserves for losses and loss expenses, future policy benefits for life and accident and health contracts, deferred policy acquisition costs, estimated gross profits for investment-oriented products, fair value determinations for certain Capital Markets assets and liabilities, other-than-temporary declines in the value of investments and flight equipment recoverability. These accounting estimates require the use of assumptions about matters, some of which are highly uncertain at the time of estimation. To the extent actual experience differs from the assumptions used, AIG's results of operations would be directly affected.

Throughout this Management's Discussion and Analysis of Financial Condition and Results of Operations, AIG's critical accounting estimates are discussed in detail. The major categories for which assumptions are developed and used to establish each critical accounting estimate are highlighted below.

RESERVES FOR LOSSES AND LOSS EXPENSES (GENERAL INSURANCE):

- *Loss trend factors:* used to establish expected loss ratios for subsequent accident years based on premium rate adequacy and the projected loss ratio with respect to prior accident years.
- *Expected loss ratios for the latest accident year:* in this case, accident year 2005 for the year end 2005 loss reserve analysis. For low-frequency, high-severity classes such as excess casualty and D&O, expected loss ratios generally are utilized for at least the three most recent accident years.
- *Loss development factors:* used to project the reported losses for each accident year to an ultimate amount.

FUTURE POLICY BENEFITS FOR LIFE AND ACCIDENT AND HEALTH CONTRACTS (LIFE INSURANCE & RETIREMENT SERVICES):

- *Interest rates:* which vary by geographical region, year of issuance and products.
- *Mortality, morbidity and surrender rates:* based upon actual experience by geographical region modified to allow for variation in policy form.

ESTIMATED GROSS PROFITS (LIFE INSURANCE & RETIREMENT SERVICES):

Estimated gross profits to be realized over the estimated duration of the contracts (investment-oriented products) affect the carrying value of deferred policy acquisition costs under FAS 97. Estimated gross profits include investment income and gains and losses on investments less required interest, actual mortality and other expenses.

DEFERRED POLICY ACQUISITION COSTS (LIFE INSURANCE & RETIREMENT SERVICES):

- Recoverability based on current and future expected profitability, which is affected by interest rates, foreign exchange rates, mortality experience, and policy persistency.

DEFERRED POLICY ACQUISITION COSTS (GENERAL INSURANCE):

- Recoverability and eligibility based upon the current terms and profitability of the underlying insurance contracts.

FAIR VALUE DETERMINATIONS OF CERTAIN ASSETS AND LIABILITIES (FINANCIAL SERVICES):

- *Valuation models:* utilizing factors, such as market liquidity and current interest, foreign exchange and volatility rates.
- *Pricing data:* AIG attempts to secure reliable and independent current market price data, such as published exchange rates from external subscription services such as Bloomberg or Reuters or third-party broker quotes for use in its models. When such prices are not available, AIG uses an internal methodology, which includes interpolation and extrapolation from verifiable prices from trades occurring on dates nearest to the dates of the transactions.

OTHER-THAN-TEMPORARY DECLINES IN THE VALUE OF INVESTMENTS:

Securities are considered a candidate for other-than-temporary impairment based upon the following criteria:

- Trading at a significant (25 percent or more) discount to par or amortized cost (if lower) for an extended period of time (nine months or longer).
- The occurrence of a discrete credit event resulting in the debtor defaulting or seeking bankruptcy or insolvency protection or voluntary reorganization.
- The probability of non-realization of a full recovery on its investment, irrespective of the occurrence of one of the foregoing events.

FLIGHT EQUIPMENT — RECOVERABILITY (FINANCIAL SERVICES)

- *Expected undiscounted future net cash flows:* based upon current lease rates, projected future lease rates and estimated terminal values of each aircraft based on third party information.

Operating Review

General Insurance Operations

AIG's General Insurance subsidiaries are multiple line companies writing substantially all lines of property and casualty insurance both domestically and abroad. See "General Insurance Operations" in Item 1. Business for more information relating to General Insurance subsidiaries.

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

A critical discipline of a successful general insurance business is the objective to produce operating income from underwriting exclusive of investment-related income. When underwriting is not profitable, premiums are inadequate to pay for insured losses and underwriting related expenses. In these situations, the addition of general insurance related investment income and realized capital gains may, however, enable a general insurance business to produce operating income. For these reasons, AIG views underwriting profit to be critical in the overall evaluation of performance. Although in and of itself not a GAAP measurement, AIG believes that underwriting profit is a useful and meaningful disclosure. See also the discussion under "Liquidity" herein.

Underwriting profit is measured in two ways: statutory underwriting profit and GAAP underwriting profit.

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

GAAP accounting requires the recognition of expenses at the same time revenues are earned, the accounting principle of matching. Therefore, to convert underwriting results to a GAAP basis, acquisition expenses are deferred (deferred policy acquisition costs (DAC)) and amortized over the period the related net premiums written are earned. Accordingly, the statutory underwriting profit has been adjusted as a result of acquisition expenses being deferred as required by GAAP. DAC is reviewed for recoverability, and such review requires management judgment. See also "Critical Accounting Estimates" herein and Notes 1 and 4 of Notes to Consolidated Financial Statements.

AIG, along with most General Insurance companies, uses the loss ratio, the expense ratio and the combined ratio as measures of underwriting performance. The loss ratio is the sum of losses and loss expenses incurred divided by net premiums earned. The expense ratio is statutory underwriting expenses divided by net premiums written. The combined ratio is the sum of the loss ratio and the expense ratio. These ratios are relative measurements that describe, for every $100 of net premiums earned or written, the cost of losses and statutory expenses, respectively. The combined ratio presents the total

cost per $100 of premium production. A combined ratio below 100 demonstrates underwriting profit; a combined ratio above 100 demonstrates underwriting loss.

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

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

General Insurance operating income is comprised of underwriting profit (loss), net investment income and realized capital gains and losses. These components, as well as net premiums written, net premiums earned and statutory ratios for 2005, 2004 and 2003 were as follows:

(in millions, except ratios)	**2005**	2004	2003
Net premiums written:			
Domestic General			
DBG	**$23,128**	$22,506	$19,563
Transatlantic	**3,466**	3,749	3,341
Personal Lines	**4,653**	4,354	3,732
Mortgage Guaranty	**628**	607	531
Foreign General	**9,997**	9,407	7,864
Total	**$41,872**	$40,623	$35,031
Net premiums earned:			
Domestic General			
DBG	**$22,602**	$21,215	$16,704
Transatlantic	**3,385**	3,661	3,171
Personal Lines	**4,634**	4,291	3,678
Mortgage Guaranty	**533**	539	496
Foreign General[f]	**9,655**	8,831	7,257
Total	**$40,809**	$38,537	$31,306
Underwriting profit (loss)[a]:			
Domestic General			
DBG	**$ (3,250)**[b][c]	$ (1,340)	$ 387
Transatlantic	**(420)**	(47)	109
Personal Lines	**(19)**	160	183
Mortgage Guaranty	**241**	278	264
Foreign General[e][f]	**1,398**	702	1,032
Total	**$ (2,050)**[d]	$ (247)	$ 1,975
Net investment income:			
Domestic General			
DBG	**$ 2,403**	$ 1,965	$ 1,433
Transatlantic	**343**	307	271
Personal Lines	**217**	186	152
Mortgage Guaranty	**123**	120	142
Intercompany adjustments and eliminations – net	**1**	–	7
Foreign General	**944**	618	561
Total	**$ 4,031**	$ 3,196	$ 2,566
Realized capital gains (losses)	**334**	228	(39)
Operating income[a]	**$ 2,315**[b][c][d]	$ 3,177	$ 4,502

(in millions, except ratios)	**2005**	2004	2003
Domestic General:			
Loss ratio	**89.59**	83.88	78.35
Expense ratio	**21.00**	19.21	17.25
Combined ratio	**110.59**	103.09	95.60
Foreign General:			
Loss ratio	**53.66**	61.61	55.52
Expense ratio[e]	**31.90**	29.20	27.82
Combined ratio[f]	**85.56**	90.81	83.34
Consolidated:			
Loss ratio	**81.09**	78.78	73.06
Expense ratio	**23.60**	21.52	19.62
Combined ratio[a]	**104.69**	100.30	92.68

(a) The effect of catastrophe related losses on the consolidated General Insurance combined ratio for 2005, 2004 and 2003 was 7.06, 2.74 and 0.27, respectively. Catastrophe related losses for 2005, 2004 and 2003 by reporting unit were as follows:

(in millions)	**2005**		2004	2003
Reporting Unit	**Insurance Related Losses**	**Net Reinstatement Premium Cost**	Insurance Related Losses	Insurance Related Losses
DBG	**$ 1,747**	**$ 122**	$ 582	$48
Transatlantic	**463**	**45**	215	4
Personal Lines	**112**	**2**	25	5
Mortgage Guaranty	**10**	**–**	–	–
Foreign General	**293**	**94**	232	26
Total	**$ 2,625**	**$ 263**	$1,054	$83

(b) Includes $197 million of additional losses incurred resulting from increased labor and material costs related to the 2004 Florida hurricanes.

(c) The 2005 operating loss for DBG includes $291 million of expenses related to changes in estimates for uncollectible reinsurance and other premium balances and $100 million of accrued expenses in connection with certain workers compensation insurance policies written between 1985 and 1996. See Note 12(i) of Notes to Consolidated Financial Statements.

(d) Includes the fourth quarter 2005 increase in net reserves of approximately $1.8 billion.

(e) Includes the results of wholly owned AIU agencies.

(f) Income statement accounts expressed in non-functional currencies are translated into U.S. dollars using average exchange rates.

General Insurance Results

General Insurance operating income in 2005 decreased after accounting for catastrophe related losses, the fourth quarter increase in reserves and changes in estimates related to remediation of the material weakness in reconciliation of balance sheet accounts. This decrease was partially offset by strong profitable growth in Foreign General's underwriting results and DBG's and Foreign General's net investment income. DBG's underwriting results also included additional losses incurred resulting from increased labor and material costs related to the 2004 Florida hurricanes. General Insurance operating income in 2004 showed positive results, even after accounting for catastrophe losses, the charge for asbestos and environmental exposures and the $232 million charge reflecting a change in estimate for salvage and subrogation recoveries. Net investment income and the capital gains realized in 2004 rather than the capital losses realized in 2003 also benefited General Insurance results.

DBG's net premiums written increased modestly in 2005 when compared to 2004, reflecting generally improving renewal retention rates and a modest change in the mix of business towards smaller accounts for which DBG purchases less reinsurance. DBG also continued to expand its relationships with a larger number and broader range of brokers. Recently, DBG has seen improvement in domestic property rates as well as increases in submission activity in the aftermath of the 2005 hurricanes. DBG attributes the increase in submissions to its overall financial strength in comparison to many insurers that experienced significant losses and reductions of surplus as a result of the hurricanes.

The DBG loss ratio increased in 2005 from 2004 principally as a result of adverse loss development, the third and fourth quarter 2005 catastrophe related losses and the $197 million of additional losses resulting from increased labor and material costs related to the 2004 hurricanes.

The DBG expense ratio increased in 2005 from 2004 principally due to an increase in net commissions resulting from the replacement of certain ceded quota share reinsurance, for which DBG earns a ceding commission, with excess-of-loss reinsurance, which generally does not include a ceding commission. Increases in other underwriting expenses at DBG relate to the changes in estimates noted above, as well as unusually high expenses for Personal Lines. The Foreign General expense ratio increased in 2005 from 2004 principally because consumer lines of business, which have higher acquisition costs, have become more significant.

Transatlantic's net premiums written and net premiums earned for 2005 decreased compared to 2004, principally due to competitive market conditions and increased ceding company retentions in certain classes of business. The great majority of the premium decrease relates to Transatlantic's domestic operations. Operating income decreased principally as a result of the increased level of catastrophe losses.

Personal Lines net premiums written and net premiums earned for 2005 increased when compared to 2004 as a result of strong growth in the Private Client Group and Agency Auto divisions due to increased agent/broker appointments, greater penetration and enhanced product offerings. AIG direct premiums are down slightly from 2004 due to aggressive re-underwriting of the previously acquired GE business and the discontinuation of underwriting homeowners business. Involuntary auto premiums were down in 2005 due to the decline in the assigned risk marketplace. Underwriting profit declined in 2005 as a result of hurricane losses and related expenses, reserve strengthening, an increase in Agency Auto's current accident year physical damage loss ratio, and expenses incurred related to terminating AIG's relationship with The Robert Plan effective December 31, 2005.

Mortgage Guaranty net premiums written were up slightly for 2005 when compared to 2004, reflecting growth in the second liens and international businesses offset by higher ceded premiums. Higher acquisition costs and lower earned premiums from certain single premium product lines resulted in lower underwriting profit in 2005 compared to 2004. UGC continued to achieve expansion of its international business in 2005.

Foreign General Insurance had strong results in 2005. Growth in net premiums written for 2005 was achieved from new business as well as new distribution channels. In Japan, the purchase in February 2005 of the insurance portfolio of the Royal & SunAlliance branch operations opened new distribution channels. In the Far East, personal accident business exhibited strong growth and had excellent results for 2005. Commercial lines in Europe exhibited healthy growth and had positive results for 2005, partially offset by rate decreases in Australia and the United Kingdom. Personal lines operations in Brazil and Latin America continue to exhibit strong growth, which translated into improved underwriting results for 2005. The Lloyd's Ascot syndicate continues to grow; however, insurance losses and reinstatement premium costs relating to the hurricanes caused a significant reduction in 2005 underwriting results. Foreign General Insurance also benefited from a decrease in the fourth quarter of 2005 in net reserves for loss and loss expense for non-asbestos and environmental reserves. Approximately half of the Foreign General Insurance net premiums written is derived from commercial insurance and the remainder from consumer lines.

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

	2005
Growth in original currency	2.6%
Foreign exchange effect	0.5
Growth as reported in U.S. dollars	3.1%

AIG's General Insurance results reflect the effects of catastrophe related losses of $2.89 billion, $1.05 billion and $83 million in 2005, 2004 and 2003, respectively. Losses caused by catastrophes can fluctuate widely from year to year, making comparisons of recurring type business more difficult. With respect to catastrophe losses, AIG believes that it has taken appropriate steps, such as careful exposure selection and obtaining reinsurance coverage, to reduce the effect of the magnitude of possible future losses. The occurrence of one or more catastrophic events of unanticipated frequency or severity, such as a terrorist attack, earthquake or hurricane, that causes insured losses, however, could have a material adverse effect on AIG's results of operations, liquidity or financial condition.

General Insurance net investment income grew in 2005 when compared to 2004. AIG is benefiting from strong cash flow, higher interest rates and increased partnership income. Cash flow for Foreign General was lower in 2005 when compared to 2004 due to payments for catastrophe related losses incurred in 2005 and 2004 and for the purchase of the Royal & SunAlliance branch operations. Partnership income was particularly strong for Foreign General due to increases in market valuations of infrastructure fund investments in Africa, Asia, China, Eastern Europe and India. Additionally, net investment income was positively affected by the compounding of previously earned and reinvested net investment income. In

2004, net investment income increased when compared to 2003. See also the discussion under "Liquidity" herein and Note 8 of Notes to Consolidated Financial Statements.

Realized capital gains and losses resulted from the ongoing investment management of the General Insurance portfolios within the overall objectives of the General Insurance operations. See the discussion on "Valuation of Invested Assets" herein.

The contribution of General Insurance operating income to AIG's consolidated income before income taxes, minority interest and cumulative effect of accounting changes was 15 percent in 2005, compared to 21 percent in 2004 and 38 percent in 2003. The decrease in contribution percentages in both 2005 and 2004 was largely the result of reserve increases and the effects of catastrophe losses.

Reinsurance

AIG is a major purchaser of reinsurance for its General Insurance operations. AIG insures risks globally, and its reinsurance programs must be coordinated in order to provide AIG the level of reinsurance protection that AIG desires. Reinsurance is an important risk management tool to manage transaction and insurance line risk retention at prudent levels set by management. AIG also purchases reinsurance to mitigate its catastrophic exposure. AIG is cognizant of the need to exercise good judgment in the selection and approval of both domestic and foreign companies participating in its reinsurance programs because one or more catastrophe losses could negatively affect AIG's reinsurers and result in an inability of AIG to collect reinsurance recoverables. AIG's reinsurance department evaluates catastrophic events and assesses the probability of occurrence and magnitude of catastrophic events through the use of state-of-the-art industry recognized program models among other techniques. AIG supplements these models through continually monitoring the risk exposure of AIG's worldwide General Insurance operations and adjusting such models accordingly. Although reinsurance arrangements do not relieve AIG from its direct obligations to its insureds, an efficient and effective reinsurance program substantially limits AIG's exposure to potentially significant losses. With respect to its property business, AIG has either renewed existing coverage or purchased new coverage that, in the opinion of management, is adequate to limit AIG's exposures.

AIG's consolidated general reinsurance assets amounted to $23.59 billion at December 31, 2005 and resulted from AIG's reinsurance arrangements. Thus, a credit exposure existed at December 31, 2005 with respect to reinsurance recoverable to the extent that any reinsurer may not be able to reimburse AIG under the terms of these reinsurance arrangements. AIG manages its credit risk in its reinsurance relationships by transacting with reinsurers that it considers financially sound, and when necessary AIG holds substantial collateral in the form of funds, securities and/or irrevocable letters of credit. This collateral can be drawn on for amounts that remain unpaid beyond specified time periods on an individual reinsurer basis. At December 31, 2005, approximately 48 percent of the general reinsurance assets were from unauthorized reinsurers. Many of these balances were collateralized, permitting statutory recognition. Additionally, with the approval of its domiciliary insurance regulators, AIG posted approximately $1.5 billion of letters of credit issued by several commercial banks in favor of certain Domestic General Insurance companies to permit statutory recognition of balances otherwise uncollateralized at December 31, 2005. The remaining 52 percent of the general reinsurance assets were from authorized reinsurers. The terms authorized and unauthorized pertain to regulatory categories, not creditworthiness. At December 31, 2005, approximately 88 percent of the balances with respect to authorized reinsurers are from reinsurers rated A (excellent) or better, as rated by A.M. Best, or A (strong) or better, as rated by S&P. These ratings are measures of financial strength.

AIG maintains a reserve for estimated unrecoverable reinsurance. While AIG has been largely successful in its previous recovery efforts, at December 31, 2005, AIG had a reserve for unrecoverable reinsurance approximating $992 million. At that date, AIG had no significant reinsurance recoverables due from any individual reinsurer that was financially troubled (e.g., liquidated, insolvent, in receivership or otherwise subject to formal or informal regulatory restriction).

AIG's Reinsurance Security Department conducts ongoing detailed assessments of the reinsurance markets and current and potential reinsurers, both foreign and domestic. Such assessments include, but are not limited to, identifying if a reinsurer is appropriately licensed and has sufficient financial capacity, and evaluating the local economic environment in which a foreign reinsurer operates. This department also reviews the nature of the risks ceded and the requirements for credit risk mitigants. For example, in AIG's treaty reinsurance contracts, AIG includes provisions that frequently require a reinsurer to post collateral when a referenced event occurs. Furthermore, AIG limits its unsecured exposure to reinsurers through the use of credit triggers, which include, but are not limited to, insurer financial strength rating downgrades, policyholder surplus declines at or below a certain predetermined level or a certain predetermined level of a reinsurance recoverable being reached. In addition, AIG's Credit Risk Committee reviews the credit limits for and concentrations with any one reinsurer.

AIG enters into intercompany reinsurance transactions, primarily through AIRCO, for its General Insurance and Life Insurance operations. AIG enters into these transactions as a sound and prudent business practice in order to maintain underwriting control and spread insurance risk among AIG's various legal entities. These reinsurance agreements have been approved by the appropriate regulatory authorities. All material intercompany transactions have been eliminated in consolidation. AIG generally obtains letters of credit in order to obtain statutory recognition of these intercompany reinsurance transactions. At December 31, 2005, approximately $3.6 billion of letters of credit were outstanding to cover intercompany reinsurance transactions with AIRCO or other General Insurance subsidiaries.

At December 31, 2005, the consolidated general reinsurance assets of $23.59 billion include reinsurance recoverables for paid losses and loss expenses of $829 million and $19.69 bil-

lion with respect to the ceded reserve for losses and loss expenses, including ceded losses incurred but not reported (IBNR) (ceded reserves) and $3.07 billion of ceded reserve for unearned premiums. The ceded reserve for losses and loss expenses represent the accumulation of estimates of ultimate ceded losses including provisions for ceded IBNR and loss expenses. The methods used to determine such estimates and to establish the resulting ceded reserves are continually reviewed and updated by management. Any adjustments thereto are reflected in income currently. It is AIG's belief that the ceded reserve for losses and loss expenses at December 31, 2005 were representative of the ultimate losses recoverable. In the future, as the ceded reserves continue to develop to ultimate amounts, the ultimate loss recoverable may be greater or less than the reserves currently ceded.

Reserve for Losses and Loss Expenses

The table below classifies as of December 31, 2005 the components of the General Insurance gross reserve for losses and loss expenses (loss reserves) by major lines of business on a statutory Annual Statement basis*:

(in millions)	
Other liability occurrence	$18,116
Other liability claims made	12,447
Workers compensation	11,630
Auto liability	6,569
Property	7,217
International	4,939
Reinsurance	2,886
Medical malpractice	2,363
Aircraft	1,844
Products liability	1,937
Commercial multiple peril	1,359
Accident and health	1,678
Fidelity/surety	1,072
Other	3,112
Total	$77,169

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

AIG's reserve for losses and loss expenses represents the accumulation of estimates of ultimate losses, including IBNR and loss expenses. The methods used to determine loss reserve estimates and to establish the resulting reserves are continually reviewed and updated by management. Any adjustments resulting therefrom are reflected in operating income currently. Because loss reserve estimates are subject to the outcome of future events, changes in estimates are unavoidable given that loss trends vary and time is often required for changes in trends to be recognized and confirmed. Reserve changes that increase previous estimates of ultimate cost are referred to as unfavorable or adverse development or reserve strengthening. Reserve changes that decrease previous estimates of ultimate cost are referred to as favorable development.

At December 31, 2005, General Insurance net loss reserves were $57.5 billion, an increase of $10.22 billion from the prior year-end. The net loss reserve increase includes the fourth quarter 2005 increase in net reserves of approximately $1.8 billion, comprised of $960 million for non-asbestos and environmental exposures, and $873 million for asbestos and environmental exposures. The increase in non-asbestos and environmental reserves includes an increase of $1.44 billion for DBG and decreases of $455 million for Foreign General Insurance and $29 million for Mortgage Guaranty. The DBG increase of $1.44 billion is $140 million greater than the amount previously announced in AIG's press release of February 9, 2006 as a result of an additional change in estimate related to a commuted reinsurance agreement. The aggregate increase in asbestos and environmental reserves includes increases of $706 million and $167 million, respectively, for DBG and Foreign General Insurance.

As discussed in more detail below, the fourth quarter 2005 reserve increase was attributable to adverse development primarily related to 2002 and prior accident years, partially offset by favorable development for accident years 2003 through 2005. This reserve action reflects the completion of both the Milliman, Inc. (Milliman) review and AIG's own actuarial studies in the fourth quarter of 2005.

The net loss reserves represent loss reserves reduced by reinsurance recoverables, net of an allowance for unrecoverable reinsurance and applicable discount for future investment income. The table below classifies the components of the General Insurance net loss reserves by business unit as of December 31, 2005.

(in millions)	
DBG[(a)]	$ 40,782
Personal Lines[(b)]	2,578
Transatlantic	5,690
Mortgage Guaranty	340
Foreign General[(c)]	8,086
Total Net Loss Reserve	$ 57,476

(a) *DBG loss reserves include approximately $3.77 billion ($4.26 billion before discount) related to business written by DBG but ceded to AIRCO and reported in AIRCO's statutory filings. DBG loss reserves also include approximately $407 million related to business included in AIUO's statutory filings.*

(b) *Personal Lines loss reserves include $878 million related to business ceded to DBG and reported in DBG's statutory filings.*

(c) *Foreign General loss reserves include approximately $2.15 billion related to business reported in DBG's statutory filings.*

The DBG net loss reserve of $40.78 billion is comprised principally of the business of AIG subsidiaries participating in the American Home/National Union pool (11 companies) and the surplus lines pool (Lexington, Starr Excess Liability Insurance Company and Landmark Insurance Company).

Beginning in 1998, DBG ceded a quota share percentage of its other liability occurrence and products liability occurrence business to AIRCO. The quota share percentage ceded was 40 percent in 1998, 65 percent in 1999, 75 percent in 2000 and 2001, 50 percent in 2002 and 2003, 40 percent in 2004 and 35 percent in 2005 and covered all business written in these years for these lines by participants in the American Home/National Union pool. In 1998 the cession reflected only the other liability occurrence business, but in 1999 and

subsequent years included products liability occurrence. AIRCO's loss reserves relating to these quota share cessions from DBG are recorded on a discounted basis. As of year-end 2005, AIRCO carried a discount of approximately $490 million applicable to the $4.26 billion in undiscounted reserves it assumed from the American Home/National Union pool via this quota share cession. AIRCO also carries approximately $440 million in net loss reserves relating to Foreign General insurance business. These reserves are carried on an undiscounted basis.

Beginning in 1997, the Personal Lines division ceded a percentage of all business written by the companies participating in the personal lines pool to the American Home/National Union pool. As noted above, the total reserves carried by participants in the American Home/National Union pool relating to this cession amounted to $878 million as of year-end 2005.

The companies participating in the American Home/National Union pool have maintained a participation in the business written by AIU for decades. As of year-end 2005, these AIU reserves carried by participants in the American Home/National Union pool amounted to approximately $2.15 billion. The remaining Foreign General reserves are carried by AIUO, AIRCO, and other smaller AIG subsidiaries domiciled outside the United States. Statutory filings in the U.S. by AIG companies reflect all the business written by U.S. domiciled entities only, and therefore exclude business written by AIUO, AIRCO, and all other internationally domiciled subsidiaries. The total reserves carried at year-end 2005 by AIUO and AIRCO were approximately $3.72 billion and $4.21 billion, respectively. AIRCO's $4.21 billion in total general insurance reserves consist of approximately $3.77 billion from business assumed from the American Home/National Union pool and an additional $440 million relating to Foreign General Insurance business.

Discounting of Reserves

At December 31, 2005, AIG's overall General Insurance net loss reserves reflects a loss reserve discount of $2.11 billion, including tabular and non-tabular calculations. The tabular workers compensation discount is calculated using a 3.5 percent interest rate and the 1979-81 Decennial Mortality Table. The non-tabular workers compensation discount is calculated separately for companies domiciled in New York and Pennsylvania, and follows the statutory regulations for each state. For New York companies, the discount is based on a five percent interest rate and the companies' own payout patterns. For Pennsylvania companies, the statute has specified discount factors for accident years 2001 and prior, which are based on a six percent interest rate and an industry payout pattern. For accident years 2002 and subsequent, the discount is based on the yield of U.S. Treasury securities ranging from one to twenty years and the company's own payout pattern, with the future expected payment for each year using the interest rate associated with the corresponding Treasury security yield for that time period. The discount is comprised of the following: $512 million — tabular discount for workers compensation in DBG; $1.11 billion — non-tabular discount for workers compensation in DBG; and, $490 million — non-tabular discount for other liability occurrence and products liability occurrence in AIRCO. The total undiscounted workers compensation loss reserve carried by DBG is approximately $9.5 billion as of year-end 2005. The other liability occurrence and products liability occurrence business in AIRCO that is assumed from DBG is discounted based on the yield of U.S. Treasury securities ranging from one to twenty years and the DBG payout pattern for this business. The undiscounted reserves assumed by AIRCO from DBG totaled approximately $4.26 billion at December 31, 2005.

Results of 2005 Reserving Process

It is management's belief that the General Insurance net loss reserves are adequate to cover General Insurance net losses and loss expenses as of December 31, 2005. While AIG annually reviews the adequacy of established loss reserves, there can be no assurance that AIG's ultimate loss reserves will not develop adversely and materially exceed AIG's loss reserves as of December 31, 2005. In the opinion of management, such adverse development and resulting increase in reserves is not likely to have a material adverse effect on AIG's consolidated financial position, although it could have a material adverse effect on AIG's consolidated results of operations for an individual reporting period. See "Risk Factors — Casualty Insurance and Underwriting Reserves" in Item 1A. Risk Factors.

As part of the 2005 year-end actuarial loss reserve analysis, AIG expanded its review processes and conducted additional studies. In addition, in August 2005, AIG commissioned Milliman to provide an independent, comprehensive review of the loss reserves of AIG's principal property-casualty insurance operations, including an independent ground up study of AIG's asbestos and environmental exposures. The Milliman review encompassed nearly all of AIG's carried loss reserves, other than those pertaining to the operations of Transatlantic and 21st Century. AIG's management carefully considered the analyses provided by its actuarial staff and by Milliman for each class of business in determining AIG's best estimate of its loss reserves.

The table below presents the reconciliation of net loss reserves for 2005, 2004 and 2003 as follows:

(in millions)	**2005**	2004	2003
Net reserve for losses and loss expenses at beginning of year	**$47,254**	$36,228	$29,347
Foreign exchange effect	**(628)**	524	580
Acquisition	**–**	–	391[(a)]
Losses and loss expenses incurred:			
Current year	**28,426**	26,793	20,509
Prior years[(b)]	**4,665**[(c)]	3,564[(d)]	2,363
Losses and loss expenses incurred	**33,091**	30,357	22,872
Losses and loss expenses paid:			
Current year	**7,331**	7,692	6,187
Prior years	**14,910**	12,163	10,775
Losses and loss expenses paid	**22,241**	19,855	16,962
Net reserve for losses and loss expenses at end of year	**$57,476**	$47,254	$36,228

(a) *Reflects the opening balances with respect to the GE U.S.-based auto and home insurance business acquired in 2003.*

(b) *Includes accretion of discount of $(15) million in 2005, including an increase of $375 million in the discount recorded in 2005; $377 million in 2004 and $296 million in 2003. Additionally, includes $269 million in 2005, $317 million in 2004 and $323 million in 2003 for the general reinsurance operations of Transatlantic, and $197 million of additional losses incurred in 2005 resulting from increased labor and material costs related to the 2004 Florida hurricanes.*

(c) *Includes fourth quarter charge of $1.8 billion.*

(d) *Includes fourth quarter charge of $850 million attributable to the change in estimate for asbestos and environmental exposures.*

For 2005, AIG's overall net loss reserve development from prior accident years was an increase of approximately $4.67 billion, including approximately $269 million from the general reinsurance operations of Transatlantic. This $4.67 billion adverse development in 2005 was comprised of approximately $8.60 billion for 2002 and prior accident years, partially offset by favorable development for accident years 2003 and 2004 for most lines of business, with the notable exception being D&O. The adverse loss development for 2002 and prior accident years is attributable to approximately $4.0 billion of development from D&O and related management liability classes of business, excess casualty, and excess workers compensation, and to approximately $873 million of development from asbestos and environmental claims. The remaining portion of the adverse development for 2002 and prior accident years includes approximately $520 million related to Transatlantic with the balance spread across many other lines of business.

The largest contributors to the $4.67 billion net adverse loss development were:

D&O and related management liability classes of business: The adverse development for 2002 and prior accident years totalled approximately $1.7 billion, principally related to 2002 and prior accident years. This adverse development resulted from significant loss cost escalation due to a variety of factors, including the following: the increase in frequency and severity of corporate bankruptcies; the increase in frequency of financial statement restatements; the sharp rise in market capitalization of publicly traded companies and the increase in the number of initial public offerings, which led to an unprecedented number of IPO allocation/laddering suits in 2001. In addition, the extensive utilization of multi-year policies during this period limited AIG's ability to respond to emerging trends as rapidly as would otherwise be the case.

AIG has experienced significant adverse loss development since 2002 as a result of these issues. AIG has taken numerous actions in response to this development, including rate increases and policy form and coverage changes to better contain future loss costs in this class of business. AIG's 2005 year-end actuarial reserve analyses for DBG exposures reflected several other noteworthy additional considerations and studies. AIG's claims staff conducted a series of ground-up claim projections covering all open claims for this class of business through accident year 2004. Given the adverse development observed for this class of business in recent years, for year-end 2005 AIG believed its reserves for this class were better estimated by benchmarking the actuarial indications to these claim projections.

Excess Casualty: The adverse development for prior years was approximately $1.3 billion related to 2001 and prior accident years. This adverse development resulted from significant loss cost increases due to both frequency and severity of claims. The primary drivers of the increasing loss costs were medical inflation, which increased the economic loss component of tort claims; advances in medical care, which extended the life span of severely injured workers; and larger jury verdicts, which increased the value of severe tort claims. An additional factor affecting AIG's excess casualty experience in recent years has been the accelerated exhaustion of underlying primary policies for homebuilders. This has led to increasing construction defect related claim activity on AIG's excess policies. As noted above for D&O, many excess casualty policies were written on a multi-year basis in the late 1990s, which limited AIG's ability to respond to emerging trends as rapidly as would otherwise be the case. AIG responded to these emerging trends by increasing rates and effecting numerous policy form and coverage changes. This led to a significant improvement in experience beginning with accident year 2001. In response to the continuing loss development, AIG increased further the loss development factors for this class of business in its 2005 year-end actuarial reserve analysis. In addition, to more accurately estimate losses for construction defects, a separate review was performed by AIG claims staff for accounts with significant exposure to these claims.

Excess Workers Compensation: The adverse development for prior years was approximately $1 billion related to 2002 and prior accident years. This adverse development resulted from significant loss cost increases, primarily attributable to rapidly increasing medical inflation and advances in medical care, which increased the cost of covered medical care and extended the life span of severely injured workers. The effect of these factors on excess workers compensation claims experience is leveraged, as frequency is increased by the rising number of claims that reach the excess layers.

In response to the continuing loss development, an additional study was conducted for the 2005 year-end actuarial reserve analysis for DBG pertaining to the selection of loss development factors for this class of business. Claims for excess workers compensation exhibit an exceptionally long tail of loss development, running for decades from the date the loss is incurred. Thus, the adequacy of loss reserves for this class is sensitive to the estimated loss development factors, as such factors may be applied to many years of loss experience. In order to better estimate the tail development for this class, AIG claims staff conducted a claim by claim projection of the expected ultimate paid loss for each open claim for 1998 and prior accident years as these are the primary years that drive the tail factors. The objective of the study was to provide a benchmark against which loss development factors in the tail could be evaluated.

For a discussion of the adverse development in asbestos and environmental exposures, see "Asbestos and Environmental Reserves" below.

The favorable development in 2005 referred to above was principally the result of the following: Most classes of business, with the notable exception of D&O, experienced favorable loss development for accident year 2003, and nearly all classes experienced favorable development for accident year 2004. These accident years are benefiting from the actions AIG has taken in response to the significant improvement in market conditions that occurred beginning in 2001 and that accelerated thereafter. Rates increased sharply for most classes of business, and policy terms and conditions were also improved significantly. In connection with AIG's 2005 year-end actuarial reserve analysis and after considering the results of the Milliman review, AIG has recognized the improving results to the extent they are credible, evidenced by up to five years of favorable loss experience across many lines of business since the market conditions improved. In addition, AIG has taken this information into consideration in determining the expected loss ratios for the 2005 accident year.

Overview of Loss Reserving Process

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

Short-Tail Reserves

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

Long-Tail Reserves

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

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

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

- Loss trend factors which are used to establish expected loss ratios for subsequent accident years based on the projected loss ratio for prior accident years.
- Expected loss ratios for the latest accident year (*i.e.*, accident year 2005 for the year end 2005 loss reserve analysis) and, in some cases, for accident years prior to the latest accident year. The expected loss ratio generally reflects the projected loss ratio from prior accident years, adjusted for the loss trend (see above) and the effect of rate changes and other quantifiable factors. For low-frequency, high-severity classes such as excess casualty and D&O, expected loss ratios generally are utilized for at least the three most recent accident years.
- Loss development factors which are used to project the reported losses for each accident year to an ultimate basis.

AIG records quarterly changes in loss reserves for each of its many General Insurance profit centers. The overall change in AIG's loss reserves is based on the sum of these profit center level changes. For most profit centers which write longer tail classes of casualty coverage, the process of recording quarterly loss reserve changes involves determining the estimated current loss ratio for each class of coverage. This loss ratio is multiplied by the current quarter's net earned premium for that

class of coverage to determine the quarter's total estimated net incurred loss and loss expense. The change in loss reserves for the quarter for each class is thus the difference between the net incurred loss and loss expense, estimated as described above, and the net paid losses and loss expenses in the quarter.

Details of the Loss Reserving Process

The process of determining the current loss ratio for each class or business segment is based on a variety of factors. These include, but are not limited to, the following considerations: prior accident year and policy year loss ratios; actual and anticipated rate changes; actual and anticipated changes in coverage, reinsurance, or mix of business; actual and anticipated changes in external factors affecting results, such as trends in loss costs or in the legal and claims environment. Each profit center's current loss ratio reflects input from actuarial, profit center and claims staff and is intended to represent management's best estimate of the current loss ratio after reflecting all of the factors described above. At the close of each quarter, the assumptions underlying the loss ratios are reviewed to determine if the loss ratios based thereon remain appropriate. This process includes a review of the actual claims experience in the quarter, actual rate changes achieved, actual changes in coverage, reinsurance or mix of business, and changes in certain other factors that may affect the loss ratio. When this review suggests that the initially determined loss ratio is no longer appropriate, the loss ratio for current business would be changed to reflect the revised assumptions.

A comprehensive annual loss reserve review is conducted in the fourth quarter of each year for each AIG General Insurance subsidiary. These reviews are conducted in full detail for each class or line of business for each subsidiary, and thus consist of literally hundreds of individual analyses. The purpose of these reviews is to confirm the appropriateness of the reserves carried by each of the individual subsidiaries, and thereby of AIG's overall carried reserves. The reserve analysis for each business class is performed by the actuarial personnel who are most familiar with that class of business. In completing these detailed actuarial reserve analyses, the actuaries are required to make numerous assumptions, including for example the selection of loss development factors and loss cost trend factors. They are also required to determine and select the most appropriate actuarial method(s) to employ for each business class. Additionally, they must determine the appropriate segmentation of data or segments from which the adequacy of the reserves can be most accurately tested. In the course of these detailed reserve reviews for each business segment, a point estimate of the loss reserve is generally determined. The sum of these point estimates for each of the individual business classes for each subsidiary provides an overall actuarial point estimate of the loss reserve for that subsidiary. The ultimate process by which the actual carried reserves are determined considers not only the actuarial point estimate but a myriad of other factors. Other crucial internal and external factors considered include a qualitative assessment of inflation and other economic conditions in the United States and abroad, changes in the legal, regulatory, judicial and social environments, underlying policy pricing, terms and conditions, and claims handling. Loss reserve development can also be affected by commutations of assumed and ceded reinsurance agreements.

AIG's annual loss reserve review does not calculate a range of loss reserve estimates. Because a large portion of the loss reserves from AIG's General Insurance business relates to long-tail casualty lines driven by severity rather than frequency of claims, such as excess casualty and D&O, developing a range around loss reserve estimates would not be meaningful. An estimate is calculated which AIG's actuaries believe provides a reasonable estimate of the required reserve. This amount is then evaluated against actual carried reserves.

Volatility of Reserve Estimates and Sensitivity Analyses

There is potential for significant variation in the development of loss reserves, particularly for long-tail casualty classes of business such as excess casualty, when actual costs differ from the assumptions used to test the reserves. Such assumptions include those made for loss trend factors and loss development factors, as described earlier. Set forth below is a sensitivity analysis demonstrating the estimated effect on the loss reserve position of alternative loss trend or loss development factor assumptions as compared to those actually used to test the carried reserves.

For the excess casualty class of business the assumed loss cost trend was approximately six percent. A five percent change in the assumed loss cost trend from each accident year to the next would cause approximately a $600 million change (either positively or negatively) to the net loss and loss expense reserve for this business. For the D&O and related management liability classes of business the assumed loss cost trend was four percent. A five percent change in this assumed loss cost trend would cause approximately a $300 million change (either positively or negatively) to the net loss and loss expense reserve for such business. The effect of the loss trend assumption for the D&O class decreased in 2005 as a result of AIG's change in methodology, as described above, whereby claim projections through accident year 2004 are utilized as a benchmark for the actuarial indications. For the excess workers compensation class of business, loss costs were trended at six percent per annum. A five percent change in the assumed loss cost trend would cause approximately a $250 million change (either positively or negatively) to the loss and loss expense reserve for this class. Actual loss cost trends in the early 1990's were negative for these classes, whereas in the late 1990's loss costs trends ran well into the double digits for each of these three classes. The sharp increase in loss costs in the late 1990's was thus much greater than the five percent changes cited above, and caused significant increases in the overall loss reserve needs for these classes. While changes in the loss cost trend assumptions can have a significant effect on the reserve needs for other smaller classes of liability business, the potential effect of these changes on AIG's overall carried reserves would be much less than for the classes noted above.

For the excess casualty class, if future loss development factors differed by five percent from those utilized in the year-end 2005 loss reserve review, there would be approximately a

$400 million change (either positively or negatively) to the overall AIG loss reserve position. The comparable effect on the D&O and related management liability classes would be approximately $200 million (either positively or negatively) if future loss development factors differed by five percent from those utilized in the year-end 2005 loss reserve review. For the excess workers compensation class, the effect would be approximately $150 million (either positively or negatively). For workers compensation reserves, other than excess workers compensation reserves, the effect of a five percent deviation from the loss development factors utilized in the year-end 2005 reserve reviews would be approximately $1.0 billion (either positively or negatively). Because loss development factors for this class have shown less volatility than higher severity classes such as excess casualty, however, actual changes in loss development factors are expected to be less than five percent. There is some degree of volatility in loss development patterns for other longer tail liability classes as well. However, the potential effect on AIG's reserves would be much less than for the classes cited above.

The calculations of the effect of the five percent change in loss development factors are made by selecting the stage of accident year development where it is believed reasonable for such a deviation to occur. For example, for workers compensation, the $1.0 billion amount is calculated by assuming that each of the most recent eight accident years develop five percent higher than estimated by the current loss development factors utilized in the reserve study, *i.e.* the factor 1.05 is multiplied by the incurred losses (including IBNR and loss expenses) for these accident years.

AIG management believes that using a five percent change in the assumptions for loss cost trends and loss development factors provides a reasonable benchmark for a sensitivity analysis of the reserves of AIG's most significant lines of general insurance business. For excess casualty business, both the loss cost trend and the loss development factor assumptions are critical. Generally, actual historical loss development factors are used to project future loss development. However, there can be no assurance that future loss development patterns will be the same as in the past. Moreover, as excess casualty is a long-tail class of business, any deviation in loss cost trends or in loss development factors might not be discernible for an extended period of time subsequent to the recording of the initial loss reserve estimates for any accident year. Thus, there is the potential for the reserves with respect to a number of accident years to be significantly affected by changes in the loss cost trends or loss development factors that were initially relied upon in setting the reserves. These changes in loss trends or loss development factors could be attributable to changes in inflation or in the judicial environment, or in other social or economic phenomena affecting claims. For example, during the lengthy periods during which losses develop for excess casualty, actual changes in loss costs from one accident year to the next have ranged from negative values to double-digit amounts. Thus, there is the potential for significant volatility in loss costs for excess casualty and, although five percent is considered a reasonable benchmark for sensitivity analysis for this business, there is the potential for variations far greater than this amount (either positively or negatively). Likewise, in the judgment of AIG's actuaries, five percent is considered an appropriate benchmark for sensitivity analysis with respect to the loss development factor assumptions used to test the reserves.

For D&O and related management liability classes of business, the loss cost trend assumption has been critical in past analyses, however, because of the utilization of claim projections for all claims through accident year 2004, as described above, the sensitivity of the reserves to this assumption has been reduced in 2005. The loss development factor assumption is important but less critical than for excess casualty. As this coverage is written on a claims-made basis, claims for a given accident year are all reported within that year. Actual changes in loss costs from one accident year to the next in the 1990s ranged from double digit negative values for several accident years in the early 1990s to nearly 50 percent per year for the period from accident year 1996 to accident year 1999. Thus, there is the potential for extreme volatility in loss costs for this business and, although five percent is considered a reasonable benchmark for sensitivity analysis, there is the potential for variations far greater than this amount (either positively or negatively). Five percent is also considered an appropriate benchmark for sensitivity analysis with respect to the loss development factor assumptions used to test the reserves for these classes. However, as noted above, the effect of such a deviation is less than that of a similar deviation in loss cost trends. For the excess workers compensation class, the loss development factor assumptions are critical and the loss trend assumption is important but not as critical. Excess workers compensation is an extremely long tail class of business, hence there is a much greater than normal uncertainty as to the appropriate loss development factors for the tail of the loss development. As noted above, the effect of a five percent change in the loss development factor is approximately $150 million. It would not be uncommon for the loss development factors to deviate by greater than five percent for this class of business.

For workers compensation, the loss development factor assumptions are important. Generally, AIG's actual historical workers compensation loss development would be expected to provide a reasonably accurate predictor of future loss development. A five percent sensitivity indicator for workers compensation would thus be considered to be toward the high end of potential deviations for this class of business. The loss cost trend assumption for workers compensation is not believed to be material with respect to AIG's loss reserves. This is primarily because AIG's actuaries are generally able to use loss development projections for all but the most recent accident year's reserves, so there is limited need to rely on loss cost trend assumptions for workers compensation business.

For casualty business other than the classes noted above, there is generally some potential for deviation in both the loss cost trend and loss development factor selections. However, the effect of such deviations would not be material when compared to the effect on the classes cited above.

Asbestos and Environmental Reserves

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

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

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

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

Estimation of asbestos and environmental claims loss reserves is a subjective process and reserves for asbestos and environmental claims cannot be estimated using conventional reserving techniques such as those that rely on historical accident year loss development factors.

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

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

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

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

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

To determine the appropriate loss reserve as of December 31, 2005 for its asbestos and environmental exposures, AIG performed a series of top-down and ground-up reserve analyses. In order to ensure it had the most comprehensive analysis possible, AIG engaged Milliman to provide an analysis of these exposures including ground-up estimates for both asbestos reserves and environmental reserves. Prior to 2005, AIG's reserve analyses for asbestos and environmental exposures was focused around a report year projection of aggregate losses for both asbestos and environmental reserves. Additional tests such as market share analyses were also performed. Ground-up analyses such as those provided by Milliman take into account policyholder-specific and claim-specific information that has been gathered over many years from a variety of sources. Ground-up studies can thus more accurately assess the exposure to AIG's layers of coverage for each policyholder, and hence

for all policyholders in the aggregate provided a sufficient sample of the policyholders can be modeled in this manner.

In order to ensure its ground-up analysis was as comprehensive as possible, AIG staff produced the information required at policy and claim level detail for nearly 1,000 asbestos defendants and over 1,100 environmental defendants. This represented nearly 90 percent of all accounts for which AIG had received any claim notice of any amount pertaining to asbestos or environmental exposure. AIG did not set any minimum thresholds such as amount of case reserve outstanding, or paid losses to date, that would have served to reduce the sample size and hence the comprehensiveness of the ground-up analysis. The results of the ground-up analysis for each significant account were examined by AIG's claims staff for reasonableness, for consistency with policy coverage terms, and any claim settlement terms applicable. Adjustments were incorporated accordingly. The results from the universe of modeled accounts, which as noted above reflects the vast majority of AIG's known exposures, were then utilized to estimate the ultimate losses from accounts that could not be modeled and to determine the appropriate provision for all unreported claims.

AIG conducted a comprehensive analysis of reinsurance recoverability to establish the appropriate asbestos and environmental reserve net of reinsurance. AIG determined the amount of reinsurance that would be ceded to insolvent reinsurers or to commuted reinsurance contracts for both reported claims and for IBNR. These amounts were then deducted from the indicated amount of reinsurance recoverable.

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

For asbestos, these tests project the expected losses to be reported over the next twenty years, i.e., from 2006 through 2025, based on the actual losses reported through 2005 and the expected future loss emergence for these claims. Three scenarios were tested, with a series of assumptions ranging from more optimistic to more conservative. In the first scenario, all carried asbestos case reserves are assumed to be within ten percent of their ultimate settlement value. The second scenario relies on an actuarial projection of report year development for asbestos claims reported from 1993 to the present to estimate case reserve adequacy as of year-end 2005. The third scenario relies on an actuarial projection of report year claims for asbestos but reflects claims reported from 1989 to the present to estimate case reserve adequacy as of year-end 2005. Based on the results of the prior report years for each of the three scenarios described above, the report year approach then projects forward to the year 2025 the expected future report year losses, based on AIG's estimate of reasonable loss trend assumptions. These calculations are performed on losses gross of reinsurance. The IBNR (including a provision for development of reported claims) on a net basis is based on applying a factor reflecting the expected ratio of net losses to gross losses for future loss emergence.

For environmental claims, an analogous series of frequency/severity tests are produced. Environmental claims from future report years, (i.e., IBNR) are projected out ten years, i.e., through the year 2015.

At year-end 2005, AIG considered a number of factors and recent experience, in addition to the results of the respective top-down and ground-up analyses performed for asbestos and environmental reserves. Among the factors considered by AIG was the continued deterioration in its asbestos report year experience. The indication from the third scenario as described above for asbestos was approximately $265 million greater than AIG's carried net asbestos reserve, prior to its increase in the fourth quarter of 2005. This marks a continuation of the trend of adverse report year development for asbestos that has been observed for the past several years. AIG also noted its asbestos paid losses in 2005 increased from 2004's levels. AIG considered the significant uncertainty that remains as to AIG's ultimate liability relating to asbestos and environmental claims. This uncertainty is due to several factors including:

- The long latency period between asbestos exposure and disease manifestation and the resulting potential for involvement of multiple policy periods for individual claims;
- The increase in the volume of claims by currently unimpaired plaintiffs;
- Claims filed under the non-aggregate premises or operations section of general liability policies;
- The number of insureds seeking bankruptcy protection and the effect of prepackaged bankruptcies;
- Diverging legal interpretations; and
- With respect to environmental claims, the difficulty in estimating the allocation of remediation cost among various parties.

After carefully considering the results of the ground-up analysis, which AIG now plans to update on an annual basis, as well as all of the above factors including the recent report year experience, AIG determined its best estimate was to recognize an increase of $843 million in its carried net asbestos reserves, and an increase of $30 million in its carried net environmental reserves at December 31, 2005. The corresponding increases in gross reserves were approximately $1.97 billion for asbestos and $56 million for environmental.

A summary of reserve activity, including estimates for applicable IBNR, relating to asbestos and environmental claims separately and combined at December 31, 2005, 2004 and 2003 follows:

	2005		2004		2003	
(in millions)	**Gross**	**Net**	Gross	Net	Gross	Net
Asbestos:						
Reserve for losses and loss expenses at beginning of year	**$2,559**	**$1,060**	$1,235	$ 386	$1,304	$ 400
Losses and loss expenses incurred*	**2,207**[(a)]	**903**[(a)]	1,595[(a)]	772[(a)]	175	43
Losses and loss expenses paid*	**(325)**	**(123)**	(271)	(98)	(244)	(57)
Reserve for losses and loss expenses at end of year	**$4,441**	**$1,840**	$2,559	$1,060	$1,235	$ 386
Environmental:						
Reserve for losses and loss expenses at beginning of year	**$ 974**	**$ 451**	$ 789	$ 283	$ 832	$ 296
Losses and loss expenses incurred*	**47**[(b)]	**27**[(b)]	314[(b)]	234[(b)]	133	52
Losses and loss expenses paid*	**(95)**	**(68)**	(129)	(66)	(176)	(65)
Reserve for losses and loss expenses at end of year	**$ 926**	**$ 410**	$ 974	$ 451	$ 789	$ 283
Combined:						
Reserve for losses and loss expenses at beginning of year	**$3,533**	**$1,511**	$2,024	$ 669	$2,136	$ 696
Losses and loss expenses incurred*	**2,254**[(c)]	**930**[(c)]	1,909[(c)]	1,006[(c)]	308	95
Losses and loss expenses paid*	**(420)**	**(191)**	(400)	(164)	(420)	(122)
Reserve for losses and loss expenses at end of year	**$5,367**	**$2,250**	$3,533	$1,511	$2,024	$ 669

* *All amounts pertain to policies underwritten in prior years.*

(a) *Includes increases to gross losses and loss expense reserves of $2.0 billion and $1.2 billion in the fourth quarter of 2005 and 2004, respectively, and increases to net losses and loss expense reserves of $843 million and $650 million for the fourth quarter of 2005 and 2004, respectively.*

(b) *Includes increases to gross losses and loss expense reserves of $56 million and $250 million in the fourth quarter of 2005 and 2004, respectively, and increases to net losses and loss expense reserves of $30 million and $200 million for the fourth quarter of 2005 and 2004, respectively.*

(c) *Includes increases to gross losses and loss expense reserves of $2.0 billion and $1.5 billion in the fourth quarter of 2005 and 2004, respectively, and increases to net losses and loss expense reserves of $873 million and $850 million for the fourth quarter of 2005 and 2004, respectively.*

The gross and net IBNR included in the reserve for losses and loss expenses, relating to asbestos and environmental claims separately and combined, at December 31, 2005, 2004 and 2003 were estimated as follows:

	2005		2004		2003	
(in millions)	**Gross**	**Net**	Gross	Net	Gross	Net
Asbestos	**$3,401**	**$1,465**	$2,033	$ 876	$ 695	$200
Environmental	**586**	**266**	606	284	347	80
Combined	**$3,987**	**$1,731**	$2,639	$1,160	$1,042	$280

A summary of asbestos and environmental claims count activity for the years ended December 31, 2005, 2004 and 2003 was as follows:

	2005			2004			2003		
	Asbestos	**Environmental**	**Combined**	Asbestos	Environmental	Combined	Asbestos	Environmental	Combined
Claims at beginning of year	**7,575**	**8,216**	**15,791**	7,474	8,852	16,326	7,085	8,995	16,080
Claims during year:									
Opened	**854**	**5,253***	**6,107**	909	2,592	3,501	669	2,106	2,775
Settled	**(67)**	**(219)**	**(286)**	(100)	(279)	(379)	(86)	(244)	(330)
Dismissed or otherwise resolved	**(1,069)**	**(3,377)**	**(4,446)**	(708)	(2,949)	(3,657)	(194)	(2,005)	(2,199)
Claims at end of year	**7,293**	**9,873**	**17,166**	7,575	8,216	15,791	7,474	8,852	16,326

* *The opened claims count increased substantially during 2005 because a court ruling led AIG to report separate opened claims for previously pending cases relating to alleged MTBE exposures that AIG previously had counted in the aggregate as only a single claim on the assumption that the cases would be consolidated into a single federal court proceeding.*

The table below presents AIG's survival ratios for asbestos and environmental claims for year end 2005, 2004 and 2003. The survival ratio is derived by dividing the year end carried loss reserve by the average payments for the three most recent calendar years for these claims. Therefore the survival ratio is a simplistic measure estimating the number of years it would be before the current ending loss reserves for these claims would be paid off using recent year average payments. Many factors, such as aggressive settlement procedures, mix of business and level of coverage provided, have a significant effect on the amount of asbestos and environmental reserves and payments and the resultant survival ratio. Thus, caution should be

exercised in attempting to determine reserve adequacy for these claims based simply on this survival ratio.

AIG's survival ratios for asbestos and environmental claims, separately and combined were based upon a three-year average payment. These ratios for the years ended December 31, 2005, 2004 and 2003 were as follows:

	Gross	Net
2005		
Survival ratios:		
Asbestos	**15.9**	**19.8**
Environmental	**6.9**	**6.2**
Combined	**13.0**	**14.2**
2004		
Survival ratios:		
Asbestos	10.7	13.5
Environmental	6.5	6.8
Combined	9.1	10.5
2003		
Survival ratios:		
Asbestos	4.7	4.5
Environmental	4.7	4.1
Combined	4.7	4.3

Life Insurance & Retirement Services Operations

AIG's Life Insurance & Retirement Services subsidiaries offer a wide range of insurance and retirement savings products both domestically and abroad. Insurance-oriented products consist of individual and group life, payout annuities, endowment and accident and health policies. Retirement savings products consist generally of fixed and variable annuities. See also Note 2 of Notes to Consolidated Financial Statements.

Domestically, AIG's Life Insurance & Retirement Services operations offer a broad range of protection products, including life insurance, group life and health products, including disability income products and payout annuities, which include single premium immediate annuities, structured settlements and terminal funding annuities. Home service operations include an array of life insurance, accident and health and annuity products sold through career agents. In addition, home service includes a small block of run-off property and casualty coverage. Retirement services include group retirement products, individual fixed and variable annuities sold through banks, broker dealers and exclusive sales representatives, and annuity runoff operations which include previously-acquired "closed blocks" and other fixed and variable annuities largely sold through distribution relationships that have been discontinued.

Overseas, AIG's Life Insurance & Retirement Services operations include insurance and investment-oriented products such as whole and term life, investment linked, universal life and endowments, personal accident and health products, group products including pension, life and health, and fixed and variable annuities.

Life Insurance & Retirement Services operations presented on a major product basis for 2005, 2004 and 2003 were as follows:

(in millions)	**2005**	2004[a]	2003[a]
GAAP Premiums:			
Domestic Life:			
Life insurance	**$ 2,108**	$ 1,888	$ 1,751
Home service	**801**	812	834
Group life/health	**1,012**	1,128	1,046
Payout annuities[b]	**1,473**	1,484	1,272
Total	**5,394**	5,312	4,903
Domestic Retirement Services:			
Group retirement products	**351**	313	250
Individual fixed annuities	**100**	59	53
Individual variable annuities	**467**	407	331
Individual fixed annuities — runoff[c]	**72**	80	86
Total	**990**	859	720
Total Domestic	**6,384**	6,171	5,623
Foreign Life:			
Life insurance	**15,631**	14,938	13,204
Personal accident & health	**5,002**	4,301	3,126
Group products[d]	**1,925**	2,215	1,267
Total	**22,558**	21,454	17,597
Foreign Retirement Services:			
Individual fixed annuities	**361**	395	255
Individual variable annuities	**97**	68	21
Total	**458**	463	276
Total Foreign	**23,016**	21,917	17,873
Total GAAP Premiums	**$ 29,400**	$ 28,088	$ 23,496
Net investment income:			
Domestic Life:			
Life insurance	**$ 1,411**	$ 1,287	$ 1,179
Home service	**605**	608	616
Group life/health	**142**	123	121
Payout annuities	**912**	801	699
Total	**3,070**	2,819	2,615
Domestic Retirement Services:			
Group retirement products	**2,233**	2,201	2,055
Individual fixed annuities	**3,393**	3,100	2,567
Individual variable annuities	**217**	239	239
Individual fixed annuities — runoff[c]	**1,046**	1,076	1,266
Total	**6,889**	6,616	6,127
Total Domestic	**9,959**	9,435	8,742

(continued)

(in millions)	**2005**	2004[a]	2003[a]
Foreign Life:			
Life insurance	**4,844**	4,065	3,356
Personal accident & health	**255**	179	161
Group products	**613**	431	326
Intercompany adjustments	**(36)**	(18)	(15)
Total	**5,676**	4,657	3,828
Foreign Retirement Services:			
Individual fixed annuities	**1,728**	1,034	368
Individual variable annuities	**771**	143	4
Total	**2,499**	1,177	372
Total Foreign	**8,175**	5,834	4,200
Total net investment income	**$ 18,134**	$ 15,269	$ 12,942
Realized capital gains (losses):			
Domestic realized capital gains (losses)[e]	**$ (302)**	$ (329)	$ (246)
Foreign realized capital gains (losses)[f]	**(260)**	147	330
Pricing net investment gains[g]	**344**	225	156
Total Foreign	**84**	372	486
Total realized capital gains (losses)	**$ (218)**	$ 43	$ 240
Operating Income:			
Domestic[h]	**3,599**	3,075	2,765
Foreign	**5,245**	4,848	4,042
Total operating income	**$ 8,844**	$ 7,923	$ 6,807
Life insurance in–force:			
Domestic	**$ 825,151**[i]	$ 772,251	$ 645,606
Foreign	**1,027,682**	1,085,843	937,425
Total	**$1,852,833**	$1,858,094	$1,583,031

(a) Adjusted to conform to 2005 presentation.

(b) Includes structured settlements, single premium immediate annuities and terminal funding annuities.

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

(d) Revenues in 2004 includes approximately $640 million of single premium from a reinsurance transaction involving terminal funding business, which is offset by a similar increase of benefit reserves.

(e) Includes the effect of hedging activities that do not qualify for hedge accounting treatment under FAS 133 and the application of FAS 52. For 2005, 2004, and 2003, respectively, the amounts included are $63 million, $(6) million, and $19 million.

(f) Includes the effect of hedging activities that do not qualify for hedge accounting treatment under FAS 133 and the application of FAS 52. For 2005, 2004, and 2003, respectively, the amounts included are $(500) million, $(134) million, and $59 million.

(g) For purposes of this presentation, pricing net investment gains are segregated as a component of total realized gains (losses). They represent certain amounts of realized capital gains where gains are an inherent element in pricing certain life products in some foreign countries.

(h) Operating income includes the effect on deferred policy acquisition cost amortization for FAS 97 products related to realized capital gains (losses) and has reduced amortization costs totaling $59 million, $44 million and $54 million for 2005, 2004 and 2003, respectively.

(i) Domestic in-force for 2005 includes the effect of the non-renewal of a single large group life case of $36 billion.

AIG's Life Insurance & Retirement Services subsidiaries report their operations through the following operating units: Domestic Life — AIG American General, including American General Life Insurance Company (AG Life), USLIFE and AGLA; Domestic Retirement Services — VALIC, AIG Annuity and AIG SunAmerica; Foreign Life — ALICO, AIRCO, AIG Edison Life, AIG Star Life, AIA, Nan Shan and Philamlife.

Life Insurance & Retirement Services Results

The increase in operating income in 2005 compared to 2004 was caused by growth in both domestic and overseas operations. Similarly, the increase in operating income in 2004 compared to 2003 was due to strong growth, particularly overseas.

Life Insurance & Retirement Services GAAP premiums grew in 2005 when compared with 2004 as well as 2004 when compared with 2003. AIG's Domestic Life operations had continued growth in term and universal life sales with good performance from the independent distribution channels. GAAP premiums for life insurance grew 12 percent in 2005 reflecting consistently strong sales from the independent distribution channels. Retail periodic life sales increased 18 percent in 2005, representing a compound rate of growth of 16 percent since 2001, compared to modest growth in the industry. Profit margins have been maintained through strict underwriting discipline and low cost. In addition, increases in product prices and retention have offset price increases by reinsurers. Payout annuities declined slightly due to the low interest rate environment and the competitive market conditions for structured settlement and single premium individual annuity business. The domestic group business is below AIG's growth standards, largely because several accounts where pricing was unacceptable were not renewed and loss experience was higher than anticipated. Restructuring efforts in this business are focused on new product introductions, cross selling and other growth strategies. AGLA, the home service business, is diversifying product offerings, enhancing the capabilities and quality of the sales force, and broadening the markets served beyond those historically serviced in an effort to accelerate growth, although it is expected to remain a slow growth business.

Domestic Retirement Services businesses faced a challenging environment in 2005 and 2004, as deposits declined approximately 17 percent for 2005 compared to 2004 and 1 percent for 2004 compared to 2003. The decrease in AIG's individual variable annuity product sales in 2005 was largely attributable to significant variable annuity sales declines at several of AIG's largest distribution firms due to lackluster equity markets, more

intense industry competition with regard to living benefit product features and heightened compliance procedures over selling practices. AIG's introduction of more competitive guaranteed minimum withdrawal features was delayed until late in the fourth quarter due to filing delays associated with the Restatements. During 2005, the interest yield curve flattened and, as a result, competing bank products such as certificates of deposit and other money market instruments with shorter durations than AIG's individual fixed annuity products became more attractive. The following table reflects deposit amounts for Domestic Retirement Services:

Domestic Retirement Services — Deposits

December 31, (in millions)	2005	2004	2003
Group retirement products*	**$ 6,436**	$ 6,502	$ 5,918
Individual fixed annuities	**7,337**	9,947	11,384
Individual variable annuities	**3,319**	4,126	3,412
Individual fixed annuities - runoff	**200**	253	350
Total	**$ 17,292**	$ 20,828	$21,064

* *Includes mutual funds.*

In 2005, AIG experienced a significant increase in surrender rates in all product lines. Group retirement products experienced higher surrenders as the average participant age increased and a greater percentage of these participants are near retirement age and/or termination of service from their employers. Individual fixed annuities surrender rates are higher in 2005 primarily due to the shape of the interest yield curve and the general aging of the in-force reserves. However, less than 20 percent of the individual fixed annuity reserves are available to surrender without charge. The increase in individual variable annuity surrender rates primarily reflects the higher shock-lapse that occurred following expiration of the surrender charge period on certain 3-year and 7-year contracts (including a large closed block of acquired business). Reflecting a widespread industry phenomenon, this lapse rate, much of which was anticipated when the products were issued, has recently been affected by investor demand to exchange existing policies for new-generation contracts with living benefits or lower fees. In addition, partial withdrawals on certain variable annuity products have increased as AIG has introduced features designed to generate a stream of income to the participants. The following chart shows the amount of reserves by surrender charge category as of December 31, 2005.

Domestic Retirement Services
Reserves Subject to Surrender Charges

(in millions)	Group Retirement Products*	Individual Fixed Annuities	Individual Variable Annuities
Zero or no surrender charge	$39,831	$ 9,324	$ 9,765
Greater than 0% - 4%	11,248	10,815	8,386
Greater than 4%	2,648	31,183	10,035
Non-Surrenderable	892	3,148	81
Total	$54,619	$54,470	$28,267

* *Excludes mutual funds.*

A continued increase in the level of surrenders in any of these businesses could increase the amortization of deferred acquisition costs in future years and will negatively affect fee income earned on assets under management. The combination of reduced sales and increased surrenders and withdrawals resulted in significantly lower net flows for total domestic Retirement Services than in the prior year. AIG expects that net flows will remain lower than in prior years as long as an environment of lackluster equity market performance persists and the yield curve remains flat. The following table reflects the net flows for Domestic Retirement Services:

Domestic Retirement Services — Net Flows[a]

December 31, (in millions)	2005	2004	2003
Group retirement products[b]	**$ 628**	$ 1,706	$ 2,756
Individual fixed annuities	**1,759**	6,169	8,679
Individual variable annuities	**(336)**	1,145	927
Individual fixed annuities - runoff	**(2,508)**	(2,084)	(1,967)
Total	**$ (457)**	$ 6,936	$10,395

(a) Net flows are defined as deposits received, less benefits, surrenders, withdrawals and death benefits.
(b) Includes mutual funds.

The majority of the growth in Life Insurance & Retirement Services GAAP premiums in Foreign Life operations was attributable to the life insurance and personal accident & health lines of business. Globally, AIG's deep and diverse distribution, which includes bancassurance, worksite marketing, direct marketing, and strong agency organizations, provides a powerful platform for growth. This growth was most significant in Japan, where AIG has benefited from a flight to quality and development of multiple distribution channels. In Southeast Asia, AIG maintains significant market share by offering an attractive and diverse product line, distributed by its strong agency force. There has been a continuing trend in Southeast Asia, as the insurance market continues to develop, for clients to purchase investment-oriented products at the expense of traditional term or whole life products. For GAAP reporting purposes, only revenues from policy charges for insurance, administration, and surrender charges are reported as GAAP premiums. This product mix shift contributed to the single digit growth rate in Foreign Life Insurance & Retirement Services GAAP premiums.

Also in Japan, AIG Edison Life has improved the quality and productivity of its sales force resulting in higher sales and improved new business persistency. AIG Star Life is growing first year premiums as a result of new product introductions and an expanded agency force, and is benefiting from growth in the bank annuity market.

However, in March of 2006, Japanese tax authorities are expected to announce a reduction in the amount of premium policyholders may deduct from their Japanese tax returns for certain accident and health products. These products are generally sold by independent agents to corporate clients and thus represent a specific niche market segment and not the mainstream accident and health products sold by AIG in Japan. A reduction in the amount of tax deduction related to these products will make them less attractive to the market and will reduce the level of future sales. In addition, a portion of existing policies may be canceled, and depending on the duration of those policies and other factors, could result in a write-off of deferred acquisition costs. At the current time, management does not believe that such losses, should they

occur, would be material to AIG's consolidated financial condition, results of operations or liquidity.

The Foreign Retirement Services business continues its strong growth based upon its success in Japan and Korea by expanding its extensive distribution network and leveraging AIG's product expertise. Somewhat offsetting this growth were the negative effects on customer demand for certain multi-currency fixed annuity products in Japan stemming from currency exchange rate fluctuations. AIG is introducing annuity products in new markets. In January 2005, AIG Star Life entered into an agreement with the Bank of Tokyo Mitsubishi, one of Japan's largest banks, to market a multi-currency fixed annuity.

Foreign Life Insurance & Retirement Services operations produced 78 percent, 78 percent and 76 percent of Life Insurance & Retirement Services GAAP premiums in 2005, 2004 and 2003, respectively.

AIG transacts business in most major foreign currencies. The following table summarizes the effect of changes in foreign currency exchange rates on the growth of Life Insurance & Retirement Services GAAP premiums.

	2005
Growth in original currency	2.7%
Foreign exchange effect	2.0
Growth as reported in U.S. dollars	4.7%

The growth in net investment income in 2005 and 2004 parallels the growth in general account reserves and surplus for both Foreign and Domestic Life Insurance & Retirement Services companies. Also, net investment income was positively affected by the compounding of previously earned and reinvested net investment income along with the addition of new cash flow from operations available for investment. The global flattening of the yield curve put additional pressure on yields and spreads, which was partially offset with income generated from other investment sources, including income from partnerships. Partnership income was $273 million and $192 million for 2005 and 2004, respectively. As of first quarter 2004, foreign separate accounts were transferred to the general account per Statement of Position 03-1, resulting in increased net investment income volatility. The positive effect of Statement of Position 03-1 on Foreign Life Insurance & Retirement Services net investment income was $1.34 billion and $271 million for 2005 and 2004, respectively. These amounts do not affect operating income as they are offset in incurred policy benefits.

AIG's domestic subsidiaries invest in certain limited liability companies that invest in synthetic fuel production facilities as a means of generating income tax credits. Net investment income includes operating losses of approximately $143 million, $121 million and $108 million, respectively, for 2005, 2004 and 2003 and income taxes includes tax credits and benefits of approximately $203 million, $160 million and $155 million, respectively, for 2005, 2004 and 2003 from these investments. See also Note 12(k) of Notes to Consolidated Financial Statements "Commitments and Contingent Liabilities."

Life Insurance & Retirement Services operating income grew by 12 percent in 2005. Operating income for the AIG Domestic Life insurance line of business was up 8 percent and in line with the growth in GAAP premiums for the current year, due in part to growth in the business base and improved mortality results, offset by higher losses recorded in 2005 from limited partnership investments in synthetic fuel production facilities. Operating income for the home service line of business declined as a result of the continued decline in premiums in force and higher insurance and acquisition expenses, combined with an increase in property casualty losses related to hurricanes. The group life/health business and operating income were affected by non-renewal of cases where acceptable margins could not be achieved. In addition, 2005 results were affected by reserve strengthening related to disability income products totaling $12 million compared to reserve strengthening of $178 million for Superior National and $68 million for all other items in 2004. Operating income for the payout annuities line of business increased 22 percent in line with the growth in policy benefit reserves. The group retirement products business recorded a modest increase in operating income due primarily to higher variable annuity fee income and growth in average reserves. Individual fixed annuity results are higher than last year due primarily to 13 percent growth in average reserves, higher surrender charges and reductions in acquisition cost amortization expense resulting from increased capital losses realized on bonds. Individual variable annuity earnings are lower in 2005 when compared to 2004 principally due to favorable deferred acquisition cost amortization variances attributable to changes in assumptions and realized capital loss activity in 2004.

Foreign Life Insurance & Retirement Services operating income of $5.25 billion for 2005 included $84 million of realized capital gains, and for 2004, operating income of $4.85 billion included $372 million of realized capital gains. Underwriting and investment results before the effects of realized capital gains (losses) increased for all lines of business. On this basis, the life insurance line of business benefited in part from lower amortization of acquisition costs for FAS 97 products, reflective of the increasing investment yields for those portfolios, particularly in Japan. In Southeast Asia, operating income growth attributable to life insurance and deposit-based businesses was partially offset by higher incurred policy benefit costs for contributions to the participating policyholder fund in Singapore, totaling $137 million, related to the settlement of a long disputed local tax issue. Growth in the personal accident & health line of business is generally in line with the growth in premiums and reflects stable profit margins. The group products business grew across all segments and maintained profit margins. The largest contributor to the growth in group products is the pension profit center which enjoyed higher fee income emanating from higher assets under management in Brazil and Southeast Asia. Growth in individual fixed annuities, emanating primarily from Japan, is generally in line with the growth in reserves and net spread rates were maintained. The individual variable annuity line of business also grew in line with the growth in reserves.

The contribution of Life Insurance & Retirement Services operating income to AIG's consolidated income before income taxes, minority interest and cumulative effect of accounting changes amounted to 58 percent in 2005, compared to 53 percent in 2004 and 57 percent in 2003.

Underwriting and Investment Risk

The risks associated with the life and accident & health products are underwriting risk and investment risk. The risk associated with the financial and investment contract products is primarily investment risk.

Underwriting risk represents the exposure to loss resulting from the actual policy experience adversely emerging in comparison to the assumptions made in the product pricing associated with mortality, morbidity, termination and expenses. The emergence of significant adverse experience would require an adjustment to DAC and benefit reserves that could have a substantial effect on AIG's results of operations.

Natural disasters such as hurricanes, earthquakes and other catastrophes have the potential to adversely affect AIG's operating results. Other risks, such as an outbreak of a pandemic disease, such as the Avian Influenza A Virus (H5N1), could adversely affect AIG's business and operating results to an extent that may be only minimally offset by reinsurance programs.

While to date, outbreaks of the Avian Flu continue to occur among poultry or wild birds in a number of countries in Asia, parts of Europe, and recently in Africa, transmission to humans has been rare. If the virus mutates to a form that can be transmitted from human to human, it has the potential to spread rapidly worldwide. If such an outbreak were to take place, early quarantine and vaccination could be critical to containment.

Both the contagion and mortality rate of any mutated H5N1 virus that can be transmitted from human to human are highly speculative. AIG continues to monitor the developing facts. A significant global outbreak could have a material adverse effect on Life Insurance & Retirement Services operating results and liquidity from increased mortality and morbidity rates.

AIG's Foreign Life Insurance & Retirement Services companies generally limit their maximum underwriting exposure on life insurance of a single life to approximately $1.7 million of coverage. AIG's Domestic Life Insurance & Retirement Services companies limit their maximum underwriting exposure on life insurance of a single life to $10 million of coverage in certain circumstances by using yearly renewable term reinsurance. See the discussion under "Liquidity" herein and Note 6 of Notes to Consolidated Financial Statements.

AIRCO acts primarily as an internal reinsurance company for AIG's foreign life operations. This facilitates insurance risk management (retention, volatility, concentrations) and capital planning locally (branch and subsidiary). It also allows AIG to pool its insurance risks and purchase reinsurance more efficiently at a consolidated level, manage global counterparty risk and relationships and manage global life catastrophe risks.

AIG's domestic Life Insurance & Retirement Services operations utilize internal and third-party reinsurance relationships to manage insurance risks and to facilitate capital management strategies. Pools of highly-rated third-party reinsurers are utilized to manage net amounts at risk in excess of retention limits. AIG's domestic life insurance companies also cede excess, non-economic reserves carried on a statutory-basis only on certain term and universal life insurance policies and certain fixed annuities to AIG Life of Bermuda Ltd., a wholly owned Bermuda reinsurer.

AIG generally obtains letters of credit in order to obtain statutory recognition of these intercompany reinsurance transactions. For this purpose, AIG entered into a $2.5 billion syndicated letter of credit facility in December 2004. Letters of credit totaling $2.17 billion were outstanding as of December 31, 2004, and letters of credit for all $2.5 billion were outstanding as of December 31, 2005, all of which relate to life intercompany reinsurance transactions. The letter of credit facility has a ten-year term, but the facility can be reduced or terminated by the lenders beginning after seven years.

In November 2005, AIG entered into a revolving credit facility for an aggregate amount of $3 billion. The facility can be drawn in the form of letters of credit with terms of up to ten years. As of December 31, 2005 and as of the date hereof, $1.86 billion principal amount of letters of credit are outstanding under this facility, of which approximately $494 million relates to life intercompany reinsurance transactions. AIG also obtained approximately $212 million letters of credit on a bilateral basis.

The investment risk represents the exposure to loss resulting from the cash flows from the invested assets, primarily long-term fixed rate investments, being less than the cash flows required to meet the obligations of the expected policy and contract liabilities and the necessary return on investments. See also the discussion under "Liquidity" herein.

To minimize its exposure to investment risk, AIG tests the cash flows from invested assets and policy and contract liabilities using various interest rate scenarios to evaluate investment risk and to confirm that assets are sufficient to pay these liabilities.

AIG actively manages the asset-liability relationship in its foreign operations, as it has been doing throughout AIG's history, even though certain territories lack qualified long-term investments or certain local regulatory authorities may impose investment restrictions. For example, in several Asian countries, the duration of the investments is shorter than the effective maturity of the related policy liabilities. Therefore, there is a risk that the reinvestment of the proceeds at the maturity of the initial investments may be at a yield below that of the interest required for the accretion of the policy liabilities. Additionally, there exists a future investment risk associated with certain policies currently in force which will have premium receipts in the future. That is, the investment of these future premium receipts may be at a yield below that required to meet future policy liabilities.

In 2005, new money investment yields increased in some markets and continued to decrease in others, leading to more frequent adjustments in new business premium rates, credited

rates, and discontinuance of some products. In regard to the inforce business, to maintain an adequate yield to match the interest necessary to support future policy liabilities, management focus is required in both the investment and product management process. Business strategies continue to evolve to maintain profitability of the overall business. As such, in some countries, sales growth may slow for some product lines and accelerate for others.

The investment of insurance cash flows and reinvestment of the proceeds of matured securities and coupons requires active management of investment yields while maintaining satisfactory investment quality and liquidity.

AIG may use alternative investments in certain foreign jurisdictions where interest rates remain low and there are limited long-dated bond markets, including equities, real estate and foreign currency denominated fixed income instruments to extend the duration or increase the yield of the investment portfolio to more closely match the requirements of the policyholder liabilities and DAC recoverability. This strategy has been effectively used in Japan and more recently by Nan Shan in Taiwan. Foreign assets comprised approximately 33 percent of Nan Shan's invested assets at December 31, 2005, slightly below the maximum allowable percentage under current regulation. In response to continued declining interest rates and the volatile exchange rate of the NT dollar, Nan Shan is emphasizing new products with lower implied guarantees, including participating endowments and variable universal life. Although the risks of a continued low interest rate environment coupled with a volatile NT dollar could increase net liabilities and require additional capital to maintain adequate local solvency margins, Nan Shan currently believes it has adequate resources to meet all future policy obligations.

AIG actively manages the asset-liability relationship in its domestic operations. This relationship is more easily managed through the ample supply of appropriate long-term investments.

AIG uses asset-liability matching as a management tool worldwide to determine the composition of the invested assets and appropriate marketing strategies. As a part of these strategies, AIG may determine that it is economically advantageous to be temporarily in an unmatched position due to anticipated interest rate or other economic changes. In addition, the absence of long-dated fixed income instruments in certain markets may preclude a matched asset-liability position in those markets.

A number of guaranteed benefits, such as living benefits or guaranteed minimum death benefits, are offered on certain variable life and variable annuity products. AIG manages its exposure resulting from these long-term guarantees through reinsurance or capital market hedging instruments. See Note 21 of Notes to Consolidated Financial Statements for a discussion of new accounting guidance for these benefits.

DAC for Life Insurance & Retirement Services products arises from the deferral of those costs that vary with, and are directly related to, the acquisition of new or renewal business. Policy acquisition costs for life insurance products are generally deferred and amortized over the premium paying period of the policy. Policy acquisition costs which relate to universal life and investment-type products, including variable and fixed annuities (investment-oriented products) are deferred and amortized, with interest, as appropriate, in relation to the historical and future incidence of estimated gross profits to be realized over the estimated lives of the contracts. Amortization expense includes the effects of current period realized capital gains and losses. With respect to universal life and investment-oriented products, AIG's policy, as appropriate, has been to adjust amortization assumptions for DAC when estimates of current or future gross profits to be realized from these contracts are revised. With respect to variable annuities sold domestically (representing the vast majority of AIG's variable annuity business), the assumption for the long-term annual net growth rate of the equity markets used in the determination of DAC amortization is approximately ten percent. A methodology referred to as "reversion to the mean" is used to maintain this long-term net growth rate assumption, while giving consideration to short-term variations in equity markets. Estimated gross profits include investment income and gains and losses on investments less interest required as well as other charges in the contract less actual mortality and expenses. Current experience and changes in the expected future gross profits are analyzed to determine the effect on the amortization of DAC. The estimation of projected gross profits requires significant management judgment. The elements with respect to the current and projected gross profits are reviewed and analyzed quarterly and are adjusted accordingly.

AIG's variable annuity earnings will be affected by changes in market returns because separate account revenues, primarily composed of mortality and expense charges and asset management fees, are a function of asset values.

DAC for both insurance-oriented and investment-oriented products as well as retirement services products are reviewed for recoverability, which involve estimating the future profitability of current business. This review also involves significant management judgment. If the actual emergence of future profitability were to be substantially different than that estimated, AIG's results of operations could be significantly affected in future periods. See also Note 4 of Notes to Consolidated Financial Statements.

Insurance and Asset Management Invested Assets

AIG's investment strategy is to invest primarily in high quality securities while maintaining diversification to avoid significant exposure to issuer, industry and/or country concentrations. With respect to Domestic General Insurance, AIG's strategy is to invest in longer duration fixed maturity investments to maximize the yields at the date of purchase. With respect to Life Insurance & Retirement Services, AIG's strategy is to produce cash flows required to meet maturing insurance liabilities. See also the discussion under "Operating Review: Life Insurance & Retirement Services Operations" herein. AIG invests in equities for various reasons, including diversifying its overall exposure to interest rate risk. Available for sale bonds and equity securities are subject to declines in fair value. Such changes in fair value are presented in unrealized appreciation or depreciation of investments, net of taxes, as a component of accumulated other comprehensive income. Generally, insurance

regulations restrict the types of assets in which an insurance company may invest. When permitted by regulatory authorities and when deemed necessary to protect insurance assets, including invested assets, from adverse movements in foreign currency exchange rates, interest rates and equity prices, AIG and its insurance subsidiaries may enter into derivative transactions as end users. See also the discussion under "Derivatives" herein.

In certain jurisdictions, significant regulatory and/or foreign governmental barriers exist which may not permit the immediate free flow of funds between insurance subsidiaries or from the insurance subsidiaries to AIG parent.

The following tables summarize the composition of AIG's insurance and asset management invested assets by segment, at December 31, 2005 and 2004:

(dollars in millions)	General Insurance	Life Insurance & Retirement Services	Asset Management	Total	Percent of Total	Percent Distribution Domestic	Percent Distribution Foreign
2005							
Fixed maturities:							
Available for sale, at market value	**$ 50,870**	**$ 273,165**	**$ 34,174**	**$ 358,209**	**66.2%**	**59.2%**	**40.8%**
Held to maturity, at amortized cost	**21,528**	**—**	**—**	**21,528**	**4.0**	**100.0**	**—**
Trading securities, at market value	**—**	**1,073**	**3,563**	**4,636**	**0.9**	**3.3**	**96.7**
Equity securities:							
Common stocks, at market value	**4,930**	**15,558**	**639**	**21,127**	**3.9**	**18.6**	**81.4**
Preferred stocks, at market value	**1,632**	**760**	**—**	**2,392**	**0.4**	**88.8**	**11.2**
Mortgage loans on real estate, policy and collateral loans	**19**	**18,406**	**4,594**	**23,019**	**4.3**	**65.5**	**34.5**
Short-term investments, including time deposits, and cash	**2,787**	**6,844**	**5,815**	**15,446**	**2.8**	**26.1**	**73.9**
Real estate	**603**	**2,729**	**1,710**	**5,042**	**0.9**	**45.2**	**54.8**
Investment income due and accrued	**1,232**	**4,073**	**402**	**5,707**	**1.1**	**56.9**	**43.1**
Securities lending collateral	**4,931**	**42,991**	**11,549**	**59,471**	**11.0**	**87.3**	**12.7**
Other invested assets	**6,272**	**7,805**	**10,459**	**24,536**	**4.5**	**85.7**	**14.3**
Total	**$ 94,804**	**$ 373,404**	**$ 72,905**	**$ 541,113**	**100.0%**	**62.3%**	**37.7%**
2004							
Fixed maturities:							
Available for sale, at market value	$44,376	$259,602	$39,077	$343,055	68.5%	61.2%	38.8%
Held to maturity, at amortized cost	18,294	–	–	18,294	3.7	100.0	–
Trading securities, at market value	–	600	2,384	2,984	0.6	1.2	98.8
Equity securities:							
Common stocks, at market value	4,165	11,280	177	15,622	3.1	21.9	78.1
Preferred stocks, at market value	1,466	565	–	2,031	0.4	91.9	8.1
Mortgage loans on real estate, policy and collateral loans	22	16,858	5,093	21,973	4.4	65.6	34.4
Short-term investments, including time deposits, and cash	2,113	5,515	9,679	17,307	3.4	37.1	62.9
Real estate	592	3,007	326	3,925	0.8	22.8	77.2
Investment income due and accrued	997	4,035	461	5,493	1.1	57.3	42.7
Securities lending collateral	4,889	34,923	9,357	49,169	9.8	86.7	13.3
Other invested assets	5,604	7,072	8,316	20,992	4.2	86.7	13.3
Total	$82,518	$343,457	$74,870	$500,845	100.0%	63.8%	36.2%

Credit Quality

At December 31, 2005, approximately 61 percent of the fixed maturities investments were domestic securities. Approximately 35 percent of such domestic securities were rated AAA by one or more of the principal rating agencies. Approximately six percent were below investment grade or not rated.

A significant portion of the foreign fixed income portfolio is rated by Moody's, S&P or similar foreign services. Similar credit quality rating services are not available in all overseas locations. AIG reviews the credit quality of the foreign portfolio nonrated fixed income investments, including mortgages. At December 31, 2005, approximately 19 percent of the foreign fixed income investments were either rated AAA or, on the basis of AIG's internal analysis, were equivalent from a credit standpoint to securities so rated. Approximately five percent were below investment grade or not rated at that date. A large portion of the foreign fixed income portfolio are sovereign fixed maturity securities supporting the policy liabilities in the country of issuance.

Any fixed income security may be subject to downgrade for a variety of reasons subsequent to any balance sheet date.

Valuation of Invested Assets

AIG has the ability to hold any fixed maturity security to its stated maturity, including those fixed maturity securities classified as available for sale. Therefore, the decision to sell

any such fixed maturity security classified as available for sale reflects the judgment of AIG's management that the security sold is unlikely to provide, on a relative value basis, as attractive a return in the future as alternative securities entailing comparable risks. With respect to distressed securities, the sale decision reflects management's judgment that the risk-discounted anticipated ultimate recovery is less than the value achievable on sale.

The valuation of invested assets involves obtaining a market value for each security. The source for the market value is generally from market exchanges or dealer quotations, with the exception of nontraded securities.

If AIG chooses to hold a security, it evaluates the security for an other-than-temporary impairment in valuation. As a matter of policy, the determination that a security has incurred an other-than-temporary decline in value and the amount of any loss recognition requires the judgment of AIG's management and a continual review of its investments.

In general, a security is considered a candidate for other-than-temporary impairment if it meets any of the following criteria:

- Trading at a significant (25 percent or more) discount to par or amortized cost (if lower) for an extended period of time (nine months or longer);
- The occurrence of a discrete credit event resulting in *(i)* the issuer defaulting on a material outstanding obligation; or *(ii)* the issuer seeking protection from creditors under the bankruptcy laws or any similar laws intended for the court supervised reorganization of insolvent enterprises; or *(iii)* the issuer proposing a voluntary reorganization pursuant to which creditors are asked to exchange their claims for cash or securities having a fair value substantially lower than par value of their claims; or
- In the opinion of AIG's management, it is probable that AIG may not realize a full recovery on its investment, irrespective of the occurrence of one of the foregoing events.

Once a security has been identified as other-than-temporarily impaired, the amount of such impairment is determined by reference to that security's contemporaneous market price and recorded as a charge to earnings.

As a result of these policies, AIG recorded other-than-temporary impairment losses net of taxes of approximately $389 million, $369 million and $1.0 billion in 2005, 2004 and 2003, respectively.

No impairment charge with respect to any one single credit was significant to AIG's consolidated financial condition or results of operations, and no individual impairment loss exceeded 1.0 percent of consolidated net income for 2005.

Excluding the other-than-temporary impairments noted above, the changes in market value for AIG's available for sale portfolio, which constitutes the vast majority of AIG's investments, were recorded in accumulated other comprehensive income as unrealized gains or losses, net of tax.

At December 31, 2005, the fair value of AIG's fixed maturities and equity securities aggregated to $409.8 billion. At December 31, 2005, aggregate unrealized gains after taxes for fixed maturity and equity securities were $10.5 billion. At December 31, 2005, the aggregate unrealized losses after taxes of fixed maturity and equity securities were approximately $2.6 billion.

The effect on net income of unrealized losses after taxes will be further mitigated upon realization, because certain realized losses will be charged to participating policyholder accounts, or realization will result in current decreases in the amortization of certain deferred policy acquisition costs.

At December 31, 2005, unrealized losses for fixed maturity securities and equity securities did not reflect any significant industry concentrations.

The amortized cost of fixed maturities available for sale in an unrealized loss position at December 31, 2005, by contractual maturity, is shown below:

(in millions)	Amortized Cost
Due in one year or less	$ 3,882
Due after one year through five years	25,919
Due after five years through ten years	56,204
Due after ten years	56,786
Total	$142,791

In the twelve months ended December 31, 2005, the pretax realized losses incurred with respect to the sale of fixed maturities and equity securities were $1.6 billion. The aggregate fair value of securities sold was $51.7 billion, which was approximately 97 percent of amortized cost. The average period of time that securities sold at a loss during the twelve months ended December 31, 2005 were trading continuously at a price below book value was approximately three months.

At December 31, 2005, aggregate pretax unrealized gains were $16.1 billion, while the pretax unrealized losses with respect to investment grade bonds, below investment grade bonds and equity securities were $3.3 billion, $404 million and $257 million, respectively. Aging of the pretax unrealized losses with respect to these securities, distributed as a percentage of cost relative to unrealized loss (the extent by which the market value is less than amortized cost or cost), including the number of respective items, was as follows:

	Less than or equal to 20% of Cost[a]			Greater than 20% to 50% of Cost[a]			Greater than 50% of Cost[a]			Total		
Aging (*dollars in millions*)	Cost[a]	Unrealized Loss	Items	Cost[a]	Unrealized Loss	Items	Cost[a]	Unrealized Loss	Items	Cost[a]	Unrealized Loss[b]	Items
Investment grade bonds												
0-6 months	$101,885	$1,984	12,264	$ 36	$ 9	11	$—	$—	—	$101,921	$1,993	12,275
7-12 months	14,271	426	1,749	1	—	1	—	—	—	14,272	426	1,750
>12 months	19,502	791	2,722	450	107	17	5	3	8	19,957	901	2,747
Total	$135,658	$3,201	16,735	$487	$116	29	$ 5	$ 3	8	$136,150	$3,320	16,772
Below investment grade bonds												
0-6 months	$ 3,651	$ 129	852	$111	$ 29	24	$11	$ 6	14	$ 3,773	$ 164	890
7-12 months	1,524	93	338	139	38	34	2	1	15	1,665	132	387
>12 months	1,113	84	225	90	24	23	—	—	11	1,203	108	259
Total	$ 6,288	$ 306	1,415	$340	$ 91	81	$13	$ 7	40	$ 6,641	$ 404	1,536
Total bonds												
0-6 months	$105,536	$2,113	13,116	$147	$ 38	35	$11	$ 6	14	$105,694	$2,157	13,165
7-12 months	15,795	519	2,087	140	38	35	2	1	15	15,937	558	2,137
>12 months	20,615	875	2,947	540	131	40	5	3	19	21,160	1,009	3,006
Total	$141,946	$3,507	18,150	$827	$207	110	$18	$10	48	$142,791	$3,724	18,308
Equity securities												
0-6 months	$ 3,041	$ 113	1,109	$ 75	$ 23	71	$30	$20	42	$ 3,146	$ 156	1,222
7-12 months	573	41	122	169	45	68	6	4	23	748	90	213
>12 months	66	4	26	30	6	13	1	1	29	97	11	68
Total	$ 3,680	$ 158	1,257	$274	$ 74	152	$37	$25	94	$ 3,991	$ 257	1,503

(a) For bonds, represents amortized cost.

(b) As more fully described above, upon realization, certain realized losses will be charged to participating policyholder accounts, or realization will result in a current decrease in the amortization of certain deferred policy acquisition costs.

As stated previously, the valuation for AIG's investment portfolio comes from market exchanges or dealer quotations, with the exception of nontraded securities. AIG considers nontraded securities to mean certain fixed income investments, certain structured securities, direct private equities, limited partnerships, and hedge funds. The aggregate carrying value of these securities at December 31, 2005 was approximately $62 billion.

The methodology used to estimate fair value of nontraded fixed income investments is by reference to traded securities with similar attributes and using a matrix pricing methodology. This technique takes into account such factors as the industry, the security's rating and tenor, its coupon rate, its position in the capital structure of the issuer, and other relevant factors. The change in fair value is recognized as a component of accumulated other comprehensive income, net of tax.

For certain structured securities, the carrying value is based on an estimate of the security's future cash flows pursuant to the requirements of Emerging Issues Task Force Issue No. 99-20, "Recognition of Interest Income and Impairment on Purchased and Retained Beneficial Interests in Securitized Financial Assets." The change in carrying value is recognized in income.

Hedge funds and limited partnerships in which AIG holds in the aggregate less than a five percent interest are carried at fair value. The change in fair value is recognized as a component of accumulated other comprehensive income, net of tax.

With respect to hedge funds and limited partnerships in which AIG holds in the aggregate a five percent or greater interest, AIG uses the equity method to record these investments. The changes in such net asset values are recorded in income.

AIG obtains the fair value of its investments in limited partnerships and hedge funds from information provided by the general partner or manager of each of these investments, the accounts of which are generally audited on an annual basis.

Each of these investment categories is tested to determine if impairment in value exists. Various valuation techniques are used with respect to each category in this determination.

Financial Services Operations

AIG's Financial Services subsidiaries engage in diversified activities including aircraft and equipment leasing, capital markets transactions, consumer finance and insurance premium financing. See also Note 2 of Notes to Consolidated Financial Statements.

Aircraft Finance

AIG's Aircraft Finance operations represent the operations of ILFC, which generates its revenues primarily from leasing new and used commercial jet aircraft to domestic and foreign airlines. Revenues also result from the remarketing of commercial jets for its own account, for airlines and for financial institutions.

ILFC finances its purchases of aircraft primarily through the issuance of a variety of debt instruments. The composite borrowing rates at December 31, 2005, 2004 and 2003 were 5.00 percent, 4.34 percent and 4.53 percent, respectively. See also the discussions under "Capital Resources" and "Liquidity" herein and Notes 2 and 9 of Notes to Consolidated Financial Statements.

ILFC's sources of revenue are principally from scheduled and charter airlines and companies associated with the airline industry. The airline industry is sensitive to changes in economic conditions, cyclical and highly competitive. Airlines and related companies may be affected by political or economic instability, terrorist activities, changes in national policy, competitive pressures on certain air carriers, fuel prices and shortages, labor stoppages, insurance costs, recessions, and other political or economic events adversely affecting world or regional trading markets. ILFC's revenues and income will be affected by its customers' ability to react and cope with the volatile competitive environment in which they operate, as well as ILFC's own competitive environment.

ILFC is exposed to operating loss and liquidity strain through nonperformance of aircraft lessees, through owning aircraft which it would be unable to sell or re-lease at acceptable rates at lease expiration and, in part, through committing to purchase aircraft which it would be unable to lease.

ILFC manages the risk of nonperformance by its lessees with security deposit requirements, through repossession rights, overhaul requirements, and closely monitoring industry conditions through its marketing force. However, there can be no assurance that ILFC would be able to successfully manage the risks relating to the effect of possible future deterioration in the airline industry. Approximately 90 percent of ILFC's fleet is leased to non-U.S. carriers, and this fleet, comprised of the most efficient aircraft in the airline industry, continues to be in high demand from such carriers.

ILFC typically contracts to re-lease aircraft before the end of the existing lease term. For aircraft returned before the end of the lease term, ILFC has generally been able to re-lease such aircraft within two to six months of its return. As a lessor, ILFC considers an aircraft "idle" or "off lease" when the aircraft is not subject to a signed lease agreement or signed letter of intent. ILFC had no aircraft off lease at December 31, 2005. As of March 10, 2006, all new aircraft deliveries in 2006 have been leased, and 76 percent of 2007 new aircraft deliveries have been leased. See also the discussions under "Capital Resources" and "Liquidity" herein.

ILFC sold two portfolios consisting of 34 and 37 aircraft in 2004 and 2003, respectively, to two trusts connected to securitization transactions. Certain of AIG's Life Insurance & Retirement Services businesses purchased a large share of the securities issued in connection with these securitizations, which included both debt and equity securities.

Management formally reviews regularly, and no less frequently than quarterly, issues affecting ILFC's fleet, including events and circumstances that may cause impairment of aircraft values. Management evaluates aircraft in the fleet as necessary, based on these events and circumstances in accordance with Statement of Financial Accounting Standards No. 144 — "Accounting for the Impairment or Disposal of Long-Lived Assets" (FAS 144). ILFC has not recognized any impairment related to its fleet, as the existing service potential of the aircraft in ILFC's portfolio has not been diminished. Further, ILFC has been able to re-lease the aircraft without diminution in lease rates to an extent that would require an impairment write-down. See also the discussions under "Liquidity" herein.

Capital Markets

Capital Markets represents the operations of AIGFP, which engages in a wide variety of financial transactions, including standard and customized interest rate, currency, equity, commodity and credit products and structured borrowings through notes, bonds and guaranteed investment agreements. AIGFP also engages in various commodity and foreign exchange trading, and market-making activities.

As Capital Markets is a transaction-oriented operation, current and past revenues and operating results may not provide a basis for predicting future performance. Also, AIG's Capital Markets operations may be adversely affected by the downgrades in AIG's credit ratings. See "Risk Factors — AIG's Credit Ratings," in Item 1A. Risk Factors for a further discussion of the potential effect of the rating downgrades on AIG's Capital Markets businesses.

AIG's Capital Markets operations derive substantially all their revenues from hedged financial positions entered in connection with counterparty transactions rather than from speculative transactions. AIGFP participates in the derivatives and financial transactions dealer markets conducting, primarily as principal, an interest rate, currency, equity, commodity, energy and credit products business.

As a dealer in financial derivatives, AIGFP marks all derivative and trading transactions to fair value daily. Thus, a gain or loss on each transaction is recognized daily. Under GAAP, in certain instances, gains and losses are required to be recorded in earnings immediately, whereas in other instances, they are required to be recognized over the life of the underlying instruments. AIGFP economically hedges the market risks arising from its transactions, although hedge accounting is not currently being applied to any of the derivatives and related assets and liabilities. Accordingly, revenues and operating income are exposed to volatility resulting from differences in the timing of revenue recognition between the derivatives and the hedged assets and liabilities. Revenues and operating income of the Capital Markets operations and the percentage change in these amounts for any given period are also significantly affected by the number, size and profitability of transactions entered into by these subsidiaries during that

period relative to those entered into during the prior period. Generally, the realization of trading revenues as measured by the receipt of funds is not a significant reporting event as the gain or loss on AIGFP's trading transactions is currently reflected in operating income as the fair values change from period to period.

Derivative transactions are entered into in the ordinary course of Capital Markets operations. Therefore, income on interest rate, currency, equity, commodity, energy and credit derivatives is recorded at fair value, determined by reference to the mark to market value of the derivative or their estimated fair value where market prices are not readily available. The resulting aggregate unrealized gains or losses from the derivative are reflected in the income statement in the current year. Where Capital Markets cannot verify significant model inputs to observable market data and verify the model value to market transactions, Capital Markets values the contract at the transaction price at inception and, consequently, records no initial gain or loss in accordance with Emerging Issues Task Force Issue No. 02-03, "Issues Involved in Accounting for Derivative Contracts Held for Trading Purposes and Contracts Involved in Energy Trading and Risk Management Activities" (EITF 02-03). Such initial gain or loss is recognized over the life of the transaction. Capital Markets periodically reevaluates its revenue recognition under EITF 02-03 based on the observability of market parameters. The mark to fair value of derivative transactions is reflected in the balance sheet in the captions "Unrealized gain on swaps, options and forward transactions," "Unrealized loss on swaps, options and forward transactions," "Trading assets" and "Trading liabilities." Unrealized gains represent the present value of the aggregate of each net receivable by counterparty, and the unrealized losses represent the present value of the aggregate of each net payable by counterparty as of December 31, 2005. These amounts will change from one period to the next due to changes in interest rates, currency rates, equity and commodity prices and other market variables, as well as cash movements, execution of new transactions and the maturing of existing transactions. See also the discussion under "Derivatives" herein and Note 20 of Notes to Consolidated Financial Statements.

Spread income on investments and borrowings is recorded on an accrual basis over the life of the transaction. Investments are classified as securities available for sale and are marked to market with the resulting unrealized gains or losses reflected in accumulated other comprehensive income. U.S. dollar denominated borrowings are carried at cost, while borrowings in any currency other than the U.S. dollar result in unrealized foreign exchange gains or losses reported in income. AIGFP hedges the economic exposure on its investments and borrowings through its derivatives portfolio. The requirements under FAS 133 hedge accounting were not met for these hedge transactions for the years ending December 31, 2005, 2004 and 2003. Thus, these hedges are marked to fair value with the unrealized gains or losses reported in income.

Consumer Finance

Domestically, AIG's Consumer Finance operations are principally conducted through AGF. AGF derives a substantial portion of its revenues from finance charges assessed on outstanding mortgages, home equity loans, secured and unsecured consumer loans and retail merchant financing. The real estate loans include first or second mortgages on residential real estate generally having a maximum term of 360 months, and are considered non-conforming. These loans may be closed-end accounts or open-end home equity lines of credit and may be fixed-rate or adjustable rate products. The secured consumer loans are secured by consumer goods, automobiles, or other personal property. Both secured and unsecured consumer loans generally have a maximum term of 60 months. The core of AGF's originations are sourced through its branches. However, a significant volume of real estate loans are also originated through broker relationships, and to lesser extents, through correspondent relationships and direct mail solicitations.

Many of AGF's borrowers are non-conforming, non-prime or sub-prime. Current economic conditions, such as interest rate and employment, have a direct effect on the borrowers' ability to repay these loans. AGF manages the credit risk inherent in its portfolio by using credit scoring models at the time of credit applications, established underwriting criteria, and in certain cases, individual loan reviews. AGF's Credit Strategy and Policy Committee monitors the quality of the finance receivables portfolio on a monthly basis when determining the appropriate level of the allowance for finance receivable losses. The Credit Strategy and Policy Committee bases its conclusions on quantitative analyses, qualitative factors, current economic conditions and trends, and each committee member's experience in the consumer finance industry. Through 2005, the credit quality of AGF's finance receivables continues to be strong.

Overseas operations, particularly those in emerging markets, provide credit cards, personal and auto loans, term deposits, savings accounts, sales finance and mortgages.

Consumer Finance operations are exposed to loss when contractual payments are not received. Credit loss exposure is managed through tight underwriting controls, mix of loans, collateral, and collection efficiency.

Financial Services operations for 2005, 2004 and 2003 were as follows:

(in millions)	**2005**	2004	2003
Revenues[a]:			
Aircraft Finance[b]	**$ 3,578**	$ 3,136	$ 2,897
Capital Markets[c][d]	**3,260**	1,278	595
Consumer Finance[e]	**3,613**	2,978	2,642
Other	**74**	103	108
Total	**$10,525**	$ 7,495	$ 6,242
Operating income (loss)[a]:			
Aircraft Finance	**$ 679**	$ 642	$ 672
Capital Markets[d]	**2,661**	662	(188)
Consumer Finance[f]	**901**	808	623
Other, including intercompany adjustments	**35**	68	75
Total	**$ 4,276**	$ 2,180	$ 1,182

(a) Includes the effect of hedging activities that do not qualify for hedge accounting treatment under FAS 133, including the related foreign exchange gains and losses. For 2005, 2004 and 2003, the effect was $(34) million, $(27) million and $49 million, respectively, in operating income for Aircraft Finance and $2.01 billion, $(122) million and $(1.01) billion in both revenues and operating income for Capital Markets.

(b) Revenues are primarily from ILFC aircraft lease rentals.

(c) Revenues, shown net of interest expense, are primarily from hedged financial positions entered into in connection with counterparty transactions and the effect of hedging activities that do not qualify for hedge accounting treatment under FAS 133 described in (a) above.

(d) Certain transactions entered into by AIGFP generate tax credits and benefits which are included in income taxes in the consolidated statement of income. The amount of such tax credits and benefits for the years ended December 31, 2005, 2004 and 2003 are $67 million, $107 million and $123 million, respectively.

(e) Revenues are primarily finance charges.

(f) Includes $62 million of catastrophe related losses for 2005.

Financial Services Results

Financial Services operating income increased in 2005 compared to 2004 as well as 2004 compared to 2003. Fluctuations in revenues and operating income from quarter to quarter are not unusual because of the transaction-oriented nature of Capital Markets operations and the effect of hedging activities that do not qualify for hedge accounting under FAS 133. Capital Markets operating income was also negatively affected in 2004 by the costs of the PNC settlement. See Item 3. Legal Proceedings.

To the extent the Financial Services subsidiaries, other than AIGFP, use derivatives to economically hedge their assets or liabilities with respect to their future cash flows, and such hedges do not qualify for hedge accounting treatment under FAS 133, the changes in fair value of such derivatives are recorded in realized capital gains (losses) or other revenues.

Financial market conditions in 2005 compared with 2004 were characterized by a general flattening of interest rate yield curves across fixed income markets globally, some tightening of credit spreads and equity valuations that were slightly higher. AIGFP's 2005 results were adversely affected by customer uncertainty surrounding the negative actions of the rating agencies and the ongoing investigations, as well as the negative effect on its structured notes business of AIG being unable to fully access the capital markets during 2005.

Financial market conditions in 2004 compared with 2003 were characterized by interest rates which were broadly unchanged across fixed income markets globally, a tightening of credit spreads and higher equity valuations. Capital Markets results in 2004 compared with 2003 reflected a shift in product activity to respond to these conditions.

The most significant component of Capital Markets operating expenses is compensation, which was approximately $481 million, $497 million and $616 million in 2005, 2004 and 2003, respectively. The amount of compensation was not affected by gains and losses not qualifying for hedge accounting treatment under FAS 133.

ILFC continued to see net improvements in lease rates, an increase in demand for the newer, modern, fuel efficient aircraft comprising the bulk of ILFC's fleet, and an increasing level of interest from traditional buyers, third-party investors and debt providers for the purchase of aircraft from ILFC's extensive lease portfolio. During 2005, ILFC's revenues and operating income also increased as a result of adding more aircraft to its fleet and earning higher revenues on existing aircraft. However, these increases were offset by increasing interest rates, fewer aircraft sales, and leasing related and other reserves.

During the fourth quarter of 2004, ATA Airlines and related entities (ATA) filed for protection under Chapter 11 of the U.S. Bankruptcy Code. On the basis of estimates of the probable outcome of the ATA bankruptcy, ILFC recorded pre-tax charges aggregating $54 million in the fourth quarter of 2004 to write down the value of the ATA securities and guarantees.

Consumer Finance operations, both domestically and internationally, did very well with increased revenues and operating income. Domestically, the Consumer Finance operations had a record year in 2005. The relatively low interest rate environment contributed to a high level of mortgage refinancing activity. Real estate finance receivables increased 21 percent during 2005. Despite high energy costs, the U.S. economy continued to expand during the year improving consumer credit quality. Both AGF's charge-off ratio and delinquency ratio improved over prior years. However, AGF incurred charges of approximately $62 million for the estimated effect of Hurricane Katrina on customers in the Gulf Coast areas affected by the storm. A new bankruptcy law went into effect in October 2005. Consumers, including some of AGF's customers, filed for personal bankruptcy protection under the old law in record numbers in third quarter 2005 ahead of the new law's effective date. AGF does not anticipate a significant effect on its earnings from this new law because 80 percent of its finance receivables are real estate loans with adequate collateral and conservative loan-to-value ratios.

Foreign Consumer Finance operations performed well, as the operations in Poland, Argentina and AIG Federal Savings Bank recorded strong earnings growth. The Hong Kong

businesses experienced solid loan and earnings growth in a strengthening economy.

Financial Services operating income represented 28 percent of AIG's consolidated income before income taxes, minority interest and cumulative effect of accounting changes in 2005. This compares to 15 percent and 10 percent in 2004 and 2003, respectively. The increase in contribution percentage in 2005 compared to 2004 and 2003 was primarily due to the fluctuation in earnings resulting from derivatives that did not qualify for hedge accounting under FAS 133 and the reduction in General Insurance operating income in 2005.

Financial Services Invested Assets

The following table is a summary of the composition of AIG's Financial Services invested assets at December 31, 2005 and 2004. See also the discussions under "Operating Review — Financial Services Operations", "Capital Resources" and "Derivatives" herein.

	2005		2004	
(dollars in millions)	**Invested Assets**	**Percent of Total**	Invested Assets	Percent of Total
Flight equipment primarily under operating leases, net of accumulated depreciation	**$ 36,245**	**24.1%**	$ 32,130	21.6%
Finance receivables, net of allowance	**27,995**	**18.6**	23,574	15.9
Unrealized gain on swaps, options and forward transactions	**18,695**	**12.4**	22,670	15.3
Securities available for sale, at market value	**37,511**	**24.9**	31,225	21.0
Trading securities, at market value	**6,499**	**4.3**	2,746	1.8
Securities purchased under agreements to resell, at contract value	**14,519**	**9.7**	26,272	17.7
Trading assets	**1,204**	**0.8**	3,433	2.3
Spot commodities	**92**	**0.1**	534	0.4
Other, including short-term investments	**7,615**	**5.1**	5,982	4.0
Total	**$150,375**	**100.0%**	$148,566	100.0%

As previously discussed, the cash used for the purchase of flight equipment is derived primarily from the proceeds of ILFC's debt financings. The primary sources for the repayment of this debt and the interest expense thereon are the cash flow from operations, proceeds from the sale of flight equipment and the rollover and refinancing of the prior debt. During 2005, ILFC acquired flight equipment costing $6.19 billion. See also the discussion under "Operating Review — Financial Services Operations" and "Capital Resources" herein.

At December 31, 2005, ILFC had committed to purchase 338 new and used aircraft deliverable from 2006 through 2015 at an estimated aggregate purchase price of $23.3 billion and had options to purchase 16 new aircraft at an estimated aggregate purchase price of $1.5 billion. As of March 10, 2006, ILFC has entered into leases for all of the new aircraft to be delivered in 2006, 65 of 85 of the new aircraft to be delivered in 2007 and 11 of 155 of the new aircraft to be delivered subsequent to 2007. ILFC will be required to find customers for any aircraft currently on order and any aircraft to be ordered, and it must arrange financing for portions of the purchase price of such equipment. ILFC has been successful to date both in placing its new aircraft on lease or under sales contract and obtaining adequate financing, but there can be no assurance that such success will continue in future environments.

AIG's Consumer Finance operations provide a wide variety of consumer finance products, including real estate mortgages, credit cards, consumer loans, retail sales finance and credit-related insurance to customers both domestically and overseas, particularly in emerging markets. These products are funded through a combination of deposits and various borrowings including commercial paper and medium term notes. AIG's Consumer Finance operations are exposed to credit risk and risk of loss resulting from adverse fluctuations in interest rates. Over half of the loan balance is related to real estate loans which are substantially collateralized by the related properties.

With respect to credit losses, the allowance for finance receivable losses is maintained at a level considered adequate to absorb anticipated credit losses existing in that portfolio.

Capital Markets derivative transactions are carried at market value or at estimated fair value when market prices are not readily available. AIGFP reduces its economic risk exposure through similarly valued offsetting transactions including swaps, trading securities, options, forwards and futures. The estimated fair values of these transactions represent assessments of the present value of expected future cash flows. These transactions are exposed to liquidity risk if AIGFP were required to sell or close out the transactions prior to maturity. AIG believes that the effect of any such event would not be significant to AIG's financial condition or its overall liquidity. See also the discussion under "Operating Review — Financial Services Operations" and "Derivatives" herein.

AIGFP uses the proceeds from the issuance of notes, bonds and GIA borrowings to invest in a diversified portfolio of securities, including securities available for sale, at market, and derivative transactions. The funds may also be temporarily invested in securities purchased under agreements to resell. The proceeds from the disposal of the aforementioned securities available for sale and securities purchased under agreements to resell have been used to fund the maturing GIAs or other AIGFP financings, or invest in new assets. See also the discussion under "Capital Resources" herein.

Securities available for sale is predominately a portfolio of fixed income securities, where the individual securities have

varying degrees of credit risk. At December 31, 2005, the average credit rating of this portfolio was AA+ or the equivalent thereto as determined through rating agencies or internal review. AIGFP has also entered into credit derivative transactions to economically hedge its credit risk associated with $125 million of these securities. Securities deemed below investment grade at December 31, 2005 amounted to approximately $166 million in fair value representing 0.4 percent of the total AIGFP securities available for sale. There have been no significant downgrades through March 1, 2006. If its securities available for sale portfolio were to suffer significant default and the collateral held declined significantly in value with no replacement or the credit default swap counterparty failed to perform, AIGFP could have a liquidity strain. AIG guarantees AIGFP's payment obligations, including its debt obligations.

AIGFP's risk management objective is to minimize interest rate, currency, commodity and equity risks associated with its securities available for sale. That is, when AIGFP purchases a security for its securities available for sale investment portfolio, it simultaneously enters into an offsetting internal hedge such that the payment terms of the hedging transaction offset the payment terms of the investment security, which achieves the economic result of converting the return on the underlying security to U.S. dollar LIBOR plus or minus a spread based on the underlying profit on each security on the initial trade date. The market risk associated with such internal hedges is managed on a portfolio basis, with third-party hedging transactions executed as necessary. As hedge accounting treatment is not achieved in accordance with FAS 133, the unrealized gains and losses on the securities related economic hedges are reflected in operating income, whereas the unrealized gains and losses on the underlying securities resulting from changes in interest rates, currency rates, commodity and equity prices, are recorded in accumulated other comprehensive income. When a security is sold, the related hedging transaction is terminated, and the realized gain or loss with respect to this security is then recorded in operating income.

Securities purchased under agreements to resell are treated as collateralized financing transactions. AIGFP takes possession of or obtains a security interest in securities purchased under agreements to resell. AIGFP further minimizes its credit risk by monitoring counterparty credit exposure and, when it deems necessary, it requires additional collateral to be deposited.

AIGFP also conducts, as principal, trading activities in foreign exchange, and commodities, primarily precious metals. AIGFP owns inventories in the commodities, which it records at the lower of cost or market, in which it trades and may reduce the exposure to market risk through the use of swaps, forwards, futures, and option contracts. AIGFP uses derivatives to manage the economic exposure of its various trading positions and transactions from adverse movements of interest rates, foreign currency exchange rates and commodity prices. AIGFP supports its trading activities largely through trading liabilities, unrealized losses on swaps, short-term borrowings, securities sold under agreements to repurchase and securities and commodities sold but not yet purchased. See also the discussions under "Capital Resources" herein and Note 20 of Notes to Consolidated Financial Statements.

Trading securities, at market value, and securities and spot commodities sold but not yet purchased, at market value, are marked to market daily with the unrealized gain or loss being recognized in income at that time. These trading securities are held to meet the short-term risk management objectives of Capital Markets operations.

The gross unrealized gains and gross unrealized losses of Capital Markets operations included in the financial services assets and liabilities at December 31, 2005 were as follows:

(in millions)	Gross Unrealized Gains	Gross Unrealized Losses
Securities available for sale, at market value[(a)]	$ 802	$ 863
Unrealized gain/loss on swaps, options and forward transactions[(b)]	18,695	12,740

(a) See also Note 8(h) of Notes to Consolidated Financial Statements.

(b) These amounts are also presented as the respective balance sheet amounts.

The senior management of AIG defines the policies and establishes general operating parameters for Capital Markets operations. AIG's senior management has established various oversight committees to review the various financial market, operational and credit issues of the Capital Markets operations. The senior management of AIGFP reports the results of its operations to and reviews future strategies with AIG's senior management.

AIGFP actively manages the exposures to limit potential losses, while maximizing the rewards afforded by these business opportunities. In doing so, AIGFP must continually manage a variety of exposures including credit, market, liquidity, operational and legal risks.

AIGFP held a large portfolio of privately negotiated financing transactions with institutional counterparties in the United Kingdom. Certain provisions in the UK Finance Bill that was published by the House of Commons on March 22, 2005 caused AIGFP's counterparties to exercise early unwind rights and terminate these transactions during the first and second quarters of 2005. Although the unwinding of these transactions did not cause AIGFP to suffer any losses, the unwinds did result in AIGFP not realizing spread income that AIGFP expected it would have realized had the transactions remained outstanding. The aggregate reduction in 2005 operating income attributable to such foregone accrual earnings was approximately $75 million.

Asset Management Operations

AIG's Asset Management operations comprise a wide variety of investment-related services and investment products including institutional and retail asset management, broker dealer services and spread-based investment business from the sale of GICs. Such services and products are offered to individuals and institutions both domestically and overseas.

As discussed above, AIG Retirement Services operations are reported with Life Insurance operations. Therefore, Asset Management operations represent the results of AIG's asset management and brokerage services operations, mutual fund operations and the foreign and domestic GIC operations.

Asset Management revenues and operating income for 2005, 2004 and 2003 were as follows:

(in millions)	**2005**	2004	2003
Revenues:			
Guaranteed Investment Contracts	**$3,547**	$3,192	$2,619
Institutional Asset Management	**1,195**	1,049	671
Brokerage Services and Mutual Funds	**257**	249	206
Other	**326**	224	155
Total	**$5,325**	$4,714	$3,651
Operating income:			
Guaranteed Investment Contracts[(a)]	**$1,185**	$1,328	$ 885
Institutional Asset Management[(b)]	**686**	515	227
Brokerage Services and Mutual Funds	**66**	70	60
Other	**316**	212	144
Total	**$2,253**	$2,125	$1,316

(a) The effect of hedging activities that do not qualify for hedge accounting treatment under FAS 133 was $149 million, $313 million and $230 million for 2005, 2004 and 2003, respectively.

(b) Includes the results of certain AIG managed private equity and real estate funds that are consolidated effective December 31, 2003 pursuant to FIN46R, "Consolidation of Variable Interest Entities". For 2005 and 2004, operating income includes $261 million and $195 million of third-party limited partner earnings offset in Minority interest expense.

Asset Management Results

Asset Management operating income increased in 2005 as a result of a diversified global product portfolio. The operating income growth was driven by growth in institutional assets under management and the associated fee revenue along with strong realized gains on sales of real estate investments and performance fees earned on various private equity investments. The level of gains and performance based fees are contingent upon various fund closings, maturity levels and market conditions, and by their nature, are not predictable. Therefore, the effect on the segment's future earnings may vary from period to period. The revenues and operating income with respect to the segment are largely affected by the general conditions in the equity and credit markets. The increases in full year segment results were achieved despite the run-off of the existing GIC portfolio and the delay in launching AIG's domestic matched investment program. GICs are sold domestically and abroad to both institutions and individuals. These products are written on an opportunistic basis when market conditions are favorable. A significant portion of the GIC portfolio consists of floating rate obligations. AIG has entered into hedges to manage against increases in short-term interest rates. AIG continues to believe these hedges are economically effective but do not qualify for hedge accounting under FAS 133. As a result, continued increases in short-term interest rates will negatively affect operating income in this segment. A positive benefit to realized capital gains (losses) will offset any negative trend in operating income. GIC revenues include income from SunAmerica partnerships supporting the GIC line of business and are significantly affected by performance in the equity markets. Thus, revenues, operating income and cash flow attributable to GICs will vary from one reporting period to the next. The decline in GIC operating income compared to 2004 reflects tighter spreads in the GIC portfolio, partially offset by improved partnership returns. Spread compression has occurred as the base portfolio yield declined due to an increase in the cost of funds in the short-term floating rate portion of the GIC portfolio, only partially offset by increased investment income from the floating rate assets backing the portfolio.

In September 2005, AIG launched a $10 billion matched investment program in the Euromarkets under which AIG debt securities will be issued. AIG also expects to launch a matched investment program in the domestic market which, along with the Euro program, will become AIG's principal spread-based investment activity. However, in light of recent developments, the timing of the launch of the domestic program is uncertain. Because AIG's credit spreads in the capital markets have widened following the ratings declines, there may be a reduction in the earnings on new business in AIG's institutional spread based funding business.

Asset Management operating income represented 15 percent of AIG's consolidated income before income taxes, minority interest and cumulative effect of accounting changes in 2005. This compares to 14 percent and 11 percent in 2004 and 2003, respectively.

At December 31, 2005, AIG's third-party assets under management, including both retail mutual funds and institutional accounts, was approximately $62 billion compared to $51 billion at year end 2004. The aggregate GIC reserve was $48.8 billion at December 31, 2005 compared to $53.8 billion at year end 2004.

Other Operations

Other operations include AIG's equity in certain partially owned companies, the distributions on the liabilities connected to trust preferred stock, as well as the unallocated corporate expenses of the parent holding company and other miscellaneous income and expenses. Other income (loss) amounted to $(2.48) billion, $(560) million and $(1.90) billion in 2005, 2004 and 2003, respectively. AIG's equity in certain partially owned subsidiaries includes $312 million and $96 million in catastrophe losses in 2005 and 2004, respectively. Included in the 2005 amount is approximately $1.6 billion for the settlements described under Item 3. Legal Proceedings. See also Notes 12(i) and 24 of Notes to Consolidated Financial Statements.

Other realized capital gains (losses) amounted to $225 million, $(227) million and $(643) million for 2005, 2004 and 2003, respectively.

Capital Resources

At December 31, 2005, AIG had total consolidated shareholders' equity of $86.32 billion and total consolidated borrowings of $109.85 billion. At that date, $99.42 billion of such borrowings were either not guaranteed by AIG or were matched borrowings under obligations of guaranteed investment agreements (GIAs), liabilities connected to trust preferred stock, or matched notes and bonds payable.

Borrowings

At December 31, 2005, AIG's net borrowings were $10.43 billion after reflecting amounts that were matched borrowings under AIGFP's obligations of GIAs, matched notes and bonds payable, amounts not guaranteed by AIG and liabilities connected to trust preferred stock. The following table summarizes borrowings outstanding at December 31, 2005 and 2004:

December 31, *(in millions)*	2005	2004
AIG's net borrowings	**$ 10,425**	$ 8,498
Liabilities connected to trust preferred stock	**1,391**	1,489
AIGFP		
GIAs	**20,811**	18,919
Matched notes and bonds payable	**24,950**	22,257
Borrowings not guaranteed by AIG	**52,272**	45,736
Total debt	**$109,849**	$96,899

Borrowings issued or guaranteed by AIG and those borrowings not guaranteed by AIG at December 31, 2005 and 2004 were as follows:

December 31, *(in millions)*	2005	2004
AIG borrowings:		
Medium term notes	**$ 112**	$ 667
Notes and bonds payable	**4,495**	2,980
Loans and mortgages payable	**814**	349
Total	**5,421**	3,996
Borrowings guaranteed by AIG:		
AIGFP		
GIAs	**20,811**	18,919
Notes and bonds payable	**26,463**	22,695
Total	**47,274**	41,614
AIG Funding, Inc. commercial paper	**2,694**	2,969
AGC Notes and bonds payable	**797**	1,095
Liabilities connected to trust preferred stock	**1,391**	1,489
Total borrowings issued or guaranteed by AIG	**57,577**	51,163
Borrowings not guaranteed by AIG:		
ILFC		
Commercial paper	**2,615**	2,670
Medium term notes	**4,689**	5,972
Notes and bonds payable[(a)]	**19,026**	15,734
Loans and mortgages payable	**–**	40[(b)]
Total	**26,330**	24,416
AGF		
Commercial paper	**3,423**	3,686
Medium term notes	**17,736**	13,709
Notes and bonds payable	**983**	1,585
Total	**22,142**	18,980
Commercial paper:		
AIG Credit Card Company (Taiwan)	**476**	359
AIG Finance (Taiwan) Limited	**–**	9
Total	**476**	368
Loans and mortgages payable:		
AIGCFG	**864**	792
AIG Finance (Hong Kong) Limited	**183**	49
Total	**1,047**	841
Other Subsidiaries	**927**	832
Variable Interest Entity debt:		
AIG Global Investment Group	**140**	165
AIG Global Real Estate Investment	**977**	8
AIG SunAmerica	**233**	126
Total	**1,350**	299
Total borrowings not guaranteed by AIG	**52,272**	45,736
Total debt	**$109,849**	$96,899

(a) Includes borrowings under Export Credit Facility of $2.6 billion.
(b) Represents capital lease obligations.

For a description of the effects on AIG's capital resources, including the cost of borrowing, of recent downgrades and rating actions by the major rating agencies, see the discussion under "Outlook" herein and "Risk Factors — AIG's Credit Ratings," in Item 1A. Risk Factors as well as Note 9 of Notes to Consolidated Financial Statements.

During 2005, AIG did not issue any medium term notes, and $555 million of previously issued notes matured.

On September 30, 2005, AIG sold $1.5 billion principal amount of notes in a Rule 144A/Regulation S offering, $500 million of which bear interest at a rate of 4.700 percent per annum and mature in 2010 and $1.0 billion of which bear interest at a rate of 5.05 percent per annum and mature in 2015. The notes are senior unsecured obligations of AIG and rank equally with all of AIG's other senior debit outstanding. AIG has agreed to use commercially reasonable efforts to consummate an exchange offer for the notes pursuant to an effective registration statement within 360 days of the date on which the notes were issued.

AIG intends to continue its customary practice of issuing debt securities from time to time to meet its financing needs

and those of certain of its subsidiaries for general corporate purposes, as well as for a matched investment program.

In September 2005, AIG entered into loan agreements with third-party banks and borrowed a total of $600 million under the loan agreements on an unsecured basis, $500 million of which matures in August 2006 but can be extended by AIG for an additional seven-month period and $100 million of which matures in September 2006.

AIGFP uses the proceeds from the issuance of notes and bonds and GIA borrowings to invest in a diversified portfolio of securities and derivative transactions. The borrowings may also be temporarily invested in securities purchased under agreements to resell. AIG guarantees the obligations of AIGFP under AIGFP's notes and bonds and GIA borrowings. See also the discussions under "Operating Review," "Liquidity" and "Derivatives" herein and Notes 1, 8, 9 and 20 of Notes to Consolidated Financial Statements.

AIGFP has a Euro Medium Term Note Program under which an aggregate nominal amount of up to $10.0 billion of notes may be outstanding at any one time. The program provides that additional notes may be issued to replace matured or redeemed notes. As of December 31, 2005, $3.48 billion of notes were outstanding under the program, including $221 million resulting from foreign exchange translation into U.S. dollars. Notes issued under this program are included in Notes and Bonds Payable in the preceding table of borrowings.

AIG Funding, Inc. (AIG Funding), through the issuance of commercial paper, helps fulfill the short-term cash requirements of AIG and its subsidiaries. AIG Funding intends to continue to meet AIG's funding requirements through the issuance of commercial paper guaranteed by AIG. The issuance of AIG Funding's commercial paper is subject to the approval of AIG's Board of Directors.

AIG and AIG Funding are parties to unsecured syndicated revolving credit facilities aggregating $2.75 billion, consisting of $1.375 billion in a 364-day revolving credit facility that expires in July of 2006 and $1.375 billion in a five-year revolving credit facility that expires in July of 2010. The 364-day facility allows for the conversion by AIG of any outstanding loans at expiration into one-year term loans. The facilities can be used for general corporate purposes and also to provide backup for AIG's commercial paper programs administered by AIG Funding. AIG expects to replace or extend these credit facilities on or prior to their expiration. There are currently no borrowings outstanding under these facilities, nor were any borrowings outstanding as of December 31, 2005.

In November 2005, AIG and AIG Funding entered into a 364-day revolving credit facility for an aggregate amount of $3 billion, which can be drawn in the form of loans or letters of credit. The credit facility expires in November 2006 but allows for the issuance of letters of credit with terms of up to ten years and provides for the conversion by AIG of any outstanding loans at expiration into one-year term loans. The facility can be used for general corporate purposes, including providing backup for AIG's commercial paper programs administered by AIG Funding and obtaining letters of credit to secure obligations under insurance and reinsurance transactions. There are currently no loans outstanding under the facility, nor were any loans outstanding as of December 31, 2005. As of such dates, $1.14 billion was available to be drawn under the facility, with the remainder having been drawn in the form of letters of credit.

AIG is also a party to an unsecured 364-day inter-company revolving credit facility provided by certain of its subsidiaries aggregating $2 billion that expires in October of 2006. The facility allows for the conversion of any outstanding loans at expiration into one-year term loans. The facility can be used for general corporate purposes and also to provide backup for AIG's commercial paper programs. AIG expects to replace or extend this credit facility on or prior to its expiration. There are currently no borrowings outstanding under the inter-company facility, nor were any borrowings outstanding as of December 31, 2005.

As of November 2001, AIG guaranteed the notes and bonds of AGC. During 2005, $300 million of previously issued notes matured.

ILFC fulfills its short term cash requirements through the issuance of commercial paper. The issuance of commercial paper is subject to the approval of ILFC's Board of Directors. The commercial paper issued by ILFC is not guaranteed by AIG. ILFC is a party to unsecured syndicated revolving credit facilities aggregating $6.0 billion at December 31, 2005. The facilities can be used for general corporate purposes and also to provide backup for ILFC's commercial paper program. They consist of $2.0 billion in a 364-day revolving credit facility that expires in October 2006, with a one-year term out option, $2.0 billion in a five-year revolving credit facility that expires in October 2009 and $2.0 billion in a five-year revolving credit facility that expires in October 2010. ILFC expects to replace or extend these credit facilities on or prior to their expiration. There are currently no borrowings outstanding under these facilities, nor were any borrowings outstanding as of December 31, 2005.

ILFC was a party to two 180-day revolving credit facilities aggregating to $1.0 billion, each of which expired in 2005.

At December 31 2005, ILFC had increased the aggregate principal amount outstanding of its medium term and long-term notes. The foreign exchange adjustment for the foreign currency denominated debt was $197 million at December 31, 2005 and $1.2 billion at December 31, 2004. ILFC had $13.13 billion of debt securities registered for public sale at December 31, 2005. As of December 31, 2005, $8.66 billion of debt securities were issued. In addition, ILFC has a Euro Medium Term Note Program for $7.0 billion, under which $4.98 billion in notes were sold through December 31, 2005. ILFC has substantially eliminated the currency exposure arising from foreign-currency denominated notes by economically hedging that portion of the note exposure not already offset by Euro denominated operating lease payments, although such hedges do not qualify for hedge accounting treatment under FAS 133. Notes issued under this program are included in Notes and Bonds Payable in the preceding table of borrowings.

ILFC had a $4.3 billion Export Credit Facility (ECA) for use in connection with the purchase of approximately 75 aircraft delivered through 2001. This facility was guaranteed by

various European Export Credit Agencies. The interest rate varies from 5.75 percent to 5.90 percent on these amortizing ten-year borrowings depending on the delivery date of the aircraft. At December 31, 2005, ILFC had $1.2 billion outstanding under this facility. The debt is collateralized by a pledge of the shares of a subsidiary of ILFC, which holds title to the aircraft financed under the facility.

In May 2004, ILFC entered into a similarly structured ECA for up to a maximum of $2.64 billion for Airbus aircraft to be delivered through May 31, 2005. The facility has since been extended to include aircraft to be delivered through May 31, 2006. The facility becomes available as the various European Export Credit Agencies provide their guarantees for aircraft based on a six-month forward-looking calendar, and the interest rate is determined through a bid process. At December 31, 2005, ILFC had $1.4 billion outstanding under this facility. Borrowings with respect to these facilities are included in Notes and Bonds Payable in the preceding table of borrowings.

In August 2004, ILFC received a commitment for an Ex-Im Bank comprehensive guarantee in the amount of $1.68 billion to support the financing of up to 30 new Boeing aircraft. The initial delivery period from September 1, 2004 through August 31, 2005 has been extended by ILFC to August 31, 2006. ILFC did not have any borrowings outstanding under this facility at December 31, 2005. From time to time, ILFC enters into various bank financings. As of December 31, 2005 the total funded amount was $1.4 billion. The financings mature through 2010. One tranche of one of the loans totaling $410 million was funded in Japanese yen and swapped to U.S. dollars.

In December of 2005, ILFC entered into two tranches of junior subordinated debt totaling $1.0 billion. Both mature on December 21, 2065, but each tranche has a different call option. The $600 million tranche has a call date of December 21, 2010 and the $400 million tranche has a call date of December 21, 2015. The note with the 2010 call date has a fixed interest rate of 5.90 percent for the first five years. The note with the 2015 call date has a fixed interest rate of 6.25 percent for the first ten years. Both tranches have interest rate adjustments if the call option is not exercised. The new interest rate is a floating quarterly reset rate based on the initial credit spread plus the highest of (i) 3 month LIBOR, (ii) 10-year constant maturity treasury and (iii) 30-year constant maturity treasury.

The proceeds of ILFC's debt financing are primarily used to purchase flight equipment, including progress payments during the construction phase. The primary sources for the repayment of this debt and the interest expense thereon are the cash flow from operations, proceeds from the sale of flight equipment and the rollover and refinancing of the prior debt. AIG does not guarantee the debt obligations of ILFC. See also the discussions under "Operating Review" and "Liquidity" herein.

AGF fulfills its short term cash requirements through the issuance of commercial paper. The issuance of commercial paper is subject to the approval of AGF's Board of Directors. The commercial paper issued by AGF is not guaranteed by AIG. AGF is a party to unsecured syndicated revolving credit facilities which, as of December 31, 2005 aggregated to $4.25 billion, consisting of $2.125 billion in a 364-day revolving credit facility that expires in July 2006 and $2.125 billion in a five-year revolving credit facility that expires in July 2010. The 364-day facility allows for the conversion by AGF of any outstanding loan at expiration into a one-year term loan. The facilities can be used for general corporate purposes and also to provide backup for AGF's commercial paper programs. AGF expects to replace or extend these credit facilities on or prior to their expiration. There are currently no borrowings under these AGF facilities, nor were any borrowings outstanding as of December 31, 2005.

During 2005, AGF issued $5.44 billion of fixed rate and variable rate medium term notes ranging in maturities from two to ten years. As of December 31, 2005, notes aggregating $17.74 billion were outstanding with maturity dates ranging from 2006 to 2015 at interest rates ranging from 1.65 percent to 7.50 percent. To the extent deemed appropriate, AGF may enter into swap transactions to manage its effective borrowing with respect to these notes.

AGF's other funding sources include private placement debt, retail note issuances and bank financings. In addition, AGF has become an established issuer of long-term debt in the international capital markets.

In addition to debt refinancing activities, proceeds from the collection of finance receivables will be used to pay the principal and interest with respect to AGF's debt. AIG does not guarantee any of the debt obligations of AGF. See also the discussion under "Operating Review — Financial Services Operations" and "Liquidity" herein.

AIG Credit Card Company (Taiwan) and AIG Finance (Taiwan) Limited, both consumer finance subsidiaries in Taiwan, have issued commercial paper for the funding of their own operations. AIG does not guarantee the commercial paper issued by these subsidiaries. See also the discussion under "Derivatives" herein and Note 9 of Notes to Consolidated Financial Statements.

Contractual Obligations and Other Commercial Commitments

The maturity schedule of AIG's contractual obligations at December 31, 2005 was as follows:

		Payments due by Period			
(in millions)	Total Payments	Less Than One Year	One Through Three Years	Four Through Five Years	After Five Years
Borrowings[a]	$ 99,291	$31,504	$20,717	$16,886	$30,184
Loss reserves[b]	77,169	21,221	23,537	11,191	21,220
Insurance and investment contract liabilities[c]	47,956	8,639	16,019	9,855	13,443
Operating leases	2,734	573	761	468	932
Aircraft purchase commitments	23,320	6,037	10,524	3,775	2,984
Total	$250,470	$67,974	$71,558	$42,175	$68,763

(a) Excludes commercial paper and obligations included as debt pursuant to FIN46R. See also Note 9 of Notes to Consolidated Financial Statements.

(b) Represents future loss and loss adjustment expense payments estimated based on historical loss development payment patterns.

(c) Insurance and investment contract liabilities include various investment-type products with contractually scheduled maturities including periodic payments of a term certain nature and guaranteed maturities under guaranteed investment contracts. Items excluded from the table include (i) liabilities for future policy benefits of approximately $109 billion, and (ii) policyholder contract deposits of approximately $182 billion. Amounts excluded from the table are generally comprised of policies or contracts where (i) AIG is currently not making payments until the occurrence of an insurable event, such as death or disability, (ii) payments are conditional on survivorship, or (iii) the occurrence of a payment due to a surrender or other non-scheduled event out of AIG's control. The determination of these liability amounts and timing of payment are not reasonably fixed and determinable. Significant uncertainties relating to these liabilities include mortality, morbidity, expenses, persistency, investment returns, inflation, and future policyholder elections as to benefits.

The maturity schedule of AIG's other commercial commitments by segment at December 31, 2005 was as follows:

		Amount of Commitment Expiration			
(in millions)	Total Amounts Committed	Less Than One Year	One Through Three Years	Four Through Five Years	After Five Years
Letters of credit:					
Life Insurance & Retirement Services	$ 185	$ 53	$ 9	$ 22	$ 101
DBG	188	188	—	—	—
Standby letters of credit:					
Capital Markets	1,758	8	52	70	1,628
Guarantees:					
Life Insurance & Retirement Services[a]	3,456	109	400	—	2,947
Aircraft Finance	147	51	14	—	82
Asset Management	82	27	9	46	—
Parent Company[b]	393	392	1	—	—
Other commercial commitments[c]:					
Capital Markets[d]	10,932	2,241	1,734	789	6,168
Aircraft Finance[e]	1,883	—	131	868	884
Life Insurance & Retirement Services[f]	3,505	626	1,286	748	845
Asset Management	607	437	155	15	—
DBG[g]	1,334	—	—	—	1,334
Total	$ 24,470	$4,132	$3,791	$2,558	$13,989

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

(b) Represents reimbursement obligations under letters of credit issued by commercial banks.

(c) Excludes commitments with respect to pension plans. The annual pension contribution for 2006 is expected to be approximately $70 million for U.S. and non-U.S. plans. See also Note 15 of Notes to Consolidated Financial Statements.

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

(e) Primarily in connection with options to acquire aircraft.

(f) Primarily AIG SunAmerica commitments to invest in partnerships.

(g) Primarily commitments to invest in limited partnerships.

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

AIG believes that any of its or its subsidiaries' contractual obligations that are subject to "ratings triggers" or financial covenants relating to "ratings triggers" would not have a material adverse effect on its financial condition or liquidity.

As a result of the downgrades of AIG's long-term senior debt ratings, AIG was required to post approximately $1.16 billion of collateral with counterparties to municipal guaranteed investment contracts and financial derivatives transactions. In the event of a further downgrade, AIG will be required to post additional collateral. It is estimated that, as of the close of business on February 28, 2006, based on AIG's outstanding municipal guaranteed investment agreements and financial derivatives transactions as of such date, a further downgrade of AIG's long-term senior debt ratings to 'Aa3' by Moody's or 'AA–' by S&P would permit counterparties to call for approximately $962 million of additional collateral. Further, additional downgrades could result in requirements for substantial additional collateral, which could have a material effect on how AIG manages its liquidity. The actual amount of additional collateral that AIG would be required to post to counterparties in the event of such downgrades depends on market conditions, the market value of the outstanding affected transactions and other factors prevailing at the time of the downgrade. Additional obligations to post collateral will increase the demand on AIG's liquidity.

Shareholders' Equity

AIG's consolidated shareholders' equity increased $6.64 billion during 2005. During 2005, retained earnings increased $8.86 billion, resulting from net income less dividends. Unrealized appreciation of investments, net of taxes, decreased $1.98 billion and the cumulative translation adjustment loss, net of taxes, increased $540 million. During 2005, there was a gain of $28 million, net of taxes, relating to derivative contracts designated as cash flow hedging instruments. See also the discussion under "Operating Review" and "Liquidity" herein, Notes 1(ee), 8(d) and 20 of Notes to Consolidated Financial Statements and the Consolidated Statement of Comprehensive Income.

AIG has in the past reinvested most of its unrestricted earnings in its operations and believes such continued reinvestment in the future will be adequate to meet any foreseeable capital needs. However, AIG may choose from time to time to raise additional funds through the issuance of additional securities.

Stock Purchase

During 2005, AIG purchased in the open market 2,477,100 shares of its common stock. AIG from time to time may buy shares of its common stock in the open market for general corporate purposes, including to satisfy its obligations under various employee benefit plans. At December 31, 2005, an additional 36,542,700 shares could be purchased under the then current authorization by AIG's Board of Directors.

Dividends from Insurance Subsidiaries

Payments of dividends to AIG by its insurance subsidiaries are subject to certain restrictions imposed by regulatory authorities. With respect to AIG's domestic insurance subsidiaries, the payment of any dividend requires formal notice to the insurance department in which the particular insurance subsidiary is domiciled. Under the laws of many states, an insurer may pay a dividend without prior approval of the insurance regulator when the amount of the dividend is below certain regulatory thresholds. Largely as a result of the restrictions, approximately 89 percent of consolidated shareholders' equity was restricted from immediate transfer to AIG parent at December 31, 2005. To enhance their current capital positions, dividends from the DBG companies were suspended in the fourth quarter of 2005, and AIG has taken various other actions. See "Regulation and Supervision" below. Furthermore, AIG cannot predict how recent regulatory investigations may affect the ability of its regulated subsidiaries to pay dividends. See "Risk Factors — Regulatory Investigations" in Item 1A. Risk Factors.

With respect to AIG's foreign insurance subsidiaries, the most significant insurance regulatory jurisdictions include Bermuda, Japan, Hong Kong, Taiwan, the United Kingdom, Thailand and Singapore.

AIG cannot predict whether the regulatory investigations currently underway or future regulatory issues will impair AIG's financial condition, results of operations or liquidity. To AIG's knowledge, no AIG company is currently on any regulatory or similar "watch list" with regard to solvency. See also the discussion under "Liquidity" herein and Note 11 of Notes to Consolidated Financial Statements, as well as "Risk Factors" in Item 1A. Risk Factors.

Regulation and Supervision

AIG's insurance subsidiaries, in common with other insurers, are subject to regulation and supervision by the states and jurisdictions in which they do business. In the U.S. the National Association of Insurance Commissioners (NAIC) has developed Risk-Based Capital (RBC) requirements. RBC relates an individual insurance company's statutory surplus to the risk inherent in its overall operations.

In connection with its Restatements, AIG examined and evaluated each of the items that have been restated or adjusted in its consolidated GAAP financial statements to determine whether restatement of the previously filed statutory financial statements of its insurance company subsidiaries would be required. In October and early November 2005, AIG completed its audited statutory financial statements for 2004 for all of the Domestic General Insurance companies. The statutory accounting treatment of the various items requiring adjustment or restatement was reviewed and agreed to with the relevant state insurance regulators in advance of the filings. Adjustments necessary to reflect the cumulative effect on statutory surplus of adjustments relating to years prior to 2004 were made to 2004 opening surplus, and 2004 statutory net income was restated accordingly. Previously reported General Insurance

statutory surplus at December 31, 2004 was reduced by approximately $3.5 billion to approximately $20.6 billion.

AIG also recently completed its 2005 unaudited statutory financial statements for all of its Domestic General Insurance subsidiaries, again after reviewing and agreeing with the relevant state insurance regulators the statutory accounting treatment of various items. The state regulators have permitted the Domestic General Insurance companies to record a $724 million reduction to opening statutory surplus as of January 1, 2005 to reflect the effects of the Second Restatement.

Statutory capital of each company continued to exceed minimum company action level requirements following the adjustments, but AIG nonetheless contributed an additional $750 million of capital into American Home effective September 30, 2005 and contributed a further $2.25 billion of capital in February 2006 for a total of approximately $3 billion of capital into Domestic General Insurance subsidiaries effective December 31, 2005. To enhance their current capital positions, dividends from the DBG companies were suspended in the fourth quarter of 2005. AIG believes it has the capital resources and liquidity to fund any necessary statutory capital contributions. AIG will review the capital position of its insurance company subsidiaries with various rating agencies and regulators to determine if additional capital contributions or other actions are warranted.

As discussed above, various regulators have commenced investigations into certain insurance business practices. In addition, the OTS and other regulators routinely conduct examinations of AIG and its subsidiaries, including AIG's consumer finance operations. AIG cannot predict the ultimate effect that these investigations and examinations, or any additional regulation arising therefrom, might have on its business. Federal, state or local legislation may affect AIG's ability to operate and expand its various financial services businesses, and changes in the current laws, regulations or interpretations thereof may have a material adverse effect on these businesses. See "Risk Factors — Regulatory Investigations" in Item 1A. Risk Factors for a further discussion of the effect these investigations may have on AIG's businesses.

AIG's U.S. operations are negatively affected under guarantee fund assessment laws which exist in most states. As a result of operating in a state which has guarantee fund assessment laws, a solvent insurance company may be assessed for certain obligations arising from the insolvencies of other insurance companies which operated in that state. AIG generally records these assessments upon notice. Additionally, certain states permit at least a portion of the assessed amount to be used as a credit against a company's future premium tax liabilities. Therefore, the ultimate net assessment cannot reasonably be estimated. The guarantee fund assessments net of credits for 2005, 2004, and 2003 were $124 million, $118 million and $77 million, respectively.

AIG is also required to participate in various involuntary pools (principally workers compensation business) which provide insurance coverage for those not able to obtain such coverage in the voluntary markets. This participation is also recorded upon notification, as these amounts cannot reasonably be estimated.

A substantial portion of AIG's General Insurance business and a majority of its Life Insurance & Retirement Services business are conducted in foreign countries. The degree of regulation and supervision in foreign jurisdictions varies. Generally, AIG, as well as the underwriting companies operating in such jurisdictions, must satisfy local regulatory requirements. Licenses issued by foreign authorities to AIG subsidiaries are subject to modification and revocation. Thus, AIG's insurance subsidiaries could be prevented from conducting future business in certain of the jurisdictions where they currently operate. AIG's international operations include operations in various developing nations. Both current and future foreign operations could be adversely affected by unfavorable political developments up to and including nationalization of AIG's operations without compensation. Adverse effects resulting from any one country may affect AIG's results of operations, liquidity and financial condition depending on the magnitude of the event and AIG's net financial exposure at that time in that country.

Foreign insurance operations are individually subject to local solvency margin requirements that require maintenance of adequate capitalization, which AIG complies with by country. In addition, certain foreign locations, notably Japan, have established regulations that can result in guarantee fund assessments. These have not had a material effect on AIG's results of operations.

Liquidity

AIG's liquidity is primarily derived from the operating cash flows of its General and Life Insurance & Retirement Services operations. Management believes that AIG's liquid assets, its net cash provided by operations, and access to short term funding through commercial paper and bank credit facilities will enable it to meet any anticipated cash requirements. See "Risk Factors — Access to Capital Markets" in Item 1A. Risk Factors.

At December 31, 2005, AIG's consolidated invested assets included $17.24 billion of cash and short-term investments. Consolidated net cash provided from operating activities in 2005 amounted to $25.14 billion.

The liquidity of the combined insurance operations is derived both domestically and abroad. The combined insurance operating cash flow is derived from two sources, underwriting operations and investment operations. Cash flow includes periodic premium collections, including policyholders' contract deposits, cash flows from investment operations and paid loss recoveries less reinsurance premiums, losses, benefits, and acquisition and operating expenses. Generally, there is a time lag from when premiums are collected and, when as a result of the occurrence of events specified in the policy, the losses and benefits are paid. Investment income cash flow is primarily derived from interest and dividends received and includes realized capital gains net of realized capital losses. See also the discussions under "Operating Review — General Insurance

Operations" and "Life Insurance & Retirement Services Operations" herein.

With respect to General Insurance operations, if paid losses accelerated beyond AIG's ability to fund such paid losses from current operating cash flows, AIG might need to liquidate a portion of its General Insurance investment portfolio and/or arrange for financing. Potential events causing such a liquidity strain could be the result of several significant catastrophic events occurring in a relatively short period of time. Additional strain on liquidity could occur if the investments sold to fund such paid losses were sold into a depressed market place and/or reinsurance recoverable on such paid losses became uncollectible or collateral supporting such reinsurance recoverable significantly decreased in value. See also the discussions under "Operating Review — General Insurance Operations" herein.

With respect to Life Insurance & Retirement Services operations, if a substantial portion of the Life Insurance & Retirement Services operations bond portfolio diminished significantly in value and/or defaulted, AIG might need to liquidate other portions of its Life Insurance & Retirement Services investment portfolio and/or arrange financing. Potential events causing such a liquidity strain could be the result of economic collapse of a nation or region in which AIG Life Insurance & Retirement Services operations exist, nationalization, terrorist acts, or other such economic or political upheaval. In addition, a significant rise in interest rates leading to a significant increase in policyholder surrenders could also create a liquidity strain. See also the discussions under "Operating Review — Life Insurance & Retirement Services Operations" herein.

In addition to the combined insurance pretax operating cash flow, AIG's insurance operations held $9.63 billion in cash and short-term investments at December 31, 2005. Operating cash flow and the cash and short-term balances held provided AIG's insurance operations with a significant amount of liquidity. AIG subsidiaries have also issued debt securities to fund insurance needs. In December 2005, Transatlantic issued $750 million of debt securities in a public offering, of which $450 million were purchased by other AIG subsidiaries. Transatlantic contributed the proceeds of the offering to a reinsurance company subsidiary.

This liquidity is available, among other things, to purchase predominately high quality and diversified fixed income securities and, to a lesser extent, marketable equity securities, and to provide mortgage loans on real estate, policy loans, and collateral loans. This cash flow coupled with proceeds of approximately $139 billion from the maturities, sales and redemptions of fixed income securities and from the sale of equity securities was used to purchase approximately $165 billion of fixed income securities and marketable equity securities during 2005.

AIG's major Financial Services operating subsidiaries consist of AIGFP, ILFC, AGF and AIGCFG. Sources of funds considered in meeting the liquidity needs of AIGFP's operations include guaranteed investment agreements, issuance of long-term and short-term debt, proceeds from maturities and sales of securities available for sale, securities sold under repurchase agreements, and securities and spot commodities sold but not yet purchased. ILFC, AGF and AIGCFG all utilize the commercial paper markets, retail and wholesale deposits, bank loans and bank credit facilities as sources of liquidity. ILFC and AGF also fund in the domestic and international capital markets without reliance on any guarantee from AIG. An additional source of liquidity for ILFC is the use of export credit facilities. AIGCFG also uses wholesale and retail bank deposits as sources of funds. On occasion, AIG has provided equity capital to ILFC, AGF and AIGCFG and provides intercompany loans to AIGCFG. An AIG subsidiary purchased additional shares of ILFC in the amount of $400 million during the third quarter of 2005. Cash flow provided from operations is a major source of liquidity for AIG's primary Financial Services operating subsidiaries.

AIG, the parent company, funds its short-term working capital needs through commercial paper issued by AIG Funding. As of December 31, 2005, AIG Funding had $2.69 billion of commercial paper outstanding with an average maturity of 32 days. At February 28, 2006, AIG Funding had $5.3 billion of commercial paper outstanding with an average maturity of 24 days. As additional liquidity, AIG parent has a $2 billion inter-company revolving credit facility provided by certain of its subsidiaries, a $1.375 billion 364-day revolving bank credit facility that expires in July 2006, a $1.375 billion five year revolving bank credit facility that expires in July 2010 and a $3 billion 364-day revolving credit facility that expires in November 2006, of which $1.14 billion is currently available as back-up liquidity. AIG parent's primary sources of cash flow are dividends and loans from its subsidiaries. Largely as a result of regulatory restrictions, approximately 89 percent of consolidated shareholders' equity was restricted from immediate transfer to AIG parent at December 31, 2005. AIG cannot predict how recent regulatory investigations may affect the ability of its regulated subsidiaries to pay dividends. See "Risk Factors — Regulatory Investigations" in Item 1A. Risk Factors. AIG parent's primary uses of cash flow are for debt service, capital contributions to subsidiaries and the payment of dividends to shareholders. See also Note 9 of Notes to Consolidated Financial Statements for additional information on debt maturities for AIG and its subsidiaries.

The capital contributions referred to under Item 1. Business — Regulation and the settlements described under Item 3. Legal Proceedings were funded using existing capacity from internal and external sources, including the issuance of commercial paper.

Special Purpose Vehicles and Off Balance Sheet Arrangements

AIG uses special purpose vehicles (SPVs) and off balance sheet arrangements in the ordinary course of business. As a result of recent changes in accounting, a number of SPVs and off balance sheet arrangements have been reflected in AIG's consolidated financial statements. In January 2003, FASB issued Interpretation No. 46, "Consolidation of Variable Interest Entities" (FIN 46). FIN 46 addressed the consolidation and disclosure rules for nonoperating entities that are now

defined as Variable Interest Entities (VIEs). In December 2003, FASB issued a revision to Interpretation No. 46 (FIN 46R).

AIG has guidelines with respect to the formation of and investment in SPVs and off balance sheet arrangements. In addition, AIG has expanded the responsibility of its Complex Structured Financial Transaction Committee (CSFT) to include the review of any transaction that could subject AIG to heightened legal, reputational, regulatory, accounting or other risk. See "Management's Report on Internal Control Over Financial Reporting" in Item 9A of Part II for a further discussion of the CSFT.

For additional information related to AIG's activities with respect to VIEs and certain guarantees see "Recent Accounting Standards" herein and also Notes 1 and 19 of Notes to Consolidated Financial Statements. Also, for additional disclosure regarding AIG's commercial commitments (including guarantors), see "Contractual Obligations and Other Commercial Commitments" herein.

Derivatives

Derivatives are financial instruments among two or more parties with returns linked to or "derived" from some underlying equity, debt, commodity or other asset, liability, or index. Derivatives payments may be based on interest rates and exchange rates and/or prices of certain securities, commodities, financial or commodity indices, or other variables. The more significant types of derivative arrangements in which AIG transacts are swaps, forwards, futures and options. In the normal course of business, with the agreement of the original counterparty, these contracts may be terminated early or assigned to another counterparty.

The overwhelming majority of AIG's derivatives activities are conducted by the Capital Markets operations, thus permitting AIG to participate in the derivatives dealer market acting primarily as principal. In these derivative operations, AIG structures transactions that generally allow its counterparties to obtain, or hedge, exposure to changes in interest and foreign currency exchange rates, credit events, securities' prices and certain commodities and financial or commodity indices. AIG's customers — such as corporations, financial institutions, multinational organizations, sovereign entities, government agencies and municipalities — use derivatives to hedge their own market exposures. For example, a futures, forward or option contract can be used to protect the customers' assets or liabilities against price fluctuations.

A counterparty may default on any obligation to AIG, including a derivative contract. Credit risk is a consequence of extending credit and/or carrying trading and investment positions. Credit risk exists for a derivative contract when that contract has a positive fair value to AIG. To help manage this risk, AIGFP's credit department operates within the guidelines set by the AIG Credit Risk Committee. This committee establishes the credit policy, sets limits for counterparties and provides limits for derivative transactions with counterparties having different credit ratings. In addition to credit ratings, this committee takes into account other factors, including the industry and country of the counterparty. Transactions which fall outside these pre-established guidelines require the specific approval of the AIG Credit Risk Committee. It is also AIG's policy to establish reserves for potential credit impairment when necessary.

In addition, AIGFP utilizes various credit enhancements, including letters of credit, guarantees, collateral, credit triggers, credit derivatives, and margin agreements to reduce the credit risk relating to its outstanding financial derivative transactions. AIGFP requires credit enhancements in connection with specific transactions based on, among other things, the creditworthiness of the counterparties, and the transaction's size and maturity.

AIG's Derivatives Review Committee provides an independent review of any proposed derivative transaction or program except those derivative transactions entered into by AIGFP with third parties. The committee examines, among other things, the nature and purpose of the derivative transaction, its potential credit exposure, if any, and the estimated benefits.

FAS 133 requires that third-party derivatives used for hedging must be specifically matched with the underlying exposures to an outside third party and documented contemporaneously to qualify for hedge accounting treatment. In most cases, AIG did not meet these hedging requirements with respect to certain hedging transactions. Not meeting the requirements of FAS 133 does not result in any changes in AIG's liquidity or its overall financial condition even though inter-period volatility of earnings is increased.

See also Note 20 of Notes to Consolidated Financial Statements for detailed information relating to AIG's derivative activities, and Note 1(ee) of Notes to Consolidated Financial Statements for AIG's derivative accounting policies.

Managing Market Risk

Market risk is the risk of loss of fair value resulting from adverse fluctuations in interest rates, foreign currencies, equities and commodity prices. AIG has exposures to these risks.

AIG analyzes market risk using various statistical techniques including Value at Risk (VaR). VaR is a summary statistical measure that applies the estimated volatility and correlation of market factors to AIG's market positions. The output from the VaR calculation is the maximum loss that could occur over a defined period of time given a certain probability. While VaR models are relatively sophisticated, the quantitative market risk information generated is limited by the assumptions and parameters established in creating the related models. AIG believes that statistical models alone do not provide a reliable method of monitoring and controlling market risk. Therefore, such models are tools and do not substitute for the experience or judgment of senior management.

Insurance

AIG has performed a separate VaR analysis for the General Insurance and Life Insurance & Retirement Services segments and for each market risk within each segment. For purposes of the VaR calculation, the insurance assets and liabilities from GICs are included in the Life Insurance & Retirement Services

segment. For the calculations in the analyses the financial instrument assets included are the insurance segments' invested assets, excluding real estate and investment income due and accrued, and the financial instrument liabilities included are reserve for losses and loss expenses, reserve for unearned premiums, future policy benefits for life and accident and health insurance contracts and other policyholders' funds.

AIG calculated the VaR with respect to the net fair value of each of AIG's insurance segments as of December 31, 2005 and December 31, 2004. The VaR number represents the maximum potential loss as of those dates that could be incurred with a 95 percent confidence (i.e., only five percent of historical scenarios show losses greater than the VaR figure) within a one-month holding period. AIG uses the historical simulation methodology that entails repricing all assets and liabilities under explicit changes in market rates within a specific historical time period. AIG uses the most recent three years of historical market information for interest rates, foreign exchange rates, and equity index prices. For each scenario, each transaction was repriced. Portfolio, business unit and finally AIG-wide scenario values are then calculated by netting the values of all the underlying assets and liabilities.

The following table presents the VaR on a combined basis and of each component of market risk for each of AIG's insurance segments as of December 31, 2005 and 2004. Due to diversification effects, the combined VaR is always smaller than the sum of its components.

	General Insurance		Life Insurance & Retirement Services	
(in millions)	**2005**	2004	**2005**	2004
Market risk:				
Combined	**$1,617**	$1,396	**$4,515**	$5,024
Interest rate	**1,717**	1,563	**4,382**	4,750
Currency	**130**	139	**541**	478
Equity	**535**	727	**762**	1,024

The following table presents the average, high and low VaRs on a combined basis and of each component of market risk for each of AIG's insurance segments for the years 2005 and 2004. Due to diversification effects, the combined VaR is always smaller than the sum of its components.

	2005			2004		
(in millions)	**Average**	**High**	**Low**	Average	High	Low
General Insurance:						
Market risk:						
Combined	**$1,585**	**$1,672**	**$1,396**	$1,299	$1,497	$1,100
Interest rate	**1,746**	**1,931**	**1,563**	1,407	1,591	1,173
Currency	**125**	**139**	**111**	111	139	88
Equity	**651**	**727**	**535**	744	797	688
Life Insurance & Retirement Services:						
Market risk:						
Combined	**$4,737**	**$5,024**	**$4,515**	$4,021	$5,024	$3,075
Interest rate	**4,488**	**4,750**	**4,382**	3,831	4,750	2,967
Currency	**511**	**560**	**442**	326	478	257
Equity	**953**	**1,024**	**762**	884	1,024	758

The Combined VaR and Interest Rate VaR for Life Insurance & Retirement Services trended higher during 2004 because of growth in the Asian life businesses. The December 2004 VaR results are equal to the maximum values observed during the year.

During 2005, the Combined VaR and Interest Rate VaR for Life Insurance & Retirement Services remained in a narrower range. The December 2005 VaR results are somewhat lower than the December 2004 figures because long-term interest rates in Asia declined during the year.

In addition, the increase in Combined and Interest Rate VaRs from 2004 to 2005 in the General Insurance division was caused by growth in this business.

Financial Services

AIG generally manages its market exposures within Financial Services by maintaining offsetting positions. Capital Markets seeks to minimize or set limits for open or uncovered market positions. Credit exposure is managed separately. See the discussion on the management of credit risk above.

AIG's Market Risk Management Department provides detailed independent review of AIG's market exposures, particularly those market exposures of the Capital Markets operations. This department determines whether AIG's market risks, as well as those market risks of individual subsidiaries, are within the parameters established by AIG's senior management. Well established market risk management techniques such as sensitivity analysis are used. Additionally, this department verifies that specific market risks of each of certain subsidiaries are managed and hedged by that subsidiary.

ILFC is exposed to market risk and the risk of loss of fair value and possible liquidity strain resulting from adverse fluctuations in interest rates. As of December 31, 2005 and December 31, 2004, AIG statistically measured the loss of fair value through the application of a VaR model. In this analysis, the net fair value of Aircraft Finance operations was determined using the financial instrument assets which included the

tax adjusted future flight equipment lease revenue, and the financial instrument liabilities which included the future servicing of the current debt. The estimated effect of the current derivative positions was also taken into account.

AIG calculated the VaR with respect to the net fair value of Aircraft Finance operations using the historical simulation methodology, as previously described. For the years 2005 and 2004, the average VaR with respect to the net fair value of Aircraft Finance operations was approximately $135 million and $70 million, respectively.

Capital Markets operations are exposed to market risk due to changes in the level and volatility of interest rates, foreign currency exchange rates, equity prices and commodity prices. AIGFP hedges its exposure to these risks primarily through swaps, options, forwards, and futures. To economically hedge interest rate risks, AIGFP may also purchase U.S. and foreign government obligations.

AIGFP does not seek to manage the market risk of each transaction through an individual third-party offsetting transaction. Rather, AIGFP takes a portfolio approach to the management of its market risk exposures. AIGFP values the predominant portion of its market-sensitive transactions by marking them to market currently through income. A smaller portion is priced by estimated fair value based upon an extrapolation of market factors. There is another limited portion of transactions where the initial fair value is not recorded through income currently and gains or losses are recognized over the life of the transactions. These valuations represent an assessment of the present values of expected future cash flows and may include reserves for such risks as are deemed appropriate by AIGFP and AIG management.

The recorded values of these transactions may be different from the values that might be realized if AIGFP were required to sell or close out the transactions prior to maturity. AIG believes that such differences are not significant to financial condition or liquidity. Such differences would be immediately recognized when the transactions are sold or closed out prior to maturity.

AIGFP attempts to secure reliable and independent current market prices, such as published exchange prices, external subscription services such as from Bloomberg or Reuters or third-party broker quotes for use in this model. When such prices are not available, AIGFP uses an internal methodology which includes extrapolation from observable and verifiable prices nearest to the dates of the transactions. Historically, actual results have not materially deviated from these models in any material respect.

Systems used by Capital Markets operations can monitor each unit's respective market positions on an intraday basis. AIGFP operates in major business centers overseas and therefore is open for business essentially 24 hours a day. Thus, the market exposure and offset strategies are monitored, reviewed and coordinated around the clock.

AIGFP applies various testing techniques which reflect significant potential market movements in interest rates, foreign exchange rates, commodity and equity prices, volatility levels, and the effect of time. These techniques vary by currency and are regularly changed to reflect factors affecting the derivatives portfolio. The results from these analyses are regularly reviewed by AIG management.

As described above, Capital Markets operations are exposed to the risk of loss of fair value from adverse fluctuations in interest rate and foreign currency exchange rates and equity and commodity prices as well as implied volatilities thereon. AIG statistically measures the losses of fair value through the application of a VaR model across Capital Markets.

Capital Markets asset and liability portfolios for which the VaR analyses were performed included over the counter and exchange traded investments, derivative instruments and commodities. Because the market risk with respect to securities available for sale, at market, is substantially hedged, segregation of market sensitive instruments into trading and other than trading was not deemed necessary. The VaR calculation is unaffected by the accounting treatment of hedged transactions under FAS 133.

In the calculation of VaR for Capital Markets operations, AIG uses the same historical simulation methodology, described under Insurance above, which entails repricing all assets and liabilities under explicit changes in market rates within a specific historical time period. In 2004, AIGFP enhanced its library of factors by including implied option volatilities to construct the historical scenarios for simulation.

The following table presents the VaR on a combined basis and of each component of market risk for Capital Markets operations as of December 31, 2005 and 2004. Due to diversification effects, the combined VaR is always smaller than the sum of its components.

(in millions)	**2005**	2004
Combined	**$22**	$17
Interest rate	**9**	11
Currency	**3**	4
Equity	**14**	16
Commodity	**9**	7

The following table presents the average, high, and low VaRs on a combined basis and of each component of market risk for Capital Markets operations for the years 2005 and 2004. Due to diversification effects, the combined VaR is always smaller than the sum of its components.

	2005			2004		
(in millions)	**Average**	**High**	**Low**	Average	High	Low
Combined	**$17**	**$22**	**$13**	$19	$24	$13
Interest rate	**9**	**11**	**6**	9	12	5
Currency	**4**	**6**	**3**	4	4	3
Equity	**9**	**16**	**5**	13	16	5
Commodity	**8**	**10**	**7**	6	7	4

Recent Accounting Standards

In December 2003, FASB issued a revision to Interpretation No. 46 (FIN46R). In March 2005, FASB issued FSP FIN46R-5, "Implicit Variable Interests under FASB Interpretation No. 46 (revised December 2003), Consolidation

of Variable Interest Entities." See also Note 19 of Notes to Consolidated Financial Statements.

In July 2003, the American Institute of Certified Public Accountants issued SOP 03-1. See also Note 21 of Notes to Consolidated Financial Statements.

In December 2003, FASB issued Statement of Financial Accounting Standards No. 132 (Revised), "Employers' Disclosures About Pensions and Other Post Retirement Benefits," which revised disclosure requirements with respect to defined benefit plans. See also Note 15 herein.

At the March 2004 meeting, the Emerging Issue Task Force (EITF) reached a consensus with respect to Issue No. 03-1, "The Meaning of Other-Than-Temporary Impairment and Its Application to Certain Investments." On September 30, 2004, the FASB issued FASB Staff Position (FSP) EITF Issue 03-1-1, Effective Date of Paragraphs 10-20 of EITF Issue No. 03-1, "The Meaning of Other-Than-Temporary Impairment and Its Application to Certain Investments." In November 2005, FASB issued FSP FAS 115-1, "The Meaning of Other-Than-Temporary Impairment and Its Application to Certain Investments," which replaces the measurement and recognition guidance set forth in Issue No. 03-1 and codifies certain existing guidance on impairment.

At the September 2004 meeting, the EITF reached a consensus with respect to Issue No. 04-8, "Accounting Issues Related to Certain Features of Contingently Convertible Debt and the Effect on Diluted Earnings per Share."

In December 2004, the FASB issued Statement No. 123 (revised 2004) (FAS 123R), "Share Based Payment." In April 2005, the SEC delayed the effective date for the revised FAS No. 123.

On December 16, 2004, the FASB issued Statement No. 153, "Exchanges of Nonmonetary Assets — An Amendment of APB Opinion No. 29" (FAS 153). FAS 153 amends APB Opinion No. 29, "Accounting for Nonmonetary Transactions."

On June 1, 2005, the FASB issued Statement No. 154, "Accounting Changes and Error Corrections" (FAS 154). FAS 154 replaces APB Opinion No. 20, "Accounting Changes" and FASB Statement No. 3, "Reporting Accounting Changes in Interim Financial Statements."

At the June 2005 meeting, the EITF reached a consensus with respect to Issue No. 04-5, "Determining Whether a General Partner, or the General Partners as a Group, Controls a Limited Partnership or Similar Entity When the Limited Partners Have Certain Rights".

On June 29, 2005, FASB issued Statement 133 Implementation Issue No. B38, "Embedded Derivatives: Evaluation of Net Settlement with Respect to the Settlement of a Debt Instrument through Exercise of an Embedded Put Option or Call Option."

On June 29, 2005, FASB issued Statement 133 Implementation Issue No. B39, "Application of Paragraph 13(b) to Call Options That Are Exercisable Only by the Debtor."

On September 19, 2005, FASB issued Statement of Position 05-1, "Accounting by Insurance Enterprises for Deferred Acquisition Costs in Connection with Modifications or Exchanges of Insurance Contracts."

On February 16, 2006, FASB issued Statement No. 155, "Accounting for Certain Hybrid Financial Instruments."

For further discussion of these recent accounting standards and their application to AIG, see Note 1(gg) of Notes to Consolidated Financial Statements.

ITEM 7A.
Quantitative and Qualitative Disclosures About Market Risk

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

ITEM 8.
Financial Statements and Supplementary Data

AMERICAN INTERNATIONAL GROUP, INC. AND SUBSIDIARIES
INDEX TO FINANCIAL STATEMENTS AND SCHEDULES

Report of Independent Registered Public Accounting Firm

To the Board of Directors and Shareholders of
American International Group, Inc.:

We have completed integrated audits of American International Group, Inc.'s 2005 and 2004 consolidated financial statements and of its internal control over financial reporting as of December 31, 2005, and an audit of its 2003 consolidated financial statements in accordance with the standards of the Public Company Accounting Oversight Board (United States). Our opinions, based on our audits, are presented below.

Consolidated financial statements and financial statement schedules

In our opinion, the consolidated financial statements listed in the accompanying index present fairly, in all material respects, the financial position of American International Group, Inc. and its subsidiaries (AIG) at December 31, 2005 and 2004, and the results of their operations and their cash flows for each of the three years in the period ended December 31, 2005 in conformity with accounting principles generally accepted in the United States of America. In addition, in our opinion, the financial statement schedules listed in the accompanying index present fairly, in all material respects, the information set forth therein when read in conjunction with the related consolidated financial statements. These financial statements and financial statement schedules are the responsibility of AIG's management. Our responsibility is to express an opinion on these financial statements and financial statement schedules based on our audits. We conducted our audits of these statements in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit of financial statements includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

As described in Note 21 to the consolidated financial statements, AIG changed its accounting for certain non-traditional long duration contracts and for separate accounts as of January 1, 2004.

Internal control over financial reporting

Also, we have audited management's assessment, included in Management's Report on Internal Control Over Financial Reporting appearing under Item 9A, that AIG did not maintain effective internal control over financial reporting as of December 31, 2005 because of the effect of the material weaknesses relating to (1) controls over certain balance sheet reconciliations, (2) controls over the accounting for certain derivative transactions and (3) controls over income tax accounting, based on criteria established in *Internal Control — Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). AIG's management is responsible for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting. Our responsibility is to express opinions on management's assessment and on the effectiveness of AIG's internal control over financial reporting based on our audit.

We conducted our audit of internal control over financial reporting in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material respects. An audit of internal control over financial reporting includes obtaining an understanding of internal control over financial reporting, evaluating management's assessment, testing and evaluating the design and operating effectiveness of internal control, and performing such other procedures as we consider necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinions.

A company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (i) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (ii) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (iii) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

A material weakness is a control deficiency, or a combination of control deficiencies, that results in more than a remote likelihood that a material misstatement of the annual or interim financial statements will not be prevented or detected. As of December 31, 2005, the following material weaknesses have been identified and included in management's assessment.

Controls over certain balance sheet reconciliations: AIG did not maintain effective controls to ensure the accuracy of certain balance sheet accounts in certain key segments of AIG's operations, principally in the Domestic Brokerage Group. Specifically, accounting personnel did not perform timely reconciliations and did not properly resolve reconciling items for premium receivables, reinsurance recoverables and in-

tercompany accounts. As a result, premiums and other considerations, incurred policy losses and benefits, insurance acquisition and other operating expenses, premiums and insurance balances receivable, reinsurance assets, reserve for losses and loss expenses, reserve for unearned premiums, other assets and retained earnings were misstated under GAAP.

Controls over the accounting for certain derivative transactions: AIG did not maintain effective controls over the evaluation and documentation of whether certain derivative transactions qualified under GAAP for hedge accounting. As a result, net investment income, realized capital gains (losses), other revenues, accumulated other comprehensive income (loss) and related balance sheet accounts were misstated under GAAP.

Controls over income tax accounting: AIG did not maintain effective controls over the determination and reporting of certain components of the provision for income taxes and related deferred income tax balances. Specifically, AIG did not maintain effective controls to review and monitor the accuracy of the components of the income tax provision calculations and related income tax balances and to monitor the differences between the income tax basis and the financial reporting basis of assets and liabilities to effectively reconcile the differences to the deferred income tax balances. As a result, income tax expense, income taxes payable, deferred income tax assets and liabilities, retained earnings and accumulated other comprehensive income were misstated under GAAP.

The control deficiencies described above resulted in the restatement in 2005 of AIG's 2004, 2003 and 2002 annual consolidated financial statements and financial statement schedules and the interim consolidated financial statements for each quarter in 2004 and 2003 and for each of the first three quarters in 2005. In addition, these control deficiencies could result in other misstatements to the aforementioned financial statement accounts and disclosures that would result in a material misstatement to the annual or interim AIG consolidated financial statements that would not be prevented or detected. Accordingly, AIG management has concluded that these control deficiencies constitute material weaknesses. These material weaknesses were considered in determining the nature, timing, and extent of audit tests applied in our audit of the 2005 consolidated financial statements, and our opinion regarding the effectiveness of AIG's internal control over financial reporting does not affect our opinion on those consolidated financial statements.

In our opinion, management's assessment that AIG did not maintain effective internal control over financial reporting as of December 31, 2005, is fairly stated, in all material respects, based on criteria established in *Internal Control — Integrated Framework* issued by the COSO. Also, in our opinion, because of the effects of the material weaknesses described above on the achievement of the objectives of the control criteria, AIG has not maintained effective internal control over financial reporting as of December 31, 2005, based on criteria established in *Internal Control — Integrated Framework* issued by the COSO.

PricewaterhouseCoopers LLP
New York, New York
March 16, 2006

Consolidated Balance Sheet

December 31, *(in millions)*	**2005**	2004
Assets:		
Investments and financial services assets:		
Fixed maturities:		
Bonds available for sale, at market value (amortized cost: 2005 – $349,612; 2004 – $329,838)	**$359,516**	$344,399
Bonds held to maturity, at amortized cost (market value: 2005 – $22,047; 2004 – $18,791)	**21,528**	18,294
Bond trading securities, at market value (cost: 2005 – $4,623; 2004 – $2,973)	**4,636**	2,984
Equity securities:		
Common stocks available for sale, at market value (cost: 2005 – $10,125; 2004 – $8,424)	**12,227**	9,772
Common stocks trading, at market value (cost: 2005 – $7,746; 2004 – $5,651)	**8,959**	5,894
Preferred stocks available for sale, at market value (cost: 2005 – $2,282; 2004 – $2,017)	**2,402**	2,040
Mortgage loans on real estate, net of allowance (2005 – $54; 2004 – $65)	**14,300**	13,146
Policy loans	**7,039**	7,035
Collateral and guaranteed loans, net of allowance (2005 – $10; 2004 – $18)	**3,570**	3,303
Financial services assets:		
Flight equipment primarily under operating leases, net of accumulated depreciation (2005 – $7,419; 2004 – $6,390)	**36,245**	32,130
Securities available for sale, at market value (cost: 2005 – $37,572; 2004 – $29,171)	**37,511**	31,225
Trading securities, at market value	**6,499**	2,746
Spot commodities	**92**	534
Unrealized gain on swaps, options and forward transactions	**18,695**	22,670
Trading assets	**1,204**	3,433
Securities purchased under agreements to resell, at contract value	**14,547**	26,272
Finance receivables, net of allowance (2005 – $670; 2004 – $571)	**27,995**	23,574
Securities lending collateral, at market value (which approximates cost)	**59,471**	49,169
Other invested assets	**27,267**	23,559
Short-term investments, at cost (approximates market value)	**15,342**	16,102
Total investments and financial services assets	**679,045**	638,281
Cash	**1,897**	2,009
Investment income due and accrued	**5,727**	5,556
Premiums and insurance balances receivable, net of allowance (2005 – $1,011; 2004 – $690)	**15,333**	15,622
Reinsurance assets, net of allowance (2005 – $992; 2004 – $832)	**24,978**	19,613
Deferred policy acquisition costs	**33,248**	29,817
Investments in partially owned companies	**1,158**	1,495
Real estate and other fixed assets, net of accumulated depreciation (2005 – $4,990; 2004 – $4,650)	**7,446**	6,192
Separate and variable accounts	**63,797**	57,741
Goodwill	**8,093**	8,556
Income taxes receivable – current	**319**	138
Other assets	**12,329**	16,125
Total assets	**$853,370**	$801,145

See Accompanying Notes to Consolidated Financial Statements.

Consolidated Balance Sheet *Continued*

December 31, *(in millions, except share data)*	**2005**	2004
Liabilities:		
Reserve for losses and loss expenses	**$ 77,169**	$ 61,878
Reserve for unearned premiums	**24,243**	23,400
Future policy benefits for life and accident and health insurance contracts	**108,807**	104,740
Policyholders' contract deposits	**227,027**	216,474
Other policyholders' funds	**10,870**	10,280
Reserve for commissions, expenses and taxes	**4,769**	4,629
Insurance balances payable	**3,564**	3,661
Funds held by companies under reinsurance treaties	**4,174**	3,404
Income taxes payable – deferred	**6,607**	6,588
Financial services liabilities:		
Borrowings under obligations of guaranteed investment agreements	**20,811**	18,919
Securities sold under agreements to repurchase, at contract value	**11,047**	23,581
Trading liabilities	**2,546**	2,503
Securities and spot commodities sold but not yet purchased, at market value	**5,975**	5,404
Unrealized loss on swaps, options and forward transactions	**12,740**	15,985
Trust deposits and deposits due to banks and other depositors	**4,877**	4,248
Commercial paper	**6,514**	6,724
Notes, bonds, loans and mortgages payable	**71,313**	61,296
Commercial paper	**2,694**	2,969
Notes, bonds, loans and mortgages payable	**7,126**	5,502
Liabilities connected to trust preferred stock	**1,391**	1,489
Separate and variable accounts	**63,797**	57,741
Minority interest	**5,124**	4,831
Securities lending payable	**60,409**	49,972
Other liabilities	**23,273**	25,055
Total liabilities	**766,867**	721,273
Preferred shareholders' equity in subsidiary companies	**186**	199
Commitments and Contingent Liabilities (See Note 12)		
Shareholders' equity:		
Common stock, $2.50 par value; 5,000,000,000 shares authorized; shares issued 2005 and 2004 – 2,751,327,476	**6,878**	6,878
Additional paid-in capital	**2,339**	2,094
Retained earnings	**72,330**	63,468
Accumulated other comprehensive income	**6,967**	9,444
Treasury stock, at cost; 2005 – 154,680,704; 2004 – 154,904,286 shares of common stock (including 119,271,176 and 119,263,196 shares, respectively, held by subsidiaries)	**(2,197)**	(2,211)
Total shareholders' equity	**86,317**	79,673
Total liabilities, preferred shareholders' equity in subsidiary companies and shareholders' equity	**$853,370**	$801,145

See Accompanying Notes to Consolidated Financial Statements.

Consolidated Statement of Income

Years Ended December 31, *(in millions, except per share data)*	**2005**	2004	2003
Revenues:			
Premiums and other considerations	**$70,209**	$66,625	$54,802
Net investment income	**22,165**	18,465	15,508
Realized capital gains (losses)	**341**	44	(442)
Other revenues	**16,190**	12,532	9,553
Total revenues	**108,905**	97,666	79,421
Benefits and expenses:			
Incurred policy losses and benefits	**63,711**	58,360	46,034
Insurance acquisition and other operating expenses	**29,981**	24,461	21,480
Total benefits and expenses	**93,692**	82,821	67,514
Income before income taxes, minority interest and cumulative effect of accounting changes	**15,213**	14,845	11,907
Income taxes:			
Current	**2,569**	2,593	2,741
Deferred	**1,689**	1,814	815
	4,258	4,407	3,556
Income before minority interest and cumulative effect of accounting changes	**10,955**	10,438	8,351
Minority interest	**(478)**	(455)	(252)
Income before cumulative effect of accounting changes	**10,477**	9,983	8,099
Cumulative effect of accounting changes, net of tax	**–**	(144)	9
Net income	**$10,477**	$ 9,839	$ 8,108
Earnings per common share:			
Basic			
Income before cumulative effect of accounting changes	**$ 4.03**	$ 3.83	$ 3.10
Cumulative effect of accounting changes, net of tax	**–**	(0.06)	–
Net income	**4.03**	3.77	3.10
Diluted			
Income before cumulative effect of accounting changes	**$ 3.99**	$ 3.79	$ 3.07
Cumulative effect of accounting changes, net of tax	**–**	(0.06)	–
Net income	**3.99**	3.73	3.07
Average shares outstanding:			
Basic	**2,597**	2,606	2,610
Diluted	**2,627**	2,637	2,637

See Accompanying Notes to Consolidated Financial Statements.

Consolidated Statement of Shareholders' Equity

Years Ended December 31, *(in millions, except per share data)*	**2005**	2004	2003
Common stock:			
Balance at beginning of year	**$ 6,878**	$ 6,878	$ 6,878
Issued under stock plans	**–**	–	–
Balance at end of year	**6,878**	6,878	6,878
Additional paid-in capital:			
Balance at beginning of year	**2,094**	2,028	1,783
Excess of cost over proceeds of common stock issued under stock plans	**(91)**	(105)	(76)
Other	**336**	171	321
Balance at end of year	**2,339**	2,094	2,028
Retained earnings:			
Balance at beginning of year	**63,468**	54,384	46,908
Net income	**10,477**	9,839	8,108
Dividends to common shareholders ($0.63, $0.29 and $0.24 per share, respectively)	**(1,615)**	(755)	(632)
Balance at end of year	**72,330**	63,468	54,384
Accumulated other comprehensive income (loss):			
Balance at beginning of year	**9,444**	7,337	4,077
Unrealized (depreciation) appreciation of investments – net of reclassification adjustments	**(3,577)**	1,868	4,159
Deferred income tax benefit (expense) on changes	**1,599**	(612)	(1,237)
Foreign currency translation adjustments	**(926)**	993	347
Applicable income tax benefit (expense) on above changes	**386**	(170)	4
Net derivative gains arising from cash flow hedging activities	**35**	83	75
Deferred income tax expense on above changes	**(7)**	(33)	(22)
Retirement plan liabilities adjustment, net of tax	**13**	(22)	(66)
Other comprehensive income	**(2,477)**	2,107	3,260
Balance at end of year	**6,967**	9,444	7,337
Treasury stock, at cost:			
Balance at beginning of year	**(2,211)**	(1,397)	(1,343)
Cost of shares acquired during year	**(176)**	(1,083)	(207)
Issued under stock plans	**173**	263	151
Other	**17**	6	2
Balance at end of year	**(2,197)**	(2,211)	(1,397)
Total shareholders' equity at end of year	**$86,317**	$79,673	$69,230

See Accompanying Notes to Consolidated Financial Statements.

Consolidated Statement of Cash Flows

Years Ended December 31, *(in millions)*	2005	2004	2003
Summary:			
Net cash provided by operating activities	**$ 25,138**	$ 30,716	$ 33,241
Net cash used in investing activities	**(57,321)**	(97,115)	(66,904)
Net cash provided by financing activities	**32,999**	66,494	33,070
Effect of exchange rate changes on cash	**(928)**	992	350
Change in cash	**(112)**	1,087	(243)
Cash at beginning of year	**2,009**	922	1,165
Cash at end of year	**$ 1,897**	$ 2,009	$ 922
Cash flows from operating activities:			
Net income	**$ 10,477**	$ 9,839	$ 8,108
Adjustments to reconcile net income to net cash provided by operating activities:			
Noncash revenues, expenses, gains and losses included in income:			
Change in:			
General and life insurance reserves	**20,912**	26,937	22,456
Premiums and insurance balances receivable and payable – net	**192**	(1,020)	(2,236)
Reinsurance assets	**(5,365)**	1,032	2,137
Deferred policy acquisition costs	**(2,263)**	(4,042)	(3,778)
Investment income due and accrued	**(171)**	(916)	(388)
Funds held under reinsurance treaties	**770**	361	832
Other policyholders' funds	**590**	1,156	687
Current and deferred income taxes – net	**1,507**	1,396	2,179
Reserve for commissions, expenses and taxes	**140**	(16)	1,005
Other assets and liabilities – net	**2,535**	1,113	579
Bonds and common stocks trading, at market value	**(4,717)**	(3,582)	544
Trading assets and liabilities – net	**2,272**	(4,783)	4,592
Trading securities, at market value	**(3,753)**	792	764
Spot commodities	**442**	(289)	240
Net unrealized (gain) loss on swaps, options and forward transactions	**728**	1,534	(4,500)
Securities purchased under agreements to resell	**11,725**	(5,427)	(3,010)
Securities sold under agreements to repurchase	**(12,534)**	5,688	7,542
Securities and spot commodities sold but not yet purchased, at market value	**571**	(269)	(6,306)
Realized capital (gains) losses	**(341)**	(44)	442
Equity in income of partially owned companies and other invested assets	**(1,421)**	(1,279)	(707)
Amortization of premium and discount on securities	**292**	324	60
Depreciation expenses, principally flight equipment	**2,200**	2,035	1,861
Provision for finance receivable losses	**435**	389	429
Other – net	**(85)**	(213)	(291)
Total adjustments	**14,661**	20,877	25,133
Net cash provided by operating activities	**$ 25,138**	$ 30,716	$ 33,241

See Accompanying Notes to Consolidated Financial Statements.

Consolidated Statement of Cash Flows *Continued*

Years Ended December 31, *(in millions)*	**2005**	2004	2003
Cash flows from investing activities:			
Cost of bonds, at market sold	**$ 111,866**	$ 91,714	$ 90,430
Cost of bonds, at market matured or redeemed	**16,017**	13,958	15,966
Cost of equity securities sold	**11,072**	11,711	10,012
Realized capital gains (losses)	**341**	44	(442)
Purchases of fixed maturities	**(152,045)**	(158,023)	(153,742)
Purchases of equity securities	**(12,972)**	(13,674)	(10,473)
Acquisitions, net of cash acquired	**–**	–	(2,091)
Mortgage, policy and collateral loans granted	**(5,306)**	(2,128)	(3,016)
Repayments of mortgage, policy and collateral loans	**3,973**	1,731	2,043
Sales of securities available for sale	**9,324**	4,291	8,376
Maturities of securities available for sale	**3,023**	5,802	4,690
Purchases of securities available for sale	**(20,642)**	(16,133)	(12,010)
Sales of flight equipment	**695**	1,329	1,212
Purchases of flight equipment	**(6,193)**	(4,860)	(5,460)
Change in securities lending collateral	**(10,302)**	(19,777)	(6,048)
Net additions to real estate and other fixed assets	**(2,018)**	(950)	(1,131)
Sales or distributions of other invested assets	**14,379**	8,453	8,730
Investments in other invested assets	**(14,387)**	(11,599)	(10,483)
Change in short-term investments	**760**	(2,542)	(1,563)
Investments in partially owned companies	**(50)**	1	255
Finance receivable originations and purchases	**(52,281)**	(21,636)	(14,690)
Finance receivable principal payments received	**47,425**	15,173	12,531
Net cash used in investing activities	**$ (57,321)**	$ (97,115)	$ (66,904)
Cash flows from financing activities:			
Receipts from policyholders' contract deposits	**$ 46,298**	$ 55,919	$ 38,867
Withdrawals from policyholders' contract deposits	**(35,797)**	(24,497)	(18,422)
Change in trust deposits and deposits due to banks and other depositors	**629**	648	641
Change in commercial paper	**(485)**	3,755	(3,174)
Proceeds from notes, bonds, loans and mortgages payable	**53,875**	31,918	23,665
Repayments on notes, bonds, loans and mortgages payable	**(42,248)**	(22,565)	(14,408)
Liquidation of zero coupon notes payable	**–**	(189)	–
Proceeds from guaranteed investment agreements	**12,388**	10,814	6,387
Maturities of guaranteed investment agreements	**(10,496)**	(7,232)	(5,900)
Change in securities lending payable	**10,437**	19,777	6,501
Redemption of subsidiary company preferred stock	**(100)**	(200)	(371)
Proceeds from common stock issued	**82**	158	74
Cash dividends to shareholders	**(1,421)**	(730)	(584)
Acquisition of treasury stock	**(176)**	(1,083)	(207)
Other – net	**13**	1	1
Net cash provided by financing activities	**$ 32,999**	$ 66,494	$ 33,070
Supplementary information:			
Taxes paid	**$ 2,593**	$ 3,060	$ 2,454
Interest paid	**$ 4,958**	$ 4,314	$ 4,128

See Accompanying Notes to Consolidated Financial Statements.

Consolidated Statement of Comprehensive Income

Years Ended December 31, *(in millions)*	**2005**	2004	2003
Comprehensive income (loss):			
Net income	**$10,477**	$ 9,839	$ 8,108
Other comprehensive income (loss):			
Unrealized (depreciation) appreciation of investments – net of reclassification adjustments	**(3,577)**	1,868	4,159
Deferred income tax benefit (expense) on above changes	**1,599**	(612)	(1,237)
Foreign currency translation adjustments	**(926)**	993	347
Applicable income tax benefit (expense) on above changes	**386**	(170)	4
Net derivative gains arising from cash flow hedging activities	**35**	83	75
Deferred income tax expense on above changes	**(7)**	(33)	(22)
Retirement plan liabilities adjustment, net of tax	**13**	(22)	(66)
Other comprehensive income (loss)	**(2,477)**	2,107	3,260
Comprehensive income (loss)	**$ 8,000**	$11,946	$11,368

See Accompanying Notes to Consolidated Financial Statements.

1. Summary of Significant Accounting Policies

(a) Principles of Consolidation: Certain of AIG's foreign subsidiaries included in the consolidated financial statements report on a fiscal year ending November 30. The consolidated financial statements include the accounts of AIG, its majority owned subsidiaries and those entities required to be consolidated under applicable accounting standards. See also Note 1(gg) herein. All material intercompany accounts and transactions have been eliminated.

(b) Basis of Presentation: The accompanying financial statements have been prepared on the basis of U.S. generally accepted accounting principles (GAAP). The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting periods. Actual results could differ from those estimates.

General Insurance Operations: AIG's General Insurance subsidiaries are multiple line companies writing substantially all lines of property and casualty insurance both domestically and abroad. Premiums are earned primarily on a pro rata basis over the term of the related coverage. The reserve for unearned premiums represents the portion of premiums written relating to the unexpired terms of coverage.

Acquisition costs represent those costs, including commissions and premium taxes, that vary with and are primarily related to the acquisition of new business. These costs are deferred and amortized over the period in which the related premiums written are earned. The deferred policy acquisition cost (DAC) asset is reviewed for recoverability based on the profitability of the underlying insurance contracts. Investment income is not anticipated in the recoverability of deferred policy acquisition costs.

Losses and loss expenses are charged to income as incurred. The reserve for losses and loss expenses represents the accumulation of estimates for reported losses and includes provisions for losses incurred but not reported. The methods of determining such estimates and establishing resulting reserves, including amounts relating to reserves for estimated unrecoverable reinsurance, are reviewed and updated. Adjustments resulting therefrom are reflected in income currently. AIG discounts its loss reserves relating to workers compensation business written by its U.S. domiciled subsidiaries as permitted by the domiciliary statutory regulatory authorities. As of year end 2005, this discount is $512 million on a tabular basis and $1.11 billion on a non-tabular basis. Additionally, AIG discounts liability business assumed by American International Reinsurance Company, Ltd. (AIRCO) from the Domestic Brokerage Group (DBG) as permitted by its domiciliary regulatory authority. As of year end 2005, this discount is $490 million. The total amount of discount is $2.11 billion or less than three percent of outstanding loss reserves as reflected on the accompanying consolidated balance sheet.

Life Insurance & Retirement Services Operations: AIG's Life Insurance & Retirement Services subsidiaries offer a wide range of insurance and retirement savings products both domestically and abroad. Insurance-oriented products consist of individual and group life, payout annuities, endowment, and accident and health policies. Retirement savings-oriented products consist generally of fixed and variable annuities.

Premiums for life insurance products and life contingent annuities are recognized as revenues when due. Estimates for premiums due but not yet collected are accrued. Benefits and expenses are provided against such revenues to recognize profits over the estimated life of the policies. Revenues for universal life and investment-type products consist of policy charges for the cost of insurance, administration, and surrenders during the period. Policy charges collected with respect to future services are deferred and recognized in a manner similar to the deferred policy acquisition costs related to such products. Expenses include interest credited to policy account balances and benefit payments made in excess of policy account balances. Personal accident products are accounted for in a manner similar to general insurance products described above.

Policy acquisition costs for life insurance products are generally deferred and amortized over the premium paying period of the policy Statement of Financial Accounting Standards No. 60, "Accounting and Reporting by Insurance Enterprises" (FAS 60). Policy acquisition costs and policy issuance costs related to universal life and investment-type products (investment-oriented products) are deferred and amortized, with interest, in relation to the incidence of estimated gross profits to be realized over the estimated lives of the contracts under Statement of Financial Accounting Standards No. 97, "Accounting and Reporting by Insurance Enterprises for Certain Long-Duration Contracts and for Realized Gains and Losses from the Sale of Investments" (FAS 97). Estimated gross profits are composed of net interest income, net realized investment gains and losses, fees, surrender charges, expenses, and mortality and morbidity gains and losses.

The resulting DAC asset is reviewed for recoverability based on the profitability (both current and projected future) of the underlying insurance contracts.

The deferred policy acquisition costs for investment-oriented products are adjusted with respect to estimated gross profits as a result of changes in the net unrealized gains or losses on debt and equity securities available for sale. That is, as debt and equity securities available for sale are carried at aggregate fair value, an adjustment is made to deferred policy acquisition costs equal to the change in amortization that would have been recorded if such securities had been sold at their stated aggregate fair value and the proceeds reinvested at current yields. The change in this adjustment, net of tax, is included with the change in net unrealized gains/losses on debt and equity securities available for sale that is credited or charged directly to comprehensive income. Deferred policy acquisition costs have been decreased by $1.14 billion at December 31, 2005 and decreased by $2.26 billion at December 31, 2004 for this adjustment. See also Note 4 herein.

Value of Business Acquired (VOBA) is determined at time of acquisition. This value is based on present value of future

1. Summary of Significant Accounting Policies

Continued

pre-tax profits discounted at current yields applicable at time of purchase. For products accounted under FAS 60, the VOBA is amortized over the life of the business similar to that for Deferred Acquisition Costs based on the assumptions at purchase. For FAS 97 products, the VOBA is amortized in relation to the estimated gross profits to date for each period. No impairments have occurred for acquired business to date.

The liabilities for future policy benefits and policyholders' contract deposits are established using assumptions described in Note 6.

Financial Services: AIG's Financial Services subsidiaries engage in diversified activities including aircraft and equipment leasing, capital markets transactions, consumer finance and insurance premium financing.

AIG's Aircraft Finance operations represent the operations of International Lease Finance Corporation (ILFC), which generates its revenues primarily from leasing new and used commercial jet aircraft to domestic and foreign airlines. Revenues also result from the remarketing of commercial jets for its own account, for airlines and for financial institutions.

ILFC, as lessor, leases flight equipment principally under operating leases. Accordingly, income is recognized over the life of the lease as rentals become receivable under the provisions of the lease or, in the case of leases with varying payments, under the straight-line method over the noncancelable term of the lease. In certain cases, leases provide for additional payments contingent on usage. Rental income is recognized at the time such usage occurs less a provision for future contractual aircraft maintenance. ILFC is also a remarketer of flight equipment for its own account and for airlines and financial institutions and provides, for a fee, fleet management services to certain third-party operators. ILFC's revenues from such operations consist of net gains on sales of flight equipment, commissions and management service fees.

The Capital Markets operations of AIG are conducted through AIG Financial Products Corp. and AIG Trading Group, Inc. and their respective subsidiaries (collectively referred to as AIGFP), which engages as principal in standard and customized interest rate, currency, equity, commodity, energy and credit products with top-tier corporations, financial institutions, governments, agencies, institutional investors, and high-net-worth individuals throughout the world. AIGFP also raises funds through municipal reinvestment contracts and other private and public securities offerings, investing the proceeds in a diversified portfolio of high grade securities and derivative transactions. AIGFP owns inventories in the commodities in which it trades and may reduce the exposure to market risk through the use of swaps, forwards, futures, and option contracts. See also Note 2 herein.

Consumer Finance operations include American General Finance, Inc. and its subsidiaries (AGF) as well as AIG Consumer Finance Group, Inc. (AIGCFG). AGF provides a wide variety of consumer finance products, including nonconforming real estate mortgages, consumer loans, retail sales finance and credit-related insurance to customers in the United States. AIGCFG, through its subsidiaries, is engaged in developing a multi-product consumer finance business with an emphasis on emerging markets. See also Note 2 herein.

Finance charges are recognized as revenue using the interest method. Revenue ceases to be accrued when contractual payments are not received for four consecutive months for loans and retail sales contracts, and for six months for revolving retail accounts and private label receivables. Extension fees, late charges, and prepayment penalties are recognized as revenue when received.

Direct costs of originating loans, net of nonrefundable points and fees, are deferred and included in the carrying amount of the related loans. The amount deferred is recognized as an adjustment to finance charge revenues, using the interest method applied on a pool basis over a term that anticipates prepayments. If loans are prepaid, any remaining deferral is charged or credited to revenue.

The allowance for finance receivable losses is maintained at a level considered adequate to absorb estimated credit losses in the existing portfolio. The portfolio is periodically evaluated on a pooled basis and factors such as economic conditions, portfolio composition, and loss and delinquency experience are considered in the evaluation of the allowance.

Foreclosure proceedings are initiated on real estate loans when four monthly installments are past due, and these loans are charged off at foreclosure. All other finance receivables are charged off when minimal or no collections have been made for six months.

Together, the Aircraft Finance, Capital Markets and Consumer Finance operations generate the vast majority of the revenues produced by AIG's consolidated Financial Services operations.

Imperial A.I. Credit Companies also contribute to Financial Services income. This operation engages principally in insurance premium financing for both AIG's customers and those of other insurers.

Asset Management Operations: AIG's Asset Management operations comprise a wide variety of investment-related services and investment products including institutional and retail asset management, broker dealer services and spread-based investment business from the sale of guaranteed investment contracts, also known as funding agreements (GICs). Such products and services are offered to individuals and institutions both domestically and overseas. The fees generated with respect to Asset Management operations are recognized as revenues when earned. Certain costs incurred in the sale of mutual funds are deferred and subsequently amortized.

(c) Investments in Fixed Maturities and Equity Securities: Bonds held to maturity are principally owned by the insurance subsidiaries and are carried at amortized cost where AIG has the ability and positive intent to hold these securities until maturity.

Where AIG may not have the positive intent to hold bonds and preferred stocks until maturity and not classified as trading, these securities are considered to be available for sale and carried at current market values. Interest income with respect to fixed maturity securities is accrued as earned.

1. Summary of Significant Accounting Policies

Continued

Premiums and discounts arising from the purchase of bonds are treated as yield adjustments over their estimated lives or call date, if applicable.

Bond trading securities are carried at current market values, and changes in fair value are recorded in income currently.

Common and preferred stocks are carried at current market values. Dividend income is generally recognized when receivable.

Unrealized gains and losses from investments in equity securities and fixed maturities available for sale are reflected as a separate component of comprehensive income, net of deferred income taxes in consolidated shareholders' equity currently. Unrealized gains and losses from investments in trading securities are reflected in income currently. Investments in fixed maturities and equity securities are recorded on a trade date basis.

Realized capital gains and losses are determined principally by specific identification. AIG evaluates its investments for impairment. As a matter of policy, the determination that a security has incurred an other-than-temporary decline in value and the amount of any loss recognition requires the judgment of AIG's management and a continual review of its investments.

In general, a security is considered a candidate for other-than-temporary impairment if it meets any of the following criteria:

- Trading at a significant (25 percent or more) discount to par or amortized cost (if lower) for an extended period of time (nine months or longer);
- The occurrence of a discrete credit event resulting in *(i)* the issuer defaulting on a material outstanding obligation; or *(ii)* the issuer seeking protection from creditors under the bankruptcy laws or any similar laws intended for the court supervised reorganization of insolvent enterprises; or *(iii)* the issuer proposing a voluntary reorganization pursuant to which creditors are asked to exchange their claims for cash or securities having a fair value substantially lower than par value of their claims; or
- In the opinion of AIG's management, it is probable that AIG may not realize a full recovery on its investment, irrespective of the occurrence of one of the foregoing events.

Once a security has been identified as other-than-temporarily impaired, the amount of such impairment is determined by reference to that security's contemporaneous market price and recorded as a charge to earnings.

AIG also enters into dollar roll agreements. These are agreements to sell mortgage-backed securities and to repurchase substantially similar securities at a specified price and date in the future. At December 31, 2005, 2004 and 2003, there were no dollar roll agreements outstanding.

(d) Mortgage Loans on Real Estate, Policy, and Collateral Loans – net: Mortgage loans on real estate, policy loans, and collateral loans are carried at unpaid principal balances. Interest income on such loans is accrued as earned.

Impairment of mortgage loans on real estate and collateral loans is based upon certain risk factors and when collection of all amounts due under the contractual term is not probable. This impairment is generally measured based on the present value of expected future cash flows discounted at the loan's effective interest rate subject to the fair value of underlying collateral. Interest income on such loans is recognized as cash is received.

There is no allowance for policy loans, as these loans serve to reduce the death benefit paid when the death claim is made and the balances are effectively collateralized by the cash surrender value of the policy.

(e) Financial Services – Flight Equipment: Flight equipment is stated at cost. Major additions, modifications and interest are capitalized. Normal maintenance and repairs, airframe and engine overhauls and compliance with return conditions of flight equipment on lease are provided by and paid for by the lessee. Under the provisions of most leases for certain airframe and engine overhauls, the lessee is reimbursed for costs incurred up to but not exceeding contingent rentals paid to AIG by the lessee. AIG provides a charge to income for such reimbursements based upon the expected reimbursements during the life of the lease. Depreciation and amortization are computed on the straight-line basis to a residual value of approximately 15 percent over the estimated useful lives of the related assets but not exceeding 25 years. ILFC's management is very active in the airline industry and remains current on issues affecting its fleet, including events and circumstances that may affect impairment of aircraft values (e.g. residual values, useful life, current and future revenue generating capacity). Aircraft in the fleet are evaluated, as necessary, based on these events and circumstances in accordance with Statement of Financial Accounting Standards (FAS) No. 144 "Accounting for the Impairment or Disposal of Long-Lived Assets" (FAS 144). FAS 144 requires that long-lived assets be reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. Recoverability of assets is measured by comparing the carrying amount of an asset to future undiscounted net cash flows expected to be generated by the asset. These evaluations for impairment are significantly affected by estimates of future revenues and other factors which involve some amount of uncertainty.

This caption also includes deposits for aircraft to be purchased. At the time the assets are retired or disposed of, the cost and associated accumulated depreciation and amortization are removed from the related accounts and the difference, net of proceeds, is recorded as a gain or loss.

(f) Financial Services – Securities Available for Sale, at market value: These securities are held to meet long-term investment objectives and are accounted for as available for sale, carried at current market values and recorded on a trade-date basis. This portfolio is hedged using interest rate, foreign exchange, commodity and equity derivatives. The market risk associated with such hedges is managed on a portfolio basis, with third party hedging transactions executed as necessary. As hedge accounting treatment is not achieved in accordance with

1. Summary of Significant Accounting Policies

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FAS 133, the unrealized gains and losses on these securities resulting from changes in interest rates, currency rates and equity prices are recorded in consolidated shareholders' equity while the unrealized gains and losses on the related economic hedges are reflected in operating income.

(g) Financial Services – Trading Securities, at market value: Trading securities are held to meet short term investment objectives, including hedging securities. These securities are recorded on a trade-date basis and carried at current market values. Unrealized gains and losses are reflected in income currently.

(h) Financial Services – Spot Commodities: Spot commodities are carried at lower of cost or market value and are recorded on a trade-date basis. The exposure to market risk may be reduced through the use of forwards, futures and option contracts. Lower of cost or market value reductions in commodity positions and unrealized gains and losses in related derivatives are reflected in income currently.

(i) Financial Services – Unrealized Gain and Unrealized Loss on Swaps, Options and Forward Transactions: Interest rate, currency, equity and commodity swaps, swaptions, options and forward transactions are accounted for as derivatives recorded on a trade-date basis and are carried at current market values or estimated fair values when market values are not available. Unrealized gains and losses are reflected in income currently, where appropriate. In certain instances, when income is not recognized upfront under EITF 02-03, "Issues Involved in Accounting for Derivative Contracts Held for Trading Purposes and Contracts Involved in Energy Trading and Risk Management Activities", (EITF 02-03), income is recognized over the life of the contract. Estimated fair values are based on the use of valuation models that utilize, among other things, current interest, foreign exchange, equity, commodity and volatility rates. AIG attempts to secure reliable and independent current market prices, such as published exchange prices, external subscription services' prices such as Bloomberg or Reuters or third-party broker quotes for use in its models. When such prices are not available, AIG uses an internal methodology which includes interpolation and extrapolation from observable and verifiable prices nearest to the dates of the transactions. These valuations represent an assessment of the present values of expected future cash flows of these transactions and reflect market and credit risk. The portfolio's discounted cash flows are evaluated with reference to current market conditions, maturities within the portfolio, and other relevant factors. Based upon this evaluation, it is determined what offsetting transactions, if any, are necessary to reduce the market risk of the portfolio. AIG manages its market risk with a variety of transactions, including swaps, trading securities, futures and forward contracts and other transactions as appropriate. Because of the limited liquidity of some of these instruments, the recorded values of these transactions may be different from the values that might be realized if AIG were to sell or close out the transactions prior to maturity. AIG believes that such differences are not significant to the financial condition or liquidity. Such differences would be immediately recognized in income when the transactions are sold or closed out prior to maturity.

(j) Financial Services – Trading Assets and Trading Liabilities: Trading assets and trading liabilities include option premiums paid and received and receivables from and payables to counterparties which relate to unrealized gains and losses on futures, forwards, and options and balances due from and due to clearing brokers and exchanges.

Futures, forwards, and options purchased and written are accounted for as derivatives on a trade-date basis and are carried at fair values. Unrealized gains and losses are reflected in income currently. The fair values of futures contracts are based on closing exchange quotations. Commodity forward transactions are carried at fair values derived from dealer quotations and underlying commodity exchange quotations. For long-dated forward transactions, where there are no dealer or exchange quotations, fair values are derived using internally developed valuation methodologies based on observable and available market information. Options are carried at fair values based on the use of valuation models that utilize, among other things, current interest or commodity rates, and foreign exchange and volatility rates, as applicable.

(k) Financial Services – Securities Purchased (Sold) Under Agreements to Resell (Repurchase), at contract value: Purchases of securities under agreements to resell and sales of securities under agreements to repurchase are accounted for as collateralized borrowing or lending transactions and are recorded at their contracted resale or repurchase amounts, plus accrued interest. AIG's policy is to take possession of or obtain a security interest in securities purchased under agreements to resell.

AIG minimizes the credit risk that counterparties to transactions might be unable to fulfill their contractual obligations by monitoring customer credit exposure and collateral value and generally requiring additional collateral to be deposited with AIG when deemed necessary.

(l) Financial Services – Finance Receivables: Finance receivables are carried at amortized cost which includes accrued finance charges on interest bearing finance receivables, unamortized deferred origination costs, and unamortized net premiums and discounts on purchased finance receivables. They are net of unamortized finance charges and unamortized points and fees. The allowance for finance receivable losses is established through the provision for finance receivable losses charged to expense.

(m) Securities Lending Collateral and Securities Lending Payable: AIG's insurance and asset management operations lend their securities and primarily take cash as collateral with respect to the securities lent. Invested collateral consists primarily of floating rate debt securities. Income earned on invested collateral, net of interest payable to the collateral provider, is recorded in net investment income.

1. Summary of Significant Accounting Policies

Continued

The market value of securities pledged under securities lending arrangements were $59.0 billion and $48.8 billion as of December 31, 2005 and 2004, respectively. Of these amounts, $58.3 billion and $48.2 billion represent securities included in bonds available for sale in AIG's consolidated balance sheet as of December 31, 2005 and 2004, respectively.

(n) Other Invested Assets: Other invested assets consist primarily of investments by AIG's insurance operations in hedge funds and limited partnerships.

Hedge funds and limited partnerships in which AIG holds in the aggregate less than a five percent interest are reported at fair value. The change in fair value is recognized as a component of other comprehensive income.

With respect to hedge funds and limited partnerships in which AIG holds in the aggregate a five percent or greater interest or less than five percent interest but AIG has more than a minor influence over the operations of the investee, AIG's carrying value is the net asset value. The changes in such net asset values accounted for under the equity method are recorded in earnings through net investment income.

AIG obtains the fair value of its investments in limited partnerships and hedge funds from information provided by the general partner or manager of each of these investments, the accounts of which are generally audited on an annual basis.

(o) Short-term investments: Short-term investments consist of interest bearing cash equivalents, time deposits, and investments maturing within one year, such as commercial paper.

(p) Reinsurance Assets: Reinsurance assets include the balances due from both reinsurance and insurance companies under the terms of AIG's reinsurance agreements for paid and unpaid losses and loss expenses, ceded unearned premiums and ceded future policy benefits for life and accident and health insurance contracts and benefits paid and unpaid. Amounts related to paid and unpaid losses and loss expenses with respect to these reinsurance agreements are substantially collateralized.

(q) Other Assets: Other assets consist of prepaid expenses, including deferred advertising costs, derivatives assets at market value, and other deferred charges. Generally, advertising costs are expensed as incurred except for certain direct response campaigns, which are deferred over the expected future benefit period in accordance with Statement of Position 93-7, "Reporting on Advertising Costs." In instances where AIG can demonstrate that its direct-response advertising, whose primary purpose is to elicit sales to customers, can be shown to have responded specifically to the advertising and that results in probable future economic benefits are capitalized. Deferred advertising costs are included in other assets, are amortized on a campaign by campaign basis over the expected economic future benefit period and reviewed regularly for recoverability. The amount reported in other assets was $915 million and $879 million at December 31, 2005 and 2004, respectively. The amount of expense amortized into earnings was $272 million, $244 million and $217 million, for 2005, 2004, and 2003, respectively.

(r) Deposit Liabilities: AIG has entered into certain insurance and reinsurance contracts, primarily in its general insurance segment, which do not contain sufficient amount and timing risk to be accounted for as insurance or reinsurance. Accordingly, these transactions are recorded based upon deposit accounting, and the premiums received, after deduction for certain related expenses, are recorded as deposits within Other liabilities on the consolidated balance sheet. Net proceeds of these deposits are invested and generate net investment income. As amounts are paid, consistent with the underlying contracts, the deposit liability is reduced. Periodically, AIG evaluates the expected payments to be made under each contract and adjusts the deposit liability through earnings in the current period.

(s) Investments in Partially Owned Companies: Generally, the equity method of accounting is used for AIG's investment in companies in which AIG's ownership interest approximates 20 percent but is not greater than 50 percent (minority owned companies). At December 31, 2005, AIG's significant investments in partially owned companies included its 24.3 percent interest in IPC Holdings, Ltd., its 23.4 percent interest in Allied World Assurance Holdings, Ltd., its 26 percent interest in Tata AIG Life Insurance Company, Ltd., its 26 percent interest in Tata AIG General Insurance Company, Ltd. and its 24.5 percent interest in The Fuji Fire and Marine Insurance Co., Ltd. This balance sheet caption also includes investments in less significant partially owned companies. The amounts of dividends received from unconsolidated entities where AIG's ownership interest is less than 50 percent were $146 million, $22 million and $13 million in 2005, 2004 and 2003, respectively. The undistributed earnings of unconsolidated entities where AIG's ownership interest is less than 50 percent were $179 million, $445 million and $320 million as of December 31, 2005, 2004 and 2003, respectively.

(t) Real Estate and Other Fixed Assets: The costs of buildings and furniture and equipment are depreciated principally on a straight-line basis over their estimated useful lives (maximum of 40 years for buildings and ten years for furniture and equipment). Expenditures for maintenance and repairs are charged to income as incurred; expenditures for betterments are capitalized and depreciated.

AIG periodically assesses the carrying value of its real estate relative to the market values of real estate within the specific local area, for the purpose of determining any asset impairment.

(u) Separate and Variable Accounts: Separate and variable accounts represent funds for which investment income and investment gains and losses accrue directly to the policyholders who predominantly bear the investment risk. Each account has specific investment objectives, and the assets are carried at market value. The assets of each account are legally segregated and are not subject to claims which arise out of any other

1. Summary of Significant Accounting Policies

Continued

business of AIG. The liabilities for these accounts are generally equal to the account assets.

(v) Financial Services – Securities and Spot Commodities Sold but not yet Purchased, at market value: Securities and spot commodities sold but not yet purchased represent sales of securities and spot commodities not owned at the time of sale. The obligations arising from such transactions are recorded on a trade-date basis and carried at market values.

(w) Liabilities Connected to Trust Preferred Stock: Liabilities connected to trust preferred stock principally relates to outstanding securities issued by AGC, a wholly owned subsidiary of AIG. Cash distributions on such preferred stock are accounted for as interest expense.

(x) Preferred Shareholders' Equity in Subsidiary Companies: Preferred shareholders' equity in subsidiary companies relates principally to outstanding preferred stock or interest of ILFC, a wholly owned subsidiary of AIG. Cash distributions on such preferred stock or interest are accounted for as interest expense.

(y) Other Policyholders' Funds: Other policyholders' funds are reported at cost and include any policyholders' funds on deposit which encompasses premium deposits and similar items.

(z) Other Liabilities: Other liabilities consist of other funds on deposits, derivatives liabilities at market value, and other payables.

(aa) Short- and Long-Term Borrowings: AIG's funding is principally obtained from medium-term and long-term borrowings. Commercial paper, when issued at a discount, is recorded at the proceeds received and accreted to its par value. Long-term borrowings are carried at the principal amount borrowed, net of unamortized discounts or premiums. See Note 9 herein for additional information.

(bb) Translation of Foreign Currencies: Financial statement accounts expressed in foreign currencies are translated into U.S. dollars in accordance with Statement of Financial Accounting Standards No. 52, "Foreign Currency Translation" (FAS 52). Under FAS 52, functional currency assets and liabilities are translated into U.S. dollars generally using current rates of exchange prevailing at the balance sheet date of each respective subsidiary and the related translation adjustments are recorded as a separate component of comprehensive income, net of any related taxes, in consolidated shareholders' equity. Functional currencies are generally the currencies of the local operating environment. Income statement accounts expressed in functional currencies are translated using average exchange rates. The adjustments resulting from translation of financial statements of foreign entities operating in highly inflationary economies are recorded in income. Exchange gains and losses resulting from foreign currency transactions are recorded in income currently. The exchange gain or loss with respect to utilization of qualifying foreign exchange hedging activities is recorded as a component of other comprehensive income. In the situation where the qualifying hedge is identified to an underlying foreign currency transaction, the hedging activity exchange or loss is transferred out of other comprehensive income and netted against the exchange gain or loss of the underlying in income.

(cc) Income Taxes: Deferred tax assets and liabilities are recorded for the effects of temporary differences between the tax basis of an asset or liability and its reported amount in the Consolidated Financial Statements. AIG assesses its ability to realize deferred tax assets primarily based on the earnings history, the future earnings potential, the reversal of taxable temporary differences, and the tax planning strategies available to the legal entities recognizing deferred tax assets, all through which realization of deferred tax assets will be achieved, as discussed in Statement of Financial Accounting Standards No. 109, "Accounting for Income Taxes." See Note 3 herein for further discussion of income taxes.

(dd) Earnings Per Share: Basic earnings per common share are based on the weighted average number of common shares outstanding, retroactively adjusted to reflect all stock dividends and stock splits. Diluted earnings per share are based on those shares used in basic earnings per share plus shares that would have been outstanding assuming issuance of common shares for all dilutive potential common shares outstanding, retroactively adjusted to reflect all stock dividends and stock splits.

The computation of earnings per share for December 31, 2005, 2004 and 2003 was as follows:

Years Ended December 31, *(in millions, except per share data)*	**2005**	2004	2003
Numerator for basic earnings per share:			
Income before cumulative effect of accounting changes	**$10,477**	$9,983	$8,099
Cumulative effect of accounting changes, net of tax	**–**	(144)	9
Net income applicable to common stock	**$10,477**	$9,839	$8,108
Denominator for basic earnings per share:			
Average shares outstanding used in the computation of per share earnings:			
Common stock issued	**2,752**	2,752	2,752
Common stock in treasury	**(155)**	(146)	(142)
Average shares outstanding – basic	**2,597**	2,606	2,610

(continued)

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Years Ended December 31, (in millions, except per share data)	2005	2004	2003
Numerator for diluted earnings per share:			
Income before cumulative effect of accounting changes	**$10,477**	$9,983	$8,099
Cumulative effect of accounting changes, net of tax	**–**	(144)	9
Net income applicable to common stock	**10,477**	9,839	8,108
Interest on contingently convertible bonds, net of tax[(a)]	**11**	11	11
Adjusted net income applicable to common stock[(a)]	**$10,488**	$9,850	$8,119
Denominator for diluted earnings per share:			
Average shares outstanding	**2,597**	2,606	2,610
Incremental shares from potential common stock:			
Average number of shares arising from outstanding employee stock plans (treasury stock method)[(b)]	**21**	22	18
Contingently convertible bonds[(a)]	**9**	9	9
Adjusted average shares outstanding – diluted[(a)]	**2,627**	2,637	2,637
Earnings per share:			
Basic:			
Income before cumulative effect of accounting changes	**$ 4.03**	$ 3.83	$ 3.10
Cumulative effect of accounting changes, net of tax	**–**	(0.06)	–
Net income	**$ 4.03**	$ 3.77	$ 3.10
Diluted:			
Income before cumulative effect of accounting changes	**$ 3.99**	$ 3.79	$ 3.07
Cumulative effect of accounting changes, net of tax	**–**	(0.06)	–
Net income	**$ 3.99**	$ 3.73	$ 3.07

(a) Assumes conversion of contingently convertible bonds due to the adoption of EITF Issue No. 04-8 "Accounting Issues Related to Certain Features of Contingently Convertible Debt and the Effect on Diluted Earnings per Share."

(b) Certain shares arising from employee stock plans were not included in the computation of diluted earnings per share where the exercise price of the options exceeded the average market price and would have been antidilutive. The number of shares excluded were 19 million, 7 million and 26 million for 2005, 2004 and 2003, respectively.

(ee) Derivatives: AIG carries all derivatives in the consolidated balance sheet at fair value. The financial statement recognition of the change in the fair value of a derivative depends on a number of factors, including the intended use of the derivative and the extent to which it is effective as part of a hedge transaction. The changes in fair value of the derivative transactions of AIGFP are currently presented as a component of AIG's operating income. However, in certain instances, when income is not recognized upfront under EITF 02-03, income is recognized over the life of the contract, where appropriate.

The discussion below relates to the derivative activities of AIG (other than those of AIGFP) that qualify for hedge accounting treatment under FAS 133.

For derivatives designated as hedges, on the date the derivative contract is entered into, AIG designates the derivative as: *(i)* a hedge of the subsequent changes in the fair value of a recognized asset or liability or of an unrecognized firm commitment ("fair value" hedge); *(ii)* a hedge of a forecasted transaction, or the variability of cash flows to be received or paid related to a recognized asset or liability ("cash flow" hedge); or *(iii)* a hedge of a net investment in a foreign operation. Fair value and cash flow hedges may involve foreign currencies ("foreign currency hedges"). The gain or loss in the fair value of a derivative that is appropriately and contemporaneously documented, designated and is highly effective as a fair value hedge is recorded in current period earnings, along with the loss or gain on the hedged item attributable to the hedged risk. The gain or loss in the fair value of a derivative that is appropriately and contemporaneously documented, designated and is highly effective as a cash flow hedge is recorded in other comprehensive income, until earnings are affected by the variability of cash flows. Of the amount deferred in Other Comprehensive Income at December 31, 2005, AIG does not expect a material amount to be reclassified into earnings over the next twelve months. The portion of the gain or loss in the fair value of a derivative in a cash flow hedge that represents hedge ineffectiveness is recognized immediately in current period earnings. The amount of ineffectiveness was not material for 2005, 2004 and 2003. The gain or loss in the fair value of a derivative that is appropriately and contemporaneously documented, designated and is highly effective as a hedge of a net investment in a foreign operation is recorded in the foreign currency translation adjustments account within other comprehensive income. Changes in the fair value of derivatives used for other than hedging activities are reported in current period earnings (principally in realized capital gains and losses for AIG's insurance operations). AIG had no hedges that were considered fair value hedges at December 31, 2005. At December 31, 2005, AIG's hedge accounting was limited to cash flow hedge accounting primarily related to the hedge of forecasted transactions.

AIG assesses, both at the hedge's inception and on an ongoing basis, whether the derivatives used in hedging transactions are highly effective in offsetting changes in fair values or cash flows of hedged items.

As of January 1, 2005 and December 31, 2005, the related balance of accumulated derivative net loss arising from cash flow hedges, net of tax, was $53 million and $25 million, respectively. Of the change in accumulated derivative net gain, $3 million represents current period changes in fair values of derivatives used in cash flow hedge transactions, and $25 million represents current period reclassifications to operating income.

1. Summary of Significant Accounting Policies

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In addition to hedging activities, AIG also uses derivative instruments with respect to investment operations, which include, among other things, credit default swaps, and purchasing investments with embedded derivatives, such as equity linked notes and convertible bonds. All changes in the market value of these derivatives are recorded in earnings. AIG bifurcates an embedded derivative where: *(i)* the economic characteristics of the embedded instruments are not clearly and closely related to those of the remaining components of the financial instrument; *(ii)* the contract that embodies both the embedded derivative instrument and the host contract is not remeasured at fair value; and *(iii)* a separate instrument with the same terms as the embedded instrument meets the definition of a derivative under Statement of Financial Accounting Standards No. 133, "Accounting for Derivative Instruments and Hedging Activities." See also Note 20 herein.

(ff) Goodwill and Intangible Assets: Goodwill is reviewed for impairment on an annual basis, or more frequently if circumstances indicate that a possible impairment has occurred. The assessment of impairment involves a two-step process whereby an initial assessment for potential impairment is performed, followed by a measurement of the amount of impairment, if any. No impairment has been recorded by AIG in 2005, 2004 or 2003.

On August 29, 2003, AIG acquired 100 percent of the outstanding common shares of GE Edison Life Insurance Company in Japan and the U.S.-based auto and home insurance business of General Electric Company (GE) for $2.1 billion. The acquisition expanded AIG's life insurance presence in Japan and AIG's auto and home insurance presence in the U.S. At the date of acquisition, the fair values of the assets acquired and liabilities assumed were $20 billion and $19 billion, respectively. Goodwill associated with this transaction as of December 31, 2003 amounted to $1.3 billion, primarily related to the life business.

Other changes in the carrying amount of goodwill are primarily caused as a result of foreign currency translation adjustments and other purchase price adjustments.

(gg) Recent Accounting Standards: In December 2003, FASB issued Interpretation No. 46R, "Consolidation of Variable Interest Entities Revised" (FIN46R). See also Note 19 herein.

In March 2005, FASB issued FSP FIN46R-5 "Implicit Variable Interests under FASB Interpretation No. 46 (revised December 2003), Consolidation of Variable Interest Entities" (FSP FIN46R-5) to address whether a reporting enterprise has an implicit variable interest in a variable interest entity (VIE) or potential VIE when specific conditions exist. Although implicit variable interests are mentioned in FIN46R, the term is not defined and only one example is provided. FSP FIN46R-5 offers additional guidance, stating that implicit variable interests are implied financial interests in an entity that change with changes in the fair value of the entity's net assets exclusive of variable interests. An implicit variable interest acts the same as an explicit variable interest except it involves the absorbing and/or receiving of variability indirectly from the entity (rather than directly). The identification of an implicit variable interest is a matter of judgment that depends on the relevant facts and circumstances. The adoption of FSP FIN46R-5 did not have a material effect on AIG's financial condition or results of operations.

In July 2003, the American Institute of Certified Public Accountants issued Statement of Position 03-1, "Accounting and Reporting by Insurance Enterprises for Certain Nontraditional Long-Duration Contracts and for Separate Accounts" (SOP 03-1). See also Note 21 herein.

In December 2003, FASB issued Statement of Financial Accounting Standards No. 132 (Revised), "Employers' Disclosures About Pensions and Other Post Retirement Benefits," which revised disclosure requirements with respect to defined benefit plans. See also Note 15 herein.

At the March 2004 meeting, the Emerging Issue Task Force (EITF) reached a consensus with respect to Issue No. 03-1, "The Meaning of Other-Than-Temporary Impairment and Its Application to Certain Investments." On September 30, 2004, the FASB issued FASB Staff Position (FSP) EITF No. 03-1-1, Effective Date of Paragraphs 10-20 of EITF Issue No. 03-1, "The Meaning of Other-Than-Temporary Impairment and Its Application to Certain Investments" delaying the effective date of this guidance until the FASB has resolved certain implementation issues with respect to this guidance, but the disclosures remain effective. This FSP, retitled FSP FAS 115-1, "The Meaning of Other-Than-Temporary Impairment and Its Application to Certain Investments," replaces the measurement and recognition guidance set forth in Issue No. 03-1 and codifies certain existing guidance on impairment. Adoption of FSP FAS 115-1 is not expected to have a material effect on AIG's financial condition or results of operations.

At the September 2004 meeting, the EITF reached a consensus with respect to Issue No. 04-8, "Accounting Issues Related to Certain Features of Contingently Convertible Debt and the Effect on Diluted Earnings per Share." This Issue addresses when the dilutive effect of contingently convertible debt (Co-Cos) with a market price trigger should be included in diluted earnings per share (EPS). The adoption of Issue No. 04-8 did not have a material effect on AIG's diluted EPS.

In December 2004, the FASB issued Statement No. 123 (revised 2004), "Share-Based Payment" (FAS 123R). FAS 123R and its related interpretive guidance replaces FAS No. 123, "Accounting for Stock-Based Compensation" (FAS 123), and supersedes Accounting Principles Board Opinion No. 25, "Accounting for Stock Issued to Employees" (APB 25). FAS 123, as originally issued in 1995, established as preferable a fair-value-based method of accounting for share-based payment transactions with employees. On January 1, 2003, AIG adopted the recognition provisions of FAS 123. See also Note 14 herein. In April 2005, the SEC delayed the effective date for FAS 123R until the first fiscal year beginning after June 15, 2005. As a result, AIG expects to adopt the provisions of the revised FAS 123R and its related interpretive guidance in the first quarter of 2006. For its service-based awards (1999 Stock Option Plan, 2002 Stock Incentive Plan, and 1999 Employee Stock Purchase Plan), AIG recognizes

1. Summary of Significant Accounting Policies

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compensation on a straight-line basis over the scheduled vesting period. Upon adoption of FAS 123R, AIG will recognize compensation expense to the scheduled retirement date for employees near retirement. AIG does not expect the effect of this change to be material to AIG's results of operations. Consistent with the requirements of FAS 123R, AIG will recognize the unvested portion of its APB 25 awards as compensation expense over the remaining vesting period.

In December, 2005 and January, 2006, C.V. Starr & Co., Inc. (Starr) made tender offers to AIG employees holding Starr common and preferred stock. In conjunction with AIG's adoption of FAS 123R, Starr is considered to be an "economic interest holder" in AIG. As a result, AIG expects to include the compensation expense related to the 2006 tender offer in its consolidated financial statements for the first quarter of 2006.

AIG is currently assessing the effect of FAS 123R and believes the effect will not be material to AIG's financial condition or results of operations.

On December 16, 2004, the FASB issued Statement No. 153, "Exchanges of Nonmonetary Assets — An Amendment of APB Opinion No. 29" (FAS 153). FAS 153 amends APB Opinion No. 29, "Accounting for Nonmonetary Transactions." The amendments made by FAS 153 are based on the principle that exchanges of nonmonetary assets should be measured based on the fair value of the assets exchanged. Further, the amendments eliminate the narrow exception for nonmonetary exchanges of similar productive assets and replace it with a broader exception for exchanges of nonmonetary assets that do not have "commercial substance." Previously, APB Opinion No. 29 required that the accounting for an exchange of a productive asset for a similar productive asset or an equivalent interest in the same or similar productive asset should be based on the recorded amount of the asset relinquished. The provisions in FAS 153 are effective for nonmonetary asset exchanges beginning July 1, 2005. The adoption of FAS 153 did not have a material effect on AIG's financial condition or results of operations.

On June 1, 2005, the FASB issued Statement No. 154, "Accounting Changes and Error Corrections" (FAS 154). FAS 154 replaces APB Opinion No. 20, "Accounting Changes" and FASB Statement No. 3, "Reporting Accounting Changes in Interim Financial Statements." FAS 154 requires that a voluntary change in accounting principle be applied retrospectively with all prior period financial statements presented on the new accounting principle, unless it is impracticable to do so. FAS 154 also provides that a correction of errors in previously issued financial statements should be termed a "restatement." The new standard is effective for accounting changes and correction of errors beginning January 1, 2006.

At the June 2005 meeting, the EITF reached a consensus with respect to Issue No. 04-5, "Determining Whether a General Partner, or the General Partners as a Group, Controls a Limited Partnership or Similar Entity When the Limited Partners Have Certain Rights". The Issue addresses what rights held by the limited partner(s) preclude consolidation in circumstances in which the sole general partner would consolidate the limited partnership in accordance with generally accepted accounting principles absent the existence of the rights held by the limited partner(s). Based on that consensus, the EITF also agreed to amend the consensus in Issue No. 96-16, "Investor's Accounting for an Investee When the Investor Has a Majority of the Voting Interest but the Minority Shareholders Have Certain Approval or Veto Rights." The guidance in this Issue is effective after June 29, 2005 for general partners of all new limited partnerships formed and for existing limited partnerships for which the partnership agreements are modified. For general partners in all other limited partnerships, the guidance in this Issue is effective beginning January 1, 2006. The effect of the adoption of this EITF Issue on existing partnerships that were modified and new partnerships entered into after June 29, 2005, was not material to AIG's financial condition or results of operations. For all other partnerships, AIG is currently assessing the effect of adopting this EITF Issue.

On June 29, 2005, FASB issued Statement 133 Implementation Issue No. B38, "Embedded Derivatives: Evaluation of Net Settlement with Respect to the Settlement of a Debt Instrument through Exercise of an Embedded Put Option or Call Option." This implementation guidance relates to the potential settlement of the debtor's obligation to the creditor that would occur upon exercise of the put option or call option, which meets the net settlement criterion in FAS 133 paragraph 9(a). The effective date of the implementation guidance is January 1, 2006. AIG is currently assessing the effect of implementing this guidance.

On June 29, 2005, FASB issued Statement 133 Implementation Issue No. B39, "Application of Paragraph 13(b) to Call Options That Are Exercisable Only by the Debtor." The conditions in FAS 133 paragraph 13(b) do not apply to an embedded call option in a hybrid instrument containing a debt host contract if the right to accelerate the settlement of the debt can be exercised only by the debtor (issuer/borrower). This guidance does not apply to other embedded derivative features that may be present in the same hybrid instrument. The effective date of the implementation guidance is January 1, 2006. AIG is currently assessing the effect of implementing this guidance.

On September 19, 2005, FASB issued Statement of Position 05-1, "Accounting by Insurance Enterprises for Deferred Acquisition Costs in Connection with Modifications or Exchanges of Insurance Contracts." SOP 05-1 provides guidance on accounting for deferred acquisition costs on internal replacements of insurance and investment contracts other than those specifically described in FASB Statement No. 97, "Accounting and Reporting by Insurance Enterprises for Certain Long-Duration Contracts and for Realized Gains and Losses from the Sale of Investments." The SOP defines an internal replacement as a modification in product benefits, features, rights, or coverage that occurs by the exchange of a contract for a new contract, or by amendment, endorsement, or rider to a contract, or by the election of a feature or

1. Summary of Significant Accounting Policies

Continued

coverage within a contract. The effective date of the implementation guidance is January 1, 2007. AIG is currently assessing the effect of implementing this guidance.

On February 16, 2006, the FASB issued FAS No. 155, "Accounting for Certain Hybrid Financial Instruments" (FAS 155), an amendment of FAS 140 and FAS 133. FAS 155 permits the Company to elect to measure any hybrid financial instrument at fair value (with changes in fair value recognized in earnings) if the hybrid instrument contains an embedded derivative that would otherwise be required to be bifurcated and accounted for separately under FAS 133. The election to measure the hybrid instrument at fair value is made on an instrument-by-instrument basis and is irrevocable. FAS 155 will be effective for all instruments acquired, issued, or subject to a remeasurement event occurring after the beginning of the AIG's fiscal year that begins after September 15, 2006, with earlier adoption permitted as of the beginning of 2006, provided that financial statements for any interim period of that fiscal year have not been issued. AIG has not yet decided whether it will early adopt FAS 155 effective January 1, 2006, and is assessing the effect of this change in accounting.

(hh) Restatements: AIG has completed two restatements of its financial statements (the Restatements). In connection with the first restatement (the First Restatement) included in the Annual Report on Form 10-K for the year ended December 31, 2004 filed on May 31, 2005, AIG restated its consolidated financial statements and financial statement schedules for the years ended December 31, 2003, 2002, 2001 and 2000, the quarters ended March 31, June 30 and September 30, 2004 and 2003 and the quarter ended December 31, 2003. In the second restatement (the Second Restatement) included in the Annual Report on Form 10-K/A for the year ended December 31, 2004 filed on March 16, 2006, AIG restated its consolidated financial statements and financial statement schedules for the years ended December 31, 2004, 2003 and 2002, along with 2001 and 2000 for purposes of preparation of the Consolidated Financial Data for 2001 and 2000, the quarterly financial information for 2004 and 2003 and the first three quarters of 2005. See Note 22 herein. AIG, however, did not amend its quarterly report on Form 10-Q for the quarter ended September 30, 2005 because the adjustments to the financial statements included therein were not material to those financial statements. The consolidated financial statements included in this Annual Report on Form 10-K reflect the Restatements.

2. Segment Information

In 2003 and prior years, AIG's operations were conducted by its subsidiaries principally through four operating segments: General Insurance, Life Insurance, Financial Services and Retirement Services & Asset Management. Beginning with the first quarter of 2004, AIG reports Retirement Services results in the same segment as Life Insurance, reflecting the convergence of protective financial and retirement products and AIG's current management of these operations. Information for years prior to 2004 included herein has been reclassified to show AIG's results of operations and financial position on a comparable basis with the 2004 presentation. These segments and their respective operations are as follows:

General Insurance: AIG's General Insurance subsidiaries are multiple line companies writing substantially all lines of property and casualty insurance both domestically and abroad. AIG's principal General Insurance operations are as follows:

DBG writes substantially all classes of business insurance in the U.S. and Canada, accepting such business mainly from insurance brokers.

Transatlantic Holdings, Inc. (Transatlantic) subsidiaries offer reinsurance capacity on both a treaty and facultative basis both in the U.S. and abroad. Transatlantic structures programs for a full range of property and casualty products with an emphasis on specialty risks.

AIG's Personal Lines operations provide automobile insurance through AIG Direct, the mass marketing operation of AIG, Agency Auto Division and 21st Century Insurance Group (21st Century), as well as a broad range of coverages for high net-worth individuals through the AIG Private Client Group.

Mortgage Guaranty operations provide guaranty insurance primarily on conventional first mortgage loans on single family dwellings and condominiums.

AIG's Foreign General Insurance group accepts risks primarily underwritten through American International Underwriters (AIU), a marketing unit consisting of wholly owned agencies and insurance companies. The Foreign General Insurance group also includes business written by AIG's foreign-based insurance subsidiaries. The Foreign General Insurance group uses various marketing methods to write both business and consumer lines insurance with certain refinements for local laws, customs and needs. AIU operates in Asia, the Pacific Rim, the United Kingdom, Europe, Africa, the Middle East and Latin America.

Life Insurance & Retirement Services: AIG's Life Insurance & Retirement Services subsidiaries offer a wide range of insurance and retirement savings products both domestically and abroad. Insurance-oriented products consist of individual and group life, payout annuities, endowment and accident and health policies. Retirement savings products consist of fixed and variable annuities.

AIG's principal overseas Life Insurance & Retirement Services operations are American Life Insurance Company (ALICO), American International Assurance Company, Limited, together with American International Assurance Company (Bermuda) Limited (AIA), Nan Shan Life Insurance Company, Ltd. (Nan Shan), The Philippine American Life and General Insurance Company (PhilamLife), AIG Edison Life Insurance Company (AIG Edison Life) and AIG Star Life Insurance Co. Ltd. (AIG Star Life).

AIG's principal domestic Life Insurance & Retirement Services operations are American General Life Insurance Company (AG Life), The United States Life Insurance Company in the City of New York (USLIFE), American

2. Segment Information

Continued

General Life and Accident Insurance Company (AGLA), AIG Annuity Insurance Company (AIG Annuity), The Variable Annuity Life Insurance Company (VALIC) and AIG Retirement Services, Inc (AIG SunAmerica).

AIRCO acts as an internal reinsurance company for AIG's foreign life operations.

Financial Services: AIG's Financial Services subsidiaries engage in diversified financial products and services including aircraft and equipment leasing, capital markets transactions, consumer finance and insurance premium financing.

AIG's Aircraft Finance operations represent the operations of ILFC, which generates its revenues primarily from leasing new and used commercial jet aircraft to domestic and foreign airlines. Revenues also result from the remarketing of commercial jets for its own account, for airlines and for financial institutions.

AIG's Capital Markets operations are conducted through AIGFP. As Capital Markets is a transaction-oriented operation, current and past revenues and operating results may not provide a basis for predicting future performance. Also, AIG's Capital Markets operations may be adversely affected by the downgrades in AIG's credit ratings.

AIG's Capital Markets operations derive substantially all their revenues from hedged financial positions entered in connection with counterparty transactions rather than from speculative transactions. These subsidiaries participate in the derivatives and financial transactions dealer markets conducting, primarily as principal, an interest rate, currency, equity, commodity, energy and credit products business.

Consumer Finance operations include AGF as well as AIGCFG. AGF and AIGCFG provide a wide variety of consumer finance products, including non-conforming real estate mortgages, consumer loans, retail sales finance and credit-related insurance to customers both domestically and overseas, particularly in emerging markets.

Asset Management: AIG's Asset Management operations comprise a wide variety of investment-related services and investment products including institutional and retail asset management, broker dealer services and spread-based investment business from the sale of guaranteed investment contracts, also known as funding agreements (GICs). Such products and services are offered to individuals and institutions both domestically and overseas.

(a) The following table summarizes the operations by major operating segment for the years ended December 31, 2005, 2004 and 2003:

	Operating Segments							
(in millions)	General Insurance	Life Insurance & Retirement Services	Financial Services	Asset Management	Other*(a)*	Total	Reclassifications and Eliminations	Consolidated
2005								
Revenues[b]	**$ 45,174**	**$ 47,316**	**$ 10,525**	**$ 5,325**	**$ 565**	**$ 108,905**	**$ –**	**$ 108,905**
Interest expense	**7**	**83**	**5,279**	**11**	**293**	**5,673**	**–**	**5,673**
Operating income (loss) before minority interest	**2,315**	**8,844**	**4,276**	**2,253**	**(2,475)[c]**	**15,213**	**–**	**15,213**
Income taxes (benefits)	**140**	**2,176**	**1,366**	**718**	**(142)**	**4,258**	**–**	**4,258**
Depreciation expense	**273**	**268**	**1,447**	**43**	**169**	**2,200**	**–**	**2,200**
Capital expenditures	**417**	**590**	**6,300**	**25**	**194**	**7,526**	**–**	**7,526**
Identifiable assets	**150,667**	**480,622**	**166,488**	**81,080**	**93,154**	**972,011**	**(118,641)**	**853,370**
2004								
Revenues[b]	$ 41,961	$ 43,400	$ 7,495	$ 4,714	$ 96	$ 97,666	$ –	$ 97,666
Interest expense	9	63	4,041	8	306	4,427	–	4,427
Operating income (loss) before minority interest	3,177	7,923	2,180	2,125	(560)	14,845	–	14,845
Income taxes (benefits)	616	2,526	654	753	(142)	4,407	–	4,407
Depreciation expense	251	262	1,366	19	137	2,035	–	2,035
Capital expenditures	350	480	4,481	11	207	5,529	–	5,529
Identifiable assets	131,658	447,841	165,995	80,075	79,890	905,459	(104,314)	801,145
2003								
Revenues[b]	$ 33,833	$ 36,678	$ 6,242	$ 3,651	$ (983)	$ 79,421	$ –	$ 79,421
Interest expense	4	68	3,817	8	322	4,219	–	4,219
Operating income (loss) before minority interest	4,502	6,807	1,182	1,316	(1,900)	11,907	–	11,907
Income taxes (benefits)	1,146	2,229	287	465	(571)	3,556	–	3,556
Depreciation expense	204	244	1,261	15	137	1,861	–	1,861
Capital expenditures	284	483	5,461	19	239	6,486	–	6,486
Identifiable assets	117,511	372,126	141,667	64,047	69,988	765,339	(89,737)	675,602

(a) Includes AIG Parent and other operations which are not required to be reported separately.

(b) Represents the sum of General Insurance net premiums earned, Life Insurance & Retirement Services GAAP premiums, net investment income, Financial Services interest, lease and finance charges, Asset Management advisory and management fees and net investment income from guaranteed investment contracts, and realized capital gains (losses).

(c) Includes settlement costs of $1.64 billion as described in Note 12(i).

2. Segment Information

Continued

(b) The following table summarizes AIG's General Insurance operations by major internal reporting unit for the years ended December 31, 2005, 2004 and 2003:

	General Insurance							
(in millions)	Domestic Brokerage Group	Transatlantic	Personal Lines	Mortgage Guaranty	Foreign General	Total Reportable Segment	Reclassifications and Eliminations	Total General Insurance
2005								
Revenues[a]	**$ 25,206**	**$ 3,766**	**$ 4,848**	**$ 655**	**$ 10,684**	**$ 45,159**	**$ 15**	**$ 45,174**
Losses & loss expenses incurred	**21,328**	**2,877**	**3,566**	**139**	**5,181**	**33,091**	**–**	**33,091**
Underwriting expenses	**4,524**	**928**	**1,087**	**153**	**3,076**	**9,768**	**–**	**9,768**
Underwriting profit (loss)[b][c][d][e]	**(3,250)**[f][g]	**(420)**	**(19)**	**241**	**1,398**[h]	**(2,050)**	**–**	**(2,050)**
Operating income (loss)[c]	**(646)**[f][g]	**(39)**	**195**	**363**	**2,427**	**2,300**	**15**	**2,315**
Depreciation expense	**114**	**2**	**48**	**4**	**105**	**273**	**–**	**273**
Capital expenditures	**119**	**2**	**94**	**6**	**196**	**417**	**–**	**417**
Identifiable assets	**95,829**	**12,365**	**5,245**	**3,165**	**39,044**	**155,648**	**(4,981)**	**150,667**
2004								
Revenues[a]	$23,332	$ 3,990	$4,488	$ 660	$ 9,473	$ 41,943	$ 18	$ 41,961
Losses & loss expenses incurred	18,808	2,755	3,211	142	5,441	30,357	–	30,357
Underwriting expenses	3,747	953	920	119	2,688	8,427	–	8,427
Underwriting profit (loss)[b][c][d]	(1,340)	(47)	160	278	702[h]	(247)	–	(247)
Operating income[c]	777	282	357	399	1,344	3,159	18	3,177
Depreciation expense	122	3	29	3	94	251	–	251
Capital expenditures	115	2	92	7	134	350	–	350
Identifiable assets	81,754	10,605	5,159	2,826	36,055	136,399	(4,741)	131,658
2003								
Revenues[a]	$18,091	$ 3,452	$3,850	$ 683	$ 7,787	$ 33,863	$ (30)	$ 33,833
Losses & loss expenses incurred	13,711	2,233	2,789	110	4,029	22,872	–	22,872
Underwriting expenses	2,606	829	706	122	2,196	6,459	–	6,459
Underwriting profit[b][c][d]	387	109	183	264	1,032[h]	1,975	–	1,975
Operating income[c]	1,774	390	355	451	1,562	4,532	(30)	4,502
Depreciation expense	97	3	19	3	82	204	–	204
Capital expenditures	83	2	45	3	151	284	–	284
Identifiable assets	73,516	8,708	4,958	2,879	31,615	121,676	(4,165)	117,511

(a) Represents the sum of General Insurance net premiums earned, net investment income and realized capital gains (losses).
(b) Underwriting profit (loss) is a GAAP measure that represents statutory underwriting profit or loss adjusted primarily for changes in deferred policy acquisition costs.
(c) Catastrophe related losses for 2005, 2004 and 2003 by reporting unit were:

(in millions)	**2005**		2004	2003
Reporting Unit	Insurance Related Losses	Net Reinstatement Premium Cost	Insurance Related Losses	Insurance Related Losses
DBG	**$1,747**	**$122**	$ 582	$48
Transatlantic	**463**	**45**	215	4
Personal Lines	**112**	**2**	25	5
Mortgage Guaranty	**10**	**–**	–	–
Foreign General	**293**	**94**	232	26
Total	**$2,625**	**$263**	$1,054	$83

(d) For Foreign General, includes the results of wholly owned AIU agencies.
(e) Includes the fourth quarter 2005 increase in net reserves of approximately $1.8 billion.
(f) Includes $197 million of additional losses incurred resulting from increased labor and material costs related to the 2004 Florida hurricanes.
(g) Includes $291 million of expenses related to changes in estimates for uncollectible reinsurance and other premium balances, and $100 million of accrued expenses in connection with certain workers compensation insurance policies written between 1985 and 1996.
(h) Income statement accounts expressed in non-functional currencies are translated into U.S. dollars using average exchange rates.

2. Segment Information

Continued

(c) The following table summarizes AIG's Life Insurance & Retirement Services operations by major internal reporting unit for the years ended December 31, 2005, 2004 and 2003:

	Life Insurance & Retirement Services							
(in millions)	ALICO/ AIG Star Life/ AIG Edison Life[(a)]	AIA, AIRCO and Nan Shan[(b)]	AGLA and AG Life[(c)]	VALIC/ AIG Annuity/ AIG SunAmerica[(d)]	Philamlife and Other	Total Reportable Segment	Reclassifications and Eliminations	Total Life Insurance & Retirement Services
2005								
Revenues[(e)]	**$ 15,233**	**$ 15,499**	**$ 9,215**	**$ 6,826**	**$ 543**	**$ 47,316**	**$ –**	**$ 47,316**
Operating income	**2,956**	**2,217**	**1,495**	**2,104**	**72**	**8,844**	**–**	**8,844**
Depreciation expense	**88**	**77**	**65**	**31**	**7**	**268**	**–**	**268**
Capital expenditures	**153**	**338**	**71**	**26**	**2**	**590**	**–**	**590**
Identifiable assets	**113,422**	**85,715**	**99,597**	**185,383**	**4,166**	**488,283**	**(7,661)**	**480,622**
2004								
Revenues[(e)]	$ 12,177	$15,450	$ 8,715	$ 6,562	$ 496	$ 43,400	$ –	$ 43,400
Operating income	2,393	2,371	1,023	2,052	84	7,923	–	7,923
Depreciation expense	101	55	62	37	7	262	–	262
Capital expenditures	308	93	47	29	3	480	–	480
Identifiable assets	102,808	74,647	91,538	183,092	2,630	454,715	(6,874)	447,841
2003								
Revenues[(e)]	$ 8,958	$13,151	$ 8,297	$ 5,822	$ 450	$ 36,678	$ –	$ 36,678
Operating income	2,187	1,766	1,233	1,532	89	6,807	–	6,807
Depreciation expense	77	56	68	36	7	244	–	244
Capital expenditures	281	51	91	58	2	483	–	483
Identifiable assets	79,648	61,426	84,094	151,672	2,523	379,363	(7,237)	372,126

(a) Reflects acquisition of AIG Edison Life in August 2003. Revenues and operating income include realized capital gains (losses) of $(74) million, $(152) million and $319 million for 2005, 2004 and 2003, respectively. The effect of FAS 133 and the application of FAS 52 included in realized capital gains (losses) are $(339) million, $(300) million and $226 million for 2005, 2004 and 2003, respectively.

(b) Revenues in 2004 include approximately $640 million of single premium from a reinsurance transaction involving terminal funding pension business, which is offset by a similar increase in benefit reserves. Revenues and operating income include realized capital gains (losses) of $144 million, $519 million and $168 million for 2005, 2004 and 2003, respectively. The effect of FAS 133 and the application of FAS 52 included in realized capital gains (losses) are $(162) million, $166 million and $(167) million for 2005, 2004 and 2003, respectively.

(c) Includes the life operations of AIG Life Insurance Company and American International Life Assurance Company of New York. 2004 includes a $178 million charge related to a workers compensation quota share reinsurance agreement with Superior National Insurance Company. See Note 12(h) herein for additional information. In addition, in 2004, as part of the business review of Group life/health, approximately $68 million was incurred for reserve strengthening and allowances for receivables. Revenues and operating income include realized capital gains (losses) of $35 million, $(120) million and $(37) million for 2005, 2004 and 2003, respectively. The effect of FAS 133 and the application of FAS 52 included in realized capital gains (losses) are $73 million, $8 million and $24 million for 2005, 2004 and 2003, respectively.

(d) "AIG SunAmerica" represents the annuity operations of AIG SunAmerica Life Assurance Company, as well as those of First SunAmerica Life Insurance Company and SunAmerica Life Insurance Company. Revenues and operating income include realized capital gains (losses) of $(337) million, $(209) million and $(209) million for 2005, 2004 and 2003, respectively. The effect of FAS 133 and the application of FAS 52 included in realized capital gains (losses) are $(10) million, $(14) million and $(5) million for 2005, 2004 and 2003, respectively.

(e) Represents the sum of Life Insurance & Retirement Services GAAP premiums, net investment income and realized capital gains (losses).

2. Segment Information

Continued

(d) The following table summarizes AIG's Financial Services operations by major internal reporting unit for the years ended December 31, 2005, 2004 and 2003:

	Financial Services						
(in millions)	Aircraft Finance	Capital Markets[a]	Consumer Finance	Other	Total Reportable Segment	Reclassifications and Eliminations	Total Financial Services
2005							
Revenues[b][c]	**$ 3,578**	**$ 3,260**	**$ 3,613**	**$ 387**	**$ 10,838**	**$ (313)**	**$ 10,525**
Interest expense[c]	**1,125**	**3,033**	**1,005**	**316**	**5,479**	**(200)**	**5,279**
Operating income[c]	**679**	**2,661**	**901[d]**	**60**	**4,301**	**(25)**	**4,276**
Depreciation expense	**1,384**	**20**	**38**	**5**	**1,447**	**—**	**1,447**
Capital expenditures	**6,193**	**3**	**54**	**50**	**6,300**	**—**	**6,300**
Identifiable assets	**37,515**	**90,090**	**30,704**	**14,872**	**173,181**	**(6,693)**	**166,488**
2004							
Revenues[b][c]	$ 3,136	$ 1,278	$ 2,978	$ 835	$ 8,227	$ (732)	$ 7,495
Interest expense[c]	993	2,300	705	144	4,142	(101)	4,041
Operating income[c]	642	662	808	90	2,202	(22)	2,180
Depreciation expense	1,273	42	33	18	1,366	–	1,366
Capital expenditures	4,400	29	35	17	4,481	–	4,481
Identifiable assets	33,997	98,303	26,560	13,985	172,845	(6,850)	165,995
2003							
Revenues[b][c]	$ 2,897	$ 595	$ 2,642	$ 641	$ 6,775	$ (533)	$ 6,242
Interest expense[c]	895	2,272	619	132	3,918	(101)	3,817
Operating income (loss)[c]	672	(188)	623	80	1,187	(5)	1,182
Depreciation expense	1,139	51	34	37	1,261	–	1,261
Capital expenditures	5,362	42	29	28	5,461	–	5,461
Identifiable assets	31,534	82,270	20,571	11,742	146,117	(4,450)	141,667

(a) Certain transactions entered into by AIGFP generate tax credits and benefits which are shown in the income tax line on the consolidated statement of income. Thus, this source of income is not reflected in the Revenue and Operating Income categories in the above table. The amount of such tax credits and benefits for the years ended December 31, 2005, 2004, and 2003 are $67 million, $107 million, and $123 million, respectively.

(b) Represents primarily the sum of ILFC aircraft lease rentals, AIGFP hedged financial positions entered into in connection with counterparty transactions and finance charges from consumer finance operations.

(c) Includes the effect of hedging activities that do not qualify for hedge accounting treatment under FAS 133, including the related foreign exchange gains and losses. For 2005, 2004 and 2003, the effect was $(34) million, $(27) million and $49 million, respectively, in operating income for Aircraft Finance and $2.01 billion, $(122) million and $(1.01) billion in both revenues and operating income for Capital Markets.

(d) Includes $62 million of catastrophe related losses.

2. Segment Information

Continued

(e) A substantial portion of AIG's operations is conducted in countries other than the United States and Canada. The following table summarizes AIG's operations by major geographic segment. Allocations have been made on the basis of the location of operations and assets.

	Geographic Segments			
(in millions)	Domestic[a]	Far East	Other Foreign	Consolidated
2005				
Revenues[b]	**$ 59,858**	**$ 32,036**	**$ 17,011**	**$ 108,905**
Real estate and other fixed assets, net of accumulated depreciation	**3,840**	**2,669**	**937**	**7,446**
Flight equipment primarily under operating leases, net of accumulated depreciation[c]	**36,245**	**–**	**–**	**36,245**
2004				
Revenues[b]	$53,827	$27,761	$16,078	$ 97,666
Real estate and other fixed assets, net of accumulated depreciation	2,341	2,834	1,017	6,192
Flight equipment primarily under operating leases, net of accumulated depreciation[c]	32,130	–	–	32,130
2003				
Revenues[b]	$43,221	$22,787	$13,413	$ 79,421
Real estate and other fixed assets, net of accumulated depreciation	2,539	2,518	909	5,966
Flight equipment primarily under operating leases, net of accumulated depreciation[c]	29,870	–	–	29,870

(a) Including revenues from General Insurance operations in Canada of $638 million, $549 million, and $433 million in 2005, 2004, and 2003, respectively.

(b) Represents the sum of General Insurance net premiums earned, Life Insurance & Retirement Services GAAP premiums, net investment income, Financial Services interest, lease and finance charges, Asset Management advisory and management fees and net investment income with respect to guaranteed investment contracts, and realized capital gains (losses).

(c) Approximately 90 percent of ILFC's fleet is operated by foreign airlines.

3. Federal Income Taxes

(a) AIG and its eligible domestic subsidiaries file a consolidated U.S. Federal income tax return. The AGC group of life insurance companies also files a consolidated U.S. Federal income tax return and will not be included in AIG's consolidated federal income tax return until 2007. Commencing with taxable year 2004, the AIG SunAmerica group of life insurance companies is included in AIG's consolidated tax return. Other U.S. entities included in the consolidated financial statements also file separate U.S. Federal income tax returns. Subsidiaries operating outside the U.S. are taxed, and income tax expense is recorded, based on applicable U.S. and foreign statutes.

U.S. federal income taxes have not been provided on $750 million of undistributed earnings of certain U.S. subsidiaries that are not included in the consolidated AIG U.S. Federal income tax return because tax planning strategies are available, and would be utilized, to eliminate the tax liability related to these earnings. U.S. federal income taxes have not been provided on the undistributed earnings of certain non-U.S. subsidiaries to the extent that such earnings have been reinvested abroad for an indefinite period of time. At December 31, 2005, the cumulative amount of undistributed earnings in these subsidiaries approximated $13.8 billion.

A component of life insurance surplus accumulated prior to 1984 is not taxable unless it exceeds certain statutory limitations or is distributed to shareholders. This surplus, accumulated in policyholder surplus accounts, totaled approximately $253 million at December 31, 2005. AIG has not made any provision in the accompanying financial statements for taxation of this amount as management has no intention of making any taxable distributions from this surplus. During 2004, the American Jobs Creation Act amended federal income tax law to permit life insurance companies to distribute amounts from policyholders' surplus accounts in 2005 and 2006 without incurring federal income tax on the distributions. During 2005, AIG reduced its policyholders' surplus accounts to $253 million and expects to eliminate its exposure to federal income taxation on the remaining balance in 2006.

Revenue Agent's Reports proposing to assess additional taxes for the years 1991-1996 and 1997-1999 have been issued to AIG. Apart from some relatively minor issues, years prior to 1991 are closed. Letters of Protest contesting the proposed assessments for 1991-1996 and 1997-1999 have been filed with the Internal Revenue Service (IRS).

In addition, Revenue Agent's Reports proposing to assess additional taxes for the years ended September 30, 1993-1994, 1995-1996, and September 30, 1997-December 31, 1998 have been issued to AIG SunAmerica. Such proposed assessments relate to years prior to AIG's acquisition of SunAmerica, Inc. Letters of Protest contesting the proposed assessments have been filed with the IRS. SunAmerica Life Insurance Company (SunAmerica Life) has also received a proposed assessment, and has filed a protest, for the year ended December 31, 1999. It is management's belief that there are substantial arguments in support of the positions taken by AIG, SunAmerica and SunAmerica Life in their Letters of Protest. Although the final outcome of any issues raised in connection with these examinations is uncertain, AIG believes that any tax obliga-

3. Federal Income Taxes

Continued

tion, including interest thereon, would not be significant to AIG's financial condition, results of operations or liquidity. American General Corporation's (AGC) tax years through 1999 have been audited and settled with the IRS.

(b) The pretax components of domestic and foreign income reflect the locations in which such pretax income was generated. The pretax domestic and foreign income was as follows for the years ended December 31, 2005, 2004 and 2003:

(in millions)	**2005**	2004	2003
Domestic	**$ 6,103**	$ 6,069	$ 4,177
Foreign	**9,110**	8,776	7,730
Total	**$ 15,213**	$14,845	$11,907

(c) The U.S. Federal income tax rate is 35 percent for 2005, 2004 and 2003. Actual tax expense on income differs from the "expected" amount computed by applying the Federal income tax rate because of the following:

	2005		2004		2003	
Years Ended December 31, *(dollars in millions)*	Amount	Percent of Pretax Income	Amount	Percent of Pretax Income	Amount	Percent of Pretax Income
"Expected" tax expense	**$5,325**	**35.0%**	$5,197	35.0%	$4,167	35.0%
Adjustments:						
Tax exempt interest	**(566)**	**(3.7)**	(440)	(2.9)	(329)	(2.8)
Dividends received deduction	**(117)**	**(0.8)**	(83)	(0.6)	(83)	(0.7)
State income taxes	**86**	**0.6**	23	0.2	12	0.1
Effect of foreign operations[(a)]	**(253)**	**(1.7)**	(11)	(0.1)	(95)	(0.8)
Synthetic fuel tax credits	**(274)**	**(1.8)**	(264)	(1.8)	(278)	(2.3)
Affordable housing tax credits	**(22)**	**(0.1)**	(46)	(0.3)	(24)	(0.2)
Nondeductible compensation	**83**	**0.5**	20	0.1	96	0.8
Penalties	**76**	**0.5**	28	0.2	–	–
Other	**(80)**	**(0.5)**	(17)	(0.1)	90	0.8
Actual tax expense	**$4,258**	**28.0%**	$4,407	29.7%	$3,556	29.9%
Foreign and domestic components of actual tax expense:						
Foreign[(b)]:						
Current	**$ 974**		$1,104		$ 882	
Deferred	**426**		561		708	
Domestic[(b)]:						
Current	**1,595**		1,489		1,859	
Deferred	**1,263**		1,253		107	
Total	**$4,258**		$4,407		$3,556	

(a) In 2005 and 2004, it was determined that the earnings of certain foreign subsidiaries are expected to be repatriated to the U.S., and, accordingly, the undistributed earnings of these subsidiaries are no longer considered indefinitely reinvested abroad. As a consequence of this determination, U.S. deferred taxes have been provided for the undistributed earnings of these foreign subsidiaries.

(b) Foreign tax expense reflects the expense resulting from local tax regulation. Domestic tax expense includes U.S. taxes incurred on foreign income.

(d) The components of the net deferred tax liability as of December 31, 2005 and 2004 were as follows:

(in millions)	**2005**	2004
Deferred tax assets*:		
Loss reserve discount	**$ 3,061**	$2,400
Unearned premium reserve reduction	**1,042**	1,074
Loan loss and other reserves	**419**	394
Investment in foreign subsidiaries and joint ventures	**349**	542
Adjustment to life policy reserves	**2,351**	3,458
Accruals not currently deductible, cumulative translation adjustment and other	**1,189**	1,031
Deferred tax liabilities:		
Deferred policy acquisition costs	**7,573**	7,956
Depreciation of flight equipment	**3,196**	2,766
Unrealized appreciation of investments	**4,025**	4,668
Other	**224**	97
Net deferred tax liability	**$ 6,607**	$6,588

* *A valuation allowance in the amount of $280 million related to the Connecticut net deferred tax asset at December 31, 2005 (including net operating losses that expire between 2020 through 2025) has been provided because it is remote that such amount will be realized. In addition, AIG has a $192 million alternative minimum tax credit carryforward that does not expire.*

4. Deferred Policy Acquisition Costs

The following reflects the policy acquisition costs deferred for amortization against future income and the related amortization charged to income for general and life insurance & retirement services operations:

Years Ended December 31, *(in millions)*	2005	2004	2003
General Insurance operations:			
Balance at beginning of year	**$ 3,998**	$ 3,619	$ 3,072
Acquisition costs deferred	**7,480**	6,617	5,223
Amortization charged to Income	**(7,430)**	(6,238)	(4,676)
Balance at end of year	**$ 4,048**	$ 3,998	$ 3,619
Life Insurance & Retirement Services operations:			
Balance at beginning of year	**$25,819**	$22,375	$18,850
Value of business acquired	**–**	–	1,538*
Acquisition costs deferred	**6,777**	6,504	5,052
Amortization charged to Income	**(3,379)**	(3,551)	(2,778)
Change in net unrealized gains (losses) on securities	**1,127**	(219)	(813)
Increase (decrease) due to foreign exchange	**(1,144)**	710	526
Balance at end of year	**$29,200**	$25,819	$22,375
Total deferred policy acquisition costs	**$33,248**	$29,817	$25,994

* *Relates to the acquisition of AIG Edison Life in August 2003.*

Included in the above table is the value of business acquired (VOBA), an intangible asset recorded during purchase accounting, which is amortized in a manner similar to deferred acquisition costs. Amortization of VOBA was $291 million, $407 million and $326 million while the unamortized balance was $2.14 billion, $2.52 billion and $3.17 billion for 2005, 2004 and 2003, respectively. The percentage of the unamortized balance of VOBA at 2005 expected to be amortized for 2006 through 2011 by year is: 12.0 percent, 10.5 percent, 9.2 percent, 8.0 percent, and 6.7 percent, respectively, with 53.7 percent being amortized after five years. These projections are based on current estimates for investment, persistency, mortality, and morbidity assumptions. The DAC amortization charged to income includes the increase or decrease of amortization for FAS 97-related realized capital gains (losses), primarily in the domestic Retirement Services business. For 2005, 2004 and 2003, respectively, the rate of amortization expense has been decreased by $57 million, $44 million and $54 million.

5. Reinsurance

In the ordinary course of business, AIG's General and Life Insurance companies place reinsurance with other insurance companies in order to provide greater diversification of AIG's business and limit the potential for losses arising from large risks.

General Reinsurance: General reinsurance is effected under reinsurance treaties and by negotiation on individual risks. Certain of these reinsurance arrangements consist of excess of loss contracts which protect AIG against losses over stipulated amounts. Ceded premiums are considered prepaid reinsurance premiums and are amortized into income over the contract period in proportion to the protection received. Amounts recoverable from general reinsurers are estimated in a manner consistent with the claims liabilities associated with the reinsurance and presented as a component of reinsurance assets.

General Insurance premiums written and earned were comprised of the following:

Years Ended December 31, *(in millions)*	Written	Earned
2005		
Gross premiums	**$ 52,725**	**$ 51,715**
Ceded premiums	**(10,853)**	**(10,906)**
Net premiums	**$ 41,872**	**$ 40,809**
2004		
Gross premiums	$ 52,046	$ 50,203
Ceded premiums	(11,423)	(11,666)
Net premiums	$ 40,623	$ 38,537
2003		
Gross premiums	$ 46,938	$ 42,745
Ceded premiums	(11,907)	(11,439)
Net premiums	$ 35,031	$ 31,306

For the years ended December 31, 2005, 2004 and 2003, reinsurance recoveries, which reduced loss and loss expenses incurred, amounted to $20.71 billion, $12.14 billion and $10.09 billion, respectively.

Life Insurance: AIG Life Insurance companies generally limit exposure to loss on any single life. For ordinary insurance, AIG generally retains a maximum of approximately $1.7 million of coverage per individual life with respect to AIG's overseas life operations and $10 million of coverage per individual life with respect to AIG's domestic life operations. There are smaller retentions for other lines of business. Life reinsurance is effected principally under yearly renewable term treaties. The premiums with respect to these treaties are considered prepaid reinsurance premiums and are amortized into income over the

5. Reinsurance

Continued

contract period in proportion to the protection provided. Amounts recoverable from life reinsurers are estimated in a manner consistent with the assumptions used for the underlying policy benefits and are presented as a component of reinsurance assets.

Life Insurance & Retirement Services GAAP premiums were comprised of the following:

Years Ended December 31, *(in millions)*	2005	2004	2003
Gross GAAP premiums	**$ 30,717**	$29,202	$24,448
Ceded premiums	**(1,317)**	(1,114)	(952)
GAAP premiums	**$ 29,400**	$28,088	$23,496

Life Insurance recoveries, which reduced death and other benefits, approximated $770 million, $779 million and $651 million, respectively, for the years ended December 31, 2005, 2004 and 2003.

Life Insurance in force ceded to other insurance companies was as follows:

Years Ended December 31, *(in millions)*	2005	2004	2003
Life Insurance in force	**$ 365,082**	$344,036	$293,064

Life Insurance assumed represented 0.8 percent, 0.7 percent and 0.1 percent of gross Life Insurance in force at December 31, 2005, 2004 and 2003, respectively, and Life Insurance & Retirement Services GAAP premiums assumed represented 0.3 percent, 2.5 percent and 0.1 percent of gross GAAP premiums for the periods ended December 31, 2005, 2004 and 2003, respectively.

Supplemental information for gross loss and benefit reserves net of ceded reinsurance at December 31, 2005 and 2004 follows:

(in millions)	As Reported	Net of Reinsurance
2005		
Reserve for losses and loss expenses	**$ (77,169)**	**$ (57,476)**
Future policy benefits for life and accident and health insurance contracts	**(108,807)**	**(107,420)**
Reserve for unearned premiums	**(24,243)**	**(21,174)**
Reinsurance assets	**24,978**	**–**
2004		
Reserve for losses and loss expenses	$ (61,878)	$ (47,254)
Future policy benefits for life and accident and health insurance contracts	(104,740)	(103,348)
Reserve for unearned premiums	(23,400)	(20,278)
Reinsurance assets	19,613	–

AIRCO acts primarily as an internal reinsurance company for AIG's foreign life operations. This facilitates insurance risk management (retention, volatility, concentrations) and capital planning locally (branch and subsidiary). It also allows AIG to pool its insurance risks and purchase reinsurance more efficiently at a consolidated level, manage global counterparty risk and relationships and manage global life catastrophe risks.

AIG's domestic Life Insurance & Retirement Services operations utilize internal and third-party reinsurance relationships to manage insurance risks and to facilitate capital management strategies. Pools of highly-rated third-party reinsurers are utilized to manage net amounts at risk in excess of retention limits. AIG's domestic life insurance companies also cede excess, non-economic reserves carried on a statutory-basis only on certain term and universal life insurance policies and certain fixed annuities to an offshore affiliate.

AIG generally obtains letters of credit in order to obtain statutory recognition of these intercompany reinsurance transactions. For this purpose, AIG entered into a $2.5 billion syndicated letter of credit facility in December 2004. Letters of credit totaling $2.17 billion were outstanding as of December 31, 2004, and letters of credit for all $2.5 billion were outstanding as of December 31, 2005, all of which relate to life intercompany reinsurance transactions. The letter of credit facility has a ten-year term, but the facility can be reduced or terminated by the lenders beginning after seven years.

In November 2005, AIG entered into a revolving credit facility for an aggregate amount of $3 billion. The facility can be drawn in the form of letters of credit with terms of up to ten years. As of December 31, 2005 and as of the date hereof, $1.86 billion principal amount of letters of credit are outstanding under this facility, of which approximately $494 million relates to life intercompany reinsurance transactions. AIG also obtained approximately $212 million letters of credit on a bilateral basis.

Reinsurance Security: AIG's reinsurance arrangements do not relieve AIG from its direct obligation to its insureds. Thus, a credit exposure exists with respect to both general and life reinsurance ceded to the extent that any reinsurer is unable to meet the obligations assumed under the reinsurance agreements. AIG holds substantial collateral as security under related reinsurance agreements in the form of funds, securities, and/or letters of credit. A provision has been recorded for estimated unrecoverable reinsurance. AIG has been largely successful in prior recovery efforts.

AIG evaluates the financial condition of its reinsurers and establishes limits per reinsurer through AIG's Credit Risk Committee. AIG believes that no exposure to a single reinsurer represents an inappropriate concentration of risk to AIG, nor is AIG's business substantially dependent upon any reinsurance contract.

6. Reserve for Losses and Loss Expenses and Future Life Policy Benefits and Policyholders' Contract Deposits

(a) The following analysis provides a reconciliation of the activity in the reserve for losses and loss expenses:

Years Ended December 31, *(in millions)*	2005	2004	2003
At beginning of year:			
Reserve for losses and loss expenses	**$ 61,878**	$ 51,871	$ 46,674
Reinsurance recoverable	**(14,624)**	(15,643)	(17,327)
	47,254	36,228	29,347
Foreign exchange effect	**(628)**	524	580
Acquisitions	**–**	–	391[a]
Losses and loss expenses incurred:			
Current year	**28,426**	26,793	20,509
Prior years[b]	**4,665**[c]	3,564[d]	2,363
Total	**33,091**	30,357	22,872
Losses and loss expenses paid:			
Current year	**7,331**	7,692	6,187
Prior years	**14,910**	12,163	10,775
Total	**22,241**	19,855	16,962
At end of year:			
Net reserve for losses and loss expenses	**57,476**	47,254	36,228
Reinsurance recoverable	**19,693**	14,624	15,643
Total	**$ 77,169**	$ 61,878	$ 51,871

(a) Reflects the opening balances with respect to the GE U.S.-based auto and home insurance business acquired in 2003.
(b) Includes accretion of discount of $(15) million in 2005, including an increase of $375 million in the discount recorded in 2005; $377 million in 2004 and $296 million in 2003.
(c) Includes fourth quarter charge of $1.8 billion.
(d) Includes fourth quarter charge of $850 million attributable to the change in estimate for asbestos and environmental exposures.

(b) The analysis of the future policy benefits and policyholders' contract deposits liabilities at December 31, 2005 and 2004 follows:

(in millions)	2005	2004
Future policy benefits:		
Long duration contracts	**$105,490**	$101,584
Short duration contracts	**3,317**	3,156
Total	**$108,807**	$104,740
Policyholders' contract deposits:		
Annuities	**$142,057**	$130,524
Guaranteed investment contracts (GICs)	**39,705**	46,472
Corporate life products	**2,077**	2,042
Universal life	**18,682**	16,771
Variable products	**7,799**	5,960
Variable investment contracts	**8,373**	7,579
Other investment contracts	**8,334**	7,126
Total	**$227,027**	$216,474

(c) Long duration contract liabilities included in future policy benefits, as presented in the preceding table, result from life products. Short duration contract liabilities are primarily accident and health products. The liability for future life policy benefits has been established based upon the following assumptions:

(i) Interest rates (exclusive of immediate/terminal funding annuities), which vary by territory, year of issuance and products, range from 1.0 percent to 12.0 percent within the first 20 years. Interest rates on immediate/terminal funding annuities are at a maximum of 11.5 percent and grade to not greater than 6.0 percent.

(ii) Mortality and surrender rates are based upon actual experience by geographical area modified to allow for variations in policy form. The weighted average lapse rate, including surrenders, for individual and group life approximated 7.9 percent.

(iii) The portions of current and prior net income and of current unrealized appreciation of investments that can inure to the benefit of AIG are restricted in some cases by the insurance contracts and by the local insurance regulations of the countries in which the policies are in force.

(iv) Participating life business represented approximately 22 percent of the gross insurance in force at December 31, 2005 and 36 percent of gross GAAP premiums in 2005. The amount of annual dividends to be paid is determined locally by the boards of directors. Provisions for future dividend payments are computed by jurisdiction, reflecting local regulations.

(d) The liability for policyholders' contract deposits has been established based on the following assumptions:

(i) Interest rates credited on deferred annuities, which vary by territory and year of issuance, range from 1.0 percent to, including bonuses, 13.4 percent. Less than 1.0 percent of the liabilities are credited at a rate greater than 9.0 percent. Current declared interest rates are generally guaranteed to remain in effect for a period of one year though some are guaranteed for longer periods. Withdrawal charges generally range from zero percent to 14.0 percent grading to zero over a period of zero to 19 years.

(ii) Domestically, GICs have market value withdrawal provisions for any funds withdrawn other than benefit responsive payments. Interest rates credited generally range from 1.4 percent to 9.0 percent. The vast majority of these GICs mature within ten years. Overseas, interest rates credited on GICs generally range from 1.2 percent to 5.6 percent and maturities range from one to five years.

(iii) Interest rates on corporate life insurance products are guaranteed at 4.0 percent and the weighted average rate credited in 2005 was 5.4 percent.

(iv) The universal life funds have credited interest rates of 1.5 percent to 7.0 percent and guarantees ranging from 1.5 percent to 5.5 percent depending on the year of issue. Additionally, universal life funds are subject to surrender

6. Reserve for Losses and Loss Expenses and Future Life Policy Benefits and Policyholders' Contract Deposits

Continued

charges that amount to 11.3 percent of the aggregate fund balance grading to zero over a period not longer than 20 years.

(v) For variable products and investment contracts, policy values are expressed in terms of investment units. Each unit is linked to an asset portfolio. The value of a unit increases or decreases based on the value of the linked asset portfolio. The current liability at any time is the sum of the current unit value of all investment units plus any liability for guaranteed minimum death or withdrawal benefits. A portion of these liabilities are classified in the GIC product line for segment reporting purposes.

(e) Certain products are subject to experience adjustments. These include group life and group medical products, credit life contracts, accident and health insurance contracts/riders attached to life policies and, to a limited extent, reinsurance agreements with other direct insurers. Ultimate premiums from these contracts are estimated and recognized as revenue, and the unearned portions of the premiums are held as reserves. Experience adjustments vary according to the type of contract and the territory in which the policy is in force and are subject to local regulatory guidance.

7. Statutory Financial Data

Statutory surplus and net income for General Insurance and Life Insurance & Retirement Services operations in accordance with regulatory accounting practices were as follows:

Years Ended December 31, *(in millions)*	2005	2004	2003
Statutory surplus[(a)]:			
General Insurance	**$24,508**	$20,632	$20,462
Life Insurance & Retirement Services	**30,739**	28,609	25,501
Statutory net income[(a)(b)]:			
General Insurance	**1,713**	3,028[(c)]	2,911
Life Insurance & Retirement Services[(a)]	**4,762**	4,474	3,453

(a) Statutory surplus and net income with respect to foreign operations are reported as of their respective fiscal year ends.

(b) Includes realized capital gains and losses and taxes.

(c) Includes catastrophe losses, net of tax of $660 million.

AIG's insurance subsidiaries file financial statements prepared in accordance with statutory accounting practices prescribed or permitted by domestic and foreign insurance regulatory authorities. The differences between statutory financial statements and financial statements prepared in accordance with U.S. GAAP vary between domestic and foreign by jurisdiction. The principal differences are that statutory financial statements do not reflect deferred policy acquisition costs, some bond portfolios may be carried at amortized cost, assets and liabilities are presented net of reinsurance, policyholder liabilities are valued using more conservative assumptions and certain assets are non-admitted.

AIG also recently completed its 2005 unaudited statutory financial statements for all of its Domestic General Insurance subsidiaries, after reviewing and agreeing with the relevant state insurance regulators the statutory accounting treatment of various items. The state regulators have permitted the Domestic General Insurance companies to record a $724 million reduction to opening statutory surplus as of January 1, 2005 to reflect the effects of the Second Restatement.

Statutory capital of each company continued to exceed minimum company action level requirements following the adjustments, but AIG nonetheless contributed an additional $750 million of capital into American Home Assurance Company (American Home) effective September 30, 2005 and contributed a further $2.25 billion of capital in February 2006 for a total of approximately $3 billion of capital into Domestic General Insurance subsidiaries effective December 31, 2005.

8. Investment Information

(a) Statutory Deposits: Cash and securities with carrying values of $11.8 billion and $9.6 billion were deposited by AIG's insurance subsidiaries under requirements of regulatory authorities as of December 31, 2005 and 2004, respectively.

(b) Net Investment Income: An analysis of the net investment income from the General and Life Insurance & Retirement Services operations follows:

Years Ended December 31, *(in millions)*	2005	2004	2003
Fixed maturities	**$17,685**	$15,884	$13,710
Equity securities	**1,730**	621	484
Short-term investments	**494**	177	94
Interest on mortgage, policy and collateral loans	**1,177**	1,096	1,047
Other invested assets	**1,905**	1,444	898
Total investment income	**22,991**	19,222	16,233
Investment expenses	**826**	757	725
Net investment income	**$22,165**	$18,465	$15,508

8. Investment Information

Continued

(c) Investment Gains and Losses: The realized capital gains (losses) and increase (decrease) in unrealized appreciation of investments were as follows:

Years Ended December 31, *(in millions)*	2005	2004	2003
Realized capital gains (losses) on investments:			
Fixed maturities	**$ (108)**	$ 178	$ (222)
Equity securities	**588**	541	(495)
Other invested assets	**(139)**	(675)	275
Realized capital gains (losses)	**$ 341**	$ 44	$ (442)
Increase (decrease) in unrealized appreciation of investments:			
Fixed maturities	**$ (4,656)**	$1,436	$2,493
Equity securities	**850**	445	1,354
Other invested assets	**229**	(13)	312
Increase (decrease) in unrealized appreciation	**$ (3,577)**	$1,868	$4,159

The gross gains and gross losses realized on available for sale securities were as follows:

(in millions)	Gross Realized Gains	Gross Realized Losses
2005		
Bonds	**$ 1,586**	**$ 1,694**
Common stocks	**930**	**409**
Preferred stocks	**101**	**34**
Total	**$ 2,617**	**$ 2,137**
2004		
Bonds	$1,560	$1,382
Common stocks	774	379
Preferred stocks	173	27
Total	$2,507	$1,788
2003		
Bonds	$2,470	$2,692
Common stocks	465	827
Preferred stocks	139	272
Total	$3,074	$3,791

(d) Market Value of Fixed Maturities and Unrealized Appreciation of Investments: At December 31, 2005 and 2004, the balance of the unrealized appreciation of investments in equity securities (before applicable taxes) included gross gains of approximately $2.5 billion and $1.6 billion, and gross losses of approximately $257 million and $256 million, respectively.

The amortized cost and estimated market value of investments in fixed maturities held to maturity and carried at amortized cost at December 31, 2005 and December 31, 2004 follows:

(in millions)	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Market Value
2005				
Fixed maturities:				
Bonds – States *	**$ 21,528**	**$ 552**	**$ 33**	**$ 22,047**
Total	**$ 21,528**	**$ 552**	**$ 33**	**$ 22,047**
2004				
Fixed maturities:				
Bonds – States *	$18,294	$510	$13	$18,791
Total	$18,294	$510	$13	$18,791

* *Including municipalities and political subdivisions.*

The amortized cost and estimated market value of bonds available for sale and carried at market value at December 31, 2005 and 2004 were as follows:

(in millions)	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Market Value
2005				
Bonds:				
U.S. government[(a)]	**$ 7,848**	**$ 124**	**$ 94**	**$ 7,878**
States[(b)]	**49,116**	**853**	**315**	**49,654**
Foreign governments	**57,509**	**4,881**	**665**	**61,725**
All other corporate	**235,139**	**7,770**	**2,650**	**240,259**
Total bonds	**$ 349,612**	**$ 13,628**	**$ 3,724**	**$ 359,516**
2004				
Bonds:				
U.S. government[(a)]	$ 8,055	$ 156	$ 37	$ 8,174
States[(b)]	37,204	1,175	83	38,296
Foreign governments	64,374	3,715	446	67,643
All other corporate	220,205	11,089	1,008	230,286
Total bonds	$329,838	$16,135	$1,574	$344,399

(a) *Including U.S. government agencies and authorities.*

(b) *Including municipalities and political subdivisions.*

The amortized cost and estimated market values of fixed maturities available for sale at December 31, 2005, by contractual maturity, are shown below. Actual maturities may differ from contractual maturities because certain borrowers have the right to call or prepay certain obligations with or without call or prepayment penalties.

(in millions)	Amortized Cost	Estimated Market Value
Fixed maturities available for sale:		
Due in one year or less	$ 10,417	$ 10,991
Due after one year through five years	68,520	70,108
Due after five years through ten years	128,353	130,446
Due after ten years	142,322	147,971
Total available for sale	$349,612	$359,516

8. Investment Information

Continued

(e) Fixed Maturities Below Investment Grade: At December 31, 2005, fixed maturities held by AIG that were below investment grade or not rated totaled $20.54 billion.

(f) Non-Income Producing Invested Assets: At December 31, 2005, non-income producing invested assets were insignificant.

(g) Gross Unrealized Losses and Estimated Fair Values on Investments:

The following table summarizes the gross unrealized losses and cost basis on insurance and asset management investment securities, aggregated by major investment category and length of time that individual securities have been in a continuous unrealized loss position, at December 31, 2005 and December 31, 2004.

	Less than 12 Months		12 Months or More		Total	
(in millions)	Cost[a]	Unrealized Losses	Cost[a]	Unrealized Losses	Cost[a]	Unrealized Losses
2005						
Bonds[b]	**$121,631**	**$2,715**	**$21,160**	**$1,009**	**$142,791**	**$3,724**
Equity securities	**3,894**	**246**	**97**	**11**	**3,991**	**257**
Total	**$125,525**	**$2,961**	**$21,257**	**$1,020**	**$146,782**	**$3,981**
2004						
Bonds[b]	$51,901	$758	$14,204	$816	$66,105	$1,574
Equity securities	2,435	256	–	–	2,435	256
Total	$54,336	$1,014	$14,204	$816	$68,540	$1,830

(a) For bonds, represents amortized cost.

(b) Primarily relates to the "All other corporate" category.

As of December 31, 2005, AIG held 18,308 and 1,503 of individual bond and stock investments that were in an unrealized loss position, of which 3,074 individual investments were in an unrealized loss position continuously for 12 months or more.

AIG recorded impairment losses net of taxes of approximately $389 million, $369 million and $1.0 billion in 2005, 2004 and 2003, respectively. See Note 1(c) herein for AIG's other-than-temporary impairment accounting policy.

The carrying value, which approximates market value, of other invested assets as of December 31, 2005 was $27.3 billion, consisting primarily of hedge funds and limited partnerships. Of the $27.3 billion, approximately $5.1 billion relates to investments accounted for on an available for sale basis, with almost all of the remaining investments being accounted for on the equity method of accounting. All of the investments are subject to impairment testing (refer to Note 1(c) herein). Of the investments accounted for as available for sale, the gross unrealized loss as of December 31, 2005 was $440 million, the majority of which represents investments that have been in a continuous unrealized loss position for less than 12 months.

(h) Hedging of Securities Available for Sale: AIGFP follows a policy of minimizing interest rate, currency, commodity, and equity risks associated with securities available for sale by entering into internal offsetting positions, on a security by security basis within its derivatives portfolio, thereby offsetting a significant portion of the unrealized appreciation and depreciation. In addition, to reduce its credit risk, AIGFP has entered into credit derivative transactions with respect to $125 million of securities available for sale to economically hedge its credit risk. As previously discussed these economic offsets do not meet the hedge accounting requirements of FAS 133 and, as such, are recorded in other revenue in the Consolidated Statement of Income.

8. Investment Information

Continued

The amortized cost and estimated market value of securities available for sale at December 31, 2005 and 2004 were as follows:

(in millions)	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Market Value
2005				
Securities available for sale:				
Corporate and bank debt	**$ 24,496**	**$ 373**	**$ 780**	**$ 24,089**
Foreign government obligations	**825**	**5**	**31**	**799**
Asset-backed and collateralized	**3,522**	**202**	**42**	**3,682**
Preferred stocks	**6,194**	**13**	**3**	**6,204**
U.S. government obligations	**2,535**	**209**	**7**	**2,737**
Total	**$ 37,572**	**$ 802**	**$ 863**	**$ 37,511**
2004				
Securities available for sale:				
Corporate and bank debt	$15,067	$1,492	$ 81	$16,478
Foreign government obligations	1,239	134	2	1,371
Asset-backed and collateralized	4,132	424	1	4,555
Preferred stocks	6,651	38	23	6,666
U.S. government obligations	2,082	78	5	2,155
Total	$ 29,171	$ 2,166	$ 112	$ 31,225

The amortized cost and estimated market values of securities available for sale at December 31, 2005, by contractual maturity, are shown below. Actual maturities may differ from contractual maturities because certain borrowers have the right to call or prepay certain obligations with or without call or prepayment penalties.

(in millions)	Amortized Cost	Estimated Market Value
Securities available for sale:		
Due in one year or less	$ 5,156	$ 5,066
Due after one year through five years	4,582	4,505
Due after five years through ten years	3,794	3,646
Due after ten years	20,518	20,612
Asset-backed and collateralized	3,522	3,682
Total securities available for sale	$37,572	$37,511

An insignificant amount of securities available for sale were below investment grade at December 31, 2005.

(i) Finance Receivables: Finance receivables, net of unearned finance charges, were as follows:

Years Ended December 31, *(in millions)*	**2005**	2004
Real estate loans	**$20,407**	$17,069
Non-real estate loans	**3,831**	3,462
Credit card loans	**1,498**	1,226
Retail sales finance	**2,522**	2,254
Other loans	**407**	134
Total finance receivables	**28,665**	24,145
Allowance for losses	**(670)**	(571)
Finance receivables, net	**$27,995**	$23,574

9. Debt Outstanding

At December 31, 2005, AIG's net borrowings were $10.43 billion after reflecting amounts not guaranteed by AIG, amounts that were matched borrowings under AIGFP's obligations of guaranteed investment agreements (GIAs), matched notes and bonds payable, and liabilities connected to trust preferred stock. The following table summarizes borrowings outstanding at December 31, 2005:

(in millions)	
AIG's net borrowings	$ 10,425
Liabilities connected to trust preferred stock	1,391
Borrowings not guaranteed by AIG[(a)]	52,272
AIGFP:	
GIAs	20,811
Matched notes and bonds payable	24,950
Total debt	109,849
Commercial paper	(9,208)
Variable interest entity (VIE) debt[(b)]	(1,350)
Total debt, excluding commercial paper and VIE	$ 99,291

(a) Includes commercial paper not guaranteed by AIG.

(b) Represents borrowings of VIEs required to be consolidated under the provisions of FIN 46R.

9. Debt Outstanding

Continued

Total debt, excluding commercial paper of $9.2 billion and VIE debt of $1.35 billion, at December 31, 2005 is shown below with year of payment due in each of the next five years and thereafter.

(in millions)	Total	2006	2007	2008	2009	2010	Thereafter
Borrowings under obligations of GIAs	$20,811	$ 7,577	$ 1,899	$1,208	$ 579	$ 562	$ 8,986
Medium term notes:							
AGF[(a)]	17,736	2,992	3,944	2,346	1,866	2,425	4,163
ILFC[(a)]	4,689	1,134	1,088	1,306	700	447	14
AIG	112	23	65	–	–	–	24
Total	22,537	4,149	5,097	3,652	2,566	2,872	4,201
Notes and bonds payable:							
AIGFP	26,463	14,841	1,009	1,064	1,498	1,802	6,249
ILFC[(a)]:							
Notes	15,011	1,727	2,204	2,548	2,282	2,482	3,768
Export credit facility[(b)]	2,616	432	432	432	381	267	672
Bank financings	1,399	725	75	25	471	103	–
Total ILFC	19,026	2,884	2,711	3,005	3,134	2,852	4,440
AGF[(a)]	983	387	75	–	399	122	–
AIG:							
Term notes	3,000	–	–	500	–	500	2,000
Zero coupon convertible debt	1,060	–	–	–	–	–	1,060
SAI	435	–	100	73	–	–	262
Total AIG	4,495	–	100	573	–	500	3,322
AGC	797	–	–	–	–	–	797
Total	51,764	18,112	3,895	4,642	5,031	5,276	14,808
Loans and mortgages payable:							
AIGCFG[(a)]	864	864	–	–	–	–	–
AIG	814	600	121	–	–	–	93
AIG Finance (Hong Kong) Limited[(a)]	183	37	7	139	–	–	–
Total	1,861	1,501	128	139	–	–	93
Other subsidiaries[(a)]	927	165	5	52	–	–	705
Liabilities connected to trust preferred stock	1,391	–	–	–	–	–	1,391
Total	$99,291	$31,504	$11,024	$9,693	$8,176	$8,710	$30,184

(a) AIG does not guarantee these borrowings.

(b) Reflects future minimum payment for ILFC's borrowing under the Export Credit Facility.

9. Debt Outstanding

Continued

At December 31, 2005, long-term borrowings were $77.00 billion and short-term borrowings were $31.50 billion, excluding $1.35 billion with respect to debt of VIE's required to be consolidated under the provisions of FIN 46R. Long-term borrowings include commercial paper and exclude that portion of long-term debt maturing in less than one year.

(a) Commercial Paper:

At December 31, 2005, the commercial paper issued and outstanding was as follows:

(dollars in millions)	Net Book Value	Unamortized Discount and Accrued Interest	Face Amount	Weighted Average Interest Rate	Weighted Average Maturity in Days
ILFC	$2,615	$10	$2,625	4.17%	36
AGF	3,423	10	3,433	4.32	29
AIG Funding	2,694	7	2,701	4.32	32
AIGCCC – Taiwan*	476	2	478	2.08	63
Total	$9,208	$29	$9,237	—	—

* *Issued in Taiwan N.T. dollars at prevailing local interest rates.*

At December 31, 2005, AIG did not guarantee the commercial paper of any of its subsidiaries other than AIG Funding.

(b) Borrowings under Obligations of Guaranteed Investment Agreements: Borrowings under obligations of guaranteed investment agreements, which are guaranteed by AIG, are recorded at the amount outstanding under each contract. Obligations may be called at various times prior to maturity at the option of the counterparty. Interest rates on these borrowings are primarily fixed, vary by maturity, and range up to 9.8 percent.

Funds received from GIA borrowings are invested in a diversified portfolio of securities and derivative transactions. At December 31, 2005, the market value of securities pledged as collateral with respect to these obligations approximated $7.0 billion.

(c) Medium Term Notes Payable:

(i) Medium Term Notes Payable Issued by AGF: AGF's Medium Term Notes are unsecured obligations which generally may not be redeemed by AGF prior to maturity and bear interest at either fixed rates set by AGF at issuance or variable rates determined by reference to an interest rate or other formula.

As of December 31, 2005, notes aggregating $17.74 billion were outstanding with maturity dates ranging from 2006 to 2015 at interest rates ranging from 1.65 percent to 7.50 percent. To the extent deemed appropriate, AGF may enter into swap transactions to manage its effective borrowing rates with respect to these notes.

(ii) Medium Term Notes Payable Issued by ILFC: ILFC's Medium Term Notes are unsecured obligations which generally may not be redeemed by ILFC prior to maturity and bear interest at either fixed rates set by ILFC at issuance or variable rates determined by an interest rate or other formula.

As of December 31, 2005, notes aggregating $4.69 billion were outstanding with maturity dates from 2006 to 2013 at interest rates ranging from 2.25 percent to 6.98 percent. To the extent deemed appropriate, ILFC may enter into swap transactions to manage its effective borrowing rates with respect to these notes.

(iii) Medium Term Notes Payable Issued by AIG: AIG's Medium Term Notes are unsecured obligations which generally may not be redeemed by AIG prior to maturity and bear interest at either fixed rates set by AIG at issuance or variable rates determined by reference to an interest rate or other formula.

An analysis of AIG's Medium Term Notes for the year ended December 31, 2005 was as follows:

(in millions)	AIG	SAI	Total
Balance December 31, 2004	$ 565	$102	$ 667
Matured during year	(500)	(55)	(555)
Balance December 31, 2005	$ 65	$ 47	$ 112

The interest rate on AIG's Medium Term Note is 0.5 percent. To the extent deemed appropriate, AIG may enter into swap transactions to manage its effective borrowing rate with respect to this note.

At December 31, 2005, Medium Term Notes originally issued by SunAmerica, Inc. (SAI), which was merged into AIG on January 1, 1999, aggregating $47 million had maturity dates ranging from 2006 to 2026 at interest rates ranging from 6.43 percent to 7.05 percent.

During 2000, AIG issued $210 million of equity-linked Medium Term Notes due May 15, 2007. These notes accrue interest at the rate of 0.50 percent and the total return on these notes is linked to the appreciation in market value of AIG's common stock. The notes may be redeemed, at the option of AIG, as a whole but not in part, at any time on or after May 15, 2003. In conjunction with the issuance of these notes, AIG entered into a series of swap transactions which effectively converted its interest expense to a fixed rate of 7.17 percent until May 15, 2003 and a floating rate of LIBOR minus 0.50 percent thereafter and transferred the equity appreciation exposure to a third party for the life of the notes. AIG is exposed to credit risk with respect to the counterparties to these swap transactions. During 2003 and 2004, $45 million and $100 million of these notes were redeemed, respectively.

9. Debt Outstanding

Continued

(d) Notes and Bonds Payable:

(i) Notes and Bonds Payable Issued by AIGFP:

At December 31, 2005, AIGFP's notes and bonds outstanding, the proceeds of which are invested in a diversified portfolio of securities and derivative transactions, were as follows:

Range of Maturities *(dollars in millions)*	Currency	Range of Interest Rates	U.S. Dollar Carrying Value
2006-2039	U.S. dollar	0.09-8.60%	$ 18,514
2006-2010	United Kingdom pound	4.59-4.68	2,370
2006-2024	Euro	0.29-9.25	2,922
2005-2009	New Zealand dollar	4.17-8.35	1,185
2006-2035	Japanese yen	0.01-4.00	1,050
2006-2015	Australian dollar	1.14-4.89	104
2007-2024	Swiss francs	0.25-1.38	247
2007-2015	Other	1.03-3.72	71
Total			$ 26,463

AIGFP economically hedges its notes and bonds. AIG guarantees all of AIGFP's debt.

(ii) Notes and Bonds Payable Issued by ILFC: As of December 31, 2005, notes aggregating $15.01 billion were outstanding with maturity dates from 2006 to 2065 and interest rates ranging from 2.95 percent to 6.63 percent. Notes aggregating $3.52 billion are at floating interest rates and the remainder are at fixed rates.

The foreign exchange adjustment for the foreign currency denominated debt was $197 million at December 31, 2005 and $1.2 billion at December 31, 2004. ILFC had $13.13 billion of debt securities registered for public sale at December 31, 2005. As of December 31, 2005, $8.66 billion of debt securities were issued. In addition, ILFC has a Euro Medium Term Note Program for $7.0 billion, under which $4.98 billion in notes were sold through December 31, 2005. ILFC has substantially eliminated the currency exposure arising from foreign currency denominated notes by economically hedging that portion of the note exposure not already offset by Euro denominated operating lease payments, although such hedges do not qualify for hedge accounting treatment under FAS 133. Notes issued under this program are included in Notes and Bonds Payable.

ILFC had a $4.3 billion Export Credit Facility (ECA) for use in connection with the purchase of approximately 75 aircraft delivered through 2001. This facility was guaranteed by various European Export Credit Agencies. The interest rate varies from 5.75 percent to 5.90 percent on these amortizing ten-year borrowings depending on the delivery date of the aircraft. At December 31, 2005, ILFC had $1.2 billion outstanding under this facility. The debt is collateralized by a pledge of the shares of a subsidiary of ILFC, which holds title to the aircraft financed under the facility.

In May 2004, ILFC entered into a similarly structured ECA for up to a maximum of $2.64 billion for Airbus aircraft to be delivered through May 31, 2005. The facility has since been extended to include aircraft to be delivered through May 31, 2006. The facility becomes available as the various European Export Credit Agencies provide their guarantees for aircraft based on a six-month forward-looking calendar, and the interest rate is determined through a bid process. At December 31, 2005, ILFC had $1.4 billion outstanding under this facility. Borrowings with respect to these facilities are included in Notes and Bonds Payable.

In August 2004, ILFC received a commitment for an Ex-Im Bank comprehensive guarantee in the amount of $1.68 billion to support the financing of up to 30 new Boeing aircraft. The initial delivery period from September 1, 2004 through August 31, 2005 has been extended by ILFC to August 31, 2006. ILFC did not have any borrowings outstanding under this facility at December 31, 2005. From time to time, ILFC enters into various bank financings. As of December 31, 2005 the total funded amount was $1.4 billion. The financings mature through 2010. One tranche of one of the loans totaling $410 million was funded in Japanese yen and swapped to U.S. dollars.

In December of 2005, ILFC entered into two tranches of junior subordinated debt totaling $1.0 billion. Both mature on December 21, 2065, but each tranche has a different call option. The $600 million tranche has a call date of December 21, 2010 and the $400 million tranche has a call date of December 21, 2015. The note with the 2010 call date has a fixed interest rate of 5.90 percent for the first five years. The note with the 2015 call date has a fixed interest rate of 6.25 percent for the first ten years. Both tranches have interest rate adjustments if the call option is not exercised. The new interest rate is a floating quarterly reset rate based on the initial credit spread plus the highest of (i) 3 month LIBOR, (ii) 10-year constant maturity treasury and (iii) 30-year constant maturity treasury.

AIG does not guarantee any of the debt obligations of ILFC.

(iii) Notes and Bonds Payable Issued by AGF: As of December 31, 2005, AGF notes aggregating $983 million were outstanding with maturity dates ranging from 2006 to 2010 at interest rates ranging from 4.03 percent to 8.45 percent.

In 2005, AGF increased its shelf registration statement by $10.0 billion. AGF had $11.1 billion of debt securities registered and available for issuance at December 31, 2005. AGF uses the proceeds from the issuance of notes and bonds for the funding of its finance receivables.

AIG does not guarantee any of the debt obligations of AGF.

(iv) Notes, Bonds and Debentures Issued by AIG:

(A) Zero Coupon Convertible Senior Debentures: On November 9, 2001, AIG issued zero coupon convertible senior debentures in the aggregate principal amount at stated maturity of $1.52 billion. The notes were offered at 65.8 percent of principal amount at stated maturity, bear no interest unless contingent interest becomes payable under certain conditions and are due November 9, 2031. The net proceeds to AIG were $990 million. Commencing January 1, 2002, holders may

9. Debt Outstanding

Continued

convert the debentures into shares of AIG common stock at a conversion rate of 6.0627 shares per $1,000 principal amount of debentures on any day if AIG's common stock price exceeds 120 percent of the conversion price on the last trading day of the preceding fiscal quarter for a set period of time, and after September 30, 2031, on any day if AIG's common stock price exceeds such amount for one day, subject to certain restrictions. The debentures are redeemable by AIG on or after November 9, 2006 at specified redemption prices. Holders may require AIG to repurchase the debentures at specified repurchase prices on November 9, 2006, 2011, 2016, 2021, and 2026. At December 31, 2005, the debentures outstanding had a face value of $1.52 billion, unamortized discount of $460 million and a net book value of $1.06 billion. The amortization of the original issue discount was recorded as a component of other operating expenses.

(B) Notes and Debentures Issued by SAI: As of December 31, 2005, notes and debentures originally issued by SAI aggregating $435 million (net of unamortized discount of $40 million) were outstanding with maturity dates from 2007 to 2097 at interest rates ranging from 5.60 percent to 9.95 percent.

(C) Term Notes: On September 30, 2005, AIG sold $1.5 billion principal amount of notes in a Rule 144A/Regulation S offering, $500 million of which bear interest at a rate of 4.700 percent per annum and mature in 2010 and $1.0 billion of which bear interest at a rate of 5.050 percent per annum and mature in 2015. The notes are senior unsecured obligations of AIG and rank equally with all of AIG's other senior debt outstanding. AIG has agreed to use commercially reasonable efforts to consummate an exchange offer for the notes pursuant to an effective registration statement within 360 days of the date on which the notes were issued.

On May 15, 2003, AIG sold $1.5 billion principal amount of notes in a Rule 144A/Regulation S offering, $500 million of which bear interest at a rate of 2.875 percent per annum and mature in 2008 and $1.0 billion of which bear interest at a rate of 4.250 percent per annum and mature in 2013. The notes are senior unsecured obligations of AIG and rank equally with all of AIG's other senior debt outstanding. AIG completed an exchange offer in April 2004 with respect to the Rule 144A/Regulation S Notes and issued in exchange substantially identical notes that are registered under the Securities Act.

(v) Notes and Bonds Payable Issued by AGC: As of December 31, 2005, AGC notes aggregating $797 million were outstanding with maturity dates ranging from 2010 to 2029 at interest rates ranging up to 7.75 percent.

As of November 2001, AIG guaranteed the notes and bonds of AGC.

(e) Loans and Mortgages Payable:

Loans and mortgages payable at December 31, 2005, consisted of the following:

(in millions)	Uncollateralized Loans Payable	Collateralized Loans and Mortgages Payable
AIG Finance (Hong Kong) Limited	$ 183	$ –
AIGCFG	864	–
AIG	814	–
Other subsidiaries	618	309
Total	$2,479	$309

(f) Liabilities Connected to Trust Preferred Stock: AGC issued Junior Subordinated Debentures (liabilities) to four trusts established by AGC, which represent the sole assets of the trusts. The trusts have no independent operations. The trusts issued mandatory redeemable preferred stock to investors. The interest terms and payment dates of the liabilities correspond to those of the preferred stock. AGC's obligations with respect to the liabilities and related agreements, when taken together, constitute a full and unconditional guarantee by AGC of payments due on the preferred securities. The liabilities are redeemable, under certain conditions, at the option of AGC on a proportionate basis.

The preferred stock consists of $300 million liquidation value of 8.5 percent preferred stock issued by American General Capital II in June 2000, $500 million liquidation value of 8.125 percent preferred stock issued by American General Institutional Capital B in March 1997, and $500 million liquidation value of 7.57 percent preferred stock issued by American General Institutional Capital A in December 1996.

In December 2005, $100 million liquidation value of 8.05 percent preferred stock were redeemed by American General Capital III.

(g) Revolving Credit Facilities: AIG and AIG Funding, Inc. (AIG Funding) are parties to unsecured syndicated revolving credit facilities aggregating $2.75 billion, consisting of $1.375 billion in a 364-day revolving credit facility that expires in July of 2006 and $1.375 billion in a five-year revolving credit facility that expires in July of 2010. The 364-day facility allows for the conversion by AIG of any outstanding loans at expiration into one-year term loans. The facilities can be used for general corporate purposes and also to provide backup for AIG's commercial paper programs administered by AIG Funding. AIG expects to replace or extend these credit facilities on or prior to their expiration. There are currently no borrowings outstanding under these facilities, nor were any borrowings outstanding as of December 31, 2005.

In November 2005, AIG and AIG Funding entered into a 364-day revolving credit facility for an aggregate amount of $3 billion, which can be drawn in the form of loans or letters of credit. The credit facility expires in November 2006 but allows for the issuance of letters of credit with terms of up to ten years and provides for the conversion by AIG of any outstanding loans at expiration into one-year term loans. The facility can be used for general corporate purposes, including

9. Debt Outstanding

Continued

providing backup for AIG's commercial paper programs administered by AIG Funding and obtaining letters of credit to secure obligations under insurance and reinsurance transactions. There are currently no loans outstanding under the facility, nor were any loans outstanding as of December 31, 2005. As of such dates, $1.14 billion was available to be drawn under the facility, with the remainder having been drawn in the form of letters of credit.

AIG is also a party to an unsecured inter-company revolving credit facility provided by certain of its subsidiaries aggregating $2 billion that expires in October of 2006. The facility allows for the conversion of any outstanding loans at expiration into one-year term loans. The facility can be used for general corporate purposes and also to provide backup for AIG's commercial paper programs. AIG expects to replace or extend this credit facility on or prior to its expiration. There are currently no borrowings outstanding under the inter-company facility, nor were any borrowings outstanding as of December 31, 2005.

AGF is a party to unsecured syndicated revolving credit facilities aggregating $4.25 billion, consisting of $2.125 billion in a 364-day revolving credit facility that expires in July 2006 and $2.125 billion in a five-year credit facility that expires in July 2010. The 364-day facility allows for the conversion by AGF of any outstanding loan at expiration into a one-year term loan. The facilities can be used for general corporate purposes and also to provide backup for AGF's commercial paper programs. AGF expects to replace or extend these credit facilities on or prior to their expiration. There are currently no borrowings outstanding under these facilities, nor were any borrowings outstanding as of December 31, 2005.

ILFC is a party to unsecured syndicated revolving credit facilities aggregating $6.0 billion. The facilities can be used for general corporate purposes and also to provide backup for ILFC's commercial paper program. They consist of $2.0 billion in a 364-day revolving credit facility that expires in October 2006, with a one-year term out option, $2.0 billion in a five-year revolving credit facility that expires in October 2009 and $2.0 billion in a five-year revolving credit facility that expires in October 2010. ILFC expects to replace or extend these credit facilities on or prior to their expiration. There are currently no borrowings outstanding under these facilities, nor were any borrowings outstanding as of December 31, 2005.

ILFC was a party to two 180-day revolving credit facilities aggregating to $1.0 billion, each of which expired in 2005.

(h) Interest Expense for All Indebtedness: Total interest expense for all indebtedness, net of capitalized interest, aggregated $5.67 billion in 2005, $4.43 billion in 2004 and $4.22 billion in 2003. Capitalized interest was $64 million in 2005, $59 million in 2004 and $52 million in 2003. Cash distributions on the preferred shareholders' equity in subsidiary companies of ILFC and liabilities connected to trust preferred stock of AGC subsidiaries are accounted for as interest expense in the consolidated statement of income. The cash distributions for ILFC were approximately $5 million, $4 million, and $4 million for the years ended December 31, 2005, 2004, and 2003, respectively. The cash distributions for AGC subsidiaries were approximately $112 million, $123 million and $128 million for the years ended December 31, 2005, 2004 and 2003, respectively.

10. Preferred Shareholders' Equity in Subsidiary Companies

As of December 31, 2005, preferred shareholders' equity in subsidiary companies represents preferred stocks issued by ILFC, a wholly owned subsidiary of AIG.

At December 31, 2005, the preferred stock consists of 1,000 shares of market auction preferred stock (MAPS) in two series (Series A and B) of 500 shares each. Each of the MAPS shares has a liquidation value of $100,000 per share and is not convertible. The dividend rate, other than the initial rate, for each dividend period for each series is reset approximately every seven weeks (49 days) on the basis of orders placed in an auction. During 2001, ILFC extended the term of the Series A to five years at a dividend rate of 5.90 percent. At December 31, 2005, the dividend rate for Series B was 4.51 percent.

11. Shareholders' Equity

(a) AIG parent depends on its subsidiaries for cash flow in the form of loans, advances, reimbursement for shared expenses, and dividends. AIG's insurance subsidiaries are subject to regulatory restrictions on the amount of dividends which can be remitted to AIG parent. These restrictions vary by state. For example, unless permitted by the New York Superintendent of Insurance, general insurance companies domiciled in New York may not pay dividends to shareholders which in any twelve month period exceed the lesser of ten percent of the company's statutory policyholders' surplus or 100 percent of its "adjusted net investment income," as defined. Generally, less severe restrictions applicable to both General and Life Insurance companies exist in most of the other states in which AIG's insurance subsidiaries are domiciled. Certain foreign jurisdictions have restrictions which could delay or limit the remittance of dividends. There are also various local restrictions limiting cash loans and advances to AIG by its subsidiaries. Largely as a result of the restrictions, approximately 89 percent of consolidated shareholders' equity was restricted from immediate transfer to AIG parent at December 31, 2005.

(b) At December 31, 2005, there were 6,000,000 shares of AIG's $5 par value serial preferred stock authorized, issuable in series, none of which were outstanding.

11. Shareholders' Equity

Continued

(c) The common share activity for the three years ended December 31, 2005 was as follows:

	2005	2004	2003
Shares outstanding at beginning of year	**2,596,423,190**	2,608,447,046	2,609,600,831
Acquired during the year	**(2,654,272)**	(16,426,114)	(3,899,991)
Issued pursuant to performance stock unit obligations	**15,757**	24,025	–
Issued under stock plans	**2,625,227**	4,310,733	2,699,584
Issued under contractual obligations	**236,870**	67,500	46,622
Shares outstanding at end of year	**2,596,646,772**	2,596,423,190	2,608,447,046

12. Commitments and Contingent Liabilities

In the normal course of business, various commitments and contingent liabilities are entered into by AIG and certain of its subsidiaries. In addition, AIG guarantees various obligations of certain subsidiaries.

(a) AIG and certain of its subsidiaries become parties to derivative financial instruments with market risk resulting from both dealer and end user activities and to reduce currency, interest rate, equity, and commodity exposures. These instruments are carried at their estimated fair values in the consolidated balance sheet. The vast majority of AIG's derivative activity is transacted by AIGFP. See also Note 20 herein.

(b) Securities sold, but not yet purchased and spot commodities sold but not yet purchased represent obligations of AIGFP to deliver specified securities and spot commodities at their contracted prices. AIGFP records a liability to repurchase the securities and spot commodities in the market at prevailing prices.

AIG has issued unconditional guarantees with respect to the prompt payment, when due, of all present and future payment obligations and liabilities of AIGFP arising from transactions entered into by AIGFP. Net revenues for the twelve months ended December 31, 2005, 2004 and 2003 from Capital Markets operations were $3.26 billion, $1.28 billion and $595 million, respectively.

(c) At December 31, 2005, ILFC had committed to purchase 338 new and used aircraft deliverable from 2006 through 2015 at an estimated aggregate price of $23.3 billion and had options to purchase 16 new aircraft at an estimated aggregate purchase price of $1.5 billion. ILFC will be required to find customers for any aircraft acquired, and it anticipates that it will be required to arrange financing for portions of the purchase price of such equipment.

(d) AIG and its subsidiaries, in common with the insurance industry in general, are subject to litigation, including claims for punitive damages, in the normal course of their business. The recent trend of increasing jury awards and settlements makes it difficult to assess the ultimate outcome of such litigation.

Although AIG annually reviews the adequacy of the established reserve for losses and loss expenses, there can be no assurance that AIG's ultimate loss reserves will not develop adversely and materially exceed AIG's current loss reserves. Estimation of ultimate net losses, loss expenses and loss reserves is a complex process for long-tail casualty lines of business, which include excess and umbrella liability, directors and officers liability (D&O), professional liability, medical malpractice, workers compensation, general liability, products liability and related classes, as well as for asbestos and environmental exposures. Generally, actual historical loss development factors are used to project future loss development. However, there can be no assurance that future loss development patterns will be the same as in the past. Moreover, any deviation in loss cost trends or in loss development factors might not be discernible for an extended period of time subsequent to the recording of the initial loss reserve estimates for any accident year. Thus, there is the potential for reserves with respect to a number of years to be significantly affected by changes in loss cost trends or loss development factors that were relied upon in setting the reserves. These changes in loss trends or loss development factors could be attributable to changes in inflation in labor and material costs or in the judicial environment, or in other social or economic phenomena affecting claims.

(e) SAI Deferred Compensation Holdings, Inc., a wholly-owned subsidiary of AIG, has established a deferred compensation plan for registered representatives of certain AIG subsidiaries, pursuant to which participants have the opportunity to invest deferred commissions and fees on a notional basis. The value of the deferred compensation fluctuates with the value of the deferred investment alternatives chosen. AIG has provided a full and unconditional guarantee of the obligations of SAI Deferred Compensation Holdings, Inc. to pay the deferred compensation under the plan.

(f) On June 27, 2005, AIG entered into agreements pursuant to which AIG agrees, subject to certain conditions, to (i) make any payment that is not promptly paid with respect to the benefits accrued by certain employees of AIG and its subsidiaries under the SICO Plans (as defined in Note 16) and (ii) make any payment to the extent not promptly paid by Starr with respect to amounts that become payable to certain employees of AIG and its subsidiaries who are also stockholders of Starr after the giving of a notice of repurchase or redemption under Starr's organizational documents. In January 2006, Starr announced that it had completed its tender offer to

12. Commitments and Contingent Liabilities

Continued

purchase interests in Starr and that all eligible shares had tendered their shares. As a result of completion of the tender offer, no executive currently holds any Starr interests.

(g) AIG and certain of its subsidiaries have been named defendants in two putative class actions in state court in Alabama that arise out of the 1999 settlement of class and derivative litigation involving Caremark Rx, Inc. (Caremark). An excess policy issued by a subsidiary of AIG with respect to the 1999 litigation was expressly stated to be without limit of liability. In the current actions, plaintiffs allege that the judge approving the 1999 settlement was misled as to the extent of available insurance coverage and would not have approved the settlement had he known of the existence and/or unlimited nature of the excess policy. They further allege that AIG, its subsidiaries, and Caremark are liable for fraud and suppression for misrepresenting and/or concealing the nature and extent of coverage. In their complaint, plaintiffs request compensatory damages for the 1999 class in the amount of $3.2 billion, plus punitive damages. AIG and its subsidiaries deny the allegations of fraud and suppression and have asserted, *inter alia*, that information concerning the excess policy was publicly disclosed months prior to the approval of the settlement. AIG and its subsidiaries further assert that the current claims are barred by the statute of limitations and that plaintiffs' assertions that the statute was tolled cannot stand against the public disclosure of the excess coverage. Plaintiffs, in turn, have asserted that the disclosure was insufficient to inform them of the nature of the coverage and did not start the running of the statute of limitations. On January 28, 2005, the Alabama trial court determined that one of the current actions may proceed as a class action on behalf of the 1999 classes that were allegedly defrauded by the settlement. AIG, its subsidiaries, and Caremark are seeking appellate relief from the Alabama Supreme Court. AIG cannot now estimate either the likelihood of its prevailing in these actions or the potential damages in the event liability is determined.

(h) On December 30, 2004, an arbitration panel issued its ruling in connection with a 1998 workers compensation quota share reinsurance agreement under which Superior National Insurance Company, among others, was reinsured by USLIFE, a subsidiary of American General Corporation. In its 2-1 ruling the arbitration panel refused to rescind the contract as requested by USLIFE. Instead, the panel reformed the contract to reduce USLIFE's participation by ten percent. USLIFE disagrees with the ruling and is pursuing all appropriate legal remedies. USLIFE has certain reinsurance recoverables in connection with the contract and the arbitration ruling established a second phase of arbitration in which USLIFE will present its challenges to cessions to the contract.

AIG recorded a $178 million pre-tax charge in the fourth quarter of 2004 related to this matter and holds a reserve of approximately $364 million as of December 31, 2005.

(i) Regulators from several states have commenced investigations into insurance brokerage practices related to contingent commissions and other broker-related conduct, such as alleged bid rigging. Various parties, including insureds and shareholders, have also asserted putative class action and other claims against AIG or its subsidiaries alleging, among other things, violations of the antitrust and federal securities laws, and AIG expects that additional claims may be made.

In February 2006, AIG reached a resolution of claims and matters under investigation with the United States Department of Justice (DOJ), the Securities and Exchange Commission (SEC), the Office of the New York Attorney General (NYAG) and the New York State Department of Insurance (DOI). The settlements resolved outstanding litigation filed by the SEC, NYAG and DOI against AIG and concluded negotiations with these authorities and the DOJ in connection with the accounting, financial reporting and insurance brokerage practices of AIG and its subsidiaries, as well as claims relating to the underpayment of certain workers compensation premium taxes and other assessments. The 2005 financial statements include a fourth quarter after-tax charge of $1.15 billion to record the settlements.

As a result of these settlements, AIG made payments totaling approximately $1.64 billion, $225 million of which represented fines and penalties. A substantial portion of the money will be available to resolve claims asserted in various regulatory and civil proceedings, including shareholder lawsuits.

Also, as part of the settlements, AIG has agreed to retain for a period of three years an independent consultant who will conduct a review that will include the adequacy of AIG's internal control over financial reporting and the remediation plan that AIG has implemented as a result of its own internal review.

Various federal and state regulatory agencies are reviewing certain other transactions and practices of AIG and its subsidiaries in connection with industry-wide and other inquiries. AIG has cooperated, and will continue to cooperate, in producing documents and other information in response to the subpoenas.

A number of lawsuits have been filed regarding the subject matter of the investigations of insurance brokerage practices, including derivative actions, individual actions and class actions under the federal securities laws, Racketeer Influenced and Corrupt Organizations Act (RICO), Employee Retirement Income Security Act (ERISA) and state common and corporate laws in both federal and state courts, including the United States District Court for the Southern District of New York (Southern District of New York), in the Commonwealth of Massachusetts Superior Court and in Delaware Chancery Court. All of these actions generally allege that AIG and its subsidiaries violated the law by allegedly concealing a scheme to "rig bids" and "steer" business between insurance companies and insurance brokers.

Since October 19, 2004, AIG or its subsidiaries have been named as a defendant in fifteen complaints that were filed in federal court and two that were originally filed in state court (Massachusetts and Florida) and removed to federal court. These cases generally allege that AIG and its subsidiaries

12. Commitments and Contingent Liabilities

Continued

violated federal and various state antitrust laws, as well as federal RICO laws, various state deceptive and unfair practice laws and certain state laws governing fiduciary duties. The alleged basis of these claims is that there was a conspiracy between insurance companies and insurance brokers with regard to the use of contingent commission agreements, bidding practices, and other broker-related conduct concerning coverage in certain sectors of the insurance industry. The Judicial Panel on Multidistrict Litigation entered an order on February 17, 2005, consolidating most of these cases and transferring them to the United States District Court for the District of New Jersey (District of New Jersey). The remainder of these cases have been transferred to the District of New Jersey. On August 15, 2005, the plaintiffs in the multidistrict litigation filed a Corrected First Consolidated Amended Commercial Class Action Complaint, which, in addition to the previously named AIG defendants, names new AIG subsidiaries as defendants. Also on August 15, 2005, AIG and two subsidiaries were named as defendants in a Corrected First Consolidated Amended Employee Benefits Class Action Complaint filed in the District of New Jersey, which asserts similar claims with respect to employee benefits insurance and a claim under ERISA on behalf of putative classes of employers and employees. On November 29, 2005, the AIG defendants, along with other insurer defendants and the broker defendants filed motions to dismiss both the Commercial and Employee Benefits Complaints. Plaintiffs have filed a motion for class certification in the consolidated action. In addition, complaints were filed against AIG and several of its subsidiaries in Massachusetts and Florida state courts, which have both been stayed. In the Florida action, the plaintiff has filed a petition for a writ of certiorari with the District Court of Appeals of the State of Florida, Fourth District with respect to the stay order. On February 9, 2006, a complaint against AIG and several of its subsidiaries was filed in Texas state court, making claims similar to those in the federal cases above.

In April and May 2005, amended complaints were filed in the consolidated derivative and securities cases, as well as in one of the ERISA lawsuits, pending in the Southern District of New York adding allegations concerning AIG's accounting treatment for non-traditional insurance products. In September 2005, a second amended complaint was filed in the consolidated securities cases adding allegations concerning AIG's First Restatement. Also in September 2005, a new securities action complaint was filed in the Southern District of New York, asserting claims premised on the same allegations made in the consolidated cases. Motions to dismiss have been filed in the securities actions. In September 2005, a consolidated complaint was filed in the ERISA case pending in the Southern District of New York. Motions to dismiss have been filed in that ERISA case. Also in April 2005, new derivative actions were filed in Delaware Chancery Court, and in July and August 2005, two new derivative actions were filed in the Southern District of New York asserting claims duplicative of the claims made in the consolidated derivative action.

In July 2005, a second amended complaint was filed in the consolidated derivative case in the Southern District of New York, expanding upon accounting-related allegations, based upon the First Restatement and, in August 2005, an amended consolidated complaint was filed. In June 2005, the derivative cases in Delaware were consolidated. AIG's Board of Directors has appointed a special committee of independent directors to review the matters asserted in the derivative complaints. The courts have approved agreements staying the derivative cases pending in the Southern District of New York and in Delaware Chancery Court while the special committee of independent directors performs its work. In September 2005, a shareholder filed suit in Delaware Chancery Court seeking documents relating to some of the allegations made in the derivative suits. AIG filed a motion to dismiss in October 2005.

In late 2002, a derivative action was filed in Delaware Chancery Court in connection with AIG's transactions with certain entities affiliated with Starr and Starr International Company, Inc. (SICO). In May 2005, the plaintiff filed an amended complaint which adds additional claims premised on allegations relating to insurance brokerage practices and AIG's non-traditional insurance products. Plaintiffs in that case have agreed to dismiss newly added allegations unrelated to transactions with entities affiliated with Starr and SICO without prejudice to pursuit of these claims in the separate derivative actions described above. On February 16, 2006, the Delaware Chancery Court entered an order dismissing the litigation with prejudice with respect to AIG's outside directors and dismissing the claims against the remaining AIG defendants without prejudice.

AIG cannot predict the outcome of the matters described above or estimate the potential costs related to these matters and, accordingly, no reserve is being established in AIG's financial statements at this time. In the opinion of AIG management, AIG's ultimate liability for the unresolved matters referred to above is not likely to have a material adverse effect on AIG's consolidated financial condition, although it is possible that the effect would be material to AIG's consolidated results of operations for an individual reporting period.

(j) On July 8, 2005, SICO filed a complaint against AIG in the Southern District of New York. The complaint alleges that AIG is in the possession of items, including artwork, which SICO claims it owns, and seeks an order causing AIG to release those items as well as actual, consequential, punitive and exemplary damages. On September 27, 2005, AIG filed its answer to SICO's complaint denying SICO's allegations and asserting counter-claims for breach of contract, unjust enrichment, conversion and breach of fiduciary duty relating to SICO's breach of its commitment to use its AIG shares for the benefit of AIG and its employees. On October 17, 2005, SICO replied to AIG's counter-claims and additionally sought a judgment declaring that SICO is neither a control person nor an affiliate of AIG for purposes of Schedule 13D under the Securities Exchange Act of 1934, as amended (the Exchange Act), and Rule 144 under the Securities Act of 1933, as

12. Commitments and Contingent Liabilities

Continued

amended (the Securities Act), respectively. AIG responded to the SICO claims on November 7, 2005.

(k) AIG subsidiaries own interests in certain limited liability companies (LLCs) which invested in six coal synthetic fuel production facilities. The sale of coal synthetic fuel produced by these six facilities generates income tax credits. Since acquiring the facilities, AIG has recognized approximately $1.0 billion of synfuel tax credits through December 31, 2005. One of the conditions a taxpayer must meet to qualify for coal synfuel tax credits is that the synfuel production facility must have been "placed in service" before July 1, 1998. On July 1, 2005 IRS field agents issued notices of proposed adjustment to the LLCs proposing to disallow all of the credits taken by the LLCs during the years 2001 through 2003. The IRS field agents subsequently conceded that one of the facilities was timely placed in service, but contended that none of the other underlying production facilities were placed in service by the statutory deadline. On October 3, 2005, IRS field agents issued 60-day letters to the LLCs proposing to disallow the tax credits taken with respect to synfuel sales by the remaining five production facilities. By letters dated February 17, 2006, the IRS field agents have advised the LLCs that they have, after further review, concluded that all six production facilities were placed in service before July 1, 1998 and that they will withdraw the 60-day letters issued to the LLCs.

Tax credits generated from the production and sale of synthetic fuel under section 29 of the Internal Revenue Code are subject to an annual phase-out provision that is based on the average wellhead price of domestic crude oil. The price range within which the tax credits are phased-out was originally established in 1980 and is adjusted annually for inflation. Depending on the price of domestic crude oil for a particular year, all or a portion of the tax credits generated in that year might be eliminated. Although AIG cannot predict the future price of domestic crude oil for the years 2006 and 2007 (the final year the tax credits are available), AIG does not expect the phase-out provision to affect tax credits generated in 2005. AIG has also entered into hedges designed to mitigate a portion of its future exposure to a sustained high price of oil. However, no assurance can be given as to the effectiveness of the hedging in actually reducing such exposure or whether such hedging will continue.

(l) AIG understands that some of its employees have received Wells notices in connection with previously disclosed SEC investigations of certain of AIG's transactions or accounting practices. Under SEC procedures, a Wells notice is an indication that the SEC staff has made a preliminary decision to recommend enforcement action that provides recipients with an opportunity to respond to the SEC staff before a formal recommendation is finalized. AIG anticipates that additional current and former employees could receive similar notices in the future as the regulatory investigations proceed.

(m) In August 2005, the Bureau of Labor Insurance in Taiwan began to levy a monthly administrative penalty against Nan Shan for not providing its agency leaders a choice between alternative government pension plans. Nan Shan has reached an agreement with the agency union and the ultimate liability is not material to AIG's consolidated financial condition or results of operations.

13. Fair Value of Financial Instruments

Statement of Financial Accounting Standards No. 107, "Disclosures about Fair Value of Financial Instruments" (FAS 107), requires disclosure of fair value information about financial instruments, as defined therein, for which it is practicable to estimate such fair value. In the measurement of the fair value of certain financial instruments, where quoted market prices are not available, other valuation techniques are utilized. These fair value estimates are derived using internally developed valuation methodologies based on available and observable market information. FAS 107 excludes certain financial instruments, including those related to insurance contracts.

The following methods and assumptions were used by AIG in estimating the fair value of the financial instruments presented:

Cash and short-term investments: The carrying amounts approximate fair values.

Fixed maturity securities: Fair values were generally based upon quoted market prices. For certain fixed maturity securities for which market prices were not readily available, fair values were estimated using values obtained from independent pricing services.

Equity securities: Fair values were based upon quoted market prices.

Mortgage loans on real estate, policy and collateral loans: Where practical, the fair values of loans on real estate and collateral loans were estimated using discounted cash flow calculations based upon AIG's current incremental lending rates for similar type loans. The fair values of the policy loans were not calculated as AIG believes it would have to expend excessive costs for the benefits derived.

Trading assets and trading liabilities: Fair values approximate the carrying values.

Finance receivables: Fair values were estimated using discounted cash flow calculations based upon the weighted average rates currently being offered for similar finance receivables.

Securities available for sale: Fair values were based on quoted market prices. Where market prices were not readily available, fair values were estimated using quoted market prices of comparable investments.

Securities lending collateral and securities lending payable: The contract values of these financial instruments approximate fair value.

Trading securities: Fair values were based on current market value where available. For securities for which market values

13. Fair Value of Financial Instruments

Continued

were not readily available, fair values were estimated using quoted market prices of comparable investments.

Spot commodities: Fair values are based on current market prices.

Unrealized gains and losses on swaps, options and forward transactions: Fair values were based on the use of valuation models that utilize, among other things, current interest, foreign exchange commodity, equity and volatility rates, as applicable.

Securities purchased (sold) under agreements to resell (repurchase), at contract value: As these securities (obligations) are short-term in nature, the contract values approximate fair values.

Other invested assets: Consisting principally of hedge funds and limited partnerships. Fair values are provided by the general partner or manager of each investment.

Policyholders' contract deposits: Fair values were estimated using discounted cash flow calculations based upon interest rates currently being offered for similar contracts with maturities consistent with those remaining for the contracts being valued.

GIAs: Fair values of AIG's obligations under investment type agreements were estimated using discounted cash flow calculations based on interest rates currently being offered for similar agreements with maturities consistent with those remaining for the agreements being valued.

Securities and spot commodities sold but not yet purchased: The carrying amounts for the securities and spot commodities sold but not yet purchased approximate fair values. Fair values for spot commodities sold short were based on current market prices.

Trust deposits and deposits due to banks and other depositors: To the extent certain amounts are not demand deposits or certificates of deposit which mature in more than one year, fair values were not calculated as AIG believes it would have to expend excessive costs for the benefits derived.

Commercial paper: The carrying amount approximates fair value.

Notes, bonds, loans and mortgages: Where practical, the fair values of these obligations were estimated using discounted cash flow calculations based upon AIG's current incremental borrowing rates for similar types of borrowings with maturities consistent with those remaining for the debt being valued.

13. Fair Value of Financial Instruments

Continued

The carrying values and fair values of AIG's financial instruments at December 31, 2005 and 2004 were as follows:

(in millions)	2005 Carrying Value*	2005 Fair Value	2004 Carrying Value*	2004 Fair Value
Assets:				
Fixed maturities	**$385,680**	**$386,199**	$365,677	$366,174
Equity securities	**23,588**	**23,588**	17,706	17,706
Mortgage loans on real estate, policy and collateral loans	**24,909**	**26,352**	23,484	23,980
Securities available for sale	**37,511**	**37,511**	31,225	31,225
Trading securities	**6,499**	**6,499**	2,746	2,746
Spot commodities	**92**	**96**	534	534
Unrealized gain on swaps, options and forward transactions	**18,695**	**18,695**	22,670	22,670
Trading assets	**1,204**	**1,204**	3,433	3,433
Securities purchased under agreements to resell	**14,547**	**14,547**	26,272	26,272
Finance receivables, net of allowance	**27,995**	**27,528**	23,574	24,133
Securities lending collateral	**59,471**	**59,471**	49,169	49,169
Other invested assets	**27,267**	**27,267**	23,559	23,559
Short-term investments	**15,342**	**15,342**	16,102	16,102
Cash	**1,897**	**1,897**	2,009	2,009
Liabilities:				
Policyholders' contract deposits	**227,027**	**223,244**	216,474	212,543
Borrowings under obligations of guaranteed investment agreements	**20,811**	**22,373**	18,919	20,897
Securities sold under agreements to repurchase	**11,047**	**11,047**	23,581	23,581
Trading liabilities	**2,546**	**2,546**	2,503	2,503
Securities and spot commodities sold but not yet purchased	**5,975**	**5,975**	5,404	5,404
Unrealized loss on swaps, options and forward transactions	**12,740**	**12,740**	15,985	15,985
Trust deposits and deposits due to banks and other depositors	**4,877**	**5,032**	4,248	4,553
Commercial paper	**9,208**	**9,208**	9,693	9,693
Notes, bonds, loans and mortgages payable	**78,439**	**79,518**	66,798	68,700
Securities lending payable	**60,409**	**60,409**	49,972	49,972

* *The carrying value of all other financial instruments approximates fair value.*

14. Stock Compensation Plans

At December 31, 2005, AIG had five types of stock-based compensation plans: *(i)* a stock option plan; *(ii)* an incentive stock plan under which restricted stock units had been issued; *(iii)* an employee stock purchase plan; *(iv)* SICO's Deferred Compensation Profit Participation Plan (SICO DCPPP) (consistent with SICO's change to equity settlement of selected awards); and *(v)* AIG's Deferred Compensation Profit Participation Plan (AIG DCPPP) which is the replacement for the SICO DCPPP.

Effective January 1, 2003, AIG adopted the recognition provision of Statement of Financial Accounting Standards No. 123, "Accounting for Stock-Based Compensation" (FAS 123). This statement establishes the financial accounting and reporting standards for stock-based employee compensation plans, such as AIG's stock purchase plan, stock option plan, stock incentive plan, SICO DCPPP, and AIG DCPPP. Under the recognition provisions of FAS 123, costs with respect to stock compensation are measured using the fair value of the shares subscribed or granted as at the date of grant recognized ratably over the vesting period. Such fair value is derived through an option pricing model or the fair value of AIG's common stock, as applicable. See Note 1(gg) herein for discussion of prospective change to AIG's accounting for retiree eligibility provisions.

Statement of Financial Accounting Standards No. 148, "Accounting for Stock-Based Compensation – Transition and Disclosure, an amendment to FASB Statement No. 123" (FAS 148), was issued in 2002. This statement amended FAS 123 and provides alternative methods of transition for a voluntary change to the recognition provisions of FAS 123. Also, FAS 148 amended certain of the disclosure requirements of FAS 123.

AIG elected the "Prospective Method" in the application of the recognition provisions as prescribed by FAS 123. Such method provides for the recognition of the fair value with respect to stock-based compensation for shares subscribed for or granted on or after January 1, 2003.

Prior to adoption of the recognition provisions of FAS 123, as amended, AIG recognized stock compensation in accordance with the provisions of APB Opinion No. 25 "Accounting for Stock Issued to Employees." Shares subscribed for or granted prior to January 1, 2003 continue to be accounted for pursuant to APB Opinion No. 25. See Note 1(gg) herein for discussion of AIG's accounting for the unvested portion of its APB 25 awards according to the requirements of FAS 123R.

14. Stock Compensation Plans

Continued

With respect to net income for December 31, 2005, 2004, and 2003, the following table provides a pro forma reconciliation as if AIG had adopted the recognition provisions of FAS 123 at the awards inception:

(in millions, except per share data)	**2005**	2004	2003
Net income, as reported	**$10,477**	$9,839	$8,108
Add back interest on contingently convertible bonds, net of tax	**11**	11	11
	10,488	9,850	8,119
Actual stock-based compensation recognized, net of tax	**53**	40	16
	10,541	9,890	8,135
Fair Value for Grants Issued prior to January 1, 2003, net of tax	**39**	49	56
Actual stock-based compensation recognized, net of tax	**53**	40	16
Net income, pro forma	**$10,449**	$9,801	$8,063
Earnings per common share:			
Basic:			
Net income, as reported	**$ 4.03**	$ 3.77	$ 3.10
Stock-based compensation, net of tax	**(0.01)**	(0.02)	(0.02)
Net income, pro forma	**$ 4.02**	$ 3.75	$ 3.08
Diluted:			
Net income, as reported	**$ 3.99**	$ 3.73	$ 3.07
Stock-based compensation, net of tax	**(0.01)**	(0.02)	(0.02)
Net income, pro forma	**$ 3.98**	$ 3.71	$ 3.05
Average shares outstanding:			
Basic	**2,597**	2,606	2,610
Diluted	**2,627**	2,637	2,637

AIG uses a binomial model to calculate the fair value of stock option grants. The model uses ten years of historical exercise behavior to account for the early exercise of employee options and five years of historical stock price data to infer the implied volatility. The fair-value model has been refined from time to time since AIG adopted FAS 123 on January 1, 2003, but valuation results have been consistent from one reporting period to the next.

The fair values of stock options granted during the three years ended December 31, 2005, 2004, and 2003 were approximately $100 million, $80 million and $180 million, respectively.

The following weighted average assumptions were used for stock options granted in 2005, 2004 and 2003, respectively: dividend yields of 0.71 percent, 0.36 percent and 0.32 percent; expected volatility of 27.3 percent, 34.4 percent and 34.0 percent; risk-free interest rates of 4.17 percent, 3.87 percent and 3.57 percent; and expected terms of seven years in each year.

Also included in the above table is the compensation expense with respect to AIG's employee stock purchase plan. The fair value calculated was derived by using the Black-Scholes model. The pro forma recognition of such fair value had an insignificant effect on the pro forma amounts disclosed above.

The fair values of purchase privileges granted during the years ended December 31, 2005, 2004 and 2003 were $13 million, $12 million and $12 million, respectively. The weighted average fair values per share of those purchase rights granted in 2005, 2004, and 2003 were $12.24, $14.82, and $11.64, respectively. The fair value of each purchase right was derived at the date of the subscription using the AIG model.

The following weighted average assumptions were used for purchase privileges granted in 2005, 2004 and 2003, respectively: dividend yields of 0.71 percent, 0.36 percent and 0.32 percent; expected volatilities of 27.3 percent, 34.4 percent and 34.0 percent; risk-free interest rates of 3.37 percent, 1.60 percent and 1.10 percent; and terms of one year.

(a) Stock Option Plan: The AIG 1999 Stock Option Plan, as amended (the 1999 Plan), provides that options to purchase a maximum of 45,000,000 shares of common stock can be granted to certain key employees and members of the Board of Directors at prices not less than fair market value at the date of grant. The 1999 Plan limits the maximum number of shares as to which stock options may be granted to any employee in any one year to 900,000 shares. Options granted under this Plan expire not more than ten years from the date of the grant. Options with respect to 32,500 shares, 25,000 shares, 25,000 shares, and 25,000 shares were granted to nonemployee members of the Board of Directors on August 11, 2005, May 19, 2004, May 14, 2003 and February 10, 2003, respectively. These options become exercisable on the first anniversary of the date of grant, expire ten years from the date of grant, and do not qualify for Incentive Stock Option Treatment under the Section 422 of the Internal Revenue Code (ISO Treatment). The 1999 Plan, and the options previously granted thereunder, were approved by the shareholders at the 2000 Annual Meeting of Shareholders, and certain amendments were approved at the 2003 Annual Meeting of Shareholders. At December 31, 2005, 20,130,562 shares were reserved for future grants under the 1999 Plan. The 1999 Plan superseded the 1991 employee stock option plan (the 1991 Plan) and the previously superseded 1987 employee stock option plan, although outstanding options granted under the 1991 Plan continue in force until exercise or expiration. At December 31, 2005, there were 29,524,565 shares reserved for issuance under the 1999 Plan and the 1991 Plan.

During 2003, AIG granted options with respect to 137,300 shares which become exercisable on the fifth anniversary of the date of grant and expire ten years from the date of grant. These options do not qualify for ISO Treatment. The agreements with respect to all other options granted to employees under these plans in 2004 and 2003 provide that 25 percent of the options granted become exercisable on the anniversary of the date of grant in each of the four years following that grant and expire 10 years from the date of the grant. As of December 31, 2005, outstanding options granted with respect to 12,009,898 shares qualified for ISO Treatment.

14. Stock Compensation Plans

Continued

At January 1, 1999, the date of the AIG/SAI merger, SAI had five stock-based compensation plans pursuant to which options, restricted stock, and deferred share and share unit obligations had been issued and remained outstanding. Options granted under these plans had an exercise price equal to the market price on the date of grant, had a maximum term of ten years, and generally became exercisable ratably over a five-year period. Substantially all of the SAI options outstanding at the merger date became fully vested on that date and were converted into options to purchase AIG common stock at the exchange ratio of 0.855 shares of AIG common stock for each share of SAI common stock. No further options can be granted under the SAI plans, but outstanding options so converted continue in force until exercise or expiration. At December 31, 2005, there were 11,526,992 shares of AIG common stock reserved for issuance on exercise of options under these plans. None of these options qualified for ISO Treatment as of December 31, 2005.

During 2005, 2004 and 2003, deferred share and share unit obligations with respect to 1,895 shares, 1,895 shares and 1,895 shares, respectively, of AIG common stock vested and were issued. No additional deferred share or share unit obligations may be granted under the SAI plans. As of December 31, 2005, deferred share and share unit obligations with respect to 59,972 shares remained outstanding under the SAI plans.

The AIG Board of Directors has construed the AIG stock option plans to allow, at the request of an optionee, the deferral of delivery of AIG shares otherwise deliverable upon the exercise of an option to a date or dates specified by the optionee. During 2005, options with respect to 1,731,471 shares were exercised with delivery deferred. At December 31, 2005, optionees had made valid elections to defer delivery of 2,067,643 shares of AIG common stock upon exercise of options expiring during 2006. In addition, nonemployee directors of AIG made valid elections to defer delivery of 21,093 shares of AIG common stock upon exercise of options expiring during 2006.

As a result of the acquisition of the Hartford Steam Boiler Inspection and Insurance Company (HSB) in November 2000, HSB options outstanding at the acquisition date were fully vested and were converted into options to purchase AIG common stock at the exchange ratio of 0.4178 shares of AIG common stock for each share of HSB common stock. No further options can be granted under the HSB option plans, but outstanding options so converted continue in force until exercise or expiration. At December 31, 2005, there were 688,648 shares of AIG common stock reserved for issuance under the HSB option plans, none of which qualified for ISO Treatment.

At August 29, 2001, AGC had stock-based compensation plans pursuant to which options and restricted share units had been issued and remained outstanding. Options granted under these plans had an exercise price equal to the market price on the date of the grant, had a maximum term of ten years, and generally became exercisable ratably over a three-year period. All of the AGC options outstanding at the acquisition date became fully vested on that date and were converted into options to purchase AIG common stock at an exchange ratio of 0.5790 shares of AIG common stock for each share of AGC common stock. No further options can be granted under the AGC plans, but outstanding options so converted continue in force until exercise or expiration. At December 31, 2005, there were 10,805,219 shares of AIG common stock reserved for issuance on exercise of options under these plans. Options with respect to 1,250,221 of these shares qualified for ISO Treatment as of December 31, 2005.

Additional information with respect to AIG's plans at December 31, 2005, and changes for the three years then ended, were as follows:

	2005		2004		2003	
	Shares	Weighted Average Exercise Price	Shares	Weighted Average Exercise Price	Shares	Weighted Average Exercise Price
Shares Under Option:						
Outstanding at beginning of year	**54,463,003**	**$51.94**	59,253,166	$48.00	54,214,016	$45.63
Granted	**4,397,500**	**62.69**	3,474,100	64.65	8,602,909	56.15
Exercised	**(2,263,377)**	**27.22**	(3,387,734)	34.02	(2,182,680)	22.69
Exercised, delivery deferred	**(1,731,471)**	**11.29**	(3,397,999)	5.98	(495,787)	8.46
Forfeited	**(2,320,230)**	**60.97**	(1,478,530)	70.69	(885,292)	66.37
Outstanding at end of year	**52,545,425**	**$54.84**	54,463,003	$51.94	59,253,166	$48.00
Options exercisable at year-end	**39,952,281**	**$52.47**	40,211,710	$47.80	43,397,566	$42.17
Weighted average fair value per share of options granted		**$21.84**		$25.61		$20.86

14. Stock Compensation Plans

Continued

In addition, at December 31, 2005, options to purchase 92,241 shares at a weighted average exercise price of $25.14 had been previously granted to AIG nonemployee directors and remained outstanding.

Information about stock options outstanding at December 31, 2005, is summarized as follows:

	Options Outstanding			Options Exercisable	
	Number Outstanding	Weighted Average Remaining Contractual Life	Weighted Average Exercise Price	Number Exercisable	Weighted Average Exercise Price
Range of Exercise Prices:					
$11.28 – 27.14	6,900,520	1.3 years	$21.38	6,900,520	$21.38
30.44 – 41.51	5,560,658	2.5 years	36.75	5,560,658	36.75
43.31 – 53.41	7,163,076	4.9 years	48.54	5,476,932	49.01
54.11 – 59.99	8,516,644	5.2 years	57.84	6,328,084	57.33
60.13 – 63.95	9,382,325	6.9 years	62.33	6,193,792	61.92
64.01 – 69.63	8,397,522	7.8 years	65.44	3,876,532	65.66
70.35 – 98.00	6,624,680	5.3 years	83.82	5,615,763	84.63
	52,545,425		$54.84	39,952,281	$52.47

(b) 2002 Stock Incentive Plan: AIG's 2002 Stock Incentive Plan was adopted at its 2002 shareholders' meeting and amended and restated by the AIG Board of Directors on September 18, 2002. This plan provides that equity-based or equity-related awards with respect to shares of common stock can be issued to officers, employees or members of the Board of Directors of AIG in any year up to a maximum of that number of shares equal to (a) 1,000,000 shares plus (b) the number of shares available but not issued in the prior calendar year. Under the Plan, no grantee may receive awards covering more than 250,000 shares of common stock. During 2005 and 2004, AIG granted restricted stock units (RSUs) relating to 3,055,835 shares and 992,481 shares of common stock to employees, respectively. These RSUs will vest on the fourth anniversary of the date of grant assuming continued employment through such date. See Note 1(gg) herein for discussion of prospective change in AIG's accounting for retiree eligibility provisions. AIG reserves the right to make payment for the RSUs in shares of common stock or the cash equivalent on the date of vesting. AIG shares delivered under the AIG DCPPP will be issued pursuant to the 2002 Stock Incentive Plan. At December 31, 2005, there were 14,675,635 shares of common stock reserved for issuance in connection with future grants of awards under the Plan.

(c) Employee Stock Purchase Plan: AIG's 1996 Employee Stock Purchase Plan, as amended and approved by AIG shareholders in 2003 (the 1996 Plan), provides that eligible employees (those employed at least one year) may receive privileges to purchase up to an aggregate of 10,000,000 shares of AIG common stock, at a price equal to 85 percent of the fair market value on the date of the grant of the purchase privilege. Purchase privileges are granted annually and are limited to the number of whole shares that can be purchased by an amount equal to 10 percent of an employee's annual salary or $10,000, whichever is less. There were 359,750 shares, 922,999 shares and 516,904 shares issued under the 1996 plan at weighted average prices of $57.06, $46.41 and $48.03 for the years ended December 31, 2005, 2004 and 2003, respectively. The excess or deficit of the proceeds over the par value or cost of the common stock issued was credited or charged to additional paid-in capital.

As of December 31, 2005, there were 1,045,329 shares of common stock subscribed to at a weighted average price of $50.91 per share pursuant to grants of privileges under the 1996 plan. There were 3,689,063 shares available for the grant of future purchase privileges under the 1996 Plan at December 31, 2005.

As a result of its changing relationship with Starr and SICO, AIG is establishing new executive compensation plans which replace existing investment opportunities and deferred compensation plans provided by Starr and SICO. The replacement plans include both share-based plans as well as cash-based plans. The share-based plans generally include performance as well as service conditions.

15. Employee Benefits

(a) Pension Plans: Employees of AIG, its subsidiaries and certain affiliated companies, including employees in foreign countries, are generally covered under various funded, unfunded and insured pension plans. Eligibility for participation in the various plans is based on either completion of a specified period of continuous service or date of hire, subject to age limitations. Some AIG subsidiaries provide retirement benefits through defined benefit plans, others employ defined contribution plans and some use both.

15. Employee Benefits

Continued

AIG's U.S. retirement plan is a qualified, noncontributory defined benefit plan which is subject to the provisions of ERISA. All employees of AIG and most of its subsidiaries and affiliates who are regularly employed in the United States, including certain U.S. citizens employed abroad on a U.S. dollar payroll, and who have attained age 21 and completed twelve months of continuous service are eligible to participate in this plan. An employee with 5 or more years of plan participation is entitled to pension benefits beginning at normal retirement at age 65. Benefits are based upon a percentage of average final compensation multiplied by years of credited service limited to 44 years of credited service. The average final compensation is subject to certain limitations. Employees may elect certain options with respect to receipt of their pension benefits including a joint and survivor annuity. An employee with 10 or more years of plan participation may retire early from age 55 to 64. An early retirement factor is applied resulting in a reduced benefit. If an employee terminates with less than five years of plan participation, the employee forfeits the right to receive any pension benefits accumulated to that time. Annual funding requirements are determined based on the "projected unit credit" cost method, which attributes a pro rata portion of the total projected benefit payable at normal retirement to each year of credited service.

The HSB retirement plan was merged into the AIG U.S. retirement plan effective April 1, 2001. Benefits for HSB participants were changed effective January 1, 2005 to be substantially similar to the AIG U.S. retirement plan benefit subject to a grandfathering agreement. The AGC retirement plan was merged into the AIG U.S. retirement plan effective January 1, 2002. Benefits for AGC participants were changed effective January 1, 2003 to be substantially similar to the AIG U.S. retirement plan benefits subject to grandfathering requirements.

AIG SunAmerica employees began participation and accruing benefits in the AIG plan on January 1, 2003. Vesting with respect to AIG SunAmerica employees in the AIG plan begins on the later of January 1, 1999, the date of acquisition or the date of hire.

21st Century sponsors its own benefit plans for its eligible employees. Assets, obligations and costs with respect to 21st Century's plans are included herein. The assumptions used in its plans were not significantly different from those used by AIG in AIG's U.S. plans.

The AIG Excess Retirement Income Plan provides a benefit equal to the reduction in benefits payable under the AIG U.S. retirement plan as a result of federal tax limitations on compensation and benefits payable thereunder. AIG has adopted a Supplemental Executive Retirement Plan (Supplemental Plan) to provide additional retirement benefits to designated executives. Under the Supplemental Plan, an annual benefit accrues at a percentage of final average pay multiplied by each year of credited service, not greater than 60 percent of final average pay, reduced by any benefits from the current and any predecessor retirement plans (including the AIG Excess Retirement Income Plan and any comparable plans), Social Security, if any, and from any qualified pension plan of prior employers. Currently, each of these plans is unfunded. AGC and HSB have adopted similar supplemental type plans. These plans are also unfunded.

Where non-U.S. retirement plans are defined benefit plans, they are generally either based on the employees' years of credited service and compensation in the years preceding retirement, or on points accumulated based on the employee's job grade and other factors during each year of service.

(b) Postretirement Plans: In addition to AIG's defined benefit pension plan, AIG and its subsidiaries provide a postretirement benefit program for medical care and life insurance domestically and in certain foreign countries. Eligibility in the various plans is generally based upon completion of a specified period of eligible service and attaining a specified age. Overseas, benefits vary by geographic location.

AIG's U.S. postretirement medical and life insurance benefits are based upon the employee electing immediate retirement and having a minimum of ten years of service. Retirees who were age 65 by May 1, 1989 and their dependents participate in the medical plan at no cost. Employees who retired after May 1, 1989 and prior to January 1, 1993 pay 50 percent of the active employee premium. Retiree contributions are subject to adjustment annually. Other cost sharing features of the medical plan include deductibles, coinsurance and Medicare coordination and a lifetime maximum benefit of $2.0 million. The maximum life insurance benefit prior to age 70 is $32,500, with a maximum of $25,000 thereafter.

Effective January 1, 1993, both plans' provisions were amended. Employees who retire after January 1, 1993 are required to pay the actual cost of the medical benefits premium reduced by a credit of a certain amount, based on years of service at retirement. The life insurance benefit varies by age at retirement from $5,000 for retirement at ages 55 through 59; $10,000 for retirement at ages 60 through 64 and $15,000 for retirement at ages 65 and over.

(c) Voluntary Savings Plans: AIG sponsors a voluntary savings plan for domestic employees (the AIG Incentive Savings plan), which, during the three years ended December 31, 2005, provided for salary reduction contributions by employees and matching contributions by AIG of up to seven percent of annual salary depending on the employees' years of service. Contributions are funded currently.

AGC sponsored a voluntary savings plan for its employees, which was merged into the AIG Incentive Savings plan on January 1, 2003.

HSB sponsored a voluntary savings plan for its employees, which was merged into the AIG Incentive Savings plan on January 1, 2002.

AIG SunAmerica sponsored a voluntary savings plan for its employees, which was merged into the AIG Incentive Savings plan on January 1, 2003. Under an AIG SunAmerica Executive Savings Plan, designated AIG SunAmerica executives also could defer up to 90 percent of cash compensation

15. Employee Benefits

Continued

and AIG SunAmerica matched four percent of the participants' base salaries deferred. The Plan was frozen to new contributions on March 31, 2003.

(d) Post Employment Benefits: AIG provides certain benefits to inactive employees who are not retirees. Certain of these benefits are insured and expensed currently; other expenses are provided for currently. Such uninsured expenses include medical and life insurance continuation, and COBRA medical subsidies.

(e) Benefit Obligations: Accumulated benefit obligations represent the present value of pension benefits earned as of December 31, 2005 based on service and compensation as of December 31, 2005. Projected benefit obligations for defined benefit plans represent the present value of pension benefits earned as of December 31, 2005 projected for estimated salary increases to an assumed date with respect to retirement, termination, disability or death. Projected benefit obligations for postretirement plans represent the present value of postretirement medical and life insurance benefits deemed earned as of December 31, 2005 projected for estimated salary and medical claim rate increases to an assumed date with respect to retirement, termination, disability, or death.

The accumulated benefit obligations with respect to both non-U.S. and U.S. pension benefit plans as of December 31, 2005 and 2004 were as follows:

(in millions)	**2005**	2004
Non-U.S. pension benefit plans	**$1,210**	$1,260
U.S. pension benefit plans	**$2,704**	$2,367

The following table sets forth the change in the projected benefit obligation of the defined benefit pension plans, including the supplemental plans, and postretirement benefit plans as of December 31, 2005 and 2004:

	Pension			Postretirement		
(in millions)	Non-U.S. Plans	U.S. Plans[a]	Total	Non-U.S. Plans	U.S. Plans	Total
2005						
Change in projected benefit obligation:						
Benefit obligation at beginning of year	**$ 1,376**	**$ 2,750**	**$ 4,126**	**$ 35**	**$ 243**	**$ 278**
Service cost	**71**	**111**	**182**	**4**	**5**	**9**
Interest cost	**32**	**153**	**185**	**2**	**11**	**13**
Participant contributions	**1**	**–**	**1**	**–**	**–**	**–**
Actuarial loss	**77**	**241**	**318**	**3**	**(38)**	**(35)**
Plan amendments, mergers and new material plans	**43**	**(29)**	**14**	**–**	**–**	**–**
Benefits paid:						
AIG assets	**(28)**	**(11)**	**(39)**	**(1)**	**(16)**	**(17)**
Plan assets	**(29)**	**(84)**	**(113)**	**–**	**–**	**–**
Effect of foreign currency fluctuation	**(184)**	**–**	**(184)**	**1**	**–**	**1**
Other	**(8)**	**–**	**(8)**	**(1)**	**–**	**(1)**
Benefit obligation at end of year	**$ 1,351**	**$ 3,131**	**$ 4,482**	**$ 43**	**$ 205**	**$ 248**
2004						
Change in projected benefit obligation:						
Benefit obligation at beginning of year	$1,348	$2,602	$3,950	$16	$247	$263
Service cost	59	101	160	3	6	9
Interest cost	33	147	180	2	14	16
Participant contributions	2	–	2	–	–	–
Actuarial loss	133	59	192	11	(6)	5
Plan amendments and mergers	(92)	(42)	(134)	–	–	–
Benefits paid:						
AIG assets	(48)	(8)	(56)	(1)	(16)	(17)
Plan assets	(27)	(71)	(98)	–	–	–
Effect of foreign currency fluctuation	67	–	67	1	–	1
Other[b]	(99)	(38)	(137)	3	(2)	1
Benefit obligation at end of year	$ 1,376	$ 2,750	$ 4,126	$ 35	$ 243	$ 278

(a) Includes excess retirement income type plans and supplemental executive type plans.

(b) With respect to AIG's non-U.S. plans obligations, the reduction resulted from transferring to the Japanese government certain Japanese plan obligations approximating $50 million. Additionally, the Japanese government also provided a subsidy with respect to certain Japanese plan obligations approximating $50 million.

15. Employee Benefits

Continued

The weighted average assumptions used to determine the benefit obligations at December 31, 2005 and 2004 were as follows:

	Pension		Postretirement	
	Non-U.S. Plans	U.S. Plans	Non-U.S. Plans	U.S. Plans
2005				
Discount rate	**1.75 - 12.00%**	**5.50%**	**4.50 - 5.50%**	**5.50%**
Rate of compensation increase	**1.50 - 10.00%**	**4.25%**	**2.50 - 3.00%**	**4.25%**
2004				
Discount rate	1.75 - 12.00%	5.75%	4.50 - 6.00%	5.75%
Rate of compensation increase	1.50 - 10.00%	4.25%	3.00%	4.25%

The benefit obligations outside the United States reflect those assumptions that were most appropriate for the local economic environments of each of the subsidiaries providing such benefits.

To measure the obligations at December 31, 2004, a 9.0 percent annual rate of increase in the per capita cost of covered healthcare benefits for AIG's U.S. plans was used for 2005. This rate was assumed to decrease gradually to 5.0 percent in 2009 and remain at that level thereafter. To measure the obligations at December 31, 2005 for AIG's U.S. plans, a 9.0 percent annual rate of increase in the per capita cost of covered medical benefits for pre-age-65 retirees, a 7.0 percent annual rate of increase in the per capita cost of covered medical benefits for post-age-65 retirees and an 11.0 percent annual rate of increase in the per capita cost of retiree prescription drug coverage was used for 2006. These rates were assumed to decrease gradually to 5.0 percent in 2013 and remain at that level thereafter.

The assumed range for 2006 with respect to the annual rates of increase in the per capita cost of covered healthcare benefits of AIG's non-U.S. plans is 7.0 to 9.0 percent. These rates are assumed to decrease gradually to 4.0 to 5.0 percent after three to four years and remain at that level thereafter.

A one percent point change in the assumed healthcare cost trend rate would have the following effect on AIG's postretirement benefit obligations at December 31, 2005:

	One Percentage Point	
(in millions)	Increase	Decrease
Non-U.S. plans	$ 8	$(6)
U.S. plans	$(2)	$ 2

Discount Rate Methodology

The projected benefit cash flows under the AIG Retirement Plan (the main US plan) were discounted using the spot rates derived from the Citigroup Pension Discount Curve as of December 31, 2005 and an equivalent single discount rate was derived resulting in the same liability. This single discount rate was rounded to the nearest 25 basis points, namely 5.5 percent, and applied to all U.S. plans.

Prior to using the Citigroup Pension Discount Curve in 2005, the discount rate assumptions were based on the yield of the Moody's Investor Service (Moody's) Aa long-term corporate bond index.

Japan represents over 70 percent of the liabilities of the non-U.S. pension plans. The discount rate for Japan was selected by reference to the published Moody's/S&P AA Corporate Bond Universe at the measurement date having regard to the duration of the plans' liabilities.

The mortality assumption for AIG's U.S. plans has been revised for the December 31, 2005 obligations. The 2004 and 2005 expense and the obligations at December 31, 2004 were based on the 1983 Group Annuity Mortality Table. The December 31, 2005 obligations were based on the RP2000 White Collar Combined Mortality Table projected to 2006. Due to continued improvements in life expectancy, the updated table is expected to better represent AIG's anticipated future experience under the plans. The mortality assumptions for AIG's non-U.S. plans vary by country. No changes have been made for the December 31, 2005 obligations. The assumptions used are expected to reasonably anticipate future mortality experience.

(f) Funded Status: The funded status of the AIG defined benefit plans is a comparison of the pension benefit obligations to the assets related to the respective plan, if any. The difference between the two represents amounts that have been appropriately recognized as expenses in prior periods or represent amounts that will be recognized as expenses in the future.

15. Employee Benefits

Continued

The following table sets forth the funded status of the plans, reconciled to the amount reported on the consolidated balance sheet at December 31, 2005 and 2004:

	Pension			Postretirement[b]		
(in millions)	Non-U.S. Plans[a]	U.S. Plans	Total	Non-U.S. Plans	U.S. Plans	Total
2005						
Fair value of plan assets	**$ 699**	**$ 2,561**	**$ 3,260**	**$ –**	**$ –**	**$ –**
Less projected benefit obligations	**1,351**	**3,130**	**4,481**	**43**	**205**	**248**
Funded status	**(652)**	**(569)**	**(1,221)**	**(43)**	**(205)**	**(248)**
Amounts not yet recognized:						
Actuarial (gains)/losses[c]	**303**	**1,093**	**1,396**	**3**	**5**	**8**
Prior service cost	**(79)**	**(23)**	**(102)**	**–**	**(32)**	**(32)**
Transition obligations	**1**	**–**	**1**	**–**	**–**	**–**
Net amount recognized	**$ (427)**	**$ 501**	**$ 74**	**$ (40)**	**$ (232)**	**$ (272)**
Composition of net amount recognized:						
Prepaid benefit cost	**$ 24**	**$ 670**	**$ 694**	**$ –**	**$ –**	**$ –**
Accrued benefit cost	**(590)**	**(217)**	**(807)**	**(40)**	**(232)**	**(272)**
Intangible asset	**3**	**6**	**9**	**–**	**–**	**–**
Accumulated other comprehensive income	**136**	**42**	**178**	**–**	**–**	**–**
Net amount recognized	**$ (427)**	**$ 501**	**$ 74**	**$ (40)**	**$ (232)**	**$ (272)**
2004						
Fair value of plan assets	$ 624	$2,247	$ 2,871	$ –	$ –	$ –
Less projected benefit obligations	1,376	2,750	4,126	35	243	278
Funded status	(752)	(503)	(1,255)	(35)	(243)	(278)
Amounts not yet recognized:						
Actuarial (gains)/losses[c]	380	840	1,220	–	44	44
Prior service cost	(101)	3	(98)	–	(39)	(39)
Transition obligations	2	–	2	–	–	–
Net amount recognized	$ (471)	$ 340	$ (131)	$ (35)	$ (238)	$ (273)
Composition of net amount recognized:						
Prepaid benefit cost	$ 13	$ 499	$ 512	$ –	$ –	$ –
Accrued benefit cost	(697)	(191)	(888)	(35)	(238)	(273)
Intangible asset	5	6	11	–	–	–
Accumulated other comprehensive income	208	26	234	–	–	–
Net amount recognized	$ (471)	$ 340	$ (131)	$ (35)	$ (238)	$ (273)

(a) A significant portion of these plans, particularly those in Japan, are not required by local regulation to be funded currently. With respect to the funded status of these Japanese plans, the projected benefit obligation amounts to approximately $410 million and $480 million and approximately $360 million and $400 million has been recognized at December 31, 2005 and December 31, 2004, respectively.

(b) AIG does not currently fund postretirement benefits.

(c) Actuarial (gains)/losses are amounts included in the projected benefit obligations but not yet recognized in the financial statements.

Defined benefit pension plan obligations where the projected benefit obligation was in excess of the related plan assets at December 31, 2005 and 2004 were as follows:

	2005		2004	
(in millions)	Non-U.S. Plans	U.S. Plans	Non-U.S. Plans	U.S. Plans
Projected benefit obligation	**$ 1,284**	**$ 3,130**	$1,344	$2,750
Accumulated benefit obligation	**1,163**	**2,704**	1,240	2,367
Fair value of plan assets	**610**	**2,561**	576	2,247

15. Employee Benefits

Continued

Defined benefit pension plan obligations where the accumulated benefit obligation was in excess of the related plan assets at December 31, 2005 and 2004 were as follows:

(in millions)	2005 Non-U.S. Plans	2005 U.S. Plans	2004 Non-U.S. Plans	2004 U.S. Plans
Projected benefit obligation	$ 1,281	$ 268	$1,324	$232
Accumulated benefit obligation	1,161	224	1,226	194
Fair value of plan assets	607	9	558	9

(g) Plan Assets:

The following table sets forth the change in plan assets as at December 31, 2005 and 2004:

(in millions)	Pension Non-U.S. Plans	Pension U.S. Plans	Pension Total	Postretirement Non-U.S. Plans	Postretirement U.S. Plans	Postretirement Total
2005						
Change in plan assets:						
Fair value of plan assets at beginning of year	$ 624	$2,247	$2,871	$ –	$ –	$ –
Actual return on plan assets net of expenses	101	113	214	–	–	–
AIG contributions	95	298	393	1	16	17
Participant contributions	1	–	1	–	–	–
Benefits paid:						
AIG assets	(28)	(11)	(39)	(1)	(16)	(17)
Plan assets	(29)	(84)	(113)	–	–	–
Effect of foreign currency fluctuation	(85)	–	(85)	–	–	–
Other	20	(2)	18	–	–	–
Fair value of plan assets at end of year	$ 699	$2,561	$3,260	$ –	$ –	$ –
2004						
Change in plan assets:						
Fair value of plan assets at beginning of year	$ 591	$2,124	$2,715	$ –	$ –	$ –
Actual return on plan assets net of expenses	40	151	191	–	–	–
AIG contributions	81	61	142	1	16	17
Participant contributions	2	–	2	–	–	–
Benefits paid:						
AIG assets	(48)	(8)	(56)	(1)	(16)	(17)
Plan assets	(27)	(71)	(98)	–	–	–
Effect of foreign currency fluctuation	30	–	30	–	–	–
Other*	(45)	(10)	(55)	–	–	–
Fair value of plan assets at end of year	$ 624	$2,247	$2,871	$ –	$ –	$ –

** Approximately $50 million was disbursed as a result of the settlement of certain Japanese plan obligations with the Japanese government.*

15. Employee Benefits

Continued

The asset allocation percentage by major asset class for AIG's U.S. plans at December 31, 2005 and 2004, and the target allocation for 2006 follows:

		Allocation	
	Target 2006	Actual 2005	Actual 2004
Asset class:			
Equity securities	0-70%	59%	63%
Debt securities	0-100	34	32
Other	0-40	7	5
Total	100%	100%	100%

The asset allocation percentage by major asset class for AIG's non-U.S. plans at December 31, 2005 and 2004, and the target allocation for 2006 follows:

		Allocation	
	Target 2006	Actual 2005	Actual 2004
Asset class:			
Equity securities	0-75%	46%	32%
Debt securities	0-100	27	14
Other	0-100	27	54
Total	100%	100%	100%

The "Other" includes alternative asset classes.

Included in equity securities at December 31, 2005 and 2004 were 0.6 million and 1.2 million shares of AIG common stock, with values of $41.1 million and $79.3 million, respectively.

The investment strategy with respect to AIG's pension plan assets is to preserve capital and to seek investment returns with a goal of fully funding the plan.

The expected rate of return with respect to AIG's domestic pension plan was 8.0 percent and 8.25 percent for the twelve months ended December 31, 2005 and 2004, respectively. These rates of return are an aggregation of expected returns within each asset category. The return with respect to each asset class considers both historical returns and the future expectations for such returns.

(h) Expected Cash Flows: With respect to AIG's U.S. pension plan, the actuarially prepared funding amount ranges from the minimum amount AIG would be required to contribute to the maximum amount that would be deductible for U.S. tax purposes. This range is generally not determined until the fourth quarter with respect to the contribution year. Contributed amounts in excess of the minimum amounts are deemed voluntary. Amounts in excess of the maximum amount would be subject to an excise tax and may not be deductible under the Internal Revenue Code. Supplemental and excess plans' payments and postretirement plan payments are deductible when paid.

AIG contributed $393 million during 2005 to its U.S. and non-U.S. pension plans. The annual pension contribution for 2006 is expected to be approximately $70 million for U.S. and non-U.S. plans.

The expected future benefit payments, net of participants' contributions with respect to the defined benefit pension plans and other postretirement benefit plans, are as follows:

	Pension		Postretirement	
(in millions)	Non-U.S. Plans	U.S. Plans	Non-U.S. Plans	U.S. Plans
2006	$ 61	$102	$1	$16
2007	63	111	1	17
2008	68	119	1	17
2009	76	128	1	18
2010	73	137	1	18
2011-2015	401	885	6	98

15. Employee Benefits

Continued

(i) Net Periodic Benefit Costs:

The following table presents the components of the net periodic benefit costs with respect to pensions and other benefits for the years ended December 31, 2005, 2004 and 2003:

	Pensions			Postretirement		
(in millions)	Non-U.S. Plans	U.S. Plans	Total	Non-U.S. Plans	U.S. Plans	Total
2005						
Components of net periodic benefit cost:						
Service cost	**$ 71**	**$ 111**	**$ 182**	**$ 4**	**$ 5**	**$ 9**
Interest cost	**32**	**153**	**185**	**2**	**11**	**13**
Expected return on assets	**(21)**	**(180)**	**(201)**	**–**	**–**	**–**
Amortization of prior service cost	**(10)**	**(3)**	**(13)**	**–**	**(6)**	**(6)**
Amortization of transitional liability	**1**	**–**	**1**	**–**	**–**	**–**
Recognition of net actuarial (gains)/losses	**21**	**55**	**76**	**–**	**–**	**–**
Other	**7**	**1**	**8**	**–**	**–**	**–**
Net periodic benefit cost	**$ 101**	**$ 137**	**$ 238**	**$ 6**	**$ 10**	**$ 16**
2004						
Components of net periodic benefit cost:						
Service cost	$ 59	$ 101	$ 160	$ 3	$ 6	$ 9
Interest cost	33	147	180	2	14	16
Expected return on assets	(22)	(170)	(192)	–	–	–
Amortization of prior service cost	(8)	–	(8)	–	(7)	(7)
Amortization of transitional liability	2	–	2	–	–	–
Recognition of net actuarial (gains)/losses	15	53	68	11	2	13
Other*	(24)	–	(24)	3	–	3
Net periodic benefit cost	$ 55	$ 131	$ 186	$19	$15	$34
2003						
Components of net periodic benefit cost:						
Service cost	$ 52	$ 79	$ 131	$ 1	$ 4	$ 5
Interest cost	33	151	184	1	15	16
Expected return on assets	(18)	(145)	(163)	–	–	–
Amortization of prior service cost	(3)	4	1	–	(6)	(6)
Amortization of transitional liability	2	1	3	–	–	–
Recognition of net actuarial (gains)/losses	19	61	80	–	1	1
Other	(26)	–	(26)	–	–	–
Net periodic benefit cost	$ 59	$ 151	$ 210	$ 2	$14	$16

* *The reduction resulted from transferring to the Japanese government certain Japanese plan obligations approximating $50 million reduced by approximately $26 million loss incurred with respect to the settlement of those obligations.*

15. Employee Benefits

Continued

The weighted average assumptions used to determine the net periodic benefit costs for the years ended December 31, 2005, 2004, and 2003 were as follows:

	Pension		Postretirement	
	Non-U.S. Plans*	U.S. Plans	Non-U.S. Plans*	U.S. Plans
2005				
Discount rate	**1.75 - 12.00%**	**5.75%**	**4.50 - 6.00%**	**5.75%**
Rate of compensation increase	**1.50 - 10.00%**	**4.25%**	**3.00%**	**4.25%**
Expected return on assets	**2.15 - 13.50%**	**8.00%**	**N/A**	**N/A**
2004				
Discount rate	2.00 - 8.00%	6.00%	5.50 - 6.00%	6.00%
Rate of compensation increase	1.50 - 7.00%	4.25%	5.50%	4.25%
Expected return on assets	2.50 - 10.00%	8.25%	N/A	N/A
2003				
Discount rate	2.00 - 8.00%	6.75%	5.50 - 6.00%	6.75%
Rate of compensation increase	1.50 - 7.00%	4.50%	5.50%	4.50%
Expected return on assets	3.00 - 10.00%	8.75%	N/A	N/A

* *The benefit obligations outside the United States reflect those assumptions that were most appropriate for each local economic environment of the subsidiaries providing such benefits.*

AIG's postretirement plans provide benefits primarily in the form of defined employer contributions as opposed to defined employer benefits. As such, a change in the assumed health-care cost trend rate has little effect on postretirement expense.

16. Benefits Provided by Starr International Company, Inc.

SICO has provided a series of two-year Deferred Compensation Profit Participation Plans (SICO Plans) to certain AIG employees. The SICO Plans came into being in 1975 when the voting shareholders and Board of Directors of SICO, a private holding company whose principal asset is AIG common stock, decided that a portion of the capital value of SICO should be used to provide an incentive plan for the current and succeeding managements of all American International companies, including AIG.

None of the costs of the various benefits provided under the SICO Plans has been paid by AIG, although AIG has recorded a charge to reported earnings for the deferred compensation amounts paid to AIG employees by SICO, with an offsetting entry to additional paid-in capital reflecting amounts deemed contributed by SICO. The SICO Plans provide that shares currently owned by SICO may be set aside by SICO for the benefit of the participant and distributed upon retirement. The SICO Board of Directors currently may permit an early payout of units under certain circumstances. Prior to payout, the participant is not entitled to vote, dispose of or receive dividends with respect to such shares, and shares are subject to forfeiture under certain conditions, including but not limited to the participant's voluntary termination of employment with AIG prior to normal retirement age. Under the SICO Plans, SICO's Board of Directors may elect to pay a participant cash in lieu of shares of AIG common stock. Following notification from SICO to participants in the SICO Plans that it will settle specific future awards under the SICO Plans with shares rather than cash, AIG modified its accounting for the SICO Plans from variable to fixed measurement accounting. AIG gave effect to this change in settlement method beginning on December 9, 2005, the date of SICO's notice to the SICO Plans' participants. See also Note 12(f) herein.

Prior to 2005, SICO also provided certain personal benefits to AIG employees. The cost of such benefits, primarily attributable to personal use of corporate aircraft, has not been included in compensation expense.

Compensation expense with respect to the SICO Plans aggregated $205 million, $62 million and $280 million for 2005, 2004 and 2003, respectively.

As a result of its changing relationship with Starr and SICO, AIG is establishing new executive compensation plans to replace the SICO plans and investment opportunities previously provided by Starr. The replacement plans include both share-based plans and cash-based plans. In addition, these replacement plans generally include performance as well as service conditions.

17. Leases

(a) AIG and its subsidiaries occupy leased space in many locations under various long-term leases and have entered into various leases covering the long-term use of data processing equipment.

At December 31, 2005, the future minimum lease payments under operating leases were as follows:

(in millions)	
2006	$ 573
2007	436
2008	325
2009	253
2010	215
Remaining years after 2010	932
Total	$2,734

Rent expense approximated $597 million, $568 million, and $524 million for the years ended December 31, 2005, 2004, and 2003 respectively.

(b) Minimum future rental income on noncancelable operating leases of flight equipment which have been delivered at December 31, 2005 was as follows:

(in millions)	
2006	$ 3,227
2007	2,813
2008	2,296
2009	1,820
2010	1,490
Remaining years after 2010	3,740
Total	$15,386

Flight equipment is leased, under operating leases, with remaining terms ranging from 1 to 16 years.

18. Ownership and Transactions With Related Parties

(a) Ownership: According to the Schedule 13D filed on March 7, 2006 by Starr, SICO, Edward E. Matthews, Maurice R. Greenberg, the Maurice R. and Corinne P. Greenberg Family Foundation, Inc. and the Universal Foundation, Inc., these reporting persons may be deemed to beneficially own 396,124,637 shares of common stock. Based on the shares of common stock outstanding as of December 31, 2005, this ownership represents approximately 15 percent of the voting stock of AIG.

(b) Transactions with Related Parties: During the ordinary course of business during 2005, AIG and its subsidiaries paid commissions to Starr and its subsidiaries for the production and management of insurance business. There are no significant receivables from/payables to related parties at December 31, 2005. Payment for the production of insurance business to Starr aggregated approximately $214 million in 2005, $205 million in 2004, and $173 million in 2003, from which Starr generally is required to pay commissions due to originating brokers and its operating expenses. AIG also received approximately $23 million in 2005, $24 million in 2004, and $24 million in 2003 from Starr and paid approximately $20,000 in 2005, $39,000 in 2004, and $114,000 in 2003 to Starr in rental fees and for services none in 2005, $262,000 in 2004 and 2003. AIG also received approximately $2 million in 2005, $1 million in 2004, and $2 million in 2003, respectively, from SICO and paid approximately $1 million in each of the years 2005, 2004 and 2003 to SICO as reimbursement for services rendered at cost. AIG also paid to SICO $3 million in 2005, $4 million in 2004, and $4 million in 2003 in rental fees.

19. Variable Interest Entities

In January 2003, FASB issued FIN46. FIN46 changed the method of determining whether certain entities should be consolidated in AIG's consolidated financial statements. An entity is subject to FIN46 and is called a Variable Interest Entity (VIE) if it has (i) equity that is insufficient to permit the entity to finance its activities without additional subordinated financial support from other parties, or (ii) equity investors that cannot make significant decisions about the entity's operations, or that do not absorb the expected losses or receive the expected returns of the entity. A VIE is consolidated by its primary beneficiary, which is the party that has a majority of the expected losses or a majority of the expected residual returns of the VIE, or both. All other entities not considered VIEs are evaluated for consolidation under other guidance. In December 2003, FASB issued a revision to Interpretation No. 46 (FIN46R).

The provisions of FIN46R had to be applied immediately to VIEs created after January 31, 2003, and to VIEs in which AIG obtains an interest after that date. For VIEs in which AIG held a variable interest that it acquired before February 1, 2003, FIN46R was applied as of December 31, 2003. For any VIEs that were consolidated under FIN46R that were created before February 1, 2003, the assets, liabilities and noncontrolling interest of the VIEs were initially measured at their fair values with any difference between the net amount added to the balance sheet and any previously recognized interest being recognized as the cumulative effect of an accounting change. In accordance with the transition provisions of FIN46R, AIG recorded a gain of $9 million ($14 million before tax) reported as a cumulative effect of an accounting change for the fourth

19. Variable Interest Entities

Continued

quarter of 2003 and added approximately $4.7 billion of assets and liabilities to its consolidated balance sheet at December 31, 2003.

Of the $4.7 billion, approximately $4.2 billion relates to assets and liabilities arising from AIG's real estate partnerships, principally affordable housing transactions involving AIG SunAmerica subsidiaries, and private equity partnerships managed by AIG Global Investment Group and AIG Capital Partners.

SunAmerica Affordable Housing Partners, Inc. (SAAHP) organizes limited partnerships that are considered to be VIEs, and that are consolidated by AIG. The partnerships invest as limited partners in operating partnerships that develop and operate low income housing and a smaller number of market rate properties across the United States. The general partners in the operating partnerships are almost exclusively unaffiliated third-party developers. AIG does not generally consolidate an operating partnership if the general partner is an unaffiliated person. Through approximately 1,000 partnerships, SAAHP has invested in developments with approximately 147,000 apartment units nationwide, and has syndicated over $5 billion in partnership equity since 1991 to other investors who will receive, among other benefits, tax credits under certain sections of the Internal Revenue Code. AIG Retirement Services, Inc. functions as the general partner in certain limited partnerships and acts as both a credit enhancer in certain transactions, through differing structures with respect to funding development costs for the operating partnerships, and as guarantor that investors will receive the tax benefits projected at the time of syndication. As part of their incentive compensation, certain key SAAHP employees have been awarded residual cash flow interests in the partnerships, subject to certain vesting requirements. The operating income of SAAHP is reported, along with other SunAmerica partnership income, as a component of AIG's Asset Management segment.

The remaining approximately $500 million involves ILFC, and arises principally from a sale-leaseback transaction which expired during 2004.

AIGFP is involved with various special purpose vehicles in the ordinary course of business that may be deemed VIEs and may hold variable interests therein. The variable interests that AIGFP may hold include debt securities, equity interests, loans, derivative instruments and other credit support arrangements. Transactions associated with these entities include an asset-backed commercial paper conduit, asset securitizations, collateralized debt obligations, investment vehicles and other structured financial transactions. AIGFP engages in these transactions to facilitate client needs, for investment purposes and to obtain attractive funding.

As of December 31, 2005, AIGFP was the primary beneficiary in the following VIEs:

- An asset-backed commercial paper conduit, with which it entered into several total return swaps covering all the conduit's assets that absorb the majority of the expected losses of the entity. The total assets of the conduit that serve as collateral to the conduit's obligations that are reflected in AIG's consolidated balance sheet at December 31, 2005 were $5.9 billion.
- Several structured financing transactions in which AIGFP held the first loss position either by investing in the equity of the entity or implicitly through a lending or derivative arrangement. The total assets of these entities that are reflected in AIG's consolidated balance sheet at December 31, 2005 were $1.6 billion. The obligations of these entities are paid solely from the cash flows of the assets held by the VIEs.

As of December 31, 2005 and 2004, AIG's consolidated balance sheet included approximately $11.8 billion and $8.1 billion of assets and liabilities connected to entities consolidated under FIN46R.

The following VIE activities are not consolidated by AIG under FIN46R:

- AIG uses VIEs primarily in connection with certain guaranteed investment contract programs (GIC Programs) written by its Life Insurance & Retirement Services subsidiaries. In the GIC Programs, AIG's Life Insurance subsidiaries (principally SunAmerica Life Insurance Company) provide guaranteed investment contracts to VIEs which are not controlled by AIG, and in which AIG does not have a direct variable interest, as defined under FIN46R, in the entity. The VIE issues notes or bonds which are sold to third-party institutional investors. Neither AIG nor the insurance company issuing the GICs has any obligation to the investors in the notes or bonds. The proceeds from the securities issued by the VIE are invested by the VIE in the GICs. The insurance company subsidiaries use the proceeds to invest in a diversified portfolio of securities, primarily investment grade bonds. Both the assets and the liabilities of the insurance companies arising from these GIC Programs are presented in AIG's consolidated balance sheet. Thus, at December 31, 2005, approximately $37 billion of policyholders' contract deposits represented liabilities from issuances of GICs included in these GIC Programs, the proceeds of which are used to invest in insurance invested assets.
- AIG manages Collateralized Bond and Loan Obligation trusts (collectively, Collateralized Debt Obligation trusts or CDO trusts). As asset manager, AIG receives fees for management of the assets held in the CDO trust, which support the issuance of securities sold by the CDO trust. AIG may take minority equity and/or fixed-income security interests in the CDO trust. AIG has entered into such arrangements to expand its asset management activities. Third-party investors have recourse only to the CDO trust and have no recourse to AIG.
- AIG's insurance operations also invest in obligations of VIEs. These VIEs are established by unrelated third parties. Investments include collateralized mortgage backed securities and similar securities backed by pools of mortgages, consumer receivables, or other assets. The investment in these VIEs allows AIG's insurance entities to purchase assets permitted by insurance regulations while maximizing their return on these assets.

19. Variable Interest Entities

Continued

AIGFP has significant variable interests in various transactions where AIGFP is not the primary beneficiary. These transactions consist principally of structured financings, in which AIGFP owns an investment interest or is a lender, financial derivatives or credit support provider. At December 31, 2005 and 2004, the total assets of these entities were $29.9 billion and $18.1 billion, respectively. AIGFP's maximum exposure to loss in these transactions, at December 31, 2005, was $15.1 billion in the aggregate.

20. Derivatives

Derivatives are financial arrangements among two or more parties with returns linked to or "derived" from some underlying equity, debt, commodity or other asset, liability, or index. Derivative payments may be based on interest rates and exchange rates and/or prices of certain securities, commodities, or financial or commodity indices or other variables. These instruments are carried at fair value in the consolidated balance sheet. Collateral is required, at the discretion of AIG, on certain transactions based on the creditworthiness of the counterparty.

The overwhelming majority of AIG's derivatives activities are conducted by the Capital Markets operations. AIGFP becomes a party to derivative financial instruments in the normal course of business and to reduce currency, interest rate, commodity, and equity exposures. Interest rate, currency, commodity, and equity risks related to such instruments are reflected in the consolidated financial statements and are carried at a market or a fair value, whichever is appropriate. The recorded estimated fair values of such instruments may be different from the values that might be realized if AIGFP was required to sell or close out the transactions prior to maturity.

AIGFP, in the ordinary course of operations and as principal, structures and enters into derivative transactions to meet the needs of counterparties who may be seeking to hedge certain aspects of such counterparties' operations or obtain a desired financial exposure. AIGFP also enters into derivative transactions to hedge the financial exposures arising from its counterparty transactions. Such derivative transactions include interest rate, currency, commodity, credit and equity swaps, swaptions, and forward commitments. Interest rate swap transactions generally involve the exchange of fixed and floating rate interest payment obligations without the exchange of the underlying principal amounts. AIGFP typically becomes a principal in the exchange of interest payments between the parties and, therefore, is exposed to counterparty credit risk and may be exposed to loss, if counterparties default. Currency, commodity, and equity swaps are similar to interest rate swaps, but involve the exchange of specific currencies or cashflows based on the underlying commodity, equity securities or indices. Also, they may involve the exchange of principal amounts at the beginning and end of the transaction. Swaptions are options where the holder has the right but not the obligation to enter into a swap transaction or cancel an existing swap transaction. At December 31, 2005, the aggregate notional principal amount of AIGFP's outstanding swap transactions approximated $1,224 billion, primarily related to interest rate swaps of approximately $837.4 billion.

Notional amount represents a standard of measurement of the volume of swaps business of Capital Markets operations. Notional amount is not a quantification of market risk or credit risk and is not recorded on the consolidated balance sheet. Notional amounts generally represent those amounts used to calculate contractual cash flows to be exchanged and are not paid or received, except for certain contracts such as currency swaps.

The timing and the amount of cash flows relating to Capital Markets foreign exchange forwards and exchange traded futures and options contracts are determined by each of the respective contractual agreements.

The following table presents the contractual and notional amounts by maturity and type of derivative of Capital Markets derivatives portfolio at December 31, 2005 and 2004:

	Remaining Life of Notional Amount*					
(in millions)	One Year	Two Through Five Years	Six Through Ten Years	After Ten Years	**Total 2005**	Total 2004
Capital Markets interest rate, currency and equity swaps and swaptions:						
Notional amount:						
Interest rate swaps	$235,255	$440,686	$141,482	$19,966	**$ 837,389**	$ 858,733
Currency swaps	57,555	103,483	35,886	14,595	**211,519**	275,466
Swaptions, equity and commodity swaps	84,960	52,566	22,148	15,423	**175,097**	151,789
Total	$377,770	$596,735	$199,516	$49,984	**$1,224,005**	$1,285,988

* *Notional amount is not representative of either market risk or credit risk and is not recorded on the consolidated balance sheet.*

Futures and forward contracts are contracts that obligate the holder to sell or purchase foreign currencies, commodities or financial indices in which the seller/purchaser agrees to make/take delivery at a specified future date of a specified instrument, at a specified price or yield. Options are contracts that allow the holder of the option to purchase or sell the underlying commodity, currency or index at a specified price and within, or at, a specified period of time. As a writer of

20. Derivatives

Continued

options, AIGFP generally receives an option premium and then manages the risk of any unfavorable change in the value of the underlying commodity, currency or index by entering into offsetting transactions with third-party market participants. Risks arise as a result of movements in current market prices from contracted prices, and the potential inability of the counterparties to meet their obligations under the contracts. At December 31, 2005, the contractual amount of Capital Markets futures, forward and option contracts approximated $321.1 billion.

The following table presents Capital Markets futures, forward and option contracts portfolio by maturity and type of derivative at December 31, 2005 and 2004:

	Remaining Life					
(in millions)	One Year	Two Through Five Years	Six Through Ten Years	After Ten Years	**Total 2005**	Total 2004
Futures, forward and options contracts:						
Exchange traded futures and options contracts contractual amount	$ 19,182	$ 4,768	$1,287	$61	**$ 25,298**	$ 27,456
Over the counter forward contracts contractual amount	287,894	7,017	867	–	**295,778**	277,935
Total	$307,076	$11,785	$2,154	$61	**$321,076**	$305,391

AIGFP enters into credit derivative transactions in the ordinary course of its business. The majority of AIGFP's credit derivatives require AIGFP to provide credit protection on a designated portfolio of loans or debt securities. AIGFP provides such credit protection on a "second loss" basis, under which AIGFP's payment obligations arise only after credit losses in the designated portfolio exceed a specified threshold amount or level of "first losses." The threshold amount of credit losses that must be realized before AIGFP has any payment obligation is negotiated by AIGFP for each transaction to provide that the likelihood of any payment obligation by AIGFP under each transaction is remote, even in severe recessionary market scenarios.

In certain cases, the credit risk associated with a designated portfolio is tranched into different layers of risk, which are then analyzed and rated by the credit rating agencies. Typically, there will be an equity layer covering the first credit losses in respect of the portfolio up to a specified percentage of the total portfolio, and then successive layers that are rated, generally a BBB-rated layer, an A-rated layer, an AA-rated layer, and an AAA-rated layer. In transactions that are rated, the risk layer or tranche that is immediately junior to the threshold level above which AIGFP's payment obligation would generally arise is rated AAA by the rating agencies. In transactions that are not rated, AIGFP applies the same risk criteria for setting the threshold level for its payment obligations. Therefore the risk layer assumed by AIGFP with respect to the designated portfolio in these transactions is often called the "super senior" risk layer, defined as the layer of credit risk senior to a risk layer that has been rated AAA by the credit rating agencies or if the transaction is not rated, equivalent thereto. For example, in a transaction with an equity layer covering credit losses from zero to two percent of the total portfolio, a BBB-rated layer covering credit losses from two to four percent, an A-rated layer from four to six percent, an AA-rated layer from six to eight percent, and a AAA-rated layer from eight to 11 percent. AIGFP would cover credit losses arising in respect of the portfolio that exceeded an 11 percent first loss threshold amount and thereby bear risk that is senior to the AAA-rated risk layer.

AIGFP continually monitors the underlying portfolios to determine whether the credit loss experience for any particular portfolio has caused the likelihood of AIGFP having a payment obligation under the transaction to be greater than super senior risk. AIGFP maintains the ability opportunistically to economically hedge specific securities in a portfolio and thereby further limit its exposure to loss and has hedged outstanding transactions in this manner on occasion. AIGFP has never had a payment obligation under these credit derivatives transactions where AIGFP is providing credit protection on the super senior risk. Furthermore, based on portfolio credit losses experienced as of December 31, 2005 under all such outstanding transactions, no transaction has experienced credit losses in an amount that has made the likelihood of AIGFP having to make a payment, in AIGFP's view, to be greater than remote, even in severe recessionary market scenarios. At December 31, 2005, the notional amount with respect to the Capital Markets credit derivative portfolio (including the super senior transactions) was $387.2 billion.

AIGFP utilizes various credit enhancements, including letters of credit, guarantees, collateral, credit triggers, credit derivatives, and margin agreements to reduce the credit exposure relating to derivative financial instruments. AIGFP requires credit enhancements in connection with specific transactions based on, among other things, the creditworthiness of the counterparties, and the transaction's size and maturity. In addition, Capital Markets derivative transactions are generally documented under ISDA Master Agreements. Management believes that such agreements provide for legally enforceable set-off and close-out netting of exposures to specific counterparties. Under such agreements, in connection with an early termination of a transaction, AIGFP is permitted to set-off its receivables from a counterparty against its payables to the same counterparty arising out of all included transactions. As a result, the fair value represents the net sum of estimated positive fair values after the application of such strategies and

20. Derivatives

Continued

agreements. After consideration of these credit enhancements, the fair value of AIGFP's interest rate, currency, commodity and equity swaps, options, swaptions, and forward commitments, futures, and forward contracts approximated $18.70 billion at December 31, 2005 and $22.67 billion at December 31, 2004. These amounts have been determined in accordance with the respective close-out netting provisions under the applicable ISDA Master Agreements. The fair value represents the maximum potential loss to AIGFP.

AIGFP independently evaluates the creditworthiness of its counterparties, taking into account credit ratings assigned by recognized statistical rating organizations. In addition, AIGFP's credit approval process involves pre-set counterparty and country credit exposure limits and, for particularly credit intensive transactions, obtaining approval from AIG's Credit Risk Committee. AIGFP estimates that the average credit rating of Capital Markets derivatives counterparties, measured by reference to the fair value of its derivative portfolio as a whole, is equivalent to the AA rating category. The maximum potential loss will increase or decrease during the life of the derivative commitments as a function of maturity and market conditions.

Capital Markets determines counterparty credit quality by reference to ratings from independent rating agencies or, where such ratings are not available, by internal analysis. At December 31, 2005 and 2004, the counterparty credit quality with respect to the fair value of Capital Markets derivatives portfolios were as follows:

	Fair Value	
(in millions)	**Total 2005**	Total 2004
Counterparty credit quality:		
AAA	**$ 4,568**	$ 9,185
AA	**8,057**	7,244
A	**3,838**	4,448
BBB	**1,709**	1,193
Below investment grade	**523**	600
Total	**$18,695**	$22,670

At December 31, 2005 and 2004, the counterparty breakdown by industry with respect to the fair value of Capital Markets derivatives portfolio was as follows:

	Fair Value	
(in millions)	**Total 2005**	Total 2004
Non-U.S. banks	**$ 6,182**	$ 7,163
Insured municipalities	**387**	543
U.S. industrials	**1,434**	2,139
Governmental	**2,158**	1,387
Non-U.S. financial service companies	**873**	1,511
Non-U.S. industrials	**2,287**	2,377
Special purpose	**2,529**	4,937
U.S. banks	**1,147**	773
U.S. financial service companies	**1,618**	1,726
Supranationals	**51**	114
Utility	**29**	–
Total	**$18,695**	$22,670

FAS 133 requires that third-party derivatives used for hedging must be specifically matched with the underlying exposures to an outside third party and documented contemporaneously to qualify for hedge accounting treatment. In many cases, AIG did not meet these hedging requirements with respect to certain hedging transactions. Not meeting the requirements of FAS 133 does not result in any changes in AIG's liquidity or its overall financial condition even though inter-period volatility of earnings is increased.

AIG and its subsidiaries also use derivatives and other instruments as part of its financial risk management programs. Interest rate derivatives (such as interest rate swaps) are used to manage interest rate risk associated with its investments in fixed income securities, commercial paper issuances, medium and long-term note offerings, and other interest rate sensitive assets and liabilities. In addition, foreign exchange derivatives (principally cross currency swaps, forwards and options) are used to economically hedge non-U.S. dollar denominated debt, net capital exposures and foreign exchange transactions. The derivatives are effective economic hedges of the exposures they are meant to offset. For accounting purposes, a limited number of these derivatives have been designated as hedging instruments under FAS 133. The effect on earnings from those derivatives that have been designated as hedges is insignificant for 2005 and 2004.

21. Variable Life and Annuity Contracts

In July 2003, the American Institute of Certified Public Accountants issued Statement of Position 03-1, "Accounting and Reporting by Insurance Enterprises for Certain Nontraditional Long-Duration Contracts and for Separate Accounts" (SOP 03-1). This Statement was effective January 1, 2004, and requires AIG to recognize a liability for guaranteed minimum death benefits and other living benefits related to its variable annuity and variable life contracts and modifies certain disclosures and financial statement presentations for these products. AIG reported for the first quarter of 2004 a one-time

21. Variable Life and Annuity Contracts

Continued

cumulative accounting charge upon adoption of $144 million to reflect the liability as of January 1, 2004.

As of January 1, 2004, approximately $11 billion of assets and liabilities representing most of the non-U.S. portion of AIG's separate and variable account assets and liabilities were reclassified in accordance with SOP 03-1 to several invested asset captions and to the Policyholders' contract deposits liability caption, respectively. Approximately $11 billion of separate and variable account assets were reclassified as follows: $4 billion to Short-term investments; $4 billion to Equity securities – common stocks trading; $2 billion to Fixed maturities – bond trading securities; and $1 billion to various other asset captions.

Except as noted above, AIG reports variable contracts through separate and variable accounts when investment income and investment gains and losses accrue directly to, and investment risk is borne by, the contract holder (traditional variable annuities). AIG also reports variable annuity and life contracts through separate and variable accounts where AIG contractually guarantees to the contract holder (variable contracts with guarantees) either *(a)* total deposits made to the contract less any partial withdrawals plus a minimum return (and in minor instances, no minimum returns) (Net Deposits Plus a Minimum Return) or *(b)* the highest contract value attained, typically on any anniversary date minus any subsequent withdrawals following the contract anniversary (Highest Contract Value Attained). These guarantees include benefits that are payable in the event of death, annuitization, or, in other instances, at specified dates during the accumulation period. Such benefits are referred to as guaranteed minimum death benefits (GMDB), guaranteed minimum income benefits (GMIB), and guaranteed minimum withdrawal benefit (GMWB), or guaranteed minimum account value benefits (GMAV), respectively. For AIG, GMDB is by far the most widely offered benefit.

The assets supporting the variable portion of both traditional variable annuities and variable contracts with guarantees are carried at fair value and reported as summary total separate and variable account assets with an equivalent summary total reported for liabilities. Amounts assessed against the contract holders for mortality, administrative, and other services are included in revenue and changes in liabilities for minimum guarantees are included in policyholder benefits in the Consolidated Statement of Income. Separate and variable account net investment income, net investment gains and losses, and the related liability changes are offset within the same line item in the Consolidated Statement of Income.

The vast majority of AIG's exposure on guarantees made to variable contract holders arises from GMDB. Details concerning AIG's GMDB exposures as of December 31, 2005 and 2004 are as follows:

(dollars in billions)	Net Deposits Plus a Minimum Return	Highest Contract Value Attained
2005		
Account Value[a]	**$59**	**$13**
Amount at Risk[b]	**7**	**1**
Average Attained Age of Contract Holders by Product	**51-70 years**	**57-70 years**
Range of Guaranteed Minimum Return Rates	**0-10%**	
2004		
Account Value[a]	$57	$12
Amount at Risk[b]	8	2
Average Attained Age of Contract Holders by Product	49-70 years	52-68 years
Range of Guaranteed Minimum Return Rates	0-10%	

(a) Included in Policyholders' Contract Deposits in the Consolidated Balance Sheet.

(b) Represents the amount of death benefit currently in excess of Account Value.

The following summarizes GMDB liabilities for guarantees on variable contracts reflected in the general account.

(in millions)	**2005**	2004
Balance at January 1	**$485**	$479*
Reserve increase	**33**	86
Benefits paid	**(76)**	(80)
Balance at December 31	**$442**	$485

** Includes amounts from the one-time cumulative accounting charge resulting from the adoption of SOP 03-1.*

The GMDB liability is determined each period end by estimating the expected value of death benefits in excess of the projected account balance and recognizing the excess ratably over the accumulation period based on total expected assessments. AIG regularly evaluates estimates used and adjusts the additional liability balance, with a related charge or credit to benefit expense, if actual experience or other evidence suggests that earlier assumptions should be revised.

The following assumptions and methodology were used to determine the domestic and foreign GMDB liability as of December 31, 2005:

- Data used was up to 5,000 stochastically generated investment performance scenarios.
- Mean investment performance assumptions ranged from approximately three percent to ten percent depending on the block of business.
- Volatility assumptions ranged from 10 percent to 30 percent depending on the block of business.
- Mortality was assumed at between 60 percent and 103 percent of various life and annuity mortality tables.

21. Variable Life and Annuity Contracts

Continued

- For domestic contracts, lapse rates vary by contract type and duration and ranged from zero percent to 40 percent. For Japan, lapse rates ranged from zero percent to 20 percent depending on the type of contract.
- For domestic contracts, the discount rate ranged from 3.25 percent to 11 percent. For Japan, the discount rate ranged from zero percent to seven percent.

In addition to GMDB, AIG's contracts currently include to a lesser extent GMIB. The GMIB liability is determined each period end by estimating the expected value of the annuitization benefits in excess of the projected account balance at the date of annuitization and recognizing the excess ratably over the accumulation period based on total expected assessments. AIG regularly evaluates estimates used and adjusts the additional liability balance, with a related charge or credit to benefit expense, if actual experience or other evidence suggests that earlier assumptions should be revised. As of December 31, 2005, most of AIG's GMIB exposure was transferred via reinsurance agreements. Contracts with GMIB not reinsured have account values of $2.8 billion with a corresponding reserve of less than $1 million.

AIG contracts currently include a minimal amount of GMAV and GMWB. GMAV and GMWB are considered to be derivatives and are recognized at fair value through earnings. AIG enters into derivative contracts to partially hedge the economic exposure that arises from GMAV and GMWB.

22. Restated Quarterly Financial Information (Unaudited)

The following quarterly financial information for each of the three months ended March 31, June 30, September 30 and December 31, 2005 and 2004 is unaudited and was restated as described in Note 2(b) of Notes to Consolidated Financial Statements in AIG's Annual Report on Form 10-K/A for the year ended December 31, 2004 and Note 1(hh) herein. In the opinion of management, all adjustments (consisting of normal recurring adjustments) necessary to present fairly the results of operations for such periods, have been made for a fair presentation of the results shown.

CONSOLIDATED STATEMENTS OF INCOME

	Three Months Ended										
	March 31,			June 30,			September 30,			December 31,	
(in millions, except per share data)	2005 Previously Reported	2005 Restated	2004	2005 Previously Reported	2005 Restated	2004	2005 Previously Reported	2005 Restated	2004	2005	2004
Revenues:											
Premiums and other considerations	$ 17,682	$17,680	$15,979	$ 17,541	$17,536	$16,175	$ 17,244	$17,243	$17,281	$17,750	$17,190
Net investment income	5,292	5,332	4,600	5,198	5,227	4,541	5,629	5,654	4,509	5,952	4,815
Realized capital gains (losses)	88	137	(86)	245	(125)	89	79	77	(78)	252	119
Other revenues	4,050	4,053	2,729	3,877	5,265	3,284	3,409	3,434	3,602	3,438	2,917
Total revenues	27,112	27,202	23,222	26,861	27,903	24,089	26,361	26,408	25,314	27,392	25,041
Benefits and expenses:											
Incurred policy losses and benefits	14,865	14,873	13,590	14,336	14,283	13,480	16,503	16,501	15,217	18,054	16,073
Insurance acquisition & other operating expenses	6,804	6,680	5,790	6,730	6,919	5,960	7,381	7,360	6,041	9,022	6,670
Total benefits and expenses	21,669	21,553	19,380	21,066	21,202	19,440	23,884	23,861	21,258	27,076	22,743
Income before income taxes, minority interest and cumulative effect of an accounting change	5,443	5,649	3,842	5,795	6,701	4,649	2,477	2,547	4,056	316	2,298
Income taxes:											
Current	987	968	1,345	790	1,015	1,092	372	372	201	214	(45)
Deferred	626	738	(215)	884	1,068	372	334	376	1,064	(493)	593
	1,613	1,706	1,130	1,674	2,083	1,464	706	748	1,265	(279)	548
Income before minority interest and cumulative effect of an accounting change	3,830	3,943	2,712	4,121	4,618	3,185	1,771	1,799	2,791	595	1,750
Minority interest	(146)	(144)	(70)	(129)	(129)	(105)	(54)	(54)	(142)	(151)	(138)
Income before cumulative effect of an accounting change	3,684	3,799	2,642	3,992	4,489	3,080	1,717	1,745	2,649	444	1,612
Cumulative effect of an accounting change, net of tax	-	-	(144)	-	-	-	-	-	-	-	-
Net income	$ 3,684	$ 3,799	$ 2,498	$ 3,992	$ 4,489	$ 3,080	$ 1,717	$ 1,745	$ 2,649	$ 444	$ 1,612
Earnings per common share:											
Basic											
Income before cumulative effect of an accounting change	$ 1.42	$ 1.46	$ 1.01	$ 1.54	$ 1.73	$ 1.19	$ 0.66	$ 0.67	$ 1.01	$ 0.17	$ 0.62
Cumulative effect of an accounting change, net of tax	-	-	(0.06)	-	-	-	-	-	-	-	-
Net income	1.42	1.46	0.95	1.54	1.73	1.19	0.66	0.67	1.01	0.17	0.62
Diluted											
Income before cumulative effect of an accounting change	$ 1.40	$ 1.45	$ 1.00	$ 1.53	$ 1.71	$ 1.17	$ 0.65	$ 0.66	$ 1.00	$ 0.17	$ 0.62
Cumulative effect of an accounting change, net of tax	-	-	(0.06)	-	-	-	-	-	-	-	-
Net income	1.40	1.45	0.94	1.53	1.71	1.17	0.65	0.66	1.00	0.17	0.62
Average shares outstanding:											
Basic	2,597	2,597	2,610	2,596	2,596	2,608	2,597	2,597	2,606	2,597	2,601
Diluted	2,624	2,624	2,642	2,623	2,623	2,640	2,624	2,624	2,638	2,626	2,632

23. Information Provided in Connection With Outstanding Debt

The following condensed consolidating financial statements are provided in compliance with Regulation S-X of the SEC.

(a) AGC is a holding company and a wholly owned subsidiary of AIG. AIG provides a full and unconditional guarantee of all outstanding debt of AGC.

AMERICAN GENERAL CORPORATION (AGC): CONDENSED CONSOLIDATING BALANCE SHEET

(in millions)	American International Group, Inc. Guarantor	AGC Issuer	Other Subsidiaries	Eliminations	Consolidated AIG
December 31, 2005					
Assets:					
Invested assets	**$ 1,392**	**$ –**	**$ 691,349**	**$ (13,696)**	**$ 679,045**
Cash	**190**	**–**	**1,707**	**–**	**1,897**
Carrying value of subsidiaries and partially owned companies, at equity	**90,723**	**27,027**	**15,577**	**(132,169)**	**1,158**
Other assets	**2,768**	**2,577**	**167,252**	**(1,327)**	**171,270**
Total assets	**$ 95,073**	**$ 29,604**	**$ 875,885**	**$ (147,192)**	**$ 853,370**
Liabilities:					
Insurance liabilities	**$ 408**	**$ –**	**$ 460,271**	**$ (56)**	**$ 460,623**
Debt	**4,607**	**2,087**	**115,212**	**(12,057)**	**109,849**
Other liabilities	**3,741**	**4,110**	**191,598**	**(3,054)**	**196,395**
Total liabilities	**8,756**	**6,197**	**767,081**	**(15,167)**	**766,867**
Preferred shareholders' equity in subsidiary companies	**–**	**–**	**186**	**–**	**186**
Total shareholders' equity	**86,317**	**23,407**	**108,618**	**(132,025)**	**86,317**
Total liabilities, preferred shareholders' equity in subsidiary companies and shareholders' equity	**$ 95,073**	**$ 29,604**	**$ 875,885**	**$ (147,192)**	**$ 853,370**
December 31, 2004					
Assets:					
Invested assets	$ 1,027	$ –	$650,238	$ (12,984)	$638,281
Cash	17	–	1,992	–	2,009
Carrying value of subsidiaries and partially owned companies, at equity	80,966	26,179	12,763	(118,413)	1,495
Other assets	2,786	2,546	154,417	(389)	159,360
Total assets	$84,796	$28,725	$819,410	$(131,786)	$801,145
Liabilities:					
Insurance liabilities	$ 405	$ –	$428,130	$ (69)	$428,466
Debt	3,647	2,482	103,027	(12,257)	96,899
Other liabilities	1,071	4,076	191,967	(1,206)	195,908
Total liabilities	5,123	6,558	723,124	(13,532)	721,273
Preferred shareholders' equity in subsidiary companies	–	–	199	–	199
Total shareholders' equity	79,673	22,167	96,087	(118,254)	79,673
Total liabilities, preferred shareholders' equity in subsidiary companies and shareholders' equity	$84,796	$28,725	$819,410	$(131,786)	$801,145

23. Information Provided in Connection With Outstanding Debt

Continued

CONDENSED CONSOLIDATING STATEMENT OF INCOME

(in millions)	American International Group, Inc. Guarantor	AGC Issuer	Other Subsidiaries	Eliminations	Consolidated AIG
Year Ended December 31, 2005					
Operating income	**$ (1,569)**	**$ (200)**	**$ 16,982**	**$ –**	**$ 15,213**
Equity in undistributed net income of consolidated subsidiaries	**10,368**	**2,530**	**–**	**(12,898)**	**–**
Dividend income from consolidated subsidiaries	**1,746**	**–**	**–**	**(1,746)**	**–**
Income taxes (benefits)	**68**	**(92)**	**4,282**	**–**	**4,258**
Minority interest	**–**	**–**	**(478)**	**–**	**(478)**
Net income (loss)	**$ 10,477**	**$ 2,422**	**$ 12,222**	**$ (14,644)**	**$ 10,477**
Year Ended December 31, 2004					
Operating income	$ 161	$ 90	$14,594	$ –	$14,845
Equity in undistributed net income of consolidated subsidiaries	8,705	2,048	–	(10,753)	–
Dividend income from consolidated subsidiaries	1,836	65	–	(1,901)	–
Income taxes (benefits)	863	31	3,513	–	4,407
Minority interest	–	–	(455)	–	(455)
Cumulative effect of an accounting change	–	–	(144)	–	(144)
Net income (loss)	$ 9,839	$2,172	$10,482	$(12,654)	$ 9,839
Year Ended December 31, 2003					
Operating income	$ (708)	$ (98)	$12,713	$ –	$11,907
Equity in undistributed net income of consolidated subsidiaries	7,708	1,804	–	(9,512)	–
Dividend income from consolidated subsidiaries	1,471	196	–	(1,667)	–
Income taxes (benefits)	363	(23)	3,216	–	3,556
Minority interest	–	–	(252)	–	(252)
Cumulative effect of an accounting change	–	–	9	–	9
Net income (loss)	$ 8,108	$1,925	$ 9,254	$(11,179)	$ 8,108

23. Information Provided in Connection With Outstanding Debt

Continued

CONDENSED CONSOLIDATING STATEMENTS OF CASH FLOW

(in millions)	American International Group, Inc. Guarantor	AGC Issuer	Other Subsidiaries	Consolidated AIG
Year Ended December 31, 2005				
Net cash provided by operating activities	**$ 1,673**	**$ 805**	**$ 22,660**	**$ 25,138**
Cash flows from investing activities:				
Invested assets disposed	**–**	**–**	**218,825**	**218,825**
Invested assets acquired	**(598)**	**–**	**(273,530)**	**(274,128)**
Other	**(1,294)**	**(247)**	**(477)**	**(2,018)**
Net cash used in investing activities	**(1,892)**	**(247)**	**(55,182)**	**(57,321)**
Cash flows from financing activities:				
Change in debts	**1,493**	**(398)**	**11,939**	**13,034**
Other	**(1,176)**	**(160)**	**21,301**	**19,965**
Net cash (used in) provided by financing activities	**317**	**(558)**	**33,240**	**32,999**
Effect of exchange rate changes on cash	**75**	**–**	**(1,003)**	**(928)**
Change in cash	**173**	**–**	**(285)**	**(112)**
Cash at beginning of year	**17**	**–**	**1,992**	**2,009**
Cash at end of year	**$ 190**	**$ –**	**$ 1,707**	**$ 1,897**
Year Ended December 31, 2004				
Net cash provided by operating activities	$ 2,732	$ 839	$ 27,145	$ 30,716
Cash flows from investing activities:				
Invested assets disposed	502	–	151,163	151,665
Invested assets acquired	(107)	–	(247,723)	(247,830)
Other	(1,039)	(408)	497	(950)
Net cash used in investing activities	(644)	(408)	(96,063)	(97,115)
Cash flows from financing activities:				
Change in debts	(400)	(349)	17,250	16,501
Other	(1,515)	(82)	51,590	49,993
Net cash (used in) provided by financing activities	(1,915)	(431)	68,840	66,494
Effect of exchange rate changes on cash	(175)	–	1,167	992
Change in cash	(2)	–	1,089	1,087
Cash at beginning of year	19	–	903	922
Cash at end of year	$ 17	$ –	$ 1,992	$ 2,009
Year Ended December 31, 2003				
Net cash provided by operating activities	$ 625	$1,376	$ 31,240	$ 33,241
Cash flows from investing activities:				
Invested assets disposed	186	–	152,054	152,240
Invested assets acquired	(830)	–	(215,092)	(215,922)
Acquisitions, net of cash acquired	–	–	(2,091)	(2,091)
Other	(842)	(926)	637	(1,131)
Net cash used in investing activities	(1,486)	(926)	(64,492)	(66,904)
Cash flows from financing activities:				
Change in debts	1,288	(376)	5,658	6,570
Other	(411)	(75)	26,986	26,500
Net cash provided by (used in) financing activities	877	(451)	32,644	33,070
Effect of exchange rate changes on cash	(15)	–	365	350
Change in cash	1	(1)	(243)	(243)
Cash at beginning of year	18	1	1,146	1,165
Cash at end of year	$ 19	$ –	$ 903	$ 922

23. Information Provided in Connection With Outstanding Debt

Continued

(b) AIG Liquidity Corp. is a wholly owned subsidiary of AIG. AIG provides a full and unconditional guarantee of all obligations of AIG Liquidity Corp., which commenced operations in 2003.

AIG LIQUIDITY CORP.: CONDENSED CONSOLIDATING BALANCE SHEET

(in millions)	American International Group, Inc. Guarantor	AIG Liquidity Corp.	Other Subsidiaries	Eliminations	Consolidated AIG
December 31, 2005					
Assets:					
Invested assets	**$ 1,392**	**$ ***	**$ 691,349**	**$ (13,696)**	**$ 679,045**
Cash	**190**	*****	**1,707**	**–**	**1,897**
Carrying value of subsidiaries and partially owned companies, at equity	**90,723**	**–**	**42,604**	**(132,169)**	**1,158**
Other assets	**2,768**	*****	**169,829**	**(1,327)**	**171,270**
Total assets	**$ 95,073**	**$ ***	**$ 905,489**	**$ (147,192)**	**$ 853,370**
Liabilities:					
Insurance liabilities	**$ 408**	**$ –**	**$ 460,271**	**$ (56)**	**$ 460,623**
Debt	**4,607**	*****	**117,299**	**(12,057)**	**109,849**
Other liabilities	**3,741**	*****	**195,708**	**(3,054)**	**196,395**
Total liabilities	**8,756**	*****	**773,278**	**(15,167)**	**766,867**
Preferred shareholders' equity in subsidiary companies	**–**	**–**	**186**	**–**	**186**
Total shareholders' equity	**86,317**	*****	**132,025**	**(132,025)**	**86,317**
Total liabilities, preferred shareholders' equity in subsidiary companies and shareholders' equity	**$ 95,073**	**$ ***	**$ 905,489**	**$ (147,192)**	**$ 853,370**
December 31, 2004					
Assets:					
Invested assets	$ 1,027	$ *	$650,238	$ (12,984)	$638,281
Cash	17	*	1,992	–	2,009
Carrying value of subsidiaries and partially owned companies, at equity	80,966	–	38,942	(118,413)	1,495
Other assets	2,786	*	156,963	(389)	159,360
Total assets	$84,796	$ *	$848,135	$(131,786)	$801,145
Liabilities:					
Insurance liabilities	$ 405	$ –	$428,130	$ (69)	$428,466
Debt	3,647	*	105,509	(12,257)	96,899
Other liabilities	1,071	*	196,043	(1,206)	195,908
Total liabilities	5,123	*	729,682	(13,532)	721,273
Preferred shareholders' equity in subsidiary companies	–	–	199	–	199
Total shareholders' equity	79,673	*	118,254	(118,254)	79,673
Total liabilities, preferred shareholders' equity in subsidiary companies and shareholders' equity	$84,796	$ *	$848,135	$(131,786)	$801,145

* *Amounts significantly less than $1 million.*

23. Information Provided in Connection With Outstanding Debt

Continued

CONDENSED CONSOLIDATING STATEMENT OF INCOME

(in millions)	American International Group, Inc. Guarantor	AIG Liquidity Corp.	Other Subsidiaries	Eliminations	Consolidated AIG
Year Ended December 31, 2005					
Operating Income	**$ (1,569)**	**$ ***	**$ 16,782**	**$ –**	**$ 15,213**
Equity in undistributed net income of consolidated subsidiaries	**10,368**	**–**	**2,530**	**(12,898)**	**–**
Dividend income from consolidated subsidiaries	**1,746**	*****	**–**	**(1,746)**	**–**
Income taxes (benefits)	**68**	**–**	**4,190**	**–**	**4,258**
Minority interest	**–**	**–**	**(478)**	**–**	**(478)**
Cumulative effect of an accounting change	**–**	**–**	**–**	**–**	**–**
Net income (loss)	**$10,477**	**$ ***	**$ 14,644**	**$ (14,644)**	**$ 10,477**
Year Ended December 31, 2004					
Operating Income	$ 161	$ *	$14,684	$ –	$14,845
Equity in undistributed net income of consolidated subsidiaries	8,705	–	2,048	(10,753)	–
Dividend income from consolidated subsidiaries	1,836	–	65	(1,901)	–
Income taxes (benefits)	863	*	3,544	–	4,407
Minority interest	–	–	(455)	–	(455)
Cumulative effect of an accounting change	–	–	(144)	–	(144)
Net income (loss)	$ 9,839	$ *	$12,654	$(12,654)	$ 9,839
Year Ended December 31, 2003					
Operating Income	$ (708)	$ *	$12,615	$ –	$11,907
Equity in undistributed net income of consolidated subsidiaries	7,708	–	1,804	(9,512)	–
Dividend income from consolidated subsidiaries	1,471	–	196	(1,667)	–
Income taxes (benefits)	363	*	3,193	–	3,556
Minority interest	–	–	(252)	–	(252)
Cumulative effect of an accounting change	–	–	9	–	9
Net income (loss)	$ 8,108	$ *	$11,179	$(11,179)	$ 8,108

* *Amounts significantly less than $1 million.*

23. Information Provided in Connection With Outstanding Debt

Continued

CONDENSED CONSOLIDATING STATEMENTS OF CASH FLOW

(in millions)	American International Group, Inc. Guarantor	AIG Liquidity Corp.	Other Subsidiaries	Consolidated AIG
Year Ended December 31, 2005				
Net cash provided by operating activities	**$ 1,673**	**$ ***	**$ 23,465**	**$ 25,138**
Cash flows from investing activities:				
Invested assets disposed	**–**	**–**	**218,825**	**218,825**
Invested assets acquired	**(598)**	**–**	**(273,530)**	**(274,128)**
Other	**(1,294)**	*****	**(724)**	**(2,018)**
Net cash used in investing activities	**(1,892)**	*****	**(55,429)**	**(57,321)**
Cash flows from financing activities:				
Change in debts	**1,493**	**–**	**11,541**	**13,034**
Other	**(1,176)**	*****	**21,141**	**19,965**
Net cash provided by financing activities	**317**	*****	**32,682**	**32,999**
Effect of exchange rate changes on cash	**75**	**–**	**(1,003)**	**(928)**
Change in cash	**173**	*****	**(285)**	**(112)**
Cash at beginning of year	**17**	**–**	**1,992**	**2,009**
Cash at end of year	**$ 190**	**$ ***	**$ 1,707**	**$ 1,897**
Year Ended December 31, 2004				
Net cash provided by operating activities	$ 2,732	$ *	$ 27,984	$ 30,716
Cash flows from investing activities:				
Invested assets disposed	502	–	151,163	151,665
Invested assets acquired	(107)	–	(247,723)	(247,830)
Other	(1,039)	*	89	(950)
Net cash used in investing activities	(644)	*	(96,471)	(97,115)
Cash flows from financing activities:				
Change in debts	(400)	–	16,901	16,501
Other	(1,515)	*	51,508	49,993
Net cash (used in) provided by financing activities	(1,915)	*	68,409	66,494
Effect of exchange rate changes on cash	(175)	–	1,167	992
Change in cash	(2)	*	1,089	1,087
Cash at beginning of year	19	–	903	922
Cash at end of year	$ 17	$ *	$ 1,992	$ 2,009
Year Ended December 31, 2003				
Net cash provided by operating activities	$ 625	$ *	$ 32,616	$ 33,241
Cash flows from investing activities:				
Invested assets disposed	186	–	152,054	152,240
Invested assets acquired	(830)	–	(215,092)	(215,922)
Acquisitions, net of cash acquired	–	–	(2,091)	(2,091)
Other	(842)	*	(289)	(1,131)
Net cash used in investing activities	(1,486)	*	(65,418)	(66,904)
Cash flows from financing activities:				
Change in debts	1,288	–	5,282	6,570
Other	(411)	*	26,911	26,500
Net cash provided by financing activities	877	*	32,193	33,070
Effect of exchange rate changes on cash	(15)	–	365	350
Change in cash	1	*	(244)	(243)
Cash at beginning of year	18	–	1,147	1,165
Cash at end of year	$ 19	$ *	$ 903	$ 922

* *Amounts significantly less than $1 million.*

ITEM 9.
Changes and Disagreements with Accountants on Accounting and Financial Disclosure

There have been no changes in accountants during the twenty-four months ended December 31, 2005.

ITEM 9A.
Controls and Procedures

Evaluation of Disclosure Controls and Procedures

In connection with the preparation of this Annual Report on Form 10-K, an evaluation was carried out by AIG's management, with the participation of AIG's Chief Executive Officer and Chief Financial Officer, of the effectiveness of AIG's disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934 (Exchange Act)) as of December 31, 2005. Disclosure controls and procedures are designed to ensure that information required to be disclosed in reports filed or submitted under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in SEC rules and forms and that such information is accumulated and communicated to management, including the Chief Executive Officer and Chief Financial Officer, to allow timely decisions regarding required disclosures.

During the evaluation of disclosure controls and procedures as of December 31, 2004 conducted during the preparation of AIG's financial statements to be included in the 2004 Form 10-K, five material weaknesses in internal control over financial reporting were identified, relating to control environment, controls over the evaluation of risk transfer, controls over certain balance sheet reconciliations, controls over the accounting for certain derivative transactions and controls over income tax accounting. As a result, AIG's new Chief Executive Officer and Chief Financial Officer concluded that, as of December 31, 2004, AIG's disclosure controls and procedures were ineffective.

Upon identification of the material weaknesses and under the direction of its Chief Executive Officer and Chief Financial Officer, AIG developed a comprehensive plan to remediate the material weaknesses.

AIG's remediation efforts were governed by a Steering Committee, under the direction of AIG's Chief Risk Officer and also including AIG's Chief Executive Officer, Chief Financial Officer, Comptroller and Senior Vice President for Strategic Planning. The status of remediation of each material weakness was reviewed with the Audit Committee and this Committee was advised of issues encountered and key decisions reached by AIG management relating to the remediation efforts.

On November 9, 2005, AIG announced that it had identified certain errors, the preponderance of which were identified during the remediation of the material weaknesses in internal control over financial reporting described above, principally relating to controls over accounting for certain derivative transactions and related assets and liabilities under FAS 133, reconciliation of certain balance sheet accounts and income tax accounting. Subsequent to that announcement, and in connection with its ongoing remediation efforts, AIG identified certain additional errors principally relating to internal controls over reconciliation of certain balance sheet accounts in the Domestic Brokerage Group. Due to the significance of these additional errors, AIG restated its consolidated financial statements and financial statement schedules for the years ended December 31, 2004, 2003 and 2002, along with 2001 and 2000 for purposes of preparation of the Selected Consolidated Financial Data for 2001 and 2000, and quarterly financial information for 2004 and 2003 and will restate the first three quarters of 2005 (the Second Restatement). AIG's September 2005 Form 10-Q will not be amended because the adjustments to correct the additional errors to the financial statements included therein are not material to those financial statements.

As of December 31, 2005 and as described under Remediation of Material Weaknesses in Internal Control Over Financial Reporting below, the material weaknesses relating to the control environment and controls over the evaluation of risk transfer were remediated, and the material weaknesses relating to controls over certain balance sheet reconciliations, controls over the accounting for certain derivative transactions and controls over income tax accounting remained, as they were not fully remediated.

As a result of these remaining material weaknesses in internal control over financial reporting, described more fully below, AIG's Chief Executive Officer and Chief Financial Officer concluded that, as of December 31, 2005, AIG's disclosure controls and procedures were ineffective.

Notwithstanding the existence of these three remaining material weaknesses, AIG believes that the consolidated financial statements in this Annual Report on Form 10-K fairly present, in all material respects, AIG's financial condition as of December 31, 2005 and 2004, and results of its operations and cash flows for the years ended December 31, 2005, 2004 and 2003, in conformity with U.S. generally accepted accounting principles (GAAP).

Management's Report on Internal Control Over Financial Reporting

Management of AIG is responsible for establishing and maintaining adequate internal control over financial reporting. AIG's internal control over financial reporting is a process, under the supervision of AIG's Chief Executive Officer and Chief Financial Officer, designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of AIG's financial statements for external purposes in accordance with GAAP.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions or that the degree of compliance with the policies or procedures may deteriorate.

AIG management conducted an assessment of the effectiveness of AIG's internal control over financial reporting as of

December 31, 2005 based on the criteria established in *Internal Control — Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO).

A material weakness is a control deficiency, or a combination of control deficiencies, that results in more than a remote likelihood that a material misstatement of AIG's annual or interim financial statements will not be prevented or detected. AIG management has concluded that, as of December 31, 2005, the following material weaknesses in internal control over financial reporting remained:

Controls over certain balance sheet reconciliations: AIG did not maintain effective controls to ensure the accuracy of certain balance sheet accounts in certain key segments of AIG's operations, principally in the Domestic Brokerage Group. Specifically, accounting personnel did not perform timely reconciliations and did not properly resolve reconciling items for premium receivables, reinsurance recoverables and intercompany accounts. As a result, premiums and other considerations, incurred policy losses and benefits, insurance acquisition and other operating expenses, premiums and insurance balances receivable, reinsurance assets, reserves for losses and loss expenses, reserve for unearned premiums, other assets and retained earnings were misstated under GAAP.

Controls over the accounting for certain derivative transactions: AIG did not maintain effective controls over the evaluation and documentation of whether certain derivative transactions qualified under GAAP for hedge accounting. As a result, net investment income, realized capital gains (losses), other revenues, accumulated other comprehensive income (loss) and related balance sheet accounts were misstated under GAAP.

Controls over income tax accounting: AIG did not maintain effective controls over the determination and reporting of certain components of the provision for income taxes and related income tax balances. Specifically, AIG did not maintain effective controls to review and monitor the accuracy of the components of the income tax provision calculations and related income tax balances and to monitor the differences between the income tax basis and the financial reporting basis of assets and liabilities to effectively reconcile the differences to the deferred income tax balances. As a result, income tax expense, income taxes payable, deferred income tax assets and liabilities, retained earnings and accumulated other comprehensive income were misstated under GAAP.

The control deficiencies described above resulted in the Second Restatement. In addition, these control deficiencies could result in other misstatements to the aforementioned financial statement accounts and disclosures that would result in a material misstatement to the annual or interim AIG consolidated financial statements that would not be prevented or detected. Accordingly, AIG management has concluded that these control deficiencies constitute material weaknesses.

As a result of the material weaknesses in internal control over financial reporting described above, AIG management has concluded that, as of December 31, 2005, AIG's internal control over financial reporting was not effective based on the criteria in *Internal Control — Integrated Framework* issued by the COSO.

Management's assessment of the effectiveness of AIG's internal control over financial reporting as of December 31, 2005 has been audited by PricewaterhouseCoopers LLP, an independent registered public accounting firm, as stated in their report, which is included in this Annual Report on Form 10-K.

Remediation of Material Weaknesses in Internal Control Over Financial Reporting

Throughout 2005 and continuing in 2006, AIG has been actively engaged in the implementation of remediation efforts to address the five material weaknesses in existence at December 31, 2004 and disclosed in its 2004 Form 10-K. These remediation efforts, outlined below, are specifically designed to address the material weaknesses identified by AIG management. As a result of its assessment of the effectiveness of internal control over financial reporting, AIG management determined that as of December 31, 2005, two material weaknesses, relating to the control environment and controls over the evaluation of risk transfer, had been remediated, and three material weaknesses, relating to the controls over certain balance sheet reconciliations, controls over the accounting for certain derivative transactions and controls over income tax accounting, had not been remediated.

Completed Remediation

Control environment: As of December 31, 2004, certain of AIG's controls within its control environment were not effective to prevent certain members of senior management, including the former Chief Executive Officer and former Chief Financial Officer, from having the ability, which in certain instances was utilized, to override certain controls and effect certain transactions and accounting entries.

AIG has taken several significant actions to improve its control environment, starting with the appointment of new senior management with a new tone and philosophy. AIG's Chief Executive Officer and Chief Financial Officer, together with other senior executives, are committed to achieving transparency and clear communication with all stakeholders through effective corporate governance, a strong control environment, high ethical standards and financial reporting integrity. To strengthen and enhance its overall financial reporting and internal control environment, AIG has increased resources for technical accounting, internal audit, enterprise risk management and compliance functions, hired additional staff with specialized financial and accounting expertise, and established stronger reporting lines within the financial reporting function.

Among the specific actions taken by AIG to remediate this material weakness and to further strengthen overall controls over financial reporting were the following:

AIG has established a Financial Disclosure Committee to assist the Chief Executive Officer and the Chief Financial Officer in fulfilling their responsibilities for oversight of the accuracy and timeliness of the disclosures made by AIG.

AIG has implemented new controls, including specific procedures with respect to post-closing adjustments and consolidating entries.

AIG has taken remedial actions with respect to certain employees in management and in the underwriting, accounting, auditing, actuarial and financial reporting functions. Such remedial actions included further training and supervision, reassignment outside areas of involvement with financial reporting, or termination. Employees identified as needing further training and supervision underwent formal ethics training and recertified their compliance with AIG's Code of Conduct.

AIG now requires that all employees complete formal ethics training developed and monitored by AIG Corporate Compliance. AIG has implemented a *Director, Executive Officer and Senior Financial Officer Code of Business Conduct and Ethics*, and requires all members of the Board of Directors, executive officers and senior financial officers to confirm that they adhere to the stated principles and procedures set forth in that Code.

AIG has strengthened the position of Chief Risk Officer, responsible for enterprise-wide credit, market, and operational risk management and oversight of the corresponding functions at the business unit level and has empowered the Chief Risk Officer to work more closely with top executives at the corporate and major business unit levels to identify, assess, quantify, manage and mitigate risks to AIG.

AIG has established an Operational Risk Management department, reporting to the Chief Risk Officer, to engage in expanded risk self-assessment processes for more effective identification and management of operational and reputational risks.

The AIG Board of Directors has established the Regulatory, Compliance and Legal Committee to provide oversight of AIG's compliance with applicable laws and regulations. AIG's Chief Compliance Officer, who reports directly to this Committee, has implemented a corporate level, centrally-managed compliance function and developed a compliance framework, within which AIG is implementing consistent compliance policies and procedures for all major business units.

AIG has expanded the scope and activities of the corporate level Complex Structured Finance Transaction Committee, to review and approve transactions that could subject AIG to heightened legal, reputational, regulatory or other risk or enable a third party to achieve an accounting or financial reporting result inconsistent with applicable accounting principles, to include the review and approval of AIG's accounting and financial reporting of identified transactions, including related party transactions. Also, AIG's major business units have implemented their own committees and processes to enhance their ability to identify, analyze and present for approval complex structured finance transactions to AIG's corporate level committee.

Although AIG continues to develop further enhancements to its control environment, based upon the significant actions taken, as listed above, and the testing and evaluation of the effectiveness of the controls, AIG management has concluded that remediation of the material weakness in AIG's control environment has been achieved as of December 31, 2005.

Controls over the evaluation of risk transfer: As of December 31, 2004, AIG did not maintain effective controls over the proper evaluation, documentation and disclosure of whether certain insurance and reinsurance transactions in the General Insurance segment involved sufficient risk transfer to qualify for insurance and reinsurance accounting.

To remediate this material weakness, AIG has developed a formal risk transfer policy for direct insurance, assumed reinsurance and ceded reinsurance in the General Insurance segment. This policy establishes guidelines for the assessment by the underwriting, and if appropriate, actuarial functions, of the adequacy of risk transfer to support insurance accounting, and requires that appropriate documentation of the assessment be provided to the accounting function to allow proper accounting for the transaction.

AIG has also established procedures to incorporate risk transfer assessments into its underwriting and financial audit processes. Although AIG continues to refine and enhance its controls over the evaluation of risk transfer, including developing a process for updating the risk transfer policy to reflect changes in accounting pronouncements, based upon the significant actions taken, as listed above, and the testing and evaluation of the effectiveness of the controls, AIG management has concluded that remediation of this material weakness has been achieved as of December 31, 2005.

Continuing Remediation

AIG has devoted significant efforts towards remediation of its three remaining material weaknesses, and remediation of AIG's control environment has aided in these efforts. Nonetheless, these material weaknesses are not yet fully remediated as of December 31, 2005. AIG management continues to assign the highest priority to AIG's remediation efforts in these areas, with the goal of remediating these material weaknesses by year-end 2006. However, due to the nature of the remediation process and the need to allow adequate time after implementation to evaluate and test the effectiveness of the controls, no assurance can be given as to the timing of achievement of remediation. AIG recognizes that further improvement in its internal control over financial reporting and consolidation processes is essential. Over time, AIG intends to reduce its reliance on the utilization of consultants to supplement current resources and the manual controls that have been established. As part of its remediation efforts, AIG intends to develop new systems and processes which will allow it to rely on front end preventative controls which will be more sustainable over the long term. AIG recognizes that to accomplish its goals, further strengthening and investment are needed in accounting and tax personnel, as well as in systems and processes. AIG is committed to making the investments necessary to make these improvements.

AIG has taken specific remediation steps with respect to its three remaining material weaknesses.

Controls over certain balance sheet reconciliations: AIG has implemented the following measures to enhance its ability to

identify, assess, measure and help to ensure the accuracy of its balance sheet accounts:

- adoption and implementation of new corporate guidelines on balance sheet reconciliations;
- implementation of new programs to train staff on the requirements of the new guidelines;
- enhancement of the oversight of the balance sheet reconciliation function by adding qualified staff and engaging outside resources; and
- enhancement of processes for evaluating and monitoring financial statement exposures related to balance sheet reconciliations.

AIG's remediation efforts during 2005 with respect to its controls over certain balance sheet reconciliations identified additional errors, contributing to the Second Restatement. Thus, AIG management believes that full remediation has not yet been achieved.

Controls over the accounting for certain derivative transactions: AIG has taken the following actions to remediate this material weakness:

- enhancement of systems and implementation of new controls over the accounting for derivatives and related assets and liabilities;
- implementation of new procedures and controls to ensure technical compliance with the provisions of FAS 133, including specific documentation requirements, prior to application of hedge accounting by AIG subsidiaries; and
- establishment of improved oversight, monitoring and supervision of derivative accounting issues in part, through the hiring of additional personnel with expertise in FAS 133.

AIG's remediation efforts with respect to its controls over the accounting for certain derivative transactions resulted in identification of previously undetected errors that contributed to the Second Restatement. Thus, AIG management believes that full remediation has not yet been achieved, and testing will continue to ensure that processes and controls over the accounting for derivative transactions are operating effectively before hedge accounting is applied again.

Controls over income tax accounting: AIG has taken the following actions to remediate this material weakness:

- implementation of new controls over its accounting for income taxes;
- enhancement of its oversight over income tax accounting through hiring of additional qualified staff;
- engagement of an outside accounting firm to assist in the analysis of its income tax accounting; and
- enhancement of processes for evaluating and monitoring financial statement exposure related to income tax accounting.

AIG's remediation efforts during 2005 with respect to its controls over income tax accounting identified additional errors, contributing to the Second Restatement. Thus, AIG management believes that remediation has not yet been achieved.

Changes in Internal Control Over Financial Reporting

Changes in AIG's internal control over financial reporting during the quarter ended December 31, 2005 that have materially affected, or are reasonably likely to materially affect, AIG's internal control over financial reporting have been described above.

ITEM 9B.
Other Information

On March 15, 2006, AIG adopted the AIG Partners Plan and amendments to the AIG Senior Partners Plan. In addition, AIG adopted amendments to its by-laws. The aforementioned compensation plans and AIG's amended and restated by-laws are filed as exhibits to this Annual Report on Form 10-K and are incorporated by reference into this Item 9B.

Part III

ITEM 10.
Directors and Executive Officers of the Registrant

Except for the information provided in Part I under the heading "Directors and Executive Officers of the Registrant", this item, including information regarding AIG's audit committee and audit committee financial expert and information relating to AIG's code of ethics that applies to its directors, executive officers and senior financial officers, is omitted because a definitive proxy statement which involves the election of directors will be filed with the SEC not later than 120 days after the close of the fiscal year pursuant to Regulation 14A.

ITEM 11.
Executive Compensation

This item is omitted because a definitive proxy statement which involves the election of directors will be filed with the SEC not later than 120 days after the close of the fiscal year pursuant to Regulation 14A.

ITEM 12.
Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters

This item is omitted because a definitive proxy statement which involves the election of directors will be filed with the SEC not later than 120 days after the close of the fiscal year pursuant to Regulation 14A.

ITEM 13.
Certain Relationships and Related Transactions

This item is omitted because a definitive proxy statement which involves the election of directors will be filed with the SEC not later than 120 days after the close of the fiscal year pursuant to Regulation 14A.

ITEM 14.
Principal Accountant Fees and Services

This item is omitted because a definitive proxy statement which involves the election of directors will be filed with the SEC not later than 120 days after the close of the fiscal year pursuant to Regulation 14A.

PART IV

ITEM 15.
Exhibits and Financial Statement Schedules

(a) Financial Statements and Schedules. See accompanying Index to Financial Statements.

(b) Exhibits. See accompanying Exhibit Index.

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, as amended, the Registrant has duly caused this Annual Report on Form 10-K to be signed on its behalf by the undersigned, thereunto duly authorized, in the City of New York and State of New York, on the 16th of March, 2006.

AMERICAN INTERNATIONAL GROUP, INC.

By /s/ MARTIN J. SULLIVAN
(Martin J. Sullivan, President and Chief Executive Officer)

KNOW ALL PERSONS BY THESE PRESENTS, that each person whose signature appears below constitutes and appoints Martin J. Sullivan and Steven J. Bensinger, and each of them severally, his or her true and lawful attorney-in-fact, with full power of substitution and resubstitution, to sign in his or her name, place and stead, in any and all capacities, to do any and all things and execute any and all instruments that such attorney may deem necessary or advisable under the Securities Exchange Act of 1934, as amended, and any rules, regulations and requirements of the U.S. Securities and Exchange Commission in connection with this Annual Report on Form 10-K and any and all amendments hereto, as fully for all intents and purposes as he or she might or could do in person, and hereby ratifies and confirms all said attorneys-in-fact and agents, each acting alone, and his or her substitute or substitutes, may lawfully do or cause to be done by virtue hereof.

Pursuant to the requirements of the Securities Exchange Act of 1934, as amended, this Annual Report on Form 10-K has been signed below by the following persons in the capacities indicated on the 16th of March, 2006.

Signature	Title
/s/ MARTIN J. SULLIVAN (Martin J. Sullivan)	President, Chief Executive Officer and Director (Principal Executive Officer)
/s/ STEVEN J. BENSINGER (Steven J. Bensinger)	Executive Vice President and Chief Financial Officer (Principal Financial Officer)
/s/ DAVID L. HERZOG (David L. Herzog)	Senior Vice President and Comptroller (Principal Accounting Officer)
/s/ M. BERNARD AIDINOFF (M. Bernard Aidinoff)	Director
/s/ PEI-YUAN CHIA (Pei-yuan Chia)	Director
/s/ MARSHALL A. COHEN (Marshall A. Cohen)	Director
/s/ WILLIAM S. COHEN (William S. Cohen)	Director
/s/ MARTIN S. FELDSTEIN (Martin S. Feldstein)	Director

Signature	Title
/s/ Ellen V. Futter (Ellen V. Futter)	Director
/s/ Stephen L. Hammerman (Stephen L. Hammerman)	Director
/s/ Carla A. Hills (Carla A. Hills)	Director
/s/ Richard C. Holbrooke (Richard C. Holbrooke)	Director
/s/ Fred H. Langhammer (Fred H. Langhammer)	Director
/s/ George L. Miles, Jr. (George L. Miles, Jr.)	Director
/s/ Morris W. Offit (Morris W. Offit)	Director
/s/ Michael H. Sutton (Michael H. Sutton)	Director
/s/ Edmund S.W. Tse (Edmund S.W. Tse)	Director
/s/ Robert B. Willumstad (Robert B. Willumstad)	Director
/s/ Frank G. Zarb (Frank G. Zarb)	Director

Exhibit Index

Exhibit Number	Description	Location
2	Plan of acquisition, reorganization, arrangement, liquidation or succession	
	Agreement and Plan of Merger, dated as of May 11, 2001, among American International Group, Inc., Washington Acquisition Corporation and American General Corporation	Incorporated by reference to Exhibit 2.1(i)(a) to AIG's Registration Statement on Form S-4 (File No. 333-62688).
3(i)(a)	Restated Certificate of Incorporation of AIG	Incorporated by reference to Exhibit 3(i) to AIG's Annual Report on Form 10-K for the year ended December 31, 1996 (File No. 1-8787).
3(i)(b)	Certificate of Amendment of Certificate of Incorporation of AIG, filed June 3, 1998	Incorporated by reference to Exhibit 3(i) to AIG's Quarterly Report on Form 10-Q for the quarter ended June 30, 1998 (File No. 1-8787).
3(i)(c)	Certificate of Merger of SunAmerica Inc. with and into AIG, filed December 30, 1998 and effective January 1, 1999	Incorporated by reference to Exhibit 3(i) to AIG's Annual Report on Form 10-K for the year ended December 31, 1998 (File No. 1-8787).
3(i)(d)	Certificate of Amendment of Certificate of Incorporation of AIG, filed June 5, 2000	Incorporated by reference to Exhibit 3(i)(c) to AIG's Registration Statement on Form S-4 (File No. 333-45828).
3(ii)	Amended and Restated By-laws of AIG	Filed herewith.
4	Instruments defining the rights of security holders, including indentures	Certain instruments defining the rights of holders of long-term debt securities of AIG and its subsidiaries are omitted pursuant to Item 601(b)(4)(iii) of Regulation S-K. AIG hereby undertakes to furnish to the Commission, upon request, copies of any such instruments.
9	Voting Trust Agreement	None.
10	Material contracts*	
	(1) AIG 1969 Employee Stock Option Plan and Agreement Form	Filed as exhibit to AIG's Registration Statement (File No. 2-44043) and incorporated herein by reference.
	(2) AIG 1972 Employee Stock Option Plan	Filed as exhibit to AIG's Registration Statement (File No. 2-44702) and incorporated herein by reference.
	(3) AIG 1972 Employee Stock Purchase Plan	Filed as exhibit to AIG's Registration Statement (File No. 2-44043) and incorporated herein by reference.
	(4) AIG 1984 Employee Stock Purchase Plan	Filed as exhibit to AIG's Registration Statement (File No. 2-91945) and incorporated herein by reference.
	(5) AIG Amended and Restated 1996 Employee Stock Purchase Plan	Filed as exhibit to AIG's Definitive Proxy Statement dated April 4, 2003 (File No. 1-8787) and incorporated herein by reference.
	(6) AIG 2003 Japan Employee Stock Purchase Plan	Incorporated by reference to Exhibit 4 to AIG's Registration Statement on Form S-8 (File No. 333-111737).
	(7) AIG 1977 Stock Option and Stock Appreciation Rights Plan	Filed as exhibit to AIG's Registration Statement (File No. 2-59317) and incorporated herein by reference.
	(8) AIG 1982 Employee Stock Option Plan	Filed as exhibit to AIG's Registration Statement (File No. 2-78291) and incorporated herein by reference.
	(9) AIG 1987 Employee Stock Option Plan	Filed as exhibit to AIG's Definitive Proxy Statement dated April 6, 1987 (File No. 0-4652) and incorporated herein by reference.
	(10) AIG 1991 Employee Stock Option Plan	Filed as exhibit to AIG's Definitive Proxy Statement dated April 4, 1997 (File No. 1-8787) and incorporated herein by reference.
	(11) AIG Amended and Restated 1999 Stock Option Plan	Filed as exhibit to AIG's Definitive Proxy Statement dated April 4, 2003 (File No. 1-8787) and incorporated herein by reference.

* *All material contracts are management contracts or compensatory plans or arrangements, except items (68), (69), (70) and (71).*

Exhibit Number		Description	Location
	(12)	Form of Stock Option Grant Agreement under the AIG Amended and Restated 1999 Stock Option Plan	Incorporated by reference to Exhibit 10(a) to AIG's Quarterly Report on Form 10-Q for the quarter ended September 30, 2004 (File No. 1-8787).
	(13)	AIG Amended and Restated 2002 Stock Incentive Plan	Incorporated by reference to Exhibit 4(a) to AIG's Registration Statement on Form S-8 (File No. 333-101967).
	(14)	Form of Restricted Stock Unit Award Agreement under the AIG Amended and Restated 2002 Stock Incentive Plan	Incorporated by reference to Exhibit 10(b) to AIG's Quarterly Report on Form 10-Q for the quarter ended September 30, 2004 (File No. 1-8787).
	(15)	AIG Executive Deferred Compensation Plan	Incorporated by reference to Exhibit 4(a) to AIG's Registration Statement on Form S-8 (File No. 333-101640).
	(16)	AIG Supplemental Incentive Savings Plan	Incorporated by reference to Exhibit 4(b) to AIG's Registration Statement on Form S-8 (File No. 333-101640).
	(17)	AIG Director Stock Plan	Filed as an exhibit to AIG's Definitive Proxy Statement dated April 5, 2004 (File No. 1-8787) and incorporated herein by reference.
	(18)	AIG Chief Executive Officer Annual Compensation Plan	Filed as an exhibit to AIG's Definitive Proxy Statement dated April 5, 2004 (File No. 1-8787) and incorporated herein by reference.
	(19)	AIRCO 1972 Employee Stock Option Plan	Incorporated by reference to AIG's Joint Proxy Statement and Prospectus (File No. 2-61994).
	(20)	AIRCO 1977 Stock Option and Stock Appreciation Rights Plan	Incorporated by reference to AIG's Joint Proxy Statement and Prospectus (File No. 2-61994).
	(21)	Purchase Agreement between AIA and Mr. E.S.W. Tse.	Incorporated by reference to Exhibit 10(l) to AIG's Annual Report on Form 10-K for the year ended December 31, 1997 (File No. 1-8787).
	(22)	Retention and Employment Agreement between AIG and Jay S. Wintrob	Incorporated by reference to Exhibit 10(m) to AIG's Annual Report on Form 10-K for the year ended December 31, 1998 (File No. 1-8787).
	(23)	SunAmerica Inc. 1988 Employee Stock Plan	Incorporated by reference to Exhibit 4(a) to AIG's Registration Statement on Form S-8 (File No. 333-70069).
	(24)	SunAmerica 1997 Employee Incentive Stock Plan	Incorporated by reference to Exhibit 4(b) to AIG's Registration Statement on Form S-8 (File No. 333-70069).
	(25)	SunAmerica Nonemployee Directors' Stock Option Plan	Incorporated by reference to Exhibit 4(c) to AIG's Registration Statement on Form S-8 (File No. 333-70069).
	(26)	SunAmerica 1995 Performance Stock Plan	Incorporated by reference to Exhibit 4(d) to AIG's Registration Statement on Form S-8 (File No. 333-70069).
	(27)	SunAmerica Inc. 1998 Long-Term Performance-Based Incentive Plan For the Chief Executive Officer	Incorporated by reference to Exhibit 4(e) to AIG's Registration Statement on Form S-8 (File No. 333-70069).
	(28)	SunAmerica Inc. Long-Term Performance-Based Incentive Plan Amended and Restated 1997	Incorporated by reference to Exhibit 4(f) to AIG's Registration Statement on Form S-8 (File No. 333-70069).
	(29)	SunAmerica Five Year Deferred Cash Plan	Incorporated by reference to Exhibit 4(a) to AIG's Registration Statement on Form S-8 (File No. 333-31346).
	(30)	SunAmerica Executive Savings Plan	Incorporated by reference to Exhibit 4(b) to AIG's Registration Statement on Form S-8 (File No. 333-31346).
	(31)	HSB Group, Inc. 1995 Stock Option Plan	Incorporated by reference to Exhibit 10(iii)(f) to HSB's Annual Report on Form 10-K for the year ended December 31, 1999 (File No. 1-13135).
	(32)	HSB Group, Inc. 1985 Stock Option Plan	Incorporated by reference to Exhibit 10(iii)(a) HSB's Quarterly Report on Form 10-Q for the quarter ended September 30, 1998 (File No. 1-13135).

Exhibit Number	Description	Location
(33)	HSB Group, Inc. Employee's Thrift Incentive Plan	Incorporated by reference to Exhibit 4(i)(c) to The Hartford Steam Boiler Inspection and Insurance Company's Registration Statement on Form S-8 (File No. 33-36519).
(34)	American General Corporation 1984 Stock and Incentive Plan	Incorporated by reference to Exhibit 10.1 to American General Corporation's Quarterly Report on Form 10-Q for the quarter ended June 30, 1998 (File No. 1-7981).
(35)	Amendment to American General Corporation 1984 Stock and Incentive Plan (January 2000)	Incorporated by reference to Exhibit 10.2 to American General Corporation's Annual Report on Form 10-K for the year ended December 31, 1999 (File No. 1-7981).
(36)	American General Corporation 1994 Stock and Incentive Plan (January 2000)	Incorporated by reference to Exhibit 10.2 to American General Corporation's Quarterly Report on Form 10-Q for the quarter ended June 30, 1998 (File No. 1-7981).
(37)	Amendment to American General Corporation 1994 Stock and Incentive Plan (January 1999)	Incorporated by reference to Exhibit 10.4 to American General Corporation's Annual Report on Form 10-K for the year ended December 31, 1999 (File No. 1-7981).
(38)	Amendment to American General Corporation 1994 Stock and Incentive Plan (January 2000)	Incorporated by reference to Exhibit 10.5 to American General Corporation's Annual Report on Form 10-K for the year ended December 31, 1999 (File No. 1-7981).
(39)	Amendment to American General Corporation 1994 Stock and Incentive Plan (November 2000)	Incorporated by reference to Exhibit 10.1 to American General Corporation's Quarterly Report on Form 10-Q for the quarter ended September 30, 2000 (File No. 1-7981).
(40)	American General Corporation 1997 Stock and Incentive Plan	Incorporated by reference to Exhibit 10.3 to American General Corporation's Quarterly Report on Form 10-Q for the quarter ended June 30, 1998 (File No. 1-7981).
(41)	Amendment to American General Corporation 1997 Stock and Incentive Plan (January 1999)	Incorporated by reference to Exhibit 10.7 to American General Corporation's Annual Report on Form 10-K for the year ended December 31, 1999 (File No. 1-7981).
(42)	Amendment to American General Corporation 1997 Stock and Incentive Plan (November 2000)	Incorporated by reference to Exhibit 10.2 to American General Corporation's Quarterly Report on Form 10-Q for the quarter ended September 30, 2000 (File No. 1-7981).
(43)	American General Corporation 1999 Stock and Incentive Plan	Incorporated by reference to Exhibit 10.4 to American General Corporation's Annual Report on Form 10-K for the year ended December 31, 1998 (File No. 1-7981).
(44)	Amendment to American General Corporation 1999 Stock and Incentive Plan (January 1999)	Incorporated by reference to Exhibit 10.9 to American General Corporation's Annual Report on Form 10-K for the year ended December 31, 1999 (File No. 1-7981).
(45)	Amendment to American General Corporation 1999 Stock and Incentive Plan (November 2000)	Incorporated by reference to Exhibit 10.3 to American General Corporation's Quarterly Report on Form 10-Q for the quarter ended September 30, 2000 (File No. 1-7981).
(46)	Amended and Restated American General Corporation Deferred Compensation Plan (12/11/00)	Incorporated by reference to Exhibit 10.13 to American General Corporation's Annual Report on Form 10-K for the year ended December 31, 2000 (File No. 1-7981).
(47)	Amended and Restated Restoration of Retirement Income Plan for Certain Employees Participating in the Restated American General Retirement Plan (Restoration of Retirement Income Plan) (12/31/98)	Incorporated by reference to Exhibit 10.14 to American General Corporation's Annual Report on Form 10-K for the year ended December 31, 2000 (File No. 1-7981).
(48)	Amended and Restated American General Supplemental Thrift Plan (12/31/98)	Incorporated by reference to Exhibit 10.15 to American General Corporation's Annual Report on Form 10-K for the year ended December 31, 2000 (File No. 1-7981).
(49)	American General Employees' Thrift and Incentive Plan (restated July 1, 2001)	Incorporated by reference to Exhibit 4(a) to AIG's Registration Statement on Form S-8 (File No. 333-68640).
(50)	American General Agents' and Managers' Thrift and Incentive Plan (restated July 1, 2001)	Incorporated by reference to Exhibit 4(b) to AIG's Registration Statement on Form S-8 (File No. 333-68640).
(51)	CommLoCo Thrift Plan (restated July 1, 2001)	Incorporated by reference to Exhibit 4(c) to AIG's Registration Statement on Form S-8 (File No. 333-68640).
(52)	Western National Corporation 1993 Stock and Incentive Plan, as amended	Incorporated by reference to Exhibit 10.18 to Western National Corporation's Annual Report on Form 10-K for the year ended December 31, 1995 (File No. 1-12540).
(53)	USLIFE Corporation 1991 Stock Option Plan, as amended	Incorporated by reference to USLIFE Corporation's Quarterly Report on Form 10-Q for the quarter ended September 30, 1995 (File No. 1-5683).

Exhibit Number	Description	Location
(54)	Employment Agreement, Amendment to Employment Agreement, and Split-Dollar Agreement, including Assignment of Life Insurance Policy as Collateral, with Rodney O. Martin, Jr.	Incorporated by reference to Exhibit 10(xx) to AIG's Annual Report on Form 10-K for the year ended December 31, 2002 (File No. 1-8787).
(55)	Employment Arrangements with Richard W. Scott	
	(a) Employment Agreement	Incorporated by reference to Exhibit 10.3 to American General Corporation's Quarterly Report on Form 10-Q for the quarter ended March 31, 2000 (File No. 1-7981).
	(b) Change in Control Severance Agreement	Incorporated by reference to Exhibit 10.32 to American General Corporation's Annual Report on Form 10-K for the year ended December 31, 1999 (File No. 1-7981).
	(c) Amendment to Employment Arrangements	Incorporated by reference to Exhibit 10(zz)(iii) to AIG's Annual Report on Form 10-K for the year ended December 31, 2003 (File No. 1-8787.)
(56)	Letter from AIG to Martin J. Sullivan, dated March 16, 2005	Incorporated by reference to Exhibit 10.1 to AIG's Current Report on Form 8-K filed with the SEC on March 17, 2005 (File No. 1-8787).
(57)	Letter from AIG to Donald P. Kanak, dated March 16, 2005	Incorporated by reference to Exhibit 10.2 to AIG's Current Report on Form 8-K filed with the SEC on March 17, 2005 (File No. 1-8787).
(58)	Letter from AIG to Steven J. Bensinger, dated March 16, 2005.	Incorporated by reference to Exhibit 10.3 to AIG's Current Report on Form 8-K filed with the SEC on March 17, 2005 (File No. 1-8787).
(59)	Employment Agreement between AIG and Martin J. Sullivan, dated as of June 27, 2005	Incorporated by reference to Exhibit 10(1) to AIG's Quarterly Report on Form 10-Q for the quarter ended March 31, 2005 (File No. 1-8787).
(60)	Employment Agreement between AIG and Donald P. Kanak, dated as of June 27, 2005	Incorporated by reference to Exhibit 10(2) to AIG's Quarterly Report on Form 10-Q for the quarter ended March 31, 2005 (File No. 1-8787).
(61)	Employment Agreement between AIG and Steven J. Bensinger, dated as of June 27, 2005	Incorporated by reference to Exhibit 10(3) to AIG's Quarterly Report on Form 10-Q for the quarter ended March 31, 2005 (File No. 1-8787).
(62)	Executive Severance Plan, effective as of June 27, 2005	Incorporated by reference to Exhibit 10(4) to AIG's Quarterly Report on Form 10-Q for the quarter ended March 31, 2005 (File No. 1-8787).
(63)	Assurance Agreement, by AIG in favor of eligible employees dated as of June 27, 2005, relating to certain obligations of C.V. Starr & Co., Inc.	Incorporated by reference to Exhibit 10(5) to AIG's Quarterly Report on Form 10-Q for the quarter ended March 31, 2005 (File No. 1-8787).
(64)	2005/2006 Deferred Compensation Profit Participation Plan	Incorporated by reference to Exhibit 10.1 to AIG's Current Report on Form 8-K filed with the SEC on September 26, 2005 (File No. 1-8787).
(65)	Summary of Director Compensation	Incorporated by reference to Exhibit 10.1 to AIG's Current Report on Form 8-K filed with the SEC on November 22, 2005 (File No. 1-8787).
(66)	AIG 2005 Senior Partners Plan	Incorporated by reference to Exhibit 10.1 to AIG's Current Report on Form 8-K filed with the SEC on December 20, 2005 (File No. 1-8787).
(67)	AIG Special Restricted Stock Unit Award Agreement with Steven J. Bensinger, dated January 6, 2006	Incorporated by reference to Exhibit 10.1 to AIG's Current Report on Form 8-K filed with the SEC on January 9, 2006 (File No. 1-8787).
(68)	Agreement with the United States Department of Justice, dated February 7, 2006	Incorporated by reference to Exhibit 10.1 to AIG's Current Report on Form 8-K filed with the SEC on February 9, 2006 (File No. 1-8787).
(69)	Final Judgment and Consent with the Securities and Exchange Commission, including the related complaint dated February 9, 2006	Incorporated by reference to Exhibit 10.2 to AIG's Current Report on Form 8-K filed with the SEC on February 9, 2006 (File No. 1-8787).
(70)	Agreement between the Attorney General of the State of New York and AIG and its Subsidiaries, dated January 18, 2006	Incorporated by reference to Exhibit 10.3 to AIG's Current Report on Form 8-K filed with the SEC on February 9, 2006 (File No. 1-8787).

Exhibit Number	Description	Location
	(71) Stipulation with the State of New York Insurance Department, dated January 18, 2006	Incorporated by reference to Exhibit 10.4 to AIG's Current Report on Form 8-K filed with the SEC on February 9, 2006 (File No. 1-8787).
	(72) AIG Senior Partners Plan (amended and restated)	Filed herewith.
	(73) AIG Partners Plan	Filed herewith.
11	Statement re computation of per share earnings	Included in Note 1(dd) of Notes to Consolidated Financial Statements.
12	Statements re computation of ratios	Filed herewith.
13	Annual report to security holders	Not required to be filed.
16	Letter re change in certifying accountant	None.
18	Letter re change in accounting principles	None.
21	Subsidiaries of the Registrant	Filed herewith.
23	Consent of PricewaterhouseCoopers LLP	Filed herewith.
24	Power of attorney	Included on the signature page hereof.
31	Rule 13a-14(a)/15d-14(a) Certifications	Filed herewith.
32	Section 1350 Certifications	Filed herewith.
99	Additional exhibits	None.

Computation of Ratios of Earnings to Fixed Charges

Exhibit 12

Years Ended December 31, *(in millions, except ratios)*	**2005**	2004	2003	2002	2001
Income before income taxes, minority interest and cumulative effect of accounting changes	**$15,213**	$14,845	$11,907	$ 7,808	$ 5,917
Less – Equity income of less than 50% owned persons	**(129)**	164	146	168	14
Add – Dividends from less than 50% owned persons	**146**	22	13	13	2
	15,488	14,703	11,774	7,653	5,905
Add – Fixed charges	**7,663**	6,049	5,762	4,893	5,695
Less – Capitalized interest	**64**	59	52	61	71
Income before income taxes, minority interest, cumulative effect of accounting changes and fixed charges	**$23,087**	$20,693	$17,484	$12,485	$11,529
Fixed charges:					
Interest costs	**$ 7,464**	$ 5,860	$ 5,588	$ 4,725	$ 5,538
Rental expense*	**199**	189	174	168	157
Total fixed charges	**$ 7,663**	$ 6,049	$ 5,762	$ 4,893	$ 5,695
Ratio of earnings to fixed charges	**3.01**	3.42	3.03	2.55	2.02
Secondary Ratio					
Interest credited to GIC and GIA policy and contract holders	**$ (4,760)**	$ (3,674)	$ (3,578)	$ (2,702)	$ (3,196)
Total fixed charges excluding interest credited to GIC and GIA policy and contract holders	**$ 2,903**	$ 2,375	$ 2,184	$ 2,191	$ 2,499
Secondary ratio of earnings to fixed charges	**6.31**	7.17	6.37	4.47	3.33

* *The proportion deemed representative of the interest factor.*

The secondary ratio is disclosed for the convenience of fixed income investors and the rating agencies that serve them and is more comparable to the ratios disclosed by all issuers of fixed income securities. The secondary ratio removes interest credited to guaranteed investment contract (GIC) policyholders and guaranteed investment agreement (GIA) contractholders. Such expenses are also removed from earnings used in this calculation. GICs and GIAs are entered into by AIG's insurance subsidiaries, principally SunAmerica Life Insurance Company and AIG Financial Products Corp. and its subsidiaries, respectively. The proceeds from GICs and GIAs are invested in a diversified portfolio of securities, primarily investment grade bonds. The assets acquired yield rates greater than the rates on the related policyholders obligation or contract, with the intent of earning a profit from the spread.

Subsidiaries of Registrant

Exhibit 21

	Jurisdiction of Incorporation or Organization	Percentage of Voting Securities Owned by its Immediate Parent[2]
American International Group, Inc. (Registrant)[1]	Delaware	[3]
AIG Aviation, Inc.	Georgia	100
AIG Bulgaria Insurance and Reinsurance Company EAD	Bulgaria	100
AIG Capital Corporation	Delaware	100
AIG Consumer Finance Group, Inc.	Delaware	100
AIG Bank Polska S.A.	Poland	99.92
AIG Credit S.A.	Poland	100
Compania Financiera Argentina S.A.	Argentina	100
AIG Equipment Finance Holdings, Inc.	Delaware	100
AIG Commercial Equipment Finance, Inc.	Delaware	100
AIG Commercial Equipment Finance Company, Canada	Canada	100
AIG Finance Holdings, Inc.	New York	100
AIG Finance (Hong Kong) Limited	Hong Kong	100
AIG Global Asset Management Holdings Corp.	Delaware	100
AIG Asset Management Services, Inc.	Delaware	100
Brazos Capital Management, L.P.	Delaware	92
AIG Capital Partners, Inc.	Delaware	100
AIG Equity Sales Corp.	New York	100
AIG Global Investment Corp.	New Jersey	100
AIG Global Securities Lending Corp.	Delaware	100
International Lease Finance Corporation	California	67.23[4]
AIG Global Real Estate Investment Corp.	Delaware	100
AIG Credit Corp.	Delaware	100
A.I. Credit Consumer Discount Corp.	Pennsylvania	100
A.I. Credit Corp.	New Hampshire	100
AICCO, Inc.	Delaware	100
AICCO, Inc.	California	100
AIG Credit Corp. of Canada	Canada	100
Imperial Premium Funding, Inc.	Delaware	100
AIG Egypt Insurance Company, S.A.E.	Egypt	89.98
AIG Federal Savings Bank	U.S.A.	100
AIG Financial Advisor Services, Inc.	Delaware	100
AIG Financial Advisor Services (Europe), S.A.	Luxembourg	100
AIG Financial Products Corp.	Delaware	100
AIG Matched Funding Corp.	Delaware	100
Banque AIG	France	90[5]
AIG Funding, Inc.	Delaware	100
AIG Global Trade & Political Risk Insurance Company	New Jersey	100
A.I.G. Golden Insurance Ltd.	Israel	50.01
AIG Life Holdings (International) LLC	Delaware	100
American International Reinsurance Company, Ltd.	Bermuda	100
AIG Edison Life Insurance Company	Japan	90[6]
American International Assurance Company, Limited	Hong Kong	100
American International Assurance Company (Australia) Limited	Australia	100
American International Assurance Company (Bermuda) Limited	Bermuda	100
American International Assurance Co. (Vietnam) Limited	Vietnam	100
Tata AIG Life Insurance Company Limited	India	26
Nan Shan Life Insurance Company, Ltd.	Taiwan	95
AIG Life Insurance Company	Delaware	79[7]
AIG Life Insurance Company of Puerto Rico	Puerto Rico	100
AIG Liquidity Corp.	Delaware	100
AIG Marketing, Inc.	Delaware	100
AIG Private Bank Ltd.	Switzerland	100

Subsidiaries of Registrant *Continued*

	Jurisdiction of Incorporation or Organization	Percentage of Voting Securities Owned by its Immediate Parent[2]
AIG Retirement Services, Inc.	Delaware	100[8]
SunAmerica Life Insurance Company	Arizona	100
SunAmerica Investments, Inc.	Georgia	70[9]
AIG Advisor Group, Inc.	Maryland	100
Advantage Capital Corporation	New York	100
FSC Securities Corporation	Delaware	100
Royal Alliance Associates, Inc.	Delaware	100
Sentra Securities Corporation	California	100
Spelman & Co., Inc.	California	100
SunAmerica Securities, Inc.	Delaware	100
AIG SunAmerica Life Assurance Company	Arizona	100[10]
AIG SunAmerica Asset Management Corp.	Delaware	100
AIG SunAmerica Capital Services, Inc.	Delaware	100
First SunAmerica Life Insurance Company	New York	100
AIG Risk Management, Inc.	New York	100
AIG Technologies, Inc.	New Hampshire	100
AIGTI, Inc.	Delaware	100
AIG Trading Group Inc.	Delaware	100
AIG International, Inc.	Delaware	100
AIU Holdings, LLC	Delaware	100
AIG Central Europe & CIS Insurance Holdings Corporation	Delaware	100
AIG Bulgaria Insurance and Reinsurance Company EAD	Bulgaria	100
AIG Czech Republic pojistovna, as	Czech Republic	100
AIG Kazakhstan Insurance Company, S.A.	Kazakhstan	88.87
AIU Africa Holdings, Inc.	Delaware	100
AIG Kenya Insurance Company, Limited	Kenya	100
AIG Memsa, Inc.	Delaware	100
AIG Iraq	Delaware	100
AIG Lebanon, S.A.L.	Lebanon	100
AIG Libya, Inc.	Delaware	100
AIG Hayleys Investment Holdings (Private) Ltd.	Sri Lanka	80
Hayleys AIG Insurance Company, Ltd.	Sri Lanka	100
AIG Sigorta A.S.	Turkey	100
Tata AIG General Insurance Company Limited	India	26
AIU Insurance Company	New York	52[11]
AIU North America, Inc.	New York	100
American General Corporation	Texas	100
American General Bancassurance Services, Inc.	Illinois	100
AGC Life Insurance Company	Missouri	100
AIG Life Holdings (Canada), ULC	Canada	100
AIG Assurance Canada	Canada	100
AIG Life Insurance Company of Canada	Canada	100
AIG Life of Bermuda, Ltd.	Bermuda	100
American General Life and Accident Insurance Company	Tennessee	100
American General Life Insurance Company	Texas	100
American General Annuity Service Corporation	Texas	100
AIG Enterprise Services, LLC	Delaware	100
American General Equity Services Corporation	Delaware	100
American General Life Companies, LLC	Delaware	100
The Variable Annuity Life Insurance Company	Texas	100
VALIC Retirement Services Company	Texas	100
VALIC Trust Company	Texas	100
American General Property Insurance Company	Tennessee	51.85[12]
American General Property Insurance Company of Florida	Florida	100
AIG Annuity Insurance Company	Texas	100

	Jurisdiction of Incorporation or Organization	Percentage of Voting Securities Owned by its Immediate Parent[2]
The United States Life Insurance Company in the City of New York	New York	100
American General Finance, Inc.	Indiana	100
American General Auto Finance, Inc.	Delaware	100
American General Finance Corporation	Indiana	100
MorEquity, Inc.	Nevada	100
Wilmington Finance, Inc.	Delaware	100
Merit Life Insurance Co.	Indiana	100
Yosemite Insurance Company	Indiana	100
CommoLoCo, Inc.	Puerto Rico	100
American General Financial Services of Alabama, Inc.	Delaware	100
American General Investment Management Corporation	Delaware	100
American General Realty Investment Corporation	Texas	100
American General Assurance Company	Illinois	100
American General Indemnity Company	Illinois	100
Knickerbocker Corporation	Texas	100
American Home Assurance Company	New York	100
AIG Domestic Claims, Inc.	Delaware	50[13]
AIG Hawaii Insurance Company, Inc.	Hawaii	100
American Pacific Insurance Company, Inc.	Hawaii	100
American International Insurance Company	New York	100
American International Insurance Company of California, Inc.	California	100
American International Insurance Company of New Jersey	New Jersey	100
Minnesota Insurance Company	Minnesota	100
American International Realty Corp.	Delaware	31.5[14]
Pine Street Real Estate Holdings Corp.	New Hampshire	31.47[14]
Transatlantic Holdings, Inc.	Delaware	33.41[15]
Transatlantic Reinsurance Company	New York	100
Putnam Reinsurance Company	New York	100
Trans Re Zurich	Switzerland	100
American International Insurance Company of Delaware	Delaware	100
American International Life Assurance Company of New York	New York	77.52[16]

Subsidiaries of Registrant *Continued*

	Jurisdiction of Incorporation or Organization	Percentage of Voting Securities Owned by its Immediate Parent[2]
American International Underwriters Corporation	New York	100
American International Underwriters Overseas, Ltd.	Bermuda	100
AIG Europe (Ireland) Limited	Ireland	100
AIG Europe (U.K.) Limited	England	100
AIG Brasil Companhia de Seguros	Brazil	50
AIG General Insurance (Vietnam) Company Limited	Vietnam	100
Universal Insurance Co., Ltd.	Thailand	100
La Seguridad de Centroamerica, Compania de Seguros S.A.	Guatemala	100
La Meridional Compania Argentina de Seguros	Argentina	100
American International Insurance Company of Puerto Rico	Puerto Rico	100
A.I.G. Colombia Seguros Generales S.A.	Colombia	100
American International Underwriters GmBH	Germany	100
Richmond Insurance Company Limited	Bermuda	100
Underwriters Adjustment Company, Inc.	Panama	100
American Life Insurance Company	Delaware	100
AIG Life (Bulgaria) Z.D. A.D	Bulgaria	100
ALICO, S.A	France	100
First American Polish Life Insurance and Reinsurance Company, S.A.	Poland	100
Inversiones Interamericana S.A. (Chile)	Chile	100
Pharaonic American Life Insurance Company	Egypt	71.63
Unibanco AIG Seguros S.A.	Brazil	47.81[17]
AIG Life Insurance Company (Switzerland) Ltd.	Switzerland	100
American Security Life Insurance Company, Ltd.	Lichtenstein	100
Birmingham Fire Insurance Company of Pennsylvania	Pennsylvania	100
Commerce and Industry Insurance Company	New York	100
Commerce and Industry Insurance Company of Canada	Ontario	100
Delaware American Life Insurance Company	Delaware	100
Hawaii Insurance Consultants, Ltd.	Hawaii	100
HSB Group, Inc.	Delaware	100
The Hartford Steam Boiler Inspection and Insurance Company	Connecticut	100
The Hartford Steam Boiler Inspection and Insurance Company of Connecticut	Connecticut	100
HSB Engineering Insurance Limited	England	100
The Boiler Inspection and Insurance Company of Canada	Canada	100
The Insurance Company of the State of Pennsylvania	Pennsylvania	100
Landmark Insurance Company	California	100
Mt. Mansfield Company, Inc.	Vermont	100
National Union Fire Insurance Company of Pittsburgh, Pa.	Pennsylvania	100
American International Specialty Lines Insurance Company	Alaska	70[18]
Lexington Insurance Company	Delaware	70[18]
AIG Centennial Insurance Company	Pennsylvania	100
AIG Premier Insurance Company	Pennsylvania	100
AIG Indemnity Insurance Company	Pennsylvania	100
AIG Preferred Insurance Company	Pennsylvania	100
AIG Auto Insurance Company of New Jersey	New Jersey	100
JI Accident & Fire Insurance Co. Ltd.	Japan	50
National Union Fire Insurance Company of Louisiana	Louisiana	100
National Union Fire Insurance Company of Vermont	Vermont	100
21st Century Insurance Group	California	33.03[19]
21st Century Insurance Company	California	100
21st Century Casualty Company	California	100
21st Century Insurance Company of the Southwest	Texas	100
Starr Excess Liability Insurance Company, Ltd.	Delaware	100
Starr Excess Liability Insurance International Ltd.	Ireland	100

	Jurisdiction of Incorporation or Organization	Percentage of Voting Securities Owned by its Immediate Parent[2]
NHIG Holding Corp.	Delaware	100
Audubon Insurance Company	Louisiana	100
Audubon Indemnity Company	Mississippi	100
Agency Management Corporation	Louisiana	100
The Gulf Agency, Inc.	Alabama	100
New Hampshire Insurance Company	Pennsylvania	100
AIG Europe, S.A.	France	70.48[20]
AI Network Corporation	Delaware	100
American International Pacific Insurance Company	Colorado	100
American International South Insurance Company	Pennsylvania	100
Granite State Insurance Company	Pennsylvania	100
New Hampshire Indemnity Company, Inc.	Pennsylvania	100
AIG National Insurance Company, Inc.	New York	100
Illinois National Insurance Co.	Illinois	100
New Hampshire Insurance Services, Inc.	New Hampshire	100
AIG Star Life Insurance Co., Ltd	Japan	100
The Philippine American Life and General Insurance Company	Philippines	99.78
Pacific Union Assurance Company	California	100
Philam Equitable Life Assurance Company, Inc.	Philippines	95.31
Philam Insurance Company, Inc.	Philippines	100
Risk Specialist Companies, Inc.	Delaware	100
United Guaranty Corporation	North Carolina	36.31[21]
A.I.G. Mortgage Holdings Israel, Ltd.	Israel	82.12
E.M.I.-Ezer Mortgage Insurance Company, Limited	Israel	100
AIG United Guaranty Agenzia DI Assicurazione S.R.L.	Italy	100
AIG United Guaranty Insurance (Asia) Limited	Hong Kong	100
AIG United Guaranty Re, Ltd.	Ireland	100
United Guaranty Insurance Company	North Carolina	100
United Guaranty Mortgage Insurance Company	North Carolina	100
United Guaranty Mortgage Insurance Company of North Carolina	North Carolina	100
United Guaranty Partners Insurance Company	Vermont	80
United Guaranty Residential Insurance Company of North Carolina	North Carolina	100
United Guaranty Residential Insurance Company	North Carolina	75.03[22]
United Guaranty Commercial Insurance Company of North Carolina	North Carolina	100
United Guaranty Mortgage Indemnity Company	North Carolina	100
United Guaranty Credit Insurance Company	North Carolina	100
United Guaranty Services, Inc.	North Carolina	100

(1) All subsidiaries listed are consolidated in the accompanying financial statements. Certain subsidiaries have been omitted from the tabulation. The omitted subsidiaries, when considered in the aggregate as a single subsidiary, do not constitute a significant subsidiary.

(2) Percentages include directors' qualifying shares.

(3) The common stock is owned approximately 12.0 percent by Starr International Company, Inc., 1.8 percent by C.V. Starr & Co., Inc. and 2.0 percent by The Starr Foundation.

(4) Also owned 32.77 percent by National Union Fire Insurance Company of Pittsburgh, Pa.

(5) Also owned 10 percent by AIG Matched Funding Corp.

(6) Also owned 10 percent by a subsidiary of American Life Insurance Company.

(7) Also owned 21 percent by Commerce and Industry Insurance Company.

(8) Formerly known as AIG SunAmerica Inc.

(9) Also owned 30 percent by AIG Retirement Services, Inc.

(10) Formerly known as Anchor National Life Insurance Company.

(11) Also owned eight percent by The Insurance Company of the State of Pennsylvania, 32 percent by National Union Fire Insurance Company of Pittsburgh, Pa. and eight percent by Birmingham Fire Insurance Company of Pennsylvania.

(12) Also owned 48.15 percent by American General Life and Accident Insurance Company.

(13) Also owned 50 percent by The Insurance Company of the State of Pennsylvania.

(14) Also owned by 11 other AIG subsidiaries.

(15) Also owned 25.95 percent by AIG.

(16) Also owned 22.48 percent by American Home Assurance Company.

(17) Also owned 1.7 percent by American International Underwriters Overseas, Ltd. and .48 percent by American Home Assurance Company.

(18) Also owned 20 percent by The Insurance Company of the State of Pennsylvania and ten percent by Birmingham Fire Insurance Company of Pennsylvania.

(19) Also owned 16.85 percent by American Home Assurance Company, 6.34 percent by Commerce and Industry Insurance Company and 6.34 percent by New Hampshire Insurance Company.

(20) 100 percent held together with other AIG companies.

(21) Also owned 45.88 percent by National Union Fire Insurance Company of Pittsburgh, Pa., 16.95 percent by New Hampshire Insurance Company and 0.86 percent by The Insurance Company of the State of Pennsylvania.

(22) Also owned 24.97 percent by United Guaranty Residential Insurance Company of North Carolina.

Consent of Independent Registered Public Accounting Firm

Exhibit 23

We hereby consent to the incorporation by reference in the Registration Statements on Form S-8 (No. 2-45346, No. 2-75875, No. 2-78291, No. 2-91945, No. 33-18073, No. 33-57250, No. 333-48639, No. 333-58095, No. 333-70069, No. 333-83813, No. 333-31346, No. 333-39976, No. 333-45828, No. 333-50198, No. 333-52938, No. 333-68640, No. 333-101640, No. 333-101967, No. 333-108466, No. 333-111737, and No. 333-115911) of American International Group, Inc. of our report dated March 16, 2006, relating to the financial statements, financial statement schedules, management's assessment of the effectiveness of internal control over financial reporting and the effectiveness of internal control over financial reporting, which appears in this Annual Report on Form 10-K.

PricewaterhouseCoopers LLP

New York, New York
March 16, 2006

CERTIFICATIONS

I, Martin J. Sullivan, certify that:

1. I have reviewed this Annual Report on Form 10-K of American International Group, Inc.;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:

(a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

(b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

(c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

(d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):

(a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

(b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

/s/ MARTIN J. SULLIVAN

Martin J. Sullivan
President and Chief Executive Officer

Date: March 16, 2006

CERTIFICATIONS

I, Steven J. Bensinger, certify that:

1. I have reviewed this Annual Report on Form 10-K of American International Group, Inc.;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:

(a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

(b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

(c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

(d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):

(a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

(b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

/s/ STEVEN J. BENSINGER

Steven J. Bensinger
Executive Vice President and Chief Financial Officer

Date: March 16, 2006

CERTIFICATION

In connection with this Annual Report on Form 10-K of American International Group, Inc. (the "Company") for the year ended December 31, 2005, as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, Martin J. Sullivan, President and Chief Executive Officer of the Company, certify, pursuant to 18 U.S.C. Section 1350, that to my knowledge:

(1) The Report fully complies with the requirements of Section 13(a) or 15(d), as applicable, of the Securities Exchange Act of 1934; and

(2) The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

/s/ MARTIN J. SULLIVAN
Martin J. Sullivan
President and Chief Executive Officer

Date: March 16, 2006

The foregoing certification is being furnished solely pursuant to 18 U.S.C. Section 1350 and is not being filed as part of the Report or as a separate disclosure document.

CERTIFICATION

In connection with this Annual Report on Form 10-K of American International Group, Inc. (the "Company") for the year ended December 31, 2005, as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, Steven J. Bensinger, Executive Vice President and Chief Financial Officer of the Company, certify, pursuant to 18 U.S.C. Section 1350, that to my knowledge:

(1) The Report fully complies with the requirements of Section 13(a) or 15(d), as applicable, of the Securities Exchange Act of 1934; and

(2) The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

/s/ Steven J. Bensinger

Steven J. Bensinger
Executive Vice President and Chief Financial Officer

Date: March 16, 2006

The foregoing certification is being furnished solely pursuant to 18 U.S.C. Section 1350 and is not being filed as part of the Report or as a separate disclosure document.

Summary Of Investments – Other than Investments in Related Parties

Schedule I

At December 31, 2005 *(in millions)*	Cost*	Value	Amount at which shown in the Balance Sheet
Fixed maturities:			
Bonds:			
United States government and government agencies and authorities	$ 7,869	$ 7,901	$ 7,901
States, municipalities and political subdivisions	70,662	71,716	71,200
Foreign governments	57,896	62,120	62,117
Public utilities	15,156	15,582	15,582
All other corporate	224,180	228,880	228,880
Total bonds	375,763	386,199	385,680
Total fixed maturities	375,763	386,199	385,680
Equity securities:			
Common stocks:			
Public utilities	250	289	289
Banks, trust and insurance companies	1,567	1,967	1,967
Industrial, miscellaneous and all other	16,054	18,930	18,930
Total common stocks	17,871	21,186	21,186
Preferred stocks	2,282	2,402	2,402
Total equity securities	20,153	23,588	23,588
Mortgage loans on real estate, policy and collateral loans	24,909	26,352	24,909
Financial services assets:			
Flight equipment primarily under operating leases, net of accumulated depreciation	36,245	—	36,245
Securities available for sale, at market value	37,572	37,511	37,511
Trading securities, at market value	—	6,499	6,499
Spot commodities	—	96	92
Unrealized gain on swaps, options and forward transactions	—	18,695	18,695
Trading assets	—	1,204	1,204
Securities purchased under agreements to resell, at contract value	14,547	—	14,547
Finance receivables, net of allowance	27,995	27,528	27,995
Securities lending collateral, at market value (approximates cost)	59,471	59,471	59,471
Other invested assets (approximates market value)	27,267	27,267	27,267
Short-term investments, at cost (approximates market value)	15,342	15,342	15,342
Total investments	—	—	$679,045

* *Original cost of equity securities and, as to fixed maturities, original cost reduced by repayments and adjusted for amortization of premiums or accrual of discounts.*

Condensed Financial Information of Registrant
Balance Sheet – Parent Company Only

Schedule II

December 31, *(in millions)*	**2005**	2004
Assets:		
Cash	**$ 190**	$ 17
Short-term investments	**1,270**	672
Invested assets	**122**	355
Carrying value of subsidiaries and partially-owned companies, at equity	**90,723**	80,966
Premiums and insurance balances receivable – net	**186**	198
Other assets	**2,582**	2,588
Total assets	**95,073**	84,796
Liabilities:		
Insurance balances payable	**408**	405
Due to affiliates – net	**3,250**	3,364
Medium term notes payable	**112**	667
Term notes payable	**3,435**	1,935
Zero coupon notes	**1,060**	1,045
Other liabilities	**491**	(2,293)
Total liabilities	**8,756**	5,123
Shareholders' equity:		
Common stock	**6,878**	6,878
Additional paid-in capital	**2,339**	2,094
Retained earnings	**72,330**	63,468
Accumulated other comprehensive income	**6,967**	9,444
Treasury stock	**(2,197)**	(2,211)
Total shareholders' equity	**86,317**	79,673
Total liabilities and shareholders' equity	**$ 95,073**	$84,796

See Accompanying Notes to Financial Statements – Parent Company Only.

STATEMENT OF INCOME – PARENT COMPANY ONLY

Years Ended December 31, *(in millions)*	**2005**	2004	2003
Agency income (loss)	**$ 3**	$ (8)	$ (1)
Financial services income	**507**	578	518
Asset management loss	**(3)**	(11)	(13)
Dividend income from consolidated subsidiaries:			
Cash	**1,746**	1,835	1,471
Other	**–**	1	–
Dividend income from partially-owned companies	**127**	11	9
Equity in undistributed net income of consolidated subsidiaries and partially-owned companies	**10,368**	8,705	7,708
Other income (expenses) – net	**(2,203)**	(409)	(1,221)
Income before income taxes	**10,545**	10,702	8,471
Income taxes	**68**	863	363
Net income	**$ 10,477**	$ 9,839	$ 8,108

See Accompanying Notes to Financial Statements – Parent Company Only.

Condensed Financial Information of Registrant – *Continued*
Statement of Cash Flows – Parent Company Only

Schedule II

Years Ended December 31, *(in millions)*	**2005**	2004	2003
Cash flows from operating activities:			
Net income	**$10,477**	$ 9,839	$ 8,108
Adjustments to reconcile net income to net cash provided by operating activities:			
Noncash revenues, expenses, gains and losses included in income:			
Equity in undistributed net income of consolidated subsidiaries and partially owned companies	**(10,368)**	(8,705)	(7,708)
Change in premiums and insurance balances receivable and payable – net	**15**	(12)	(4)
Other – net	**1,549**	1,610	229
Total adjustments	**(8,804)**	(7,107)	(7,483)
Net cash provided by operating activities	**1,673**	2,732	625
Cash flows from investing activities:			
Purchase of investments	**–**	(107)	–
Sale of investments	**–**	200	186
Change in short-term investments	**(598)**	302	(830)
Contributions to subsidiaries and investments in partially owned companies	**(1,500)**	(1,026)	(573)
Other – net	**206**	(13)	(269)
Net cash used in investing activities	**(1,892)**	(644)	(1,486)
Cash flows from financing activities:			
Change in medium term notes	**(555)**	(124)	(207)
Change in term notes	**1,500**	1	1,500
Redemption of zero coupon notes	**–**	(189)	–
Proceeds from common stock issued	**82**	158	74
Change in loans payable	**548**	(88)	(5)
Cash dividends to shareholders	**(1,420)**	(730)	(584)
Acquisition of treasury stock	**(176)**	(1,083)	(207)
Other – net	**338**	140	306
Net cash (used in) provided by financing activities	**317**	(1,915)	877
Effect of exchange rate changes on cash	**75**	(175)	(15)
Change in cash	**173**	(2)	1
Cash at beginning of year	**17**	19	18
Cash at end of year	**$ 190**	$ 17	$ 19

NOTES TO FINANCIAL STATEMENTS – PARENT COMPANY ONLY

(1) Agency operations conducted in New York through the North American Division of AIU are included in the financial statements of the parent company.

(2) Certain accounts have been reclassified in the 2004 and 2003 financial statements to conform to their 2005 presentation.

(3) "Equity in undistributed net income of consolidated subsidiaries and partially-owned companies" in the accompanying Statement of Income – Parent Company Only – includes equity in income of the minority-owned insurance operations.

Supplementary Insurance Information

Schedule III

At December 31, 2005, 2004 and 2003 and for the years then ended

Segment *(in millions)*	Deferred Policy Acquisition Costs	Reserves for Losses and Loss Expenses, Future Policy Benefits[a]	Reserve for Unearned Premiums	Policy and Contract Claims[b]	Premium Revenue	Net Investment Income	Losses and Loss Expenses Incurred, Benefits	Amortization of Deferred Policy Acquisition Costs	Other Operating Expenses	Net Premiums Written
2005										
General Insurance	**$ 4,048**	**$ 77,169**	**$ 24,243**	**$ –**	**$ 40,809**	**$ 4,031**	**$ 33,091**	**$ 7,430**	**$ 2,338**	**$ 41,872**
Life Insurance & Retirement Services	**29,200**	**108,807**	**–**	**2,473**	**29,400**	**18,134**	**30,620**	**3,377**	**4,475**	**–**
	$ 33,248	**$ 185,976**	**$ 24,243**	**$ 2,473**	**$ 70,209**	**$ 22,165**	**$ 63,711**	**$ 10,807**	**$ 6,813**	**$ 41,872**
2004										
General Insurance	$ 3,998	$ 61,878	$ 23,400	$ –	$ 38,537	$ 3,196	$ 30,357	$ 6,238	$ 2,189	$ 40,623
Life Insurance & Retirement Services	25,819	104,740	–	2,435	28,088	15,269	28,003	3,551	3,923	–
	$ 29,817	$ 166,618	$ 23,400	$ 2,435	$ 66,625	$ 18,465	$ 58,360	$ 9,789	$ 6,112	$ 40,623
2003										
General Insurance	$ 3,619	$ 51,871	$ 21,235	$ –	$ 31,306	$ 2,566	$ 22,872	$ 4,676	$ 1,783	$ 35,031
Life Insurance & Retirement Services	22,375	92,915	–	2,006	23,496	12,942	23,162	2,778	3,931	–
	$ 25,994	$ 144,786	$ 21,235	$ 2,006	$ 54,802	$ 15,508	$ 46,034	$ 7,454	$ 5,714	$ 35,031

(a) Reserves for losses and loss expenses with respect to the General Insurance operations are net of discounts of $2.11 billion, $1.55 billion and $1.52 billion at December 31, 2005, 2004 and 2003, respectively.

(b) Reflected in insurance balances payable on the accompanying consolidated balance sheet.

Reinsurance

Schedule IV

At December 31, 2005, 2004 and 2003 and for the years then ended

(dollars in millions)	Gross Amount	Ceded to Other Companies	Assumed from Other Companies	Net Amount	Percent of Amount Assumed to Net
2005					
Life Insurance in-force	**$ 1,838,337**	**$ 365,082**	**$ 14,496**	**$ 1,487,751**	**1.0%**
Premiums:					
General Insurance	**$ 46,689**	**$ 10,853**	**$ 6,036**	**$ 41,872**	**14.4%**
Life Insurance & Retirement Services	**30,637**	**1,317**	**80**	**29,400***	**0.3**
Total premiums	**$ 77,326**	**$ 12,170**	**$ 6,116**	**$ 71,272**	**8.6%**
2004					
Life Insurance in-force	$1,844,189	$344,036	$13,905	$1,514,058	0.9%
Premiums:					
General Insurance	$ 44,692	$ 11,423	$ 7,354	$ 40,623	18.1%
Life Insurance & Retirement Services	28,486	1,114	716	28,088*	2.5
Total premiums	$ 73,178	$ 12,537	$ 8,070	$ 68,711	11.7%
2003					
Life Insurance in-force	$1,580,982	$293,064	$ 2,049	$1,289,967	0.2%
Premiums:					
General Insurance	$ 40,786	$ 11,907	$ 6,152	$ 35,031	17.6%
Life Insurance & Retirement Services	24,412	952	36	23,496*	0.2
Total premiums	$ 65,198	$ 12,859	$ 6,188	$ 58,527	10.6%

* *Includes accident and health premiums of $6.51 billion, $5.63 billion and $4.17 billion in 2005, 2004 and 2003, respectively.*

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

Form 10-Q

(Mark One)

☑ QUARTERLY REPORT UNDER SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended March 31, 2006

or

☐ TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the transition period from to

Commission File Number 1-8787

American International Group, Inc.

(Exact name of registrant as specified in its charter)

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

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

Former name, former address and former fiscal year, if changed since last report: None

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

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of accelerated filer and large accelerated filer in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer ☑ Accelerated filer ☐ Non-accelerated filer ☐

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes ☐ No ☑

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of March 31, 2006: 2,597,469,137.

CONSOLIDATED BALANCE SHEET

(in millions) (unaudited)

	March 31, 2006	December 31, 2005
Assets:		
Investments and financial services assets:		
Fixed maturities:		
Bonds available for sale, at market value (amortized cost: 2006 – $358,275; 2005 – $349,612) (includes hybrid financial instruments: 2006 – $512)	**$364,510**	$359,516
Bonds held to maturity, at amortized cost (market value: 2006 – $21,841; 2005 – $22,047)	**21,520**	21,528
Bond trading securities, at market value (cost: 2006 – $5,230; 2005 – $4,623)	**5,229**	4,636
Equity securities:		
Common stocks available for sale, at market value (cost: 2006 – $10,838; 2005 – $10,125)	**13,569**	12,227
Common stocks trading, at market value (cost: 2006 – $8,785; 2005 – $7,746)	**10,270**	8,959
Preferred stocks available for sale, at market value (cost: 2006 – $2,381; 2005 – $2,282)	**2,456**	2,402
Mortgage loans on real estate, net of allowance (2006 – $55; 2005 – $54)	**14,968**	14,300
Policy loans	**7,218**	7,039
Collateral and guaranteed loans, net of allowance (2006 – $10; 2005 – $10)	**4,114**	3,570
Financial services assets:		
Flight equipment primarily under operating leases, net of accumulated depreciation (2006 – $7,728; 2005 – $7,419)	**37,580**	36,245
Securities available for sale, at market value (cost: 2006 – $38,446; 2005 – $37,572)	**38,225**	37,511
Trading securities, at market value	**6,350**	6,499
Spot commodities	**230**	92
Unrealized gain on swaps, options and forward transactions	**17,792**	18,695
Trading assets	**1,411**	1,204
Securities purchased under agreements to resell, at contract value	**12,297**	14,547
Finance receivables, net of allowance (2006 – $743; 2005 – $670)	**27,219**	27,995
Securities lending collateral, at market value (which approximates cost)	**62,967**	59,471
Other invested assets	**29,296**	27,267
Short-term investments, at cost (approximates market value)	**17,343**	15,342
Total investments and financial services assets	**694,564**	679,045
Cash	**1,248**	1,897
Investment income due and accrued	**5,733**	5,727
Premiums and insurance balances receivable, net of allowance (2006 – $1,025; 2005 – $1,011)	**18,001**	15,333
Reinsurance assets, net of allowance (2006 – $979; 2005 – $992)	**24,857**	24,978
Deferred policy acquisition costs	**35,988**	33,248
Investments in partially owned companies	**1,167**	1,158
Real estate and other fixed assets, net of accumulated depreciation (2006 – $5,135; 2005 – $4,990)	**8,059**	7,446
Separate and variable accounts	**67,597**	63,797
Goodwill	**8,208**	8,093
Other assets	**14,376**	12,329
Total assets	**$879,798**	$853,051

See Accompanying Notes to Consolidated Financial Statements.

CONSOLIDATED BALANCE SHEET *(continued)*

(in millions, except share data) (unaudited)

	March 31, 2006	December 31, 2005
Liabilities:		
Reserve for losses and loss expenses	**$ 78,100**	$ 77,169
Reserve for unearned premiums	**25,044**	24,243
Future policy benefits for life and accident and health insurance contracts	**114,606**	108,807
Policyholders' contract deposits	**231,045**	227,027
Other policyholders' funds	**10,684**	10,870
Reserve for commissions, expenses and taxes	**4,939**	4,769
Insurance balances payable	**3,987**	3,564
Funds held by companies under reinsurance treaties	**4,195**	4,174
Income taxes payable	**6,615**	6,288
Financial services liabilities:		
Borrowings under obligations of guaranteed investment agreements	**21,600**	20,811
Securities sold under agreements to repurchase, at contract value	**9,691**	11,047
Trading liabilities	**2,389**	2,546
Hybrid financial instrument liabilities, at fair value	**6,109**	–
Securities and spot commodities sold but not yet purchased, at market value	**6,429**	5,975
Unrealized loss on swaps, options and forward transactions	**11,267**	12,740
Trust deposits and deposits due to banks and other depositors	**4,384**	4,877
Commercial paper	**7,500**	6,514
Notes, bonds, loans and mortgages payable	**68,790**	71,313
Commercial paper	**5,965**	2,694
Notes, bonds, loans and mortgages payable	**7,427**	7,126
Liabilities connected to trust preferred stock	**1,390**	1,391
Separate and variable accounts	**67,597**	63,797
Securities lending payable	**63,959**	60,409
Minority interest	**5,872**	5,124
Other liabilities	**21,635**	23,273
Total liabilities	**791,219**	766,548
Preferred shareholders' equity in subsidiary companies	**189**	186
Commitments and Contingent Liabilities (See Note 6)		
Shareholders' equity:		
Common stock, $2.50 par value; 5,000,000,000 shares authorized; shares issued 2006 and 2005 – 2,751,327,476	**6,878**	6,878
Additional paid-in capital	**2,513**	2,339
Retained earnings	**75,433**	72,330
Accumulated other comprehensive income (loss)	**5,709**	6,967
Treasury stock, at cost; 2006 – 153,858,339; 2005 – 154,680,704 shares of common stock	**(2,143)**	(2,197)
Total shareholders' equity	**88,390**	86,317
Total liabilities, preferred shareholders' equity in subsidiary companies and shareholders' equity	**$879,798**	$853,051

See Accompanying Notes to Consolidated Financial Statements.

CONSOLIDATED STATEMENT OF INCOME

(in millions, except per share data) (unaudited)

Three Months Ended March 31,	**2006**	2005
Revenues:		
Premiums and other considerations	**$18,242**	$17,680
Net investment income	**5,827**	5,332
Realized capital gains (losses)	**169**	137
Other revenues	**3,021**	4,053
Total revenues	**27,259**	27,202
Benefits and expenses:		
Incurred policy losses and benefits	**15,000**	14,873
Insurance acquisition and other operating expenses	**7,466**	6,680
Total benefits and expenses	**22,466**	21,553
Income before income taxes, minority interest and cumulative effect of an accounting change	**4,793**	5,649
Income taxes	**1,435**	1,706
Income before minority interest and cumulative effect of an accounting change	**3,358**	3,943
Minority interest	**(197)**	(144)
Income before cumulative effect of an accounting change	**3,161**	3,799
Cumulative effect of an accounting change, net of tax	**34**	–
Net income	**$ 3,195**	$ 3,799
Earnings per common share:		
Basic		
Income before cumulative effect of an accounting change	**$ 1.21**	$ 1.46
Cumulative effect of an accounting change, net of tax	**0.01**	–
Net income	**1.22**	1.46
Diluted		
Income before cumulative effect of an accounting change	**$ 1.21**	$ 1.45
Cumulative effect of an accounting change, net of tax	**0.01**	–
Net income	**1.22**	1.45
Dividends declared per common share	**$ 0.150**	$ 0.175
Average shares outstanding:		
Basic	**2,605**	2,597
Diluted	**2,624**	2,624

See Accompanying Notes to Consolidated Financial Statements.

CONSOLIDATED STATEMENT OF CASH FLOWS

(in millions) (unaudited)

Three Months Ended March 31,	**2006**	2005
Summary:		
Net cash provided by (used in) operating activities	**$ 3,066**	$ (434)
Net cash used in investing activities	**(19,937)**	(20,118)
Net cash provided by financing activities	**15,672**	20,961
Effect of exchange rate changes on cash	**550**	(57)
Change in cash	**(649)**	352
Cash at beginning of period	**1,897**	2,009
Cash at end of period	**$ 1,248**	$ 2,361
Cash flows from operating activities:		
Net income	**$ 3,195**	$ 3,799
Adjustments to reconcile net income to net cash provided by (used in) operating activities:		
Noncash revenues, expenses, gains and losses included in income:		
Change in:		
General and life insurance reserves	**7,263**	5,605
Premiums and insurance balances receivable and payable – net	**(2,245)**	8
Reinsurance assets	**121**	241
Deferred policy acquisition costs	**(1,715)**	(944)
Investment income due and accrued	**(6)**	(53)
Funds held under reinsurance treaties	**21**	(267)
Other policyholders' funds	**(186)**	(68)
Income taxes payable	**761**	1,457
Reserve for commissions, expenses and taxes	**170**	143
Other assets and liabilities – net	**(3,125)**	(962)
Bonds and common stocks trading, at market value	**(1,904)**	(1,082)
Trading assets and liabilities – net	**(364)**	905
Trading securities, at market value	**149**	(345)
Spot commodities	**(138)**	(120)
Net unrealized (gain) loss on swaps, options and forward transactions	**(570)**	(598)
Securities purchased under agreements to resell	**2,250**	(6,321)
Securities sold under agreements to repurchase	**(1,356)**	(1,939)
Securities and spot commodities sold but not yet purchased, at market value	**454**	182
Realized capital (gains) losses	**(169)**	(137)
Equity in income of partially owned companies and other invested assets	**(480)**	(445)
Amortization of premium and discount on securities	**105**	113
Depreciation expenses, principally flight equipment	**554**	526
Provision for finance receivable losses	**160**	86
Other – net	**121**	(218)
Total adjustments	**(129)**	(4,233)
Net cash provided by (used in) operating activities	**$ 3,066**	$ (434)

See Accompanying Notes to Consolidated Financial Statements.

CONSOLIDATED STATEMENT OF CASH FLOWS *(continued)*

(in millions) (unaudited)

Three Months Ended March 31,	2006	2005
Cash flows from investing activities:		
Cost of bonds, at market sold	**$ 22,598**	$ 27,572
Cost of bonds, at market matured or redeemed	**3,628**	2,823
Cost of equity securities sold	**3,425**	2,724
Realized capital gains (losses)	**169**	137
Purchases of fixed maturities	**(34,507)**	(42,094)
Purchases of equity securities	**(4,285)**	(3,608)
Mortgage, policy, collateral and guaranteed loans granted	**(1,449)**	(1,578)
Repayments of mortgage, policy, collateral and guaranteed loans	**58**	575
Sales of securities available for sale	**1,166**	804
Maturities of securities available for sale	**360**	2,164
Purchases of securities available for sale	**(2,386)**	(2,316)
Sales of flight equipment	**195**	41
Purchases of flight equipment	**(1,897)**	(2,141)
Change in securities lending collateral	**(3,496)**	(2,721)
Net additions to real estate and other fixed assets	**(322)**	(188)
Sales or distributions of other invested assets	**2,161**	2,163
Other invested assets	**(3,290)**	(3,339)
Change in short-term investments	**(2,676)**	301
Investments in partially owned companies	**(5)**	4
Finance receivable originations and purchases	**(7,696)**	(10,605)
Finance receivable principal payments received	**8,312**	9,164
Net cash used in investing activities	**$(19,937)**	$(20,118)
Cash flows from financing activities:		
Receipts from policyholders' contract deposits	**$ 14,108**	$ 16,279
Withdrawals from policyholders' contract deposits	**(10,090)**	(7,149)
Change in trust deposits and deposits due to banks and other depositors	**(493)**	364
Change in commercial paper	**4,257**	2,263
Proceeds from notes, bonds, loans and mortgages payable, and hybrid financial instrument liabilities	**9,527**	16,244
Repayments on notes, bonds, loans and mortgages payable, and hybrid financial instrument liabilities	**(5,644)**	(13,081)
Proceeds from guaranteed investment agreements	**3,306**	4,955
Maturities of guaranteed investment agreements	**(2,517)**	(1,183)
Change in securities lending payable	**3,550**	2,721
Proceeds from common stock issued	**34**	31
Cash dividends to shareholders	**(390)**	(325)
Acquisition of treasury stock	**(2)**	(166)
Other – net	**26**	8
Net cash provided by financing activities	**$ 15,672**	$ 20,961
Supplementary information:		
Taxes paid	**$ 460**	$ 382
Interest paid	**$ 1,284**	$ 1,147

See Accompanying Notes to Consolidated Financial Statements.

CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME

(in millions) (unaudited)

Three Months Ended March 31,	**2006**	2005
Comprehensive income (loss):		
Net income	**$ 3,195**	$ 3,799
Other comprehensive income (loss):		
Unrealized appreciation (depreciation) of investments – net of reclassification adjustments	**(2,599)**	(2,535)
Deferred income tax benefit (expense) on above changes	**1,100**	1,256
Foreign currency translation adjustments	**550**	(53)
Applicable income tax benefit (expense) on above changes	**(290)**	4
Net derivative gains arising from cash flow hedging activities	**4**	150
Deferred income tax (expense) benefit on above changes	**13**	(111)
Retirement plan liabilities adjustment, net of tax	**(36)**	(30)
Other comprehensive income (loss)	**(1,258)**	(1,319)
Comprehensive income (loss)	**$ 1,937**	$ 2,480

See Accompanying Notes to Consolidated Financial Statements.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

1. Financial Statement Presentation

These statements are unaudited. In the opinion of management, all material adjustments including normal recurring accruals have been made for a fair statement of the results presented herein. All material intercompany accounts and transactions have been eliminated. Certain accounts have been reclassified in the 2005 financial statements to conform to their 2006 presentation. For further information, refer to the Annual Report on Form 10-K of American International Group, Inc. (AIG) for the year ended December 31, 2005 (2005 Annual Report on Form 10-K).

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

2. Segment Information

AIG identifies its reportable segments by product line consistent with its management structure. AIG's major product and service groupings are general insurance, life insurance & retirement services, financial services and asset management. **The following table summarizes the operations by the major operating segments for the three months ended March 31, 2006 and 2005:**

Operating Segments *(in millions) (unaudited)*	**2006**	2005
Revenues[(a)]:		
General Insurance[(b)]	**$11,656**	$11,219
Life Insurance & Retirement Services[(c)]	**12,639**	11,775
Financial Services[(d)]	**1,615**	2,436
Asset Management[(e)]	**1,239**	1,377
Other	**110**	395
Consolidated	**$27,259**	$27,202
Operating income (loss)[(a)(f)]:		
General Insurance	**$ 2,331**	$ 1,642
Life Insurance & Retirement Services[(g)]	**2,555**	2,181
Financial Services[(g)]	**(159)**	1,045
Asset Management	**461**	590
Other[(h)]	**(395)**	191
Consolidated	**$ 4,793**	$ 5,649

(a) Includes the effect of hedging activities that do not qualify for hedge accounting treatment under FAS 133, including the related foreign exchange gains and losses. For the first three months of 2006 and 2005, the effect was $0 and $15 million, respectively, in operating income for Aircraft Finance and $(678) million and $468 million in revenues and operating income, respectively, for Capital Markets. These amounts result primarily from interest rate and foreign currency derivatives hedging available for sale securities and borrowings.

(b) Represents the sum of General Insurance net premiums earned, net investment income and realized capital gains (losses).

(c) Represents the sum of Life Insurance & Retirement Services GAAP premiums, net investment income and realized capital gains (losses). Included in realized capital gains (losses) is the effect of hedging activities that do not qualify for hedge accounting treatment under FAS 133 and the application of FAS 52 of $278 million and $(79) million in the first three months of 2006 and 2005, respectively.

(d) Represents interest, lease and finance charges.

(e) Represents management and advisory fees and net investment income with respect to GICs.

(f) Represents income before income taxes, minority interest and cumulative effect of an accounting change.

(g) Results of operations of AIG Credit Card Company (Taiwan) are shared equally by the Life Insurance & Retirement Services segment and the Financial Services segment. In 2006, additional allowances of $44 million were recorded by each segment for losses in these credit card operations.

(h) Represents unallocated corporate expenses, relating primarily to interest expense and certain compensation related expenses, and other realized capital gains (losses) of $(57) million and $155 million in the first three months of 2006 and 2005, respectively.

The following table summarizes AIG's General Insurance operations by major internal reporting unit for the three months ended March 31, 2006 and 2005:

General Insurance *(in millions) (unaudited)*	**2006**	2005
Revenues:		
Domestic Brokerage Group	**$ 6,555**	$ 6,289
Transatlantic	**1,016**	982
Personal Lines	**1,215**	1,171
Mortgage Guaranty	**198**	169
Foreign General	**2,670**	2,602
Reclassifications and Eliminations	**2**	6
Total General Insurance	**$11,656**	$11,219
Operating Income*:		
Domestic Brokerage Group	**$ 1,357**	$ 713
Transatlantic	**141**	114
Personal Lines	**101**	109
Mortgage Guaranty	**109**	104
Foreign General	**621**	596
Reclassifications and Eliminations	**2**	6
Total General Insurance	**$ 2,331**	$ 1,642

** Includes $103 million and $171 million of additional losses incurred and net reinstatement premium costs in 2006 and 2005, respectively, related primarily to prior year catastrophes.*

The following table summarizes AIG's Life Insurance & Retirement Services operations by major internal reporting unit for the three months ended March 31, 2006 and 2005:

Life Insurance & Retirement Services *(in millions) (unaudited)*	**2006**	2005
Revenues[(a)]:		
Foreign:		
AIA, AIRCO and Nan Shan[(b)]	**$ 4,352**	$ 4,066
ALICO, AIG Star Life and AIG Edison Life[(c)]	**4,095**	3,519
Philamlife and Other	**124**	130
Domestic:		
AGLA and AG Life[(d)]	**2,367**	2,388
VALIC, AIG Annuity and AIG SunAmerica[(e)]	**1,701**	1,672
Total Life Insurance & Retirement Services	**$12,639**	$11,775
Operating Income:		
Foreign:		
AIA, AIRCO and Nan Shan[(b)]	**$ 700**	$ 588
ALICO, AIG Star Life and AIG Edison Life[(c)]	**958**	596
Philamlife and Other	**11**	16
Domestic:		
AGLA and AG Life[(d)]	**366**	466
VALIC, AIG Annuity and AIG SunAmerica[(e)]	**520**	515
Total Life Insurance & Retirement Services	**$ 2,555**	$ 2,181

(a) Represents the sum of Life Insurance & Retirement Services GAAP premiums, net investment income and realized capital gains (losses).

(b) Represents the operations of American International Assurance Company, Limited together with American International Assurance Company (Bermuda) Limited (AIA), American International Reinsurance Company, Ltd. (AIRCO), and Nan Shan Life Insurance Company, Ltd. (Nan Shan). Revenues and operating income include realized capital gains (losses) of $213 million and $66 million for the first three months of 2006 and 2005, respectively. The effects of FAS 133 and the application of FAS 52 included in realized capital gains (losses) are gains of $173 million and

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(continued)*

2. Segment Information *(continued)*

$10 million for the first three months of 2006 and 2005, respectively. Includes $44 million in additional allowances for losses in AIG Credit Card Company (Taiwan) in 2006.

(c) Represents the operations of American Life Insurance Company (ALICO), AIG Star Life Insurance Co., Ltd. (AIG Star Life), and AIG Edison Life Insurance Company (AIG Edison Life). Revenues and operating income include realized capital gains of $149 million and losses of $(139) million for the first three months of 2006 and 2005, respectively. The effects of FAS 133 and the application of FAS 52 included in realized capital gains (losses) are gains of $40 million and losses of $(213) million for the first three months of 2006 and 2005, respectively.

(d) Includes the life operations of American General Life Insurance Company (AG Life), AIG Life Insurance Company and American International Life Assurance Company of New York. Also includes the operations of American General Life and Accident Insurance Company (AGLA). Revenues and operating income include realized capital gains of $8 million and $72 million for the first three months of 2006 and 2005, respectively. The effects of FAS 133 and the application of FAS 52 included in realized capital gains (losses) are gains of $86 million and $104 million for the first three months of 2006 and 2005, respectively.

(e) "AIG SunAmerica" represents the annuity operations of AIG SunAmerica Life Assurance Company, as well as those of First SunAmerica Life Insurance Company and SunAmerica Life Insurance Company. Also includes the operations of The Variable Annuity Life Insurance Company (VALIC) and AIG Annuity Insurance Company (AIG Annuity). Revenues and operating income include realized capital losses of $(202) million and $(79) million for the first three months of 2006 and 2005, respectively. The effects of FAS 133 and the application of FAS 52 included in realized capital gains (losses) are gains of $3 million and $20 million for the first three months of 2006 and 2005, respectively.

The following table summarizes AIG's Financial Services operations by major internal reporting unit for the three months ended March 31, 2006 and 2005:

Financial Services *(in millions) (unaudited)*	**2006**	2005
Revenues[(a)]:		
Aircraft Finance[(b)]	**$ 965**	$ 827
Capital Markets[(c)(d)]	**(300)**	756
Consumer Finance[(e)]	**924**	833
Other	**26**	20
Total Financial Services	**$1,615**	$2,436
Operating income (loss)[(a)]:		
Aircraft Finance	**$ 129**	$ 187
Capital Markets[(d)]	**(470)**	620
Consumer Finance[(f)]	**175**	221
Other	**7**	17
Total Financial Services	**$ (159)**	$1,045

(a) Includes the effect of hedging activities that do not qualify for hedge accounting treatment under FAS 133, including the related foreign exchange gains and losses. For the first three months of 2006 and 2005, the effect was $0 and $15 million, respectively, in operating income for Aircraft Finance and $(678) million and $468 million in both revenues and operating income for Capital Markets. These amounts result primarily from interest rate and foreign currency derivatives hedging available for sale securities and borrowings.

(b) Revenues are primarily from International Lease Finance Corporation (ILFC) aircraft lease rentals.

(c) Revenues, shown net of interest expense, are primarily from hedged financial positions entered into in connection with counterparty transactions and the effect of hedging activities that do not qualify for hedge accounting treatment under FAS 133 described in (a) above.

(d) Certain transactions entered into by AIGFP generate tax credits and benefits which are included in income taxes in the consolidated statement of income. The amount of such tax credits and benefits for the first three months of 2006 and 2005 are $18 million, and $19 million, respectively.

(e) Revenues are primarily finance charges.

(f) Includes $44 million in additional allowances for losses in AIG Credit Card Company (Taiwan) in 2006.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(continued)*

2. Segment Information *(continued)*

The following table summarizes AIG's Asset Management revenues and operating income for the three months ended March 31, 2006 and 2005:

Asset Management *(in millions) (unaudited)*	**2006**	2005
Revenues:		
Guaranteed Investment Contracts	**$ 822**	$ 896
Institutional Asset Management	**279**	319
Brokerage Services and Mutual Funds	**73**	63
Other	**65**	99
Total Asset Management	**$1,239**	$1,377
Operating income:		
Guaranteed Investment Contracts[(a)]	**$ 218**	$ 319
Institutional Asset Management[(b)(c)]	**159**	161
Brokerage Services and Mutual Funds	**23**	13
Other	**61**	97
Total Asset Management	**$ 461**	$ 590

(a) The effect of hedging activities that do not qualify for hedge accounting treatment under FAS 133 was $0 and $62 million for the first three months of 2006 and 2005, respectively.

(b) Includes the full results of certain AIG managed private equity and real estate funds that are consolidated effective December 31, 2003 pursuant to FIN46R, "Consolidation of Variable Interest Entities". For the first three months of 2006 and 2005, operating income includes $27 million and $75 million, respectively, of third-party limited partner earnings offset in minority interest expense.

(c) Includes the full results of certain AIG managed partnerships that are consolidated effective January 1, 2006 pursuant to EITF 04-5, "Determining Whether a General Partner, or the General Partners as a Group, Controls a Limited Partnership or Similar Entity When the Limited Partners Have Certain Rights." For the first three months of 2006, operating income includes $69 million of third-party limited partner earnings offset in minority interest expense.

3. Earnings Per Share

Earnings per share of AIG are based on the weighted average number of common shares outstanding during the period. See also Note 10 herein.

Computation of Earnings Per Share:

Three Months Ended March 31, *(in millions, except per share data) (unaudited)*	**2006**	2005
Numerator for basic earnings per share:		
Income before cumulative effect of an accounting change	**$3,161**	$3,799
Cumulative effect of an accounting change, net of tax	**34**	–
Net income applicable to common stock	**$3,195**	$3,799
Denominator for basic earnings per share:		
Average shares outstanding used in the computation of per share earnings:		
Common stock issued	**2,752**	2,752
Common stock in treasury	**(154)**	(155)
Deferred shares	**7**	–
Average shares outstanding – basic	**2,605**	2,597

Three Months Ended March 31, *(in millions, except per share data) (unaudited)*	**2006**	2005
Numerator for diluted earnings per share:		
Income before cumulative effect of an accounting change	**$3,161**	$3,799
Cumulative effect of an accounting change, net of tax	**34**	–
Net income applicable to common stock	**3,195**	3,799
Interest on contingently convertible bonds, net of tax[(a)]	**3**	3
Adjusted net income applicable to common stock[(a)]	**$3,198**	$3,802
Denominator for diluted earnings per share:		
Average shares outstanding	**2,605**	2,597
Incremental shares from potential common stock:		
Average number of shares arising from outstanding employee stock plans (treasury stock method)[(b)]	**10**	18
Contingently convertible bonds[(a)]	**9**	9
Adjusted average shares outstanding – diluted[(b)]	**2,624**	2,624
Earnings per share:		
Basic:		
Income before cumulative effect of an accounting change	**$ 1.21**	$ 1.46
Cumulative effect of an accounting change, net of tax	**0.01**	–
Net income	**$ 1.22**	$ 1.46
Diluted:		
Income before cumulative effect of an accounting change	**$ 1.21**	$ 1.45
Cumulative effect of an accounting change, net of tax	**0.01**	–
Net income	**$ 1.22**	$ 1.45

(a) Assumes conversion of contingently convertible bonds due to the adoption of EITF Issue No. 04-8 "Accounting Issues Related to Certain Features of Contingently Convertible Debt and the Effect on Diluted Earnings per Share."

(b) Certain shares arising from employee stock plans were not included in the computation of diluted earnings per share where the exercise price of the options exceeded the average market price and would have been antidilutive. The number of shares excluded were 7 million and 22 million for the first three months of 2006 and 2005, respectively.

During the three months ended March 31, 2005, AIG purchased in the open market 2,477,100 shares of its common stock. From time to time, AIG may buy shares of its common stock in the open market for general corporate purposes, including to satisfy its obligations under various employee benefit plans. At March 31, 2006 and December 31, 2005, an additional 36,542,700 shares could be purchased under the then current authorization by AIG's Board of Directors. Although AIG has authorization to purchase additional shares, AIG has not repurchased shares in 2006.

The quarterly dividend rate per common share, commencing with the dividend declared in May 2005 and paid on

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(continued)*

3. Earnings Per Share *(continued)*

September 16, 2005, is $0.15. The declared dividend amount of $0.175 for the first three months of 2005 includes a $0.05 increase to the amount previously declared in the fourth quarter of 2004 for payment in March 2005 as well as the $0.125 dividend declared in March 2005 for payment in June 2005. See also Note 10 herein.

4. Benefits Provided by Starr International Company, Inc. and C.V. Starr & Co., Inc.

Starr International Company, Inc. (SICO) has provided a series of two-year Deferred Compensation Profit Participation Plans (SICO Plans) to certain AIG employees. The SICO Plans came into being in 1975 when the voting shareholders and Board of Directors of SICO, a private holding company whose principal asset is AIG common stock, decided that a portion of the capital value of SICO should be used to provide an incentive plan for the current and succeeding managements of all American International companies, including AIG.

None of the costs of the various benefits provided under the SICO Plans has been paid by AIG, although AIG has recorded a charge to reported earnings for the deferred compensation amounts paid to AIG employees by SICO, with an offsetting amount credited to additional paid-in capital reflecting amounts deemed contributed by SICO. The SICO Plans provide that shares currently owned by SICO are set aside by SICO for the benefit of the participant and distributed upon retirement. The SICO Board of Directors currently may permit an early payout of units under certain circumstances. Prior to payout, the participant is not entitled to vote, dispose of or receive dividends with respect to such shares, and shares are subject to forfeiture under certain conditions, including but not limited to the participant's voluntary termination of employment with AIG prior to normal retirement age. Under the SICO Plans, SICO's Board of Directors may elect to pay a participant cash in lieu of shares of AIG common stock. Following notification from SICO to participants in the SICO Plans that it will settle specific future awards under the SICO Plans with shares rather than cash, AIG modified its accounting for the SICO Plans from variable to fixed measurement accounting, although variable accounting will continue to be applied where SICO makes cash payments pursuant to elections made prior to March 2005. AIG gave effect to this change in settlement method beginning on December 9, 2005, the date of SICO's notice to participants in the SICO Plans. See also Note 6(f) herein.

Compensation expense with respect to the SICO Plans aggregated $76 million, including various adjustments totalling $61 million, primarily relating to stock-split adjustments and other miscellaneous items, and $7 million for the first three months of 2006 and 2005, respectively. See also Note 10 herein.

In January 2006, C.V. Starr & Co., Inc. (Starr) completed its tender offer to purchase Starr interests from AIG employees. In conjunction with AIG's adoption of FAS 123R, Starr is considered to be an "economic interest holder" in AIG. As a result, compensation expense of $54 million with respect to the Starr offer was included in the first three months of 2006.

As a result of its changing relationship with Starr and SICO, AIG has established new executive compensation plans to replace the SICO plans and investment opportunities previously provided by Starr. The replacement plans include both share-based plans and cash-based plans (AIG Senior Partners Plan). In addition, these replacement plans generally include performance as well as service conditions. See also Note 10 herein.

5. Ownership and Transactions With Related Parties

(a) Ownership: According to the Schedule 13D filed on March 7, 2006 by Starr, SICO, Edward E. Matthews, Maurice R. Greenberg, the Maurice R. and Corinne P. Greenberg Family Foundation, Inc. and the Universal Foundation, Inc., these reporting persons may be deemed to beneficially own 396,124,637 shares of common stock. Based on the shares of common stock outstanding as of March 31, 2006, this ownership represents approximately 15 percent of the voting stock of AIG.

(b) Transactions with Related Parties: During the ordinary course of business, AIG and its subsidiaries pay commissions to Starr and its subsidiaries for the production and management of insurance business. There were no significant receivables from/payables to related parties at March 31, 2006.

6. Commitments and Contingent Liabilities

In the normal course of business, various commitments and contingent liabilities are entered into by AIG and certain of its subsidiaries. In addition, AIG guarantees various obligations of certain subsidiaries.

(a) AIG and certain of its subsidiaries become parties to derivative financial instruments with market risk resulting from both dealer and end user activities and to reduce currency, interest rate, equity and commodity exposures. These instruments are carried at their estimated fair values in the consolidated balance sheet. The vast majority of AIG's derivative activity is transacted by AIGFP. (See also Note 20 of Notes to Consolidated Financial Statements in AIG's 2005 Annual Report on Form 10-K.)

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(continued)*

6. Commitments and Contingent Liabilities *(continued)*

(b) Securities sold, but not yet purchased and spot commodities sold but not yet purchased represent obligations of AIGFP to deliver specified securities and spot commodities at their contracted prices. AIGFP records a liability to repurchase the securities and spot commodities in the market at prevailing prices.

AIG has issued unconditional guarantees with respect to the prompt payment, when due, of all present and future payment obligations and liabilities of AIGFP arising from transactions entered into by AIGFP.

(c) At March 31, 2006, ILFC had committed to purchase 308 new and used aircraft deliverable from 2006 through 2015 at an estimated aggregate purchase price of $21.4 billion and had options to purchase 16 new aircraft at an estimated aggregate purchase price of $1.5 billion. ILFC will be required to find customers for any aircraft acquired, and it must arrange financing for portions of the purchase price of such equipment.

(d) AIG and its subsidiaries, in common with the insurance industry in general, are subject to litigation, including claims for punitive damages, in the normal course of their business. The recent trend of increasing jury awards and settlements makes it difficult to assess the ultimate outcome of such litigation.

Although AIG regularly reviews the adequacy of the established reserve for losses and loss expenses, there can be no assurance that AIG's ultimate loss reserves will not develop adversely and materially exceed AIG's current loss reserves. Estimation of ultimate net losses, loss expenses and loss reserves is a complex process for long-tail casualty lines of business, which include excess and umbrella liability, directors and officers liability (D&O), professional liability, medical malpractice, workers compensation, general liability, products liability and related classes, as well as for asbestos and environmental exposures. Generally, actual historical loss development factors are used to project future loss development. However, there can be no assurance that future loss development patterns will be the same as in the past. Moreover, any deviation in loss cost trends or in loss development factors might not be discernible for an extended period of time subsequent to the recording of the initial loss reserve estimates for any accident year. Thus, there is the potential for reserves with respect to a number of years to be significantly affected by changes in loss cost trends or loss development factors that were relied upon in setting the reserves. These changes in loss trends or loss development factors could be attributable to changes in inflation in labor and material costs or in the judicial environment, or in other social or economic phenomena affecting claims.

(e) SAI Deferred Compensation Holdings, Inc., a wholly-owned subsidiary of AIG, has established a deferred compensation plan for registered representatives of certain AIG subsidiaries, pursuant to which participants have the opportunity to invest deferred commissions and fees on a notional basis. The value of the deferred compensation fluctuates with the value of the deferred investment alternatives chosen. AIG has provided a full and unconditional guarantee of the obligations of SAI Deferred Compensation Holdings, Inc. to pay the deferred compensation under the plan.

(f) On June 27, 2005, AIG entered into an agreement pursuant to which AIG agrees, subject to certain conditions, to make any payment that is not promptly paid with respect to the benefits accrued by certain employees of AIG and its subsidiaries under the SICO Plans (as defined in Note 4).

(g) AIG and certain of its subsidiaries have been named defendants in two putative class actions in state court in Alabama that arise out of the 1999 settlement of class and derivative litigation involving Caremark Rx, Inc. (Caremark). An excess policy issued by a subsidiary of AIG with respect to the 1999 litigation was expressly stated to be without limit of liability. In the current actions, plaintiffs allege that the judge approving the 1999 settlement was misled as to the extent of available insurance coverage and would not have approved the settlement had he known of the existence and/or unlimited nature of the excess policy. They further allege that AIG, its subsidiaries, and Caremark are liable for fraud and suppression for misrepresenting and/or concealing the nature and extent of coverage. In their complaint, plaintiffs request compensatory damages for the 1999 class in the amount of $3.2 billion, plus punitive damages. AIG and its subsidiaries deny the allegations of fraud and suppression and have asserted, *inter alia*, that information concerning the excess policy was publicly disclosed months prior to the approval of the settlement. AIG and its subsidiaries further assert that the current claims are barred by the statute of limitations and that plaintiffs' assertions that the statute was tolled cannot stand against the public disclosure of the excess coverage. Plaintiffs, in turn, have asserted that the disclosure was insufficient to inform them of the nature of the coverage and did not start the running of the statute of limitations. On January 28, 2005, the Alabama trial court determined that one of the current actions may proceed as a class action on behalf of the 1999 classes that were allegedly defrauded by the settlement. AIG, its subsidiaries, and Caremark are seeking appellate relief from the Alabama Supreme Court. AIG cannot now estimate either the likelihood of its prevailing in these actions or the potential damages in the event liability is determined.

(h) On December 30, 2004, an arbitration panel issued its ruling in connection with a 1998 workers compensation quota share reinsurance agreement under which Superior National Insurance Company, among others, was reinsured by

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(continued)*

6. Commitments and Contingent Liabilities *(continued)*

The United States Life Insurance Company in the City of New York (USLIFE), a subsidiary of American General Corporation. In its 2-1 ruling the arbitration panel refused to rescind the contract as requested by USLIFE. Instead, the panel reformed the contract to reduce USLIFE's participation by ten percent. USLIFE is pursuing certain reinsurance recoverables in connection with the contract. Further, the arbitration ruling established a second phase of arbitration which is pending, in which USLIFE is presenting its challenges to certain cessions to the contract. AIG holds a reserve of approximately $369 million related to this matter as of March 31, 2006.

(i) Regulators from several states have commenced investigations into insurance brokerage practices related to contingent commissions and other broker-related conduct, such as alleged bid rigging. Various parties, including insureds and shareholders, have also asserted putative class action and other claims against AIG or its subsidiaries alleging, among other things, violations of the antitrust and federal securities laws, and AIG expects that additional claims may be made.

In February 2006, AIG reached a resolution of claims and matters under investigation with the United States Department of Justice (DOJ), the Securities and Exchange Commission (SEC), the Office of the New York Attorney General (NYAG) and the New York State Department of Insurance (DOI). The settlements resolved outstanding litigation filed by the SEC, NYAG and DOI against AIG and concluded negotiations with these authorities and the DOJ in connection with the accounting, financial reporting and insurance brokerage practices of AIG and its subsidiaries, as well as claims relating to the underpayment of certain workers compensation premium taxes and other assessments. In the fourth quarter of 2005 AIG recorded an after-tax charge of $1.15 billion for the settlements.

As a result of these settlements, AIG made payments or placed amounts in escrow in the first three months of 2006 totaling approximately $1.64 billion, $225 million of which represented fines and penalties. Of these amounts, $676 million held in escrow is included in other assets and other liabilities at March 31, 2006. A substantial portion of the money will be available to resolve claims asserted in various regulatory and civil proceedings, including shareholder lawsuits.

Also, as part of the settlements, AIG has agreed to retain for a period of three years an independent consultant who will conduct a review that will include the adequacy of AIG's internal control over financial reporting and the remediation plan that AIG has implemented as a result of its own internal review.

Various federal and state regulatory agencies are reviewing certain transactions and practices of AIG and its subsidiaries in connection with industry-wide and other inquiries. AIG has cooperated, and will continue to cooperate, in producing documents and other information in response to the subpoenas.

A number of lawsuits have been filed regarding the subject matter of the investigations of insurance brokerage practices, including derivative actions, individual actions and class actions under the federal securities laws, Racketeer Influenced and Corrupt Organizations Act (RICO), Employee Retirement Income Security Act (ERISA) and state common and corporate laws in both federal and state courts, including the United States District Court for the Southern District of New York (Southern District of New York), in the Commonwealth of Massachusetts Superior Court and in Delaware Chancery Court. All of these actions generally allege that AIG and its subsidiaries violated the law by allegedly concealing a scheme to "rig bids" and "steer" business between insurance companies and insurance brokers.

Since October 19, 2004, AIG or its subsidiaries have been named as a defendant in sixteen complaints that were filed in federal court and two that were originally filed in state court (Massachusetts and Florida) and removed to federal court. These cases generally allege that AIG and its subsidiaries violated federal and various state antitrust laws, as well as federal RICO laws, various state deceptive and unfair practice laws and certain state laws governing fiduciary duties. The alleged basis of these claims is that there was a conspiracy between insurance companies and insurance brokers with regard to the use of contingent commission agreements, bidding practices, and other broker-related conduct concerning coverage in certain sectors of the insurance industry. The Judicial Panel on Multidistrict Litigation entered an order on February 17, 2005, consolidating most of these cases and transferring them to the United States District Court for the District of New Jersey (District of New Jersey). The remainder of these cases have been transferred to the District of New Jersey. On August 15, 2005, the plaintiffs in the multidistrict litigation filed a Corrected First Consolidated Amended Commercial Class Action Complaint, which, in addition to the previously named AIG defendants, names new AIG subsidiaries as defendants. Also on August 15, 2005, AIG and two subsidiaries were named as defendants in a Corrected First Consolidated Amended Employee Benefits Class Action Complaint filed in the District of New Jersey, which asserts similar claims with respect to employee benefits insurance and a claim under ERISA on behalf of putative classes of employers and employees. On November 29, 2005, the AIG defendants, along with other insurer defendants and the broker defendants filed motions to dismiss both the Commercial and Employee Benefits Complaints. Plaintiffs have filed a motion for class certification in

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(continued)*

6. Commitments and Contingent Liabilities *(continued)*

the consolidated action. Defendants have filed an opposition to the motion for class certification. On April 4, 2006, a complaint against AIG and several of its subsidiaries was filed in the United States District Court for the Northern District of Georgia alleging claims similar to what was alleged in the consolidated complaint. The defendants are seeking to transfer this case to the District of New Jersey for consolidation. In addition, complaints were filed against AIG and several of its subsidiaries in Massachusetts and Florida state courts, which have both been stayed. In the Florida action, the plaintiff has filed a petition for a writ of certiorari with the District Court of Appeals of the State of Florida, Fourth District with respect to the stay order. On February 9, 2006, a complaint against AIG and several of its subsidiaries was filed in Texas state court, making claims similar to those in the federal cases above.

In April and May 2005, amended complaints were filed in the consolidated derivative and securities cases, as well as in one of the ERISA lawsuits, pending in the Southern District of New York adding allegations concerning AIG's accounting treatment for non-traditional insurance products. In September 2005, a second amended complaint was filed in the consolidated securities cases adding allegations concerning AIG's first restatement of its financial statements described in the 2005 Annual Report on Form 10-K (the "First Restatement"), and a new securities action complaint was filed in the Southern District of New York, asserting claims premised on the same allegations made in the consolidated cases. In April 2006, motions to dismiss were denied in the securities actions. Also in September 2005, a class action complaint was filed to consolidate the ERISA cases pending in the Southern District of New York. Motions to dismiss in the consolidated action were filed in January 2006. Also in April 2005, new derivative actions were filed in Delaware Chancery Court, and in July and August 2005, two new derivative actions were filed in the Southern District of New York asserting claims duplicative of the claims made in the consolidated derivative action.

In July 2005, a second amended complaint was filed in the consolidated derivative case in the Southern District of New York, expanding upon accounting-related allegations, based upon the First Restatement. In June 2005, the derivative cases in Delaware were consolidated and, in August 2005, an amended consolidated complaint was filed. AIG's Board of Directors has appointed a special committee of independent directors to review the matters asserted in the derivative complaints. The courts have approved agreements staying the derivative cases pending in the Southern District of New York and in Delaware Chancery Court while the special committee of independent directors performs its work. In September 2005, a shareholder filed suit in Delaware Chancery Court seeking documents relating to some of the allegations made in the derivative suits. AIG filed a motion to dismiss in October 2005.

In late 2002, a derivative action was filed in Delaware Chancery Court in connection with AIG's transactions with certain entities affiliated with Starr and Starr International Company, Inc. (SICO). In May 2005, the plaintiff filed an amended complaint which adds additional claims premised on allegations relating to insurance brokerage practices and AIG's non-traditional insurance products. Plaintiffs in that case have agreed to dismiss newly added allegations unrelated to transactions with entities affiliated with Starr and SICO without prejudice to pursuit of these claims in the separate derivative actions described above. On February 16, 2006, the Delaware Chancery Court entered an order dismissing the litigation with prejudice with respect to AIG's outside directors and dismissing the claims against the remaining AIG defendants without prejudice.

AIG cannot predict the outcome of the matters described above or estimate the potential costs related to these matters and, accordingly, no reserve is being established in AIG's financial statements at this time. In the opinion of AIG management, AIG's ultimate liability for the matters referred to above is not likely to have a material adverse effect on AIG's consolidated financial condition, although it is possible that the effect would be material to AIG's consolidated results of operations for an individual reporting period.

(j) On July 8, 2005, SICO filed a complaint against AIG in the Southern District of New York. The complaint alleges that AIG is in the possession of items, including artwork, which SICO claims it owns, and seeks an order causing AIG to release those items as well as actual, consequential, punitive and exemplary damages. On September 27, 2005, AIG filed its answer to SICO's complaint denying SICO's allegations and asserting counter-claims for breach of contract, unjust enrichment, conversion and breach of fiduciary duty relating to SICO's breach of its commitment to use its AIG shares for the benefit of AIG and its employees. On October 17, 2005, SICO replied to AIG's counter-claims and additionally sought a judgment declaring that SICO is neither a control person nor an affiliate of AIG for purposes of Schedule 13D under the Securities Exchange Act of 1934, as amended (the Exchange Act), and Rule 144 under the Securities Act of 1933, as amended (the Securities Act), respectively. AIG responded to the SICO claims on November 7, 2005.

(k) AIG understands that some of its employees have received Wells notices in connection with previously disclosed SEC investigations of certain of AIG's transactions or accounting practices. Under SEC procedures, a Wells notice is an indication that the SEC staff has made a preliminary decision to recommend enforcement action that provides recipients with an opportunity to respond to the SEC staff before a

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(continued)*

6. Commitments and Contingent Liabilities *(continued)*

formal recommendation is finalized. AIG anticipates that additional current and former employees could receive similar notices in the future as the regulatory investigations proceed.

(l) AIG generates income tax credits as a result of investing in synthetic fuel production. Tax credits generated from the production and sale of synthetic fuel under Section 29 of the Internal Revenue Code are subject to an annual phase-out provision that is based on the average wellhead price of domestic crude oil. The price range within which the tax credits are phased-out was originally established in 1980 and is adjusted annually for inflation. Depending on the price of domestic crude oil for a particular year, all or a portion of the tax credits generated in that year might be eliminated. Tax credits reflected in the income tax provision for the first three months of 2006 have been reduced to reflect the estimated annual average oil price for 2006. Should the actual average oil price for 2006 exceed this estimate, further reductions in the tax credits could be required. Regardless of oil prices, the tax credits expire after 2007.

7. Employee Benefits

The following table presents the components of the net periodic benefit costs with respect to pensions and other benefits for the three months ended March 31, 2006 and 2005:

	Pensions			Postretirement		
(in millions)	Non-U.S. Plans	U.S. Plans	Total	Non-U.S. Plans	U.S. Plans	Total
2006						
Components of net period benefit cost:						
Service cost	**$ 19**	**$ 31**	**$ 50**	**$ 1**	**$ 1**	**$ 2**
Interest cost	**9**	**40**	**49**	**1**	**3**	**4**
Expected return on assets	**(7)**	**(48)**	**(55)**	**–**	**–**	**–**
Amortization of prior service cost	**(2)**	**(1)**	**(3)**	**–**	**(2)**	**(2)**
Recognized actuarial loss	**4**	**19**	**23**	**–**	**–**	**–**
Net period benefit cost	**$ 23**	**$ 41**	**$ 64**	**$ 2**	**$ 2**	**$ 4**
2005						
Components of net period benefit cost:						
Service cost	$ 19	$ 26	$ 45	$ 1	$ 2	$ 3
Interest cost	8	37	45	–	4	4
Expected return on assets	(5)	(41)	(46)	–	–	–
Amortization of prior service cost	(3)	(1)	(4)	–	(2)	(2)
FAS 88 loss due to settlements	1	–	1	–	–	–
Recognized actuarial loss	6	16	22	–	1	1
Net period benefit cost	$ 26	$ 37	$ 63	$ 1	$ 5	$ 6

8. Recent Accounting Standards

In March 2005, FASB issued FSP FIN46R-5 "Implicit Variable Interests under FASB Interpretation No. 46 (revised December 2003), Consolidation of Variable Interest Entities" (FSP FIN46R-5) to address whether a reporting enterprise has an implicit variable interest in a variable interest entity (VIE) or potential VIE when specific conditions exist. The identification of an implicit variable interest is a matter of judgment that depends on the relevant facts and circumstances. AIG's adoption of FSP FIN46R-5 on April 1, 2005 did not have a material effect on AIG's financial condition or results of operations.

At the March 2004 meeting, the Emerging Issue Task Force (EITF) reached a consensus with respect to Issue No. 03-1, "The Meaning of Other-Than-Temporary Impairment and Its Application to Certain Investments." On September 30, 2004, the FASB issued FASB Staff Position (FSP) EITF No. 03-1-1, Effective Date of Paragraphs 10-20 of EITF Issue No. 03-1, "The Meaning of Other-Than-Temporary Impairment and Its Application to Certain Investments" delaying the effective date of this guidance until the FASB has resolved certain implementation issues with respect to this guidance, but the disclosures remain effective. This FSP, retitled FSP FAS 115-1, "The Meaning of Other-Than-Temporary Impairment and Its Application to Certain Investments," replaces the measurement and recognition guidance set forth in Issue No. 03-1 and codifies certain existing guidance on impairment. AIG's adoption of FSP FAS 115-1 on January 1, 2006 did not have a material effect on AIG's consolidated financial condition or results of operations.

In December 2004, the FASB issued Statement No. 123 (revised 2004), "Share-Based Payment" (FAS 123R). FAS 123R and its related interpretive guidance replaces FAS No. 123, "Accounting for Stock-Based Compensation" (FAS 123), supersedes Accounting Principles Board Opinion

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(continued)*

8. Recent Accounting Standards *(continued)*

No. 25, "Accounting for Stock Issued to Employees" (APB 25) and amends FAS 95 "Statement of Cash Flows". FAS 123, as originally issued in 1995, established as preferable a fair-value-based method of accounting for share-based payment transactions with employees. On January 1, 2003, AIG adopted the recognition provisions of FAS 123. See also Note 10 herein. In April 2005, the SEC delayed the effective date for FAS 123R until the first fiscal year beginning after June 15, 2005. As a result, AIG adopted the provisions of the revised FAS 123R and its related interpretive guidance on January 1, 2006.

For its service-based awards (e.g. 1999 Stock Option Plan, 2002 Stock Incentive Plan and 1996 Employee Stock Purchase Plan), AIG recognizes compensation on a straight-line basis over the scheduled vesting period. Unrecognized unvested compensation expense for stock option awards granted under APB 25 (i.e., before January 1, 2003) will be recognized from January 1, 2006 to the vesting date. However, for the SICO Plans and the AIG Deferred Compensation Profit Participant Plan, which contain both performance and service conditions, AIG recognizes compensation utilizing a graded vesting expense attribution method. The effect of this approach is to recognize compensation cost over the requisite service period for each separately vesting tranche of the award.

AIG's share-based plans generally provide for accelerated vesting at retirement or after the participant turns 65. For awards granted after January 1, 2006, compensation expense is recognized ratably from the date of grant through the shorter of age 65 or the vesting period. The effect of this change was not material to AIG's consolidated financial position or results of operations. Awards granted prior to January 1, 2006 will continue to be recognized over the vesting period with accelerated expense recognition upon an actual retirement. SICO compensation expense for participants retiring after age 65 had been reflected in prior years' results consistent with vested status under the SICO Plans.

On June 1, 2005, FASB issued Statement No. 154, "Accounting Changes and Error Corrections" (FAS 154). FAS 154 replaces APB Opinion No. 20, "Accounting Changes" and FASB Statement No. 3, "Reporting Accounting Changes in Interim Financial Statements." FAS 154 requires that a voluntary change in accounting principles be applied retrospectively with all prior period financial statements presented based on the new accounting principle, unless it is impracticable to do so. FAS 154 also provides that a correction of errors in previously issued financial statements should be termed a "restatement." The new standard is effective for accounting changes and correction of errors beginning January 1, 2006.

At the June 2005 meeting, the EITF reached a consensus with respect to Issue No. 04-5, "Determining Whether a General Partner, or the General Partners as a Group, Controls a Limited Partnership or Similar Entity When the Limited Partners Have Certain Rights". The Issue addresses what rights held by the limited partner(s) preclude consolidation in circumstances in which the sole general partner would consolidate the limited partnership in accordance with generally accepted accounting principles absent the existence of the rights held by the limited partner(s). Based on that consensus, the EITF also agreed to amend the consensus in Issue No. 96-16, "Investor's Accounting for an Investee When the Investor Has a Majority of the Voting Interest but the Minority Shareholders Have Certain Approval or Veto Rights." The guidance in this Issue is effective after June 29, 2005 for general partners of all new limited partnerships formed and for existing limited partnerships for which the partnership agreements are modified. For general partners in all other limited partnerships, the guidance in this Issue is effective beginning January 1, 2006. The effect of the adoption of this EITF Issue was not material to AIG's consolidated financial condition or results of operations.

On June 29, 2005, FASB issued Statement 133 Implementation Issue No. B38, "Embedded Derivatives: Evaluation of Net Settlement with Respect to the Settlement of a Debt Instrument through Exercise of an Embedded Put Option or Call Option." This implementation guidance relates to the potential settlement of the debtor's obligation to the creditor that would occur upon exercise of the put option or call option, which meets the net settlement criterion in FAS 133. The effective date of the implementation guidance is January 1, 2006. The adoption of this guidance did not have a material effect on AIG's consolidated financial condition or results of operations.

On June 29, 2005, FASB issued Statement 133 Implementation Issue No. B39, "Application of Paragraph 13(b) to Call Options That Are Exercisable Only by the Debtor." The conditions in FAS 133 paragraph 13(b) do not apply to an embedded call option in a hybrid instrument containing a debt host contract if the right to accelerate the settlement of the debt can be exercised only by the debtor (issuer/borrower). This guidance does not apply to other embedded derivative features that may be present in the same hybrid instrument. The effective date of the implementation guidance is January 1, 2006. The adoption of this guidance did not have a material effect on AIG's consolidated financial condition or results of operations.

On September 19, 2005, FASB issued Statement of Position 05-1, "Accounting by Insurance Enterprises for Deferred Acquisition Costs in Connection with Modifications or Exchanges of Insurance Contracts." SOP 05-1 provides guidance on accounting for deferred acquisition costs on internal

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(continued)*

8. Recent Accounting Standards *(continued)*

replacements of insurance and investment contracts other than those specifically described in FASB Statement No. 97, "Accounting and Reporting by Insurance Enterprises for Certain Long-Duration Contracts and for Realized Gains and Losses from the Sale of Investments." The SOP defines an internal replacement as a modification in product benefits, features, rights, or coverage that occurs by the exchange of a contract for a new contract, or by amendment, endorsement, or rider to a contract, or by the election of a feature or coverage within a contract. The effective date of the implementation guidance is January 1, 2007. AIG is currently assessing the effect of implementing this guidance.

On February 16, 2006, FASB issued FAS No. 155, "Accounting for Certain Hybrid Financial Instruments" (FAS 155), an amendment of FAS 140 and FAS 133. FAS 155 allows AIG to include changes in fair value in earnings on an instrument-by-instrument basis for any hybrid financial instrument that contains an embedded derivative that would otherwise be required to be bifurcated and accounted for separately under FAS 133. The election to measure the hybrid instrument at fair value is irrevocable at the acquisition or issuance date.

AIG has elected to early adopt FAS 155 as of January 1, 2006, and apply FAS 155 fair value measurement to certain structured note liabilities and structured investments in AIG's available for sale portfolio that existed at December 31, 2005. The effect of this adoption resulted in an $11 million after-tax ($18 million pre-tax) decrease to opening retained earnings as of January 1, 2006, representing the difference between the fair value of these hybrid financial instruments and the prior carrying value as of December 31, 2005. The effect of adoption on after-tax gross gains and losses was $218 million ($336 million pre-tax) and $229 million ($354 million pre-tax), respectively.

Effective with AIG's early adoption of FAS 155, structured note liabilities of $6.1 billion and hybrid financial instruments of $512 million at March 31, 2006 are now carried at fair value. The effect on earnings in the first three months of 2006 for changes in the fair value of hybrid financial instruments was a pre-tax gain of $30 million and is reflected in income.

On March 27, 2006, FASB issued FSP FTB 85-4-1, "Accounting for Life Settlement Contracts by Third-Party Investors" (FSP 85-4-1), an amendment of FTB 85-4, "Accounting for Purchases of Life Insurance". Life settlements are designed to assist life insurance policyholders in monetizing the existing value of life insurance policies. FSP 85-4-1 allows AIG to measure life settlement contracts using either the investment method or fair value method. The election is made on an instrument-by-instrument basis and is irrevocable. AIG elected to early adopt FSP 85-4-1 as of January 1, 2006 using the investment method for pre-existing investments held at December 31, 2005. The effect of this adoption resulted in a $319 million after tax ($487 million pre-tax) increase to opening retained earnings for its share of the life settlement contracts held in certain non-consolidated trusts.

On April 13, 2006, FASB issued FSP FIN 46(R)-6, "Determining the Variability to be Considered in Applying FASB Interpretation No. 46(R)" (FIN 46(R)-6 or FSP). The FSP affects the identification of which entities are variable interest entities through a "by design" approach in identifying and measuring the variable interests of the variable interest entity and its primary beneficiary. Under FIN 46(R), "Consolidation of Variable Interest Entities", the requirements are to be applied to all such variable interest entities after September 30, 2006. The new requirements need not be applied to entities that have previously been analyzed under FIN 46(R) unless a reconsideration event occurs. The adoption of this guidance is not expected to have a material effect on AIG's consolidated financial condition or results of operations.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(continued)*

9. Information Provided in Connection with Outstanding Debt

The following condensed consolidating financial statements are provided in compliance with Regulation S-X of the Securities and Exchange Commission.

(a) American General Corporation (AGC) is a holding company and a wholly owned subsidiary of AIG. AIG provides a full and unconditional guarantee of all outstanding debt of AGC.

American General Corporation:

Condensed Consolidating Balance Sheet

March 31, 2006 *(in millions) (unaudited)*	**American International Group, Inc. Guarantor**	**AGC Issuer**	**Other Subsidiaries**	**Eliminations**	**Consolidated AIG**
Assets:					
Invested assets	**$ 112**	**$ –**	**$ 708,296**	**$ (13,844)**	**$694,564**
Cash	**125**	**–**	**1,123**	**–**	**1,248**
Carrying value of subsidiaries and partially owned companies, at equity	**95,636**	**26,262**	**11,295**	**(132,026)**	**1,167**
Other assets	**3,755**	**2,618**	**178,292**	**(1,846)**	**182,819**
Total assets	**$99,628**	**$28,880**	**$ 899,006**	**$ (147,716)**	**$879,798**
Liabilities:					
Insurance liabilities	**$ 354**	**$ –**	**$ 472,310**	**$ (64)**	**$472,600**
Debt	**4,587**	**2,086**	**125,655**	**(13,547)**	**118,781**
Other liabilities	**6,297**	**3,915**	**191,799**	**(2,173)**	**199,838**
Total liabilities	**11,238**	**6,001**	**789,764**	**(15,784)**	**791,219**
Preferred shareholders' equity in subsidiary companies	**–**	**–**	**189**	**–**	**189**
Total shareholders' equity	**88,390**	**22,879**	**109,053**	**(131,932)**	**88,390**
Total liabilities, preferred shareholders' equity in subsidiary companies and shareholders' equity	**$99,628**	**$28,880**	**$ 899,006**	**$ (147,716)**	**$879,798**

December 31, 2005 *(in millions) (unaudited)*	American International Group, Inc. Guarantor	AGC Issuer	Other Subsidiaries	Eliminations	Consolidated AIG
Assets:					
Invested assets	$ 1,392	$ –	$691,349	$ (13,696)	$679,045
Cash	190	–	1,707	–	1,897
Carrying value of subsidiaries and partially owned companies, at equity	90,723	27,027	15,577	(132,169)	1,158
Other assets	2,768	2,577	166,933	(1,327)	170,951
Total assets	$95,073	$29,604	$875,566	$(147,192)	$853,051
Liabilities:					
Insurance liabilities	$ 408	$ –	$460,271	$ (56)	$460,623
Debt	4,607	2,087	115,212	(12,057)	109,849
Other liabilities	3,741	4,110	191,279	(3,054)	196,076
Total liabilities	8,756	6,197	766,762	(15,167)	766,548
Preferred shareholders' equity in subsidiary companies	–	–	186	–	186
Total shareholders' equity	86,317	23,407	108,618	(132,025)	86,317
Total liabilities, preferred shareholders' equity in subsidiary companies and shareholders' equity	$95,073	$29,604	$875,566	$(147,192)	$853,051

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(continued)*

9. Information Provided in Connection with Outstanding Debt *(continued)*

Condensed Consolidating Statement of Income

Three Months Ended March 31, 2006 *(in millions) (unaudited)*	**American International Group, Inc. Guarantor**	**AGC Issuer**	**Other Subsidiaries**	**Eliminations**	**Consolidated AIG**
Operating income (loss)	**$ (286)**	**$ (38)**	**$5,117**	**$ –**	**$4,793**
Equity in undistributed net income of consolidated subsidiaries	**3,260**	**359**	**–**	**(3,619)**	**–**
Dividend income from consolidated subsidiaries	**187**	**304**	**–**	**(491)**	**–**
Income taxes (benefits)	*****	**(13)**	**1,448**	**–**	**1,435**
Minority interest	**–**	**–**	**(197)**	**–**	**(197)**
Cumulative effect of an accounting change, net of tax	**34**	**–**	**–**	**–**	**34**
Net income (loss)	**$3,195**	**$638**	**$3,472**	**$(4,110)**	**$3,195**

** Amounts significantly less than $1 million.*

Three Months Ended March 31, 2005 *(in millions) (unaudited)*	American International Group, Inc. Guarantor	AGC Issuer	Other Subsidiaries	Eliminations	Consolidated AIG
Operating income (loss)	$ (10)	$ (36)	$5,695	$ –	$5,649
Equity in undistributed net income of consolidated subsidiaries	3,646	701	–	(4,347)	–
Dividend income from consolidated subsidiaries	271	–	–	(271)	–
Income taxes (benefits)	108	(12)	1,610	–	1,706
Minority interest	–	–	(144)	–	(144)
Net income (loss)	$3,799	$677	$3,941	$(4,618)	$3,799

Condensed Consolidating Statements of Cash Flow

Three Months Ended March 31, 2006 *(in millions) (unaudited)*	**American International Group, Inc. Guarantor**	**AGC Issuer**	**Other Subsidiaries**	**Consolidated AIG**
Net cash provided by operating activities	**$(1,139)**	**$ 45**	**$ 4,160**	**$ 3,066**
Cash flows from investing:				
Invested assets disposed	**1,269**	**–**	**38,122**	**39,391**
Invested assets acquired	**–**	**–**	**(59,006)**	**(59,006)**
Other	**(2,283)**	**–**	**1,961**	**(322)**
Net cash used in investing activities	**(1,014)**	**–**	**(18,923)**	**(19,937)**
Cash flows from financing activities:				
Change in debts	**2,262**	**(1)**	**6,668**	**8,929**
Other	**(174)**	**(44)**	**6,961**	**6,743**
Net cash (used in) provided by financing activities	**2,088**	**(45)**	**13,629**	**15,672**
Effect of exchange rate changes on cash	**–**	**–**	**550**	**550**
Change in cash	**(65)**	**–**	**(584)**	**(649)**
Cash at beginning of period	**190**	**–**	**1,707**	**1,897**
Cash at end of period	**$ 125**	**$ –**	**$ 1,123**	**$ 1,248**

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(continued)*

9. Information Provided in Connection with Outstanding Debt *(continued)*

Three Months Ended March 31, 2005 *(in millions) (unaudited)*	American International Group, Inc. Guarantor	AGC Issuer	Other Subsidiaries	Consolidated AIG
Net cash (used in) provided by operating activities	$ 373	$ 155	$ (962)	$ (434)
Cash flows from investing:				
Invested assets disposed	265	–	48,207	48,472
Invested assets acquired	–	–	(68,402)	(68,402)
Other	(72)	(120)	4	(188)
Net cash (used in) provided by investing activities	193	(120)	(20,191)	(20,118)
Cash flows from financing activities:				
Change in debts	(34)	1	9,231	9,198
Other	(429)	(36)	12,228	11,763
Net cash provided by (used in) financing activities	(463)	(35)	21,459	20,961
Effect of exchange rate changes on cash	30	–	(87)	(57)
Change in cash	133	–	219	352
Cash at beginning of period	17	–	1,992	2,009
Cash at end of period	$ 150	$ –	$ 2,211	$ 2,361

(b) AIG Liquidity Corp. is a wholly owned subsidiary of AIG. AIG provides a full and unconditional guarantee of all obligations of AIG Liquidity Corp., which commenced operations in 2003.

AIG Liquidity Corp.:

Condensed Consolidating Balance Sheet

March 31, 2006 *(in millions) (unaudited)*	**American International Group, Inc. Guarantor**	**AIG Liquidity Corp.**	**Other Subsidiaries**	**Eliminations**	**Consolidated AIG**
Assets:					
Invested assets	**$ 112**	**$ ***	**$708,296**	**$ (13,844)**	**$694,564**
Cash	**125**	****	**1,123**	**–**	**1,248**
Carrying value of subsidiaries and partially owned companies, at equity	**95,636**	**–**	**37,557**	**(132,026)**	**1,167**
Other assets	**3,755**	****	**180,910**	**(1,846)**	**182,819**
Total assets	**$99,628**	**$ ***	**$927,886**	**$ (147,716)**	**$879,798**
Liabilities:					
Insurance liabilities	**$ 354**	**$ –**	**$472,310**	**$ (64)**	**$472,600**
Debt	**4,587**	****	**127,741**	**(13,547)**	**118,781**
Other liabilities	**6,297**	****	**195,714**	**(2,173)**	**199,838**
Total liabilities	**11,238**	****	**795,765**	**(15,784)**	**791,219**
Preferred shareholders' equity in subsidiary companies	**–**	**–**	**189**	**–**	**189**
Total shareholders' equity	**88,390**	****	**131,932**	**(131,932)**	**88,390**
Total liabilities, preferred shareholders' equity in subsidiary companies and shareholders' equity	**$99,628**	**$ ***	**$927,886**	**$ (147,716)**	**$879,798**

** Amounts significantly less than $1 million.*

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(continued)*

9. Information Provided in Connection with Outstanding Debt *(continued)*

December 31, 2005 *(in millions) (unaudited)*	American International Group, Inc. Guarantor	AIG Liquidity Corp.	Other Subsidiaries	Eliminations	Consolidated AIG
Assets:					
Invested assets	$ 1,392	$ *	$691,349	$ (13,696)	$679,045
Cash	190	*	1,707	–	1,897
Carrying value of subsidiaries and partially owned companies, at equity	90,723	–	42,604	(132,169)	1,158
Other assets	2,768	*	169,510	(1,327)	170,951
Total assets	$95,073	$ *	$905,170	$(147,192)	$853,051
Liabilities:					
Insurance liabilities	$ 408	$ –	$460,271	$ (56)	$460,623
Debt	4,607	*	117,299	(12,057)	109,849
Other liabilities	3,741	*	195,389	(3,054)	196,076
Total liabilities	8,756	*	772,959	(15,167)	766,548
Preferred shareholders' equity in subsidiary companies	–	–	186	–	186
Total shareholders' equity	86,317	*	132,025	(132,025)	86,317
Total liabilities, preferred shareholders' equity in subsidiary companies and shareholders' equity	$95,073	$ *	$905,170	$(147,192)	$853,051

**Amounts significantly less than $1 million.*

Condensed Consolidating Statement of Income

Three Months Ended March 31, 2006 *(in millions) (unaudited)*	**American International Group, Inc. Guarantor**	**AIG Liquidity Corp.**	**Other Subsidiaries**	**Eliminations**	**Consolidated AIG**
Operating income (loss)	**$ (286)**	**$ ***	**$5,079**	**$ –**	**$4,793**
Equity in undistributed net income of consolidated subsidiaries	**3,260**	**–**	**359**	**(3,619)**	**–**
Dividend income from consolidated subsidiaries	**187**	**–**	**304**	**(491)**	**–**
Income taxes	*****	*****	**1,435**	**–**	**1,435**
Minority interest	**–**	**–**	**(197)**	**–**	**(197)**
Cumulative effect of an accounting change, net of tax	**34**	**–**	**–**	**–**	**34**
Net income (loss)	**$3,195**	**$ ***	**$4,110**	**$(4,110)**	**$3,195**

**Amounts significantly less than $1 million.*

Three Months Ended March 31, 2005 *(in millions) (unaudited)*	American International Group, Inc. Guarantor	AIG Liquidity Corp.	Other Subsidiaries	Eliminations	Consolidated AIG
Operating income (loss)	$ (10)	$ *	$ 5,659	$ –	$5,649
Equity in undistributed net income of consolidated subsidiaries	3,646	–	701	(4,347)	–
Dividend income from consolidated subsidiaries	271	–	–	(271)	–
Income taxes	108	*	1,598	–	1,706
Minority interest	–	–	(144)	–	(144)
Net income (loss)	$3,799	$ *	$ 4,618	$(4,618)	$3,799

**Amounts significantly less than $1 million.*

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(continued)*

9. Information Provided in Connection with Outstanding Debt *(continued)*

Condensed Consolidating Statements of Cash Flow

Three Months Ended March 31, 2006 *(in millions) (unaudited)*	**American International Group, Inc. Guarantor**	**AIG Liquidity Corp.**	**Other Subsidiaries**	**Consolidated AIG**
Net cash provided by operating activities	**$(1,139)**	**$ ***	**$ 4,205**	**$ 3,066**
Cash flows from investing:				
Invested assets disposed	**1,269**	**–**	**38,122**	**39,391**
Invested assets acquired	**–**	**–**	**(59,006)**	**(59,006)**
Other	**(2,283)**	*****	**1,961**	**(322)**
Net cash used in investing activities	**(1,014)**	*****	**(18,923)**	**(19,937)**
Cash flows from financing activities:				
Change in debts	**2,262**	**–**	**6,667**	**8,929**
Other	**(174)**	*****	**6,917**	**6,743**
Net cash (used in) provided by financing activities	**2,088**	*****	**13,584**	**15,672**
Effect of exchange rate changes on cash	**–**	**–**	**550**	**550**
Change in cash	**(65)**	*****	**(584)**	**(649)**
Cash at beginning of period	**190**	**–**	**1,707**	**1,897**
Cash at end of period	**$ 125**	**$ ***	**$ 1,123**	**$ 1,248**

**Amounts significantly less than $1 million.*

Three Months Ended March 31, 2005 *(in millions) (unaudited)*	American International Group, Inc. Guarantor	AIG Liquidity Corp.	Other Subsidiaries	Consolidated AIG
Net cash (used in) provided by operating activities	$ 373	$ *	$ (807)	$ (434)
Cash flows from investing:				
Invested assets disposed	265	–	48,207	48,472
Invested assets acquired	–	–	(68,402)	(68,402)
Other	(72)	*	(116)	(188)
Net cash (used in) provided by investing activities	193	*	(20,311)	(20,118)
Cash flows from financing activities:				
Change in debts	(34)	–	9,232	9,198
Other	(429)	*	12,192	11,763
Net cash (used in) provided by financing activities	(463)	*	21,424	20,961
Effect of exchange rate changes on cash	30	–	(87)	(57)
Change in cash	133	*	219	352
Cash at beginning of period	17	–	1,992	2,009
Cash at end of period	$ 150	$ *	$ 2,211	$ 2,361

**Amounts significantly less than $1 million.*

10. Stock Compensation Plans

At March 31, 2006, AIG employees could receive compensation pursuant to six different stock-based compensation plan arrangements: (i) AIG 1999 Stock Option Plan, as amended (1999 Plan); (ii) AIG 1996 Employee Stock Purchase Plan, as amended (the 1996 Plan); (iii) AIG 2002 Stock Incentive Plan, as amended (2002 Plan) under which AIG has to date issued only restricted stock units (RSUs); (iv) SICO's Deferred Compensation Profit Participation Plans (SICO Plans); (v) AIG's 2005-2006 Deferred Compensation Profit Participation Plan (AIG DCPPP) and (vi) the AIG Partners Plan. The AIG DCPPP was adopted as a replacement for the SICO Plans for the 2005-2006 period, and the AIG Partners Plan will replace the AIG DCPPP for future years, although no awards have been made under this plan as of March 31, 2006. Stock-based compensation earned under the AIG DCPPP and the AIG Partners Plan will be issued as awards under the 2002 Plan. AIG currently settles share option exercises and other share awards to participants through the issuance of shares it has previously acquired and holds in its treasury account, except for share awards made by SICO, which are settled by SICO.

At March 31, 2006, AIG's non-employee directors received stock-based compensation in two forms, options granted pursuant to the 1999 Plan and grants of AIG common stock with delivery deferred until retirement from the Board, pursuant to the AIG Director Stock Plan, which was approved by the shareholders at the 2004 Annual Meeting of Shareholders.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(continued)*

10. Stock Compensation Plans *(continued)*

Effective January 1, 2003, AIG adopted FAS 123 utilizing the prospective method to account for awards granted after January 1, 2003. Prior to adoption of FAS 123, AIG followed the provisions of Accounting Principles Board Opinion No. 25. See Note 8 herein. Under the recognition provisions of FAS 123, costs with respect to stock compensation were measured using the fair value of the shares subscribed or granted at the date of grant recognized ratably over the vesting period. Such fair value was derived through an option pricing model or the fair value of AIG's common stock, as applicable.

Effective January 1, 2006, AIG adopted FAS 123R utilizing the modified prospective application method which provides that previously issued financial statements need not be restated. Awards granted or modified after January 1, 2006 and outstanding awards not yet vested as of January 1, 2006 will be accounted for under FAS 123R.

FAS 123R requires AIG to estimate forfeitures in calculating the expense relating to stock-based compensation, rather than recognizing these forfeitures and corresponding reductions in expense as they occur. The pre-tax cumulative effect of adoption, recognized as a reduction in stock-based compensation expense of $46 million ($34 million after-tax), was recorded as the cumulative effect of an accounting change, net of tax in the consolidated statement of income during the first three months of 2006.

The effect of the adoption of FAS 123R on the consolidated statements of income and cash flows was as follows:

Three Months Ended March 31, 2006 *(in millions, except per share data)*	**Pre-adoption of FAS 123R**	**Effect of Adoption of FAS 123R**	**Including Effect of Adoption of FAS 123R**
Income before income taxes, minority interest and cumulative effect of an accounting change	**$ 4,801**	**$ (8)**	**$ 4,793**
Provision for income taxes	**$ 1,438**	**$ (3)**	**$ 1,435**
Income before minority interest and cumulative effect of an accounting change	**$ 3,363**	**$ (5)**	**3,358**
Cumulative effect of an accounting change, net of tax	**$ –**	**$ 34**	**$ 34**
Net income	**$ 3,166**	**$ 29**	**$ 3,195**
Net cash provided by operating activities	**$ 3,068**	**$ (2)**	**$ 3,066**
Net cash provided by financing activities	**$15,670**	**$ 2**	**$15,672**
Basic earnings per share	**$ 1.22**	**$ –**	**$ 1.22**
Diluted earnings per share	**$ 1.22**	**$ –**	**$ 1.22**

The following table presents share-based compensation expenses, including the cumulative effect of adoption of FAS 123R, included in AIG's consolidated statement of income:

Three Months Ended March 31, 2006 *(in millions)*	
Share-based compensation expense before tax	**$154**
Income tax benefit	**$ 12**
After-tax compensation expense	**$142**

Included in share-based compensation expense of $154 million was approximately $54 million related to the Starr tender offer and various adjustments totalling $61 million, primarily relating to stock-split adjustments and other miscellaneous items for the SICO plans, offset by a $46 million pre-tax adjustment for the cumulative effect of the adoption of FAS 123R. See Note 4 herein for a discussion of the Starr tender offer and Note 8 herein for discussion of prospective change to the accounting for retiree eligibility provisions and forfeiture treatment.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(continued)*

If AIG had adopted the FAS 123 provisions for recognizing compensation expense commencing at the date of grant of the awards, the effect would not have been material to net income or basic or diluted earnings per share for the three months ended March 31, 2005.

1999 Stock Option Plan

The 1999 Plan provides that options to purchase a maximum of 45,000,000 shares of common stock can be granted to certain key employees and members of the Board of Directors at prices not less than fair market value at the date of grant.

The 1999 Plan was approved by the shareholders at the 2000 Annual Meeting of Shareholders, with certain amendments approved at the 2003 Annual Meeting of Shareholders. The 1999 Plan superseded the 1991 employee stock option plan (the 1991 Plan), although outstanding options granted under the 1991 Plan continue in force until exercise or expiration. The maximum number of shares that may be granted to any employee in any one year under the 1999 Plan is 900,000. Options granted under the 1999 Plan generally vest over four years (25 percent vesting per year) and expire 10 years from the date of grant.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(continued)*

10. Stock Compensation Plans *(continued)*

At March 31, 2006, there were 20,431,101 shares reserved for future grants under the 1999 Plan and 28,935,898 shares reserved for issuance under the 1999 and 1991 Plans.

In 2004, AIG developed a binomial lattice model to calculate the fair value of stock option grants. In prior years, a Black-Scholes model was used. A more detailed description of the valuation methodology is provided below.

The following weighted average assumptions were used for stock options granted in the first three months of 2006:

Expected annual dividend yield[1]	0.71%
Expected volatility[2]	27.3%
Risk-free interest rate[3]	4.17%
Expected term[4]	7 years

(1) The dividend yield is based on the dividend yield over the twelve month period prior to the grant date.

(2) Expected volatility is the average of historical volatility (based on seven years of daily stock price changes) and the implied volatility of actively traded options on AIG shares.

(3) The interest rate curves used in the valuation model were the US Treasury STRIP rates with terms from 3 months to 10 years.

(4) The contractual term of the option is generally 10 years with an expected term of 7 years calculated based on an analysis of historical employee exercise behavior and employee turnover (post-vesting terminations). The early exercise rate is a function of time elapsed since the grant. Fifteen years of historical data was used to estimate the early exercise rate.

Additional information with respect to AIG's stock option plans at March 31, 2006, and changes for the three months then ended, were as follows:

Options:	Shares	Weighted Average Exercise Price
Outstanding at beginning of year	52,545,425	$54.84
Granted	41,000	$68.65
Exercised	(538,784)	$40.80
Forfeited or expired	(374,181)	$69.57
Outstanding at end of period	51,673,460	$54.89
Options exercisable at end of period	40,389,118	$52.59
Weighted average fair value per share of options granted		$22.38

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(continued)*

10. Stock Compensation Plans *(continued)*

Information about stock options outstanding at March 31, 2006, is summarized as follows:

	Options Outstanding				Options Exercisable			
Range of Exercise Prices	Number Outstanding	Weighted Average Remaining Contractual Life	Weighted Average Exercise Price	Aggregate Intrinsic Values (in millions)	Number Exercisable (vested)	Weighted Average Remaining Contractual Life	Weighted Average Exercise Price	Aggregate Intrinsic Values (in millions)
$11.28-$27.14	6,755,947	1.06	$21.32	$302	6,755,947	1.06	$21.32	$302
$30.44-$41.51	5,402,644	2.29	$36.87	158	5,402,644	2.29	$36.87	158
$43.31-$53.40	7,056,736	4.61	$48.56	124	6,234,130	4.31	$48.77	108
$54.11-$59.99	8,440,050	4.86	$57.84	70	6,324,940	3.32	$57.34	55
$60.13-$63.95	9,241,271	6.67	$62.33	35	6,099,845	6.27	$61.92	26
$64.01-$69.63	8,302,783	7.56	$65.45	6	3,837,847	5.61	$65.66	2
$70.35-$98.00	6,474,029	5.16	$83.88	–	5,733,765	5.07	$84.48	–
Total	51,673,460	4.86	$54.89	$695	40,389,118	3.87	$52.59	$651

Vested or expected-to-vest options as of March 31, 2006 were 46,168,298 shares, of which 40,389,118 were vested, with a weighted average exercise price of $53.70, a weighted average contractual life of 4.32 years and an aggregate intrinsic value of $678 million, of which $651 million is attributable to the vested options.

As of March 31, 2006, total unrecognized compensation cost (net of expected forfeitures) totalled $204 million and $4 million related to nonvested share-based compensation awards granted under the 1999 Plan and the 1996 Plan, respectively, with a blended weighted-average period of 1.40 years and 0.5 years, respectively. The costs of awards outstanding under these plans at March 31, 2006 is expected to be recognized over approximately three years and one year for the 1999 Plan and the 1996 Plan, respectively.

The intrinsic value of options exercised during the three months ending March 31, 2006 was approximately $15 million. The fair value of options vesting during the period was approximately $26 million. AIG received $27 million and $19 million in cash from the exercise of stock options during the three months ended March 31, 2006 and 2005, respectively. AIG did not cash-settle any share-based payment awards during the three months ended March 31, 2006 and 2005. The tax benefits realized as a result of stock option exercises were $4 million and $6 million for the first three months of 2006 and 2005, respectively.

2002 Stock Incentive Plan

AIG's 2002 Plan was adopted at the 2002 shareholders meeting and amended and restated by the AIG Board of Directors on September 18, 2002 (the 2002 Plan). The 2002 Plan provides that equity-based or equity-related awards with respect to shares of common stock can be issued to employees in any year up to a maximum of that number of shares equal to (a) 1,000,000 shares plus (b) the number of shares available but not issued in the prior calendar year. The maximum award that a grantee may receive under the 2002 Plan per year is rights with respect to 250,000 shares. For the three months ended March 31, 2006 and 2005, respectively, 66,715 and 13,940 RSUs were granted by AIG. There were 14,665,260 shares reserved for issuance in connection with future awards as of March 31, 2006. Substantially all RSUs granted to date under the 2002 Plan vest on the fourth anniversary of the date of grant.

Director Stock Awards

The methodology used for valuing employee stock options is also used to value director stock options. Director stock options vest one year after the grant date, but are otherwise the same as employee stock options. Options with respect to 5,000 shares and no shares were granted during the first three months of 2006 and 2005, respectively.

AIG also granted 3,750 shares and 1,250 shares, with delivery deferred, to directors during the first three months of 2006 and 2005, respectively, under the Director Stock Plan. At March 31, 2006, there were 81,250 shares reserved for future grants under the Director Stock Plan.

Employee Stock Purchase Plan

AIG's 1996 Plan provides that eligible employees (those employed at least one year) may receive privileges to purchase

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(continued)*

10. Stock Compensation Plans *(continued)*

up to an aggregate of 10,000,000 shares of AIG common stock, at a price equal to 85 percent of the fair market value on the date of the grant of the purchase privilege. Purchase privileges are granted quarterly and are limited to the number of whole shares that can be purchased on an annual basis by an amount equal to the lesser of 10 percent of an employee's annual salary or $10,000.

SICO Plans

The SICO Plans provide that shares of AIG common stock currently held by SICO are set aside for the benefit of the participant and distributed upon retirement. The SICO Board of Directors currently may permit an early payout of units under certain circumstances. Prior to payout, the participant is not entitled to vote, dispose of or receive dividends with respect to such shares, and shares are subject to forfeiture under certain conditions, including but not limited to the participant's termination of employment with AIG prior to normal retirement age.

Historically, SICO's Board of Directors could elect to pay a participant cash in lieu of shares of AIG common stock. On December 9, 2005, SICO notified participants that essentially all subsequent distributions would be made only in shares, and not cash. As of that date, AIG modified its accounting for the SICO Plans from variable to fixed measurement accounting. Variable measurement accounting will still be used for those few awards for which cash elections had been made prior to March 2005. The SICO Plans are also described in Note 4 herein.

Although none of the costs of the various benefits provided under the SICO Plans has been paid by AIG, AIG has recorded a charge to reported earnings for the deferred compensation amounts paid to AIG employees by SICO, with an offsetting amount credited to additional paid-in capital reflecting amounts deemed contributed by SICO.

As of December 9, 2005, there were 12,650,292 non-vested AIG shares under the SICO Plans with a weighted-average fair value per share of $61.92. As of March 31, 2006, there were 12,307,967 non-vested AIG shares under the SICO Plans with a weighted-average fair value per share of $61.92.

A significant portion of the awards under the SICO Plans vest upon retirement if the participant reaches age 65. The portion of the awards for which early payout is available vest on the applicable payout date.

AIG DCPPP

Effective September 21, 2005, AIG adopted the AIG DCPPP, which provides equity-based compensation to key AIG employees, including senior executive officers. The AIG DCPPP was modeled on the SICO Plans.

The AIG DCPPP will contingently allocate a fixed number of shares to each participant if AIG's cumulative adjusted earnings per share for 2005 and 2006 exceed that for 2003 and 2004. The performance period is September 21, 2005 to December 31, 2006. At the end of the performance period, common shares are contingently allocated. The service period and related vesting consists of three pre-retirement tranches and a final retirement tranche at age 65.

At March 31, 2006, there were units representing 4,898,880 shares granted to participants.

AIG Partners Plan

The AIG Partners Plan was approved on March 16, 2006 by AIG's Compensation Committee. No awards have been made under the Plan as of March 31, 2006.

VALUATION

The fair value of each award granted under the 2002 Plan, the SICO Plans, the AIG DCPPP, and the AIG Partners Plan is based on the closing price of AIG stock on the date of grant.

A summary of shares relating to outstanding awards not yet vested under the foregoing plans as of March 31, 2006, and changes during the three months ended March 31, 2006 is presented below:

	Number of Shares			Weighted Average Grant-Date Fair Value		
	2002 Plan	SICO Plan	AIG DCPPP	2002 Plan	SICO Plan	AIG DCPPP
Not yet vested at January 1, 2006	4,322,265	12,650,292	4,898,880	$63.63	$61.92	$52.55
Granted	66,715	–	–	$69.13	–	–
Vested	(3,620)	(132,511)	–	$65.13	$61.92	–
Forfeited	(56,340)	(209,814)	(165,450)	$60.66	$61.92	$59.40
Not yet vested at March 31, 2006	4,329,020	12,307,967	4,733,430	$63.75	$61.92	$52.31

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(continued)*

10. Stock Compensation Plans *(continued)*

At March 31, 2006, the total unrecognized compensation cost (net of expected forfeitures) related to nonvested share-based compensation awards granted under the 2002 Plan, the SICO Plans, and the AIG DCPPP and the blended weighted-average period over which that cost is expected to be recognized is as follows:

	Unrecognized Compensation Cost *(in millions)*	Blended Weighted-Average Period
2002 Plan	$196	1.83 years
SICO Plans	$357	6.08 years
AIG DCPPP	$248	11.62 years

The total cost for awards outstanding as of March 31, 2006 under the 2002 Plan, the SICO Plans and the AIG DCPPP is expected to be recognized over approximately four years, 12 years and 23 years, respectively.

The AIG Board of Directors has construed the AIG stock option plans to allow, at the request of an optionee, the deferral of delivery of AIG shares otherwise deliverable upon the exercise of an option to a date or dates specified by the optionee. During 2005, options with respect to 1,731,471 shares were exercised with delivery deferred. At December 31, 2005, optionees had made valid elections to defer delivery of 2,067,643 shares of AIG common stock upon exercise of options expiring during 2006. In addition, nonemployee directors of AIG had made valid elections to defer delivery of 21,093 shares of AIG common stock upon exercise of options expiring during 2006.

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Management's Discussion and Analysis of Financial Condition and Results of Operations is designed to provide the reader a narrative with respect to AIG's operations, financial condition and liquidity and certain other significant matters.

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Cautionary Statement Regarding Projections and Other Information About Future Events

This Quarterly Report and other publicly available documents may include, and AIG's officers and representatives may from time to time make, projections concerning financial information and statements concerning future economic performance and events, plans and objectives relating to management, operations, products and services, and assumptions underlying these projections and statements. These projections and statements are not historical facts but instead represent only AIG's belief regarding future events, many of which, by their nature, are inherently uncertain and outside AIG's control. These projections and statements may address, among other things, the status and potential future outcome of the current regulatory and civil proceedings against AIG and their potential effect on AIG's businesses, financial position, results of operations, cash flows and liquidity, the effect of the credit rating downgrades on AIG's businesses and competitive position, the unwinding and resolving of various relationships between AIG and Starr and SICO, and AIG's strategy for growth, product development, market position, financial results and reserves. It is possible that AIG's actual results and financial condition may differ, possibly materially, from the anticipated results and financial condition indicated in these projections and statements. Factors that could cause AIG's actual results to differ, possibly materially, from those in the specific projections and statements are discussed throughout this Management's Discussion and Analysis of Financial Condition and Results of Operations and in "Risk Factors" in Item 1A. of Part I of AIG's 2005 Annual Report on Form 10-K and Item 1A. of Part II of this Quarterly Report. AIG is not under any obligation (and expressly disclaims any such obligations) to update or alter any projections or other statement, whether written or oral, that may be made from time to time, whether as a result of new information, future events or otherwise.

Throughout this Management's Discussion and Analysis of Financial Condition and Results of Operations, AIG presents its operations in the way it believes will be most meaningful. Statutory loss ratios and combined ratios are presented in accordance with accounting principles prescribed by insurance regulatory authorities because these are standard measures of performance filed with insurance regulatory authorities and used for analysis in the insurance industry and thus allow more meaningful comparisons with AIG's insurance competitors. AIG has also incorporated into this discussion a number of cross-references to additional information included throughout this Form 10-Q and its 2005 Annual Report on Form 10-K to assist readers seeking related information on a particular subject.

Overview of Operations and Business Results

AIG identifies its reportable segments by product line, consistent with its management structure. AIG's major product and service groupings are General Insurance, Life Insurance & Retirement Services, Financial Services and Asset Management. AIG's operations in 2006 are conducted by its subsidiaries principally through these segments. Through these segments, AIG provides insurance and investment products and services to both businesses and individuals in more than 130 countries and jurisdictions. This geographic, product and service diversification is one of AIG's major strengths and sets it apart from its competitors.

AIG's subsidiaries serve commercial, institutional and individual customers through an extensive property-casualty and life insurance and retirement services network. In the United States, AIG companies are the largest underwriters of commercial and industrial insurance and one of the largest life insurance and retirement services operations as well. AIG's Financial Services businesses include commercial aircraft and equipment leasing, capital markets operations and consumer finance, both in the United States and abroad. AIG also provides asset management services and offers guaranteed investment contracts (GICs) to institutions and individuals.

AIG's operating performance reflects implementation of various long-term strategies and defined goals in its various operating segments. A primary goal of AIG in managing its General Insurance operations is to achieve an underwriting profit. To achieve this goal, AIG must be disciplined in its risk selection and premiums must be adequate and terms and conditions appropriate to cover the risk accepted. AIG also believes in strict control of expenses.

A central focus of AIG operations in recent years is the development and expansion of new distribution channels. In 2005 and the first three months of 2006, AIG expanded its distribution channels, which now include banks, credit card companies and television-media home shopping in many Asian countries. Examples of new distribution channels used both domestically and overseas include banks, affinity groups, direct response and e-commerce.

AIG patiently builds relationships in markets around the world where it sees long-term growth opportunities. For example, the fact that AIG has the only wholly-owned foreign life insurance operations in eight cities in China is the result of relationships developed over nearly 30 years. AIG's more recent extensions of operations into India, Vietnam, Russia and other emerging markets reflect the same growth strategy. Moreover, AIG believes in investing in the economies and infrastructures of these countries and growing with them. When AIG companies enter a new jurisdiction, they typically offer both basic protection and savings products. As the economies evolve, AIG's products evolve with them, to more sophisticated and investment-oriented models.

Growth for AIG may be generated both internally and through acquisitions which both fulfill strategic goals and offer adequate return on capital. Recently AIG announced its acquisition of Travel Guard International, one of the nation's leading providers of travel insurance programs and emergency travel assistance, and its plans to acquire Central Insurance Co., Ltd., a leading general insurance company in Taiwan.

The following table summarizes AIG's revenues, income before income taxes, minority interest and cumulative effect of an accounting change and net income for the three months ended March 31, 2006 and 2005:

(in millions)	**2006**	2005
Total revenues	**$27,259**	$27,202
Income before income taxes, minority interest and cumulative effect of an accounting change	**4,793**	5,649
Net income	**$ 3,195**	$ 3,799

Consolidated Results

The small increase in revenues in the first three months of 2006 was primarily attributable to the growth in net premiums earned from global General Insurance operations as well as growth in both General Insurance and Life Insurance & Retirement Services net investment income and Life Insurance & Retirement Services GAAP premiums, offset, in part, by decreases in revenue in the Financial Services and Asset Management segments.

AIG's income before income taxes, minority interest and cumulative effect of an accounting change decreased 15 percent in the first three months of 2006 when compared to the same period of 2005. Increases in General Insurance and Life Insurance & Retirement Services operating income were offset by an operating loss in Financial Services driven by the effects of hedging activities that do not qualify for hedge accounting treatment under FAS 133 and a decrease in Asset

Management operating income. Results for the first three months of 2006 were negatively affected by the compensation expense relating to the Starr tender offer ($54 million before tax and after tax) and an additional allowance for losses in AIG Credit Card Company (Taiwan) ($88 million before tax and $57 million after tax). Results were also negatively affected by certain adjustments, primarily relating to deferred advertising costs in General Insurance under SOP 93-7 ($59 million before tax and $38 million after tax) and various adjustments relating to the SICO Plans ($61 million before tax and after tax).

The following table summarizes the operations of each principal segment for the three months ended March 31, 2006 and 2005. (See also Note 2 of Notes to Consolidated Financial Statements).

(in millions)	**2006**	2005
Revenues[(a)]:		
General Insurance[(b)]	**$11,656**	$11,219
Life Insurance & Retirement Services[(c)]	**12,639**	11,775
Financial Services[(d)]	**1,615**	2,436
Asset Management[(e)]	**1,239**	1,377
Other	**110**	395
Consolidated	**$27,259**	$27,202
Operating Income (loss)[(a)(f)]:		
General Insurance	**$ 2,331**	$ 1,642
Life Insurance & Retirement Services[(g)]	**2,555**	2,181
Financial Services[(g)]	**(159)**	1,045
Asset Management	**461**	590
Other[(h)]	**(395)**	191
Consolidated	**$ 4,793**	$ 5,649

(a) Includes the effect of hedging activities that do not qualify for hedge accounting treatment under FAS 133, including the related foreign exchange gains and losses. For the first three months of 2006 and 2005, the effect was $0 and $15 million, respectively, in operating income for Aircraft Finance and $(678) million and $468 million in revenues and operating income, respectively, for Capital Markets. These amounts result primarily from interest rate and foreign currency derivatives hedging available for sale securities and borrowings.

(b) Represents the sum of General Insurance net premiums earned, net investment income and realized capital gains (losses).

(c) Represents the sum of Life Insurance & Retirement Services GAAP premiums, net investment income and realized capital gains (losses).

(d) Represents interest, lease and finance charges.

(e) Represents management and advisory fees and net investment income with respect to GICs.

(f) Represents income before income taxes, minority interest and cumulative effect of an accounting change.

(g) Results of operations of AIG Credit Card Company (Taiwan) are shared equally by the Life Insurance & Retirement Services segment and the Financial Services segment. In 2006, additional allowances of $44 million were recorded by each segment for losses in these credit card operations.

(h) Represents unallocated corporate expenses, relating primarily to interest expense and certain compensation related expenses, and other realized capital gains (losses) of $(57) million and $155 million in the first three months of 2006 and 2005, respectively.

General Insurance

AIG's General Insurance operations provide property and casualty products and services throughout the world. The increase in General Insurance operating income in the first three months of 2006 compared to the same period of 2005 was primarily attributable to improvement in underwriting results with respect to the Domestic Brokerage Group (DBG). General Insurance operating income included adverse development in the first three months of 2006 and 2005 from catastrophes in prior years.

Life Insurance & Retirement Services

AIG's Life Insurance & Retirement Services operations provide insurance, financial and investment products throughout the world. Foreign operations provided approximately 65 percent and 55 percent of AIG's Life Insurance & Retirement Services operating income for the first three months of 2006 and 2005, respectively.

Life Insurance & Retirement Services operating income increased by 17 percent in the first three months of 2006 when compared to the same period of 2005 driven by a 39 percent increase in Foreign Life Insurance & Retirement Services operating income, offset, in part, by an approximately 10 percent decrease in the Domestic Life Insurance & Retirement Services operating income, primarily due to lower partnership income. Realized capital gains included in revenues and operating income were $158 million in the first three months of 2006 compared to realized capital losses of $82 million in the same period of 2005. The increase in realized capital gains in the first three months of 2006 compared to the same period of 2005 was due to the effect of hedging activities that do not qualify for hedge accounting under FAS 133 and the foreign exchange gains and losses related to the application of FAS 52, offset by other-than-temporary declines in the value of investments.

Financial Services

AIG's Financial Services subsidiaries engage in diversified activities including aircraft and equipment leasing, capital market transactions, consumer finance and insurance premium financing.

Financial Services operating income decreased in the first three months of 2006 compared to the same period of 2005, primarily due to the fluctuation in earnings resulting from the accounting effect of FAS 133. Fluctuations in revenues and operating income from quarter to quarter are not unusual because of the transaction-oriented nature of Capital Markets operations and the effect of not qualifying for hedge accounting treatment under FAS 133 for hedges on securities available for sale and borrowings. Consumer Finance revenues increased but operating income decreased, primarily as a result of increasing the allowance for losses in connection with the industry-wide credit deterioration in the Taiwan credit card market.

Asset Management

AIG's Asset Management operations include institutional and retail asset management and broker dealer services and spread-based investment business from the sale of GICs. These products and services are offered to individuals and institutions, both domestically and overseas.

Asset Management operating income decreased 22 percent in the first three months of 2006 when compared to the same period of 2005 as a result of continued run off in AIG's GIC portfolio combined with spread compression. In addition, there was a decline in realized gains on sales of real estate investments and performance fees earned on various private equity investments.

Capital Resources

At March 31, 2006, AIG had total consolidated shareholders' equity of $88.39 billion and total consolidated borrowings of $118.8 billion. At that date, $104.1 billion of such borrowings were either not guaranteed by AIG or were AIGFP's matched borrowings under obligations of guaranteed investment agreements (GIAs), liabilities connected to trust preferred stock, or matched notes and bonds payable.

During the period from January 1, 2006 through March 31, 2006, AIG did not purchase any shares of its common stock under its existing common stock repurchase authorization.

Liquidity

At March 31, 2006, AIG's consolidated invested assets included $18.59 billion in cash and short-term investments. Consolidated net cash provided from operating activities in the first three months of 2006 amounted to $3.07 billion. AIG believes that its liquid assets, cash provided by operations and access to short term funding through commercial paper and bank credit facilities will enable it to meet any anticipated cash requirements.

Outlook

Despite industry price erosion in some classes of general insurance, AIG expects to continue to identify profitable opportunities and build attractive new General Insurance businesses as a result of AIG's broad product line and extensive distribution networks. In December 2005, American International Underwriters Overseas, Ltd. (AIUO) received a license from the government of Vietnam to operate a wholly owned general insurance company in Vietnam. This license, the first general insurance license granted by Vietnam to a U.S.-based insurance organization, permits AIG to operate a general insurance company throughout Vietnam.

In China, AIG has wholly-owned life insurance operations in eight cities. These operations should benefit from China's rapid rate of economic growth and growing middle class, a segment that is a prime market for life insurance. Chinese insurance regulators have indicated satisfaction with the implementation of corrective measures to stop AIG's Hong Kong based agents from selling life insurance to mainland Chinese. In April 2006, applications for provincial expansion of AIG's life insurance operations in Guangdong and Jiangsu and of general insurance operations in Guangdong were approved, and AIG resubmitted its application to serve the group insurance market, a business where AIG expects future growth.

In Japan, AIG Star Life Insurance Co., Ltd. (AIG Star Life) and AIG Edison Life Insurance Company (AIG Edison Life) continue to grow new business by expanding distribution and new product offerings. AIG has developed a leadership position in the distribution of annuities through banks in both Japan and Korea. Also, American Life Insurance Company (ALICO) has launched new life products to the Japan bank market after further deregulation of banks in December 2005. AIG is a leader in direct marketing through sponsors and in the broad market in Japan and Korea. AIG also is investing in expanding distribution channels with emphasis in India, Korea and Vietnam.

Domestically, AIG anticipates its life insurance and retirement services businesses to continue growing in 2006 through distribution channel expansion and new and enhanced products. The home service operation, which is expected to be a slow growth business, has not met business objectives, although its cash flow has been strong. Domestic group life/health results continue to be weak reflecting the ongoing restructuring activities including the consideration of exiting certain product lines. AIG Retirement Services individual fixed annuities business will continue to be challenged due to the interest rate environment and increased competition from bank products.

In the airline industry, changes in market conditions are not immediately apparent in operating results. Lease rates have firmed as a result of strong demand spurred by the recovering global commercial aviation market, especially in Asia. Sales have begun to increase, and AIG expects an increasing level of interest from a variety of purchasers. However, higher interest rates are expected to continue to compress lease margins. AIG's Consumer Finance operations overseas have been negatively affected in 2006 by industry-wide credit deterioration in the Taiwan credit card market.

GICs, which are sold domestically and abroad to both institutions and individuals, are written on an opportunistic basis when market conditions are favorable. In September 2005, AIG launched a $10 billion medium term note program in the Euromarkets under which AIG debt securities are issued primarily for a matched investment program. In April 2006, AIG issued its first debt securities under the matched investment program, selling Euro 500 million principal amount of notes. AIG also expects to launch a matched investment program in the domestic market which, along with

the Euro program, will become AIG's principal spread-based investment activity. However, the timing of the launch of the domestic program remains uncertain. Because AIG's credit spreads in the capital markets have widened following the ratings declines described in Item 1A. Risk Factors, there may be a reduction in the earnings on new business in AIG's spread based funding businesses.

AIG has many promising growth initiatives underway around the world. Cooperative agreements such as those with PICC Property and Casualty Company Limited and various banks in the U.S., Japan and Korea are expected to expand distribution networks for AIG's products and provide models for future growth.

Critical Accounting Estimates

AIG considers its most critical accounting estimates those with respect to reserves for losses and loss expenses, future policy benefits for life and accident and health contracts, deferred policy acquisition costs, estimated gross profits for investment-oriented products, fair value determinations for certain Capital Markets assets and liabilities, other-than-temporary declines in the value of investments and flight equipment recoverability. These accounting estimates require the use of assumptions about matters, some of which are highly uncertain at the time of estimation. To the extent actual experience differs from the assumptions used, AIG's results of operations would be directly affected.

Throughout this Management's Discussion and Analysis of Financial Condition and Results of Operations, AIG's critical accounting estimates are discussed in detail. The major categories for which assumptions are developed and used to establish each critical accounting estimate are highlighted below.

Reserves for Losses and Loss Expenses (General Insurance):

- *Loss trend factors:* used to establish expected loss ratios for subsequent accident years based on premium rate adequacy and the projected loss ratio with respect to prior accident years.
- *Expected loss ratios for the latest accident year:* for example, accident year 2005 for the year end 2005 loss reserve analysis. For low frequency, high severity classes such as excess casualty and directors and officers liability (D&O), expected loss ratios generally are utilized for at least the three most recent accident years.
- *Loss development factors:* used to project the reported losses for each accident year to an ultimate amount.

Future Policy Benefits for Life and Accident and Health Contracts (Life Insurance & Retirement Services):

- *Interest rates:* which vary by geographical region, year of issuance and products.
- *Mortality, morbidity and surrender rates:* based upon actual experience by geographical region modified to allow for variation in policy form.

Estimated Gross Profits (Life Insurance & Retirement Services):

- *Estimated gross profits* to be realized over the estimated duration of the contracts (investment-oriented products) affect the carrying value of deferred policy acquisition costs under FAS 97. Estimated gross profits include investment income and gains and losses on investments less required interest, actual mortality and other expenses.

Deferred Policy Acquisition Costs (Life Insurance & Retirement Services):

- Recoverability based on current and future expected profitability, which is affected by interest rates, foreign exchange rates, mortality experience, and policy persistency.

Deferred Policy Acquisition Costs (General Insurance):

- Recoverability and eligibility based upon the current terms and profitability of the underlying insurance contracts.

Fair Value Determinations of Certain Assets and Liabilities (Financial Services – Capital Markets):

- *Valuation models:* utilizing factors, such as market liquidity and current interest, foreign exchange and volatility rates.
- AIG attempts to secure reliable and independent current market price data, such as published exchange rates from external subscription services such as Bloomberg or Reuters or third-party broker quotes for use in its model. When such prices are not available, AIG uses an internal methodology, which includes interpolation and extrapolation from verifiable prices from trades occurring on dates nearest to the dates of the transactions.

Other-Than-Temporary Declines in the Value of Investments:

A security is considered a candidate for other-than-temporary impairment based upon the following criteria:

- Trading at a significant (25 percent or more) discount to par or amortized cost (if lower) for an extended period of time (nine months or longer).
- The occurrence of a discrete credit event resulting in the debtor defaulting or seeking bankruptcy or insolvency protection or voluntary reorganization.
- The probability of non-realization of a full recovery on its investment, irrespective of the occurrence of one of the foregoing events.

At each balance sheet date, AIG evaluates its securities holdings in an unrealized loss position. Where AIG does not intend to hold such securities until they have fully recovered their carrying value, based on the circumstances present at the date of evaluation, AIG records the unrealized loss in income. If events or circumstances change, such as unexpected changes in creditworthiness of the obligor, general interest rate environment, tax circumstances, liquidity events,

and statutory capital management considerations among others, AIG revisits its intent to determine if a loss should be recorded in income. Further, if a loss is recognized from a sale subsequent to a balance sheet date pursuant to these changes in circumstances, the loss is recognized in the period in which the intent to hold the securities to recovery no longer exists.

Flight Equipment — Recoverability (Financial Services):

- *Expected undiscounted future net cash flows:* based upon current lease rates, projected future lease rates and estimated terminal values of each aircraft based on third party information.

Operating Review

General Insurance Operations

AIG's General Insurance subsidiaries are multiple line companies writing substantially all lines of property and casualty insurance both domestically and abroad.

Domestic General Insurance operations are comprised of DBG, which includes the operations of The Hartford Steam Boiler Inspection and Insurance Company (HSB); Transatlantic Holdings, Inc. (Transatlantic); Personal Lines, including 21st Century Insurance Group (21st Century); and United Guaranty Corporation (UGC).

AIG's primary domestic division is DBG. DBG's business in the United States and Canada is conducted through its General Insurance subsidiaries including American Home Assurance Company (American Home), National Union Fire Insurance Company of Pittsburgh, Pa. (National Union), Lexington Insurance Company (Lexington) and certain other General Insurance company subsidiaries of AIG.

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

In addition to writing substantially all classes of business insurance, including large commercial or industrial property insurance, excess liability, inland marine, environmental, workers compensation and excess and umbrella coverages, DBG offers many specialized forms of insurance such as aviation, accident and health, equipment breakdown, directors and officers liability (D&O), difference-in-conditions, kidnap-ransom, export credit and political risk, and various types of professional errors and omissions coverages. The AIG Risk Management operation provides insurance and risk management programs for large corporate customers. The AIG Risk Finance operation is a leading provider of customized structured insurance products. Also included in DBG are the operations of AIG Environmental, which focuses specifically on providing specialty products to clients with environmental exposures. Lexington writes surplus lines, those risks for which conventional insurance companies do not readily provide insurance coverage, either because of complexity or because the coverage does not lend itself to conventional contracts.

Certain of the products of the DBG companies include funding components or have been structured in a manner such that little or no insurance risk is actually transferred. Funds received in connection with these products are recorded as deposits and included in other liabilities, rather than premiums and incurred losses.

The AIG Worldsource Division introduces and coordinates AIG's products and services to U.S.-based multinational clients and foreign corporations doing business in the U.S.

Transatlantic subsidiaries offer reinsurance capacity on both a treaty and facultative basis both in the U.S. and abroad. Transatlantic structures programs for a full range of property and casualty products with an emphasis on specialty risk.

AIG's Personal Lines operations provide automobile insurance through AIG Direct, the mass marketing operation of AIG, Agency Auto Division and 21st Century, as well as a broad range of coverages for high net-worth individuals through the AIG Private Client Group.

The main business of the UGC subsidiaries is the issuance of residential mortgage guaranty insurance on conventional first lien mortgages for the purchase or refinance of one to four family residences. UGC subsidiaries also write second lien and private student loan guaranty insurance.

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

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

A critical discipline of a successful general insurance business is the objective to produce profit from underwriting activities exclusive of investment-related income. When underwriting is not profitable, premiums are inadequate to pay for insured losses and underwriting related expenses. In these situations, the addition of general insurance related investment income and realized capital gains may, however, enable a general insurance business to produce operating income. For these reasons, AIG views underwriting results to be criti-

cal in the overall evaluation of performance. (See also the discussion under "Liquidity" herein.)

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

GAAP provides for the recognition of expenses at the same time revenues are earned, the accounting principle of matching. Therefore, acquisition expenses are deferred and amortized over the period the related net premiums written are earned. DAC is reviewed for recoverability, and such review requires management judgment. (See also "Critical Accounting Estimates" herein.)

AIG, along with most General Insurance companies, uses the loss ratio, the expense ratio and the combined ratio as measures of underwriting performance. The loss ratio is the sum of losses and loss expenses incurred divided by net premiums earned. The expense ratio is statutory underwriting expenses divided by net premiums written. The combined ratio is the sum of the loss ratio and the expense ratio. These ratios are relative measurements that describe, for every $100 of net premiums earned or written, the cost of losses and statutory expenses, respectively. The combined ratio presents the total cost per $100 of premium production. A combined ratio below 100 demonstrates underwriting profit; a combined ratio above 100 demonstrates underwriting loss.

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

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

General Insurance operating income is comprised of statutory underwriting results, changes in DAC, net investment income and realized capital gains and losses. Operating income, as well as net premiums written, net premiums earned, net investment income and realized capital gains (losses) and statutory ratios for the three months ended March 31, 2006 and 2005 were as follows:

(in millions, except ratios)	**2006**	2005
Net premiums written:		
Domestic General		
DBG	**$ 5,900**	$ 5,720
Transatlantic	**914**	885
Personal Lines	**1,198**	1,186
Mortgage Guaranty	**197**	165
Foreign General	**3,046**	2,834
Total	**$11,255**	$10,790
Net premiums earned:		
Domestic General		
DBG	**$ 5,763**	$ 5,573
Transatlantic	**908**	888
Personal Lines	**1,159**	1,120
Mortgage Guaranty	**166**	140
Foreign General[(a)]	**2,474**	2,419
Total	**$10,470**	$10,140
Net investment income:		
Domestic General		
DBG	**$ 745**	$ 659
Transatlantic	**102**	85
Personal Lines	**57**	52
Mortgage Guaranty	**32**	28
Intercompany adjustments and eliminations – net	**–**	1
Foreign General	**182**	190
Total	**$ 1,118**	$ 1,015
Realized capital gains (losses)	**68**	64
Operating Income[(b)]:		
Domestic General		
DBG	**$ 1,357**	$ 713
Transatlantic	**141**	114
Personal Lines	**101**	109
Mortgage Guaranty	**109**	104
Foreign General	**621**	596
Reclassifications and Eliminations	**2**	6
Total	**$ 2,331**	$ 1,642
Domestic General:		
Loss Ratio	**70.94**	77.23
Expense Ratio	**20.18**	19.76
Combined Ratio	**91.12**	96.99
Foreign General:		
Loss Ratio	**52.74**	54.43
Expense Ratio[(c)(d)]	**28.85**	27.25
Combined ratio[(a)]	**81.59**	81.68

(in millions, except ratios)	**2006**	2005
Consolidated:		
Loss Ratio[(b)]	**66.64**	71.79
Expense Ratio	**22.53**	21.73
Combined Ratio	**89.17**	93.52

(a) Income statement accounts expressed in non-functional currencies are translated into U.S. dollars using average exchange rates.

(b) Includes $103 million and $171 million of additional losses incurred and net reinstatement premium costs in the first three months of 2006 and 2005, respectively, related primarily to prior year catastrophes, resulting in increases of 0.97 points and 1.66 points, respectively, in the consolidated General Insurance loss ratio.

(c) Includes the results of wholly owned AIU agencies.

(d) Includes amortization of advertising costs.

General Insurance Results

General Insurance operating income in the first three months of 2006 showed significant improvement from the prior year results. The increase in General Insurance operating income in the first three months of 2006 was primarily attributable to improvement in DBG's underwriting results and growth in overall General Insurance net investment income. Underwriting results in the first three months of 2006 and 2005 included $103 million and $171 million, respectively, of additional losses incurred and net reinstatement premium costs resulting primarily from increased costs related to the 2005 and 2004 catastrophes. The $103 million of losses and net reinstatement premium costs incurred in the first three months of 2006 includes $78 million attributable to 2005 hurricanes and $25 million attributable to 2004 hurricanes. The losses and net reinstatement premium costs attributable to the 2004 hurricanes are primarily related to multi-event and multi-location claims that required extensive investigation to determine the full extent and value of the insured damage. The $171 million of losses and net reinstatement premium costs incurred in the first three months of 2005 is primarily attributable to 2004 hurricanes as well as $44 million from a January 2005 European storm. At March 31, 2006, the inception to date incurred losses and net reinstatement premium costs for 2005 hurricanes were approximately $2.7 billion. At March 31, 2006, the inception to date incurred losses and net reinstatement premium costs for 2004 hurricanes were approximately $1.2 billion.

DBG's net premiums written increased modestly in the first three months of 2006 when compared to the same period of 2005, reflecting generally improving renewal retention, a modest change in the mix of business towards smaller accounts and a reduction in the amount of reinsurance purchased. DBG also continued to expand its relationships with a larger number and broader range of brokers. Recently, DBG has seen improvement in domestic property rates as well as increases in submission activity in the aftermath of the 2005 hurricanes. DBG attributes the increase in submissions to its overall financial strength in comparison to many insurers that experienced significant losses and reductions of surplus as a result of the hurricanes.

The improvement in DBG's underwriting results for the first three months of 2006 compared to the same period of 2005 was due to a reduction in the loss ratio of 8.1 points, primarily due to lower accident year loss ratios for 2006 compared to the loss ratios recorded in the first three months of 2005 for accident year 2005. The improvement in 2006 loss ratios is based on a comprehensive actuarial study conducted at the end of 2005 and updated as of March 31, 2006 as described below under "Quarterly Reserving Process". In addition, the first three months of 2006 includes $28 million for losses related to prior year hurricanes compared to the first three months of 2005 which included $118 million for losses related to prior year hurricanes.

The DBG expense ratio was approximately the same for the first three months of 2006 and 2005.

Transatlantic's net premiums written and net premiums earned for the first three months of 2006 increased compared to the same period of 2005 due largely to increased domestic specialty casualty and property premiums offset, in part, by the adverse effect of changes in foreign currency exchange rates on international premiums. Operating income in the first three months of 2006 increased due to improved underwriting profit, resulting largely from reduced significant net catastrophe losses and lower net adverse development on loss reserves, offset, in part, by higher commission costs, and increased net investment income.

Personal Lines net premiums written for the first three months of 2006 increased slightly when compared to the same period of 2005 as strong growth in the Private Client Group and Agency Auto divisions offset the runoff of the involuntary auto business and a small decline in the AIG Direct and 21st Century divisions. The reduction in the involuntary business is a result of terminating an MGA relationship. The Private Client Group and Agency Auto divisions continue to grow as they expand their agency/broker relationships with multiple product offerings. The AIG Direct and 21st Century decline is due largely to a reduction in response rates. The loss ratio improved in 2006 due to favorable loss development trends in the AIG Direct and 21st Century businesses. The expense ratio increased in 2006 over 2005 driven by an investment in people and technology in the Agency Auto Division, higher compensation expenses in 21st Century due to implementing FAS 123R, and accelerated amortization of direct response advertising costs in AIG Direct resulting from a change in estimated future premiums.

Mortgage Guaranty's net premiums written were up for the first three months of 2006 when compared to the same period of 2005. Strong growth was reported in all business segments as domestic first lien, domestic second lien and international operations grew 9 percent, 22 percent and 84 percent, respectively. Underwriting results for the first three

months of 2006 improved slightly from the same period of 2005 as strong earned premium growth was partially offset by loss development in the domestic second lien business.

Foreign General Insurance had strong results in the first three months of 2006 even after additional losses incurred related to the 2005 catastrophes and a pre-tax adjustment of $53 million to expenses for a write-off of deferred advertising costs. Growth in net premiums written for this period was achieved in consumer lines due to new business as well as new distribution channels. Commercial lines had modest growth in net premiums written. Commercial lines in Europe exhibited strong growth and had positive results for the first three months of 2006, partially offset by rate decreases in Australia and the United Kingdom. The Ascot Lloyd's syndicate reported growth for this period due to rate increases on its U.S. book of business along with contractual terms on renewals that reflect better conditions and higher deductibles. In the Far East, personal accident business exhibited strong growth. Europe, Southeast Asia and Latin America also had strong growth in personal accident business. Personal lines operations in Latin America and Brazil continue to exhibit strong growth. For the first three months of 2006, 55 percent of Foreign General Insurance net premiums written was derived from commercial insurance and the remainder from consumer lines. The Foreign General Insurance loss ratio decreased in the first three months of 2006 from the same period of 2005 primarily due to the lower accident year loss ratio for 2006 compared to the loss ratio recorded in the first three months of 2005 for accident year 2005. The Foreign General Insurance expense ratio increased in the first three months of 2006 from the same period in 2005 principally due to the $53 million write-off of advertising costs.

AIG transacts business in most major foreign currencies. The following table summarizes the effect of changes in foreign currency exchange rates on the growth of General Insurance net premiums written for the first three months of 2006:

	2006
Growth in original currency	6.0%
Foreign exchange effect	(1.7)
Growth as reported in U.S. dollars	4.3%

As previously noted, General Insurance results include $103 million and $171 million of additional losses incurred and net reinstatement premium costs in the first three months of 2006 and 2005, respectively, related primarily to the 2005 and 2004 catastrophes. The losses attributable to the 2004 hurricanes are primarily related to multi-event and multi-location claims that required extensive investigation to determine the full extent and value of the insured damage. Losses caused by catastrophes can fluctuate widely from year to year, making comparisons of recurring type business more difficult. With respect to catastrophe losses, AIG believes that it has taken appropriate steps, such as careful exposure selection and obtaining reinsurance coverage, to reduce the effect of the magnitude of possible future losses. The occurrence of one or more catastrophic events of unanticipated frequency or severity, such as a terrorist attack, earthquake or hurricane, that causes insured losses, however, could have a material adverse effect on AIG's results of operations, liquidity or financial condition.

General Insurance net investment income grew in the first three months of 2006 when compared to the same period of 2005. AIG is benefiting from strong cash flow and higher interest rates. Additionally, net investment income was positively affected by the compounding of previously earned and reinvested net investment income. Foreign General Insurance net investment income declined in the first three months of 2006 when compared to the same period of 2005 due to lower partnership income. Market valuations by partnerships in the private equity sector did not match the increases in 2005, the results of which benefited from initial public offering activity of partnership investments.

Realized capital gains and losses resulted from the ongoing investment management of the General Insurance portfolios within the overall objectives of the General Insurance operations. (See the discussion on "Valuation of Invested Assets" herein.)

The contribution of General Insurance operating income to AIG's consolidated income before income taxes, minority interest and cumulative effect of an accounting change was 49 percent in the first three months of 2006 compared to 29 percent in the same period of 2005.

Reinsurance

AIG is a major purchaser of reinsurance for its General Insurance operations. AIG insures risks globally, and its reinsurance programs must be coordinated in order to provide AIG the level of reinsurance protection that AIG desires. Reinsurance is an important risk management tool to manage transaction and insurance line risk retention at prudent levels set by management. AIG also purchases reinsurance to mitigate its catastrophic exposure. AIG is cognizant of the need to exercise good judgment in the selection and approval of both domestic and foreign companies participating in its reinsurance programs because one or more catastrophe losses could negatively affect AIG's reinsurers and result in an inability of AIG to collect reinsurance recoverables. AIG's reinsurance department evaluates catastrophic events and assesses the probability of occurrence and magnitude of catastrophic events through the use of state-of-the-art industry recognized program models, among other techniques. AIG supplements these models through continually monitoring the risk exposure of AIG's worldwide General Insurance operations and adjusting such models accordingly. Although reinsurance ar-

rangements do not relieve AIG from its direct obligations to its insureds, an efficient and effective reinsurance program substantially limits AIG's exposure to potentially significant losses. With respect to its property business, AIG has either renewed existing coverage or purchased new coverage that, in the opinion of management, is adequate to limit AIG's exposures.

AIG's consolidated general reinsurance assets amounted to $23.44 billion at March 31, 2006 and resulted from AIG's reinsurance arrangements. Thus, a credit exposure existed at March 31, 2006 with respect to reinsurance recoverable to the extent that any reinsurer may not be able to reimburse AIG under the terms of these reinsurance arrangements. AIG manages its credit risk in its reinsurance relationships by transacting with reinsurers that it considers financially sound, and when necessary AIG holds substantial collateral in the form of funds, securities and/or irrevocable letters of credit. This collateral can be drawn on for amounts that remain unpaid beyond specified time periods on an individual reinsurer basis. At December 31, 2005, approximately 48 percent of the general reinsurance assets were from unauthorized reinsurers. Many of these balances were collateralized, permitting statutory recognition. Additionally, with the approval of its domiciliary insurance regulators, AIG posted approximately $1.5 billion of letters of credit issued by several commercial banks in favor of certain Domestic General Insurance companies to permit statutory recognition of balances otherwise uncollateralized at December 31, 2005. The remaining 52 percent of the general reinsurance assets were from authorized reinsurers. The terms authorized and unauthorized pertain to regulatory categories, not creditworthiness. At December 31, 2005, approximately 88 percent of the balances with respect to authorized reinsurers are from reinsurers rated A (excellent) or better, as rated by A.M. Best, or A (strong) or better, as rated by Standard & Poor's, a division of The McGraw-Hill Companies, Inc. (S&P). Through March 31, 2006, there has been no significant deterioration in the rating profile of AIG's reinsurers representing more than five percent of AIG's reinsurance assets as of December 31, 2005. These ratings are measures of financial strength.

AIG maintains an allowance for estimated unrecoverable reinsurance. Although AIG has been largely successful in its previous recovery efforts, at March 31, 2006 AIG had an allowance for unrecoverable reinsurance approximating $979 million. At that date, AIG had no significant reinsurance recoverables due from any individual reinsurer that was financially troubled (e.g., liquidated, insolvent, in receivership or otherwise subject to formal or informal regulatory restriction).

AIG's Reinsurance Security Department conducts ongoing detailed assessments of the reinsurance markets and current and potential reinsurers, both foreign and domestic. Such assessments include, but are not limited to, identifying if a reinsurer is appropriately licensed and has sufficient financial capacity, and evaluating the local economic environment in which a foreign reinsurer operates. This department also reviews the nature of the risks ceded and the requirements for credit risk mitigants. For example, in AIG's treaty reinsurance contracts, AIG includes provisions that frequently require a reinsurer to post collateral when a referenced event occurs. Furthermore, AIG limits its unsecured exposure to reinsurers through the use of credit triggers, which include, but are not limited to, insurer financial strength rating downgrades, policyholder surplus declines at or below a certain predetermined level or a certain predetermined level of a reinsurance recoverable being reached. In addition, AIG's Credit Risk Committee reviews the credit limits for and concentrations with any one reinsurer.

AIG enters into intercompany reinsurance transactions, primarily through American International Reinsurance Company, Ltd. (AIRCO), for its General Insurance and Life Insurance operations. AIG enters into these transactions as a sound and prudent business practice in order to maintain underwriting control and spread insurance risk among AIG's various legal entities. All material intercompany transactions have been eliminated in consolidation. AIG generally obtains letters of credit in order to obtain statutory recognition of these intercompany reinsurance transactions. At March 31, 2006, approximately $3.5 billion of letters of credit were outstanding to cover intercompany reinsurance transactions with AIRCO or other General Insurance subsidiaries.

At March 31, 2006, consolidated general reinsurance assets of $23.44 billion include reinsurance recoverables for paid losses and loss expenses of $1.17 billion and $19.21 billion with respect to the ceded reserve for losses and loss expenses, including ceded losses incurred but not reported (IBNR) (ceded reserves) and $3.07 billion of ceded reserve for unearned premiums. The ceded reserve for losses and loss expenses represent the accumulation of estimates of ultimate ceded losses including provisions for ceded IBNR and loss expenses. The methods used to determine such estimates and to establish the resulting ceded reserves are continually reviewed and updated by management. Any adjustments thereto are reflected in income currently. It is AIG's belief that the ceded reserves for losses and loss expenses at March 31, 2006 were representative of the ultimate losses recoverable. In the future, as the ceded reserves continue to develop to ultimate amounts, the ultimate loss recoverable may be greater or less than the reserves currently ceded.

Reserve for Losses and Loss Expenses

The table below classifies as of March 31, 2006 the components of the General Insurance gross reserve for losses and loss expenses (loss reserves) by major lines of business on a statutory Annual Statement basis*:

(in millions)	
Other liability occurrence	$18,437
Other liability claims made	12,137
Workers compensation	11,909
Auto liability	6,274
Property	7,541
International	5,494
Reinsurance	3,039
Medical malpractice	2,173
Aircraft	1,589
Products liability	1,988
Commercial multiple peril	1,449
Accident and health	1,641
Fidelity/surety	988
Other	3,441
Total	$78,100

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

AIG's reserve for losses and loss expenses represents the accumulation of estimates of ultimate losses, including IBNR and loss expenses. The methods used to determine loss reserve estimates and to establish the resulting reserves are continually reviewed and updated by management. Any adjustments resulting therefrom are reflected in operating income currently. Because loss reserve estimates are subject to the outcome of future events, changes in estimates are unavoidable given that loss trends vary and time is often required for changes in trends to be recognized and confirmed. Reserve changes that increase previous estimates of ultimate cost are referred to as unfavorable or adverse development or reserve strengthening. Reserve changes that decrease previous estimates of ultimate cost are referred to as favorable development.

At March 31, 2006, General Insurance net loss reserves increased $1.42 billion from the prior year end to $58.89 billion. The net loss reserves represent loss reserves reduced by reinsurance recoverables, net of an allowance for unrecoverable reinsurance and applicable discount for future investment income. The table below classifies the components of the General Insurance net loss reserves by business unit as of March 31, 2006.

(in millions)	
DBG[(a)]	$41,807
Personal Lines[(b)]	2,556
Transatlantic	5,737
Mortgage Guaranty	349
Foreign General[(c)]	8,443
Total Net Loss Reserve	$58,892

(a) DBG loss reserves include approximately $3.59 billion ($4.04 billion before discount) related to business written by DBG but ceded to AIRCO and reported in AIRCO's statutory filings. DBG loss reserves also include approximately $462 million related to business included in AIUO's statutory filings.

(b) Personal Lines loss reserves include $885 million related to business ceded to DBG and reported in DBG's statutory filings.

(c) Foreign General loss reserves include approximately $2.57 billion related to business reported in DBG's statutory filings.

The DBG net loss reserve of $41.81 billion is comprised principally of the business of AIG subsidiaries participating in the American Home/National Union pool (11 companies) and the surplus lines pool (Lexington, Starr Excess Liability Insurance Company and Landmark Insurance Company).

Beginning in 1998, DBG ceded a quota share percentage of its other liability occurrence and products liability occurrence business to AIRCO. The quota share percentage ceded was 40 percent in 1998, 65 percent in 1999, 75 percent in 2000 and 2001, 50 percent in 2002 and 2003, 40 percent in 2004, 35 percent in 2005 and 20 percent in 2006 and covered all business written in these years for these lines by participants in the American Home/National Union pool. In 1998 the cession reflected only the other liability occurrence business, but in 1999 and subsequent years included products liability occurrence. AIRCO's loss reserves relating to these quota share cessions from DBG are recorded on a discounted basis. As of March 31, 2006, AIRCO carried a discount of approximately $450 million applicable to the $4.04 billion in undiscounted reserves it assumed from the American Home/National Union pool via this quota share cession. AIRCO also carries approximately $465 million in net loss reserves relating to Foreign General insurance business. These reserves are carried on an undiscounted basis.

Beginning in 1997, the Personal Lines division ceded a percentage of all business written by the companies participating in the personal lines pool to the American Home/National Union pool. As noted above, the total reserves carried by participants in the American Home/National Union pool relating to this cession amounted to $885 million as of March 31, 2006.

The companies participating in the American Home/National Union pool have maintained a participation in the business written by AIU for decades. As of March 31, 2006, these AIU reserves carried by participants in the American Home/National Union pool amounted to approximately $2.57 billion. The remaining Foreign General reserves are carried by AIUO, AIRCO, and other smaller AIG subsidiaries domiciled outside the United States. Statutory filings in the U.S. by AIG companies reflect all the business written by U.S. domiciled entities only, and therefore exclude business written by AIUO, AIRCO, and all other internationally domiciled subsidiaries. The total reserves carried at March 31, 2006 by AIUO and AIRCO were approximately $3.92 billion and $4.06 billion, respectively. AIRCO's $4.06 billion in total general insurance reserves consist of approximately $3.59 billion from business assumed from the American Home/National Union pool and an additional $465 million relating to Foreign General Insurance business.

Discounting of Reserves

At March 31, 2006, AIG's overall General Insurance net loss reserves reflects a loss reserve discount of $2.11 billion, including tabular and non-tabular calculations. The tabular workers compensation discount is calculated using a 3.5 percent interest rate and the 1979-81 Decennial Mortality Table. The non-tabular workers compensation discount is calculated separately for companies domiciled in New York and Pennsylvania, and follows the statutory regulations for each state. For New York companies, the discount is based on a five percent interest rate and the companies' own payout patterns. For Pennsylvania companies, the statute has specified discount factors for accident years 2001 and prior, which are based on a six percent interest rate and an industry payout pattern. For accident years 2002 and subsequent, the discount is based on the yield of U.S. Treasury securities ranging from one to twenty years and the company's own payout pattern, with the future expected payment for each year using the interest rate associated with the corresponding Treasury security yield for that time period. The discount is comprised of the following: $512 million – tabular discount for workers compensation in DBG; $1.15 billion – non-tabular discount for workers compensation in DBG; and, $450 million – non-tabular discount for other liability occurrence and products liability occurrence in AIRCO. The total undiscounted workers compensation loss reserve carried by DBG is approximately $9.9 billion as of March 31, 2006. The other liability occurrence and products liability occurrence business in AIRCO that is assumed from DBG is discounted based on the yield of U.S. Treasury securities ranging from one to twenty years and the DBG payout pattern for this business. The undiscounted reserves assumed by AIRCO from DBG totaled approximately $4.04 billion at March 31, 2006.

Quarterly Reserving Process

It is management's belief that the General Insurance net loss reserves are adequate to cover General Insurance net losses and loss expenses as of March 31, 2006. While AIG regularly reviews the adequacy of established loss reserves, there can be no assurance that AIG's ultimate loss reserves will not develop adversely and materially exceed AIG's loss reserves as of March 31, 2006. In the opinion of management, such adverse development and resulting increase in reserves is not likely to have a material adverse effect on AIG's consolidated financial position, although it could have a material adverse effect on AIG's consolidated results of operations for an individual reporting period.

The table below presents the reconciliation of net loss reserves for the first three months ended March 31, 2006 and 2005 as follows:

(in millions)	**2006**	2005
Net reserve for losses and loss expenses at beginning of year	**$57,476**	$47,254
Foreign exchange effect	**117**	28
Losses and loss expenses incurred:		
Current year	**6,841**	7,039
Prior years, other than accretion of discount*	**35**	143
Prior years, accretion of discount	**101**	97
Losses and loss expenses incurred	**6,977**	7,279
Losses and loss expenses paid	**5,678**	5,227
Net reserve for losses and loss expenses at end of period	**$58,892**	$49,334

* *Includes $35 million in the first three months of 2006 and $55 million in the first three months of 2005 for the general reinsurance operations of Transatlantic and $98 million and $118 million of additional losses incurred in the first three months of 2006 and 2005 resulting from increased costs related to the 2005 and 2004 catastrophes.*

The loss ratios recorded by AIG for the first three months of 2006 take into account the results of the comprehensive reserve reviews that were completed in the fourth quarter of 2005. As explained more fully in the 2005 Annual Report on Form 10-K, AIG's year-end 2005 reserve review reflected careful consideration of the reserve analyses prepared by AIG's internal actuarial staff with the assistance of third party actuaries. In determining the appropriate loss ratios for accident year 2006 for each class of business, AIG gave appropriate consideration to the loss ratios resulting from the reserve analyses as well as all other relevant information including rate changes, expected changes in loss costs, changes in coverage, reinsurance or mix of business, and other factors that may affect the loss ratios.

In the first three months of 2006, AIG enhanced its process of determining the quarterly loss development from prior accident years. Beginning with the first three months of 2006, additional analyses are conducted to determine the change in estimated ultimate loss for each accident year for each profit center. For example, if loss emergence for a profit center is different than expected for certain accident years in the quarter, the actuaries now take additional steps to examine the indicated effect such emergence would have on the reserves of that profit center. In some cases, the higher or lower than expected emergence may result in no clear change in the ultimate loss estimate for the accident years in question, and no adjustment would be made to the profit center's reserves for prior accident years. In other cases, the higher or lower than expected emergence may result in a larger change, either favorable or unfavorable, than the difference between the actual and expected loss emergence. Such additional analyses were conducted for each profit center, as appropriate, in the first three months of 2006 to determine the loss development from prior accident years for the first three months.

In the first three months of 2006, net loss development from prior accident years was approximately $35 million, including approximately $98 million pertaining to catastrophes in 2004 and 2005 and $35 million from the general reinsurance operations of Transatlantic, but excluding approximately $101 million pertaining to accretion of loss reserve discount applicable to accident years 2005 and prior. Excluding catastrophes and Transatlantic, as well as accretion of discount, net loss development from prior accident years in the first three months of 2006 was favorable by approximately $98 million. The majority of the $98 million in favorable development is attributable to shorter tail classes of business within Foreign General. Net loss development from prior accident years for DBG in the first three months of 2006 was nearly flat, excluding catastrophes and accretion of discount. Within the overall favorable development of $98 million, accident years 2003 through 2005 experienced favorable development of approximately $330 million, offset by approximately $230 million of adverse development from accident years 2002 and prior.

Most classes of business throughout AIG experienced favorable loss emergence in the first three months of 2006 for accident years 2003 through 2005. The adverse development noted above from accident years 2002 and prior was primarily attributable to the excess casualty class of business, and to a lesser extent excess workers compensation. After conducting the more enhanced analyses described above, AIG determined that there was no overall adverse development in the first three months of 2006 for excess casualty, whereas there was determined to be $35 million of prior period adverse development for excess workers compensation from accident years 2002 and prior. For excess casualty, the adverse development for accident years 2002 and prior was offset by favorable development from accident years 2003 and 2004, and to a lesser extent 2005.

In the first three months of 2005, net loss reserve development from prior accident years was approximately $143 million, including approximately $118 million pertaining to catastrophes in 2004 and $55 million from the general reinsurance operations of Transatlantic, but excluding approximately $97 million pertaining to the accretion of loss reserve discount pertaining to accident years 2004 and prior. Excluding catastrophes and Transatlantic, as well as accretion of discount, net loss development from prior accident years in the first three months of 2005 was favorable by approximately $30 million. In the first three months of 2005, the overall favorable emergence of $30 million was comprised of approximately $360 million of favorable emergence from accident years 2003 and 2004, offset by approximately $330 million of higher than expected loss emergence from accident years 2002 and prior. Most classes of business throughout AIG contributed to the favorable emergence from accident years 2003 and 2004 in the first three months of 2005. The majority of the higher than expected emergence from accident years 2002 and prior was attributable to the directors and officers and related management liability classes of business, as well as excess casualty.

Loss Reserving Process

The General Insurance loss reserves can generally be categorized into two distinct groups. One group is long-tail casualty lines of business which include excess and umbrella liability, D&O, professional liability, medical malpractice, workers compensation, general liability, products liability, and related classes. The other group is short-tail lines of business consisting principally of property lines, personal lines and certain classes of casualty lines. These lines of business and actuarial assumptions made in the review of these lines of business are described in the 2005 Annual Report on Form 10-K.

The process of determining the current loss ratio for each class or business segment is based on a variety of factors and is described in detail in AIG's 2005 Annual Report on Form 10-K. AIG uses the process described above to update AIG's reserves on a quarterly basis. AIG's 2005 Annual Report on Form 10-K also includes a discussion and analysis of the volatility of AIG's 2005 reserve estimates and a sensitivity analysis.

Asbestos and Environmental Reserves

The estimation of loss reserves relating to asbestos and environmental claims on insurance policies written many years ago is subject to greater uncertainty than other types of claims due to inconsistent court decisions as well as judicial interpretations and legislative actions that in some cases have tended to broaden coverage beyond the original intent of such policies and in others have expanded theories of liability.

As described more fully in the 2005 Annual Report on Form 10-K, AIG's reserves relating to asbestos and environmental claims reflect the results of the comprehensive ground up analysis which was completed in the fourth quarter of 2005. AIG plans to update the ground up analysis on an annual basis. In the first three months of 2006, AIG maintained the ultimate loss estimates for asbestos and environmental claims resulting from the recently completed reserve analyses. A minor amount of incurred loss emergence pertaining to asbestos was reflected in the first three months of 2006, as depicted in the table that follows. This minor development is primarily attributable to the general reinsurance operations of Transatlantic.

A summary of reserve activity, including estimates for applicable IBNR, relating to asbestos and environmental claims separately and combined for the three months ended March 31, 2006 and 2005 follows:

	2006		2005	
(in millions)	**Gross**	**Net**	Gross	Net
Asbestos:				
Reserve for losses and loss expenses at beginning of year	**$4,441**	**$1,840**	$2,559	$1,060
Losses and loss expenses incurred*	**5**	**2**	78	24
Losses and loss expenses paid*	**(149)**	**(54)**	(91)	(29)
Reserve for losses and loss expenses at end of period	**$4,297**	**$1,788**	$2,546	$1,055
Environmental:				
Reserve for losses and loss expenses at beginning of year	**$ 926**	**$ 410**	$ 974	$ 451
Losses and loss expenses incurred*	**–**	**–**	(13)	(3)
Losses and loss expenses paid*	**(21)**	**(9)**	(30)	(16)
Reserve for losses and loss expenses at end of period	**$ 905**	**$ 401**	$ 931	$ 432
Combined:				
Reserve for losses and loss expenses at beginning of year	**$5,367**	**$2,250**	$3,533	$1,511
Losses and loss expenses incurred*	**5**	**2**	65	21
Losses and loss expenses paid*	**(170)**	**(63)**	(121)	(45)
Reserve for losses and loss expenses at end of period	**$5,202**	**$2,189**	$3,477	$1,487

** All amounts pertain to policies underwritten in prior years.*

The gross and net IBNR included in the reserve for losses and loss expenses, relating to asbestos and environmental claims separately and combined, at March 31, 2006 and 2005 were estimated as follows:

	2006		2005	
(in millions)	**Gross**	**Net**	Gross	Net
Asbestos	**$3,314**	**$1,425**	$1,864	$ 786
Environmental	**572**	**256**	554	248
Combined	**$3,886**	**$1,681**	$2,418	$1,034

A summary of asbestos and environmental claims count activity for the three months ended March 31, 2006 and 2005 was as follows:

	2006			2005		
	Asbestos	**Environmental**	**Combined**	Asbestos	Environmental	Combined
Claims at beginning of year	**7,293**	**9,873**	**17,166**	7,575	8,216	15,791
Claims during year:						
Opened	**286**	**388**	**674**	259	759	1,018
Settled	**(37)**	**(42)**	**(79)**	(19)	(52)	(71)
Dismissed or otherwise resolved	**(295)**	**(296)**	**(591)**	(130)	(879)	(1,009)
Claims at end of period	**7,247**	**9,923**	**17,170**	7,685	8,044	15,729

The table below presents AIG's survival ratios for asbestos and environmental claims at March 31, 2006 and 2005. The survival ratio is derived by dividing the current carried loss reserve by the average payments for the three most recent calendar years for these claims. Therefore, the survival ratio is a simplistic measure estimating the number of years it would be before the current ending loss reserves for these claims would be paid off using recent year average payments. Many factors, such as aggressive settlement procedures, mix of business and level of coverage provided, have a significant effect on the amount of asbestos and environmental reserves and payments and the resultant survival ratio. Thus, caution should be exercised in attempting to determine reserve adequacy for these claims based simply on this survival ratio.

AIG's survival ratios for asbestos and environmental claims, separately and combined were based upon a three-year average payment. These ratios at March 31, 2006 and 2005 were as follows:

(number of years)	**Gross**	**Net**
2006		
Survival ratios:		
Asbestos	**14.7**	**17.8**
Environmental	**7.1**	**6.4**
Combined	**12.4**	**13.5**
2005		
Survival ratios:		
Asbestos	9.8	12.7
Environmental	6.3	6.7
Combined	8.5	10.1

Life Insurance & Retirement Services Operations

AIG's Life Insurance & Retirement Services subsidiaries offer a wide range of insurance and retirement savings products both domestically and abroad. Insurance-oriented products consist of individual and group life, payout annuities, endowment and accident and health policies. Retirement savings products consist generally of fixed and variable annuities. (See also Note 2 of Notes to Consolidated Financial Statements.)

Domestically, AIG's Life Insurance & Retirement Services operations offer a broad range of protection products, such as life insurance, group life and health products, including disability income products and payout annuities, which include single premium immediate annuities, structured settlements and terminal funding annuities. Home service operations include an array of life insurance, accident and health and annuity products sold through career agents. In addition, home service includes a small block of run-off property and casualty coverage. Retirement services include group retirement products, individual fixed and variable annuities sold through banks, broker dealers and exclusive sales representatives, and annuity runoff operations, which include previously-acquired "closed blocks" and other fixed and variable annuities largely sold through distribution relationships that have been discontinued.

Overseas, AIG's Life Insurance & Retirement Services operations include insurance and investment-oriented products such as whole and term life, investment linked, universal life and endowments, personal accident and health products, group products including pension, life and health, and fixed and variable annuities.

Life Insurance & Retirement Services operations presented on a sub-product basis for the three months ended March 31, 2006 and 2005 were as follows:

(in millions)		**2006**		2005
GAAP premiums:				
Domestic Life:				
Life insurance[a]	**$**	**516**	$	497
Home service		**200**		203
Group life/health		**246**		268
Payout annuities[b]		**450**		397
Total		**1,412**		1,365
Domestic Retirement Services:				
Group retirement products		**94**		84
Individual fixed annuities		**29**		20
Individual variable annuities		**128**		112
Individual fixed annuities-runoff[c]		**20**		23
Total		**271**		239
Total Domestic		**1,683**		1,604
Foreign Life:				
Life insurance		**4,081**		4,089
Personal accident & health		**1,306**		1,221
Group products		**573**		517
Total		**5,960**		5,827
Foreign Retirement Services:				
Individual fixed annuities		**95**		84
Individual variable annuities		**34**		25
Total		**129**		109
Total Foreign		**6,089**		5,936
Total GAAP premiums	**$**	**7,772**	$	7,540
Net investment income:				
Domestic Life:				
Life insurance	**$**	**338**	$	372
Home service		**158**		147
Group life/health		**54**		46
Payout annuities		**237**		210
Total		**787**		775
Domestic Retirement Services:				
Group retirement products		**572**		549
Individual fixed annuities		**932**		827
Individual variable annuities		**52**		58
Individual fixed annuities-runoff[c]		**236**		254
Total		**1,792**		1,688
Total Domestic		**2,579**		2,463

(in millions)	**2006**	2005
Foreign Life:		
Life insurance	**1,210**	1,164
Personal accident & health	**64**	54
Group products	**177**	131
Intercompany adjustments	**(10)**	(8)
Total	**1,441**	1,341
Foreign Retirement Services:		
Individual fixed annuities	**496**	377
Individual variable annuities	**193**	136
Total	**689**	513
Total Foreign	**2,130**	1,854
Total net investment income	**$ 4,709**	$ 4,317
Realized capital gains (losses):		
Domestic realized capital gains (losses)	**$ (194)**	$ (7)
Foreign realized capital gains (losses)	**228**	(156)
Pricing net investment gains[(d)]	**124**	81
Total Foreign	**352**	(75)
Total realized capital gains (losses)[(d)]	**$ 158**	$ (82)
Operating Income:		
Domestic	**$ 886**	$ 981
Foreign	**1,669**	1,200
Total operating income	**$ 2,555**	$ 2,181
Life insurance in-force[(e)]:		
Domestic	**$ 847,211**	$ 825,151
Foreign	**1,057,469**	1,027,682
Total	**$1,904,680**	$1,852,833

(a) Effective January 1, 2006, the Broker/Dealer operations of the Domestic Life Insurance companies are being reported and managed within AIG Capital Advisors in Asset Management. Included in GAAP premiums were revenues of $24 million for the first three months of 2005.

(b) Includes structured settlements, single premium immediate annuities and terminal funding annuities.

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

(d) For purposes of this presentation, pricing net investment gains are segregated as a component of total realized gains (losses). They represent certain amounts of realized capital gains where gains are an inherent element in pricing certain life products in some foreign countries.

(e) Amounts presented were as at March 31, 2006 and December 31, 2005.

AIG's Life Insurance & Retirement Services subsidiaries report their operations through the following operating units: Domestic Life — AIG American General, including American General Life Insurance Company (AG Life), United States Life Insurance in the City of New York (USLIFE) and American General Life and Accident Insurance Company (AGLA); Domestic Retirement Services — The Variable Annuity Life Insurance Company (VALIC), AIG Annuity Insurance Company (AIG Annuity) and AIG SunAmerica; Foreign Life — ALICO, AIRCO, AIG Edison Life, AIG Star Life, American International Assurance Company, Limited together with American International Assurance Company (Bermuda) Limited (AIA), Nan Shan Life Insurance Company, Ltd. (Nan Shan) and The Philippine American Life and General Insurance Company (Philamlife).

Life Insurance & Retirement Services Results

The increase in operating income in the first three months of 2006 when compared to the same period of 2005 is the net result of growth in domestic and foreign operations and increases in realized capital gains, somewhat offset by the negative effect of foreign exchange translation primarily related to a weaker Yen in 2006 as compared to the same period of 2005. The increase in realized capital gains in the first three months of 2006 compared to the first three months of 2005 were due to the effect of hedging activities that do not qualify for hedge accounting under FAS 133, foreign exchange gains and losses under FAS 52, offset by other-than-temporary declines in value of investments.

Life Insurance & Retirement Services GAAP premiums grew in the first three months of 2006 when compared to the same period of 2005. AIG's Domestic Life operations had continued growth of life insurance GAAP premiums. This growth reflects sustained strong periodic life sales from the independent distribution platform. Retail periodic life sales in the first three months of 2006 and 2005 were $207 million and $126 million, respectively. While not sustainable at this pace due to forthcoming product pricing changes, this result has positioned the Life segment to achieve another solid sales year. Strong growth of payout annuities GAAP premium emanated from sales of single premium immediate annuities. The group life/health business GAAP premium continued to decline reflecting lower growth in the credit business, and tightened pricing and underwriting in the group employer lines. Restructuring efforts in this business continue to focus on new product introductions, cross selling, other growth strategies, and exiting certain product lines. AGLA, the home service business, is diversifying product offerings, enhancing the capabilities and quality of the sales force and broadening the markets served beyond those historically serviced in an effort to accelerate growth, although it is expected to remain a slower growth business.

Domestic Retirement Services businesses faced a challenging environment in the first three months of 2006, as deposits declined approximately 7 percent compared to the same period last year. While individual variable annuity deposits grew 15 percent and group retirement deposits grew 19 percent, overall deposits declined from lower individual fixed annuity deposits. Individual fixed annuity deposits continued to decline due to the flat yield curve, which makes bank products such as certificates of deposit and other money market instruments with shorter duration more attractive than fixed annuities. Individual variable annuity deposit growth has improved since the introduction of new products in November 2005, primarily products with income and asset accumulation benefits. The following table reflects deposits for Domestic Retirement Services for the three months ended March 31, 2006 and 2005:

(in millions)	**2006**	2005
Group retirement products*	**$1,941**	$1,631
Individual fixed annuities	**1,687**	2,463
Individual variable annuities	**1,027**	891
Individual fixed annuities - runoff	**43**	49
Total	**$4,698**	$5,034

* *Includes mutual funds.*

In the first three months of 2006, surrender rates increased for individual fixed annuities, individual variable annuities and group retirement products compared to the first three months of 2005. Surrender rates for group retirement products improved modestly when compared to fourth quarter 2005. The increase in surrender rate for fixed annuities continues to be driven by the shape of the yield curve and general aging of the in-force block; however, less than 20 percent of the individual fixed annuity reserves are available to be surrendered without charge. Individual variable annuity surrenders primarily reflect the higher shock-lapse that occurs following expiration of the surrender charge period on certain 3-year and 7-year contracts (including a large closed block of acquired business). Reflecting a widespread industry phenomenon, this lapse rate, much of which was anticipated when the products were issued, has recently been affected by investor demand to exchange existing policies for new-generation contracts with living benefits or lower fees. In addition, partial withdrawals on certain variable annuity products have increased as AIG has introduced features designed to generate a stream of income to the participants. The following chart shows the amount of reserves by surrender charge category for Domestic Retirement Services as of March 31, 2006:

(in millions)	**Group Retirement Products***	**Individual Fixed Annuities**	**Individual Variable Annuities**
Zero or no surrender charge	$40,633	$ 9,927	$10,210
Between 0 percent - 4 percent	11,988	10,927	8,708
Greater than 4 percent	2,335	30,987	10,105
Non-Surrenderable	892	3,150	81
Total	$55,848	$54,991	$29,104

* *Excludes mutual funds.*

A continued increase in the level of surrenders in any of these businesses or in the individual fixed annuities runoff block could accelerate the amortization of deferred acquisition costs in future years and will negatively affect fee income earned on assets under management. The combination of deposits and surrenders resulted in negative net flows for the first three months of 2006. The following table reflects the net flows by line of business for Domestic Retirement Services as of March 31, 2006 and 2005:

Domestic Retirement Services – Net Flows[a]

(in millions)	**2006**	2005
Group retirement products[b]	**$ 441**	$ 279
Individual fixed annuities	**(1)**	1,385
Individual variable annuities	**(133)**	72
Individual fixed annuities - runoff	**(826)**	(566)
Total	**$(519)**	$1,170

(a) Net flows are defined as deposits received, less benefits, surrenders, withdrawals and death benefits.

(b) Includes mutual funds.

Foreign Life Insurance & Retirement Services GAAP premiums increased by approximately 3 percent, or approximately 8 percent in original currency. AIG transacts business in most major foreign currencies. Globally, AIG's deep and diverse distribution, which includes bancassurance, worksite marketing, direct marketing and strong agency organizations, provides a powerful distribution platform for our diverse product lines. In Japan, distribution of single premium life insurance products through banks was deregulated in December 2005 resulting in strong sales of products designed for that market during the first three months of 2006. This new distribution outlet adds to the existing multiple distribution platform in Japan where AIG remains the leading foreign provider. In Southeast Asia, there has been a continuing trend, as the market develops, for clients to purchase investment-oriented products. AIG's life operations in that region have responded to this trend by offering a wide array of investment linked products, both periodic pay and single premium, with multiple fund selection, but with minimal investment guarantees. For GAAP reporting purposes, only revenues from policy charges for insurance, administration, and surrender charges are reported as GAAP premiums for these life products. This product mix shift contributed to the single digit growth rate in Foreign Life Insurance & Retirement Services GAAP premiums, while continuing to grow total reserves by double digits.

Japanese tax authorities are expected to announce shortly a reduction in the amount of premium that policyholders may deduct from their Japanese tax returns for a certain group of accident and health products. Foreign life operations in Japan experienced a decline in sales of those specific products in the first three months of 2006; however, total accident and health sales continued to be strong overall due to growth in sales of core health products and the success of a new cancer insurance product sold by AIG Edison. In the first three months of 2006, Japan life operations launched a

new product for the corporate market and plans to launch additional products with full tax deductibility in the near future to replace those that will lose that feature. With respect to the existing products that have exposure to the change in tax regulation, the amount of first year premium reported for the full year 2005 was approximately $129 million and the deferred acquisition cost asset at December 31, 2005 was $267 million. To date, lapse experience has remained within pricing assumptions. Management continues to believe that any increase in policy lapses would not be material to AIG's consolidated financial condition or results of operations.

The Foreign Retirement Services business continued to grow in Japan and Korea by expanding distribution and leveraging AIG's product expertise. Reserves for individual fixed annuities continue to grow although demand for multi-currency fixed annuities in Japan has slowed due to currency rate fluctuations, and rising local interest rates and equity markets. Growth of individual variable annuities has accelerated as those products have become more popular with consumers in Japan and Europe coupled with improved performance of equity markets.

Foreign Life Insurance & Retirement Services operations produced 78 percent and 79 percent of Life Insurance & Retirement Services GAAP premiums in the first three months of 2006 and 2005, respectively.

AIG transacts business in most major foreign currencies. The following table summarizes the effect of changes in foreign currency exchange rates on the growth of Life Insurance & Retirement Services GAAP premiums:

	2006
Growth in original currency	**7.1%**
Foreign exchange effect	**(4.0)**
Growth as reported in U.S. dollars	**3.1%**

The growth in net investment income in the first three months of 2006 and 2005 parallels the growth in general account reserves and surplus for both Domestic and Foreign Life Insurance & Retirement Services companies. Also, net investment income was positively affected by the compounding of previously earned and reinvested investment cash flows along with the addition of new net cash flows from operations. Investment income includes income generated from traditional fixed income investments as well as income generated from other sources. The following table summarizes the components of net investment income for the three months ended March 31, 2006 and 2005:

(in millions)	**2006**	2005
Domestic		
Fixed maturities, including short term investments	**$2,308**	$2,232
Equity securities	**5**	–
Interest on mortgage, policy and collateral loans	**189**	167
Partnership income – excluding Synfuels	**141**	154
Partnership income – Synfuels	**(37)**	(36)
Other	**(3)**	(27)
Total investment income	**2,603**	2,490
Investment expenses	**24**	27
Net investment income	**$2,579**	$2,463
Foreign		
Fixed maturities, including short term investments	**$1,531**	$1,373
Equity securities	**71**	42
Interest on mortgage, policy and collateral loans	**108**	113
Partnership income	**17**	12
Policyholder trading gains (losses)*	**385**	278
Other	**73**	83
Total investment income	**2,185**	1,901
Investment expenses	**55**	47
Net investment income	**$2,130**	$1,854
Total		
Fixed maturities, including short term investments	**$3,839**	$3,605
Equity securities	**76**	42
Interest on mortgage, policy and collateral loans	**297**	280
Partnership income – excluding Synfuels	**158**	166
Partnership income – Synfuels	**(37)**	(36)
Policyholder trading gains (losses)*	**385**	278
Other	**70**	56
Total investment income	**4,788**	4,391
Investment expenses	**79**	74
Net investment income	**$4,709**	$4,317

** Relates principally to trading and investment activity in accordance with SOP 03-1. These amounts are offset by a similar change included in incurred policy losses and benefits.*

AIG generates income tax credits as a result of investing in synthetic fuel production (synfuels) related to the investment loss shown in the above table and records those benefits in its provision for income taxes. The amount of those income tax credits was $40 million and $54 million for the first three months of 2006 and 2005, respectively. See Note 6(l) of Notes to Consolidated Financial Statements for a further discussion of the effect of the change in oil prices on synfuel tax credits.

Realized capital gains (losses) include normal portfolio transactions as well as derivative gains (losses) for transactions that do not qualify for hedge accounting treatment under FAS 133, transactional foreign exchange gains and losses and other-than-temporary decline in the value of investments, related primarily to declines in certain high-yield credit positions. The following table summarizes realized

capital gains (losses) by major category for the three months ended March 31, 2006 and 2005:

(in millions)	**2006**	2005
Domestic life		
Fixed maturities	**$ (22)**	$ (6)
Equity securities	**2**	–
Other:		
FAS 52	**(1)**	–
FAS 133	**87**	104
Other-than-temporary decline	**(54)**	(23)
Other	**(4)**	(3)
Total domestic life	**8**	72
Domestic retirement services:		
Fixed maturities	**(72)**	(60)
Equity securities	**14**	7
Other:		
FAS 133	**3**	20
Other-than-temporary decline	**(125)**	(42)
Other	**(22)**	(4)
Total domestic retirement services	**(202)**	(79)
Foreign		
Fixed maturities	**(23)**	65
Equity securities	**152**	53
Other:		
FAS 52	**(37)**	(111)
FAS 133	**226**	(92)
Other-than-temporary decline	**(37)**	(5)
Other	**71**	15
Total foreign	**352**	(75)
Total	**$ 158**	$ (82)

Life Insurance & Retirement Services operating income grew by 17 percent in the first three months of 2006. Domestic Life operations continued to perform well in its core life insurance businesses that included growth of retail periodic sales in the first three months of 2006. Domestic Retirement Services results reflect the increase in underlying reserves which grew 6 percent over the same period last year. Foreign Life Insurance & Retirement Services operating income growth on a local currency basis was strong, but results reported in U.S. dollars were dampened by a significantly weaker Yen compared to the same period last year.

Line of business results for Domestic Life Insurance & Retirement Services exclude the effect of realized capital gains (losses), but include the related effect on the amortization of deferred acquisition costs. In addition, period to period comparisons of operating income for some lines of business are affected by yield enhancement activity, particularly partnership income. The following table summarizes Domestic Life Insurance & Retirement Services partnership income by line of business for the three months ended March 31, 2006 and 2005:

(in millions)	**2006**	2005
Domestic life – excluding Synfuels:		
Life insurance	**$ 8**	$ 79
Home service	**2**	1
Subtotal	**10**	80
Domestic life – Synfuels:		
Life insurance	**(25)**	(24)
Home service	**(12)**	(12)
Subtotal	**(37)**	(36)
Total domestic life	**(27)**	44
Retirement services:		
Group retirement products	**42**	25
Individual fixed annuities	**89**	49
Total retirement services	**131**	74
Total	**$104**	$118

Operating income for the AIG Domestic Life Insurance line of business declined 20 percent due to lower partnership income. Operating income for the home service line of business grew 12 percent in the first three months of 2006. These earnings grew due to higher investment income related to call and tender income on fixed maturity securities. The group life/health business results continue to reflect the effects of non-renewal of cases where acceptable margins could not be achieved. Payout annuities line of business increased operating income, generally in line with growth in reserves.

Group retirement products operating income grew in line with growth in underlying reserves which drives growth in fee revenues and a modest amount of additional income from yield enhancement investments. Operating income for individual fixed annuities grew as a result of growth in reserves, higher net investment income spread from partnership income and lower DAC amortization related to realized capital losses. Individual variable annuities operating income for the first three months of 2006 was negatively affected by higher deferred policy acquisition cost amortization related to increased current year surrenders. Operating income for individual fixed annuities-runoff grew 22 percent due to higher spreads from decreases in crediting rates, which have temporarily outpaced the decline in earned rates. A number of these policies will be exiting the surrender charge period in 2006.

Foreign Life Insurance & Retirement Services operating income of $1.67 billion for the first three months of 2006 included $352 million of realized capital gains, and for the first three months of 2005, operating income of $1.20 billion included $75 million of realized capital losses.

Foreign Life Insurance & Retirement Services results before the effect of realized capital gains (losses) reflects a decline of Life insurance operating income for the first three months of 2006 compared to the same period last year. The 2006 results include a $40 million operating loss attributable to this segment's share of the losses from AIG Credit Card Company (Taiwan) compared to a gain of $10 million in the first three months of 2005. Also, an additional provision was made to the Singapore and Malaysia participating policyholder reserve of $18 million. These items coupled with a $29 million positive effect from DAC unlocking in the same period in 2005 resulted in lower year-on-year operating in-

come growth. On a comparable basis, the growth in Life insurance results was generally in line with the growth in reserves. Personal accident & health results reflect continued stable profit margins, but year-on-year comparisons in U.S. dollars are affected by the weakening Yen exchange rate given the large concentration of that product line in Japan. Group results grew across all segments and were greatly improved against last year. The largest contributor to the growth in group products is the pension profit center which experienced higher growth in fee income emanating from increased assets under management. Growth of individual fixed annuities operating income, emanating primarily from Japan, is in line with the growth in average assets under management and the greater benefits from increasing scale. The growth of individual variable annuities reflects strong growth in assets under management related to the increased demand for that product in Japan.

The contribution of Life Insurance & Retirement Services operating income to AIG's consolidated income before income taxes, minority interest and cumulative effect of an accounting change amounted to 53 percent in the first three months of 2006, compared to 39 percent in the same period of 2005.

Underwriting and Investment Risk

The risks associated with life and accident and health products are underwriting risk and investment risk. The risk associated with the financial and investment contract products is primarily investment risk.

Underwriting risk represents the exposure to loss resulting from the actual policy experience adversely emerging in comparison to the assumptions made in the product pricing associated with mortality, morbidity, termination and expenses. The emergence of significant adverse experience would require an adjustment to DAC and benefit reserves that could have a substantial effect on AIG's results of operations.

Natural disasters such as hurricanes, earthquakes and other catastrophes have the potential to adversely affect AIG's operating results. Other risks, such as an outbreak of a pandemic disease, such as the Avian Influenza A Virus (H5N1), could adversely affect AIG's business and operating results to an extent that may be only minimally offset by reinsurance programs.

While outbreaks of the Avian Flu continue to occur among poultry or wild birds in a number of countries in Asia, Europe, and Africa, transmission to humans has been rare to date. If the virus mutates to a form that can be transmitted from human to human, it has the potential to spread rapidly worldwide. If such an outbreak were to take place, early quarantine and vaccination could be critical to containment.

Both the contagion and mortality rate of any mutated H5N1 virus that can be transmitted from human to human are highly speculative. AIG continues to monitor the developing facts. A significant global outbreak could have a material adverse effect on Life Insurance & Retirement Services operating results and liquidity from increased mortality and morbidity rates.

AIG's Foreign Life Insurance & Retirement Services companies generally limit their maximum underwriting exposure on life insurance of a single life to approximately $1.7 million of coverage. AIG's Domestic Life Insurance & Retirement Services companies limit their maximum underwriting exposure on life insurance of a single life to $10 million of coverage in certain circumstances by using yearly renewable term reinsurance. (See also the discussion under "Liquidity" herein.)

AIRCO acts primarily as an internal reinsurance company for AIG's foreign life operations. This facilitates insurance risk management (retention, volatility, concentrations) and capital planning locally (branch and subsidiary). It also allows AIG to pool its insurance risks and purchase reinsurance more efficiently at a consolidated level, manage global counterparty risk and relationships and manage global life catastrophe risks.

AIG's domestic Life Insurance & Retirement Services operations utilize internal and third-party reinsurance relationships to manage insurance risks and to facilitate capital management strategies. Pools of highly-rated third-party reinsurers are utilized to manage net amounts at risk in excess of retention limits. AIG's domestic life insurance companies also cede excess, non-economic reserves carried on a statutory-basis only on certain term and universal life insurance policies and certain fixed annuities to AIG Life of Bermuda Ltd., a wholly owned Bermuda reinsurer.

AIG generally obtains letters of credit in order to obtain statutory recognition of these intercompany reinsurance transactions. For this purpose, AIG entered into a $2.5 billion syndicated letter of credit facility in December 2004. Letters of credit totaling $2.50 billion were outstanding as of March 31, 2006. The letter of credit facility has a ten-year term, but the facility can be reduced or terminated by the lenders beginning after seven years.

In November 2005, AIG entered into a revolving credit facility for an aggregate amount of $3 billion. The facility can be drawn in the form of letters of credit with terms of up to ten years. As of March 31, 2006, $1.99 billion principal amount of letters of credit are outstanding under this facility, of which approximately $620 million relates to life intercompany reinsurance transactions. AIG also obtained approximately $273 million letters of credit on a bilateral basis.

Investment risk represents the exposure to loss resulting from the cash flows from the invested assets, primarily long-

term fixed rate investments, being less than the cash flows required to meet the obligations of the expected policy and contract liabilities and the necessary return on investments. (See also the discussion under "Liquidity" herein.)

To minimize its exposure to investment risk, AIG tests the cash flows from the invested assets and policy and contract liabilities using various interest rate scenarios to evaluate investment risk and to confirm that assets are sufficient to pay these liabilities.

AIG actively manages the asset-liability relationship in its foreign operations, as it has been doing throughout AIG's history, even though certain territories lack qualified long-term investments or certain local regulatory authorities may impose investment restrictions. For example, in several Southeast Asian countries, the duration of investments is shorter than the effective maturity of the related policy liabilities. Therefore, there is risk that the reinvestment of the proceeds at the maturity of the initial investments may be at a yield below that of the interest required for the accretion of the policy liabilities. Additionally, there exists a future investment risk associated with certain policies currently in force which will have premium receipts in the future. That is, the investment of these future premium receipts may be at a yield below that required to meet future policy liabilities.

In the first three months of 2006, new money investment yields have been generally rising in some markets, such as Japan, Thailand and the U.S., which is generally favorable to AIG's spread-based businesses. In regard to inforce business, management focus is required in both the investment and product management process to maintain an adequate yield to match the interest necessary to support future policy liabilities. Business strategies continue to evolve to maintain profitability of the overall business. As such, in some countries, new products are being introduced with minimal investment guarantees resulting in a shift toward investment linked savings products and away from traditional savings products with higher guarantees.

The investment of insurance cash flows and reinvestment of the proceeds of matured securities and coupons requires active management of investment yields while maintaining satisfactory investment quality and liquidity.

AIG may use alternative investments in certain foreign jurisdictions where interest rates remain low and there are limited long-dated bond markets, including equities, real estate and foreign currency denominated fixed income instruments to extend the duration or increase the yield of the investment portfolio to more closely match the requirements of the policyholder liabilities and DAC recoverability. This strategy has been effectively used in Japan and more recently by Nan Shan in Taiwan. Foreign assets comprised approximately 31 percent of Nan Shan's invested assets at March 31, 2006, slightly below the maximum allowable percentage under current regulation. In response to the low interest rate environment and the volatile exchange rate of the NT dollar, Nan Shan is emphasizing new products with lower implied guarantees, including participating endowments and variable universal life. Although the risks of a continued low interest rate environment coupled with a volatile NT dollar could increase net liabilities and require additional capital to maintain adequate local solvency margins, Nan Shan currently believes it has adequate resources to meet all future policy obligations.

AIG actively manages the asset-liability relationship in its domestic operations. This relationship is more easily managed through the ample supply of qualified long-term investments.

AIG uses asset-liability matching as a management tool worldwide to determine the composition of the invested assets and appropriate marketing strategies. As a part of these strategies, AIG may determine that it is economically advantageous to be temporarily in an unmatched position due to anticipated interest rate or other economic changes. In addition, the absence of long-dated fixed income instruments in certain markets may preclude a matched asset-liability position in those markets.

A number of guaranteed benefits, such as living benefits or guaranteed minimum death benefits, are offered on certain variable life and variable annuity products. AIG manages its exposure resulting from these long-term guarantees through reinsurance or capital market hedging instruments.

DAC for Life Insurance & Retirement Services products arises from the deferral of those costs that vary with, and are directly related to, the acquisition of new or renewal business. Policy acquisition costs for life insurance products are generally deferred and amortized over the premium paying period of the policy. Policy acquisition costs that relate to universal life and investment-type products, including variable and fixed annuities (investment-oriented products) are deferred and amortized, with interest, as appropriate, in relation to the historical and future incidence of estimated gross profits to be realized over the estimated lives of the contracts. Amortization expense includes the effects of current period realized capital gains and losses for investment type products. With respect to investment-oriented products, AIG's policy is to adjust amortization assumptions for DAC when estimates of current or future gross profits to be realized from these contracts are revised. With respect to variable annuities sold domestically (representing the vast majority of AIG's variable annuity business), the assumption for the long-term annual net growth rate of the equity markets used in the determination of DAC amortization is approximately ten percent. A methodology referred to as "reversion to the mean" is used to maintain this long-term net growth rate assumption, while giving consideration to short-term variations in equity markets. Estimated gross profits include investment income and gains and losses less interest required on policyholder

reserves, as well as other charges in the contract less actual mortality and expenses. Current experience and changes in the expected future gross profits are analyzed to determine the effect on the amortization of DAC. The estimation of projected gross profits requires significant management judgment. The assumptions with respect to the current and projected gross profits are reviewed and analyzed quarterly and are adjusted accordingly.

The following table summarizes the major components of the changes in deferred acquisition costs and the value of business acquired (VOBA) for the three months ended March 31, 2006 and 2005:

(in millions)	**2006**			2005		
	DAC	**VOBA**	**Total**	DAC	VOBA	Total
Domestic Life Insurance & Retirement Services:						
Balance at beginning of year	**$10,505**	**$ 865**	**$11,370**	$ 8,830	$ 836	$ 9,666
Acquisition costs deferred	**557**	**–**	**557**	541	–	541
Amortization (charged) or credited to operating income:						
Related to realized capital gains (losses)	**13**	**6**	**19**	10	(2)	8
Related to unlocking future assumptions	**2**	**–**	**2**	–	–	–
All other amortization	**(365)**	**(26)**	**(391)**	(362)	(21)	(383)
Change in unrealized gains (losses) on securities	**1,094**	**91**	**1,185**	826	65	891
Increase (decrease) due to foreign exchange	**(1)**	**–**	**(1)**	(2)	–	(2)
Balance at end of period	**$11,805**	**$ 936**	**$12,741**	$ 9,843	$ 878	$10,721
Foreign Life Insurance & Retirement Services:						
Balance at beginning of year	**$16,552**	**$1,278**	**$17,830**	$14,472	$1,681	$16,153
Acquisition costs deferred	**1,206**	**–**	**1,206**	1,163	–	1,163
Amortization (charged) or credited to operating income:						
Related to realized capital gains (losses)	**1**	**–**	**1**	–	–	–
Related to unlocking future assumptions	**17**	**–**	**17**	31	–	31
All other amortization	**(524)**	**(44)**	**(568)**	(487)	(60)	(547)
Change in unrealized gains (losses) on securities	**5**	**(4)**	**1**	(81)	1	(80)
Increase (decrease) due to foreign exchange	**473**	**41**	**514**	149	(19)	130
Balance at end of period	**$17,730**	**$1,271**	**$19,001**	$15,247	$1,603	$16,850
Total Life Insurance & Retirement Services:						
Balance at beginning of year	**$27,057**	**$2,143**	**$29,200**	$23,302	$2,517	$25,819
Acquisition costs deferred	**1,763**	**–**	**1,763**	1,704	–	1,704
Amortization (charged) or credited to operating income:						
Related to realized capital gains (losses)	**14**	**6**	**20**	10	(2)	8
Related to unlocking future assumptions	**19**	**–**	**19**	31	–	31
All other amortization	**(889)**	**(70)**	**(959)**	(849)	(81)	(930)
Change in unrealized gains (losses) on securities	**1,099**	**87**	**1,186**	745	66	811
Increase (decrease) due to foreign exchange	**472**	**41**	**513**	147	(19)	128
Balance at end of period	**$29,535**	**$2,207**	**$31,742**	$25,090	$2,481	$27,571

AIG's variable annuity earnings will be affected by changes in market returns because separate account revenues, primarily composed of mortality and expense charges and asset management fees, are a function of asset values.

DAC for both insurance-oriented and investment-oriented products as well as retirement services products are reviewed for recoverability, which involves estimating the future profitability of current business. This review also involves significant management judgment. If the actual emergence of future profitability were to be substantially different than that estimated, AIG's results of operations could be significantly affected in future periods.

Invested Assets

The following tables summarize the composition of AIG's invested assets by segment, at March 31, 2006 and December 31, 2005:

(in millions)	General Insurance	Life Insurance & Retirement Services	Asset Management	Financial Services	Other	Total
2006						
Fixed maturities:						
Bonds available for sale, at market value	$ 55,348	$275,955	$31,894	$ 1,313	$ –	$364,510
Bonds held to maturity, at amortized cost	21,520	–	–	–	–	21,520
Bond trading securities, at market value	–	1,226	4,003	–	–	5,229
Equity securities:						
Common stocks available for sale, at market value	4,753	8,510	243	–	63	13,569
Common stocks trading, at market value	434	9,435	401	–	–	10,270
Preferred stocks available for sale, at market value	1,690	757	–	9	–	2,456
Mortgage loans on real estate, net of allowance	14	10,830	4,059	65	–	14,968
Policy loans	2	7,166	48	2	–	7,218
Collateral and guaranteed loans, net of allowance	3	1,202	609	2,202	98	4,114
Financial services assets:						
Flight equipment primarily under operating leases, net of accumulated depreciation	–	–	–	37,580	–	37,580
Securities available for sale, at market value	–	–	–	38,225	–	38,225
Trading securities, at market value	–	–	–	6,350	–	6,350
Spot commodities	–	–	–	230	–	230
Unrealized gain on swaps, options and forward transactions	–	–	–	17,792	–	17,792
Trading assets	–	–	–	1,411	–	1,411
Securities purchased under agreements to resell, at contract value	–	–	–	12,297	–	12,297
Finance receivables, net of allowance	–	–	–	27,219	–	27,219
Securities lending collateral, at market value	5,082	45,791	12,034	60	–	62,967
Other invested assets	6,828	8,422	11,083	2,953	10	29,296
Short-term investments, at cost	2,810	6,650	6,589	1,293	1	17,343
Total investments and financial services assets as shown in the balance sheet	98,484	375,944	70,963	149,001	172	694,564
Cash	243	652	68	282	3	1,248
Investment income due and accrued	1,141	4,163	406	19	4	5,733
Real estate, net of accumulated depreciation	610	2,786	2,229	24	29	5,678
Total invested assets	$100,478	$383,545	$73,666	$149,326	$208	$707,223

(in millions)	General Insurance	Life Insurance & Retirement Services	Asset Management	Financial Services	Other	Total
2005						
Fixed maturities:						
Bonds available for sale, at market value	$50,870	$273,165	$34,174	$ 1,307	$ –	$359,516
Bonds held to maturity, at amortized cost	21,528	–	–	–	–	21,528
Bond trading securities, at market value	–	1,073	3,563	–	–	4,636
Equity securities:						
Common stocks available for sale, at market value	4,505	7,436	227	–	59	12,227
Common stocks trading, at market value	425	8,122	412	–	–	8,959
Preferred stocks available for sale, at market value	1,632	760	–	10	–	2,402
Mortgage loans on real estate, net of allowance	14	10,247	3,968	71	–	14,300
Policy loans	2	6,987	48	2	–	7,039
Collateral and guaranteed loans, net of allowance	3	1,172	578	1,719	98	3,570
Financial services assets:						
Flight equipment primarily under operating leases, net of accumulated depreciation	–	–	–	36,245	–	36,245
Securities available for sale, at market value	–	–	–	37,511	–	37,511
Trading securities, at market value	–	–	–	6,499	–	6,499
Spot commodities	–	–	–	92	–	92
Unrealized gain on swaps, options and forward transactions	–	–	–	18,695	–	18,695
Trading assets	–	–	–	1,204	–	1,204
Securities purchased under agreements to resell, at contract value	–	28	–	14,519	–	14,547
Finance receivables, net of allowance	–	–	–	27,995	–	27,995
Securities lending collateral, at market value	4,931	42,991	11,549	–	–	59,471
Other invested assets	6,272	7,777	10,459	2,751	8	27,267
Short-term investments, at cost	2,482	5,855	5,619	1,382	4	15,342
Total investments and financial services assets as shown in the balance sheet	92,664	365,613	70,597	150,002	169	679,045
Cash	305	989	196	331	76	1,897
Investment income due and accrued	1,232	4,073	402	18	2	5,727
Real estate, net of accumulated depreciation	603	2,729	1,710	24	32	5,098
Total invested assets	$94,804	$373,404	$72,905	$150,375	$279	$691,767

Insurance and Asset Management Invested Assets

AIG's investment strategy is to invest primarily in high quality securities while maintaining diversification to avoid significant exposure to issuer, industry and/or country concentrations. With respect to Domestic General Insurance, AIG's strategy is to invest in longer duration fixed maturity investments to maximize the yields at the date of purchase. With respect to Life Insurance & Retirement Services, AIG's strategy is to produce cash flows required to meet maturing insurance liabilities. (See also the discussion under "Operating Review: Life Insurance & Retirement Services Operations" herein.) AIG invests in equities for various reasons, including diversifying its overall exposure to interest rate risk. Available for sale bonds and equity securities are subject to declines in fair value. Such declines in fair value are presented in unrealized appreciation or depreciation of investments, net of taxes as a component of accumulated other comprehensive income. Declines that are determined to be other-than-temporary are reflected in income in the period in which the intent to hold the securities to recovery no longer exists. See "Valuation of Invested Assets". Generally, insurance regulations restrict the types of assets in which an insurance company may invest. When permitted by regulatory authorities and when deemed necessary to protect insurance assets, including invested assets, from adverse movements in foreign currency exchange rates, interest rates and equity prices, AIG and its insurance subsidiaries may enter into derivative transactions as end users. (See also the discussion under "Derivatives" herein.)

In certain jurisdictions, significant regulatory and/or foreign governmental barriers exist which may not permit the immediate free flow of funds between insurance subsidiaries or from the insurance subsidiaries to AIG parent.

The following tables summarize the composition of AIG's insurance and asset management invested assets by segment, at March 31, 2006 and December 31, 2005:

(dollars in millions)	General Insurance	Life Insurance & Retirement Services	Asset Management	Total	Percent of Total	Percent Distribution Domestic	Percent Distribution Foreign
2006							
Fixed maturities:							
Bonds available for sale, at market value	$ 55,348	$275,955	$31,894	$363,197	65.1%	58.0%	42.0%
Bonds held to maturity, at amortized cost	21,520	–	–	21,520	3.9	100.0	–
Bond trading securities, at market value	–	1,226	4,003	5,229	0.9	3.9	96.1
Equity securities:							
Common stocks available for sale, at market value	4,753	8,510	243	13,506	2.4	27.6	72.4
Common stocks trading, at market value	434	9,435	401	10,270	1.9	4.2	95.8
Preferred stocks available for sale, at market value	1,690	757	–	2,447	0.4	86.9	13.1
Mortgage loans on real estate, net of allowance	14	10,830	4,059	14,903	2.7	84.5	15.5
Policy loans	2	7,166	48	7,216	1.3	41.6	58.4
Collateral and guaranteed loans, net of allowance	3	1,202	609	1,814	0.3	1.3	98.7
Securities lending collateral, at market value	5,082	45,791	12,034	62,907	11.3	85.8	14.2
Other invested assets	6,828	8,422	11,083	26,333	4.7	85.7	14.3
Short-term investments, at cost	2,810	6,650	6,589	16,049	2.9	26.2	73.8
Cash	243	652	68	963	0.2	19.4	80.6
Investment income due and accrued	1,141	4,163	406	5,710	1.0	57.5	42.5
Real estate, net of accumulated depreciation	610	2,786	2,229	5,625	1.0	50.7	49.3
Total	$100,478	$383,545	$73,666	$557,689	100.0%	61.2%	38.8%

(dollars in millions)	General Insurance	Life Insurance & Retirement Services	Asset Management	Total	Percent of Total	Percent Distribution Domestic	Percent Distribution Foreign
2005							
Fixed maturities:							
Bonds available for sale, at market value	$50,870	$273,165	$34,174	$358,209	66.2%	59.2%	40.8%
Bonds held to maturity, at amortized cost	21,528	–	–	21,528	4.0	100.0	–
Bond trading securities, at market value	–	1,073	3,563	4,636	0.9	3.3	96.7
Equity securities:							
Common stocks available for sale, at market value	4,505	7,436	227	12,168	2.2	28.7	71.3
Common stocks trading, at market value	425	8,122	412	8,959	1.7	4.8	95.2
Preferred stocks available for sale, at market value	1,632	760	–	2,392	0.4	88.8	11.2
Mortgage loans on real estate, net of allowance	14	10,247	3,968	14,229	2.7	84.6	15.4
Policy Loans	2	6,987	48	7,037	1.3	42.8	57.2
Collateral and guaranteed loans, net of allowance	3	1,172	578	1,753	0.3	1.2	98.8
Securities purchased under agreements to resell, at contract value	–	28	–	28	–	–	100.0
Securities lending collateral, at market value	4,931	42,991	11,549	59,471	11.0	87.3	12.7
Other invested assets	6,272	7,777	10,459	24,508	4.5	85.8	14.2
Short-term investments, at cost	2,482	5,855	5,619	13,956	2.6	27.3	72.7
Cash	305	989	196	1,490	0.2	15.0	85.0
Investment income due and accrued	1,232	4,073	402	5,707	1.1	56.9	43.1
Real estate, net of accumulated depreciation	603	2,729	1,710	5,042	0.9	45.2	54.8
Total	$94,804	$373,404	$72,905	$541,113	100.0%	62.3%	37.7%

Credit Quality

At March 31, 2006, approximately 60 percent of the fixed maturities investments were domestic securities. Approximately 36 percent of such domestic securities were rated AAA by one or more of the principal rating agencies. Approximately six percent were below investment grade or not rated.

A significant portion of the foreign fixed income portfolio is rated by Moody's Investors Service (Moody's), S&P or similar foreign services. Similar credit quality rating services are not available in all overseas locations. AIG reviews the credit quality of the foreign portfolio nonrated fixed income investments, including mortgages. At March 31, 2006, approximately 18 percent of the foreign fixed income investments were either rated AAA or, on the basis of AIG's internal analysis, were equivalent from a credit standpoint to securities so rated. Approximately six percent were below investment grade or not rated at that date. A large portion of the foreign fixed income portfolio are sovereign fixed maturity securities supporting the policy liabilities in the country of issuance.

Any fixed income security may be subject to downgrade for a variety of reasons subsequent to any balance sheet date.

Valuation of Invested Assets

AIG has the ability to hold any fixed maturity security to its stated maturity, including those fixed maturity securities classified as available for sale. Therefore, the decision to sell any such fixed maturity security classified as available for sale reflects the judgment of AIG's management that the security sold is unlikely to provide, on a relative value basis, as attractive a return in the future as alternative securities entailing comparable risks. With respect to distressed securities, the sale decision reflects management's judgment that the risk-discounted anticipated ultimate recovery is less than the value achievable on sale.

The valuation of invested assets involves obtaining a market value for each security. The source for the market value is generally from market exchanges or dealer quotations, with the exception of nontraded securities.

If AIG chooses to hold a security, it evaluates the security for an other-than-temporary impairment in valuation. As a

matter of policy, the determination that a security has incurred an other-than-temporary decline in value and the amount of any loss recognition requires the judgment of AIG's management and a continual review of its investments.

In general, a security is considered a candidate for other-than-temporary impairment if it meets any of the following criteria:

- Trading at a significant (25 percent or more) discount to par or amortized cost (if lower) for an extended period of time (nine months or longer);
- The occurrence of a discrete credit event resulting in (i) the issuer defaulting on a material outstanding obligation; or (ii) the issuer seeking protection from creditors under the bankruptcy laws or any similar laws intended for the court supervised reorganization of insolvent enterprises; or (iii) the issuer proposing a voluntary reorganization pursuant to which creditors are asked to exchange their claims for cash or securities having a fair value substantially lower than par value of their claims; or
- In the opinion of AIG's management, it is probable that AIG may not realize a full recovery on its investment, irrespective of the occurrence of one of the foregoing events.

At each balance sheet date, AIG evaluates its securities holdings in an unrealized loss position. Where AIG does not intend to hold such securities until they have fully recovered their carrying value based on the circumstances present at the date of evaluation, AIG records the unrealized loss in income. If events or circumstances change, such as unexpected changes in creditworthiness of the obligor, general interest rate environment, tax circumstances, liquidity events, and statutory capital management considerations among others, AIG revisits its intent to determine if a loss should be recorded in income. Further, if a loss is recognized from a sale subsequent to a balance sheet date pursuant to these changes in circumstances, the loss is recognized in the period in which the intent to hold the securities to recovery no longer exists.

Once a security has been identified as other-than-temporarily impaired, the amount of such impairment is determined by reference to that security's contemporaneous market price and recorded as a charge to earnings.

As a result of these policies, AIG recorded other-than-temporary impairment losses, net of taxes, of $147 million and $61 million in the first three months of 2006 and 2005, respectively.

No impairment charge with respect to any one single credit was significant to AIG's consolidated financial condition or results of operations, and no individual impairment loss exceeded 1.0 percent of consolidated net income for the first three months of 2006.

Excluding the other-than-temporary impairments noted above, the changes in market value for AIG's available for sale portfolio, which constitutes the vast majority of AIG's investments, were recorded in accumulated other comprehensive income as unrealized gains or losses, net of tax.

At March 31, 2006, the fair value of AIG's fixed maturities and equity securities aggregated to $417.9 billion. At March 31, 2006, aggregate unrealized gains after taxes for fixed maturity and equity securities were $9.5 billion. At March 31, 2006, the aggregate unrealized losses after taxes of fixed maturity and equity securities were approximately $3.7 billion.

The effect on net income of unrealized losses after taxes will be further mitigated upon realization, because certain realized losses will be charged to participating policyholder accounts, or realization will result in current decreases in the amortization of certain deferred policy acquisition costs.

At March 31, 2006, unrealized losses for fixed maturity securities and equity securities did not reflect any significant industry concentrations.

The amortized cost of fixed maturities available for sale in an unrealized loss position at March 31, 2006, by contractual maturity, is shown below:

(in millions)	Amortized Cost
Due in one year or less	$ 4,876
Due after one year through five years	31,523
Due after five years through ten years	74,930
Due after ten years	75,950
Total	$187,279

In the three months ended March 31, 2006, the pretax realized losses incurred with respect to the sale of fixed maturities and equity securities were $380 million. The aggregate fair value of securities sold was $13.9 billion, which was approximately 97 percent of amortized cost. The average period of time that securities sold at a loss during the three months ended March 31, 2006 were trading continuously at a price below book value was approximately four months.

At March 31, 2006, aggregate pretax unrealized gains were $14.7 billion, while the pretax unrealized losses with respect to investment grade bonds, below investment grade bonds and equity securities were $5.2 billion, $270 million and $206 million, respectively. Aging of the pretax unrealized losses with respect to these securities, distributed as a percentage of cost relative to unrealized loss (the extent by which the market value is less than amortized cost or cost), including the number of respective items, was as follows:

	Less than or equal to 20% of Cost[a]			Greater than 20% to 50% of Cost[a]			Greater than 50% of Cost[a]			Total		
Aging (dollars in millions)	Cost[a]	Unrealized Loss	Items	Cost[a]	Unrealized Loss	Items	Cost[a]	Unrealized Loss	Items	Cost[a]	Unrealized Loss[b]	Items
Investment grade bonds												
0-6 months	$118,849	$2,558	14,911	$ 2	$ 1	1	$32	$23	5	$118,883	$2,582	14,917
7-12 months	38,129	1,480	4,804	1	–	2	–	–	3	38,130	1,480	4,809
>12 months	23,053	1,046	3,595	179	38	16	5	4	4	23,237	1,088	3,615
Total	$180,031	$5,084	23,310	$182	$39	19	$37	$27	12	$180,250	$5,150	23,341
Below investment grade bonds												
0-6 months	$ 3,868	$ 71	806	$ 64	$16	16	$14	$11	6	$ 3,946	$ 98	828
7-12 months	1,527	60	256	49	12	11	–	–	–	1,576	72	267
>12 months	1,476	91	312	30	8	5	1	1	25	1,507	100	342
Total	$ 6,871	$ 222	1,374	$143	$36	32	$15	$12	31	$ 7,029	$ 270	1,437
Total bonds												
0-6 months	$122,717	$2,629	15,717	$ 66	$17	17	$46	$34	11	$122,829	$2,680	15,745
7-12 months	39,656	1,540	5,060	50	12	13	–	–	3	39,706	1,552	5,076
>12 months	24,529	1,137	3,907	209	46	21	6	5	29	24,744	1,188	3,957
Total	$186,902	$5,306	24,684	$325	$75	51	$52	$39	43	$187,279	$5,420	24,778
Equity securities												
0-6 months	$ 2,986	$ 105	1,659	$ 50	$13	76	$25	$15	23	$ 3,061	$ 133	1,758
7-12 months	597	42	386	78	23	152	8	5	22	683	70	560
>12 months	22	2	14	4	1	2	–	–	–	26	3	16
Total	$ 3,605	$ 149	2,059	$132	$37	230	$33	$20	45	$ 3,770	$ 206	2,334

(a) For bonds, represents amortized cost.

(b) As more fully described above, upon realization, certain realized losses will be charged to participating policyholder accounts, or realization will result in a current decrease in the amortization of certain deferred policy acquisition costs.

As stated previously, the valuation for AIG's investment portfolio comes from market exchanges or dealer quotations, with the exception of nontraded securities. AIG considers nontraded securities to mean certain fixed income investments, certain structured securities, direct private equities, limited partnerships and hedge funds. The aggregate carrying value of these securities at March 31, 2006 was approximately $65 billion.

The methodology used to estimate fair value of nontraded fixed income investments is by reference to traded securities with similar attributes and using a matrix pricing methodology. This technique takes into account such factors as the industry, the security's rating and tenor, its coupon rate, its position in the capital structure of the issuer, and other relevant factors. The change in fair value is recognized as a component of accumulated other comprehensive income, net of tax.

For certain structured securities, the carrying value is based on an estimate of the security's future cash flows pursuant to the requirements of Emerging Issues Task Force Issue No. 99-20, "Recognition of Interest Income and Impairment on Purchased and Retained Beneficial Interests in Securitized Financial Assets." The change in carrying value is recognized in income.

Hedge funds and limited partnerships in which AIG holds in the aggregate less than a five percent interest are reported at fair value. The change in fair value is recognized as a component of accumulated other comprehensive income, net of tax.

With respect to hedge funds and limited partnerships in which AIG holds in the aggregate a five percent or greater interest, AIG uses the equity method to record these investments. The changes in such net asset values are recorded in income.

AIG obtains the fair value of its investments in limited partnerships and hedge funds from information provided by the general partner or manager of each of these investments, the accounts of which are generally audited on an annual basis.

Each of these investment categories is regularly tested to determine if impairment in value exists. Various valuation

techniques are used with respect to each category in this determination.

Financial Services Operations

AIG's Financial Services subsidiaries engage in diversified activities including aircraft and equipment leasing, capital markets transactions, consumer finance and insurance premium financing. (See also Note 2 of Notes to Consolidated Financial Statements.)

Aircraft Finance

AIG's Aircraft Finance operations represent the operations of ILFC, which generates its revenues primarily from leasing new and used commercial jet aircraft to domestic and foreign airlines. Revenues also result from the remarketing of commercial jets for its own account, and remarketing and fleet management for airlines and financial institutions.

ILFC finances its purchases of aircraft primarily through the issuance of a variety of debt instruments. The composite borrowing rates, which include the effect of economic hedges, at the end of the first three months of 2006 and 2005 were 5.12 percent and 4.49 percent, respectively. (See also the discussions under "Capital Resources" and "Liquidity" herein and Note 2 of Notes to Consolidated Financial Statements.)

ILFC's sources of revenue are principally from scheduled and charter airlines and companies associated with the airline industry. The airline industry is sensitive to changes in economic conditions, cyclical and highly competitive. Airlines and related companies may be affected by political or economic instability, terrorist activities, changes in national policy, competitive pressures on certain air carriers, fuel prices and shortages, labor stoppages, insurance costs, recessions, world health issues and other political or economic events adversely affecting world or regional trading markets. ILFC's revenues and income will be affected by its customers' ability to react and cope with the volatile competitive environment in which they operate, as well as ILFC's own competitive environment.

ILFC is exposed to operating loss and liquidity strain through nonperformance of aircraft lessees, through owning aircraft which it would be unable to sell or re-lease at acceptable rates at lease expiration and, in part, through committing to purchase aircraft which it would be unable to lease.

ILFC manages the risk of nonperformance by its lessees with security deposit requirements, through repossession rights, overhaul requirements, and closely monitoring industry conditions through its marketing force. However, there can be no assurance that ILFC would be able to successfully manage the risks relating to the effect of possible future deterioration in the airline industry. Approximately 90 percent of ILFC's fleet is leased to non-U.S. carriers, and the fleet, comprised of the most efficient aircraft in the airline industry, continues to be in high demand from such carriers.

ILFC typically contracts to re-lease aircraft before the end of the existing lease term. For aircraft returned before the end of the lease term, ILFC has generally been able to re-lease such aircraft within two to six months of its return. As a lessor, ILFC considers an aircraft "idle" or "off lease" when the aircraft is not subject to a signed lease agreement or signed letter of intent. ILFC had no aircraft off lease at March 31, 2006, and all new aircraft deliveries in 2006 have been leased. (See also the discussions under "Capital Resources" and "Liquidity" herein.)

Management formally reviews regularly, and no less frequently than quarterly, issues affecting ILFC's fleet, including events and circumstances that may cause impairment of aircraft values. Management evaluates aircraft in the fleet as necessary, based on these events and circumstances in accordance with Statement of Financial Accounting Standards No. 144, "Accounting for the Impairment or Disposal of Long-Lived Assets" (FAS 144). ILFC has not recognized any impairment related to its fleet. ILFC has been able to re-lease the aircraft without diminution in lease rates to an extent that would require an impairment write-down. (See also the discussions under "Liquidity" herein.)

Capital Markets

Capital Markets represents the operations of AIGFP, which engages as principal in a wide variety of financial transactions, including standard and customized financial products involving commodities, credit, currencies, energy, equities and rates. AIGFP also invests in a diversified portfolio of securities and engages in borrowing activities involving issuing standard and structured notes and other securities, and entering into guaranteed investment agreements.

As Capital Markets is a transaction-oriented operation, current and past revenues and operating results may not provide a basis for predicting future performance. Also, AIG's Capital Markets operations may be adversely affected by the downgrades in AIG's credit ratings. See Item 1A. in Part II of this Quarterly Report, for a further discussion of the potential effect of the rating downgrades on AIG's Capital Markets businesses herein.

AIG's Capital Markets operations derive substantially all their revenues from hedged financial positions entered in connection with counterparty transactions rather than from speculative transactions. AIGFP participates as a dealer in a wide variety of financial derivatives transactions.

As a dealer in financial derivatives, AIGFP marks all derivative and trading transactions to fair value daily. Thus, a gain or loss on each transaction is recognized daily. Under GAAP, in certain instances, gains and losses are required to be recorded in earnings immediately, whereas in other in-

stances, they are required to be recognized over the life of the underlying instruments. AIGFP economically hedges the market risks arising from its transactions, although hedge accounting is not currently being applied to any of the derivatives and related assets and liabilities. Accordingly, revenues and operating income are exposed to volatility resulting from differences in the timing of revenue recognition between the derivatives and the hedged assets and liabilities. Revenues and operating income of the Capital Markets operations and the percentage change in these amounts for any given period are also significantly affected by the number, size and profitability of transactions entered into by these subsidiaries during that period relative to those entered into during the prior period. Generally, the realization of transaction revenues as measured by the receipt of funds is not a significant reporting event as the gain or loss on AIGFP's trading transactions is currently reflected in operating income as the fair values change from period to period.

Derivative transactions are entered into in the ordinary course of Capital Markets operations. Therefore, income on derivatives is recorded at fair value, determined by reference to the mark to market value of the derivative or their estimated fair value where market prices are not readily available. The resulting aggregate unrealized gains or losses from the derivative are reflected in the income statement. Where Capital Markets cannot verify significant model inputs to observable market data and verify the model value to market transactions, Capital Markets values the contract at the transaction price at inception and, consequently, records no initial gain or loss in accordance with Emerging Issues Task Force Issue No. 02-03, "Issues Involved in Accounting for Derivative Contracts Held for Trading Purposes and Contracts Involved in Energy Trading and Risk Management Activities" (EITF 02-03). Such initial gain or loss is recognized over the life of the transaction. Capital Markets periodically reevaluates its revenue recognition under EITF 02-03 based on the observability of market parameters. The mark to fair value of derivative transactions is reflected in the balance sheet in the captions "Unrealized gain on swaps, options and forward transactions," "Unrealized loss on swaps, options and forward transactions," "Trading assets" and "Trading liabilities." Unrealized gains represent the present value of the aggregate of each net receivable by counterparty, and the unrealized losses represent the present value of the aggregate of each net payable by counterparty as of March 31, 2006. These amounts will change from one period to the next due to changes in interest rates, currency rates, equity and commodity prices and other market variables, as well as cash movements, execution of new transactions and the maturing of existing transactions. (See also the discussion under "Derivatives" herein.)

Spread income on investments and borrowings is recorded on an accrual basis over the life of the transaction. Investments are classified as securities available for sale and are marked to market with the resulting unrealized gains or losses reflected in accumulated other comprehensive income. U.S. dollar denominated borrowings are carried at cost, while borrowings in any currency other than the U.S. dollar result in unrealized foreign exchange gains or losses reported in income. AIGFP hedges the economic exposure on its investments and borrowings on a portfolio basis using derivatives and other financial instruments. While these hedges are highly effective economic hedges, the requirements under FAS 133 hedge accounting were not met. The change in the fair value of the derivatives used to hedge these economic exposures is therefore included in other revenues while the offsetting change in fair value of the hedged items is not recognized in earnings.

Consumer Finance

Domestically, AIG's Consumer Finance operations are principally conducted through American General Finance, Inc. (AGF). AGF derives a substantial portion of its revenues from finance charges assessed on outstanding real estate loans, secured and unsecured non-real estate loans and retail sales finance receivables. The real estate loans include first or second mortgages on residential real estate generally having a maximum term of 360 months, and are considered non-conforming. These loans may be closed-end accounts or open-end home equity lines of credit and may be fixed-rate or adjustable rate products. The non-real estate loans are secured by consumer goods, automobiles, or other personal property or are unsecured. Both secured and unsecured non-real estate loans generally have a maximum term of 60 months. The core of AGF's originations is sourced through its branches. However, a significant volume of real estate loans is also originated through broker relationships, and to lesser extents, through correspondent relationships and direct mail solicitations. In the first three months of 2006, two wholly-owned subsidiaries of AGF discontinued originating real estate loans through an arrangement with AIG Bank and began originating such loans under their own state licenses.

Many of AGF's borrowers are non-prime or sub-prime. Current economic conditions, such as interest rate and employment, have a direct effect on the borrowers' ability to repay these loans. AGF manages the credit risk inherent in its portfolio by using credit scoring models at the time of credit applications, established underwriting criteria, and in certain cases, individual loan reviews. AGF's Credit Strategy and Policy Committee monitors the quality of the finance receivables portfolio on a monthly basis when determining the appropriate level of the allowance for losses. The Credit Strategy and Policy Committee bases its conclusions on quantitative analyses, qualitative factors, current economic conditions and trends, and each committee member's experience in the consumer finance industry. Through the first three months of 2006, the credit quality of AGF's finance receivables continues to be strong. However, declines in the

strength of the U.S. housing market or economy may adversely affect the future credit quality of these receivables.

Internationally, AIG's Consumer Finance operations are principally conducted through AIG Consumer Finance Group (CFG). CFG operates primarily in emerging and developing markets. CFG has operations in Hong Kong, Taiwan, the Philippines, Thailand, Poland, Argentina, and Mexico. While products vary by market, the businesses generally provide credit cards, unsecured and secured non-real estate loans, term deposits, savings accounts, retail sales finance and real estate loans.

Consumer Finance operations are exposed to loss when contractual payments are not received. Credit loss exposure is managed through underwriting controls, mix of finance receivables, collateral and collection efficiency.

CFG monitors the quality of its finance receivable portfolio through a combination of a monthly Credit Review and quarterly Credit Reserve Committee review when determining the appropriate level of the allowance for losses. The Credit Reserve Committee bases its conclusions on quantitative analysis, qualitative factors, current economic conditions and trends, political and regulatory implications, competition, and the judgment of the committee's members. As a result of such a review and in light of industry-wide deteriorating credit conditions and tightening of overall consumer credit, the aggregate allowance for losses in AIG Credit Card Company (Taiwan) was increased by $88 million pre-tax to approximately $130 million, CFG's best estimate of the overall exposure at March 31, 2006. The allowance, which represents approximately 20 percent of CFG's outstanding credit card receivables for Taiwan at that date, was shared equally by the Financial Services and Life Insurance & Retirement Services segments.

Financial Services operations for the three months ended March 31, 2006 and 2005 were as follows:

(in millions)	**2006**	2005
Revenues[(a)]:		
Aircraft Finance[(b)]	**$ 965**	$ 827
Capital Markets[(c)(d)]	**(300)**	756
Consumer Finance[(e)]	**924**	833
Other	**26**	20
Total	**$1,615**	$2,436
Operating income (loss)[(a)]:		
Aircraft Finance	**$ 129**	$ 187
Capital Markets[(d)]	**(470)**	620
Consumer Finance[(f)]	**175**	221
Other, including intercompany adjustments	**7**	17
Total	**$ (159)**	$1,045

(a) Includes the effect of hedging activities that do not qualify for hedge accounting treatment under FAS 133, including the related foreign exchange gains and losses. For the first three months of 2006 and 2005, the effect was $0 and $15 million, respectively, in operating income for Aircraft Finance and $(678) million and $468 million in both revenues and operating income for Capital Markets. These amounts result primarily from interest rate and foreign currency derivatives hedging available for sale securities and borrowings.

(b) Revenues are primarily from ILFC aircraft lease rentals.

(c) Revenues, shown net of interest expense, are primarily from hedged financial positions entered into in connection with counterparty transactions and the effect of hedging activities that do not qualify for hedge accounting treatment under FAS 133 described in (a) above.

(d) Certain transactions entered into by AIGFP generate tax credits and benefits which are included in income taxes in the consolidated statement of income. The amount of such tax credits and benefits for the first three months of 2006 and 2005 are $18 million, and $19 million, respectively.

(e) Revenues are primarily finance charges.

(f) Includes $44 million in additional allowance for losses from AIG Credit Card Company (Taiwan) in 2006.

Financial Services Results

Financial Services operating income decreased in the first three months of 2006 compared to the same period of 2005 due to the effect of hedging activities that do not qualify for hedge accounting under FAS 133.

Fluctuations in revenues and operating income from quarter to quarter are not unusual because of the transaction-oriented nature of Capital Markets operations and the volatility resulting from the accounting treatment for the economic hedges under FAS 133. The overwhelming majority of AIG's financial derivatives are conducted by the Capital Markets operations. Capital Markets enters into derivative transactions to hedge the interest rate and foreign currency exposures associated with its available for sale assets and borrowings. While the derivatives entered into to hedge its outstanding transactions and positions are highly effective economic hedges, AIG did not meet the requirements for hedge accounting under FAS 133. The change in the fair value of these derivatives is included in other revenues while the offsetting change in fair value of the hedged items is not recognized in earnings.

The effect of the Capital Markets' derivatives not qualifying for hedge accounting on revenues and operating income in the first three months of 2006 and 2005 was $(678) million and $468 million, respectively. The majority of the net loss on AIGFP's derivatives recognized in the first three months of 2006 was due to the rise in long-term U.S. interest rates, which resulted in a decrease in the fair value of its interest rate derivatives hedging its borrowings. To a lesser extent, the net loss was also due to slight weakening in the U.S. dollar against other currencies resulting in a decrease in the fair value of the foreign currency derivatives hedging AIGFP's available for sale securities. The majority of the net gain on AIGFP's derivatives in the first three months of 2005 was due to the strengthening of the U.S. dollar against the Euro, which increased the fair value of the foreign currency derivatives hedging available for sale securities. Long-term rates remained relatively flat in the first three months of 2005, thus having minimal effect on the fair value of the derivatives hedging AIGFP's borrowings.

To the extent the Financial Services subsidiaries, other than AIGFP, use derivatives to economically hedge their assets or liabilities with respect to their future cash flows, and such hedges do not qualify for hedge accounting treatment under FAS 133, the changes in fair value of such derivatives are recorded in realized capital gains (losses) or other revenues.

Financial market conditions in the first three months of 2006 continued to be characterized by a general flattening of interest rate yield curves across fixed income markets globally, tightening of credit spreads and equity valuations that were slightly higher. The decline in Capital Markets operating results for the first three months of 2006 was principally due to losses on derivatives not qualifying for hedge accounting under FAS 133, which was partially offset by improved transaction flow in AIGFP's credit, commodity index and equity products.

The most significant component of Capital Markets operating expenses is compensation, which was approximately $136 million and $111 million in the first three months of 2006 and 2005, respectively. The amount of compensation was not affected by gains and losses not qualifying for hedge accounting treatment under FAS 133.

As a result of AIG's early adoption of FAS 155, AIGFP elected to apply the fair value option to certain of its structured notes and other financial liabilities containing embedded derivatives outstanding as of January 1, 2006. The cumulative effect from the adoption of FAS 155 on these instruments at January 1, 2006 was a loss of approximately $29 million pre-tax. The application of the fair value option to these hybrid financial instruments did not have a significant effect on AIGFP's operating income for the three months ended March 31, 2006.

ILFC's operating income decreased in the first three months of 2006 compared to the same period of 2005 as improvements in sales environment and increased lease revenues were offset by increased borrowing costs and certain adjustments for credit and tax reserves and lease-related accruals. ILFC's revenues increased in the first three months of 2006 compared to the same period of 2005 as a result of growth in the number of aircraft in ILFC's fleet, continued net improvements in lease rates and an increase in overhaul revenue.

Consumer Finance's operating income decreased in the first three months of 2006 compared to the same period of 2005 primarily due to the increase in borrowing costs and increases in the allowance for losses related to industry-wide credit deterioration in the Taiwan credit card market, which is going through credit tightening and uncertain regulatory developments.

Domestically, the relatively low interest rate environment throughout 2005 and the first three months of 2006 contributed to a high level of mortgage refinancing activity. AGF's average net finance receivables increased 14 percent in the first three months of 2006 when compared to the same period in 2005. However, net originations and purchases of finance receivables in AGF's centralized real estate business segment decreased in the first three months of 2006 as compared to the same period in 2005 primarily caused by a less robust U.S. housing market. The increase in AGF's revenues that principally resulted from portfolio growth was offset by higher interest expense and depressed whole loan sale prices resulting from a flattened yield curve. Both short-term and long-term market interest rates continued to increase significantly over the past year. AGF's short-term and long-term borrowing costs were 4.59 percent and 4.84 percent in the first three months of 2006, respectively, compared to 3.03 percent and 4.34 percent in the same period in 2005, respectively. Despite high energy costs, the U.S. economy continued to expand during the first three months of 2006, improving consumer credit quality. AGF's charge-off ratio improved 37 basis points in the first three months of 2006 when compared to the same period in 2005. AGF's delinquency ratio at March 31, 2006 improved 24 basis points when compared to March 31, 2005. At March 31, 2006, AGF's allowance ratio was 2.10 percent compared to 2.12 percent at March 31, 2005.

Financial Services Invested Assets

The following table is a summary of the composition of AIG's Financial Services invested assets at March 31, 2006 and December 31, 2005. (See also the discussions under "Operating Review: Financial Services Operations," "Capital Resources" and "Derivatives" herein.)

	2006		2005	
(dollars in millions)	**Invested Assets**	**Percent of Total**	Invested Assets	Percent of Total
Fixed maturities:				
Bonds available for sale, at market value	**$ 1,313**	**0.9%**	$ 1,307	0.9%
Equity securities:				
Preferred stocks available for sale, at market value	**9**	**–**	10	–
Mortgage loans on real estate, net of allowance	**65**	**–**	71	–
Policy loans	**2**	**–**	2	–
Collateral and guaranteed loans, net of allowance	**2,202**	**1.5**	1,719	1.2
Financial services assets:				
Flight equipment primarily under operating leases, net of accumulated depreciation	**37,580**	**25.2**	36,245	24.1
Securities available for sale, at market value	**38,225**	**25.6**	37,511	24.9
Trading securities, at market value	**6,350**	**4.3**	6,499	4.3
Spot commodities	**230**	**0.2**	92	0.1
Unrealized gain on swaps, options and forward transactions	**17,792**	**11.9**	18,695	12.4
Trading assets	**1,411**	**0.9**	1,204	0.8
Securities purchased under agreements to resell, at contract value	**12,297**	**8.2**	14,519	9.7
Finance receivables, net of allowance	**27,219**	**18.2**	27,995	18.6
Securities lending collateral, at market value	**60**	**–**	–	–
Other invested assets	**2,953**	**2.0**	2,751	1.9
Short-term investments, at cost	**1,293**	**0.9**	1,382	0.9
Cash	**282**	**0.2**	331	0.2
Investment income due and accrued	**19**	**–**	18	–
Real estate, net of accumulated depreciation	**24**	**–**	24	–
Total	**$149,326**	**100.0%**	$150,375	100.0%

As previously discussed, the cash used for the purchase of flight equipment is derived primarily from the proceeds of ILFC's debt financings. The primary sources for the repayment of this debt and the interest expense thereon are the cash flow from operations, proceeds from the sale of flight equipment and the rollover and refinancing of the prior debt. During the first three months of 2006, ILFC acquired flight equipment costing $1.90 billion. (See also the discussion under "Operating Review: Financial Services Operations" and "Capital Resources" herein.)

At March 31, 2006, ILFC had committed to purchase 308 new and used aircraft deliverable from 2006 through 2015 at an estimated aggregate purchase price of $21.4 billion and had options to purchase 16 new aircraft at an estimated aggregate purchase price of $1.5 billion. As of March 31, 2006, ILFC has entered into leases for all of the new aircraft to be delivered in 2006. ILFC will be required to find customers for any aircraft currently on order and any aircraft to be ordered, and it must arrange financing for portions of the purchase price of such equipment. ILFC has been successful to date both in placing its new aircraft on lease or under sales contract and obtaining adequate financing, but there can be no assurance that such success will continue in future environments.

AIG's Consumer Finance operations provide a wide variety of consumer finance products, including real estate loans, credit card loans, non-real estate loans, retail sales finance and credit-related insurance to customers both domestically and overseas, particularly in emerging markets. These products are funded through a combination of deposits and various borrowings including commercial paper and medium term notes. AIG's Consumer Finance operations are exposed to credit risk and risk of loss resulting from adverse fluctuations in interest rates. Over half of the finance receivable balance is related to real estate loans which are substantially collateralized by the related properties.

With respect to credit losses, the allowance for losses is maintained at a level considered adequate to absorb anticipated credit losses existing in that portfolio.

Capital Markets derivative transactions are carried at market value or at estimated fair value when market prices are not readily available. AIGFP reduces its economic risk exposure through similarly valued offsetting transactions including swaps, trading securities, options, forwards and futures. The estimated fair values of these transactions represent assessments of the present value of expected future cash flows. These transactions are exposed to liquidity risk if AIGFP were required to sell or close out the transactions

prior to maturity. AIG believes that the effect of any such event would not be significant to AIG's financial condition or its overall liquidity. (See also the discussion under "Operating Review: Financial Services Operations" and "Derivatives" herein.)

AIGFP uses the proceeds from the issuance of notes and bonds and borrowings under guaranteed investment agreements (GIAs) to invest in a diversified portfolio of securities, including securities available for sale, at market, and derivative transactions. The funds may also be temporarily invested in securities purchased under agreements to resell. The proceeds from the disposal of the aforementioned securities available for sale and securities purchased under agreements to resell have been used to fund the maturing GIAs or other AIGFP financings, or invest in new assets. (See also the discussion under "Capital Resources" herein.)

Securities available for sale is predominantly a portfolio of fixed income securities, where the individual securities have varying degrees of credit risk. At March 31, 2006, the average credit rating of this portfolio was AA+ or the equivalent thereto as determined through rating agencies or internal review. AIGFP has also entered into credit derivative transactions to economically hedge its credit risk associated with $105 million of these securities. Securities deemed below investment grade at March 31, 2006 amounted to approximately $154 million in fair value representing 0.3 percent of the total AIGFP securities available for sale. There have been no significant downgrades through March 31, 2006. If its securities available for sale portfolio were to suffer significant default and the collateral held declined significantly in value with no replacement or the credit default swap counterparty failed to perform, AIGFP could have a liquidity strain. AIG guarantees AIGFP's payment obligations, including its debt obligations.

AIGFP's risk management objective is to minimize interest rate, currency, commodity and equity risks associated with its securities available for sale. That is, when AIGFP purchases a security for its securities available for sale investment portfolio, it simultaneously enters into an offsetting internal hedge such that the payment terms of the hedging transaction offset the payment terms of the investment security, which achieves the economic result of converting the return on the underlying security to U.S. dollar LIBOR plus or minus a spread based on the underlying profit on each security on the initial trade date. The market risk associated with such internal hedges is managed on a portfolio basis, with third-party hedging transactions executed as necessary. As hedge accounting treatment is not achieved in accordance with FAS 133, the unrealized gains and losses on the securities related economic hedges are reflected in operating income, whereas the unrealized gains and losses on the underlying securities resulting from changes in interest rates, currency rates, commodity and equity prices, are recorded in accumulated other comprehensive income. When a security is sold, the related hedging transaction is terminated, and the realized gain or loss with respect to this security is then recorded in operating income.

Securities purchased under agreements to resell are treated as collateralized financing transactions. AIGFP takes possession of or obtains a security interest in securities purchased under agreements to resell. AIGFP further minimizes its credit risk by monitoring counterparty credit exposure and, when it deems necessary, it requires additional collateral to be deposited.

AIGFP owns inventories in certain commodities in which it trades, and may reduce the exposure to market risk through the use of swaps, forwards, futures and option contracts. Physical commodities held in AIGFP's wholly-owned broker dealer subsidiary are recorded at market value. All other commodities are recorded at the lower of cost or market.

Trading securities, at market value, and securities and spot commodities sold but not yet purchased, at market value are marked to market daily with the unrealized gain or loss being recognized in income at that time. These trading securities are held to meet the short-term risk management objectives of Capital Markets operations.

The gross unrealized gains and gross unrealized losses of Capital Markets operations included in the financial services assets and liabilities at March 31, 2006 were as follows:

(in millions)	Gross Unrealized Gains	Gross Unrealized Losses
Securities available for sale, at market value	$ 1,193	$ 1,414
Unrealized gain/loss on swaps, options and forward transactions *	17,792	11,267

** These amounts are also presented as the respective balance sheet amounts.*

The senior management of AIG defines the policies and establishes general operating parameters for Capital Markets operations. AIG's senior management has established various oversight committees to review the various financial market, operational and credit issues of the Capital Markets operations. The senior management of AIGFP reports the results of its operations to and reviews future strategies with AIG's senior management.

AIG actively manages the exposures to limit potential losses, while maximizing the rewards afforded by these business opportunities. In doing so, AIG must continually manage a variety of exposures including credit, market, liquidity, operational and legal risks.

Asset Management Operations

AIG's Asset Management operations comprise a wide variety of investment-related services and investment products including institutional and retail asset management, broker dealer services and spread-based investment business from

the sale of guaranteed investment contracts, also known as funding agreements (GICs). Such services and products are offered to individuals and institutions both domestically and overseas.

Asset Management revenues and operating income for the three months ended March 31, 2006 and 2005 were as follows:

(in millions)	**2006**	2005
Revenues:		
Guaranteed investment contracts	**$ 822**	$ 896
Institutional Asset Management	**279**	319
Brokerage Services and Mutual Funds	**73**	63
Other	**65**	99
Total	**$1,239**	$1,377
Operating income:		
Guaranteed investment contracts[(a)]	**$ 218**	$ 319
Institutional Asset Management[(b)(c)]	**159**	161
Brokerage Services and Mutual Funds	**23**	13
Other	**61**	97
Total	**$ 461**	$ 590

(a) The effect of hedging activities that do not qualify for hedge accounting treatment under FAS 133 was $0 and $62 million for the first three months of 2006 and 2005, respectively.

(b) Includes the full results of certain AIG managed private equity and real estate funds that are consolidated effective December 31, 2003 pursuant to FIN46R, "Consolidation of Variable Interest Entities". For the first three months of 2006 and 2005, operating income includes $27 million and $75 million of third-party limited partner earnings offset in minority interest expense.

(c) Includes the full results of certain AIG managed partnerships that are consolidated effective January 1, 2006 pursuant to EITF 04-5, "Determining Whether a General Partner, or the General Partners as a Group, Controls a Limited Partnership or Similar Entity When the Limited Partners Have Certain Rights". For the first three months of 2006, operating income includes $69 million of third-party limited partner earnings offset in minority interest expense.

Asset Management Results

Asset Management operating income decreased in the first three months of 2006 compared to the same period of 2005 as a result of the continued run-off of AIG's GIC portfolio combined with spread compression. In addition, there was a decline in realized gains on sales of real estate investments and performance fees earned on various private equity investments. The revenues and operating income with respect to the segment are largely affected by the general conditions in the equity and credit markets. The decrease for the quarter was primarily due to the decline in the GIC business. GICs were sold domestically and abroad to both institutions and individuals. These products were written on an opportunistic basis when the market conditions were favorable. A significant portion of the remaining GIC portfolio consists of floating rate obligations. AIG has entered into hedges to manage against increases in short-term interest rates. AIG continues to believe these hedges are economically effective but do not qualify for hedge accounting under FAS 133. As a result, continued increases in short-term interest rates will negatively affect operating income in the segment. Realized capital gains from the hedges offset the negative trend in operating income. GIC revenues include income from Sun America partnerships supporting the GIC line of business and are significantly affected by performance in the equity markets. Thus, revenues, operating income and cash flow attributable to GICs will vary among reporting periods. The decline in GIC operating income in the first three months of 2006 compared to the same period of 2005 reflects tighter spreads in the GIC portfolio, partially offset by improved net partnership returns. Spread compression has occurred as the base portfolio yield declined primarily due to an increase in the cost of funds in the short-term floating rate portion of the GIC portfolio, only partially offset by increased investment income from the floating rate assets backing the portfolio. As mentioned above, the lower level of gains and performance based fees also contributed to the decline in operating income for the first three months of 2006. These gains and performance fees are contingent upon various fund closings, maturity levels and market conditions, and by their nature, are not predictable. Therefore, the effect on the segment's earnings may vary from period to period.

In September 2005, AIG launched a $10 billion medium term note program in the Euromarkets under which AIG debt securities are issued primarily for a matched investment program. AIG issued its first debt securities under the matched investment program in April 2006, selling Euro 500 million principal amount of notes. AIG also expects to launch a matched investment program in the domestic market which, along with the Euro program, will become AIG's principal spread-based investment activity. However, the timing of the launch of the domestic program remains uncertain. Because AIG's credit spreads in the capital markets have widened following the ratings declines, there may be a reduction in the earnings on new business in AIG's institutional spread based funding business.

Asset Management operating income represented 10 percent of AIG's consolidated income before income taxes, minority interest and cumulative effect of an accounting change in the first three months of 2006. This compares to 10 percent in the same period of 2005.

At March 31, 2006 and 2005, AIG's third party assets under management, including both retail mutual funds and institutional accounts, exceeded $65 billion and $55 billion and the aggregate GIC reserve was $48.1 billion and $55.8 billion, respectively.

Other Operations

Other operations include AIG's equity in certain partially owned companies, the distributions on the liabilities connected to trust preferred stock, as well as the unallocated corporate expenses of the parent holding company and other miscellaneous income and expenses. Other income (loss) amounted to $(338) million and $36 million in the first three

months of 2006 and 2005, respectively. Included in the 2006 amount is compensation expense related to the 2006 Starr tender offer of $54 million. See also Note 4 of Notes to the Consolidated Financial Statements. In addition, included in the 2006 amount is compensation expense with respect to the SICO Plans of $76 million, including various adjustments totalling $61 million, primarily relating to stock-split adjustments and other miscellaneous items. See also Note 4 of Notes to the Consolidated Financial Statements.

Other realized capital gains (losses), amounted to $(57) million and $155 million for the three months ended March 31, 2006 and 2005, respectively.

Capital Resources

At March 31, 2006, AIG had total consolidated shareholders' equity of $88.39 billion and total consolidated borrowings of $118.8 billion. At that date, $104.1 billion of such borrowings were either not guaranteed by AIG or were AIGFP's matched borrowings under obligations of GIAs, liabilities connected to trust preferred stock, or matched notes and bonds payable.

Borrowings

At March 31, 2006, AIG's net borrowings were $14.67 billion after reflecting amounts that were matched borrowings under AIGFP's obligations of GIAs, matched notes and bonds payable, amounts not guaranteed by AIG and liabilities connected to trust preferred stock. The following table summarizes borrowings outstanding at March 31, 2006 and December 31, 2005:

(in millions)	**2006**	2005
AIG's net borrowings	**$ 14,665**	$ 10,425
Liabilities connected to trust preferred stock	**1,390**	1,391
AIGFP		
GIAs	**21,600**	20,811
Matched notes and bonds payable	**25,874**	24,950
Borrowings not guaranteed by AIG	**55,252**	52,272
Total	**$118,781**	$ 109,849

Borrowings issued or guaranteed by AIG and those borrowings not guaranteed by AIG at March 31, 2006 and December 31, 2005 were as follows:

(in millions)	**2006**	2005
AIG borrowings:		
Medium term notes	**$ 89**	$ 112
Notes and bonds payable	**4,498**	4,495
Loans and mortgages payable	**2,008**	814
Total	**6,595**	5,421
Borrowings guaranteed by AIG:		
AIGFP		
GIAs	**21,600**	20,811
Notes and bonds payable	**21,949**	26,463
Hybrid financial instrument liabilities	**6,109**	—
Total	**49,658**	47,274
AIG Funding, Inc. commercial paper	**5,089**	2,694
AGC Notes and bonds payable	**797**	797
Liabilities connected to trust preferred stock	**1,390**	1,391
Total borrowings issued or guaranteed by AIG	**63,529**	57,577
Borrowings not guaranteed by AIG:		
ILFC		
Commercial paper	**2,917**	2,615
Medium term notes	**5,157**	4,689
Notes and bonds payable*	**19,451**	19,026
Total	**27,525**	26,330
AGF		
Commercial paper	**4,209**	3,423
Medium term notes	**16,866**	17,736
Notes and bonds payable	**1,692**	983
Total	**22,767**	22,142
Commercial paper:		
AIG Credit Card Company (Taiwan)	**373**	476
AIG Finance (Taiwan) Limited	**1**	–
Total	**374**	476
Loans and mortgages payable:		
AIGCFG	**967**	864
AIG Finance (Hong Kong) Limited	**204**	183
Total	**1,171**	1,047
Other Subsidiaries	**935**	927
Variable Interest Entity debt:		
A.I. Credit	**876**	–
AIG Global Investment Group	**140**	140
AIG Global Real Estate Investment	**1,222**	977
AIG SunAmerica	**242**	233
Total	**2,480**	1,350
Total borrowings not guaranteed by AIG	**55,252**	52,272
Total Debt	**$118,781**	$109,849

** Includes borrowings under Export Credit Facility of $2.8 billion and $2.6 billion, at March 31, 2006 and December 31, 2005, respectively.*

AIG intends to continue its customary practice of issuing debt securities from time to time to meet its financing needs and those of certain of its subsidiaries for general corporate purposes, as well as for a matched investment program.

On April 20, 2006, AIG sold $1.0 billion principal amount of notes in a Rule 144A/Regulation S offering bearing interest at a rate of 6.250 percent per annum and maturing in 2036. On September 30, 2005, AIG sold $1.5 billion principal amount of notes in a Rule 144A/Regulation S offering, $500 million of which bear interest at a rate of 4.700 percent per annum and mature in 2010 and $1.0 billion of which bear interest at a rate of 5.05 percent per annum and mature in 2015. These notes are senior unsecured obligations of AIG and rank equally with all of AIG's other senior debt outstanding. AIG has agreed to use commercially reasonable efforts to consummate an exchange offer for these notes by having declared effective a registration statement for the September 2005 and April 2006 notes within 360 days and 240 days, respectively, of the date on which the notes were issued.

On April 26, 2006, AIG completed its first offering of debt securities under its European medium term note program, selling Euro 750 million principal amount of notes bearing interest at a rate of 4.375 percent and maturing in 2016, Euro 500 million principal amount of floating rate notes maturing in 2011, and British Pound Sterling 500 million principal amount of notes bearing interest at a rate of 5.000 percent and maturing in 2023.

Except for the Euro 500 million principal amount of floating rate notes, the proceeds of which were used to fund the matched investment program, the proceeds from each issuance of 144A/Regulation S notes and European medium term notes were used for general corporate purposes, including the repayment of commercial paper.

In March 2006, AIG borrowed a total of $1.3 billion on an unsecured basis pursuant to loan agreements with third-party banks, $500 million of which matures in February 2007 but can be extended by AIG for an additional seven-month period and $800 million of which matures in March 2007. In September 2005, AIG borrowed a total of $600 million on an unsecured basis pursuant to loan agreements with third-party banks, $500 million of which matures in August 2006 but can be extended by AIG for an additional seven-month period and $100 million of which matures in September 2006.

AIGFP uses the proceeds from the issuance of notes and bonds and GIA borrowings to invest in a diversified portfolio of securities and derivative transactions. The borrowings may also be temporarily invested in securities purchased under agreements to resell. AIG guarantees the obligations of AIGFP under AIGFP's structured notes and bonds and GIA borrowings. Certain of AIGFP's notes contain embedded derivatives that are required to be accounted for separately under FAS 133. Upon AIG's early adoption of FAS 155, AIGFP has elected the fair value option for these instruments. Those notes that are accounted for using the fair value option are reported separately under hybrid financial instrument liabilities. (See also the discussions under "Operating Review: Financial Services Operations," "Liquidity" and "Derivatives" herein.)

AIGFP has a Euro Medium Term Note Program under which an aggregate nominal amount of up to $10.0 billion of notes may be outstanding at any one time. The Program provides that additional notes may be issued to replace matured or redeemed notes. As of March 31, 2006, $8.85 billion of notes had been issued under the program, $3.50 billion of which were outstanding including $317 million resulting from foreign exchange translation into U.S. dollars. Notes issued under this program are included in Notes and Bonds Payable in the preceding table of borrowings.

AIG Funding, Inc. (AIG Funding), through the issuance of commercial paper, helps fulfill the short-term cash requirements of AIG and its subsidiaries. AIG Funding intends to continue to meet AIG's funding requirements through the issuance of commercial paper guaranteed by AIG. The issuance of AIG Funding's commercial paper is subject to the approval of AIG's Board of Directors.

AIG and AIG Funding are parties to unsecured syndicated revolving credit facilities aggregating $2.75 billion, consisting of $1.375 billion in a 364-day revolving credit facility that expires in July of 2006 and $1.375 billion in a five-year revolving credit facility that expires in July of 2010. The 364-day facility allows for the conversion by AIG of any outstanding loans at expiration into one-year term loans. The facilities can be used for general corporate purposes and also to provide backup for AIG's commercial paper programs administered by AIG Funding. AIG expects to replace or extend these credit facilities on or prior to their expiration. There are currently no borrowings outstanding under these facilities, nor were any borrowings outstanding as of March 31, 2006.

In November 2005, AIG and AIG Funding entered into a 364-day revolving credit facility for an aggregate amount of $3 billion, which can be drawn in the form of loans or letters of credit. The credit facility expires in November 2006 but allows for the issuance of letters of credit with terms of up to ten years and provides for the conversion by AIG of any outstanding loans at expiration into one-year term loans. The facility can be used for general corporate purposes, including providing backup for AIG's commercial paper programs administered by AIG Funding and obtaining letters of credit to secure obligations under insurance and reinsurance transactions. There are currently no loans outstanding under the facility, nor were any loans outstanding as of March 31, 2006. As of such dates, $1.01 billion was available to be drawn under the facility, with the remainder having been drawn in the form of letters of credit.

AIG is also a party to an unsecured 364-day inter-company revolving credit facility provided by certain of its subsidiaries aggregating $2 billion that expires in October of 2006. The facility allows for the conversion of any outstanding loans at expiration into one-year term loans. The facility can be used for general corporate purposes and also to pro-

vide backup for AIG's commercial paper programs. AIG expects to replace or extend this credit facility on or prior to its expiration. There are currently no borrowings outstanding under the inter-company facility, nor were any borrowings outstanding as of March 31, 2006.

ILFC fulfills its short term cash requirements through the issuance of commercial paper. The issuance of commercial paper is subject to the approval of ILFC's Board of Directors and is not guaranteed by AIG. ILFC is a party to unsecured syndicated revolving credit facilities aggregating $6.0 billion at March 31, 2006. The facilities can be used for general corporate purposes and also to provide backup for ILFC's commercial paper program. They consist of $2.0 billion in a 364-day revolving credit facility that expires in October 2006, with a one-year term out option, $2.0 billion in a five-year revolving credit facility that expires in October 2009 and $2.0 billion in a five-year revolving credit facility that expires in October 2010. ILFC expects to replace or extend these credit facilities on or prior to their expiration. There are currently no borrowings under these facilities, nor were any borrowings outstanding as of March 31, 2006.

At March 31, 2006, ILFC had increased the aggregate principal amount outstanding of its medium term and long-term notes. The foreign exchange adjustment for the foreign currency denominated debt was $328 million at March 31, 2006 and $197 million at December 31, 2005. ILFC had $13.13 billion of debt securities registered for public sale at March 31, 2006. As of March 31, 2006, $9.96 billion of debt securities were issued. In addition, ILFC has a Euro Medium Term Note Program for $7.0 billion, under which $4.98 billion in notes were sold through March 31, 2006. ILFC has substantially eliminated the currency exposure arising from foreign currency denominated notes by economically hedging the portion of the note exposure not already offset by Euro denominated operating lease payments, although such hedges do not qualify for hedge accounting treatment under FAS 133. Notes issued under the Euro Medium Term Note program are included in Notes and Bonds Payable in the preceding table of borrowings.

ILFC had a $4.3 billion Export Credit Facility for use in connection with the purchase of approximately 75 aircraft delivered through 2001. This facility was guaranteed by various European Export Credit Agencies. The interest rate varies from 5.75 percent to 5.90 percent on these amortizing ten-year borrowings depending on the delivery date of the aircraft. At March 31, 2006, ILFC had $1.2 billion outstanding under this facility. The debt is collateralized by a pledge of the shares of a subsidiary of ILFC, which holds title to the aircraft financed under the facility.

In May 2004, ILFC entered into a similarly structured Export Credit Facility for up to a maximum of $2.64 billion for Airbus aircraft to be delivered through May 31, 2005. The facility has since been extended to include aircraft to be delivered through May 31, 2006. The facility becomes available as the various European Export Credit Agencies provide their guarantees for aircraft based on a six-month forward-looking calendar, and the interest rate is determined through a bid process. At March 31, 2006, ILFC had $1.6 billion outstanding under this facility. Borrowings with respect to these facilities are included in Notes and Bonds Payable in the preceding table of borrowings.

In August 2004, ILFC received a commitment for an Ex-Im Bank comprehensive guarantee in the amount of $1.68 billion to support the financing of up to 30 new Boeing aircraft. The initial delivery period from September 1, 2004 through August 31, 2005 has been extended by ILFC to August 31, 2006. ILFC did not have any borrowings outstanding under this facility at March 31, 2006. From time to time, ILFC enters into various bank financings. As of March 31, 2006 the total funded amount was $1.6 billion. The financings mature through 2011. One tranche of one of the loans totaling $410 million was funded in Japanese yen and swapped to U.S. dollars.

In December of 2005, ILFC entered into two tranches of junior subordinated debentures totaling $1.0 billion. Both mature on December 21, 2065, but each tranche has a different call option. The $600 million tranche has a call date of December 21, 2010 and the $400 million tranche has a call date of December 21, 2015. The debenture with the 2010 call date has a fixed interest rate of 5.90 percent for the first five years. The debenture with the 2015 call date has a fixed interest rate of 6.25 percent for the first ten years. Both tranches have interest rate adjustments if the call option is not exercised. If the call option is not exercised, the new interest rate will be a floating quarterly reset rate based on the initial credit spread plus the highest of (i) 3 month LIBOR, (ii) 10-year constant maturity treasury and (iii) 30-year constant maturity treasury.

The proceeds of ILFC's debt financing are primarily used to purchase flight equipment, including progress payments during the construction phase. The primary sources for the repayment of this debt and the interest expense thereon are the cash flow from operations, proceeds from the sale of flight equipment and the rollover and refinancing of the prior debt. AIG does not guarantee the debt obligations of ILFC. (See also the discussions under "Operating Review: Financial Services Operations" and "Liquidity" herein.)

AGF fulfills its short term cash requirements through the issuance of commercial paper. The issuance of commercial paper is subject to the approval of AGF's Board of Directors and is not guaranteed by AIG. AGF is a party to unsecured syndicated revolving credit facilities aggregating $4.25 billion, consisting of $2.125 billion in a 364-day revolving credit facility that expires in July of 2006 and $2.125 billion in a five-year revolving credit facility that expires in July of 2010. The 364-day facility allows for the conversion by AGF of any outstanding loans at expiration into a one-year term

loan. The facilities can be used for general corporate purposes and also to provide backup for AGF's commercial paper programs. AGF expects to replace or extend these credit facilities on or prior to their expiration. There are currently no borrowings under these AGF facilities, nor were any borrowings outstanding as of March 31, 2006.

During 2005, AGF issued $5.44 billion of fixed rate and variable rate medium term notes ranging in maturities from two to ten years. As of March 31, 2006, notes aggregating $16.87 billion were outstanding with maturity dates ranging from 2006 to 2015 at interest rates ranging from 1.84 percent to 7.50 percent. To the extent deemed appropriate, AGF may enter into swap transactions to manage its effective borrowing with respect to these notes.

AGF's other funding sources include private placement debt, retail note issuances, securitizations of finance receivables that AGF accounts for as on-balance-sheet secured financings and bank financings. In addition, AGF has become an established issuer of long-term debt in the international capital markets.

In addition to debt refinancing activities, proceeds from the collection of finance receivables will be used to pay the principal and interest with respect to AGF's debt. AIG does not guarantee any of the debt obligations of AGF. See also the discussion under "Operating Review — Financial Services Operations" and "Liquidity" herein.

AIG Credit Card Company (Taiwan) and AIG Finance (Taiwan) Limited, both consumer finance subsidiaries in Taiwan, have issued commercial paper for the funding of their own operations. AIG did not guarantee the commercial paper issued by either of these subsidiaries.

Contractual Obligations and Other Commercial Commitments

The maturity schedule of AIG's contractual obligations at March 31, 2006 was as follows:
(in millions)

		Payments due by Period			
	Total Payments	Less Than One Year	One Through Three Years	Four Through Five Years	After Five Years
Borrowings[(a)]	$103,712	$ 43,853	$ 22,024	$ 19,156	$ 18,679
Loss reserves[(b)]	78,100	21,477	23,821	11,325	21,477
Insurance and investment contract liabilities[(c)]	628,401	30,819	47,966	45,005	504,611
Aircraft purchase commitments	21,428	4,146	10,523	3,775	2,984
Total	$831,641	$100,295	$104,334	$ 79,261	$547,751

(a) Excludes commercial paper and obligations included as debt pursuant to FIN 46R and includes hybrid financial instrument liabilities.

(b) Represents future loss and loss adjustment expense payments estimated based on historical loss development payment patterns.

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

The maturity schedule of AIG's other commercial commitments by segment at March 31, 2006 was as follows:
(in millions)

	Total Amounts Committed	Amount of Commitment Expiration: Less Than One Year	One Through Three Years	Four Through Five Years	After Five Years
Letters of credit:					
Life Insurance & Retirement Services	$ 185	$ 50	$ 5	$ 22	$ 108
DBG	250	250	–	–	–
Standby letters of credit:					
Capital Markets	1,749	12	33	49	1,655
Guarantees:					
Life Insurance & Retirement Services[(a)]	3,437	109	388	–	2,940
Aircraft Finance	125	3	40	–	82
Asset Management	88	49	7	32	–
Parent Company[(b)]	397	396	1	–	–
Other commercial commitments[(c)]:					
Capital Markets[(d)]	11,152	2,786	1,277	700	6,389
Aircraft Finance[(e)]	1,883	–	131	868	884
Life Insurance & Retirement Services[(f)]	3,424	562	1,193	822	847
Asset Management	549	394	140	15	–
DBG[(g)]	1,086	–	–	–	1,086
Total	$ 24,325	$ 4,611	$ 3,215	$ 2,508	$13,991

(a) Primarily AIG SunAmerica construction guarantees connected to affordable housing investments.
(b) Represents reimbursement obligations under letters of credit issued by commercial banks.
(c) Excludes commitments with respect to pension plans. The annual pension contribution for 2006 is expected to be approximately $70 million for U.S. and non-U.S. Plans.
(d) Primarily liquidity facilities provided in connection with certain municipal swap transactions and collateralized bond obligations.
(e) Primarily in connection with options to acquire aircraft.
(f) Primarily AIG SunAmerica commitments to invest in partnerships.
(g) Primarily commitments to invest in limited partnerships.

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

AIG believes that any of its or its subsidiaries' contractual obligations that are subject to "ratings triggers" or financial covenants relating to "ratings triggers" would not have a material adverse effect on its financial condition or liquidity.

As a result of the downgrades of AIG's long-term senior debt ratings, AIG was required to post approximately $1.16 billion of collateral with counterparties to municipal guaranteed investment agreements and financial derivatives transactions. In the event of a further downgrade, AIG will be required to post additional collateral. It is estimated that, as of the close of business on April 30, 2006 based on AIG's outstanding municipal guaranteed investment agreements and financial derivatives transactions as of such date, a further downgrade of AIG's long-term senior debt ratings to 'Aa3' by Moody's or 'AA–' by S&P would permit counterparties to call for approximately $896 million of additional collateral. Further, additional downgrades could result in requirements for substantial additional collateral, which could have a material effect on how AIG manages its liquidity. The actual amount of additional collateral that AIG would be required to post to counterparties in the event of such downgrades depends on market conditions, the market value of the outstanding affected transactions and other factors prevailing at the time of the downgrade. Any additional obligations to post collateral will increase the demand on AIG's liquidity.

Shareholders' Equity

AIG's consolidated shareholders' equity increased $2.07 billion during the first three months of 2006. Retained earnings increased $3.10 billion, resulting from net income of $3.2 billion and $308 million reflecting the cumulative effect of accounting changes relating to the adoption of FSP 85-4-1 and FAS 155 less dividends of $400 million. Unrealized appreciation of investments, net of taxes decreased $1.50 billion and the cumulative translation adjustment loss, net of taxes, decreased $260 million. During the first three months of 2006 there was a gain of $17 million, net of taxes, relating to derivative contracts designated as cash flow hedging instruments. (See also the discussion under "Operating Review"

and "Liquidity" herein and the Consolidated Statement of Comprehensive Income.)

AIG has in the past reinvested most of its unrestricted earnings in its operations and believes such continued reinvestment in the future will be adequate to meet any foreseeable capital needs. However, AIG may choose from time to time to raise additional funds through the issuance of additional securities.

Stock Purchase

During the period January 1, 2006 through March 31, 2006, AIG did not purchase any shares of its common stock under its existing share repurchase authorization. AIG from time to time may buy shares of its common stock in the open market for general corporate purposes, including to satisfy its obligations under various employee benefit plans. At March 31, 2006, an additional 36,542,700 shares could be purchased under the then current authorization by AIG's Board of Directors.

Dividends from Insurance Subsidiaries

Payments of dividends to AIG by its insurance subsidiaries are subject to certain restrictions imposed by regulatory authorities. With respect to AIG's domestic insurance subsidiaries, the payment of any dividend requires formal notice to the insurance department in which the particular insurance subsidiary is domiciled. Under the laws of many states, an insurer may pay a dividend without prior approval of the insurance regulator when the amount of the dividend is below certain regulatory thresholds. To enhance their current capital positions, dividends from the DBG companies were suspended in the fourth quarter of 2005, and AIG has taken various other actions. See "Regulation and Supervision" below. Furthermore, AIG cannot predict how recent regulatory investigations may affect the ability of its regulated subsidiaries to pay dividends.

With respect to AIG's foreign insurance subsidiaries, the most significant insurance regulatory jurisdictions include Bermuda, Japan, Hong Kong, Taiwan, the United Kingdom, Thailand and Singapore.

AIG cannot predict whether the regulatory investigations currently underway or future regulatory issues will impair AIG's financial condition, results of operations or liquidity. To AIG's knowledge, no AIG company is currently on any regulatory or similar "watch list" with regard to solvency. (See also the discussion under "Liquidity" herein.)

Regulation and Supervision

AIG's insurance subsidiaries, in common with other insurers, are subject to regulation and supervision by the states and jurisdictions in which they do business. In the U.S. the National Association of Insurance Commissioners (NAIC) has developed Risk-Based Capital (RBC) requirements. RBC relates an individual insurance company's statutory surplus to the risk inherent in its overall operations.

AIG's insurance subsidiaries file financial statements prepared in accordance with statutory accounting practices prescribed or permitted by domestic and foreign insurance regulatory authorities. The principal differences between statutory financial statements and financial statements prepared in accordance with U.S. GAAP for domestic companies are that statutory financial statements do not reflect deferred policy acquisition costs, some bond portfolios may be carried at amortized cost, assets and liabilities are presented net of reinsurance, policyholder liabilities are valued using more conservative assumptions and certain assets are non-admitted.

AIG recently filed the 2005 statutory financial statements for its domestic General Insurance companies after reviewing and agreeing with the relevant state insurance regulators on the statutory accounting treatment of various items. The regulatory authorities have also permitted certain of the domestic and foreign insurance subsidiaries to support the carrying value of their investments in certain non-insurance and foreign insurance subsidiaries by utilizing the AIG audited consolidated financial statements to satisfy the requirement that the U.S. GAAP-basis equity of such entities be audited. In addition, the regulatory authorities have permitted the domestic General Insurance companies to utilize audited financial statements prepared on a basis of accounting other than U.S. GAAP to value investments in joint ventures, limited partnerships and hedge funds. These permitted practices did not affect the domestic General Insurance companies' compliance with minimum regulatory capital requirements.

Statutory capital of each company continued to exceed minimum company action level requirements following the adjustments, but AIG nonetheless contributed an additional $750 million of capital into American Home effective September 30, 2005 and contributed a further $2.25 billion of capital in February 2006 for a total of approximately $3 billion of capital into Domestic General Insurance subsidiaries effective December 31, 2005. To enhance their current capital positions, dividends from the DBG companies were suspended in the fourth quarter of 2005. AIG believes it has the capital resources and liquidity to fund any necessary statutory capital contributions. AIG will review the capital position of its insurance company subsidiaries with various rating agencies and regulators to determine if additional capital contributions or other actions are warranted.

As discussed above, various regulators have commenced investigations into certain insurance business practices. In addition, the OTS and other regulators routinely conduct examinations of AIG and its subsidiaries, including AIG's consumer finance operations. AIG cannot predict the ultimate effect that these investigations and examinations, or any additional regulation arising therefrom, might have on its

business. Federal, state or local legislation may affect AIG's ability to operate and expand its various financial services businesses, and changes in the current laws, regulations or interpretations thereof may have a material adverse effect on these businesses. See "Risk Factors — Regulatory Investigations" in Item 1A. of Part I of AIG's 2005 Annual Report on Form 10-K for a further discussion of the effect these investigations may have on AIG's businesses.

AIG's U.S. operations are negatively affected under guarantee fund assessment laws which exist in most states. As a result of operating in a state which has guarantee fund assessment laws, a solvent insurance company may be assessed for certain obligations arising from the insolvencies of other insurance companies which operated in that state. AIG generally records these assessments upon notice. Additionally, certain states permit at least a portion of the assessed amount to be used as a credit against a company's future premium tax liabilities. Therefore, the ultimate net assessment cannot reasonably be estimated. The guarantee fund assessments net of credits for the first three months of 2006 were $3 million.

AIG is also required to participate in various involuntary pools (principally workers compensation business) which provide insurance coverage for those not able to obtain such coverage in the voluntary markets. This participation is also recorded upon notification, as these amounts cannot reasonably be estimated.

A substantial portion of AIG's General Insurance business and a majority of its Life Insurance & Retirement Services business are conducted in foreign countries. The degree of regulation and supervision in foreign jurisdictions varies. Generally, AIG, as well as the underwriting companies operating in such jurisdictions, must satisfy local regulatory requirements. Licenses issued by foreign authorities to AIG subsidiaries are subject to modification and revocation. Thus, AIG's insurance subsidiaries could be prevented from conducting future business in certain of the jurisdictions where they currently operate. AIG's international operations include operations in various developing nations. Both current and future foreign operations could be adversely affected by unfavorable political developments up to and including nationalization of AIG's operations without compensation. Adverse effects resulting from any one country may affect AIG's results of operations, liquidity and financial condition depending on the magnitude of the event and AIG's net financial exposure at that time in that country.

Foreign operations are individually subject to local solvency margin requirements that require maintenance of adequate capitalization, which AIG complies with by country. In addition, certain foreign locations, notably Japan, have established regulations that can result in guarantee fund assessments. These have not had a material effect on AIG's operations.

Liquidity

AIG's liquidity is primarily derived from the operating cash flows of its General and Life Insurance & Retirement Services operations. Management believes that AIG's liquid assets, its net cash provided by operations, and access to short-term funding through commercial paper and bank credit facilities will enable it to meet any anticipated cash requirements.

At March 31, 2006, AIG's consolidated invested assets included $18.59 billion of cash and short-term investments. Consolidated net cash provided by operating activities in the first three months of 2006 amounted to $3.07 billion.

The liquidity of the combined insurance operations is derived both domestically and abroad. The combined insurance operating cash flow is derived from two sources, underwriting operations and investment operations. Cash flow includes periodic premium collections, including policyholders' contract deposits, cash flows from investment operations and paid loss recoveries less reinsurance premiums, losses, benefits, and acquisition and operating expenses. Generally, there is a time lag from when premiums are collected and, when as a result of the occurrence of events specified in the policy, the losses and benefits are paid. Investment income cash flow is primarily derived from interest and dividends received and includes realized capital gains net of realized capital losses. (See also the discussions under "Operating Review: General Insurance Operations" and "Life Insurance & Retirement Services Operations" herein.)

With respect to General Insurance operations, if paid losses accelerated beyond AIG's ability to fund such paid losses from current operating cash flows, AIG might need to liquidate a portion of its General Insurance investment portfolio and/or arrange for financing. Potential events causing such a liquidity strain could be the result of several significant catastrophic events occurring in a relatively short period of time. Additional strain on liquidity could occur if the investments sold to fund such paid losses were sold into a depressed market place and/or reinsurance recoverable on such paid losses became uncollectible or collateral supporting such reinsurance recoverable significantly decreased in value. (See also the discussions under "Operating Review: General Insurance Operations" herein.)

With respect to Life Insurance & Retirement Services operations, if a substantial portion of the Life Insurance & Retirement Services operations bond portfolio diminished significantly in value and/or defaulted, AIG might need to liquidate other portions of its Life Insurance & Retirement Services investment portfolio and/or arrange financing. Potential events causing such a liquidity strain could be the result of economic collapse of a nation or region in which AIG Life Insurance & Retirement Services operations exist, nationalization, terrorist acts, or other such economic or political upheaval. In addition, a significant rise in interest rates leading to a significant increase in policyholder surrenders

could also create a liquidity strain. (See also the discussions under "Operating Review: Life Insurance & Retirement Services Operations" herein.)

In addition to the combined insurance pretax operating cash flow, AIG's insurance operations held $10.36 billion in cash and short-term investments at March 31, 2006. Operating cash flow and the cash and short-term balances held provided AIG's insurance operations with a significant amount of liquidity. AIG subsidiaries have also issued debt securities to meet capital needs. In December 2005, Transatlantic issued $750 million of debt securities in a public offering, of which $450 million were purchased by other AIG subsidiaries. Transatlantic contributed the proceeds of the offering to a reinsurance company subsidiary.

This liquidity is available, among other things, to purchase predominately high quality and diversified fixed income securities and, to a lesser extent, marketable equity securities, and to provide mortgage loans on real estate, policy loans and collateral loans. This cash flow coupled with proceeds of approximately $30 billion from the maturities, sales and redemptions of fixed income securities and from the sale of equity securities was used to purchase approximately $39 billion of fixed income securities and marketable equity securities during the first three months of 2006.

AIG's major Financial Services operating subsidiaries consist of AIGFP, ILFC, AGF and AIGCFG. Sources of funds considered in meeting the liquidity needs of AIGFP's operations include guaranteed investment agreements, issuance of long-term and short-term debt, proceeds from maturities and sales of securities available for sale, securities sold under repurchase agreements, and securities and spot commodities sold but not yet purchased. ILFC, AGF and AIGCFG all utilize the commercial paper markets, retail and wholesale deposits, bank loans and bank credit facilities as sources of liquidity. ILFC and AGF also fund in the domestic and international capital markets without reliance on any guarantee from AIG. An additional source of liquidity for ILFC is the use of export credit facilities. AIGCFG also uses wholesale and retail bank deposits as sources of funds. On occasion, AIG has provided equity capital to ILFC, AGF and AIGCFG and provides intercompany loans to AIGCFG. An AIG subsidiary purchased additional shares of ILFC in the amount of $400 million during the third quarter of 2005. Cash flow provided from operations is a major source of liquidity for AIG's primary Financial Services operating subsidiaries.

AIG, the parent company, funds its short-term working capital needs through commercial paper issued by AIG Funding. As of March 31, 2006, AIG Funding had $5.09 billion of commercial paper outstanding with an average maturity of 25 days. As additional liquidity, AIG parent has a $2 billion inter-company revolving credit facility provided by certain of its subsidiaries, a $1.375 billion 364-day revolving bank credit facility that expires in July 2006, a $1.375 billion five year revolving bank credit facility that expires in July 2010 and a $3 billion 364-day revolving credit facility that expires in November 2006, of which $1.01 billion is currently available as back-up liquidity. AIG parent's primary sources of cash flow are dividends and loans from its subsidiaries. AIG parent's primary uses of cash flow are for debt service, capital contributions to subsidiaries and the payment of dividends to shareholders. As of March 31, 2006, including debt obligations of AGC that are guaranteed by AIG, remaining debt and loan maturities due in 2006 are $0, $600 million and $0 for the second, third and fourth quarters, respectively. According to the terms of the Zero Coupon Convertible Senior Debentures issued by AIG on November 9, 2001, holders can require AIG to repurchase the debentures once every five years beginning on November 9, 2006. Assuming that all of the outstanding debentures are required to be repurchased by AIG on November 9, 2006, the aggregate repurchase price payable by AIG on that date will be approximately $1.10 billion. See also Note 9 of Notes to Consolidated Financial Statements in AIG's 2005 Annual Report on Form 10-K for additional information on debt maturities for AIG and its subsidiaries.

Special Purpose Vehicles and Off Balance Sheet Arrangements

AIG uses special purpose vehicles (SPVs) and off balance sheet arrangements in the ordinary course of business. As a result of recent changes in accounting, a number of SPVs and off balance sheet arrangements have been reflected in AIG's consolidated financial statements. In January 2003, FASB issued Interpretation No. 46, "Consolidation of Variable Interest Entities" (FIN 46). FIN 46 addressed the consolidation and disclosure rules for nonoperating entities that are now defined as Variable Interest Entities (VIEs). In December 2003, FASB issued a revision to Interpretation No. 46 (FIN 46R).

AIG has guidelines with respect to the formation of and investment in SPVs and off balance sheet arrangements. In addition, AIG has expanded the responsibility of its Complex Structured Financial Transaction Committee (CSFT) to include the review of any transaction that could subject AIG to heightened legal, reputational, regulatory, accounting or other risk. See "Management's Report on Internal Control Over Financial Reporting" in Item 9A. of Part II included in AIG's 2005 Annual Report on Form 10-K for a further discussion of the CSFT.

For additional information related to AIG's activities with respect to VIEs and certain guarantees see "Recent Accounting Standards" herein and also Note 8 of Notes to Consolidated Financial Statements. Also, for additional disclosure regarding AIG's commercial commitments (including guarantors), see "Contractual Obligations and Other Commercial Commitments" herein.

Derivatives

Derivatives are financial instruments among two or more parties with returns linked to or "derived" from some underlying equity, debt, commodity or other asset, liability, or index. Derivatives payments may be based on interest rates and exchange rates and/or prices of certain securities, commodities, financial or commodity indices, or other variables. The more significant types of derivative arrangements in which AIG transacts are swaps, forwards, futures and options. In the normal course of business, with the agreement of the original counterparty, these contracts may be terminated early or assigned to another counterparty.

The overwhelming majority of AIG's derivatives activities are conducted by the Capital Markets operations, thus permitting AIG to participate in the derivatives dealer market acting primarily as principal. In these derivative operations, AIG structures transactions that generally allow its counterparties to obtain or hedge exposure to changes in interest and foreign currency exchange rates, credit events, securities' prices and certain commodities and financial or commodity indices. AIG's customers – such as corporations, financial institutions, multinational organizations, sovereign entities, government agencies and municipalities – use derivatives to hedge their own market exposures. For example, a futures, forward or option contract can be used to protect the customers' assets or liabilities against price fluctuations.

A counterparty may default on any obligation to AIG, including a derivative contract. Credit risk is a consequence of extending credit and/or carrying trading and investment positions. Credit risk exists for a derivative contract when that contract has a positive fair value to AIG. To help manage this risk, AIGFP's credit department operates within the guidelines set by the AIG Credit Risk Committee. This committee establishes the credit policy, sets limits for counterparties and provides limits for derivative transactions with counterparties having different credit ratings. In addition to credit ratings, this committee takes into account other factors, including the industry and country of the counterparty. Transactions which fall outside these pre-established guidelines require the specific approval of the AIG Credit Risk Committee. It is also AIG's policy to establish reserves for potential credit impairment when necessary.

In addition, AIGFP utilizes various credit enhancements, including letters of credit, guarantees, collateral, credit triggers, credit derivatives, and margin agreements to reduce the credit risk relating to its outstanding financial derivative transactions. AIGFP requires credit enhancements in connection with specific transactions based on, among other things, the creditworthiness of the counterparties, and the transaction's size and maturity.

AIG's Derivatives Review Committee provides an independent review of any proposed derivative transaction or program except those derivative transactions entered into by AIGFP with third parties. The committee examines, among other things, the nature and purpose of the derivative transaction, its potential credit exposure, if any, and the estimated benefits.

Managing Market Risk

Market risk is the risk of loss of fair value resulting from adverse fluctuations in interest rates, foreign currencies, equities and commodity prices. AIG has exposures to these risks.

AIG analyzes market risk using various statistical techniques including Value at Risk (VaR). VaR is a summary statistical measure that applies the estimated volatility and correlation of market factors to AIG's market positions. The output from the VaR calculation is the maximum loss that could occur over a defined period of time given a certain probability. While VaR models are relatively sophisticated, the quantitative market risk information generated is limited by the assumptions and parameters established in creating the related models. AIG believes that statistical models alone do not provide a reliable method of monitoring and controlling market risk. Therefore, such models are tools and do not substitute for the experience or judgment of senior management.

Insurance

AIG has performed a separate VaR analysis for the General Insurance and Life Insurance & Retirement Services segments and for each market risk within each segment. For purposes of the VaR calculation, the insurance assets and liabilities from GICs are included in the Life Insurance & Retirement Services segment. For the calculations in the analyses the financial instrument assets included are the insurance segments' invested assets, excluding real estate and investment income due and accrued, and the financial instrument liabilities included are reserve for losses and loss expenses, reserve for unearned premiums, future policy benefits for life and accident and health insurance contracts and other policyholders' funds.

AIG calculated the VaR with respect to the net fair value of each of AIG's insurance segments as of March 31, 2006 and December 31, 2005. The VaR number represents the maximum potential loss as of those dates that could be incurred with a 95 percent confidence (i.e., only five percent of historical scenarios show losses greater than the VaR figure) within a one-month holding period. AIG uses the historical simulation methodology that entails repricing all assets and liabilities under explicit changes in market rates within a specific historical time period. AIG uses the most recent three years of historical market information for interest rates, foreign exchange rates, and equity index prices. For each scenario, each transaction was repriced. Portfolio, business unit and finally AIG-wide scenario values are then calculated by netting the values of all the underlying assets and liabilities.

The following table presents the VaR on a combined basis and of each component of market risk for each of AIG's insurance segments as of March 31, 2006 and December 31, 2005. Due to diversification effects, the combined VaR is always smaller than the sum of its components.

	General Insurance		Life Insurance & Retirement Services	
(in millions)	**2006**	2005	**2006**	2005
Market risk:				
Combined	**$1,673**	$1,617	**$5,260**	$4,515
Interest rate	**1,636**	1,717	**5,032**	4,382
Currency	**119**	130	**597**	541
Equity	**560**	535	**795**	762

The following table presents the average, high and low VaRs on a combined basis and of each component of market risk for each of AIG's insurance segments as of March 31, 2006 and December 31, 2005. Due to diversification effects, the combined VaR is always smaller than the sum of its components.

	2006			2005		
(in millions)	**Average**	**High**	**Low**	Average	High	Low
General Insurance:						
Market risk:						
Combined	**$1,645**	**$1,673**	**$1,617**	$1,585	$1,672	$1,396
Interest rate	**1,677**	**1,717**	**1,636**	1,746	1,931	1,563
Currency	**125**	**130**	**119**	125	139	111
Equity	**547**	**560**	**535**	651	727	535
Life Insurance & Retirement Services:						
Market risk:						
Combined	**$4,888**	**$5,260**	**$4,515**	$4,737	$5,024	$4,515
Interest rate	**4,707**	**5,032**	**4,382**	4,488	4,750	4,382
Currency	**569**	**597**	**541**	511	560	442
Equity	**778**	**795**	**762**	953	1,024	762

In the Life Insurance & Retirement Services segment, the increase in Combined VaR and Interest rate VaR in 2006 was primarily the result of growth in the Foreign Life business. In most Asian markets, interest rates and interest rate volatilities were stable during the quarter.

Financial Services

AIG generally manages its market exposures within Financial Services by maintaining offsetting positions. Capital Markets seeks to minimize or set limits for open or uncovered market positions. Credit exposure is managed separately. (See the discussion on the management of credit risk above.)

AIG's Market Risk Management Department provides detailed independent review of AIG's market exposures, particularly those market exposures of the Capital Markets operations. This department determines whether AIG's market risks, as well as those market risks of individual subsidiaries, are within the parameters established by AIG's senior management. Well established market risk management techniques such as sensitivity analysis are used. Additionally, this department verifies that specific market risks of each of certain subsidiaries are managed and hedged by that subsidiary.

ILFC is exposed to market risk and the risk of loss of fair value and possible liquidity strain resulting from adverse fluctuations in interest rates. As of March 31, 2006 and December 31, 2005, AIG statistically measured the loss of fair value through the application of a VaR model. In this analysis, the net fair value of Aircraft Finance operations was determined using the financial instrument assets which included the tax adjusted future flight equipment lease revenue, and the financial instrument liabilities which included the future servicing of the current debt. The estimated effect of the current derivative positions was also taken into account.

AIG calculated the VaR with respect to the net fair value of Aircraft Finance operations using the historical simulation methodology, as previously described. As of March 31, 2006 and December 31, 2005, the average VaR with respect to the net fair value of Aircraft Finance operations was approximately $196 million and $129 million, respectively. In late 2005, ILFC lengthened the average maturity of its debt, leading to an increase in its VaR.

Capital Markets operations are exposed to market risk due to changes in the level and volatility of interest rates, foreign currency exchange rates, equity prices and commodity prices. AIGFP hedges its exposure to these risks primarily through swaps, options, forwards and futures. To economically hedge interest rate risks, AIGFP may also purchase U.S. and foreign government obligations.

AIGFP does not seek to manage the market risk of each transaction through an individual third party offsetting transaction. Rather, AIGFP takes a portfolio approach to the management of its market risk exposures. AIGFP values the

predominant portion of its market-sensitive transactions by marking them to market currently through income. A smaller portion is priced by estimated fair value based upon an extrapolation of market factors. There is another limited portion of transactions where the initial fair value is not recorded through income currently and gains or losses are recognized over the life of the transactions. These valuations represent an assessment of the present values of expected future cash flows and may include reserves for such risks as are deemed appropriate by AIGFP and AIG management.

The recorded values of these transactions may be different from the values that might be realized if AIGFP were required to sell or close out the transactions prior to maturity. AIG believes that such differences are not significant to its financial condition or liquidity. Such differences would be immediately recognized when the transactions are sold or closed out prior to maturity.

AIGFP attempts to secure reliable and independent current market prices, such as published exchange prices, external subscription services such as from Bloomberg or Reuters or third-party broker quotes for use in this model. When such prices are not available, AIGFP use an internal methodology which includes extrapolation from observable and verifiable prices nearest to the dates of the transactions. Historically, actual results have not materially deviated from these models in any material respect.

Systems used by Capital Markets operations can monitor each unit's respective market positions on an intraday basis. AIGFP operates in major business centers overseas and therefore is open for business essentially 24 hours a day. Thus, the market exposure and offset strategies are monitored, reviewed and coordinated around the clock.

AIGFP applies various testing techniques which reflect significant potential market movements in interest rates, foreign exchange rates, commodity and equity prices, volatility levels and the effect of time. These techniques vary by currency and are regularly changed to reflect factors affecting the derivatives portfolio. The results from these analyses are regularly reviewed by AIG management.

As described above, Capital Markets operations are exposed to the risk of loss of fair value from adverse fluctuations in interest rate and foreign currency exchange rates and equity and commodity prices as well as implied volatilities thereon. AIG statistically measures the losses of fair value through the application of a VaR model across Capital Markets.

Capital Markets asset and liability portfolios for which the VaR analyses were performed included over the counter and exchange traded investments, derivative instruments and commodities. Because the market risk with respect to securities available for sale, at market, is substantially hedged, segregation of market sensitive instruments into trading and other than trading was not deemed necessary. The VaR calculation is unaffected by the accounting treatment of hedged transactions under FAS 133.

In the calculation of VaR for Capital Markets operations, AIG uses the same historical simulation methodology, described under Insurance above, which entails repricing all assets and liabilities under explicit changes in market rates within a specific historical time period. AIGFP has recently enhanced its library of factors by including implied option volatilities to construct the historical scenarios for simulation.

The following table presents the VaR on a combined basis and of each component of market risk for Capital Markets operations as of March 31, 2006 and December 31, 2005. Due to diversification effects, the combined VaR is always smaller than the sum of its components.

(in millions)	**2006**	2005
Combined	**$20**	$22
Interest rate	**8**	9
Currency	**6**	3
Equity	**12**	14
Commodity	**16**	9

The following table presents the average, high and low VaRs on a combined basis and of each component of market risk for Capital Markets operations as of March 31, 2006 and December 31, 2005. Due to diversification effects, the combined VaR is always smaller than the sum of its components.

	2006			2005		
(in millions)	**Average**	**High**	**Low**	Average	High	Low
Combined	**$21**	**$22**	**$20**	$17	$22	$13
Interest rate	**8**	**9**	**8**	9	11	6
Currency	**5**	**6**	**3**	4	6	3
Equity	**13**	**14**	**12**	9	16	5
Commodity	**13**	**16**	**9**	8	10	7

Recent Accounting Standards

At the March 2004 meeting, the Emerging Issue Task Force (EITF) reached a consensus with respect to Issue No. 03-1, "The Meaning of Other-Than Temporary Impairment and Its Application to Certain Investments." On September 30, 2004, the FASB issued FASB Staff Position (FSP) EITF Issue 03-1-1, Effective Date of Paragraphs 10-20 of EITF Issue No. 03-1, "The Meaning of Other-Than-Temporary Impairment and Its Application to Certain Investments." In November 2005, FASB issued FSP FAS 115-1, "The Meaning of Other-Than-Temporary Impairment and Its Application to Certain Investments," which replaces the measurement and

recognition guidance set forth in Issue No. 03-1 and codifies certain existing guidance on impairment.

In March 2005, FASB issued FSP FIN46R-5 "Implicit Variable Interests under FASB Interpretation No. 46 (revised December 2003), Consolidation of Variable Interest Entities."

On June 1, 2005, the FASB issued Statement No. 154, "Accounting Changes and Error Corrections" (FAS 154). FAS 154 replaces APB Opinion No. 20, "Accounting Changes" and FASB Statement No. 3, "Reporting Accounting Changes in Interim Financial Statements."

At the June 2005 meeting, the EITF reached a consensus with respect to Issue No. 04-5, "Determining Whether a General Partner, or the General Partners as a Group, Controls a Limited Partnership or Similar Entity When the Limited Partners have Certain Rights."

On June 29, 2005, FASB issued Statement 133 Implementation Issue No. B38, "Embedded Derivatives: Evaluation of Net Settlement with Respect to the Settlement of a Debt Instrument through Exercise of an Embedded Put Option or Call Option."

On June 29, 2005, FASB issued Statement 133 Implementation issue No. B39, "Application of Paragraph 13(b) to Call Options That Are Exercisable Only by the Debtor."

On September 19, 2005, FASB issued Statement of Position 05-1, "Accounting by Insurance Enterprises for Deferred Acquisition Costs in Connection with Modifications or Exchanges of Insurance Contracts."

On February 16, 2006, FASB issued FAS No. 155, "Accounting for Certain Hybrid Financial Instruments."

On March 27, 2006, the FASB issued FSP FTB 85-4-1, "Accounting for Life Settlement Contracts by Third-Party Investors" (FSP 85-4-1), an amendment of FTB 85-4, "Accounting for Purchases of Life Insurance."

On April 13, 2006, the FASB issued FSP FIN 46(R)-6, "Determining the Variability to be Considered in Applying FASB Interpretation No. 46(R)."

From January 1, 2003 through December 31, 2005, AIG accounted for share-based payment transactions with employees under FAS 123, "Accounting for Stock-Based Compensation." Share-based employee compensation expense was not recognized in the statement of income in prior periods. Effective January 1, 2006, AIG adopted the fair value recognition provisions of Statement of Financial Accounting Standards No. 123R "Share-Based Payments" (FAS 123R). FAS 123R requires that companies use a fair value method to value share-based payments and recognize the related compensation expense in net earnings. AIG adopted FAS 123R using the Modified Prospective Application method, and accordingly, financial statement amounts for the prior periods presented have not been restated to reflect the fair value method of expensing share-based compensation under FAS 123R. The modified prospective application method provides for the recognition of the fair value with respect to share-based compensation for shares subscribed for or granted on or after January 1, 2006 and all previously granted but unvested awards as of January 1, 2006.

The adoption of FAS 123R resulted in share-based compensation expense of approximately $8 million during the first three months of 2006, related to awards which were accounted for under the provisions of Accounting Principles Board Opinion No. 25, "Accounting for Stock Issued to Employees." Consistent with AIG's prospective adoption of the requirements of FAS 123, AIG did not include the compensation expense related to these awards in its Consolidated Statement of Income. Instead, the effect of these awards was disclosed in the pro forma disclosures required by FAS 123. AIG expects this expense to approximate $31 million for fiscal 2006. FAS 123R also requires AIG to estimate forfeitures in calculating the expense relating to share-based compensation, rather than recognizing these forfeitures and corresponding reductions in expense as they occur. The pretax cumulative effect of adoption, recognized as a reduction in stock-based compensation of $46 million, was recorded as a cumulative effect of an accounting change net of tax. FAS 123R requires AIG to reflect the cash savings resulting from excess tax benefits in its financial statements as cash flow from financing activities, rather than as cash flow from operating activities as in prior periods. The amount of this excess tax benefit for the three months ending March 31, 2006 was $1.7 million.

As a result of FAS 123R, excluding the cumulative effect of adoption, AIG's income before income taxes and net income for the three months ended March 31, 2006 was $8 million and $5 million, respectively, lower than if AIG had continued to account for share-based compensation under FAS 123. The effect on basic and diluted earnings for the three months ended March 31, 2006 was less than $0.01 per share.

AIG uses a variety of assumptions and a binomial model to calculate the fair value of share-based compensation programs.

The contractual term of options granted is generally 10 years with an expected term of 7 years calculated based on an analysis of historical employee exercise behavior and employee turnover (post-vesting terminations).

Expected volatility is the average of historical volatility and the implied volatility of actively traded options on AIG shares.

Dividend yield is based on the twelve month period prior to the grant date. Interest rate curves used in the valuation model were the US Treasury STRIP rates with terms from 3 months to 10 years.

As of March 31, 2006, the total unrecognized compensation costs (net of expected forfeitures) related to

share-based awards granted and not yet vested under AIG's plans, and the blended weighted-average period over which those costs are expected to be recognized, are as follows:

	Unrecognized Pre-Tax Compensation Cost *(in millions)*	Blended Weighted-Average Period
1996 Employee Stock Purchase Plan, as amended	$ 4	0.5 years
1999 Stock Option Plan, as amended	$204	1.40 years
2002 Stock Incentive Plan	$196	1.83 years
SICO Deferred Compensation Profit Participation Plans	$357	6.08 years
2005-2006 AIG Deferred Compensation Profit Participation Plan	$248	11.62 years

The total cost for awards outstanding under each plan as of March 31, 2006 is expected to be recognized over approximately double the respective plan's blended weighted average period.

Historically, SICO's Board of Directors could elect to pay a participant cash in lieu of shares of AIG common stock. On December 9, 2005, SICO notified plan participants that substantially all future payments would be settled with shares rather than cash. On that date, AIG modified its accounting for the SICO Plans (as described in Note 4 of Notes to the Consolidated Financial Statements) from variable to fixed measurement accounting. See Note 10 herein and Note 16 of Notes to the Consolidated Financial Statements in the 2005 Annual Report on Form 10-K. Using fixed measurement accounting, the compensation expense relating to the SICO Plans for the three months ending March 31, 2006 was approximately $14 million. In addition, various adjustments totalling $61 million, primarily relating to stock-split adjustments and other miscellaneous items, were recorded in the three months ending March 31, 2006.

In December, 2005 and January, 2006, Starr made tender offers to AIG employees holding Starr common and preferred stock. In conjunction with AIG's adoption of FAS 123R, Starr is considered to be an "economic interest holder" in AIG. As a result, the compensation expense related to the 2006 tender offer is included in AIG's consolidated financial statements for the three months ending March 31, 2006. The amount of one-time compensation cost attributable to the 2006 tender offer is approximately $54 million.

For further discussion of these recent accounting standards and their application to AIG, see Note 10 of Notes to Consolidated Financial Statements.

CONTROLS AND PROCEDURES

In connection with the preparation of this First Quarter Form 10-Q, an evaluation was carried out by AIG's management, with the participation of AIG's current Chief Executive Officer and Chief Financial Officer, of the effectiveness of AIG's disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934 (Exchange Act)). Disclosure controls and procedures are designed to ensure that information required to be disclosed in reports filed or submitted under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in SEC rules and forms and that such information is accumulated and communicated to management, including the Chief Executive Officer and Chief Financial Officer, to allow timely decisions regarding required disclosures. Based on its evaluation, and in light of the previously identified material weaknesses in internal control over financial reporting, as of December 31, 2005, described within the 2005 Annual Report on Form 10-K, AIG's Chief Executive Officer and Chief Financial Officer concluded that, as of March 31, 2006, AIG's disclosure controls and procedures were ineffective. In addition, there has been no change in AIG's internal control over financial reporting (as defined in Rule 13a-15(f) under the Exchange Act) that occurred during the first three months of 2006 that has materially affected, or is reasonably likely to materially affect, AIG's internal control over financial reporting.

Part II

ITEM 1A. Risk Factors

The following discussion supplements and amends the significant risk factors that may affect AIG as described in detail under "Risk Factors" in Item 1A. of Part I of the 2005 Annual Report on Form 10-K.

AIG's Credit Ratings

The downgrades in AIG's credit ratings will increase AIG's borrowing costs, may lessen AIG's ability to compete in certain business and will require AIG to post additional collateral.

From March through June of 2005, the major rating agencies downgraded AIG's ratings in a series of actions. Standard & Poor's, a division of the McGraw-Hill Companies, Inc. (S&P), lowered the long-term senior debt and counterparty ratings of AIG from 'AAA' to 'AA' (second highest of eight rating categories) and changed the rating outlook to negative. S&P's outlook indicates the potential direction of a rating over the intermediate term (typically six months to two years). A negative outlook means that a rating may be lowered; however, an outlook is not necessarily a precursor to a rating change. Moody's Investors Service (Moody's) lowered AIG's long-term senior debt rating from 'Aaa' to 'Aa2' (second highest of nine rating categories) with a stable outlook. Moody's appends numerical modifiers 1, 2, and 3 to the generic rating categories to show relative position within rating categories. Fitch Ratings (Fitch) downgraded the long-term senior debt ratings of AIG from 'AAA' to 'AA' (second highest of nine rating categories) and placed the ratings on Rating Watch Negative. A Fitch Rating Watch notifies investors that there is a reasonable probability of a rating change and the likely direction of such change. A Rating Watch Negative indicates a potential downgrade. Rating Watch is typically resolved over a relatively short period. In April 2006, Fitch removed AIG from Rating Watch Negative and affirmed its rating with a stable outlook.

The agencies also took rating actions on AIG's insurance subsidiaries. S&P lowered the financial strength ratings of AIG's insurance subsidiaries to 'AA+' (second highest rating of eight rating categories) and assigned a negative rating outlook. Fitch also lowered the financial strength ratings of AIG's insurance companies to 'AA+' (second highest of nine rating categories) and placed them on Rating Watch Negative. In April 2006, Fitch removed the financial strength ratings from Rating Watch Negative and affirmed them with a stable outlook. S&P and Fitch ratings may be modified by the addition of a plus or minus sign to show relative standing within the major rating categories. Moody's lowered the insurance financial strength ratings generally to either 'Aa1' or 'Aa2' (both within the second highest of nine rating categories) with a stable outlook. A.M. Best downgraded the financial strength ratings of most of AIG's insurance subsidiaries from 'A++' to 'A+' (second highest of fourteen rating levels) and the issuer credit ratings from 'aa+' to 'aa–' (remaining within the second highest of nine rating levels) and placed the ratings under review with negative implications. An under review modifier by A.M. Best is assigned to a company whose rating opinion is under review and may be subject to change in the near-term, generally defined as six months. Negative implications indicates a potential downgrade.

In addition, S&P changed the outlook on the 'AA–' long-term senior debt rating (second highest out of eight rating categories) of ILFC (a wholly owned subsidiary of AIG) to negative. Moody's affirmed ILFC's long-term and short-term senior debt ratings ('A1'/'P-1') (third highest of nine, and highest of three, rating categories, respectively). Fitch downgraded ILFC's long-term senior debt rating from 'AA–' to 'A+' (third highest of nine rating categories), placed it on Rating Watch Negative and downgraded ILFC's short-term debt rating from 'F1+' to 'F1' (remaining within the highest of five rating categories). In April 2006, Fitch removed ILFC's long-term senior debt rating from Rating Watch Negative and affirmed it with a stable outlook.

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

These ratings actions have affected and will continue to affect AIG's business and results of operations in a number of ways.

- **Downgrades in AIG's debt ratings will adversely affect AIG's results of operations.** AIG relies on external sources of financing to fund several of its operations. The cost and availability of unsecured financing are generally dependent on the issuer's long-term and short-term debt ratings. These downgrades and any future downgrades in AIG's debt ratings may adversely affect AIG's borrowing costs and therefore adversely affect AIG's results of operations.
- **The downgrade in AIG's long-term senior debt ratings will adversely affect AIGFP's ability to compete for certain businesses.** Credit ratings are very important to the ability of financial institutions to compete in the derivative and structured transaction marketplaces. Historically, AIG's triple-A ratings provided AIGFP a competitive advantage. The downgrades have reduced this advantage and, for specialized financial transactions that generally are conducted only by triple-A rated financial institutions, counterparties may be unwilling to transact business with AIGFP except on a secured basis. This could require AIGFP to post more collateral to counterparties in the future. See below for a

further discussion of the effect that posting collateral may have on AIG's liquidity.

- **Although the financial strength ratings of AIG's insurance company subsidiaries remain high compared to many of their competitors, the downgrades have reduced the previous ratings differential.** The competitive advantage of the ratings to AIG's insurance company subsidiaries may be lessened accordingly.
- **As a result of the downgrades of AIG's long-term senior debt ratings, AIG was required to post approximately $1.16 billion of collateral with counterparties to municipal guaranteed investment contracts and financial derivatives transactions.** In the event of a further downgrade, AIG will be required to post additional collateral. It is estimated that, as of the close of business on April 30, 2006 based on AIG's outstanding municipal guaranteed investment agreements and financial derivatives transactions as of such date, a further downgrade of AIG's long-term senior debt ratings to 'Aa3' by Moody's or 'AA–' by S&P would permit counterparties to call for approximately $896 million of additional collateral. Further, additional downgrades could result in requirements for substantial additional collateral, which could have a material effect on how AIG manages its liquidity. The actual amount of additional collateral that AIG would be required to post to counterparties in the event of such downgrades depends on market conditions, the market value of the outstanding affected transactions and other factors prevailing at the time of the downgrade. Any additional obligations to post collateral will increase the demand on AIG's liquidity.

ITEM 2. Unregistered Sales of Equity Securities and Use of Proceeds

The table below provides information with respect to purchases of AIG Common stock during the three months ended March 31, 2006.

Period	Total Number of Shares Purchased[1]	Average Price Paid per Share	Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs	Maximum Number of Shares that May Yet Be Purchased Under the Plans or Programs at End of Month[2]
January 1 - 31	–	$ –	–	36,542,700
February 1 - 28	–	–	–	36,542,700
March 1 - 31	–	–	–	36,542,700
Total	–	$ –	–	

(1) Does not include 29,514 shares delivered or attested to in satisfaction of the exercise price by holders of AIG employee stock options exercised during the three months ended March 31, 2006.

(2) On July 19, 2002, AIG announced that its Board of Directors had authorized the open market purchase of up to 10 million shares of common stock. On February 13, 2003, AIG announced that the Board had expanded the existing program through the authorization of an additional 50 million shares. The purchase program has no set expiration or termination date.

ITEM 6. Exhibits

See accompanying Exhibit Index.

SIGNATURE

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

AMERICAN INTERNATIONAL GROUP, INC.
(Registrant)

/s/ STEVEN J. BENSINGER

Steven J. Bensinger
Executive Vice President and Chief Financial Officer

/s/ DAVID L. HERZOG

David L. Herzog
Senior Vice President and Comptroller
(Principal Accounting Officer)

Dated: May 10, 2006

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EXHIBIT INDEX

Exhibit Number	Description	Location
11	Statement re computation of per share earnings	Included in Note (3) of Notes to Consolidated Financial Statements.
12	Statement re computation of ratios	Filed herewith.
31	Rule 13a-14(a)/15d-14(a) Certifications	Filed herewith.
32	Section 1350 Certifications	Filed herewith.

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Exhibit 12

American International Group, Inc.

Computation of Ratios of Earnings to Fixed Charges

Three Months Ended March 31, *(in millions, except ratios)*	**2006**	2005
Income before income taxes, minority interest and cumulative effect of an accounting change	**$ 4,793**	$ 5,649
Less – Equity income of less than 50% owned persons	**20**	63
Add – Dividends from less than 50% owned persons	**3**	3
	4,776	5,589
Add – Fixed charges	**1,948**	1,730
Less – Capitalized interest	**15**	15
Income before income taxes, minority interest, cumulative effect of an accounting change and fixed charges	**$ 6,709**	$ 7,304
Fixed charges:		
Interest costs	**$ 1,896**	$ 1,679
Rental expense*	**52**	51
Total fixed charges	**$ 1,948**	$ 1,730
Ratio of earnings to fixed charges	**3.44**	4.22
Secondary Ratio		
Interest credited to GIC and GIA policy and contract holders	**$(1,090)**	$(1,094)
Total fixed charges excluding interest credited to GIC and GIA policy and contract holders	**$ 858**	$ 636
Secondary ratio of earnings to fixed charges	**6.55**	9.76

**The proportion deemed representative of the interest factor.*

The secondary ratio is disclosed for the convenience of fixed income investors and the rating agencies that serve them and is more comparable to the ratios disclosed by all issuers of fixed income securities. The secondary ratio removes interest credited to guaranteed investment contract (GIC) policyholders and guaranteed investment agreement (GIA) contractholders. Such expenses are also removed from income before income taxes, minority interest and cumulative effect of an accounting change used in this calculation. GICs and GIAs are entered into by AIG's insurance subsidiaries, principally Sun America Life Insurance Company and AIG Financial Products Corp. and its subsidiaries, respectively. The proceeds from GICs and GIAs are invested in a diversified portfolio of securities, primarily investment grade bonds. The assets acquired yield rates greater than the rates on the related policyholders obligation or agreement, with the intent of earning operating income from the spread.

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Exhibit 31

CERTIFICATIONS

I, Martin J. Sullivan, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q of American International Group, Inc.;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:

(a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

(b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

(c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

(d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):

(a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

(b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

/s/ Martin J. Sullivan

Martin J. Sullivan
President and Chief Executive Officer

Date: May 10, 2006

CERTIFICATIONS

I, Steven J. Bensinger, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q of American International Group, Inc.;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:

(a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

(b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

(c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

(d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):

(a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

(b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

/s/ Steven J. Bensinger

Steven J. Bensinger
Executive Vice President and Chief Financial Officer

Date: May 10, 2006

Exhibit 32

CERTIFICATION

In connection with the Quarterly Report on Form 10-Q of American International Group, Inc. (the "Company") for the quarter ended March 31, 2006, as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, Martin J. Sullivan, President and Chief Executive Officer of the Company, certify, pursuant to 18 U.S.C. Section 1350, that to my knowledge:

1. The Report fully complies with the requirements of Section 13(a) or 15(d), as applicable, of the Securities Exchange Act of 1934; and

2. The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

/s/ Martin J. Sullivan

Martin J. Sullivan
President and Chief Executive Officer

Date: May 10, 2006

The foregoing certification is being furnished solely pursuant to 18 U.S.C. Section 1350 and is not being filed as part of the Report or as a separate disclosure document.

CERTIFICATION

In connection with the Quarterly Report on Form 10-Q of American International Group, Inc. (the "Company") for the quarter ended March 31, 2006, as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, Steven J. Bensinger, Executive Vice President and Chief Financial Officer of the Company, certify, pursuant to 18 U.S.C. Section 1350, that to my knowledge:

1. The Report fully complies with the requirements of Section 13(a) or 15(d), as applicable, of the Securities Exchange Act of 1934; and

2. The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

/s/ Steven J. Bensinger

Steven J. Bensinger
Executive Vice President and Chief Financial Officer

Date: May 10, 2006

The foregoing certification is being furnished solely pursuant to 18 U.S.C. Section 1350 and is not being filed as part of the Report or as a separate disclosure document.

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

Form 10-Q

(Mark One)

☑ QUARTERLY REPORT UNDER SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended June 30, 2006

or

☐ TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the transition period from to

Commission File Number 1-8787

American International Group, Inc.

(Exact name of registrant as specified in its charter)

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

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

Former name, former address and former fiscal year, if changed since last report: None

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

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of accelerated filer and large accelerated filer in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer ☑ Accelerated filer ☐ Non-accelerated filer ☐

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes ☐ No ☑

Applicable only to corporate issuers

As of July 31, 2006, there were 2,598,763,423 shares outstanding of each of the issuer's classes of common stock.

TABLE OF CONTENTS

Part I – FINANCIAL INFORMATION

ITEM 1. Financial Statements (unaudited)

CONSOLIDATED BALANCE SHEET

(in millions) (unaudited)

	June 30, 2006	December 31, 2005
Assets:		
Investments and financial services assets:		
Fixed maturities:		
Bonds available for sale, at market value (amortized cost: 2006 – $362,825; 2005 – $349,612) (includes hybrid financial instruments: 2006 – $495)	**$362,183**	$359,516
Bonds held to maturity, at amortized cost (market value: 2006 – $21,522; 2005 – $22,047)	**21,510**	21,528
Bond trading securities, at market value (cost: 2006 – $6,565; 2005 – $4,623)	**6,487**	4,636
Equity securities:		
Common stocks available for sale, at market value (cost: 2006 – $12,008; 2005 – $10,125)	**13,829**	12,227
Common and preferred stocks trading, at market value (cost: 2006 – $9,589; 2005 – $7,746)	**10,857**	8,959
Preferred stocks available for sale, at market value (cost: 2006 – $2,464; 2005 – $2,282)	**2,447**	2,402
Mortgage loans on real estate, net of allowance (2006 – $55; 2005 – $54)	**16,180**	14,300
Policy loans	**7,366**	7,039
Collateral and guaranteed loans, net of allowance (2006 – $10; 2005 – $10)	**4,058**	3,570
Financial services assets:		
Flight equipment primarily under operating leases, net of accumulated depreciation (2006 – $8,100; 2005 – $7,419)	**39,307**	36,245
Securities available for sale, at market value (cost: 2006 – $38,386; 2005 – $37,572)	**38,678**	37,511
Trading securities, at market value	**5,165**	6,499
Spot commodities	**797**	92
Unrealized gain on swaps, options and forward transactions	**18,901**	18,695
Trading assets	**1,345**	1,204
Securities purchased under agreements to resell, at contract value	**14,085**	14,547
Finance receivables, net of allowance (2006 – $713; 2005 – $670)	**27,515**	27,995
Securities lending collateral, at market value (which approximates cost)	**68,732**	59,471
Other invested assets	**29,410**	27,267
Short-term investments, at cost (which approximates market value)	**21,186**	15,342
Total investments and financial services assets	**710,038**	679,045
Cash	**2,140**	1,897
Investment income due and accrued	**5,732**	5,727
Premiums and insurance balances receivable, net of allowance (2006 – $869; 2005 – $1,011)	**18,236**	15,333
Reinsurance assets, net of allowance (2006 – $932; 2005 – $992)	**24,271**	24,978
Deferred policy acquisition costs	**38,301**	33,248
Investments in partially owned companies	**1,375**	1,158
Real estate and other fixed assets, net of accumulated depreciation (2006 – $5,307; 2005 – $4,990)	**8,415**	7,446
Separate and variable accounts	**67,596**	63,797
Goodwill	**8,425**	8,093
Other assets	**16,141**	12,329
Total assets	**$900,670**	$853,051

See Accompanying Notes to Consolidated Financial Statements.

CONSOLIDATED BALANCE SHEET *(continued)*

(in millions, except share data) (unaudited)

	June 30, 2006	December 31, 2005
Liabilities:		
Reserve for losses and loss expenses	**$ 78,966**	$ 77,169
Unearned premiums	**26,113**	24,243
Future policy benefits for life and accident and health insurance contracts	**117,645**	108,807
Policyholders' contract deposits	**233,865**	227,027
Other policyholders' funds	**11,157**	10,870
Commissions, expenses and taxes payable	**5,060**	4,769
Insurance balances payable	**4,362**	3,564
Funds held by companies under reinsurance treaties	**3,221**	4,174
Income taxes payable	**5,101**	6,288
Financial services liabilities:		
Borrowings under obligations of guaranteed investment agreements	**21,571**	20,811
Securities sold under agreements to repurchase, at contract value	**7,803**	11,047
Trading liabilities	**2,273**	2,546
Hybrid financial instrument liabilities, at fair value	**6,652**	–
Securities and spot commodities sold but not yet purchased, at market value	**5,727**	5,975
Unrealized loss on swaps, options and forward transactions	**11,956**	12,740
Trust deposits and deposits due to banks and other depositors	**4,542**	4,877
Commercial paper	**9,833**	6,514
Notes, bonds, loans and mortgages payable	**70,561**	71,313
Commercial paper	**3,230**	2,694
Notes, bonds, loans and mortgages payable	**12,851**	7,126
Liabilities connected to trust preferred stock	**1,399**	1,391
Separate and variable accounts	**67,596**	63,797
Securities lending payable	**69,754**	60,409
Minority interest	**6,038**	5,124
Other liabilities (includes hybrid financial instruments: 2006 — $138)	**25,492**	23,273
Total liabilities	**812,768**	766,548
Preferred shareholders' equity in subsidiary companies	**193**	186
Commitments and Contingent Liabilities (See Note 6)		
Shareholders' equity:		
Common stock, $2.50 par value; 5,000,000,000 shares authorized; shares issued 2006 and 2005 – 2,751,327,476	**6,878**	6,878
Additional paid-in capital	**2,533**	2,339
Retained earnings	**78,192**	72,330
Accumulated other comprehensive income (loss)	**2,201**	6,967
Treasury stock, at cost; 2006 – 153,134,393; 2005 – 154,680,704 shares of common stock	**(2,095)**	(2,197)
Total shareholders' equity	**87,709**	86,317
Total liabilities, preferred shareholders' equity in subsidiary companies and shareholders' equity	**$900,670**	$853,051

See Accompanying Notes to Consolidated Financial Statements.

CONSOLIDATED STATEMENT OF INCOME

(in millions, except per share data) (unaudited)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2006	2005	**2006**	2005
Revenues:				
Premiums and other considerations	**$18,303**	$17,536	**$36,545**	$35,216
Net investment income	**5,912**	5,227	**11,739**	10,559
Realized capital gains (losses)	**(214)**	(125)	**(45)**	12
Other revenues	**2,742**	5,265	**5,763**	9,318
Total revenues	**26,743**	27,903	**54,002**	55,105
Benefits and expenses:				
Incurred policy losses and benefits	**13,988**	14,283	**28,988**	29,156
Insurance acquisition and other operating expenses	**7,514**	6,919	**14,980**	13,599
Total benefits and expenses	**21,502**	21,202	**43,968**	42,755
Income before income taxes, minority interest and cumulative effect of an accounting change	**5,241**	6,701	**10,034**	12,350
Income taxes	**1,688**	2,083	**3,123**	3,789
Income before minority interest and cumulative effect of an accounting change	**3,553**	4,618	**6,911**	8,561
Minority interest	**(363)**	(129)	**(560)**	(273)
Income before cumulative effect of an accounting change	**3,190**	4,489	**6,351**	8,288
Cumulative effect of an accounting change, net of tax	**–**	–	**34**	–
Net income	**$ 3,190**	$ 4,489	**$ 6,385**	$ 8,288
Earnings per common share:				
Basic				
Income before cumulative effect of an accounting change	**$ 1.23**	$ 1.73	**$ 2.44**	$ 3.19
Cumulative effect of an accounting change, net of tax	**–**	–	**0.01**	–
Net income	**$ 1.23**	$ 1.73	**$ 2.45**	$ 3.19
Diluted				
Income before cumulative effect of an accounting change	**$ 1.21**	$ 1.71	**$ 2.42**	$ 3.16
Cumulative effect of an accounting change, net of tax	**–**	–	**0.01**	–
Net income	**$ 1.21**	$ 1.71	**$ 2.43**	$ 3.16
Dividends declared per common share	**$ 0.165**	$ 0.125	**$ 0.315**	$ 0.30
Average shares outstanding:				
Basic	**2,606**	2,596	**2,606**	2,596
Diluted	**2,625**	2,623	**2,624**	2,623

See Accompanying Notes to Consolidated Financial Statements.

CONSOLIDATED STATEMENT OF CASH FLOWS

(in millions) (unaudited)

Six Months Ended June 30,	2006	2005
Summary:		
Net cash provided by (used in) operating activities	**$ 6,978**	$ 13,689
Net cash used in investing activities	**(40,048)**	(35,230)
Net cash provided by financing activities	**32,243**	22,097
Effect of exchange rate changes on cash	**1,070**	(827)
Change in cash	**243**	(271)
Cash at beginning of period	**1,897**	2,009
Cash at end of period	**$ 2,140**	$ 1,738
Cash flows from operating activities:		
Net income	**$ 6,385**	$ 8,288
Adjustments to reconcile net income to net cash provided by (used in) operating activities:		
Noncash revenues, expenses, gains and losses included in income:		
Change in:		
General and life insurance reserves	**12,434**	7,562
Premiums and insurance balances receivable and payable – net	**(1,229)**	87
Reinsurance assets	**707**	137
Deferred policy acquisition costs	**(3,150)**	(1,267)
Investment income due and accrued	**(5)**	(91)
Funds held under reinsurance treaties	**(953)**	376
Other policyholders' funds	**287**	52
Income taxes payable	**918**	1,170
Commissions, expenses and taxes payable	**291**	119
Other assets and liabilities – net	**(1,869)**	(235)
Bonds, common and preferred stocks trading, at market value	**(3,749)**	(1,775)
Trading assets and liabilities – net	**(414)**	1,111
Trading securities, at market value	**1,334**	(1,181)
Spot commodities	**(705)**	80
Net unrealized (gain) loss on swaps, options and forward transactions	**(990)**	(788)
Securities purchased under agreements to resell	**462**	13,696
Securities sold under agreements to repurchase	**(3,244)**	(13,084)
Securities and spot commodities sold but not yet purchased, at market value	**(248)**	(534)
Realized capital (gains) losses	**45**	(12)
Equity in income of partially owned companies and other invested assets	**(1,410)**	(899)
Amortization of premium and discount on securities	**201**	187
Depreciation expenses, principally flight equipment	**1,137**	836
Provision for finance receivable losses	**245**	175
Finance receivables held for sale – originations and purchases	**(4,911)**	(5,144)
Finance receivables sold	**5,250**	4,775
Other – net	**159**	48
Total adjustments	**593**	5,401
Net cash provided by (used in) operating activities	**$ 6,978**	$ 13,689

See Accompanying Notes to Consolidated Financial Statements.

CONSOLIDATED STATEMENT OF CASH FLOWS *(continued)*

(in millions) (unaudited)

Six Months Ended June 30,	2006	2005
Cash flows from investing activities:		
Cost of bonds, at market sold	**$ 50,578**	$ 62,719
Cost of bonds, at market matured or redeemed	**8,087**	7,717
Cost of equity securities sold	**6,739**	5,896
Realized capital gains (losses)	**(45)**	12
Purchases of fixed maturities	**(71,965)**	(86,153)
Purchases of equity securities	**(8,615)**	(7,151)
Mortgage, policy, collateral and guaranteed loans granted	**(4,343)**	(2,702)
Repayments of mortgage, policy, collateral and guaranteed loans	**1,648**	1,520
Sales of securities available for sale	**2,608**	1,949
Maturities of securities available for sale	**210**	2,451
Purchases of securities available for sale	**(3,604)**	(7,350)
Sales of flight equipment	**354**	243
Purchases of flight equipment	**(4,171)**	(4,243)
Change in securities lending collateral	**(9,261)**	(7,156)
Net additions to real estate and other fixed assets	**(739)**	(400)
Sales or distributions of other invested assets	**7,814**	5,835
Other invested assets	**(7,970)**	(7,169)
Change in short-term investments	**(6,529)**	1,992
Investments in partially owned companies	**(21)**	(3)
Finance receivables held for investment – originations and purchases	**(7,053)**	(9,267)
Finance receivable principal payments received	**6,230**	6,030
Net cash used in investing activities	**$(40,048)**	$(35,230)
Cash flows from financing activities:		
Receipts from policyholders' contract deposits	**$ 27,069**	$ 26,038
Withdrawals from policyholders' contract deposits	**(20,231)**	(17,032)
Change in trust deposits and deposits due to banks and other depositors	**(335)**	(94)
Change in commercial paper	**2,979**	3,171
Proceeds from notes, bonds, loans and mortgages payable, and hybrid financial instrument liabilities	**22,392**	25,645
Repayments on notes, bonds, loans and mortgages payable, and hybrid financial instrument liabilities	**(9,037)**	(23,903)
Proceeds from guaranteed investment agreements	**6,471**	6,760
Maturities of guaranteed investment agreements	**(5,711)**	(4,880)
Change in securities lending payable	**9,345**	7,156
Proceeds from common stock issued	**63**	36
Cash dividends to shareholders	**(780)**	(641)
Acquisition of treasury stock	**(4)**	(168)
Other – net	**22**	9
Net cash provided by financing activities	**$ 32,243**	$ 22,097
Supplementary information:		
Taxes paid	**$ 2,100**	$ 1,466
Interest paid	**$ 2,870**	$ 2,649

See Accompanying Notes to Consolidated Financial Statements.

CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME (LOSS)

(in millions, except per share data) (unaudited)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2006	2005	**2006**	2005
Comprehensive income (loss):				
Net income	**$ 3,190**	$ 4,489	**$ 6,385**	$ 8,288
Other comprehensive income (loss):				
Unrealized appreciation (depreciation) of investments – net of reclassification adjustments	**(5,734)**	4,817	**(8,333)**	2,282
Deferred income tax benefit (expense) on above changes	**1,743**	(1,759)	**2,843**	(503)
Foreign currency translation adjustments	**520**	(773)	**1,070**	(826)
Deferred income tax benefit (expense) on above changes	**(59)**	497	**(349)**	501
Net derivative gains (losses) arising from cash flow hedging activities	**4**	(80)	**8**	70
Deferred income tax (expense) benefit on above changes	**(16)**	40	**(3)**	(71)
Retirement plan liabilities adjustment, net of tax	**34**	2	**(2)**	(28)
Other comprehensive income (loss)	**(3,508)**	2,744	**(4,766)**	1,425
Comprehensive income (loss)	**$ (318)**	$ 7,233	**$ 1,619**	$ 9,713

See Accompanying Notes to Consolidated Financial Statements.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited)*

1. Financial Statement Presentation

These unaudited condensed consolidated financial statements do not include certain financial information required by U.S. generally accepted accounting principles (GAAP) for complete financial statements and should be read in conjunction with the audited consolidated financial statements and the related notes, included in the Annual Report on Form 10-K/A of American International Group, Inc. (AIG) for the year ended December 31, 2005 (2005 Annual Report on Form 10-K/A).

In the opinion of management, the consolidated financial statements contain the normal recurring adjustments necessary for a fair statement of the results presented herein. Intercompany accounts and transactions have been eliminated. Certain accounts have been reclassified in the 2005 financial statements to conform to their 2006 presentation. See also Note 11 herein.

During the second quarter of 2006, as part of its continuing remediation efforts, AIG identified and recorded an out of period adjustment related to the accounting for certain interests in unit investment trusts in accordance with FIN 46(R), "Consolidation of Variable Interest Entities" and APB Opinion No. 18, "The Equity Method of Accounting for Investments in Common Stock". These investments had previously been accounted for as available for sale securities, with changes in market values being reflected in other comprehensive income, net of deferred income taxes. Beginning with the second quarter of 2006, the changes in market values are included in AIG's net investment income. The adjustment decreased Unrealized appreciation (depreciation) of investments – net of reclassification adjustments, and the related Deferred income tax benefit (expense), in the Consolidated Statement of Comprehensive Income (Loss) by approximately $576 million and approximately $202 million, respectively, for the three and six-month periods ended June 30, 2006 and increased Net investment income by $653 million, increased Incurred policy losses and benefits, related to certain participating policyholder funds, by $77 million, and increased Income taxes by $202 million in the Consolidated Statement of Income for the three and six-month periods ended June 30, 2006. There was no effect on Total shareholders' equity as of June 30, 2006 or December 31, 2005.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

2. Segment Information

AIG identifies its reportable segments by product line consistent with its management structure. AIG's major product and service groupings are general insurance, life insurance & retirement services, financial services and asset management. **The following table summarizes the operations by major operating segment for the three and six-month periods ended June 30, 2006 and 2005:**

Operating Segments	**Three Months Ended June 30,**		**Six Months Ended June 30,**	
(in millions)	**2006**	2005	**2006**	2005
Revenues[(a)]:				
General Insurance[(b)(h)]	**$12,167**	$11,405	**$23,823**	$22,624
Life Insurance & Retirement Services[(c)(h)]	**11,705**	11,517	**24,344**	23,292
Financial Services[(d)]	**1,226**	3,778	**2,841**	6,214
Asset Management[(e)]	**1,621**	1,219	**2,860**	2,596
Other	**24**	(16)	**134**	379
Consolidated	**$26,743**	$27,903	**$54,002**	$55,105
Operating income (loss)[(a)(f)]:				
General Insurance[(h)]	**$ 2,863**	$ 1,885	**$ 5,194**	$ 3,527
Life Insurance & Retirement Services[(g)(h)]	**2,302**	2,324	**4,857**	4,505
Financial Services[(g)]	**(548)**	2,214	**(707)**	3,259
Asset Management	**811**	524	**1,272**	1,114
Other[(i)]	**(187)**	(246)	**(582)**	(55)
Consolidated	**$ 5,241**	$ 6,701	**$10,034**	$12,350

(a) Includes the effect of hedging activities that do not qualify for hedge accounting treatment under FAS 133, including the related foreign exchange gains and losses. For the three-month periods ended June 30, 2006 and 2005, the effect was $(1.08) billion and $1.63 billion, respectively, in revenues and $(1.08) billion and $1.61 billion, respectively, in operating income. For the six-month periods ended June 30, 2006 and 2005, the effect was $(1.30) billion and $2.56 billion, respectively, in revenues and $(1.30) billion and $2.62 billion, respectively, in operating income. These amounts result primarily from interest rate and foreign currency derivatives which are hedging available for sale securities and borrowings.

(b) Represents the sum of General Insurance net premiums earned, net investment income and realized capital gains (losses).

(c) Represents the sum of Life Insurance & Retirement Services GAAP premiums, net investment income and realized capital gains (losses). Included in realized capital gains (losses) is the effect of hedging activities that do not qualify for hedge accounting treatment under FAS 133 and the application of FAS 52 of $(21) million and $(103) million in the three-month periods ended June 30, 2006 and 2005, respectively, and $335 million and $(183) million in the six-month periods ended June 30, 2006 and 2005, respectively.

(d) Represents interest, lease and finance charges.

(e) Represents management and advisory fees and net investment income with respect to Guaranteed Investment Contracts (GICs).

(f) Represents income before income taxes, minority interest and cumulative effect of an accounting change.

(g) Results of operations of AIG Credit Card Company (Taiwan) are shared equally by the Life Insurance & Retirement Services segment and the Financial Services segment. Additional allowances of $44 million were recorded in the first quarter of 2006, by each segment, for losses in these credit card operations.

(h) Includes the effect of an out of period adjustment related to the accounting for certain interests in unit investment trusts. For the three and six-month periods ended June 30, 2006 the effect was an increase of $432 million in revenues and operating income for General Insurance and an increase of $221 million and $144 million in revenues and operating income, respectively, for Life Insurance & Retirement Services.

(i) The operating loss for the Other category is as follows:

	Three Months Ended June 30,		**Six Months Ended June 30,**	
(in millions)	**2006**	2005	**2006**	2005
Operating income (loss):				
Equity earnings in unconsolidated subsidiaries	**$ 111**	$ 36	**$ 130**	$ 96
Compensation expense – SICO Plans	**(14)**	(60)	**(90)**	(67)
Compensation expense – C.V. Starr tender offer	**–**	–	**(54)**	–
Interest expense	**(223)**	(127)	**(406)**	(251)
Unallocated corporate expenses	**(71)**	(108)	**(261)**	(195)
Realized capital gains (losses)	**24**	(16)	**134**	379
Other miscellaneous, net	**(14)**	29	**(35)**	(17)
Total Other	**$ (187)**	$ (246)	**$ (582)**	$ (55)

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

2. Segment Information *(continued)*

Each of the General Insurance sub-segments is comprised of groupings of major products and services as follows: Domestic Brokerage Group is comprised of domestic commercial insurance products and services; Transatlantic is comprised of reinsurance products and services sold to other general insurance companies; Personal Lines are comprised of general insurance products and services sold to individuals; Mortgage Guaranty is comprised of products insuring against losses arising under certain loan agreements; and Foreign General is comprised of general insurance products sold overseas.

The following table summarizes AIG's General Insurance operations by major internal reporting unit for the three and six-month periods ended June 30, 2006 and 2005:

General Insurance	**Three Months Ended June 30,**		**Six Months Ended June 30,**	
(in millions)	**2006**	2005	**2006**	2005
Revenues:				
Domestic Brokerage Group	**$ 6,605**	$ 6,241	**$13,160**	$12,530
Transatlantic	**1,015**	948	**2,031**	1,930
Personal Lines	**1,223**	1,209	**2,438**	2,380
Mortgage Guaranty	**212**	173	**410**	342
Foreign General[(a)]	**3,112**	2,835	**5,782**	5,437
Reclassifications and Eliminations	**–**	(1)	**2**	5
Total General Insurance	**$12,167**	$11,405	**$23,823**	$22,624
Operating Income[(b)]:				
Domestic Brokerage Group	**$ 1,534**	$ 805	**$ 2,891**	$ 1,518
Transatlantic	**143**	99	**284**	213
Personal Lines	**118**	102	**219**	211
Mortgage Guaranty	**107**	109	**216**	213
Foreign General[(a)]	**961**	771	**1,582**	1,367
Reclassifications and Eliminations	**–**	(1)	**2**	5
Total General Insurance	**$ 2,863**	$ 1,885	**$ 5,194**	$ 3,527

[(a)] *Includes the effect of an out of period adjustment related to the accounting for certain interests in unit investment trusts. For the three and six-month periods ended June 30, 2006 the effect was an increase of $412 million in revenues and operating income.*

[(b)] *Includes additional (reduction in) losses incurred and net reinstatement premiums primarily related to prior year catastrophes of $(51) million and $27 million, in the three-month periods ended June 30, 2006 and 2005, respectively. Such losses and premiums were $48 million and $198 million in the six-month periods ended June 30, 2006 and 2005, respectively.*

Life Insurance & Retirement Services is comprised of two major groupings of products and services: insurance-oriented products and services and retirement savings products and services. Substantially all of the retirement savings products are reported in the VALIC, AIG Annuity and AIG SunAmerica sub-segment.

The following table summarizes AIG's Life Insurance & Retirement Services operations by major internal reporting unit for the three and six-month periods ended June 30, 2006 and 2005:

Life Insurance & Retirement Services	**Three Months Ended June 30,**		**Six Months Ended June 30,**	
(in millions)	**2006**	2005	**2006**	2005
Revenues:				
Foreign:				
AIA, AIRCO and Nan Shan[(a) (e)]	**$ 4,165**	$ 3,858	**$ 8,517**	$ 7,924
ALICO, AIG Star Life and AIG Edison Life[(b)]	**3,652**	3,609	**7,747**	7,128
Philamlife and Other	**153**	127	**277**	257
Domestic:				
AGLA and AG Life[(c)]	**2,222**	2,114	**4,589**	4,502
VALIC, AIG Annuity and AIG SunAmerica[(d)]	**1,513**	1,809	**3,214**	3,481
Total Life Insurance & Retirement Services	**$11,705**	$11,517	**$24,344**	$23,292
Operating Income:				
Foreign:				
AIA, AIRCO and Nan Shan[(a) (e)]	**$ 736**	$ 649	**$ 1,436**	$ 1,237
ALICO, AIG Star Life and AIG Edison Life[(b)]	**955**	798	**1,913**	1,394
Philamlife and Other	**30**	17	**41**	33
Domestic:				
AGLA and AG Life[(c)]	**235**	240	**601**	706
VALIC, AIG Annuity and AIG SunAmerica[(d)]	**346**	620	**866**	1,135
Total Life Insurance & Retirement Services	**$ 2,302**	$ 2,324	**$ 4,857**	$ 4,505

(a) Represents the operations of American International Assurance Company, Limited together with American International Assurance Company (Bermuda) Limited (AIA), American International Reinsurance Company, Ltd. (AIRCO), and Nan Shan Life Insurance Company, Ltd. (Nan Shan). Revenues and operating income include realized capital gains (losses) of $(15) million and $110 million for the three-month periods ended June 30, 2006 and 2005, respectively, and $198 million and $176 million for the six-month periods ended June 30, 2006 and 2005, respectively. The effects of FAS 133 and the application of FAS 52 included in realized capital gains (losses) are losses of $(131) million and gains of $50 million for the three-month periods ended June 30, 2006 and 2005, respectively, and gains of $112 million and $61 million for the six-month periods ended June 30, 2006 and 2005, respectively. Includes $44 million in additional allowances for losses recorded in the first quarter of 2006 from AIG Credit Card Company (Taiwan).

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

2. Segment Information *(continued)*

(b) Represents the operations of American Life Insurance Company (ALICO), AIG Star Life Insurance Co., Ltd. (AIG Star Life), and AIG Edison Life Insurance Company (AIG Edison Life). Revenues and operating income include realized capital gains of $162 million and $11 million for the three-month periods ended June 30, 2006 and 2005, respectively, and gains of $311 million and losses of $(128) million for the six-month periods ended June 30, 2006 and 2005, respectively. The effects of FAS 133 and the application of FAS 52 included in realized capital gains (losses) are gains of $111 million and losses of $(78) million for the three-month periods ended June 30, 2006 and 2005, respectively, and gains of $157 million and losses of $(263) million for the six-month periods ended June 30, 2006 and 2005, respectively.

(c) Includes the life operations of American General Life Insurance Company (AG Life), AIG Life Insurance Company and American International Life Assurance Company of New York. Also includes the operations of American General Life and Accident Insurance Company (AGLA). Revenues and operating income include realized capital losses of $(75) million and $(135) million for the three-month periods ended June 30, 2006 and 2005, respectively, and losses of $(67) million and $(63) million for the six-month periods ended June 30, 2006 and 2005, respectively. The effects of FAS 133 and the application of FAS 52 included in realized capital gains (losses) are gains of $29 million and losses of $(171) million for the three-month periods ended June 30, 2006 and 2005, respectively, and gains of $115 million and losses of $(66) million for the six-month periods ended June 30, 2006 and 2005, respectively.

(d) "AIG SunAmerica" represents the annuity operations of AIG SunAmerica Life Assurance Company, as well as those of First SunAmerica Life Insurance Company and SunAmerica Life Insurance Company. Also includes the operations of The Variable Annuity Life Insurance Company (VALIC) and AIG Annuity Insurance Company (AIG Annuity). Revenues and operating income include realized capital losses of $(307) million and gains of $57 million for the three-month periods ended June 30, 2006 and 2005, respectively, and losses of $(509) million and $(22) million for the six-month periods ended June 30, 2006 and 2005, respectively. The effects of FAS 133 and the application of FAS 52 included in realized capital gains (losses) are losses of $(42) million and gains of $96 million for the three month periods ended June 30, 2006 and 2005, respectively, and losses of $(36) million and gains of $85 million for the six-month periods ended June 30, 2006 and 2005, respectively.

(e) Includes the effect of an out of period adjustment related to the accounting for certain interests in unit investment trusts. For the three and six-month periods ended June 30, 2006 the effect was an increase of $221 million in revenues and $144 million in operating income.

The following table summarizes AIG's Financial Services operations by major internal reporting unit for the three and six-month periods ended June 30, 2006 and 2005:

Financial Services	**Three Months Ended June 30,**		**Six Months Ended June 30,**	
(in millions)	**2006**	2005	**2006**	2005
Revenues[(a)]:				
Aircraft Finance[(b)]	**$1,042**	$ 891	**$ 2,007**	$1,718
Capital Markets[(c)(d)]	**(788)**	1,975	**(1,088)**	2,731
Consumer Finance[(e)]	**939**	891	**1,863**	1,724
Other	**33**	21	**59**	41
Total Financial Services	**$1,226**	$3,778	**$ 2,841**	$6,214
Operating income (loss)[(a)]:				
Aircraft Finance	**$ 189**	$ 124	**$ 318**	$ 311
Capital Markets[(d)]	**(952)**	1,836	**(1,422)**	2,456
Consumer Finance[(f)]	**199**	238	**374**	459
Other	**16**	16	**23**	33
Total Financial Services	**$ (548)**	$2,214	**$ (707)**	$3,259

(a) Includes the effect of hedging activities that do not qualify for hedge accounting treatment under FAS 133, including the related foreign exchange gains and losses. For the three and six-month periods ended June 30, 2005, the effect was $(64) million and $(49) million, respectively, in operating income for Aircraft Finance. During 2006, Aircraft Finance's derivative gains and losses are reported as part of the Other category and not reported in Aircraft Finance's operating income. For the three-month periods ended June 30, 2006 and 2005, the effect was $(1.16) billion and $1.70 billion in both revenues and operating income, respectively, for Capital Markets. For the six-month periods ended June 30, 2006 and 2005, the effect was $(1.84) billion and $2.16 billion in both revenues and operating income, respectively, for Capital Markets. These amounts result primarily from interest rate and foreign currency derivatives which are hedging available for sale securities and borrowings.

(b) Revenues are primarily from International Lease Finance Corporation (ILFC) aircraft lease rentals.

(c) Revenues, shown net of interest expense, are primarily from hedged financial positions entered into in connection with counterparty transactions and the effect of hedging activities that do not qualify for hedge accounting treatment under FAS 133 described in (a) above.

(d) Certain transactions entered into by AIGFP generate tax credits and benefits which are included in income taxes in the consolidated statement of income. The amount of such tax credits and benefits for the three-month periods ended June 30, 2006 and 2005 are $8 million and $21 million, respectively. The amount of such tax credits and benefits for the six-month periods ended June 30, 2006 and 2005 are $26 million and $40 million, respectively.

(e) Revenues are primarily finance charges.

(f) Includes $44 million in additional allowances for losses recorded in the first quarter of 2006 from AIG Credit Card Company (Taiwan).

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

2. Segment Information *(continued)*

The following table summarizes AIG's Asset Management revenues and operating income for the three and six-month periods ended June 30, 2006 and 2005:

Asset Management *(in millions)*	**Three Months Ended June 30,** **2006**	2005	**Six Months Ended June 30,** **2006**	2005
Revenues:				
Guaranteed Investment Contracts	**$ 850**	$ 903	**$1,672**	$1,799
Institutional Asset Management	**619**	178	**898**	497
Brokerage Services and Mutual Funds	**73**	62	**146**	125
Other	**79**	76	**144**	175
Total Asset Management	**$1,621**	$1,219	**$2,860**	$2,596
Operating income:				
Guaranteed Investment Contracts[(a)]	**$ 242**	$ 326	**$ 460**	$ 645
Institutional Asset Management[(b)(c)]	**473**	108	**632**	269
Brokerage Services and Mutual Funds	**21**	17	**44**	30
Other	**75**	73	**136**	170
Total Asset Management	**$ 811**	$ 524	**$1,272**	$1,114

(a) Includes the effect of hedging activities that do not qualify for hedge accounting treatment under FAS 133, including the related foreign exchange gains and losses. For the three and six-month periods ended June 30, 2005, the effect was $47 million and $109 million, respectively, in operating income. During 2006, these derivative gains and losses are reported as part of the Other category, and not reported in Asset Management operating income.

(b) Includes the full results of certain AIG managed private equity and real estate funds that are consolidated pursuant to FIN 46(R), "Consolidation of Variable Interest Entities". Also includes $183 million and $37 million for the three-month periods ended June 30, 2006 and 2005, respectively, and $210 million and $112 million for the six-month periods ended June 30, 2006 and 2005, respectively, of third-party limited partner earnings offset in minority interest expense, which is not a component of operating income.

(c) Includes the full results of certain AIG managed partnerships that are consolidated effective January 1, 2006 pursuant to EITF 04-5, "Determining Whether a General Partner, or the General Partners as a Group, Controls a Limited Partnership or Similar Entity When the Limited Partners Have Certain Rights." For the three and six-month periods ended June 30, 2006, operating income includes $87 million and $156 million, respectively, of third-party limited partner earnings offset in minority interest expense, which is not a component of operating income.

3. Earnings Per Share

Earnings per share of AIG are based on the weighted average number of common shares outstanding during the period. See also Note 10 herein.

Computation of Earnings Per Share (EPS):

(in millions, except per share data)	**Three Months Ended June 30,** **2006**	2005	**Six Months Ended June 30,** **2006**	2005
Numerator for earnings per share:				
Income before cumulative effect of an accounting change	**$3,190**	$4,489	**$6,351**	$8,288
Cumulative effect of an accounting change, net of tax	**–**	–	**34**	–
Net income applicable to common stock for basic EPS	**$3,190**	$4,489	**$6,385**	$8,288
Interest on contingently convertible bonds, net of tax[(a)]	**3**	2	**6**	5
Net income applicable to common stock for diluted EPS	**$3,193**	$4,491	**$6,391**	$8,293
Cumulative effect of an accounting change, net of tax	**–**	–	**34**	–
Income before cumulative effect of an accounting change applicable to common stock for diluted EPS	**$3,193**	$4,491	**$6,357**	$8,293
Denominator for earnings per share:				
Weighted-average shares outstanding used in the computation of EPS:				
Common stock issued	**2,752**	2,752	**2,752**	2,752
Common stock in treasury	**(153)**	(156)	**(153)**	(156)
Deferred shares	**7**	–	**7**	–

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

3. Earnings Per Share *(continued)*

(in millions, except per share data)	Three Months Ended June 30, 2006	Three Months Ended June 30, 2005	Six Months Ended June 30, 2006	Six Months Ended June 30, 2005
Weighted-average shares outstanding — basic	**2,606**	2,596	**2,606**	2,596
Incremental shares from potential common stock:				
Weighted-average number of shares arising from outstanding employee stock plans (treasury stock method)[(b)]	**10**	18	**9**	18
Contingently convertible bonds[(a)]	**9**	9	**9**	9
Weighted-adjusted average shares outstanding — diluted[(b)]	**2,625**	2,623	**2,624**	2,623
Earnings per share:				
Basic:				
Income before cumulative effect of an accounting change	**$ 1.23**	$ 1.73	**$ 2.44**	$ 3.19
Cumulative effect of an accounting change, net of tax	**–**	–	**0.01**	–
Net Income	**$ 1.23**	$ 1.73	**$ 2.45**	$ 3.19
Diluted:				
Income before cumulative effect of an accounting change	**$ 1.21**	$ 1.71	**$ 2.42**	$ 3.16
Cumulative effect on an accounting change, net of tax	**–**	–	**0.01**	–
Net income	**$ 1.21**	$ 1.71	**$ 2.43**	$ 3.16

(a) Assumes conversion of contingently convertible bonds due to the adoption of EITF Issue No. 04-8 "Accounting Issues Related to Certain Features of Contingently Convertible Debt and the Effect on Diluted Earnings per Share."

(b) Certain share equivalents arising from employee stock plans were not included in the computation of diluted earnings per share where the exercise price of the options exceeded the average market price and would have been antidilutive. The number of share equivalents excluded were 15 million and 23 million for the first six months of 2006 and 2005, respectively.

From time to time, AIG may buy shares of its common stock in the open market for general corporate purposes, including to satisfy its obligations under various employee benefit plans. At June 30, 2006 and December 31, 2005, an additional 36,542,700 shares could be purchased under the then current authorization by AIG's Board of Directors. Although AIG has authorization to purchase additional shares, AIG has not repurchased shares in 2006. During the six months ended June 30, 2005, AIG purchased in the open market 2,477,100 shares of its common stock.

4. Benefits Provided by Starr International Company, Inc. and C.V. Starr & Co., Inc.

Starr International Company, Inc. (SICO) has provided a series of two-year Deferred Compensation Profit Participation Plans (SICO Plans) to certain AIG employees. The SICO Plans came into being in 1975 when the voting shareholders and Board of Directors of SICO, a private holding company whose principal asset is AIG common stock, decided that a portion of the capital value of SICO should be used to provide an incentive plan for the current and succeeding managements of all American International companies, including AIG.

None of the costs of the various benefits provided under the SICO Plans has been paid by AIG, although AIG has recorded a charge to reported earnings for the deferred compensation amounts paid to AIG employees by SICO, with an offsetting amount credited to additional paid-in capital reflecting amounts deemed contributed by SICO. The SICO Plans provide that shares currently owned by SICO are set aside by SICO for the benefit of the participant and distributed upon retirement. The SICO Board of Directors currently may permit an early payout of units under certain circumstances. Prior to payout, the participant is not entitled to vote, dispose of or receive dividends with respect to such shares, and shares are subject to forfeiture under certain conditions, including but not limited to the participant's voluntary termination of employment with AIG prior to normal retirement age. Under the SICO Plans, SICO's Board of Directors may elect to pay a participant cash in lieu of shares of AIG common stock. Following notification from SICO to participants in the SICO Plans that it will settle specific future awards under the SICO Plans with shares rather than cash, AIG modified its accounting for the SICO Plans from variable to fixed measurement accounting, although variable accounting will continue to be applied where SICO makes cash payments pursuant to elections made prior to March 2005. AIG gave effect to this change in settlement method beginning on December 9, 2005, the date of SICO's notice to participants in the SICO Plans. See also Note 6(f) herein.

Compensation expense with respect to the SICO Plans aggregated $14 million and $60 million for the three-month periods ended June 30, 2006 and 2005, respectively, and $90 million and $67 million for the six-month periods ended June 30, 2006 and 2005, respectively. Compensation expense in the first quarter of 2006 included various out of period

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

4. Benefits Provided by Starr International Company, Inc. *(continued)*

adjustments totaling $61 million, primarily relating to stock-splits and other miscellaneous items. See also Note 10 herein.

In January 2006, C.V. Starr & Co., Inc. (Starr) completed its tender offer to purchase Starr interests from AIG employees. In conjunction with AIG's adoption of FAS 123R, Starr is considered to be an "economic interest holder" in AIG. As a result, compensation expense of $54 million recorded in the first quarter with respect to the Starr offer, was included in the first six months of 2006.

As a result of its changing relationship with Starr and SICO, AIG has established new executive compensation plans to replace the SICO plans and investment opportunities previously provided by Starr. The replacement plans include both share-based plans and cash-based plans. In addition, these replacement plans generally include performance as well as service conditions. See also Note 10 herein.

5. Ownership and Transactions With Related Parties

(a) ***Ownership:*** According to the Schedule 13D filed on May 26, 2006 by Starr, SICO, Edward E. Matthews, Maurice R. Greenberg, the Maurice R. and Corinne P. Greenberg Family Foundation, Inc., the Universal Foundation, Inc. and the Maurice R. and Corinne P. Greenberg Joint Tenancy Company, LLC, these reporting persons may be deemed to beneficially own 393,157,543 shares of common stock. Based on the shares of common stock outstanding as of July 31, 2006, this ownership represents approximately 15 percent of the voting stock of AIG.

(b) ***Transactions with Related Parties:*** In the ordinary course of business during the first six months of 2006, AIG and its subsidiaries paid commissions to Starr and its subsidiaries for the production and management of insurance business. As of July 25, 2006, none of the Starr agencies serve as agents for AIG companies. There were no significant receivables from/payables to related parties at June 30, 2006.

6. Commitments and Contingent Liabilities

In the normal course of business, various commitments and contingent liabilities are entered into by AIG and certain of its subsidiaries. In addition, AIG guarantees various obligations of certain subsidiaries.

(a) AIG and certain of its subsidiaries become parties to derivative financial instruments with market risk resulting from both dealer and end user activities and to reduce currency, interest rate, equity and commodity exposures. These instruments are carried at their estimated fair values in the consolidated balance sheet. The vast majority of AIG's derivative activity is transacted by AIGFP. (See also Note 20 of Notes to Consolidated Financial Statements in AIG's 2005 Annual Report on Form 10-K/A.)

(b) Securities sold, but not yet purchased and spot commodities sold but not yet purchased represent obligations of AIGFP to deliver specified securities and spot commodities at their contracted prices. AIGFP records a liability to repurchase the securities and spot commodities in the market at prevailing prices.

AIG has issued unconditional guarantees with respect to the prompt payment, when due, of all present and future payment obligations and liabilities of AIGFP arising from transactions entered into by AIGFP.

(c) At June 30, 2006, ILFC had committed to purchase 266 new aircraft deliverable from 2006 through 2015 at an estimated aggregate purchase price of $18.9 billion and had options to purchase 13 new aircraft at an estimated aggregate purchase price of $1.4 billion. ILFC will be required to find customers for any aircraft acquired, and it must arrange financing for portions of the purchase price of such equipment.

(d) AIG and its subsidiaries, in common with the insurance industry in general, are subject to litigation, including claims for punitive damages, in the normal course of their business. The trend of increasing jury awards and settlements makes it difficult to assess the ultimate outcome of such litigation.

Although AIG regularly reviews the adequacy of the established reserve for losses and loss expenses, there can be no assurance that AIG's ultimate loss reserves will not develop adversely and materially exceed AIG's current loss reserves. Estimation of ultimate net losses, loss expenses and loss reserves is a complex process for long-tail casualty lines of business, which include excess and umbrella liability, directors and officers liability (D&O), professional liability, medical malpractice, workers compensation, general liability, products liability and related classes, as well as for asbestos and environmental exposures. Generally, actual historical loss development factors are used to project future loss development. However, there can be no assurance that future loss development patterns will be the same as in the past. Moreover, any deviation in loss cost trends or in loss development factors might not be discernible for an extended period of time subsequent to the recording of the initial loss reserve estimates for any accident year. Thus, there is the potential for reserves with respect to a number of years to be significantly affected by changes in loss cost trends or loss development factors that were relied upon in setting the reserves. These changes in loss trends or loss development factors could be attributable to changes in inflation in labor and material costs or in the judicial environment, or in other social or economic phenomena affecting claims.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

6. Commitments and Contingent Liabilities *(continued)*

(e) SAI Deferred Compensation Holdings, Inc., a wholly-owned subsidiary of AIG, has established a deferred compensation plan for registered representatives of certain AIG subsidiaries, pursuant to which participants have the opportunity to invest deferred commissions and fees on a notional basis. The value of the deferred compensation fluctuates with the value of the deferred investment alternatives chosen. AIG has provided a full and unconditional guarantee of the obligations of SAI Deferred Compensation Holdings, Inc. to pay the deferred compensation under the plan.

(f) On June 27, 2005, AIG entered into an agreement pursuant to which AIG agrees, subject to certain conditions, to make any payment that is not promptly paid with respect to the benefits accrued by certain employees of AIG and its subsidiaries under the SICO Plans (as defined in Note 4).

(g) AIG and certain of its subsidiaries have been named defendants in two putative class actions in state court in Alabama that arise out of the 1999 settlement of class and derivative litigation involving Caremark Rx, Inc. (Caremark). An excess policy issued by a subsidiary of AIG with respect to the 1999 litigation was expressly stated to be without limit of liability. In the current actions, plaintiffs allege that the judge approving the 1999 settlement was misled as to the extent of available insurance coverage and would not have approved the settlement had he known of the existence and/or unlimited nature of the excess policy. They further allege that AIG, its subsidiaries, and Caremark are liable for fraud and suppression for misrepresenting and/or concealing the nature and extent of coverage. In their complaint, plaintiffs request compensatory damages for the 1999 class in the amount of $3.2 billion, plus punitive damages. AIG and its subsidiaries deny the allegations of fraud and suppression and have asserted, *inter alia*, that information concerning the excess policy was publicly disclosed months prior to the approval of the settlement. AIG and its subsidiaries further assert that the current claims are barred by the statute of limitations and that plaintiffs' assertions that the statute was tolled cannot stand against the public disclosure of the excess coverage. Plaintiffs, in turn, have asserted that the disclosure was insufficient to inform them of the nature of the coverage and did not start the running of the statute of limitations. On January 28, 2005, the Alabama trial court determined that one of the current actions may proceed as a class action on behalf of the 1999 classes that were allegedly defrauded by the settlement. AIG, its subsidiaries, and Caremark are seeking appellate relief from the Alabama Supreme Court. AIG cannot now estimate either the likelihood of its prevailing in these actions or the potential damages in the event liability is determined.

(h) On December 30, 2004, an arbitration panel issued its ruling in connection with a 1998 workers compensation quota share reinsurance agreement under which Superior National Insurance Company, among others, was reinsured by The United States Life Insurance Company in the City of New York (USLIFE), a subsidiary of American General Corporation. In its 2-1 ruling the arbitration panel refused to rescind the contract as requested by USLIFE. Instead, the panel reformed the contract to reduce USLIFE's participation by ten percent. USLIFE is pursuing certain reinsurance recoverables in connection with the contract. Further, the arbitration ruling established a second phase of arbitration for USLIFE to present its challenges to certain cessions to the contract. AIG holds a reserve of approximately $374 million related to this matter as of June 30, 2006.

(i) Regulators from several states have commenced investigations into insurance brokerage practices related to contingent commissions and other broker-related conduct, such as alleged bid rigging. Various parties, including insureds and shareholders, have also asserted putative class action and other claims against AIG or its subsidiaries alleging, among other things, violations of the antitrust and federal securities laws, and AIG expects that additional claims may be made.

In February 2006, AIG reached a resolution of claims and matters under investigation with the United States Department of Justice (DOJ), the Securities and Exchange Commission (SEC), the Office of the New York Attorney General (NYAG) and the New York State Department of Insurance (DOI). The settlements resolved outstanding litigation filed by the SEC, NYAG and DOI against AIG and concluded negotiations with these authorities and the DOJ in connection with the accounting, financial reporting and insurance brokerage practices of AIG and its subsidiaries, as well as claims relating to the underpayment of certain workers compensation premium taxes and other assessments. In the fourth quarter of 2005 AIG recorded an after-tax charge of $1.15 billion for the settlements.

As a result of these settlements, AIG made payments or placed amounts in escrow in the first six months of 2006 totaling approximately $1.64 billion, $225 million of which represented fines and penalties. Amounts held in escrow totaling $685 million, including interest thereon, are included in other assets and other liabilities at June 30, 2006. A substantial portion of the money will be available to resolve claims asserted in various regulatory and civil proceedings, including shareholder lawsuits.

Also, as part of the settlements, AIG has agreed to retain for a period of three years an independent consultant who will conduct a review that will include the adequacy of AIG's internal control over financial reporting and the remediation plan that AIG has implemented as a result of its own internal review.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

6. Commitments and Contingent Liabilities *(continued)*

Various federal and state regulatory agencies are reviewing certain transactions and practices of AIG and its subsidiaries in connection with industry-wide and other inquiries. AIG has cooperated, and will continue to cooperate, in producing documents and other information in response to the subpoenas.

A number of lawsuits have been filed regarding the subject matter of the investigations of insurance brokerage practices, including derivative actions, individual actions and class actions under the federal securities laws, Racketeer Influenced and Corrupt Organizations Act (RICO), Employee Retirement Income Security Act (ERISA) and state common and corporate laws in both federal and state courts, including the United States District Court for the Southern District of New York (Southern District of New York), in the Commonwealth of Massachusetts Superior Court and in Delaware Chancery Court. All of these actions generally allege that AIG and its subsidiaries violated the law by allegedly concealing a scheme to "rig bids" and "steer" business between insurance companies and insurance brokers.

Since October 19, 2004, AIG or its subsidiaries have been named as a defendant in sixteen complaints that were filed in federal court and two that were originally filed in state court (Massachusetts and Florida) and removed to federal court. These cases generally allege that AIG and its subsidiaries violated federal and various state antitrust laws, as well as federal RICO laws, various state deceptive and unfair practice laws and certain state laws governing fiduciary duties. The alleged basis of these claims is that there was a conspiracy between insurance companies and insurance brokers with regard to the use of contingent commission agreements, bidding practices, and other broker-related conduct concerning coverage in certain sectors of the insurance industry. The Judicial Panel on Multidistrict Litigation entered an order on February 17, 2005, consolidating most of these cases and transferring them to the United States District Court for the District of New Jersey (District of New Jersey). The remainder of these cases have been transferred to the District of New Jersey. On August 15, 2005, the plaintiffs in the multidistrict litigation filed a Corrected First Consolidated Amended Commercial Class Action Complaint, which, in addition to the previously named AIG defendants, names new AIG subsidiaries as defendants. Also on August 15, 2005, AIG and two subsidiaries were named as defendants in a Corrected First Consolidated Amended Employee Benefits Class Action Complaint filed in the District of New Jersey, which asserts similar claims with respect to employee benefits insurance and a claim under ERISA on behalf of putative classes of employers and employees.

On November 29, 2005, the AIG defendants, along with other insurer defendants and the broker defendants filed motions to dismiss both the Commercial and Employee Benefits Complaints. Plaintiffs have filed a motion for class certification in the consolidated action, in response to which defendants have filed an opposition. On April 4, 2006, a complaint against AIG and several of its subsidiaries was filed in the United States District Court for the Northern District of Georgia alleging claims similar to what was alleged in the consolidated complaint. A conditional transfer order was issued on May 31, 2006. In addition, complaints were filed against AIG and several of its subsidiaries in Massachusetts and Florida state courts, which have both been stayed. In the Florida action, the plaintiff has filed a petition for a writ of certiorari with the District Court of Appeals of the State of Florida, Fourth District with respect to the stay order. On February 9, 2006, a complaint against AIG and several of its subsidiaries was filed in Texas state court, making claims similar to those in the federal cases above. On April 17, 2006, the AIG defendants moved to stay this action pending resolution of the consolidated action.

In April and May 2005, amended complaints were filed in the consolidated derivative and securities cases, as well as in one of the ERISA lawsuits, pending in the Southern District of New York adding allegations concerning AIG's accounting treatment for non-traditional insurance products.

In September 2005, a second amended complaint was filed in the consolidated securities cases adding allegations concerning AIG's first restatement of its financial statements described in the 2005 Annual Report on Form 10-K (the "First Restatement"), and a new securities action complaint was filed in the Southern District of New York, asserting claims premised on the same allegations made in the consolidated cases. In April 2006, motions to dismiss were denied in the securities actions. AIG filed answers in both securities actions in June 2006, as did other defendants.

Also in September 2005, a class action complaint was filed to consolidate the ERISA cases pending in the Southern District of New York. Motions to dismiss in the consolidated action were filed in January 2006.

In April 2005, new derivative actions were filed in Delaware Chancery Court, and in July and August 2005, two new derivative actions were filed in the Southern District of New York asserting claims duplicative of the claims made in the consolidated derivative action.

In July 2005, a second amended complaint was filed in the consolidated derivative case in the Southern District of New York, expanding upon accounting-related allegations, based upon the First Restatement. In June 2005, the derivative cases in Delaware were consolidated and, in August 2005, an amended consolidated complaint was filed. AIG's

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

6. Commitments and Contingent Liabilities *(continued)*

Board of Directors has appointed a special committee of independent directors to review the matters asserted in the derivative complaints. The courts have approved agreements staying the derivative cases pending in the Southern District of New York and in Delaware Chancery Court while the special committee of independent directors performs its work. In September 2005, a shareholder filed suit in Delaware Chancery Court seeking documents relating to some of the allegations made in the derivative suits. The court approved a stipulation dismissing that action on May 15, 2006.

On June 20, 2006, SICO filed suit in Delaware Chancery Court seeking the inspection of certain books and records of AIG.

In late 2002, a derivative action was filed in Delaware Chancery Court in connection with AIG's transactions with certain entities affiliated with Starr and SICO. In May 2005, the plaintiff filed an amended complaint which adds additional claims premised on allegations relating to insurance brokerage practices and AIG's non-traditional insurance products. On February 16, 2006, the Delaware Chancery Court entered an order dismissing the litigation with prejudice with respect to AIG's outside directors and dismissing the claims against the remaining AIG defendants without prejudice. In response to an order, dated July 5, 2006, dismissing certain of its claims, the plaintiff filed a second amended complaint on July 21, 2006, which adds additional claims against Starr.

AIG cannot predict the outcome of the matters described above or estimate the potential costs related to these matters and, accordingly, no reserve is being established in AIG's financial statements at this time. In the opinion of AIG management, AIG's ultimate liability for the matters referred to above is not likely to have a material adverse effect on AIG's consolidated financial condition, although it is possible that the effect would be material to AIG's consolidated results of operations for an individual reporting period.

(j) On July 8, 2005, SICO filed a complaint against AIG in the Southern District of New York. The complaint alleges that AIG is in the possession of items, including artwork, which SICO claims it owns, and seeks an order causing AIG to release those items as well as actual, consequential, punitive and exemplary damages. On September 27, 2005, AIG filed its answer to SICO's complaint denying SICO's allegations and asserting counter-claims for breach of contract, unjust enrichment, conversion and breach of fiduciary duty relating to SICO's breach of its commitment to use its AIG shares for the benefit of AIG and its employees. On October 17, 2005, SICO replied to AIG's counter-claims and additionally sought a judgment declaring that SICO is neither a control person nor an affiliate of AIG for purposes of Schedule 13D under the Securities Exchange Act of 1934, as amended (the Exchange Act), and Rule 144 under the Securities Act of 1933, as amended (the Securities Act), respectively. AIG responded to the SICO claims on November 7, 2005.

(k) AIG understands that some of its employees have received Wells notices in connection with previously disclosed SEC investigations of certain of AIG's transactions or accounting practices. Under SEC procedures, a Wells notice is an indication that the SEC staff has made a preliminary decision to recommend enforcement action that provides recipients with an opportunity to respond to the SEC staff before a formal recommendation is finalized. AIG anticipates that additional current and former employees could receive similar notices in the future as the regulatory investigations proceed.

(l) AIG generates income tax credits as a result of investing in synthetic fuel production. Tax credits generated from the production and sale of synthetic fuel under the Internal Revenue Code are subject to an annual phase-out provision that is based on the average wellhead price of domestic crude oil. The price range within which the tax credits are phased-out was originally established in 1980 and is adjusted annually for inflation. Depending on the price of domestic crude oil for a particular year, all or a portion of the tax credits generated in that year might be eliminated. Tax credits reflected in the income tax provision for the first six months of 2006 have been reduced to reflect an estimated phase-out of the tax credits from 2006 synthetic fuel production based on the observed price of domestic crude oil. Since the phase-out of tax credits from 2006 synthetic fuel production will depend on the average wellhead price of domestic crude oil for the entire 2006 calendar year, it is not possible to determine the extent to which the 2006 tax credits actually will be phased-out. As a result, the actual level of tax credits from 2006 synthetic fuel production may be higher or lower than the current estimate. AIG evaluates the production levels of its synthetic fuel production facilities in light of the risk of phase-out of the associated tax credits. As a result of the current high domestic crude oil prices, AIG has determined to reduce its production levels for the month of August 2006 and intends to continue to evaluate and possibly adjust production levels in light of this risk for the remainder of 2006. Regardless of oil prices, the tax credits expire after 2007.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

7. Employee Benefits

The following table presents the components of the net periodic benefit costs with respect to pensions and other benefits for the three and six-month periods ended June 30, 2006 and 2005:

	Pensions			Postretirement		
(in millions)	Non-U.S. Plans	U.S. Plans	Total	Non-U.S. Plans	U.S. Plans	Total
Three Months Ended June 30, 2006						
Components of net period benefit cost:						
Service cost	**$ 18**	**$ 31**	**$ 49**	**$ 1**	**$ 2**	**$ 3**
Interest cost	**8**	**41**	**49**	**–**	**2**	**2**
Expected return on assets	**(7)**	**(49)**	**(56)**	**–**	**–**	**–**
Amortization of prior service cost	**(2)**	**–**	**(2)**	**–**	**(1)**	**(1)**
Recognized actuarial loss	**4**	**19**	**23**	**–**	**–**	**–**
Net period benefit cost	**$ 21**	**$ 42**	**$ 63**	**$ 1**	**$ 3**	**$ 4**
Three Months Ended June 30, 2005						
Components of net period benefit cost:						
Service cost	$ 19	$ 26	$ 45	$ 1	$ 2	$ 3
Interest cost	8	37	45	–	4	4
Expected return on assets	(5)	(41)	(46)	–	–	–
Amortization of prior service cost	(3)	–	(3)	–	(2)	(2)
FAS 88 loss due to settlements	1	–	1	–	–	–
Recognized actuarial loss	6	16	22	–	1	1
Net period benefit cost	$ 26	$ 38	$ 64	$ 1	$ 5	$ 6
Six Months Ended June 30, 2006						
Components of net period benefit cost:						
Service cost	**$ 37**	**$ 62**	**$ 99**	**$ 2**	**$ 3**	**$ 5**
Interest cost	**17**	**81**	**98**	**1**	**5**	**6**
Expected return on assets	**(14)**	**(97)**	**(111)**	**–**	**–**	**–**
Amortization of prior service cost	**(4)**	**(1)**	**(5)**	**–**	**(3)**	**(3)**
Recognized actuarial loss	**8**	**38**	**46**	**–**	**–**	**–**
Net period benefit cost	**$ 44**	**$ 83**	**$ 127**	**$ 3**	**$ 5**	**$ 8**
Six Months Ended June 30, 2005						
Components of net period benefit cost:						
Service cost	$ 37	$ 52	$ 89	$ 2	$ 3	$ 5
Interest cost	16	74	90	1	7	8
Expected return on assets	(11)	(82)	(93)	–	–	–
Amortization of prior service cost	(5)	(2)	(7)	–	(3)	(3)
FAS 88 loss due to settlements	3	–	3	–	–	–
Amortization of transition liability	1	–	1	–	–	–
Recognized actuarial loss	11	33	44	–	1	1
Net period benefit cost	$ 52	$ 75	$ 127	$ 3	$ 8	$ 11

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

8. Recent Accounting Standards

Accounting Changes

At the March 2004 meeting, the Emerging Issue Task Force (EITF) reached a consensus with respect to Issue No. 03-1, "The Meaning of Other-Than-Temporary Impairment and Its Application to Certain Investments." On September 30, 2004, the FASB issued FASB Staff Position (FSP) EITF No. 03-1-1, Effective Date of Paragraphs 10-20 of EITF Issue No. 03-1, "The Meaning of Other-Than-Temporary Impairment and Its Application to Certain Investments" delaying the effective date of this guidance until the FASB has resolved certain implementation issues with respect to this guidance, but the disclosures remain effective. This FSP, retitled FSP FAS 115-1, "The Meaning of Other-Than-Temporary Impairment and Its Application to Certain Investments," replaces the measurement and recognition guidance set forth in Issue No. 03-1 and codifies certain existing guidance on impairment and accretion of income. AIG's adoption of FSP FAS 115-1 on January 1, 2006 did not have a material effect on AIG's consolidated financial condition or results of operations.

In December 2004, the FASB issued Statement No. 123 (revised 2004), "Share-Based Payment" (FAS 123R). FAS 123R and its related interpretive guidance replaces FAS No. 123, "Accounting for Stock-Based Compensation" (FAS 123), supersedes Accounting Principles Board Opinion No. 25, "Accounting for Stock Issued to Employees" (APB 25) and amends FAS 95, "Statement of Cash Flows." FAS 123, as originally issued in 1995, established as preferable a fair-value-based method of accounting for share-based payment transactions with employees. On January 1, 2003, AIG adopted the recognition provisions of FAS 123. See also Note 10 herein. AIG adopted the provisions of the revised FAS 123R and its related interpretive guidance on January 1, 2006.

For its service-based awards under the 1999 Stock Option Plan, 2002 Stock Incentive Plan and 1996 Employee Stock Purchase Plan, AIG recognizes compensation on a straight-line basis over the scheduled vesting period. Unrecognized unvested compensation expense for stock option awards granted under APB 25 (i.e., before January 1, 2003) will be recognized from January 1, 2006 to the vesting date. However, for the SICO Plans, the AIG Deferred Compensation Profit Participant Plan and the AIG Partners Plan, which contain both performance and service conditions, AIG recognizes compensation utilizing a graded vesting expense attribution method. The effect of this approach is to recognize compensation cost over the requisite service period for each separately vesting tranche of the award.

AIG's share-based plans generally provide for accelerated vesting after the participant turns 65 and retires. For awards granted after January 1, 2006, compensation expense is recognized ratably from the date of grant through the shorter of age 65 or the vesting period. The effect of this change is not material to AIG's consolidated financial position or results of operations. Awards granted prior to January 1, 2006 will continue to be recognized over the vesting period with accelerated expense recognition upon an actual retirement. SICO compensation expense for participants retiring after age 65 had been reflected in prior years' results consistent with vested status under the SICO Plans.

On June 1, 2005, the FASB issued Statement No. 154, "Accounting Changes and Error Corrections" (FAS 154). FAS 154 replaces APB Opinion No. 20, "Accounting Changes" and FASB Statement No. 3, "Reporting Accounting Changes in Interim Financial Statements." FAS 154 requires that a voluntary change in accounting principles be applied retrospectively with all prior period financial statements presented based on the new accounting principle, unless it is impracticable to do so. FAS 154 also provides that a correction of errors in previously issued financial statements should be termed a "restatement." The new standard is effective for accounting changes and correction of errors beginning January 1, 2006.

At the June 2005 meeting, the EITF reached a consensus with respect to Issue No. 04-5, "Determining Whether a General Partner, or the General Partners as a Group, Controls a Limited Partnership or Similar Entity When the Limited Partners Have Certain Rights". The Issue addresses what rights held by the limited partner(s) preclude consolidation in circumstances in which the sole general partner would consolidate the limited partnership in accordance with generally accepted accounting principles absent the existence of the rights held by the limited partner(s). Based on that consensus, the EITF also agreed to amend the consensus in Issue No. 96-16, "Investor's Accounting for an Investee When the Investor Has a Majority of the Voting Interest but the Minority Shareholders Have Certain Approval or Veto Rights." The guidance in this Issue is effective after June 29, 2005 for general partners of all new limited partnerships formed and for existing limited partnerships for which the partnership agreements are modified. For general partners in all other limited partnerships, the guidance in this Issue is effective beginning January 1, 2006. The effect of the adoption of this EITF Issue was not material to AIG's consolidated financial condition or results of operations.

On June 29, 2005, FASB issued Statement 133 Implementation Issue No. B38, "Embedded Derivatives: Evaluation of Net Settlement with Respect to the Settlement of a Debt Instrument through Exercise of an Embedded Put Option or Call Option." This implementation guidance relates to the potential settlement of the debtor's obligation to the creditor that would occur upon exercise of the put option or call option, which meets the net settlement criterion in FAS 133. The effective date of the implementation guidance is January 1, 2006. The adoption of this guidance did not have a material effect on AIG's consolidated financial condition or results of operations.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

8. Recent Accounting Standards *(continued)*

On June 29, 2005, the FASB issued Statement 133 Implementation Issue No. B39, "Application of Paragraph 13(b) to Call Options That Are Exercisable Only by the Debtor." The conditions in FAS 133 paragraph 13(b) do not apply to an embedded call option in a hybrid instrument containing a debt host contract if the right to accelerate the settlement of the debt can be exercised only by the debtor (issuer/borrower). This guidance does not apply to other embedded derivative features that may be present in the same hybrid instrument. The effective date of the implementation guidance is January 1, 2006. The adoption of this guidance did not have a material effect on AIG's consolidated financial condition or results of operations.

On February 16, 2006, the FASB issued FAS No. 155, "Accounting for Certain Hybrid Financial Instruments" (FAS 155), an amendment of FAS 140 and FAS 133. FAS 155 allows AIG to include changes in fair value in earnings on an instrument-by-instrument basis for any hybrid financial instrument that contains an embedded derivative that would otherwise be required to be bifurcated and accounted for separately under FAS 133. The election to measure the hybrid instrument at fair value is irrevocable at the acquisition or issuance date.

AIG elected to early adopt FAS 155 as of January 1, 2006, and apply FAS 155 fair value measurement to certain structured note liabilities and structured investments in AIG's available for sale portfolio that existed at December 31, 2005. The effect of this adoption resulted in an $11 million after-tax ($18 million pre-tax) decrease to opening retained earnings as of January 1, 2006, representing the difference between the fair value of these hybrid financial instruments and the prior carrying value as of December 31, 2005. The effect of adoption on after-tax gross gains and losses was $218 million ($336 million pre-tax) and $229 million ($354 million pre-tax), respectively.

In connection with AIG's early adoption of FAS 155, structured note liabilities of $6.7 billion, other structured liabilities in conjunction with equity derivative transactions of $138 million, and hybrid financial instruments of $495 million at June 30, 2006 are now carried at fair value. The effect on earnings for the three and six-month periods ended June 30, 2006, for changes in the fair value of hybrid financial instruments, was a pre-tax loss of $153 million and $123 million, respectively, and is reflected in income.

On March 27, 2006, the FASB issued FSP FTB 85-4-1, "Accounting for Life Settlement Contracts by Third-Party Investors" (FSP 85-4-1), an amendment of FTB 85-4, "Accounting for Purchases of Life Insurance." Life settlements are designed to assist life insurance policyholders in monetizing the existing value of life insurance policies. FSP 85-4-1 allows AIG to measure life settlement contracts using either the investment method or fair value method. The election is made on an instrument-by-instrument basis and is irrevocable. AIG elected to early adopt FSP 85-4-1 as of January 1, 2006 using the investment method for pre-existing investments held at December 31, 2005. The effect of this adoption resulted in a $319 million after tax ($487 million pre-tax) increase to opening retained earnings.

On June 29, 2006, AIG restructured its ownership of life settlement contracts with no effect on the economic substance of these investments. At the same time, AIG paid $610 million to its former co-investors to acquire all the remaining interests in life settlement contracts held in previously non-consolidated trusts.

At June 30, 2006, the carrying value of AIG's life settlement contracts was $1.20 billion, and is included in Other invested assets on the consolidated balance sheet. These investments are monitored for impairment on a contract by contract basis quarterly. During the three month period ended June 30, 2006, income recognized on life settlement contracts previously held in non-consolidated trusts was $5 million, and is included in net investment income on the consolidated statement of income. Such income totaled $13 million for the six month period then ended. Further information regarding life settlement contracts as of June 30, 2006 is as follows:

(dollars in millions)

Remaining Life Expectancy of Insureds	Number of Contracts	Carrying Value	Face Value (Death Benefits)
0 – 1 year	2	$ 3	$ 4
1 – 2 years	20	12	15
2 – 3 years	83	69	111
3 – 4 years	132	115	208
4 – 5 years	136	72	154
Thereafter	1,501	925	3,454
Total	1,874	$1,196	$3,946

As of June 30, 2006, the anticipated life insurance premiums required to keep the life settlement contracts in force, payable in the ensuing twelve months ending June 30, 2007, and the four succeeding years ending June 30, 2011 are $80 million, $83 million, $88 million, $89 million, and $89 million, respectively.

Future Application of Accounting Standards

On September 19, 2005, the FASB issued Statement of Position 05-1, "Accounting by Insurance Enterprises for Deferred Acquisition Costs in Connection with Modifications or Exchanges of Insurance Contracts" (SOP 05-1). SOP 05-1 provides guidance on accounting for deferred acquisition costs on internal replacements of insurance and investment contracts other than those specifically described in FASB Statement No. 97, "Accounting and Reporting by Insurance Enterprises for Certain Long-Duration Contracts and for Realized Gains and Losses from the Sale of Investments." The SOP defines an internal replacement as a modification in

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

8. Recent Accounting Standards *(continued)*

product benefits, features, rights, or coverage that occurs by the exchange of a contract for a new contract, or by amendment, endorsement, or rider to a contract, or by the election of a feature or coverage within a contract. The effective date of the implementation guidance is January 1, 2007. AIG is currently assessing the effect of implementing this guidance.

On April 13, 2006, the FASB issued FSP FIN 46(R)-6, "Determining the Variability to be Considered in Applying FASB Interpretation No. 46(R)" (FIN 46(R)-6 or FSP). The FSP affects the identification of which entities are variable interest entities through a "by design" approach in identifying and measuring the variable interests of the variable interest entity and its primary beneficiary. The requirements are effective beginning in the third quarter of 2006 and are to be applied to all new variable interest entities with which AIG becomes involved. The new requirements need not be applied to entities that have previously been analyzed under FIN 46(R) unless a reconsideration event occurs. The adoption of this guidance is not expected to have a material effect on AIG's consolidated financial condition or results of operations.

On July 13, 2006, the FASB issued FASB Interpretation No. 48, "Accounting for Uncertainty in Income Taxes – an interpretation of FASB Statement No. 109" (FIN 48), which clarifies the accounting for uncertainty in tax positions. This Interpretation prescribes a recognition threshold and measurement attribute for the financial statement recognition and measurement of an income tax position taken or expected to be taken in a tax return. This Interpretation also provides guidance on derecognition, classification, interest and penalties, accounting in interim periods, and additional disclosures. The effective date of this implementation guidance is January 1, 2007, with the cumulative effect of the change in accounting principle recorded as an adjustment to opening retained earnings. AIG is currently assessing the effect of implementing this guidance.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

9. Information Provided in Connection with Outstanding Debt

The following condensed consolidating financial statements are provided in compliance with Regulation S-X of the Securities and Exchange Commission.

(a) American General Corporation (AGC) is a holding company and a wholly owned subsidiary of AIG. AIG provides a full and unconditional guarantee of all outstanding debt of AGC.

American General Corporation, as issuer:

Condensed Consolidating Balance Sheet

June 30, 2006 *(in millions)*	**American International Group, Inc. Guarantor**	**AGC**	**Other Subsidiaries**	**Eliminations**	**Consolidated AIG**
Assets:					
Invested assets	**$ 3,151**	**$ –**	**$722,978**	**$ (16,091)**	**$710,038**
Cash	**53**	**–**	**2,087**	**–**	**2,140**
Carrying value of subsidiaries and partially owned companies, at equity	**95,249**	**25,747**	**14,784**	**(134,405)**	**1,375**
Other assets	**3,788**	**2,607**	**183,147**	**(2,425)**	**187,117**
Total assets	**$102,241**	**$28,354**	**$922,996**	**$ (152,921)**	**$900,670**
Liabilities:					
Insurance liabilities	**$ 355**	**$ –**	**$480,098**	**$ (64)**	**$480,389**
Debt	**9,190**	**2,096**	**129,383**	**(14,572)**	**126,097**
Other liabilities	**4,987**	**3,841**	**201,413**	**(3,959)**	**206,282**
Total liabilities	**14,532**	**5,937**	**810,894**	**(18,595)**	**812,768**
Preferred shareholders' equity in subsidiary companies	**–**	**–**	**193**	**–**	**193**
Total shareholders' equity	**87,709**	**22,417**	**111,909**	**(134,326)**	**87,709**
Total liabilities, preferred shareholders' equity in subsidiary companies and shareholders' equity	**$102,241**	**$28,354**	**$922,996**	**$ (152,921)**	**$900,670**

December 31, 2005 *(in millions)*	American International Group, Inc. Guarantor	AGC	Other Subsidiaries	Eliminations	Consolidated AIG
Assets:					
Invested assets	$ 1,392	$ –	$691,349	$ (13,696)	$679,045
Cash	190	–	1,707	–	1,897
Carrying value of subsidiaries and partially owned companies, at equity	90,723	27,027	15,577	(132,169)	1,158
Other assets	2,768	2,577	166,933	(1,327)	170,951
Total assets	$95,073	$29,604	$875,566	$(147,192)	$853,051
Liabilities:					
Insurance liabilities	$ 408	$ –	$460,271	$ (56)	$460,623
Debt	4,607	2,087	115,212	(12,057)	109,849
Other liabilities	3,741	4,110	191,279	(3,054)	196,076
Total liabilities	8,756	6,197	766,762	(15,167)	766,548
Preferred shareholders' equity in subsidiary companies	–	–	186	–	186
Total shareholders' equity	86,317	23,407	108,618	(132,025)	86,317
Total liabilities, preferred shareholders' equity in subsidiary companies and shareholders' equity	$95,073	$29,604	$875,566	$(147,192)	$853,051

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

9. Information Provided in Connection with Outstanding Debt *(continued)*

Condensed Consolidating Statement of Income

Three Months Ended June 30, 2006 *(in millions)*	**American International Group, Inc. Guarantor**	**AGC**	**Other Subsidiaries**	**Eliminations**	**Consolidated AIG**
Operating income (loss)	**$ (436)**	**$ (48)**	**$5,725**	**$ –**	**$5,241**
Equity in undistributed net income of consolidated subsidiaries	**3,507**	**309**	**–**	**(3,816)**	**–**
Dividend income from consolidated subsidiaries	**380**	**154**	**–**	**(534)**	**–**
Income taxes (benefits)	**261**	**(17)**	**1,444**	**–**	**1,688**
Minority interest	**–**	**–**	**(363)**	**–**	**(363)**
Net income (loss)	**$3,190**	**$432**	**$3,918**	**$(4,350)**	**$3,190**

Three Months Ended June 30, 2005 *(in millions)*	American International Group, Inc. Guarantor	AGC	Other Subsidiaries	Eliminations	Consolidated AIG
Operating income (loss)	$ 150	$ (40)	$6,591	$ –	$6,701
Equity in undistributed net income of consolidated subsidiaries	3,784	590	–	(4,374)	–
Dividend income from consolidated subsidiaries	657	–	–	(657)	–
Income taxes (benefits)	102	(14)	1,995	–	2,083
Minority interest	–	–	(129)	–	(129)
Net income (loss)	$4,489	$564	$4,467	$(5,031)	$4,489

Six Months Ended June 30, 2006 *(in millions)*	**American International Group, Inc. Guarantor**	**AGC**	**Other Subsidiaries**	**Eliminations**	**Consolidated AIG**
Operating income (loss)	**$ (722)**	**$ (86)**	**$10,842**	**$ –**	**$10,034**
Equity in undistributed net income of consolidated subsidiaries	**6,767**	**668**	**–**	**(7,435)**	**–**
Dividend income from consolidated subsidiaries	**567**	**458**	**–**	**(1,025)**	**–**
Income taxes (benefits)	**261**	**(30)**	**2,892**	**–**	**3,123**
Minority interest	**–**	**–**	**(560)**	**–**	**(560)**
Cumulative effect of an accounting change, net of tax	**34**	**–**	**–**	**–**	**34**
Net income (loss)	**$6,385**	**$1,070**	**$ 7,390**	**$(8,460)**	**$ 6,385**

Six Months Ended June 30, 2005 *(in millions)*	American International Group, Inc. Guarantor	AGC Issuer	Other Subsidiaries	Eliminations	Consolidated AIG
Operating income (loss)	$ 140	$ (76)	$12,286	$ –	$12,350
Equity in undistributed net income of consolidated subsidiaries	7,430	1,291	–	(8,721)	–
Dividend income from consolidated subsidiaries	928	–	–	(928)	–
Income taxes (benefits)	210	(26)	3,605	–	3,789
Minority interest	–	–	(273)	–	(273)
Net income (loss)	$8,288	$1,241	$ 8,408	$(9,649)	$ 8,288

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

9. Information Provided in Connection with Outstanding Debt *(continued)*

Condensed Consolidating Statements of Cash Flow

Six Months Ended June 30, 2006 *(in millions)*	**American International Group, Inc. Guarantor**	**AGC**	**Other Subsidiaries**	**Consolidated AIG**
Net cash provided by operating activities	**$(1,106)**	**$112**	**$ 7,972**	**$ 6,978**
Cash flows from investing:				
Invested assets disposed	**–**	**–**	**77,673**	**77,673**
Invested assets acquired	**(1,577)**	**–**	**(115,405)**	**(116,982)**
Other	**(2,629)**	**(17)**	**1,907**	**(739)**
Net cash used in investing activities	**(4,206)**	**(17)**	**(35,825)**	**(40,048)**
Cash flows from financing activities:				
Change in debts	**5,733**	**–**	**11,361**	**17,094**
Other	**(557)**	**(95)**	**15,801**	**15,149**
Net cash (used in) provided by financing activities	**5,176**	**(95)**	**27,162**	**32,243**
Effect of exchange rate changes on cash	**(1)**	**–**	**1,071**	**1,070**
Change in cash	**(137)**	**–**	**380**	**243**
Cash at beginning of period	**190**	**–**	**1,707**	**1,897**
Cash at end of period	**$ 53**	**$ –**	**$ 2,087**	**$ 2,140**

Six Months Ended June 30, 2005 *(in millions)*	American International Group, Inc. Guarantor	AGC	Other Subsidiaries	Consolidated AIG
Net cash provided by operating activities	$ 721	$ 642	$ 12,326	$ 13,689
Cash flows from investing:				
Invested assets disposed	158	–	96,203	96,361
Invested assets acquired	–	–	(131,191)	(131,191)
Other	(173)	(270)	43	(400)
Net cash used in investing activities	(15)	(270)	(34,945)	(35,230)
Cash flows from financing activities:				
Change in debts	(35)	(299)	7,127	6,793
Other	(657)	(73)	16,034	15,304
Net cash (used in) provided by financing activities	(692)	(372)	23,161	22,097
Effect of exchange rate changes on cash	40	–	(867)	(827)
Change in cash	54	–	(325)	(271)
Cash at beginning of period	17	–	1,992	2,009
Cash at end of period	$ 71	$ –	$ 1,667	$ 1,738

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

9. Information Provided in Connection with Outstanding Debt *(continued)*

(b) AIG Liquidity Corp. is a wholly owned subsidiary of AIG. AIG provides a full and unconditional guarantee of all obligations of AIG Liquidity Corp., which commenced operations in 2003.

AIG Liquidity Corp., as issuer:

Condensed Consolidating Balance Sheet

June 30, 2006 *(in millions)*	**American International Group, Inc. Guarantor**	**AIG Liquidity Corp.**	**Other Subsidiaries**	**Eliminations**	**Consolidated AIG**
Assets:					
Invested assets	**$ 3,151**	**$ ***	**$722,978**	**$ (16,091)**	**$710,038**
Cash	**53**	****	**2,087**	**–**	**2,140**
Carrying value of subsidiaries and partially owned companies, at equity	**95,249**	**–**	**40,531**	**(134,405)**	**1,375**
Other assets	**3,788**	****	**185,754**	**(2,425)**	**187,117**
Total assets	**$102,241**	**$ ***	**$951,350**	**$ (152,921)**	**$900,670**
Liabilities:					
Insurance liabilities	**$ 355**	**$ –**	**$480,098**	**$ (64)**	**$480,389**
Debt	**9,190**	****	**131,479**	**(14,572)**	**126,097**
Other liabilities	**4,987**	****	**205,254**	**(3,959)**	**206,282**
Total liabilities	**14,532**	****	**816,831**	**(18,595)**	**812,768**
Preferred shareholders' equity in subsidiary companies	**–**	**–**	**193**	**–**	**193**
Total shareholders' equity	**87,709**	****	**134,326**	**(134,326)**	**87,709**
Total liabilities, preferred shareholders' equity in subsidiary companies and shareholders' equity	**$102,241**	**$ ***	**$951,350**	**$ (152,921)**	**$900,670**

** Amounts significantly less than $1 million.*

December 31, 2005 *(in millions)*	American International Group, Inc. Guarantor	AIG Liquidity Corp.	Other Subsidiaries	Eliminations	Consolidated AIG
Assets:					
Invested assets	$ 1,392	$ *	$691,349	$ (13,696)	$679,045
Cash	190	*	1,707	–	1,897
Carrying value of subsidiaries and partially owned companies, at equity	90,723	–	42,604	(132,169)	1,158
Other assets	2,768	*	169,510	(1,327)	170,951
Total assets	$95,073	$ *	$905,170	$(147,192)	$853,051
Liabilities:					
Insurance liabilities	$ 408	$ –	$460,271	$ (56)	$460,623
Debt	4,607	*	117,299	(12,057)	109,849
Other liabilities	3,741	*	195,389	(3,054)	196,076
Total liabilities	8,756	*	772,959	(15,167)	766,548
Preferred shareholders' equity in subsidiary companies	–	–	186	–	186
Total shareholders' equity	86,317	*	132,025	(132,025)	86,317
Total liabilities, preferred shareholders' equity in subsidiary companies and shareholders' equity	$95,073	$ *	$905,170	$(147,192)	$853,051

**Amounts significantly less than $1 million.*

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

9. Information Provided in Connection with Outstanding Debt *(continued)*

Condensed Consolidating Statement of Income

Three Months Ended June 30, 2006 *(in millions)*	**American International Group, Inc. Guarantor**	**AIG Liquidity Corp.**	**Other Subsidiaries**	**Eliminations**	**Consolidated AIG**
Operating income (loss)	**$ (436)**	**$ ***	**$5,677**	**$ –**	**$5,241**
Equity in undistributed net income of consolidated subsidiaries	**3,507**	**–**	**309**	**(3,816)**	**–**
Dividend income from consolidated subsidiaries	**380**	**–**	**154**	**(534)**	**–**
Income taxes	**261**	*****	**1,427**	**–**	**1,688**
Minority interest	**–**	**–**	**(363)**	**–**	**(363)**
Net income (loss)	**$3,190**	**$ ***	**$4,350**	**$(4,350)**	**$3,190**

**Amounts significantly less than $1 million.*

Three Months Ended June 30, 2005 *(in millions)*	American International Group, Inc. Guarantor	AIG Liquidity Corp.	Other Subsidiaries	Eliminations	Consolidated AIG
Operating income	$ 150	$ *	$6,551	$ –	$ 6,701
Equity in undistributed net income of consolidated subsidiaries	3,784	–	590	(4,374)	–
Dividend income from consolidated subsidiaries	657	–	–	(657)	–
Income taxes	102	*	1,981	–	2,083
Minority interest	–	–	(129)	–	(129)
Net income (loss)	$4,489	$ *	$5,031	$(5,031)	$ 4,489

**Amounts significantly less than $1 million.*

Six Months Ended June 30, 2006 *(in millions)*	**American International Group, Inc. Guarantor**	**AIG Liquidity Corp.**	**Other Subsidiaries**	**Eliminations**	**Consolidated AIG**
Operating income (loss)	**$ (722)**	**$ ***	**$10,756**	**$ –**	**$10,034**
Equity in undistributed net income of consolidated subsidiaries	**6,767**	**–**	**668**	**(7,435)**	**–**
Dividend income from consolidated subsidiaries	**567**	**–**	**458**	**(1,025)**	**–**
Income taxes	**261**	*****	**2,862**	**–**	**3,123**
Minority interest	**–**	**–**	**(560)**	**–**	**(560)**
Cumulative effect of an accounting change, net of tax	**34**	**–**	**–**	**–**	**34**
Net income (loss)	**$6,385**	**$ ***	**$ 8,460**	**$(8,460)**	**$ 6,385**

** Amounts significantly less than $1 million.*

Six Months Ended June 30, 2005 *(in millions)*	American International Group, Inc. Guarantor	AIG Liquidity Corp.	Other Subsidiaries	Eliminations	Consolidated AIG
Operating income	$ 140	$ *	$12,210	$ –	$ 12,350
Equity in undistributed net income of consolidated subsidiaries	7,430	–	1,291	(8,721)	–
Dividend income from consolidated subsidiaries	928	–	–	(928)	–
Income taxes	210	*	3,579	–	3,789
Minority interest	–	–	(273)	–	(273)
Net income (loss)	$8,288	$ *	$ 9,649	$(9,649)	$ 8,288

**Amounts significantly less than $1 million.*

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

9. Information Provided in Connection with Outstanding Debt *(continued)*

Condensed Consolidating Statements of Cash Flow

Six Months Ended June 30, 2006 *(in millions)*	**American International Group, Inc. Guarantor**	**AIG Liquidity Corp.**	**Other Subsidiaries**	**Consolidated AIG**
Net cash provided by operating activities	**$(1,106)**	**$ ***	**$ 8,084**	**$ 6,978**
Cash flows from investing:				
Invested assets disposed	**–**	**–**	**77,673**	**77,673**
Invested assets acquired	**(1,577)**	**–**	**(115,405)**	**(116,982)**
Other	**(2,629)**	*****	**1,890**	**(739)**
Net cash used in investing activities	**(4,206)**	*****	**(35,842)**	**(40,048)**
Cash flows from financing activities:				
Change in debts	**5,733**	**–**	**11,361**	**17,094**
Other	**(557)**	*****	**15,706**	**15,149**
Net cash (used in) provided by financing activities	**5,176**	*****	**27,067**	**32,243**
Effect of exchange rate changes on cash	**(1)**	**–**	**1,071**	**1,070**
Change in cash	**(137)**	*****	**380**	**243**
Cash at beginning of period	**190**	**–**	**1,707**	**1,897**
Cash at end of period	**$ 53**	**$ ***	**$ 2,087**	**$ 2,140**

**Amounts significantly less than $1 million.*

Six Months Ended June 30, 2005 *(in millions)*	American International Group, Inc. Guarantor	AIG Liquidity Corp.	Other Subsidiaries	Consolidated AIG
Net cash (used in) provided by operating activities	$ 721	$ *	$ 12,968	$ 13,689
Cash flows from investing:				
Invested assets disposed	158	–	96,203	96,361
Invested assets acquired	–	–	(131,191)	(131,191)
Other	(173)	*	(227)	(400)
Net cash used in investing activities	(15)	*	(35,215)	(35,230)
Cash flows from financing activities:				
Change in debts	(35)	–	6,828	6,793
Other	(657)	*	15,961	15,304
Net cash (used in) provided by financing activities	(692)	*	22,789	22,097
Effect of exchange rate changes on cash	40	–	(867)	(827)
Change in cash	54	*	(325)	(271)
Cash at beginning of period	17	–	1,992	2,009
Cash at end of period	$ 71	$ *	$ 1,667	$ 1,738

**Amounts significantly less than $1 million.*

10. Stock Compensation Plans

At June 30, 2006, AIG employees could be awarded compensation pursuant to six different stock-based compensation plan arrangements: (i) AIG 1999 Stock Option Plan, as amended (1999 Plan); (ii) AIG 1996 Employee Stock Purchase Plan, as amended (the 1996 Plan); (iii) AIG 2002 Stock Incentive Plan, as amended (2002 Plan) under which AIG has issued only restricted stock units (RSUs) and performance restricted stock units (Performance RSUs); (iv) SICO's Deferred Compensation Profit Participation Plans (SICO Plans); (v) AIG's 2005-2006 Deferred Compensation Profit Participation Plan (AIG DCPPP) and (vi) the AIG Partners Plan. The AIG DCPPP was adopted as a replacement for the SICO Plans for the 2005-2006 period, and the AIG Partners Plan replaces the AIG DCPPP. Stock-based compensation earned under the AIG DCPPP and the AIG Partners Plan is issued as awards under the 2002 Plan. AIG currently settles share option exercises and other share awards to participants through the issuance of shares it has previously acquired and holds in its treasury account, except for share awards made by SICO, which are settled by SICO.

At June 30, 2006, AIG's non-employee directors received stock-based compensation in two forms, options granted pursuant to the 1999 Plan and grants of AIG common stock with delivery deferred until retirement from the Board, pursuant to the AIG Director Stock Plan, which was approved by the shareholders at the 2004 Annual Meeting of Shareholders.

From January 1, 2003 through December 31, 2005, AIG accounted for share-based payment transactions with employ-

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

10. Stock Compensation Plans *(continued)*

ees under FAS 123, "Accounting for Stock-Based Compensation." Share-based employee compensation expense from option awards was not recognized in the statement of income in prior periods. Effective January 1, 2006, AIG adopted the fair value recognition provisions of Statement of Financial Accounting Standards No. 123R "Share-Based Payments" (FAS 123R). FAS 123R requires that companies use a fair value method to value share-based payments and recognize the related compensation expense in net earnings. AIG adopted FAS 123R using the modified prospective application method, and accordingly, financial statement amounts for the prior periods presented have not been restated to reflect the fair value method of expensing share-based compensation under FAS 123R. The modified prospective application method provides for the recognition of the fair value with respect to share-based compensation for shares subscribed for or granted on or after January 1, 2006 and all previously granted but unvested awards as of January 1, 2006.

The adoption of FAS 123R resulted in share-based compensation expense of approximately $9 million during the first six months of 2006, related to awards which were accounted for under the provisions of Accounting Principles Board Opinion No. 25, "Accounting for Stock Issued to Employees." AIG expects this expense to approximate $19 million for fiscal 2006. FAS 123R also requires AIG to estimate forfeitures in calculating the expense relating to share-based compensation, rather than recognizing these forfeitures and corresponding reductions in expense as they occur. The pre-tax cumulative effect of adoption, recognized as a reduction in stock-based compensation of $46 million, was recorded as a cumulative effect of an accounting change, net of tax, in the first quarter of 2006. FAS 123R requires AIG to reflect the cash savings resulting from excess tax benefits in its financial statements as cash flow from financing activities, rather than as cash flow from operating activities as in prior periods. The amount of this excess tax benefit for the three and six-month periods ended June 30, 2006 was $0.6 million and $2.3 million, respectively.

The effect of the adoption of FAS 123R on the consolidated statements of income and cash flows was as follows:

	Three Months Ended June 30, 2006			Six Months Ended June 30, 2006		
(in millions, except per share data)	Pre-adoption of FAS 123R	Effect of Adoption of FAS 123R	Including Effect of Adoption of FAS 123R	Pre-adoption of FAS 123R	Effect of Adoption of FAS 123R	Including Effect of Adoption of FAS 123R
Income before income taxes, minority interest and cumulative effect of an accounting change	$ 5,242	$(1)	$ 5,241	$10,043	$ (9)	$10,034
Provision for income taxes	$ 1,686	$ 2	$ 1,688	$ 3,124	$ (1)	$ 3,123
Income before minority interest and cumulative effect of an accounting change	$ 3,556	$(3)	$ 3,553	$ 6,919	$ (8)	$ 6,911
Cumulative effect of an accounting change, net of tax	$ –	$ –	$ –	$ –	$ 34	$ 34
Net income	$ 3,193	$(3)	$ 3,190	$ 6,359	$ 26	$ 6,385
Net cash provided by operating activities	$ 2,923	$ –	$ 2,923	$ 6,980	$ (2)	$ 6,978
Net cash provided by financing activities	$16,571	$ –	$16,571	$32,241	$ 2	$32,243
Basic earnings per share	$ 1.23	$ –	$ 1.23	$ 2.44	$0.01	$ 2.45
Diluted earnings per share	$ 1.21	$ –	$ 1.21	$ 2.42	$0.01	$ 2.43

The following table presents share-based compensation expenses, including the cumulative effect of adoption of FAS 123R, included in AIG's consolidated statement of income:

(in millions)	Three Months Ended June 30, 2006	Six Months Ended June 30, 2006
Share-based compensation expense before tax	$57	$211
Income tax benefit	$16	$ 28
After-tax share-based compensation expense	$41	$183

Included in share-based compensation expense of $211 million for the six months ended June 30, 2006 was a one-time compensation cost of approximately $54 million related to the Starr tender offer and various out of period adjustments totalling $61 million, primarily relating to stock-splits and other miscellaneous items for the SICO plans, offset by a $46 million pre-tax adjustment for the cumulative effect of the adoption of FAS 123R. These items were recorded in the first quarter of 2006. See Note 4 herein for a discussion of the Starr tender offer and Note 8 herein for discussion of the prospective change to the accounting for retiree eligibility provisions and forfeiture treatment.

If AIG had adopted the FAS 123 provisions for recognizing compensation expense commencing at the date of grant of the awards, the effect would not have been material to net income or basic or diluted earnings per share for the three and six-month periods ended June 30, 2005.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

10. Stock Compensation Plans *(continued)*

1999 Stock Option Plan

The 1999 Plan provides that options to purchase a maximum of 45,000,000 shares of common stock can be granted to certain key employees and members of the Board of Directors at prices not less than fair market value at the date of grant.

The 1999 Plan was approved by the shareholders at the 2000 Annual Meeting of Shareholders, with certain amendments approved at the 2003 Annual Meeting of Shareholders. The 1999 Plan superseded the 1991 employee stock option plan (the 1991 Plan), although outstanding options granted under the 1991 Plan continue in force until exercise or expiration. The maximum number of shares that may be granted to any employee in any one year under the 1999 Plan is 900,000. Options granted under the 1999 Plan generally vest over four years (25 percent vesting per year) and expire 10 years from the date of grant.

At June 30, 2006, there were 20,761,320 shares reserved for future grants under the 1999 Plan and 28,321,678 shares reserved for issuance under the 1999 and 1991 Plans.

Deferrals

During 2005, options with respect to 1,731,471 shares were exercised with delivery deferred. At December 31, 2005 optionees had made valid elections to defer delivery of 2,067,643 shares of AIG common stock upon exercise of options expiring during 2006. In addition, non-employee directors of AIG had made valid elections to defer delivery of 21,093 shares of AIG common stock upon exercise of options expiring during 2006.

Valuation Methodology

In 2004, AIG developed a binomial lattice model to calculate the fair value of stock option grants. In prior years, a Black-Scholes model was used. A more detailed description of the valuation methodology is provided below.

The following weighted average assumptions were used for stock options granted in the first six months of 2006 and 2005:

	2006	2005
Expected annual dividend yield[(a)]	**0.71%**	0.36%
Expected volatility[(b)]	**27.3%**	34.4%
Risk-free interest rate[(c)]	**4.17%**	3.87%
Expected term[(d)]	**7 years**	7 years

(a) The dividend yield is based on the dividend yield over the twelve month period prior to the grant date.

(b) In 2006, expected volatility is the average of historical volatility (based on seven years of daily stock price changes) and the implied volatility of actively traded options on AIG shares and in 2005, expected volatility is the historical volatility based on five years of daily stock price changes.

(c) The interest rate curves used in the valuation model were the U.S. Treasury STRIP rates with terms from 3 months to 10 years.

(d) The contractual term of the option is generally 10 years with an expected term of 7 years calculated based on an analysis of historical employee exercise behavior and employee turnover (post-vesting terminations). The early exercise rate is a function of time elapsed since the grant. Fifteen years of historical data was used to estimate the early exercise rate.

Additional information with respect to AIG's stock option plans at June 30, 2006, and changes for the six months then ended, were as follows:

Options:	**Shares**	**Weighted Average Exercise Price**
Outstanding at beginning of year	52,545,425	$54.84
Granted	103,000	$65.43
Exercised	(858,053)	$42.80
Forfeited or expired	(805,027)	$68.50
Outstanding at end of period	50,985,345	$54.85
Options exercisable at end of period	39,907,861	$52.54
Weighted average fair value per share of options granted		$21.28

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

10. Stock Compensation Plans *(continued)*

Information about stock options outstanding at June 30, 2006, is summarized as follows:

	Options Outstanding				Options Exercisable			
Range of Exercise Prices	Number Outstanding	Weighted Average Remaining Contractual Life	Weighted Average Exercise Price	Aggregate Intrinsic Values (in millions)	Number Exercisable (vested)	Weighted Average Remaining Contractual Life	Weighted Average Exercise Price	Aggregate Intrinsic Values (in millions)
$11.28-$27.14	6,685,805	0.81	$21.31	$252	6,685,805	0.81	$21.31	$252
$30.44-$41.51	5,374,574	2.04	36.86	119	5,374,574	2.04	36.86	119
$43.31-$53.40	6,936,485	4.34	48.59	73	6,136,895	4.03	48.80	63
$54.11-$59.99	8,337,923	4.58	57.84	11	6,280,376	3.06	57.34	11
$60.13-$63.95	9,083,916	6.44	62.33	–	5,974,994	6.02	61.92	–
$64.01-$69.63	8,208,831	7.30	65.45	–	3,822,360	5.35	65.67	–
$70.35-$98.00	6,357,811	4.91	83.87	–	5,632,857	4.82	84.47	–
Total	50,985,345	4.60	$54.85	$455	39,907,861	3.61	$52.54	$445

Vested and expected-to-vest options as of June 30, 2006, included in the table above, totaled 45,531,044, with a weighted average exercise price of $53.65, a weighted average contractual life of 4.06 years and an aggregate intrinsic value of $455 million.

As of June 30, 2006, total unrecognized compensation cost (net of expected forfeitures) was $153 million, and $3 million related to non-vested share-based compensation awards granted under the 1999 Plan and the 1996 Plan, respectively, with blended weighted average periods of 1.38 years and 0.41 years, respectively. The cost of awards outstanding under these plans at June 30, 2006 is expected to be recognized over approximately three years and one year, respectively, for the 1999 Plan and the 1996 Plan.

The intrinsic value of options exercised during the six months ended June 30, 2006 was approximately $20 million. The fair value of options vesting for the six months ended June 30, 2006 was approximately $42 million. AIG received $40 million and $22 million for the six-month periods ended June 30, 2006 and 2005, respectively, from the exercise of stock options. AIG did not cash-settle any share-based payment awards for the six-month periods ended June 30, 2006 and 2005. The tax benefits realized as a result of stock option exercises were $5 million and $6 million for the six-month periods ended June 30, 2006 and 2005, respectively.

2002 Stock Incentive Plan

AIG's 2002 Plan was adopted at the 2002 shareholders meeting and amended and restated by the AIG Board of Directors on September 18, 2002 (the 2002 Plan). The 2002 Plan provides that equity-based or equity-related awards with respect to shares of common stock can be issued to employees in any year up to a maximum of that number of shares equal to (a) 1,000,000 shares plus (b) the number of shares available but not issued in the prior calendar year. The maximum award that a grantee may receive under the 2002 Plan per year is rights with respect to 250,000 shares. For the six-month periods ended June 30, 2006 and 2005, 3,663,835 RSUs, including performance RSUs, and 31,500 RSUs, respectively, were granted by AIG. There were 6,443,028 shares reserved for issuance in connection with future awards at June 30, 2006. Substantially all RSUs granted to date under the 2002 Plan other than Performance RSUs granted under the Partners Plan vest on the fourth anniversary of the date of grant.

Director Stock Awards

The methodology used for valuing employee stock options is also used to value director stock options. Director stock options vest one year after the grant date, but are otherwise the same as employee stock options. Options with respect to 37,500 shares were granted during the six months ended June 30, 2006, and no shares were granted during the first six months of 2005.

AIG also granted 7,500 shares and 3,000 shares, with delivery deferred, to directors for the six-month periods ended June 30, 2006 and 2005, respectively, under the Director Stock Plan. At June 30, 2006, there were 77,500 shares reserved for future grants under the Director Stock Plan.

Employee Stock Purchase Plan

AIG's 1996 Plan provides that eligible employees (those employed at least one year) may receive privileges to purchase up to an aggregate of 10,000,000 shares of AIG common stock, at a price equal to 85 percent of the fair market value on the date of the grant of the purchase privilege. Purchase privileges are granted quarterly and are limited to the number of whole shares that can be purchased on an annual basis by an amount equal to the lesser of 10 percent of an employee's annual salary or $10,000.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

10. Stock Compensation Plans *(continued)*

SICO Plans

The SICO Plans provide that shares of AIG common stock currently held by SICO are set aside for the benefit of the participant and distributed upon retirement. The SICO Board of Directors currently may permit an early payout of units under certain circumstances. Prior to payout, the participant is not entitled to vote, dispose of or receive dividends with respect to such shares, and shares are subject to forfeiture under certain conditions, including but not limited to the participant's termination of employment with AIG prior to normal retirement age.

Historically, SICO's Board of Directors could elect to pay a participant cash in lieu of shares of AIG common stock. On December 9, 2005, SICO notified participants that essentially all subsequent distributions would be made only in shares, and not cash. As of that date, AIG modified its accounting for the SICO Plans from variable to fixed measurement accounting. Variable measurement accounting is used for those few awards for which cash elections had been made prior to March 2005. The SICO Plans are also described in Note 4 herein.

Although none of the costs of the various benefits provided under the SICO Plans has been paid by AIG, AIG has recorded a charge to reported earnings for the deferred compensation amounts paid to AIG employees by SICO, with an offsetting amount credited to additional paid-in capital reflecting amounts deemed contributed by SICO.

As of December 9, 2005, there were 12,650,292 non-vested AIG shares under the SICO Plans with a weighted-average fair value per share of $61.92. As of June 30, 2006, there were 11,740,679 non-vested AIG shares under the SICO Plans with a weighted-average fair value per share of $61.76.

A significant portion of the awards under the SICO Plans vest upon retirement if the participant reaches age 65. The portion of the awards for which early payout is available vest on the applicable payout date.

AIG DCPPP

Effective September 21, 2005, AIG adopted the AIG DCPPP, which provides equity-based compensation to key AIG employees, including senior executive officers. The AIG DCPPP was modeled on the SICO Plans.

The AIG DCPPP contingently allocates a fixed number of shares to each participant if AIG's cumulative adjusted earnings per share for 2005 and 2006 exceed that for 2003 and 2004. The performance period is September 21, 2005 to December 31, 2006. At the end of the performance period, common shares are contingently allocated. The service period and related vesting consists of three pre-retirement tranches and a final retirement tranche at age 65.

At June 30, 2006, there were units representing 4,674,382 shares granted to participants.

AIG Partners Plan

On June 26, 2006, AIG's Compensation Committee approved two grants under the AIG Partners Plan. The first grant has a performance period which runs from January 1, 2006 through December 31, 2007. The second grant has a performance period which runs from January 1, 2007 through December 31, 2008. Both grants vest 50 percent on the fourth and sixth anniversaries of the first day of the related performance period. In addition, the Compensation Committee approved the performance metrics for the two grants prior to the date of grant. The measurement of the grants is deemed to have occurred on June 26, 2006 when there was mutual understanding of the key terms and conditions of the grants. Consistent with this treatment: a) 1,069,355 Performance RSUs for the first grant and 2,490,365 Performance RSUs for the second grant and b) Unrecognized Compensation of $60 million for the first grant and $139 million for the second grant are included in the related disclosure tables. Performance RSUs related to the first grant are excluded from AIG's diluted shares calculation because an insufficient amount of time has elapsed to conclusively determine that the performance metric will be achieved at the end of the related performance period. Because the performance period for the second grant does not begin until January 1, 2007, compensation expense for the second grant is not included in AIG's 2006 results and diluted shares calculation.

VALUATION

The fair value of each award granted under the 2002 Plan, the AIG DCPPP, the AIG Partners Plan, and the SICO Plans is based on the closing price of AIG stock on the date of grant.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

10. Stock Compensation Plans *(continued)*

A summary of shares relating to outstanding awards unvested under the foregoing plans as of June 30, 2006, and changes during the six months ended June 30, 2006 is presented below:

	Number of Shares					Weighted Average Grant-Date Fair Value			
	2002 Plan	AIG DCPPP	AIG Partners Plan	Total 2002 Plan	SICO Plan	2002 Plan	AIG DCPPP	AIG Partners Plan	SICO Plan
Unvested at January 1, 2006	4,322,265	4,898,880	–	9,221,145	12,650,292	$63.63	$52.55	$ –	$61.92
Granted	104,115	–	3,559,720	3,663,835	–	67.33	–	55.89	–
Vested	(5,080)	–	–	(5,080)	(617,064)	64.25	–	–	65.53
Forfeited	(105,610)	(224,498)	–	(330,108)	(292,549)	61.95	59.40	–	58.92
Unvested at June 30, 2006	4,315,690	4,674,382	3,559,720	12,549,792	11,740,679	$63.76	$52.22	$55.89	$61.76

At June 30, 2006, the total unrecognized compensation cost (net of expected forfeitures) related to non-vested share-based compensation awards granted under the 2002 Plan, the AIG DCPPP, the AIG Partners Plan and the SICO plans and the blended weighted-average period over which that cost is expected to be recognized is as follows:

	Unrecognized Compensation Cost *(in millions)*	Blended Weighted-Average Period
2002 Plan	$183	1.71 years
AIG DCPPP	$239	11.12 years
AIG Partners Plan	$199	2.89 years
Total 2002 Plan	$621	—
SICO Plans	$327	6.07 years

The total cost for awards outstanding as of June 30, 2006 under the 2002 Plan, the AIG DCPPP, the AIG Partners Plan, and the SICO Plans is expected to be recognized over approximately 4 years, 12 years, 6 years and 23 years, respectively.

11. Cash Flows

During the second quarter of 2006, AIG began presenting cash flows related to the origination and sale of finance receivables held for sale as cash flows within operating activities in the Consolidated Statement of Cash Flows. Previously these amounts were presented as cash flows within investing activities. In addition, certain intercompany transactions included in Finance receivables held for sale — originations and purchases and Finance receivable principal payments received in the Consolidated Statement of Cash Flows were not eliminated in 2005. After evaluating the effect of these items during the second quarter of 2006, AIG has revised the 2005 presentation to conform to the 2006 presentation.

The effect of these revisions are summarized in the table below:

(in millions)

For the Three Months Ended March 31, 2006	As Previously Reported	Revisions	As Revised
Cash flows from operating activities			
Finance receivables held for sale — originations and purchases	$ —	$ (2,267)	$ (2,267)
Finance receivables sold	$ —	$ 2,671	$ 2,671
Other assets and liabilities — net	$ (3,125)	$ 585	$ (2,540)
Net cash provided by (used in) operating activities	$ 3,066	$ 989	$ 4,055
Cash flows from investing activities			
Finance receivables held for investment — originations and purchases	$ (7,696)	$ 4,295	$ (3,401)
Finance receivable principal payments received	$ 8,312	$ (5,284)	$ 3,028
Net cash used in investing activities	$(19,937)	$ (989)	$(20,926)

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

11. Cash Flows *(continued)*

(in millions)

For the Six Months Ended June 30, 2005	As Previously Reported	Revisions	As Revised
Cash flows from operating activities			
Finance receivables held for sale — originations and purchases	$ —	$ (5,144)	$ (5,144)
Finance receivables sold	$ —	$ 4,775	$ 4,775
Other assets and liabilities — net	$ (476)	$ 241	$ (235)
Net cash provided by (used in) operating activities	$ 13,817	$ (128)	$ 13,689
Cash flows from investing activities			
Finance receivables held for investment — originations and purchases	$(23,778)	$ 14,511	$ (9,267)
Finance receivable principal payments received	$ 20,413	$(14,383)	$ 6,030
Net cash used in investing activities	$(35,358)	$ 128	$(35,230)

(in millions)

For the Year Ended December 31, 2005	As Previously Reported	Revisions	As Revised
Cash flows from operating activities			
Finance receivables held for sale — originations and purchases	$ —	$(13,070)	$(13,070)
Finance receivables sold	$ —	$ 12,821	$ 12,821
Other assets and liabilities — net	$ 2,535	$ 162	$ 2,697
Net cash provided by (used in) operating activities	$ 25,138	$ (87)	$ 25,051
Cash flows from investing activities			
Finance receivables held for investment — originations and purchases	$(52,281)	$ 35,005	$(17,276)
Finance receivable principal payments received	$ 47,425	$(34,918)	$ 12,507
Net cash used in investing activities	$(57,321)	$ 87	$(57,234)

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Management's Discussion and Analysis of Financial Condition and Results of Operations is designed to provide the reader a narrative with respect to AIG's operations, financial condition and liquidity and certain other significant matters.

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Cautionary Statement Regarding Projections and Other Information About Future Events

This Quarterly Report and other publicly available documents may include, and AIG's officers and representatives may from time to time make, projections concerning financial information and statements concerning future economic performance and events, plans and objectives relating to management, operations, products and services, and assumptions underlying these projections and statements. These projections and statements are not historical facts but instead represent only AIG's belief regarding future events, many of which, by their nature, are inherently uncertain and outside AIG's control. These projections and statements may address, among other things, the status and potential future outcome of the current regulatory and civil proceedings against AIG and their potential effect on AIG's businesses, financial position, results of operations, cash flows and liquidity, the effect of the credit rating downgrades on AIG's businesses and competitive position, the unwinding and resolving of various relationships between AIG and Starr and SICO, and AIG's strategy for growth, product development, market position, financial results and reserves. It is possible that AIG's actual results and financial condition may differ, possibly materially, from the anticipated results and financial condition indicated in these projections and statements. Factors that could cause AIG's actual results to differ, possibly materially, from those in the specific projections and statements are discussed throughout this Management's Discussion and Analysis of Financial Condition and Results of Operations and in "Risk Factors" in Item 1A. of Part I of AIG's 2005 Annual Report on Form 10-K and Item 1A. of Part II of AIG's Quarterly Report on Form 10-Q for the quarter ended March 31, 2006. AIG is not under any obligation (and expressly disclaims any such obligations) to update or alter any projections or other statement, whether written or oral, that may be made from time to time, whether as a result of new information, future events or otherwise.

Throughout this Management's Discussion and Analysis of Financial Condition and Results of Operations, AIG presents its operations in the way it believes will be most meaningful. Statutory loss ratios and combined ratios are presented in accordance with accounting principles prescribed by insurance regulatory authorities because these are standard measures of performance filed with insurance regulatory authorities and used for analysis in the insurance industry and thus allow more meaningful comparisons with AIG's insurance competitors. AIG has also incorporated into this discussion a number of cross-references to additional information included throughout this Form 10-Q and its 2005 Annual Report on Form 10-K/A for the year ended December 31, 2005 (2005 Annual Report on Form 10-K/A) to assist readers seeking related information on a particular subject.

Overview of Operations and Business Results

AIG identifies its reportable segments by product line, consistent with its management structure. AIG's major product and service groupings are General Insurance, Life Insurance & Retirement Services, Financial Services and Asset Management. AIG's operations in 2006 are conducted by its subsidiaries principally through these segments. Through these segments, AIG provides insurance and investment products and services to both businesses and individuals in more than 130 countries and jurisdictions. This geographic, product and service diversification is one of AIG's major strengths and sets it apart from its competitors. The Other category consists of items not allocated to AIG's operating segments.

AIG's subsidiaries serve commercial, institutional and individual customers through an extensive property-casualty and life insurance and retirement services network. In the United States, AIG companies are the largest underwriters of commercial and industrial insurance and one of the largest life insurance and retirement services operations as well. AIG's Financial Services businesses include commercial aircraft and equipment leasing, capital markets operations and consumer finance, both in the United States and abroad. AIG also provides asset management services to institutions and individuals. As part of its spread-based business activities, AIG issues various debt instruments in the public and private markets.

AIG's operating performance reflects implementation of various long-term strategies and defined goals in its various operating segments. A primary goal of AIG in managing its General Insurance operations is to achieve an underwriting profit. To achieve this goal, AIG must be disciplined in its risk selection and premiums must be adequate and terms and conditions appropriate to cover the risk accepted. AIG also believes in strict control of expenses.

A central focus of AIG operations in recent years is the development and expansion of new distribution channels. In 2005 and the first six months of 2006, AIG expanded its distribution channels, which now include banks, credit card companies and television-media home shopping in many Asian countries. Examples of new distribution channels used both domestically and overseas include banks, affinity groups, direct response and e-commerce.

AIG patiently builds relationships in markets around the world where it sees long-term growth opportunities. For example, the fact that AIG has the only wholly-owned foreign life insurance operations in eight cities in China is the result of relationships developed over nearly 30 years. AIG's more recent extensions of operations into India, Vietnam, Russia and other emerging markets reflect the same growth strategy. Moreover, AIG believes in investing in the economies and infrastructures of these countries and growing with them. When AIG companies enter a new jurisdiction, they typically offer both basic protection and savings products. As the economies evolve, AIG's products evolve with them, to more sophisticated and investment-oriented models.

Growth for AIG may be generated both internally and through acquisitions which both fulfill strategic goals and offer adequate return on capital. Recently AIG acquired Travel Guard International, one of the nation's leading providers of travel insurance programs and emergency travel assistance, and acquired Central Insurance Co., Ltd., a leading general insurance company in Taiwan.

Consolidated Results

The following table summarizes AIG's revenues, income before income taxes, minority interest and cumulative effect of an accounting change and net income for the three and six-month periods ended June 30, 2006 and 2005:

	Three Months Ended June 30,		Six Months Ended June 30,	
(in millions)	**2006**	2005	**2006**	2005
Total revenues	**$26,743**	$27,903	**$54,002**	$55,105
Income before income taxes, minority interest and cumulative effect of an accounting change	**5,241**	6,701	**10,034**	12,350
Net income	**$ 3,190**	$ 4,489	**$ 6,385**	$ 8,288

Revenues in the second quarter and first six months of 2006 decreased 4 percent and 2 percent, respectively, largely as a result of decreased revenues in the Financial Services segment from hedging activities that do not qualify for hedge accounting treatment under FAS 133, the effects of which are reported in other revenues. The decrease was offset by the growth in net premiums earned from global General Insurance operations as well as growth in both General Insurance

and Life Insurance & Retirement Services net investment income, Life Insurance & Retirement Services GAAP premiums and increased revenues from Asset Management activities.

Income before income taxes, minority interest and cumulative effect of an accounting change in the three and six-month periods ended June 30, 2006 decreased 22 percent and 19 percent, respectively. Increases in General Insurance and Asset Management operating income were more than offset by an operating loss in Financial Services driven by the effects of hedging activities that do not qualify for hedge accounting treatment under FAS 133. Life Insurance & Retirement Services operating income decreased slightly in the second quarter of 2006 from the comparable prior year period, and increased 8 percent on a year-to-date basis.

Results for the first six months of 2006 were negatively affected by a one-time charge relating to the Starr tender offer ($54 million before and after tax) and an additional allowance for losses in AIG Credit Card Company (Taiwan) ($88 million before and after tax), both of which were recorded in first quarter of 2006.

During the second quarter of 2006, as part of its continuing remediation efforts, AIG identified and recorded an out of period adjustment related to the accounting for certain interests in unit investment trusts in accordance with FIN 46(R), "Consolidation of Variable Interest Entities" and APB Opinion No. 18, "The Equity Method of Accounting for Investments in Common Stock." These investments had previously been accounted for as available for sale securities, with changes in market values being reflected in other comprehensive income, net of deferred income taxes. Beginning with the second quarter of 2006, the changes in market values are included in AIG's net investment income. The adjustment decreased Unrealized appreciation (depreciation) of investments — net of reclassification adjustments, and the related Deferred income tax benefit (expense), in the Consolidated Statement of Comprehensive Income (Loss) by approximately $576 million and approximately $202 million, respectively, for the three and six-month periods ended June 30, 2006 and increased Net investment income by $653 million, increased Incurred policy losses and benefits, related to certain participating policyholder funds, by $77 million, and increased Income taxes by $202 million in the Consolidated Statement of Income for the three and six-month periods ended June 30, 2006. There was no effect on Total shareholders' equity as of June 30, 2006 or December 31, 2005.

In the second quarter of 2006, AIG also recorded other out of period adjustments of $85 million ($55 million after tax) of interest income related to interest earned on deposit contracts and $32 million ($21 million after tax) of expenses related to the remediation of a material weakness in controls over certain balance sheet reconciliations. AIG also recorded other out of period adjustments in the first quarter of 2006 of $61 million (before and after tax) of expenses related to the SICO plans, $59 million ($38 million after tax) of expenses related to deferred advertising costs in General Insurance, $300 million ($145 million after tax) of revenues related to the remediation of a material weakness in accounting for certain derivative transactions under FAS 133, and $126 million of income tax expense related to AIG's remediation of a material weakness in controls over income tax accounting.

The effective income tax rate increased from 29.9 percent in the first quarter of 2006 to 32.2 percent and 31.1 percent for the three and six-month periods ended June 30, 2006, respectively, reflecting changes in the sources of foreign taxable income and the effect of the phase out of synfuel tax credits on the estimated full year tax rate.

The following table summarizes the operations of each principal segment for the three and six-month periods ended June 30, 2006 and 2005. (See also Note 2 of Notes to Consolidated Financial Statements).

	Three Months Ended June 30,		Six Months Ended June 30,	
(in millions)	**2006**	2005	**2006**	2005
Revenues[(a)]:				
General Insurance[(b)(h)]	**$12,167**	$11,405	**$23,823**	$22,624
Life Insurance & Retirement Services[(c)(h)]	**11,705**	11,517	**24,344**	23,292
Financial Services[(d)]	**1,226**	3,778	**2,841**	6,214
Asset Management[(e)]	**1,621**	1,219	**2,860**	2,596
Other	**24**	(16)	**134**	379
Consolidated	**$26,743**	$27,903	**$54,002**	$55,105
Operating Income (loss)[(a)(f)]:				
General Insurance[(h)]	**$ 2,863**	$ 1,885	**$ 5,194**	$ 3,527
Life Insurance & Retirement Services[(g)(h)]	**2,302**	2,324	**4,857**	4,505
Financial Services[(g)]	**(548)**	2,214	**(707)**	3,259
Asset Management	**811**	524	**1,272**	1,114
Other	**(187)**	(246)	**(582)**	(55)
Consolidated	**$ 5,241**	$ 6,701	**$10,034**	$12,350

(a) Includes the effect of hedging activities that do not qualify for hedge accounting treatment under FAS 133, including the related foreign exchange gains and losses. For the three-month periods ended June 30, 2006 and 2005, the effect was $(1.08) billion and $1.63 billion, respectively, in revenues and $(1.08) billion and $1.61 billion, respectively, in operating income. For the six-month periods ended June 30, 2006 and 2005, the effect was $(1.30) billion and $2.56 billion, respectively, in revenues and $(1.30) billion and $2.62 billion, respectively, in operating income. These amounts result primarily from interest rate and foreign currency derivatives which are hedging available for sale securities and borrowings.

(b) Represents the sum of General Insurance net premiums earned, net investment income and realized capital gains (losses).

(c) Represents the sum of Life Insurance & Retirement Services GAAP premiums, net investment income and realized capital gains (losses).

(d) Represents interest, lease and finance charges.

(e) Represents management and advisory fees and net investment income with respect to GICs.

(f) Represents income before income taxes, minority interest and cumulative effect of an accounting change.

(g) Results of operations of AIG Credit Card Company (Taiwan) are shared equally by the Life Insurance & Retirement Services segment and the Financial Services segment. Additional allowances of $44 million were recorded in the first quarter of 2006, by each segment, for losses in these credit card operations.

(h) Includes the effect of an out of period adjustment related to the accounting for certain interests in unit investment trusts. For the three and six-month periods ended June 30, 2006 the effect was an increase of $432 million in revenues and operating income for General Insurance and an increase of $221 million and $144 million in revenues and operating income, respectively, for Life Insurance & Retirement Services.

General Insurance

AIG's General Insurance operations provide property and casualty products and services throughout the world. The increase in General Insurance operating income in the three and six-month periods ended June 30, 2006 compared to the same periods of 2005 was primarily attributable to improvement in underwriting results for the Domestic Brokerage Group (DBG). General Insurance operating income included adverse development in the first six months of 2006 and 2005 from catastrophes in prior years, which were more than offset by favorable development on non-catastrophe losses. Operating income for the three and six-month periods ended June 30, 2006 also increased due to the effect of the out of period adjustment related to the accounting for certain interests in unit investment trusts.

Life Insurance & Retirement Services

AIG's Life Insurance & Retirement Services operations provide insurance, financial and investment products throughout the world. Foreign operations provided approximately 75 percent and 63 percent of AIG's Life Insurance & Retirement Services operating income for the three months ended June 30, 2006 and 2005, respectively, and 70 percent and 59 percent, respectively, for the first six months of 2006 and 2005.

Life Insurance & Retirement Services operating income decreased slightly in the second quarter of 2006 when compared to the same period of 2005 as a result of lower earnings in the Domestic Life Operations and higher realized capital losses, which were partially offset by the effect of an out of period adjustment related to the accounting for certain interests in unit investment trusts and growth in earnings from Foreign Life and Domestic Retirement Services. Realized capital losses included in revenues and operating income were $218 million in the second quarter of 2006 compared to realized capital gains of $46 million in the same period of 2005.

Life Insurance & Retirement Services operating income increased by 8 percent in the first six months of 2006 when compared to the same period of 2005 due, in part, to the effect of an out of period adjustment related to the accounting for certain interests in unit investment trusts. Realized capital losses included in revenues and operating income were $60 million in the first six months of 2006 compared to realized capital losses of $36 million in the same period of 2005.

Financial Services

AIG's Financial Services subsidiaries engage in diversified activities including aircraft and equipment leasing, capital market transactions, consumer finance and insurance premium financing.

Financial Services incurred operating losses in the three and six-month periods ended June 30, 2006 compared to the same periods of 2005, due to the effect of hedge activities that do not qualify for hedge accounting treatment under FAS 133. Fluctuations in revenues and operating income from quarter to quarter are not unusual because of the transaction-oriented nature of Capital Markets operations and the effect of not qualifying for hedge accounting treatment under FAS 133 for hedges on securities available for sale and borrowings.

Asset Management

AIG's Asset Management operations include institutional and retail asset management and broker dealer services and AIG's spread-based investment businesses. The AIG Matched Investment Program (MIP), which was launched in September of 2005, is replacing AIG's GIC program as AIG's principal spread-based investment activity. The GIC program products and services are offered to individuals and institutions, both domestically and overseas.

Asset Management operating income increased 55 percent for the second quarter of 2006 when compared to the same period of 2005 due to continued strong asset flows and increased transaction driven fees and the effects of FIN 46(R) and EITF 04-5 which are offset in minority interest expense, which is not a component of operating income; operating income also increased 14 percent in the first six months of 2006 when compared to the same period of 2005 reflecting strong results in the segment's core businesses and the effects of FIN 46(R) and EITF 04-5 which are offset in minority interest expense, which is not a component of operating income.

Capital Resources

At June 30, 2006, AIG had total consolidated shareholders' equity of $87.71 billion and total consolidated borrowings of $126.1 billion. At that date, $110.8 billion of such borrowings were either not guaranteed by AIG or were AIGFP's

matched borrowings under obligations of guaranteed investment agreements (GIAs), liabilities connected to trust preferred stock, or matched notes and bonds payable.

AIG has not purchased any shares of its common stock under its existing common stock repurchase authorization during 2006.

Liquidity

At June 30, 2006, AIG's consolidated invested assets included $23.33 billion in cash and short-term investments. Consolidated net cash provided from operating activities in the first six months of 2006 amounted to $7.0 billion. AIG believes that its liquid assets, cash provided by operations and access to the capital markets will enable it to meet any anticipated cash requirements.

Outlook

Despite industry price erosion in some classes of general insurance, AIG expects to continue to identify profitable opportunities and build attractive new General Insurance businesses as a result of AIG's broad product line and extensive distribution networks. In December 2005, American International Underwriters Overseas, Ltd. (AIUO) received a license from the government of Vietnam to operate a wholly owned general insurance company in Vietnam. This license, the first general insurance license granted by Vietnam to a U.S.-based insurance organization, permits AIG to operate a general insurance company throughout Vietnam.

During the second quarter of 2006, the Canadian Parliament passed legislation that will allow UGC to begin writing business in Canada, the world's second largest mortgage guaranty market, when provincial licenses are issued.

In China, AIG currently has wholly-owned life insurance operations in eight cities. In April 2006, applications for provincial expansion of AIG's life insurance operations in Guangdong and Jiangsu and of general insurance operations in Guangdong were approved. AIG's operations are expanding resources in these regions with the opening of additional sales and service centers. AIG's application to serve the group insurance market was also approved.

In Japan, earnings growth for AIG Star Life Insurance Co., Ltd. and AIG Edison Life Insurance Company reflects the runoff of the more profitable in-force business in comparison to new business currently being generated. In May 2006, AIG announced the merger of these companies, which is expected to be completed by October 2007 after meeting all regulatory requirements. The merger is expected to enhance the combined entity's ability to grow new business by expanding distribution and gaining efficiency of scale. In the fiscal year ended March 31, 2006, AIG's life operations in Japan retained their position as the largest foreign life operation on a total premium basis. AIG has developed a leadership position in the distribution of annuities through banks in both Japan and Korea. Also, American Life Insurance Company (ALICO) has launched new life products to the Japan bank market after further deregulation of banks in December 2005. AIG is a leader in direct marketing through sponsors and in the broad market in Japan and Korea. AIG also is investing in expanding distribution channels with emphasis in India, Korea and Vietnam.

Domestically, AIG anticipates its Life Insurance & Retirement Services businesses to continue growing in 2006 through distribution channel expansion and new and enhanced products. The home service operation, which is expected to be a slow growth business, has not met business objectives, although its cash flow has been strong. Domestic group life/health results continue to be weak, reflecting the ongoing restructuring activities which may result in the exiting of certain product lines. AIG Retirement Services individual fixed annuities business will continue to be challenged due to the interest rate environment and increased competition from bank products, while variable annuity products with living benefits will continue to be the product of consumer choice.

Changes in market conditions in the aircraft leasing business are not immediately apparent in operating results. Lease rates have firmed as a result of strong demand from the global commercial aviation market, especially in Asia. Sales have increased and AIG expects an increasing level of interest from a variety of purchasers. However, higher interest rates are expected to continue to compress lease margins. AIG's Consumer Finance operations overseas were negatively affected in the first quarter of 2006 by industry-wide credit deterioration in the Taiwan credit card market. The operating results of AIG's Consumer Finance operations in the U.S. could be affected by the residential housing market, interest rates and unemployment.

AIG's GIC program is in runoff and is being replaced by the new MIP, which was launched in September 2005. AIG expects the MIP to be AIG's principal spread-based investment activity. AIG's credit spreads will affect the profitability of this business.

AIG has many promising growth initiatives underway around the world. Cooperative agreements such as those with PICC Property and Casualty Company Limited and various banks in the U.S., Japan and Korea are expected to expand distribution networks for AIG's products and provide models for future growth.

Critical Accounting Estimates

AIG considers its most critical accounting estimates those with respect to reserves for losses and loss expenses, future policy benefits for life and accident and health contracts,

deferred policy acquisition costs, estimated gross profits for investment-oriented products, fair value determinations for certain Capital Markets assets and liabilities, other-than-temporary declines in the value of investments and flight equipment recoverability. These accounting estimates require the use of assumptions about matters, some of which are highly uncertain at the time of estimation. To the extent actual experience differs from the assumptions used, AIG's results of operations would be directly affected.

Throughout this Management's Discussion and Analysis of Financial Condition and Results of Operations, AIG's critical accounting estimates are discussed in detail. The major categories for which assumptions are developed and used to establish each critical accounting estimate are highlighted below.

Reserves for Losses and Loss Expenses and Reinsurance Recoverable (General Insurance):

- *Loss trend factors:* used to establish expected loss ratios for subsequent accident years based on premium rate adequacy and the projected loss ratio with respect to prior accident years.
- *Expected loss ratios for the latest accident year:* for example, accident year 2005 for the year end 2005 loss reserve analysis. For low frequency, high severity classes such as excess casualty, expected loss ratios generally are utilized for at least the three most recent accident years.
- *Loss development factors:* used to project the reported losses for each accident year to an ultimate amount.
- *Reinsurance recoverable on unpaid losses:* the expected recoveries from reinsurers on losses that have not yet been reported and/or settled.

Future Policy Benefits for Life and Accident and Health Contracts (Life Insurance & Retirement Services):

- *Interest rates:* which vary by geographical region, year of issuance and products.
- *Mortality, morbidity and surrender rates:* based upon actual experience by geographical region modified to allow for variation in policy form.

Estimated Gross Profits (Life Insurance & Retirement Services):

- *Estimated gross profits* to be realized over the estimated duration of the contracts (investment-oriented products) affect the carrying value of deferred policy acquisition costs under FAS 97. Estimated gross profits include investment income and gains and losses on investments less required interest, actual mortality and other expenses.

Deferred Policy Acquisition Costs (Life Insurance & Retirement Services):

- Recoverability based on current and future expected profitability, which is affected by interest rates, foreign exchange rates, mortality experience, and policy persistency.

Deferred Policy Acquisition Costs (General Insurance):

- Recoverability and eligibility based upon the current terms and profitability of the underlying insurance contracts.

Fair Value Determinations of Certain Assets and Liabilities (Financial Services – Capital Markets):

- *Valuation models:* utilizing factors, such as market liquidity and current interest, foreign exchange and volatility rates.
- AIG attempts to secure reliable and independent current market price data, such as published exchange rates from external subscription services such as Bloomberg or Reuters or third-party broker quotes for use in its model. When such prices are not available, AIG uses an internal methodology, which includes interpolation and extrapolation from verifiable prices from trades occurring on dates nearest to the dates of the transactions.

Other-Than-Temporary Declines in the Value of Investments:

A security is considered a candidate for other-than-temporary impairment based upon the following criteria:

- Trading at a significant (25 percent or more) discount to par or amortized cost (if lower) for an extended period of time (nine months or longer).
- The occurrence of a discrete credit event resulting in the debtor defaulting or seeking bankruptcy or insolvency protection or voluntary reorganization.
- The probability of non-realization of a full recovery on its investment, irrespective of the occurrence of one of the foregoing events.

At each balance sheet date, AIG evaluates its securities holdings in an unrealized loss position. Where AIG does not intend to hold such securities until they have fully recovered their carrying value, based on the circumstances present at the date of evaluation, AIG records the unrealized loss in income. If events or circumstances change, such as unexpected changes in creditworthiness of the obligor, general interest rate environment, tax circumstances, liquidity events, and statutory capital management considerations among others, AIG revisits its intent to determine if a loss should be recorded in income. Further, if a loss is recognized from a sale subsequent to a balance sheet date pursuant to these changes in circumstances, the loss is recognized in the period in which the intent to hold the securities to recovery no longer exists.

Flight Equipment — Recoverability (Financial Services):

- *Expected undiscounted future net cash flows:* based upon current lease rates, projected future lease rates and estimated terminal values of each aircraft based on third party information.

Operating Review

General Insurance Operations

AIG's General Insurance subsidiaries are multiple line companies writing substantially all lines of property and casualty insurance both domestically and abroad.

Domestic General Insurance operations are comprised of DBG, which includes the operations of The Hartford Steam Boiler Inspection and Insurance Company (HSB); Transatlantic Holdings, Inc. (Transatlantic); Personal Lines, including 21st Century Insurance Group (21st Century); and United Guaranty Corporation (UGC).

AIG's primary domestic division is DBG. DBG's business in the United States and Canada is conducted through its General Insurance subsidiaries including American Home Assurance Company (American Home), National Union Fire Insurance Company of Pittsburgh, Pa. (National Union), Lexington Insurance Company (Lexington) and certain other General Insurance company subsidiaries of AIG.

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

In addition to writing substantially all classes of business insurance, including large commercial or industrial property insurance, excess liability, inland marine, environmental, workers compensation and excess and umbrella coverages, DBG offers many specialized forms of insurance such as aviation, accident and health, equipment breakdown, directors and officers liability (D&O), difference-in-conditions, kidnap-ransom, export credit and political risk, and various types of professional errors and omissions coverages. The AIG Risk Management operation provides insurance and risk management programs for large corporate customers. The AIG Risk Finance operation is a leading provider of customized structured insurance products. Also included in DBG are the operations of AIG Environmental, which focuses specifically on providing specialty products to clients with environmental exposures. Lexington writes surplus lines, those risks for which conventional insurance companies do not readily provide insurance coverage, either because of complexity or because the coverage does not lend itself to conventional contracts.

Certain of the products of the DBG companies include funding components or have been structured in a manner such that little or no insurance risk is actually transferred. Funds received in connection with these products are recorded as deposits and included in other liabilities, rather than premiums and incurred losses.

The AIG Worldsource Division introduces and coordinates AIG's products and services to U.S.-based multinational clients and foreign corporations doing business in the U.S.

Transatlantic subsidiaries offer reinsurance capacity on both a treaty and facultative basis both in the U.S. and abroad. Transatlantic structures programs for a full range of property and casualty products with an emphasis on specialty risk.

AIG's Personal Lines operations provide automobile insurance through AIG Direct, the mass marketing operation of AIG, Agency Auto Division and 21st Century, as well as a broad range of coverages for high net-worth individuals through the AIG Private Client Group.

The main business of the UGC subsidiaries is the issuance of residential mortgage guaranty insurance, both domestically and internationally, on conventional first lien mortgages for the purchase or refinance of one to four family residences. UGC subsidiaries also write second lien and private student loan guaranty insurance.

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

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

A critical discipline of a successful general insurance business is the objective to produce profit from underwriting activities exclusive of investment-related income. When underwriting is not profitable, premiums are inadequate to pay for insured losses and underwriting related expenses. In these situations, the addition of general insurance related investment income and realized capital gains may, however, enable a general insurance business to produce operating income. For these reasons, AIG views underwriting results to be critical in the overall evaluation of performance.

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

GAAP provides for the recognition of expenses at the same time revenues are earned, the accounting principle of matching. Therefore, acquisition expenses are deferred and amortized over the period the related net premiums written are earned. DAC is reviewed for recoverability, and such review requires management judgment. (See also "Critical Accounting Estimates" herein.)

AIG, along with most General Insurance companies, uses the loss ratio, the expense ratio and the combined ratio as measures of underwriting performance. The loss ratio is the sum of losses and loss expenses incurred divided by net premiums earned. The expense ratio is statutory underwriting expenses divided by net premiums written. The combined ratio is the sum of the loss ratio and the expense ratio. These ratios are relative measurements that describe, for every $100 of net premiums earned or written, the cost of losses and statutory expenses, respectively. The combined ratio presents the total cost per $100 of premium production. A combined ratio below 100 demonstrates underwriting profit; a combined ratio above 100 demonstrates underwriting loss.

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

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

General Insurance operating income is comprised of statutory underwriting results, changes in DAC, net investment income and realized capital gains and losses. Operating income, as well as net premiums written, net premiums earned, net investment income and realized capital gains (losses) and statutory ratios for the three and six-month periods ended June 30, 2006 and 2005 were as follows:

	Three Months Ended June 30,		Six Months Ended June 30,	
(in millions, except ratios)	**2006**	2005	**2006**	2005
Net premiums written:				
Domestic General				
DBG	**$ 6,480**	$ 5,846	**$12,380**	$11,566
Transatlantic	**914**	884	**1,828**	1,769
Personal Lines	**1,180**	1,173	**2,378**	2,359
Mortgage Guaranty	**193**	145	**390**	310
Foreign General	**2,867**	2,596	**5,913**	5,430
Total	**$11,634**	$10,644	**$22,889**	$21,434
Net premiums earned:				
Domestic General				
DBG	**$ 5,836**	$ 5,587	**$11,599**	$11,160
Transatlantic	**909**	862	**1,817**	1,750
Personal Lines	**1,167**	1,157	**2,326**	2,277
Mortgage Guaranty	**179**	143	**345**	283
Foreign General[(a)]	**2,587**	2,483	**5,061**	4,902
Total	**$10,678**	$10,232	**$21,148**	$20,372
Net investment income:				
Domestic General				
DBG	**$ 813**	$ 555	**$ 1,558**	$ 1,214
Transatlantic	**108**	84	**210**	169
Personal Lines	**55**	54	**112**	106
Mortgage Guaranty	**36**	31	**68**	59
Intercompany adjustments and eliminations – net	**–**	(1)	**–**	–
Foreign General[(b)]	**602**	337	**784**	527
Total	**$ 1,614**	$ 1,060	**$ 2,732**	$ 2,075

(in millions, except ratios)	Three Months Ended June 30, 2006	Three Months Ended June 30, 2005	Six Months Ended June 30, 2006	Six Months Ended June 30, 2005
Realized capital gains (losses)	**(125)**	113	**(57)**	177
Operating Income[c]:				
Domestic General				
DBG	**$ 1,534**	$ 805	**$ 2,891**	$ 1,518
Transatlantic	**143**	99	**284**	213
Personal Lines	**118**	102	**219**	211
Mortgage Guaranty	**107**	109	**216**	213
Foreign General[b][d]	**961**	771	**1,582**	1,367
Reclassifications and Eliminations	**–**	(1)	**2**	5
Total	**$ 2,863**	$ 1,885	**$ 5,194**	$ 3,527
Statutory underwriting profit[c][f]				
Domestic General				
DBG	**$ 696**	$ 190	**$ 1,223**	$ 246
Transatlantic	**33**	12	**63**	32
Personal Lines	**53**	44	**93**	85
Mortgage Guaranty	**73**	83	**143**	152
Foreign General[d]	**368**	411	**658**	741
Total	**$ 1,223**	$ 740	**$ 2,180**	$ 1,256
Domestic General:				
Loss Ratio	**67.79**	75.07	**69.36**	76.15
Expense Ratio	**19.97**	19.93	**20.07**	19.85
Combined Ratio	**87.76**	95.00	**89.43**	96.00
Foreign General:				
Loss Ratio[a]	**49.43**	52.31	**51.04**	53.35
Expense Ratio[d][e]	**32.82**	29.75	**30.77**	28.44
Combined ratio	**82.25**	82.06	**81.81**	81.79
Consolidated:				
Loss Ratio[c]	**63.34**	69.55	**64.98**	70.66
Expense Ratio	**23.13**	22.33	**22.84**	22.03
Combined Ratio	**86.47**	91.88	**87.82**	92.69

(a) Income statement accounts expressed in non-functional currencies are translated into U.S. dollars using average exchange rates.

(b) Includes the effect of an out of period adjustment related to the accounting for certain interests in unit investment trusts. For the three and six-month periods ended June 30, 2006 the effect was an increase of $412 million.

(c) Includes a reduction in incurred losses in the three-month period ended June 30, 2006 of $51 million and additional losses incurred and net reinstatement premiums in the three-month period ended June 30, 2005 of $27 million, related primarily to prior year catastrophes, resulting in (decreases) increases of (0.49) points and 0.26 points, respectively, in the consolidated General Insurance loss ratio. The effect on the six-month periods ended June 30, 2006 and 2005 included $48 million and $198 million, respectively, of additional losses incurred and net reinstatement premiums primarily relating to prior year catastrophes, resulting in increases of 0.22 points and 0.96 points, respectively, in the consolidated General Insurance loss ratio.

(d) Includes the results of wholly owned AIU agencies.

(e) Includes amortization of advertising costs.

(f) Statutory underwriting profit (loss) is a measure that U.S. domiciled insurance companies are required to report to their regulatory authorities. The following table reconciles statutory underwriting profit (loss) to income before income taxes, minority interest and cumulative effect of an accounting change for the General Insurance segment for the three and six month periods ended June 30, 2006 and 2005.

(in millions)	Domestic Brokerage Group	Transatlantic	Personal Lines	Mortgage Guaranty	Foreign General	Reclassifications and Eliminations	Total
Three months ended June 30, 2006:							
Statutory underwriting profit	**$ 696**	**$ 33**	**$ 53**	**$ 73**	**$ 368**	**$ –**	**$1,223**
Increase in deferred acquisition costs	**69**	**4**	**9**	**1**	**68**	**–**	**151**
Net investment income	**813**	**108**	**55**	**36**	**602**	**–**	**1,614**
Realized capital gains (losses)	**(44)**	**(2)**	**1**	**(3)**	**(77)**	**–**	**(125)**
Income before income taxes, minority interest and cumulative effect of an accounting change	**$1,534**	**$143**	**$118**	**$107**	**$ 961**	**$ –**	**$2,863**
Three months ended June 30, 2005:							
Statutory underwriting profit	$ 190	$ 12	$ 44	$ 83	$ 411	$ –	$ 740
Increase (decrease) in deferred acquisition costs	(39)	1	6	(4)	8	–	(28)
Net investment income	555	84	54	31	337	(1)	1,060
Realized capital gains (losses)	99	2	(2)	(1)	15	–	113
Income before income taxes, minority interest and cumulative effect of an accounting change	$ 805	$ 99	$102	$109	$ 771	$ (1)	$1,885
Six months ended June 30, 2006:							
Statutory underwriting profit	**$1,223**	**$ 63**	**$ 93**	**$143**	**$ 658**	**$ –**	**$2,180**
Increase in deferred acquisition costs	**107**	**7**	**14**	**8**	**203**	**–**	**339**
Net investment income	**1,558**	**210**	**112**	**68**	**784**	**–**	**2,732**
Realized capital gains (losses)	**3**	**4**	**–**	**(3)**	**(63)**	**2**	**(57)**
Income before income taxes, minority interest and cumulative effect of an accounting change	**$2,891**	**$284**	**$219**	**$216**	**$1,582**	**$ 2**	**$5,194**
Six months ended June 30, 2005:							
Statutory underwriting profit	$ 246	$ 32	$ 85	$152	$ 741	$ –	$1,256
Increase (decrease) in deferred acquisition costs	(98)	1	23	2	91	–	19
Net investment income	1,214	169	106	59	527	–	2,075
Realized capital gains (losses)	156	11	(3)	–	8	5	177
Income before income taxes, minority interest and cumulative effect of an accounting change	$1,518	$213	$211	$213	$1,367	$ 5	$3,527

AIG transacts business in most major foreign currencies. The following table summarizes the effect of changes in foreign currency exchange rates on the growth of General Insurance net premiums written for the three and six-month periods ended June 30, 2006:

	Three Months Ended June 30, 2006	Six Months Ended June 30, 2006
Growth in original currency	**9.7%**	**7.9%**
Foreign exchange effect	**(0.4)**	**(1.1)**
Growth as reported in U.S. dollars	**9.3%**	**6.8%**

General Insurance Results

General Insurance operating income increased 52 percent in the second quarter of 2006 compared to the same period in 2005 due primarily to improvement in statutory underwriting profit for DBG as a result of improved loss ratios for the current accident year compared to the loss ratios recorded in the second quarter of 2005 for accident year 2005, as well as growth in net investment income. Included in net investment income in the second quarter of 2006 is the $432 million effect of an out of period adjustment related to the accounting for certain interests in unit investment trusts. The combined ratio improved to 86.5 during the second quarter of 2006, a reduction of 5.4 points from the prior period in 2005, led by a reduction in the loss ratio of 6.2 points. Net premiums written increased 9 percent in the second quarter of 2006 compared to the same period in 2005 as domestic property rates improved and submission activity increased in the aftermath of the 2005 hurricanes and through the expansion of distribution channels within Foreign General. The increase in

net premiums written was tempered by an increase in ceded reinsurance necessary to manage the increase in property exposures retained by AIG. AIG is evaluating additional reinsurance programs to manage retained property exposures as direct property business increases.

General Insurance operating income increased 47 percent in the first six months of 2006 compared to the same period of 2005 due to improvement in statutory underwriting profit for DBG as a result of improved loss ratios for the current accident year compared to the loss ratios recorded in the first six months of 2005 for accident year 2005, as well as growth in net investment income. Included in net investment income for the first six months of 2006 is the $432 million effect of the aforementioned out of period adjustment. The combined ratio improved to 87.8, a reduction of 4.9 points from the first six months of 2005, led by a reduction in the loss ratio of 5.7 points. Net premiums written increased 7 percent as domestic property rates improved and submission activity increased in the aftermath of the 2005 hurricanes and through the expansion of distribution channels within Foreign General.

Quarterly DBG Results

DBG's net premiums written increased 11 percent in the second quarter of 2006 compared to the same period in 2005 as property rates improved and submission activity increased in the aftermath of the 2005 hurricanes. DBG attributes the increase in submissions to its strong distribution channels and overall financial strength in comparison to many insurers that experienced significant losses and reductions of surplus as a result of the hurricanes. This increase was tempered by an increase in ceded reinsurance necessary to manage the level of property exposures retained by DBG.

Operating income increased 91 percent to $1.53 billion in the second quarter of 2006 compared to the same period in 2005, reflecting increases in statutory underwriting profit and net investment income. The improvement in DBG's statutory underwriting profit for the second quarter of 2006 was primarily due to lower accident year loss ratios for the 2006 accident year compared to the loss ratios recorded in the second quarter of 2005 for accident year 2005. In addition, the second quarter of 2006 includes a $53 million reduction in the estimated ultimate losses related to prior year hurricanes compared to the same period of 2005 which included an insignificant increase in losses related to prior year hurricanes. Favorable reserve development on non-catastrophic prior year losses totaled $57 million for the second quarter of 2006 compared to adverse development of $112 million for the same period of 2005. The 2006 development relates primarily to classes of business which did not require reserve strengthening in connection with AIG's year-end 2005 reserve study.

DBG's expense ratio decreased slightly in the second quarter of 2006 to 17.9 compared to 18.1 in the same period of 2005. Direct acquisition expenses declined, reflecting an increase in lines of business, such as property, that have a lower commission rate, as well as a modest decrease in overall commission rates. Net acquisition expenses declined due to the items cited above as well as the new quota share reinsurance program added in 2006 to manage the level of property exposures retained by DBG. Other operating expense as a percent of net premium written increased primarily due to an increase in bad debt expense, due largely to an out of period adjustment of $32 million relating to reconciliation remediation activities.

Year-to-date DBG Results

DBG's net premiums written increased 7 percent in the first six months of 2006 compared to the same period of 2005 due to property rate increases as well as increases in submission activity in the aftermath of the 2005 hurricanes. Operating income increased 90 percent to $2.89 billion in the first six months of 2006 reflecting increases in statutory underwriting profit and net investment income. The improvement in DBG's statutory underwriting profit for 2006 was due to lower accident year loss ratios for the 2006 accident year compared to the loss ratios recorded in the first six months of 2005 for accident year 2005. In addition, year to date 2006 operating income includes a $25 million reduction in the estimated ultimate losses related to prior year hurricanes compared to the same period of 2005 which included $118 million of increased losses related to prior year hurricanes. Favorable reserve development on non-catastrophic prior year losses totaled $62 million for the first six months of 2006 compared to adverse development of $215 million for the same period of 2005. The 2006 development relates primarily to classes of business which did not require reserve strengthening in connection with AIG's year-end 2005 reserve study.

DBG's expense ratio decreased slightly to 18.1 compared to 18.3 in the first six months of 2006. Direct acquisition expenses declined, reflecting an increase in lines of business such as property that have a lower commission rate as well as a modest decrease in overall commission rates. Net acquisition expenses declined due to the items cited above as well as the new quota share reinsurance program added in 2006 to manage the level of property exposures retained by DBG. Other operating expenses increased primarily due to an increase in bad debt expense, partially offset by a favorable $23 million out of period adjustment relating to reconciliation remediation activities.

Quarterly Transatlantic Results

Transatlantic's net premiums written and net premiums earned in the second quarter of 2006 increased by 3 percent and 5 percent, respectively, when compared to the same period in 2005 primarily due to increases in domestic auto liability and specialty casualty net premiums written. These increases were partially offset by decreases in international property and auto liability premiums. Second quarter 2006 operating income increased $44 million, due largely to increased net investment income and lower catastrophe incurred losses and net reinstatement premiums related to prior year catastrophes.

Year-to-date Transatlantic Results

Transatlantic's net premiums written and net premiums earned increased in the first six months of 2006 by 3 percent and 4 percent, respectively, compared to the same period of 2005 due primarily to increases in domestic specialty casualty and property net premiums written. These increases were offset, in part, by decreases in international premiums caused, in part, by the adverse effect of changes in foreign currency exchange rates between periods, with the most significant decreases in the auto liability and property lines. Operating income increased in the first six months of 2006 compared to the same period of 2005 due to increased net investment income and improved statutory underwriting profit, resulting largely from reduced net catastrophe costs (including the effect of net reinstatement premiums), and lower net adverse development on loss reserves, offset, in part, by higher commission costs.

Quarterly Personal Lines Results

Personal Lines net premiums written increased slightly in the second quarter of 2006 compared to the same period in 2005, as growth in the Private Client Group and Agency Auto divisions was offset by the runoff of the involuntary auto business and a small decline in the AIG Direct and 21st Century divisions. The reduction in the involuntary business was a result of terminating an MGA relationship on December 31, 2005. Growth in the Private Client Group spans multiple products as it continues to penetrate the high net worth market. Agency Auto growth was due to expanded agent/broker appointments and enhanced product offerings. AIG Direct premiums were down due to a decline in response rates. 21st Century experienced strong growth outside of California, but not enough to offset the decline in the soft California market. Operating income in the second quarter of 2006 increased from the same period in 2005 driven by a lower combined ratio. The improved loss ratio reflects favorable prior year loss reserve development in the direct businesses. The expense ratio increased from a year ago as 21st Century expenses were up due primarily to its national expansion efforts and higher stock-based compensation. AIG Direct acquisition expenses were up primarily due to lower response rates driving up acquisition cost per policy.

Year-to-date Personal Lines Results

Personal Lines net premiums written increased slightly in the first six months of 2006 compared to the same period in 2005, reflecting growth in the Private Client Group and Agency Auto divisions which offset the runoff of the involuntary auto business and a small decline in the AIG Direct and 21st Century divisions. Operating income was up slightly for the first six months of 2006 compared to the same period of 2005, driven primarily by an increase in net investment income as the combined ratio remained relatively unchanged. The loss ratio in the first six months of 2006 improved from a year ago due to favorable prior year loss development in the AIG Direct and 21st Century businesses, while the expense ratio increased as a result of, among other things, investment in people, technology, national expansion efforts and lower response rates.

Quarterly UGC Results

UGC's net premiums written increased in the second quarter of 2006 when compared to the same period in 2005, primarily driven by growth in domestic second lien and international operations. Operating income during the second quarter of 2006 was down slightly when compared to the same period in 2005 as improved underwriting results in the domestic second lien and international groups and increased investment income were offset by a decline in the domestic first lien business. The loss ratio increased to 33.1 in the second quarter of 2006 from 17.4 in the year ago quarter, a period with an unusually low frequency of defaults. Operating income for the second quarter of 2006 includes favorable development on prior accident years, offset by higher 2006 accident year loss ratios. The increase in the loss ratio also reflects UGC's change in business mix.

Year-to-date UGC Results

UGC's net premiums written were up 26 percent in the first six months of 2006 compared to the same period in 2005 on growth from all business units. Operating income was up slightly for the first six months of 2006 when compared to the same period in 2005, primarily due to an increase in net investment income, which was offset by a 10.6 point increase in the loss ratio to 31.8. The loss ratio for the first six months of 2005 was unusually low due to historically low defaults in the first half of 2005. Operating income for the first six months of 2006 includes favorable development on prior accident years, offset by higher 2006 accident year loss ratios. The increase in the loss ratio also reflects UGC's change in business mix.

Quarterly Foreign General Insurance Results

Foreign General Insurance's net premiums written as reported in U.S. dollars and in original currency increased 10 percent and 12 percent, respectively, in the second quarter of 2006 when compared to the same period in 2005, reflecting growth in both the commercial and consumer lines due to new business, as well as new distribution channels. Foreign General Insurance net premiums written were essentially equally derived from the commercial insurance and consumer lines. The personal accident business in the Far East region increased net premiums written in the second quarter of 2006 from a year ago, but an increase in loss frequency negatively affected operating income. Southeast Asia had increased net premiums written in the second quarter of 2006 when compared to the same period in 2005 in the personal accident business which led to increased operating income. The commercial lines business in both Europe and the United Kingdom increased net premiums written from a year ago due to new business with a resulting increase in operating income compared to the second quarter of 2005. Energy had modest growth in net premiums written, but several high severity losses caused a reduction in second quarter 2006 operating income when compared to the same period of 2005. The Ascot Lloyd's syndicate reported strong growth in net premiums written during the second quarter of 2006 due to rate increases on its U.S. book of business along with contractual terms on renewals that reflect better conditions and higher deductibles. This led to improved operating income from a year ago, but higher than expected profit commission payments related to prior underwriting years totaling $34 million negatively affected operating income during the second quarter of 2006.

The combined ratio for Foreign General Insurance for the second quarter of 2006 was 82.25, slightly higher than the 82.06 in the comparable period of 2005. The Foreign General Insurance loss ratio decreased 2.88 points in the second quarter of 2006 compared to the same period of 2005 due to lower current accident year losses and favorable loss development from prior accident years. The Foreign General Insurance expense ratio increased 3.07 points in the second quarter of 2006 from the same period in 2005 principally due to higher commissions, employee compensation costs and accelerated amortization of advertising costs.

Year-to-date Foreign General Insurance Results

Foreign General Insurance's net premiums written as reported in U.S. dollars and in original currency increased 9 percent and 13 percent, respectively, in the first six months of 2006 when compared to the same period in 2005, reflecting growth in both the commercial and consumer lines. The personal accident business in the Far East region, the commercial lines business in both Europe and the United Kingdom, and the Ascot Lloyd's syndicate all contributed to the growth in net premiums written. Rate decreases in the commercial lines business in the United Kingdom, additional losses incurred relating to 2005 catastrophes and higher than expected profit commission payments related to prior underwriting years for Ascot Lloyd's had a negative effect on operating income in the first six months of 2006 when compared to the same period of 2005.

The combined ratio for Foreign General Insurance for the first six months of 2006 was 81.81, essentially unchanged from the comparable period of 2005. The Foreign General Insurance loss ratio decreased 2.31 points in the first six months of 2006 from the same period of 2005 due to lower current accident year losses for 2006 and favorable loss development from prior accident years, excluding catastrophe losses. The Foreign General Insurance expense ratio increased 2.33 points in the first six months of 2006 from the same period in 2005 principally due to higher commissions, employee compensation costs and accelerated amortization of advertising costs.

General Insurance Net Investment Income

General Insurance net investment income increased by $554 million and $657 million in the second quarter and the first six months of 2006, respectively, when compared to the same periods of 2005, principally due to the effects of an out of period adjustment of $432 million related to the accounting for certain interests in unit investment trusts and an $85 million out of period adjustment related to interest earned on a DBG deposit contract. The increase also reflects higher interest income, strong cash flows, including the effect of capital contributions from the parent, higher interest rates and the positive effect of compounding previously earned and reinvested net investment income as well as higher dividend and partnership income for DBG. Foreign General Insurance net investment income increased in the three and six-month periods ended June 30, 2006 when compared to the same periods of 2005 due to the effects of the aforementioned out of period adjustment, offset by a decline in partnership income. Foreign General partnership income in the second quarter and first half of 2005 benefited from increases in market valuations due to increased initial public offering activity. Foreign General cash flows declined for the first six months of 2006 compared to the year ago period, due to payments related to catastrophe related losses incurred in 2005.

Realized capital gains and losses resulted from the ongoing investment management of the General Insurance portfolios within the overall objectives of the General Insurance operations. See the discussion on "Valuation of Invested Assets" herein.

Reinsurance

AIG is a major purchaser of reinsurance for its General Insurance operations. AIG insures risks globally, and its reinsurance programs must be coordinated in order to provide AIG

the level of reinsurance protection that AIG desires. Reinsurance is an important risk management tool to manage transaction and insurance line risk retention at prudent levels set by management. AIG also purchases reinsurance to mitigate its catastrophic exposure. AIG is cognizant of the need to exercise good judgment in the selection and approval of both domestic and foreign companies participating in its reinsurance programs because one or more catastrophe losses could negatively affect AIG's reinsurers and result in an inability of AIG to collect reinsurance recoverables. AIG's reinsurance department evaluates catastrophic events and assesses the probability of occurrence and magnitude of catastrophic events through the use of state-of-the-art industry recognized program models, among other techniques. AIG supplements these models through continually monitoring the risk exposure of AIG's worldwide General Insurance operations and adjusting such models accordingly. For a further discussion of catastrophe exposures, see "Managing Risk – Catastrophe Exposures". Although reinsurance arrangements do not relieve AIG from its direct obligations to its insureds, an efficient and effective reinsurance program substantially limits AIG's exposure to potentially significant losses. AIG continually evaluates the reinsurance markets and the relative attractiveness of various arrangements for coverage, including structures such as catastrophe bonds, insurance risk securitizations and "sidecar" and similar vehicles. With respect to its property business, AIG has either renewed existing coverage or purchased new coverage that, in the opinion of management, is adequate to limit AIG's exposures.

AIG's consolidated general reinsurance assets amounted to $22.87 billion at June 30, 2006 and resulted from AIG's reinsurance arrangements. Thus, a credit exposure existed at June 30, 2006 with respect to reinsurance recoverable to the extent that any reinsurer may not be able to reimburse AIG under the terms of these reinsurance arrangements. AIG manages its credit risk in its reinsurance relationships by transacting with reinsurers that it considers financially sound, and when necessary AIG holds substantial collateral in the form of funds, securities and/or irrevocable letters of credit. This collateral can be drawn on for amounts that remain unpaid beyond specified time periods on an individual reinsurer basis. At December 31, 2005, approximately 48 percent of the general reinsurance assets were from unauthorized reinsurers. Many of these balances were collateralized, permitting statutory recognition. Additionally, with the approval of its domiciliary insurance regulators, AIG posted approximately $1.5 billion of letters of credit issued by several commercial banks in favor of certain Domestic General Insurance companies to permit statutory recognition of balances otherwise uncollateralized at December 31, 2005. The remaining 52 percent of the general reinsurance assets were from authorized reinsurers. The terms authorized and unauthorized pertain to regulatory categories, not creditworthiness. At December 31, 2005, approximately 88 percent of the balances with respect to authorized reinsurers are from reinsurers rated A (excellent) or better, as rated by A.M. Best, or A (strong) or better, as rated by Standard & Poor's, a division of The McGraw-Hill Companies, Inc. (S&P). These ratings are measures of financial strength. Through June 30, 2006, there has been no significant deterioration in the rating profile of AIG's reinsurers representing more than five percent of AIG's reinsurance assets as of December 31, 2005.

AIG maintains an allowance for estimated unrecoverable reinsurance. Although AIG has been largely successful in its previous recovery efforts, at June 30, 2006, AIG had an allowance for unrecoverable reinsurance approximating $932 million. At that date, AIG had no significant reinsurance recoverables due from any individual reinsurer that was financially troubled (e.g., liquidated, insolvent, in receivership or otherwise subject to formal or informal regulatory restriction).

AIG's Reinsurance Security Department conducts ongoing detailed assessments of the reinsurance markets and current and potential reinsurers, both foreign and domestic. Such assessments include, but are not limited to, identifying if a reinsurer is appropriately licensed and has sufficient financial capacity, and evaluating the local economic environment in which a foreign reinsurer operates. This department also reviews the nature of the risks ceded and the requirements for credit risk mitigants. For example, in AIG's treaty reinsurance contracts, AIG includes provisions that frequently require a reinsurer to post collateral when a referenced event occurs. Furthermore, AIG limits its unsecured exposure to reinsurers through the use of credit triggers, which include, but are not limited to, insurer financial strength rating downgrades, policyholder surplus declines at or below a certain predetermined level or a certain predetermined level of a reinsurance recoverable being reached. In addition, AIG's Credit Risk Committee reviews the credit limits for and concentrations with any one reinsurer.

AIG enters into intercompany reinsurance transactions, primarily through American International Reinsurance Company, Ltd. (AIRCO), for its General Insurance and Life Insurance operations. AIG enters into these transactions as a sound and prudent business practice in order to maintain underwriting control and spread insurance risk among AIG's various legal entities. All material intercompany transactions have been eliminated in consolidation. AIG generally obtains letters of credit in order to obtain statutory recognition of these intercompany reinsurance transactions. At June 30, 2006, approximately $3.7 billion of letters of credit were outstanding to cover intercompany reinsurance transactions with AIRCO or other General Insurance subsidiaries.

At June 30, 2006, consolidated general reinsurance assets of $22.87 billion include reinsurance recoverables for paid losses and loss expenses of $1.05 billion and $18.75 billion with respect to the ceded reserve for losses and loss expenses, including ceded losses incurred but not reported

(IBNR) (ceded reserves) and $3.07 billion of ceded reserve for unearned premiums. The ceded reserve for losses and loss expenses represent the accumulation of estimates of ultimate ceded losses including provisions for ceded IBNR and loss expenses. The methods used to determine such estimates and to establish the resulting ceded reserves involve significant judgment in projecting the frequency and severity of losses over multiple years and are continually reviewed and updated by management. Any adjustments thereto are reflected in income currently. It is AIG's belief that the ceded reserves for losses and loss expenses at June 30, 2006 were representative of the ultimate losses recoverable. In the future, as the ceded reserves continue to develop to ultimate amounts, the ultimate loss recoverable may be greater or less than the reserves currently ceded.

Reserve for Losses and Loss Expenses

The table below classifies as of June 30, 2006 and December 31, 2005 the components of the General Insurance gross reserve for losses and loss expenses (loss reserves) by major lines of business on a statutory Annual Statement basis*:

(in millions)	**June 30, 2006**	December 31, 2005
Other liability occurrence	$18,666	$18,116
Other liability claims made	12,526	12,447
Workers compensation	12,318	11,630
Property	7,028	7,217
Auto liability	6,318	6,569
International	5,409	4,939
Reinsurance	3,194	2,886
Medical malpractice	2,196	2,363
Products liability	1,988	1,937
Accident and health	1,700	1,678
Aircraft	1,615	1,844
Commercial multiple peril	1,449	1,359
Fidelity/surety	1,006	1,072
Other	3,553	3,112
Total	$78,966	$77,169

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

AIG's gross reserve for losses and loss expenses represents the accumulation of estimates of ultimate losses, including IBNR and loss expenses. The methods used to determine loss reserve estimates and to establish the resulting reserves are continually reviewed and updated by management. Any adjustments resulting therefrom are reflected in operating income currently. Because loss reserve estimates are subject to the outcome of future events, changes in estimates are unavoidable given that loss trends vary and time is often required for changes in trends to be recognized and confirmed. Reserve changes that increase previous estimates of ultimate cost are referred to as unfavorable adverse development or reserve strengthening. Reserve changes that decrease previous estimates of ultimate cost are referred to as favorable development.

At June 30, 2006, General Insurance net loss reserves increased $2.74 billion from the prior year end to $60.21 billion. The net loss reserves represent loss reserves reduced by reinsurance recoverables, net of an allowance for unrecoverable reinsurance and applicable discount for future investment income. The table below classifies the components of the General Insurance net loss reserves by business unit as of June 30, 2006 and December 31, 2005.

(in millions)	**June 30, 2006**	December 31, 2005
DBG[(a)]	**$ 42,508**	$40,782
Transatlantic	**5,893**	5,690
Personal Lines[(b)]	**2,533**	2,578
Mortgage Guaranty	**367**	340
Foreign General[(c)]	**8,913**	8,086
Total Net Loss Reserve	**$ 60,214**	$57,476

(a) At June 30, 2006 and December 31, 2005, DBG loss reserves include approximately $3.55 billion and $3.77 billion, respectively, ($3.96 billion and $4.26 billion, respectively, before discount) related to business written by DBG but ceded to AIRCO and reported in AIRCO's statutory filings. DBG loss reserves also include approximately $498 million and $407 million related to business included in AIUO's statutory filings at June 30, 2006 and December 31, 2005, respectively.

(b) At June 30, 2006 and December 31, 2005, Personal Lines loss reserves include $885 million and $878 million, respectively, related to business ceded to DBG and reported in DBG's statutory filings.

(c) At June 30, 2006 and December 31, 2005, Foreign General loss reserves include approximately $2.68 billion and $2.15 billion, respectively, related to business reported in DBG's statutory filings.

The DBG net loss reserve of $42.51 billion is comprised principally of the business of AIG subsidiaries participating in the American Home/National Union pool (11 companies) and the surplus lines pool (Lexington, Starr Excess Liability Insurance Company and Landmark Insurance Company).

Beginning in 1998, DBG ceded a quota share percentage of its other liability occurrence and products liability occurrence business to AIRCO. The quota share percentage ceded was 40 percent in 1998, 65 percent in 1999, 75 percent in 2000 and 2001, 50 percent in 2002 and 2003, 40 percent in 2004, 35 percent in 2005 and 20 percent in 2006 and covered all business written in these years for these lines by participants in the American Home/National Union pool. In 1998 the cession reflected only the other liability occurrence business, but in 1999 and subsequent years included products liability occurrence. AIRCO's loss reserves relating to these quota share cessions from DBG are recorded on a discounted basis. As of June 30, 2006, AIRCO carried a discount of approximately $410 million applicable to the $3.96 billion in undiscounted reserves it assumed from the American Home/National Union pool via this quota share cession. AIRCO also carries approximately $478 million in net loss reserves relating to Foreign General insurance business. These reserves are carried on an undiscounted basis.

Beginning in 1997, the Personal Lines division ceded a percentage of all business written by the companies participating in the personal lines pool to the American Home/National Union pool. As noted above, the total reserves carried by participants in the American Home/National Union

pool relating to this cession amounted to $885 million as of June 30, 2006.

The companies participating in the American Home/National Union pool have maintained a participation in the business written by AIU for decades. As of June 30, 2006, these AIU reserves carried by participants in the American Home/National Union pool amounted to approximately $2.68 billion. The remaining Foreign General reserves are carried by AIUO, AIRCO, and other smaller AIG subsidiaries domiciled outside the United States. Statutory filings in the U.S. by AIG companies reflect all the business written by U.S. domiciled entities only, and therefore exclude business written by AIUO, AIRCO, and all other internationally domiciled subsidiaries. The total reserves carried at June 30, 2006 by AIUO and AIRCO were approximately $4.21 billion and $4.03 billion, respectively. AIRCO's $4.03 billion in total general insurance reserves consist of approximately $3.55 billion from business assumed from the American Home/National Union pool and an additional $478 million relating to Foreign General Insurance business.

Discounting of Reserves

At June 30, 2006, AIG's overall General Insurance net loss reserves reflects a loss reserve discount of $2.11 billion, including tabular and non-tabular calculations. The tabular workers compensation discount is calculated using a 3.5 percent interest rate and the 1979-81 Decennial Mortality Table. The non-tabular workers compensation discount is calculated separately for companies domiciled in New York and Pennsylvania, and follows the statutory regulations for each state. For New York companies, the discount is based on a five percent interest rate and the companies' own payout patterns. For Pennsylvania companies, the statute has specified discount factors for accident years 2001 and prior, which are based on a six percent interest rate and an industry payout pattern. For accident years 2002 and subsequent, the discount is based on the yield of U.S. Treasury securities ranging from one to twenty years and the company's own payout pattern, with the future expected payment for each year using the interest rate associated with the corresponding Treasury security yield for that time period. The discount is comprised of the following: $512 million – tabular discount for workers compensation in DBG; $1.19 billion – non-tabular discount for workers compensation in DBG; and, $410 million – non-tabular discount for other liability occurrence and products liability occurrence in AIRCO. The total undiscounted workers compensation loss reserve carried by DBG is approximately $10.2 billion as of June 30, 2006. The other liability occurrence and products liability occurrence business in AIRCO that is assumed from DBG is discounted based on the yield of U.S. Treasury securities ranging from one to twenty years and the DBG payout pattern for this business. The undiscounted reserves assumed by AIRCO from DBG totaled approximately $3.96 billion at June 30, 2006.

Quarterly Reserving Process

It is management's belief that the General Insurance net loss reserves are adequate to cover General Insurance net losses and loss expenses as of June 30, 2006. While AIG regularly reviews the adequacy of established loss reserves, there can be no assurance that AIG's ultimate loss reserves will not develop adversely and materially exceed AIG's loss reserves as of June 30, 2006. In the opinion of management, such adverse development and resulting increase in reserves is not likely to have a material adverse effect on AIG's consolidated financial position, although it could have a material adverse effect on AIG's consolidated results of operations for an individual reporting period.

The table below presents the reconciliation of General Insurance net loss reserves for the three and six-month periods ended June 30, 2006 and 2005 as follows:

	Three Months Ended June 30,		Six Months Ended June 30,	
(in millions)	**2006**	2005	**2006**	2005
Net reserve for losses and loss expenses at beginning of period	**$58,892**	$49,334	**$57,476**	$47,254
Foreign exchange effect	**370**	(349)	**487**	(321)
Losses and loss expenses incurred:				
Current year	**6,911**	7,032	**13,752**	14,071
Prior years, other than accretion of discount*	**(248)**	(13)	**(213)**	130
Prior years, accretion of discount	**101**	97	**202**	194
Losses and loss expenses incurred	**6,764**	7,116	**13,741**	14,395
Losses and loss expenses paid	**5,812**	5,537	**11,490**	10,764
Net reserve for losses and loss expenses at end of period	**$60,214**	$50,564	**$60,214**	$50,564

* *Includes $30 million and $35 million in the three-month periods ended June 30, 2006 and 2005, respectively, for the general reinsurance operations of Transatlantic and $(63) million and $0, respectively, of additional losses incurred resulting from increased costs related to the 2005 and 2004 catastrophes. Includes $65 million and $90 million in the six-month periods ended June 30, 2006 and 2005, respectively, for the general reinsurance operations of Transatlantic and $35 million and $118 million, respectively, of additional losses incurred resulting from increased costs related to the 2005 and 2004 catastrophes. Transatlantic includes $10 million of prior year adverse catastrophe development in both the three months and six months ended June 30, 2006.*

The loss ratios recorded by AIG for the first six months of 2006 take into account the results of the comprehensive reserve reviews that were completed in the fourth quarter of 2005. As explained more fully in the 2005 Annual Report on Form 10-K/A, AIG's year-end 2005 reserve review reflected careful consideration of the reserve analyses prepared by AIG's internal actuarial staff with the assistance of third party actuaries. In determining the appropriate loss ratios for accident year 2006 for each class of business, AIG gave appropriate consideration to the loss ratios resulting from the reserve analyses as well as all other relevant information including rate changes, expected changes in loss costs, changes in coverage, reinsurance or mix of business, and other factors that may affect the loss ratios.

In the first six months of 2006, AIG enhanced its process of determining the quarterly loss development from prior accident years. In the first quarter of 2006, AIG began conducting additional analyses to determine the change in estimated ultimate loss for each accident year for each profit center. For example, if loss emergence for a profit center is different than expected for certain accident years in the quarter, the actuaries now take additional steps to examine the indicated effect such emergence would have on the reserves of that profit center. In some cases, the higher or lower than expected emergence may result in no clear change in the ultimate loss estimate for the accident years in question, and no adjustment would be made to the profit center's reserves for prior accident years. In other cases, the higher or lower than expected emergence may result in a larger change, either favorable or unfavorable, than the difference between the actual and expected loss emergence. Such additional analyses were conducted for each profit center, as appropriate, in the first and second quarters of 2006 to determine the loss development from prior accident years for the first and second quarters of 2006.

In the second quarter of 2006, net loss development from prior accident years was favorable by approximately $248 million. This reflects approximately $63 million of favorable development pertaining to catastrophes in 2005, partially offset by adverse development of approximately $30 million from Transatlantic. Excluding catastrophes and Transatlantic, as well as accretion of discount of approximately $101 million, net loss development from prior accident years in the second quarter of 2006 was favorable by approximately $215 million. The majority of the favorable development was attributable to shorter tail classes of business throughout General Insurance. This favorable development relates primarily to classes of business which did not require reserve strengthening in connection with AIG's year-end 2005 reserve study. DBG accounted for approximately $57 million of the $215 million of overall favorable development in the second quarter of 2006, excluding catastrophes. Accident years 2003 through 2005 continued to develop favorably in the second quarter for most classes of business throughout AIG. Accident years 2001 and prior continued to develop adversely in the quarter, primarily due to approximately $125 million of adverse development from excess casualty business and approximately $35 million from the excess workers compensation class of business. The $215 million of overall net favorable development was comprised of approximately $190 million of adverse development from accident years 2002 and prior, offset by approximately $410 million of favorable development from accident years 2003 through 2005.

In the first six months of 2006, net loss development from prior accident years was favorable by approximately $213 million. This reflects approximately $35 million of adverse development pertaining to catastrophes in 2004 and 2005 and approximately $65 million of adverse development from Transatlantic. Excluding catastrophes and Transatlantic, as well as accretion of discount of approximately $202 million, net loss development from prior accident years in the first six months of 2006 was favorable by approximately $313 million. The majority of the favorable development was attributable to shorter tail classes of business throughout General Insurance. DBG accounted for approximately $62 million of the $313 million of overall favorable development in the first six months of 2006, excluding catastrophes. Accident years 2003 through 2005 developed favorably in the first six months of 2006 for most classes of business throughout AIG. Accident years 2002 and prior developed adversely in the first six months, primarily due to approximately $300 million of adverse development from excess casualty business and approximately $70 million from the excess workers compensation class of business. The $313 million of overall net favorable development was comprised of approximately $420 million of adverse development from accident years 2002 and prior, offset by approximately $735 million of favorable development from accident years 2003 through 2005.

In the second quarter of 2005, net loss development from prior accident years was favorable by approximately $13 million, including negligible development pertaining to catastrophes and approximately $35 million of adverse development from Transatlantic. Excluding catastrophes and Transatlantic, as well as accretion of discount of approximately $97 million, net loss development from prior accident years in the second quarter of 2005 was favorable by approximately $48 million. In the second quarter of 2005, most classes of business experienced favorable development for accident years 2002 through 2004, with the exception of D&O which continued to experience adverse development for accident year 2002. The $48 million of overall net favorable development was comprised of approximately $400 million of adverse development from accident years 2001 and prior, offset by approximately $350 million of favorable development from accident year 2004 and approximately $100 million of favorable development from accident

year 2003. The majority of the adverse developments from accident years 2001 and prior pertained to the excess casualty and D&O classes of business.

In the first six months of 2005, net loss development from prior accident years was adverse by approximately $130 million, including approximately $118 million pertaining to catastrophes in 2004 and approximately $90 million of adverse development from Transatlantic. Excluding catastrophes and Transatlantic, as well as accretion of discount of approximately $194 million, net loss development from prior accident years in the first six months of 2005 was favorable by approximately $78 million. In the first six months of 2005, most classes of business experienced favorable development for accident years 2002 through 2004, with the exception of D&O which experienced approximately $100 million of adverse development for accident year 2002. The $78 million of overall net favorable development included approximately $750 million of adverse development pertaining to accident years 2001 and prior, offset by approximately $250 million of favorable development from accident year 2003 and $570 million of favorable development from accident year 2004. The majority of the adverse development from accident years 2001 and prior emanated from the excess casualty and D&O classes of business.

Loss Reserving Process

The General Insurance loss reserves can generally be categorized into two distinct groups. One group is long-tail casualty lines of business which include excess and umbrella liability, D&O, professional liability, medical malpractice, workers compensation, general liability, products liability, and related classes. The other group is short-tail lines of business consisting principally of property lines, personal lines and certain classes of casualty lines. These lines of business and actuarial assumptions made in the review of these lines of business are described in the 2005 Annual Report on Form 10-K/A.

The process of determining the current loss ratio for each class or business segment is based on a variety of factors and is described in detail in AIG's 2005 Annual Report on Form 10-K/A. AIG uses the process described above to update AIG's reserves on a quarterly basis. AIG's 2005 Annual Report on Form 10-K/A also includes a discussion and analysis of the volatility of AIG's 2005 reserve estimates and a sensitivity analysis.

Asbestos and Environmental Reserves

The estimation of loss reserves relating to asbestos and environmental claims on insurance policies written many years ago is subject to greater uncertainty than other types of claims due to inconsistent court decisions as well as judicial interpretations and legislative actions that in some cases have tended to broaden coverage beyond the original intent of such policies and in others have expanded theories of liability.

As described more fully in the 2005 Annual Report on Form 10-K/A, AIG's reserves relating to asbestos and environmental claims reflect the results of the comprehensive ground up analysis which was completed in the fourth quarter of 2005. AIG plans to update the ground up analysis on an annual basis. In the first six months of 2006, AIG maintained the ultimate loss estimates for asbestos and environmental claims resulting from the recently completed reserve analyses. A minor amount of incurred loss emergence pertaining to asbestos was reflected in the first six months of 2006, as depicted in the table that follows. This minor development is primarily attributable to the general reinsurance operations of Transatlantic.

A summary of reserve activity, including estimates for applicable IBNR, relating to asbestos and environmental claims separately and combined for the six months ended June 30, 2006 and 2005 follows:

	2006		2005	
(in millions)	**Gross**	**Net**	Gross	Net
Asbestos:				
Reserve for losses and loss expenses at beginning of year	**$4,441**	**$1,840**	$2,559	$1,060
Losses and loss expenses incurred*	**(1)**	**4**	96	27
Losses and loss expenses paid*	**(277)**	**(96)**	(151)	(51)
Reserve for losses and loss expenses at end of period	**$4,163**	**$1,748**	$2,504	$1,036
Environmental:				
Reserve for losses and loss expenses at beginning of year	**$ 926**	**$ 410**	$ 974	$ 451
Losses and loss expenses incurred*	**1**	**–**	(12)	(3)
Losses and loss expenses paid*	**(55)**	**(33)**	(56)	(31)
Reserve for losses and loss expenses at end of period	**$ 872**	**$ 377**	$ 906	$ 417
Combined:				
Reserve for losses and loss expenses at beginning of year	**$5,367**	**$2,250**	$3,533	$1,511
Losses and loss expenses incurred*	**–**	**4**	84	24
Losses and loss expenses paid*	**(332)**	**(129)**	(207)	(82)
Reserve for losses and loss expenses at end of period	**$5,035**	**$2,125**	$3,410	$1,453

** All amounts pertain to policies underwritten in prior years.*

As indicated in the table above, asbestos loss payments increased significantly in the first six months of 2006 compared to the same period in the prior years, primarily as a result of payments pertaining to settlements that had been negotiated in earlier periods. There was negligible development of asbestos and environmental reserves in the first six months of 2006.

The gross and net IBNR included in the reserve for losses and loss expenses, relating to asbestos and environmental claims separately and combined, at June 30, 2006 and 2005 were estimated as follows:

	2006		2005	
(in millions)	**Gross**	**Net**	Gross	Net
Asbestos	**$3,100**	**$1,351**	$1,710	$ 753
Environmental	**562**	**241**	543	264
Combined	**$3,662**	**$1,592**	$2,253	$1,017

A summary of asbestos and environmental claims count activity for the six months ended June 30, 2006 and 2005 was as follows:

	2006			2005		
	Asbestos	**Environmental**	**Combined**	Asbestos	Environmental	Combined
Claims at beginning of year	**7,293**	**9,873**	**17,166**	7,575	8,216	15,791
Claims during year:						
Opened	**453**	**900**	**1,353**	484	1,324	1,808
Settled	**(73)**	**(83)**	**(156)**	(32)	(108)	(140)
Dismissed or otherwise resolved	**(493)**	**(893)**	**(1,386)**	(580)	(1,770)	(2,350)
Claims at end of period	**7,180**	**9,797**	**16,977**	7,447	7,662	15,109

The table below presents AIG's survival ratios for asbestos and environmental claims at June 30, 2006 and 2005. The survival ratio is derived by dividing the current carried loss reserve by the average payments for the three most recent calendar years for these claims. Therefore, the survival ratio is a simplistic measure estimating the number of years it would be before the current ending loss reserves for these claims would be paid off using recent year average payments. Many factors, such as aggressive settlement procedures, mix of business and level of coverage provided, have a significant effect on the amount of asbestos and environmental reserves and payments and the resultant survival ratio. Thus, caution should be exercised in attempting to determine reserve adequacy for these claims based simply on this survival ratio.

AIG's survival ratios for asbestos and environmental claims, separately and combined were based upon a three-year average payment. These ratios at June 30, 2006 and 2005 were as follows:

(number of years)	**Gross**	**Net**
2006		
Survival ratios:		
Asbestos	**13.2**	**15.9**
Environmental	**6.3**	**5.5**
Combined	**11.1**	**11.9**
2005		
Survival ratios:		
Asbestos	9.5	12.6
Environmental	6.4	6.6
Combined	8.4	10.0

Life Insurance & Retirement Services Operations

AIG's Life Insurance & Retirement Services subsidiaries offer a wide range of insurance and retirement savings products both domestically and abroad. Insurance-oriented products consist of individual and group life, payout annuities, endowment and accident and health policies. Retirement savings products consist generally of fixed and variable annuities.

Domestically, AIG's Life Insurance & Retirement Services operations offer a broad range of protection products, such as life insurance, group life and health products, including disability income products and payout annuities, which include single premium immediate annuities, structured settlements and terminal funding annuities. Home service operations include an array of life insurance, accident and health and annuity products sold through career agents. In addition, home service includes a small block of run-off property and casualty coverage. Retirement services include group retirement products, individual fixed and variable annuities sold through banks, broker dealers and exclusive sales representatives, and annuity runoff operations, which include previously-acquired "closed blocks" and other fixed and variable annuities largely sold through distribution relationships that have been discontinued.

Overseas, AIG's Life Insurance & Retirement Services operations include insurance and investment-oriented products such as whole and term life, investment linked, universal life and endowments, personal accident and health products, group products including pension, life and health, and fixed and variable annuities.

Life Insurance & Retirement Services operations presented on a sub-product basis for the three and six-month periods ended June 30, 2006 and 2005 were as follows:

	Three Months Ended June 30,		Six Months Ended June 30,	
(in millions)	**2006**	2005	**2006**	2005
GAAP premiums:				
Domestic Life:				
Life insurance[a]	**$ 557**	$ 503	**$ 1,073**	$ 1,000
Home service	**197**	202	**397**	405
Group life/health	**241**	265	**487**	533
Payout annuities[b]	**397**	346	**847**	743
Total	**1,392**	1,316	**2,804**	2,681
Domestic Retirement Services:				
Group retirement products	**96**	86	**190**	170
Individual fixed annuities	**35**	27	**64**	47
Individual variable annuities	**130**	114	**258**	226
Individual fixed annuities-runoff[c]	**14**	18	**34**	41
Total	**275**	245	**546**	484
Total Domestic	**1,667**	1,561	**3,350**	3,165
Foreign Life:				
Life insurance	**3,936**	3,904	**8,017**	7,993
Personal accident & health	**1,380**	1,267	**2,686**	2,488
Group products	**507**	461	**1,080**	978
Total	**5,823**	5,632	**11,783**	11,459
Foreign Retirement Services:				
Individual fixed annuities	**94**	92	**189**	176
Individual variable annuities	**41**	19	**75**	44
Total	**135**	111	**264**	220
Total Foreign	**5,958**	5,743	**12,047**	11,679
Total GAAP premiums	**$7,625**	$ 7,304	**$ 15,397**	$ 14,844
Net investment income:				
Domestic Life:				
Life insurance	**$ 313**	$ 324	**$ 651**	$ 696
Home service	**145**	157	**303**	304
Group life/health	**52**	51	**106**	97
Payout annuities	**244**	239	**481**	449
Total	**754**	771	**1,541**	1,546
Domestic Retirement Services:				
Group retirement products	**539**	547	**1,111**	1,096
Individual fixed annuities	**880**	819	**1,812**	1,646
Individual variable annuities	**50**	53	**102**	111
Individual fixed annuities-runoff[c]	**227**	250	**463**	504
Total	**1,696**	1,669	**3,488**	3,357
Total Domestic	**2,450**	2,440	**5,029**	4,903
Foreign Life:				
Life insurance[d]	**1,380**	1,149	**2,590**	2,313
Personal accident & health	**71**	56	**135**	110
Group products	**115**	136	**292**	267
Intercompany adjustments	**(10)**	(8)	**(20)**	(16)
Total	**1,556**	1,333	**2,997**	2,674
Foreign Retirement Services:				
Individual fixed annuities	**458**	377	**954**	754
Individual variable annuities	**(166)**	17	**27**	153
Total	**292**	394	**981**	907
Total Foreign	**1,848**	1,727	**3,978**	3,581
Total net investment income	**$4,298**	$ 4,167	**$ 9,007**	$ 8,484
Realized capital gains (losses):				
Domestic	**$ (382)**	$ (78)	**$ (576)**	$ (85)

(in millions)	Three Months Ended June 30, 2006	Three Months Ended June 30, 2005	Six Months Ended June 30, 2006	Six Months Ended June 30, 2005
Foreign	**76**	24	**304**	(132)
Pricing net investment gains[e]	**88**	100	**212**	181
Total Foreign	**164**	124	**516**	49
Total realized capital gains (losses)[e]	**$ (218)**	$ 46	**$ (60)**	$ (36)
Operating Income:				
Domestic	**$ 581**	$ 860	**$ 1,467**	$ 1,841
Foreign[d]	**1,721**	1,464	**3,390**	2,664
Total operating income	**$2,302**	$ 2,324	**$ 4,857**	$ 4,505
Life insurance in-force[f]:				
Domestic			**$ 879,181**	$ 825,151
Foreign			**1,097,362**	1,027,682
Total			**$1,976,543**	$1,852,833

(a) Effective January 1, 2006, the Broker/Dealer operations of the Domestic Life Insurance companies are being reported and managed within the Asset Management segment. Included in GAAP premiums were revenues of $40 million and $64 million, respectively, for the three and six-month periods ended June 30, 2005.

(b) Includes structured settlements, single premium immediate annuities and terminal funding annuities.

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

(d) Includes the effect of an out of period adjustment related to the accounting for certain interests in unit investment trusts. For the three and six-month periods ended June 30, 2006 the effect was an increase of $221 million and $144 million in net investment income and operating income, respectively.

(e) For purposes of this presentation, pricing net investment gains are segregated as a component of total realized capital gains (losses). They represent certain amounts of realized capital gains where gains are an inherent element in pricing certain life products in some foreign countries.

(f) Amounts presented were as at June 30, 2006 and December 31, 2005.

AIG's Life Insurance & Retirement Services subsidiaries report their operations through the following operating units: Domestic Life — AIG American General, including American General Life Insurance Company (AG Life), United States Life Insurance in the City of New York (USLIFE) and American General Life and Accident Insurance Company (AGLA); Domestic Retirement Services — The Variable Annuity Life Insurance Company (VALIC), AIG Annuity Insurance Company (AIG Annuity) and AIG SunAmerica; Foreign Life — ALICO, AIRCO, AIG Edison Life, AIG Star Life, American International Assurance Company, Limited together with American International Assurance Company (Bermuda) Limited (AIA), Nan Shan Life Insurance Company, Ltd. (Nan Shan) and The Philippine American Life and General Insurance Company (Philamlife).

AIG transacts business in most major foreign currencies. The following table summarizes the effect of changes in foreign currency exchange rates on the growth of Life Insurance & Retirement Services GAAP premiums for the three and six-month periods ended June 30, 2006:

	Three Months Ended June 30, 2006	Six Months Ended June 30, 2006
Growth in original currency*	6.8%	7.0%
Foreign exchange effect	(2.4)	(3.3)
Growth as reported in U.S. dollars	4.4%	3.7%

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

Life Insurance & Retirement Services Results

Life Insurance & Retirement Services GAAP premiums increased 4 percent to $7.6 billion in the second quarter of 2006 compared to the same period in 2005. Net investment income increased for the second quarter of 2006 when compared to the same period in 2005. The increase includes the effect of an out of period adjustment relating to the accounting for certain interests in unit investment trusts totaling $221 million, reduced by lower policyholder trading gains (losses), which are linked mainly to equities, and which are offset by an equal change in incurred policy losses and benefits. In addition, certain operations experienced lower investment income related to short-term volatility of yield enhancement investments in structured notes linked to emerging market sovereign debt, which had mark-to-market losses of $46 million in the quarter.

Operating income including realized capital gains (losses) decreased slightly in the second quarter of 2006 when compared to the same period in 2005. Domestic Life operations continued to perform well in its core life insurance businesses that included growth of retail periodic sales, but operating income declined in the quarter due to lower investment income from calls and tenders, and additional reserves for legal contingencies. Domestic Retirement Services operating income grew for the quarter due to strong partnership income, lower amortization of deferred policy acquisition costs related to realized capital losses and an increase in underlying reserves which grew 3 percent in the second quarter. Foreign Life Insurance & Retirement Services operating income growth in the quarter included the effect of the aforementioned out of period adjustment and was dampened by a

significantly weaker Yen exchange rate compared to the same three month period last year. Realized capital gains (losses) for the second quarter of 2006 totaled a net loss of $218 million versus a gain of $46 million during the same period last year. The loss in the current quarter was primarily due to the write-down of certain fixed income securities for interest rate-related other-than-temporary declines in value where the companies' intent to hold until recovery changed.

Life Insurance & Retirement Services GAAP premiums increased 4 percent to $15.4 billion for the first six months of 2006 compared to the same period of 2005. Net investment income increased for the first six months of 2006 reflecting a higher level of invested assets and the effect of the aforementioned out of period adjustment. Operating income, including realized capital gains (losses), grew 8 percent for the first six months of 2006 compared to the same period of 2005. Domestic Life operating income declined for the first six months of 2006 primarily due to lower investment income from calls and tenders and additional reserves for legal contingencies. Domestic Retirement Services operating income declined 22 percent for the first six months of 2006 primarily due to significant realized capital losses which more than offset increased income from growth in underlying reserves, higher partnership income and lower amortization of deferred policy acquisition costs related to capital losses. Foreign Life Insurance & Retirement Services operating income grew 27 percent for the first six months of 2006 on a U.S. dollar basis due to higher realized capitalized gains and the effect of the aforementioned out of period adjustment. Operating income growth in U.S. dollars is lower than growth on a local currency basis primarily due to a weaker Japanese Yen in the first six months of 2006 compared to the same period last year. Realized capital losses were $60 million for the first six months of 2006 compared to losses of $36 million during the same period of 2005.

Domestic Life Operations

The following table reflects retail periodic Life insurance sales by product for the three and six-month periods ended June 30, 2006 and 2005:

Domestic Life Insurance Periodic Premium Sales*

	Three Months Ended June 30,		Six Months Ended June 30,	
(in millions)	**2006**	2005	**2006**	2005
By product:				
Universal life	**$107**	$ 54	**$243**	$112
Variable universal life	**18**	10	**27**	24
Term life	**63**	60	**123**	113
Whole life/other	**3**	3	**6**	6
Total	**$191**	$127	**$399**	$255

** Periodic premium represents premium from new business expected to be collected over a one year period.*

Quarterly Domestic Life Results

AIG's Domestic Life operations had continued growth of GAAP premiums for the second quarter of 2006 when compared to the same period last year. The life insurance product line had strong periodic universal life sales from the independent distribution platform. While not sustainable at this pace in a very competitive environment, this result has positioned the Life insurance product line to achieve another solid sales year. AGLA, the home service business, is diversifying product offerings, enhancing the capabilities and quality of the sales force which has resulted in improved agent productivity and better persistency of in-force business. Strong growth of payout annuities GAAP premiums emanated from sales of single premium immediate annuities that remained strong during the quarter. GAAP premiums for the group life/health product line were slightly lower in the second quarter of 2006 compared to 2005 reflecting slower growth in the credit business, and tightened pricing and underwriting in the group employer lines. Restructuring efforts in this business continue to focus on new product introductions, cross selling, other growth strategies, and may include exiting certain product lines.

Operating income for the Domestic Life Insurance line of business declined 2 percent for the second quarter of 2006 due to lower investment income related to yield enhancement activities that included mark-to-market losses of $8 million on structured notes linked to emerging market sovereign debt and lower call and tender income. Operating income for the home service line of business declined from the second quarter of 2005 due to lower investment income from calls and tenders on fixed maturity securities and mark-to-market losses of $8 million on structured notes linked to emerging market sovereign debt. The group life/health business operating income results for the second quarter of 2006 included a $24 million reserve increase related to litigation and contingencies. The payout annuities line of business operating income declined for the quarter primarily due to lower calls and tenders on fixed maturity securities when compared to the second quarter of 2005.

Year-to-date Domestic Life Results

GAAP premiums for the Domestic Life operations grew 5 percent for the first six months of 2006 compared to the same period of 2005 reflecting strong sales of universal life and single premium immediate annuities. The life insurance product line experienced strong periodic sales from the independent distribution platform for the first six months of 2006. The home service business GAAP premiums declined for the first six months of 2006 as the reduction of premium in-force outpaced the positive sales growth for the period. The payout annuities GAAP premiums growth for the first six months of 2006 reflects strong sales of single premium annuities when compared to the same period last year. GAAP premiums for the group life/health product line for the first

six months of 2006 reflect the restructuring efforts in certain product lines.

Operating income for the life insurance product line declined for the first six months of 2006 due to lower investment income related to yield enhancement activities, including mark-to-market losses on structured notes linked to emerging market debt of $5 million, that offset the positive effect of higher sales. Operating income for the home service line of business grew from the same period last year due to improved persistency of premium in-force and lower acquisition costs, partially offset by mark-to-market losses of $4 million on structured notes linked to emerging market sovereign debt. The group life/health business operating income for the first six months of 2006 is lower than the same period last year due to additional reserves related to litigation and contingencies in the credit life and A&H business and transition costs related to the outsourcing of back office operations. The payout annuities product line operating income declined for the first six months of 2006 primarily due to lower calls and tenders on fixed maturity securities when compared to the same period last year.

Quarterly Domestic Retirement Services Results

Domestic Retirement Services total deposits declined approximately 6 percent for the second quarter of 2006 when compared to the year ago quarter. The decline is due to lower fixed annuity sales that continued to face increased competition from bank products in the flat yield curve environment. Individual variable annuity deposits grew 46 percent in the second quarter of 2006 from the year ago quarter reflecting strong growth in products with new guarantee features. Group retirement deposits were flat in the quarter compared to last year reflecting the increased number of policyholders nearing retirement age. New products have been launched that are designed to meet the needs of retirement age policyholders and retain assets under management.

Group retirement products operating earnings for the second quarter of 2006 were lower than the same period last year principally due to slightly lower investment spreads, mark-to-market losses of $14 million on structured notes linked to emerging market sovereign debt and higher amortization of deferred acquisition costs related to internal replacements of existing contracts into new contracts. Individual fixed annuity operating income grew 38 percent for the second quarter of 2006 compared to last year principally due to lower amortization of deferred policy acquisition costs related to realized capital losses, higher partnership income, increased net investment spreads and growth in underlying reserves, partially offset by mark-to-market losses of $14 million on structured notes linked to emerging market sovereign debt. Operating income for individual variable annuities grew 7 percent in the second quarter of 2006 from the year ago quarter in line with growth in underlying reserves.

Year-to-date Domestic Retirement Services Results

Domestic Retirement Services total deposits declined approximately 6 percent for the first six months of 2006 when compared to the first six months of 2005. The decrease in total deposits reflects declining fixed annuity sales partially offset by strong growth in individual variable annuity sales. In addition, surrender rates during the first six months of 2006 are higher when compared to the same period last year. Net flows for the six months of 2006 were negative $2.2 billion compared to positive net flows of $1.1 billion last year reflecting lower deposits and higher surrenders. The negative flows primarily reflect runoff annuity business sold through discontinued distribution relationships.

Group retirement products operating earnings grew 4 percent for the first six months due to higher partnership income and growth in underlying reserves, partially offset by mark-to-market losses of $9 million on structured notes linked to emerging market sovereign debt. Individual fixed annuity operating income for the first six months of 2006 grew 38 percent primarily from growth in partnership income, lower amortization of deferred policy acquisition costs related to capital losses, growth in average underlying reserves and slightly lower average crediting rates, partially offset by mark-to-market losses of $8 million on structured notes linked to emerging market sovereign debt. The individual variable annuity product line grew operating earnings for the first six months as fee income increased on higher sales volumes and increased underlying reserves.

Domestic Retirement Services Supplemental Data

The following table reflects deposits for Domestic Retirement Services for the three and six-month periods ended June 30, 2006 and 2005:

	Three Months Ended June 30,		Six Months Ended June 30,	
(in millions)	**2006**	2005	**2006**	2005
Group retirement products*	**$1,608**	$1,608	**$3,549**	$3,239
Individual fixed annuities	**1,331**	1,951	**3,018**	4,414
Individual variable annuities	**1,148**	785	**2,175**	1,676
Individual fixed annuities - runoff	**42**	58	**85**	107
Total	**$4,129**	$4,402	**$8,827**	$9,436

** Includes mutual funds of $256 million and $239 million for the three months of 2006 and 2005, respectively and $801 million and $462 million for six months of 2006 and 2005, respectively.*

The following chart shows the amount of reserves by surrender charge category for Domestic Retirement Services as of June 30, 2006:

(in millions)	Group Retirement Products*	Individual Fixed Annuities	Individual Variable Annuities
Zero or no surrender charge	$41,237	$10,302	$10,259
Between 0 percent - 4 percent	10,762	10,555	8,141
Greater than 4 percent	2,531	30,749	10,239
Non-Surrenderable	888	3,154	87
Total	$55,418	$54,760	$28,726

** Excludes mutual funds.*

In the three months and six months ended June 30, 2006 surrender rates increased for individual fixed annuities, individual variable annuities and group retirement products compared to the same periods in 2005. The increase in surrender rate for fixed annuities continues to be driven by the shape of the yield curve and general aging of the in-force block; however, less than 20 percent of the individual fixed annuity reserves as of June 30, 2006 are available to be surrendered without charge. Individual variable annuity surrender rates for the second quarter and first six months of 2006 primarily reflect the higher shock-lapse that occurs following expiration of the surrender charge period on certain 3-year and 7-year contracts. Reflecting a widespread industry phenomenon, this lapse rate, much of which was anticipated when the products were issued, has recently been affected by investor demand to exchange existing policies for new-generation contracts with living benefits or lower fees. In addition, partial withdrawals on certain variable annuity products have increased as AIG has introduced features designed to generate a stream of income to the participants.

A continued increase in the level of surrenders in any of these businesses or in the individual fixed annuities runoff block could accelerate the amortization of deferred acquisition costs in future years and negatively affect fee income earned on assets under management.

The following table reflects the net flows by line of business for Domestic Retirement Services for the three and six-month periods ended June 30, 2006 and 2005:

Domestic Retirement Services – Net Flows[(a)]

	Three Months Ended June 30,		Six Months Ended June 30,	
(in millions)	**2006**	2005	**2006**	2005
Group retirement products[(b)]	**$ 194**	$ 299	**$ 635**	$ 578
Individual fixed annuities	**(736)**	448	**(737)**	1,833
Individual variable annuities	**88**	(126)	**(45)**	(54)
Individual fixed annuities - runoff	**(1,253)**	(684)	**(2,079)**	(1,250)
Total	**$(1,707)**	$ (63)	**$(2,226)**	$ 1,107

(a) Net flows are defined as deposits received, less benefits, surrenders, withdrawals and death benefits.

(b) Includes mutual funds.

The combination of lower deposits and higher surrenders in the individual fixed annuity and individual fixed annuity-runoff blocks resulted in negative net flows for the three and six-month periods ended June 30, 2006. The continuation of the current interest rate and competitive environment could prolong this trend.

Quarterly Foreign Life Insurance & Retirement Services Results

Foreign Life Insurance & Retirement Services operations produced 78 percent and 79 percent of Life Insurance & Retirement Services GAAP premiums for the three months ended June 30, 2006 and 2005, respectively. Foreign Life Insurance & Retirement Services GAAP premiums increased in the second quarter of 2006 by approximately 4 percent compared to the same period in 2005 on a U.S. dollar basis and 7 percent excluding the effect of currency changes. AIG transacts business in most major foreign currencies and therefore premiums reported in U.S. dollars will vary both by volume and by changes in foreign currency translation rates. Foreign life GAAP premiums growth is also affected by a continuing trend for clients to purchase investment-oriented products. This is particularly true in Southeast Asia, including Taiwan, where AIG's life operations in that region have responded to this trend by offering a wide array of investment-linked products, both periodic pay and single premium, with multiple fund selection, but with minimal investment guarantees. For GAAP reporting purposes, only revenues from policy charges for insurance, administration, and surrender charges are reported as GAAP premiums for these life products. This product mix shift contributed to the single digit growth rate in Foreign Life Insurance & Retirement Services GAAP premiums, while continuing to grow total reserves by double digits.

Foreign Life Insurance & Retirement Services operating income of $1.72 billion for the second quarter of 2006 included $164 million of realized capital gains compared to $124 million of gains in the year ago quarter and the effect of an out of period adjustment related to the accounting for certain interests in unit investment trusts that increased operating income by $144 million in the three and six-month periods ended June 30, 2006. Foreign Life Insurance & Retirement Services operating income grew 18 percent on a U.S. dollar basis. Similar to the effect of exchange rates on GAAP premiums, operating income results for foreign operations are negatively affected by exchange rates when compared to last year. On a comparable basis, the growth in life insurance product line results for the quarter were generally in line with the growth in underlying reserves. Personal accident & health results for the second quarter of 2006 reflect continued stable profit margins, but year-on-year comparisons in U.S. dollars are affected by the weakening Yen exchange rate given the large concentration of that product line in Japan. Group products operating income results declined slightly in the second quarter of 2006 due to higher mortality and morbidity costs when compared to the same period last year. Growth of

individual fixed annuities operating income for the second quarter of 2006, emanating primarily from Japan, is in line with the growth in average assets under management and the greater benefits from increasing scale. The growth of individual variable annuities operating income in the second quarter of 2006 reflects continued strong growth in assets under management related to the increased demand for those products in Japan and in Europe.

During the second quarter of 2006, Japanese tax authorities announced a reduction in the amount of premium that policyholders may deduct from their Japanese tax returns for certain accident and health products. Foreign life operations in Japan experienced a decline in sales of those products and an increase in terminations during the quarter. The effect on second quarter 2006 operating income of higher terminations amounted to approximately $10 million of higher expenses. If terminations continue at current experience levels, operating results will continue to be negatively affected. Higher than anticipated terminations result in accelerated amortization of deferred acquisition costs, offset somewhat by the release of policy benefit reserves in excess of cash value. The amount of deferred acquisition costs related to the policies in-force for these products amounted to $278 million as of June 30, 2006. In response to the tax law change, AIG has developed new products, both life and health, to meet the needs of clients in that market. AIG continues to believe that any increase in policy terminations would not be material to AIG's consolidated financial condition or results of operations.

Year-to-date Foreign Life Insurance & Retirement Services Results

Foreign Life Insurance & Retirement Services operations produced 78 percent and 79 percent of Life Insurance & Retirement Services GAAP premiums in the first six months of 2006 and 2005, respectively. GAAP premiums grew approximately 3 percent for the first six months of 2006 on a U.S. dollar basis and 7 percent when measured on an original currency basis compared to the year ago periods. Globally, AIG's deep and diverse distribution, which includes bancassurance, worksite marketing, direct marketing and strong agency organizations, provides a powerful distribution platform for AIG's diverse product lines. In Japan, distribution of single premium life insurance products through banks was deregulated in December 2005 resulting in strong sales of products designed for that market during the first six months of 2006. This new distribution outlet adds to the existing multiple distribution platform in Japan where AIG remains the leading foreign provider.

Foreign Life Insurance & Retirement Services operating income for the first six months of 2006 was $3.39 billion, which included $516 million of realized capital gains and the $144 million effect of the aforementioned out of period adjustment included in life insurance, compared with $2.66 billion of operating income for the same period of 2005, which included $49 million of realized capital gains. The first six months of 2006 results for the life insurance product line also included a $37 million operating loss attributable to this segment's share of the losses from AIG Credit Card Company (Taiwan) compared to a gain of $20 million in the first six months of 2005, due to the allowance for losses recorded in the first quarter of 2006. The positive effect of DAC and value of business acquired (VOBA) unlocking for the life insurance product line was $17 million and $58 million for the first six months of 2006 and 2005, respectively. Personal accident and health product line results for the first six months of 2006 reflect the growth of underlying premium in-force, although growth is dampened by a weaker Yen exchange rate when compared to the same period last year. The Foreign Retirement Services business continued to grow in Japan and Korea by expanding distribution and leveraging AIG's product expertise. Reserves for individual fixed annuities continue to grow although demand for multi-currency fixed annuities in Japan has slowed due to currency rate fluctuations, rising local interest rates and equity markets. Growth of individual variable annuities has accelerated as those products have become more popular with consumers in Japan and Europe coupled with improved performance of equity markets. The largest contributor to the growth in group products is the pension profit center which experienced higher growth in fee income emanating from increased assets under management.

Life Insurance & Retirement Services Net Investment Income and Realized Capital Gains (losses)

The following table summarizes the components of net investment income for the three and six-month periods ended June 30, 2006 and 2005:

	Three Months Ended June 30,		Six Months Ended June 30,	
(in millions)	**2006**	2005	**2006**	2005
Domestic				
Fixed maturities, including short term investments	**$2,219**	$2,317	**$4,527**	$4,549
Equity securities	**2**	6	**7**	6
Interest on mortgage, policy and collateral loans	**195**	177	**384**	344
Partnership income – excluding Synfuels	**72**	25	**213**	179
Partnership income (loss) – Synfuels	**(22)**	(43)	**(59)**	(79)
Other	**13**	(8)	**10**	(35)
Total investment income	**2,479**	2,474	**5,082**	4,964
Investment expenses	**29**	34	**53**	61
Net investment income	**$2,450**	$2,440	**$5,029**	$4,903
Foreign				
Fixed maturities, including short term investments	**$1,718**	$1,524	**$3,249**	$2,897
Equity securities	**95**	70	**166**	112
Interest on mortgage, policy and collateral loans	**110**	109	**218**	222
Partnership income	**23**	8	**40**	20
Other[(a)]	**293**	120	**366**	203
Total investment income before policyholder trading gains (losses)	**2,239**	1,831	**4,039**	3,454
Policyholder trading gains (losses)[(b)]	**(324)**	(54)	**61**	224
Total investment income	**1,915**	1,777	**4,100**	3,678
Investment expenses	**67**	50	**122**	97
Net investment income	**$1,848**	$1,727	**$3,978**	$3,581
Total				
Fixed maturities, including short term investments	**$3,937**	$3,841	**$7,776**	$7,446
Equity securities	**97**	76	**173**	118
Interest on mortgage, policy and collateral loans	**305**	286	**602**	566
Partnership income – excluding Synfuels	**95**	33	**253**	199
Partnership income (loss) – Synfuels	**(22)**	(43)	**(59)**	(79)
Other[(a)]	**306**	112	**376**	168
Total investment income before policyholder trading gains (losses)	**4,718**	4,305	**9,121**	8,418
Policyholder trading gains (losses)[(b)]	**(324)**	(54)	**61**	224
Total investment income	**4,394**	4,251	**9,182**	8,642
Investment expenses	**96**	84	**175**	158
Net investment income	**$4,298**	$4,167	**$9,007**	$8,484

(a) Includes the effect of an out of period adjustment relating to the accounting for certain interests in unit investment trusts. For the three and six-month periods ended June 30, 2006, the effect was an increase of $221 million.

(b) Relates principally to assets held in various trading securities accounts that do not qualify for separate account treatment under SOP 03-1. These amounts are offset by an equal change included in incurred policy losses and benefits.

The following table summarizes Domestic Life Insurance & Retirement Services partnership income (loss) by line of business for the three and six-month periods ended June 30, 2006 and 2005:

	Three Months Ended June 30,		Six Months Ended June 30,	
(in millions)	**2006**	2005	**2006**	2005
Domestic life – excluding Synfuels:				
Life insurance	**$ 2**	$ 25	**$ 10**	$ 104
Home service	**–**	1	**2**	2
Subtotal	**2**	26	**12**	106
Domestic life – Synfuels:				
Life insurance	**(16)**	(29)	**(41)**	(53)
Home service	**(6)**	(14)	**(18)**	(26)
Subtotal	**(22)**	(43)	**(59)**	(79)
Total domestic life	**(20)**	(17)	**(47)**	27
Retirement services:				
Group retirement products	**35**	–	**77**	25
Individual fixed annuities	**35**	(1)	**124**	48
Total retirement services	**70**	(1)	**201**	73
Total	**$ 50**	$ (18)	**$ 154**	$ 100

Quarterly Life Insurance & Retirement Services Net Investment Income and Realized Capital Gains (Losses)

Net investment income increased 3 percent for the second quarter of 2006 when compared to the same period in 2005 as a result of the above mentioned out of period adjustment. This adjustment offset a decline which was mostly attributable to lower policyholder trading gains (losses), which are linked mainly to equities, and are offset by an equal change in incurred policy losses and benefits. Investment income results for certain operations were reduced in the second quarter of 2006 by losses related to investments in structured notes linked to emerging market sovereign debt that incorporates both interest rate risk and currency risk. Mark-to-market losses related to these structured notes were $46 million and $28 million for the three and six months ended June 30, 2006, respectively. In addition, period to period comparisons of investment income for some lines of business are affected by yield enhancement activity, particularly partnership income as shown in the above table.

AIG generates income tax credits as a result of investing in synthetic fuel production (synfuels) related to the investment loss shown in the above table and records those benefits in its provision for income taxes. The amount of those income tax credits was $21 million and $61 million for the three months ended June 30, 2006 and 2005, respectively. See Note 6(l) of Notes to Consolidated Financial Statements for a further discussion of the effect of the change in oil prices on synfuel tax credits. AIG may reduce future production levels depending upon oil prices which affect the availability of the synthetic fuel tax credit.

Year-to-date Life Insurance & Retirement Services Net Investment Income and Realized Capital Gains (Losses)

The growth in net investment income for the first six months of 2006 compared to a year ago parallels the growth in general account reserves and surplus for both Domestic and Foreign Life Insurance & Retirement Services companies and the effect of the aforementioned out of period adjustment. Also, net investment income was positively affected by the compounding of previously earned and reinvested investment cash flows along with the addition of new net cash flows from operations. Investment income includes income generated from traditional fixed income investments as well as income generated from other sources.

The amount of income tax credits generated as a result of investing in synthetic fuel production (synfuels) was $59 million and $115 million for the first six months of 2006 and 2005, respectively.

The following table summarizes realized capital gains (losses) by major category for the three and six-month periods ended June 30, 2006 and 2005:

	Three Months Ended June 30,		Six Months Ended June 30,	
(in millions)	**2006**	2005	**2006**	2005
Domestic life:				
Fixed maturities	**$ (42)**	$ 28	**$ (64)**	$ 23
Equity securities	**4**	7	**6**	7
Other:				
FAS 52	**1**	–	**–**	–
FAS 133	**28**	(171)	**115**	(66)
Other-than-temporary declines	**(58)**	(2)	**(112)**	(25)
Other	**(8)**	3	**(12)**	(2)
Total domestic life	**(75)**	(135)	**(67)**	(63)
Domestic retirement services:				
Fixed maturities	**(22)**	(14)	**(94)**	(44)
Equity securities	**17**	24	**31**	31
Other:				
FAS 133	**(42)**	95	**(36)**	85
Other-than-temporary declines	**(249)**	(72)	**(374)**	(114)
Other	**(11)**	24	**(36)**	20
Total domestic retirement services	**(307)**	57	**(509)**	(22)
Foreign:				
Fixed maturities	**(125)**	72	**(146)**	137
Equity securities	**250**	104	**401**	157
Other:				
FAS 52	**(95)**	(65)	**(90)**	(176)
FAS 133	**87**	38	**346**	(26)
Other-than-temporary declines	**(4)**	(21)	**(45)**	(26)
Other	**51**	(4)	**50**	(17)
Total foreign	**164**	124	**516**	49
Total	**$(218)**	$ 46	**$ (60)**	$ (36)

Realized capital gains (losses) include normal portfolio transactions as well as derivative gains (losses) for transactions that do not qualify for hedge accounting treatment under FAS 133, transactional foreign exchange gains and losses and other-than-temporary declines in the value of investments. Line of business results for Domestic Life Insurance & Retirement Services exclude the effect of realized capital gains (losses), but include the related effect on the amortization of deferred acquisition costs.

Life Insurance & Retirement Services Underwriting and Investment Risk

The risks associated with life and accident and health products are underwriting risk and investment risk. The risk associated with the financial and investment contract products is primarily investment risk.

Underwriting risk represents the exposure to loss resulting from the actual policy experience adversely emerging in comparison to the assumptions made in the product pricing associated with mortality, morbidity, termination and expenses. The emergence of significant adverse experience would require an adjustment to DAC and benefit reserves that could have a substantial effect on AIG's results of operations.

Natural disasters such as hurricanes, earthquakes and other catastrophes have the potential to adversely affect AIG's operating results. Other risks, such as an outbreak of a pandemic disease, such as the Avian Influenza A Virus (H5N1), could adversely affect AIG's business and operating results to an extent that may be only minimally offset by reinsurance programs.

While outbreaks of the Avian Flu continue to occur among poultry or wild birds in a number of countries in Asia, Europe, and Africa, transmission to humans has been rare to date. If the virus mutates to a form that can be transmitted from human to human, it has the potential to spread rapidly worldwide. If such an outbreak were to take place, early quarantine and vaccination could be critical to containment.

Both the contagion and mortality rate of any mutated H5N1 virus that can be transmitted from human to human are highly speculative. AIG continues to monitor the developing facts. A significant global outbreak could have a material adverse effect on Life Insurance & Retirement Services operating results and liquidity from increased mortality and morbidity rates. For a further discussion of pandemic influenza, see "Managing Market Risk – Catastrophe Exposures – Pandemic Influenza."

AIG's Foreign Life Insurance & Retirement Services companies generally limit their maximum underwriting exposure on life insurance of a single life to approximately $1.7 million of coverage. AIG's Domestic Life Insurance & Retirement Services companies limit their maximum underwriting exposure on life insurance of a single life to $10 million of coverage in certain circumstances by using yearly renewable term reinsurance. (See also the discussion under "Liquidity" herein.)

AIRCO acts primarily as an internal reinsurance company for AIG's foreign life operations. This facilitates insurance risk management (retention, volatility, concentrations) and capital planning locally (branch and subsidiary). It also allows AIG to pool its insurance risks and purchase reinsurance more efficiently at a consolidated level, manage global counterparty risk and relationships and manage global life catastrophe risks.

AIG's domestic Life Insurance & Retirement Services operations utilize internal and third-party reinsurance relationships to manage insurance risks and to facilitate capital management strategies. Pools of highly-rated third-party reinsurers are utilized to manage net amounts at risk in excess of retention limits. AIG's domestic life insurance companies also cede excess, non-economic reserves carried on a statutory-basis only on certain term and universal life insurance policies and certain fixed annuities to AIG Life of Bermuda Ltd., a wholly owned Bermuda reinsurer.

AIG generally obtains letters of credit in order to obtain statutory recognition of these intercompany reinsurance transactions. For this purpose, AIG entered into a $2.5 billion syndicated letter of credit facility in December 2004. Letters of credit totaling $2.5 billion were outstanding as of June 30, 2006. The letter of credit facility has a ten-year term, but the facility can be reduced or terminated by the lenders beginning after seven years.

In November 2005, AIG entered into a revolving credit facility for an aggregate amount of $3 billion. The facility can be drawn in the form of letters of credit with terms of up to ten years. As of June 30, 2006, $2.33 billion principal amount of letters of credit are outstanding under this facility, of which approximately $939 million relates to life intercompany reinsurance transactions. AIG also obtained approximately $298 million letters of credit on a bilateral basis.

Investment risk represents the exposure to loss resulting from the cash flows from the invested assets, primarily long-term fixed rate investments, being less than the cash flows required to meet the obligations of the expected policy and contract liabilities and the necessary return on investments. (See also the discussion under "Liquidity" herein.)

To minimize its exposure to investment risk, AIG tests the cash flows from the invested assets and policy and contract liabilities using various interest rate scenarios to evaluate investment risk and to confirm that assets are sufficient to pay these liabilities.

AIG actively manages the asset-liability relationship in its foreign operations, as it has been doing throughout AIG's history, even though certain territories lack qualified long-term investments or certain local regulatory authorities may impose investment restrictions. For example, in several

Southeast Asian countries, the duration of investments is shorter than the effective maturity of the related policy liabilities. Therefore, there is risk that the reinvestment of the proceeds at the maturity of the initial investments may be at a yield below that of the interest required for the accretion of the policy liabilities. Additionally, there exists a future investment risk associated with certain policies currently in force which will have premium receipts in the future. That is, the investment of these future premium receipts may be at a yield below that required to meet future policy liabilities.

In the first six months of 2006, new money investment yields have been generally rising in some markets, such as Japan, Thailand and the U.S., which is generally favorable to AIG's spread-based businesses. In regard to inforce business, management focus is required in both the investment and product management process to maintain an adequate yield to match the interest necessary to support future policy liabilities. Business strategies continue to evolve to maintain profitability of the overall business. As such, in some countries, new products are being introduced with minimal investment guarantees resulting in a shift toward investment linked savings products and away from traditional savings products with higher guarantees.

The investment of insurance cash flows and reinvestment of the proceeds of matured securities and coupons requires active management of investment yields while maintaining satisfactory investment quality and liquidity.

AIG may use alternative investments in certain foreign jurisdictions where interest rates remain low and there are limited long-dated bond markets, including equities, real estate and foreign currency denominated fixed income instruments to extend the duration or increase the yield of the investment portfolio to more closely match the requirements of the policyholder liabilities and DAC recoverability. This strategy has been effectively used in Japan and more recently by Nan Shan in Taiwan. Foreign assets comprised approximately 29 percent of Nan Shan's invested assets at June 30, 2006, slightly below the maximum allowable percentage under current regulation. In response to the low interest rate environment and the volatile exchange rate of the NT dollar, Nan Shan is emphasizing new products with lower implied guarantees, including participating endowments and variable universal life. Although the risks of a continued low interest rate environment coupled with a volatile NT dollar could increase net liabilities and require additional capital to maintain adequate local solvency margins, Nan Shan currently believes it has adequate resources to meet all future policy obligations.

AIG actively manages the asset-liability relationship in its domestic operations. This relationship is more easily managed through the ample supply of qualified long-term investments.

AIG uses asset-liability matching as a management tool worldwide to determine the composition of the invested assets and appropriate marketing strategies. As a part of these strategies, AIG may determine that it is economically advantageous to be temporarily in an unmatched position due to anticipated interest rate or other economic changes. In addition, the absence of long-dated fixed income instruments in certain markets may preclude a matched asset-liability position in those markets.

A number of guaranteed benefits, such as living benefits or guaranteed minimum death benefits, are offered on certain variable life and variable annuity products. AIG manages its exposure resulting from these long-term guarantees through reinsurance or capital market hedging instruments.

DAC for Life Insurance & Retirement Services products arises from the deferral of those costs that vary with, and are directly related to, the acquisition of new or renewal business. Policy acquisition costs for life insurance products are generally deferred and amortized over the premium paying period of the policy. Policy acquisition costs that relate to universal life and investment-type products, including variable and fixed annuities (investment-oriented products) are deferred and amortized, with interest, as appropriate, in relation to the historical and future incidence of estimated gross profits to be realized over the estimated lives of the contracts. Amortization expense includes the effects of current period realized capital gains and losses for investment type products. With respect to investment-oriented products, AIG's policy is to adjust amortization assumptions for DAC when estimates of current or future gross profits to be realized from these contracts are revised. With respect to variable annuities sold domestically (representing the vast majority of AIG's variable annuity business), the assumption for the long-term annual net growth rate of the equity markets used in the determination of DAC amortization is approximately ten percent. A methodology referred to as "reversion to the mean" is used to maintain this long-term net growth rate assumption, while giving consideration to short-term variations in equity markets. Estimated gross profits include investment income and gains and losses less interest required on policyholder reserves, as well as other charges in the contract less actual mortality and expenses. Current experience and changes in the expected future gross profits are analyzed to determine the effect on the amortization of DAC. The estimation of projected gross profits requires significant management judgment. The assumptions with respect to the current and projected gross profits are reviewed and analyzed quarterly and are adjusted accordingly.

The following table summarizes the major components of the changes in DAC and VOBA for the six months ended June 30, 2006 and 2005:

(in millions)	2006			2005		
	DAC	**VOBA**	**Total**	DAC	VOBA	Total
Domestic Life Insurance & Retirement Services:						
Balance at beginning of year	**$10,505**	**$ 865**	**$11,370**	$ 8,830	$ 836	$ 9,666
Acquisition costs deferred	**1,104**	**–**	**1,104**	1,057	–	1,057
Amortization (charged) or credited to operating income:						
Related to realized capital gains (losses)	**85**	**16**	**101**	6	–	6
Related to unlocking future assumptions	**4**	**(3)**	**1**	–	–	–
All other amortization	**(766)**	**(45)**	**(811)**	(725)	(47)	(772)
Related to change in unrealized gains (losses) on securities	**1,854**	**154**	**2,008**	58	(37)	21
Increase (decrease) due to foreign exchange	**16**	**4**	**20**	(4)	(2)	(6)
Balance at end of period	**$12,802**	**$ 991**	**$13,793**	$ 9,222	$ 750	$ 9,972
Foreign Life Insurance & Retirement Services:						
Balance at beginning of year	**$16,552**	**$1,278**	**$17,830**	$14,472	$1,681	$16,153
Acquisition costs deferred	**2,481**	**–**	**2,481**	2,302	–	2,302
Amortization (charged) or credited to operating income:						
Related to realized capital gains (losses)	**1**	**–**	**1**	(2)	1	(1)
Related to unlocking future assumptions	**28**	**–**	**28**	62	–	62
All other amortization	**(1,168)**	**(95)**	**(1,263)**	(909)	(123)	(1,032)
Related to change in unrealized gains (losses) on securities	**83**	**(5)**	**78**	(241)	(8)	(249)
Increase (decrease) due to foreign exchange	**856**	**78**	**934**	(223)	(70)	(293)
Balance at end of period	**$18,833**	**$1,256**	**$20,089**	$15,461	$1,481	$16,942
Total Life Insurance & Retirement Services:						
Balance at beginning of year	**$27,057**	**$2,143**	**$29,200**	$23,302	$2,517	$25,819
Acquisition costs deferred	**3,585**	**–**	**3,585**	3,359	–	3,359
Amortization (charged) or credited to operating income:						
Related to realized capital gains (losses)	**86**	**16**	**102**	4	1	5
Related to unlocking future assumptions	**32**	**(3)**	**29**	62	–	62
All other amortization	**(1,934)**	**(140)**	**(2,074)**	(1,634)	(170)	(1,804)
Related to change in unrealized gains (losses) on securities	**1,937**	**149**	**2,086**	(183)	(45)	(228)
Increase (decrease) due to foreign exchange	**872**	**82**	**954**	(227)	(72)	(299)
Balance at end of period	**$31,635**	**$2,247**	**$33,882**	$24,683	$2,231	$26,914

AIG's variable annuity earnings will be affected by changes in market returns because separate account revenues, primarily composed of mortality and expense charges and asset management fees, are a function of asset values.

DAC for both insurance-oriented and investment-oriented products as well as retirement services products are reviewed for recoverability, which involves estimating the future profitability of current business. This review also involves significant management judgment. If the actual emergence of future profitability were to be substantially different than that estimated, AIG's results of operations could be significantly affected in future periods.

Invested Assets

The following tables summarize the composition of AIG's invested assets by segment, at June 30, 2006 and December 31, 2005:

(in millions)	General Insurance	Life Insurance & Retirement Services	Asset Management	Financial Services	Other	Total
2006						
Fixed maturities:						
Bonds available for sale, at market value	$ 58,449	$271,261	$31,175	$ 1,298	$ –	$362,183
Bonds held to maturity, at amortized cost	21,510	–	–	–	–	21,510
Bond trading securities, at market value	–	1,312	5,175	–	–	6,487
Equity securities:						
Common stocks available for sale, at market value	4,522	9,019	227	–	61	13,829
Common and preferred stocks trading, at market value	344	10,140	373	–	–	10,857
Preferred stocks available for sale, at market value	1,797	644	–	6	–	2,447
Mortgage loans on real estate, net of allowance	13	11,882	4,215	70	–	16,180
Policy loans	2	7,314	48	2	–	7,366
Collateral and guaranteed loans, net of allowance	3	1,204	751	2,002	98	4,058
Financial services assets:						
Flight equipment primarily under operating leases, net of accumulated depreciation	–	–	–	39,307	–	39,307
Securities available for sale, at market value	–	–	–	38,678	–	38,678
Trading securities, at market value	–	–	–	5,165	–	5,165
Spot commodities	–	–	–	797	–	797
Unrealized gain on swaps, options and forward transactions	–	–	–	18,901	–	18,901
Trading assets	–	–	–	1,345	–	1,345
Securities purchased under agreements to resell, at contract value	–	–	–	14,085	–	14,085
Finance receivables, net of allowance	–	–	–	27,515	–	27,515
Securities lending collateral, at market value	5,700	49,357	13,611	64	–	68,732
Other invested assets	7,330	8,644	11,566	1,869	1	29,410
Short-term investments, at cost	3,950	8,050	8,125	1,055	6	21,186
Total investments and financial services assets as shown in the balance sheet	103,620	378,827	75,266	152,159	166	710,038
Cash	635	350	863	284	8	2,140
Investment income due and accrued	1,160	4,182	366	19	5	5,732
Real estate, net of accumulated depreciation	634	2,762	2,470	24	36	5,926
Total invested assets	$106,049	$386,121	$78,965	$152,486	$215	$723,836

(in millions)	General Insurance	Life Insurance & Retirement Services	Asset Management	Financial Services	Other	Total
2005						
Fixed maturities:						
Bonds available for sale, at market value	$50,870	$273,165	$34,174	$ 1,307	$ –	$359,516
Bonds held to maturity, at amortized cost	21,528	–	–	–	–	21,528
Bond trading securities, at market value	–	1,073	3,563	–	–	4,636
Equity securities:						
Common stocks available for sale, at market value	4,505	7,436	227	–	59	12,227
Common stocks trading, at market value	425	8,122	412	–	–	8,959
Preferred stocks available for sale, at market value	1,632	760	–	10	–	2,402
Mortgage loans on real estate, net of allowance	14	10,247	3,968	71	–	14,300
Policy loans	2	6,987	48	2	–	7,039
Collateral and guaranteed loans, net of allowance	3	1,172	578	1,719	98	3,570
Financial services assets:						
Flight equipment primarily under operating leases, net of accumulated depreciation	–	–	–	36,245	–	36,245
Securities available for sale, at market value	–	–	–	37,511	–	37,511
Trading securities, at market value	–	–	–	6,499	–	6,499
Spot commodities	–	–	–	92	–	92
Unrealized gain on swaps, options and forward transactions	–	–	–	18,695	–	18,695
Trading assets	–	–	–	1,204	–	1,204
Securities purchased under agreements to resell, at contract value	–	28	–	14,519	–	14,547
Finance receivables, net of allowance	–	–	–	27,995	–	27,995
Securities lending collateral, at market value	4,931	42,991	11,549	–	–	59,471
Other invested assets	6,272	7,777	10,459	2,751	8	27,267
Short-term investments, at cost	2,482	5,855	5,619	1,382	4	15,342
Total investments and financial services assets as shown in the balance sheet	92,664	365,613	70,597	150,002	169	679,045
Cash	305	989	196	331	76	1,897
Investment income due and accrued	1,232	4,073	402	18	2	5,727
Real estate, net of accumulated depreciation	603	2,729	1,710	24	32	5,098
Total invested assets	$94,804	$373,404	$72,905	$150,375	$279	$691,767

Insurance and Asset Management Invested Assets

AIG's investment strategy is to invest primarily in high quality securities while maintaining diversification to avoid significant exposure to issuer, industry and/or country concentrations. With respect to Domestic General Insurance, AIG's strategy is to invest in longer duration fixed maturity investments to maximize the yields at the date of purchase. With respect to Life Insurance & Retirement Services, AIG's strategy is to produce cash flows required to meet maturing insurance liabilities. (See also the discussion under "Operating Review: Life Insurance & Retirement Services Operations" herein.) AIG invests in equities for various reasons, including diversifying its overall exposure to interest rate risk. Available for sale bonds and equity securities are subject to declines in fair value. Such declines in fair value are presented in unrealized appreciation or depreciation of investments, net of taxes as a component of accumulated other comprehensive income. Declines that are determined to be other-than-temporary are reflected in income in the period in which the intent to hold the securities to recovery no longer exists. See "Valuation of Invested Assets". Generally, insurance regulations restrict the types of assets in which an insurance company may invest. When permitted by regulatory authorities and when deemed necessary to protect insurance assets, including invested assets, from adverse movements in foreign currency exchange rates, interest rates and equity prices, AIG and its insurance subsidiaries may enter into derivative transactions as end users. (See also the discussion under "Derivatives" herein.)

In certain jurisdictions, significant regulatory and/or foreign governmental barriers exist which may not permit the immediate free flow of funds between insurance subsidiaries or from the insurance subsidiaries to AIG parent.

The following tables summarize the composition of AIG's insurance and asset management invested assets by segment, at June 30, 2006 and December 31, 2005:

(dollars in millions)	General Insurance	Life Insurance & Retirement Services	Asset Management	Total	Percent of Total	Percent Distribution Domestic	Percent Distribution Foreign
2006							
Fixed maturities:							
Bonds available for sale, at market value	$ 58,449	$271,261	$31,175	$360,885	63.2%	57.4%	42.6%
Bonds held to maturity, at amortized cost	21,510	–	–	21,510	3.8	100.0	–
Bond trading securities, at market value	–	1,312	5,175	6,487	1.1	3.0	97.0
Equity securities:							
Common stocks available for sale, at market value	4,522	9,019	227	13,768	2.4	26.1	73.9
Common and preferred stocks trading, at market value	344	10,140	373	10,857	1.9	3.2	96.8
Preferred stocks available for sale, at market value	1,797	644	–	2,441	0.4	83.0	17.0
Mortgage loans on real estate, net of allowance	13	11,882	4,215	16,110	2.8	83.5	16.5
Policy loans	2	7,314	48	7,364	1.3	40.9	59.1
Collateral and guaranteed loans, net of allowance	3	1,204	751	1,958	0.4	5.2	94.8
Securities lending collateral, at market value	5,700	49,357	13,611	68,668	12.0	86.9	13.1
Other invested assets	7,330	8,644	11,566	27,540	4.8	86.4	13.6
Short-term investments, at cost	3,950	8,050	8,125	20,125	3.6	35.4	64.6
Cash	635	350	863	1,848	0.3	27.6	72.4
Investment income due and accrued	1,160	4,182	366	5,708	1.0	55.2	44.8
Real estate, net of accumulated depreciation	634	2,762	2,470	5,866	1.0	51.2	48.8
Total	$106,049	$386,121	$78,965	$571,135	100.0%	61.0%	39.0%

(dollars in millions)	General Insurance	Life Insurance & Retirement Services	Asset Management	Total	Percent of Total	Percent Distribution Domestic	Percent Distribution Foreign
2005							
Fixed maturities:							
Bonds available for sale, at market value	$50,870	$273,165	$34,174	$358,209	66.2%	59.2%	40.8%
Bonds held to maturity, at amortized cost	21,528	–	–	21,528	4.0	100.0	–
Bond trading securities, at market value	–	1,073	3,563	4,636	0.9	3.3	96.7
Equity securities:							
Common stocks available for sale, at market value	4,505	7,436	227	12,168	2.2	28.7	71.3
Common stocks trading, at market value	425	8,122	412	8,959	1.7	4.8	95.2
Preferred stocks available for sale, at market value	1,632	760	–	2,392	0.4	88.8	11.2
Mortgage loans on real estate, net of allowance	14	10,247	3,968	14,229	2.7	84.6	15.4
Policy Loans	2	6,987	48	7,037	1.3	42.8	57.2
Collateral and guaranteed loans, net of allowance	3	1,172	578	1,753	0.3	1.2	98.8
Securities purchased under agreements to resell, at contract value	–	28	–	28	–	–	100.0
Securities lending collateral, at market value	4,931	42,991	11,549	59,471	11.0	87.3	12.7
Other invested assets	6,272	7,777	10,459	24,508	4.5	85.8	14.2
Short-term investments, at cost	2,482	5,855	5,619	13,956	2.6	27.3	72.7
Cash	305	989	196	1,490	0.2	15.0	85.0
Investment income due and accrued	1,232	4,073	402	5,707	1.1	56.9	43.1
Real estate, net of accumulated depreciation	603	2,729	1,710	5,042	0.9	45.2	54.8
Total	$94,804	$373,404	$72,905	$541,113	100.0%	62.3%	37.7%

Credit Quality

At June 30, 2006, approximately 59 percent of the fixed maturities investments were domestic securities. Approximately 37 percent of such domestic securities were rated AAA by one or more of the principal rating agencies. Approximately seven percent were below investment grade or not rated.

A significant portion of the foreign fixed income portfolio is rated by Moody's Investors Service (Moody's), S&P or similar foreign services. Similar credit quality rating services are not available in all overseas locations. AIG reviews the credit quality of the foreign portfolio nonrated fixed income investments, including mortgages. At June 30, 2006, approximately 18 percent of the foreign fixed income investments were either rated AAA or, on the basis of AIG's internal analysis, were equivalent from a credit standpoint to securities so rated. Approximately six percent were below investment grade or not rated at that date. A large portion of the foreign fixed income portfolio are sovereign fixed maturity securities supporting the policy liabilities in the country of issuance.

Any fixed income security may be subject to downgrade for a variety of reasons subsequent to any balance sheet date.

Valuation of Invested Assets

AIG has the ability to hold any fixed maturity security to its stated maturity, including those fixed maturity securities classified as available for sale. Therefore, the decision to sell any such fixed maturity security classified as available for sale reflects the judgment of AIG's management that the security sold is unlikely to provide, on a relative value basis, as attractive a return in the future as alternative securities entailing comparable risks. With respect to distressed securities, the sale decision reflects management's judgment that the risk-discounted anticipated ultimate recovery is less than the value achievable on sale.

The valuation of invested assets involves obtaining a market value for each security. The source for the market value is generally from market exchanges or dealer quotations, with the exception of nontraded securities.

If AIG chooses to hold a security, it evaluates the security for an other-than-temporary impairment in valuation. As a

matter of policy, the determination that a security has incurred an other-than-temporary decline in value and the amount of any loss recognition requires the judgment of AIG's management and a continual review of its investments.

In general, a security is considered a candidate for other-than-temporary impairment if it meets any of the following criteria:

- Trading at a significant (25 percent or more) discount to par or amortized cost (if lower) for an extended period of time (nine months or longer);
- The occurrence of a discrete credit event resulting in (i) the issuer defaulting on a material outstanding obligation; or (ii) the issuer seeking protection from creditors under the bankruptcy laws or any similar laws intended for the court supervised reorganization of insolvent enterprises; or (iii) the issuer proposing a voluntary reorganization pursuant to which creditors are asked to exchange their claims for cash or securities having a fair value substantially lower than par value of their claims; or
- In the opinion of AIG's management, it is probable that AIG may not realize a full recovery on its investment, irrespective of the occurrence of one of the foregoing events.

At each balance sheet date, AIG evaluates its securities holdings in an unrealized loss position. Where AIG does not intend to hold such securities until they have fully recovered their carrying value based on the circumstances present at the date of evaluation, AIG records the unrealized loss in income. If events or circumstances change, such as unexpected changes in creditworthiness of the obligor, general interest rate environment, tax circumstances, liquidity events, and statutory capital management considerations among others, AIG revisits its intent to determine if a loss should be recorded in income. Further, if a loss is recognized from a sale subsequent to a balance sheet date pursuant to these changes in circumstances, the loss is recognized in the period in which the intent to hold the securities to recovery no longer exists.

Once a security has been identified as other-than-temporarily impaired, the amount of such impairment is determined by reference to that security's contemporaneous market price and recorded as a charge to earnings.

As a result of these policies, AIG recorded, in realized capital gains (losses), other-than-temporary impairment pretax losses of $370 million and $107 million for the three-month periods ended June 30, 2006 and 2005, respectively, and $596 million and $200 million for the six-month periods ended June 30, 2006 and 2005, respectively.

No impairment charge with respect to any one single credit was significant to AIG's consolidated financial condition or results of operations, and no individual impairment loss exceeded 1.0 percent of consolidated net income for the first six months of 2006.

Excluding the other-than-temporary impairments noted above, the changes in market value for AIG's available for sale portfolio, which constitutes the vast majority of AIG's investments, were recorded in accumulated other comprehensive income as unrealized gains or losses, net of tax.

At June 30, 2006, the fair value of AIG's fixed maturities and equity securities aggregated to $417.3 billion. At June 30, 2006, aggregate unrealized gains after taxes for fixed maturity and equity securities were $7.0 billion. At June 30, 2006, the aggregate unrealized losses after taxes of fixed maturity and equity securities were approximately $6.2 billion.

The effect on net income of unrealized losses after taxes will be further mitigated upon realization, because certain realized losses will be charged to participating policyholder accounts, or realization will result in current decreases in the amortization of certain deferred policy acquisition costs.

At June 30, 2006, unrealized losses for fixed maturity securities and equity securities did not reflect any significant industry concentrations.

The amortized cost of fixed maturities available for sale in an unrealized loss position at June 30, 2006, by contractual maturity, is shown below:

(in millions)	Amortized Cost
Due in one year or less	$ 5,690
Due after one year through five years	36,505
Due after five years through ten years	92,162
Due after ten years	93,329
Total	$227,686

In the six months ended June 30, 2006, the pretax realized losses incurred with respect to the sale of fixed maturities and equity securities were $790 million. The aggregate fair value of securities sold was $25.8 billion, which was approximately 97 percent of amortized cost. The average period of time that securities sold at a loss during the six months ended June 30, 2006 were trading continuously at a price below book value was approximately five months.

At June 30, 2006, aggregate pretax unrealized gains were $10.79 billion, while the pretax unrealized losses with respect to investment grade bonds, non-investment grade bonds and equity securities were $9.0 billion, $320 million and $338 million, respectively. Aging of the pretax unrealized losses with respect to these securities, distributed as a percentage of cost relative to unrealized loss (the extent by which the market value is less than amortized cost or cost), including the number of respective items, was as follows:

	Less than or equal to 20% of Cost[a]			Greater than 20% to 50% of Cost[a]			Greater than 50% of Cost[a]			Total		
Aging (dollars in millions)	Cost[a]	Unrealized Loss	Items	Cost[a]	Unrealized Loss	Items	Cost[a]	Unrealized Loss	Items	Cost[a]	Unrealized Loss[b]	Items
Investment grade bonds												
0-6 months	$117,600	$3,355	15,449	$ 46	$10	4	$28	$20	10	$117,674	$3,385	15,463
7-12 months	76,863	4,237	9,561	59	14	5	—	—	5	76,922	4,251	9,571
>12 months	23,185	1,267	3,015	172	41	11	8	6	13	23,365	1,314	3,039
Total	$217,648	$8,859	28,025	$277	$65	20	$36	$26	28	$217,961	$8,950	28,073
Non-investment grade bonds												
0-6 months	$ 7,214	$ 164	1,494	$ 31	$ 9	8	$14	$11	11	$ 7,259	$ 184	1,513
7-12 months	1,401	68	207	6	2	2	—	—	1	1,407	70	210
>12 months	1,043	62	214	14	3	4	2	1	16	1,059	66	234
Total	$ 9,658	$ 294	1,915	$ 51	$14	14	$16	$12	28	$ 9,725	$ 320	1,957
Total bonds												
0-6 months	$124,814	$3,519	16,943	$ 77	$19	12	$42	$31	21	$124,933	$3,569	16,976
7-12 months	78,264	4,305	9,768	65	16	7	—	—	6	78,329	4,321	9,781
>12 months	24,228	1,329	3,229	186	44	15	10	7	29	24,424	1,380	3,273
Total	$227,306	$9,153	29,940	$328	$79	34	$52	$38	56	$227,686	$9,270	30,030
Equity securities												
0-6 months	$ 4,251	$ 200	2,325	$144	$36	175	$10	$ 6	22	$ 4,405	$ 242	2,522
7-12 months	944	56	415	92	25	132	20	15	27	1,056	96	574
>12 months	—	—	—	—	—	—	—	—	—	—	—	—
Total	$ 5,195	$ 256	2,740	$236	$61	307	$30	$21	49	$ 5,461	$ 338	3,096

(a) For bonds, represents amortized cost.

(b) As more fully described above, upon realization, certain realized losses will be charged to participating policyholder accounts, or realization will result in a current decrease in the amortization of certain deferred policy acquisition costs.

As stated previously, the valuation for AIG's investment portfolio comes from market exchanges or dealer quotations, with the exception of nontraded securities. AIG considers nontraded securities to mean certain fixed income investments, certain structured securities, direct private equities, limited partnerships and hedge funds. The aggregate carrying value of these securities at June 30, 2006 was approximately $68 billion.

The methodology used to estimate fair value of nontraded fixed income investments is by reference to traded securities with similar attributes and using a matrix pricing methodology. This technique takes into account such factors as the industry, the security's rating and tenor, its coupon rate, its position in the capital structure of the issuer, and other relevant factors. The change in fair value is recognized as a component of accumulated other comprehensive income, net of tax.

For certain structured securities, the carrying value is based on an estimate of the security's future cash flows pursuant to the requirements of Emerging Issues Task Force Issue No. 99-20, "Recognition of Interest Income and Impairment on Purchased and Retained Beneficial Interests in Securitized Financial Assets." The change in carrying value is recognized in income.

Hedge funds and limited partnerships in which AIG holds in the aggregate less than a five percent interest are reported at fair value. The change in fair value is recognized as a component of accumulated other comprehensive income, net of tax.

With respect to hedge funds and limited partnerships in which AIG holds in the aggregate a five percent or greater interest, AIG uses the equity method to record these investments. The changes in such net asset values are recorded in income.

AIG obtains the fair value of its investments in limited partnerships and hedge funds from information provided by the general partner or manager of each of these investments, the accounts of which are generally audited on an annual basis.

Each of these investment categories is regularly tested to determine if impairment in value exists. Various valuation techniques are used with respect to each category in this determination.

Financial Services Operations

AIG's Financial Services subsidiaries engage in diversified activities including aircraft and equipment leasing, capital markets transactions, consumer finance and insurance premium financing. (See also Note 2 of Notes to Consolidated Financial Statements.)

Aircraft Finance

AIG's Aircraft Finance operations represent the operations of ILFC, which generates its revenues primarily from leasing new and used commercial jet aircraft to domestic and foreign airlines. Revenues also result from the remarketing of commercial jets for its own account, and remarketing and fleet management for airlines and financial institutions.

ILFC finances its purchases of aircraft primarily through the issuance of a variety of debt instruments. The composite borrowing rates, which include the effect of economic hedges, at June 30, 2006 and 2005 were 5.24 percent and 4.52 percent, respectively. (See also the discussions under "Capital Resources" and "Liquidity" herein and Note 2 of Notes to Consolidated Financial Statements.)

ILFC's sources of revenue are principally from scheduled and charter airlines and companies associated with the airline industry. The airline industry is sensitive to changes in economic conditions, cyclical and highly competitive. Airlines and related companies may be affected by political or economic instability, terrorist activities, changes in national policy, competitive pressures on certain air carriers, fuel prices and shortages, labor stoppages, insurance costs, recessions, world health issues and other political or economic events adversely affecting world or regional trading markets. ILFC's revenues and income will be affected by its customers' ability to react and cope with the volatile competitive environment in which they operate, as well as ILFC's own competitive environment.

ILFC is exposed to operating loss and liquidity strain through nonperformance of aircraft lessees, through owning aircraft which it would be unable to sell or re-lease at acceptable rates at lease expiration and, in part, through committing to purchase aircraft which it would be unable to lease.

ILFC manages the risk of nonperformance by its lessees with security deposit requirements, through repossession rights, overhaul requirements, and closely monitoring industry conditions through its marketing force. However, there can be no assurance that ILFC would be able to successfully manage the risks relating to the effect of possible future deterioration in the airline industry. Approximately 90 percent of ILFC's fleet is leased to non-U.S. carriers, and the fleet, comprised of the most efficient aircraft in the airline industry, continues to be in high demand from such carriers.

ILFC typically contracts to re-lease aircraft before the end of the existing lease term. For aircraft returned before the end of the lease term, ILFC has generally been able to re-lease such aircraft within two to six months of its return. As a lessor, ILFC considers an aircraft "idle" or "off lease" when the aircraft is not subject to a signed lease agreement or signed letter of intent. ILFC had no aircraft off lease at June 30, 2006, and all new aircraft deliveries in 2006 have been leased. (See also the discussions under "Capital Resources" and "Liquidity" herein.)

Management formally reviews regularly, and no less frequently than quarterly, issues affecting ILFC's fleet, including events and circumstances that may cause impairment of aircraft values. Management evaluates aircraft in the fleet as necessary, based on these events and circumstances in accordance with Statement of Financial Accounting Standards No. 144, "Accounting for the Impairment or Disposal of Long-Lived Assets" (FAS 144). ILFC has not recognized any impairment related to its fleet. ILFC has been able to re-lease the aircraft without diminution in lease rates to an extent that would require an impairment write-down. (See also the discussions under "Liquidity" herein.)

Capital Markets

Capital Markets represents the operations of AIGFP, which engages as principal in a wide variety of financial transactions, including standard and customized financial products involving commodities, credit, currencies, energy, equities and rates. AIGFP also invests in a diversified portfolio of securities and engages in borrowing activities involving issuing standard and structured notes and other securities, and entering into guaranteed investment agreements (GIAs).

As Capital Markets is a transaction-oriented operation, current and past revenues and operating results may not provide a basis for predicting future performance. AIG's Capital Markets operations derive substantially all their revenues from hedged financial positions entered in connection with counterparty transactions rather than from speculative transactions. AIGFP also participates as a dealer in a wide variety of financial derivatives transactions. AIGFP economically hedges the market risks arising from its transactions, although hedge accounting under FAS 133 is not currently being applied to any of the derivatives and related assets and liabilities. Accordingly, revenues and operating income are exposed to volatility resulting from differences in the timing of revenue recognition between the derivatives and the hedged assets and liabilities. Revenues and operating income of the Capital Markets operations and the percentage change in these amounts for any given period are also significantly affected by the number, size and profitability of transactions

entered into by these subsidiaries during that period relative to those entered into during the prior period. Generally, the realization of transaction revenues as measured by the receipt of funds is not a significant reporting event as the gain or loss on AIGFP's trading transactions is currently reflected in operating income as the fair values change from period to period.

The overwhelming majority of AIG's financial derivatives are conducted by the Capital Markets operations. Capital Markets enters into derivative transactions to hedge the interest rate and foreign currency exposures associated with its available for sale assets and borrowings. While the derivatives entered into to hedge its outstanding transactions and positions are highly effective economic hedges, AIG did not meet the requirements for hedge accounting under FAS 133. The change in the fair value of these derivatives is included in other revenues while the offsetting change in fair value of the hedged items is not recognized in earnings.

Derivative transactions are entered into in the ordinary course of Capital Markets operations. Income on derivatives is recorded at fair value, determined by reference to the mark to market value of the derivative or their estimated fair value where market prices are not readily available. The resulting aggregate unrealized gains or losses from the derivative are reflected in the income statement. Where Capital Markets cannot verify significant model inputs to observable market data and verify the model value to market transactions, Capital Markets values the contract at the transaction price at inception and, consequently, records no initial gain or loss in accordance with Emerging Issues Task Force Issue No. 02-03, "Issues Involved in Accounting for Derivative Contracts Held for Trading Purposes and Contracts Involved in Energy Trading and Risk Management Activities" (EITF 02-03). Such initial gain or loss is recognized over the life of the transaction. Capital Markets periodically reevaluates its revenue recognition under EITF 02-03 based on the observability of market parameters. The mark to fair value of derivative transactions is reflected in the balance sheet in the captions "Unrealized gain on swaps, options and forward transactions," "Unrealized loss on swaps, options and forward transactions," "Trading assets" and "Trading liabilities." Unrealized gains represent the present value of the aggregate of each net receivable, by counterparty, and the unrealized losses represent the present value of the aggregate of each net payable, by counterparty as of June 30, 2006. These amounts will change from one period to the next due to changes in interest rates, currency rates, equity and commodity prices and other market variables, as well as cash movements, execution of new transactions and the maturing of existing transactions. (See also the discussion under "Derivatives" herein.)

Spread income on investments and borrowings is recorded on an accrual basis over the life of the transaction. Investments are classified as securities available for sale and are marked to market with the resulting unrealized gains or losses reflected in accumulated other comprehensive income. U.S. dollar denominated borrowings are carried at cost, while borrowings in any currency other than the U.S. dollar result in unrealized foreign exchange gains or losses reported in income. AIGFP hedges the economic exposure on its investments and borrowings on a portfolio basis using derivatives and other financial instruments. While these hedges are highly effective economic hedges, the requirements under FAS 133 hedge accounting were not met.

To the extent the Financial Services subsidiaries, other than AIGFP, use derivatives to economically hedge their assets or liabilities with respect to their future cash flows, and such hedges do not qualify for hedge accounting treatment under FAS 133, the changes in fair value of such derivatives are recorded in realized capital gains (losses) or other revenues. Amounts recorded in realized capital gains (losses) are reported as part of the Other category.

Consumer Finance

Domestically, AIG's Consumer Finance operations are principally conducted through American General Finance, Inc. (AGF). AGF derives a substantial portion of its revenues from finance charges assessed on outstanding real estate loans, secured and unsecured non-real estate loans and retail sales finance receivables. The real estate loans include first or second mortgages on residential real estate generally having a maximum term of 360 months, and are considered non-conforming. These loans may be closed-end accounts or open-end home equity lines of credit and may be fixed-rate or adjustable rate products. The non-real estate loans are secured by consumer goods, automobiles, or other personal property or are unsecured. Both secured and unsecured non-real estate loans generally have a maximum term of 60 months. The core of AGF's originations is sourced through its branches. However, a significant volume of real estate loans is also originated through broker relationships, and to lesser extents, through correspondent relationships and direct mail solicitations. In the first quarter of 2006, two wholly-owned subsidiaries of AGF discontinued originating real estate loans through an arrangement with AIG Federal Savings Bank, a federally chartered thrift, and began originating such loans under their own state licenses.

Many of AGF's borrowers are non-prime or sub-prime. Current economic conditions, such as interest rate and employment, have a direct effect on the borrowers' ability to repay these loans. AGF manages the credit risk inherent in its portfolio by using credit scoring models at the time of credit applications, established underwriting criteria, and in certain cases, individual loan reviews. AGF's Credit Strategy and Policy Committee monitors the quality of the finance receivables portfolio monthly when determining the appropriate level of the allowance for losses. The Credit Strategy and Policy Committee bases its conclusions on quantitative analyses, qualitative factors, current economic conditions and trends, and each committee member's experience in the con-

sumer finance industry. Through the first six months of 2006, the credit quality of AGF's finance receivables continues to be strong. However, declines in the strength of the U.S. housing market or economy may adversely affect the future credit quality of these receivables.

Internationally, AIG's Consumer Finance operations are principally conducted through AIG Consumer Finance Group (CFG). CFG operates primarily in emerging and developing markets. CFG has operations in Hong Kong, Taiwan, the Philippines, Thailand, Poland, Argentina, and Mexico. While products vary by market, the businesses generally provide credit cards, unsecured and secured non-real estate loans, term deposits, savings accounts, retail sales finance and real estate loans.

Consumer Finance operations are exposed to loss when contractual payments are not received. Credit loss exposure is managed through underwriting controls, mix of finance receivables, collateral and collection efficiency.

CFG monitors the quality of its finance receivable portfolio through a combination of a monthly Credit Review and quarterly Credit Reserve Committee review when determining the appropriate level of the allowance for losses. The Credit Reserve Committee bases its conclusions on quantitative analysis, qualitative factors, current economic conditions and trends, political and regulatory implications, competition, and the judgment of the committee's members. As a result of such a review and in light of industry-wide deteriorating credit conditions and tightening of overall consumer credit, the aggregate allowance for losses in AIG Credit Card Company (Taiwan) was increased by $88 million in the first quarter of 2006 to $130 million at March 31, 2006. The remaining balance, net of write-offs during the second quarter, is approximately $96 million at June 30, 2006. This balance, representing approximately 17 percent of CFG's outstanding credit card receivables for Taiwan, continues to be CFG's best estimate of the overall exposure and hence no additional increases to the allowance for losses were deemed necessary at June 30, 2006. The results of AIG Credit Card Company (Taiwan) are shared equally by the Financial Services and Life Insurance & Retirement Services segments.

Financial Services Results

Financial Services operations for the three and six-month periods ended June 30, 2006 and 2005 were as follows:

	Three Months Ended June 30,		Six Months Ended June 30,	
(in millions)	**2006**	2005	**2006**	2005
Revenues[(a)]:				
Aircraft Finance[(b)]	**$1,042**	$ 891	**$ 2,007**	$1,718
Capital Markets[(c)(d)]	**(788)**	1,975	**(1,088)**	2,731
Consumer Finance[(e)]	**939**	891	**1,863**	1,724
Other	**33**	21	**59**	41
Total	**$1,226**	$3,778	**$ 2,841**	$6,214
Operating income (loss)[(a)]:				
Aircraft Finance	**$ 189**	$ 124	**$ 318**	$ 311
Capital Markets[(d)]	**(952)**	1,836	**(1,422)**	2,456
Consumer Finance[(f)]	**199**	238	**374**	459
Other, including intercompany adjustments	**16**	16	**23**	33
Total	**$ (548)**	$2,214	**$ (707)**	$3,259

(a) Includes the effect of hedging activities that do not qualify for hedge accounting treatment under FAS 133, including the related foreign exchange gains and losses. For the three and six-month periods ended June 30, 2005, the effect was $(64) million and $(49) million, respectively, in operating income for Aircraft Finance. During 2006, Aircraft Finance's derivative gains and losses are reported as part of the Other category, and not reported in Aircraft Finance's operating income. For the three-month periods ended June 30, 2006 and 2005, the effect was $(1.16) billion and $1.70 billion in both revenues and operating income, respectively, for Capital Markets. For the six-month periods ended June 30, 2006 and 2005, the effect was $(1.84) billion and $2.16 billion in both revenues and operating income for Capital Markets. These amounts result primarily from interest rate and foreign currency derivatives which are hedging available for sale securities and borrowings.

(b) Revenues are primarily from ILFC aircraft lease rentals.

(c) Revenues, shown net of interest expense, are primarily from hedged financial positions entered into in connection with counterparty transactions and the effect of hedging activities that do not qualify for hedge accounting treatment under FAS 133 described in (a) above.

(d) Certain transactions entered into by AIGFP generate tax credits and benefits which are included in income taxes in the consolidated statement of income. The amount of such tax credits and benefits for the three-month periods ended June 30, 2006 and 2005 are $8 million and $21 million, respectively. The amount of such tax credits and benefits for the six-month periods ended June 30, 2006 and 2005 are $26 million and $40 million, respectively.

(e) Revenues are primarily finance charges.

(f) Includes $44 million in additional allowances for losses recorded in the first quarter of 2006 from AIG Credit Card Company (Taiwan).

Financial Services operating income decreased in the second quarter and first six months of 2006 compared to the same periods of 2005 due to the effect of hedging activities that do not qualify for hedge accounting under FAS 133. The effect of not applying hedge accounting under FAS 133 was partially offset by improved results in Capital Markets.

Quarterly Aircraft Finance Results

ILFC's operating income increased by $65 million, or 52 percent, in the second quarter of 2006 compared to the same period of 2005. The increase was due to a 2005 loss of $64 million relating to the effect of derivatives not qualifying for hedge accounting treatment. In 2006, such derivative gains and losses are reported as part of the Other category. Increased lease rental revenues driven by a larger fleet size and higher utilization of ILFC's aircraft were almost entirely offset by higher depreciation expense caused by a larger fleet, higher interest expense resulting from the rising cost of funds and additional outstanding borrowings, and charges related to bankrupt airlines. ILFC's fleet of aircraft under operating leases increased by approximately 78 planes from June 30, 2005 to June 30, 2006.

On August 4, 2006, ILFC announced a restatement of certain of its financial statements to correct its accounting for certain derivative transactions under FAS 133. AIG's consolidated financial statements were unaffected by ILFC's announced restatement because these derivative transactions were eliminated in consolidation.

Year-to-date Aircraft Finance Results

ILFC's operating income increased slightly in the first six months of 2006 compared to the same period of 2005. The increase was due to a 2005 loss of $49 million relating to the effect of derivatives not qualifying for hedge accounting treatment. In 2006, such derivative gains and losses are reported as part of the Other category. Higher lease rental revenues driven by a larger fleet size and higher utilization of ILFC's aircraft were more than offset by higher depreciation expense caused by a larger fleet, higher interest expense resulting from the rising cost of funds and additional outstanding borrowings, charges related to bankrupt airlines and the settlement of a tax dispute in Australia related to the restructuring of ownership of aircraft.

Quarterly Capital Markets Results

Capital Markets' operating income in the second quarter of 2006 decreased by $2.79 billion compared to the same period of 2005. Improved results, primarily from increased transaction flow in AIGFP's credit, commodity index and equity products, were more than offset by the loss resulting from the effect of derivatives not qualifying for hedge accounting treatment of $1.16 billion in the current quarter compared to a gain of $1.70 billion in the comparable period last year, a decrease of $2.86 billion. The majority of the net loss on AIGFP's derivatives recognized in the second quarter of 2006 was due to the effect of the weakening of the U.S. dollar primarily against the British Pound and Euro resulting in a decrease in the fair value of the foreign currency derivatives which are hedging AIGFP's available for sale securities. To a lesser extent, the increase in long term U.S. interest rates had a similar effect on AIGFP's interest rate derivatives hedging its assets and liabilities. The majority of the net gain on AIGFP's derivatives in the second quarter of 2005 was due to falling long term interest rates which increased the fair value of AIGFP's derivatives hedging its assets and liabilities. To a lesser extent, the strengthening of the U.S. dollar primarily against the Euro and British Pound increased the fair value of the foreign currency derivatives hedging available for sale securities.

Financial market conditions in the second quarter of 2006 continued to be characterized by higher levels of interest rates globally, unchanged credit spreads and equity valuations that were slightly lower. The decline in Capital Markets operating income for the second quarter of 2006 was principally due to losses on derivatives not qualifying for hedge accounting under FAS 133, which was partially offset by improved transaction flow in AIGFP's credit, commodity index and equity products.

The most significant component of Capital Markets operating expenses is compensation, which was approximately $129 million and $110 million in the second quarter of 2006 and 2005, respectively. The amount of compensation was not affected by gains and losses not qualifying for hedge accounting treatment under FAS 133.

Year-to-date Capital Markets Results

Capital Markets' operating income in the six month period ended June 30, 2006 decreased by $3.88 billion compared to the same period of 2005. Improved results, primarily from increased transaction flow in AIGFP's credit, commodity index and equity products, were more than offset by the loss resulting from the effect of derivatives not qualifying for hedge accounting treatment of $1.84 billion in the current period compared to a gain of $2.16 billion in the comparable period last year, a decrease of $4.0 billion. The majority of the net loss on AIGFP's derivatives recognized in the first six months of 2006 was due to the weakening in the U.S. dollar primarily against the British Pound and Euro resulting in a decrease in the fair value of the foreign currency derivatives hedging AIGFP's available for sale securities. To a lesser extent, the net loss was due to the rise in long-term U.S. interest rates which resulted in a decrease in the fair value of its derivatives hedging its assets and liabilities. The majority of the net gain on AIGFP's derivatives in the first six months of 2005 was due to falling long term U.S. interest rates which increased the fair value of AIGFP's derivatives hedging its assets and liabilities. To a lesser extent, the strengthening of the U.S. dollar primarily against the British Pound and Euro

increased the fair value of the foreign currency derivatives hedging available for sale securities.

Financial market conditions in the first six months of 2006 continued to be characterized by a general flattening of interest rate yield curves across fixed income markets globally, tightening of credit spreads and equity valuations that were slightly higher.

The compensation expense of Capital Markets was approximately $265 million and $221 million in the first six months of 2006 and 2005, respectively. The amount of compensation was not affected by gains and losses not qualifying for hedge accounting treatment under FAS 133.

As a result of AIG's early adoption of FAS 155, AIGFP elected to apply the fair value option to certain of its structured notes and other financial liabilities containing embedded derivatives outstanding as of January 1, 2006. The cumulative effect from the adoption of FAS 155 on these instruments at January 1, 2006 was a loss of approximately $29 million pre-tax. The application of the fair value option to these hybrid financial instruments did not have a significant effect on AIGFP's operating income for the second quarter or first six months of 2006.

Quarterly Consumer Finance Results

Consumer Finance's operating income decreased in the second quarter of 2006 compared to the same period of 2005 in both the domestic and foreign operations.

Domestically, the relatively low interest rate environment throughout 2005 contributed to a high level of mortgage refinancing activity. AGF's average net finance receivables increased 8 percent in the second quarter of 2006 when compared to the same period in 2005. However, net originations and purchases of finance receivables in AGF's centralized real estate business segment decreased in the second quarter of 2006 compared to the same period in 2005 primarily caused by a less robust U.S. housing market. The increase in AGF's revenues that principally resulted from portfolio growth was offset by higher interest expense and depressed whole loan sale prices resulting from a flattened yield curve. Both short-term and long-term market interest rates continued to increase significantly over the past year. AGF's short-term and long-term borrowing costs were 5.03 percent and 5.01 percent in the second quarter of 2006, respectively, compared to 3.46 percent and 4.31 percent, respectively, in the same period in 2005. Despite high energy costs, the U.S. economy continued to expand during the second quarter of 2006, improving consumer credit quality as compared to the second quarter of 2005. AGF's charge-off ratio improved 23 basis points in the second quarter of 2006 when compared to the same period in 2005.

Revenues from the foreign consumer finance operations increased by approximately 15 percent in the second quarter of 2006 compared to the same period in 2005. Portfolio growth was the primary driver behind higher revenues in 2006. These revenues were offset by increasing cost of funds and higher expenses in connection with branch expansions and new product promotions, resulting in a lower operating income for the second quarter of 2006 compared to the same period in 2005.

Year-to-date Consumer Finance Results

Consumer Finance's operating income decreased 19 percent in the first six months of 2006 compared to the same period of 2005 in both the domestic and foreign operations.

Domestically, the relatively low interest rate environment throughout 2005 contributed to a high level of mortgage refinancing activity. AGF's average net finance receivables increased 11 percent in the first six months of 2006 when compared to the same period in 2005. However, net originations and purchases of finance receivables in AGF's centralized real estate business segment decreased in the first six months of 2006 compared to the same period in 2005 primarily caused by a less robust U.S. housing market. The increase in AGF's revenues that principally resulted from portfolio growth was offset by higher interest expense and depressed whole loan sale prices resulting from a flattened yield curve. AGF's short-term and long-term borrowing costs were 4.85 percent and 4.89 percent in the first six months of 2006, respectively, compared to 3.25 percent and 4.31 percent, respectively, in the same period in 2005. Despite high energy costs, the U.S. economy continued to expand during the first six months of 2006, improving consumer credit quality. AGF's charge-off ratio improved 30 basis points in the first six months of 2006 when compared to the same period in 2005. AGF's delinquency ratio at June 30, 2006 improved 10 basis points when compared to June 30, 2005. At June 30, 2006, AGF's allowance ratio was 2.07 percent compared to 2.04 percent at June 30, 2005.

Revenues from the foreign consumer finance operations increased by approximately 20 percent in the first six months of 2006 compared to the same period in 2005. Portfolio growth was the primary driver behind higher revenues. Higher revenues were offset by increases in the allowance for losses related to industry-wide credit deterioration in the Taiwan credit card market, increasing cost of funds and higher expenses in connection with branch expansions and new product promotions, resulting in a lower operating income for the first six months of 2006 compared to the same period in 2005.

Financial Services Invested Assets

The following table is a summary of the composition of AIG's Financial Services invested assets at June 30, 2006 and December 31, 2005. (See also the discussions under "Operating Review: Financial Services Operations," "Capital Resources" and "Derivatives" herein.)

	2006		2005	
(dollars in millions)	**Invested Assets**	**Percent of Total**	Invested Assets	Percent of Total
Fixed maturities:				
Bonds available for sale, at market value	**$ 1,298**	**0.9%**	$ 1,307	0.9%
Equity securities:				
Preferred stocks available for sale, at market value	**6**	**–**	10	–
Mortgage loans on real estate, net of allowance	**70**	**–**	71	–
Policy loans	**2**	**–**	2	–
Collateral and guaranteed loans, net of allowance	**2,002**	**1.3**	1,719	1.2
Financial services assets:				
Flight equipment primarily under operating leases, net of accumulated depreciation	**39,307**	**25.8**	36,245	24.1
Securities available for sale, at market value	**38,678**	**25.4**	37,511	24.9
Trading securities, at market value	**5,165**	**3.4**	6,499	4.3
Spot commodities	**797**	**0.5**	92	0.1
Unrealized gain on swaps, options and forward transactions	**18,901**	**12.4**	18,695	12.4
Trading assets	**1,345**	**0.9**	1,204	0.8
Securities purchased under agreements to resell, at contract value	**14,085**	**9.2**	14,519	9.7
Finance receivables, net of allowance	**27,515**	**18.1**	27,995	18.6
Securities lending collateral, at market value	**64**	**–**	–	–
Other invested assets	**1,869**	**1.2**	2,751	1.9
Short-term investments, at cost	**1,055**	**0.7**	1,382	0.9
Cash	**284**	**0.2**	331	0.2
Investment income due and accrued	**19**	**–**	18	–
Real estate, net of accumulated depreciation	**24**	**–**	24	–
Total	**$152,486**	**100.0%**	$150,375	100.0%

As previously discussed, the cash used for the purchase of flight equipment is derived primarily from the proceeds of ILFC's debt financings. The primary sources for the repayment of this debt and the interest expense thereon are the cash flow from operations, proceeds from the sale of flight equipment and the rollover and refinancing of the prior debt. During the first six months of 2006, ILFC acquired flight equipment costing $4.17 billion. (See also the discussion under "Operating Review: Financial Services Operations" and "Capital Resources" herein.)

At June 30, 2006, ILFC had committed to purchase 266 new aircraft deliverable from 2006 through 2015 at an estimated aggregate purchase price of $18.9 billion and had options to purchase 13 new aircraft at an estimated aggregate purchase price of $1.4 billion. As of June 30, 2006, ILFC has entered into leases for all of the new aircraft to be delivered in 2006. ILFC will be required to find customers for any aircraft currently on order and any aircraft to be ordered, and it must arrange financing for portions of the purchase price of such equipment. ILFC has been successful to date both in placing its new aircraft on lease or under sales contract and obtaining adequate financing, but there can be no assurance that such success will continue in future environments.

AIG's Consumer Finance operations provide a wide variety of consumer finance products, including real estate loans, credit card loans, non-real estate loans, retail sales finance and credit-related insurance to customers both domestically and overseas, particularly in emerging markets. These products are funded through a combination of deposits and various borrowings including commercial paper and medium term notes. AIG's Consumer Finance operations are exposed to credit risk and risk of loss resulting from adverse fluctuations in interest rates. Over half of the finance receivables are real estate loans which are substantially collateralized by the related properties.

With respect to credit losses, the allowance for losses is maintained at a level considered adequate to absorb anticipated credit losses existing in that portfolio.

Capital Markets derivative transactions are carried at market value or at estimated fair value when market prices are not readily available. AIGFP reduces its economic risk exposure through similarly valued offsetting transactions including swaps, trading securities, options, forwards and futures. The estimated fair values of these transactions represent assessments of the present value of expected future cash flows. These transactions are exposed to liquidity risk if AIGFP were required to sell or close out the transactions

prior to maturity. AIG believes that the effect of any such event would not be significant to AIG's financial condition or its overall liquidity. (See also the discussion under "Operating Review: Financial Services Operations" and "Derivatives" herein.)

AIGFP uses the proceeds from the issuance of notes and bonds and GIAs to invest in a diversified portfolio of securities, including securities available for sale, at market, and derivative transactions. The funds may also be invested in securities purchased under agreements to resell. The proceeds from the disposal of the aforementioned securities available for sale and securities purchased under agreements to resell are used to fund the maturing GIAs or other AIGFP financings, or invest in new assets. (See also the discussion under "Capital Resources" herein.)

Securities available for sale is predominantly a diversified portfolio of high grade fixed income securities, where the individual securities have varying degrees of credit risk. At June 30, 2006, the average credit rating of this portfolio was in the AA category or the equivalent thereto as determined through rating agencies or internal review. AIGFP has also entered into credit derivative transactions to economically hedge its credit risk associated with $130 million of these securities. Securities deemed below investment grade at June 30, 2006 amounted to approximately $153 million in fair value representing 0.4 percent of the total AIGFP securities available for sale. There have been no significant downgrades through June 30, 2006. If its securities available for sale portfolio were to suffer significant default and the collateral held declined significantly in value with no replacement or the credit default swap counterparty failed to perform, AIGFP could have a liquidity strain. AIG guarantees AIGFP's payment obligations, including its debt obligations.

AIGFP's risk management objective is to minimize interest rate, currency, commodity and equity risks associated with its securities available for sale. That is, when AIGFP purchases a security for its securities available for sale investment portfolio, it simultaneously enters into an offsetting internal hedge such that the payment terms of the hedging transaction offset the payment terms of the investment security, which achieves the economic result of converting the return on the underlying security to U.S. dollar LIBOR plus or minus a spread based on the underlying profit on each security on the initial trade date. The market risk associated with such internal hedges is managed on a portfolio basis, with third-party hedging transactions executed as necessary. As hedge accounting treatment is not achieved in accordance with FAS 133, the unrealized gains and losses on the derivative transactions with unaffiliated third parties are reflected in operating income, whereas the unrealized gains and losses on the underlying securities resulting from changes in interest rates, currency rates, commodity and equity prices, are recorded in accumulated other comprehensive income. When a security is sold, the realized gain or loss with respect to this security is then recorded in operating income.

Securities purchased under agreements to resell are treated as collateralized financing transactions. AIGFP takes possession of or obtains a security interest in securities purchased under agreements to resell.

AIGFP owns inventories in certain commodities in which it trades, and may reduce the exposure to market risk through the use of swaps, forwards, futures and option contracts. Physical commodities held in AIGFP's wholly-owned broker dealer subsidiary are recorded at market value. All other commodities are recorded at the lower of cost or market.

Trading securities, at market value, and securities and spot commodities sold but not yet purchased, at market value are marked to market daily with the unrealized gain or loss being recognized in income at that time. These trading securities are purchased and sold as necessary to meet the risk management objectives of Capital Markets operations.

The gross unrealized gains and gross unrealized losses of Capital Markets operations included in the financial services assets and liabilities at June 30, 2006 were as follows:

(in millions)	Gross Unrealized Gains	Gross Unrealized Losses
Securities available for sale, at market value	$ 490	$ 198
Unrealized gain/loss on swaps, options and forward transactions*	18,901	11,956

** These amounts are also presented as the respective balance sheet amounts.*

The senior management of AIG defines the policies and establishes general operating parameters for Capital Markets operations. AIG's senior management has established various oversight committees to monitor on an ongoing basis the various financial market, operational and credit risk attendant to the Capital Markets operations. The senior management of AIGFP reports the results of its operations to and reviews future strategies with AIG's senior management.

AIG actively manages the exposures to limit potential losses, while maximizing the rewards afforded by these business opportunities. In doing so, AIG must continually manage a variety of exposures including credit, market, liquidity, operational and legal risks.

Asset Management Operations

AIG's Asset Management operations comprise a wide variety of investment-related services and investment products including institutional and retail asset management, broker dealer services and spread-based investment business from the sale of guaranteed investment contracts, also known as funding agreements (GICs). Such services and products are offered to individuals and institutions both domestically and overseas.

Asset Management Results

Asset Management revenues and operating income for the three and six-month periods ended June 30, 2006 and 2005 were as follows:

(in millions)	Three Months Ended June 30, 2006	Three Months Ended June 30, 2005	Six Months Ended June 30, 2006	Six Months Ended June 30, 2005
Revenues:				
Guaranteed investment contracts	**$ 850**	$ 903	**$1,672**	$1,799
Institutional Asset Management	**619**	178	**898**	497
Brokerage Services and Mutual Funds	**73**	62	**146**	125
Other	**79**	76	**144**	175
Total	**$1,621**	$1,219	**$2,860**	$2,596
Operating income:				
Guaranteed investment contracts[(a)]	**$ 242**	$ 326	**$ 460**	$ 645
Institutional Asset Management[(b)(c)]	**473**	108	**632**	269
Brokerage Services and Mutual Funds	**21**	17	**44**	30
Other	**75**	73	**136**	170
Total	**$ 811**	$ 524	**$1,272**	$1,114

(a) Includes the effect of hedging activities that do not qualify for hedge accounting treatment under FAS 133, including the related foreign exchange gains and losses. For the three and six-month periods ended June 30, 2005, the effect was $47 million and $109 million, respectively, in operating income. During 2006, these derivative gains and losses are reported as part of the Other category, and not reported in Asset Management operating income.

(b) Includes the full results of certain AIG managed private equity and real estate funds that are consolidated pursuant to FIN 46(R), "Consolidation of Variable Interest Entities". Also includes $183 million and $37 million for the three-month periods ended June 30, 2006 and 2005, respectively, and $210 million and $112 million for the six-month periods ended June 30, 2006 and 2005, respectively, of third-party limited partner earnings offset in minority interest expense which is not a component of operating income.

(c) Includes the full results of certain AIG managed partnerships that are consolidated effective January 1, 2006 pursuant to EITF 04-5, "Determining Whether a General Partner, or the General Partners as a Group, Controls a Limited Partnership or Similar Entity When the Limited Partners Have Certain Rights". For the three and six-month periods ended June 30, 2006, operating income includes $87 million and $156 million, respectively, of third-party limited partner earnings offset in minority interest expense which is not a component of operating income.

Quarterly Asset Management Results

Asset management operating income increased 55 percent in the second quarter of 2006 compared to the same period of 2005 on revenues that grew 33 percent as increases in Institutional Asset Management operating income were partially offset by lower income on the GIC portfolio. Continued growth in fees driven by higher levels of assets under management were augmented by increases in realized gains on sales of real estate investments, as well as performance fees earned on various private equity and structured fixed income investments. The MIP began to show positive operating income during the second quarter of 2006. The revenues and operating income with respect to Asset Management are largely affected by the general conditions in the equity and credit markets. Realized gains and performance fees are contingent upon various fund closings, maturity levels and market conditions, and by their nature, are not predictable. Therefore, the effect on Asset Management's earnings may vary from period to period.

The GIC portfolio, historically AIG's principal spread-based investment activity, continues to run off as anticipated. The MIP has replaced the GIC program as AIG's principal spread-based investment activity. A significant portion of the remaining GIC portfolio consists of floating rate obligations. AIG has entered into hedges to manage against increases in short-term interest rates. AIG continues to believe these hedges are economically effective even though they do not qualify for hedge accounting under FAS 133. As a result, continued increases in short-term interest rates will negatively affect operating income in the segment. Realized capital gains from the hedges offset the negative trend in GIC related operating income. GIC revenues include income from Sun America partnerships supporting the GIC line of business and are significantly affected by performance in the equity markets. Thus, revenues, operating income and cash flow attributable to GICs will vary among reporting periods.

The decrease in GIC operating income in the second quarter of 2006 compared to the same period of 2005 also reflects spread compression in the existing GIC portfolio. Spread compression has occurred as the base portfolio yield declined primarily due to an increase in the cost of funds in the short-term floating rate portion of the GIC portfolio, only partially offset by increased investment income from the floating rate assets backing the portfolio.

The MIP, a spread-based investment activity providing for the issuance of AIG debt securities, was initially launched in the Euromarkets in September 2005 through AIG's $10 billion Euro medium term note program. Through June 30, 2006, AIG has issued the equivalent of $947.1 million under the Euro medium term note program for the MIP, and in addition, in July 2006, AIG issued the equivalent of $635.4 million under the Euro medium term note program for the MIP. Also, in June 2006, AIG issued $750 million principal amount of notes in a Rule 144A offering for the MIP. AIG also plans to issue registered debt securities for the MIP in the domestic market under its universal shelf registration statement.

Year-to-date Asset Management Results

Asset Management operating income increased 14 percent in the first six months of 2006 compared to the same period of 2005 on revenues that increased 10 percent. Continued growth in fees driven by increasing levels of assets under management were augmented by increases in realized

gains on sales of real estate investments as well as performance fees earned on various private equity and structured fixed income investments. The decrease in GIC operating income in the first six months of 2006 compared to the same period of 2005 reflects the continued run-off of GIC balances combined with spread compression in the remaining GIC portfolio.

At June 30, 2006 and 2005, AIG's third party assets under management, including both retail mutual funds and institutional accounts, exceeded $66 billion and $61 billion and the aggregate GIC reserve was $48.5 billion and $51.6 billion, respectively.

Other Operations

The operating income (loss) for Other operations for the three and six-month periods ended June 30, 2006 and 2005 was as follows:

Other *(in millions)*	Three Months Ended June 30, **2006**	2005	Six Months Ended June 30, **2006**	2005
Operating Income (Loss):				
Equity earnings in unconsolidated subsidiaries	**$ 111**	$ 36	**$ 130**	$ 96
Compensation expense – SICO Plans	**(14)**	(60)	**(90)**	(67)
Compensation expense – C.V. Starr tender offer	**–**	–	**(54)**	–
Interest expense	**(223)**	(127)	**(406)**	(251)
Unallocated corporate expenses	**(71)**	(108)	**(261)**	(195)
Realized capital gains (losses)	**24**	(16)	**134**	379
Other miscellaneous, net	**(14)**	29	**(35)**	(17)
Total Other	**$(187)**	$(246)	**$(582)**	$ (55)

Other operating loss amounted to $187 million and $246 million in the three-month periods ended June 30, 2006 and 2005, respectively, as interest expense increased, primarily reflecting increased borrowings by the parent holding company. This decline was partially offset by increased equity earnings in unconsolidated subsidiaries. The second quarter of 2006 also reflects a decrease in unallocated corporate expenses, primarily relating to a reduction in unallocated stock compensation expense and pension expense of $39 million, and a decrease in compensation expense with respect to the SICO Plans.

Other operating loss amounted to $582 million and $55 million in the six-month periods ended June 30, 2006 and 2005, respectively, as interest expense increased, primarily reflecting increased borrowings by the parent holding company. The first six months of 2006 also reflects an increase in unallocated corporate expenses, reflecting expenses of $29 million in the first six months of 2006 relating to certain executive departures (of which approximately $18 million related to departures in 2005), and an overall increase in corporate operating expenses primarily resulting from on-going efforts to remediate material weaknesses in internal controls. Also reflected in operating loss in the first six months of 2006 is an out of period adjustment totaling $61 million with respect to the SICO Plans and a one-time charge related to the Starr tender offer of $54 million, both of which were recorded in the first quarter of 2006. See also Note 4 of Notes to the Consolidated Financial Statements for further discussion. These declines were partially offset by increased equity earnings in unconsolidated subsidiaries. Realized capital gains declined, primarily reflecting lower levels of realized gains for the parent holding company.

Capital Resources

At June 30, 2006, AIG had total consolidated shareholders' equity of $87.71 billion and total consolidated borrowings of $126.1 billion. At that date, $110.8 billion of such borrowings were either not guaranteed by AIG or were AIGFP's matched borrowings under obligations of GIAs, liabilities connected to trust preferred stock, or matched notes and bonds payable.

Borrowings

At June 30, 2006, AIG's net borrowings were $15.32 billion after reflecting amounts that were matched borrowings under AIGFP's obligations of GIAs, matched notes and bonds payable, amounts not guaranteed by AIG and liabilities connected to trust preferred stock. The following table summarizes borrowings outstanding at June 30, 2006 and December 31, 2005:

(in millions)	**2006**	2005
AIG's net borrowings	**$ 15,323**	$ 10,425
Liabilities connected to trust preferred stock	**1,399**	1,391
AIG Matched Investment Program		
Matched notes and bonds payable	**1,716**	–
AIGFP		
GIAs	**21,571**	20,811
Matched notes and bonds payable	**28,054**	24,950
Borrowings not guaranteed by AIG	**58,034**	52,272
Total	**$126,097**	$ 109,849

Borrowings issued or guaranteed by AIG and those borrowings not guaranteed by AIG at June 30, 2006 and December 31, 2005 were as follows:

(in millions)	**2006**	2005
AIG borrowings:		
Notes and bonds payable	**$ 7,474**	$ 4,607
Loans and mortgages payable	**2,028**	814
AIG Matched Investment Program		
Matched notes and bonds payable	**1,716**	–
Total	**11,218**	5,421
Borrowings guaranteed by AIG:		
AIGFP		
GIAs	**21,571**	20,811
Notes and bonds payable	**23,196**	26,463
Hybrid financial instrument liabilities	**6,652**	—
Total	**51,419**	47,274
AIG Funding, Inc. commercial paper	**3,230**	2,694
AGC Notes and bonds payable	**797**	797
Liabilities connected to trust preferred stock	**1,399**	1,391
Total borrowings issued or guaranteed by AIG	**68,063**	57,577
Borrowings not guaranteed by AIG:		
ILFC		
Commercial paper	**3,950**	2,615
Notes and bonds payable*	**25,490**	23,715
Total	**29,440**	26,330
AGF		
Commercial paper	**4,670**	3,423
Notes and bonds payable	**18,778**	18,719
Total	**23,448**	22,142
Commercial paper:		
AIG Credit Card Company (Taiwan)	**334**	476
AIG Finance (Taiwan) Limited	**3**	–
Total	**337**	476
Loans and mortgages payable:		
AIGCFG	**1,011**	864
AIG Finance (Hong Kong) Limited	**204**	183
Total	**1,215**	1,047
Other Subsidiaries	**960**	927
Variable Interest Entity debt:		
A.I. Credit	**876**	–
AIG Global Investment Group	**54**	140
AIG Global Real Estate Investment	**1,518**	977
AIG SunAmerica	**186**	233
Total	**2,634**	1,350
Total borrowings not guaranteed by AIG	**58,034**	52,272
Total Debt	**$126,097**	$109,849

** Includes borrowings under Export Credit Facility of $2.8 billion and $2.6 billion, at June 30, 2006 and December 31, 2005, respectively.*

AIG intends to continue its customary practice of issuing debt securities from time to time to meet its financing needs and those of certain of its subsidiaries for general corporate purposes, as well as for a matched investment program. In July 2006, AIG filed and had declared effective a post-effective amendment to its universal shelf registration statement to sell up to $25.1 billion of debt securities, preferred and common stock and other securities.

On April 20, 2006, AIG sold $1.0 billion principal amount of senior notes in a Rule 144A/Regulation S offering bearing interest at a rate of 6.25 percent per annum and maturing in 2036, and on September 30, 2005, AIG sold $1.5 billion principal amount of senior notes in a Rule 144A/Regulation S offering, $500 million of which bear interest at a rate of 4.7 percent per annum and mature in 2010 and $1.0 billion of which bear interest at a rate of 5.05 percent per annum and mature in 2015. The proceeds from these offerings were used by AIG for general corporate purposes. In July 2006, AIG commenced exchange offers for these notes pursuant to which AIG will issue in exchange substantially identical notes that are registered under the Securities Act.

On June 16, 2006, AIG sold $750 million principal amount of senior, floating rate notes in a Rule 144A offering that matures in 2009. The proceeds of this offering were used to fund the MIP.

AIG has a Euro medium term note program under which an aggregate nominal amount of up to $10.0 billion of notes may be outstanding at any one time. The program provides that additional notes may be issued to replace matured or redeemed notes. AIG completed its first offerings under the program in April 2006, and, as of June 30, 2006, the equivalent of $2.8 billion principal amount of notes were outstanding under the program, of which the proceeds from $1.0 billion of notes were used to fund the matched investment program. The aggregate amount outstanding includes $85 million resulting from foreign exchange translation into U.S. dollars, of which $67 million relates to notes issued by AIG for general corporate purposes and $18 million relates to notes issued to fund the MIP. AIG has hedged the currency exposure arising from foreign currency denominated notes by economically hedging that exposure, although such hedges do not qualify for hedge accounting treatment under FAS 133. In addition, in July 2006, AIG sold the equivalent of $635.4 million under the program, the proceeds of which were used to fund the MIP.

In March 2006, AIG borrowed a total of $1.3 billion on an unsecured basis pursuant to loan agreements with third-party banks, $500 million of which matures in February 2007 but can be extended by AIG for an additional seven-month period and $800 million of which matures in March 2007. In September 2005, AIG borrowed a total of $600 million on an unsecured basis pursuant to loan agreements with third-party banks, $500 million of which matures in August 2006 but can be extended by AIG for an additional seven-month period and $100 million of which matures in September 2006.

AIGFP uses the proceeds from the issuance of notes and bonds and GIA borrowings to invest in a diversified portfolio

of securities and derivative transactions. The borrowings may also be temporarily invested in securities purchased under agreements to resell. AIG guarantees the obligations of AIGFP under AIGFP's structured notes and bonds and GIA borrowings. Certain of AIGFP's notes contain embedded derivatives that are required to be accounted for separately under FAS 133. Upon AIG's early adoption of FAS 155, AIGFP has elected the fair value option for these instruments. Those notes that are accounted for using the fair value option are reported separately under hybrid financial instrument liabilities. (See also the discussions under "Operating Review: Financial Services Operations," "Liquidity" and "Derivatives" herein.)

On June 16, 2006, AIGFP sold an aggregate of $2.0 billion principal amount of senior, floating rate notes in Rule 144A offerings, of which $1.0 billion matures in 2007 and $1.0 billion matures in 2008. AIGFP has a Euro Medium Term Note Program under which an aggregate nominal amount of up to $10.0 billion of notes may be outstanding at any one time. The Program provides that additional notes may be issued to replace matured or redeemed notes. As of June 30, 2006, $10.09 billion of notes had been issued under the program, $4.66 billion of which were outstanding including $310 million resulting from foreign exchange translation into U.S. dollars. Notes issued under this program are included in Notes and Bonds Payable in the preceding table of borrowings.

AIG Funding, Inc. (AIG Funding), through the issuance of commercial paper, helps fulfill the short-term cash requirements of AIG and its subsidiaries. AIG Funding intends to continue to meet AIG's funding requirements through the issuance of commercial paper guaranteed by AIG. The issuance of AIG Funding's commercial paper is subject to the approval of AIG's Board of Directors.

AIG and AIG Funding are parties to unsecured syndicated revolving credit facilities, which as of June 30, 2006, aggregated to $2.75 billion, consisting of $1.375 billion in a 364-day revolving credit facility and $1.375 billion in a five-year revolving credit facility. In July 2006, these credit facilities were renewed and increased to an aggregate of $3.25 billion, consisting of $1.625 billion in the 364-day facility that expires in July of 2007 and $1.625 billion in the five-year facility that expires in July of 2011. The 364-day facility allows for the conversion by AIG of any outstanding loans at expiration into one-year term loans. The facilities can be used for general corporate purposes and also to provide backup for AIG's commercial paper programs administered by AIG Funding. AIG expects to replace or extend these credit facilities on or prior to their expiration. There are currently no borrowings outstanding under these facilities, nor were any borrowings outstanding as of June 30, 2006.

In November 2005, AIG and AIG Funding entered into a 364-day revolving credit facility for an aggregate amount of $3 billion, which can be drawn in the form of loans or letters of credit. The credit facility expires in November 2006 but allows for the issuance of letters of credit with terms of up to ten years and provides for the conversion by AIG of any outstanding loans at expiration into one-year term loans. The facility can be used for general corporate purposes, including providing backup for AIG's commercial paper programs administered by AIG Funding and obtaining letters of credit to secure obligations under insurance and reinsurance transactions. There are currently no loans outstanding under the facility, nor were any loans outstanding as of June 30, 2006. As of such dates, $669 million was available to be drawn under the facility, with the remainder having been drawn in the form of letters of credit.

AIG is also a party to an unsecured 364-day inter-company revolving credit facility provided by certain of its subsidiaries aggregating $2 billion that expires in October of 2006. The facility allows for the conversion of any outstanding loans at expiration into one-year term loans. The facility can be used for general corporate purposes and also to provide backup for AIG's commercial paper programs. AIG expects to replace or extend this credit facility on or prior to its expiration. There are currently no borrowings outstanding under the inter-company facility, nor were any borrowings outstanding as of June 30, 2006.

ILFC fulfills its short term cash requirements through the issuance of commercial paper. The issuance of commercial paper is subject to the approval of ILFC's Board of Directors and is not guaranteed by AIG. ILFC is a party to unsecured syndicated revolving credit facilities aggregating $6.0 billion at June 30, 2006. The facilities can be used for general corporate purposes and also to provide backup for ILFC's commercial paper program. They consist of $2.0 billion in a 364-day revolving credit facility that expires in October 2006, with a one-year term out option, $2.0 billion in a five-year revolving credit facility that expires in October 2009 and $2.0 billion in a five-year revolving credit facility that expires in October 2010. ILFC expects to replace or extend these credit facilities on or prior to their expiration. There are currently no borrowings under these facilities, nor were any borrowings outstanding as of June 30, 2006.

At June 30, 2006, ILFC had increased the aggregate principal amount outstanding of its medium term and long-term notes. The foreign exchange adjustment for the foreign currency denominated debt was $570 million at June 30, 2006 and $197 million at December 31, 2005. ILFC had $13.13 billion of debt securities registered for public sale at June 30, 2006. As of June 30, 2006, $11.58 billion of debt securities were issued. In addition, ILFC has a Euro Medium Term Note Program for $7.0 billion, under which $4.28 billion in notes were sold through June 30, 2006. ILFC has substantially eliminated the currency exposure arising from foreign currency denominated notes by economically hedging the portion of the note exposure not already offset by Euro denominated operating lease payments, although such hedges

do not qualify for hedge accounting treatment under FAS 133. Notes issued under the Euro Medium Term Note program are included in Notes and Bonds Payable in the preceding table of borrowings.

ILFC had a $4.3 billion Export Credit Facility for use in connection with the purchase of approximately 75 aircraft delivered through 2001. This facility was guaranteed by various European Export Credit Agencies. The interest rate varies from 5.75 percent to 5.90 percent on these amortizing ten-year borrowings depending on the delivery date of the aircraft. At June 30, 2006, ILFC had $1.1 billion outstanding under this facility. The debt is collateralized by a pledge of the shares of a subsidiary of ILFC, which holds title to the aircraft financed under the facility.

In May 2004, ILFC entered into a similarly structured Export Credit Facility for up to a maximum of $2.64 billion for Airbus aircraft to be delivered through May 31, 2005. The facility has since been extended to include aircraft to be delivered through May 31, 2006. The facility was subsequently increased to $3.64 billion and extended to include aircraft to be delivered through May 31, 2007. The facility becomes available as the various European Export Credit Agencies provide their guarantees for aircraft based on a six-month forward-looking calendar, and the interest rate is determined through a bid process. At June 30, 2006, ILFC had $1.7 billion outstanding under this facility. Borrowings with respect to these facilities are included in Notes and Bonds Payable in the preceding table of borrowings.

In August 2004, ILFC received a commitment for an Ex-Im Bank comprehensive guarantee in the amount of $1.68 billion to support the financing of up to 30 new Boeing aircraft. The initial delivery period from September 1, 2004 through August 31, 2005 has been extended by ILFC to August 31, 2006. ILFC did not have any borrowings outstanding under this facility at June 30, 2006. From time to time, ILFC enters into various bank financings. As of June 30, 2006 the total funded amount was $1.5 billion. The financings mature through 2011. One tranche of one of the loans totaling $410 million was funded in Japanese yen and swapped to U.S. dollars.

In December of 2005, ILFC entered into two tranches of junior subordinated debentures totaling $1.0 billion. Both mature on December 21, 2065, but each tranche has a different call option. The $600 million tranche has a call date of December 21, 2010 and the $400 million tranche has a call date of December 21, 2015. The debenture with the 2010 call date has a fixed interest rate of 5.90 percent for the first five years. The debenture with the 2015 call date has a fixed interest rate of 6.25 percent for the first ten years. Both tranches have interest rate adjustments if the call option is not exercised. If the call option is not exercised, the new interest rate will be a floating quarterly reset rate based on the initial credit spread plus the highest of (i) 3 month LIBOR, (ii) 10-year constant maturity treasury and (iii) 30-year constant maturity treasury.

The proceeds of ILFC's debt financing are primarily used to purchase flight equipment, including progress payments during the construction phase. The primary sources for the repayment of this debt and the interest expense thereon are the cash flow from operations, proceeds from the sale of flight equipment and the rollover and refinancing of the prior debt. AIG does not guarantee the debt obligations of ILFC. (See also the discussions under "Operating Review: Financial Services Operations" and "Liquidity" herein.)

AGF fulfills its short term cash requirements through the issuance of commercial paper. The issuance of commercial paper is subject to the approval of AGF's Board of Directors and is not guaranteed by AIG. AGF is a party to unsecured syndicated revolving committed credit facilities aggregating $4.25 billion, including a $2.125 billion 364-day revolving credit facility that expires in July of 2007 and a $2.125 billion five-year revolving credit facility that expires in July of 2010. The 364-day facility allows for the conversion by AGF of any outstanding loans at expiration into a one-year term loan. The facilities can be used for general corporate purposes and also to provide backup for AGF's commercial paper programs. AGF expects to replace or extend these credit facilities on or prior to their expiration. There are currently no borrowings under these AGF facilities, nor were any borrowings outstanding as of June 30, 2006.

During 2005, AGF issued $5.44 billion of fixed rate and variable rate medium term notes ranging in maturities from two to ten years. As of June 30, 2006, notes aggregating $17.23 billion were outstanding with maturity dates ranging from 2006 to 2015 at interest rates ranging from 1.90 percent to 7.50 percent. To the extent deemed appropriate, AGF may enter into swap transactions to manage its effective borrowing with respect to these notes.

AGF's other funding sources include private placement debt, retail note issuances, securitizations of finance receivables that AGF accounts for as on-balance-sheet secured financings and bank financings. In addition, AGF has become an established issuer of long-term debt in the international capital markets.

In addition to debt refinancing activities, proceeds from the collection of finance receivables will be used to pay the principal and interest with respect to AGF's debt. AIG does not guarantee any of the debt obligations of AGF. See also the discussion under "Operating Review — Financial Services Operations" and "Liquidity" herein.

AIG Credit Card Company (Taiwan) and AIG Finance (Taiwan) Limited, both consumer finance subsidiaries in Taiwan, have issued commercial paper for the funding of their own operations. AIG did not guarantee the commercial paper issued by either of these subsidiaries.

Contractual Obligations and Other Commercial Commitments

The maturity schedule of AIG's contractual obligations at June 30, 2006 was as follows:
(in millions)

		Payments due by Period			
	Total Payments	Less Than One Year	One Through Three Years	Four Through Five Years	After Five Years
Borrowings[(a)]	$111,276	$31,851	$ 24,258	$20,278	$ 34,889
Loss reserves[(b)]	78,966	21,716	24,084	11,450	21,716
Insurance and investment contract liabilities[(c)]	627,747	22,049	49,972	46,068	509,658
Aircraft purchase commitments	18,876	1,601	10,143	4,148	2,984
Total	$836,865	$77,217	$108,457	$81,944	$569,247

(a) Excludes commercial paper and obligations included as debt pursuant to FIN 46(R) and includes hybrid financial instrument liabilities recorded at fair value.

(b) Represents future loss and loss adjustment expense payments estimated based on historical loss development payment patterns.

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

The maturity schedule of AIG's other commercial commitments by segment at June 30, 2006 was as follows:
(in millions)

		Amount of Commitment Expiration			
	Total Amounts Committed	Less Than One Year	One Through Three Years	Four Through Five Years	After Five Years
Letters of credit:					
Life Insurance & Retirement Services	$ 185	$ 37	$ 24	$ –	$ 124
DBG	184	184	–	–	–
Standby letters of credit:					
Capital Markets	1,750	511	75	39	1,125
Guarantees:					
Life Insurance & Retirement Services[(a)]	3,537	109	398	–	3,030
Aircraft Finance	127	2	45	–	80
Asset Management	285	56	59	–	170
Parent Company[(b)]	533	421	1	111	–
Other commercial commitments[(c)]:					
Capital Markets[(d)]	15,007	4,528	2,460	1,764	6,255
Aircraft Finance[(e)]	1,752	–	–	868	884
Life Insurance & Retirement Services[(f)]	4,469	1,187	1,394	993	895
Asset Management	632	412	148	57	15
Life Settlement	253	–	253	–	–
DBG[(g)]	913	–	–	–	913
Parent Company	194	53	108	33	–
Total	$ 29,821	$ 7,500	$ 4,965	$ 3,865	$13,491

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

(b) Represents reimbursement obligations under letters of credit issued by commercial banks.

(c) Excludes commitments with respect to pension plans. The annual pension contribution for 2006 is expected to be approximately $70 million for U.S. and non-U.S. Plans.

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

(e) Primarily in connection with options to acquire aircraft.

(f) Primarily AIG SunAmerica commitments to invest in partnerships.

(g) Primarily commitments to invest in limited partnerships.

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

AIG believes that any of its or its subsidiaries' contractual obligations that are subject to "ratings triggers" or financial covenants relating to "ratings triggers" would not have a material adverse effect on its financial condition or liquidity.

As a result of the downgrades of AIG's long-term senior debt ratings, AIG was required to post approximately $1.16 billion of collateral with counterparties to municipal guaranteed investment agreements and financial derivatives transactions. In the event of a further downgrade, AIG will be required to post additional collateral. It is estimated that, as of the close of business on July 31, 2006 based on AIG's outstanding municipal guaranteed investment agreements and financial derivatives transactions as of such date, a further downgrade of AIG's long-term senior debt ratings to 'Aa3' by Moody's or 'AA–' by S&P would permit counterparties to call for approximately $873 million of additional collateral. Further, additional downgrades could result in requirements for substantial additional collateral, which could have a material effect on how AIG manages its liquidity. The actual amount of additional collateral that AIG would be required to post to counterparties in the event of such downgrades depends on market conditions, the market value of the outstanding affected transactions and other factors prevailing at the time of the downgrade. Any additional obligations to post collateral will increase the demand on AIG's liquidity.

Shareholders' Equity

AIG's consolidated shareholders' equity increased $1.39 billion during the first six months of 2006. Retained earnings increased $5.86 billion, resulting from net income of $6.39 billion and $308 million reflecting the cumulative effect of accounting changes less dividends of $831 million. Unrealized appreciation of investments, net of taxes, decreased $5.49 billion and the cumulative translation adjustment loss, net of taxes, decreased $721 million. During the first six months of 2006 there was a gain of $5 million, net of taxes, relating to derivative contracts designated as cash flow hedging instruments. (See also the discussion under "Operating Review" and "Liquidity" herein and the Consolidated Statement of Comprehensive Income.)

AIG has in the past reinvested most of its unrestricted earnings in its operations and believes such continued reinvestment in the future will be adequate to meet any foreseeable capital needs. However, AIG may choose from time to time to raise additional funds through the issuance of additional securities.

Stock Purchase

During 2006, AIG did not purchase any shares of its common stock under its existing share repurchase authorization. AIG from time to time may buy shares of its common stock in the open market for general corporate purposes, including to satisfy its obligations under various employee benefit plans. At June 30, 2006, an additional 36,542,700 shares could be purchased under the then current authorization by AIG's Board of Directors.

Dividends from Insurance Subsidiaries

Payments of dividends to AIG by its insurance subsidiaries are subject to certain restrictions imposed by regulatory authorities. With respect to AIG's domestic insurance subsidiaries, the payment of any dividend requires formal notice to the insurance department in which the particular insurance subsidiary is domiciled. Under the laws of many states, an insurer may pay a dividend without prior approval of the insurance regulator when the amount of the dividend is below certain regulatory thresholds. To enhance their current capital positions, dividends from the DBG companies were suspended in the fourth quarter of 2005, and AIG has taken various other actions. See "Regulation and Supervision" below. Furthermore, AIG cannot predict how recent regulatory investigations may affect the ability of its regulated subsidiaries to pay dividends.

With respect to AIG's foreign insurance subsidiaries, the most significant insurance regulatory jurisdictions include Bermuda, Japan, Hong Kong, Taiwan, the United Kingdom, Thailand and Singapore.

AIG cannot predict whether the regulatory investigations currently underway or future regulatory issues will impair AIG's financial condition, results of operations or liquidity. To AIG's knowledge, no AIG company is currently on any regulatory or similar "watch list" with regard to solvency. (See also the discussion under "Liquidity" herein.)

Regulation and Supervision

AIG's insurance subsidiaries, in common with other insurers, are subject to regulation and supervision by the states and jurisdictions in which they do business. In the U.S. the National Association of Insurance Commissioners (NAIC) has developed Risk-Based Capital (RBC) requirements. RBC relates an individual insurance company's statutory surplus to the risk inherent in its overall operations.

AIG's insurance subsidiaries file financial statements prepared in accordance with statutory accounting practices prescribed or permitted by domestic and foreign insurance regulatory authorities. The principal differences between statutory financial statements and financial statements prepared

in accordance with U.S. GAAP for domestic companies are that statutory financial statements do not reflect deferred policy acquisition costs, some bond portfolios may be carried at amortized cost, assets and liabilities are presented net of reinsurance, policyholder liabilities are valued using more conservative assumptions and certain assets are non-admitted.

In connection with the filing of the 2005 statutory financial statements for AIG's domestic General Insurance companies, AIG agreed with the relevant state insurance regulators on the statutory accounting treatment of various items. The regulatory authorities have also permitted certain of the domestic and foreign insurance subsidiaries to support the carrying value of their investments in certain non-insurance and foreign insurance subsidiaries by utilizing the AIG audited consolidated financial statements to satisfy the requirement that the U.S. GAAP-basis equity of such entities be audited. In addition, the regulatory authorities have permitted the domestic General Insurance companies to utilize audited financial statements prepared on a basis of accounting other than U.S. GAAP to value investments in joint ventures, limited partnerships and hedge funds. These permitted practices did not affect the domestic General Insurance companies' compliance with minimum regulatory capital requirements.

Statutory capital of each company continued to exceed minimum company action level requirements following the adjustments, but AIG nonetheless contributed an additional $750 million of capital into American Home effective September 30, 2005 and contributed a further $2.25 billion of capital in February 2006 for a total of approximately $3 billion of capital into Domestic General Insurance subsidiaries effective December 31, 2005. To enhance their current capital positions, dividends from the DBG companies were suspended in the fourth quarter of 2005. AIG believes it has the capital resources and liquidity to fund any necessary statutory capital contributions. AIG will review the capital position of its insurance company subsidiaries with various rating agencies and regulators to determine if additional capital contributions or other actions are warranted.

As discussed above, various regulators have commenced investigations into certain insurance business practices. In addition, the OTS and other regulators routinely conduct examinations of AIG and its subsidiaries, including AIG's consumer finance operations. AIG cannot predict the ultimate effect that these investigations and examinations, or any additional regulation arising therefrom, might have on its business. Federal, state or local legislation may affect AIG's ability to operate and expand its various financial services businesses, and changes in the current laws, regulations or interpretations thereof may have a material adverse effect on these businesses. See "Risk Factors — Regulatory Investigations" in Item 1A. of Part I of AIG's 2005 Annual Report on Form 10-K for a further discussion of the effect these investigations may have on AIG's businesses.

AIG's U.S. operations are negatively affected under guarantee fund assessment laws which exist in most states. As a result of operating in a state which has guarantee fund assessment laws, a solvent insurance company may be assessed for certain obligations arising from the insolvencies of other insurance companies which operated in that state. AIG generally records these assessments upon notice. Additionally, certain states permit at least a portion of the assessed amount to be used as a credit against a company's future premium tax liabilities. Therefore, the ultimate net assessment cannot reasonably be estimated. The guarantee fund assessments net of credits for the first six months of 2006 were $17 million.

AIG is also required to participate in various involuntary pools (principally workers compensation business) which provide insurance coverage for those not able to obtain such coverage in the voluntary markets. This participation is also recorded upon notification, as these amounts cannot reasonably be estimated.

A substantial portion of AIG's General Insurance business and a majority of its Life Insurance & Retirement Services business are conducted in foreign countries. The degree of regulation and supervision in foreign jurisdictions varies. Generally, AIG, as well as the underwriting companies operating in such jurisdictions, must satisfy local regulatory requirements. Licenses issued by foreign authorities to AIG subsidiaries are subject to modification and revocation. Thus, AIG's insurance subsidiaries could be prevented from conducting future business in certain of the jurisdictions where they currently operate. AIG's international operations include operations in various developing nations. Both current and future foreign operations could be adversely affected by unfavorable political developments up to and including nationalization of AIG's operations without compensation. Adverse effects resulting from any one country may affect AIG's results of operations, liquidity and financial condition depending on the magnitude of the event and AIG's net financial exposure at that time in that country.

Foreign operations are individually subject to local solvency margin requirements that require maintenance of adequate capitalization, which AIG complies with by country. In addition, certain foreign locations, notably Japan, have established regulations that can result in guarantee fund assessments. These have not had a material effect on AIG's financial condition or results of operations.

Liquidity

AIG's liquidity is primarily derived from the operating cash flows of its General and Life Insurance & Retirement Services operations. Management believes that AIG's liquid assets, its net cash provided by operations, and access to the capital markets will enable it to meet any anticipated cash requirements.

At June 30, 2006, AIG's consolidated invested assets included $23.33 billion of cash and short-term investments. Consolidated net cash provided by operating activities in the first six months of 2006 amounted to $7.0 billion.

During the second quarter of 2006, AIG began presenting cash flows related to the origination and sale of finance receivables held for sale as cash flows within operating activities in the Consolidated Statement of Cash Flows. Previously these amounts were presented as cash flows within investing activities. In addition, certain intercompany transactions included in Finance receivables held for sale — originations and purchases and Finance receivable principal payments received in the Consolidated Statement of Cash Flows were not eliminated in 2005. After evaluating the effect of these items during the second quarter of 2006, AIG has revised the 2005 presentation to conform to the 2006 presentation. See Note 11 of Notes to the Consolidated Financial Statements.

The liquidity of the combined insurance operations is derived both domestically and abroad. The combined insurance operating cash flow is derived from two sources, underwriting operations and investment operations. Cash flow includes periodic premium collections, including policyholders' contract deposits, cash flows from investment operations and paid loss recoveries less reinsurance premiums, losses, benefits, and acquisition and operating expenses. Generally, there is a time lag from when premiums are collected and, when as a result of the occurrence of events specified in the policy, the losses and benefits are paid. Investment income cash flow is primarily derived from interest and dividends received and includes realized capital gains net of realized capital losses. (See also the discussions under "Operating Review: General Insurance Operations" and "Life Insurance & Retirement Services Operations" herein.)

With respect to General Insurance operations, if paid losses accelerated beyond AIG's ability to fund such paid losses from current operating cash flows, AIG might need to liquidate a portion of its General Insurance investment portfolio and/or arrange for financing. Potential events causing such a liquidity strain could be the result of several significant catastrophic events occurring in a relatively short period of time. Additional strain on liquidity could occur if the investments sold to fund such paid losses were sold into a depressed market place and/or reinsurance recoverable on such paid losses became uncollectible or collateral supporting such reinsurance recoverable significantly decreased in value. (See also the discussions under "Operating Review: General Insurance Operations" herein.)

With respect to Life Insurance & Retirement Services operations, if a substantial portion of the Life Insurance & Retirement Services operations bond portfolio diminished significantly in value and/or defaulted, AIG might need to liquidate other portions of its Life Insurance & Retirement Services investment portfolio and/or arrange financing. Potential events causing such a liquidity strain could be the result of economic collapse of a nation or region in which Life Insurance & Retirement Services operations exist, nationalization, terrorist acts, or other such economic or political upheaval. In addition, a significant rise in interest rates leading to a significant increase in policyholder surrenders could also create a liquidity strain. (See also the discussions under "Operating Review: Life Insurance & Retirement Services Operations" herein.)

In addition to the combined insurance pretax operating cash flow, AIG's insurance operations held $12.99 billion in cash and short-term investments at June 30, 2006. Operating cash flow and the cash and short-term balances held provided AIG's insurance operations with a significant amount of liquidity. AIG subsidiaries have also issued debt securities to meet capital needs. In December 2005, Transatlantic issued $750 million of debt securities in a public offering, of which $450 million were purchased by other AIG subsidiaries. Transatlantic contributed the proceeds of the offering to a reinsurance company subsidiary.

This liquidity is available, among other things, to purchase predominately high quality and diversified fixed income securities and, to a lesser extent, marketable equity securities, and to provide mortgage loans on real estate, policy loans and collateral loans. This cash flow coupled with proceeds of approximately $65 billion from the maturities, sales and redemptions of fixed income securities and from the sale of equity securities was used to purchase approximately $81 billion of fixed income securities and marketable equity securities during the first six months of 2006.

AIG's major Financial Services operating subsidiaries consist of AIGFP, ILFC, AGF and AIGCFG. Sources of funds considered in meeting the liquidity needs of AIGFP's operations include guaranteed investment agreements, issuance of long-term and short-term debt, proceeds from maturities and sales of securities available for sale, securities sold under repurchase agreements, and securities and spot commodities sold but not yet purchased. ILFC, AGF and AIGCFG all utilize the commercial paper markets, retail and wholesale deposits, bank loans and bank credit facilities as sources of liquidity. ILFC and AGF also fund in the domestic and international capital markets without reliance on any guarantee from AIG. An additional source of liquidity for ILFC is the use of export credit facilities. AIGCFG also uses wholesale and retail bank deposits as sources of funds. On occasion, AIG has provided equity capital to ILFC, AGF and AIGCFG and provides intercompany loans to AIGCFG. An AIG subsidiary purchased additional shares of ILFC in the amount of $400 million during the third quarter of 2005. Cash flow provided from operations is a major source of liquidity for AIG's primary Financial Services operating subsidiaries.

AIG, the parent company, funds its short-term working capital needs through commercial paper issued by AIG Fund-

ing. As of June 30, 2006, AIG Funding had $3.23 billion of commercial paper outstanding with an average maturity of 28 days. As additional liquidity, AIG parent has a $2 billion inter-company revolving credit facility provided by certain of its subsidiaries, a $1.625 billion 364-day revolving bank credit facility that expires in July 2007, a $1.625 billion five year revolving bank credit facility that expires in July 2011 and a $3 billion 364-day revolving credit facility that expires in November 2006, of which $669 million is currently available as back-up liquidity. AIG parent's primary sources of cash flow are dividends and loans from its subsidiaries. AIG parent's primary uses of cash flow are for debt service, capital contributions to subsidiaries and the payment of dividends to shareholders. As of June 30, 2006, including debt obligations of AGC that are guaranteed by AIG, remaining debt and loan maturities due in 2006 are $600 million and $0 for the third and fourth quarters, respectively. According to the terms of the Zero Coupon Convertible Senior Debentures issued by AIG on November 9, 2001, holders can require AIG to repurchase the debentures once every five years beginning on November 9, 2006. Assuming that all of the outstanding debentures are required to be repurchased by AIG on November 9, 2006, the aggregate repurchase price payable by AIG on that date will be approximately $1.10 billion. See also Note 9 of Notes to Consolidated Financial Statements in AIG's 2005 Annual Report on Form 10-K/A for additional information on debt maturities for AIG and its subsidiaries.

Special Purpose Vehicles and Off Balance Sheet Arrangements

AIG uses special purpose vehicles (SPVs) and off balance sheet arrangements in the ordinary course of business. As a result of recent changes in accounting, a number of SPVs and off balance sheet arrangements have been reflected in AIG's consolidated financial statements. In January 2003, FASB issued Interpretation No. 46, "Consolidation of Variable Interest Entities" (FIN 46). FIN 46 addressed the consolidation and disclosure rules for nonoperating entities that are now defined as Variable Interest Entities (VIEs). In December 2003, FASB issued a revision to Interpretation No. 46 (FIN 46(R)).

AIG has guidelines with respect to the formation of and investment in SPVs and off balance sheet arrangements. In addition, AIG has expanded the responsibility of its Complex Structured Financial Transaction Committee (CSFT) to include the review of any transaction that could subject AIG to heightened legal, reputational, regulatory, accounting or other risk. See "Management's Report on Internal Control Over Financial Reporting" in Item 9A. of Part II included in AIG's 2005 Annual Report on Form 10-K for a further discussion of the CSFT.

For additional information related to AIG's activities with respect to VIEs and certain guarantees see "Recent Accounting Standards" herein and also Note 8 of Notes to Consolidated Financial Statements. Also, for additional disclosure regarding AIG's commercial commitments (including guarantors), see "Contractual Obligations and Other Commercial Commitments" herein.

Derivatives

Derivatives are financial instruments among two or more parties with returns linked to or "derived" from some underlying equity, debt, commodity or other asset, liability, or index. Derivatives payments may be based on interest rates and exchange rates and/or prices of certain securities, commodities, financial or commodity indices, or other variables. The more significant types of derivative arrangements in which AIG transacts are swaps, forwards, futures and options. In the normal course of business, with the agreement of the original counterparty, these contracts may be terminated early or assigned to another counterparty.

The overwhelming majority of AIG's derivatives activities are conducted by the Capital Markets operations, thus permitting AIG to participate in the derivatives dealer market acting primarily as principal. In these derivative operations, AIG structures transactions that generally allow its counterparties to obtain or hedge exposure to changes in interest and foreign currency exchange rates, credit events, securities' prices and certain commodities and financial or commodity indices. AIG's customers – such as corporations, financial institutions, multinational organizations, sovereign entities, government agencies and municipalities – use derivatives to hedge their own market exposures. For example, a futures, forward or option contract can be used to protect the customers' assets or liabilities against price fluctuations.

A counterparty may default on any obligation to AIG, including a derivative contract. Credit risk is a consequence of extending credit and/or carrying trading and investment positions. Credit risk exists for a derivative contract when that contract has a positive fair value to AIG. To help manage this risk, AIGFP's credit department operates within the guidelines set by the AIG Credit Risk Committee. This committee establishes the credit policy, sets limits for counterparties and provides limits for derivative transactions with counterparties having different credit ratings. In addition to credit ratings, this committee takes into account other factors, including the industry and country of the counterparty. Transactions which fall outside these pre-established guidelines require the specific approval of the AIG Credit Risk Committee. It is also AIG's policy to establish reserves for potential credit impairment when necessary.

In addition, AIGFP utilizes various credit enhancements, including letters of credit, guarantees, collateral, credit triggers, credit derivatives, and margin agreements to reduce the credit risk relating to its outstanding financial derivative transactions. AIGFP requires credit enhancements in connection with specific transactions based on, among other things,

the creditworthiness of the counterparties, and the transaction's size and maturity.

AIG's Derivatives Review Committee provides an independent review of any proposed derivative transaction or program except those derivative transactions entered into by AIGFP with third parties. The committee examines, among other things, the nature and purpose of the derivative transaction, its potential credit exposure, if any, and the estimated benefits.

Managing Risk

Market Risk

Market risk is the risk of loss of fair value resulting from adverse fluctuations in interest rates, foreign currencies, equities and commodity prices. AIG has exposures to these risks.

AIG analyzes market risk using various statistical techniques including Value at Risk (VaR). VaR is a summary statistical measure that applies the estimated volatility and correlation of market factors to AIG's market positions. The output from the VaR calculation is the maximum loss that could occur over a defined period of time given a certain probability. While VaR models are relatively sophisticated, the quantitative market risk information generated is limited by the assumptions and parameters established in creating the related models. AIG believes that statistical models alone do not provide a reliable method of monitoring and controlling market risk. Therefore, such models are tools and do not substitute for the experience or judgment of senior management.

Insurance

AIG has performed a separate VaR analysis for the General Insurance and Life Insurance & Retirement Services segments and for each market risk within each segment. For purposes of the VaR calculation, the insurance assets and liabilities from GICs are included in the Life Insurance & Retirement Services segment. For the calculations in the analyses the financial instrument assets included are the insurance segments' invested assets, excluding real estate and investment income due and accrued, and the financial instrument liabilities included are reserve for losses and loss expenses, unearned premiums, future policy benefits for life and accident and health insurance contracts and other policyholders' funds.

AIG calculated the VaR with respect to the net fair value of each of AIG's insurance segments as of June 30, 2006 and December 31, 2005. The VaR number represents the maximum potential loss as of those dates that could be incurred with a 95 percent confidence (i.e., only five percent of historical scenarios show losses greater than the VaR figure) within a one-month holding period. AIG uses the historical simulation methodology that entails repricing all assets and liabilities under explicit changes in market rates within a specific historical time period. AIG uses the most recent three years of historical market information for interest rates, foreign exchange rates, and equity index prices. For each scenario, each transaction was repriced. Portfolio, business unit and finally AIG-wide scenario values are then calculated by netting the values of all the underlying assets and liabilities.

The following table presents the period-end, average, high and low VaRs on a combined basis and of each component of market risk for each of AIG's insurance segments as of June 30, 2006 and December 31, 2005. Due to diversification effects, the combined VaR is always smaller than the sum of its components.

	2006				2005			
	As of June 30,	For the six months ended June 30,			As of December 31,	For the year ended December 31,		
(in millions)		Average	High	Low		Average	High	Low
General Insurance:								
Market risk:								
Combined	**$1,776**	**$1,689**	**$1,776**	**$1,617**	$1,617	$1,585	$1,672	$1,396
Interest rate	**1,716**	**1,690**	**1,717**	**1,636**	1,717	1,746	1,931	1,563
Currency	**150**	**133**	**150**	**119**	130	125	139	111
Equity	**553**	**549**	**560**	**535**	535	651	727	535
Life Insurance & Retirement Services:								
Market risk:								
Combined	**$4,857**	**$4,878**	**$5,260**	**$4,515**	$4,515	$4,737	$5,024	$4,515
Interest rate	**4,843**	**4,752**	**5,032**	**4,382**	4,382	4,488	4,750	4,382
Currency	**475**	**538**	**597**	**475**	541	511	560	442
Equity	**967**	**841**	**967**	**762**	762	953	1,024	762

In the Life Insurance & Retirement Services segment, the increase in Combined VaR and interest rate VaR in 2006 was primarily the result of growth in the Foreign Life business. In most Asian markets, interest rates and interest rate volatilities were stable during the first six months of 2006.

Financial Services

AIG generally manages its market exposures within Financial Services by maintaining offsetting positions. Capital Markets seeks to minimize or set limits for open or uncovered market positions. Credit exposure is managed separately. (See the discussion on the management of credit risk above.)

AIG's Market Risk Management Department provides detailed independent review of AIG's market exposures, particularly those market exposures of the Capital Markets operations. This department determines whether AIG's market risks, as well as those market risks of individual subsidiaries, are within the parameters established by AIG's senior management. Well established market risk management techniques such as sensitivity analysis are used. Additionally, this department verifies that specific market risks of each of certain subsidiaries are managed and hedged by that subsidiary.

ILFC is exposed to market risk and the risk of loss of fair value and possible liquidity strain resulting from adverse fluctuations in interest rates. As of June 30, 2006 and December 31, 2005, AIG statistically measured the loss of fair value through the application of a VaR model. In this analysis, the net fair value of Aircraft Finance operations was determined using the financial instrument assets which included the tax adjusted future flight equipment lease revenue, and the financial instrument liabilities which included the future servicing of the current debt. The estimated effect of the current derivative positions was also taken into account.

AIG calculated the VaR with respect to the net fair value of Aircraft Finance operations using the historical simulation methodology, as previously described. As of June 30, 2006 and December 31, 2005, the average VaR with respect to the net fair value of Aircraft Finance operations was approximately $182 million and $129 million, respectively. In late 2005, ILFC lengthened the average maturity of its debt, leading to an increase in its VaR.

Capital Markets operations are exposed to market risk due to changes in the level and volatility of interest rates, foreign currency exchange rates, equity prices and commodity prices. AIGFP hedges its exposure to these risks primarily through swaps, options, forwards and futures. To economically hedge interest rate risks, AIGFP may also purchase U.S. and foreign government obligations.

AIGFP does not seek to manage the market risk of each transaction through an individual third party offsetting transaction. Rather, AIGFP takes a portfolio approach to the management of its market risk exposures. AIGFP values the predominant portion of its market-sensitive transactions by marking them to market currently through income. A smaller portion is priced by estimated fair value based upon an extrapolation of market factors. There is another limited portion of transactions where the initial fair value is not recorded through income currently and gains or losses are recognized over the life of the transactions. These valuations represent an assessment of the present values of expected future cash flows and may include reserves for such risks as are deemed appropriate by AIGFP and AIG management.

The recorded values of these transactions may be different from the values that might be realized if AIGFP were required to sell or close out the transactions prior to maturity. AIG believes that such differences are not significant to its financial condition or liquidity. Such differences would be immediately recognized when the transactions are sold or closed out prior to maturity.

AIGFP attempts to secure reliable and independent current market prices, such as published exchange prices, external subscription services such as from Bloomberg or Reuters or third-party broker quotes for use in this model. When such prices are not available, AIGFP use an internal methodology which includes extrapolation from observable and verifiable prices nearest to the measurement date of the reporting period. Historically, actual results have not materially deviated from these models in any material respect.

Systems used by Capital Markets operations can monitor each unit's respective market positions on an intraday basis. AIGFP operates in major business centers overseas and therefore is open for business essentially 24 hours a day. Thus, the market exposure and offset strategies are monitored, reviewed and coordinated around the clock.

AIGFP applies various testing techniques which reflect significant potential market movements in interest rates, foreign exchange rates, commodity and equity prices, volatility levels and the effect of time. These techniques vary by currency and are regularly changed to reflect factors affecting the derivatives portfolio. The results from these analyses are regularly reviewed by AIG management.

As described above, Capital Markets operations are exposed to the risk of loss of fair value from adverse fluctuations in interest rate and foreign currency exchange rates and equity and commodity prices as well as implied volatilities thereon. AIG statistically measures the losses of fair value through the application of a VaR model across Capital Markets.

Capital Markets asset and liability portfolios for which the VaR analyses were performed included over the counter and exchange traded investments, derivative instruments and commodities. Because the market risk with respect to securities available for sale, at market, is substantially hedged, segregation of market sensitive instruments into trading and other than trading was not deemed necessary. The VaR calculation is unaffected by the accounting treatment of hedged transactions under FAS 133.

In the calculation of VaR for Capital Markets operations, AIG uses the same historical simulation methodology, described under Insurance above, which entails repricing all assets and liabilities under explicit changes in market rates within a specific historical time period.

The following table presents the VaR on a combined basis and of each component of market risk for Capital Markets operations as of June 30, 2006 and December 31, 2005. Due to diversification effects, the combined VaR is always smaller than the sum of its components.

(in millions)	**2006**	2005
Combined	**$20**	$22
Interest rate	**7**	9
Currency	**9**	3
Equity	**13**	14
Commodity	**10**	9

The following table presents the average, high and low VaRs on a combined basis and of each component of market risk for Capital Markets operations as of June 30, 2006 and December 31, 2005. Due to diversification effects, the combined VaR is always smaller than the sum of its components.

	2006			2005		
(in millions)	**Average**	**High**	**Low**	Average	High	Low
Combined	**$21**	**$22**	**$20**	$17	$22	$13
Interest rate	**8**	**9**	**7**	9	11	6
Currency	**6**	**9**	**3**	4	6	3
Equity	**13**	**14**	**12**	9	16	5
Commodity	**12**	**16**	**9**	8	10	7

Catastrophe Exposures

The nature of AIG's business exposes it to various catastrophic events in which multiple losses across multiple lines of business can occur in any calendar year. In order to control this exposure, AIG uses a combination of techniques, including setting aggregate limits in key business units, monitoring and modeling accumulated exposures, and purchasing catastrophe reinsurance to supplement its other reinsurance protections.

AIG evaluates catastrophic events and assesses the probability of occurrence and magnitude of catastrophic events through the use of third party models generally recognized as industry standards. Following is an overview of modeled losses associated with the more significant natural perils. The modeled results assume that all reinsurers perform their obligations to AIG in accordance with their terms.

It is important to recognize that there is no standard methodology to project the possible losses from total property and workers compensation exposures and that the use of different models could result in materially different projected losses. Further, there are no industry standard assumptions to be utilized in projecting these losses. The use of different assumptions could materially change the projected losses. Therefore, these modeled losses may not be comparable to estimates made by other companies.

These estimates are inherently uncertain and may not reflect AIG's maximum exposures to these events. It is highly likely that AIG's losses will vary, perhaps significantly, from these estimates.

Natural Catastrophe Exposures

The modeled results provided in the table below were based on the aggregate exceedence probability (AEP) losses which represent total property and workers compensation losses that may occur in any single year from one or more natural events. The model, which has been updated to reflect 2005 catastrophes, generally used 2005 exposure data and the current reinsurance program structure. The values provided were based on 100 year return period losses, which have a 1 percent likelihood of being exceeded in any single year. Thus, there is a one percent probability that AIG could incur in any year losses in excess of the modeled amounts for these perils.

(in millions)

Natural Peril	**Gross**	**Net of Reinsurance**	**Net, After Income Taxes**	**% of Consolidated Shareholders' Equity at December 31, 2005**
Earthquake	$3,412	$2,283	$1,484	1.7%
Tropical Cyclone*	$5,336	$3,907	$2,540	2.9%

** Includes hurricanes, typhoons and other wind-related events.*

In addition, AIG also evaluates potential single event earthquake and hurricane losses that may be incurred. The single events utilized are a subset of potential events identified and utilized by Lloyd's[1] and referred to as Realistic Disaster Scenarios (RDSs). The purpose of this analysis was to utilize these RDSs to provide a reference frame and place into context the model results. However, it is important to note that the specific events used for this analysis do not necessarily represent the worst case loss that AIG could incur from this type of an event in these regions. The losses associated with the RDSs are included in the table below.

Single event modeled property and workers compensation losses to AIG's worldwide portfolio of risk for key geographic areas. Gross values represent AIG's liability after the application of policy limits and deductibles, and net values represent losses after all reinsurance is applied.

(in millions)

Natural Peril	**Gross**	**Net of Reinsurance**
Miami Hurricane	$4,530	$2,911
Northeast Hurricane	3,732	2,498
San Francisco Earthquake	3,628	2,229
Los Angeles Earthquake	3,285	2,145
Gulf Coast Hurricane	2,581	1,391
Japanese Earthquake	339	153
European Windstorm	135	41
Japanese Typhoon	125	105

ACTUAL RESULTS IN ANY PERIOD ARE LIKELY TO VARY, PERHAPS MATERIALLY, FROM THE MODELED SCENARIOS, AND THE OCCURRENCE OF ONE OR MORE SEVERE EVENTS COULD HAVE A MATERIAL ADVERSE EFFECT ON AIG'S FINANCIAL CONDITION, RESULTS OF OPERATIONS AND LIQUIDITY.

[1] *Lloyd's Realistic Disaster Scenarios, Scenario Specifications, April 2006*

Measures Implemented to Control Hurricane and Earthquake Catastrophic Risk

Catastrophic risk from the earthquake and hurricane perils is proactively managed through reinsurance programs, and aggregate accumulation monitoring. Catastrophe reinsurance is purchased by AIG from financially sound reinsurers. Recoveries under this program, along with other non-catastrophic reinsurance protections, are reflected in the net values provided in the tables above. In addition to the catastrophic reinsurance programs, hurricane and earthquake exposures are also controlled by monitoring aggregate exposures on a regular basis. The aggregate exposures are calculated by compiling total liability within AIG defined hurricane and earthquake catastrophe risk zones and therefore represent the maximum that could be lost in any individual zone. These aggregate accumulations are tracked over time in order to monitor both long and short term trends. AIG's major property writers, Lexington and The Private Client Group, have also implemented catastrophe related underwriting procedures and manage their books at an account level. Lexington individually models most accounts prior to binding in order to specifically quantify catastrophic risk for each account.

Pandemic Influenza

The potential for a pandemic influenza outbreak has received media attention during the past year. AIG continues to analyze its exposure to this serious threat and, as such, has engaged an external risk management firm to model loss scenarios associated with an outbreak of Avian Flu. Using a 1 in 100 year return period, AIG estimates its after-tax net losses under its life insurance policies due to Avian Flu at approximately 0.9 percent of consolidated shareholders' equity as of December 31, 2005. This estimate was calculated over a 3 year period, although the majority of the losses would be incurred in the first year. The modeled losses calculated were based on 2005 policy data representing approximately 90 percent of AIG's Individual Life, Group Life, and Credit Life books of business, net of reinsurance. This estimate does not include claims that could be made under other policies, such as business interruption or general liability policies, and does not reflect estimates for losses resulting from disruption of AIG's own business operations that may arise out of such a pandemic. The model used to generate this estimate has only recently been developed. The reasonableness of the model and its underlying assumptions cannot readily be verified by reference to comparable historical events. As a result, AIG's actual losses from a pandemic influenza outbreak are likely to vary significantly from those predicted by the model.

Terrorism

Terrorism risk is also monitored to control AIG's exposure. AIG shares its exposures to terrorism risks under the Terrorism Risk Insurance Act (TRIA). AIG's current deductible under TRIA is $3.3 billion and AIG would share 10 percent of certified terrorism losses in excess of the $3.3 billion.

Recent Accounting Standards

At the March 2004 meeting, the Emerging Issue Task Force (EITF) reached a consensus with respect to Issue No. 03-1, "The Meaning of Other-Than Temporary Impairment and Its Application to Certain Investments." On September 30, 2004, the FASB issued FASB Staff Position (FSP) EITF Issue 03-1-1, Effective Date of Paragraphs 10-20 of EITF Issue No. 03-1, "The Meaning of Other-Than-Temporary Impairment and its Application to Certain Investments." In November 2005, FASB issued FSP FAS 115-1, "The Meaning of Other-Than-Temporary Impairment and Its Application to Certain Investments," which replaces the measurement and recognition guidance set forth in Issue No. 03-1 and codifies certain existing guidance on impairment.

On June 1, 2005, the FASB issued Statement No. 154, "Accounting Changes and Error Corrections" (FAS 154). FAS 154 replaces APB Opinion No. 20, "Accounting Changes" and FASB Statement No. 3, "Reporting Accounting Changes in Interim Financial Statements."

At the June 2005 meeting, the EITF reached a consensus with respect to Issue No. 04-5, "Determining Whether a General Partner, or the General Partners as a Group, Controls a Limited Partnership or Similar Entity When the Limited Partners have Certain Rights."

On June 29, 2005, the FASB issued Statement 133 Implementation Issues No. B38, "Embedded Derivatives: Evaluation of Net Settlement with Respect to the Settlement of a Debt Instrument through Exercise of an Embedded Put Option or Call Option" and No. B39, "Application of Paragraph 13(b) to Call Options That are Exercisable Only by the Debtor."

On September 19, 2005, the FASB issued Statement of Position 05-1, "Accounting by Insurance Enterprises for Deferred Acquisition Costs in Connection with Modifications or Exchanges of Insurance Contracts."

On February 16, 2006, the FASB issued FAS No. 155, "Accounting for Certain Hybrid Financial Instruments."

On March 27, 2006, the FASB issued FASB FTB 85-4-1, "Accounting for Life Settlement Contracts by Third-Party Investors" (FSP 85-4-1), an amendment of FTB 85-4, "Accounting for Purchases of Life Insurance."

On April 13, 2006, the FASB issued FSP FIN 46(R)-6, "Determining the Variability to be Considered in Applying FASB Interpretation No. 46(R)."

On July 13, 2006, the FASB issued FASB Interpretation No. 48, "Accounting for Uncertainty in Income Taxes - an interpretation of FASB Statement No. 109" (FIN 48).

Effective January 1, 2006, AIG adopted the fair value recognition provisions of Statement of Financial Accounting Standards No. 123R "Share-Based Payments" (FAS 123R). For further discussion of these recent accounting standards and its application to AIG, see Note 10 of Notes to Consolidated Financial Statements.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Included in Item 2. Managements Discussion and Analysis of Financial Condition and Results of Operations.

ITEM 4. CONTROLS AND PROCEDURES

In connection with the preparation of this Form 10-Q, an evaluation was carried out by AIG's management, with the participation of AIG's Chief Executive Officer and Chief Financial Officer, of the effectiveness of AIG's disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934 (Exchange Act)). Disclosure controls and procedures are designed to ensure that information required to be disclosed in reports filed or submitted under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in SEC rules and forms and that such information is accumulated and communicated to management, including the Chief Executive Officer and Chief Financial Officer, to allow timely decisions regarding required disclosures. Based on its evaluation, and in light of the previously identified material weaknesses in internal control over financial reporting, as of December 31, 2005, described within the 2005 Annual Report on Form 10-K, AIG's Chief Executive Officer and Chief Financial Officer concluded that, as of June 30, 2006, AIG's disclosure controls and procedures were ineffective. In addition, there has been no change in AIG's internal control over financial reporting (as defined in Rule 13a-15(f) under the Exchange Act) that occurred during the quarter ended June 30, 2006 that has materially affected, or is reasonably likely to materially affect, AIG's internal control over financial reporting.

Part II – OTHER INFORMATION

ITEM 2. Unregistered Sales of Equity Securities and Use of Proceeds.

The table below provides information with respect to purchases of AIG Common stock during the three months ended June 30, 2006.

Period	Total Number of Shares Purchased[1]	Average Price Paid per Share	Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs	Maximum Number of Shares that May Yet Be Purchased Under the Plans or Programs at End of Month[2]
April 1 - 30	–	$ –	–	36,542,700
May 1 - 31	–	–	–	36,542,700
June 1 - 30	–	–	–	36,542,700
Total	–	$ –	–	

(1) Does not include 30,518 shares delivered or attested to in satisfaction of the exercise price by holders of AIG employee stock options exercised during the three months ended June 30, 2006.

(2) On July 19, 2002, AIG announced that its Board of Directors had authorized the open market purchase of up to 10 million shares of common stock. On February 13, 2003, AIG announced that the Board had expanded the existing program through the authorization of an additional 50 million shares. The purchase program has no set expiration or termination date.

ITEM 4. Submission of Matters to a Vote of Security Holders.

At the Annual Meeting of Shareholders held on May 17, 2006, the Shareholders:

(a) Elected fifteen directors as follows:

Nominee	Shares For	Shares Withheld
Pei-yuan Chia	2,245,278,647	112,943,402
Marshall A. Cohen	1,738,721,381	619,500,668
Martin S. Feldstein	1,780,147,427	578,074,622
Ellen V. Futter	1,801,720,202	556,501,847
Stephen L. Hammerman	2,280,495,958	77,726,091
Richard C. Holbrooke	1,791,353,064	566,868,985
Fred H. Langhammer	2,300,193,254	58,028,795
George L. Miles, Jr.	2,290,670,840	67,551,209
Morris W. Offit	2,251,884,371	106,337,678
James F. Orr III	2,300,512,200	57,709,849
Martin J. Sullivan	1,849,146,165	509,075,884
Michael H. Sutton	2,299,458,677	58,763,372
Edmund S.W. Tse	2,294,329,520	63,892,529
Robert B. Willumstad	2,300,312,892	57,909,157
Frank G. Zarb	1,832,805,886	525,416,163

(b) Approved by a vote of 1,745,063,449 shares to 576,509,051 shares, with 36,649,549 abstaining, a proposal to ratify the selection of PricewaterhouseCoopers LLP as the independent registered public accounting firm for 2006.

(c) Approved by a vote of 2,169,404,151 shares to 148,588,891 shares, with 40,229,007 abstaining, a proposal to adopt an Executive Incentive Plan.

ITEM 6. Exhibits.

See accompanying Exhibit Index.

SIGNATURE

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

AMERICAN INTERNATIONAL GROUP, INC.
(Registrant)

/s/ STEVEN J. BENSINGER

Steven J. Bensinger
Executive Vice President and Chief Financial Officer

/s/ DAVID L. HERZOG

David L. Herzog
Senior Vice President and Comptroller
(Principal Accounting Officer)

Dated: August 9, 2006

EXHIBIT INDEX

Exhibit Number	Description	Location
11	Statement re computation of per share earnings	Included in Note (3) of Notes to Consolidated Financial Statements.
12	Statement re computation of ratios	Filed herewith.
31	Rule 13a-14(a)/15d-14(a) Certifications	Filed herewith.
32	Section 1350 Certifications	Filed herewith.

Exhibit 12

American International Group, Inc.
Computation of Ratios of Earnings to Fixed Charges

(in millions, except ratios)	Three Months Ended June 30, 2006	Three Months Ended June 30, 2005	Six Months Ended June 30, 2006	Six Months Ended June 30, 2005
Income before income taxes, minority interest and cumulative effect of an accounting change	**$ 5,241**	$6,701	**$10,034**	$12,350
Less – Equity income of less than 50% owned persons	**110**	30	**130**	93
Add – Dividends from less than 50% owned persons	**15**	123	**18**	126
	5,146	6,794	**9,922**	12,383
Add – Fixed charges	**2,048**	1,739	**3,996**	3,469
Less – Capitalized interest	**14**	15	**29**	30
Income before income taxes, minority interest, cumulative effect of an accounting change and fixed charges	**$ 7,180**	$8,518	**$13,889**	$15,822
Fixed charges:				
Interest costs	**$ 1,995**	$1,687	**$ 3,891**	$ 3,366
Rental expense*	**53**	52	**105**	103
Total fixed charges	**$ 2,048**	$1,739	**$ 3,996**	$ 3,469
Ratio of earnings to fixed charges	**3.51**	4.90	**3.48**	4.56
Secondary Ratio				
Interest credited to GIC and GIA policy and contract holders	**$ (1,097)**	$ (968)	**$ (2,187)**	$ (2,062)
Total fixed charges excluding interest credited to GIC and GIA policy and contract holders	**$ 951**	$ 771	**$ 1,809**	$ 1,407
Secondary ratio of earnings to fixed charges	**6.40**	9.79	**6.47**	9.78

**The portion deemed representative of the interest factor.*

The secondary ratio is disclosed for the convenience of fixed income investors and the rating agencies that serve them and is more comparable to the ratios disclosed by all issuers of fixed income securities. The secondary ratio removes interest credited to guaranteed investment contract (GIC) policyholders and guaranteed investment agreement (GIA) contractholders. Such expenses are also removed from income before income taxes, minority interest and cumulative effect of an accounting change used in this calculation. GICs and GIAs are entered into by AIG's insurance subsidiaries, principally Sun America Life Insurance Company and AIG Financial Products Corp. and its subsidiaries, respectively. The proceeds from GICs and GIAs are invested in a diversified portfolio of securities, primarily investment grade bonds. The assets acquired yield rates greater than the rates on the related policyholders obligation or agreement, with the intent of earning operating income from the spread.

Exhibit 31

CERTIFICATIONS

I, Martin J. Sullivan, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q of American International Group, Inc.;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:

(a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

(b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

(c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

(d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):

(a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

(b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

/s/ MARTIN J. SULLIVAN

Martin J. Sullivan
President and Chief Executive Officer

Date: August 9, 2006

CERTIFICATIONS

I, Steven J. Bensinger, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q of American International Group, Inc.;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:

(a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

(b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

(c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

(d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):

(a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

(b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

/s/ STEVEN J. BENSINGER

Steven J. Bensinger
Executive Vice President and Chief Financial Officer

Date: August 9, 2006

Exhibit 32

CERTIFICATION

In connection with the Quarterly Report on Form 10-Q of American International Group, Inc. (the "Company") for the quarter ended June 30, 2006, as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, Martin J. Sullivan, President and Chief Executive Officer of the Company, certify, pursuant to 18 U.S.C. Section 1350, that to my knowledge:

1. The Report fully complies with the requirements of Section 13(a) or 15(d), as applicable, of the Securities Exchange Act of 1934; and

2. The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

/s/ MARTIN J. SULLIVAN

Martin J. Sullivan
President and Chief Executive Officer

Date: August 9, 2006

The foregoing certification is being furnished solely pursuant to 18 U.S.C. Section 1350 and is not being filed as part of the Report or as a separate disclosure document.

CERTIFICATION

In connection with the Quarterly Report on Form 10-Q of American International Group, Inc. (the "Company") for the quarter ended June 30, 2006, as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, Steven J. Bensinger, Executive Vice President and Chief Financial Officer of the Company, certify, pursuant to 18 U.S.C. Section 1350, that to my knowledge:

1. The Report fully complies with the requirements of Section 13(a) or 15(d), as applicable, of the Securities Exchange Act of 1934; and

2. The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

/s/ STEVEN J. BENSINGER

Steven J. Bensinger
Executive Vice President and Chief Financial Officer

Date: August 9, 2006

The foregoing certification is being furnished solely pursuant to 18 U.S.C. Section 1350 and is not being filed as part of the Report or as a separate disclosure document.

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

Form 10-Q

(Mark One)

☑ QUARTERLY REPORT UNDER SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended September 30, 2006

or

☐ TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the transition period from to

Commission File Number 1-8787

American International Group, Inc.

(Exact name of registrant as specified in its charter)

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

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

Former name, former address and former fiscal year, if changed since last report: None

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

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of accelerated filer and large accelerated filer in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer ☑ Accelerated filer ☐ Non-accelerated filer ☐

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes ☐ No ☑

Applicable only to corporate issuers

As of October 31, 2006, there were 2,599,721,215 shares outstanding of the issuer's common stock.

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Part I – FINANCIAL INFORMATION

ITEM 1. Financial Statements (unaudited)

CONSOLIDATED BALANCE SHEET

(in millions) (unaudited)

	September 30, 2006	December 31, 2005
Assets:		
Investments and financial services assets:		
Fixed maturities:		
Bonds available for sale, at market value (amortized cost: 2006 – $368,532; 2005 – $349,612) (includes hybrid financial instruments: 2006 – $407)	**$376,036**	$359,516
Bonds held to maturity, at amortized cost (market value: 2006 – $22,148; 2005 – $22,047)	**21,484**	21,528
Bond trading securities, at market value (cost: 2006 – $7,267; 2005 – $4,623)	**7,238**	4,636
Equity securities:		
Common stocks available for sale, at market value (cost: 2006 – $10,125; 2005 – $10,125)	**11,835**	12,227
Common and preferred stocks trading, at market value (cost: 2006 – $10,098; 2005 – $7,746)	**11,528**	8,959
Preferred stocks available for sale, at market value (cost: 2006 – $2,450; 2005 – $2,282)	**2,500**	2,402
Mortgage loans on real estate, net of allowance (2006 – $57; 2005 – $54)	**16,842**	14,300
Policy loans	**7,385**	7,039
Collateral and guaranteed loans, net of allowance (2006 – $7; 2005 – $10)	**3,597**	3,570
Financial services assets:		
Flight equipment primarily under operating leases, net of accumulated depreciation (2006 – $8,480; 2005 – $7,419)	**39,460**	36,245
Securities available for sale, at market value (cost: 2006 – $40,501; 2005 – $37,572)	**41,232**	37,511
Trading securities, at market value	**5,822**	6,499
Spot commodities	**118**	92
Unrealized gain on swaps, options and forward transactions	**20,235**	18,695
Trading assets	**2,194**	1,204
Securities purchased under agreements to resell, at contract value	**27,041**	14,547
Finance receivables, net of allowance (2006 – $679; 2005 – $670) (includes finance receivables held for sale: 2006 – $863; 2005 – $1,110)	**28,634**	27,995
Securities lending collateral, at market value (which approximates cost)	**71,388**	59,471
Other invested assets	**32,777**	27,267
Short-term investments, at cost (which approximates market value)	**22,716**	15,342
Total investments and financial services assets	**750,062**	679,045
Cash	**1,425**	1,897
Investment income due and accrued	**6,202**	5,727
Premiums and insurance balances receivable, net of allowance (2006 – $881; 2005 – $1,011)	**17,540**	15,333
Reinsurance assets, net of allowance (2006 – $447; 2005 – $992)	**24,364**	24,978
Deferred policy acquisition costs	**36,342**	33,248
Investments in partially owned companies	**1,031**	1,158
Real estate and other fixed assets, net of accumulated depreciation (2006 – $5,424; 2005 – $4,990)	**9,141**	7,446
Separate and variable accounts	**70,652**	63,797
Goodwill	**8,576**	8,093
Other assets	**16,209**	12,329
Total assets	**$941,544**	$853,051

See Accompanying Notes to Consolidated Financial Statements.

CONSOLIDATED BALANCE SHEET *(continued)*

(in millions, except share data) (unaudited)

	September 30, 2006	December 31, 2005
Liabilities:		
Reserve for losses and loss expenses	**$ 79,863**	$ 77,169
Unearned premiums	**26,068**	24,243
Future policy benefits for life and accident and health insurance contracts	**118,273**	108,807
Policyholders' contract deposits	**236,342**	227,027
Other policyholders' funds	**10,534**	10,870
Commissions, expenses and taxes payable	**5,125**	4,769
Insurance balances payable	**4,722**	3,564
Funds held by companies under reinsurance treaties	**2,442**	4,174
Income taxes payable	**8,497**	6,288
Financial services liabilities:		
Borrowings under obligations of guaranteed investment agreements	**21,091**	20,811
Securities sold under agreements to repurchase, at contract value	**15,071**	11,047
Trading liabilities	**2,914**	2,546
Hybrid financial instrument liabilities, at fair value	**8,150**	–
Securities and spot commodities sold but not yet purchased, at market value	**5,645**	5,975
Unrealized loss on swaps, options and forward transactions	**12,764**	12,740
Trust deposits and deposits due to banks and other depositors	**4,813**	4,877
Commercial paper	**8,814**	6,514
Notes, bonds, loans and mortgages payable	**79,834**	71,313
Commercial paper	**4,484**	2,694
Notes, bonds, loans and mortgages payable	**13,350**	7,126
Liabilities connected to trust preferred stock	**1,399**	1,391
Separate and variable accounts	**70,652**	63,797
Securities lending payable	**72,264**	60,409
Minority interest	**6,290**	5,124
Other liabilities (includes hybrid financial instruments: 2006 – $70)	**25,800**	23,273
Total liabilities	**845,201**	766,548
Preferred shareholders' equity in subsidiary companies	**189**	186
Commitments and Contingent Liabilities (See Note 6)		
Shareholders' equity:		
Common stock, $2.50 par value; 5,000,000,000 shares authorized; shares issued 2006 and 2005 – 2,751,327,476	**6,878**	6,878
Additional paid-in capital	**2,572**	2,339
Retained earnings	**81,987**	72,330
Accumulated other comprehensive income (loss)	**6,744**	6,967
Treasury stock, at cost; 2006 – 152,107,902; 2005 – 154,680,704 shares of common stock	**(2,027)**	(2,197)
Total shareholders' equity	**96,154**	86,317
Total liabilities, preferred shareholders' equity in subsidiary companies and shareholders' equity	**$941,544**	$853,051

See Accompanying Notes to Consolidated Financial Statements.

CONSOLIDATED STATEMENT OF INCOME

(in millions, except per share data) (unaudited)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2006	2005	**2006**	2005
Revenues:				
Premiums and other considerations	**$18,856**	$17,243	**$55,401**	$52,459
Net investment income	**6,263**	5,654	**18,002**	16,213
Realized capital gains (losses)	**(87)**	77	**(132)**	89
Other income	**4,167**	3,434	**9,930**	12,752
Total revenues	**29,199**	26,408	**83,201**	81,513
Benefits and expenses:				
Incurred policy losses and benefits	**14,737**	16,501	**43,725**	45,657
Insurance acquisition and other operating expenses	**8,161**	7,360	**23,141**	20,959
Total benefits and expenses	**22,898**	23,861	**66,866**	66,616
Income before income taxes, minority interest and cumulative effect of an accounting change	**6,301**	2,547	**16,335**	14,897
Income taxes	**1,943**	748	**5,066**	4,537
Income before minority interest and cumulative effect of an accounting change	**4,358**	1,799	**11,269**	10,360
Minority interest	**(134)**	(54)	**(694)**	(327)
Income before cumulative effect of an accounting change	**4,224**	1,745	**10,575**	10,033
Cumulative effect of an accounting change, net of tax	**–**	–	**34**	–
Net income	**$ 4,224**	$ 1,745	**$10,609**	$10,033
Earnings per common share:				
Basic				
Income before cumulative effect of an accounting change	**$ 1.62**	$ 0.67	**$ 4.06**	$ 3.86
Cumulative effect of an accounting change, net of tax	**–**	–	**0.01**	–
Net income	**$ 1.62**	$ 0.67	**$ 4.07**	$ 3.86
Diluted				
Income before cumulative effect of an accounting change	**$ 1.61**	$ 0.66	**$ 4.03**	$ 3.82
Cumulative effect of an accounting change, net of tax	**–**	–	**0.01**	–
Net income	**$ 1.61**	$ 0.66	**$ 4.04**	$ 3.82
Dividends declared per common share	**$ 0.165**	$ 0.175	**$ 0.48**	$ 0.475
Average shares outstanding:				
Basic	**2,607**	2,597	**2,607**	2,597
Diluted	**2,626**	2,624	**2,625**	2,624

See Accompanying Notes to Consolidated Financial Statements.

CONSOLIDATED STATEMENT OF CASH FLOWS

(in millions) (unaudited)

Nine Months Ended September 30,	2006	2005
Summary:		
Net cash provided by (used in) operating activities	**$ 6,004**	$ 20,190
Net cash used in investing activities	**(51,400)**	(52,577)
Net cash provided by financing activities	**44,865**	32,576
Effect of exchange rate changes on cash	**59**	(90)
Change in cash	**(472)**	99
Cash at beginning of period	**1,897**	2,009
Cash at end of period	**$ 1,425**	$ 2,108
Cash flows from operating activities:		
Net income	**$ 10,609**	$ 10,033
Adjustments to reconcile net income to net cash provided by (used in) operating activities:		
Noncash revenues, expenses, gains and losses included in income:		
Realized capital (gains) losses	**394**	296
Foreign exchange transaction (gains) losses	**845**	(2,889)
Equity in income of partially owned companies and other invested assets	**(2,655)**	(1,217)
Amortization of premium and discount on securities	**100**	357
Depreciation expenses, principally flight equipment	**1,743**	1,311
Provision for finance receivable losses	**329**	315
Changes in operating assets and liabilities:		
General and life insurance reserves	**10,507**	17,257
Premiums and insurance balances receivable and payable – net	**(173)**	89
Reinsurance assets	**614**	(2,163)
Deferred policy acquisition costs	**(3,210)**	(2,351)
Investment income due and accrued	**(475)**	(399)
Funds held under reinsurance treaties	**(1,732)**	544
Other policyholders' funds	**(510)**	613
Income taxes payable	**1,905**	2,532
Commissions, expenses and taxes payable	**356**	516
Other assets and liabilities – net	**(120)**	1,233
Bonds, common and preferred stocks trading, at market value	**(4,410)**	(3,532)
Trading assets and liabilities – net	**(622)**	1,711
Trading securities, at market value	**677**	(3,532)
Spot commodities	**(26)**	82
Net unrealized (gain) loss on swaps, options and forward transactions	**(966)**	694
Securities purchased under agreements to resell	**(12,494)**	14,143
Securities sold under agreements to repurchase	**4,024**	(12,887)
Securities and spot commodities sold but not yet purchased, at market value	**(330)**	249
Finance receivables held for sale – originations and purchases	**(7,965)**	(9,111)
Sales of finance receivables – held for sale	**7,888**	8,409
Other – net	**1,701**	(2,113)
Total adjustments	**(4,605)**	10,157
Net cash provided by (used in) operating activities	**$ 6,004**	$ 20,190

See Accompanying Notes to Consolidated Financial Statements.

CONSOLIDATED STATEMENT OF CASH FLOWS *(continued)*

(in millions) (unaudited)

Nine Months Ended September 30,	2006	2005
Cash flows from investing activities:		
Cost of bonds, at market sold	**$ 70,737**	$ 93,690
Cost of bonds, at market matured or redeemed	**11,794**	12,553
Cost of equity securities sold	**8,891**	9,271
Realized capital gains (losses)	**(325)**	24
Sales of securities available for sale	**4,300**	4,913
Maturities of securities available for sale	**974**	2,190
Sales of flight equipment	**380**	376
Sales or distributions of other invested assets	**11,591**	7,480
Finance receivable principal payments received	**9,131**	8,842
Mortgage, policy, collateral and guaranteed loans payments received	**3,081**	2,715
Purchases of fixed maturity securities	**(98,852)**	(130,547)
Purchases of equity securities	**(11,032)**	(10,947)
Purchases of securities available for sale	**(8,162)**	(12,992)
Purchases of flight equipment	**(4,860)**	(5,482)
Purchases of other invested assets	**(11,935)**	(8,874)
Net additions to real estate and other assets	**(1,405)**	(1,398)
Finance receivables held for investment – originations and purchases	**(9,947)**	(13,021)
Mortgage, policy, collateral and guaranteed loans granted	**(5,793)**	(3,941)
Change in securities lending collateral	**(11,917)**	(8,458)
Change in short-term investments	**(8,051)**	1,029
Net cash used in investing activities	**$ (51,400)**	$ (52,577)
Cash flows from financing activities:		
Policyholders' contract deposits	**37,998**	39,254
Policyholders' contract withdrawals	**(30,475)**	(26,562)
Change in trust deposits and deposits due to banks and other depositors	**(64)**	7
Change in commercial paper	**3,216**	21
Proceeds from notes, bonds, loans and mortgages payable, and hybrid financial instrument liabilities	**40,345**	43,791
Repayments on notes, bonds, loans and mortgages payable, and hybrid financial instrument liabilities	**(16,851)**	(32,929)
Proceeds from issuance of guaranteed investment agreements	**9,411**	9,743
Maturities of guaranteed investment agreements	**(9,480)**	(8,059)
Change in securities lending payable	**11,855**	8,458
Proceeds from issuance of common stock	**94**	44
Cash dividends paid to shareholders	**(1,209)**	(1,031)
Acquisition of treasury stock	**(7)**	(170)
Other – net	**32**	9
Net cash provided by financing activities	**$ 44,865**	$ 32,576
Supplementary disclosure of cash flow information:		
Cash paid during the period for:		
Interest	**$ 4,254**	$ 3,587
Taxes	**$ 3,252**	$ 2,031
Non-cash activity:		
Interest credited to policyholder accounts included in financing activities	**$ 7,253**	$ 7,074

See Accompanying Notes to Consolidated Financial Statements.

CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME (LOSS)

(in millions, except per share data) (unaudited)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2006	2005	**2006**	2005
Net income	**$ 4,224**	$ 1,745	**$10,609**	$10,033
Other comprehensive income (loss):				
Unrealized appreciation (depreciation) of investments – net of reclassification adjustments	**7,200**	(2,493)	**(1,133)**	(211)
Deferred income tax benefit (expense) on above changes	**(2,562)**	993	**281**	490
Foreign currency translation adjustments	**(115)**	222	**955**	(604)
Deferred income tax benefit (expense) on above changes	**17**	(379)	**(332)**	122
Net derivative gains (losses) arising from cash flow hedging activities	**4**	(63)	**12**	7
Deferred income tax (expense) benefit on above changes	**(1)**	90	**(4)**	19
Retirement plan liabilities adjustment, net of tax	**—**	(42)	**(2)**	(70)
Other comprehensive income (loss)	**4,543**	(1,672)	**(223)**	(247)
Comprehensive income (loss)	**$ 8,767**	$ 73	**$10,386**	$ 9,786

See Accompanying Notes to Consolidated Financial Statements.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited)*

1. Financial Statement Presentation

These unaudited condensed consolidated financial statements do not include certain financial information required by U.S. generally accepted accounting principles (GAAP) for complete financial statements and should be read in conjunction with the audited consolidated financial statements and the related notes included in the Annual Report on Form 10-K/A of American International Group, Inc. (AIG) for the year ended December 31, 2005 (2005 Annual Report on Form 10-K/A).

In the opinion of management, these consolidated financial statements contain the normal recurring adjustments necessary for a fair statement of the results presented herein. All material intercompany accounts and transactions have been eliminated. Certain accounts have been reclassified in the 2005 financial statements to conform to their 2006 presentation. See also Note 11 herein.

Information with respect to the three and nine months ended September 30, 2005 includes the effects of corrections and reclassifications made in conjunction with the Second Restatement. See also AIG's 2005 Annual Report on Form 10-K/A.

2. Segment Information

AIG identifies its reportable segments by product line consistent with its management structure. AIG's major product and service groupings are general insurance, life insurance & retirement services, financial services and asset management. **The following table summarizes the operations by major operating segment for the three and nine-month periods ended September 30, 2006 and 2005:**

Operating Segments	**Three Months Ended September 30,**		**Nine Months Ended September 30,**	
(in millions)	**2006**	2005	**2006**	2005
Revenues[a]:				
General Insurance[b][h]	**$12,615**	$11,192	**$36,438**	$33,816
Life Insurance & Retirement Services[c][h]	**12,356**	11,760	**36,819**	35,086
Financial Services[d]	**3,187**	1,926	**6,028**	8,140
Asset Management[e]	**1,238**	1,355	**4,098**	3,951
Other	**(197)**	175	**(182)**	520
Consolidated	**$29,199**	$26,408	**$83,201**	$81,513
Operating income (loss)[a][f][i][j]:				
General Insurance[h]	**$ 2,625**	$ (137)	**$ 7,819**	$ 3,390
Life Insurance & Retirement Services[g][h]	**2,448**	2,248	**7,424**	6,787
Financial Services[g]	**1,357**	224	**650**	3,483
Asset Management	**341**	568	**1,613**	1,682
Other[k]	**(470)**	(356)	**(1,171)**	(445)
Consolidated	**$ 6,301**	$ 2,547	**$16,335**	$14,897

(a) Includes the effect of hedging activities that do not qualify for hedge accounting treatment under FAS 133, including the related foreign exchange gains and losses. For the three-month periods ended September 30, 2006 and 2005, the effect was $165 million and $(353) million, respectively, in revenues and $165 million and $(345) million, respectively, in operating income. For the nine-month periods ended September 30, 2006 and 2005, the effect was $(1.13) billion and $2.21 billion, respectively, in revenues and $(1.13) billion and $2.28 billion, respectively, in operating income. These amounts result primarily from interest rate and foreign currency derivatives which are hedging available for sale securities and borrowings.

(b) Represents the sum of General Insurance net premiums earned, net investment income and realized capital gains (losses).

(c) Represents the sum of Life Insurance & Retirement Services GAAP premiums, net investment income and realized capital gains (losses). Included in realized capital gains (losses) is the effect of hedging activities that do not qualify for hedge accounting treatment under FAS 133 and foreign exchange gains (losses) of $(190) million and $(264) million in the three-month periods ended September 30, 2006 and 2005, respectively, and $145 million and $(447) million in the nine-month periods ended September 30, 2006 and 2005, respectively.

(d) Represents interest, lease and finance charges.

(e) Represents net investment income with respect to Guaranteed Investment Contracts (GICs) and management and advisory fees.

(f) Represents income before income taxes, minority interest and cumulative effect of an accounting change.

(g) Results of operations of AIG Credit Card Company (Taiwan) are shared equally by the Life Insurance & Retirement Services segment and the Financial Services segment. Additional allowances of $44 million were recorded in the first quarter of 2006, by each segment, for losses in these credit card operations.

(h) Includes the effect of out of period adjustments related to the accounting for certain interests in unit investment trusts and other mutual funds (unit investment trusts). For the three and nine-month periods ended September 30, 2006 the effect was an increase of $92 million and $524 million, respectively, in both revenues and operating income for General Insurance and an increase of $24 million in both revenues and operating income for the three-month period ended September 30, 2006 and $245 million and $168 million in revenues and operating income, respectively, for the nine-month period ended September 30, 2006, for Life Insurance & Retirement Services.

(i) Includes current year catastrophe related losses of $2.44 billion in both the third quarter and first nine months of 2005. There were no significant catastrophe related losses in the third quarter and first nine months of 2006.

(j) Includes additional losses incurred and net reinstatement premiums related to prior year catastrophes of $28 million and $39 million in the three-month periods ended September 30, 2006 and 2005, respectively. Such losses and premiums were $87 million and $252 million in the nine-month periods ended September 30, 2006 and 2005, respectively.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

2. Segment Information *(continued)*

(k) The operating loss for the Other category is as follows:

(in millions)	Three Months Ended September 30, 2006	Three Months Ended September 30, 2005	Nine Months Ended September 30, 2006	Nine Months Ended September 30, 2005
Operating income (loss):				
Equity earnings in unconsolidated subsidiaries*	**$ 48**	$ (205)	**$ 178**	$ (109)
Compensation expense – SICO Plans	**(14)**	(63)	**(104)**	(130)
Compensation expense – C.V. Starr tender offer	**–**	–	**(54)**	–
Interest expense	**(227)**	(131)	**(633)**	(382)
Unallocated corporate expenses	**(95)**	(92)	**(356)**	(287)
Realized capital gains (losses)	**(197)**	175	**(182)**	520
Other miscellaneous, net	**15**	(40)	**(20)**	(57)
Total Other	**$ (470)**	$ (356)	**$ (1,171)**	$ (445)

** Includes current year catastrophe related losses from unconsolidated subsidiaries of $246 million for both the third quarter and first nine months of 2005. There were no significant catastrophe related losses in the third quarter and first nine months of 2006. Also includes unfavorable development from unconsolidated subsidiaries related to prior year catastrophe related losses of $1 million and $15 million for the first nine months of 2006 and 2005, respectively.*

Each of the General Insurance sub-segments is comprised of groupings of major products and services as follows: Domestic Brokerage Group is comprised of domestic commercial insurance products and services; Transatlantic is comprised of reinsurance products and services sold to other general insurance and reinsurance companies; Personal Lines are comprised of general insurance products and services sold to individuals; Mortgage Guaranty is comprised of products insuring against losses arising under certain loan agreements; and Foreign General is comprised of general insurance products sold overseas.

The following table summarizes AIG's General Insurance operations by major internal reporting unit for the three and nine-month periods ended September 30, 2006 and 2005:

General Insurance *(in millions)*	Three Months Ended September 30, 2006	Three Months Ended September 30, 2005	Nine Months Ended September 30, 2006	Nine Months Ended September 30, 2005
Revenues[a]:				
Domestic Brokerage Group	**$ 7,196**	$ 6,282	**$20,356**	$18,812
Transatlantic	**1,004**	944	**3,035**	2,874
Personal Lines	**1,214**	1,235	**3,652**	3,615
Mortgage Guaranty	**226**	146	**636**	488
Foreign General	**2,975**	2,580	**8,757**	8,017
Reclassifications and eliminations	**–**	5	**2**	10
Total General Insurance	**$12,615**	$11,192	**$36,438**	$33,816
Operating income (loss)[b][c]:				
Domestic Brokerage Group	**$ 1,557**	(283)	**$ 4,448**	$ 1,235
Transatlantic	**143**	(275)	**427**	(62)
Personal Lines	**133**	18	**352**	229
Mortgage Guaranty	**85**	72	**301**	285
Foreign General[a]	**707**	326	**2,289**	1,693
Reclassifications and eliminations	**–**	5	**2**	10
Total General Insurance	**$ 2,625**	$ (137)	**$ 7,819**	$ 3,390

[a] *Includes the effect of out of period adjustments related to the accounting for certain interests in unit investment trusts. For the three and nine-month periods ended September 30, 2006 the effect was an increase of $92 million and $524 million, respectively, in both revenues and operating income.*

[b] *Includes current year catastrophe related losses of $2.11 billion for both the three and nine-month periods ended September 30, 2005. There were no significant catastrophe related losses in the third quarter and first nine months of 2006.*

[c] *Includes additional losses incurred and net reinstatement premiums related to prior year catastrophes of $50 million and $39 million in the three-month periods ended September 30, 2006 and 2005, respectively. Such losses and premiums were $108 million and $237 million in the nine-month periods ended September 30, 2006 and 2005, respectively.*

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

2. Segment Information *(continued)*

Life Insurance & Retirement Services is comprised of two major groupings of products and services: insurance-oriented products and services and retirement savings products and services. Substantially all of the retirement savings products are reported in the VALIC, AIG Annuity and AIG SunAmerica sub-segment.

The following table summarizes AIG's Life Insurance & Retirement Services operations by major internal reporting unit for the three and nine-month periods ended September 30, 2006 and 2005:

Life Insurance & Retirement Services	**Three Months Ended September 30,**		**Nine Months Ended September 30,**	
(in millions)	**2006**	2005	**2006**	2005
Revenues:				
Foreign:				
AIA, AIRCO and Nan Shan[(a) (e)]	**$ 3,998**	$ 3,640	**$12,515**	$11,564
ALICO, AIG Star Life and AIG Edison Life[(b) (f)]	**4,137**	3,955	**11,884**	11,083
Philamlife and Other	**127**	133	**404**	390
Domestic:				
AGLA and AG Life[(c)]	**2,259**	2,291	**6,848**	6,793
VALIC, AIG Annuity and AIG SunAmerica[(d)]	**1,835**	1,741	**5,168**	5,256
Total Life Insurance & Retirement Services	**$12,356**	$11,760	**$36,819**	$35,086
Operating Income:				
Foreign:				
AIA, AIRCO and Nan Shan[(a) (e)]	**$ 605**	$ 556	**$ 2,041**	$ 1,793
ALICO, AIG Star Life and AIG Edison Life[(b) (f)]	**969**	800	**2,882**	2,194
Philamlife and Other	**10**	14	**51**	47
Domestic:				
AGLA and AG Life[(c)]	**261**	352	**862**	1,058
VALIC, AIG Annuity and AIG SunAmerica[(d)]	**603**	526	**1,588**	1,695
Total Life Insurance & Retirement Services	**$ 2,448**	$ 2,248	**$ 7,424**	$ 6,787

(a) Represents the operations of American International Assurance Company, Limited together with American International Assurance Company (Bermuda) Limited (AIA), American International Reinsurance Company, Ltd. (AIRCO), and Nan Shan Life Insurance Company, Ltd. (Nan Shan). Revenues and operating income include realized capital gains (losses) of $(87) million and $(23) million for the three-month periods ended September 30, 2006 and 2005, respectively, and $111 million and $154 million for the nine-month periods ended September 30, 2006 and 2005, respectively. The effects of hedging activities that do not qualify for hedge accounting treatment under FAS 133, including the related foreign exchange gains and losses included in realized capital gains (losses) are losses of $102 million and $174 million for the three-month periods ended September 30, 2006 and 2005, respectively, and gains of $11 million and losses of $113 million for the nine-month periods ended September 30, 2006 and 2005, respectively. Includes $44 million in additional allowances for losses recorded in the first quarter of 2006 from AIG Credit Card Company (Taiwan).

(b) Represents the operations of American Life Insurance Company (ALICO), AIG Star Life Insurance Co., Ltd. (AIG Star Life), and AIG Edison Life Insurance Company (AIG Edison Life). Revenues and operating income include realized capital gains of $65 million and $44 million for the three-month periods ended September 30, 2006 and 2005, respectively, and gains of $376 million and losses of $85 million for the nine-month periods ended September 30, 2006 and 2005, respectively. The effects of hedging activities that do not qualify for hedge accounting treatment under FAS 133, including the related foreign exchange gains and losses included in realized capital gains (losses) are gains of $28 million and losses of $102 million for the three-month periods ended September 30, 2006 and 2005, respectively, and gains of $184 million and losses of $365 million for the nine-month periods ended September 30, 2006 and 2005, respectively.

(c) Includes the life operations of American General Life Insurance Company (AG Life), AIG Life Insurance Company and American International Life Assurance Company of New York. Also includes the operations of American General Life and Accident Insurance Company (AGLA). Revenues and operating income include realized capital gains (losses) of $(123) million and $41 million for the three-month periods ended September 30, 2006 and 2005, respectively, and losses of $190 million and $22 million for the nine-month periods ended September 30, 2006 and 2005, respectively. The effects of hedging activities that do not qualify for hedge accounting treatment under FAS 133, including the related foreign exchange gains and losses included in realized capital gains (losses) are losses of $104 million and gains of $122 million for the three-month periods ended September 30, 2006 and 2005, respectively, and gains of $11 million and $56 million for the nine-month periods ended September 30, 2006 and 2005, respectively.

(d) "AIG SunAmerica" represents the annuity operations of AIG SunAmerica Life Assurance Company, as well as those of First SunAmerica Life Insurance Company and SunAmerica Life Insurance Company. Also includes the operations of The Variable Annuity Life Insurance Company (VALIC) and AIG Annuity Insurance Company (AIG Annuity). Revenues and operating income include realized capital losses of $24 million and $83 million for the three-month periods ended September 30, 2006 and 2005, respectively, and losses of $414 million and $71 million for the nine-month periods ended September 30, 2006 and 2005, respectively. The effects of hedging activities that do not qualify for hedge accounting treatment under FAS 133, including the related foreign exchange gains and losses included in realized capital gains (losses) are $0 and losses of $110 million for the three month periods ended September 30, 2006 and 2005, respectively, and losses of $36 million and $25 million for the nine-month periods ended September 30, 2006 and 2005, respectively.

(e) Includes the effect of out of period adjustments related to the accounting for certain interests in unit investment trusts. For the three-month period ended September 30, 2006 the effect was an increase of $9 million in both revenues and operating income. For the nine-month period ended September 30, 2006 the effect was an increase of $230 million in revenues and $153 million in operating income.

(f) Includes the effect of out of period adjustments related to the accounting for certain interests in unit investment trusts. For the three and nine-month periods ended September 30, 2006 the effect was an increase of $15 million in both revenues and operating income.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

2. Segment Information *(continued)*

The following table summarizes AIG's Financial Services operations by major internal reporting unit for the three and nine-month periods ended September 30, 2006 and 2005:

Financial Services *(in millions)*	**Three Months Ended September 30,**		**Nine Months Ended September 30,**	
	2006	2005	**2006**	2005
Revenues[(a)]:				
Aircraft Finance[(b)]	**$1,060**	$ 943	**$ 3,067**	$2,661
Capital Markets[(c)(d)]	**1,118**	23	**30**	2,754
Consumer Finance[(e)]	**970**	940	**2,833**	2,664
Other	**39**	20	**98**	61
Total Financial Services	**$3,187**	$1,926	**$ 6,028**	$8,140
Operating income (loss)[(a)]:				
Aircraft Finance	**$ 157**	$ 165	**$ 475**	$ 476
Capital Markets[(d)]	**965**	(150)	**(457)**	2,306
Consumer Finance[(f)(g)]	**220**	190	**594**	649
Other	**15**	19	**38**	52
Total Financial Services	**$1,357**	$ 224	**$ 650**	$3,483

(a) Includes the effect of hedging activities that do not qualify for hedge accounting treatment under FAS 133, including the related foreign exchange gains and losses. For the three and nine-month periods ended September 30, 2005, the effect was $(10) million and $(59) million, respectively, in operating income for Aircraft Finance. During 2006, Aircraft Finance derivative gains and losses are reported as part of the Other category and not reported in Aircraft Finance operating income. For the three-month periods ended September 30, 2006 and 2005, the effect was $783 million and $(365) million in both revenues and operating income, respectively, for Capital Markets. For the nine-month periods ended September 30, 2006 and 2005, the effect was $(1.06) billion and $1.80 billion in both revenues and operating income, respectively, for Capital Markets. These amounts result primarily from interest rate and foreign currency derivatives which are hedging available for sale securities and borrowings.

(b) Revenues are primarily aircraft lease rentals from International Lease Finance Corporation (ILFC).

(c) Revenues, shown net of interest expense, are primarily from hedged financial positions entered into in connection with counterparty transactions and the effect of hedging activities that do not qualify for hedge accounting treatment under FAS 133 described in (a) above.

(d) Certain transactions entered into by AIGFP generate tax credits and benefits which are included in income taxes in the consolidated statement of income. The amount of such tax credits and benefits for the three-month periods ended September 30, 2006 and 2005 are $3 million and $23 million, respectively. The amount of such tax credits and benefits for the nine-month periods ended September 30, 2006 and 2005 are $29 million and $63 million, respectively.

(e) Revenues are primarily finance charges.

(f) Includes $44 million in additional allowances for losses recorded in the first quarter of 2006 from AIG Credit Card Company (Taiwan).

(g) Includes catastrophe related losses of $62 million recorded in the third quarter of 2005 resulting from hurricane Katrina, which were reduced by $22 million in the third quarter of 2006.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

2. Segment Information *(continued)*

The following table summarizes AIG's Asset Management revenues and operating income for the three and nine-month periods ended September 30, 2006 and 2005:

Asset Management *(in millions)*	**Three Months Ended September 30, 2006**	2005	**Nine Months Ended September 30, 2006**	2005
Revenues:				
Guaranteed Investment Contracts	**$ 845**	$ 908	**$2,517**	$2,707
Institutional Asset Management	**265**	279	**1,163**	776
Brokerage Services and Mutual Funds	**71**	67	**217**	192
Other	**57**	101	**201**	276
Total Asset Management	**$1,238**	$1,355	**$4,098**	$3,951
Operating income:				
Guaranteed Investment Contracts[(a)]	**$ 175**	$ 294	**$ 635**	$ 939
Institutional Asset Management[(b)(c)]	**89**	155	**721**	424
Brokerage Services and Mutual Funds	**23**	20	**67**	50
Other	**54**	99	**190**	269
Total Asset Management	**$ 341**	$ 568	**$1,613**	$1,682

(a) Includes the effect of hedging activities that do not qualify for hedge accounting treatment under FAS 133, including the related foreign exchange gains and losses. For the three and nine-month periods ended September 30, 2005, the effect was $18 million and $127 million, respectively, in operating income. During 2006, these derivative gains and losses are reported as part of the Other category, and not reported in Asset Management operating income.

(b) Includes the full results of certain AIG managed private equity and real estate funds that are consolidated pursuant to FIN 46(R), "Consolidation of Variable Interest Entities". Also includes $(3) million and $77 million for the three-month periods ended September 30, 2006 and 2005, respectively, and $207 million and $189 million for the nine-month periods ended September 30, 2006 and 2005, respectively, of third-party limited partner earnings offset in minority interest expense, which is not a component of operating income.

(c) Includes the full results of certain AIG managed partnerships that are consolidated effective January 1, 2006 pursuant to EITF 04-5, "Determining Whether a General Partner, or the General Partners as a Group, Controls a Limited Partnership or Similar Entity When the Limited Partners Have Certain Rights." For the three and nine-month periods ended September 30, 2006, operating income includes $47 million and $203 million, respectively, of third-party limited partner earnings offset in minority interest expense, which is not a component of operating income.

3. Earnings Per Share

Earnings per share of AIG are based on the weighted average number of common shares outstanding during the period. See also Note 10 herein.

Computation of Earnings Per Share (EPS):

(in millions, except per share data)	**Three Months Ended September 30, 2006**	2005	**Nine Months Ended September 30, 2006**	2005
Numerator for earnings per share:				
Income before cumulative effect of an accounting change	**$4,224**	$1,745	**$10,575**	$10,033
Cumulative effect of an accounting change, net of tax	**–**	–	**34**	–
Net income applicable to common stock for basic EPS	**$4,224**	$1,745	**$10,609**	$10,033
Interest on contingently convertible bonds, net of tax[(a)]	**2**	3	**8**	8
Net income applicable to common stock for diluted EPS	**$4,226**	$1,748	**$10,617**	$10,041
Cumulative effect of an accounting change, net of tax	**–**	–	**34**	–
Income before cumulative effect of an accounting change applicable to common stock for diluted EPS	**$4,226**	$1,748	**$10,583**	$10,041
Denominator for earnings per share:				
Weighted-average shares outstanding used in the computation of EPS:				
Common stock issued	**2,751**	2,751	**2,751**	2,751
Common stock in treasury	**(153)**	(155)	**(153)**	(155)
Deferred shares	**9**	1	**9**	1

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

3. Earnings Per Share *(continued)*

(in millions, except per share data)	Three Months Ended September 30, 2006	Three Months Ended September 30, 2005	Nine Months Ended September 30, 2006	Nine Months Ended September 30, 2005
Weighted-average shares outstanding — basic	**2,607**	2,597	**2,607**	2,597
Incremental shares from potential common stock:				
Weighted-average number of shares arising from outstanding employee stock plans (treasury stock method)[(b)]	**10**	18	**9**	18
Contingently convertible bonds[(a)]	**9**	9	**9**	9
Weighted-adjusted average shares outstanding — diluted[(b)]	**2,626**	2,624	**2,625**	2,624
Earnings per share:				
Basic:				
Income before cumulative effect of an accounting change	**$ 1.62**	$ 0.67	**$ 4.06**	$ 3.86
Cumulative effect of an accounting change, net of tax	**–**	–	**0.01**	–
Net Income	**$ 1.62**	$ 0.67	**$ 4.07**	$ 3.86
Diluted:				
Income before cumulative effect of an accounting change	**$ 1.61**	$ 0.66	**$ 4.03**	$ 3.82
Cumulative effect on an accounting change, net of tax	**–**	–	**0.01**	–
Net income	**$ 1.61**	$ 0.66	**$ 4.04**	$ 3.82

(a) Assumes conversion of contingently convertible bonds due to the adoption of EITF Issue No. 04-8 "Accounting Issues Related to Certain Features of Contingently Convertible Debt and the Effect on Diluted Earnings per Share."

(b) Certain share equivalents arising from employee stock plans were not included in the computation of diluted earnings per share where the exercise price of the options exceeded the average market price and would have been antidilutive. The number of share equivalents excluded were 14 million and 21 million for the first nine months of 2006 and 2005, respectively.

From time to time, AIG may buy shares of its common stock in the open market for general corporate purposes, including to satisfy its obligations under various employee benefit plans. At September 30, 2006 and December 31, 2005, an additional 36,542,700 shares could be purchased under the then current authorization by AIG's Board of Directors. Although AIG has authorization to purchase additional shares, AIG has not repurchased shares in 2006. During the nine months ended September 30, 2005, AIG purchased in the open market 2,477,100 shares of its common stock, all of which were acquired in the first quarter.

The quarterly dividend rate per common share, commencing with the dividend declared in May 2006 and paid on September 15, 2006, is $0.165. The declared dividend amount of $0.175 for the three months ended September 30, 2005 includes a $0.025 increase to the amount previously declared in the second quarter of 2005 for payment in September 2005 as well as the $0.125 dividend declared in May 2005 for payment in September 2005.

4. Benefits Provided by Starr International Company, Inc. and C.V. Starr & Co., Inc.

Starr International Company, Inc. (SICO) has provided a series of two-year Deferred Compensation Profit Participation Plans (SICO Plans) to certain AIG employees. The SICO Plans came into being in 1975 when the voting shareholders and Board of Directors of SICO, a private holding company whose principal asset is AIG common stock, decided that a portion of the capital value of SICO should be used to provide an incentive plan for the current and succeeding managements of all American International companies, including AIG.

None of the costs of the various benefits provided under the SICO Plans has been paid by AIG, although AIG has recorded a charge to reported earnings for the deferred compensation amounts paid to AIG employees by SICO, with an offsetting amount credited to additional paid-in capital reflecting amounts deemed contributed by SICO. The SICO Plans provide that shares currently owned by SICO are set aside by SICO for the benefit of the participant and distributed upon retirement. The SICO Board of Directors currently may permit an early payout of units under certain circumstances. Prior to payout, the participant is not entitled to vote, dispose of or receive dividends with respect to such shares, and shares are subject to forfeiture under certain conditions, including but not limited to the participant's voluntary termination of employment with AIG prior to normal retirement age. Under the SICO Plans, SICO's Board of Directors may elect to pay a participant cash in lieu of shares of AIG common stock. Following notification from SICO to participants in the SICO Plans that it will settle specific future awards under the SICO Plans with shares rather than cash, AIG modified its accounting for the SICO Plans from variable to fixed measurement accounting, although variable accounting will continue to be applied where SICO makes cash pay-

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

4. Benefits Provided by Starr International Company, Inc. *(continued)*

ments pursuant to elections made prior to March 2005. AIG gave effect to this change in settlement method beginning on December 9, 2005, the date of SICO's notice to participants in the SICO Plans. See also Note 6(b) "Commitments" herein.

Compensation expense with respect to the SICO Plans aggregated $14 million and $62 million for the three-month periods ended September 30, 2006 and 2005, respectively, and $104 million and $129 million for the nine-month periods ended September 30, 2006 and 2005, respectively. Compensation expense in the first quarter of 2006 included various out of period adjustments totaling $61 million, primarily relating to stock-splits and other miscellaneous items. See also Note 10 herein.

In January 2006, C.V. Starr & Co., Inc. (Starr) completed its tender offer to purchase Starr interests from AIG employees. In conjunction with AIG's adoption of FAS 123R, Starr is considered to be an "economic interest holder" in AIG. As a result, compensation expense of $54 million recorded in the first quarter with respect to the Starr offer, was included in the first nine months of 2006.

As a result of its changing relationship with Starr and SICO, AIG has established new executive compensation plans to replace the SICO plans and investment opportunities previously provided by Starr. The replacement plans include both share-based plans and cash-based plans. In addition, these replacement plans generally include performance as well as service conditions. See also Note 10 herein.

5. Ownership and Transactions With Related Parties

(a) Ownership: According to the Schedule 13D filed on May 26, 2006 by Starr, SICO, Edward E. Matthews, Maurice R. Greenberg, the Maurice R. and Corinne P. Greenberg Family Foundation, Inc., the Universal Foundation, Inc. and the Maurice R. and Corinne P. Greenberg Joint Tenancy Company, LLC, these reporting persons could be deemed to beneficially own 393,157,543 shares of common stock at that date. Based on the shares of common stock outstanding as of October 31, 2006, this ownership would represent approximately 15 percent of the voting stock of AIG. Although these reporting persons have made filings under Section 16 of the Securities Exchange Act of 1934, as amended (the Exchange Act), reporting sales of shares of common stock, no amendment to the Schedule 13D has been filed to report a change in ownership.

(b) Transactions with Related Parties: In the ordinary course of business during the first nine months of 2006, AIG and its subsidiaries paid commissions to Starr and its subsidiaries for the production and management of insurance business. As of July 25, 2006, none of the Starr agencies serve as agents for AIG companies. There were no significant receivables from/payables to related parties at September 30, 2006.

6. Commitments, Contingencies and Guarantees

In the normal course of business, various commitments and contingent liabilities are entered into by AIG and certain of its subsidiaries. In addition, AIG guarantees various obligations of certain subsidiaries.

Litigation and Investigations

(a) AIG and its subsidiaries, in common with the insurance industry in general, are subject to litigation, including claims for punitive damages, in the normal course of their business. The trend of increasing jury awards and settlements makes it difficult to assess the ultimate outcome of such litigation.

Although AIG regularly reviews the adequacy of the established reserve for losses and loss expenses, there can be no assurance that AIG's ultimate loss reserves will not develop adversely and materially exceed AIG's current loss reserves. Estimation of ultimate net losses, loss expenses and loss reserves is a complex process for long-tail casualty lines of business, which include excess and umbrella liability, directors and officers liability (D&O), professional liability, medical malpractice, workers compensation, general liability, products liability and related classes, as well as for asbestos and environmental exposures. Generally, actual historical loss development factors are used to project future loss development. However, there can be no assurance that future loss development patterns will be the same as in the past. Moreover, any deviation in loss cost trends or in loss development factors might not be discernible for an extended period of time subsequent to the recording of the initial loss reserve estimates for any accident year. Thus, there is the potential for reserves with respect to a number of years to be significantly affected by changes in loss cost trends or loss development factors that were relied upon in setting the reserves. These changes in loss trends or loss development factors could be attributable to changes in inflation, in labor and material costs or in the judicial environment, or in other social or economic phenomena affecting claims.

(b) AIG and certain of its subsidiaries have been named defendants in two putative class actions in state court in Alabama that arise out of the 1999 settlement of class and derivative litigation involving Caremark Rx, Inc. (Caremark). An excess policy issued by a subsidiary of AIG with respect to the 1999 litigation was expressly stated to be without limit of liability. In the current actions, plaintiffs allege that the judge approving the 1999 settlement was misled as to the extent of

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

6. Commitments, Contingencies and Guarantees *(continued)*

available insurance coverage and would not have approved the settlement had he known of the existence and/or unlimited nature of the excess policy. They further allege that AIG, its subsidiaries, and Caremark are liable for fraud and suppression for misrepresenting and/or concealing the nature and extent of coverage. In their complaint, plaintiffs request compensatory damages for the 1999 class in the amount of $3.2 billion, plus punitive damages. AIG and its subsidiaries deny the allegations of fraud and suppression and have asserted, *inter alia*, that information concerning the excess policy was publicly disclosed months prior to the approval of the settlement. AIG and its subsidiaries further assert that the current claims are barred by the statute of limitations and that plaintiffs' assertions that the statute was tolled cannot stand against the public disclosure of the excess coverage. Plaintiffs, in turn, have asserted that the disclosure was insufficient to inform them of the nature of the coverage and did not start the running of the statute of limitations. On January 28, 2005, the Alabama trial court determined that one of the current actions may proceed as a class action on behalf of the 1999 classes that were allegedly defrauded by the settlement. AIG, its subsidiaries, and Caremark sought appellate relief from the Alabama Supreme Court, which was granted in substantial part in August 2006. The matter is in the process of being remanded to the trial court to proceed with a class certification determination under the standards set by the Alabama Supreme Court. AIG cannot now estimate either the likelihood of its prevailing in these actions or the potential damages in the event liability is determined.

(c) Regulators from several states have commenced investigations into insurance brokerage practices related to contingent commissions and other broker-related conduct, such as alleged bid rigging. Various parties, including insureds and shareholders, have also asserted putative class action and other claims against AIG or its subsidiaries alleging, among other things, violations of the antitrust and federal securities laws, and AIG expects that additional claims may be made.

In February 2006, AIG reached a resolution of claims and matters under investigation with the United States Department of Justice (DOJ), the Securities and Exchange Commission (SEC), the Office of the New York Attorney General (NYAG) and the New York State Department of Insurance (DOI). The settlements resolved outstanding litigation filed by the SEC, NYAG and DOI against AIG and concluded negotiations with these authorities and the DOJ in connection with the accounting, financial reporting and insurance brokerage practices of AIG and its subsidiaries, as well as claims relating to the underpayment of certain workers compensation premium taxes and other assessments. In the fourth quarter of 2005 AIG recorded an after-tax charge of $1.15 billion for the settlements.

As a result of these settlements, AIG made payments or placed amounts in escrow in the first nine months of 2006 totaling approximately $1.64 billion, $225 million of which represented fines and penalties. Amounts held in escrow totaling $692 million, including interest thereon, are included in other assets and other liabilities at September 30, 2006. A substantial portion of the money will be available to resolve claims asserted in various regulatory and civil proceedings, including shareholder lawsuits.

Also, as part of the settlements, AIG has agreed to retain for a period of three years an independent consultant who will conduct a review that will include the adequacy of AIG's internal control over financial reporting and the remediation plan that AIG has implemented as a result of its own internal review.

Various federal and state regulatory agencies are reviewing certain transactions and practices of AIG and its subsidiaries in connection with industry-wide and other inquiries. AIG has cooperated, and will continue to cooperate, in producing documents and other information in response to the subpoenas.

A number of lawsuits have been filed regarding the subject matter of the investigations of insurance brokerage practices, including derivative actions, individual actions and class actions under the federal securities laws, Racketeer Influenced and Corrupt Organizations Act (RICO), Employee Retirement Income Security Act (ERISA) and state common and corporate laws in both federal and state courts, including the United States District Court for the Southern District of New York (Southern District of New York), in the Commonwealth of Massachusetts Superior Court and in Delaware Chancery Court. All of these actions generally allege that AIG and its subsidiaries violated the law by allegedly concealing a scheme to "rig bids" and "steer" business between insurance companies and insurance brokers.

Since October 19, 2004, AIG or its subsidiaries have been named as a defendant in eighteen complaints that were filed in federal court and two that were originally filed in state court (Massachusetts and Florida) and removed to federal court. These cases generally allege that AIG and its subsidiaries violated federal and various state antitrust laws, as well as federal RICO laws, various state deceptive and unfair practice laws and certain state laws governing fiduciary duties. The alleged basis of these claims is that there was a conspiracy between insurance companies and insurance brokers with regard to the use of contingent commission agreements, bidding practices, and other broker-related conduct concerning coverage in certain sectors of the insurance industry. The Judicial Panel on Multidistrict Litigation entered an

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

6. Commitments, Contingencies and Guarantees *(continued)*

order on February 17, 2005, consolidating most of these cases and transferring them to the United States District Court for the District of New Jersey (District of New Jersey). The remainder of these cases have been transferred to the District of New Jersey. On August 15, 2005, the plaintiffs in the multidistrict litigation filed a Corrected First Consolidated Amended Commercial Class Action Complaint, which, in addition to the previously named AIG defendants, names new AIG subsidiaries as defendants. Also on August 15, 2005, AIG and two subsidiaries were named as defendants in a Corrected First Consolidated Amended Employee Benefits Class Action Complaint filed in the District of New Jersey, which asserts similar claims with respect to employee benefits insurance and a claim under ERISA on behalf of putative classes of employers and employees.

On November 29, 2005, the AIG defendants, along with other insurer defendants and the broker defendants filed motions to dismiss both the Commercial and Employee Benefits Complaints. On October 3, 2006, the Court reserved in part and denied in part the motions to dismiss. The Court denied the motions to dismiss the ERISA claims, but ordered an expedited discovery schedule, and the Court reserved on the state law claims. Plaintiffs have filed a motion for class certification in the consolidated action, in response to which defendants have filed an opposition. In addition, complaints were filed against AIG and several of its subsidiaries in Massachusetts and Florida state courts, which have both been stayed. In the Florida action, the plaintiff filed a petition for a writ of certiorari with the District Court of Appeals of the State of Florida, Fourth District with respect to the stay order which was granted on August 16, 2006. The Fourth District Court remanded to the trial court to reconsider whether a stay should be granted. On February 9, 2006, a complaint against AIG and several of its subsidiaries was filed in Texas state court, making claims similar to those in the federal cases above. On October 17, 2006, the court stayed the case until January 31, 2007.

In April and May 2005, amended complaints were filed in the consolidated derivative and securities cases, as well as in one of the ERISA lawsuits, pending in the Southern District of New York adding allegations concerning AIG's accounting treatment for non-traditional insurance products.

In September 2005, a second amended complaint was filed in the consolidated securities cases adding allegations concerning AIG's first restatement of its financial statements described in the 2005 Annual Report on Form 10-K (the "First Restatement"), and a new securities action complaint was filed in the Southern District of New York, asserting claims premised on the same allegations made in the consolidated cases. In April 2006, motions to dismiss were denied in the securities actions. AIG filed answers in both securities actions in June 2006, as did other defendants.

Also in September 2005, a class action complaint was filed to consolidate the ERISA cases pending in the Southern District of New York. Motions to dismiss in the consolidated action were filed in January 2006.

In April 2005, new derivative actions were filed in Delaware Chancery Court, and in July and August 2005, two new derivative actions were filed in the Southern District of New York asserting claims duplicative of the claims made in the consolidated derivative action.

In July 2005, a second amended complaint was filed in the consolidated derivative case in the Southern District of New York, expanding upon accounting-related allegations, based upon the First Restatement. In June 2005, the derivative cases in Delaware were consolidated and, in August 2005, an amended consolidated complaint was filed. AIG's Board of Directors has appointed a special committee of independent directors to review the matters asserted in the derivative complaints. The courts have approved agreements staying the derivative cases pending in the Southern District of New York and in Delaware Chancery Court while the special committee of independent directors performs its work. In September 2005, a shareholder filed suit in Delaware Chancery Court seeking documents relating to some of the allegations made in the derivative suits. The court approved a stipulation dismissing that action on May 15, 2006.

On June 20, 2006, SICO filed suit in Delaware Chancery Court seeking the inspection of certain books and records of AIG. The Chancery court has dismissed the action with prejudice by agreement of the parties.

In late 2002, a derivative action was filed in Delaware Chancery Court in connection with AIG's transactions with certain entities affiliated with Starr and SICO. In May 2005, the plaintiff filed an amended complaint which adds additional claims premised on allegations relating to insurance brokerage practices and AIG's non-traditional insurance products. On February 16, 2006, the Delaware Chancery Court entered an order dismissing the litigation with prejudice with respect to AIG's outside directors and dismissing the claims against the remaining AIG defendants without prejudice. In response to an order, dated July 5, 2006, dismissing certain of its claims, the plaintiff filed a second amended complaint on July 21, 2006, which adds additional claims against Starr. Defendants filed answers in September 2006.

AIG cannot predict the outcome of the matters described above or estimate the potential costs related to these matters and, accordingly, no reserve is being established in AIG's financial statements at this time. In the opinion of AIG man-

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

6. Commitments, Contingencies and Guarantees *(continued)*

agement, AIG's ultimate liability for the matters referred to above is not likely to have a material adverse effect on AIG's consolidated financial condition, although it is possible that the effect would be material to AIG's consolidated results of operations for an individual reporting period.

(d) On July 8, 2005, SICO filed a complaint against AIG in the Southern District of New York. The complaint alleges that AIG is in the possession of items, including artwork, which SICO claims it owns, and seeks an order causing AIG to release those items as well as actual, consequential, punitive and exemplary damages. On September 27, 2005, AIG filed its answer to SICO's complaint denying SICO's allegations and asserting counter-claims for breach of contract, unjust enrichment, conversion and breach of fiduciary duty relating to SICO's breach of its commitment to use its AIG shares for the benefit of AIG and its employees. On October 17, 2005, SICO replied to AIG's counter-claims and additionally sought a judgment declaring that SICO is neither a control person nor an affiliate of AIG for purposes of Schedule 13D under the Exchange Act, or Rule 144 under the Securities Act of 1933, as amended (the Securities Act), respectively. AIG responded to the SICO claims on November 7, 2005.

(e) AIG understands that some of its employees have received Wells notices in connection with previously disclosed SEC investigations of certain of AIG's transactions or accounting practices. Under SEC procedures, a Wells notice is an indication that the SEC staff has made a preliminary decision to recommend enforcement action that provides recipients with an opportunity to respond to the SEC staff before a formal recommendation is finalized. AIG anticipates that additional current and former employees could receive similar notices in the future as the regulatory investigations proceed.

Commitments

(a) At September 30, 2006, ILFC had committed to purchase 268 new aircraft deliverable from 2006 through 2015 at an estimated aggregate purchase price of $19.2 billion and had options to purchase three new aircraft at an estimated aggregate purchase price of $453 million. ILFC will be required to find customers for any aircraft acquired, and it must arrange financing for portions of the purchase price of such equipment.

(b) On June 27, 2005, AIG entered into an agreement pursuant to which AIG agrees, subject to certain conditions, to make any payment that is not promptly paid with respect to the benefits accrued by certain employees of AIG and its subsidiaries under the SICO Plans (as defined in Note 4).

Contingencies

(a) On December 30, 2004, an arbitration panel issued its ruling in connection with a 1998 workers compensation quota share reinsurance agreement under which Superior National Insurance Company, among others, was reinsured by The United States Life Insurance Company in the City of New York (USLIFE), a subsidiary of American General Corporation. In its 2-1 ruling, the arbitration panel refused to rescind the contract as requested by USLIFE. Instead, the panel reformed the contract to reduce USLIFE's participation by ten percent. USLIFE is pursuing certain reinsurance recoverables in connection with the contract. Further, the arbitration ruling established a second phase of arbitration for USLIFE to present its challenges to certain cessions to the contract. AIG holds a reserve of approximately $379 million related to this matter as of September 30, 2006.

(b) AIG generates income tax credits as a result of investing in synthetic fuel production. Tax credits generated from the production and sale of synthetic fuel under the Internal Revenue Code are subject to an annual phase-out provision that is based on the average wellhead price of domestic crude oil. The price range within which the tax credits are phased-out was originally established in 1980 and is adjusted annually for inflation. Depending on the price of domestic crude oil for a particular year, all or a portion of the tax credits generated in that year might be eliminated. Tax credits reflected in the income tax provision for the first nine months of 2006 have been reduced to reflect an estimated phase-out of the tax credits from 2006 synthetic fuel production based on the observed price of domestic crude oil. Since the phase-out of tax credits from 2006 synthetic fuel production will depend on the average wellhead price of domestic crude oil for the entire 2006 calendar year, it is not possible to determine the extent to which the 2006 tax credits actually will be phased-out. As a result, the actual level of tax credits from 2006 synthetic fuel production may be higher or lower than the current estimate. AIG evaluates the production levels of its synthetic fuel production facilities in light of the risk of phase-out of the associated tax credits. As a result of fluctuating domestic crude oil prices, AIG intends to evaluate and possibly adjust production levels in light of this risk for the remainder of 2006. Regardless of oil prices, the tax credits expire after 2007.

Guarantees

(a) AIG and certain of its subsidiaries become parties to derivative financial instruments with market risk resulting from both dealer and end user activities and to reduce currency, interest rate, equity and commodity exposures. These instruments are carried at their estimated fair values in the consolidated balance sheet. The vast majority of AIG's derivative activity is transacted by AIGFP. (See also Note 20 of Notes to

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

6. Commitments, Contingencies and Guarantees *(continued)*

Consolidated Financial Statements in AIG's 2005 Annual Report on Form 10-K/A.)

(b) AIG has issued unconditional guarantees with respect to the prompt payment, when due, of all present and future payment obligations and liabilities of AIGFP arising from transactions entered into by AIGFP.

(c) SAI Deferred Compensation Holdings, Inc., a wholly-owned subsidiary of AIG, has established a deferred compensation plan for registered representatives of certain AIG subsidiaries, pursuant to which participants have the opportunity to invest deferred commissions and fees on a notional basis. The value of the deferred compensation fluctuates with the value of the deferred investment alternatives chosen. AIG has provided a full and unconditional guarantee of the obligations of SAI Deferred Compensation Holdings, Inc. to pay the deferred compensation under the plan.

7. Employee Benefits

The following table presents the components of the net periodic benefit costs with respect to pensions and postretirement benefits for the three and nine-month periods ended September 30, 2006 and 2005:

	Pensions			Postretirement		
(in millions)	Non-U.S. Plans	U.S. Plans	Total	Non-U.S. Plans	U.S. Plans	Total
Three Months Ended September 30, 2006						
Components of net period benefit cost:						
Service cost	**$ 18**	**$ 32**	**$ 50**	**$ 1**	**$ 1**	**$ 2**
Interest cost	**9**	**41**	**50**	**1**	**3**	**4**
Expected return on assets	**(7)**	**(48)**	**(55)**	**–**	**–**	**–**
Amortization of prior service cost	**(3)**	**(1)**	**(4)**	**–**	**(2)**	**(2)**
Amortization of transitional liability	**1**	**–**	**1**	**–**	**–**	**–**
Recognized actuarial loss	**4**	**18**	**22**	**–**	**–**	**–**
Net period benefit cost	**$ 22**	**$ 42**	**$ 64**	**$ 2**	**$ 2**	**$ 4**
Three Months Ended September 30, 2005						
Components of net period benefit cost:						
Service cost	$ 19	$ 26	$ 45	$ 1	$ 2	$ 3
Interest cost	8	37	45	–	4	4
Expected return on assets	(5)	(41)	(46)	–	–	–
Amortization of prior service cost	(3)	–	(3)	–	(2)	(2)
Loss due to settlements	1	–	1	–	–	–
Recognized actuarial loss	6	16	22	–	1	1
Net period benefit cost	$ 26	$ 38	$ 64	$ 1	$ 5	$ 6
Nine Months Ended September 30, 2006						
Components of net period benefit cost:						
Service cost	**$ 55**	**$ 94**	**$ 149**	**$ 3**	**$ 4**	**$ 7**
Interest cost	**26**	**122**	**148**	**2**	**8**	**10**
Expected return on assets	**(21)**	**(145)**	**(166)**	**–**	**–**	**–**
Amortization of prior service cost	**(7)**	**(2)**	**(9)**	**–**	**(5)**	**(5)**
Amortization of transitional liability	**1**	**–**	**1**	**–**	**–**	**–**
Recognized actuarial loss	**12**	**56**	**68**	**–**	**–**	**–**
Net period benefit cost	**$ 66**	**$ 125**	**$ 191**	**$ 5**	**$ 7**	**$ 12**
Nine Months Ended September 30, 2005						
Components of net period benefit cost:						
Service cost	$ 56	$ 78	$ 134	$ 3	$ 5	$ 8
Interest cost	24	111	135	1	11	12
Expected return on assets	(16)	(123)	(139)	–	–	–
Amortization of prior service cost	(8)	(2)	(10)	–	(5)	(5)
Loss due to settlements	4	–	4	–	–	–
Amortization of transition liability	1	–	1	–	–	–
Recognized actuarial loss	17	49	66	–	2	2
Net period benefit cost	$ 78	$ 113	$ 191	$ 4	$ 13	$ 17

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

8. Recent Accounting Standards

Accounting Changes

At the March 2004 meeting, the Emerging Issue Task Force (EITF) reached a consensus with respect to Issue No. 03-1, "The Meaning of Other-Than-Temporary Impairment and Its Application to Certain Investments." On September 30, 2004, the Financial Accounting Standards Board (FASB) issued FASB Staff Position (FSP) EITF No. 03-1-1, Effective Date of Paragraphs 10-20 of EITF Issue No. 03-1, "The Meaning of Other-Than-Temporary Impairment and Its Application to Certain Investments" delaying the effective date of this guidance until the FASB has resolved certain implementation issues with respect to this guidance, but the disclosures remain effective. This FSP, retitled FSP FAS 115-1, "The Meaning of Other-Than-Temporary Impairment and Its Application to Certain Investments," replaces the measurement and recognition guidance set forth in Issue No. 03-1 and codifies certain existing guidance on impairment and accretion of income. AIG's adoption of FSP FAS 115-1 on January 1, 2006 did not have a material effect on AIG's consolidated financial condition or results of operations.

In December 2004, the FASB issued Statement No. 123 (revised 2004), "Share-Based Payment" (FAS 123R). FAS 123R and its related interpretive guidance replaces FAS No. 123, "Accounting for Stock-Based Compensation" (FAS 123), supersedes Accounting Principles Board Opinion No. 25, "Accounting for Stock Issued to Employees" (APB 25) and amends FAS 95, "Statement of Cash Flows." FAS 123, as originally issued in 1995, established as preferable a fair-value-based method of accounting for share-based payment transactions with employees. On January 1, 2003, AIG adopted the recognition provisions of FAS 123. See also Note 10 herein. AIG adopted the provisions of the revised FAS 123R and its related interpretive guidance on January 1, 2006.

For its service-based awards under the 1999 Stock Option Plan, 2002 Stock Incentive Plan and 1996 Employee Stock Purchase Plan, AIG recognizes compensation on a straight-line basis over the scheduled vesting period. Unrecognized unvested compensation expense for stock option awards granted under APB 25 (i.e., before January 1, 2003) will be recognized from January 1, 2006 to the vesting date. However, for the SICO Plans, the AIG Deferred Compensation Profit Participant Plan and the AIG Partners Plan, which contain both performance and service conditions, AIG recognizes compensation utilizing a graded vesting expense attribution method. The effect of this approach is to recognize compensation cost over the requisite service period for each separately vesting tranche of the award.

AIG's share-based plans generally provide for accelerated vesting after the participant turns 65 and retires. For awards granted after January 1, 2006, compensation expense is recognized ratably from the date of grant through the shorter of age 65 or the vesting period. The effect of this change is not material to AIG's consolidated financial position or results of operations. Awards granted prior to January 1, 2006 will continue to be recognized over the vesting period with accelerated expense recognition upon an actual retirement. SICO compensation expense for participants retiring after age 65 had been reflected in prior years' results consistent with vested status under the SICO Plans.

On June 1, 2005, the FASB issued Statement No. 154, "Accounting Changes and Error Corrections" (FAS 154). FAS 154 replaces APB Opinion No. 20, "Accounting Changes" and FASB Statement No. 3, "Reporting Accounting Changes in Interim Financial Statements." FAS 154 requires that a voluntary change in accounting principles be applied retrospectively with all prior period financial statements presented based on the new accounting principle, unless it is impracticable to do so. FAS 154 also provides that a correction of errors in previously issued financial statements should be termed a "restatement." The new standard was effective for accounting changes and correction of errors beginning January 1, 2006.

At the June 2005 meeting, the EITF reached a consensus with respect to Issue No. 04-5, "Determining Whether a General Partner, or the General Partners as a Group, Controls a Limited Partnership or Similar Entity When the Limited Partners Have Certain Rights." The Issue addresses what rights held by the limited partner(s) preclude consolidation in circumstances in which the sole general partner would consolidate the limited partnership in accordance with generally accepted accounting principles absent the existence of the rights held by the limited partner(s). Based on that consensus, the EITF also agreed to amend the consensus in Issue No. 96-16, "Investor's Accounting for an Investee When the Investor Has a Majority of the Voting Interest but the Minority Shareholders Have Certain Approval or Veto Rights." The guidance in this Issue is effective after June 29, 2005 for general partners of all new limited partnerships formed and for existing limited partnerships for which the partnership agreements are modified. For general partners in all other limited partnerships, the guidance in this Issue was effective beginning January 1, 2006. The effect of the adoption of this EITF Issue was not material to AIG's consolidated financial condition or results of operations.

On June 29, 2005, FASB issued Statement 133 Implementation Issue No. B38, "Embedded Derivatives: Evaluation of Net Settlement with Respect to the Settlement of a Debt Instrument through Exercise of an Embedded Put Option or Call Option." This implementation guidance relates to the potential settlement of the debtor's obligation to the creditor that would occur upon exercise of the put option or call option, which meets the net settlement criterion in FAS 133. The effective date of the implementation guidance is January 1, 2006. The adop-

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

8. Recent Accounting Standards *(continued)*

tion of this guidance did not have a material effect on AIG's consolidated financial condition or results of operations.

On June 29, 2005, the FASB issued Statement 133 Implementation Issue No. B39, "Application of Paragraph 13(b) to Call Options That Are Exercisable Only by the Debtor." The conditions in FAS 133 paragraph 13(b) do not apply to an embedded call option in a hybrid instrument containing a debt host contract if the right to accelerate the settlement of the debt can be exercised only by the debtor (issuer/borrower). This guidance does not apply to other embedded derivative features that may be present in the same hybrid instrument. The effective date of the implementation guidance is January 1, 2006. The adoption of this guidance did not have a material effect on AIG's consolidated financial condition or results of operations.

On February 16, 2006, the FASB issued FAS No. 155, "Accounting for Certain Hybrid Financial Instruments" (FAS 155), an amendment of FAS 140 and FAS 133. FAS 155 allows AIG to include changes in fair value in earnings on an instrument-by-instrument basis for any hybrid financial instrument that contains an embedded derivative that would otherwise be required to be bifurcated and accounted for separately under FAS 133. The election to measure the hybrid instrument at fair value is irrevocable at the acquisition or issuance date.

AIG elected to early adopt FAS 155 as of January 1, 2006, and apply FAS 155 fair value measurement to certain structured note liabilities and structured investments in AIG's available for sale portfolio that existed at December 31, 2005. The effect of this adoption resulted in an $11 million after-tax ($18 million pre-tax) decrease to opening retained earnings as of January 1, 2006, representing the difference between the fair value of these hybrid financial instruments and the prior carrying value as of December 31, 2005. The effect of adoption on after-tax gross gains and losses was $218 million ($336 million pre-tax) and $229 million ($354 million pre-tax), respectively.

In connection with AIG's early adoption of FAS 155, structured note liabilities of $8.1 billion, other structured liabilities in conjunction with equity derivative transactions of $70 million, and hybrid financial instruments of $407 million at September 30, 2006 are now carried at fair value. The effect on earnings for the three and nine-month periods ended September 30, 2006, for changes in the fair value of hybrid financial instruments, was a pre-tax gain of $79 million and a pre-tax loss of $44 million, respectively, and is reflected in Other income.

On March 27, 2006, the FASB issued FSP FTB 85-4-1, "Accounting for Life Settlement Contracts by Third-Party Investors" (FSP 85-4-1), an amendment of FTB 85-4, "Accounting for Purchases of Life Insurance." Life settlements are designed to assist life insurance policyholders in monetizing the existing value of life insurance policies. FSP 85-4-1 allows AIG to measure life settlement contracts using either the investment method or fair value method. The election is made on an instrument-by-instrument basis and is irrevocable. AIG elected to early adopt FSP 85-4-1 as of January 1, 2006 using the investment method for pre-existing investments held at December 31, 2005. The effect of this adoption resulted in a $319 million after tax ($487 million pre-tax) increase to opening retained earnings.

On June 29, 2006, AIG restructured its ownership of life settlement contracts with no effect on the economic substance of these investments. At the same time, AIG paid $610 million to its former co-investors to acquire all the remaining interests in life settlement contracts held in previously non-consolidated trusts.

At September 30, 2006, the carrying value of AIG's life settlement contracts was $1.21 billion, and is included in Other invested assets on the consolidated balance sheet. These investments are monitored for impairment on a contract by contract basis quarterly. During the three month period ended September 30, 2006, income recognized on life settlement contracts previously held in non-consolidated trusts was $5 million, and is included in net investment income on the consolidated statement of income. Such income totaled $18 million for the nine month period then ended. Further information regarding life settlement contracts as of September 30, 2006 is as follows:

(dollars in millions)

Remaining Life Expectancy of Insureds	Number of Contracts	Carrying Value	Face Value (Death Benefits)
0 – 1 year	4	$ 6	$ 7
1 – 2 years	24	14	20
2 – 3 years	64	38	59
3 – 4 years	135	131	229
4 – 5 years	137	85	175
Thereafter	1,540	935	3,495
Total	1,904	$1,209	$3,985

As of September 30, 2006, the anticipated life insurance premiums required to keep the life settlement contracts in force, payable in the ensuing twelve months ending September 30, 2007, and the four succeeding years ending September 30, 2011 are $84 million, $88 million, $93 million, $94 million, and $95 million, respectively.

On April 13, 2006, the FASB issued FSP FIN 46(R)-6, "Determining the Variability to be Considered in Applying FASB Interpretation No. 46(R)" (FIN 46(R)-6 or FSP). The FSP affects the identification of which entities are variable interest entities through a "by design" approach in identifying and measuring the variable interests of the variable interest entity and its primary beneficiary. The requirements became effective beginning in the third quarter of 2006 and are to be applied to all new variable interest entities with

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

8. Recent Accounting Standards *(continued)*

which AIG becomes involved. The new requirements need not be applied to entities that have previously been analyzed under FIN 46(R) unless a reconsideration event occurs. The adoption of this guidance did not have a material effect on AIG's consolidated financial condition or results of operations.

Future Application of Accounting Standards

On September 19, 2005, the FASB issued Statement of Position 05-1, "Accounting by Insurance Enterprises for Deferred Acquisition Costs in Connection with Modifications or Exchanges of Insurance Contracts" (SOP 05-1). SOP 05-1 provides guidance on accounting for deferred acquisition costs on internal replacements of insurance and investment contracts other than those specifically described in FASB Statement No. 97, "Accounting and Reporting by Insurance Enterprises for Certain Long-Duration Contracts and for Realized Gains and Losses from the Sale of Investments." The SOP defines an internal replacement as a modification in product benefits, features, rights, or coverage that occurs by the exchange of a contract for a new contract, or by amendment, endorsement, or rider to a contract, or by the election of a feature or coverage within a contract. The effective date of the implementation guidance is January 1, 2007. AIG is currently assessing the effect of implementing this guidance.

On July 13, 2006, the FASB issued FASB Interpretation No. 48, "Accounting for Uncertainty in Income Taxes – an interpretation of FASB Statement No. 109" (FIN 48), which clarifies the accounting for uncertainty in income tax positions. FIN 48 prescribes a recognition threshold and measurement attribute for the financial statement recognition and measurement of an income tax position taken or expected to be taken in a tax return. FIN 48 also provides guidance on derecognition, classification, interest and penalties, accounting in interim periods, and additional disclosures. The effective date of this implementation guidance is January 1, 2007, with the cumulative effect of the change in accounting principle recorded as an adjustment to opening retained earnings. AIG is currently assessing the effect of implementing this guidance.

On September 13, 2006, the SEC issued Staff Accounting Bulletin No. 108, "Considering the Effects of Prior Year Misstatements when Quantifying Misstatements in Current Year Financial Statements" (SAB 108). SAB 108 provides interpretive guidance on how the effects of the carryover or reversal of prior year misstatements should be considered in quantifying a current year misstatement. SAB 108 requires registrants to quantify errors using both a balance sheet and an income statement approach and evaluate whether either approach results in quantifying a misstatement that, when all relevant quantitative and qualitative factors are considered, is material. SAB 108 is effective for registrants' financial statements for fiscal years ending on or after November 15, 2006, with early application encouraged. The adoption of SAB 108 is not expected to have a material effect on AIG's consolidated financial statements.

In September 2006, the FASB issued FAS No. 157, "Fair Value Measurements" (FAS 157). FAS 157 defines fair value, establishes a framework for measuring fair value and expands disclosures about fair value measurements. FAS 157 is effective for financial statements issued for fiscal years beginning after November 15, 2007. AIG is currently assessing the effect of implementing this guidance.

In September 2006, the FASB issued FAS No. 158, "Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans – an amendment of FASB Statements No. 87, 88, 106 and 132(R)" (FAS No. 158). FAS No. 158 requires an employer to prospectively recognize the over funded or under funded status of a defined benefit postretirement plan as an asset or liability in its balance sheet and to recognize changes in that funded status in the year in which the changes occur through other comprehensive income. FAS No. 158 also requires an employer to measure the funded status of a plan as of the date of its year-end balance sheet, with limited exceptions. AIG is required to adopt this standard in its financial statements for the year ending December 31, 2006. The estimated cumulative effect, including deferred income taxes, on AIG's consolidated balance sheet at December 31, 2006 as a result of the adoption of this standard is a net reduction in shareholders' equity through a charge to Other comprehensive income of approximately $720 million, with a corresponding net decrease of approximately $350 million in total assets, and a net increase of approximately $370 million in total liabilities. The actual effect of the adoption at December 31, 2006 may differ from the above estimates due to changes in assumptions such as the discount rate, actuarial assumptions, the measurements of fair value of plan assets and the recognition of any additional minimum liabilities determined under the provisions of FAS 87 prior to the adoption of FAS 158. In addition, AIG is in the process of determining the realizability of additional deferred tax assets that would be generated by plans in foreign locations. Accordingly, the net after tax effect of the adoption of FAS 158 may change pending the outcome of this review during the fourth quarter.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

9. Information Provided in Connection with Outstanding Debt

The following condensed consolidating financial statements are provided in compliance with Regulation S-X of the Securities and Exchange Commission.

(a) American General Corporation (AGC) is a holding company and a wholly owned subsidiary of AIG. AIG provides a full and unconditional guarantee of all outstanding debt of AGC.

American General Corporation, as issuer:

Condensed Consolidating Balance Sheet

September 30, 2006 *(in millions)*	**American International Group, Inc. Guarantor**	**AGC**	**Other Subsidiaries**	**Eliminations**	**Consolidated AIG**
Assets:					
Invested assets	**$ 4,756**	**$ –**	**$760,818**	**$ (15,512)**	**$750,062**
Cash	**28**	**–**	**1,397**	**–**	**1,425**
Carrying value of subsidiaries and partially owned companies, at equity	**103,611**	**26,913**	**5,608**	**(135,101)**	**1,031**
Other assets	**3,806**	**2,646**	**184,638**	**(2,064)**	**189,026**
Total assets	**$112,201**	**$29,559**	**$952,461**	**$ (152,677)**	**$941,544**
Liabilities:					
Insurance liabilities	**$ 332**	**$ –**	**$483,079**	**$ (42)**	**$483,369**
Debt	**10,816**	**2,096**	**138,942**	**(14,732)**	**137,122**
Other liabilities	**4,899**	**3,826**	**218,867**	**(2,882)**	**224,710**
Total liabilities	**16,047**	**5,922**	**840,888**	**(17,656)**	**845,201**
Preferred shareholders' equity in subsidiary companies	**–**	**–**	**189**	**–**	**189**
Total shareholders' equity	**96,154**	**23,637**	**111,384**	**(135,021)**	**96,154**
Total liabilities, preferred shareholders' equity in subsidiary companies and shareholders' equity	**$112,201**	**$29,559**	**$952,461**	**$ (152,677)**	**$941,544**

December 31, 2005 *(in millions)*	American International Group, Inc. Guarantor	AGC	Other Subsidiaries	Eliminations	Consolidated AIG
Assets:					
Invested assets	$ 1,392	$ –	$691,349	$ (13,696)	$679,045
Cash	190	–	1,707	–	1,897
Carrying value of subsidiaries and partially owned companies, at equity	90,723	27,027	15,577	(132,169)	1,158
Other assets	2,768	2,577	166,933	(1,327)	170,951
Total assets	$95,073	$29,604	$875,566	$(147,192)	$853,051
Liabilities:					
Insurance liabilities	$ 408	$ –	$460,271	$ (56)	$460,623
Debt	4,607	2,087	115,212	(12,057)	109,849
Other liabilities	3,741	4,110	191,279	(3,054)	196,076
Total liabilities	8,756	6,197	766,762	(15,167)	766,548
Preferred shareholders' equity in subsidiary companies	–	–	186	–	186
Total shareholders' equity	86,317	23,407	108,618	(132,025)	86,317
Total liabilities, preferred shareholders' equity in subsidiary companies and shareholders' equity	$95,073	$29,604	$875,566	$(147,192)	$853,051

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

9. Information Provided in Connection with Outstanding Debt *(continued)*

Condensed Consolidating Statement of Income

Three Months Ended September 30, 2006 *(in millions)*	**American International Group, Inc. Guarantor**	**AGC**	**Other Subsidiaries**	**Eliminations**	**Consolidated AIG**
Operating income (loss)	**$ (215)**	**$ (49)**	**$6,565**	**$ –**	**$6,301**
Equity in undistributed net income of consolidated subsidiaries	**4,223**	**420**	**–**	**(4,643)**	**–**
Dividend income from consolidated subsidiaries	**287**	**134**	**–**	**(421)**	**–**
Income taxes (benefits)	**71**	**(17)**	**1,889**	**–**	**1,943**
Minority interest	**–**	**–**	**(134)**	**–**	**(134)**
Net income (loss)	**$4,224**	**$522**	**$4,542**	**$(5,064)**	**$4,224**

Three Months Ended September 30, 2005 *(in millions)*	American International Group, Inc. Guarantor	AGC	Other Subsidiaries	Eliminations	Consolidated AIG
Operating income (loss)	$ (41)	$ (54)	$2,642	$ –	$2,547
Equity in undistributed net income of consolidated subsidiaries	1,857	615	–	(2,472)	–
Dividend income from consolidated subsidiaries	223	–	–	(223)	–
Income taxes (benefits)	294	(19)	473	–	748
Minority interest	–	–	(54)	–	(54)
Net income (loss)	$1,745	$580	$2,115	$(2,695)	$1,745

Nine Months Ended September 30, 2006 *(in millions)*	**American International Group, Inc. Guarantor**	**AGC**	**Other Subsidiaries**	**Eliminations**	**Consolidated AIG**
Operating income (loss)	**$ (937)**	**$ (135)**	**$17,407**	**$ –**	**$16,335**
Equity in undistributed net income of consolidated subsidiaries	**10,990**	**1,088**	**–**	**(12,078)**	**–**
Dividend income from consolidated subsidiaries	**854**	**592**	**–**	**(1,446)**	**–**
Income taxes (benefits)	**332**	**(47)**	**4,781**	**–**	**5,066**
Minority interest	**–**	**–**	**(694)**	**–**	**(694)**
Cumulative effect of an accounting change, net of tax	**34**	**–**	**–**	**–**	**34**
Net income (loss)	**$10,609**	**$1,592**	**$11,932**	**$(13,524)**	**$10,609**

Nine Months Ended September 30, 2005 *(in millions)*	American International Group, Inc. Guarantor	AGC Issuer	Other Subsidiaries	Eliminations	Consolidated AIG
Operating income (loss)	$ 99	$ (130)	$14,928	$ –	$14,897
Equity in undistributed net income of consolidated subsidiaries	9,287	1,906	–	(11,193)	–
Dividend income from consolidated subsidiaries	1,151	–	–	(1,151)	–
Income taxes (benefits)	504	(45)	4,078	–	4,537
Minority interest	–	–	(327)	–	(327)
Net income (loss)	$10,033	$1,821	$10,523	$(12,344)	$10,033

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

9. Information Provided in Connection with Outstanding Debt *(continued)*

Condensed Consolidating Statements of Cash Flow

Nine Months Ended September 30, 2006 *(in millions)*	**American International Group, Inc. Guarantor**	**AGC**	**Other Subsidiaries**	**Consolidated AIG**
Net cash (used in) provided by operating activities	**$ (228)**	**$ 160**	**$ 6,072**	**$ 6,004**
Cash flows from investing:				
Invested assets disposed	**2,681**	**–**	**117,873**	**120,554**
Invested assets acquired	**(5,554)**	**–**	**(164,995)**	**(170,549)**
Other	**(2,374)**	**(17)**	**986**	**(1,405)**
Net cash used in investing activities	**(5,247)**	**(17)**	**(46,136)**	**(51,400)**
Cash flows from financing activities:				
Change in debts	**6,201**	**–**	**20,440**	**26,641**
Other	**(888)**	**(143)**	**19,255**	**18,224**
Net cash (used in) provided by financing activities	**5,313**	**(143)**	**39,695**	**44,865**
Effect of exchange rate changes on cash	**–**	**–**	**59**	**59**
Change in cash	**(162)**	**–**	**(310)**	**(472)**
Cash at beginning of period	**190**	**–**	**1,707**	**1,897**
Cash at end of period	**$ 28**	**$ –**	**$ 1,397**	**$ 1,425**

Nine Months Ended September 30, 2005 *(in millions)*	American International Group, Inc. Guarantor	AGC	Other Subsidiaries	Consolidated AIG
Net cash provided by operating activities	$ 1,487	$ 685	$ 18,018	$ 20,190
Cash flows from investing:				
Invested assets disposed	124	–	142,959	143,083
Invested assets acquired	(1,761)	–	(192,501)	(194,262)
Other	(305)	(270)	(823)	(1,398)
Net cash used in investing activities	(1,942)	(270)	(50,365)	(52,577)
Cash flows from financing activities:				
Change in debts	1,659	(299)	11,207	12,567
Other	(1,119)	(116)	21,244	20,009
Net cash (used in) provided by financing activities	540	(415)	32,451	32,576
Effect of exchange rate changes on cash	–	–	(90)	(90)
Change in cash	85	–	14	99
Cash at beginning of period	17	–	1,992	2,009
Cash at end of period	$ 102	$ –	$ 2,006	$ 2,108

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

9. Information Provided in Connection with Outstanding Debt *(continued)*

(b) AIG Liquidity Corp. is a wholly owned subsidiary of AIG. AIG provides a full and unconditional guarantee of all obligations of AIG Liquidity Corp., which commenced operations in 2003.

AIG Liquidity Corp., as issuer:

Condensed Consolidating Balance Sheet

September 30, 2006 *(in millions)*	**American International Group, Inc. Guarantor**	**AIG Liquidity Corp.**	**Other Subsidiaries**	**Eliminations**	**Consolidated AIG**
Assets:					
Invested assets	**$ 4,756**	**$ ***	**$760,818**	**$ (15,512)**	**$750,062**
Cash	**28**	****	**1,397**	**–**	**1,425**
Carrying value of subsidiaries and partially owned companies, at equity	**103,611**	**–**	**32,521**	**(135,101)**	**1,031**
Other assets	**3,806**	****	**187,284**	**(2,064)**	**189,026**
Total assets	**$112,201**	**$ ***	**$982,020**	**$ (152,677)**	**$941,544**
Liabilities:					
Insurance liabilities	**$ 332**	**$ –**	**$483,079**	**$ (42)**	**$483,369**
Debt	**10,816**	****	**141,038**	**(14,732)**	**137,122**
Other liabilities	**4,899**	****	**222,693**	**(2,882)**	**224,710**
Total liabilities	**16,047**	****	**846,810**	**(17,656)**	**845,201**
Preferred shareholders' equity in subsidiary companies	**–**	**–**	**189**	**–**	**189**
Total shareholders' equity	**96,154**	****	**135,021**	**(135,021)**	**96,154**
Total liabilities, preferred shareholders' equity in subsidiary companies and shareholders' equity	**$112,201**	**$ ***	**$982,020**	**$ (152,677)**	**$941,544**

**Amounts significantly less than $1 million.*

December 31, 2005 *(in millions)*	American International Group, Inc. Guarantor	AIG Liquidity Corp.	Other Subsidiaries	Eliminations	Consolidated AIG
Assets:					
Invested assets	$ 1,392	$ *	$691,349	$ (13,696)	$679,045
Cash	190	*	1,707	–	1,897
Carrying value of subsidiaries and partially owned companies, at equity	90,723	–	42,604	(132,169)	1,158
Other assets	2,768	*	169,510	(1,327)	170,951
Total assets	$95,073	$ *	$905,170	$(147,192)	$853,051
Liabilities:					
Insurance liabilities	$ 408	$ –	$460,271	$ (56)	$460,623
Debt	4,607	*	117,299	(12,057)	109,849
Other liabilities	3,741	*	195,389	(3,054)	196,076
Total liabilities	8,756	*	772,959	(15,167)	766,548
Preferred shareholders' equity in subsidiary companies	–	–	186	–	186
Total shareholders' equity	86,317	*	132,025	(132,025)	86,317
Total liabilities, preferred shareholders' equity in subsidiary companies and shareholders' equity	$95,073	$ *	$905,170	$(147,192)	$853,051

**Amounts significantly less than $1 million.*

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

9. Information Provided in Connection with Outstanding Debt *(continued)*

Condensed Consolidating Statement of Income

Three Months Ended September 30, 2006 *(in millions)*	**American International Group, Inc. Guarantor**	**AIG Liquidity Corp.**	**Other Subsidiaries**	**Eliminations**	**Consolidated AIG**
Operating income (loss)	**$ (215)**	**$ ***	**$6,516**	**$ –**	**$6,301**
Equity in undistributed net income of consolidated subsidiaries	**4,223**	**–**	**420**	**(4,643)**	**–**
Dividend income from consolidated subsidiaries	**287**	**–**	**134**	**(421)**	**–**
Income taxes	**71**	*****	**1,872**	**–**	**1,943**
Minority interest	**–**	**–**	**(134)**	**–**	**(134)**
Net income (loss)	**$4,224**	**$ ***	**$5,064**	**$(5,064)**	**$4,224**

**Amounts significantly less than $1 million.*

Three Months Ended September 30, 2005 *(in millions)*	American International Group, Inc. Guarantor	AIG Liquidity Corp.	Other Subsidiaries	Eliminations	Consolidated AIG
Operating income	$ (41)	$ *	$2,588	$ –	$2,547
Equity in undistributed net income of consolidated subsidiaries	1,857	–	615	(2,472)	–
Dividend income from consolidated subsidiaries	223	–	–	(223)	–
Income taxes	294	*	454	–	748
Minority interest	–	–	(54)	–	(54)
Net income (loss)	$1,745	$ *	$2,695	$(2,695)	$1,745

**Amounts significantly less than $1 million.*

Nine Months Ended September 30, 2006 *(in millions)*	**American International Group, Inc. Guarantor**	**AIG Liquidity Corp.**	**Other Subsidiaries**	**Eliminations**	**Consolidated AIG**
Operating income (loss)	**$ (937)**	**$ ***	**$17,272**	**$ –**	**$16,335**
Equity in undistributed net income of consolidated subsidiaries	**10,990**	**–**	**1,088**	**(12,078)**	**–**
Dividend income from consolidated subsidiaries	**854**	**–**	**592**	**(1,446)**	**–**
Income taxes	**332**	*****	**4,734**	**–**	**5,066**
Minority interest	**–**	**–**	**(694)**	**–**	**(694)**
Cumulative effect of an accounting change, net of tax	**34**	**–**	**–**	**–**	**34**
Net income (loss)	**$10,609**	**$ ***	**$13,524**	**$(13,524)**	**$10,609**

**Amounts significantly less than $1 million.*

Nine Months Ended September 30, 2005 *(in millions)*	American International Group, Inc. Guarantor	AIG Liquidity Corp.	Other Subsidiaries	Eliminations	Consolidated AIG
Operating income	$ 99	$ *	$14,798	$ –	$14,897
Equity in undistributed net income of consolidated subsidiaries	9,287	–	1,906	(11,193)	–
Dividend income from consolidated subsidiaries	1,151	–	–	(1,151)	–
Income taxes	504	*	4,033	–	4,537
Minority interest	—	–	(327)	–	(327)
Net income (loss)	$10,033	$ *	$12,344	$(12,344)	$10,033

**Amounts significantly less than $1 million.*

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

9. Information Provided in Connection with Outstanding Debt *(continued)*

Condensed Consolidating Statements of Cash Flow

Nine Months Ended September 30, 2006 *(in millions)*	**American International Group, Inc. Guarantor**	**AIG Liquidity Corp.**	**Other Subsidiaries**	**Consolidated AIG**
Net cash (used in) provided by operating activities	**$ (228)**	**$ ***	**$ 6,232**	**$ 6,004**
Cash flows from investing:				
Invested assets disposed	**2,681**	**–**	**117,873**	**120,554**
Invested assets acquired	**(5,554)**	**–**	**(164,995)**	**(170,549)**
Other	**(2,374)**	*****	**969**	**(1,405)**
Net cash used in investing activities	**(5,247)**	*****	**(46,153)**	**(51,400)**
Cash flows from financing activities:				
Change in debts	**6,201**	**–**	**20,440**	**26,641**
Other	**(888)**	*****	**19,112**	**18,224**
Net cash (used in) provided by financing activities	**5,313**	*****	**39,552**	**44,865**
Effect of exchange rate changes on cash	**–**	**–**	**59**	**59**
Change in cash	**(162)**	*****	**(310)**	**(472)**
Cash at beginning of period	**190**	**–**	**1,707**	**1,897**
Cash at end of period	**$ 28**	**$ ***	**$ 1,397**	**$ 1,425**

**Amounts significantly less than $1 million.*

Nine Months Ended September 30, 2005 *(in millions)*	American International Group, Inc. Guarantor	AIG Liquidity Corp.	Other Subsidiaries	Consolidated AIG
Net cash (used in) provided by operating activities	$ 1,487	$ *	$ 18,703	$ 20,190
Cash flows from investing:				
Invested assets disposed	124	–	142,959	143,083
Invested assets acquired	(1,761)	–	(192,501)	(194,262)
Other	(305)	*	(1,093)	(1,398)
Net cash used in investing activities	(1,942)	*	(50,635)	(52,577)
Cash flows from financing activities:				
Change in debts	1,659	–	10,908	12,567
Other	(1,119)	*	21,128	20,009
Net cash (used in) provided by financing activities	540	*	32,036	32,576
Effect of exchange rate changes on cash	–	–	(90)	(90)
Change in cash	85	*	14	99
Cash at beginning of period	17	–	1,992	2,009
Cash at end of period	$ 102	$ *	$ 2,006	$ 2,108

**Amounts significantly less than $1 million.*

10. Stock Compensation Plans

At September 30, 2006, AIG employees could be awarded compensation pursuant to six different stock-based compensation plan arrangements: (i) AIG 1999 Stock Option Plan, as amended (1999 Plan); (ii) AIG 1996 Employee Stock Purchase Plan, as amended (1996 Plan); (iii) AIG 2002 Stock Incentive Plan, as amended (2002 Plan) under which AIG has issued time-vested restricted stock units (RSUs) and performance restricted stock units (Performance RSUs); (iv) SICO's Deferred Compensation Profit Participation Plans (SICO Plans); (v) AIG's 2005-2006 Deferred Compensation Profit Participation Plan (AIG DCPPP) and (vi) the AIG Partners Plan. The AIG DCPPP was adopted as a replacement for the SICO Plans for the 2005-2006 period, and the AIG Partners Plan replaces the AIG DCPPP. Stock-based compensation earned under the AIG DCPPP and the AIG Partners Plan is issued as awards under the 2002 Plan. AIG currently settles share option exercises and other share awards to participants through the issuance of shares it has previously acquired and holds in its treasury account, except for share awards made by SICO, which are settled by SICO.

At September 30, 2006, AIG's non-employee directors received stock-based compensation in two forms, options granted pursuant to the 1999 Plan and grants of AIG common stock with delivery deferred until retirement from the Board, pursuant to the AIG Director Stock Plan, which was approved by the shareholders at the 2004 Annual Meeting of Shareholders.

From January 1, 2003 through December 31, 2005, AIG accounted for share-based payment transactions with employ-

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

10. Stock Compensation Plans *(continued)*

ees under FAS 123, "Accounting for Stock-Based Compensation." Share-based employee compensation expense from option awards was not recognized in the statement of income in prior periods. Effective January 1, 2006, AIG adopted the fair value recognition provisions of Statement of Financial Accounting Standards No. 123R "Share-Based Payments" (FAS 123R). FAS 123R requires that companies use a fair value method to value share-based payments and recognize the related compensation expense in net earnings. AIG adopted FAS 123R using the modified prospective application method, and accordingly, financial statement amounts for the prior periods presented have not been restated to reflect the fair value method of expensing share-based compensation under FAS 123R. The modified prospective application method provides for the recognition of the fair value with respect to share-based compensation for shares subscribed for or granted on or after January 1, 2006 and all previously granted but unvested awards as of January 1, 2006.

The adoption of FAS 123R resulted in share-based compensation expense of approximately $14 million during the first nine months of 2006, related to awards which were accounted for under the provisions of Accounting Principles Board Opinion No. 25, "Accounting for Stock Issued to Employees." AIG expects this expense to approximate $19 million for fiscal 2006. FAS 123R also requires AIG to estimate forfeitures in calculating the expense relating to share-based compensation, rather than recognizing these forfeitures and corresponding reductions in expense as they occur. The pre-tax cumulative effect of adoption, recognized as a reduction in stock-based compensation of $46 million, was recorded as a cumulative effect of an accounting change, net of tax, in the first quarter of 2006. FAS 123R requires AIG to reflect the cash savings resulting from excess tax benefits in its financial statements as cash flow from financing activities, rather than as cash flow from operating activities as in prior periods. The amount of this excess tax benefit for the three and nine-month periods ended September 30, 2006 was $3.9 million and $6.2 million, respectively.

The effect of the adoption of FAS 123R on the consolidated statements of income and cash flows was as follows:

	Three Months Ended September 30, 2006			Nine Months Ended September 30, 2006		
(in millions, except per share data)	Pre-adoption of FAS 123R	Effect of Adoption of FAS 123R	Including Effect of Adoption of FAS 123R	Pre-adoption of FAS 123R	Effect of Adoption of FAS 123R	Including Effect of Adoption of FAS 123R
Income before income taxes, minority interest and cumulative effect of an accounting change	$ 6,306	$ (5)	$ 6,301	$16,349	$ (14)	$16,335
Provision for income taxes	$ 1,944	$ (1)	$ 1,943	$ 5,068	$ (2)	$ 5,066
Income before minority interest and cumulative effect of an accounting change	$ 4,362	$ (4)	$ 4,358	$11,281	$ (12)	$11,269
Cumulative effect of an accounting change, net of tax	$ –	$ –	$ –	$ –	$ 34	$ 34
Net income	$ 4,228	$ (4)	$ 4,224	$10,587	$ 22	$10,609
Net cash provided by (used in) operating activities	$ (615)	$ (4)	$ (619)	$ 6,010	$ (6)	$ 6,004
Net cash provided by financing activities	$16,922	$ 4	$16,926	$44,859	$ 6	$44,865
Basic earnings per share	$ 1.62	$ –	$ 1.62	$ 4.06	$0.01	$ 4.07
Diluted earnings per share	$ 1.61	$ –	$ 1.61	$ 4.03	$0.01	$ 4.04

The following table presents share-based compensation expenses, including the cumulative effect of adoption of FAS 123R, included in AIG's consolidated statement of income:

(in millions)	Three Months Ended September 30, 2006	Nine Months Ended September 30, 2006
Share-based compensation expense before tax	$66	$277
Income tax benefit	14	42
After-tax share-based compensation expense	$52	$235

Included in share-based compensation expense of $277 million for the nine months ended September 30, 2006 was a one-time compensation cost of approximately $54 million related to the Starr tender offer and various out of period adjustments totalling $61 million, primarily relating to stock-splits and other miscellaneous items for the SICO plans, offset by a $46 million pre-tax adjustment for the cumulative effect of the adoption of FAS 123R. These items were recorded in the first quarter of 2006. See Note 4 herein for a discussion of the Starr tender offer and Note 8 herein for discussion of the prospective change to the accounting for retiree eligibility provisions.

If AIG had adopted the FAS 123 provisions for recognizing compensation expense commencing at the date of grant of the awards, the effect would not have been material to net income or basic or diluted earnings per share for the three and nine-month periods ended September 30, 2005.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

10. Stock Compensation Plans *(continued)*

1999 Stock Option Plan

The 1999 Plan provides that options to purchase a maximum of 45,000,000 shares of common stock can be granted to certain key employees and members of the Board of Directors at prices not less than fair market value at the date of grant.

The 1999 Plan was approved by the shareholders at the 2000 Annual Meeting of Shareholders, with certain amendments approved at the 2003 Annual Meeting of Shareholders. The 1999 Plan superseded the 1991 employee stock option plan (the 1991 Plan), although outstanding options granted under the 1991 Plan continue in force until exercise or expiration. The maximum number of shares that may be granted to any employee in any one year under the 1999 Plan is 900,000. Options granted under the 1999 Plan generally vest over four years (25 percent vesting per year) and expire 10 years from the date of grant.

At September 30, 2006, there were 20,997,720 shares reserved for future grants under the 1999 Plan and 27,787,332 shares reserved for issuance under the 1999 and 1991 Plans.

Deferrals

During 2005, options with respect to 1,731,471 shares were exercised with delivery deferred. At December 31, 2005 optionees had made valid elections to defer delivery of 2,067,643 shares of AIG common stock upon exercise of options expiring during 2006. Of these elections, 1,780,027 shares were exercised and deferred in the third quarter of 2006. In addition, non-employee directors of AIG had made valid elections to defer delivery of 21,093 shares of AIG common stock upon exercise of options expiring during 2006.

Valuation Methodology

In 2004, AIG developed a binomial lattice model to calculate the fair value of stock option grants. In prior years, a Black-Scholes model was used. A more detailed description of the valuation methodology is provided below.

The following weighted average assumptions were used for stock options granted in the first nine months of 2006 and 2005:

	2006	2005
Expected annual dividend yield[(a)]	**0.71%**	0.36%
Expected volatility[(b)]	**27.3%**	34.4%
Risk-free interest rate[(c)]	**4.17%**	3.87%
Expected term[(d)]	**7 years**	7 years

(a) The dividend yield is based on the dividend yield over the twelve month period prior to the grant date.

(b) In 2006, expected volatility is the average of historical volatility (based on seven years of daily stock price changes) and the implied volatility of actively traded options on AIG shares and in 2005, expected volatility is the historical volatility based on five years of daily stock price changes.

(c) The interest rate curves used in the valuation model were the U.S. Treasury STRIP rates with terms from 3 months to 10 years.

(d) The contractual term of the option is generally 10 years with an expected term of 7 years calculated based on an analysis of historical employee exercise behavior and employee turnover (post-vesting terminations). The early exercise rate is a function of time elapsed since the grant. Fifteen years of historical data was used to estimate the early exercise rate.

Additional information with respect to AIG's stock option plans at September 30, 2006, and changes for the nine months then ended, were as follows:

Options:	**Shares**	**Weighted Average Exercise Price**
Outstanding at beginning of year	52,545,425	$54.84
Granted	123,500	$64.55
Exercised	(1,617,411)	$34.02
Shares subject to deferred delivery	(1,780,027)	$15.80
Forfeited or expired	(1,167,789)	$69.77
Outstanding at end of period	48,103,698	$56.65
Options exercisable at end of period	37,700,495	$54.81
Weighted average fair value per share of options granted		$21.11

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

10. Stock Compensation Plans *(continued)*

Information about stock options outstanding at September 30, 2006, is summarized as follows:

	Options Outstanding				Options Exercisable			
Range of Exercise Prices	Number Outstanding	Weighted Average Remaining Contractual Life	Weighted Average Exercise Price	Aggregate Intrinsic Values (in millions)	Number Exercisable (vested)	Weighted Average Remaining Contractual Life	Weighted Average Exercise Price	Aggregate Intrinsic Values (in millions)
$11.28-$27.14	4,284,284	0.83	$24.16	$180	4,284,284	0.83	$24.16	$180
$30.44-$41.51	5,351,821	1.79	36.86	157	5,351,821	1.79	36.86	157
$43.31-$53.40	6,877,098	4.07	48.60	122	6,089,836	3.77	48.81	106
$54.11-$59.99	8,324,097	4.34	57.84	71	6,778,940	3.27	57.49	60
$60.13-$63.95	8,956,414	6.19	62.33	35	5,921,540	5.79	61.92	26
$64.01-$69.63	8,141,722	7.05	65.45	7	3,787,201	5.10	65.66	3
$70.35-$98.00	6,168,262	4.68	83.89	–	5,486,873	4.60	84.46	–
Total	48,103,698	4.55	$56.65	$572	37,700,495	3.64	$54.81	$532

Vested and expected-to-vest options as of September 30, 2006, included in the table above, totaled 44,125,436, with a weighted average exercise price of $56.01, a weighted average contractual life of 4.27 years and an aggregate intrinsic value of $553 million.

As of September 30, 2006, total unrecognized compensation cost (net of expected forfeitures) was $132 million and $3 million related to non-vested share-based compensation awards granted under the 1999 Plan and the 1996 Plan, respectively, with blended weighted average periods of 1.32 years and 0.41 years, respectively. The cost of awards outstanding under these plans at September 30, 2006 is expected to be recognized over approximately three years and one year, respectively, for the 1999 Plan and the 1996 Plan.

The intrinsic value of options exercised during the nine months ended September 30, 2006 was approximately $138 million. The fair value of options vesting for the nine months ended September 30, 2006 was approximately $63 million. AIG received $55 million and $28 million for the nine-month periods ended September 30, 2006 and 2005, respectively, from the exercise of stock options. AIG did not cash-settle any share-based payment awards for the nine-month periods ended September 30, 2006 and 2005. The tax benefits realized as a result of stock option exercises were $15 million for both the nine-month periods ended September 30, 2006 and 2005, respectively.

2002 Stock Incentive Plan

AIG's 2002 Plan was adopted at the 2002 shareholders meeting and amended and restated by the AIG Board of Directors on September 18, 2002 (the 2002 Plan). The 2002 Plan provides that equity-based or equity-related awards with respect to shares of common stock can be issued to employees in any year up to a maximum of that number of shares equal to (a) 1,000,000 shares plus (b) the number of shares available but not issued in the prior calendar year. The maximum award that a grantee may receive under the 2002 Plan per year is rights with respect to 250,000 shares. For the nine-month periods ended September 30, 2006 and 2005, 3,919,170 RSUs, including performance RSUs, and 1,133,405 RSUs, respectively, were granted by AIG. There were 6,316,623 shares reserved for issuance in connection with future awards at September 30, 2006. Substantially all RSUs granted to date under the 2002 Plan other than performance RSUs granted under the Partners Plan vest on the fourth anniversary of the date of grant.

Director Stock Awards

The methodology used for valuing employee stock options is also used to value director stock options. Director stock options vest one year after the grant date, but are otherwise the same as employee stock options. Options with respect to 40,000 shares and 32,500 shares were granted during the nine months ended September 30, 2006 and 2005, respectively.

AIG also granted 10,750 shares and 4,625 shares, with delivery deferred, to directors for the nine-month periods ended September 30, 2006 and 2005, respectively, under the Director Stock Plan. At September 30, 2006, there were 74,250 shares reserved for future grants under the Director Stock Plan.

Employee Stock Purchase Plan

AIG's 1996 Plan provides that eligible employees (those employed at least one year) may receive privileges to purchase up to an aggregate of 10,000,000 shares of AIG common stock, at a price equal to 85 percent of the fair market value on the date of the grant of the purchase privilege. Purchase privileges are granted quarterly and are limited to the number of whole shares that can be purchased on an annual basis by

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

10. Stock Compensation Plans *(continued)*

an amount equal to the lesser of 10 percent of an employee's annual salary or $10,000.

SICO Plans

The SICO Plans provide that shares of AIG common stock currently held by SICO are set aside for the benefit of the participant and distributed upon retirement. The SICO Board of Directors currently may permit an early payout of units under certain circumstances. Prior to payout, the participant is not entitled to vote, dispose of or receive dividends with respect to such shares, and shares are subject to forfeiture under certain conditions, including but not limited to the participant's termination of employment with AIG prior to normal retirement age.

Historically, SICO's Board of Directors could elect to pay a participant cash in lieu of shares of AIG common stock. On December 9, 2005, SICO notified participants that essentially all subsequent distributions would be made only in shares, and not cash. As of that date, AIG modified its accounting for the SICO Plans from variable to fixed measurement accounting. Variable measurement accounting is used for those few awards for which cash elections had been made prior to March 2005. The SICO Plans are also described in Note 4 herein.

Although none of the costs of the various benefits provided under the SICO Plans has been paid by AIG, AIG has recorded a charge to reported earnings for the deferred compensation amounts paid to AIG employees by SICO, with an offsetting amount credited to additional paid-in capital reflecting amounts deemed contributed by SICO.

As of December 9, 2005, there were 12,650,292 non-vested AIG shares under the SICO Plans with a weighted-average fair value per share of $61.92. As of September 30, 2006, there were 11,656,065 non-vested AIG shares under the SICO Plans with a weighted-average fair value per share of $61.90.

A significant portion of the awards under the SICO Plans vest upon retirement if the participant reaches age 65. The portion of the awards for which early payout is available vest on the applicable payout date.

AIG DCPPP

Effective September 21, 2005, AIG adopted the AIG DCPPP, which provides equity-based compensation to key AIG employees, including senior executive officers. The AIG DCPPP was modeled on the SICO Plans.

The AIG DCPPP contingently allocates a fixed number of shares to each participant if AIG's cumulative adjusted earnings per share for 2005 and 2006 exceed that for 2003 and 2004. The performance period is September 21, 2005 to December 31, 2006. At the end of the performance period, common shares are contingently allocated. The service period and related vesting consists of three pre-retirement tranches and a final retirement tranche at age 65.

At September 30, 2006, there were units representing 4,643,722 shares granted to participants.

AIG Partners Plan

On June 26, 2006, AIG's Compensation Committee approved two grants under the AIG Partners Plan. The first grant has a performance period which runs from January 1, 2006 through December 31, 2007. The second grant has a performance period which runs from January 1, 2007 through December 31, 2008. Both grants vest 50 percent on the fourth and sixth anniversaries of the first day of the related performance period. In addition, the Compensation Committee approved the performance metrics for the two grants prior to the date of grant. The measurement of the grants is deemed to have occurred on June 26, 2006 when there was mutual understanding of the key terms and conditions of the grants. Consistent with this treatment: a) 1,068,605 performance RSUs for the first grant and 2,488,865 performance RSUs for the second grant and b) unrecognized compensation of $55 million for the first grant and $138 million for the second grant are included in the related disclosure tables. Performance RSUs related to the first grant are excluded from AIG's diluted shares calculation because an insufficient amount of time has elapsed to conclusively determine that the performance metric will be achieved at the end of the related performance period. Because the performance period for the second grant does not begin until January 1, 2007, compensation expense for the second grant is not included in AIG's 2006 results and diluted shares calculation.

VALUATION

The fair value of each award granted under the 2002 Plan, the AIG DCPPP, the AIG Partners Plan, and the SICO Plans is based on the closing price of AIG stock on the date of grant.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

10. Stock Compensation Plans *(continued)*

A summary of shares relating to outstanding awards unvested under the foregoing plans as of September 30, 2006, and changes during the nine months ended September 30, 2006 is presented below:

	Number of Shares					Weighted Average Grant-Date Fair Value				
	2002 Plan	AIG DCPPP	AIG Partners Plan	Total 2002 Plan	SICO Plans	2002 Plan	AIG DCPPP	AIG Partners Plan	Total 2002 Plan	SICO Plans
Unvested at January 1, 2006	4,322,265	4,898,880	–	9,221,145	12,650,292	$63.63	$52.55	$ –	$57.74	$61.92
Granted	315,170	–	3,604,000	3,919,170	–	62.11	–	56.42	56.88	–
Vested	(5,080)	–	–	(5,080)	(653,486)	64.25	–	–	64.25	64.55
Forfeited	(187,680)	(255,158)	(16,200)	(459,038)	(340,741)	62.47	59.40	56.22	60.54	61.01
Unvested at September 30, 2006	4,444,675	4,643,722	3,587,800	12,676,197	11,656,065	$63.57	$52.17	$56.42	$57.37	$61.90

At September 30, 2006, the total unrecognized compensation cost (net of expected forfeitures) related to non-vested share-based compensation awards granted under the 2002 Plan, the AIG DCPPP, the AIG Partners Plan and the SICO plans and the blended weighted-average period over which that cost is expected to be recognized is as follows:

	Unrecognized Compensation Cost *(in millions)*	Blended Weighted-Average Period
2002 Plan	$178	1.62 years
AIG DCPPP	$231	4.57 years
AIG Partners Plan	$195	2.56 years
Total 2002 Plan	$604	3.05 years
SICO Plans	$313	6.06 years

The total cost for awards outstanding as of September 30, 2006 under the 2002 Plan, the AIG DCPPP, the AIG Partners Plan, and the SICO Plans is expected to be recognized over approximately 4 years, 12 years, 6 years and 23 years, respectively.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

11. Cash Flows

As part of its remediation activities during the third quarter of 2006, AIG determined that certain non-cash activities and adjustments, including the effects of changes in foreign exchange translation on assets and liabilities, previously were misclassified within the operating, investing and financing sections of the Consolidated Statement of Cash Flows. The more significant line items revised include the change in General and life insurance reserves and Deferred policy acquisition costs within operating activities; Purchases of fixed maturity securities within investing activities; and Proceeds from notes, bonds, loans and mortgages payable, and hybrid financial instrument liabilities within financing activities. After evaluating the effect of these items during the third quarter of 2006, AIG has revised the previous periods presented below to conform to the third quarter 2006 presentation:

(in millions)

	Six Months Ended June 30, 2006	Three Months Ended March 31, 2006	Year Ended December 31, 2005	Nine Months Ended September 30, 2005	Six Months Ended June 30, 2005	Three Months Ended March 31, 2005
Cash flows from operating activities — As previously reported	$ 6,978	$ 3,066	$ 25,138	$ 20,865*	$ 13,817	$ (434)
Revisions	(355)	1,076	(52)	(675)	(2,163)	(1,563)
Cash flows from operating activities — As revised	$ 6,623	$ 4,142	$ 25,086	$ 20,190	$ 11,654	$ (1,997)
Cash flows from investing activities — As previously reported	$(40,048)	$(19,937)	$ (57,321)	$(47,391)*	$(35,358)	$(20,118)
Revisions	5,682	1,724	(7,544)	(5,186)	(2,863)	775
Cash flows from investing activities — As revised	$(34,366)	$(18,213)	$ (64,865)	$(52,577)	$(38,221)	$(19,343)
Cash flows from financing activities — As previously reported	$ 32,243	$ 15,672	$ 32,999	$ 27,230*	$ 22,097	$ 20,961
Revisions	(4,304)	(2,273)	6,831	5,346	4,275	725
Cash flows from financing activities — As revised	$ 27,939	$ 13,399	$ 39,830	$ 32,576	$ 26,372	$ 21,686
Effect of exchange rate changes on cash — As previously reported	$ 1,070	$ 550	$ (928)	$ (605)*	$ (827)	$ (57)
Revisions	(1,023)	(527)	765	515	751	63
Effect of exchange rate changes on cash — As revised	$ 47	$ 23	$ (163)	$ (90)	$ (76)	$ 6

**Includes the effects of corrections and reclassifications made in conjunction with the Second Restatement. See also AIG's 2005 Annual Report on Form 10-K/A.*

There was no effect on ending cash balances.

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Management's Discussion and Analysis of Financial Condition and Results of Operations is designed to provide the reader a narrative with respect to AIG's operations, financial condition and liquidity and certain other significant matters.

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Cautionary Statement Regarding Projections and Other Information About Future Events

This Quarterly Report and other publicly available documents may include, and AIG's officers and representatives may from time to time make, projections concerning financial information and statements concerning future economic performance and events, plans and objectives relating to management, operations, products and services, and assumptions underlying these projections and statements. These projections and statements are not historical facts but instead represent only AIG's belief regarding future events, many of which, by their nature, are inherently uncertain and outside AIG's control. These projections and statements may address, among other things, the status and potential future outcome of the current regulatory and civil proceedings against AIG and their potential effect on AIG's businesses, financial position, results of operations, cash flows and liquidity, the effect of the credit rating downgrades on AIG's businesses and competitive position, the unwinding and resolving of various relationships between AIG and Starr and SICO, and AIG's strategy for growth, product development, market position, financial results and reserves. It is possible that AIG's actual results and financial condition may differ, possibly materially, from the anticipated results and financial condition indicated in these projections and statements. Factors that could cause AIG's actual results to differ, possibly materially, from those in the specific projections and statements are discussed throughout this Management's Discussion and Analysis of Financial Condition and Results of Operations and in "Risk Factors" in Item 1A. of Part I of AIG's 2005 Annual Report on Form 10-K, Item 1A. of Part II of AIG's Quarterly Report on Form 10-Q for the quarter ended March 31, 2006 and Item 1A. of Part II of this Quarterly Report. AIG is not under any obligation (and expressly disclaims any such obligations) to update or alter any projections or other statement, whether written or oral, that may be made from time to time, whether as a result of new information, future events or otherwise.

Throughout this Management's Discussion and Analysis of Financial Condition and Results of Operations, AIG presents its operations in the way it believes will be most meaningful. Statutory loss ratios and combined ratios are presented in accordance with accounting principles prescribed by insurance regulatory authorities because these are standard measures of performance filed with insurance regulatory authorities and used for analysis in the insurance industry and thus allow more meaningful comparisons with AIG's insurance competitors. AIG has also incorporated into this discussion a number of cross-references to additional information included throughout this Form 10-Q and its 2005 Annual Report on Form 10-K/A for the year ended December 31, 2005 (2005 Annual Report on Form 10-K/A) to assist readers seeking related information on a particular subject.

Overview of Operations and Business Results

AIG identifies its reportable segments by product line, consistent with its management structure. AIG's major product and service groupings are General Insurance, Life Insurance & Retirement Services, Financial Services and Asset Management. AIG's operations in 2006 are conducted by its subsidiaries principally through these segments. Through these segments, AIG provides insurance and investment products and services to both businesses and individuals in more than 130 countries and jurisdictions. This geographic, product and service diversification is one of AIG's major strengths and sets it apart from its competitors. The Other category consists of items not allocated to AIG's operating segments.

AIG's subsidiaries serve commercial, institutional and individual customers through an extensive property-casualty and life insurance and retirement services network. In the United States, AIG companies are the largest underwriters of commercial and industrial insurance and one of the largest life insurance and retirement services operations as well. AIG's Financial Services businesses include commercial aircraft and equipment leasing, capital markets operations and consumer finance, both in the United States and abroad. AIG also provides asset management services to institutions and individuals. As part of its spread-based business activities, AIG issues various debt instruments in the public and private markets.

AIG's operating performance reflects implementation of various long-term strategies and defined goals in its various operating segments. A primary goal of AIG in managing its General Insurance operations is to achieve an underwriting profit. To achieve this goal, AIG must be disciplined in its risk selection and premiums must be adequate and terms and conditions appropriate to cover the risk accepted. AIG also believes in strict control of expenses.

A central focus of AIG operations in recent years is the development and expansion of new distribution channels. In 2005 and the first nine months of 2006, AIG expanded its distribution channels, which now include banks, credit card companies and television-media home shopping in many Asian countries. Examples of new distribution channels used both domestically and overseas include banks, affinity groups, direct response and e-commerce.

AIG patiently builds relationships in markets around the world where it sees long-term growth opportunities. For example, the fact that AIG has the only wholly-owned foreign life insurance operations in eight cities in China is the result of relationships developed over nearly 30 years. AIG's more recent extensions of operations into India, Vietnam, Russia and other emerging markets reflect the same growth strategy. Moreover, AIG believes in investing in the economies and infrastructures of these countries and growing with them. When AIG companies enter a new jurisdiction, they typically offer both basic protection and savings products. As the economies evolve, AIG's products evolve with them, to more sophisticated and investment-oriented models.

Growth for AIG may be generated both internally and through acquisitions which both fulfill strategic goals and offer adequate return on capital. Recently AIG acquired Travel Guard International, one of the nation's leading providers of travel insurance programs and emergency travel assistance, and Central Insurance Co., Ltd., a leading general insurance company in Taiwan.

Consolidated Results

The following table summarizes AIG's revenues, income before income taxes, minority interest and cumulative effect of an accounting change and net income for the three and nine-month periods ended September 30, 2006 and 2005:

	Three Months Ended September 30,		Nine Months Ended September 30,	
(in millions)	**2006**	2005	**2006**	2005
Total revenues	**$29,199**	$26,408	**$83,201**	$81,513
Income before income taxes, minority interest and cumulative effect of an accounting change	**6,301**	2,547	**16,335**	14,897
Net income	**$ 4,224**	$ 1,745	**$10,609**	$10,033

Revenues in the third quarter and first nine months of 2006 increased 11 percent and 2 percent, respectively, largely as a result of the growth in net premiums earned and net investment income from global General Insurance operations and growth in Life Insurance & Retirement Services net investment income and GAAP premiums. Revenues in the Financial Services segment increased in the third quarter of 2006, but decreased for the first nine months of 2006 largely

as a result of hedging activities that do not qualify for hedge accounting treatment under FAS 133, the effects of which are reported in other income.

Income before income taxes, minority interest and cumulative effect of an accounting change in the three and nine-month periods ended September 30, 2006 increased 147 percent and 10 percent, respectively, with the significant increase primarily a reflection of the negative effect of $2.44 billion in catastrophe related losses incurred in the third quarter of 2005. The 2006 periods also included higher General Insurance and Life Insurance & Retirement Services operating income. Fluctuations in Financial Services operating income in all periods presented were driven by the transaction oriented nature of Capital Markets operations and the effects of hedging activities that do not qualify for hedge accounting treatment under FAS 133.

During the third quarter and nine months ended September 30, 2006, as part of its continuing remediation efforts, AIG recorded certain out of period and other adjustments. These adjustments collectively increased net income by $73 million in the third quarter of 2006 and decreased net income by $29 million for the first nine months of 2006. The third quarter adjustments included the following: an increase in realized capital gains relating to foreign exchange of $36 million ($23 million after tax); increases in bad debt expense of $225 million ($146 million after tax) and earned premiums of $99 million ($65 million after tax), both of which relate to balance sheet reconciliations; an increase in partnership income of $121 million ($79 million after tax), which relates to improved valuation information; a further increase in unit investment trust income of $116 million ($75 million after tax), as described below; and an increase in income tax expense of $39 million relating to AIG's ongoing remediation of internal controls over income tax accounting. See also the discussion of AIG's reportable segments in Management's Discussion & Analysis of Financial Condition and Results of Operations.

During the second quarter of 2006, AIG identified and recorded an out of period adjustment related to the accounting for certain interests in unit investment trusts in accordance with FIN 46(R), "Consolidation of Variable Interest Entities" and APB Opinion No. 18, "The Equity Method of Accounting for Investments in Common Stock." These investments had previously been accounted for as available for sale securities, with changes in market values being reflected in other comprehensive income, net of deferred income taxes. Beginning with the second quarter of 2006, the changes in market values are included in AIG's net investment income. During the second quarter of 2006, the adjustment decreased Unrealized appreciation (depreciation) of investments — net of reclassification adjustments, and the related Deferred income tax benefit (expense), in the Consolidated Statement of Comprehensive Income (Loss) by approximately $576 million and approximately $202 million, respectively, and increased Net investment income by $653 million, increased Incurred policy losses and benefits, related to certain participating policyholder funds, by $77 million, and increased Income taxes by $202 million in the Consolidated Statement of Income. There was no effect on Total shareholders' equity as of September 30, 2006 or December 31, 2005.

In the second quarter of 2006, AIG also recorded other out of period adjustments of $85 million ($55 million after tax) of interest income related to interest earned on deposit contracts and $32 million ($21 million after tax) of expenses related to the remediation of a material weakness in controls over certain balance sheet reconciliations.

AIG also recorded other out of period adjustments in the first quarter of 2006 of $61 million (before and after tax) of expenses related to the SICO plans, $59 million ($38 million after tax) of expenses related to deferred advertising costs in General Insurance, a decrease of $300 million ($145 million after tax) in revenues related to the remediation of a material weakness in accounting for certain derivative transactions under FAS 133, and $126 million of income tax expense related to AIG's remediation of a material weakness in controls over income tax accounting.

Results for the first nine months of 2006 were negatively affected by a one-time charge relating to the Starr tender offer ($54 million before and after tax) and an additional allowance for losses in AIG Credit Card Company (Taiwan) ($88 million before and after tax), both of which were recorded in first quarter of 2006.

The effective income tax rate increased from 28.0 percent for full year 2005 to 30.8 percent and 31.0 percent for the three and nine-month periods ended September 30, 2006, respectively, reflecting changes in the sources of foreign taxable income, the effect of the phase out of synfuel tax credits on the estimated full year tax rate and the aforementioned out of period adjustments.

The following table summarizes the operations of each principal segment for the three and nine-month periods ended September 30, 2006 and 2005. (See also Note 2 of Notes to Consolidated Financial Statements).

(in millions)	Three Months Ended September 30, **2006**	2005	Nine Months Ended September 30, **2006**	2005
Revenues[(a)]:				
General Insurance[(b)(h)]	**$12,615**	$11,192	**$36,438**	$33,816
Life Insurance & Retirement Services[(c)(h)]	**12,356**	11,760	**36,819**	35,086
Financial Services[(d)]	**3,187**	1,926	**6,028**	8,140
Asset Management[(e)]	**1,238**	1,355	**4,098**	3,951
Other	**(197)**	175	**(182)**	520
Consolidated	**$29,199**	$26,408	**$83,201**	$81,513
Operating Income (loss)[(a)(f)(i)(j)]:				
General Insurance[(h)]	**$ 2,625**	$ (137)	**$ 7,819**	$ 3,390
Life Insurance & Retirement Services[(g)(h)]	**2,448**	2,248	**7,424**	6,787
Financial Services[(g)]	**1,357**	224	**650**	3,483
Asset Management	**341**	568	**1,613**	1,682
Other[(k)]	**(470)**	(356)	**(1,171)**	(445)
Consolidated	**$ 6,301**	$ 2,547	**$16,335**	$14,897

(a) Includes the effect of hedging activities that do not qualify for hedge accounting treatment under FAS 133, including the related foreign exchange gains and losses. For the three-month periods ended September 30, 2006 and 2005, the effect was $165 million and $(353) million, respectively, in revenues and $165 million and $(345) million, respectively, in operating income. For the nine-month periods ended September 30, 2006 and 2005, the effect was $(1.13) billion and $2.21 billion, respectively, in revenues and $(1.13) billion and $2.28 billion, respectively, in operating income. These amounts result primarily from interest rate and foreign currency derivatives which are hedging available for sale securities and borrowings.

(b) Represents the sum of General Insurance net premiums earned, net investment income and realized capital gains (losses).

(c) Represents the sum of Life Insurance & Retirement Services GAAP premiums, net investment income and realized capital gains (losses).

(d) Represents interest, lease and finance charges.

(e) Represents net investment income with respect to GICs and management and advisory fees.

(f) Represents income before income taxes, minority interest and cumulative effect of an accounting change.

(g) Results of operations of AIG Credit Card Company (Taiwan) are shared equally by the Life Insurance & Retirement Services segment and the Financial Services segment. Additional allowances of $44 million were recorded in the first quarter of 2006, by each segment, for losses in these credit card operations.

(h) Includes the effect of out of period adjustments related to the accounting for certain interests in unit investment trusts. For the three and nine-month periods ended September 30, 2006 the effect was an increase of $92 million and $524 million in both revenues and operating income for General Insurance and an increase of $24 million in both revenues and operating income for the three-month period ended September 30, 2006 and $245 million and $168 million in revenues and operating income, respectively, for the nine-month period ended September 30, 2006, for Life Insurance & Retirement Services.

(i) Includes current year catastrophe related losses of $2.44 billion in both the third quarter and first nine months of 2005. There were no significant catastrophe related losses in the third quarter and first nine months of 2006.

(j) Includes additional losses incurred and net reinstatement premiums related to prior year catastrophes of $28 million and $39 million in the three-month periods ended September 30, 2006 and 2005, respectively. Such losses and premiums were $87 million and $252 million in the nine-month periods ended September 30, 2006 and 2005, respectively.

(k) Includes current year catastrophe related losses from unconsolidated subsidiaries of $246 million for both the third quarter and first nine months of 2005. There were no significant catastrophe related losses in the third quarter and first nine months of 2006. Also includes unfavorable development from unconsolidated subsidiaries related to prior year catastrophe related losses of $1 million and $15 million for the first nine months of 2006 and 2005, respectively.

General Insurance

AIG's General Insurance operations provide property and casualty products and services throughout the world. The increase in General Insurance operating income in the three and nine-month periods ended September 30, 2006 compared to the same periods of 2005 was primarily attributable to catastrophe related losses of $2.11 billion in the third quarter of 2005 and the improvement in underwriting results for the Domestic Brokerage Group (DBG). General Insurance operating income included adverse development in the first nine months of 2006 and 2005 from catastrophes in prior years and certain long-tail casualty lines, which were more than offset by favorable development in other lines. Operating income for the three and nine-month periods ended September 30, 2006 also increased due to the effect of the out of period adjustments related to the accounting for certain interests in unit investment trusts, partially offset by reconciliation adjustments.

Life Insurance & Retirement Services

AIG's Life Insurance & Retirement Services operations provide insurance, financial and investment products throughout the world. Foreign operations provided approximately 65 percent and 61 percent of AIG's Life Insurance & Retirement Services operating income for the three months ended September 30, 2006 and 2005, respectively, and 67 percent and 59 percent, respectively, for the first nine months of 2006 and 2005.

Life Insurance & Retirement Services operating income increased $200 million in the third quarter of 2006 from the same period of 2005. Results for the quarter were particularly strong in the Foreign Life operations that were helped by

higher investment returns and lower acquisition costs. Domestic Life and Retirement Services results improved over the prior year with growth in the in-force business and lower catastrophe and synfuel losses. Life Insurance & Retirement Services operating income included $12 million in catastrophe related losses in the third quarter of 2005. Realized capital losses included in revenues and operating income were $176 million in the third quarter of 2006 compared to realized capital losses of $16 million in the same period of 2005.

Life Insurance & Retirement Services operating income increased by 9 percent in the first nine months of 2006 when compared to the same period of 2005 due, in part, to the effect of an out of period adjustment related to the accounting for certain interests in unit investment trusts. Realized capital losses included in revenues and operating income were $117 million in the first nine months of 2006 compared to realized capital losses of $18 million in the same period of 2005.

Financial Services

AIG's Financial Services subsidiaries engage in diversified activities including aircraft and equipment leasing, capital market transactions, consumer finance and insurance premium financing.

Financial Services operating income increased in the third quarter of 2006 and decreased in the first nine months of 2006 compared to the same periods of 2005 primarily due to the effects of hedging activities that do not qualify for hedge accounting treatment under FAS 133. Financial Services operating income in 2005 included catastrophe related losses of $62 million recorded in the third quarter of 2005 resulting from hurricane Katrina, which were reduced by $22 million in the third quarter of 2006. Fluctuations in revenues and operating income from quarter to quarter are not unusual because of the transaction-oriented nature of Capital Markets operations and the effect of not qualifying for hedge accounting treatment under FAS 133 for hedges on securities available for sale and borrowings.

Asset Management

AIG's Asset Management operations include institutional and retail asset management and broker dealer services and AIG's spread-based investment businesses. The AIG Matched Investment Program (MIP), which was launched in September of 2005, is replacing AIG's GIC program as AIG's principal spread-based investment activity.

Asset Management operating income decreased 40 percent for the third quarter of 2006 when compared to the same period of 2005 due to the continued run-off of GICs and decreased transaction-driven fees partially offset by growth in the asset management fees within Institutional Asset Management and income from AIG's MIP. Gains and losses arising from the consolidation of certain variable interest entities and partnerships are included in operating income, but are offset in minority interest expense, which is not a component of operating income. Operating income decreased 4 percent in the first nine months of 2006 when compared to the same period of 2005, primarily due to the continued run-off of GIC balances combined with spread compression in the remaining GIC portfolio.

Capital Resources

At September 30, 2006, AIG had total consolidated shareholders' equity of $96.15 billion and total consolidated borrowings of $137.1 billion. At that date, $122.1 billion of such borrowings were either not guaranteed by AIG or were AIGFP's matched borrowings under obligations of guaranteed investment agreements (GIAs), liabilities connected to trust preferred stock, or matched notes and bonds payable.

AIG has not purchased any shares of its common stock under its existing common stock repurchase authorization during 2006.

Liquidity

At September 30, 2006, AIG's consolidated invested assets included $24.14 billion in cash and short-term investments. Consolidated net cash provided from operating activities in the first nine months of 2006 amounted to $6.0 billion. AIG believes that its liquid assets, cash provided by operations and access to the capital markets will enable it to meet its anticipated cash requirements.

Outlook

The commercial property and casualty insurance industry has historically experienced cycles of price erosion followed by rate strengthening as a result of catastrophe or other significant losses that affect the overall capacity of the industry to provide coverage. Despite industry price erosion in some classes of general insurance, AIG expects to continue to identify profitable opportunities and build attractive new general insurance businesses as a result of AIG's broad product line and extensive distribution networks. There can be no assurance, however, that price erosion will not become more widespread or that AIG's profitability will not deteriorate from current levels in major commercial lines, as well as in personal lines and specialty coverages, such as mortgage guaranty, where the loss ratio is expected to increase due to softening in the U.S. housing market and the weakening performance of non-traditional mortgage products.

In December 2005, American International Underwriters Overseas, Ltd. (AIUO) received a license from the government of Vietnam to operate a wholly owned general insurance company in Vietnam. This license, the first general insurance license granted by Vietnam to a U.S.-based insurance organization, permits AIG to operate a general insurance company throughout Vietnam.

During the second quarter of 2006, the Canadian Parliament passed legislation that will allow UGC to begin writing business in Canada, the world's second largest mortgage guaranty market, when provincial licenses are issued.

In China, applications for provincial expansion of AIG's life insurance operations in Guangdong and Jiangsu and of general insurance operations in Guangdong were approved in April 2006. AIG's wholly-owned life insurance operations in eight cities have now been structured into four regional management teams located in Shanghai, Beijing, Guangdong Province and Jiangsu Province. AIG's operations are expanding resources in these regions with the opening of additional offices.

In Japan, earnings growth for AIG Star Life Insurance Co., Ltd. and AIG Edison Life Insurance Company reflects the runoff of the more profitable in-force business in comparison to new business currently being generated. In May 2006, AIG announced the merger of these companies, which is expected to enhance the combined entity's ability to grow new business by expanding distribution and gaining efficiency of scale. In the fiscal year ended March 31, 2006, AIG's life operations in Japan retained their position as the largest foreign life operation on a total premium basis. AIG has developed a leadership position in the distribution of annuities through banks in both Japan and Korea. Also, American Life Insurance Company (ALICO) has launched new life products to the Japan bank market after further deregulation of banks in December 2005. AIG is a leader in direct marketing through sponsors and in the broad market in Japan and Korea. AIG also is investing in expanding distribution channels with emphasis in India, Korea and Vietnam.

Domestically, AIG anticipates its Life Insurance & Retirement Services businesses to continue growing in 2006 through distribution channel expansion and new and enhanced products. The home service operation, which is expected to be a slow growth business, has not met business objectives, although its cash flow has been strong. Domestic group life/health results continue to be weak, resulting in ongoing restructuring activities which may result in the exiting of certain product lines. AIG Retirement Services individual fixed annuities business will continue to be challenged due to the interest rate environment and increased competition from bank products, while variable annuity products with living benefits will continue to be the product of consumer choice.

Globally, heightened regulatory scrutiny of financial services companies in many jurisdictions has the potential to affect future financial results through higher compliance costs or other charges. This is particularly true in Japan and Southeast Asia where financial institutions have received an increased number of remediation orders affecting consumer/policyholder rights over the last twelve months.

Changes in market conditions in the aircraft leasing business are not immediately apparent in operating results. Lease rates have firmed as a result of continued demand from the global commercial aviation market, especially in Asia. However, higher interest rates are expected to continue to compress lease margins. AIG's Consumer Finance operations overseas were negatively affected in the first quarter of 2006 by industry-wide credit deterioration in the Taiwan credit card market. The operating results of AIG's Consumer Finance operations in the U.S. could be affected by the residential housing market, interest rates and unemployment. Also, AIG continues to explore opportunities to expand its Consumer Finance operations into new foreign markets.

The GIC portfolio continues to run-off. The MIP has replaced the GIC program as AIG's principal spread-based investment activity. Although the MIP is beginning to show positive operating income, because the asset mix under the MIP does not include the alternative investments utilized in the GIC program, AIG does not expect that the income growth in the MIP will offset the run-off in the GIC portfolio for the foreseeable future.

AIG has many promising growth initiatives underway around the world. Cooperative agreements such as those with PICC Property and Casualty Company Limited and various banks in the U.S., Japan and Korea are expected to expand distribution networks for AIG's products and provide models for future growth.

Critical Accounting Estimates

AIG considers its most critical accounting estimates those with respect to reserves for losses and loss expenses, future policy benefits for life and accident and health contracts, deferred policy acquisition costs, estimated gross profits for investment-oriented products, fair value determinations for certain Capital Markets assets and liabilities, other-than-temporary declines in the value of investments and flight equipment recoverability. These accounting estimates require the use of assumptions about matters, some of which are highly uncertain at the time of estimation. To the extent actual experience differs from the assumptions used, AIG's results of operations would be directly affected.

Throughout this Management's Discussion and Analysis of Financial Condition and Results of Operations, AIG's critical accounting estimates are discussed in detail. The major categories for which assumptions are developed and used to establish each critical accounting estimate are highlighted below.

Reserves for Losses and Loss Expenses and Reinsurance Recoverable (General Insurance):

- *Loss trend factors:* used to establish expected loss ratios for subsequent accident years based on premium rate adequacy and the projected loss ratio with respect to prior accident years.
- *Expected loss ratios for the latest accident year:* for example, accident year 2005 for the year end 2005 loss reserve analysis. For low frequency, high severity classes

such as excess casualty, expected loss ratios generally are utilized for at least the three most recent accident years.

- *Loss development factors:* used to project the reported losses for each accident year to an ultimate amount.
- *Reinsurance recoverable on unpaid losses:* the expected recoveries from reinsurers on losses that have not yet been reported and/or settled.

Future Policy Benefits for Life and Accident and Health Contracts (Life Insurance & Retirement Services):

- *Interest rates:* which vary by geographical region, year of issuance and products.
- *Mortality, morbidity and surrender rates:* based upon actual experience by geographical region modified to allow for variation in policy form.

Estimated Gross Profits (Life Insurance & Retirement Services):

- *Estimated gross profits* to be realized over the estimated duration of the contracts (investment-oriented products) affect the carrying value of deferred policy acquisition costs under FAS 97. Estimated gross profits include investment income and gains and losses on investments less required interest, actual mortality and other expenses.

Deferred Policy Acquisition Costs (Life Insurance & Retirement Services):

- Recoverability based on current and future expected profitability, which is affected by interest rates, foreign exchange rates, mortality experience, and policy persistency.

Deferred Policy Acquisition Costs (General Insurance):

- Recoverability and eligibility based upon the current terms and profitability of the underlying insurance contracts.

Fair Value Determinations of Certain Assets and Liabilities (Financial Services – Capital Markets):

- *Valuation models:* utilizing factors, such as market liquidity and current interest, foreign exchange and volatility rates.
- AIG attempts to secure reliable and independent current market price data, such as published exchange rates from external subscription services such as Bloomberg or Reuters or third-party broker quotes for use in its model. When such prices are not available, AIG uses an internal methodology, which includes interpolation and extrapolation from verifiable prices from trades occurring on dates nearest to the dates of the transactions.

Other-Than-Temporary Declines in the Value of Investments:

A security is considered a candidate for other-than-temporary impairment based upon the following criteria:

- Trading at a significant (25 percent or more) discount to par or amortized cost (if lower) for an extended period of time (nine months or longer).
- The occurrence of a discrete credit event resulting in the debtor defaulting or seeking bankruptcy or insolvency protection or voluntary reorganization.
- The probability of non-realization of a full recovery on its investment, irrespective of the occurrence of one of the foregoing events.

At each balance sheet date, AIG evaluates its securities holdings in an unrealized loss position. Where AIG does not intend to hold such securities until they have fully recovered their carrying value, based on the circumstances present at the date of evaluation, AIG records the unrealized loss in income. If events or circumstances change, such as unexpected changes in creditworthiness of the obligor, general interest rate environment, tax circumstances, liquidity events, and statutory capital management considerations among others, AIG revisits its intent to determine if a loss should be recorded in income. Further, if a loss is recognized from a sale subsequent to a balance sheet date pursuant to these changes in circumstances, the loss is recognized in the period in which the intent to hold the securities to recovery no longer exists.

Flight Equipment — Recoverability (Financial Services):

- *Expected undiscounted future net cash flows:* based upon current lease rates, projected future lease rates and estimated terminal values of each aircraft based on third party information.

Operating Review

General Insurance Operations

AIG's General Insurance subsidiaries are multiple line companies writing substantially all lines of property and casualty insurance both domestically and abroad.

Domestic General Insurance operations are comprised of DBG, which includes the operations of The Hartford Steam Boiler Inspection and Insurance Company (HSB); Transatlantic Holdings, Inc. (Transatlantic); Personal Lines, including 21st Century Insurance Group (21st Century); and United Guaranty Corporation (UGC).

AIG's primary domestic division is DBG. DBG's business in the United States and Canada is conducted through its General Insurance subsidiaries including American Home Assurance Company (American Home), National Union Fire Insurance Company of Pittsburgh, Pa. (National Union), Lexington Insurance Company (Lexington) and certain other General Insurance company subsidiaries of AIG.

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

In addition to writing substantially all classes of business insurance, including large commercial or industrial property insurance, excess liability, inland marine, environmental,

workers compensation and excess and umbrella coverages, DBG offers many specialized forms of insurance such as aviation, accident and health, equipment breakdown, directors and officers liability (D&O), difference-in-conditions, kidnap-ransom, export credit and political risk, and various types of professional errors and omissions coverages. The AIG Risk Management operation provides insurance and risk management programs for large corporate customers. The AIG Risk Finance operation is a leading provider of customized structured insurance products. Also included in DBG are the operations of AIG Environmental, which focuses specifically on providing specialty products to clients with environmental exposures. Lexington writes surplus lines, those risks for which conventional insurance companies do not readily provide insurance coverage, either because of complexity or because the coverage does not lend itself to conventional contracts.

Certain of the products of the DBG companies include funding components or have been structured in a manner such that little or no insurance risk is actually transferred. Funds received in connection with these products are recorded as deposits, and are included in other liabilities, rather than as premium revenue. Amounts paid by AIG are recorded as reductions to the deposit liability rather than as incurred losses.

The AIG Worldsource Division introduces and coordinates AIG's products and services to U.S.-based multinational clients and foreign corporations doing business in the U.S.

Transatlantic subsidiaries offer reinsurance capacity on both a treaty and facultative basis both in the U.S. and abroad. Transatlantic structures programs for a full range of property and casualty products with an emphasis on specialty risk.

AIG's Personal Lines operations provide automobile insurance through AIG Direct, the mass marketing operation of AIG, Agency Auto Division and 21st Century, as well as a broad range of coverages for high net-worth individuals through the AIG Private Client Group.

The main business of the UGC subsidiaries is the issuance of residential mortgage guaranty insurance, both domestically and internationally, on conventional first lien mortgages for the purchase or refinance of one to four family residences. UGC subsidiaries also write second lien and private student loan guaranty insurance.

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

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

A critical discipline of a successful general insurance business is the objective to produce profit from underwriting activities exclusive of investment-related income. When underwriting is not profitable, premiums are inadequate to pay for insured losses and underwriting related expenses. In these situations, the addition of general insurance related investment income and realized capital gains may, however, enable a general insurance business to produce operating income. For these reasons, AIG views underwriting results to be critical in the overall evaluation of performance.

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

GAAP provides for the recognition of expenses at the same time revenues are earned, the accounting principle of matching. Therefore, acquisition expenses are deferred and amortized over the period the related net premiums written are earned. DAC is reviewed for recoverability, and such review requires management judgment. (See also "Critical Accounting Estimates" herein.)

AIG, along with most General Insurance companies, uses the loss ratio, the expense ratio and the combined ratio as measures of underwriting performance. The loss ratio is the sum of losses and loss expenses incurred divided by net premiums earned. The expense ratio is statutory underwriting expenses divided by net premiums written. The combined ratio is the sum of the loss ratio and the expense ratio. These ratios are relative measurements that describe, for every $100 of net premiums earned or written, the cost of losses and statutory expenses, respectively. The combined ratio presents the total cost per $100 of premium production. A combined ratio below 100 demonstrates underwriting profit; a combined ratio above 100 demonstrates underwriting loss.

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

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

General Insurance operating income is comprised of statutory underwriting results, changes in DAC, net investment income and realized capital gains and losses. Operating income, as well as net premiums written, net premiums earned, net investment income and realized capital gains (losses) and statutory ratios for the three and nine-month periods ended September 30, 2006 and 2005 were as follows:

	Three Months Ended September 30,		Nine Months Ended September 30,	
(in millions, except ratios)	**2006**	2005	**2006**	2005
Net premiums written:				
Domestic General				
DBG	**$ 6,074**	$ 5,505	**$18,454**	$17,071
Transatlantic	**895**	858	**2,723**	2,627
Personal Lines	**1,162**	1,191	**3,540**	3,550
Mortgage Guaranty	**232**	149	**622**	459
Foreign General	**2,861**	2,609	**8,774**	8,039
Total	**$11,224**	$10,312	**$34,113**	$31,746
Net premiums earned:				
Domestic General				
DBG	**$ 6,290**	$ 5,613	**$17,889**	$16,773
Transatlantic	**895**	844	**2,712**	2,594
Personal Lines	**1,158**	1,182	**3,484**	3,459
Mortgage Guaranty	**191**	114	**536**	397
Foreign General[a]	**2,683**	2,381	**7,744**	7,283
Total	**$11,217**	$10,134	**$32,365**	$30,506
Net investment income[b]:				
Domestic General				
DBG	**$ 880**	$ 589	**$ 2,438**	$ 1,803
Transatlantic	**107**	87	**317**	256
Personal Lines	**56**	54	**168**	160
Mortgage Guaranty	**35**	32	**103**	91
Intercompany adjustments and eliminations – net	**1**	1	**1**	1
Foreign General	**291**	224	**1,075**	751
Total	**$ 1,370**	$ 987	**$ 4,102**	$ 3,062
Realized capital gains (losses)	**$ 28**	$ 71	**$ (29)**	$ 248
Operating Income (loss)[b][c][d]:				
Domestic General				
DBG	**$ 1,557**	$ (283)	**$ 4,448**	$ 1,235
Transatlantic	**143**	(275)	**427**	(62)
Personal Lines	**133**	18	**352**	229
Mortgage Guaranty	**85**	72	**301**	285
Foreign General[e]	**707**	326	**2,289**	1,693
Reclassifications and Eliminations	**–**	5	**2**	10
Total	**$ 2,625**	$ (137)	**$ 7,819**	$ 3,390
Statutory underwriting profit (loss)[c][d][g]				
Domestic General				
DBG	**$ 681**	$ (1,001)	**$ 1,904**	$ (755)
Transatlantic	**34**	(380)	**97**	(348)
Personal Lines	**83**	(40)	**176**	45
Mortgage Guaranty	**48**	43	**191**	195
Foreign General[e]	**376**	113	**1,034**	854
Total	**$ 1,222**	$ (1,265)	**$ 3,402**	$ (9)
Domestic General[c][d]:				
Loss Ratio	**66.85**	97.13	**68.49**	83.15
Expense Ratio	**23.72**	20.76	**21.28**	20.15
Combined Ratio	**90.57**	117.89	**89.77**	103.30
Foreign General[c][d]:				
Loss Ratio[a]	**48.91**	60.31	**50.30**	55.63
Expense Ratio[e][f]	**34.76**	31.91	**32.07**	29.57

(in millions, except ratios)	Three Months Ended September 30, 2006	2005	Nine Months Ended September 30, 2006	2005
Combined ratio	**83.67**	92.22	**82.37**	85.20
Consolidated[(c)(d)]:				
Loss Ratio	**62.56**	88.48	**64.14**	76.58
Expense Ratio	**26.54**	23.58	**24.05**	22.53
Combined Ratio	**89.10**	112.06	**88.19**	99.11

(a) Income statement accounts expressed in non-functional currencies are translated into U.S. dollars using average exchange rates.

(b) Includes the effect of out of period adjustments related to the accounting for certain interests in unit investment trusts. For DBG, for the three and nine-month periods ended September 30, 2006 the effect was an increase of $70 million and $90 million, respectively, and for Foreign General, for the three and nine-month periods ended September 30, 2006, the effect was an increase of $22 million and $434 million, respectively.

(c) Includes current year catastrophe related losses of $2.11 billion for both the three and nine-month periods ended September 30, 2005. There were no significant catastrophe related losses in the third quarter and first nine months of 2006.

(d) Includes additional losses incurred and net reinstatement premiums related to prior year catastrophes of $50 million and $39 million, in the three-month periods ended September 30, 2006 and 2005, respectively. Such losses and premiums were $108 million and $237 million in the nine-month periods ended September 30, 2006 and 2005, respectively.

(e) Includes the results of wholly owned Foreign General agencies.

(f) Includes amortization of advertising costs.

(g) Statutory underwriting profit (loss) is a measure that U.S. domiciled insurance companies are required to report to their regulatory authorities. The following table reconciles statutory underwriting profit (loss) to income before income taxes, minority interest and cumulative effect of an accounting change for the General Insurance segment for the three and nine-month periods ended September 30, 2006 and 2005.

(in millions)	Domestic Brokerage Group	Transatlantic	Personal Lines	Mortgage Guaranty	Foreign General	Reclassifications and Eliminations	Total
Three months ended September 30, 2006:							
Statutory underwriting profit	**$ 681**	**$ 34**	**$ 83**	**$ 48**	**$ 376**	**$ –**	**$ 1,222**
Increase (decrease) in deferred acquisition costs	**(30)**	**–**	**(6)**	**2**	**39**	**–**	**5**
Net investment income	**880**	**107**	**56**	**35**	**291**	**1**	**1,370**
Realized capital gains (losses)	**26**	**2**	**–**	**–**	**1**	**(1)**	**28**
Income before income taxes, minority interest and cumulative effect of an accounting change	**$ 1,557**	**$ 143**	**$133**	**$ 85**	**$ 707**	**$ –**	**$ 2,625**
Three months ended September 30, 2005:							
Statutory underwriting profit (loss)	$(1,001)	$(380)	$ (40)	$ 43	$ 113	$ –	$(1,265)
Increase (decrease) in deferred acquisition costs	49	5	5	(3)	14	–	70
Net investment income	589	87	54	32	224	1	987
Realized capital gains (losses)	80	13	(1)	–	(25)	4	71
Income before income taxes, minority interest and cumulative effect of an accounting change	$ (283)	$(275)	$ 18	$ 72	$ 326	$ 5	$ (137)
Nine months ended September 30, 2006:							
Statutory underwriting profit	**$ 1,904**	**$ 97**	**$176**	**$191**	**$1,034**	**$ –**	**$ 3,402**
Increase in deferred acquisition costs	**77**	**7**	**8**	**10**	**242**	**–**	**344**
Net investment income	**2,438**	**317**	**168**	**103**	**1,075**	**1**	**4,102**
Realized capital gains (losses)	**29**	**6**	**–**	**(3)**	**(62)**	**1**	**(29)**
Income before income taxes, minority interest and cumulative effect of an accounting change	**$ 4,448**	**$ 427**	**$352**	**$301**	**$2,289**	**$ 2**	**$ 7,819**

(in millions)	Domestic Brokerage Group	Transatlantic	Personal Lines	Mortgage Guaranty	Foreign General	Reclassifications and Eliminations	Total
Nine months ended September 30, 2005:							
Statutory underwriting profit (loss)	$ (755)	$(348)	$ 45	$195	$ 854	$ –	$ (9)
Increase (decrease) in deferred acquisition costs	(49)	6	28	(1)	105	–	89
Net investment income	1,803	256	160	91	751	1	3,062
Realized capital gains (losses)	236	24	(4)	–	(17)	9	248
Income before income taxes, minority interest and cumulative effect of an accounting change	$ 1,235	$ (62)	$229	$285	$1,693	$10	$ 3,390

AIG transacts business in most major foreign currencies. The following table summarizes the effect of changes in foreign currency exchange rates on the growth of General Insurance net premiums written for the three and nine-month periods ended September 30, 2006:

	Three Months Ended September 30, 2006	Nine Months Ended September 30, 2006
Growth in original currency	**8.5%**	**8.1%**
Foreign exchange effect	**0.3**	**(0.6)**
Growth as reported in U.S. dollars	**8.8%**	**7.5%**

General Insurance Results

General Insurance operating income increased in the third quarter of 2006 compared to the same period in 2005 due primarily to the effects of the catastrophes in the third quarter of 2005. Other factors contributing to the increase were an improvement in statutory underwriting profit for DBG as a result of improved loss ratios for the current accident year compared to the loss ratios recorded in the third quarter of 2005 for accident year 2005, as well as growth in net investment income. The combined ratio improved to 89.1 during the third quarter of 2006, a reduction of 23.0 points from the same period in 2005, primarily due to an improvement in the loss ratio of 25.9 points. The reduction in catastrophe losses represented 20.0 points of the overall decrease. Net premiums written increased 9 percent in the third quarter of 2006 compared to the same period in 2005 as domestic property rates improved, submission activity increased in both property and non-property lines in the aftermath of the 2005 hurricanes and distribution channels within Foreign General expanded. Net premiums written for the third quarter of 2005 included a reduction of $258 million for reinstatement premiums related to catastrophes, accounting for approximately 3 percentage points of the 2006 increase in net premiums written compared to the third quarter of 2005. The increase in net premiums written was tempered by an increase in ceded reinsurance necessary to manage the increase in property exposures retained by AIG.

In the third quarter of 2006, certain adjustments were made in conjunction with the remediation of balance sheet account reconciliations which increased earned premiums by $99 million and increased bad debt expense by $225 million. These adjustments reflect continuing progress in AIG's ongoing remediation efforts. The combined effect of these adjustments increased the expense ratio by 2.0 points and decreased the loss ratio by 0.6 points. Included in net investment income for the three and nine-month periods ended September 30, 2006 are $213 million and $645 million of out of period adjustments related to the accounting for certain investments in unit investment trusts and additional partnership income arising from improved valuations.

General Insurance operating income increased in the first nine months of 2006 compared to the same period of 2005 due to the reduction in catastrophe losses combined with the improvement in statutory underwriting profit for DBG as a result of improved loss ratios for the current accident year compared to the loss ratios recorded in the first nine months of 2005 for accident year 2005, as well as growth in net investment income. The combined ratio improved to 88.2, a reduction of 10.9 points from the first nine months of 2005, primarily due to an improvement in the loss ratio of 12.4 points. The reduction in catastrophe losses represented 6.7 points of the overall reduction. Net premiums written increased 7 percent as domestic property rates improved, submission activity increased in the aftermath of the 2005 hurricanes and the distribution channels within Foreign General expanded. Net premiums written for the first nine months of 2005 included a reduction of $258 million for reinstatement premiums related to catastrophes, accounting for approximately 1 percentage point of the 2006 increase in net premiums written compared to the first nine months of 2005.

Quarterly DBG Results

Operating income increased to $1.56 billion in the third quarter of 2006 compared to a loss of $283 million in the same period in 2005, an improvement of $1.84 billion.

The improvement is also reflected in the combined ratio, which declined to 90.0 in the third quarter of 2006 compared to 118.2 in the same period in 2005. The third quarter of

2005 included $1.37 billion of losses and net reinstatement premiums for major catastrophes, which increased the 2005 combined ratio by 24.3 points.

DBG's net premiums written increased 10 percent in the third quarter of 2006 compared to the same period in 2005 as property rates improved and submission activity increased in the aftermath of the 2005 hurricanes. DBG attributes the increase in submissions to its strong distribution channels and overall financial strength in comparison to many insurers that experienced significant losses and reductions of surplus as a result of the hurricanes. Net premiums written for the third quarter of 2005 were reduced by $122 million due to reinstatement premiums related to catastrophes; net premiums written for the third quarter of 2006 were increased by $47 million due to the reversal of a reinsurance contract previously accounted for as reinsurance and now accounted for as a deposit, the overall effect of which was largely offset in losses and underwriting expenses. The combined effect of these two items contributed approximately 3 percentage points to the increase in net premiums written.

The loss ratio for the third quarter of 2006 declined to 66.9 compared to 99.4 for the same period in 2005, primarily due to the effects of the catastrophes in the third quarter of 2005. Lines of business that were not directly affected by the 2005 major catastrophes also improved primarily due to lower accident year loss ratios for the 2006 accident year compared to the loss ratios recorded in the third quarter of 2005 for accident year 2005. The improvement in accident year loss ratios for the third quarter of 2006 was partially offset by an increase of $21 million in the estimated ultimate losses related to prior year hurricanes compared to the same period of 2005 which included an increase of $39 million in losses related to prior year hurricanes. Reserve development on non-catastrophic prior year losses increased incurred losses by $40 million for the third quarter of 2006 compared to an increase of $190 million for the same period of 2005.

DBG's expense ratio increased in the third quarter of 2006 to 23.1 compared to 18.8 in the same period of 2005. Net acquisition expenses as a percent of net premiums written increased by 0.5 in the third quarter of 2006 compared to the same period in 2005 due to an increase in premium assessments, partially offset by ceding commissions on quota share reinsurance programs added in 2006 to manage the level of property exposures retained by DBG. Other operating expense as a percent of net premiums written increased by 3.9 points primarily due to an increase in bad debt expense, due largely to a charge of $225 million relating to reconciliation remediation activities. Adjustments from AIG's ongoing remediation activities described above also resulted in increases of $155 million and $191 million to earned premiums and net investment income, respectively, for a net increase in operating income of $121 million in the third quarter of 2006. Incurred losses did not change as a result of the above increase to earned premiums because the adjustment was isolated to the reconciliation of unearned premium balances.

The combined effect of the out of period and other adjustments in the third quarter of 2006 was a decrease in the DBG loss ratio of 1.7 points and an increase in the expense ratio of 3.7 points.

Year-to-date DBG Results

Operating income increased to $4.45 billion in the first nine months of 2006 compared to $1.24 billion in the same period in 2005, an improvement of $3.21 billion.

The improvement is also reflected in the combined ratio, which declined to 88.7 in the first nine months of 2006 compared to 104.2 in the same period in 2005. The first nine months of 2005 included $1.37 billion of losses and net reinstatement premiums for major catastrophes, which increased the 2005 combined ratio by 8.1 points.

DBG's net premiums written increased 8 percent in the first nine months of 2006 compared to the same period of 2005 due to property rate increases as well as increases in submission activity in the aftermath of the 2005 hurricanes. Net premiums written for the first nine months of 2005 were reduced by $122 million due to reinstatement premiums related to catastrophes; net premiums written for the first nine months of 2006 were increased by $47 million due to the reversal of a reinsurance contract previously accounted for as reinsurance and now accounted for as a deposit, the overall effect of which was largely offset in losses and underwriting expenses. The combined effect of these two items contributed approximately 1 percentage point to the increase in net premiums written.

The loss ratio for the first nine months of 2006 declined to 69.0 compared to 85.7 for the same period in 2005, primarily due to the effects of the catastrophes in the first nine months of 2005. Lines of business that were not directly affected by the 2005 major catastrophes also improved, primarily due to lower accident year loss ratios for the 2006 accident year compared to the loss ratios recorded in the third quarter of 2005 for accident year 2005. In addition, year-to-date 2006 operating income included a $4 million reduction in the estimated ultimate losses related to prior year hurricanes compared to the same period of 2005, which included $157 million of increased losses related to prior year hurricanes. Favorable reserve development on non-catastrophic prior year losses totaled $25 million for the first nine months of 2006 compared to adverse development of $410 million for the same period of 2005. The 2006 development relates primarily to classes of business which did not require reserve strengthening in connection with AIG's year-end 2005 reserve study.

DBG's expense ratio increased to 19.8 percent in the first nine months of 2006 compared to 18.4 percent for the same pe-

riod in 2005. Net acquisition expenses as a percent of net premiums written declined 0.5 points in the first nine months of 2006 compared to the same period in 2005 despite the increase in premium assessments in the third quarter of 2006, reflecting an increase in lines of business such as property that have a lower commission rate, a modest decrease in overall commission rates and the new quota share reinsurance programs added in 2006 to manage the level of property exposures retained by DBG. Other operating expenses as a percent of net premiums written increased 1.3 points primarily due to an increase in bad debt expense, due largely to a charge of $225 million relating to reconciliation remediation activities.

Quarterly Transatlantic Results

Transatlantic's net premiums written and net premiums earned in the third quarter of 2006 increased by 4 percent and 6 percent, respectively, when compared to the same period in 2005 primarily due to increases in domestic other liability, medical malpractice and accident and health net premiums written. These increases were partially offset by decreases in domestic property, principally homeowners, and international medical malpractice premiums. Third quarter 2006 operating income increased due largely to lower catastrophe losses and net ceded reinstatement premiums and increased net investment income.

Year-to-date Transatlantic Results

Transatlantic's net premiums written and net premiums earned increased in the first nine months of 2006 by 4 percent and 5 percent, respectively, compared to the same period of 2005 due primarily to increases in domestic other liability, medical malpractice and accident and health net premiums written. These increases were offset, in part, by decreases in international premiums with the most significant decreases in the auto liability and property lines. Operating income increased in the first nine months of 2006 compared to the same period of 2005 due to lower catastrophe losses and net ceded reinstatement premiums, and increased net investment income.

Quarterly Personal Lines Results

Personal Lines net premiums written and net premiums earned decreased slightly in the third quarter of 2006 compared to the same period in 2005, as growth in the Private Client Group was offset by the run-off of the involuntary auto business and declines in the AIG Direct, Agency Auto and 21st Century divisions. Growth in the Private Client Group spans multiple products, with continued penetration into the high net worth market and strong brand and innovative loss prevention programs. The soft auto market, with flat to declining rates, is adversely affecting growth in the direct business of AIG Direct and 21st Century. 21st Century is experiencing solid performance outside of California, however, it is not outpacing the decline in California. Agency Auto growth is down due to pricing and underwriting pressure in certain markets. Operating income in the third quarter of 2006 increased from the same period in 2005 driven by an improved loss ratio. Operating income in 2005 included $62 million of hurricane Katrina losses and related reinstatement premiums whereas operating income in 2006 is benefiting from favorable development of prior period reserves.

Year-to-date Personal Lines Results

Personal Lines net premiums written decreased slightly in the first nine months of 2006 compared to the same period in 2005, with growth in the Private Client Group and Agency Auto divisions being offset by the run-off of the involuntary auto business and small declines in the AIG Direct and 21st Century divisions. Operating income increased for the first nine months of 2006 compared to the same period of 2005, driven primarily by a lower loss ratio. Operating income in 2005 included $62 million of hurricane Katrina losses and related reinstatement premiums whereas operating income in 2006 is benefiting from an absence of catastrophes and favorable prior year reserve development. The expense ratio has increased in 2006, compared to the year ago period, primarily due to investments in people and technology, national expansion efforts and lower response rates.

Quarterly UGC Results

Mortgage Guaranty net premiums written were up 56 percent for the third quarter of 2006 compared to the same period in 2005. All business segments contributed to the increase. Operating income for the three months ended September 30, 2005 was negatively affected by $29 million of ceded premiums for the domestic first lien business. Incurred losses were up compared to the third quarter of 2005 due to aging of the first lien portfolio and a slowing domestic housing market. Additionally, early loss development of alternative risk products and growth in insurance in–force in 2006 drove the increases in domestic second lien losses. Operating income for the third quarter of 2006 was up 18 percent compared to the prior period, with improvements in all business units.

Year-to-date UGC Results

Mortgage Guaranty net premiums written were up 36 percent for the first nine months of 2006 compared to the same period in 2005. All business units contributed to the increase. Operating income for the first nine months of 2005 was negatively affected by $29 million of ceded premiums for domestic first lien business. Incurred losses increased from the same period in 2005, due to aging of the first lien portfolio, a slowing domestic housing market, early loss development of alternative risk second lien product and growth in the domestic second lien insurance in–force. Operating income for the first nine months of 2006 increased by 6 percent over the prior year period.

Quarterly Foreign General Insurance Results

Foreign General Insurance net premiums written increased 10 percent (9 percent in original currency) in the third quarter of 2006 when compared to the same period in 2005. This increase is due to growth in both the commercial and consumer lines driven by new business, new distribution channels, including the acquisition of Central Insurance Co., Ltd. in Taiwan, and higher premiums for the Ascot Lloyd's syndicate. Lower reinstatement premium costs, which in 2005 were unusually high due to hurricanes Katrina and Rita, contributed two percent to the increase in net premiums written. The personal accident business net premiums written increased in the third quarter of 2006 from a year ago, but an increase in loss frequency negatively affected operating income. The commercial lines net premiums written in Europe, the Far East and the United Kingdom increased from a year ago due to new business with a resulting increase in operating income compared to the third quarter of 2005. Operating income from energy lines, primarily in the United Kingdom, and the Ascot Lloyd's syndicate both increased compared to the third quarter of 2005 due to increased net premiums written in 2006 and losses incurred in the third quarter of 2005 relating to catastrophe events.

The combined ratio for Foreign General Insurance for the third quarter of 2006 was 83.7, an improvement of 8.5 points from 92.2 in the comparable period of 2005. The Foreign General Insurance loss ratio decreased 11.4 points in the third quarter of 2006 compared to the same period of 2005. The results of 2006 benefited from lower current accident year losses and favorable loss development from prior accident years, excluding catastrophes, of $105 million, offset by $21 million of adverse loss development on the 2005 hurricanes and by $22 million of losses related to a typhoon in Japan during the third quarter of 2006. The results for 2005 included several catastrophic events, principally hurricanes Katrina and Rita. The Foreign General Insurance expense ratio increased 2.9 points in the third quarter of 2006 from the same period in 2005, principally due to higher commission costs, the increased significance of consumer lines of business, which have higher acquisition costs, accelerated amortization of advertising costs and premium reductions of $56 million relating to reconciliation remediation activities. Due to the current mix of business, AIG expects commission costs to continue to increase over the next quarter, principally for classes of business with historically lower than average loss ratios.

Year-to-date Foreign General Insurance Results

Foreign General Insurance net premiums written increased 9 percent (12 percent in original currency) in the first nine months of 2006 compared to the same period in 2005, reflecting growth in both the commercial and consumer lines. The personal accident business in the Far East region, the commercial lines business in both Europe and the United Kingdom, and the Ascot Lloyd's syndicate all contributed to the growth in net premiums written. Operating income showed corresponding increases over the prior year, which included significant losses related to hurricanes Katrina and Rita.

The combined ratio for Foreign General Insurance for the first nine months of 2006 was 82.4, an improvement of 2.8 points from 2005. The Foreign General Insurance loss ratio decreased 5.3 points in the first nine months of 2006 from the same period of 2005 due to lower current accident year losses, favorable loss development from prior accident years and fewer catastrophes. The Foreign General Insurance expense ratio increased 2.5 points in the first nine months of 2006 from the same period in 2005 principally due to higher commission costs, the increased significance of consumer lines of business, which have higher acquisition costs and accelerated amortization of advertising costs.

Quarterly General Insurance Net Investment Income

General Insurance net investment income increased by $383 million in the third quarter of 2006, when compared to the same period of 2005 due to strong cash flows, including the effect of capital contributions from the parent, higher partnership income for DBG and the out of period adjustments relating to unit investment trust and partnership investments. Foreign General net investment income for the third quarter increased compared to the same period in 2005 due to strong cash flows, resulting from higher premium collections and reinsurance loss recoveries, as well as higher interest rates.

Year-to-date General Insurance Net Investment Income

General Insurance net investment income increased by $1.04 billion in the first nine months of 2006, when compared to the same period of 2005. The increase for the nine month period is principally due to the effects of out of period adjustments of $524 million related to the accounting for certain interests in unit investment trusts, $121 million of out of period adjustments for partnership income and a second quarter 2006 $85 million out of period adjustment related to interest earned on a DBG deposit contract. Foreign General Insurance net investment income increased in the nine-month period ended September 30, 2006 compared to the same period of 2005 due to the effects of the out of period adjustments, offset by a decline in partnership income. Foreign General partnership income in the first nine months of 2005 benefited from increases in market valuations due to increased initial public offering activity.

Realized capital gains and losses resulted from the ongoing investment management of the General Insurance portfolios within the overall objectives of the General Insurance operations. See the discussion on "Valuation of Invested Assets" herein.

Reinsurance

AIG is a major purchaser of reinsurance for its General Insurance operations. AIG insures risks globally, and its reinsurance programs must be coordinated in order to provide AIG the level of reinsurance protection that AIG desires. Reinsurance is an important risk management tool to manage transaction and insurance line risk retention at prudent levels set by management. AIG also purchases reinsurance to mitigate its catastrophic exposure. AIG is cognizant of the need to exercise good judgment in the selection and approval of both domestic and foreign companies participating in its reinsurance programs because one or more catastrophe losses could negatively affect AIG's reinsurers and result in an inability of AIG to collect reinsurance recoverables. AIG's reinsurance department evaluates catastrophic events and assesses the probability of occurrence and magnitude of catastrophic events through the use of state-of-the-art industry recognized program models, among other techniques. AIG supplements these models through continually monitoring the risk exposure of AIG's worldwide General Insurance operations and adjusting such models accordingly. For a further discussion of catastrophe exposures, see "Managing Risk – Catastrophe Exposures." Although reinsurance arrangements do not relieve AIG from its direct obligations to its insureds, an efficient and effective reinsurance program substantially limits AIG's exposure to potentially significant losses. With respect to its property business, AIG has either renewed existing reinsurance coverage or purchased new coverage that, in the opinion of management, is adequate to limit AIG's exposures. AIG continually evaluates the reinsurance markets and the relative attractiveness of various arrangements for coverage, including structures such as catastrophe bonds, insurance risk securitizations and "sidecar" and similar vehicles. Effective July 15, 2006, AIG's Lexington Insurance Company (Lexington) and Concord Re Limited (Concord Re), a "sidecar" reinsurer that was established exclusively to reinsure Lexington, entered into a quota share reinsurance agreement covering the U.S. commercial property insurance business written by Lexington. Concord Re was capitalized with approximately $730 million through the issuance of equity securities and loans from third party investors. AIG and its subsidiaries invest in a wide variety of investment vehicles managed by third parties where AIG has no control over investment decisions. Accordingly, there can be no assurance that such vehicles do not, or will not, hold securities of Concord Re.

AIG's consolidated general reinsurance assets amounted to $22.99 billion at September 30, 2006 and resulted from AIG's reinsurance arrangements. Thus, a credit exposure existed at September 30, 2006 with respect to reinsurance recoverable to the extent that any reinsurer may not be able to reimburse AIG under the terms of these reinsurance arrangements. AIG manages its credit risk in its reinsurance relationships by transacting with reinsurers that it considers financially sound, and when necessary AIG holds substantial collateral in the form of funds, securities and/or irrevocable letters of credit. This collateral can be drawn on for amounts that remain unpaid beyond specified time periods on an individual reinsurer basis. At December 31, 2005, approximately 48 percent of the general reinsurance assets were from unauthorized reinsurers. Many of these balances were collateralized, permitting statutory recognition. Additionally, with the approval of its domiciliary insurance regulators, AIG posted approximately $1.5 billion of letters of credit issued by several commercial banks in favor of certain Domestic General Insurance companies to permit those companies statutory recognition of balances otherwise uncollateralized at December 31, 2005. The remaining 52 percent of the general reinsurance assets were from authorized reinsurers. The terms authorized and unauthorized pertain to regulatory categories, not creditworthiness. At December 31, 2005, approximately 88 percent of the balances with respect to authorized reinsurers are from reinsurers rated A (excellent) or better, as rated by A.M. Best, or A (strong) or better, as rated by Standard & Poor's, a division of The McGraw-Hill Companies, Inc. (S&P). These ratings are measures of financial strength. Through September 30, 2006, there has been no significant deterioration in the rating profile of AIG's reinsurers representing more than five percent of AIG's reinsurance assets as of December 31, 2005.

AIG maintains an allowance for estimated unrecoverable reinsurance. Although AIG has been largely successful in its previous recovery efforts, at September 30, 2006, AIG had an allowance for unrecoverable reinsurance approximating $447 million. The allowance was reduced substantially during 2006, as uncollectible amounts due from individual reinsurers were charged off against the allowance, primarily due to the balance sheet reconciliation remediation process; in addition, a portion of the allowance was reclassified to align it with the related receivable. The reduction for charge offs was partially offset by additional provisions totaling $92 million during the nine months ended September 30, 2006. At September 30, 2006, AIG had no significant reinsurance recoverables due from any individual reinsurer that was financially troubled (e.g., liquidated, insolvent, in receivership or otherwise subject to formal or informal regulatory restriction).

AIG's Reinsurance Security Department conducts ongoing detailed assessments of the reinsurance markets and current and potential reinsurers, both foreign and domestic. Such assessments include, but are not limited to, identifying if a reinsurer is appropriately licensed and has sufficient financial capacity, and evaluating the local economic environment in which a foreign reinsurer operates. This department also reviews the nature of the risks ceded and the requirements for credit risk mitigants. For example, in AIG's treaty reinsurance contracts, AIG includes provisions that frequently require a reinsurer to post collateral when a referenced event occurs.

Furthermore, AIG limits its unsecured exposure to reinsurers through the use of credit triggers, which include, but are not limited to, insurer financial strength rating downgrades, policyholder surplus declines at or below a certain predetermined level or a certain predetermined level of a reinsurance recoverable being reached. In addition, AIG's Credit Risk Committee reviews the credit limits for and concentrations with any one reinsurer.

AIG enters into intercompany reinsurance transactions, primarily through American International Reinsurance Company, Ltd. (AIRCO), for its General Insurance and Life Insurance operations. AIG enters into these transactions as a sound and prudent business practice in order to maintain underwriting control and spread insurance risk among AIG's various legal entities. All material intercompany transactions have been eliminated in consolidation. AIG generally obtains letters of credit in order to obtain statutory recognition of these intercompany reinsurance transactions. At September 30, 2006, approximately $3.7 billion of letters of credit were outstanding to cover intercompany reinsurance transactions with AIRCO or other General Insurance subsidiaries.

At September 30, 2006, consolidated general reinsurance assets of $22.99 billion include reinsurance recoverables for paid losses and loss expenses of $1.58 billion and $18.35 billion with respect to the ceded reserve for losses and loss expenses, including ceded losses incurred but not reported (IBNR) (ceded reserves) and $3.07 billion of ceded reserve for unearned premiums. The ceded reserve for losses and loss expenses represent the accumulation of estimates of ultimate ceded losses including provisions for ceded IBNR and loss expenses. The methods used to determine such estimates and to establish the resulting ceded reserves involve significant judgment in projecting the frequency and severity of losses over multiple years and are continually reviewed and updated by management. Any adjustments thereto are reflected in income currently. It is AIG's belief that the ceded reserves for losses and loss expenses at September 30, 2006 were representative of the ultimate losses recoverable. In the future, as the ceded reserves continue to develop to ultimate amounts, the ultimate loss recoverable may be greater or less than the reserves currently ceded.

Reserve for Losses and Loss Expenses

The table below classifies as of September 30, 2006 and December 31, 2005 the components of the General Insurance gross reserve for losses and loss expenses (loss reserves) by major lines of business on a statutory Annual Statement basis*:

(in millions)	**September 30, 2006**	December 31, 2005
Other liability occurrence	**$18,879**	$18,116
Other liability claims made	**12,768**	12,447
Workers compensation	**12,751**	11,630
Property	**6,634**	7,217
Auto liability	**6,351**	6,569
International	**5,376**	4,939
Reinsurance	**3,419**	2,886
Medical malpractice	**2,200**	2,363
Products liability	**1,988**	1,937
Accident and health	**1,727**	1,678
Aircraft	**1,642**	1,844
Commercial multiple peril	**1,449**	1,359
Fidelity/surety	**1,015**	1,072
Other	**3,664**	3,112
Total	**$79,863**	$77,169

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

AIG's gross reserve for losses and loss expenses represents the accumulation of estimates of ultimate losses, including IBNR and loss expenses. The methods used to determine loss reserve estimates and to establish the resulting reserves are continually reviewed and updated by management. Any adjustments resulting therefrom are reflected in operating income currently. Because loss reserve estimates are subject to the outcome of future events, changes in estimates are unavoidable given that loss trends vary and time is often required for changes in trends to be recognized and confirmed. Reserve changes that increase previous estimates of ultimate cost are referred to as unfavorable or adverse development or reserve strengthening. Reserve changes that decrease previous estimates of ultimate cost are referred to as favorable development.

At September 30, 2006, General Insurance net loss reserves increased $4.04 billion from the prior year end to $61.51 billion. The net loss reserves represent loss reserves reduced by reinsurance recoverables, net of an allowance for unrecoverable reinsurance and applicable discount for future investment income. The table below classifies the components of the General Insurance net loss reserves by business unit as of September 30, 2006 and December 31, 2005.

(in millions)	**September 30, 2006**	December 31, 2005
DBG[(a)]	**$ 43,383**	$40,782
Transatlantic	**6,118**	5,690
Personal Lines[(b)]	**2,486**	2,578
Mortgage Guaranty	**390**	340
Foreign General[(c)]	**9,136**	8,086
Total Net Loss Reserve	**$ 61,513**	$57,476

(a) At September 30, 2006 and December 31, 2005, DBG loss reserves include approximately $3.50 billion and $3.77 billion, respectively, ($3.87 billion and $4.26 billion, respectively, before discount) related to

business written by DBG but ceded to AIRCO and reported in AIRCO's statutory filings. DBG loss reserves also include approximately $532 million and $407 million related to business included in AIUO's statutory filings at September 30, 2006 and December 31, 2005, respectively.

(b) At September 30, 2006 and December 31, 2005, Personal Lines loss reserves include $876 million and $878 million, respectively, related to business ceded to DBG and reported in DBG's statutory filings.

(c) At September 30, 2006 and December 31, 2005, Foreign General loss reserves include approximately $2.70 billion and $2.15 billion, respectively, related to business reported in DBG's statutory filings.

The DBG net loss reserve of $43.38 billion is comprised principally of the business of AIG subsidiaries participating in the American Home/National Union pool (11 companies) and the surplus lines pool (Lexington, Starr Excess Liability Insurance Company and Landmark Insurance Company).

Beginning in 1998, DBG ceded a quota share percentage of its other liability occurrence and products liability occurrence business to AIRCO. The quota share percentage ceded was 40 percent in 1998, 65 percent in 1999, 75 percent in 2000 and 2001, 50 percent in 2002 and 2003, 40 percent in 2004, 35 percent in 2005 and 20 percent in 2006 and covered all business written in these years for these lines by participants in the American Home/National Union pool. In 1998 the cession reflected only the other liability occurrence business, but in 1999 and subsequent years included products liability occurrence. AIRCO's loss reserves relating to these quota share cessions from DBG are recorded on a discounted basis. As of September 30, 2006, AIRCO carried a discount of approximately $370 million applicable to the $3.87 billion in undiscounted reserves it assumed from the American Home/National Union pool via this quota share cession. AIRCO also carries approximately $478 million in net loss reserves relating to Foreign General insurance business. These reserves are carried on an undiscounted basis.

Beginning in 1997, the Personal Lines division ceded a percentage of all business written by the companies participating in the personal lines pool to the American Home/National Union pool. As noted above, the total reserves carried by participants in the American Home/National Union pool relating to this cession amounted to $876 million as of September 30, 2006.

The companies participating in the American Home/National Union pool have maintained a participation in the business written by AIU for decades. As of September 30, 2006, these AIU reserves carried by participants in the American Home/National Union pool amounted to approximately $2.70 billion. The remaining Foreign General reserves are carried by AIUO, AIRCO, and other smaller AIG subsidiaries domiciled outside the United States. Statutory filings in the U.S. by AIG companies reflect all the business written by U.S. domiciled entities only, and therefore exclude business written by AIUO, AIRCO, and all other internationally domiciled subsidiaries. The total reserves carried at September 30, 2006 by AIUO and AIRCO were approximately $4.35 billion and $3.98 billion, respectively. AIRCO's $3.98 billion in total general insurance reserves consist of approximately $3.50 billion from business assumed from the American Home/National Union pool and an additional $478 million relating to Foreign General Insurance business.

Discounting of Reserves

At September 30, 2006, AIG's overall General Insurance net loss reserves reflects a loss reserve discount of $2.11 billion, including tabular and non-tabular calculations. The tabular workers compensation discount is calculated using a 3.5 percent interest rate and the 1979-81 Decennial Mortality Table. The non-tabular workers compensation discount is calculated separately for companies domiciled in New York and Pennsylvania, and follows the statutory regulations for each state. For New York companies, the discount is based on a five percent interest rate and the companies' own payout patterns. For Pennsylvania companies, the statute has specified discount factors for accident years 2001 and prior, which are based on a six percent interest rate and an industry payout pattern. For accident years 2002 and subsequent, the discount is based on the yield of U.S. Treasury securities ranging from one to twenty years and the company's own payout pattern, with the future expected payment for each year using the interest rate associated with the corresponding Treasury security yield for that time period. The discount is comprised of the following: $512 million – tabular discount for workers compensation in DBG; $1.23 billion – non-tabular discount for workers compensation in DBG; and, $370 million – non-tabular discount for other liability occurrence and products liability occurrence in AIRCO. The total undiscounted workers compensation loss reserve carried by DBG is approximately $10.6 billion as of September 30, 2006. The other liability occurrence and products liability occurrence business in AIRCO that is assumed from DBG is discounted based on the yield of U.S. Treasury securities ranging from one to twenty years and the DBG payout pattern for this business. The undiscounted reserves assumed by AIRCO from DBG totaled approximately $3.87 billion at September 30, 2006.

Quarterly Reserving Process

It is management's belief that the General Insurance net loss reserves are adequate to cover General Insurance net losses and loss expenses as of September 30, 2006. While AIG regularly reviews the adequacy of established loss reserves, there can be no assurance that AIG's ultimate loss reserves will not develop adversely and materially exceed AIG's loss reserves as of September 30, 2006. In the opinion of management, such adverse development and resulting increase in reserves is not likely to have a material adverse effect on AIG's consolidated financial position, although it could have a material adverse effect on AIG's consolidated results of operations for an individual reporting period.

The table below presents the reconciliation of General Insurance net loss reserves for the three and nine-month periods ended September 30, 2006 and 2005 as follows:

(in millions)	Three Months Ended September 30, 2006	Three Months Ended September 30, 2005	Nine Months Ended September 30, 2006	Nine Months Ended September 30, 2005
Net reserve for losses and loss expenses at beginning of period	**$60,214**	$50,564	**$57,476**	$47,254
Foreign exchange effect	**34**	(33)	**521**	(354)
Acquisition[(a)]	**55**	—	**55**	—
Losses and loss expenses incurred:				
Current year	**6,957**	8,626	**20,710**	22,697
Prior years, other than accretion of discount[(b)]	**(41)**	244	**(255)**	374
Prior years, accretion of discount	**101**	97	**303**	291
Losses and loss expenses incurred	**7,017**	8,967	**20,758**	23,362
Losses and loss expenses paid	**5,807**	5,439	**17,297**	16,203
Net reserve for losses and loss expenses at end of period	**$61,513**	$54,059	**$61,513**	$54,059

(a) *Reflects the opening balance with respect to the acquisition of the Central Insurance Co., Ltd. in the third quarter of 2006.*

(b) *Includes $24 million and $30 million in the three-month periods ended September 30, 2006 and 2005, respectively, for the general reinsurance operations of Transatlantic and $43 million and $39 million, respectively, of additional losses incurred resulting from 2005 and 2004 catastrophes. Includes $89 million and $120 million in the nine-month periods ended September 30, 2006 and 2005, respectively, for the general reinsurance operations of Transatlantic and $80 million and $157 million, respectively, of additional losses incurred resulting from 2005 and 2004 catastrophes. Transatlantic included $4 million and $24 million of prior years adverse catastrophe development in the three and nine months ended September 30, 2006, respectively.*

The loss ratios recorded by AIG for the first nine months of 2006 take into account the results of the comprehensive reserve reviews that were completed in the fourth quarter of 2005. As explained more fully in the 2005 Annual Report on Form 10-K/A, AIG's year-end 2005 reserve review reflected careful consideration of the reserve analyses prepared by AIG's internal actuarial staff with the assistance of third party actuaries. In determining the appropriate loss ratios for accident year 2006 for each class of business, AIG gave appropriate consideration to the loss ratios resulting from the reserve analyses as well as all other relevant information including rate changes, expected changes in loss costs, changes in coverage, reinsurance or mix of business, and other factors that may affect the loss ratios.

In the first nine months of 2006, AIG enhanced its process of determining the quarterly loss development from prior accident years. In the first quarter of 2006, AIG began conducting additional analyses to determine the change in estimated ultimate loss for each accident year for each profit center. For example, if loss emergence for a profit center is different than expected for certain accident years in the quarter, the actuaries now take additional steps to examine the indicated effect such emergence would have on the reserves of that profit center. In some cases, the higher or lower than expected emergence may result in no clear change in the ultimate loss estimate for the accident years in question, and no adjustment would be made to the profit center's reserves for prior accident years. In other cases, the higher or lower than expected emergence may result in a larger change, either favorable or unfavorable, than the difference between the actual and expected loss emergence. Such additional analyses were conducted for each profit center, as appropriate, in the first, second and third quarters of 2006 to determine the loss development from prior accident years for the first, second and third quarters of 2006. As part of its quarterly reserving process, AIG also considers notices of claims received with respect to emerging issues, such as those related to stock option backdating.

In the third quarter of 2006, net loss development from prior accident years was favorable by approximately $41 million, including approximately $43 million of adverse development pertaining to the major hurricanes in 2005 and 2004 and $24 million of adverse development pertaining to the general reinsurance operations of Transatlantic. Excluding catastrophes and Transatlantic, as well as accretion of discount of approximately $101 million, net loss development from prior accident years in the third quarter of 2006 was favorable by approximately $108 million. This overall favorable development of $108 million consisted of approximately $490 million of favorable development from accident years 2003 through 2005, partially offset by approximately $380 million of adverse development from accident years 2002 and prior. The $490 million of favorable development from accident years 2003 through 2005 included approximately $310 million from accident year 2005, $160 million from accident year 2004, and $20 million from accident year 2003. The adverse development from accident years 2002 and prior included approximately $130 million from accident year 1999, primarily due to two significant claims, with the balance spread across many accident years. Foreign General prior accident year reserves, excluding catastrophes, developed favorably by approximately $105 million in the quarter. DBG prior accident year reserves, excluding catastrophes, developed adversely by approximately $40 million. The overall development also included approximately $22 million of favorable development from Personal Lines and approximately $21 million of favorable development from UGC. The

favorable developments experienced in Foreign General included both short tail as well as longer tail classes of business.

In the first nine months of 2006, net loss development from prior accident years was favorable by approximately $255 million, including approximately $80 million of adverse development pertaining to the major hurricanes in 2004 and 2005 and $89 million of adverse development from the general reinsurance operations of Transatlantic. Excluding catastrophes and Transatlantic, as well as accretion of discount of approximately $303 million, net loss development from prior accident years in the first nine months of 2006 was favorable by approximately $424 million. This overall favorable development of $424 million consisted of approximately $1.23 billion of favorable development from accident years 2003 through 2005, partially offset by approximately $805 million of adverse development from accident years 2002 and prior. The $1.23 billion of favorable development from accident years 2003 through 2005 included approximately $550 million from accident year 2005, $450 million from accident year 2004, and $230 million from accident year 2003. The adverse developments from accident years 2002 and prior were widely spread among many accident years. The overall favorable development of $424 million included approximately $235 million from Foreign General, $80 million from Personal Lines, $85 million from UGC, and $25 million from DBG. For both the third quarter and the first nine months of 2006, most classes of business throughout AIG continued to experience favorable development for accident years 2003 through 2005. The adverse development from accident years 2002 and prior reflected developments from excess casualty, workers compensation, excess workers compensation, and post-1986 environmental liability classes of business, all within DBG.

As a result of the continued favorable experience for accident years 2003 through 2005, the expected loss ratios for accident year 2006 were improved for a number of casualty classes of business in the third quarter of 2006. For those classes of business where the expected loss ratio for accident year 2006 was adjusted in the third quarter, the revised loss ratio was generally applied to the cumulative 2006 net earned premium for the class. The overall effect on the third quarter results was approximately a $100 million improvement. This amount represents the application of the revised expected loss ratios to the net premiums earned reported for the first six months of 2006.

In the third quarter of 2005, net loss development from prior accident years was adverse by approximately $244 million, including approximately $39 million of adverse development pertaining to the major hurricanes from accident year 2004 and approximately $30 million of adverse development pertaining to the general reinsurance operations of Transatlantic. Excluding catastrophes and Transatlantic, as well as accretion of discount of approximately $97 million, net loss development from prior accident years in the third quarter of 2005 was adverse by approximately $175 million. In the third quarter of 2005, most classes of business experienced favorable development for accident years 2003 and 2004 and adverse development for accident years 2001 and prior. The overall development of $175 million consisted of approximately $350 million of adverse development from accident years 2001 and prior, partially offset by approximately $170 million of favorable development from accident year 2004 and $30 million of favorable development from accident year 2003. Accident year 2002 experienced adverse development for D&O and excess casualty, with an overall adverse development of approximately $20 million in the quarter. For all accident years combined, the D&O and excess casualty classes accounted for the vast majority of the $175 million overall adverse development in the quarter. The $175 million of overall adverse development, excluding catastrophes, was comprised of approximately $190 million of adverse development from DBG, $15 million of adverse development from Foreign General, and $15 million of favorable development from each of the Personal Lines and UGC segments.

In the first nine months of 2005, net loss development from prior accident years was adverse by approximately $375 million, including approximately $157 million of adverse development from the major hurricanes from accident year 2004 and approximately $120 million of adverse development from the general reinsurance operations of Transatlantic. Excluding catastrophes and Transatlantic, as well as accretion of discount of approximately $291 million, net loss development from prior accident years in the first nine months of 2005 was adverse by approximately $98 million. The overall development of $98 million consisted of approximately $1.13 billion of adverse development from accident years 2002 and prior, offset by approximately $740 million of favorable development from accident year 2004 and approximately $290 million of favorable development from accident year 2003. Most classes of business produced favorable development for accident years 2003 and 2004, and adverse development for accident years 2001 and prior. The majority of the adverse development from accident year 2002 and prior was attributable to the D&O and excess casualty classes of business. Accident year 2002 experienced favorable development for many classes of business. However, in total, accident year 2002 experienced approximately $50 million of adverse development primarily attributable to approximately $125 million of adverse development from the D&O class. The overall adverse development of $98 million for all prior accident years, excluding catastrophes, was comprised of approximately $410 million of adverse development from DBG, $190 million of favorable development from Foreign General, $60 million of favorable development from Personal Lines, and $62 million of favorable development from UGC.

Loss Reserving Process

The General Insurance loss reserves can generally be categorized into two distinct groups. One group is long-tail casualty lines of business which include excess and umbrella liability, D&O, professional liability, medical malpractice, workers compensation, general liability, products liability, and related classes. The other group is short-tail lines of business consisting principally of property lines, personal lines and certain classes of casualty lines. These lines of business and actuarial assumptions made in the review of these lines of business are described in the 2005 Annual Report on Form 10-K/A.

The process of determining the current loss ratio for each class or business segment is based on a variety of factors and is described in detail in AIG's 2005 Annual Report on Form 10-K/A. AIG uses the process described above to update AIG's reserves on a quarterly basis. AIG's 2005 Annual Report on Form 10-K/A also includes a discussion and analysis of the volatility of AIG's 2005 reserve estimates and a sensitivity analysis.

Asbestos and Environmental Reserves

The estimation of loss reserves relating to asbestos and environmental claims on insurance policies written many years ago is subject to greater uncertainty than other types of claims due to inconsistent court decisions as well as judicial interpretations and legislative actions that in some cases have tended to broaden coverage beyond the original intent of such policies and in others have expanded theories of liability.

As described more fully in the 2005 Annual Report on Form 10-K/A, AIG's reserves relating to asbestos and environmental claims reflect the results of the comprehensive ground up analysis which was completed in the fourth quarter of 2005. AIG is in the process of updating its ground up analysis and expects to continue to do so on an annual basis. In the first nine months of 2006, AIG maintained the ultimate loss estimates for asbestos and environmental claims resulting from the recently completed reserve analyses. A minor amount of incurred loss emergence pertaining to asbestos was reflected in the first nine months of 2006, as depicted in the table that follows. This minor development is primarily attributable to the general reinsurance operations of Transatlantic.

A summary of reserve activity, including estimates for applicable IBNR, relating to asbestos and environmental claims separately and combined for the nine months ended September 30, 2006 and 2005 follows:

	2006		2005	
(in millions)	**Gross**	**Net**	Gross	Net
Asbestos:				
Reserve for losses and loss expenses at beginning of year	**$4,441**	**$1,840**	$2,559	$1,060
Losses and loss expenses incurred*	**2**	**7**	120	33
Losses and loss expenses paid*	**(404)**	**(151)**	(239)	(91)
Reserve for losses and loss expenses at end of period	**$4,039**	**$1,696**	$2,440	$1,002
Environmental:				
Reserve for losses and loss expenses at beginning of year	**$ 926**	**$ 410**	$ 974	$ 451
Losses and loss expenses incurred*	**(3)**	**—**	(9)	(2)
Losses and loss expenses paid*	**(80)**	**(43)**	(81)	(52)
Reserve for losses and loss expenses at end of period	**$ 843**	**$ 367**	$ 884	$ 397
Combined:				
Reserve for losses and loss expenses at beginning of year	**$5,367**	**$2,250**	$3,533	$1,511
Losses and loss expenses incurred*	**(1)**	**7**	111	31
Losses and loss expenses paid*	**(484)**	**(194)**	(320)	(143)
Reserve for losses and loss expenses at end of period	**$4,882**	**$2,063**	$3,324	$1,399

** All amounts pertain to policies underwritten in prior years.*

As indicated in the table above, asbestos loss payments increased significantly in the first nine months of 2006 compared to the same period in the prior years, primarily as a result of payments pertaining to settlements that had been negotiated in earlier periods. There was negligible development of asbestos and environmental reserves in the first nine months of 2006.

The gross and net IBNR included in the reserve for losses and loss expenses, relating to asbestos and environmental claims separately and combined, at September 30, 2006 and 2005 were estimated as follows:

	2006		2005	
(in millions)	**Gross**	**Net**	Gross	Net
Asbestos	**$2,863**	**$1,312**	$1,550	$ 684
Environmental	**567**	**242**	558	253
Combined	**$3,430**	**$1,554**	$2,108	$ 937

A summary of asbestos and environmental claims count activity for the nine months ended September 30, 2006 and 2005 was as follows:

	2006			2005		
	Asbestos	**Environmental**	**Combined**	Asbestos	Environmental	Combined
Claims at beginning of year	**7,293**	**9,873**	**17,166**	7,575	8,216	15,791
Claims during year:						
Opened	**538**	**1,032**	**1,570**	646	4,583	5,229
Settled	**(126)**	**(120)**	**(246)**	(49)	(178)	(227)
Dismissed or otherwise resolved	**(678)**	**(1,295)**	**(1,973)**	(831)	(2,934)	(3,765)
Claims at end of period	**7,027**	**9,490**	**16,517**	7,341	9,687	17,028

The table below presents AIG's survival ratios for asbestos and environmental claims at September 30, 2006 and 2005. The survival ratio is derived by dividing the current carried loss reserve by the average payments for the three most recent calendar years for these claims. Therefore, the survival ratio is a simplistic measure estimating the number of years it would be before the current ending loss reserves for these claims would be paid off using recent year average payments. The 2006 survival ratio is lower than the ratio at December 31, 2005 because the more recent periods included in the rolling average reflect higher claims payments. Many factors, such as aggressive settlement procedures, mix of business and level of coverage provided, have a significant effect on the amount of asbestos and environmental reserves and payments and the resultant survival ratio. Thus, caution should be exercised in attempting to determine reserve adequacy for these claims based simply on this survival ratio.

AIG's survival ratios for asbestos and environmental claims, separately and combined, were based upon a three-year average payment. These ratios at September 30, 2006 and 2005 were as follows:

(number of years)	**Gross**	**Net**
2006		
Survival ratios:		
Asbestos	**11.9**	**13.6**
Environmental	**6.5**	**5.3**
Combined	**10.4**	**10.7**
2005		
Survival ratios:		
Asbestos	9.0	11.0
Environmental	6.5	6.0
Combined	8.1	8.9

Life Insurance & Retirement Services Operations

AIG's Life Insurance & Retirement Services subsidiaries offer a wide range of insurance and retirement savings products both domestically and abroad. Insurance-oriented products consist of individual and group life, payout annuities, endowment and accident and health policies. Retirement savings products consist generally of fixed and variable annuities.

Domestically, AIG's Life Insurance & Retirement Services operations offer a broad range of protection products, such as life insurance, group life and health products, including disability income products and payout annuities, which include single premium immediate annuities, structured settlements and terminal funding annuities. Home service operations include an array of life insurance, accident and health and annuity products sold primarily through career agents. In addition, home service includes a small block of run-off property and casualty coverage. Retirement services include group retirement products, individual fixed and variable annuities sold through banks, broker dealers and exclusive sales representatives, and annuity runoff operations, which include previously-acquired "closed blocks" and other fixed and variable annuities largely sold through distribution relationships that have been discontinued.

Overseas, AIG's Life Insurance & Retirement Services operations include insurance and investment-oriented products such as whole and term life, investment linked, universal life and endowments, personal accident and health products, group products including pension, life and health, and fixed and variable annuities.

Life Insurance & Retirement Services operations presented on a sub-product basis for the three and nine-month periods ended September 30, 2006 and 2005 were as follows:

(in millions)	Three Months Ended September 30, 2006	Three Months Ended September 30, 2005	Nine Months Ended September 30, 2006	Nine Months Ended September 30, 2005
GAAP premiums:				
Domestic Life:				
Life insurance[a]	**$ 546**	$ 506	**$ 1,619**	$ 1,506
Home service	**196**	201	**593**	606
Group life/health	**256**	272	**743**	805
Payout annuities[b]	**414**	375	**1,261**	1,118
Total	**1,412**	1,354	**4,216**	4,035
Domestic Retirement Services:				
Group retirement products	**94**	91	**284**	261
Individual fixed annuities	**32**	25	**96**	72
Individual variable annuities	**132**	119	**390**	345
Individual fixed annuities-runoff[c]	**16**	17	**50**	58
Total	**274**	252	**820**	736
Total Domestic	**1,686**	1,606	**5,036**	4,771
Foreign Life:				
Life insurance	**3,834**	3,671	**11,851**	11,664
Personal accident & health	**1,398**	1,258	**4,084**	3,746
Group products	**588**	469	**1,668**	1,447
Total	**5,820**	5,398	**17,603**	16,857
Foreign Retirement Services:				
Individual fixed annuities	**85**	80	**274**	256
Individual variable annuities	**48**	25	**123**	69
Total	**133**	105	**397**	325
Total Foreign	**5,953**	5,503	**18,000**	17,182
Total GAAP Premiums	**$7,639**	$7,109	**$ 23,036**	$ 21,953
Net investment income:				
Domestic Life:				
Life insurance	**$ 347**	$ 314	**$ 998**	$ 1,010
Home service	**167**	147	**470**	451
Group life/health	**55**	51	**161**	148
Payout annuities	**253**	230	**734**	679
Total	**822**	742	**2,363**	2,288
Domestic Retirement Services:				
Group retirement products	**563**	569	**1,674**	1,665
Individual fixed annuities	**893**	863	**2,705**	2,509
Individual variable annuities	**51**	54	**153**	165
Individual fixed annuities-runoff[c]	**226**	240	**689**	744
Total	**1,733**	1,726	**5,221**	5,083
Total Domestic	**2,555**	2,468	**7,584**	7,371
Foreign Life:				
Life insurance[d]	**1,401**	1,270	**3,991**	3,583
Personal accident & health	**78**	66	**213**	176
Group products	**171**	158	**463**	425
Intercompany adjustments	**(10)**	(10)	**(30)**	(26)
Total	**1,640**	1,484	**4,637**	4,158
Foreign Retirement Services:				
Individual fixed annuities	**516**	486	**1,470**	1,240
Individual variable annuities	**182**	229	**209**	382
Total	**698**	715	**1,679**	1,622
Total Foreign	**2,338**	2,199	**6,316**	5,780
Total net investment income	**$4,893**	$4,667	**$ 13,900**	$ 13,151

(in millions)	Three Months Ended September 30, 2006	Three Months Ended September 30, 2005	Nine Months Ended September 30, 2006	Nine Months Ended September 30, 2005
Realized capital gains (losses):				
Domestic realized capital gains (losses)	**$ (147)**	$ (42)	**$ (604)**	$ (93)
Foreign realized capital gains (losses)	**(103)**	(62)	**201**	(194)
Pricing net investment gains[e]	**74**	88	**286**	269
Total Foreign	**(29)**	26	**487**	75
Total realized capital gains (losses)[e]	**$ (176)**	$ (16)	**$ (117)**	$ (18)
Operating Income:				
Domestic	**$ 864**	$ 878	**$ 2,450**	$ 2,753
Foreign[d]	**1,584**	1,370	**4,974**	4,034
Total operating income	**$2,448**	$2,248	**$ 7,424**	$ 6,787
Life insurance in-force[f]:				
Domestic			**$ 902,202**	$ 825,151
Foreign			**1,112,392**	1,027,682
Total			**$2,014,594**	$1,852,833

(a) *Effective January 1, 2006, the Broker/Dealer operations of the Domestic Life Insurance companies are being reported and managed within the Asset Management segment. Included in GAAP premiums were revenues of $15 million and $79 million, respectively, for the three and nine-month periods ended September 30, 2005.*

(b) *Includes structured settlements, single premium immediate annuities and terminal funding annuities.*

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

(d) *Includes the effect of out of period adjustments related to the accounting for certain interests in unit investment trusts. For the nine month period ended September 30, 2006, the effect was an increase of $245 million and $168 million in net investment income and operating income, respectively.*

(e) *For purposes of this presentation, pricing net investment gains are segregated as a component of total realized capital gains (losses). They represent certain amounts of realized capital gains where gains are an inherent element in pricing certain life products in some foreign countries.*

(f) *Amounts presented were as at September 30, 2006 and December 31, 2005.*

AIG's Life Insurance & Retirement Services subsidiaries report their operations through the following operating units: Domestic Life — AIG American General, including American General Life Insurance Company (AG Life), United States Life Insurance in the City of New York (USLIFE) and American General Life and Accident Insurance Company (AGLA); Domestic Retirement Services — The Variable Annuity Life Insurance Company (VALIC), AIG Annuity Insurance Company (AIG Annuity) and AIG SunAmerica; Foreign Life — ALICO, AIRCO, AIG Edison Life, AIG Star Life, American International Assurance Company, Limited together with American International Assurance Company (Bermuda) Limited (AIA), Nan Shan Life Insurance Company, Ltd. (Nan Shan) and The Philippine American Life and General Insurance Company (Philamlife).

AIG transacts business in most major foreign currencies. The following table summarizes the effect of changes in foreign currency exchange rates on the growth of Life Insurance & Retirement Services GAAP premiums for the three and nine-month periods ended September 30, 2006:

	Three Months Ended September 30, 2006	Nine Months Ended September 30, 2006
Growth in original currency*	7.9%	7.3%
Foreign exchange effect	(0.4)	(2.4)
Growth as reported in U.S. dollars	7.5%	4.9%

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

Life Insurance & Retirement Services Results

Life Insurance & Retirement Services GAAP premiums increased 7.5 percent to $7.6 billion in the third quarter of 2006 compared to the same period in 2005. Net investment income increased $226 million for the third quarter of 2006 when compared to the same period in 2005. Net investment income includes policyholder trading gains (losses) amounting to $221 million in the third quarter of 2006 compared to $359 million in same period of 2005. Policyholder trading gains (losses) are linked primarily to equities and are offset by an equal change in incurred policy losses and benefits.

Operating income increased 9 percent in the third quarter of 2006 when compared to the same period in 2005. Domestic Life operations continued to perform well in its core life insurance businesses with growth in GAAP premium and invested assets supporting the underlying reserves. Domestic Retirement Services operating income growth in the quarter was driven by individual fixed and variable annuity business, offset in part by lower growth and spread compression in the group retirement products line. Foreign Life Insurance & Retirement Services operating income grew 16 percent in the quarter helped by higher investment returns. Realized capital gains (losses) for the third quarter of 2006

totaled a net loss of $176 million versus a loss of $16 million during the same period last year. The loss in the current quarter was primarily due to the effect of hedging activities that do not qualify for hedge accounting treatment under FAS 133, partially offset by foreign currency gains.

Life Insurance & Retirement Services GAAP premiums increased 4.9 percent to $23 billion for the first nine months of 2006 compared to the same period of 2005. Net investment income increased for the first nine months of 2006 reflecting a higher level of invested assets. The increase in net investment income also includes the effect of out of period adjustments relating to the accounting for certain interests in unit investment trusts totaling $24 million and $245 million for the three and nine-month periods ending September 30, 2006, respectively. Operating income grew 9 percent for the first nine months of 2006 compared to the same period of 2005. Domestic Life earnings for the core life and payout annuity businesses continue to demonstrate earnings growth, but was more than offset by lower investment income from calls and tenders, lower partnership income and additional reserves for legal contingencies. Domestic Retirement Services earnings declined for the first nine months of 2006 primarily due to realized capital losses which more than offset increased income from growth in invested assets and lower amortization of deferred policy acquisition costs related to capital losses. Foreign Life Insurance & Retirement Services operating income grew 23 percent for the first nine months of 2006 due to higher realized capital gains and the effect of the aforementioned out of period adjustments. Operating income growth in U.S. dollars is lower than growth on a local currency basis primarily due to a weaker Japanese Yen in the first nine months of 2006 compared to the same period last year. Realized capital losses were $117 million for the first nine months of 2006 compared to $18 million during the same period of 2005.

Domestic Life Operations

The following table reflects retail periodic Life insurance sales by product for the three and nine-month periods ended September 30, 2006 and 2005, respectively:

Domestic Life Insurance Periodic Premium Sales*

	Three Months Ended September 30,		Nine Months Ended September 30,	
(in millions)	**2006**	2005	**2006**	2005
By product:				
Universal life	**$ 46**	$ 79	**$289**	$191
Variable universal life	**15**	11	**42**	35
Term life	**59**	59	**182**	172
Whole life/other	**3**	1	**9**	7
Total	**$123**	$150	**$522**	$405

** Periodic premium represents premium from new business expected to be collected over a one year period.*

Quarterly Domestic Life Results

AIG's Domestic Life operations had growth of GAAP premiums for the third quarter of 2006 when compared to the same period last year. In the life insurance product line, periodic life sales declined due to re-pricing of certain universal life products and tightened underwriting standards for certain markets to maintain margins. AGLA, the home service business, is diversifying product offerings and enhancing the capabilities and quality of the sales force, which has resulted in improved agent productivity and better persistency of in-force business. Growth of payout annuities GAAP premiums emanated from sales of single premium immediate annuities and structured settlements. GAAP premiums for the group life/health product line were slightly lower in the third quarter of 2006 compared to 2005 reflecting slower growth in the credit insurance business, and tightened pricing and underwriting in the group employer lines. Management continues to focus on new product introductions, cross selling, other growth strategies, and options that may include exiting certain product lines.

Earnings for the Domestic Life Insurance line of business grew 9 percent for the third quarter of 2006 reflecting growth in in-force business and higher net investment income. Earnings for the home service line of business increased 37 percent compared to the third quarter of 2005, which included approximately $8 million of hurricane losses, and also due to higher investment income from partnerships of $17 million. The group life/health line of business results for the third quarter of 2006 reflect continuing restructuring efforts in that business. The payout annuities line of business earnings increased over last year due to growth in single premium annuities and also due to a $12 million reserve strengthening in the third quarter of 2005.

Year-to-date Domestic Life Results

GAAP premiums for the Domestic Life operations grew 5 percent for the first nine months of 2006 compared to the same period of 2005 reflecting improved sales of universal life and single premium immediate annuities. The life insurance product line experienced increased periodic sales from the independent distribution platform during the first nine months of 2006. The home service business GAAP premiums declined slightly for the first nine months of 2006 as the reduction of premium in-force from normal lapses and maturities exceeded sales growth for the period. The payout annuities GAAP premium growth for the first nine months of 2006 reflects increased sales of single premium annuities and structured settlements when compared to the same period last year. GAAP premiums for the group life/health product line for the first nine months of 2006 reflect the restructuring efforts in certain product lines.

Earnings for the life insurance product line declined for the first nine months of 2006 due to lower investment income

related to yield enhancement activities that offset growth in in-force business. Earnings for the home service line of business grew from the same period last year due to increased net investment income from partnerships and lower catastrophe and acquisition costs. The group life/health line of business earnings for the first nine months of 2006 are lower than the same period last year due to reserves related to litigation and contingencies in the credit life and A&H business and transition costs related to the outsourcing of back office operations. The payout annuities product line earnings declined for the first nine months of 2006 primarily due to lower calls and tenders on fixed maturity securities when compared to the same period last year.

Quarterly Domestic Retirement Services Results

Domestic Retirement Services total deposits declined slightly for the third quarter of 2006 when compared to the year ago quarter driven by lower fixed annuity sales that continued to face increased competition from bank products in the flat yield curve environment, partially offset by substantially higher variable annuity sales. Individual variable annuity deposits grew 36 percent in the third quarter of 2006 from the year ago quarter reflecting growth in products with new guarantee features. Group retirement deposits grew only slightly in the quarter compared to third quarter 2005, reflecting the increased number of policyholders nearing retirement age. New products have been launched that are designed to meet the needs of retirement age policyholders and retain assets under management. While total deposits within the group retirement business are growing moderately, annuity deposits are down $49 million, and group mutual fund deposits are up $69 million, for the third quarter of 2006 when compared to the same period last year, due to market demand for lower cost group retirement products. Over time, this will result in a gradual reduction in profitability of this business, due to lower profit margins in the mutual fund product compared to the annuity product.

Group retirement products earnings for the third quarter of 2006 were lower than the same period last year principally due to lower partnership income and higher amortization of deferred acquisition costs related to internal replacements of existing contracts into new contracts. Individual fixed annuity earnings grew 9 percent for the third quarter of 2006 compared to the same period last year as a result of increased net investment spreads and lower DAC amortization due to realized capital losses. Earnings for individual variable annuities grew $7 million in the third quarter of 2006 from the year ago quarter principally due to higher fee income as a result of increased assets under management.

Year-to-date Domestic Retirement Services Results

Domestic Retirement Services total deposits declined approximately 5 percent for the first nine months of 2006 when compared to the first nine months of 2005. The decrease in total deposits reflects declining fixed annuity sales partially offset by growth in individual variable annuity sales. In addition, fixed annuity surrender rates increased during the first nine months of 2006 when compared to the same period last year. Net flows for the nine months of 2006 were negative $4.1 billion compared to positive net flows of $0.3 billion last year reflecting the lower deposits and higher surrenders.

Group retirement products earnings were flat for the first nine months with slightly compressed spreads offsetting the effect of separate account growth. Individual fixed annuity earnings for the first nine months of 2006 grew 28 percent primarily from growth in partnership income, lower amortization of deferred policy acquisition costs related to capital losses, growth in average underlying reserves and lower average crediting rates. The individual variable annuity product line earnings grew for the first nine months as fee income increased on higher sales volumes and increased underlying reserves.

Domestic Retirement Services Supplemental Data

The following table reflects deposits for Domestic Retirement Services for the three and nine-month periods ended September 30, 2006 and 2005:

	Three Months Ended September 30,		Nine Months Ended September 30,	
(in millions)	**2006**	2005	**2006**	2005
Group retirement products:				
Annuities	**$1,335**	$1,384	**$ 4,083**	$ 4,161
Mutual funds	**284**	215	**1,085**	677
Individual fixed annuities	**1,194**	1,498	**4,212**	5,912
Individual variable annuities	**1,059**	781	**3,234**	2,457
Individual fixed annuities - runoff	**37**	48	**122**	155
Total	**$3,909**	$3,926	**$12,736**	$13,362

The following chart shows the amount of reserves by surrender charge category for Domestic Retirement Services as of September 30, 2006:

(in millions)	Group Retirement Products*	Individual Fixed Annuities	Individual Variable Annuities
Zero or no surrender charge	$41,266	$10,465	$10,721
Between 0 percent - 4 percent	11,434	10,948	8,513
Greater than 4 percent	2,755	29,685	10,222
Non-Surrenderable	887	3,163	89
Total	$56,342	$54,261	$29,545

** Excludes mutual funds.*

For the three months and nine months ended September 30, 2006 surrender rates increased for individual fixed annuities and individual variable annuities, while surrender rates for group retirement products declined as a result of successful asset retention efforts. The increase in surrender rate for fixed annuities continues to be driven by the shape of the yield curve and general aging of the in-force block; however, less than 20 percent of the individual fixed annuity reserves as of September 30, 2006 are available to be surren-

dered without charge. Individual variable annuity surrender rates for the third quarter and the first nine months of 2006 primarily reflect higher shock-lapses that occur following expiration of the surrender charge period on certain 3-year and 7-year contracts, although the trend has moderated during the year. Reflecting a widespread industry phenomenon, this lapse rate, much of which was anticipated when the products were issued, has recently been affected by investor demand to exchange existing policies for new-generation contracts with living benefits or lower fees. In addition, the high lapse rates are in part due to the surrenders within certain acquired blocks of business.

A further increase in the level of surrenders in any of these businesses or in the individual fixed annuities runoff block could accelerate the amortization of deferred acquisition costs and negatively affect fee income earned on assets under management.

The following table reflects the net flows by line of business for Domestic Retirement Services for the three and nine-month periods ended September 30, 2006 and 2005:

Domestic Retirement Services – Net Flows[(a)]

	Three Months Ended September 30,		Nine Months Ended September 30,	
(in millions)	**2006**	2005	**2006**	2005
Group retirement products[(b)]	**$ 158**	$ (58)	**$ 793**	$ 520
Individual fixed annuities	**(1,021)**	13	**(1,758)**	1,846
Individual variable annuities	**11**	(155)	**(34)**	(209)
Individual fixed annuities - runoff	**(1,042)**	(607)	**(3,121)**	(1,857)
Total	**$(1,894)**	$(807)	**$(4,120)**	$ 300

(a) Net flows are defined as deposits received, less benefits, surrenders, withdrawals and death benefits.

(b) Includes mutual funds.

The combination of lower deposits and higher surrenders in the individual fixed annuity and individual fixed annuity-runoff blocks resulted in negative net flows for the three and nine-month periods ended September 30, 2006. The continuation of the current interest rate and competitive environment could prolong this trend.

Quarterly Foreign Life Insurance & Retirement Services Results

Foreign Life Insurance & Retirement Services operations produced 78 percent and 77 percent of Life Insurance & Retirement Services GAAP premiums for the three months ended September 30, 2006 and 2005, respectively. Foreign Life Insurance & Retirement Services GAAP premiums increased in the third quarter of 2006 by approximately 8 percent compared to the same period in 2005 driven primarily by growth in southeast Asia outside of Japan and Taiwan. Currency changes had little effect on GAAP premiums in the quarter when compared to prior year. Foreign life GAAP premium growth is affected by a continuing trend for clients to purchase investment-oriented products. This is particularly true in Southeast Asia, including Taiwan, where AIG's life operations in that region have responded to this trend by offering a wide array of investment-linked products, both periodic pay and single premium, with multiple fund selection, but with minimal investment guarantees. For GAAP reporting purposes, only revenues from policy charges for insurance, administration, and surrender charges are reported as GAAP premiums for these life products. This product mix shift contributed to the single digit growth rate in Foreign Life Insurance & Retirement Services GAAP premiums, while continuing to grow total reserves.

Foreign Life Insurance & Retirement Services operating income grew by $214 million or 16 percent, to $1.6 billion for the third quarter of 2006 and included $29 million of realized capital losses compared to $26 million of gains in the year ago quarter. On a comparable basis, the growth in life insurance earnings for the quarter were generally in line with the growth in invested assets and increased overall compared to the third quarter of 2005, helped by higher seasonal dividend income of approximately $35 million in Taiwan, actuarial adjustments of $30 million and out of period adjustments of $24 million related to unit investment trusts and $18 million related to a reinsurance adjustment. The 2005 earnings included a charge to income of $20 million related to a wind down of operations in Chile. Personal accident & health earnings for the third quarter of 2006 reflect continued stable profit margins and revenue growth. Group products earnings grew in the third quarter of 2006 due to improved mortality and morbidity costs when compared to the same period last year. Growth of individual fixed annuities earnings for the third quarter of 2006, emanating primarily from Japan, is in line with the growth in average assets under management and lower acquisition costs from DAC unlocking. The growth of individual variable annuities earnings in the third quarter of 2006 reflects continued growth in assets under management related to the increased demand for those products in Japan and in Europe.

During the second quarter of 2006, Japanese tax authorities announced a reduction in the amount of premium that policyholders may deduct from their Japanese tax returns for certain accident and health products. Foreign life operations in Japan continued to experience a decline in sales of those products and an increase in terminations during the quarter, which resulted in approximately $23 million of higher expenses. This negative effect was more than offset by a $29 million benefit to operating income from the personal accident line of business as a result of an actuarial change in estimate. If terminations continue at current experience levels, results will continue to be negatively affected. Higher than anticipated terminations result in accelerated amortization of deferred acquisition costs, offset somewhat by the release of policy benefit reserves in excess of cash value. The amount of deferred acquisition costs related to the policies in-force for these products amounted to $240 million as of Sep-

tember 30, 2006. In response to the tax law change, AIG has developed new products, both life and health, to meet the needs of clients in that market. AIG continues to believe that any increase in policy terminations would not be material to AIG's consolidated financial condition or results of operations.

Year-to-date Foreign Life Insurance & Retirement Services Results

Foreign Life Insurance & Retirement Services operations produced 78 percent of Life Insurance & Retirement Services GAAP premiums in the first nine months of 2006 and 2005. GAAP premiums grew approximately 5 percent for the first nine months of 2006 (7 percent in original currency) compared to the same period in 2005. AIG transacts business in most major foreign currencies and therefore premiums reported in U.S. dollars will vary by volume and from changes in foreign currency translation rates. Globally, AIG's deep and diverse distribution, which includes bancassurance, worksite marketing, direct marketing and strong agency organizations, provides a powerful distribution platform for AIG's diverse product lines. In Japan, distribution of single premium life insurance products through banks was deregulated in December 2005 resulting in increased sales of products designed for that market during the first nine months of 2006. This new distribution outlet adds to the existing multiple distribution platform in Japan where AIG remains the leading foreign provider.

Foreign Life Insurance & Retirement Services operating income for the first nine months of 2006 was $5.0 billion, which included $487 million of realized capital gains and the effect of out of period adjustments related to the accounting for certain interests in unit investment trusts that increased operating income by $168 million, compared with $4.0 billion of operating income for the same period of 2005, which included $75 million of realized capital gains. The first nine months of 2006 results for the life insurance product line also included a $38 million operating loss attributable to this segment's share of the operating results from AIG Credit Card Company (Taiwan) compared to a gain of $29 million in the first nine months of 2005, due to an increase in allowance for losses recorded in the first quarter of 2006. The positive effect of DAC and value of business acquired (VOBA) unlocking for the life insurance product line was $31 million and $91 million for the first nine months of 2006 and 2005, respectively. Personal accident and health product line results for the first nine months of 2006 generally reflect the growth of underlying premium in-force, although growth was negatively affected by a weaker Yen exchange rate when compared to the same period last year. The Foreign Retirement Services business continued to grow in Japan and Korea by expanding distribution and leveraging AIG's product expertise. The positive effect of DAC and VOBA unlocking for the Retirement Services lines of business was $32 million and $13 million for the first nine months of 2006 and 2005, respectively. Reserves for individual fixed annuities continue to grow although demand for multi-currency fixed annuities in Japan has slowed due to currency rate fluctuations, rising local interest rates and stronger equity markets. Growth of individual variable annuity deposits has accelerated as those products have become more popular with consumers in Japan and Europe coupled with improved performance of equity markets.

Life Insurance & Retirement Services Net Investment Income and Realized Capital Gains (Losses)

The following table summarizes the components of net investment income for the three and nine-month periods ended September 30, 2006 and 2005:

	Three Months Ended September 30,		Nine Months Ended September 30,	
(in millions)	**2006**	2005	**2006**	2005
Domestic				
Fixed maturities, including short term investments	**$2,268**	$2,175	**$ 6,795**	$ 6,724
Equity securities	**6**	1	**13**	7
Interest on mortgage, policy and collateral loans	**201**	188	**585**	532
Partnership income – excluding Synfuels	**103**	132	**316**	311
Partnership income (loss) – Synfuels	**(20)**	(36)	**(79)**	(115)
Equity earnings on unit investment trusts	**2**	—	**2**	—
Other	**23**	35	**33**	–
Total investment income	**2,583**	2,495	**7,665**	7,459
Investment expenses	**28**	27	**81**	88
Net investment income	**$2,555**	$2,468	**$ 7,584**	$ 7,371
Foreign				
Fixed maturities, including short term investments	**$1,737**	$1,538	**$ 4,986**	$ 4,435
Equity securities	**119**	130	**285**	242
Interest on mortgage, policy and collateral loans	**114**	111	**332**	333
Partnership income	**36**	29	**76**	49
Equity earnings on unit investment trusts[(a)]	**75**	—	**259**	—
Other	**89**	92	**271**	295
Total investment income before policyholder trading gains (losses)	**2,170**	1,900	**6,209**	5,354
Policyholder trading gains (losses)[(b)]	**221**	359	**282**	583
Total investment income	**2,391**	2,259	**6,491**	5,937
Investment expenses	**53**	60	**175**	157
Net investment income	**$2,338**	$2,199	**$ 6,316**	$ 5,780
Total				
Fixed maturities, including short term investments	**$4,005**	$3,713	**$11,781**	$11,159
Equity securities	**125**	131	**298**	249
Interest on mortgage, policy and collateral loans	**315**	299	**917**	865
Partnership income – excluding Synfuels	**139**	161	**392**	360
Partnership income (loss) – Synfuels	**(20)**	(36)	**(79)**	(115)
Equity earnings on unit investment trusts[(a)]	**77**	—	**261**	—
Other	**112**	127	**304**	295
Total investment income before policyholder trading gains (losses)	**4,753**	4,395	**13,874**	12,813
Policyholder trading gains (losses)[(b)]	**221**	359	**282**	583
Total investment income	**4,974**	4,754	**14,156**	13,396
Investment expenses	**81**	87	**256**	245
Net investment income[(c)]	**$4,893**	$4,667	**$13,900**	$13,151

(a) Includes the effect of an out of period adjustment relating to the accounting for certain interests in unit investment trusts. For the three and nine-month periods ending September 30, 2006, the effect was an increase of $24 million and $245 million, respectively.

(b) Relates principally to assets held in various trading securities accounts that do not qualify for separate account treatment under SOP 03-1. These amounts are offset by an equal change included in incurred policy losses and benefits.

(c) Includes call and tender income.

The following table summarizes Domestic Life Insurance & Retirement Services partnership income (losses) by line of business for the three and nine-month periods ended September 30, 2006 and 2005:

	Three Months Ended September 30,		Nine Months Ended September 30,	
(in millions)	**2006**	2005	**2006**	2005
Domestic life – excluding Synfuels:				
Life insurance	**$ 14**	$ 19	**$ 24**	$ 123
Home service	**10**	(2)	**12**	–
Subtotal	**24**	17	**36**	123
Domestic life – Synfuels:				
Life insurance	**(14)**	(25)	**(55)**	(78)
Home service	**(6)**	(11)	**(24)**	(37)
Subtotal	**(20)**	(36)	**(79)**	(115)
Total domestic life	**4**	(19)	**(43)**	8
Retirement services:				
Group retirement products	**35**	49	**112**	74
Individual fixed annuities	**44**	66	**168**	114
Total retirement services	**79**	115	**280**	188
Total	**$ 83**	$ 96	**$ 237**	$ 196

Quarterly Life Insurance & Retirement Services Net Investment Income and Realized Capital Gains (Losses)

Net investment income increased 5 percent for the third quarter of 2006 when compared to the same period in 2005. Growth was negatively affected by lower policyholder trading gains (losses) in the third quarter of 2006 when compared to 2005. Policyholder trading gains (losses), which are linked mainly to equities, are offset by an equal change in incurred policy losses and benefits. Investment income results for certain operations include investments in structured notes linked to emerging market sovereign debt that incorporates both interest rate risk and currency risk. Mark-to-market adjustments related to these structured notes were a gain of $6 million and a loss of $22 million for the three and nine months ended September 30, 2006, respectively. In Taiwan, dividend income increased $35 million over the same quarter last year due to the increased allocation of invested assets from fixed maturities to equities and the seasonality of dividend payments. In addition, period to period comparisons of investment income for some lines of business are affected by yield enhancement activity, particularly partnership income as shown in the above table.

AIG generates income tax credits as a result of investing in synthetic fuel production (synfuels) related to the investment loss shown in the above table and records those benefits in its provision for income taxes. The amount of those income tax credits was $20 million and $52 million for the three months ended September 30, 2006 and 2005, respectively. See Note 6(b) "Contingencies" of Notes to Consolidated Financial Statements for a further discussion of the effect of fluctuating domestic crude oil prices on synfuel tax credits. For the remainder of 2006, AIG may adjust production levels depending upon oil prices which affect the availability of the synthetic fuel tax credit. Regardless of oil prices, the tax credits expire after 2007.

Year-to-date Life Insurance & Retirement Services Net Investment Income and Realized Capital Gains (Losses)

The growth in net investment income for the first nine months of 2006 compared to a year ago parallels the growth in general account reserves and surplus for both Domestic and Foreign Life Insurance & Retirement Services companies and the effect of the aforementioned out of period adjustment. Also, net investment income was positively affected by the compounding of previously earned and reinvested investment cash flows along with the addition of new net cash flows from operations. Investment income includes income generated from traditional fixed income investments as well as income generated from other sources.

The amount of income tax credits generated as a result of investing in synthetic fuel production (synfuels) was $79 million and $167 million for the first nine months of 2006 and 2005, respectively.

The following table summarizes realized capital gains (losses) by major category for the three and nine-month periods ended September 30, 2006 and 2005:

	Three Months Ended September 30,		Nine Months Ended September 30,	
(in millions)	**2006**	2005	**2006**	2005
Domestic life				
Fixed maturities	**$ 1**	$ (10)	**$ (60)**	$ 13
Equity securities	**8**	2	**14**	9
Other:				
Foreign exchange transactions	**(6)**	1	**(6)**	1
Derivatives instruments	**(98)**	121	**17**	55
Other-than-temporary decline	**(24)**	(71)	**(139)**	(96)
Other	**(4)**	(2)	**(16)**	(4)
Total domestic life	**$(123)**	$ 41	**$(190)**	$ (22)
Domestic retirement services:				
Fixed maturities	**19**	90	**(69)**	32
Equity securities	**(8)**	11	**23**	42
Other:				
Foreign exchange transactions	**(13)**	–	**(13)**	–
Derivatives instruments	**13**	(110)	**(23)**	(25)
Other-than-temporary decline	**(41)**	(64)	**(301)**	(129)
Other	**6**	(10)	**(31)**	9
Total domestic retirement services	**$ (24)**	$ (83)	**$(414)**	$ (71)
Foreign				
Fixed maturities	**(28)**	102	**(174)**	239
Equity securities	**14**	48	**415**	205
Other:				
Foreign exchange transactions	**133**	(27)	**43**	(203)
Derivatives instruments	**(219)**	(249)	**127**	(275)
Other-than-temporary decline	**(33)**	(5)	**(78)**	(31)
Other	**104**	157	**154**	140
Total foreign	**$ (29)**	$ 26	**$ 487**	$ 75
Total	**$(176)**	$ (16)	**$(117)**	$ (18)

Realized capital gains (losses) include normal portfolio transactions as well as derivative gains (losses) for transactions that do not qualify for hedge accounting treatment under FAS 133, transactional foreign exchange gains and losses and other-than-temporary declines in the value of investments. Line of business results for Domestic Life Insurance & Retirement Services exclude the effect of realized capital gains (losses), but include the related effect on the amortization of deferred acquisition costs.

Life Insurance & Retirement Services Underwriting and Investment Risk

The risks associated with life and accident and health products are underwriting risk and investment risk. The risk associated with the financial and investment contract products is primarily investment risk.

Underwriting risk represents the exposure to loss resulting from the actual policy experience adversely emerging in comparison to the assumptions made in the product pricing associated with mortality, morbidity, termination and expenses. The emergence of significant adverse experience would require an adjustment to DAC and benefit reserves that could have a substantial effect on AIG's results of operations.

Natural disasters such as hurricanes, earthquakes and other catastrophes have the potential to adversely affect AIG's operating results. Other risks, such as an outbreak of a pandemic disease, such as the Avian Influenza A Virus (H5N1), could adversely affect AIG's business and operating results to an extent that may be only minimally offset by reinsurance programs.

While outbreaks of the Avian Flu continue to occur among poultry or wild birds in a number of countries in Asia, Europe, and Africa, transmission to humans has been rare to date. If the virus mutates to a form that can be transmitted from human to human, it has the potential to spread rapidly worldwide. If such an outbreak were to take place, early quarantine and vaccination could be critical to containment.

Both the contagion and mortality rate of any mutated H5N1 virus that can be transmitted from human to human are highly speculative. AIG continues to monitor the developing facts. A significant global outbreak could have a material adverse effect on Life Insurance & Retirement Services operating results and liquidity from increased mortality and morbidity rates. For a further discussion of pandemic influenza, see "Managing Market Risk — Catastrophe Exposures — Pandemic Influenza."

AIG's Foreign Life Insurance & Retirement Services companies generally limit their maximum underwriting expo-

sure on life insurance of a single life to approximately $1.7 million of coverage. AIG's Domestic Life Insurance & Retirement Services companies limit their maximum underwriting exposure on life insurance of a single life to $10 million of coverage in certain circumstances by using yearly renewable term reinsurance. (See also the discussion under "Liquidity" herein.)

AIRCO acts primarily as an internal reinsurance company for AIG's foreign life operations. This facilitates insurance risk management (retention, volatility, concentrations) and capital planning locally (branch and subsidiary). It also allows AIG to pool its insurance risks and purchase reinsurance more efficiently at a consolidated level, manage global counterparty risk and relationships and manage global life catastrophe risks.

AIG's domestic Life Insurance & Retirement Services operations utilize internal and third-party reinsurance relationships to manage insurance risks and to facilitate capital management strategies. Pools of highly-rated third-party reinsurers are utilized to manage net amounts at risk in excess of retention limits. AIG's life insurance companies also cede excess, non-economic reserves carried on a statutory-basis only on certain term and universal life insurance and accident and health policies and certain fixed annuities to AIG Life of Bermuda Ltd., a wholly owned Bermuda reinsurer.

AIG generally obtains letters of credit in order to obtain statutory recognition of these intercompany reinsurance transactions. For this purpose, AIG entered into a $2.5 billion syndicated letter of credit facility in December 2004. Letters of credit totaling $2.5 billion were outstanding as of September 30, 2006. The letter of credit facility has a ten-year term, but the facility can be reduced or terminated by the lenders beginning after seven years.

In November 2005, AIG entered into a revolving credit facility for an aggregate amount of $3 billion. The facility can be drawn in the form of letters of credit with terms of up to ten years. As of September 30, 2006, $2.49 billion principal amount of letters of credit are outstanding under this facility, of which approximately $1.09 billion relates to life intercompany reinsurance transactions. AIG also obtained approximately $298 million letters of credit on a bilateral basis.

Investment risk represents the exposure to loss resulting from the cash flows from the invested assets, primarily long-term fixed rate investments, being less than the cash flows required to meet the obligations of the expected policy and contract liabilities and the necessary return on investments. (See also the discussion under "Liquidity" herein.)

To minimize its exposure to investment risk, AIG tests the cash flows from the invested assets and policy and contract liabilities using various interest rate scenarios to evaluate investment risk and to confirm that assets are sufficient to pay these liabilities.

AIG actively manages the asset-liability relationship in its foreign operations, as it has been doing throughout AIG's history, even though certain territories lack qualified long-term investments or certain local regulatory authorities may impose investment restrictions. For example, in several Southeast Asian countries, the duration of investments is shorter than the effective maturity of the related policy liabilities. Therefore, there is risk that the reinvestment of the proceeds at the maturity of the initial investments may be at a yield below that of the interest required for the accretion of the policy liabilities. Additionally, there exists a future investment risk associated with certain policies currently in-force which will have premium receipts in the future. That is, the investment of these future premium receipts may be at a yield below that required to meet future policy liabilities.

In the first nine months of 2006, new money investment rates have generally risen in the U.S. and Japan and have generally fallen in Taiwan and Thailand. In regard to inforce business, management focus is required in both the investment and product management process to maintain an adequate yield to match the interest necessary to support future policy liabilities. Business strategies continue to evolve to maintain profitability of the overall business. As such, in some countries, new products are being introduced with minimal investment guarantees resulting in a shift toward investment linked savings products and away from traditional savings products with higher guarantees.

The investment of insurance cash flows and reinvestment of the proceeds of matured securities and coupons requires active management of investment yields while maintaining satisfactory investment quality and liquidity.

AIG may use alternative investments in certain foreign jurisdictions where interest rates remain low and there are limited long-dated bond markets, including equities, real estate and foreign currency denominated fixed income instruments to extend the duration or increase the yield of the investment portfolio to more closely match the requirements of the policyholder liabilities and DAC recoverability. This strategy has been effectively used in Japan and more recently by Nan Shan in Taiwan. Foreign assets comprised approximately 32 percent of Nan Shan's invested assets at September 30, 2006, slightly below the maximum allowable percentage under current regulation. The majority of Nan Shan's in-force policy portfolio is traditional life and endowment insurance products with implicit interest rate guarantees. New business with lower interest rate guarantees are gradually reducing the overall interest requirements, but asset portfolio yields have declined faster due to the prolonged low interest rate environment. As a result, although the investment margins for a large block of in-force policies are negative, the block remains profitable because the mortality and expense margins presently exceed the negative investment spread. In response to the low interest rate environment and the volatile exchange rate of the NT dollar, Nan Shan is

emphasizing new products with lower implied guarantees, including participating endowments and investment-linked products. Although the risks of a continued low interest rate environment coupled with a volatile NT dollar could increase net liabilities and require additional capital to maintain adequate local solvency margins, Nan Shan currently believes it has adequate resources to meet all future policy obligations.

AIG actively manages the asset-liability relationship in its domestic operations. This relationship is more easily managed through the availability of qualified long-term investments.

AIG uses asset-liability matching as a management tool worldwide to determine the composition of the invested assets and appropriate marketing strategies. As a part of these strategies, AIG may determine that it is economically advantageous to be temporarily in an unmatched position due to anticipated interest rate or other economic changes. In addition, the absence of long-dated fixed income instruments in certain markets may preclude a matched asset-liability position in those markets.

A number of guaranteed benefits, such as living benefits or guaranteed minimum death benefits, are offered on certain variable life and variable annuity products. AIG manages its exposure resulting from these long-term guarantees through reinsurance or capital market hedging instruments.

DAC for Life Insurance & Retirement Services products arises from the deferral of those costs that vary with, and are directly related to, the acquisition of new or renewal business. Policy acquisition costs for life insurance products are generally deferred and amortized over the premium paying period of the policy. Policy acquisition costs that relate to universal life and investment-type products, including variable and fixed annuities (investment-oriented products) are deferred and amortized, with interest, as appropriate, in relation to the historical and future incidence of estimated gross profits to be realized over the estimated lives of the contracts. Amortization expense includes the effects of current period realized capital gains and losses for investment type products. With respect to investment-oriented products, AIG's policy is to adjust amortization assumptions for DAC when estimates of current or future gross profits to be realized from these contracts are revised. With respect to variable annuities sold domestically (representing the vast majority of AIG's variable annuity business), the assumption for the long-term annual net growth rate of the equity markets used in the determination of DAC amortization is approximately ten percent. A methodology referred to as "reversion to the mean" is used to maintain this long-term net growth rate assumption, while giving consideration to short-term variations in equity markets. Estimated gross profits include investment income and gains and losses less interest required on policyholder reserves, as well as other charges in the contract less actual mortality and expenses. Current experience and changes in the expected future gross profits are analyzed to determine the effect on the amortization of DAC. The estimation of projected gross profits requires significant management judgment. The assumptions with respect to the current and projected gross profits are reviewed and analyzed quarterly and are adjusted accordingly.

The following table summarizes the major components of the changes in deferred acquisition costs and the value of business acquired (VOBA) for the nine months ended September 30, 2006 and 2005:

(in millions)	2006			2005		
	DAC	**VOBA**	**Total**	DAC	VOBA	Total
Domestic Life Insurance & Retirement Services:						
Balance at beginning of year	**$10,505**	**$ 865**	**$11,370**	$ 8,830	$ 836	$ 9,666
Acquisition costs deferred	**1,379**	**–**	**1,379**	1,569	–	1,569
Amortization (charged) or credited to operating income:						
Related to realized capital gains (losses)	**72**	**11**	**83**	22	3	25
Related to unlocking future assumptions	**4**	**(3)**	**1**	–	–	–
All other amortization	**(1,049)**	**(59)**	**(1,108)**	(1,119)	(72)	(1,191)
Related to change in unrealized gains (losses) on securities	**692**	**30**	**722**	737	59	796
Increase (decrease) due to foreign exchange	**20**	**–**	**20**	12	3	15
Other*	**(903)**	**–**	**(903)**	–	–	–
Balance at end of period	**$10,720**	**$ 844**	**$11,564**	$10,051	$ 829	$10,880
Foreign Life Insurance & Retirement Services:						
Balance at beginning of year	**$16,552**	**$1,278**	**$17,830**	$14,472	$1,681	$16,153
Acquisition costs deferred	**3,733**	**–**	**3,733**	3,380	–	3,380
Amortization (charged) or credited to operating income:						
Related to realized capital gains (losses)	**2**	**1**	**3**	–	(1)	(1)
Related to unlocking future assumptions	**49**	**14**	**63**	96	8	104
All other amortization	**(1,750)**	**(142)**	**(1,892)**	(1,380)	(166)	(1,546)
Related to change in unrealized gains (losses) on securities	**230**	**(3)**	**227**	(243)	(12)	(255)
Increase (decrease) due to foreign exchange	**529**	**27**	**556**	(491)	(102)	(593)
Other*	**(186)**	**–**	**(186)**	–	–	–
Balance at end of period	**$19,159**	**$1,175**	**$20,334**	$15,834	$1,408	$17,242
Total Life Insurance & Retirement Services:						
Balance at beginning of year	**$27,057**	**$2,143**	**$29,200**	$23,302	$2,517	$25,819
Acquisition costs deferred	**5,112**	**–**	**5,112**	4,949	–	4,949
Amortization (charged) or credited to operating income:						
Related to realized capital gains (losses)	**74**	**12**	**86**	22	2	24
Related to unlocking future assumptions	**53**	**11**	**64**	96	8	104
All other amortization	**(2,799)**	**(201)**	**(3,000)**	(2,499)	(238)	(2,737)
Related to change in unrealized gains (losses) on securities	**922**	**27**	**949**	494	47	541
Increase (decrease) due to foreign exchange	**549**	**27**	**576**	(479)	(99)	(578)
Other*	**(1,089)**	**–**	**(1,089)**	–	–	–
Balance at end of period	**$29,879**	**$2,019**	**$31,898**	$25,885	$2,237	$28,122

** Represents sales inducement assets reclassified from DAC to Other assets.*

AIG's variable annuity earnings will be affected by changes in market returns because separate account revenues, primarily composed of mortality and expense charges and asset management fees, are a function of asset values.

DAC for both insurance-oriented and investment-oriented products as well as retirement services products are reviewed for recoverability, which involves estimating the future profitability of current business. This review also involves significant management judgment. If the actual emergence of future profitability were to be substantially different than that estimated, AIG's results of operations could be significantly affected in future periods.

Invested Assets

The following tables summarize the composition of AIG's invested assets by segment, at September 30, 2006 and December 31, 2005:

(in millions)	General Insurance	Life Insurance & Retirement Services	Asset Management	Financial Services	Other	Total
2006						
Fixed maturities:						
Bonds available for sale, at market value	$ 63,651	$279,230	$31,819	$ 1,336	$ –	$376,036
Bonds held to maturity, at amortized cost	21,484	–	–	–	–	21,484
Bond trading securities, at market value	4	1,326	5,908	–	–	7,238
Equity securities:						
Common stocks available for sale, at market value	3,921	7,625	225	–	64	11,835
Common and preferred stocks trading, at market value	372	10,792	364	–	–	11,528
Preferred stocks available for sale, at market value	1,840	655	–	5	–	2,500
Mortgage loans on real estate, net of allowance	13	12,471	4,266	92	–	16,842
Policy loans	2	7,333	48	2	–	7,385
Collateral and guaranteed loans, net of allowance	3	665	693	2,152	84	3,597
Financial services assets:						
Flight equipment primarily under operating leases, net of accumulated depreciation	–	–	–	39,460	–	39,460
Securities available for sale, at market value	–	–	–	41,232	–	41,232
Trading securities, at market value	–	–	–	5,822	–	5,822
Spot commodities	–	–	–	118	–	118
Unrealized gain on swaps, options and forward transactions	–	–	–	20,235	–	20,235
Trading assets	–	–	–	2,194	–	2,194
Securities purchased under agreements to resell, at contract value	–	–	–	27,041	–	27,041
Finance receivables, net of allowance	–	–	–	28,634	–	28,634
Securities lending collateral, at market value	5,435	52,426	13,451	76	–	71,388
Other invested assets	8,482	10,490	11,861	1,934	10	32,777
Short-term investments, at cost	3,622	8,117	9,670	1,306	1	22,716
Total investments and financial services assets as shown in the balance sheet	108,829	391,130	78,305	171,639	159	750,062
Cash	488	523	133	279	2	1,425
Investment income due and accrued	1,262	4,549	369	22	–	6,202
Real estate, net of accumulated depreciation	667	2,903	2,748	24	37	6,379
Total invested assets	$111,246	$399,105	$81,555	$171,964	$198	$764,068

(in millions)	General Insurance	Life Insurance & Retirement Services	Asset Management	Financial Services	Other	Total
2005						
Fixed maturities:						
Bonds available for sale, at market value	$50,870	$273,165	$34,174	$ 1,307	$ –	$359,516
Bonds held to maturity, at amortized cost	21,528	–	–	–	–	21,528
Bond trading securities, at market value	–	1,073	3,563	–	–	4,636
Equity securities:						
Common stocks available for sale, at market value	4,505	7,436	227	–	59	12,227
Common stocks trading, at market value	425	8,122	412	–	–	8,959
Preferred stocks available for sale, at market value	1,632	760	–	10	–	2,402
Mortgage loans on real estate, net of allowance	14	10,247	3,968	71	–	14,300
Policy loans	2	6,987	48	2	–	7,039
Collateral and guaranteed loans, net of allowance	3	1,172	578	1,719	98	3,570
Financial services assets:						
Flight equipment primarily under operating leases, net of accumulated depreciation	–	–	–	36,245	–	36,245
Securities available for sale, at market value	–	–	–	37,511	–	37,511
Trading securities, at market value	–	–	–	6,499	–	6,499
Spot commodities	–	–	–	92	–	92
Unrealized gain on swaps, options and forward transactions	–	–	–	18,695	–	18,695
Trading assets	–	–	–	1,204	–	1,204
Securities purchased under agreements to resell, at contract value	–	28	–	14,519	–	14,547
Finance receivables, net of allowance	–	–	–	27,995	–	27,995
Securities lending collateral, at market value	4,931	42,991	11,549	–	–	59,471
Other invested assets	6,272	7,777	10,459	2,751	8	27,267
Short-term investments, at cost	2,482	5,855	5,619	1,382	4	15,342
Total investments and financial services assets as shown in the balance sheet	92,664	365,613	70,597	150,002	169	679,045
Cash	305	989	196	331	76	1,897
Investment income due and accrued	1,232	4,073	402	18	2	5,727
Real estate, net of accumulated depreciation	603	2,729	1,710	24	32	5,098
Total invested assets	$94,804	$373,404	$72,905	$150,375	$279	$691,767

Insurance and Asset Management Invested Assets

AIG's investment strategy is to invest primarily in high quality securities while maintaining diversification to avoid significant exposure to issuer, industry and/or country concentrations. With respect to Domestic General Insurance, AIG's strategy is to invest in longer duration fixed maturity investments to maximize the yields at the date of purchase. With respect to Life Insurance & Retirement Services, AIG's strategy is to produce cash flows required to meet maturing insurance liabilities. (See also the discussion under "Operating Review: Life Insurance & Retirement Services Operations" herein.) AIG invests in equities for various reasons, including diversifying its overall exposure to interest rate risk. Available for sale bonds and equity securities are subject to declines in fair value. Such declines in fair value are presented in unrealized appreciation or depreciation of investments, net of taxes as a component of accumulated other comprehensive income. Declines that are determined to be other-than-temporary are reflected in income in the period in which the intent to hold the securities to recovery no longer exists. See "Valuation of Invested Assets". Generally, insurance regulations restrict the types of assets in which an insurance company may invest. When permitted by regulatory authorities and when deemed necessary to protect insurance assets, including invested assets, from adverse movements in foreign currency exchange rates, interest rates and equity prices, AIG and its insurance subsidiaries may enter into derivative transactions as end users. (See also the discussion under "Derivatives" herein.)

In certain jurisdictions, significant regulatory and/or foreign governmental barriers exist which may not permit the immediate free flow of funds between insurance subsidiaries or from the insurance subsidiaries to AIG parent.

The following tables summarize the composition of AIG's insurance and asset management invested assets by segment, at September 30, 2006 and December 31, 2005:

(dollars in millions)	General Insurance	Life Insurance & Retirement Services	Asset Management	Total	Percent of Total	Percent Distribution Domestic	Percent Distribution Foreign
2006							
Fixed maturities:							
Bonds available for sale, at market value	$ 63,651	$279,230	$31,819	$374,700	63.3%	57.1%	42.9%
Bonds held to maturity, at amortized cost	21,484	–	–	21,484	3.6	100.0	—
Bond trading securities, at market value	4	1,326	5,908	7,238	1.2	2.6	97.4
Equity securities:							
Common stocks available for sale, at market value	3,921	7,625	225	11,771	2.0	28.9	71.1
Common and preferred stocks trading, at market value	372	10,792	364	11,528	2.0	3.2	96.8
Preferred stocks available for sale, at market value	1,840	655	–	2,495	0.4	81.4	18.6
Mortgage loans on real estate, net of allowance	13	12,471	4,266	16,750	2.8	83.5	16.5
Policy loans	2	7,333	48	7,383	1.2	41.1	58.9
Collateral and guaranteed loans, net of allowance	3	665	693	1,361	0.2	2.6	97.4
Securities lending collateral, at market value	5,435	52,426	13,451	71,312	12.1	87.3	12.7
Other invested assets	8,482	10,490	11,861	30,833	5.2	79.3	20.7
Short-term investments, at cost	3,622	8,117	9,670	21,409	3.6	32.1	67.9
Cash	488	523	133	1,144	0.2	39.1	60.9
Investment income due and accrued	1,262	4,549	369	6,180	1.1	53.2	46.8
Real estate, net of accumulated depreciation	667	2,903	2,748	6,318	1.1	52.2	47.8
Total	$111,246	$399,105	$81,555	$591,906	100.0%	60.7%	39.3%

(dollars in millions)	General Insurance	Life Insurance & Retirement Services	Asset Management	Total	Percent of Total	Percent Distribution Domestic	Percent Distribution Foreign
2005							
Fixed maturities:							
Bonds available for sale, at market value	$50,870	$273,165	$34,174	$358,209	66.2%	59.2%	40.8%
Bonds held to maturity, at amortized cost	21,528	–	–	21,528	4.0	100.0	–
Bond trading securities, at market value	–	1,073	3,563	4,636	0.9	3.3	96.7
Equity securities:							
Common stocks available for sale, at market value	4,505	7,436	227	12,168	2.2	28.7	71.3
Common stocks trading, at market value	425	8,122	412	8,959	1.7	4.8	95.2
Preferred stocks available for sale, at market value	1,632	760	–	2,392	0.4	88.8	11.2
Mortgage loans on real estate, net of allowance	14	10,247	3,968	14,229	2.7	84.6	15.4
Policy Loans	2	6,987	48	7,037	1.3	42.8	57.2
Collateral and guaranteed loans, net of allowance	3	1,172	578	1,753	0.3	1.2	98.8
Securities purchased under agreements to resell, at contract value	–	28	–	28	–	–	100.0
Securities lending collateral, at market value	4,931	42,991	11,549	59,471	11.0	87.3	12.7
Other invested assets	6,272	7,777	10,459	24,508	4.5	85.8	14.2
Short-term investments, at cost	2,482	5,855	5,619	13,956	2.6	27.3	72.7
Cash	305	989	196	1,490	0.2	15.0	85.0
Investment income due and accrued	1,232	4,073	402	5,707	1.1	56.9	43.1
Real estate, net of accumulated depreciation	603	2,729	1,710	5,042	0.9	45.2	54.8
Total	$94,804	$373,404	$72,905	$541,113	100.0%	62.3%	37.7%

Credit Quality

At September 30, 2006, approximately 58 percent of the fixed maturities investments were domestic securities. Approximately 39 percent of such domestic securities were rated AAA by one or more of the principal rating agencies. Approximately six percent were below investment grade or not rated.

A significant portion of the foreign fixed income portfolio is rated by Moody's Investors Service (Moody's), S&P or similar foreign services. Similar credit quality rating services are not available in all overseas locations. AIG reviews the credit quality of the foreign portfolio nonrated fixed income investments, including mortgages. At September 30, 2006, approximately 19 percent of the foreign fixed income investments were either rated AAA or, on the basis of AIG's internal analysis, were equivalent from a credit standpoint to securities so rated. Approximately five percent were below investment grade or not rated at that date. A large portion of the foreign fixed income portfolio are sovereign fixed maturity securities supporting the policy liabilities in the country of issuance.

Any fixed income security may be subject to downgrade for a variety of reasons subsequent to any balance sheet date.

Valuation of Invested Assets

AIG has the ability to hold any fixed maturity security to its stated maturity, including those fixed maturity securities classified as available for sale. Therefore, the decision to sell any such fixed maturity security classified as available for sale reflects the judgment of AIG's management that the security sold is unlikely to provide, on a relative value basis, as attractive a return in the future as alternative securities entailing comparable risks. With respect to distressed securities, the sale decision reflects management's judgment that the risk-discounted anticipated ultimate recovery is less than the value achievable on sale.

The valuation of invested assets involves obtaining a market value for each security. The source for the market value is generally from market exchanges or dealer quotations, with the exception of nontraded securities.

AIG periodically evaluates its securities for other-than-temporary impairments in valuation. As a matter of policy,

the determination that a security has incurred an other-than-temporary decline in value and the amount of any loss recognition requires the judgment of AIG's management and a continual review of its investments.

In general, a security is considered a candidate for other-than-temporary impairment if it meets any of the following criteria:

- Trading at a significant (25 percent or more) discount to par or amortized cost (if lower) for an extended period of time (nine months or longer);
- The occurrence of a discrete credit event resulting in (i) the issuer defaulting on a material outstanding obligation; or (ii) the issuer seeking protection from creditors under the bankruptcy laws or any similar laws intended for the court supervised reorganization of insolvent enterprises; or (iii) the issuer proposing a voluntary reorganization pursuant to which creditors are asked to exchange their claims for cash or securities having a fair value substantially lower than par value of their claims; or
- In the opinion of AIG's management, it is probable that AIG may not realize a full recovery on its investment, irrespective of the occurrence of one of the foregoing events.

At each balance sheet date, AIG evaluates its securities holdings in an unrealized loss position. Where AIG does not intend to hold such securities until they have fully recovered their carrying value based on the circumstances present at the date of evaluation, AIG records the unrealized loss in income. If events or circumstances change, such as unexpected changes in creditworthiness of the obligor, general interest rate environment, tax circumstances, liquidity events, and statutory capital management considerations among others, AIG revisits its intent to determine if a loss should be recorded in income. Further, if a loss is recognized from a sale subsequent to a balance sheet date pursuant to these changes in circumstances, the loss is recognized in the period in which the intent to hold the securities to recovery no longer exists.

Once a security has been identified as other-than-temporarily impaired, the amount of such impairment is determined by reference to that security's contemporaneous market price and recorded as a charge to earnings.

As a result of these policies, AIG recorded, in realized capital gains (losses), other-than-temporary impairment pretax losses of $170 million and $184 million for the three-month periods ended September 30, 2006 and 2005, respectively, and $766 million and $384 million for the nine-month periods ended September 30, 2006 and 2005, respectively.

No impairment charge with respect to any one single credit was significant to AIG's consolidated financial condition or results of operations, and no individual impairment loss exceeded 1.0 percent of consolidated net income for the first nine months of 2006.

Excluding the other-than-temporary impairments noted above, the changes in market value for AIG's available for sale portfolio, which constitutes the vast majority of AIG's investments, were recorded in accumulated other comprehensive income as unrealized gains or losses, net of tax.

At September 30, 2006, the fair value of AIG's fixed maturities and equity securities aggregated $431.3 billion. At September 30, 2006, aggregate unrealized gains after taxes for fixed maturity and equity securities were $8.9 billion. At September 30, 2006, the aggregate unrealized losses after taxes of fixed maturity and equity securities were approximately $2.9 billion.

The effect on net income of unrealized losses after taxes will be further mitigated upon realization, because certain realized losses will be charged to participating policyholder accounts, or realization will result in current decreases in the amortization of certain deferred policy acquisition costs.

At September 30, 2006, unrealized losses for fixed maturity securities and equity securities did not reflect any significant industry concentrations.

The amortized cost of fixed maturities available for sale in an unrealized loss position at September 30, 2006, by contractual maturity, is shown below:

(in millions)	Amortized Cost
Due in one year or less	$ 4,734
Due after one year through five years	30,234
Due after five years through ten years	56,708
Due after ten years	64,918
Total	$156,594

In the nine months ended September 30, 2006, the pretax realized losses incurred with respect to the sale of fixed maturities and equity securities were $1.1 billion. The aggregate fair value of securities sold was $34 billion, which was approximately 97 percent of amortized cost. The average period of time that securities sold at a loss during the nine months ended September 30, 2006 were trading continuously at a price below book value was approximately four months.

At September 30, 2006, aggregate pretax unrealized gains were $13.71 billion, while the pretax unrealized losses with respect to investment grade bonds, non-investment grade bonds and equity securities were $4.0 billion, $115 million and $281 million, respectively. Aging of the pretax unrealized losses with respect to these securities, distributed as a percentage of cost relative to unrealized loss (the extent by which the market value is less than amortized cost or cost), including the number of respective items, was as follows:

	Less than or equal to 20% of Cost[a]			Greater than 20% to 50% of Cost[a]			Greater than 50% of Cost[a]			Total		
Aging (dollars in millions)	Cost[a]	Unrealized Loss	Items	Cost[a]	Unrealized Loss	Items	Cost[a]	Unrealized Loss	Items	Cost[a]	Unrealized Loss[b]	Items
Investment grade bonds												
0-6 months	$ 38,228	$ 591	5,368	$ 57	$13	6	$ –	$ –	–	$ 38,285	$ 604	5,374
7-12 months	67,729	1,815	9,159	–	–	–	–	–	–	67,729	1,815	9,159
>12 months	45,864	1,593	6,142	11	3	3	5	4	4	45,880	1,600	6,149
Total	$151,821	$3,999	20,669	$ 68	$16	9	$ 5	$ 4	4	$151,894	$4,019	20,682
Non-investment grade bonds												
0-6 months	$ 2,550	$ 25	543	$ 5	$ 1	8	$ 2	$ 1	14	$ 2,557	$ 27	565
7-12 months	914	20	163	1	1	2	–	–	–	915	21	165
>12 months	1,222	63	217	5	3	3	1	1	9	1,228	67	229
Total	$ 4,686	$ 108	923	$ 11	$ 5	13	$ 3	$ 2	23	$ 4,700	$ 115	959
Total bonds												
0-6 months	$ 40,778	$ 616	5,911	$ 62	$14	14	$ 2	$ 1	14	$ 40,842	$ 631	5,939
7-12 months	68,643	1,835	9,322	1	1	2	–	–	–	68,644	1,836	9,324
>12 months	47,086	1,656	6,359	16	6	6	6	5	13	47,108	1,667	6,378
Total	$156,507	$4,107	21,592	$ 79	$21	22	$ 8	$ 6	27	$156,594	$4,134	21,641
Equity securities												
0-6 months	$ 3,275	$ 162	2,256	$183	$42	231	$22	$12	14	$ 3,480	$ 216	2,501
7-12 months	404	31	424	96	29	176	8	5	23	508	65	623
>12 months	–	–	–	–	–	–	–	–	–	–	–	–
Total	$ 3,679	$ 193	2,680	$279	$71	407	$30	$17	37	$ 3,988	$ 281	3,124

(a) For bonds, represents amortized cost.

(b) As more fully described above, upon realization, certain realized losses will be charged to participating policyholder accounts, or realization will result in a current decrease in the amortization of certain deferred policy acquisition costs.

As stated previously, the valuation for AIG's investment portfolio comes from market exchanges or dealer quotations, with the exception of nontraded securities. AIG considers nontraded securities to mean certain fixed income investments, certain structured securities, direct private equities, limited partnerships and hedge funds. The aggregate carrying value of these securities at September 30, 2006 was approximately $70 billion.

The methodology used to estimate fair value of nontraded fixed income investments is by reference to traded securities with similar attributes and using a matrix pricing methodology. This technique takes into account such factors as the industry, the security's rating and tenor, its coupon rate, its position in the capital structure of the issuer, and other relevant factors. The change in fair value is recognized as a component of accumulated other comprehensive income, net of tax.

For certain structured securities, the carrying value is based on an estimate of the security's future cash flows pursuant to the requirements of Emerging Issues Task Force Issue No. 99-20, "Recognition of Interest Income and Impairment on Purchased and Retained Beneficial Interests in Securitized Financial Assets." The change in carrying value is recognized in income.

Hedge funds and limited partnerships in which AIG holds in the aggregate less than a five percent interest are reported at fair value. The change in fair value is recognized as a component of accumulated other comprehensive income, net of tax.

With respect to hedge funds and limited partnerships in which AIG holds in the aggregate a five percent or greater interest, AIG uses the equity method to record these investments. The changes in such net asset values are recorded in income.

AIG obtains the fair value of its investments in limited partnerships and hedge funds from information provided by the general partner or manager of each of these investments, the accounts of which are generally audited on an annual basis.

Each of these investment categories is regularly tested to determine if impairment in value exists. Various valuation techniques are used with respect to each category in this determination.

Financial Services Operations

AIG's Financial Services subsidiaries engage in diversified activities including aircraft and equipment leasing, capital markets transactions, consumer finance and insurance premium financing.

Aircraft Finance

AIG's Aircraft Finance represents the operations of ILFC, which generates its revenues primarily from leasing new and used commercial jet aircraft to domestic and foreign airlines. Revenues also result from the remarketing of commercial jets for its own account, and remarketing and fleet management for airlines and financial institutions.

ILFC finances its purchases of aircraft primarily through the issuance of a variety of debt instruments. The composite borrowing rates at September 30, 2006 and 2005 were 5.14 percent and 4.43 percent, respectively. The composite borrowing rates do not reflect the benefit of hedging ILFC's floating rate and foreign currency denominated debt. ILFC hedges these exposures using interest rate and foreign currency derivatives. These derivatives are effective economic hedges; however, since hedge accounting under FAS 133 is not applied, the benefits of using derivatives to hedge these exposures is not reflected in ILFC's borrowing rates. (See also the discussions under "Capital Resources" and "Liquidity" herein.)

ILFC's sources of revenue are principally from scheduled and charter airlines and companies associated with the airline industry. The airline industry is sensitive to changes in economic conditions, cyclical and highly competitive. Airlines and related companies may be affected by political or economic instability, terrorist activities, changes in national policy, competitive pressures on certain air carriers, fuel prices and shortages, labor stoppages, insurance costs, recessions, world health issues and other political or economic events adversely affecting world or regional trading markets.

For a discussion of ILFC's potential exposure to airframe and engine manufacturers, see "Risk Factors" in Item 1A. of Part II of this Quarterly Report.

ILFC is exposed to operating loss and liquidity strain through nonperformance of aircraft lessees, through owning aircraft which it would be unable to sell or re-lease at acceptable rates at lease expiration and, in part, through committing to purchase aircraft which it would be unable to lease.

ILFC's revenues and income may be adversely affected by the volatile competitive environment in which its customers operate. ILFC manages the risk of nonperformance by its lessees with security deposit requirements, repossession rights, overhaul requirements, and close monitoring industry conditions through its marketing force. However, there can be no assurance that ILFC would be able to successfully manage the risks relating to the effect of possible future deterioration in the airline industry. Approximately 90 percent of ILFC's fleet is leased to non-U.S. carriers, and the fleet, comprised of the most efficient aircraft in the airline industry, continues to be in high demand from such carriers.

ILFC typically contracts to re-lease aircraft before the end of the existing lease term. For aircraft returned before the end of the lease term, ILFC has generally been able to re-lease such aircraft within two to six months of its return. As a lessor, ILFC considers an aircraft "idle" or "off lease" when the aircraft is not subject to a signed lease agreement or signed letter of intent. ILFC had one aircraft off lease at September 30, 2006, and all new aircraft, but one, scheduled for delivery through 2007 have been leased. (See also the discussions under "Capital Resources" and "Liquidity" herein.)

Management formally reviews regularly, and no less frequently than quarterly, issues affecting ILFC's fleet, including events and circumstances that may cause impairment of aircraft values. Management evaluates aircraft in the fleet as necessary, based on these events and circumstances in accordance with Statement of Financial Accounting Standards No. 144, "Accounting for the Impairment or Disposal of Long-Lived Assets" (FAS 144). ILFC has not recognized any impairment related to its fleet. ILFC has been able to re-lease the aircraft without diminution in lease rates that would result in an impairment under FAS 144. (See also the discussions under "Liquidity" herein.)

Capital Markets

Capital Markets represents the operations of AIGFP, which engages as principal in a wide variety of financial transactions, including standard and customized financial products involving commodities, credit, currencies, energy, equities and rates. AIGFP also invests in a diversified portfolio of securities and engages in borrowing activities involving issuing standard and structured notes and other securities, and entering into guaranteed investment agreements (GIAs).

As Capital Markets is a transaction-oriented operation, current and past revenues and operating results may not provide a basis for predicting future performance. AIG's Capital Markets operations derive substantially all their revenues from hedged financial positions entered in connection with counterparty transactions rather than from speculative transactions. AIGFP also participates as a dealer in a wide variety of financial derivatives transactions. AIGFP economically hedges the market risks arising from its transactions, although hedge accounting under FAS 133 is not currently being applied to any of the derivatives and related assets and

liabilities. Accordingly, revenues and operating income are exposed to volatility resulting from differences in the timing of revenue recognition between the derivatives and the hedged assets and liabilities. Revenues and operating income of the Capital Markets operations and the percentage change in these amounts for any given period are also significantly affected by the number, size and profitability of transactions entered into by these subsidiaries during that period relative to those entered into during the prior period. Generally, the realization of transaction revenues as measured by the receipt of funds is not a significant reporting event as the gain or loss on AIGFP's trading transactions is currently reflected in operating income as the fair values change from period to period.

A significant majority of AIG's financial derivative transactions are conducted by the Capital Markets operations. Capital Markets enters into derivative transactions to hedge the interest rate and foreign currency exposures associated with its available for sale assets and borrowings. Although the derivatives entered into to hedge its outstanding transactions and positions are highly effective economic hedges, AIG did not meet the requirements for hedge accounting under FAS 133.

Derivative transactions are entered into in the ordinary course of Capital Markets operations. Income on derivatives is recorded at fair value, determined by reference to the mark to market value of the derivative or their estimated fair value where market prices are not readily available. The resulting aggregate unrealized gains or losses from the derivatives are reflected in the income statement. Where Capital Markets cannot verify significant model inputs to observable market data and verify the model value to market transactions, Capital Markets values the contract at the transaction price at inception and, consequently, records no initial gain or loss in accordance with Emerging Issues Task Force Issue No. 02-03, "Issues Involved in Accounting for Derivative Contracts Held for Trading Purposes and Contracts Involved in Energy Trading and Risk Management Activities" (EITF 02-03). Such initial gain or loss is recognized over the life of the transaction. Capital Markets periodically reevaluates its revenue recognition under EITF 02-03 based on the observability of market parameters. The mark to fair value of derivative transactions is reflected in the balance sheet in the captions "Unrealized gain on swaps, options and forward transactions" and "Unrealized loss on swaps, options and forward transactions." Unrealized gains represent the present value of the aggregate of each net receivable, by counterparty, and the unrealized losses represent the present value of the aggregate of each net payable, by counterparty, as of September 30, 2006. These amounts will change from one period to the next due to changes in interest rates, currency rates, equity and commodity prices and other market variables, as well as cash movements, execution of new transactions and the maturing of existing transactions. (See also the discussion under "Derivatives" herein.)

Spread income on investments and borrowings is recorded on an accrual basis over the life of the transaction. Investments are classified as securities available for sale and are marked to market with the resulting unrealized gains or losses reflected in accumulated other comprehensive income. U.S. dollar denominated borrowings are carried at cost, while borrowings in any currency other than the U.S. dollar result in unrealized foreign exchange gains or losses reported in income. AIGFP hedges the economic exposure on its investments and borrowings on a portfolio basis using derivatives and other financial instruments. While these hedges are highly effective economic hedges, they do not qualify for hedge accounting treatment under FAS 133. The change in the fair value of the derivatives used to hedge these economic exposures is therefore included in Other income, while the offsetting change in fair value of the hedged investments and borrowings is not recognized in earnings.

To the extent the Financial Services subsidiaries, other than AIGFP, use derivatives to economically hedge their assets or liabilities with respect to their future cash flows, and such hedges do not qualify for hedge accounting treatment under FAS 133, the changes in fair value of such derivatives are recorded in realized capital gains (losses) or other revenues. Amounts recorded in realized capital gains (losses) are reported as part of the Other category.

Consumer Finance

Domestically, AIG's Consumer Finance operations are principally conducted through American General Finance, Inc. (AGF). AGF derives a substantial portion of its revenues from finance charges assessed on outstanding real estate loans, secured and unsecured non-real estate loans and retail sales finance receivables. The real estate loans include first or second mortgages on residential real estate generally having a maximum term of 360 months, and are considered non-conforming. These loans may be closed-end accounts or open-end home equity lines of credit and may be fixed-rate or adjustable rate products. The non-real estate loans are secured by consumer goods, automobiles, or other personal property or are unsecured. Both secured and unsecured non-real estate loans generally have a maximum term of 60 months. The core of AGF's originations is sourced through its branches. However, a significant volume of real estate loans is also originated through broker relationships, and to lesser extents, through correspondent relationships and direct mail solicitations. In the first quarter of 2006, two wholly-owned subsidiaries of AGF discontinued originating real estate loans through an arrangement with AIG Federal Savings Bank, a federally chartered thrift, and began originating such loans under their own state licenses.

Many of AGF's borrowers are non-prime or sub-prime. Current economic conditions, such as interest rate and employment levels, have a direct effect on the borrowers' ability to repay these loans. AGF manages the credit risk inherent in

its portfolio by using credit scoring models at the time of credit applications, established underwriting criteria, and in certain cases, individual loan reviews. AGF's Credit Strategy and Policy Committee monitors the quality of the finance receivables portfolio monthly when determining the appropriate level of the allowance for losses. The Credit Strategy and Policy Committee bases its conclusions on quantitative analyses, qualitative factors, current economic conditions and trends, and each committee member's experience in the consumer finance industry. Through the first nine months of 2006, the credit quality of AGF's finance receivables continues to be strong. However, declines in the strength of the U.S. housing market or economy may adversely affect the future credit quality of these receivables.

Internationally, AIG's Consumer Finance operations are principally conducted through AIG Consumer Finance Group Inc. (CFG). CFG operates primarily in emerging and developing markets. CFG has operations in Hong Kong, Taiwan, the Philippines, Thailand, China, Poland, Argentina, and Mexico. While products vary by market, the businesses generally provide credit cards, unsecured and secured non-real estate loans, term deposits, savings accounts, retail sales finance and real estate loans. CFG originates finance receivables through its branches and direct solicitation. CFG also originates finance receivables indirectly through relationships with retailers, auto dealers, and independent agents.

Consumer Finance operations are exposed to loss when contractual payments are not received. Credit loss exposure is managed through a combination of underwriting controls, mix of finance receivables, collateral and collection efficiency.

CFG monitors the quality of its finance receivable portfolio through a combination of a monthly Credit Review and quarterly Credit Reserve Committee review when determining the appropriate level of the allowance for losses. The Credit Reserve Committee bases its conclusions on quantitative analysis, qualitative factors, current economic conditions and trends, political and regulatory implications, competition, and the judgment of the committee's members. As a result of such a review and in light of industry-wide deteriorating credit conditions and tightening of overall consumer credit, the aggregate allowance for losses in AIG Credit Card Company (Taiwan) was increased by $88 million in the first quarter of 2006 to $130 million at March 31, 2006. The remaining balance, net of write-offs during the second and third quarters, is approximately $69 million at September 30, 2006. This balance, representing approximately 14 percent of CFG's outstanding credit card receivables for Taiwan, continues to be CFG's best estimate of the overall exposure and hence no additional increases to the allowance for losses were deemed necessary at September 30, 2006. The results of AIG Credit Card Company (Taiwan) are shared equally by the Financial Services and Life Insurance & Retirement Services segments.

Financial Services Results

Financial Services operations for the three and nine-month periods ended September 30, 2006 and 2005 were as follows:

	Three Months Ended September 30,		Nine Months Ended September 30,	
(in millions)	**2006**	2005	**2006**	2005
Revenues[(a)]:				
Aircraft Finance[(b)]	**$1,060**	$ 943	**$3,067**	$2,661
Capital Markets[(c)(d)]	**1,118**	23	**30**	2,754
Consumer Finance[(e)]	**970**	940	**2,833**	2,664
Other	**39**	20	**98**	61
Total	**$3,187**	$1,926	**$6,028**	$8,140
Operating income (loss)[(a)]:				
Aircraft Finance	**$ 157**	$ 165	**$ 475**	$ 476
Capital Markets[(d)]	**965**	(150)	**(457)**	2,306
Consumer Finance[(f)(g)]	**220**	190	**594**	649
Other, including intercompany adjustments	**15**	19	**38**	52
Total	**$1,357**	$ 224	**$ 650**	$3,483

(a) Includes the effect of hedging activities that do not qualify for hedge accounting treatment under FAS 133, including the related foreign exchange gains and losses. For the three and nine-month periods ended September 30, 2005, the effect was $(10) million and $(59) million, respectively, in operating income for Aircraft Finance. During 2006, Aircraft Finance derivative gains and losses are reported as part of the Other category, and not reported in Aircraft Finance operating income. For the three-month periods ended September 30, 2006 and 2005, the effect was $783 million and $(365) million in both revenues and operating income, respectively, for Capital Markets. For the nine-month periods ended September 30, 2006 and 2005, the effect was $(1.06) billion and $1.80 billion in both revenues and operating income for Capital Markets. These amounts result primarily from interest rate and foreign currency derivatives which are hedging available for sale securities and borrowings.

(b) Revenues are primarily aircraft lease rentals from ILFC.

(c) Revenues, shown net of interest expense, are primarily from hedged financial positions entered into in connection with counterparty transactions and the effect of hedging activities that do not qualify for hedge accounting treatment under FAS 133 described in (a) above.

(d) Certain transactions entered into by AIGFP generate tax credits and benefits which are included in income taxes in the consolidated statement of income. The amount of such tax credits and benefits for the three-month periods ended September 30, 2006 and 2005 are $3 million and $23 million, respectively. The amount of such tax credits and benefits for the nine-month periods ended September 30, 2006 and 2005 are $29 million and $63 million, respectively.

(e) Revenues are primarily finance charges.

(f) Includes $44 million in additional allowances for losses recorded in the first quarter of 2006 from AIG Credit Card Company (Taiwan).

(g) Includes catastrophe related losses of $62 million recorded in the third quarter of 2005 resulting from hurricane Katrina, which were reduced by $22 million in the third quarter of 2006.

Financial Services operating income increased in the third quarter and decreased in the first nine months of 2006 compared to the same periods of 2005 due primarily to the effect of hedging activities that do not qualify for hedge accounting under FAS 133.

Quarterly Aircraft Finance Results

ILFC's operating income decreased slightly in the third quarter of 2006 compared to the same period of 2005. Rental revenues increased by $120 million or 13 percent driven by a larger aircraft fleet. At September 30, 2006, ILFC had 818 aircraft subject to operating leases compared to 734 aircraft at September 30, 2005. The increase in rental revenues was more than offset by increases in depreciation and interest expense. Depreciation expense increased by $47 million or 13 percent in line with the increase in the size of aircraft fleet. Interest expense increased by $91 million or 30 percent driven by the rising cost of funds and additional borrowings to fund aircraft purchases. ILFC's interest expense does not reflect the benefit of hedging ILFC's floating rate and foreign currency denominated debt, ILFC hedges these exposures using interest rate and foreign currency derivatives. These derivatives are effective economic hedges. Since hedge accounting under FAS 133 is not applied, the benefits of using derivatives to hedge these exposures is not reflected in its borrowing rates.

Year-to-date Aircraft Finance Results

ILFC's operating income remained relatively stable in the first nine months of 2006 compared to the same period of 2005. Rental revenues increased by $392 million or 15 percent driven by a larger aircraft fleet and increased utilization. The increase in rental revenues was offset by increases in depreciation, interest expense, charges related to bankrupt airlines as well as the settlement of a tax dispute in Australia related to the restructuring of ownership of aircraft. Depreciation expense increased by $134 million or 13 percent in line with the increase in the size of aircraft fleet. Interest expense increased by $166 million or 19 percent driven by rising cost of funds and additional borrowings funding aircraft purchases. As discussed above, ILFC's interest expense does not reflect the benefit of hedging ILFC's floating rate and foreign currency denominated debt.

Quarterly Capital Markets Results

Capital Markets operating income in the third quarter of 2006 increased by $1.12 billion compared to the same period of 2005 primarily due to a gain related to derivatives not qualifying for hedge accounting treatment of $783 million in the current quarter compared to a loss of $365 million in the comparable period last year. A large part of the net gain on AIGFP's derivatives recognized in the third quarter of 2006 was due to the decrease in long term U.S. interest rates which increased the fair value of AIGFP's derivatives hedging its assets and liabilities. The performance of the U.S. dollar against other currencies in the third quarter of 2006 did not have a significant effect on the fair value of the derivatives hedging AIGFP's assets and liabilities. The majority of the net loss on AIGFP's derivatives in the third quarter of 2005 was due to rising long term interest rates, which decreased the fair value of AIGFP's derivatives hedging its assets and liabilities. This net loss was slightly offset by the strengthening of the U.S. dollar primarily against the Euro and British Pound, which increased the fair value of the foreign currency derivatives hedging available for sale securities.

Financial market conditions in the third quarter of 2006 were characterized by lower levels of interest rates globally, unchanged credit spreads and higher equity valuations. The increase in Capital Markets operating income for the third quarter of 2006 was principally due to gains on derivatives not qualifying for hedge accounting under FAS 133. AIGFP's transaction flow in credit, commodity and equity products improved during the third quarter of 2006 compared to the third quarter of 2005, although this was more than offset by reduced revenues from other product groups.

The most significant component of Capital Markets operating expenses is compensation, which was approximately $115 million and $138 million in the third quarter of 2006 and 2005, respectively. The amount of compensation was not affected by gains and losses not qualifying for hedge accounting treatment under FAS 133.

AIG elected to early adopt FAS 155 in 2006 and, accordingly, AIGFP has elected to account for a significant majority of its hybrid financial instruments at fair value. The change in fair value of these hybrid financial instruments is included in operating income. AIGFP economically hedges these hybrid financial instruments with other derivative positions with third parties. The change in fair value of these positions is reflected in operating income. The net effect of these hybrid financial instruments and the derivatives economically hedging these instruments had a minimal effect on AIGFP's operating income for the third quarter of 2006.

Year-to-date Capital Markets Results

Capital Markets operating income in the nine month period ended September 30, 2006 decreased by $2.76 billion compared to the same period of 2005. Improved results, primarily from increased transaction flow in AIGFP's credit, commodity index and equity products, were more than offset by the loss resulting from the effect of derivatives not qualifying for hedge accounting treatment of $1.06 billion in the current period compared to a gain of $1.80 billion in the comparable period last year, a decrease of $2.86 billion. A large part of the net loss on AIGFP's derivatives recognized in the first nine months of 2006 was due to the weakening of the U.S. dollar, primarily against the British Pound and Euro, resulting in a decrease in the fair value of the foreign currency derivatives hedging AIGFP's available for sale securities. The majority of the net gain on AIGFP's derivatives in the first nine months of 2005 was due to the strengthening of the U.S. dollar, primarily against the British Pound and Euro, which increased the fair value of the foreign currency derivatives hedging available for sale securities. To a lesser extent, the net gain in 2005 was due to the decrease in long term U.S. interest rates which

increased the fair value of derivatives hedging AIGFP's assets and liabilities.

Financial market conditions in the first nine months of 2006 were characterized by a general flattening of interest rate yield curves across fixed income markets globally, tightening of credit spreads and equity valuations that were higher.

The compensation expense of Capital Markets was approximately $380 million and $359 million in the first nine months of 2006 and 2005, respectively. The amount of compensation was not affected by gains and losses not qualifying for hedge accounting treatment under FAS 133.

As a result of AIG's early adoption of FAS 155, AIGFP elected to apply the fair value option to its structured notes and other financial liabilities containing embedded derivatives outstanding as of January 1, 2006. The cumulative effect from the adoption of FAS 155 on these instruments at January 1, 2006 was a loss of approximately $29 million pretax.

The application of the fair value option to these hybrid financial instruments did not have a significant effect on AIGFP's operating income for the first nine months of 2006.

Quarterly Consumer Finance Results

Consumer Finance operating income increased in the third quarter of 2006 compared to the same period of 2005 in the domestic operations and decreased slightly in foreign operations.

Domestically, the relatively low interest rate environment throughout 2005 contributed to a high level of mortgage refinancing activity. AGF's average net finance receivables increased 5 percent in the third quarter of 2006 when compared to the same period in 2005. However, net originations and purchases of finance receivables in AGF's centralized real estate business segment decreased in the third quarter of 2006 compared to the same period in 2005 primarily caused by a less robust U.S. housing market. The increase in AGF's revenues that principally resulted from portfolio growth was offset by higher interest expense and depressed whole loan sale prices resulting from a flattened yield curve. Both short-term and long-term market interest rates continued to increase significantly over the past year. AGF's short-term borrowing costs were 5.38 percent in the third quarter of 2006 compared to 3.96 percent in the third quarter of 2005. AGF's long-term borrowing costs were 5.09 percent in the third quarter of 2006 compared to 4.47 percent in the third quarter of 2005. Despite high energy costs, the U.S. economy continued to expand during the third quarter of 2006, improving consumer credit quality compared to the third quarter of 2005. AGF's charge-off ratio improved 17 basis points in the third quarter of 2006 when compared to the same period in 2005.

AGF's results included catastrophe related losses of $62 million in the third quarter of 2005 resulting from hurricane Katrina. However, after a reassessment of payment and charge-off experience during the past year, AGF reduced the reserve by $22 million in the third quarter of 2006. At September 30, 2006, AGF's allowance ratio was 1.99 percent compared to 2.24 percent at September 30, 2005.

Revenues from foreign consumer finance operations increased by approximately 15 percent in the third quarter of 2006 compared to the same period in 2005. Loan growth was the primary driver behind higher revenues in 2006. Higher revenues were offset by higher loan loss provisions due to loan growth and higher operating expenses in connection with expansion of distribution channels and new product promotions, resulting in slightly lower operating income for the third quarter of 2006 compared to the same period in 2005.

Year-to-date Consumer Finance Results

Consumer Finance operating income decreased in the first nine months of 2006 compared to the same period of 2005. The domestic operations remain essentially unchanged year over year while the foreign operations decreased primarily due to the credit deterioration in the Taiwan credit card market.

Domestically, the relatively low interest rate environment throughout 2005 contributed to a high level of mortgage refinancing activity. AGF's average net finance receivables increased 9 percent in the first nine months of 2006 when compared to the same period in 2005. However, net originations and purchases of finance receivables in AGF's centralized real estate business decreased in the first nine months of 2006 compared to the same period in 2005 primarily caused by a less robust U.S. housing market. The increase in AGF's revenues that principally resulted from portfolio growth was offset by higher interest expense and depressed whole loan sale prices resulting from a flattened yield curve. AGF's short-term borrowing costs were 5.06 percent in the first nine months of 2006 compared to 3.47 percent in the same period in 2005. AGF's long-term borrowing costs were 4.97 percent in the first nine months of 2006 compared to 4.36 percent in the same period in 2005. Despite high energy costs, the U.S. economy continued to expand during the first nine months of 2006, improving consumer credit quality. AGF's charge-off ratio improved 25 basis points in the first nine months of 2006 when compared to the same period in 2005. AGF's delinquency ratio at September 30, 2006 remained the same when compared to September 30, 2005. At September 30, 2006, AGF's allowance ratio was 1.99 percent compared to 2.24 percent at September 30, 2005.

During the third quarter of 2006, AGF reassessed the adequacy of the reserve established in September 2005 resulting from hurricane Katrina as discussed above.

Revenues from the foreign consumer finance operations increased by approximately 20 percent in the first nine months of 2006 compared to the same period in 2005. Loan growth was the primary driver behind higher revenues. Higher revenues were more than offset by increases in the allowance for losses related to industry-wide credit deterioration in the Taiwan credit card market, increased cost of funds, and higher operating expenses in connection with expansion of distribution channels and new product promotions, resulting in a lower operating income for the first nine months of 2006 compared to the same period in 2005.

Financial Services Invested Assets

The following table is a summary of the composition of AIG's Financial Services invested assets at September 30, 2006 and December 31, 2005. (See also the discussions under "Operating Review: Financial Services Operations," "Capital Resources" and "Derivatives" herein.)

	2006		2005	
(dollars in millions)	**Invested Assets**	**Percent of Total**	Invested Assets	Percent of Total
Fixed maturities:				
Bonds available for sale, at market value	**$ 1,336**	**0.8%**	$ 1,307	0.9%
Equity securities:				
Preferred stocks available for sale, at market value	**5**	**–**	10	–
Mortgage loans on real estate, net of allowance	**92**	**–**	71	–
Policy loans	**2**	**–**	2	–
Collateral and guaranteed loans, net of allowance	**2,152**	**1.3**	1,719	1.2
Financial services assets:				
Flight equipment primarily under operating leases, net of accumulated depreciation	**39,460**	**22.9**	36,245	24.1
Securities available for sale, at market value	**41,232**	**24.0**	37,511	24.9
Trading securities, at market value	**5,822**	**3.4**	6,499	4.3
Spot commodities	**118**	**0.1**	92	0.1
Unrealized gain on swaps, options and forward transactions	**20,235**	**11.8**	18,695	12.4
Trading assets	**2,194**	**1.3**	1,204	0.8
Securities purchased under agreements to resell, at contract value	**27,041**	**15.7**	14,519	9.7
Finance receivables, net of allowance	**28,634**	**16.7**	27,995	18.6
Securities lending collateral, at market value	**76**	**–**	–	–
Other invested assets	**1,934**	**1.1**	2,751	1.9
Short-term investments, at cost	**1,306**	**0.7**	1,382	0.9
Cash	**279**	**0.2**	331	0.2
Investment income due and accrued	**22**	**–**	18	–
Real estate, net of accumulated depreciation	**24**	**–**	24	–
Total	**$171,964**	**100.0%**	$150,375	100.0%

As previously discussed, the cash used for the purchase of flight equipment is derived primarily from the proceeds of ILFC's debt financings. The primary sources for the repayment of this debt and the interest thereon are the cash flow from operations, proceeds from the sale of flight equipment and the rollover and refinancing of the prior debt. During the first nine months of 2006, ILFC acquired flight equipment costing $4.86 billion. (See also the discussion under "Operating Review: Financial Services Operations" and "Capital Resources" herein.)

At September 30, 2006, ILFC had committed to purchase 268 new aircraft deliverable from 2006 through 2015 at an estimated aggregate purchase price of $19.2 billion and had options to purchase three new aircraft at an estimated aggregate purchase price of $453 million. As of September 30, 2006, ILFC has entered into leases for all, but one, of the new aircraft scheduled for delivery through 2007. ILFC will be required to find customers for any aircraft currently on order and any aircraft to be ordered, and it must arrange financing for portions of the purchase price of such equipment. ILFC has been successful to date both in placing its new aircraft on lease or under sales contract and obtaining adequate financing, but there can be no assurance that such success will continue in future environments.

AIG's Consumer Finance operations provide a wide variety of consumer finance products, including real estate loans, credit card loans, non-real estate loans, retail sales finance and credit-related insurance to customers both domestically and overseas, particularly in emerging markets. These products are funded through a combination of deposits and various borrowings including commercial paper and medium term notes. AIG's Consumer Finance operations are exposed to credit risk and risk of loss resulting from adverse fluctuations in interest rates. Over half of the finance receivables are real estate loans which are substantially collateralized by the related properties.

With respect to credit losses, the allowance for losses is maintained at a level considered adequate to absorb anticipated credit losses existing in that portfolio as of the balance sheet date.

Capital Markets derivative transactions are carried at market value or at estimated fair value when market prices are not readily available. AIGFP reduces its economic risk exposure through similarly valued offsetting transactions including swaps, trading securities, options, forwards and futures. The estimated fair values of these transactions represent assessments of the present value of expected future cash flows. These transactions are exposed to liquidity risk if AIGFP were required to sell or close out the transactions prior to maturity. AIG believes that the effect of any such event would not be significant to AIG's financial condition or its overall liquidity. (See also the discussion under "Operating Review: Financial Services Operations" and "Derivatives" herein.)

AIGFP uses the proceeds from the issuance of notes and bonds and GIAs to invest in a diversified portfolio of securities, including securities available for sale, at market, and derivative transactions. The funds may also be invested in securities purchased under agreements to resell. The proceeds from the disposal of the aforementioned securities available for sale and securities purchased under agreements to resell are used to fund the maturing GIAs or other AIGFP financings, or invest in new assets. (See also the discussion under "Capital Resources" herein.)

Securities available for sale is predominantly a diversified portfolio of high grade fixed income securities, where the individual securities have varying degrees of credit risk. At September 30, 2006, the average credit rating of this portfolio was in the AA category or the equivalent thereto as determined through rating agencies or internal review. AIGFP has also entered into credit derivative transactions to economically hedge its credit risk associated with $128 million of these securities. Securities deemed below investment grade at September 30, 2006 amounted to approximately $259 million in fair value representing 0.6 percent of the total AIGFP securities available for sale. There have been no significant downgrades through September 30, 2006. If its securities available for sale portfolio were to suffer significant default and the collateral held declined significantly in value with no replacement or the credit default swap counterparty failed to perform, AIGFP could have a liquidity strain. AIG guarantees AIGFP's payment obligations, including its debt obligations.

AIGFP's risk management objective is to minimize interest rate, currency, commodity and equity risks associated with its securities available for sale. That is, when AIGFP purchases a security for its securities available for sale investment portfolio, it simultaneously enters into an offsetting internal hedge such that the payment terms of the hedging transaction offset the payment terms of the investment security, which achieves the economic result of converting the return on the underlying security to U.S. dollar LIBOR plus or minus a spread based on the underlying profit on each security on the initial trade date. The market risk associated with such internal hedges is managed on a portfolio basis, with third-party hedging transactions executed as necessary. As hedge accounting treatment is not achieved in accordance with FAS 133, the unrealized gains and losses on the derivative transactions with unaffiliated third parties are reflected in operating income, whereas the unrealized gains and losses on the underlying securities available for sale resulting from changes in interest rates, currency rates, commodity and equity prices, are recorded in accumulated other comprehensive income. When a security is sold, the realized gain or loss with respect to this security is then recorded in operating income.

Securities purchased under agreements to resell are treated as collateralized financing transactions. AIGFP takes possession of or obtains a security interest in securities purchased under agreements to resell.

AIGFP owns inventories in certain commodities in which it trades, and may reduce the exposure to market risk through the use of swaps, forwards, futures and option contracts. Physical commodities held in AIGFP's wholly-owned broker dealer subsidiary are recorded at market value. All other commodities are recorded at the lower of cost or market.

Trading securities, at market value, and securities and spot commodities sold but not yet purchased, at market value are marked to market daily with the unrealized gain or loss being recognized in income at that time. These trading securities are purchased and sold as necessary to meet the risk management objectives of Capital Markets operations.

The gross unrealized gains and gross unrealized losses of Capital Markets operations included in the financial services assets and liabilities at September 30, 2006 were as follows:

(in millions)	Gross Unrealized Gains	Gross Unrealized Losses
Securities available for sale, at market value	$ 749	$ 18
Unrealized gain/loss on swaps, options and forward transactions*	20,235	12,764

** These amounts are also presented as the respective balance sheet amounts.*

The senior management of AIG defines the policies and establishes general operating parameters for Capital Markets operations. AIG's senior management has established various oversight committees to monitor on an ongoing basis the various financial market, operational and credit risk attendant to the Capital Markets operations. The senior management of AIGFP reports the results of its operations to and reviews future strategies with AIG's senior management.

AIG actively manages the exposures to limit potential losses, while maximizing the rewards afforded by these business opportunities. In doing so, AIG must continually manage a variety of exposures including credit, market, liquidity, operational and legal risks.

Asset Management Operations

AIG's Asset Management operations comprise a wide variety of investment-related services and investment products including institutional and retail asset management, broker dealer services and spread-based investment business from the sale of guaranteed investment contracts, also known as funding agreements (GICs). Such services and products are offered to individuals and institutions both domestically and overseas.

Asset Management Results

Asset Management revenues and operating income for the three and nine-month periods ended September 30, 2006 and 2005 were as follows:

	Three Months Ended September 30,		Nine Months Ended September 30,	
(in millions)	**2006**	2005	**2006**	2005
Revenues:				
Guaranteed investment contracts	**$ 845**	$ 908	**$2,517**	$2,707
Institutional Asset Management	**265**	279	**1,163**	776
Brokerage Services and Mutual Funds	**71**	67	**217**	192
Other	**57**	101	**201**	276
Total	**$1,238**	$1,355	**$4,098**	$3,951
Operating income:				
Guaranteed investment contracts[(a)]	**$ 175**	$ 294	**$ 635**	$ 939
Institutional Asset Management[(b)(c)]	**89**	155	**721**	424
Brokerage Services and Mutual Funds	**23**	20	**67**	50
Other	**54**	99	**190**	269
Total	**$ 341**	$ 568	**$1,613**	$1,682

(a) Includes the effect of hedging activities that do not qualify for hedge accounting treatment under FAS 133, including the related foreign exchange gains and losses. For the three and nine-month periods ended September 30, 2005, the effect was a gain of $18 million and $127 million, respectively, in operating income. During 2006, these derivative gains and losses are reported as part of the Other category, and not reported in Asset Management operating income.

(b) Includes the full results of certain AIG managed private equity and real estate funds that are consolidated pursuant to FIN 46(R), "Consolidation of Variable Interest Entities". Also includes $(3) million and $77 million for the three-month periods ended September 30, 2006 and 2005, respectively, and $207 million and $189 million for the nine-month periods ended September 30, 2006 and 2005, respectively, of third-party limited partner earnings offset in minority interest expense which is not a component of operating income.

(c) Includes the full results of certain AIG managed partnerships that are consolidated effective January 1, 2006 pursuant to EITF 04-5, "Determining Whether a General Partner, or the General Partners as a Group, Controls a Limited Partnership or Similar Entity When the Limited Partners Have Certain Rights". For the three and nine-month periods ended September 30, 2006, operating income includes $47 million and $203 million, respectively, of third-party limited partner earnings offset in minority interest expense which is not a component of operating income.

Quarterly Asset Management Results

Asset Management operating income decreased 40 percent in the third quarter of 2006 compared to the same period of 2005 on revenues that declined 9 percent due to the continued run-off of GIC balances combined with spread compression in the remaining GIC portfolio. The spread compression has occurred due to an increase in the cost of funds in the short-term floating rate portion of the GIC portfolio, only partially offset by increased investment income from the floating rate assets backing the portfolio.

Operating income in the third quarter of 2006 also declined from the year-ago quarter due to lower transaction-driven revenues that were partially offset by growth in asset-based management fees within Institutional Asset Management.

The GIC portfolio continues to run-off. The MIP has replaced the GIC program as AIG's principal spread-based investment activity. Although the MIP is beginning to show positive operating income, because the asset mix under the MIP does not include the alternative investments utilized in the GIC program, AIG does not expect that the income growth in the MIP will offset the run-off in the GIC portfolio for the foreseeable future. A significant portion of the remaining GIC portfolio consists of floating rate obligations. AIG has entered into hedges to manage against increases in short-term interest rates. AIG continues to believe these hedges are economically effective but do not qualify for hedge accounting treatment under FAS 133. As a result, continued increases in short-term interest rates will negatively affect operating income in the segment. Realized capital gains from the hedges offset the negative trend in GIC related operating income. GIC revenues include income from Sun America partnerships supporting the GIC line of business and are significantly affected by performance in the equity markets. Thus, revenues, operating income and cash flow attributable to GICs will vary among reporting periods.

The MIP was initially launched in the Euromarkets in September 2005 through AIG's $10 billion Euro medium term note program. Through September 30, 2006, AIG has issued the equivalent of $3.3 billion for the MIP in the Euro, U.S. Rule 144A and U.S. public markets.

The revenues and operating income for this segment are largely affected by the general conditions in the equity and credit markets. Realized gains and performance fees are contingent upon various fund closings, maturity levels and market conditions, and by their nature are not predictable. Therefore, the segment's earnings may vary from period to period.

Year-to-date Asset Management Results

Asset Management revenues and operating income decreased 4 percent in the first nine months of 2006 compared to the same period of 2005 due to the decline in operating income from the GIC portfolio, reflecting the continued run-off of GIC balances, combined with spread compression in the remaining GIC portfolio. The decrease in revenues and operating income was partially offset by growth in asset management fees in Institutional Asset Management.

At September 30, 2006 and 2005, AIG's non-affiliated client assets under management, including both retail mutual funds and institutional accounts, were approximately $70 billion and $59 billion and the aggregate GIC reserve was $49.2 billion and $49.7 billion, respectively.

Other Operations

The operating income (loss) for Other operations for the three and nine-month periods ended September 30, 2006 and 2005 was as follows:

Other (in millions)	Three Months Ended September 30, 2006	Three Months Ended September 30, 2005	Nine Months Ended September 30, 2006	Nine Months Ended September 30, 2005
Operating Income (Loss):				
Equity earnings in unconsolidated subsidiaries	**$ 48**	$(205)	**$ 178**	$(109)
Compensation expense – SICO Plans	**(14)**	(63)	**(104)**	(130)
Compensation expense – C.V. Starr tender offer	**–**	–	**(54)**	–
Interest expense	**(227)**	(131)	**(633)**	(382)
Unallocated corporate expenses	**(95)**	(92)	**(356)**	(287)
Realized capital gains (losses)	**(197)**	175	**(182)**	520
Other miscellaneous, net	**15**	(40)	**(20)**	(57)
Total Other	**$(470)**	$(356)	**$(1,171)**	$(445)

Other operating loss amounted to $470 million and $356 million in the three-month periods ended September 30, 2006 and 2005, respectively, as interest expense increased, primarily reflecting increased borrowings by the parent holding company. The third quarter of 2006 also reflects net realized capital losses, primarily reflecting the effect of hedging activities of the Financial Services and Asset Management segments that do not qualify for hedge accounting treatment under FAS 133, partially offset by a gain in the parent company of $86 million from the sale of AIG's investment in IPC Holdings, Ltd. These declines were partially offset by increased equity earnings in certain unconsolidated subsidiaries driven primarily by a decrease in catastrophe losses of $246 million. The third quarter of 2006 also reflects a decrease in compensation expense with respect to the SICO Plans, and income of $21 million resulting from a change in accounting estimate relating to a favorable resolution of a litigation matter.

Other operating loss amounted to $1.17 billion and $445 million in the nine-month periods ended September 30, 2006 and 2005, respectively, as interest expense increased, primarily reflecting increased borrowings by the parent holding company. The first nine months of 2006 also reflects net realized capital losses, as discussed in the preceding paragraph, and an increase in unallocated corporate expenses, reflecting expenses of $29 million in the first nine months of 2006 relating to certain executive departures (of which approximately $18 million related to departures in 2005), and an overall increase in corporate operating expenses primarily resulting from on-going efforts to improve internal controls at the parent holding company. Also reflected in operating loss in the first nine months of 2006 is an out of period adjustment totaling $61 million with respect to the SICO Plans and a one-time charge related to the Starr tender offer of $54 million, both of which were recorded in the first quarter of 2006. See also Note 4 of Notes to the Consolidated Financial Statements for further discussion. These declines

were partially offset by increased equity earnings in certain unconsolidated subsidiaries, and income of $21 million resulting from a change in accounting estimate, as discussed in the preceding paragraph.

Capital Resources

At September 30, 2006, AIG had total consolidated shareholders' equity of $96.15 billion and total consolidated borrowings of $137.1 billion. At that date, $122.1 billion of such borrowings were either not guaranteed by AIG or were AIGFP's matched borrowings under obligations of GIAs, liabilities connected to trust preferred stock, or matched notes and bonds payable.

Borrowings

At September 30, 2006, AIG's net borrowings were $14.98 billion after reflecting amounts that were matched borrowings under AIGFP's obligations of GIAs, matched notes and bonds payable, amounts not guaranteed by AIG and liabilities connected to trust preferred stock. The following table summarizes borrowings outstanding at September 30, 2006 and December 31, 2005:

(in millions)	**2006**	2005
AIG's net borrowings	**$ 14,982**	$ 10,425
Liabilities connected to trust preferred stock	**1,399**	1,391
AIG Matched Investment Program		
Matched notes and bonds payable	**3,333**	–
AIGFP		
GIAs	**21,091**	20,811
Matched notes and bonds payable	**38,184**	24,950
Borrowings not guaranteed by AIG	**58,133**	52,272
Total	**$137,122**	$ 109,849

Borrowings issued or guaranteed by AIG and those borrowings not guaranteed by AIG at September 30, 2006 and December 31, 2005 were as follows:

(in millions)	**2006**	2005
AIG borrowings:		
Notes and bonds payable	**$ 7,482**	$ 4,607
Loans and mortgages payable	**833**	814
AIG Matched Investment Program		
Matched notes and bonds payable	**3,333**	–
Total	**11,648**	5,421
Borrowings guaranteed by AIG:		
AIGFP		
GIAs	**21,091**	20,811
Notes and bonds payable	**31,420**	26,463
Hybrid financial instrument liabilities	**8,150**	—
Total	**60,661**	47,274
AIG Funding, Inc. commercial paper	**4,484**	2,694
AGC Notes and bonds payable	**797**	797
Liabilities connected to trust preferred stock	**1,399**	1,391
Total borrowings issued or guaranteed by AIG	**78,989**	57,577
Borrowings not guaranteed by AIG:		
ILFC		
Commercial paper	**3,148**	2,615
Notes and bonds payable*	**26,085**	23,715
Total	**29,233**	26,330
AGF		
Commercial paper	**4,534**	3,423
Notes and bonds payable	**18,983**	18,719
Total	**23,517**	22,142
Commercial paper:		
AIG Credit Card Company (Taiwan)	**243**	476
AIG Finance (Taiwan) Limited	**9**	–
Total	**252**	476
Loans and mortgages payable:		
AIGCFG	**1,046**	864
AIG Finance (Hong Kong) Limited	**190**	183
Total	**1,236**	1,047
Other Subsidiaries	**1,128**	927
Variable Interest Entity debt:		
A.I. Credit	**880**	–
AIG Global Investment Group	**55**	140
AIG Global Real Estate Investment	**1,555**	977
AIG SunAmerica	**193**	233
ALICO	**84**	–
Total	**2,767**	1,350
Total borrowings not guaranteed by AIG	**58,133**	52,272
Total Debt	**$137,122**	$109,849

** Includes borrowings under Export Credit Facility of $2.7 billion and $2.6 billion, at September 30, 2006 and December 31, 2005, respectively.*

AIG intends to continue its customary practice of issuing debt securities from time to time to meet its financing needs and those of certain of its subsidiaries for general corporate purposes, as well as for a matched investment program. In July 2006, AIG filed and had declared effective a post-effec-

tive amendment to its universal shelf registration statement to sell up to $25.1 billion of debt securities, preferred and common stock and other securities.

In October 2006, AIG established a medium term note program under its shelf registration statement providing for the issuance of up to $25.1 billion of AIG debt securities, the proceeds of which may be used by either AIG or AIGFP for general corporate purposes or to fund the MIP. In October 2006, AIG issued under the program $750 million principal amount of senior notes maturing in 2016 for AIG's general corporate purposes and an aggregate of $1.0 billion principal amount of senior notes maturing in 2011 to fund the MIP.

On April 20, 2006, AIG sold $1.0 billion principal amount of senior notes in a Rule 144A/Regulation S offering maturing in 2036, and on September 30, 2005, AIG sold $1.5 billion principal amount of senior notes in a Rule 144A/Regulation S offering, of which $500 million matures in 2010 and $1.0 billion matures in 2015. The proceeds from these offerings were used by AIG for general corporate purposes. In August 2006, AIG completed exchange offers for these notes pursuant to which AIG issued in exchange substantially identical notes that are registered under the Securities Act.

On June 16, 2006, AIG sold $750 million principal amount of senior, floating rate notes in a Rule 144A offering that matures in 2009. The proceeds of this offering were used to fund the MIP.

AIG has a Euro medium term note program under which an aggregate nominal amount of up to $10.0 billion of notes may be outstanding at any one time. The program provides that additional notes may be issued to replace matured or redeemed notes. As of September 30, 2006, the equivalent of $4.4 billion principal amount of notes were outstanding under the program, of which the proceeds from $2.6 billion of notes were used to fund the MIP. The aggregate amount outstanding includes $76 million resulting from foreign exchange translation into U.S. dollars, of which $72 million relates to notes issued by AIG for general corporate purposes and $4 million relates to notes issued to fund the MIP. AIG has hedged the currency exposure arising from foreign currency denominated notes by economically hedging that exposure, although such hedges do not qualify for hedge accounting treatment under FAS 133. In addition, in October 2006, AIG sold the equivalent of $218 million under the program, of which $180 million was used to fund the MIP and $38 million was used for AIG's general corporate purposes.

In March 2006, AIG borrowed a total of $1.3 billion on an unsecured basis pursuant to loan agreements with third-party banks, of which $500 million matures in February 2007 but can be extended by AIG for an additional seven months and $200 million matures in March 2007; $600 million was repaid in September 2006.

AIGFP uses the proceeds from the issuance of notes and bonds and GIA borrowings to invest in a diversified portfolio of securities and derivative transactions. The borrowings may also be temporarily invested in securities purchased under agreements to resell. AIG guarantees the obligations of AIGFP under AIGFP's structured notes and bonds and GIA borrowings. Certain of AIGFP's notes contain embedded derivatives that are required to be accounted for separately under FAS 133. Upon AIG's early adoption of FAS 155, AIGFP has elected the fair value option for these instruments. Those notes that are accounted for using the fair value option are reported separately under hybrid financial instrument liabilities. (See also the discussions under "Operating Review: Financial Services Operations," "Liquidity" and "Derivatives" herein.)

On June 16, 2006, AIGFP sold an aggregate of $2.0 billion principal amount of senior, floating rate notes in Rule 144A offerings, of which $1.0 billion matures in 2007 and $1.0 billion matures in 2008. AIGFP has a Euro medium term note program under which an aggregate nominal amount of up to $10.0 billion of notes may be outstanding at any one time. The program provides that additional notes may be issued to replace matured or redeemed notes. As of September 30, 2006, $5.39 billion of notes were outstanding under the program, including $283 million resulting from foreign exchange translation into U.S. dollars. Notes issued under this program are included in Notes and Bonds Payable in the preceding table of borrowings.

AIG Funding, Inc. (AIG Funding), through the issuance of commercial paper, helps fulfill the short-term cash requirements of AIG and its subsidiaries. AIG Funding intends to continue to meet AIG's funding requirements through the issuance of commercial paper guaranteed by AIG. The issuance of AIG Funding's commercial paper is subject to the approval of AIG's Board of Directors.

AIG and AIG Funding are parties to unsecured syndicated revolving credit facilities, which as of September 30, 2006, aggregated to $3.25 billion, consisting of $1.625 billion in a 364-day facility that expires in July of 2007 and $1.625 billion in a five-year facility that expires in July of 2011. The 364-day facility allows for the conversion by AIG of any outstanding loans at expiration into one-year term loans. The facilities can be used for general corporate purposes and also to provide backup for AIG's commercial paper programs administered by AIG Funding. AIG expects to replace or extend these credit facilities on or prior to their expiration. There are currently no borrowings outstanding under these facilities, nor were any borrowings outstanding as of September 30, 2006.

In November 2005, AIG and AIG Funding entered into a 364-day revolving credit facility for an aggregate amount of $3 billion, which can be drawn in the form of loans or letters of credit. The credit facility expires in November 2006 but

allows for the issuance of letters of credit with terms of up to ten years and provides for the conversion by AIG of any outstanding loans at expiration into one-year term loans. The facility can be used for general corporate purposes, including providing backup for AIG's commercial paper programs administered by AIG Funding and obtaining letters of credit to secure obligations under insurance and reinsurance transactions. There are currently no loans outstanding under the facility, nor were any loans outstanding as of September 30, 2006. As of such dates, $511 million was available to be drawn under the facility, with the remainder having been drawn in the form of letters of credit.

AIG is also a party to an unsecured 364-day inter-company revolving credit facility provided by certain of its subsidiaries aggregating $2 billion that expires in October of 2007. The facility allows for the conversion of any outstanding loans at expiration into one-year term loans. The facility can be used for general corporate purposes and also to provide backup for AIG's commercial paper programs. AIG expects to replace or extend this credit facility on or prior to its expiration. There are currently no borrowings outstanding under the inter-company facility, nor were any borrowings outstanding as of September 30, 2006.

ILFC fulfills its short term cash requirements through operating cash flows and the issuance of commercial paper. The issuance of commercial paper is subject to the approval of ILFC's Board of Directors and is not guaranteed by AIG. ILFC is a party to unsecured syndicated revolving credit facilities aggregating $6.0 billion at September 30, 2006. The facilities can be used for general corporate purposes and also to provide backup for ILFC's commercial paper program. They consist of $2.0 billion in a 364-day revolving credit facility that expires in October 2006, with a one-year term out option, $2.0 billion in a five-year revolving credit facility that expires in October 2009 and $2.0 billion in a five-year revolving credit facility that expires in October 2010. Subsequent to September 30, 2006, ILFC replaced the $2.0 billion 364-day facility with a five-year, $2.5 billion facility expiring in October 2011. ILFC expects to replace or extend these credit facilities on or prior to their expiration. There are currently no borrowings under these facilities, nor were any borrowings outstanding as of September 30, 2006.

As a well-known seasoned issuer, ILFC has filed an automatic shelf registration statement with the SEC allowing ILFC immediate access to the U.S. public debt markets. For the nine months ended September 30, 2006, $1.2 billion of debt securities were issued under this registration statement and $5.8 billion were issued under a prior registration statement. In addition, ILFC has a Euro medium term note program for $7.0 billion, under which $4.28 billion in notes were sold through September 30, 2006. Notes issued under the Euro medium term note program are included in Notes and bonds payable in the preceding table of borrowings. The foreign exchange adjustment for the foreign currency denominated debt was $534 million at September 30, 2006 and $197 million at December 31, 2005. ILFC has substantially eliminated the currency exposure arising from foreign currency denominated notes by economically hedging the portion of the note exposure not already offset by Euro denominated operating lease payments, although such hedges do not qualify for hedge accounting treatment under FAS 133.

ILFC had a $4.3 billion Export Credit Facility for use in connection with the purchase of approximately 75 aircraft delivered through 2001. This facility was guaranteed by various European Export Credit Agencies. The interest rate varies from 5.75 percent to 5.90 percent on these amortizing ten-year borrowings depending on the delivery date of the aircraft. At September 30, 2006, ILFC had $1.0 billion outstanding under this facility. The debt is collateralized by a pledge of the shares of a subsidiary of ILFC, which holds title to the aircraft financed under the facility.

In May 2004, ILFC entered into a similarly structured Export Credit Facility for up to a maximum of $2.64 billion for Airbus aircraft to be delivered through May 31, 2005. The facility was subsequently increased to $3.64 billion and extended to include aircraft to be delivered through May 31, 2007. The facility becomes available as the various European Export Credit Agencies provide their guarantees for aircraft based on a six-month forward-looking calendar, and the interest rate is determined through a bid process. At September 30, 2006, ILFC had $1.7 billion outstanding under this facility. Borrowings with respect to these facilities are included in Notes and Bonds Payable in the preceding table of borrowings.

In December of 2005, ILFC entered into two tranches of junior subordinated debentures totaling $1.0 billion. Both mature on December 21, 2065, but each tranche has a different call option. The $600 million tranche has a call date of December 21, 2010 and the $400 million tranche has a call date of December 21, 2015. The debenture with the 2010 call date has a fixed interest rate of 5.90 percent for the first five years. The debenture with the 2015 call date has a fixed interest rate of 6.25 percent for the first ten years. Both tranches have interest rate adjustments if the call option is not exercised. If the call option is not exercised, the new interest rate will be a floating quarterly reset rate based on the initial credit spread plus the highest of (i) 3 month LIBOR, (ii) 10-year constant maturity treasury and (iii) 30-year constant maturity treasury.

The proceeds of ILFC's debt financing are primarily used to purchase flight equipment, including progress payments during the construction phase. The primary sources for the repayment of this debt and the interest expense thereon are the cash flow from operations, proceeds from the sale of flight equipment and the rollover and refinancing of the prior debt. AIG does not guarantee the debt obligations of ILFC.

(See also the discussions under "Operating Review: Financial Services Operations" and "Liquidity" herein.)

AGF fulfills its short term cash requirements through the issuance of commercial paper. The issuance of commercial paper is subject to the approval of AGF's Board of Directors and is not guaranteed by AIG. AGF is a party to unsecured syndicated revolving committed credit facilities aggregating $4.25 billion, including a $2.125 billion 364-day revolving credit facility that expires in July of 2007 and a $2.125 billion five-year revolving credit facility that expires in July of 2010. The 364-day facility allows for the conversion by AGF of any outstanding loans at expiration into a one-year term loan. The facilities can be used for general corporate purposes and also to provide backup for AGF's commercial paper programs. AGF expects to replace or extend these credit facilities on or prior to their expiration. There are currently no borrowings under these AGF facilities, nor were any borrowings outstanding as of September 30, 2006.

AGF issued $5.44 billion during 2005 and $1.76 billion in the first nine months of 2006 of fixed rate and variable rate medium term notes ranging in maturities from two to ten years. As of September 30, 2006, notes aggregating $17.48 billion were outstanding with maturity dates ranging from 2006 to 2016 at interest rates ranging from 1.94 percent to 7.50 percent. To the extent deemed appropriate, AGF may enter into swap transactions to manage its effective borrowing with respect to these notes. As a well-known seasoned issuer, AGF has filed an automatic shelf registration statement with the SEC allowing AGF immediate access to the U.S. public debt markets.

AGF's other funding sources include private placement debt, retail note issuances, securitizations of finance receivables that AGF accounts for as on-balance-sheet secured financings and bank financings. In addition, AGF has become an established issuer of long-term debt in the international capital markets.

In addition to debt refinancing activities, proceeds from the collection of finance receivables may be used to pay the principal and interest on AGF's debt. AIG does not guarantee any of the debt obligations of AGF. See also the discussion under "Operating Review — Financial Services Operations" and "Liquidity" herein.

AIG Credit Card Company (Taiwan) and AIG Finance (Taiwan) Limited, both consumer finance businesses in Taiwan, have issued commercial paper for the funding of their own operations. AIG did not guarantee the commercial paper issued by either of these subsidiaries.

Contractual Obligations and Other Commercial Commitments

The maturity schedule of AIG's contractual obligations at September 30, 2006 was as follows:
(in millions)

		Payments due by Period			
	Total Payments	Less Than One Year	1-3 Years	3+-5 Years	Over Five Years
Borrowings[(a)]	$121,937	$28,800	$ 28,763	$26,120	$ 38,254
Interest payments on borrowings	45,021	4,133	8,351	5,988	26,549
Loss reserves[(b)]	79,863	21,962	24,358	11,580	21,963
Insurance and investment contract liabilities[(c)]	633,884	18,756	53,186	48,687	513,255
Aircraft purchase commitments	19,213	983	10,143	4,833	3,254
Total	$899,918	$74,634	$124,801	$97,208	$603,275

(a) Excludes commercial paper and obligations included as debt pursuant to FIN 46(R) and includes hybrid financial instrument liabilities recorded at fair value.

(b) Represents future loss and loss adjustment expense payments estimated based on historical loss development payment patterns.

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

The maturity schedule of AIG's other commercial commitments by segment at September 30, 2006 was as follows:
(in millions)

		Amount of Commitment Expiration			
	Total Amounts Committed	Less Than One Year	1-3 Years	3+-5 Years	Over Five Years
Letters of credit:					
Life Insurance & Retirement Services	$ 185	$ 31	$ 1	$ 23	$ 130
Parent Company[(b)]	540	426	1	113	–
DBG	183	183	–	–	–
Standby letters of credit:					
Capital Markets	1,749	1,457	77	42	173
Guarantees:					
Life Insurance & Retirement Services[(a)]	2,140	112	419	7	1,602
Aircraft Finance	170	–	–	52	118
Asset Management	252	23	59	–	170
Other commercial commitments[(c)]:					
Capital Markets[(d)]	14,585	4,414	1,515	2,616	6,040
Aircraft Finance[(e)]	797	–	–	183	614
Life Insurance & Retirement Services[(f)]	4,281	1,008	1,306	1,080	887
Asset Management	1,193	934	176	47	36
Life Settlement	252	–	252	–	–
DBG[(g)]	873	245	188	440	–
Parent Company	200	58	118	24	–
Total	$ 27,400	$8,891	$4,112	$4,627	$9,770

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

(b) Represents reimbursement obligations under letters of credit issued by commercial banks.

(c) Excludes commitments with respect to pension plans. The annual pension contribution for 2006 is expected to be approximately $70 million for U.S. and non-U.S. Plans.

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

(e) Primarily in connection with options to acquire aircraft.

(f) Primarily AIG SunAmerica commitments to invest in partnerships.

(g) Primarily commitments to invest in limited partnerships.

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

AIG believes that any of its or its subsidiaries' contractual obligations that are subject to "ratings triggers" or financial covenants relating to "ratings triggers" would not have a material adverse effect on its financial condition or liquidity.

As a result of the downgrades of AIG's long-term senior debt ratings, AIG was required to post approximately $1.16 billion of collateral with counterparties to municipal guaranteed investment agreements and financial derivatives transactions. In the event of a further downgrade, AIG will be required to post additional collateral. It is estimated that, as of the close of business on October 31, 2006 based on AIG's outstanding municipal guaranteed investment agreements and financial derivatives transactions as of such date, a further downgrade of AIG's long-term senior debt ratings to 'Aa3' by Moody's or 'AA–' by S&P would permit counterparties to call for approximately $1.1 billion of additional collateral. Further, additional downgrades could result in requirements for substantial additional collateral, which could have a material effect on how AIG manages its liquidity. The actual amount of additional collateral that AIG would be required to post to counterparties in the event of such downgrades depends on market conditions, the market value of the outstanding affected transactions and other factors prevailing at the time of the downgrade. Any additional obligations to post collateral will increase the demand on AIG's liquidity.

Shareholders' Equity

AIG's consolidated shareholders' equity increased during the first nine months of 2006 and twelve months of 2005 as follows:

(in millions)	September 30, 2006	December 31, 2005
Beginning of year	**$86,317**	$79,673
Net income	**10,609**	10,477
Unrealized appreciation (depreciation) of investments, net of taxes	**(852)**	(1,978)
Cumulative translation adjustment, net of taxes	**623**	(540)
Dividends to shareholders	**(1,260)**	(1,615)
Other*	**717**	300
End of period	**$96,154**	$86,317

** Reflects the effects of employee stock transactions and in 2006 also reflects the cumulative effect of accounting changes.*

(See also the discussion under "Operating Review" and "Liquidity" herein and the Consolidated Statement of Comprehensive Income.)

AIG has in the past reinvested most of its unrestricted earnings in its operations and believes such continued reinvestment in the future will be adequate to meet any foreseeable capital needs. However, AIG may choose from time to time to raise additional funds through the issuance of additional securities.

Stock Purchase

During 2006, AIG did not purchase any shares of its common stock under its existing share repurchase authorization. AIG from time to time may buy shares of its common stock in the open market for general corporate purposes, including to satisfy its obligations under various employee benefit plans. At September 30, 2006, an additional 36,542,700 shares could be purchased under the then current authorization by AIG's Board of Directors.

Dividends from Insurance Subsidiaries

Payments of dividends to AIG by its insurance subsidiaries are subject to certain restrictions imposed by regulatory authorities. With respect to AIG's domestic insurance subsidiaries, the payment of any dividend requires formal notice to the insurance department in which the particular insurance subsidiary is domiciled. Under the laws of many states, an insurer may pay a dividend without prior approval of the insurance regulator when the amount of the dividend is below certain regulatory thresholds. To enhance their current capital positions, dividends from the DBG companies were suspended in the fourth quarter of 2005, and AIG has taken various other actions. See "Regulation and Supervision" below. Furthermore, AIG cannot predict how recent regulatory investigations may affect the ability of its regulated subsidiaries to pay dividends.

With respect to AIG's foreign insurance subsidiaries, the most significant insurance regulatory jurisdictions include Bermuda, Japan, Hong Kong, Taiwan, the United Kingdom, Thailand and Singapore.

AIG cannot predict whether the regulatory investigations currently underway or future regulatory issues will impair AIG's financial condition, results of operations or liquidity. To AIG's knowledge, no AIG company is currently on any regulatory or similar "watch list" with regard to solvency. (See also the discussion under "Liquidity" herein.)

Regulation and Supervision

AIG's insurance subsidiaries, in common with other insurers, are subject to regulation and supervision by the states and jurisdictions in which they do business. In the U.S. the National Association of Insurance Commissioners (NAIC) has developed Risk-Based Capital (RBC) requirements. RBC relates an individual insurance company's statutory surplus to the risk inherent in its overall operations.

AIG's insurance subsidiaries file financial statements prepared in accordance with statutory accounting practices prescribed or permitted by domestic and foreign insurance regulatory authorities. The principal differences between statutory financial statements and financial statements prepared in accordance with U.S. GAAP for domestic companies are that statutory financial statements do not reflect deferred policy acquisition costs, some bond portfolios may be carried at amortized cost, assets and liabilities are presented net of reinsurance, policyholder liabilities are valued using more conservative assumptions and certain assets are non-admitted.

In connection with the filing of the 2005 statutory financial statements for AIG's domestic General Insurance companies, AIG agreed with the relevant state insurance regulators on the statutory accounting treatment of various items. The regulatory authorities have also permitted certain of the domestic and foreign insurance subsidiaries to support the carrying value of their investments in certain non-insurance and foreign insurance subsidiaries by utilizing the AIG audited consolidated financial statements to satisfy the requirement that the U.S. GAAP-basis equity of such entities be audited. In addition, the regulatory authorities have permitted the domestic General Insurance companies to utilize audited financial statements prepared on a basis of accounting other than

U.S. GAAP to value investments in joint ventures, limited partnerships and hedge funds. These permitted practices did not affect the domestic General Insurance companies' compliance with minimum regulatory capital requirements.

Statutory capital of each company continued to exceed minimum company action level requirements following the adjustments, but AIG nonetheless contributed an additional $750 million of capital into American Home effective September 30, 2005 and contributed a further $2.25 billion of capital in February 2006 for a total of approximately $3 billion of capital into Domestic General Insurance subsidiaries effective December 31, 2005. To enhance their current capital positions, dividends from the DBG companies were suspended in the fourth quarter of 2005. AIG believes it has the capital resources and liquidity to fund any necessary statutory capital contributions. AIG will review the capital position of its insurance company subsidiaries with various rating agencies and regulators to determine if additional capital contributions or other actions are warranted.

As discussed above, various regulators have commenced investigations into certain insurance business practices. In addition, the OTS and other regulators routinely conduct examinations of AIG and its subsidiaries, including AIG's consumer finance operations. AIG cannot predict the ultimate effect that these investigations and examinations, or any additional regulation arising therefrom, might have on its business. Federal, state or local legislation may affect AIG's ability to operate and expand its various financial services businesses, and changes in the current laws, regulations or interpretations thereof may have a material adverse effect on these businesses. See "Risk Factors — Regulatory Investigations" in Item 1A. of Part I of AIG's 2005 Annual Report on Form 10-K for a further discussion of the effect these investigations may have on AIG's businesses.

AIG's U.S. operations are negatively affected under guarantee fund assessment laws which exist in most states. As a result of operating in a state which has guarantee fund assessment laws, a solvent insurance company may be assessed for certain obligations arising from the insolvencies of other insurance companies which operated in that state. AIG generally records these assessments upon notice. Additionally, certain states permit at least a portion of the assessed amount to be used as a credit against a company's future premium tax liabilities. Therefore, the ultimate net assessment cannot reasonably be estimated. The guarantee fund assessments net of credits for the first nine months of 2006 were $74 million.

AIG is also required to participate in various involuntary pools (principally workers compensation business) which provide insurance coverage for those not able to obtain such coverage in the voluntary markets. This participation is also recorded upon notification, as these amounts cannot reasonably be estimated.

A substantial portion of AIG's General Insurance business and a majority of its Life Insurance & Retirement Services business are conducted in foreign countries. The degree of regulation and supervision in foreign jurisdictions varies. Generally, AIG, as well as the underwriting companies operating in such jurisdictions, must satisfy local regulatory requirements. Licenses issued by foreign authorities to AIG subsidiaries are subject to modification and revocation. Thus, AIG's insurance subsidiaries could be prevented from conducting future business in certain of the jurisdictions where they currently operate. AIG's international operations include operations in various developing nations. Both current and future foreign operations could be adversely affected by unfavorable political developments up to and including nationalization of AIG's operations without compensation. Adverse effects resulting from any one country may affect AIG's results of operations, liquidity and financial condition depending on the magnitude of the event and AIG's net financial exposure at that time in that country.

Foreign operations are individually subject to local solvency margin requirements that require maintenance of adequate capitalization, which AIG complies with by country. In addition, certain foreign locations, notably Japan, have established regulations that can result in guarantee fund assessments. These have not had a material effect on AIG's financial condition or results of operations.

Liquidity

AIG's liquidity is primarily derived from the operating cash flows of its General and Life Insurance & Retirement Services operations. Management believes that AIG's liquid assets, its net cash provided by operations, and access to the capital markets will enable it to meet any anticipated cash requirements.

At September 30, 2006, AIG's consolidated invested assets included $24.14 billion of cash and short-term investments. Consolidated net cash provided by operating activities in the first nine months of 2006 amounted to $6.0 billion.

During the second quarter of 2006, AIG began presenting cash flows related to the origination and sale of finance receivables held for sale as cash flows within operating activities in the Consolidated Statement of Cash Flows. Previously these amounts were presented as cash flows within investing activities. In addition, certain intercompany transactions included in Finance receivables held for sale — originations and purchases and Finance receivable principal payments received in the Consolidated Statement of Cash Flows were not eliminated in 2005. After evaluating the effect of these items during the second quarter of 2006, AIG has revised the 2005 presentation to conform to the 2006 presentation. See Note 11 of Notes to the Consolidated Financial Statements.

The liquidity of the combined insurance operations is derived both domestically and abroad. The combined insurance operating cash flow is derived from two sources, underwriting operations and investment operations. Cash flow includes periodic premium collections, including policyholders' contract deposits, cash flows from investment operations and paid loss recoveries less reinsurance premiums, losses, benefits, and acquisition and operating expenses. Generally, there is a time lag from when premiums are collected and, when as a result of the occurrence of events specified in the policy, the losses and benefits are paid. Investment income cash flow is primarily derived from interest and dividends received and includes realized capital gains net of realized capital losses. (See also the discussions under "Operating Review: General Insurance Operations" and "Life Insurance & Retirement Services Operations" herein.)

With respect to General Insurance operations, if paid losses accelerated beyond AIG's ability to fund such paid losses from current operating cash flows, AIG might need to liquidate a portion of its General Insurance investment portfolio and/or arrange for financing. Potential events causing such a liquidity strain could be the result of several significant catastrophic events occurring in a relatively short period of time. Additional strain on liquidity could occur if the investments sold to fund such paid losses were sold into a depressed market place and/or reinsurance recoverable on such paid losses became uncollectible or collateral supporting such reinsurance recoverable significantly decreased in value. (See also the discussions under "Operating Review: General Insurance Operations" herein.)

With respect to Life Insurance & Retirement Services operations, if a substantial portion of the Life Insurance & Retirement Services operations bond portfolio diminished significantly in value and/or defaulted, AIG might need to liquidate other portions of its Life Insurance & Retirement Services investment portfolio and/or arrange financing. Potential events causing such a liquidity strain could be the result of economic collapse of a nation or region in which Life Insurance & Retirement Services operations exist, nationalization, terrorist acts, or other such economic or political upheaval. In addition, a significant rise in interest rates leading to a significant increase in policyholder surrenders could also create a liquidity strain. (See also the discussions under "Operating Review: Life Insurance & Retirement Services Operations" herein.)

In addition to the combined insurance pretax operating cash flow, AIG's insurance operations held $12.75 billion in cash and short-term investments at September 30, 2006. Operating cash flow and the cash and short-term balances held provided AIG's insurance operations with a significant amount of liquidity. AIG subsidiaries have also issued debt securities to meet capital needs. In December 2005, Transatlantic issued $750 million of debt securities in a public offering, of which $450 million were purchased by other AIG subsidiaries. Transatlantic contributed the proceeds of the offering to a reinsurance company subsidiary.

This liquidity is available, among other things, to purchase predominately high quality and diversified fixed income securities and, to a lesser extent, marketable equity securities, and to provide mortgage loans on real estate, policy loans and collateral loans. This cash flow coupled with proceeds of approximately $91 billion from the maturities, sales and redemptions of fixed income securities and from the sale of equity securities was used to purchase approximately $110 billion of fixed income securities and marketable equity securities during the first nine months of 2006.

AIG's major Financial Services operating subsidiaries consist of AIGFP, ILFC, AGF, AIGCFG and AI Credit. Sources of funds considered in meeting the liquidity needs of AIGFP's operations include guaranteed investment agreements, issuance of long-term and short-term debt, proceeds from maturities and sales of securities available for sale, securities sold under repurchase agreements, and securities and spot commodities sold but not yet purchased. ILFC, AGF, AIGCFG and AI Credit all utilize the commercial paper markets, retail and wholesale deposits, bank loans and bank credit facilities as sources of liquidity. ILFC and AGF also fund in the domestic and international capital markets without reliance on any guarantee from AIG. An additional source of liquidity for ILFC is the use of export credit facilities. AIGCFG also uses wholesale and retail bank deposits as sources of funds. On occasion, AIG has provided equity capital to ILFC, AGF and AIGCFG and provides intercompany loans to AIGCFG. An AIG subsidiary purchased additional shares of ILFC in the amount of $400 million during the third quarter of 2005. Cash flow provided from operations is a major source of liquidity for AIG's primary Financial Services operating subsidiaries.

AIG, the parent company, funds its short-term working capital needs through commercial paper issued by AIG Funding. As of September 30, 2006, AIG Funding had $4.48 billion of commercial paper outstanding with an average maturity of 27 days. As additional liquidity, AIG parent has a $2 billion inter-company revolving credit facility provided by certain of its subsidiaries, a $1.625 billion 364-day revolving bank credit facility that expires in July 2007, a $1.625 billion five year revolving bank credit facility that expires in July 2011 and a $3 billion 364-day revolving credit facility that expires in November 2006, of which $511 million is currently available as back-up liquidity. AIG parent's primary sources of cash flow are dividends and loans from its subsidiaries. AIG parent's primary uses of cash flow are for debt service, capital contributions to subsidiaries and the payment of dividends to shareholders. On November 9, 2006, AIG intends to redeem its Zero Coupon Convertible Senior Debentures that were issued on November 9, 2001. The aggregate redemption price payable by AIG is approximately $1.07 billion. See also Note 9 of Notes to Consolidated Fi-

nancial Statements in AIG's 2005 Annual Report on Form 10-K/A for additional information on debt maturities for AIG and its subsidiaries.

Special Purpose Vehicles and Off Balance Sheet Arrangements

AIG uses special purpose vehicles (SPVs) and off balance sheet arrangements in the ordinary course of business. As a result of recent changes in accounting, a number of SPVs and off balance sheet arrangements have been reflected in AIG's consolidated financial statements. In January 2003, FASB issued Interpretation No. 46, "Consolidation of Variable Interest Entities" (FIN 46). FIN 46 addressed the consolidation and disclosure rules for nonoperating entities that are now defined as Variable Interest Entities (VIEs). In December 2003, FASB issued a revision to Interpretation No. 46 (FIN 46(R)).

AIG has guidelines with respect to the formation of and investment in SPVs and off balance sheet arrangements. In addition, AIG has expanded the responsibility of its Complex Structured Financial Transaction Committee (CSFT) to include the review of any transaction that could subject AIG to heightened legal, reputational, regulatory, accounting or other risk. See "Management's Report on Internal Control Over Financial Reporting" in Item 9A. of Part II included in AIG's 2005 Annual Report on Form 10-K for a further discussion of the CSFT.

For additional information related to AIG's activities with respect to VIEs and certain guarantees see "Recent Accounting Standards" herein and also Note 8 of Notes to Consolidated Financial Statements. Also, for additional disclosure regarding AIG's commercial commitments (including guarantors), see "Contractual Obligations and Other Commercial Commitments" herein.

Derivatives

Derivatives are financial instruments among two or more parties with returns linked to or "derived" from some underlying equity, debt, commodity or other asset, liability, or index. Derivatives payments may be based on interest rates and exchange rates and/or prices of certain securities, commodities, financial or commodity indices, or other variables. The more significant types of derivative arrangements in which AIG transacts are swaps, forwards, futures and options. In the normal course of business, with the agreement of the original counterparty, these contracts may be terminated early or assigned to another counterparty.

The overwhelming majority of AIG's derivatives activities are conducted by the Capital Markets operations, thus permitting AIG to participate in the derivatives dealer market acting primarily as principal. In these derivative operations, AIG structures transactions that generally allow its counterparties to obtain or hedge exposure to changes in interest and foreign currency exchange rates, credit events, securities' prices and certain commodities and financial or commodity indices. AIG's customers – such as corporations, financial institutions, multinational organizations, sovereign entities, government agencies and municipalities – use derivatives to hedge their own market exposures. For example, a futures, forward or option contract can be used to protect the customers' assets or liabilities against price fluctuations.

A counterparty may default on any obligation to AIG, including a derivative contract. Credit risk is a consequence of extending credit and/or carrying trading and investment positions. Credit risk exists for a derivative contract when that contract has a positive fair value to AIG. To help manage this risk, AIGFP's credit department operates within the guidelines set by the AIG Credit Risk Committee. This committee establishes the credit policy, sets limits for counterparties and provides limits for derivative transactions with counterparties having different credit ratings. In addition to credit ratings, this committee takes into account other factors, including the industry and country of the counterparty. Transactions which fall outside these pre-established guidelines require the specific approval of the AIG Credit Risk Committee. It is also AIG's policy to establish reserves for potential credit impairment when necessary.

In addition, AIGFP utilizes various credit enhancements, including letters of credit, guarantees, collateral, credit triggers, credit derivatives, and margin agreements to reduce the credit risk relating to its outstanding financial derivative transactions. AIGFP requires credit enhancements in connection with specific transactions based on, among other things, the creditworthiness of the counterparties, and the transaction's size and maturity.

AIG's Derivatives Review Committee provides an independent review of any proposed derivative transaction or program except those derivative transactions entered into by AIGFP with third parties. The committee examines, among other things, the nature and purpose of the derivative transaction, its potential credit exposure, if any, and the estimated benefits.

Managing Risk

Market Risk

Market risk is the risk of loss of fair value resulting from adverse fluctuations in interest rates, foreign currencies, equities and commodity prices. AIG has exposures to these risks.

AIG analyzes market risk using various statistical techniques including Value at Risk (VaR). VaR is a summary statistical measure that applies the estimated volatility and correlation of market factors to AIG's market positions. The output from the VaR calculation is the maximum loss that could occur over a defined period of time given a certain probability. While VaR models are relatively sophisticated, the quantitative market risk information generated is limited by the assumptions and parameters established in creating the related models. AIG believes that statistical models alone do

not provide a reliable method of monitoring and controlling market risk. Therefore, such models are tools and do not substitute for the experience or judgment of senior management.

Insurance

AIG has performed a separate VaR analysis for the General Insurance and Life Insurance & Retirement Services segments and for each market risk within each segment. For purposes of the VaR calculation, the insurance assets and liabilities from GICs are included in the Life Insurance & Retirement Services segment. For the calculations in the analyses the financial instrument assets included are the insurance segments' invested assets, excluding real estate and investment income due and accrued, and the financial instrument liabilities included are reserve for losses and loss expenses, unearned premiums, future policy benefits for life and accident and health insurance contracts and other policyholders' funds.

AIG calculated the VaR with respect to the net fair value of each of AIG's insurance segments as of September 30, 2006 and December 31, 2005. The VaR number represents the maximum potential loss as of those dates that could be incurred with a 95 percent confidence (i.e., only five percent of historical scenarios show losses greater than the VaR figure) within a one-month holding period. AIG uses the historical simulation methodology that entails repricing all assets and liabilities under explicit changes in market rates within a specific historical time period. AIG uses the most recent three years of historical market information for interest rates, foreign exchange rates, and equity index prices. For each scenario, each transaction was repriced. Portfolio, business unit and finally AIG-wide scenario values are then calculated by netting the values of all the underlying assets and liabilities.

The following table presents the period-end, average, high and low VaRs on a combined basis and of each component of market risk for each of AIG's insurance segments as of September 30, 2006 and December 31, 2005. Due to diversification effects, the combined VaR is always smaller than the sum of its components.

	2006				2005*			
	As of September 30,	**For the nine months ended September 30,**			As of December 31,	For the year ended December 31,		
(in millions)		**Average**	**High**	**Low**		Average	High	Low
General Insurance:								
Market risk:								
Combined	**$1,703**	**$1,692**	**$1,776**	**$1,617**	$1,617	$1,585	$1,672	$1,396
Interest rate	**1,566**	**1,659**	**1,717**	**1,566**	1,717	1,746	1,931	1,563
Currency	**200**	**150**	**200**	**119**	130	125	139	111
Equity	**535**	**546**	**560**	**535**	535	651	727	535
Life Insurance & Retirement Services:								
Market risk:								
Combined	**$4,469**	**$4,794**	**$5,276**	**$4,442**	$4,515	$4,737	$5,024	$4,515
Interest rate	**4,218**	**4,619**	**5,032**	**4,218**	4,382	4,488	4,750	4,382
Currency	**580**	**548**	**597**	**475**	541	511	560	442
Equity	**1,312**	**1,222**	**1,312**	**1,143**	762	953	1,024	762

* The calculations of Equity VaR for the Life Insurance & Retirement Services segment shown above for all 2006 periods include structured exposures and exposures related to equity-linked guarantees on variable annuity products. These exposures are not included in the Equity VaR calculations for the 2005 periods.

In the Life Insurance & Retirement Services segment, the Combined VaR is near the low point in the range for 2006 and is similar to the Combined VaR at the end of 2005. The Equity VaR increase during 2006 did not cause a corresponding increase in Combined VaR due to both diversification effects and to declines in interest rate volatilities, which reduced Interest Rate VaR during 2006.

Financial Services

AIG generally manages its market exposures within Financial Services by maintaining offsetting positions. Capital Markets seeks to minimize or set limits for open or uncovered market positions. Credit exposure is managed separately. (See the discussion on the management of credit risk above.)

AIG's Market Risk Management Department provides detailed independent review of AIG's market exposures, particularly those market exposures of the Capital Markets operations. This department determines whether AIG's market risks, as well as those market risks of individual subsidiaries, are within the parameters established by AIG's senior management. Well established market risk management techniques such as sensitivity analysis are used. Additionally, this department verifies that specific market risks of each of certain subsidiaries are managed and hedged by that subsidiary.

ILFC is exposed to market risk and the risk of loss of fair value and possible liquidity strain resulting from adverse fluctuations in interest rates. As of September 30, 2006 and December 31, 2005, AIG statistically measured the loss of fair value through the application of a VaR model. In this analysis, the net fair value of Aircraft Finance operations was determined using the financial instrument assets which included the tax adjusted future flight equipment lease revenue, and the financial instrument liabilities which included the

future servicing of the current debt. The estimated effect of the current derivative positions was also taken into account.

AIG calculated the VaR with respect to the net fair value of Aircraft Finance operations using the historical simulation methodology, as previously described. As of September 30, 2006 and December 31, 2005, the average VaR with respect to the net fair value of Aircraft Finance operations was approximately $165 million and $129 million, respectively. In late 2005, ILFC lengthened the average maturity of its debt, leading to an increase in its VaR.

Capital Markets operations are exposed to market risk due to changes in the level and volatility of interest rates, foreign currency exchange rates, equity prices and commodity prices. AIGFP hedges its exposure to these risks primarily through swaps, options, forwards and futures. To economically hedge interest rate risks, AIGFP may also purchase U.S. and foreign government obligations.

AIGFP does not seek to manage the market risk of each transaction through an individual third party offsetting transaction. Rather, AIGFP takes a portfolio approach to the management of its market risk exposures. AIGFP values the predominant portion of its market-sensitive transactions by marking them to market currently through income. A smaller portion is priced by estimated fair value based upon an extrapolation of market factors. There is another limited portion of transactions where the initial fair value is not recorded through income currently and gains or losses are recognized over the life of the transactions. These valuations represent an assessment of the present values of expected future cash flows and may include reserves for such risks as are deemed appropriate by AIGFP and AIG management.

The recorded values of these transactions may be different from the values that might be realized if AIGFP were required to sell or close out the transactions prior to maturity. AIG believes that such differences are not significant to its financial condition or liquidity. Such differences would be immediately recognized in income when the transactions are sold or closed out prior to maturity.

AIGFP attempts to secure reliable and independent current market prices, such as published exchange prices, external subscription services such as from Bloomberg or Reuters or third-party broker quotes for use in this model. When such prices are not available, AIGFP use an internal methodology which includes extrapolation from observable and verifiable prices nearest to the measurement date of the reporting period. Historically, actual results have not materially deviated from these models in any material respect.

Systems used by Capital Markets operations can monitor each unit's respective market positions on an intraday basis. AIGFP operates in major business centers overseas and therefore is open for business essentially 24 hours a day. Thus, the market exposure and offset strategies are regularly monitored, reviewed and coordinated.

AIGFP applies various testing techniques which reflect significant potential market movements in interest rates, foreign exchange rates, commodity and equity prices, volatility levels and the effect of time. These techniques vary by currency and are regularly changed to reflect factors affecting the derivatives portfolio. The results from these analyses are regularly reviewed by AIG management.

As described above, Capital Markets operations are exposed to the risk of loss of fair value from adverse fluctuations in interest rate and foreign currency exchange rates and equity and commodity prices as well as implied volatilities thereon. AIG statistically measures the losses of fair value through the application of a VaR model across Capital Markets.

Capital Markets asset and liability portfolios for which the VaR analyses were performed included over the counter and exchange traded investments, derivative instruments and commodities. Because the market risk with respect to securities available for sale, at market, is substantially hedged, segregation of market sensitive instruments into trading and other than trading was not deemed necessary. The VaR calculation is unaffected by the accounting treatment of hedged transactions under FAS 133.

In the calculation of VaR for Capital Markets operations, AIG uses the same historical simulation methodology, described under Insurance above, which entails repricing all assets and liabilities under explicit changes in market rates within a specific historical time period.

The following table presents the VaR on a combined basis and of each component of market risk for Capital Markets operations as of September 30, 2006 and December 31, 2005. Due to diversification effects, the combined VaR is always smaller than the sum of its components.

(in millions)	**2006**	2005
Combined	**$19**	$22
Interest rate	**9**	9
Currency	**7**	3
Equity	**15**	14
Commodity	**14**	9

The following table presents the average, high and low VaRs on a combined basis and of each component of market risk for Capital Markets operations as of September 30, 2006 and December 31, 2005. Due to diversification effects, the combined VaR is always smaller than the sum of its components.

	2006			2005		
(in millions)	**Average**	**High**	**Low**	Average	High	Low
Combined	**$20**	**$22**	**$19**	$17	$22	$13
Interest rate	**8**	**9**	**7**	9	11	6
Currency	**6**	**9**	**3**	4	6	3
Equity	**14**	**15**	**12**	9	16	5
Commodity	**12**	**16**	**9**	8	10	7

Catastrophe Exposures

The nature of AIG's business exposes it to various catastrophic events in which multiple losses across multiple lines of business can occur in any calendar year. In order to control this exposure, AIG uses a combination of techniques, including setting aggregate limits in key business units, monitoring and modeling accumulated exposures, and purchasing catastrophe reinsurance to supplement its other reinsurance protections.

AIG evaluates catastrophic events and assesses the probability of occurrence and magnitude of catastrophic events through the use of third party models generally recognized as industry standards. Following is an overview of modeled losses associated with the more significant natural perils. The modeled results assume that all reinsurers perform their obligations to AIG in accordance with their terms.

It is important to recognize that there is no standard methodology to project the possible losses from total property and workers compensation exposures and that the use of different models could result in materially different projected losses. Further, there are no industry standard assumptions to be utilized in projecting these losses. The use of different assumptions could materially change the projected losses. Therefore, these modeled losses may not be comparable to estimates made by other companies.

These estimates are inherently uncertain and may not reflect AIG's maximum exposures to these events. It is highly likely that AIG's losses will vary, perhaps significantly, from these estimates.

Natural Catastrophe Exposures

The modeled results provided in the table below were based on the aggregate exceedence probability (AEP) losses which represent total property and workers compensation losses that may occur in any single year from one or more natural events. The model, which has been updated to reflect 2005 catastrophes, generally used 2005 exposure data and the current reinsurance program structure. The values provided were based on 100 year return period losses, which have a 1 percent likelihood of being exceeded in any single year. Thus, there is a one percent probability that AIG could incur in any year losses in excess of the modeled amounts for these perils.

(in millions)

Natural Peril	Gross	Net of Reinsurance	Net, After Income Taxes	% of Consolidated Shareholders' Equity at December 31, 2005
Earthquake	$3,412	$2,283	$1,484	1.7%
Tropical Cyclone*	$5,336	$3,907	$2,540	2.9%

** Includes hurricanes, typhoons and other wind-related events.*

In addition, AIG also evaluates potential single event earthquake and hurricane losses that may be incurred. The single events utilized are a subset of potential events identified and utilized by Lloyd's[1] and referred to as Realistic Disaster Scenarios (RDSs). The purpose of this analysis was to utilize these RDSs to provide a reference frame and place into context the model results. However, it is important to note that the specific events used for this analysis do not necessarily represent the worst case loss that AIG could incur from this type of an event in these regions. The losses associated with the RDSs are included in the table below.

Single event modeled property and workers compensation losses to AIG's worldwide portfolio of risk for key geographic areas. Gross values represent AIG's liability after the application of policy limits and deductibles, and net values represent losses after all reinsurance is applied.

(in millions)

Natural Peril	Gross	Net of Reinsurance
Miami Hurricane	$4,530	$2,911
Northeast Hurricane	3,732	2,498
San Francisco Earthquake	3,628	2,229
Los Angeles Earthquake	3,285	2,145
Gulf Coast Hurricane	2,581	1,391
Japanese Earthquake	339	153
European Windstorm	135	41
Japanese Typhoon	125	105

Because the specific international RDS events do not necessarily correspond to AIG's international exposures, AIG also runs simulations against its own exposures where statistical return period losses associated with the written exposure specific to AIG's exposures provide the basis for monitoring risk. Based on these simulations, the 100 year return period for Japanese Earthquake is $359 million gross, and $113 million net, the 100 year return period for European Windstorm is $168 million gross, and $54 million net, and the 100 year return period for the Japanese Typhoon is $313 million gross, and $260 million net.

ACTUAL RESULTS IN ANY PERIOD ARE LIKELY TO VARY, PERHAPS MATERIALLY, FROM THE MODELED SCENARIOS, AND THE OCCURRENCE OF ONE OR

[1] *Lloyd's Realistic Disaster Scenarios, Scenario Specifications, April 2006*

MORE SEVERE EVENTS COULD HAVE A MATERIAL ADVERSE EFFECT ON AIG'S FINANCIAL CONDITION, RESULTS OF OPERATIONS AND LIQUIDITY.

Measures Implemented to Control Hurricane and Earthquake Catastrophic Risk

Catastrophic risk from the earthquake and hurricane perils is proactively managed through reinsurance programs, and aggregate accumulation monitoring. Catastrophe reinsurance is purchased by AIG from financially sound reinsurers. Recoveries under this program, along with other non-catastrophic reinsurance protections, are reflected in the net values provided in the tables above. In addition to the catastrophic reinsurance programs, hurricane and earthquake exposures are also controlled by monitoring aggregate exposures on a regular basis. The aggregate exposures are calculated by compiling total liability within AIG defined hurricane and earthquake catastrophe risk zones and therefore represent the maximum that could be lost in any individual zone. These aggregate accumulations are tracked over time in order to monitor both long and short term trends. AIG's major property writers, Lexington and The Private Client Group, have also implemented catastrophe related underwriting procedures and manage their books at an account level. Lexington individually models most accounts prior to binding in order to specifically quantify catastrophic risk for each account.

Pandemic Influenza

The potential for a pandemic influenza outbreak has received media attention during the past year. AIG continues to analyze its exposure to this serious threat and, as such, has engaged an external risk management firm to model loss scenarios associated with an outbreak of Avian Flu. Using a 1 in 100 year return period, AIG estimates its after-tax net losses under its life insurance policies due to Avian Flu at approximately 0.9 percent of consolidated shareholders' equity as of December 31, 2005. This estimate was calculated over a 3 year period, although the majority of the losses would be incurred in the first year. The modeled losses calculated were based on 2005 policy data representing approximately 90 percent of AIG's Individual Life, Group Life, and Credit Life books of business, net of reinsurance. This estimate does not include claims that could be made under other policies, such as business interruption or general liability policies, and does not reflect estimates for losses resulting from disruption of AIG's own business operations that may arise out of such a pandemic. The model used to generate this estimate has only recently been developed. The reasonableness of the model and its underlying assumptions cannot readily be verified by reference to comparable historical events. As a result, AIG's actual losses from a pandemic influenza outbreak are likely to vary significantly from those predicted by the model.

Terrorism

Terrorism risk is also monitored to control AIG's exposure. AIG shares its exposures to terrorism risks under the Terrorism Risk Insurance Act (TRIA). AIG's current deductible under TRIA is $3.3 billion and AIG would share 10 percent of certified terrorism losses in excess of the $3.3 billion.

Recent Accounting Standards

At the March 2004 meeting, the Emerging Issue Task Force (EITF) reached a consensus with respect to Issue No. 03-1, "The Meaning of Other-Than Temporary Impairment and Its Application to Certain Investments." On September 30, 2004, the FASB issued FASB Staff Position (FSP) EITF Issue 03-1-1, Effective Date of Paragraphs 10-20 of EITF Issue No. 03-1, "The Meaning of Other-Than-Temporary Impairment and its Application to Certain Investments." In November 2005, FASB issued FSP FAS 115-1, "The Meaning of Other-Than-Temporary Impairment and Its Application to Certain Investments," which replaces the measurement and recognition guidance set forth in Issue No. 03-1 and codifies certain existing guidance on impairment.

On June 1, 2005, the FASB issued Statement No. 154, "Accounting Changes and Error Corrections" (FAS 154). FAS 154 replaces APB Opinion No. 20, "Accounting Changes" and FASB Statement No. 3, "Reporting Accounting Changes in Interim Financial Statements."

At the June 2005 meeting, the EITF reached a consensus with respect to Issue No. 04-5, "Determining Whether a General Partner, or the General Partners as a Group, Controls a Limited Partnership or Similar Entity When the Limited Partners have Certain Rights."

On June 29, 2005, the FASB issued Statement 133 Implementation Issues No. B38, "Embedded Derivatives: Evaluation of Net Settlement with Respect to the Settlement of a Debt Instrument through Exercise of an Embedded Put Option or Call Option" and No. B39, "Application of Paragraph 13(b) to Call Options That are Exercisable Only by the Debtor."

On September 19, 2005, the FASB issued Statement of Position 05-1, "Accounting by Insurance Enterprises for Deferred Acquisition Costs in Connection with Modifications or Exchanges of Insurance Contracts."

On February 16, 2006, the FASB issued FAS No. 155, "Accounting for Certain Hybrid Financial Instruments."

On March 27, 2006, the FASB issued FASB FTB 85-4-1, "Accounting for Life Settlement Contracts by Third-Party Investors" (FSP 85-4-1), an amendment of FTB 85-4, "Accounting for Purchases of Life Insurance."

On April 13, 2006, the FASB issued FSP FIN 46(R)-6, "Determining the Variability to be Considered in Applying FASB Interpretation No. 46(R)."

On July 13, 2006, the FASB issued FASB Interpretation No. 48, "Accounting for Uncertainty in Income Taxes - an interpretation of FASB Statement No. 109" (FIN 48).

Effective January 1, 2006, AIG adopted the fair value recognition provisions of Statement of Financial Accounting Standards No. 123R "Share-Based Payments" (FAS 123R). For further discussion of these recent accounting standards and its application to AIG, see Note 10 of Notes to Consolidated Financial Statements.

On September 13, 2006, the SEC issued Staff Accounting Bulletin No. 108, "Considering the Effects of Prior Year Misstatements when Quantifying Misstatements in Current Year Financial Statements" (SAB 108).

In September 2006, the FASB issued FAS No. 157, "Fair Value Measurements" (FAS No. 157).

In September 2006, the FASB issued FAS No. 158, "Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans, an amendment of FASB Statements No. 87, 88, 106 and 132(R)" (FAS No. 158).

For further discussion of these recent accounting standards and its application to AIG, see Note 8 of the Notes to Consolidated Financial Statements.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Included in Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations.

ITEM 4. CONTROLS AND PROCEDURES

In connection with the preparation of this Form 10-Q, an evaluation was carried out by AIG's management, with the participation of AIG's Chief Executive Officer and Chief Financial Officer, of the effectiveness of AIG's disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934 (Exchange Act)). Disclosure controls and procedures are designed to ensure that information required to be disclosed in reports filed or submitted under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in SEC rules and forms and that such information is accumulated and communicated to management, including the Chief Executive Officer and Chief Financial Officer, to allow timely decisions regarding required disclosures. Based on its evaluation, and in light of the previously identified material weaknesses in internal control over financial reporting, as of December 31, 2005, described within the 2005 Annual Report on Form 10-K, AIG's Chief Executive Officer and Chief Financial Officer concluded that, as of September 30, 2006, AIG's disclosure controls and procedures were ineffective. In addition, there has been no change in AIG's internal control over financial reporting (as defined in Rule 13a-15(f) under the Exchange Act) that occurred during the quarter ended September 30, 2006 that has materially affected, or is reasonably likely to materially affect, AIG's internal control over financial reporting.

Part II – OTHER INFORMATION

ITEM 1A. Risk Factors.

The following supplements the significant factors that may affect our business and operations described under "Risk Factors" in Item 1A. of Part I of AIG's 2005 Annual Report on Form 10-K and Item 1A. of Part II of AIG's Quarterly Report on Form 10-Q for the quarter ended March 31, 2006.

There are limited suppliers of aircraft and engines.

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

ITEM 2. Unregistered Sales of Equity Securities and Use of Proceeds.

The table below provides information with respect to purchases of AIG Common stock during the three months ended September 30, 2006.

Period	Total Number of Shares Purchased[1]	Average Price Paid per Share	Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs	Maximum Number of Shares that May Yet Be Purchased Under the Plans or Programs at End of Month[2]
July 1 - 31	–	$ –	–	36,542,700
August 1 - 31	–	–	–	36,542,700
September 1 - 30	–	–	–	36,542,700
Total	–	$ –	–	

(1) Does not include 41,230 shares delivered or attested to in satisfaction of the exercise price by holders of AIG employee stock options exercised during the three months ended September 30, 2006.

(2) On July 19, 2002, AIG announced that its Board of Directors had authorized the open market purchase of up to 10 million shares of common stock. On February 13, 2003, AIG announced that the Board had expanded the existing program through the authorization of an additional 50 million shares. The purchase program has no set expiration or termination date.

ITEM 6. Exhibits.

See accompanying Exhibit Index.

SIGNATURE

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

AMERICAN INTERNATIONAL GROUP, INC.
(Registrant)

/s/ STEVEN J. BENSINGER

Steven J. Bensinger
Executive Vice President and Chief Financial Officer

/s/ DAVID L. HERZOG

David L. Herzog
Senior Vice President and Comptroller
(Principal Accounting Officer)

Dated: November 9, 2006

EXHIBIT INDEX

Exhibit Number	Description	Location
11	Statement re computation of per share earnings	Included in Note (3) of Notes to Consolidated Financial Statements.
12	Statement re computation of ratios	Filed herewith.
31	Rule 13a-14(a)/15d-14(a) Certifications	Filed herewith.
32	Section 1350 Certifications	Filed herewith.

Exhibit 12

American International Group, Inc.
Computation of Ratios of Earnings to Fixed Charges

(in millions, except ratios)	Three Months Ended September 30, 2006	2005	Nine Months Ended September 30, 2006	2005
Income before income taxes, minority interest and cumulative effect of an accounting change	**$ 6,301**	$ 2,547	**$16,335**	$14,897
Less – Equity income of less than 50% owned persons	**44**	(208)	**174**	(115)
Add – Dividends from less than 50% owned persons	**8**	17	**26**	143
	6,265	2,772	**16,187**	15,155
Add – Fixed charges	**2,306**	2,440	**6,302**	5,909
Less – Capitalized interest	**14**	15	**43**	45
Income before income taxes, minority interest, cumulative effect of an accounting change and fixed charges	**$ 8,557**	$ 5,197	**$22,446**	$21,019
Fixed charges:				
Interest costs	**$ 2,254**	$ 2,389	**$ 6,145**	$ 5,755
Rental expense*	**52**	51	**157**	154
Total fixed charges	**$ 2,306**	$ 2,440	**$ 6,302**	$ 5,909
Ratio of earnings to fixed charges	**3.71**	2.13	**3.56**	3.56
Secondary Ratio				
Interest credited to GIC and GIA policy and contract holders	**$ (1,266)**	$ (1,677)	**$ (3,453)**	$ (3,739)
Total fixed charges excluding interest credited to GIC and GIA policy and contract holders	**$ 1,040**	$ 763	**$ 2,849**	$ 2,170
Secondary ratio of earnings to fixed charges	**7.01**	4.61	**6.67**	7.96

**The portion deemed representative of the interest factor.*

The secondary ratio is disclosed for the convenience of fixed income investors and the rating agencies that serve them and is more comparable to the ratios disclosed by all issuers of fixed income securities. The secondary ratio removes interest credited to guaranteed investment contract (GIC) policyholders and guaranteed investment agreement (GIA) contractholders. Such expenses are also removed from income before income taxes, minority interest and cumulative effect of an accounting change used in this calculation. GICs and GIAs are entered into by AIG's insurance subsidiaries, principally Sun America Life Insurance Company and AIG Financial Products Corp. and its subsidiaries, respectively. The proceeds from GICs and GIAs are invested in a diversified portfolio of securities, primarily investment grade bonds. The assets acquired yield rates greater than the rates on the related policyholders obligation or agreement, with the intent of earning operating income from the spread.

Exhibit 31

CERTIFICATIONS

I, Martin J. Sullivan, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q of American International Group, Inc.;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:

(a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

(b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

(c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

(d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):

(a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

(b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

/s/ MARTIN J. SULLIVAN

Martin J. Sullivan
President and Chief Executive Officer

Date: November 9, 2006

CERTIFICATIONS

I, Steven J. Bensinger, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q of American International Group, Inc.;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:

(a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

(b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

(c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

(d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):

(a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

(b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

/s/ STEVEN J. BENSINGER

Steven J. Bensinger
Executive Vice President and Chief Financial Officer

Date: November 9, 2006

Exhibit 32

CERTIFICATION

In connection with the Quarterly Report on Form 10-Q of American International Group, Inc. (the "Company") for the quarter ended September 30, 2006, as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, Martin J. Sullivan, President and Chief Executive Officer of the Company, certify, pursuant to 18 U.S.C. Section 1350, that to my knowledge:

1. The Report fully complies with the requirements of Section 13(a) or 15(d), as applicable, of the Securities Exchange Act of 1934; and

2. The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

/s/ MARTIN J. SULLIVAN

Martin J. Sullivan
President and Chief Executive Officer

Date: November 9, 2006

The foregoing certification is being furnished solely pursuant to 18 U.S.C. Section 1350 and is not being filed as part of the Report or as a separate disclosure document.

CERTIFICATION

In connection with the Quarterly Report on Form 10-Q of American International Group, Inc. (the "Company") for the quarter ended September 30, 2006, as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, Steven J. Bensinger, Executive Vice President and Chief Financial Officer of the Company, certify, pursuant to 18 U.S.C. Section 1350, that to my knowledge:

1. The Report fully complies with the requirements of Section 13(a) or 15(d), as applicable, of the Securities Exchange Act of 1934; and

2. The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

/s/ STEVEN J. BENSINGER

Steven J. Bensinger
Executive Vice President and Chief Financial Officer

Date: November 9, 2006

The foregoing certification is being furnished solely pursuant to 18 U.S.C. Section 1350 and is not being filed as part of the Report or as a separate disclosure document.

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

Form 10-K

(Mark One)

☑ ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the fiscal year ended December 31, 2006

or

☐ TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the transition period from to

Commission file number 1-8787

American International Group, Inc.

(Exact name of registrant as specified in its charter)

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

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

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

Title of each class	Name of each exchange on which registered
Common Stock, Par Value $2.50 Per Share	New York Stock Exchange, Inc.

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

Title of each class
None

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

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

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

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

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of ''accelerated filer and large accelerated filer'' in Rule 12b-2 of the Exchange Act. (Check one):

Large Accelerated Filer ☑ Accelerated Filer ☐ Non-Accelerated Filer ☐

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes ☐ No ☑

The aggregate market value of the voting and nonvoting common equity held by nonaffiliates of the registrant computed by reference to the price at which the common equity was last sold as of June 30, 2006 (the last business day of the registrant's most recently completed second fiscal quarter), was approximately $130,207,300,000.

As of January 31, 2007, there were outstanding 2,601,583,676 shares of Common Stock, $2.50 par value per share, of the registrant.

Documents Incorporated by Reference:

Portions of the registrant's definitive proxy statement filed or to be filed with the Securities and Exchange Commission pursuant to Regulation 14A involving the election of directors at the Annual Meeting of Shareholders of the registrant scheduled to be held on May 16, 2007 are incorporated by reference in Part III of this Form 10-K.

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* *Except for the information provided in Part I under the heading ''Directors and Executive Officers of AIG,'' Part III Items 10, 11, 12, 13 and 14 are included in AIG's Definitive Proxy Statement to be used in connection with AIG's Annual Meeting of Shareholders scheduled to be held on May 16, 2007.*

Part I

Item 1.
Business

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

General Insurance

American Home Assurance Company (American Home)

National Union Fire Insurance Company of Pittsburgh, Pa. (National Union)

New Hampshire Insurance Company (New Hampshire)

Lexington Insurance Company (Lexington)

The Hartford Steam Boiler Inspection and Insurance Company (HSB)

Transatlantic Reinsurance Company

United Guaranty Residential Insurance Company

American International Underwriters Overseas, Ltd. (AIUO)

Life Insurance & Retirement Services

Domestic:

American General Life Insurance Company (AIG American General)

American General Life and Accident Insurance Company (AGLA)

The United States Life Insurance Company in the City of New York (USLIFE)

The Variable Annuity Life Insurance Company (VALIC)

AIG Annuity Insurance Company (AIG Annuity)

SunAmerica Life Insurance Company (SunAmerica Life)

AIG SunAmerica Life Assurance Company

Foreign:

American Life Insurance Company (ALICO)

AIG Star Life Insurance Co., Ltd. (AIG Star Life)

AIG Edison Life Insurance Company (AIG Edison Life)

American International Assurance Company, Limited, together with American International Assurance Company (Bermuda) Limited (AIA)

American International Reinsurance Company Limited (AIRCO)

Nan Shan Life Insurance Company, Ltd. (Nan Shan)

The Philippine American Life and General Insurance Company (Philamlife)

Financial Services

International Lease Finance Corporation (ILFC)

AIG Financial Products Corp. and AIG Trading Group Inc. and their respective subsidiaries (collectively, AIGFP)

American General Finance, Inc. (AGF)

AIG Consumer Finance Group, Inc. (AIGCFG)

Imperial A.I. Credit Companies

Asset Management

AIG SunAmerica Asset Management Corp. (SAAMCo)

AIG Global Asset Management Holdings Corp. and its subsidiaries and affiliated companies (collectively, AIGGIG)

At December 31, 2006, AIG and its subsidiaries had approximately 106,000 employees.

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

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

**For information on AIG's business segments, see Note 2 of Notes to Consolidated Financial Statements.*

The following table presents the general development of the business of AIG on a consolidated basis, the contributions made to AIG's consolidated revenues and operating income and the assets held, in the periods indicated, by its General Insurance, Life Insurance & Retirement Services, Financial Services and Asset Management operations and other realized capital gains (losses). For additional information, see Item 6. Selected Financial Data, Management's Discussion and Analysis of Financial Condition and Results of Operations and Notes 1 and 2 of Notes to Consolidated Financial Statements.

Years Ended December 31, *(in millions)*	**2006**	2005	2004	2003	2002
General Insurance operations:					
Gross premiums written	**$ 56,280**	$ 52,725	$ 52,046	$ 46,938	$ 36,678
Net premiums written	**44,866**	41,872	40,623	35,031	26,718
Net premiums earned	**43,451**	40,809	38,537	31,306	23,595
Net investment income[(a)]	**5,696**	4,031	3,196	2,566	2,350
Realized capital gains (losses)	**59**	334	228	(39)	(345)
Operating income[(a)(b)(c)(d)]	**10,412**	2,315	3,177	4,502	923
Identifiable assets	**167,004**	150,667	131,658	117,511	105,891
Statutory measures[(e)]:					
Statutory underwriting profit (loss)[(b)(c)(d)]	**4,408**	(2,165)	(564)	1,559	(1,843)
Loss ratio	**64.6**	81.1	78.8	73.1	83.1
Expense ratio	**24.5**	23.6	21.5	19.6	21.8
Combined ratio[(d)]	**89.1**	104.7	100.3	92.7	104.9
Life Insurance & Retirement Services operations:					
GAAP premiums	**30,636**	29,400	28,088	23,496	20,694
Net investment income[(a)]	**19,439**	18,134	15,269	12,942	11,243
Realized capital gains (losses)[(f)]	**88**	(158)	45	362	(295)
Operating income[(a)]	**10,032**	8,904	7,925	6,929	5,258
Identifiable assets	**534,977**	480,622	447,841	372,126	289,914
Insurance in-force at end of year[(g)]	**2,070,600**	1,852,833	1,858,094	1,583,031	1,298,592
Financial Services operations:					
Interest, lease and finance charges[(h)]	**8,010**	10,525	7,495	6,242	6,822
Operating income[(h)]	**524**	4,276	2,180	1,182	2,125
Identifiable assets	**206,845**	166,488	165,995	141,667	128,104
Asset Management operations:					
Net investment income from spread-based products and advisory and management fees	**5,814**	5,325	4,714	3,651	3,467
Operating income	**2,346**	2,253	2,125	1,316	1,125
Identifiable assets	**97,913**	81,080	80,075	64,047	53,732
Other operations:					
Realized capital gains (losses)	**(41)**	165	(229)	(765)	(1,013)
All other[(i)]	**(1,586)**	(2,700)	(333)	(1,257)	(610)
Revenues[(j)(k)]	**113,194**	108,905	97,666	79,421	66,171
Total operating income[(a)(j)(l)]	**21,687**	15,213	14,845	11,907	7,808
Total assets	**979,414**	853,051	801,007	675,602	561,131

(a) Includes the effect of out of period adjustments related to the accounting for certain interests in unit investment trusts and other mutual funds (unit investment trusts). For 2006, the effect was an increase of $490 million in both revenues and operating income for General Insurance and an increase of $240 million and $169 million in revenues and operating income, respectively, for Life Insurance & Retirement Services.

(b) Includes current year catastrophe-related losses of $2.89 billion and $1.05 billion in 2005 and 2004, respectively. There were no significant catastrophe-related losses in 2006.

(c) Includes additional losses incurred and net reinstatement premiums related to prior year catastrophes of $199 million and $277 million in 2006 and 2005, respectively.

(d) Operating income was reduced by fourth quarter charges of $1.8 billion, $850 million and $2.1 billion for 2005, 2004 and 2002, respectively, resulting from the annual review of General Insurance loss and loss adjustment reserves. In 2006, 2005 and 2004, changes in estimates for asbestos and environmental reserves were $198 million, $873 million and $850 million, respectively.

(e) Calculated on the basis under which the U.S.-domiciled insurance companies are required to report such measurements to regulatory authorities.

(f) Includes the effect of hedging activities that did not qualify for hedge accounting treatment under Statement of Financial Accounting Standards No. 133, ''Accounting for Derivative Instruments and Hedging Activities'' (FAS 133) and the application of Statement of Financial Accounting Standards No. 52, ''Foreign Currency Translation'' (FAS 52). For 2006, 2005, 2004, 2003 and 2002, respectively, the amounts included are $355 million, $(495) million, $(140) million, $78 million and $(91) million.

(g) 2005 includes the effect of the non-renewal of a single large group life case of $36 billion. Also, the foreign in-force is translated to U.S. dollars at the appropriate balance sheet exchange rate in each period.

(h) Includes the effect of hedging activities that did not qualify for hedge accounting treatment under FAS 133, including the related foreign exchange gains and losses. For 2006, 2005, 2004, 2003 and 2002, respectively, the effect was $(1.82) billion, $2.01 billion, $(122) million, $(1.01) billion and $220 million in both revenues and operating income for Capital Markets. These amounts result primarily from interest rate and foreign currency derivatives that are economically hedging available for sale securities and borrowings. For 2004, 2003 and 2002, respectively, the effect was $(27) million, $49 million and $20 million in operating income for Aircraft Leasing. In 2006 and 2005, Aircraft Leasing derivative gains and losses were reported as part of AIG's Other category, and were not reported in Aircraft Leasing operating income.

(i) Includes $1.6 billion of regulatory settlement costs in 2005 as described under Item 3. Legal Proceedings.

(j) Includes the effect of hedging activities that did not qualify for hedge accounting treatment under FAS 133, including the related foreign exchange gains and losses. For 2006, 2005, 2004, 2003 and 2002, respectively, the effect was $(1.86) billion, $2.02 billion, $385 million, $(1.50) billion and $(216) million in revenues and $(1.86) billion, $2.02 billion, $671 million, $(1.22) billion and $(58) million in operating income. These amounts result primarily from interest rate and foreign currency derivatives that are hedging available for sale securities and borrowings.

(k) Represents the sum of General Insurance net premiums earned, Life Insurance & Retirement Services GAAP premiums, net investment income, Financial Services interest, lease and finance charges, Asset Management net investment income from spread-based products and advisory and management fees, and realized capital gains (losses).

(l) Represents income before income taxes, minority interest and cumulative effect of accounting changes.

General Insurance Operations

AIG's General Insurance subsidiaries are multiple line companies writing substantially all lines of commercial property and casualty insurance and various personal lines both domestically and abroad. Domestic General Insurance operations are comprised of the Domestic Brokerage Group (DBG), Reinsurance, Personal Lines, and Mortgage Guaranty.

AIG is diversified both in terms of classes of business and geographic locations. In General Insurance, workers compensation business is the largest class of business written and represented approximately 15 percent of net premiums written for the year ended December 31, 2006. During 2006, 8 percent and 7 percent of the direct General Insurance premiums written (gross premiums less return premiums and cancellations, excluding reinsurance assumed and before deducting reinsurance ceded) were written in California and New York, respectively. No other state accounted for more than five percent of such premiums.

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

DBG

AIG's primary Domestic General Insurance division is DBG. DBG's business in the United States and Canada is conducted through American Home, National Union, Lexington, HSB and certain other General Insurance company subsidiaries of AIG. During 2006, DBG accounted for 54 percent of AIG's General Insurance net premiums written.

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

In addition to writing substantially all classes of business insurance, including large commercial or industrial property insurance, excess liability, inland marine, environmental, workers compensation and excess and umbrella coverages, DBG offers many specialized forms of insurance such as aviation, accident and health, equipment breakdown, directors and officers liability (D&O), difference-in-conditions, kidnap-ransom, export credit and political risk, and various types of professional errors and omissions coverages. The AIG Risk Management operation provides insurance and risk management programs for large corporate customers. The AIG Risk Finance operation is a leading provider of customized structured insurance products. Also included in DBG are the operations of AIG Environmental, which focuses specifically on providing specialty products to clients with environmental exposures. Lexington writes surplus lines for risks which conventional insurance companies do not readily provide insurance coverage, either because of complexity or because the coverage does not lend itself to conventional contracts. The AIG Worldsource Division introduces and coordinates AIG's products and services to U.S.-based multinational clients and foreign corporations doing business in the U.S.

Certain of the products of the DBG companies include funding components or have been structured so that little or no insurance risk is actually transferred. Funds received in connection with these products are recorded as deposits and included in other liabilities, rather than premiums and incurred losses.

Reinsurance

The subsidiaries of Transatlantic Holdings, Inc. (Transatlantic) offer reinsurance on both a treaty and facultative basis to insurers in the U.S. and abroad. Transatlantic structures programs for a full range of property and casualty products with an emphasis on specialty risk. Transatlantic is a public company owned 59.2 percent by AIG and therefore is included in AIG's consolidated financial statements.

Personal Lines

AIG's Personal Lines operations provide automobile insurance through AIG Direct, a mass marketing operation, the Agency Auto Division and 21st Century Insurance Group (21st Century), as well as a broad range of coverages for high net-worth individuals through the AIG Private Client Group. 21st Century is a public company owned 61.9 percent by AIG and therefore is included in AIG's consolidated financial statements. During the first quarter of 2007, AIG offered to acquire the outstanding shares of 21st Century not already owned by AIG and its subsidiaries.

Mortgage Guaranty

The main business of the subsidiaries of United Guaranty Corporation (UGC) is the issuance of residential mortgage guaranty insurance, both domestically and internationally, on conventional first lien mortgages for the purchase or refinance of one to four family residences. UGC subsidiaries also write second lien and private student loan guaranty insurance.

Foreign General Insurance

AIG's Foreign General Insurance group accepts risks primarily underwritten through American International Underwriters (AIU), a marketing unit consisting of wholly owned agencies and insurance companies. The Foreign General Insurance group also includes business written by AIG's foreign-based insurance subsidiaries. The Foreign General Insurance group uses various marketing methods and multiple distribution channels to write both commercial and consumer lines insurance with certain refinements for local laws, customs and needs. AIU operates in Asia, the Pacific Rim, Europe, including the U.K., Africa, the Middle East and Latin America. During 2006, the Foreign General Insurance group accounted for 25 percent of AIG's General Insurance net premiums written.

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

The reserve for net losses and loss expenses represents the accumulation of estimates for reported losses (case basis reserves) and provisions for losses incurred but not reported

(IBNR), both reduced by applicable reinsurance recoverable and the discount for future investment income, where permitted. Losses and loss expenses are charged to income as incurred.

Loss reserves established with respect to foreign business are set and monitored in terms of the respective local or functional currency. Therefore, no assumption is included for changes in currency rates. See also Note 1(b) of Notes to Consolidated Financial Statements.

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

The ''Analysis of Consolidated Losses and Loss Expense Reserve Development'' table presents the development of net losses and loss expense reserves for calendar years 1996 through 2006. Immediately following this table is a second table that presents all data on a basis that excludes asbestos and environmental net losses and loss expense reserve development. The opening reserves held are shown at the top of the table for each year end date. The amount of loss reserve discount included in the opening reserve at each date is shown immediately below the reserves held for each year. The undiscounted reserve at each date is thus the sum of the discount and the reserve held.

The upper half of the table presents the cumulative amounts paid during successive years related to the undiscounted opening loss reserves. For example, in the table that excludes asbestos and environmental losses, with respect to the net losses and loss expense reserve of $24.75 billion as of December 31, 1999, by the end of 2006 (seven years later) $29.16 billion had actually been paid in settlement of these net loss reserves. In addition, as reflected in the lower section of the table, the original undiscounted reserve of $25.82 billion was reestimated to be $36.28 billion at December 31, 2006. This increase from the original estimate would generally result from a combination of a number of factors, including reserves being settled for larger amounts than originally estimated. The original estimates will also be increased or decreased as more information becomes known about the individual claims and overall claim frequency and severity patterns. The redundancy (deficiency) depicted in the table, for any particular calendar year, presents the aggregate change in estimates over the period of years subsequent to the calendar year reflected at the top of the respective column heading. For example, the redundancy of $259 million at December 31, 2006 related to December 31, 2005 net losses and loss expense reserves of $57.34 billion represents the cumulative amount by which reserves for 2005 and prior years have developed favorably during 2006.

The bottom of each table below presents the remaining undiscounted and discounted net loss reserve for each year. For example, in the table that excludes asbestos and environmental losses, for the 2001 year end, the remaining undiscounted reserves held as of December 31, 2006 are $12.25 billion, with a corresponding discounted net reserve of $11.35 billion.

The reserves for net losses and loss expenses with respect to Transatlantic and 21st Century are included only in consolidated net losses and loss expenses commencing with the year ended December 31, 1998, the year they were first consolidated in AIG's financial statements. Reserve development for these operations is included only for 1998 and subsequent periods. Thus, the presentation for 1997 and prior year ends is not fully comparable to that for 1998 and subsequent years in the tables below.

Analysis of Consolidated Losses and Loss Expense Reserve Development

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

(in millions)	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005	**2006**
Net Reserves Held	$20,496	$20,901	$25,418	$25,636	$25,684	$26,005	$29,347	$36,228	$47,254	$57,476	**$62,630**
Discount (in Reserves Held)	393	619	897	1,075	1,287	1,423	1,499	1,516	1,553	2,110	**2,264**
Net Reserves Held (Undiscounted)	20,889	21,520	26,315	26,711	26,971	27,428	30,846	37,744	48,807	59,586	**64,894**
Paid (Cumulative) as of:											
One year later	5,712	5,607	7,205	8,266	9,709	11,007	10,775	12,163	14,910	15,326	
Two years later	9,244	9,754	12,382	14,640	17,149	18,091	18,589	21,773	24,377		
Three years later	11,943	12,939	16,599	19,901	21,930	23,881	25,513	28,763			
Four years later	14,152	15,484	20,263	23,074	26,090	28,717	30,757				
Five years later	16,077	17,637	22,303	25,829	29,473	32,685					
Six years later	17,551	18,806	24,114	28,165	32,421						
Seven years later	18,415	19,919	25,770	30,336							
Eight years later	19,200	21,089	27,309								
Nine years later	20,105	22,177									
Ten years later	20,972										

(in millions)	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005	**2006**
Net Reserves Held (undiscounted)	$20,889	$21,520	$26,315	$ 26,711	$ 26,971	$ 27,428	$ 30,846	$ 37,744	$48,807	$59,586	**$64,894**
Undiscounted Liability as of:											
One year later	20,795	21,563	25,897	26,358	26,979	31,112	32,913	40,931	53,486	59,533	
Two years later	20,877	21,500	25,638	27,023	30,696	33,363	37,583	49,463	55,009		
Three years later	20,994	21,264	26,169	29,994	32,732	37,964	46,179	51,497			
Four years later	20,776	21,485	28,021	31,192	36,210	45,203	48,427				
Five years later	20,917	22,405	28,607	33,910	41,699	47,078					
Six years later	21,469	22,720	30,632	38,087	43,543						
Seven years later	21,671	24,209	33,861	39,597							
Eight years later	22,986	26,747	34,986								
Nine years later	25,264	27,765									
Ten years later	26,091										
Net Redundancy/(Deficiency)	(5,202)	(6,245)	(8,671)	(12,886)	(16,572)	(19,650)	(17,581)	(13,753)	(6,202)	53	
Remaining Reserves (Undiscounted)	5,119	5,588	7,677	9,261	11,122	14,393	17,670	22,734	30,632	44,207	
Remaining Discount	360	427	517	623	748	894	1,079	1,265	1,484	1,809	
Remaining Reserves	4,759	5,161	7,160	8,638	10,374	13,499	16,591	21,469	29,148	42,398	

The following table presents the gross liability (before discount), reinsurance recoverable and net liability recorded at each year end and the reestimation of these amounts as of December 31, 2006.

(in millions)	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005	**2006**
Gross Liability, End of Year	$32,605	$ 32,049	$ 36,973	$ 37,278	$ 39,222	$ 42,629	$ 48,173	$ 53,387	$63,431	$79,279	**$82,263**
Reinsurance Recoverable, End of Year	11,716	10,529	10,658	10,567	12,251	15,201	17,327	15,643	14,624	19,693	**17,369**
Net Liability, End of Year	20,889	21,520	26,315	26,711	26,971	27,428	30,846	37,744	48,807	59,586	**64,894**
Reestimated Gross Liability	41,685	43,993	53,004	58,320	63,768	67,554	68,657	69,007	70,895	78,946	
Reestimated Reinsurance Recoverable	15,594	16,227	18,018	18,723	20,224	20,476	20,229	17,511	15,886	19,413	
Reestimated Net Liability	26,091	27,766	34,986	39,597	43,544	47,078	48,428	51,496	55,009	59,533	
Cumulative Gross Redundancy/(Deficiency)	(9,080)	(11,944)	(16,031)	(21,042)	(24,546)	(24,925)	(20,484)	(15,620)	(7,464)	333	

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

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

(in millions)	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005	**2006**
Net Reserves Held	$19,753	$20,113	$24,554	$24,745	$24,829	$25,286	$28,650	$35,559	$45,742	$55,227	**$60,451**
Discount (in Reserves Held)	393	619	897	1,075	1,287	1,423	1,499	1,516	1,553	2,110	**2,264**
Net Reserves Held (Undiscounted)	20,146	20,732	25,451	25,820	26,116	26,709	30,149	37,075	47,295	57,336	**62,715**
Paid (Cumulative) as of:											
One year later	5,603	5,467	7,084	8,195	9,515	10,861	10,632	11,999	14,718	15,047	
Two years later	8,996	9,500	12,190	14,376	16,808	17,801	18,283	21,419	23,906		
Three years later	11,582	12,618	16,214	19,490	21,447	23,430	25,021	28,129			
Four years later	13,724	14,972	19,732	22,521	25,445	28,080	29,987				
Five years later	15,460	16,983	21,630	25,116	28,643	31,771					
Six years later	16,792	18,014	23,282	27,266	31,315						
Seven years later	17,519	18,972	24,753	29,162							
Eight years later	18,149	19,960	26,017								
Nine years later	18,873	20,779									
Ten years later	19,471										

(in millions)	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005	**2006**
Net Reserves Held (undiscounted)	$20,146	$20,732	$25,451	$ 25,820	$ 26,116	$ 26,709	$ 30,149	$ 37,075	$47,295	$57,336	**$62,715**
Undiscounted Liability as of:											
One year later	19,904	20,576	24,890	25,437	26,071	30,274	32,129	39,261	51,048	57,077	
Two years later	19,788	20,385	24,602	26,053	29,670	32,438	35,803	46,865	52,364		
Three years later	19,777	20,120	25,084	28,902	31,619	36,043	43,467	48,691			
Four years later	19,530	20,301	26,813	30,014	34,102	42,348	45,510				
Five years later	19,633	21,104	27,314	31,738	38,655	44,018					
Six years later	20,070	21,336	28,345	34,978	40,294						
Seven years later	20,188	21,836	30,636	36,283							
Eight years later	20,515	23,441	31,556								
Nine years later	21,858	24,261									
Ten years later	22,486										
Net Redundancy/(Deficiency)	(2,340)	(3,529)	(6,105)	(10,463)	(14,178)	(17,309)	(15,361)	(11,616)	(5,069)	259	
Remaining Reserves (undiscounted)	3,015	3,482	5,539	7,121	8,979	12,247	15,523	20,562	28,458	42,030	
Remaining Discount	360	427	517	623	748	894	1,079	1,265	1,484	1,809	
Remaining Reserves	2,655	3,055	5,022	6,498	8,231	11,353	14,444	19,297	26,974	40,221	

The following table presents the gross liability (before discount), reinsurance recoverable and net liability recorded at each year end and the reestimation of these amounts as of December 31, 2006.

(in millions)	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005	**2006**
Gross Liability, End of Year	$30,302	$29,740	$34,474	$ 34,666	$ 36,777	$ 40,400	$ 46,036	$ 51,363	$59,897	$73,912	**$77,211**
Reinsurance Recoverable, End of Year	10,156	9,008	9,023	8,846	10,661	13,691	15,887	14,288	12,602	16,576	**14,495**
Net Liability, End of Year	20,146	20,732	25,451	25,820	26,116	26,709	30,149	37,075	47,295	57,336	**62,715**
Reestimated Gross Liability	32,186	34,940	44,281	50,004	55,974	60,289	61,735	62,488	64,772	73,241	
Reestimated Reinsurance Recoverable	9,699	10,679	12,725	13,722	15,680	16,270	16,225	13,797	12,409	16,164	
Reestimated Net Liability	22,487	24,261	31,556	36,282	40,294	44,019	45,510	48,691	52,363	57,077	
Cumulative Gross Redundancy/(Deficiency)	(1,884)	(5,200)	(9,807)	(15,338)	(19,197)	(19,889)	(15,699)	(11,125)	(4,875)	671	

The reserve for losses and loss expenses as reported in AIG's consolidated balance sheet at December 31, 2006 differs from the total reserve reported in the Annual Statements filed with state insurance departments and, where appropriate, with foreign regulatory authorities. The differences at December 31, 2006 relate primarily to reserves for certain foreign operations not required to be reported in the United States for statutory reporting purposes. Further, statutory practices in the United States require reserves to be shown net of applicable reinsurance recoverable.

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

For further discussion regarding net reserves for losses and loss expenses, see Management's Discussion and Analysis of Financial Condition and Results of Operations — Operating Review — General Insurance Operations — Reserve for Losses and Loss Expenses.

Life Insurance & Retirement Services Operations

AIG's Life Insurance & Retirement Services subsidiaries offer a wide range of insurance and retirement savings products both domestically and abroad. Insurance-oriented products consist of individual and group life, payout annuities (including structured settlements), endowment and accident and health policies. Retirement savings products consist generally of fixed and variable annuities.

There was no significant adverse effect on AIG's Life Insurance & Retirement Services results of operations from economic conditions in any one state, country or geographic region for the year ended December 31, 2006.

Foreign Life Insurance & Retirement Services

In its Life Insurance & Retirement Services businesses, AIG operates overseas principally through ALICO, AIG Star Life, AIG Edison Life, AIA, AIRCO, Nan Shan and Philamlife. ALICO is incorporated in Delaware and all of its business is written outside of the United States. ALICO has operations either directly or through subsidiaries in Europe, including the U.K., Latin America, the Caribbean, the Middle East, South Asia and the Far East, with Japan being the largest territory. AIA operates primarily in China (including Hong Kong), Singapore, Malaysia, Thailand, Korea, Australia, New Zealand, Vietnam, Indonesia, and India. The operations in India are conducted through a joint venture, Tata AIG Life Insurance Company Limited. Nan Shan operates in Taiwan. Philamlife is the largest life insurer in the Philippines. AIG Star Life and AIG Edison Life operate in Japan. Operations in foreign countries comprised 78 percent of Life Insurance & Retirement Services GAAP premiums and 68 percent of Life Insurance & Retirement Services operating income in 2006.

The Foreign Life Insurance & Retirement Services companies have over 270,000 full and part-time agents, as well as independent producers, and sell their products largely to indigenous persons in local and foreign currencies. In addition to the agency outlets, these companies also distribute their products through direct marketing channels, such as mass marketing, and through brokers and other distribution outlets, such as financial institutions.

Life insurance products such as whole life and endowment continue to be significant in the overseas companies, especially in Southeast Asia, while a mixture of life insurance, accident and health and retirement services products are sold in Japan.

AIG also has subsidiary operations in Canada, Egypt, Mexico, Poland, Switzerland, Russia and Puerto Rico, and conducts life insurance business through a joint venture in Brazil and in certain countries in Central and South America.

Domestic Life Insurance & Retirement Services

AIG's principal domestic Life Insurance & Retirement Services operations include AGLA, AIG American General, AIG Annuity, USLIFE, VALIC and SunAmerica Life. These companies utilize multiple distribution channels including independent producers, brokerage, career agents and banks to offer life insurance, annuity and accident and health products and services, as well as financial and other investment products. The domestic Life Insurance & Retirement Services operations comprised 22 percent of total Life Insurance & Retirement Services GAAP premiums and 32 percent of Life Insurance & Retirement Services operating income in 2006.

Reinsurance

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

Various AIG profit centers, including DBG, AIU, AIG Reinsurance Advisors, Inc. and AIG Risk Finance, as well as certain Foreign Life subsidiaries, use AIRCO as a reinsurer for certain of their businesses, and AIRCO also receives premiums from offshore captives of AIG clients. In accordance with permitted accounting practices in Bermuda, AIRCO discounts reserves attributable to certain classes of business assumed from other AIG subsidiaries.

For a further discussion of reinsurance, see Item 1A. Risk Factors — Reinsurance, Management's Discussion and Analysis of Financial Condition and Results of Operations — Risk Management — Reinsurance and Note 5 of Notes to Consolidated Financial Statements.

Insurance Investment Operations

A significant portion of AIG's General Insurance and Life Insurance & Retirement Services revenues are derived from AIG's

insurance investment operations, which are summarized in the following table.

The following table summarizes the investment results of the insurance operations.

Years Ended December 31, *(in millions)*	Annual Average Cash and Invested Assets: Cash (including short-term investments)	Invested Assets[(a)(b)]	Total	Return on Average Cash and Assets[(c)]	Return on Average Assets[(d)]
General Insurance:					
2006	**$3,201**	**$102,231**	**$105,432**	**5.4%**	**5.6%**
2005	2,450	86,211	88,661	4.5	4.7
2004	2,012	73,338	75,350	4.2	4.4
2003	1,818	59,855	61,673	4.2	4.3
2002	1,537	47,477	49,014	4.8	5.0
Life Insurance & Retirement Services:					
2006	**$7,205**	**$384,724**	**$391,929**	**5.0%**	**5.1%**
2005	6,180	352,250	358,430	5.1	5.1
2004	5,089	307,659	312,748	4.9	5.0
2003	4,680	247,608	252,288	5.1	5.2
2002	3,919	199,750	203,669	5.5	5.6

(a) Including investment income due and accrued and real estate.

(b) Includes collateral assets invested under the securities lending program.

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

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

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

Financial Services Operations

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

Aircraft Leasing

AIG's Aircraft Leasing operations represent the operations of ILFC, which generates its revenues primarily from leasing new and used commercial jet aircraft to foreign and domestic airlines. Revenues also result from the remarketing of commercial jets for its own account, and remarketing and fleet management services for airlines and for financial institutions. See also Note 2 of Notes to Consolidated Financial Statements.

Capital Markets

The Capital Markets operations of AIG are conducted primarily through AIGFP, which engages as principal in standard and customized interest rate, currency, equity, commodity, energy and credit products with top-tier corporations, financial institutions, governments, agencies, institutional investors, and high-net-worth individuals throughout the world. AIGFP also invests in a diversified portfolio of securities and principal investments and engages in borrowing activities that include issuing standard and structured notes and other securities and entering into guaranteed investment agreements (GIAs). See also Note 2 of Notes to Consolidated Financial Statements.

Consumer Finance

Consumer Finance operations include AGF as well as AIGCFG. AGF provides a wide variety of consumer finance products, including real estate and non-real estate loans, retail sales finance and credit-related insurance to customers in the United States, Puerto Rico, and the U.S. Virgin Islands. AIGCFG, through its subsidiaries, is engaged in developing a multi-product consumer finance business with an emphasis on emerging markets.

Asset Management Operations

AIG's Asset Management operations comprise a wide variety of investment-related services and investment products, including institutional and retail asset management, broker-dealer services and institutional spread-based investment business. Such services and products are offered to individuals and institutions both domestically and overseas. Asset Management's spread-based

investment business includes the results of AIG's proprietary institutional spread-based investment operation, the Matched Investment Program (MIP), which was launched in September of 2005 and replaced the GIC program.

AIG's principal Asset Management operations are conducted through certain subsidiaries of AIG Retirement Services, Inc., including SAAMCo and the AIG Advisor Group broker dealers (AIG SunAmerica); and through AIGGIG, including AIG Global Investment Corp., AIG Global Real Estate and AIG Private Bank. AIG SunAmerica sells and manages mutual funds and provides financial advisory services through independent-contractor registered representatives. AIGGIG manages invested assets on a global basis for AIG subsidiaries and affiliates, as well as third-party institutional, retail, and private banking clients. AIGGIG offers equity, fixed income and alternative investment funds and provides securities lending and custodial services and numerous forms of structured investment products across all asset classes. Each of these subsidiary operations receives fees for investment products and services provided.

Other Operations

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

AIG also has several other subsidiaries which engage in various businesses. Mt. Mansfield Company, Inc. owns and operates the ski slopes, lifts, school and an inn located at Stowe, Vermont. Also included in AIG's Other operations are unallocated corporate expenses, including interest expense and the settlement costs more fully described in Item 3. Legal Proceedings and Note 12(a) of Notes to Consolidated Financial Statements.

Additional Investments

AIG's significant investments in partially owned companies (which are accounted for under the equity method) include a 19.4 percent interest in Allied World Assurance Holdings, Ltd. (AWAC), a property-casualty insurance holding company, a 24.5 percent interest in The Fuji Fire and Marine Insurance Co., Ltd., a general insurance company, a 26 percent interest in Tata AIG Life Insurance Company, Ltd. and a 26 percent interest in Tata AIG General Insurance Company, Ltd. For a discussion of AIG's investments in partially owned companies, see Note 1(u) of Notes to Consolidated Financial Statements.

Locations of Certain Assets

As of December 31, 2006, approximately 37 percent of the consolidated assets of AIG were located in foreign countries (other than Canada), including $6.5 billion of cash and securities on deposit with foreign regulatory authorities. Foreign operations and assets held abroad may be adversely affected by political developments in foreign countries, including such possibilities as tax changes, nationalization, and changes in regulatory policy, as well as by consequence of hostilities and unrest. The risks of such occurrences and their overall effect upon AIG vary from country to country and cannot easily be predicted. If expropriation or nationalization does occur, AIG's policy is to take all appropriate measures to seek recovery of such assets. Certain of the countries in which AIG's business is conducted have currency restrictions which generally cause a delay in a company's ability to repatriate assets and profits. See also Notes 1 and 2 of Notes to Consolidated Financial Statements and Item 1A. Risk Factors — Foreign Operations.

Regulation

AIG's operations around the world are subject to regulation by many different types of regulatory authorities, including insurance, securities, investment advisory, banking and thrift regulators in the United States and abroad. The regulatory environment can have a significant effect on AIG and its business. AIG's operations have become more diverse and consumer-oriented, increasing the scope of regulatory supervision and the possibility of intervention. In addition, the investigations into financial accounting practices that led to two restatements of AIG's consolidated financial statements have heightened regulatory scrutiny of AIG worldwide.

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

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

Certain states require registration and periodic reporting by insurance companies that are licensed in such states and are controlled by other corporations. Applicable legislation typically

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

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

In preparing both its 2004 and 2005 audited statutory financial statements for its Domestic General Insurance companies, AIG agreed with the relevant regulatory agencies on the statutory accounting treatment of the various items requiring adjustment or restatement. These adjustments and restatements reduced previously reported General Insurance statutory surplus at December 31, 2004 by approximately $3.5 billion to approximately $20.6 billion.

With respect to the 2005 audited statutory financial statements, the state regulators permitted the Domestic General Insurance companies to record a $724 million reduction to opening statutory surplus as of January 1, 2005.

AIG has taken various steps to enhance the capital positions of the Domestic General Insurance companies. AIG entered into capital maintenance agreements with the Domestic General Insurance companies that set forth procedures through which AIG will provide ongoing capital support. Dividends from the Domestic General Insurance companies were suspended from fourth quarter 2005 through 2006, but AIG expects that dividend payments will resume in the first quarter of 2007. AIG contributed an additional $750 million of capital into American Home effective September 30, 2005, and contributed a further $2.25 billion of capital in February 2006 for a total of approximately $3 billion of capital into Domestic General Insurance subsidiaries effective December 31, 2005. Furthermore, in order to allow the Domestic General Insurance companies to record as an admitted asset at December 31, 2006 certain reinsurance ceded to non-U.S. reinsurers (which has the effect of increasing the statutory surplus of such Domestic General Insurance companies), AIG obtained and entered into reimbursement agreements for approximately $2 billion of letters of credit issued by several commercial banks in favor of certain Domestic General Insurance companies.

Risk-Based Capital (RBC) is designed to measure the adequacy of an insurer's statutory surplus in relation to the risks inherent in its business. Thus, inadequately capitalized general and life insurance companies may be identified.

The RBC formula develops a risk-adjusted target level of statutory surplus by applying certain factors to various asset, premium and reserve items. Higher factors are applied to more risky items and lower factors are applied to less risky items. Thus, the target level of statutory surplus varies not only as a result of the insurer's size, but also based on the risk profile of the insurer's operations.

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

The statutory surplus of each of AIG's Domestic General and Life Insurance subsidiaries exceeded their RBC target levels as of December 31, 2006.

To the extent that any of AIG's insurance entities would fall below prescribed levels of statutory surplus, it would be AIG's intention to infuse necessary capital to support that entity.

A substantial portion of AIG's General Insurance business and a majority of its Life Insurance business is carried on in foreign countries. The degree of regulation and supervision in foreign jurisdictions varies. Generally, AIG, as well as the underwriting companies operating in such jurisdictions, must satisfy local regulatory requirements. Licenses issued by foreign authorities to AIG subsidiaries are subject to modification or revocation by such authorities, and AIU or other AIG subsidiaries could be prevented from conducting business in certain of the jurisdictions where they currently operate. In the past, AIU has been allowed to modify its operations to conform with new licensing requirements in most jurisdictions.

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

See also Management's Discussion and Analysis of Financial Condition and Results of Operations — Capital Resources and Liquidity — Regulation and Supervision and Note 11 of Notes to Consolidated Financial Statements.

Competition

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

The insurance industry in particular is highly competitive. Within the United States, AIG's General Insurance subsidiaries compete with approximately 3,100 other stock companies, specialty insurance organizations, mutual companies and other underwriting organizations. AIG's subsidiaries offering Life Insurance & Retirement Services compete in the United States with approximately 2,000 life insurance companies and other participants in related financial services fields. Overseas, AIG subsidiaries compete for business with foreign insurance operations of the larger U.S. insurers, global insurance groups, and local companies in particular areas in which they are active.

AIG's strong ratings have historically provided a competitive advantage. For a discussion of the possible adverse effects on AIG's competitive position as a result of a ratings downgrade, see Item 1A. Risk Factors — AIG's Credit Ratings.

Directors and Executive Officers of AIG

Set forth below is information concerning the directors and executive officers of AIG. All directors are elected for one-year terms at the annual meeting of shareholders. All executive officers are elected to one-year terms, but serve at the pleasure of the Board of Directors.

Except as hereinafter noted, each of the executive officers has, for more than five years, occupied an executive position with AIG or companies that are now its subsidiaries. Other than the employment contracts between AIG and Messrs. Sullivan and Bensinger, there are no other arrangements or understandings between any executive officer and any other person pursuant to which the executive officer was elected to such position. From January 2000 until joining AIG in May 2004, Dr. Frenkel served as Chairman of Merrill Lynch International, Inc. Prior to joining AIG in September 2002, Mr. Bensinger was Executive Vice President and Chief Financial Officer of Combined Specialty Group, Inc. (a division of Aon Corporation) commencing in March 2002, and served as Executive Vice President of Trenwick Group, Ltd. from October 1999 through December 2001. Prior to joining AIG in September 2006, Ms. Kelly served as Executive Vice President and General Counsel of MCI/WorldCom. Previously, she was Senior Vice President and General Counsel of Sears, Roebuck and Co. from 1999 to 2003.

Name	Title	Age	Served as Director or Officer Since
Marshall A. Cohen	Director	71	1992
Martin S. Feldstein	Director	67	1987
Ellen V. Futter	Director	57	1999
Stephen L. Hammerman	Director	68	2005
Richard C. Holbrooke	Director	65	2001
Fred H. Langhammer	Director	63	2006
George L. Miles, Jr.	Director	65	2005
Morris W. Offit	Director	70	2005
James F. Orr III	Director	63	2006
Virginia M. Rometty	Director	49	2006
Martin J. Sullivan	Director, President and Chief Executive Officer	52	2002
Michael H. Sutton	Director	66	2005
Edmund S. W. Tse	Director, Senior Vice Chairman – Life Insurance	69	1996
Robert B. Willumstad	Director and Chairman	61	2006
Frank G. Zarb	Director	72	2001
Jacob A. Frenkel	Vice Chairman – Global Economic Strategies	63	2004
Frank G. Wisner	Vice Chairman – External Affairs	68	1997
Steven J. Bensinger	Executive Vice President and Chief Financial Officer	52	2002
Anastasia D. Kelly	Executive Vice President, General Counsel and Senior Regulatory and Compliance Officer	57	2006
Rodney O. Martin, Jr.	Executive Vice President – Life Insurance	54	2002
Kristian P. Moor	Executive Vice President – Domestic General Insurance	47	1998
Win J. Neuger	Executive Vice President and Chief Investment Officer	57	1995
Robert M. Sandler	Executive Vice President – Domestic Personal Lines	64	1980
Nicholas C. Walsh	Executive Vice President – Foreign General Insurance	56	2005
Jay S. Wintrob	Executive Vice President – Retirement Services	49	1999
William N. Dooley	Senior Vice President – Financial Services	54	1992
David L. Herzog	Senior Vice President and Comptroller	47	2005
Robert E. Lewis	Senior Vice President and Chief Risk Officer	55	1993
Brian T. Schreiber	Senior Vice President – Strategic Planning	41	2002

Item 1A.
Risk Factors

Casualty Insurance Underwriting and Reserves

Casualty insurance liabilities are difficult to predict and may exceed the related reserves for losses and loss expenses. Although AIG annually reviews the adequacy of the established reserve for losses and loss expenses, there can be no assurance that AIG's ultimate loss reserves will not develop adversely and materially exceed AIG's current loss reserves. Estimation of ultimate net losses, loss expenses and loss reserves is a complex process for long-tail casualty lines of business, which include excess and umbrella liability, D&O, professional liability, medical malpractice, workers compensation, general liability, products liability and related classes, as well as for asbestos and environmental exposures. Generally, actual historical loss development factors are used to project future loss development. However, there can be no assurance that future loss development patterns will be the same as in the past. Moreover, any deviation in loss cost trends or in loss development factors might not be discernible for an extended period of time subsequent to the recording of the initial loss reserve estimates for any accident year. Thus, there is the potential for reserves with respect to a number of years to be significantly affected by changes in loss cost trends or loss development factors that were relied upon in setting the reserves. These changes in loss cost trends or loss development factors could be attributable to changes in inflation or in the judicial environment, or in other social or economic phenomena affecting claims. See also Management's Discussion and Analysis of Financial Condition and Results of Operations — Operating Review — General Insurance Operations — Reserve for Losses and Loss Expenses.

Adjustments to Life Insurance & Retirement Services Deferred Policy Acquisition Costs

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

DAC for both insurance-oriented and investment-oriented products as well as retirement services products is reviewed for recoverability, which involves estimating the future profitability of current business. This review involves significant management judgment. If the actual emergence of future profitability were to be substantially lower than estimated, AIG could be required to accelerate its DAC amortization and such acceleration could adversely affect AIG's results of operations. See also Management's Discussion and Analysis of Financial Condition and Results of Operations — Critical Accounting Estimates and Notes 1 and 4 of Notes to Consolidated Financial Statements.

Reinsurance

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

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

A Material Weakness

The remaining material weakness in AIG's internal control over financial reporting relating to income tax accounting could affect the accuracy or timing of future regulatory filings. As of December 31, 2006, AIG's management concluded that the material weakness relating to the controls over income tax accounting was not fully remediated. Remediation of this material weakness is ongoing. Until remediated, this weakness could affect the accuracy or timing of future filings with the SEC and other regulatory authorities. See also Item 9A. Controls and Procedures — Management's Report on Internal Control Over Financial Reporting.

Catastrophe Exposures

The occurrence of catastrophic events could adversely affect AIG's consolidated financial condition or results of operations. The occurrence of events such as hurricanes, earthquakes, pandemic disease, acts of terrorism and other catastrophes could adversely affect AIG's consolidated financial condition or results of

operations, including by exposing AIG's businesses to the following:

- widespread claim costs associated with property, workers compensation, mortality and morbidity claims;
- loss resulting from the cash flows from invested assets being less than the cash flows required to meet the policy and contract liabilities; or
- loss resulting from the actual policy experience adversely emerging in comparison to the assumptions made in the product pricing associated with mortality, morbidity, termination and expenses.

Legal Proceedings

Significant legal proceedings adversely affected AIG's results of operations in 2005. As a result of the settlements discussed below under Item 3. Legal Proceedings, AIG recorded an after-tax charge of approximately $1.15 billion in the fourth quarter of 2005. AIG is party to numerous other legal proceedings and regulatory investigations. It is possible that the effect of the unresolved matters could be material to AIG's consolidated results of operations for an individual reporting period. For a discussion of these unresolved matters, see Item 3. Legal Proceedings.

Regulation

AIG is subject to extensive regulation in the jurisdictions in which it conducts its businesses. AIG's operations around the world are subject to regulation by different types of regulatory authorities, including insurance, securities, investment advisory, banking and thrift regulators in the United States and abroad. AIG's operations have become more diverse and consumer-oriented, increasing the scope of regulatory supervision and the possibility of intervention. In particular, AIG's consumer lending business is subject to a broad array of laws and regulations governing lending practices and permissible loan terms, and AIG would expect increased regulatory oversight relating to this business.

The regulatory environment could have a significant effect on AIG and its businesses. Among other things, AIG could be fined, prohibited from engaging in some of its business activities or subject to limitations or conditions on its business activities. Significant regulatory action against AIG could have material adverse financial effects, cause significant reputational harm, or harm business prospects. New laws or regulations or changes in the enforcement of existing laws or regulations applicable to clients may also adversely affect AIG and its businesses.

Foreign Operations

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

The degree of regulation and supervision in foreign jurisdictions varies. Generally, AIG, as well as the underwriting companies operating in such jurisdictions, must satisfy local regulatory requirements. Licenses issued by foreign authorities to AIG subsidiaries are subject to modification and revocation. Thus, AIG's insurance subsidiaries could be prevented from conducting future business in certain of the jurisdictions where they currently operate. AIG's international operations include operations in various developing nations. Both current and future foreign operations could be adversely affected by unfavorable political developments including tax changes, regulatory restrictions and nationalization of AIG's operations without compensation. Adverse actions from any one country may adversely affect AIG's results of operations, liquidity and financial condition depending on the magnitude of the event and AIG's net financial exposure at that time in that country.

Information Technology

A failure in AIG's operational systems or infrastructure or those of third parties could disrupt business, damage AIG's reputation and cause losses. AIG's operations rely on the secure processing, storage and transmission of confidential and other information in its computer systems and networks. AIG's business depends on effective information systems and the integrity and timeliness of the data it uses to run its business. AIG's ability to adequately price its products and services, establish reserves, provide effective and efficient service to its customers, and to timely and accurately report its financial results also depends significantly on the integrity of the data in its information systems. Although AIG takes protective measures and endeavors to modify them as circumstances warrant, its computer systems, software and networks may be vulnerable to unauthorized access, computer viruses or other malicious code and other events that could have security consequences. If one or more of such events occur, this potentially could jeopardize AIG's or its clients' or counterparties' confidential and other information processed and stored in, and transmitted through, its computer systems and networks, or otherwise cause interruptions or malfunctions in AIG's, its clients', its counterparties' or third parties' operations, which could result in significant losses or reputational damage. AIG may be required to expend significant additional resources to modify its protective measures or to investigate and remediate vulnerabilities or other exposures, and AIG may be subject to litigation and financial losses that are either not insured against or not fully covered by insurance maintained.

Despite the contingency plans and facilities AIG has in place, its ability to conduct business may be adversely affected by a disruption of the infrastructure that supports AIG's business in the communities in which it is located. This may include a disruption involving electrical, communications, transportation or other services used by AIG. These disruptions may occur, for example, as a result of events that affect only the buildings occupied by AIG or as a result of events

with a broader effect on the cities where those buildings are located. If a disruption occurs in one location and AIG's employees in that location are unable to occupy its offices and conduct business or communicate with or travel to other locations, AIG's ability to service and interact with its clients may suffer and it may not be able to successfully implement contingency plans that depend on communication or travel.

AIG's Credit Ratings

Financial strength and credit ratings by major ratings agencies are an important factor in establishing the competitive position of insurance companies and other financial institutions and affect the availability and cost of borrowings. Any ratings downgrade may lessen AIG's ability to compete in certain businesses and may increase AIG's interest expense. Financial strength ratings measure an insurance company's ability to meet its obligations to contract holders and policyholders, help to maintain public confidence in a company's products, facilitate marketing of products and enhance a company's competitive position. Credit ratings measure a company's ability to repay its obligations and directly affect the cost and availability to that company of unsecured financing. Historically, AIG's credit and financial strength ratings have provided AIG a competitive advantage.

From March through June of 2005, the major rating agencies downgraded the ratings of AIG and its insurance subsidiaries in a series of actions. Many of the ratings were put on negative watch or negative outlook, which indicates a potential downgrade. Since then, however, the agencies have affirmed the ratings of AIG and all of its subsidiaries with a stable outlook, which indicates that the rating is not likely to change in the near term, except that S&P maintains a negative outlook on Transatlantic and on the senior long-term debt rating of ILFC.

A downgrade of the credit or financial strength ratings of AIG or its subsidiaries could adversely affect AIG's business and its consolidated results of operations in a number of ways, including:

- increasing AIG's interest expense;
- reducing AIGFP's ability to compete in the structured products and derivatives businesses;
- reducing the competitive advantage of AIG's insurance subsidiaries, which may result in reduced product sales and/or lower prices;
- adversely affecting relationships with agents and sales representatives; and
- in the case of a downgrade of AGF or ILFC, increasing their interest expense and reducing their ability to compete in their respective businesses.

As a result of the downgrades in 2005 discussed above, AIG was required to post approximately $1.16 billion of collateral with counterparties to municipal guaranteed investment contracts and financial derivatives transactions. In the event of a further downgrade, AIG would be required to post additional collateral. It is estimated that, as of the close of business on February 15, 2007, based on AIG's outstanding municipal GIAs and financial derivatives transactions as of such date, a further downgrade of AIG's long-term senior debt ratings to Aa3 by Moody's or AA- by S&P would permit counterparties to call for approximately $864 million of additional collateral. Further, additional downgrades could result in requirements for substantial additional collateral, which could have a material effect on how AIG manages its liquidity. For a further discussion of AIG's credit ratings and the potential effect of posting collateral on AIG's liquidity, see Management's Discussion and Analysis of Financial Condition and Results of Operations — Capital Resources and Liquidity — Credit Ratings and — Liquidity.

Liquidity

Liquidity risk represents the potential inability of AIG to meet all payment obligations when they become due. AIG's liquidity could be impaired by an inability to access the capital markets or by unforeseen significant outflows of cash. This situation may arise due to circumstances that AIG may be unable to control, such as a general market disruption or an operational problem that affects third parties or AIG. AIG depends on dividends, distributions and other payments from its subsidiaries to fund dividend payments and to fund payments on AIG's obligations, including debt obligations. Regulatory and other legal restrictions may limit AIG's ability to transfer funds freely, either to or from its subsidiaries. In particular, many of AIG's subsidiaries, including AIG's insurance subsidiaries, are subject to laws and regulations that authorize regulatory bodies to block or reduce the flow of funds to the parent holding company, or that prohibit such transfers altogether in certain circumstances. These laws and regulations may hinder AIG's ability to access funds that AIG may need to make payments on its obligations. See also Item 1. Business — Regulation.

Some of AIG's investments are relatively illiquid. AIG's investments in certain fixed income investments, certain structured securities, direct private equities, limited partnerships, hedge funds and real estate are relatively illiquid. These asset classes represented nine percent of the carrying value of AIG's total cash and invested assets as of December 31, 2006. If AIG requires significant amounts of cash on short notice in excess of normal cash requirements, AIG may have difficulty selling these investments in a timely manner or be forced to sell them for less than what AIG might otherwise have been able to, or both.

Concentration of AIG's investment portfolios in any particular segment of the economy may have adverse effects. The concentration of AIG's investment portfolios in any particular industry, group of related industries or geographic sector could have an adverse effect on the investment portfolios and consequently on AIG's results of operations and financial position. While AIG seeks to mitigate this risk by having a broadly diversified portfolio, events or developments that have a negative effect on any particular industry, group of related industries or geographic region may have a greater adverse effect on the investment portfolios to the extent that the portfolios are concentrated rather than diversified. Further, AIG's ability to sell assets relating to such particular industry, group of related industries or geographic region may be limited if other market participants are seeking to sell at the same time.

See also Management's Discussion and Analysis of Financial Condition and Results of Operations — Capital Resources and Liquidity — Liquidity.

The Relationships Between AIG and the Starr Entities

The relationships between AIG and the Starr entities may take an extended period of time to unwind and/or resolve, and the consequences of such resolution are uncertain. During 2006, AIG unwound and resolved its most significant relationships with C.V. Starr & Co, Inc. (Starr) and began unwinding and resolving various relationships with Starr International Company, Inc. (SICO). AIG cannot predict what its future relationship with Starr and SICO will be.

The agency relationships between AIG subsidiaries and Starr have been terminated and litigation with Starr has been resolved, but there can be no assurance that AIG will compete successfully for the business previously produced by the Starr agencies. In January 2006, Starr announced that it had completed its tender offers to purchase interests in Starr and that all eligible shareholders had tendered their shares. As a result of completion of the tender offers, no AIG executive currently holds any Starr interest.

AIG has entered into agreements pursuant to which AIG agrees, subject to certain conditions, to assure AIG's current employees that all payments are made under a series of two-year Deferred Compensation Profit Participation Plans provided by SICO (SICO Plans). For a further discussion of the SICO plans, see Note 16 of Notes to Consolidated Financial Statements. Nevertheless, there can be no assurance that AIG will be able to effectively address the consequences for its executives of the unwinding of their participation in the SICO plans and programs. Finally, litigation between AIG and SICO remains pending, and the timing, terms and effect on AIG of any resolution cannot currently be predicted. See also Item 3. Legal Proceedings.

Employee Error and Misconduct

Employee error and misconduct may be difficult to detect and prevent and may result in significant losses. Losses may result from, among other things, fraud, errors, failure to document transactions properly or to obtain proper internal authorization or failure to comply with regulatory requirements.

There have been a number of highly publicized cases involving fraud or other misconduct by employees in the financial services industry in recent years, and AIG runs the risk that employee misconduct could occur. It is not always possible to deter or prevent employee misconduct and the precautions AIG takes to prevent and detect this activity may not be effective in all cases.

Aircraft Suppliers

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

Item 1B.
Unresolved Staff Comments

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

Item 2.
Properties

AIG and its subsidiaries operate from approximately 2,300 offices in the United States, 6 offices in Canada and numerous offices in approximately 100 foreign countries. The offices in Greensboro and Winston-Salem, North Carolina; Springfield, Illinois; Amarillo, Ft. Worth and Houston, Texas; Wilmington, Delaware; San Juan, Puerto Rico; Tampa, Florida; Livingston, New Jersey; Evansville, Indiana; Nashville, Tennessee; 70 Pine Street, 72 Wall Street and 175 Water Street in New York, New York; and offices in more than 30 foreign countries and jurisdictions including Bermuda, Chile, Hong Kong, the Philippines, Japan, United Kingdom, Singapore, Malaysia, Switzerland, Taiwan and Thailand are located in buildings owned by AIG and its subsidiaries. The remainder of the office space utilized by AIG subsidiaries is leased.

Item 3.
Legal Proceedings

General

AIG and its subsidiaries, in common with the insurance industry in general, are subject to litigation, including claims for punitive damages, in the normal course of their business. See also Note 12(a) of Notes to Consolidated Financial Statements, as well as the discussion and analysis of Consolidated Net Losses and Loss Expense Reserve Development and Management's Discussion and Analysis of Financial Condition and Results of Operations herein.

2006 Regulatory Settlements

In February 2006, AIG reached a final settlement with the SEC, the United States Department of Justice (DOJ), the Office of the New York Attorney General (NYAG) and the New York State Department of Insurance (DOI). The settlements resolved investigations conducted by the SEC, NYAG and DOI in connection with the accounting, financial reporting and insurance brokerage practices of AIG and its subsidiaries, as well as claims relating to the underpayment of certain workers compensation premium taxes and other assessments. The 2005 financial statements included in this Annual Report on Form 10-K include a fourth quarter after-tax charge of $1.15 billion relating to the settlements.

As part of the settlement with the SEC, the SEC filed a civil complaint, alleging that from 2000 until 2005, AIG materially falsified its financial statements through a variety of transactions and entities in order to strengthen the appearance of its financial results to analysts and investors. AIG, without admitting or denying the allegations in the SEC complaint, consented to the issuance of a final judgment on February 9, 2006:
(a) permanently restraining and enjoining AIG from violating Section 17(a) of the Securities Act of 1933 (Securities Act) and Sections 10(b), 13(a), 13(b)(2) and 13(b)(5) and Rules 10b-5, 12b-20, 13a-1, 13a-13 and 13b2-1 of the Exchange Act;
(b) ordering AIG to pay disgorgement in the amount of $700 million; and (c) ordering AIG to pay a civil penalty in the amount of $100 million. The $800 million was deposited into a fund under the supervision of the SEC to be available to resolve claims asserted against AIG by investors, including the shareholder lawsuits described below.

In February 2006, AIG and the DOJ entered into a letter agreement whereby AIG agreed to cooperate with the DOJ in the DOJ's ongoing criminal investigation of violations of federal criminal law in connection with misstatements in periodic financial reports that AIG filed with the SEC between 2000 and 2004 relating to certain transactions, accepted responsibility for certain of its actions and those of its employees relating to these transactions, and paid $25 million in penalties.

In February 2006, AIG entered into agreements with the NYAG and the DOI, resolving claims under New York's Martin Act and insurance laws. Under the agreements, $375 million was paid into a fund under the supervision of the NYAG and the DOI to be available principally to pay certain insureds who purchased AIG excess casualty policies through Marsh & McLennan Companies, Inc. or Marsh Inc. (Marsh). In addition, a fund of approximately $343 million was created to pay obligations resulting from the underpayment by AIG of its workers compensation premium taxes and related fees and assessments. In addition, AIG paid a $100 million fine to the State of New York.

As part of these settlements, AIG has agreed to retain, for a period of three years, an independent consultant who will conduct a review that will include, among other things, the adequacy of AIG's internal controls over financial reporting, the policies, procedures and effectiveness of AIG's regulatory, compliance and legal functions, and the remediation plan that AIG has implemented as a result of its own internal review.

PNC Settlement

In November 2004, AIG and AIGFP reached a final settlement with the SEC, the Fraud Section of the DOJ and the United States Attorney for the Southern District of Indiana with respect to issues arising from certain structured transactions entered into with Brightpoint, Inc. and The PNC Financial Services Group, Inc. (PNC), the marketing of transactions similar to the PNC transactions and related matters.

As part of the settlement, the SEC filed against AIG a civil complaint, based on the conduct of AIG primarily through AIGFP, alleging violations of certain antifraud provisions of the federal securities laws and aiding and abetting violations of reporting and record keeping provisions of those laws. AIG, without admitting or denying the allegations in the SEC complaint, consented to the issuance of a final judgment permanently enjoining it and its employees and related persons from violating certain provisions of the Exchange Act, Exchange Act rules and the Securities Act, ordering disgorgement of fees it received in the PNC transactions and providing for AIG to establish a transaction review committee to review the appropriateness of certain future transactions and to retain an independent consultant to examine certain transactions entered into between 2000 and 2004 and review the policies and procedures of the transaction review committee. AIG expects that the review by the independent consultant of transactions entered into by AIG during the 2000 to 2004 period will be completed during 2007.

The settlement with the DOJ consists of separate agreements with AIG and AIGFP and a criminal complaint alleging violations of federal securities laws filed against, and deferred prosecution agreement with, a wholly owned subsidiary of AIGFP. Under the terms of the settlement, AIGFP paid a penalty of $80 million. On January 17, 2006, the court approved an order dismissing the complaint with prejudice.

Regulatory Investigations

Regulators from several states have commenced investigations into insurance brokerage practices related to contingent commissions and other industry-wide practices as well as other broker-related conduct, such as alleged bid rigging.

In addition, various federal and state regulatory agencies are reviewing certain other transactions and practices of AIG and its subsidiaries in connection with industry-wide and other inquiries. AIG has cooperated, and will continue to cooperate, with all these investigations, including by producing documents and other information in response to subpoenas.

Pending Private Litigation

Securities Actions. Beginning in October 2004, a number of putative securities fraud class action suits were filed against AIG and consolidated as *In re American International Group, Inc. Securities Litigation.* Subsequently, a separate, though similar, securities fraud action was also brought against AIG by certain Florida pension funds. The lead plaintiff in the class action is a group of public retirement systems and pension funds benefiting Ohio state employees, suing on behalf of themselves and all purchasers of AIG's publicly traded securities between October 28, 1999 and April 1, 2005. The named defendants are AIG and a number of present and former AIG officers and directors, as well as Starr, SICO, General Reinsurance Corporation and PricewaterhouseCoopers LLP (PwC), among others. The lead plaintiff alleges, among other things, that AIG: (1) concealed that it engaged in anti-competitive conduct through alleged payment of contingent commissions to brokers and participation in illegal bid-rigging; (2) concealed that it used ''income smoothing'' products and other techniques to inflate its earnings; (3) concealed that it marketed and sold ''income smoothing'' insurance products to other companies; and (4) misled investors about the scope of

government investigations. In addition, the lead plaintiff alleges that AIG's former Chief Executive Officer manipulated AIG's stock price. The lead plaintiff asserts claims for violations of Sections 11 and 15 of the Securities Act, Section 10(b) of the Exchange Act, and Rule 10b-5 promulgated thereunder, Section 20(a) of the Exchange Act, and Section 20A of the Exchange Act. In April 2006, the court denied the defendants' motions to dismiss the second amended class action complaint and the Florida complaint. In December 2006, a third amended class action complaint was filed, which does not differ substantially from the prior complaint. Fact and class discovery is currently ongoing.

ERISA Action. Between November 30, 2004 and July 1, 2005, several Employee Retirement Income Security Act of 1974 (ERISA) actions were filed on behalf of a purported class of participants and beneficiaries of three pension plans sponsored by AIG or its subsidiaries. A consolidated complaint filed on September 26, 2005 alleges a class period between September 30, 2000 and May 31, 2005 and names as defendants AIG, the members of AIG's Retirement Board and the Administrative Boards of the plans at issue, and four present or former members of AIG's Board of Directors. The factual allegations in the complaint are essentially identical to those in the securities actions described above. Plaintiffs allege that defendants violated duties under ERISA by allowing the plans to offer AIG stock as a permitted investment, when defendants allegedly knew it was not a prudent investment, and by failing to provide participants with accurate information about AIG stock. AIG's motion to dismiss was denied on December 12, 2006. Discovery will be consolidated with proceedings in the securities actions.

Derivative Actions — Southern District of New York. Between October 25, 2004 and July 14, 2005, seven separate derivative actions were filed in the Southern District of New York, five of which were consolidated into a single action. The New York derivative complaint contains nearly the same types of allegations made in the securities fraud and ERISA actions described above. The named defendants include current and former officers and directors of AIG, as well as Marsh, SICO, Starr, ACE Limited and subsidiaries (ACE), General Reinsurance Corporation, PwC, and certain employees or officers of these entity defendants. Plaintiffs assert claims for breach of fiduciary duty, gross mismanagement, waste of corporate assets, unjust enrichment, insider selling, auditor breach of contract, auditor professional negligence and disgorgement from AIG's former Chief Executive Officer and Chief Financial Officer of incentive-based compensation and AIG share proceeds under Section 304 of the Sarbanes-Oxley Act, among others. Plaintiffs seek, among other things, compensatory damages, corporate governance reforms, and a voiding of the election of certain AIG directors. AIG's Board of Directors has appointed a special committee of independent directors (special committee) to review the matters asserted in the operative consolidated derivative complaint. The court has approved agreements staying the derivative case pending in the Southern District of New York while the special committee performs its work. The current stay extends until March 14, 2007.

Derivative Actions — Delaware Chancery Court. From October 2004 to April 2005, AIG shareholders filed five derivative complaints in the Delaware Chancery Court. All of these derivative lawsuits have been consolidated into a single action. The amended consolidated complaint names 43 defendants (not including nominal defendant AIG) who, like the New York consolidated derivative litigation, are current and former officers and directors of AIG, as well as other entities and certain of their current and former employees and directors. The factual allegations, legal claims and relief sought in the Delaware action are similar to those alleged in the New York derivative actions, except that plaintiffs in the Delaware derivative action assert claims only under state law. The court has approved agreements staying the derivative case pending in the Delaware Chancery Court while the special committee performs its work. The current stay extends until March 14, 2007.

An additional derivative lawsuit, filed in the Delaware Chancery Court in December 2002 against twenty directors and executives of AIG as well as against AIG as a nominal defendant, alleges, among other things, that the directors of AIG breached the fiduciary duties of loyalty and care by approving the payment of commissions to Starr and of rental and service fees to SICO and the executives breached their duty of loyalty by causing AIG to enter into contracts with Starr and SICO and their fiduciary duties by usurping AIG's corporate opportunity. The complaint further alleges that the Starr agencies did not provide any services that AIG was not capable of providing itself, and that the diversion of commissions to these entities was solely for the benefit of Starr's owners. The complaint also alleged that the service fees and rental payments made to SICO and its subsidiaries were improper. Under the terms of a stipulation approved by the Court on February 16, 2006, the claims against the outside independent directors were dismissed with prejudice, while the claims against the other directors were dismissed without prejudice. On October 31, 2005, Messrs. Greenberg, Matthews and Smith, SICO and Starr filed motions to dismiss the amended complaint. In an opinion dated June 21, 2006, the Court denied defendants' motion to dismiss, except with respect to plaintiff's challenge to payments made to Starr before January 1, 2000. On July 21, 2006, plaintiff filed its second amended complaint, which alleges that, between January 1, 2000 and May 31, 2005, individual defendants breached their duty of loyalty by causing AIG to enter into contracts with Starr and SICO and breached their fiduciary duties by usurping AIG's corporate opportunity. Starr is charged with aiding and abetting breaches of fiduciary duty and unjust enrichment for its acceptance of the fees. SICO is no longer named as a defendant. Discovery is currently ongoing.

Policyholder Actions. After the NYAG filed its complaint against insurance broker Marsh, policyholders brought multiple federal antitrust and the Racketeer Influenced and Corrupt Organizations Act (RICO) class actions in jurisdictions across the nation against insurers and brokers, including AIG and a number of its subsidiaries, alleging that the insurers and brokers engaged in a broad conspiracy to allocate customers, steer business, and rig bids. These actions, including 18 complaints filed in different federal courts naming AIG or an AIG subsidiary as a defendant, were

consolidated by the judicial panel on multi-district litigation and transferred to the United States District Court for the District of New Jersey for coordinated pretrial proceedings. The consolidated actions have proceeded in that court in two parallel actions, *In re Insurance Brokerage Antitrust Litigation* (the *Commercial Complaint*) and *In re Employee Benefit Insurance Brokerage Antitrust Litigation* (the *Employee Benefits Complaint*, and together with the *Commercial Complaint*, the multi-district litigation).

The plaintiffs in the *Commercial Complaint* are nineteen corporations, individuals and public entities that contracted with the broker defendants for the provision of insurance brokerage services for a variety of insurance needs. The broker defendants are alleged to have placed insurance coverage on the plaintiffs' behalf with a number of insurance companies named as defendants, including AIG subsidiaries. The *Commercial Complaint* also named ten brokers and fourteen other insurers (one of which has since settled) as defendants. The *Commercial Complaint* alleges that defendants engaged in a widespread conspiracy to allocate customers through ''bid-rigging'' and ''steering'' practices. The *Commercial Complaint* also alleges that the insurer defendants permitted brokers to place business with AIG subsidiaries through wholesale intermediaries affiliated with or owned by those same brokers rather than placing the business with AIG subsidiaries directly. Finally, the *Commercial Complaint* alleges that the insurer defendants entered into agreements with broker defendants that tied insurance placements to reinsurance placements in order to provide additional compensation to each broker. Plaintiffs assert that the defendants violated the Sherman Antitrust Act, RICO, the antitrust laws of 48 states and the District of Columbia, and are liable under common law breach of fiduciary duty and unjust enrichment theories. Plaintiffs seek treble damages plus interest and attorneys' fees as a result of the alleged RICO and Sherman Act violations.

The plaintiffs in the *Employee Benefits Complaint* are nine individual employees and corporate and municipal employers alleging claims on behalf of two separate nationwide purported classes: an employee class and an employer class that acquired insurance products from the defendants from August 26, 1994 to the date of any class certification. The *Employee Benefits Complaint* names AIG, as well as eleven brokers and five other insurers, as defendants. The activities alleged in the *Employee Benefits Complaint,* with certain exceptions, track the allegations of contingent commissions, bid-rigging and tying made in the *Commercial Complaint.*

On October 3, 2006, Judge Hochberg of the District of New Jersey reserved in part and denied in part motions filed by the insurer defendants and broker defendants to dismiss the multi-district litigation. The Court also ordered the plaintiffs in both actions to file supplemental statements of particularity to elaborate on the allegations in their complaints. Plaintiffs filed their supplemental statements on October 25, 2006, and the AIG defendants, along with other insurer and broker defendants in the two consolidated actions, filed renewed motions to dismiss on November 30, 2006. Briefing has been completed on the renewed motions to dismiss, as well as plaintiffs' motion for class certification in both cases. On February 16, 2007, Chief Judge Brown of the District of New Jersey transferred the multi-district litigation to himself. Oral argument on the renewed motions to dismiss has been scheduled before Chief Judge Brown on March 1, 2007. Fact discovery in the multi-district litigation is ongoing.

A number of complaints making allegations similar to those in the *Commercial Complaint* have been filed against AIG and other defendants in state and federal courts around the country. The defendants have thus far been successful in having the federal actions transferred to the District of New Jersey and consolidated into the multi-district litigation. The defendants have also sought to have state court actions making similar allegations stayed pending resolution of the multi-district litigation. In one state court action pending in Florida, the trial court recently decided not to grant an additional stay, but instead to allow the case to proceed.

Litigation Relating to 21st Century. Shortly after the announcement in late January 2007 of AIG's offer to acquire the outstanding shares of 21st Century not already owned by AIG and its subsidiaries, two related class actions were filed in the Superior Court of California, Los Angeles County against AIG, 21st Century and the individual members of 21st Century's Board of Directors, two of whom are current executive officers of AIG. The actions were filed purportedly on behalf of the minority shareholders of 21st Century and assert breaches of fiduciary duty in connection with the AIG proposal. The complaints allege that the proposed per share price is unfair and seek preliminary and permanent injunctive relief to enjoin the consummation of the proposed transaction.

SICO. In July, 2005, SICO filed a complaint against AIG in the Southern District of New York, claiming that AIG had refused to provide SICO access to certain artwork and asked the court to order AIG immediately to release the property to SICO. AIG filed an answer denying SICO's allegations and setting forth defenses to SICO's claims. In addition, AIG filed counterclaims asserting breach of contract, unjust enrichment, conversion, breach of fiduciary duty, a constructive trust and declaratory judgment, relating to SICO's breach of its commitment to use its AIG shares only for the benefit of AIG and AIG employees. Fact and expert discovery has been substantially concluded and briefing on SICO's motion for summary judgment is underway.

Effect on AIG

In the opinion of AIG management, AIG's ultimate liability for the unresolved matters referred to above is not likely to have a material adverse effect on AIG's consolidated financial condition, although it is possible that the effect would be material to AIG's consolidated results of operations for an individual reporting period.

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

There were no matters submitted to a vote of security holders during the fourth quarter of 2006.

Part II

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

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

The following table presents the high and low closing sales prices and the dividends paid per share of AIG's common stock on the New York Stock Exchange Composite Tape, for each quarter of 2006 and 2005.

	2006			2005		
	High	Low	Dividends Paid	High	Low	Dividends Paid
First quarter	**$70.83**	**$65.35**	**$0.150**	$73.46	$54.18	$0.125
Second quarter	**66.54**	**58.67**	**0.150**	58.94	49.91	0.125
Third quarter	**66.48**	**57.76**	**0.165**	63.73	56.00	0.150
Fourth quarter	**72.81**	**66.30**	**0.165**	64.40	60.43	0.150

The approximate number of holders of common stock as of January 31, 2007, based upon the number of record holders, was 58,000.

Subject to the dividend preference of any of AIG's serial preferred stock that may be outstanding, the holders of shares of common stock are entitled to receive such dividends as may be declared by AIG's Board of Directors from funds legally available therefor.

In February 2007, AIG's Board of Directors adopted a new dividend policy, to take effect with the dividend to be declared in the second quarter of 2007, providing that under ordinary circumstances, AIG's plan will be to increase its common stock dividend by approximately 20 percent annually. The payment of any dividend, however, is at the discretion of AIG's Board of Directors, and the future payment of dividends will depend on various factors, including the performance of AIG's businesses, AIG's consolidated financial position, results of operations and liquidity and the existence of investment opportunities.

For a discussion of certain restrictions on the payment of dividends to AIG by some of its insurance subsidiaries, see Note 11 of Notes to Consolidated Financial Statements.

The following table summarizes AIG's stock repurchases for the three-month period ended December 31, 2006:

Period	Total Number of Shares Purchased[(a)(b)]	Average Price Paid per Share	Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs	Maximum Number of Shares that May Yet Be Purchased Under the Plans or Programs at End of Month[(b)]
October 1 - 31, 2006	—	$ —	—	36,542,700
November 1 - 30, 2006	—	—	—	36,542,700
December 1 - 31, 2006	—	—	—	36,542,700
Total	—	$ —	—	

(a) Does not include 165,190 shares delivered or attested to in satisfaction of the exercise price by holders of AIG employee stock options exercised during the three months ended December 31, 2006 or 17,000 shares purchased by ILFC to satisfy obligations under employee benefit plans.

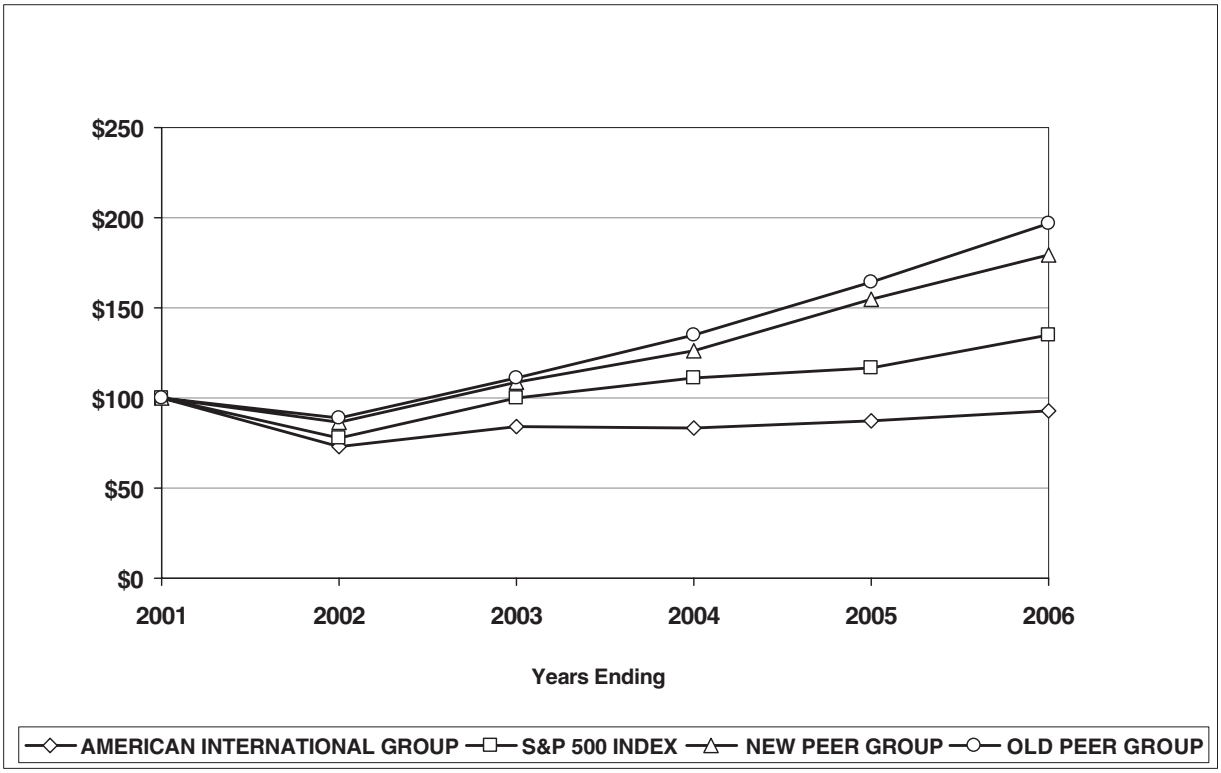
(b) On July 19, 2002, AIG announced that its Board of Directors had authorized the open market purchase of up to 10 million shares of common stock. On February 13, 2003, AIG announced that its Board of Directors had expanded the existing program through the authorization of an additional 50 million shares. The purchase program has no set expiration or termination date. In February 2007, AIG's Board of Directors increased the repurchase program by authorizing the repurchase of shares with an aggregate purchase price of $8 billion.

AIG's table of equity compensation plans previously approved by security holders and equity compensation plans not previously approved by security holders will be included in AIG's Definitive Proxy Statement in connection with its 2007 Annual Meeting of Shareholders, which will be filed with the SEC within 120 days of AIG's fiscal year end.

Performance Graph

The following Performance Graph compares the cumulative total shareholder return on AIG common stock for a five-year period (December 31, 2001 to December 31, 2006) with the cumulative total return of the Standard & Poor's 500 stock index (which includes AIG) and a peer group of companies (the New Peer Group) consisting of nine insurance companies to which AIG compares its business and operations: ACE Limited, Aflac Incorporated, The Chubb Corporation, The Hartford Financial Services Group, Inc., Lincoln National Corporation, MetLife, Inc., Prudential Financial, Inc., The Travelers Companies, Inc. (formerly The St. Paul Travelers Companies, Inc.) and XL Capital Ltd. The Performance Graph also compares the cumulative total shareholder return on AIG common stock to the return of a group of companies comprised of The Allstate Corporation, The Chubb Corporation, CNA Financial Corporation, The Hartford Financial Services Group, Inc., Lincoln National Corporation, MetLife, Inc., Prudential Financial, Inc. and The Travelers Companies, Inc. (the Old Peer Group), to which AIG compared itself in the Performance Graph included in its Definitive Proxy Statement in connection with AIG's 2006 Annual Meeting of Shareholders. ACE Limited, Aflac Incorporated, and XL Capital Ltd have been added to the New Peer Group to reflect their status as significant competitors of AIG's business. The Allstate Corporation and CNA Financial Corporation have been excluded because AIG no longer believes these companies to be comparable to AIG in its overall business and operations. Dividend reinvestment has been assumed and returns have been weighted to reflect relative stock market capitalization.

FIVE-YEAR CUMULATIVE TOTAL SHAREHOLDER RETURNS
Value of $100 Invested on December 31, 2001



	2001	2002	2003	2004	2005	2006
AIG	$100.00	$73.07	$ 84.04	$ 83.61	$ 87.67	**$ 92.97**
S&P 500	100.00	77.90	100.25	111.15	116.61	**135.03**
New Peer Group	100.00	86.49	109.07	126.05	155.01	**179.36**
Old Peer Group	100.00	88.84	111.14	134.80	164.51	**196.58**

Item 6.
Selected Financial Data

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

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

Years Ended December 31, *(in millions, except per share data)*	**2006**	2005	2004	2003	2002
Revenues[(a)(b)(c)]:					
Premiums and other considerations	**$ 74,083**	$ 70,209	$ 66,625	$ 54,802	$ 44,289
Net investment income	**25,292**	22,165	18,465	15,508	13,593
Realized capital gains (losses)	**106**	341	44	(442)	(1,653)
Other income	**13,713**	16,190	12,532	9,553	9,942
Total revenues	**113,194**	108,905	97,666	79,421	66,171
Benefits and expenses:					
Incurred policy losses and benefits	**59,706**	63,558	58,212	46,034	40,005
Insurance acquisition and other operating expenses	**31,801**	30,134	24,609	21,480	18,358
Total benefits and expenses	**91,507**	93,692	82,821	67,514	58,363
Income before income taxes, minority interest and cumulative effect of accounting changes[(b)(c)(d)(e)]	**21,687**	15,213	14,845	11,907	7,808
Income taxes	**6,537**	4,258	4,407	3,556	1,919
Income before minority interest and cumulative effect of accounting changes	**15,150**	10,955	10,438	8,351	5,889
Minority interest	**(1,136)**	(478)	(455)	(252)	(160)
Income before cumulative effect of accounting changes	**14,014**	10,477	9,983	8,099	5,729
Cumulative effect of accounting changes, net of tax	**34**	—	(144)	9	—
Net income	**14,048**	10,477	9,839	8,108	5,729
Earnings per common share:					
Basic					
Income before cumulative effect of accounting changes	**5.38**	4.03	3.83	3.10	2.20
Cumulative effect of accounting changes, net of tax	**0.01**	—	(0.06)	—	—
Net income	**5.39**	4.03	3.77	3.10	2.20
Diluted					
Income before cumulative effect of accounting changes	**5.35**	3.99	3.79	3.07	2.17
Cumulative effect of accounting changes, net of tax	**0.01**	—	(0.06)	—	—
Net income	**5.36**	3.99	3.73	3.07	2.17
Dividends declared per common share	**0.65**	0.63	0.29	0.24	0.18
Total assets	**979,414**	853,051	801,007	675,602	561,131
Long-term debt and commercial paper[(f)]					
Guaranteed by AIG	**17,126**	10,425	8,498	7,469	7,144
Liabilities connected to trust preferred stock	**1,440**	1,391	1,489	1,682	—
Matched/not guaranteed by AIG	**130,113**	98,033	86,912	71,198	63,866
Total liabilities	**877,546**	766,548	721,135	606,180	500,696
Shareholders' equity	**$101,677**	$ 86,317	$ 79,673	$ 69,230	$ 58,303

(a) Represents the sum of General Insurance net premiums earned, Life Insurance & Retirement Services GAAP premiums and net investment income, Financial Services interest, lease and finance charges, Asset Management net investment income from spread-based products and advisory and management fees, and realized capital gains (losses).

(b) Includes the effect of hedging activities that did not qualify for hedge accounting treatment under FAS 133, including the related foreign exchange gains and losses. For 2006, 2005, 2004, 2003 and 2002, respectively, the effect was $(1.86) billion, $2.02 billion, $385 million, $(1.50) billion and $(216) million in revenues and $(1.86) billion, $2.02 billion, $671 million, $(1.22) billion and $(58) million in operating income. These amounts result primarily from interest rate and foreign currency derivatives that are economically hedging available for sale securities and borrowings.

(c) Includes the effect of out of period adjustments related to the accounting for certain interests in unit investment trusts. For 2006 the effect was an increase of $490 million in both revenues and operating income for General Insurance and an increase of $240 million and $169 million in revenues and operating income, respectively, for Life Insurance & Retirement Services.

(d) Includes current year catastrophe-related losses of $3.28 billion in 2005 and $1.16 billion in 2004. There were no significant catastrophe-related losses in 2006.

(e) Operating income was reduced by fourth quarter charges of $1.8 billion, $850 million and $2.1 billion for 2005, 2004 and 2002, respectively, related to the annual review of General Insurance loss and loss adjustment reserves. In 2006, 2005 and 2004, changes in estimates for asbestos and environmental reserves were $198 million, $873 million and $850 million, respectively.

(f) Including that portion of long-term debt maturing in less than one year. See also Note 9 of Notes to Consolidated Financial Statements.

Management's Discussion and Analysis of Financial Condition and Results of Operations

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

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

Management's Discussion and Analysis of Financial Condition and Results of Operations is designed to provide the reader a narrative explanation of AIG's operations, financial condition and liquidity and certain other significant matters.

Cautionary Statement Regarding Projections and Other Information About Future Events

This Annual Report on Form 10-K and other publicly available documents may include, and AIG's officers and representatives may from time to time make, projections concerning financial information and statements concerning future economic performance and events, plans and objectives relating to management, operations, products and services, and assumptions underlying these projections and statements. These projections and statements are not historical facts but instead represent only AIG's belief regarding future events, many of which, by their nature, are inherently uncertain and outside AIG's control. These projections and statements may address, among other things, the status and potential future outcome of the current regulatory and civil proceedings against AIG and their potential effect on AIG's businesses, financial position, results of operations, cash flows and liquidity, the effect of credit rating changes on AIG's businesses and competitive position, the unwinding and resolving of various relationships between AIG and SICO and AIG's strategy for growth, product development, market position, financial results and reserves. It is possible that AIG's actual results and financial condition may differ, possibly materially, from the anticipated results and financial condition indicated in these projections and statements. Factors that could cause AIG's actual results to differ, possibly materially, from those in the specific projections and statements are discussed throughout this Management's Discussion and Analysis of Financial Condition and Results of Operations and in Item 1A. Risk Factors of this Annual Report on Form 10-K. AIG is not under any obligation (and expressly disclaims any such obligations) to update or alter any projection or other statement, whether written or oral, that may be made from time to time, whether as a result of new information, future events or otherwise.

Overview of Operations and Business Results

AIG identifies its reportable segments by product or service line, consistent with its management structure. AIG's major product and service groupings are General Insurance, Life Insurance & Retirement Services, Financial Services and Asset Management. AIG's operations in 2006 were conducted by its subsidiaries through these segments. Through these segments, AIG provides insurance, financial and investment products and services to both businesses and individuals in more than 130 countries and jurisdictions. This geographic, product and service diversification is one of AIG's major strengths and sets it apart from its competitors. AIG's Other category consists of items not allocated to AIG's operating segments.

AIG's subsidiaries serve commercial, institutional and individual customers through an extensive property-casualty and life insurance and retirement services network. In the United States, AIG companies are the largest underwriters of commercial and industrial insurance and are among the largest life insurance and retirement services operations as well. AIG's Financial Services businesses include commercial aircraft and equipment leasing, capital markets operations and consumer finance, both in the United States and abroad. AIG also provides asset management services to institutions and individuals. As part of its spread-based business activities, AIG issues various debt instruments in the public and private markets.

AIG's operating performance reflects implementation of various long-term strategies and defined goals in its various operating segments. A primary goal of AIG in managing its General Insurance operations is to achieve an underwriting profit. To achieve this goal, AIG must be disciplined in its risk selection, and premiums must be adequate and terms and conditions appropriate to cover the risks accepted and expenses incurred. Expense efficiency is also a primary goal of AIG.

A central focus of AIG operations in recent years has been the development and expansion of distribution channels. In 2006, AIG continued to expand its distribution channels, which now include banks, credit card companies, television-media home shopping, affinity groups, direct response, worksite marketing and e-commerce.

AIG patiently builds relationships in markets around the world where it sees long-term growth opportunities. For example, the fact that AIG has the only wholly owned foreign life insurance operations in eleven cities in China is the result of relationships developed over nearly 30 years. AIG's more recent extensions of operations into India, Vietnam, Russia and other emerging markets reflect the same growth strategy. Moreover, AIG believes in investing in the economies and infrastructures of these countries and growing with them. When AIG companies enter a new jurisdiction, they typically offer both basic protection and savings products. As the economies evolve, AIG's products evolve with them, to more sophisticated and investment-oriented models.

Growth for AIG may be generated internally as well as through acquisitions which both fulfill strategic goals and offer adequate return on capital. During 2006, AIG acquired Travel Guard International, one of the nation's leading providers of travel insurance programs and emergency travel assistance, and acquired Central Insurance Co., Ltd., a leading general insurance company in Taiwan.

Outlook

The commercial property and casualty insurance industry has historically experienced cycles of price erosion followed by rate strengthening as a result of catastrophe or other significant losses that affect the overall capacity of the industry to provide coverage. Despite industry price erosion in commercial lines, AIG expects to continue to identify profitable opportunities and build attractive new general insurance businesses as a result of AIG's broad product line and extensive distribution networks in the U.S. and abroad. Workers compensation remains under considerable pricing pressure, as statutory rates continue to decline. Rates for D&O insurance also continue to decline due to competitive pressures. There can be no assurance that price erosion will not become more widespread or that AIG's profitability will not deteriorate from current levels in major commercial lines, as well as in personal lines and specialty coverages, such as mortgage guaranty, where the loss ratio has increased due to softening in the U.S. housing market and the weakening performance of non-traditional mortgage products. In Foreign General, opportunities for growth exist in the consumer lines due to increased demand in emerging markets and the trend toward privatization of health insurance. Growth in the Personal Lines marketplace remains challenged from flat renewal pricing, consumer price shopping and increased advertising spending by market leaders. However, the high net worth market continues to provide opportunities for growth as a result of AIG's innovative products and services specifically designed for that market. AIG expects that the acquisition of the remaining interest in 21st Century will enhance AIG's ability to grow the Personal Lines business while gaining efficiencies of scale.

Losses caused by catastrophes can fluctuate widely from year to year, making comparisons of results more difficult. With respect to catastrophe losses, AIG believes that it has taken appropriate steps, such as careful exposure selection and adequate reinsurance coverage, to reduce the effect of possible future losses. The occurrence of one or more catastrophic events of unanticipated frequency or severity, such as a terrorist attack, earthquake or hurricane, that causes insured losses, however, could have a material adverse effect on AIG's results of operations, liquidity or financial condition.

AIG's operations in China continue to expand, but AIG expects competition in China to remain strong and AIG's success in China will depend on its ability to execute its growth strategy.

In India, AIG expects to grow all segments, both organically and through acquisitions and joint ventures.

In Japan, AIG expects its Life Insurance & Retirement Services earnings growth may be challenged by increased competition in light of a new industry-wide mortality table, the continued runoff of the older, higher-margin in-force business of AIG Star Life and AIG Edison Life and lower consumer demand for certain accident and health products in light of tax law changes. The flat yield curve and declining Yen foreign exchange environment may continue to constrain certain fixed annuity production. To leverage

AIG's leadership position in the distribution of annuities through banks in Japan, ALICO launched new life products in this distribution channel. Although ALICO's direct marketing activities in Japan could experience a contraction while it re-positions its brand and products in a very competitive market, AIG expects that further deregulation will provide additional growth opportunities. In addition, AIG expects that the planned integration of AIG Star Life and AIG Edison Life will provide enhanced distribution opportunities and scale economies with an anticipated completion date of 2009.

AIG is a leader in direct marketing through sponsors and in the broad market in Japan and Korea, and AIG is investing in expanding distribution channels in India, Korea and Vietnam.

Through new operations in Bahrain designed to comply with Islamic law, AIG is tapping into a growing market. Islamic insurance, called Takaful, is an alternative to conventional insurance based on the concept of mutual assistance through pooling of resources.

Domestically, AIG plans to continue expansion of its Life Insurance & Retirement Services businesses through direct marketing and independent agent distribution channels. The aging population in the U.S. provides a growth opportunity for a variety of products, including longevity, guaranteed income and supplemental accident and health products. Certain other demographic groups that have traditionally been underserved provide additional growth opportunities. The home service operation, a slow growth business, has not met business objectives, although its cash flow has been steady. Domestic group life/health operations continue to face competitors with greater scale in group benefits. At the end of 2006, AIG exited the financial institutions credit life business in the U.S. as a result of competition from bank products and low profit margins. The individual fixed annuities business will continue to be challenged due to the interest rate environment and increased competition from bank products, while lower margin variable annuity products with living benefits will continue to be the product of consumer choice in the individual variable annuity markets. The group annuity market is undergoing a transition from group annuities to mutual fund products that have lower profit margins.

Globally, heightened regulatory scrutiny of financial services companies in many jurisdictions has the potential to affect future financial results through higher compliance costs. This is particularly true in Japan and Southeast Asia where financial institutions have received remediation orders affecting consumer and policyholder rights.

Within Financial Services, demand for ILFC's modern, fuel efficient aircraft remains strong, and ILFC plans to increase its fleet by purchasing 83 aircraft in 2007. However, ILFC's margins may be adversely affected by further increases in interest rates. AIGFP expects opportunities for growth across its product segments, but AIGFP is a transaction-oriented business, and its operating results will depend to a significant extent on actual transaction flow, which can be affected by market conditions and other variables outside its control. AIG continues to explore opportunities to expand its Consumer Finance operations into new foreign markets. Consumer Finance operations overseas were negatively affected in 2006 by industry-wide credit deterioration in the Taiwan credit card market, however, and operating results in the U.S. could be affected by the residential housing market, interest rates and unemployment.

The GIC portfolio, which is reported within the Asset Management segment, continues to run off and the MIP has replaced the GIC program as AIG's principal institutional spread-based investment activity. The MIP program is expected to continue to grow in 2007. Because the asset mix under the MIP does not include the alternative investments utilized in the GIC program, however, AIG does not expect that the income growth in the MIP will offset the runoff in the GIC portfolio for the foreseeable future.

For a description of important factors that may affect the operations and initiatives described above, see Item 1A. Risk Factors.

Consolidated Results

The following table summarizes AIG's consolidated revenues, income before income taxes, minority interest and cumulative effect of accounting changes and net income for the years ended December 31, 2006, 2005 and 2004:

Years Ended December 31, *(in millions)*	**2006**	2005	2004
Total revenues	**$113,194**	$108,905	$97,666
Income before income taxes, minority interest and cumulative effect of accounting changes	**21,687**	15,213	14,845
Net income	**$ 14,048**	$ 10,477	$ 9,839

2006 and 2005 Comparison

The 4 percent growth in revenues in 2006 was primarily attributable to the growth in net premiums earned and net investment income from General Insurance operations and growth in Life Insurance & Retirement Services GAAP premiums and net investment income. Revenues in the Financial Services segment declined as a result of the effect of hedging activities for AIGFP that did not qualify for hedge accounting treatment under FAS 133, decreasing revenues by $1.8 billion in 2006 and increasing revenues by $2.01 billion in 2005.

Income before income taxes, minority interest and cumulative effect of accounting changes increased 43 percent in 2006 compared to 2005, reflecting higher General Insurance and Life Insurance & Retirement Services operating income. These increases were partially offset by lower Financial Services operating income reflecting the effects of hedging activities that did not qualify for hedge accounting treatment under FAS 133. Results in

2005 reflected the negative effect of $3.28 billion (pre-tax) in catastrophe-related losses incurred that year. Net income in 2005 also reflected the charges related to regulatory settlements, as described in Item 3. Legal Proceedings, and the fourth quarter charge resulting from the annual review of General Insurance loss and loss adjustment reserves.

2005 and 2004 Comparison

Revenues grew 12 percent in 2005 compared to 2004 primarily due to the growth in net premiums earned from General Insurance operations as well as growth in both General Insurance and Life Insurance & Retirement Services net investment income and Life Insurance & Retirement Services GAAP premiums. Hedging activities for AIGFP that did not qualify for hedge accounting treatment under FAS 133 caused an increase in Financial Services revenues of $2.01 billion in 2005 and a decrease of $122 million in 2004.

AIG's income before income taxes, minority interest and cumulative effect of accounting changes increased 2 percent in 2005 compared to 2004. Life Insurance & Retirement Services, Financial Services and Asset Management operating income gains accounted for the increase over 2004 in both pretax income and net income. Offsetting these gains was the effect of the charges related to regulatory settlements.

Remediation and Other Items

Throughout 2006, as part of its continuing remediation efforts, AIG recorded out of period adjustments. The net effect of out of period adjustments relating to prior years increased 2006 net income by $65 million. The more significant adjustments included increases in unit investment trust income of $773 million ($428 million after tax) (more fully described below) and other expenses of $356 million ($231 million after tax), and a decrease in revenues for certain derivative transactions of $300 million ($145 million after tax).

During the fourth quarter, as part of its ongoing remediation efforts, AIG recorded out of period adjustments. These adjustments collectively increased net income in the fourth quarter by $56 million but were offset by fourth quarter charges to expense within Domestic Life for the adverse ruling in the Superior National arbitration of $125 million ($81 million after tax) and a charge of $66 million ($43 million after tax) in connection with the exit of the financial institutions credit life business. The more significant out of period adjustments included the following: a decrease in income tax expense of $181 million relating to AIG's ongoing remediation of internal controls over income tax accounting, an increase in other expenses of $167 million ($109 million after tax) relating to AIG's remediation of internal controls over reconciliation of certain balance sheet accounts, an increase in incurred policy losses and benefits of $103 million ($67 million after tax) in Domestic General Insurance for corrections of certain reserves for losses and loss expenses, a reduction in incurred policy benefits in the Foreign Life participating policyholder fund stemming from deferred tax adjustments in Foreign Life of $190 million ($124 million after tax), an increase in insurance operating expenses of $61 million ($40 million after tax) within Foreign Life for corrections of expense allocations to certain par fund accounts, and a $79 million ($51 million after tax) charge related to purchases of life insurance policies for AIG's life settlements portfolio that were issued by AIG subsidiaries.

During 2006, AIG identified and recorded out of period adjustments related to the accounting for certain interests in unit investment trusts in accordance with FIN 46(R), ''Consolidation of Variable Interest Entities'' and APB Opinion No. 18, ''The Equity Method of Accounting for Investments in Common Stock.'' These investments had previously been accounted for as available for sale securities, with changes in market values being reflected in other comprehensive income, net of deferred income taxes. Beginning with the second quarter of 2006, the changes in market values are included in net investment income. The adjustments decreased unrealized appreciation (depreciation) of investments — net of reclassification adjustments, and the related deferred income tax benefit (expense), in the Consolidated Statement of Comprehensive Income (Loss) by approximately $659 million and approximately $231 million, respectively, and increased net investment income by $844 million, increased Incurred policy losses and benefits (related to certain participating policyholder funds) by $71 million, increased Income taxes by $231 million and increased minority interest expense by $114 million in the Consolidated Statement of Income. There was no effect on Total shareholders' equity at December 31, 2006 or December 31, 2005.

Results for 2006 were negatively affected by a one-time charge relating to the Starr tender offer ($54 million before and after tax) and an additional allowance for losses in AIG Credit Card Company (Taiwan) ($94 million before and after tax).

The effective income tax rate increased from 28.0 percent for 2005 to 30.1 percent for 2006, reflecting changes in the sources of foreign taxable income, the effect of the phase out of synfuel tax credits, the effect of consolidating certain limited partnerships and a reduction in the proportion of total income derived from tax exempt income, which was partially offset by the aforementioned out of period income tax adjustments.

There were no significant catastrophe-related losses for the year ended December 31, 2006.

The following table summarizes the net effect of catastrophe-related losses for the years ended December 31, 2005 and 2004.

(in millions)	2005	2004
Pretax*	$3,280	$1,155
Net of tax and minority interest	2,109	729

* *Includes $312 million and $96 million in catastrophe-related losses from partially owned companies in 2005 and 2004, respectively.*

Segment Results

The following table summarizes the operations of each principal segment for the years ended December 31, 2006, 2005 and 2004. See also Note 2 of Notes to Consolidated Financial Statements.

(in millions)	**2006**	2005	2004
Revenues[(a)]:			
General Insurance[(b)(c)]	**$ 49,206**	$ 45,174	$41,961
Life Insurance & Retirement Services[(c)(d)]	**50,163**	47,376	43,402
Financial Services[(e)(f)]	**8,010**	10,525	7,495
Asset Management[(g)]	**5,814**	5,325	4,714
Other[(h)]	**1**	505	94
Total	**$113,194**	$108,905	$97,666
Operating Income[(a)(i)(j)]:			
General Insurance[(c)]	**$ 10,412**	$ 2,315	$ 3,177
Life Insurance & Retirement Services[(c)]	**10,032**	8,904	7,925
Financial Services[(f)]	**524**	4,276	2,180
Asset Management	**2,346**	2,253	2,125
Other[(h)(k)]	**(1,627)**	(2,535)	(562)
Total	**$ 21,687**	$ 15,213	$14,845

(a) Includes the effect of hedging activities that did not qualify for hedge accounting treatment under FAS 133, including the related foreign exchange gains and losses. For 2006, 2005 and 2004, respectively, the effect was $(1.86) billion, $2.02 billion and $385 million in revenues and $(1.86) billion, $2.02 billion and $671 million in operating income. These amounts result primarily from interest rate and foreign currency derivatives that are hedging available for sale securities and borrowings.

(b) Represents the sum of General Insurance net premiums earned, net investment income and realized capital gains (losses).

(c) Includes the effect of out of period adjustments related to the accounting for certain interests in unit investment trusts. For 2006, the effect was an increase of $490 million in both revenues and operating income for General Insurance and an increase of $240 million and $169 million in revenues and operating income, respectively, for Life Insurance & Retirement Services.

(d) Represents the sum of Life Insurance & Retirement Services GAAP premiums, net investment income and realized capital gains (losses). Included in realized capital gains (losses) and operating income is the effect of hedging activities that did not qualify for hedge accounting treatment under FAS 133 and the application of FAS 52, of $355 million, $(495) million and $(140) million for 2006, 2005 and 2004, respectively.

(e) Represents interest, lease and finance charges.

(f) Includes the effect of hedging activities that did not qualify for hedge accounting treatment under FAS 133, including the related foreign exchange gains and losses. For 2006, 2005 and 2004, respectively, the effect was $(1.82) billion, $2.01 billion, and $(122) million in both revenues and operating income for Capital Markets. These amounts result primarily from interest rate and foreign currency derivatives that are economically hedging available for sale securities and borrowings. For 2004, the effect was $(27) million in operating income for Aircraft Leasing. During 2006 and 2005, Aircraft Leasing derivative gains and losses were reported as part of AIG's Other category, and were not reported in Aircraft Leasing operating income.

(g) Represents net investment income with respect to spread-based products and management and advisory fees.

(h) Includes consolidation and elimination adjustments which increased revenues and operating income by $296 million and $74 million, respectively, in 2006.

(i) Represents income before income taxes, minority interest, and cumulative effect of accounting changes.

(j) Includes current year catastrophe-related losses of $3.28 billion and $1.16 billion in 2005 and 2004, respectively. There were no significant catastrophe-related losses in 2006. Includes additional losses incurred and net reinstatement premiums related to prior year catastrophes of $165 million and $292 million in 2006 and 2005, respectively.

(k) Includes current year catastrophe-related losses from unconsolidated subsidiaries of $312 million and $96 million in 2005 and 2004. There were no significant catastrophe-related losses in 2006.

General Insurance

AIG's General Insurance operations provide property and casualty products and services throughout the world. The increase in General Insurance operating income in 2006 compared to 2005 was primarily attributable to an improvement in underwriting results for DBG, including the absence of catastrophe-related losses, which amounted to $2.89 billion in 2005. Operating income for 2006 also reflected higher net investment income, including the effect of the out of period adjustments related to the accounting for certain interests in unit investment trusts.

Life Insurance & Retirement Services

AIG's Life Insurance & Retirement Services operations provide insurance, financial and investment products throughout the world. Foreign operations contributed approximately 68 percent, 59 percent and 61 percent of AIG's Life Insurance & Retirement Services operating income in 2006, 2005 and 2004, respectively.

Life Insurance & Retirement Services operating income increased 13 percent in 2006 compared to 2005 on higher GAAP premiums and an increase in net investment income. Net investment income in 2006 included the effect of an out of period adjustment related to the accounting for certain interests in unit investment trusts. Realized capital gains included in revenues and operating income were $88 million in 2006 compared to realized capital losses of $158 million in 2005. Results for 2006 were particularly strong in the Foreign Life operations that were helped by increased net investment income, higher realized gains and lower acquisition costs. Domestic Life Insurance & Retirement Services operating income declined from the prior year on lower realized gains, the charge discussed above relating to the Superior National arbitration and the exiting of the financial institutions credit insurance business.

Financial Services

AIG's Financial Services subsidiaries engage in diversified activities including aircraft and equipment leasing, capital markets, consumer finance and insurance premium finance.

Financial Services operating income decreased in 2006 compared to 2005 primarily due to the effects of hedging activities that did not qualify for hedge accounting treatment under FAS 133. AIG is reinstituting hedge accounting in the first quarter of 2007 for AIGFP. In addition to the effects of FAS 133, fluctuations in revenues and operating income from period to

period are not unusual because of the transaction-oriented nature of Capital Markets operations.

Asset Management

AIG's Asset Management operations include institutional and retail asset management, broker-dealer services and institutional spread-based investment businesses. The MIP has replaced the GIC program as AIG's principal spread-based investment activity.

Asset Management operating income increased 4 percent in 2006 compared to 2005 due primarily to growth in asset management fees within Institutional Asset Management and income from the MIP. These increases were partially offset by the continued runoff of GIC balances, spread compression in the remaining GIC portfolio as well as decreased performance-based fees. Gains and losses arising from the consolidation of certain variable interest entities (VIEs) and partnerships are included in operating income, but are offset in minority interest expense, which is not a component of operating income.

Capital Resources

At December 31, 2006, AIG had total consolidated shareholders' equity of $101.68 billion and total consolidated borrowings of $148.68 billion. At that date, $131.55 billion of such borrowings were not guaranteed by AIG, were matched borrowings by AIG or AIGFP, or represented liabilities connected to trust preferred stock.

AIG did not purchase shares of its common stock under its common stock repurchase authorization during 2006. In February 2007, AIG's Board of Directors increased the repurchase program by authorizing the repurchase of shares with an aggregate purchase price of $8 billion.

In 2007, AIG expects to issue capital securities in one or more series. The proceeds will be used to repurchase shares of common stock or to otherwise improve the efficiency of AIG's capital structure.

Liquidity

AIG manages liquidity at both the subsidiary and parent company levels. At December 31, 2006, AIG's consolidated invested assets, primarily held by its subsidiaries, included $26.8 billion in cash and short-term investments. Consolidated net cash provided from operating activities in 2006 amounted to $6.8 billion. At the parent company level, liquidity management activities are conducted in a manner to preserve and enhance funding stability, flexibility, and diversity through the full range of potential operating environments and market conditions. AIG's primary sources of cash flow are dividends and other payments from its regulated and unregulated subsidiaries, as well as issuances of debt securities. Primary uses of cash flow are for debt service, subsidiary funding and shareholder dividend payments. Management believes that AIG's liquid assets, cash provided by operations and access to the capital markets will enable it to meet its anticipated cash requirements, including the funding of increased dividends under AIG's new dividend policy and repurchases of common stock.

Critical Accounting Estimates

AIG considers its most critical accounting estimates to be those relating to reserves for losses and loss expenses, future policy benefits for life and accident and health contracts, recoverability of DAC, estimated gross profits for investment-oriented products, fair value determinations for certain Capital Markets assets and liabilities, other-than-temporary declines in the value of investments and flight equipment recoverability. These accounting estimates require the use of assumptions about matters, some of which are highly uncertain at the time of estimation. To the extent actual experience differs from the assumptions used, AIG's results of operations would be directly affected.

Throughout this Management's Discussion and Analysis of Financial Condition and Results of Operations, AIG's critical accounting estimates are discussed in detail. The major categories for which assumptions are developed and used to establish each critical accounting estimate are highlighted below. For a discussion regarding the significant accounting policies relating to these estimates, see Note 1 of Notes to Consolidated Financial Statements.

Reserves for Losses and Loss Expenses (General Insurance):

- *Loss trend factors:* used to establish expected loss ratios for subsequent accident years based on premium rate adequacy and the projected loss ratio with respect to prior accident years.
- *Expected loss ratios for the latest accident year:* in this case, accident year 2006 for the year end 2006 loss reserve analysis. For low-frequency, high-severity classes such as excess casualty, expected loss ratios generally are utilized for at least the three most recent accident years.
- *Loss development factors:* used to project the reported losses for each accident year to an ultimate amount.
- *Reinsurance recoverable on unpaid losses:* the expected recoveries from reinsurers on losses that have not yet been reported and/or settled.

Future Policy Benefits for Life and Accident and Health Contracts (Life Insurance & Retirement Services):

- *Interest rates:* which vary by geographical region, year of issuance and products.
- *Mortality, morbidity and surrender rates:* based upon actual experience by geographical region modified to allow for variation in policy form, risk classification and distribution channel.

Estimated Gross Profits (Life Insurance & Retirement Services):

- *Estimated gross profits:* to be realized over the estimated duration of the contracts (investment-oriented products) affect the carrying value of DAC, unearned revenue liability and associated amortization patterns under FAS 97 and Sales Inducement Assets under SOP 03-1. Estimated gross profits include investment income and gains and losses on investments less required interest, actual mortality and other expenses.

Deferred Policy Acquisition Costs (Life Insurance & Retirement Services):

- *Recoverability:* based on current and future expected profitability, which is affected by interest rates, foreign exchange rates, mortality experience, and policy persistency.

Deferred Policy Acquisition Costs (General Insurance):

- *Recoverability and eligibility:* based upon the current terms and profitability of the underlying insurance contracts.

Fair Value Determinations Of Certain Assets And Liabilities (Financial Services):

- *Valuation models:* utilizing factors, such as market liquidity and current interest, foreign exchange and volatility rates.
- *Market price data:* AIG attempts to secure reliable and independent current market price data, such as published exchange rates from external subscription services such as Bloomberg or Reuters or third-party broker quotes for use in its models. When such data is not available, AIG uses an internal methodology, which includes interpolation and extrapolation from verifiable prices from trades occurring on dates nearest to the dates of the transactions.

Other-Than-Temporary Declines In The Value Of Investments:

A security is considered a candidate for other-than-temporary impairment if it meets any of the following criteria:

- Trading at a significant (25 percent or more) discount to par or amortized cost (if lower) for an extended period of time (nine months or longer);
- The occurrence of a discrete credit event resulting in the debtor defaulting or seeking bankruptcy or insolvency protection or voluntary reorganization; or
- The probability of non-realization of a full recovery on its investment, irrespective of the occurrence of one of the foregoing events.

At each balance sheet date, AIG evaluates its securities holdings in an unrealized loss position. Where AIG does not intend to hold such securities until they have fully recovered their carrying value, based on the circumstances present at the date of evaluation, AIG records the unrealized loss in income. If events or circumstances change, such as unexpected changes in the creditworthiness of the obligor, unanticipated changes in interest rates, tax laws, statutory capital positions and unforeseen liquidity events, among others, AIG revisits its intent. Further, if a loss is recognized from a sale subsequent to a balance sheet date pursuant to these unexpected changes in circumstances, the loss is recognized in the period in which the intent to hold the securities to recovery no longer existed.

In periods subsequent to the recognition of an other-than-temporary impairment loss for debt securities, AIG amortizes the discount or reduced premium over the remaining life of the security in a prospective manner based on the amount and timing of estimated future cash flows.

Flight Equipment — Recoverability (Financial Services):

- *Expected undiscounted future net cash flows:* based upon current lease rates, projected future lease rates and estimated terminal values of each aircraft based on third party information.

Operating Review

General Insurance Operations

AIG's General Insurance subsidiaries are multiple line companies writing substantially all lines of commercial property and casualty insurance and various personal lines both domestically and abroad.

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

A critical discipline of a successful general insurance business is the objective to produce profit from underwriting activities exclusive of investment-related income. When underwriting is not profitable, premiums are inadequate to pay for insured losses and underwriting related expenses. In these situations, the addition of general insurance related investment income and realized capital gains may, however, enable a general insurance business to produce operating income. For these reasons, AIG views underwriting results to be critical in the overall evaluation of performance. See also Liquidity herein.

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

GAAP provides for the recognition of expenses at the same time revenues are earned, the accounting principle of matching. Therefore, acquisition expenses are deferred and amortized over the period the related net premiums written are earned. DAC is reviewed for recoverability, and such review requires management judgment. The most comparable GAAP measure to statutory underwriting profit is income before income taxes, minority interest and cumulative effect of an accounting change. A table reconciling statutory underwriting profit to income before income taxes, minority interest and cumulative effect of an accounting change is contained in footnote (g) to the following table. See also Critical Accounting Estimates herein and Notes 1 and 4 of Notes to Consolidated Financial Statements.

AIG, along with most general insurance companies, uses the loss ratio, the expense ratio and the combined ratio as measures of underwriting performance. The loss ratio is the sum of losses and loss expenses incurred divided by net premiums earned. The expense ratio is statutory underwriting expenses divided by net premiums written. These ratios are relative measurements that describe, for every $100 of net premiums earned or written, the

cost of losses and statutory expenses, respectively. The combined ratio is the sum of the loss ratio and the expense ratio. The combined ratio presents the total cost per $100 of premium production. A combined ratio below 100 demonstrates underwriting profit; a combined ratio above 100 demonstrates underwriting loss.

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

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

General Insurance Results

General Insurance operating income is comprised of statutory underwriting results, changes in DAC, net investment income and realized capital gains and losses. Operating income, as well as net premiums written, net premiums earned, net investment income and realized capital gains (losses) and statutory ratios for 2006, 2005 and 2004 were as follows:

(in millions, except ratios)	**2006**	2005	2004
Net premiums written:			
Domestic General			
DBG	**$24,345**	$23,128	$22,506
Transatlantic	**3,633**	3,466	3,749
Personal Lines	**4,654**	4,653	4,354
Mortgage Guaranty	**866**	628	607
Foreign General[(a)]	**11,368**	9,997	9,407
Total	**$44,866**	$41,872	$40,623
Net premiums earned:			
Domestic General			
DBG	**$23,936**	$22,602	$21,215
Transatlantic	**3,604**	3,385	3,661
Personal Lines	**4,645**	4,634	4,291
Mortgage Guaranty	**740**	533	539
Foreign General[(a)]	**10,526**	9,655	8,831
Total	**$43,451**	$40,809	$38,537
Net investment income[(b)]:			
Domestic General			
DBG	**$ 3,411**	$ 2,403	$ 1,965
Transatlantic	**435**	343	307
Personal Lines	**225**	217	186
Mortgage Guaranty	**140**	123	120
Intercompany adjustments and eliminations — net	**1**	1	—
Foreign General	**1,484**	944	618
Total	**$ 5,696**	$ 4,031	$ 3,196
Realized capital gains (losses)	**$ 59**	$ 334	$ 228
Operating income (loss)[(b)(c)(d)]:			
Domestic General			
DBG	**$ 5,985**	$ (646)	$ 777
Transatlantic	**589**	(39)	282
Personal Lines	**432**	195	357
Mortgage Guaranty	**328**	363	399
Foreign General[(e)]	**3,088**	2,427	1,344
Reclassifications and eliminations	**(10)**	15	18
Total	**$10,412**	$ 2,315	$ 3,177
Statutory underwriting profit (loss)[(c)(d)(g)]:			
Domestic General			
DBG	**$ 2,450**	$ (3,227)	$ (1,500)
Transatlantic	**129**	(434)	(77)
Personal Lines	**204**	(38)	136
Mortgage Guaranty	**188**	249	234
Foreign General[(e)]	**1,437**	1,285	643
Total	**$ 4,408**	$ (2,165)	$ (564)

(continued)

(in millions, except ratios)	**2006**	2005	2004
Domestic General[(c)(d)]:			
Loss ratio	**69.1**	89.6	83.9
Expense ratio	**21.5**	21.0	19.2
Combined ratio	**90.6**	110.6	103.1
Foreign General[(c)(d)]:			
Loss ratio[(a)]	**50.5**	53.7	61.6
Expense ratio[(e)(f)]	**33.2**	31.9	29.2
Combined ratio	**83.7**	85.6	90.8
Consolidated[(c)(d)]:			
Loss ratio	**64.6**	81.1	78.8
Expense ratio	**24.5**	23.6	21.5
Combined ratio	**89.1**	104.7	100.3

(a) Income statement accounts expressed in non-functional currencies are translated into U.S. dollars using average exchange rates.

(b) Includes the effect of out of period adjustments related to the accounting for certain interests in unit investment trusts in 2006. For DBG, the effect was an increase of $66 million, and for Foreign General, the effect was an increase of $424 million.

(c) Catastrophe-related losses increased the consolidated General Insurance combined ratio for 2005 and 2004 by 7.06 points and 2.74 points, respectively. There were no significant catastrophe-related losses in 2006. Catastrophe-related losses for 2005 and 2004 by reporting unit were as follows:

	2005		2004	
(in millions)	Insurance Related Losses	Net Reinstatement Premium Cost	Insurance Related Losses	Net Reinstatement Premium Cost
Reporting Unit:				
DBG	$1,747	$122	$ 582	$ —
Transatlantic	463	45	215	—
Personal Lines	112	2	25	—
Mortgage Guaranty	10	—	—	—
Foreign General	293	94	232	—
Total	$2,625	$263	$1,054	$ —

(d) Includes additional losses incurred and net reinstatement premiums related to prior year catastrophes of $199 million and $277 million, in 2006 and 2005, respectively.

(e) Includes the results of wholly owned Foreign General agencies.

(f) Includes amortization of advertising costs.

(g) Statutory underwriting profit (loss) is a measure that U.S. domiciled insurance companies are required to report to their regulatory authorities. The following table reconciles statutory underwriting profit (loss) to operating income for General Insurance for the years ended December 31, 2006, 2005 and 2004:

(in millions)	Domestic Brokerage Group	Transatlantic	Personal Lines	Mortgage Guaranty	Foreign General	Reclassifications and Eliminations	Total
2006:							
Statutory underwriting profit (loss)	**$ 2,450**	**$ 129**	**$204**	**$188**	**$1,437**	**$ —**	**$ 4,408**
Increase (decrease) in DAC	**26**	**14**	**2**	**3**	**204**	**—**	**249**
Net investment income	**3,411**	**435**	**225**	**140**	**1,484**	**1**	**5,696**
Realized capital gains (losses)	**98**	**11**	**1**	**(3)**	**(37)**	**(11)**	**59**
Operating income (loss)	**$ 5,985**	**$ 589**	**$432**	**$328**	**$3,088**	**$(10)**	**$10,412**
2005:							
Statutory underwriting profit (loss)	$(3,227)	$(434)	$ (38)	$249	$1,285	$ —	$ (2,165)
Increase (decrease) in DAC	(23)	14	19	(8)	113	—	115
Net investment income	2,403	343	217	123	944	1	4,031
Realized capital gains (losses)	201	38	(3)	(1)	85	14	334
Operating income (loss)	$ (646)	$ (39)	$195	$363	$2,427	$ 15	$ 2,315
2004:							
Statutory underwriting profit (loss)	$(1,500)	$ (77)	$136	$234	$ 643	$ —	$ (564)
Increase (decrease) in DAC	160	30	24	44	59	—	317
Net investment income	1,965	307	186	120	618	—	3,196
Realized capital gains (losses)	152	22	11	1	24	18	228
Operating income (loss)	$ 777	$ 282	$357	$399	$1,344	$ 18	$ 3,177

AIG transacts business in most major foreign currencies. The following table summarizes the effect of changes in foreign currency exchange rates on the growth of General Insurance net premiums written for the years ended December 31, 2006 and 2005.

	2006	2005
Growth in original currency*	**7.4%**	2.6%
Foreign exchange effect	**(0.2)**	0.5
Growth as reported in U.S. dollars	**7.2%**	3.1%

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

2006 and 2005 Comparison

General Insurance operating income increased in 2006 compared to 2005 due to growth in net premiums, a reduction in both catastrophe losses and prior accident year development, and growth in net investment income. The combined ratio improved to 89.1, a reduction of 15.6 points from 2005, including an improvement in the loss ratio of 16.5 points. The reduction in catastrophe losses represented 6.9 points and the reduction in prior year adverse development represented 11.5 points of the overall reduction. Net premiums written increased $3.0 billion or 7 percent in 2006 compared to 2005. Domestic General accounted for $1.6 billion of the increase as property rates improved and submission activity increased due to the strength of AIG's capacity, commitment to difficult markets and diverse product offerings. Foreign General contributed $1.4 billion to the increase in net premiums written. In 2005, Domestic General net premiums written increased by $300 million and Foreign General net premiums written decreased by the same amount as a result of the commutation of the Richmond reinsurance contract. The commutation partially offset the increase in Domestic General net premiums written in 2006 compared to 2005 and increased Foreign General net premiums written in 2006 compared to 2005.

In 2006, certain adjustments were made in conjunction with the remediation of the material weakness relating to balance sheet account reconciliations which increased earned premiums by $189 million and increased other expenses by $415 million. These adjustments reflect continuing progress in AIG's ongoing remediation efforts. The combined effect of these adjustments increased the expense ratio by 0.9 points and decreased the loss ratio by 0.3 points.

General Insurance net investment income increased $1.67 billion in 2006 to $5.7 billion on higher levels of invested assets, strong cash flows, slightly higher yields and increased partnership income, and included increases from out of period adjustments of $490 million related to the accounting for certain interests in unit investment trusts, $43 million related to partnership income and $85 million related to interest earned on a DBG deposit contract. See also Capital Resources and Liquidity — Liquidity and Invested Assets herein.

2005 and 2004 Comparison

General Insurance operating income in 2005 decreased from 2004 due to higher catastrophe-related losses and the fourth quarter 2005 increase in reserves and changes in estimates related to remediation of the material weakness in reconciliation of balance sheet accounts. Catastrophe-related losses were $2.89 billion and $1.05 billion in 2005 and 2004, respectively. These decreases in operating income were partially offset by strong growth in statutory underwriting profit and increases in net investment income. General Insurance operating income in 2004 also included a $232 million charge reflecting a change in estimate for salvage and subrogation recoveries.

General Insurance net investment income grew in 2005 compared to 2004 due to strong cash flows, higher interest rates and increased partnership income. See also Capital Resources and Liquidity — Liquidity herein and Note 8 of Notes to Consolidated Financial Statements.

DBG Results

2006 and 2005 Comparison

DBG's operating income increased to $5.99 billion in 2006 compared to a loss of $646 million in 2005, an improvement of $6.63 billion. The improvement is also reflected in the combined ratio, which declined to 89.4 in 2006 compared to 113.8 in 2005 primarily due to an improvement in the loss ratio of 24.9 points. The reduction in prior year adverse development and the reduction in catastrophe losses and related reinstatement premiums accounted for 21.0 points and 8.2 points, respectively, of the improvement.

DBG's net premiums written increased 5 percent in 2006 compared to 2005 as property rates improved and submission activity increased due to the strength of AIG's capacity, commitment to difficult markets and diverse product offerings. Net premiums written in 2005 were reduced by $122 million due to reinstatement premiums related to catastrophes, offset by increases of $300 million for the Richmond commutation and $147 million related to an accrual for workers compensation premiums for payroll not yet reported by insured employers. The combined effect of these items reduced the growth rate for net premiums written by 1.5 percent.

The loss ratio for 2006 declined 24.9 points to 69.4. The 2005 loss ratio was negatively affected by catastrophe-related losses of $1.7 billion and related reinstatement premiums of $122 million. Adverse development on reserves for loss and loss adjustment expenses declined to $110 million in 2006 compared to $4.9 billion in 2005, accounting for 21.0 points of the decrease in the loss ratio.

DBG's expense ratio increased to 20.0 in 2006 compared to 19.5 in 2005, primarily due to an increase in other expenses that amounted to $498 million in 2006 (including out of period charges of $356 million) compared to $372 million in 2005. This increase added 0.4 points to the expense ratio. Overall allowances decreased, however, due to charge-offs against previously established allowances resulting from AIG's remediation activities.

DBG's net investment income increased by $1.0 billion in 2006 compared to 2005, as interest income increased $482 million on growth in the bond portfolio resulting from investment of operating cash flows and capital contributions. Partnership income

increased from 2005 due to improved performance of the underlying investments, including initial public offering activity. Net investment income in 2006 included increases relating to out of period adjustments of $109 million for the accounting for certain investments in unit investment trusts and partnerships and $85 million related to interest earned on a deposit contract that did not exist in the prior year.

2005 and 2004 Comparison

DBG's net premiums written increased modestly in 2005 compared to 2004, reflecting generally improving renewal retention rates and a modest change in the mix of business towards smaller accounts for which DBG purchases less reinsurance. DBG also continued to expand its relationships with a larger number and broader range of brokers. DBG saw improvement in domestic property rates as well as increases in submission activity in the aftermath of the 2005 hurricanes. DBG attributes the increase in submissions to its overall financial strength in comparison to many insurers that experienced significant losses and reductions of surplus as a result of the hurricanes.

The DBG loss ratio increased in 2005 from 2004 principally as a result of adverse loss development, higher catastrophe-related losses and $197 million of losses incurred in 2005 resulting from the 2004 catastrophes.

The DBG expense ratio increased in 2005 from 2004, principally due to an increase in net commissions resulting from the replacement of certain ceded quota share reinsurance, for which DBG earns a ceding commission, with excess-of-loss reinsurance, which generally does not include a ceding commission. Increases in other underwriting expenses reflect a change in estimates for salvage and subrogation recoveries.

DBG's net investment income increased in 2005 compared to 2004 due to strong cash flows, higher interest rates and increased partnership income.

Transatlantic Results

2006 and 2005 Comparison

Transatlantic's net premiums written and net premiums earned increased in 2006 by 5 percent and 6 percent, respectively, compared to 2005 due primarily to increased writings in domestic operations. Operating income increased in 2006 compared to 2005 due largely to lower catastrophe losses and net ceded reinstatement premiums, and increased net investment income.

2005 and 2004 Comparison

Transatlantic's net premiums written and net premiums earned for 2005 decreased compared to 2004, principally due to competitive market conditions and increased ceding company retentions in certain classes of business, largely resulting from Transatlantic's domestic operations. Operating income decreased principally as a result of the increased level of catastrophe losses.

Personal Lines Results

2006 and 2005 Comparison

Personal Lines operating income increased $237 million in 2006 compared to 2005 reflecting a reduction in the loss ratio of 5.8 points. Favorable development on prior accident years reduced incurred losses by $111 million in 2006 compared to an increase of $14 million in 2005, accounting for 2.7 points of the decrease in the loss ratio. The 2005 catastrophe-related losses of $112 million added 2.4 points to the loss ratio. The loss ratio for the 2006 accident year improved 0.7 points primarily due to the termination of The Robert Plan relationship effective December 31, 2005 and growth in the Private Client Group. The improvement in the loss ratio was partially offset by an increase in the expense ratio of 0.6 points primarily due to investments in people and technology, national expansion efforts and lower response rates. Net premiums written were flat in 2006 compared to 2005, with growth in the Private Client Group and Agency Auto divisions offset by termination of The Robert Plan relationship. Growth in the Private Client Group spans multiple products, with a continued penetration of the high net worth market, strong brand promotion and innovative loss prevention programs.

2005 and 2004 Comparison

Personal Lines net premiums written and net premiums earned for 2005 increased compared to 2004 as a result of strong growth in the Private Client Group and Agency Auto divisions due to increased agent/broker appointments, greater market penetration and enhanced product offerings. AIG direct premiums in 2005 were down slightly from 2004 due to aggressive re-underwriting of the previously acquired GE business and the discontinuation of underwriting homeowners business. Involuntary auto premiums were down in 2005 due to the decline in the assigned risk marketplace. Statutory underwriting profit declined in 2005 as a result of hurricane losses and related expenses, reserve strengthening, an increase in Agency Auto's current accident year physical damage loss ratio, and expenses incurred related to terminating AIG's relationship with The Robert Plan effective December 31, 2005.

Mortgage Guaranty Results

2006 and 2005 Comparison

UGC's operating income declined $35 million in 2006, down 10 percent from 2005 due primarily to unfavorable loss experience on third-party originated second lien business with a credit quality lower than typical for UGC and a softening U.S. housing market. This increased UGC's consolidated loss ratio for 2006 to 47.2 compared to 26.0 in 2005. The writing of this second lien coverage, which began in 2005, was discontinued as of year end 2006. Losses in the second lien business have been mitigated by a policy year aggregate limitation provision that is typically established for each lender.

Net premiums written increased 38 percent from growth in the domestic second lien and international businesses as well as improved persistency in the domestic first lien business. The

expense ratio remained flat as premium growth covered increased expenses related to expansion internationally and continued investment in risk management resources. UGC had approximately $27 billion of guaranty risk in force at December 31, 2006.

2005 and 2004 Comparison

UGC's net premiums written were up slightly for 2005 compared to 2004 as strong growth in the international and domestic second lien businesses was mostly offset by lower persistency in domestic first lien residential renewal premiums. Statutory underwriting profit rose from 2004 due to lower contract underwriting expenses and favorable loss development.

Foreign General Insurance Results

2006 and 2005 Comparison

Foreign General's operating income increased $661 million or 27 percent in 2006 compared to 2005 due to out of period adjustments related to the accounting for interests in unit investment trusts, the absence of significant catastrophe-related losses in 2006, rate increases and lower current accident year losses by the Lloyd's syndicate Ascot (Ascot) on its U.S. book of business and lower asbestos and environmental reserve increases. Partially offsetting these increases in operating income were lower favorable loss development from prior accident years and adverse loss development on the 2005 hurricanes. Statutory underwriting profit increased $152 million in 2006 compared to 2005. Catastrophes in 2005 resulted in losses of $293 million and reinstatement premiums of $94 million.

Net premiums written increased $1.4 billion or 14 percent (15 percent in original currency) in 2006 compared to 2005, reflecting growth in both commercial and consumer lines driven by new business from both established and new distribution channels, including a wholly owned insurance company in Vietnam and Central Insurance Co., Ltd. in Taiwan. Ascot also contributed to the growth in net premiums written as a result of rate increases on its U.S. business. Consumer lines in Latin America and commercial lines in Europe, including the U.K., also contributed to the increase. Net premiums written for 2005 were reduced by reinstatement premiums related to catastrophes and a portfolio transfer of unearned premium reserves to DBG related to the Richmond commutation, accounting for 3 percent of the increase in 2006 compared to 2005.

The 2006 combined ratio declined to 83.7, a decrease of 1.9 points from 2005. The 2005 catastrophes added 3.5 points to the 2005 loss ratio. The expense ratio in 2006 increased by 1.3 points as a result of increased amortization of deferred advertising costs and a continued change in the business mix towards products with higher acquisition costs but historically lower loss ratios. The loss ratio decreased 3.2 points in 2006 as the absence of significant catastrophes in 2006 resulted in a decrease of 3.5 points, rate increases and lower current year losses by Ascot on its U.S. book of business accounted for 1.3 points of the decrease and lower asbestos and environmental reserve increases accounted for 1.2 points of the decrease. These declines were partially offset by lower favorable loss development from prior accident years and adverse development on 2005 hurricanes.

The expense ratio increased 1.3 points in 2006 compared to 2005. Underwriting expenses for 2006 increased $59 million due to an out of period adjustment for amortization of deferred advertising costs and premiums were reduced by $61 million due to reconciliation remediation activities, in aggregate accounting for 0.7 points of the increase in the expense ratio. The expense ratio also increased due to growth in consumer business lines, which have higher acquisition expenses but historically lower loss ratios. The expense ratio for 2005 increased by 1.2 points due to the decline in net premiums written from reinstatement premiums related to catastrophes and the portfolio transfer of the Richmond unearned premium reserves. Due to the current mix of business, AIG expects the expense ratio to continue to increase during 2007, principally for classes of business with historically lower than average loss ratios.

Net investment income increased $540 million or 57 percent in 2006 compared to 2005 primarily due to a $424 million out of period adjustment related to the accounting for interests in unit investment trusts.

2005 and 2004 Comparison

Foreign General operating income increased 81 percent in 2005 compared to 2004 due primarily to favorable loss development from prior accident years and increased net investment income.

Net premiums written increased 6 percent (4 percent in original currency) in 2005 compared to 2004 as a result of new business as well as new distribution channels such as the February 2005 purchase of the insurance portfolio of the Royal & Sun Alliance branch operations in Japan. The personal accident business in the Far East and the personal lines operations in Latin America also contributed to the growth. Partially offsetting these increases was the portfolio transfer of Richmond's unearned premium reserves to DBG, which reduced net premiums in 2005 and reinstatement premiums related to catastrophes.

The 2005 combined ratio of 85.6 decreased 5.3 points from 2004. The loss ratio decreased 8.0 points in 2005 from 2004. The loss ratio decreased 4.7 points due to favorable loss development from prior accident years, excluding catastrophes, and 2.3 points related to a 2004 loss reserve restatement adjustment. The loss ratio increased 0.9 points due to higher catastrophe losses in 2005 related to hurricanes. The expense ratio increased 2.7 points in 2005 from 2004 principally due to the portfolio transfer of Richmond's unearned premium reserves to DBG in 2005, loyalty business initiatives in the consumer business lines, which have higher acquisition costs, and also due to reinstatement premiums.

Foreign General net investment income increased $326 million in 2005 compared to 2004 on increased partnership income, reflecting increases in market valuations of infrastructure fund investments in Africa, Asia, China, Eastern Europe and India. Additionally, net investment income was positively affected by positive cash flows, higher interest rates and the compounding of previously earned and reinvested net investment income. Cash flow was lower in 2005 compared to 2004 due to payments for

catastrophe-related losses incurred in 2005 and 2004 and for the purchase of the Royal & Sun Alliance branch operations.

Reserve for Losses and Loss Expenses

The following table presents the components of the General Insurance gross reserve for losses and loss expenses (loss reserves) as of December 31, 2006 and 2005 by major lines of business on a statutory Annual Statement basis*:

(in millions)	**2006**	2005
Other liability occurrence	**$19,156**	$18,116
Workers compensation	**13,465**	11,630
Other liability claims made	**12,394**	12,447
Property	**6,663**	7,217
Auto liability	**5,931**	6,569
International	**5,810**	4,939
Reinsurance	**2,960**	2,886
Medical malpractice	**2,308**	2,363
Products liability	**2,168**	1,937
Accident and health	**1,649**	1,678
Commercial multiple peril	**1,621**	1,359
Aircraft	**1,562**	1,844
Fidelity/surety	**1,127**	1,072
Other	**3,185**	3,112
Total	**$79,999**	$77,169

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

AIG's gross reserve for losses and loss expenses represents the accumulation of estimates of ultimate losses, including IBNR and loss expenses. The methods used to determine loss reserve estimates and to establish the resulting reserves are continually reviewed and updated by management. Any adjustments resulting therefrom are reflected in operating income currently. Because loss reserve estimates are subject to the outcome of future events, changes in estimates are unavoidable given that loss trends vary and time is often required for changes in trends to be recognized and confirmed. Reserve changes that increase previous estimates of ultimate cost are referred to as unfavorable or adverse development or reserve strengthening. Reserve changes that decrease previous estimates of ultimate cost are referred to as favorable development.

At December 31, 2006, General Insurance net loss reserves increased $5.15 billion from 2005 to $62.63 billion. The net loss reserves represent loss reserves reduced by reinsurance recoverables, net of an allowance for unrecoverable reinsurance and applicable discount for future investment income.

The following table classifies the components of the General Insurance net loss reserves by business unit as of December 31, 2006 and 2005.

(in millions)	**2006**	2005
DBG[(a)]	**$43,998**	$40,782
Transatlantic	**6,207**	5,690
Personal Lines[(b)]	**2,440**	2,578
Mortgage Guaranty	**460**	340
Foreign General[(c)]	**9,525**	8,086
Total Net Loss Reserve	**$62,630**	$57,476

(a) At December 31, 2006 and 2005, respectively, DBG loss reserves include approximately $3.33 billion and $3.77 billion ($3.66 billion and $4.26 billion, respectively, before discount), related to business written by DBG but ceded to AIRCO and reported in AIRCO's statutory filings. DBG loss reserves also include approximately $535 million and $407 million related to business included in AIUO's statutory filings at December 31, 2006 and 2005, respectively.

(b) At December 31, 2006 and 2005, respectively, Personal Lines loss reserves include $861 million and $878 million related to business ceded to DBG and reported in DBG's statutory filings.

(c) At December 31, 2006 and 2005, respectively, Foreign General loss reserves include approximately $2.87 billion and $2.15 billion related to business reported in DBG's statutory filings.

The DBG net loss reserve of $44.0 billion is comprised principally of the business of AIG subsidiaries participating in the American Home/National Union pool (11 companies) and the surplus lines pool (Lexington, Starr Excess Liability Insurance Company and Landmark Insurance Company).

Beginning in 1998, DBG ceded a quota share percentage of its other liability occurrence and products liability occurrence business to AIRCO. The quota share percentage ceded was 40 percent in 1998, 65 percent in 1999, 75 percent in 2000 and 2001, 50 percent in 2002 and 2003, 40 percent in 2004, 35 percent in 2005 and 20 percent in 2006 and covered all business written in these years for these lines by participants in the American Home/National Union pool. In 1998 the cession reflected only the other liability occurrence business, but in 1999 and subsequent years included products liability occurrence. AIRCO's loss reserves relating to these quota share cessions from DBG are recorded on a discounted basis. As of year-end 2006, AIRCO carried a discount of approximately $330 million applicable to the $3.66 billion in undiscounted reserves it assumed from the American Home/National Union pool via this quota share cession. AIRCO also carries approximately $467 million in net loss reserves relating to Foreign General insurance business. These reserves are carried on an undiscounted basis.

Beginning in 1997, the Personal Lines division ceded a percentage of all business written by the companies participating in the personal lines pool to the American Home/National Union pool. As noted above, the total reserves carried by participants in the American Home/National Union pool relating to this cession amounted to $861 million as of year-end 2006.

The companies participating in the American Home/National Union pool have maintained a participation in the business written by AIU for decades. As of year-end 2006, these AIU reserves carried by participants in the American Home/National Union pool amounted to approximately $2.87 billion. The remaining Foreign

General reserves are carried by AIUO, AIRCO, and other smaller AIG subsidiaries domiciled outside the United States. Statutory filings in the U.S. by AIG companies reflect all the business written by U.S. domiciled entities only, and therefore exclude business written by AIUO, AIRCO, and all other internationally domiciled subsidiaries. The total reserves carried at year-end 2006 by AIUO and AIRCO were approximately $4.57 billion and $3.80 billion, respectively. AIRCO's $3.80 billion in total general insurance reserves consists of approximately $3.33 billion from business assumed from the American Home/National Union pool and an additional $467 million relating to Foreign General Insurance business.

Discounting of Reserves

At December 31, 2006, AIG's overall General Insurance net loss reserves reflect a loss reserve discount of $2.26 billion, including tabular and non-tabular calculations. The tabular workers compensation discount is calculated using a 3.5 percent interest rate and the 1979-81 Decennial Mortality Table. The non-tabular workers compensation discount is calculated separately for companies domiciled in New York and Pennsylvania, and follows the statutory regulations for each state. For New York companies, the discount is based on a five percent interest rate and the companies' own payout patterns. For Pennsylvania companies, the statute has specified discount factors for accident years 2001 and prior, which are based on a six percent interest rate and an industry payout pattern. For accident years 2002 and subsequent, the discount is based on the yield of U.S. Treasury securities ranging from one to twenty years and the company's own payout pattern, with the future expected payment for each year using the interest rate associated with the corresponding Treasury security yield for that time period. The discount is comprised of the following: $662 million — tabular discount for workers compensation in DBG; $1.27 billion — non-tabular discount for workers compensation in DBG; and, $330 million — non-tabular discount for other liability occurrence and products liability occurrence in AIRCO. The total undiscounted workers compensation loss reserve carried by DBG is approximately $11.5 billion as of year-end 2006. The other liability occurrence and products liability occurrence business in AIRCO that is assumed from DBG is discounted based on the yield of U.S. Treasury securities ranging from one to twenty years and the DBG payout pattern for this business. The undiscounted reserves assumed by AIRCO from DBG totaled approximately $3.66 billion at December 31, 2006.

Results of 2006 Reserving Process

Management believes that the General Insurance net loss reserves are adequate to cover General Insurance net losses and loss expenses as of December 31, 2006. While AIG regularly reviews the adequacy of established loss reserves, there can be no assurance that AIG's ultimate loss reserves will not develop adversely and materially exceed AIG's loss reserves as of December 31, 2006. In the opinion of management, such adverse development and resulting increase in reserves is not likely to have a material adverse effect on AIG's consolidated financial condition, although it could have a material adverse effect on AIG's consolidated results of operations for an individual reporting period. See also Item 1A. Risk Factors — Casualty Insurance and Underwriting Reserves.

The following table presents the reconciliation of net loss reserves for 2006, 2005 and 2004 as follows:

(in millions)	**2006**	2005	2004
Net reserve for losses and loss expenses at beginning of year	**$57,476**	$47,254	$36,228
Foreign exchange effect	**741**	(628)	524
Acquisition[(a)]	**55**	—	—
Losses and loss expenses incurred:			
Current year	**27,805**	28,426	26,793
Prior years, other than accretion of discount	**(53)**	4,680[(b)]	3,187[(c)]
Prior years, accretion of discount	**300**	(15)	377
Losses and loss expenses incurred	**28,052**	33,091	30,357
Losses and loss expenses paid:			
Current year	**8,368**	7,331	7,692
Prior years	**15,326**	14,910	12,163
Losses and loss expenses paid	**23,694**	22,241	19,855
Net reserve for losses and loss expenses at end of year	**$62,630**	$57,476	$47,254

(a) Reflects the opening balance with respect to the acquisition of the Central Insurance Co., Ltd. in the third quarter of 2006.

(b) Includes fourth quarter charge of $1.8 billion.

(c) Includes fourth quarter charge of $850 million attributable to the change in estimate for asbestos and environmental exposures.

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

(in millions)	**2006**	2005	2004
Prior Accident Year Development by Reporting Unit:			
DBG	**$ 110**	$4,871	$2,857
Personal Lines	**(111)**	14	75
UGC	**(115)**	(103)	(102)
Foreign General	**(118)**	(371)	40
Sub total	**(234)**	4,411	2,870
Transatlantic	**181**	269	317
Prior years, other than accretion of discount	**$ (53)**	$4,680	$3,187

(in millions)	**2006**	2005	2004
Prior Accident Year Development by Major Class of Business:			
Excess casualty (DBG)	**$ 102**	$ 1,191	$ 1,240
D&O and related management liability (DBG)	**(20)**	1,627	930
Excess workers compensation (DBG)	**74**	983	279
Reinsurance (Transatlantic)	**181**	269	317
Asbestos and environmental (primarily DBG)	**208**	930	1,006
All other, net	**(598)**	(320)	(585)
Prior years, other than accretion of discount	**$ (53)**	$ 4,680	$ 3,187

Accident Year *(in millions)*	Calendar Year **2006**	2005	2004
Prior Accident Year Development by Accident Year:			
2005	**$(1,576)**		
2004	**(511)**	$(3,853)	
2003	**(212)**	(63)	$(1,483)
2002	**373**	1,360	69
2001	**29**	1,749	1,123
2000	**338**	1,323	760
1999	**382**	944	693
1998	**41**	605	536
1997	**197**	281	174
1996 & Prior	**886**	2,334	1,315
Prior years, other than accretion of discount	**$ (53)**	$ 4,680	$ 3,187

The loss ratios recorded by AIG for 2006 took into account the results of the comprehensive reserve reviews that were completed in the fourth quarter of 2005. AIG's year-end 2005 reserve review reflected careful consideration of the reserve analyses prepared by AIG's internal actuarial staff with the assistance of third party actuaries. In determining the appropriate loss ratios for accident year 2006 for each class of business, AIG gave consideration to the loss ratios resulting from the 2005 reserve analyses as well as all other relevant information including rate changes, expected changes in loss costs, changes in coverage, reinsurance or mix of business, and other factors that may affect the loss ratios.

In 2006, AIG enhanced its process of determining the quarterly loss development from prior accident years. In the first quarter of 2006, AIG began conducting additional analyses to determine the change in estimated ultimate loss for each accident year for each profit center. For example, if loss emergence for a profit center is different than expected for certain accident years, the actuaries now take additional steps to examine the indicated effect such emergence would have on the reserves of that profit center. In some cases, the higher or lower than expected emergence may result in no clear change in the ultimate loss estimate for the accident years in question, and no adjustment would be made to the profit center's reserves for prior accident years. In other cases, the higher or lower than expected emergence may result in a larger change, either favorable or unfavorable, than the difference between the actual and expected loss emergence. Such additional analyses were conducted for each profit center, as appropriate, in the first, second and third quarters of 2006 to determine the loss development from prior accident years for the first, second and third quarters of 2006. As part of its quarterly reserving process, AIG also considers notices of claims received with respect to emerging issues, such as those related to stock option backdating. In the fourth quarter of 2006, a comprehensive loss reserve review was completed for each AIG general insurance subsidiary. The prior accident year loss reserve development shown in the tables above for 2006 reflects the results of these comprehensive reviews, including the effect of actual loss emergence in the fourth quarter of 2006.

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

For 2005, net loss development from prior accident years was adverse by approximately $4.68 billion, including approximately $269 million from the general reinsurance operations of Transatlantic. This $4.68 billion adverse development in 2005 was comprised of approximately $8.60 billion for the 2002 and prior accident years, partially offset by favorable development for accident years 2003 and 2004 for most classes of business, with the notable exception of D&O. The adverse loss development for 2002 and prior accident years was attributable to approximately $4.0 billion of development from the D&O and related management liability classes of business, excess casualty, and excess workers compensation, and to approximately $900 million of adverse development from asbestos and environmental claims. The remaining portion of the adverse development from 2002 and

prior accident years included approximately $520 million related to Transatlantic with the balance spread across many other classes of business. Most classes of business produced favorable development for accident years 2003 and 2004, and adverse development for accident years 2001 and prior.

For 2004, AIG's overall net loss reserve development from prior accident years was an increase of approximately $3.19 billion, including approximately $317 million from the general reinsurance operations of Transatlantic and excluding approximately $377 million from accretion of loss reserve discount. This $3.19 billion adverse development in 2004 was comprised of approximately $4.67 billion of adverse development for the 2002 and prior accident years, partially offset by approximately $1.48 billion of favorable development for accident year 2003. The adverse development for the 2002 and prior accident years was primarily attributable to excess casualty, D&O and related management liability classes, and asbestos and environmental reserves, all within DBG, and also to Transatlantic. Most classes of business throughout AIG produced favorable development for accident year 2003.

The following is a discussion of the primary reasons for the development in 2006, 2005 and 2004 for those classes of business that experienced significant prior accident year developments during the three-year period. See Asbestos and Environmental Reserves below for a further discussion of asbestos and environmental reserves and developments.

Excess Casualty: Excess Casualty reserves experienced significant adverse loss development in 2004 and 2005, but in 2006 there was only a relatively minor amount of adverse development. The adverse development for all periods shown related principally to accident years 2000 and prior, and to a lesser extent 2001, and resulted from significant loss cost increases due to both frequency and severity of claims. The increase in loss costs resulted primarily from medical inflation, which increased the economic loss component of tort claims, advances in medical care, which extended the life span of severely injured claimants, and larger jury verdicts, which increased the value of severe tort claims. An additional factor affecting AIG's excess casualty experience in recent years has been the accelerated exhaustion of underlying primary policies for homebuilders. This has led to increased construction defect-related claims activity on AIG's excess policies. Many excess casualty policies were written on a multi-year basis in the late 1990s, which limited AIG's ability to respond to emerging market trends as rapidly as would otherwise be the case. In subsequent years, AIG responded to these emerging trends by increasing rates and implementing numerous policy form and coverage changes. This led to a significant improvement in experience beginning with accident year 2001.

In the year-end 2004 loss reserve review, AIG's actuaries responded to the adverse development for excess casualty by increasing the loss development factor assumptions. In the year-end 2004 reserve study, the development factors applicable to accident years 1998 and subsequent were increased by approximately 12 percent. In addition, the expected loss ratios for accident years 2002 and subsequent were increased to take into account the higher ultimate loss ratios for accident years 2001 and prior.

For the year-end 2005 loss reserve review, AIG's actuaries responded to the continuing adverse development by further increasing the loss development factors applicable to accident years 1999 and subsequent by approximately 5 percent. In addition, to more accurately estimate losses for construction defect-related claims, a separate review was performed by AIG claims staff for accounts with significant exposure to these claims.

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

Loss reserves pertaining to the excess casualty class of business are generally included in the Other liability occurrence line of business, with a small portion of the excess casualty reserves included in the Other liability claims made line of business, as presented in the table on page 37.

D&O and Related Management Liability Classes of Business: These classes of business experienced significant adverse development in 2004 and 2005, but experienced slightly favorable development in 2006. The adverse development in 2004 and 2005 related principally to accident years 2002 and prior. This adverse development resulted from significant loss cost escalation due to a variety of factors, including the following: the increase in frequency and severity of corporate bankruptcies; the increase in frequency of financial statement restatements; the sharp rise in market capitalization of publicly traded companies; and the increase in the number of initial public offerings, which led to an unprecedented number of IPO allocation/laddering suits in 2001. In addition, extensive utilization of multi-year policies during this period limited AIG's ability to respond to emerging trends as rapidly as would otherwise be the case. AIG experienced significant adverse loss development since 2002 as a result of these issues. AIG responded to this development with rate increases and policy form and coverage changes to better contain future loss costs in this class of business.

In the year-end 2004 loss reserve review, AIG's actuaries responded to the adverse development for D&O and related management liability classes by increasing the loss development factor assumptions. The development factors applicable to accident years 1997 and subsequent were increased by approximately 5 percent in the year-end 2004 reserve study. In addition, the expected loss ratios for accident years 2002 and subsequent were increased to take into account the higher ultimate loss ratios for accident years 2001 and prior. The loss ratios for the older accident years increased due to the combination of higher than expected loss development in the year and the increase in the loss development factor assumptions.

For the year-end 2005 loss reserve review, AIG's actuaries responded to the continuing adverse development by further increasing the loss development factor assumptions. The loss development factors applicable to 1997 and subsequent accident years were increased by approximately 4 percent. In addition, AIG's actuaries began to give greater weight to loss development methods for accident years 2002 and 2003, in order to more fully respond to the recent loss experience. AIG's claims staff also conducted a series of ground-up claim projections covering all open claims for this business through accident year 2004. AIG's actuaries benchmarked the loss reserve indications for all accident years through 2004 to these claim projections.

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

Loss reserves pertaining to D&O and related management liability classes of business are included in the Other liability claims made line of business, as presented in the table on page 37.

Excess Workers Compensation: This class of business experienced significant adverse development in 2005, and a relatively minor amount of adverse development in 2006. The adverse development in 2005 related to 2002 and prior accident years. This adverse development resulted primarily from significant loss cost increases, primarily attributable to rapidly increasing medical inflation and advances in medical care, which increased the cost of covered medical care and extended the life span of severely injured workers. The effect of these factors on excess workers compensation claims experience is leveraged, as frequency is increased by the rising number of claims that reach the excess layers.

In response to the significantly adverse loss development in 2005, an additional study was conducted for the 2005 year-end actuarial reserve analysis for DBG pertaining to the selection of loss development factors for this class of business. Claims for excess workers compensation exhibit an exceptionally long-tail of loss development, running for decades from the date the loss is incurred. Thus, the adequacy of loss reserves for this class is sensitive to the estimated loss development factors, as such factors may be applied to many years of loss experience. In order to better estimate the tail development for this class, AIG claims staff conducted a claim-by-claim projection of the expected ultimate paid loss for each open claim for 1998 and prior accident years as these are the primary years from which the tail factors are derived. The objective of the study was to provide a benchmark against which loss development factors in the tail could be evaluated. The resulting loss development factors utilized by the actuaries in the year-end 2005 study reflected an increase of approximately 18 percent from the factors used in the prior year study without the benefit of the claims benchmark. In addition, the loss cost trend assumption for excess workers compensation was increased from approximately 2.5 percent to 6 percent for the 2005 study.

For the year-end 2006 loss reserve review, AIG claims staff updated the claim-by-claim projection for each open claim for accident years 1999 and prior. These updated claims projections were utilized by the actuaries as a benchmark for loss development factors in the year-end 2006 study. AIG's actuaries determined that no significant changes in the assumptions were required. Prior accident year development in 2006 was adverse by approximately $70 million, a relatively minor amount for this class.

Overview of Loss Reserving Process

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

Short-Tail Reserves

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

Long-Tail Reserves

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

AIG's carried net long-tail loss reserves are tested using loss trend factors that AIG considers appropriate for each class of business. A variety of actuarial methods and assumptions is normally employed to estimate net losses for long-tail casualty classes of businesses. These methods ordinarily involve the use of loss trend factors intended to reflect the annual growth in loss costs from one accident year to the next. For the majority of long-tail casualty classes of business, net loss trend factors approximated five percent. Loss trend factors reflect many items

including changes in claims handling, exposure and policy forms, current and future estimates of monetary inflation and social inflation and increases in litigation and awards. These factors are periodically reviewed and adjusted, as appropriate, to reflect emerging trends which are based upon past loss experience. Thus, many factors are implicitly considered in estimating the year to year growth in loss costs.

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

- Loss trend factors which are used to establish expected loss ratios for subsequent accident years based on the projected loss ratio for prior accident years.
- Expected loss ratios for the latest accident year (i.e., accident year 2006 for the year-end 2006 loss reserve analysis) and, in some cases for accident years prior to the latest accident year. The expected loss ratio generally reflects the projected loss ratio from prior accident years, adjusted for the loss trend (see above) and the effect of rate changes and other quantifiable factors on the loss ratio. For low-frequency, high-severity classes such as excess casualty, expected loss ratios generally are used for at least the three most recent accident years.
- Loss development factors which are used to project the reported losses for each accident year to an ultimate basis. Generally, the actual loss development factors observed from prior accident years would be used as a basis to determine the loss development factors for the subsequent accident years.

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

Details of the Loss Reserving Process

The process of determining the current loss ratio for each class of business is based on a variety of factors. These include, but are not limited to, the following considerations: prior accident year and policy year loss ratios; rate changes; changes in coverage, reinsurance, or mix of business; and actual and anticipated changes in external factors affecting results, such as trends in loss costs or in the legal and claims environment. The current loss ratio for each class of business reflects input from actuarial, underwriting and claims staff and is intended to represent management's best estimate of the current loss ratio after reflecting all of the factors described above. At the close of each quarter, the assumptions underlying the loss ratios are reviewed to determine if the loss ratios based thereon remain appropriate. This process includes a review of the actual claims experience in the quarter, actual rate changes achieved, actual changes in coverage, reinsurance or mix of business, and changes in certain other factors that may affect the loss ratio. When this review suggests that the initially determined loss ratio is no longer appropriate, the loss ratio for current business is changed to reflect the revised assumptions.

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

Actuarial Methods for Major Classes of Business

In testing the reserves for each class of business, a determination is made by AIG's actuaries as to the most appropriate actuarial methods. This determination is based on a variety of factors including the nature of the claims associated with the class of business, such as frequency or severity. Other factors considered include the loss development characteristics associated with the claims, the volume of claim data available for the applicable class, and the applicability of various actuarial methods to the class. In addition to determining the actuarial methods, the actuaries determine the appropriate loss reserve groupings of data. For example, AIG writes a great number of unique subclasses of professional liability. For pricing or other purposes, it is appropriate to evaluate the profitability of each subclass individually. However, for purposes of estimating the loss reserves for professional liability, it is appropriate to combine the subclasses

into larger groups. The greater degree of credibility in the claims experience of the larger groups may outweigh the greater degree of homogeneity of the individual subclasses. This determination of data segmentation and actuarial methods is carefully considered for each class of business. The segmentation and actuarial methods chosen are those which together are expected to produce the most accurate estimate of the loss reserves.

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

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

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

Frequency/severity methods generally rely on the determination of an ultimate number of claims and an average severity for each claim for each accident year. Multiplying the estimated ultimate number of claims for each accident year by the expected average severity of each claim produces the estimated ultimate loss for the accident year. Frequency/severity methods generally require a sufficient volume of claims in order for the average severity to be predictable. Average severity for subsequent accident years is generally determined by applying an estimated annual loss cost trend to the estimated average claim severity from prior accident years. Frequency/severity methods have the advantage that ultimate claim counts can generally be estimated more quickly and accurately than can ultimate losses. Thus, if the average claim severity can be accurately estimated, these methods can more quickly respond to changes in loss experience than other methods. However, for average severity to be predictable, the

class of business must consist of homogeneous types of claims for which loss severity trends from one year to the next are reasonably consistent. Generally these methods work best for high frequency, low severity classes of business such as personal auto. AIG utilizes these methods in pricing subclasses of professional liability. However, AIG does not generally utilize frequency/severity methods to test loss reserves, due to the general nature of AIG's reserves being applicable to lower frequency, higher severity commercial classes of business where average claim severity is volatile.

Excess Casualty: AIG generally uses a combination of loss development methods and expected loss ratio methods for excess casualty classes. Expected loss ratio methods are generally utilized for at least the three latest accident years, due to the relatively low credibility of the reported losses. The loss experience is generally reviewed separately for lead umbrella classes and for other excess classes, due to the relatively shorter tail for lead umbrella business. Automobile-related claims are generally reviewed separately from non-auto claims, due to the shorter tail nature of the automobile related claims. The expected loss ratios utilized for recent accident years are based on the projected ultimate loss ratios of prior years, adjusted for rate changes, estimated loss cost trends and all other changes that can be quantified. The estimated loss cost trend utilized in the year-end 2006 reviews averaged approximately 6 percent for excess casualty classes. Frequency/severity methods are generally not utilized as the vast majority of reported claims do not result in a claim payment. In addition, the average severity varies significantly from accident year to accident year due to large losses which characterize this class of business, as well as changing proportions of claims which do not result in a claim payment.

D&O: AIG generally utilizes a combination of loss development methods and expected loss ratio methods for D&O and related management liability classes of business. Expected loss ratio methods are given more weight in the two most recent accident years, whereas loss development methods are given more weight in more mature accident years. Beginning with the year-end 2005 loss reserve review, AIG's actuaries began to utilize claim projections provided by AIG claims staff as a benchmark for determining the indicated ultimate losses for accident years 2004 and prior. For the year end 2006 loss reserve review, claims projections for accident years 2005 and prior were utilized. In prior years, AIG's actuaries had utilized these claims projections as a benchmark for profitability studies for major classes of D&O and related management liability business. The track record of these claims projections has indicated a very low margin of error, thus providing support for their usage as a benchmark in determining the estimated loss reserve. These classes of business reflect claims made coverage, and losses are characterized by low frequency and high severity. Thus, the claim projections can produce an accurate overall indicator of the ultimate loss exposure for these classes by identifying and estimating all large losses. Frequency/severity methods are generally not utilized for these classes as the overall losses are driven by large losses more than by claim frequency. Severity trends have varied significantly from accident year to accident year.

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

Excess Workers Compensation: AIG generally utilizes a combination of loss development methods and expected loss ratio methods. Loss development methods are given the greater weight for mature accident years such as 2000 and prior. Expected loss ratio methods are given the greater weight for the more recent accident years. Excess workers compensation is an extremely long-tail class of business, with loss emergence extending for decades. Therefore there is limited credibility in the reported losses for many of the more recent accident years. Beginning with the year-end 2005 loss reserve review, AIG's actuaries began to utilize claims projections provided by AIG claims staff to help determine the loss development factors for this class of business.

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

utilize frequency/severity methods to test reserves for this business, due to significant changes and growth in AIG's general liability and products liability business over the years.

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

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

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

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

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

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

Mortgage Guaranty: AIG tests mortgage guaranty reserves using loss development methods, supplemented by an internal claim analysis by actuaries and staff who specialize in the mortgage guaranty business. The claim analysis projects ultimate losses for claims within each of several categories of default based on actual historical experience and is essentially a frequency/severity analysis for each category of default.

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

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

Loss Adjustment Expenses: AIG determines reserves for legal defense and cost containment loss adjustment expenses for each

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

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

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

Volatility of Reserve Estimates and Sensitivity Analyses

As described above, AIG uses numerous assumptions in determining its best estimate of reserves for each class of business. The importance of any specific assumption can vary by both class of business and accident year. If actual experience differs from key assumptions used in establishing reserves, there is potential for significant variation in the development of loss reserves, particularly for long-tail casualty classes of business such as excess casualty, D&O or workers compensation. Set forth below is a sensitivity analysis that estimates the effect on the loss reserve position of using alternative loss trend or loss development factor assumptions rather than those actually used in determining AIG's best estimates in the year-end loss reserve analyses for 2006. The analysis addresses each major class of business for which a material deviation to AIG's overall reserve position is believed reasonably possible, and uses what AIG believes is a reasonably likely range of potential deviation for each class. There can be no assurance, however, that actual reserve development will be consistent with either the original or the adjusted loss trend or loss development factor assumptions, or that other assumptions made in the reserving process will not materially affect reserve development for a particular class of business.

Excess Casualty: For the excess casualty class of business, the assumed loss cost trend was approximately six percent. After evaluating the historical loss cost trends from prior accident years since the early 1990s, in AIG's judgment, it is reasonably likely that actual loss cost trends applicable to the year-end 2006 loss reserve review for excess casualty will range from negative four percent to positive 16 percent, or approximately ten percent lower or higher than the assumption actually utilized in the year-end 2006 reserve review. A ten percent change in the assumed loss cost trend for excess casualty would cause approximately a $1.7 billion increase or a $1.2 billion decrease in the net loss and loss expense reserve for this class of business. It should be emphasized that the ten percent deviations are not considered the highest possible deviations that might be expected, but rather what is considered by AIG to reflect a reasonably likely range of potential deviation. Actual loss cost trends in the early 1990s were negative for several years, including amounts below the negative four percent cited above, whereas actual loss cost trends in the late 1990s ran well into the double digits for several years, including amounts greater than the 16 percent cited above. Thus, there can be no assurance that loss trends will not deviate by more than ten percent. The loss cost trend assumption is critical for the excess casualty class of business due the long-tail nature of the claims and therefore is applied across many accident years.

For the excess casualty class of business, the assumed loss development factors are also a key assumption. After evaluating the historical loss development factors from prior accident years since the early 1990s, in AIG's judgment, it is reasonably likely that actual loss development factors will range from approximately 3.25 percent below those actually utilized in the year-end 2006 reserve review to approximately ten percent above those factors actually utilized. If the loss development factor assumptions were changed by 3.25 percent and ten percent, respectively, the net loss reserves for the excess casualty class would decrease by approximately $450 million under the lower assumptions or increase by approximately $1.25 billion under the higher assumptions. Generally, actual historical loss development factors are used to project future loss development. However there can be no assurance that future loss development patterns will be the same as in the past, or that they will not deviate by more than the amounts illustrated above. Moreover, as excess casualty is a long-tail class of business, any deviation in loss cost trends or in loss development factors might not be discernible for an extended period of time subsequent to the recording of the initial loss reserve estimates for any accident year. Thus, there is the potential for the reserves with respect to a number of accident years to be significantly affected by changes in the loss cost trends or loss development factors that were initially relied upon in setting the reserves. These changes in loss trends or loss development factors could be attributable to changes in inflation or in the judicial environment, or in other social or economic conditions affecting claims. Thus, there is the potential for

variations greater than the amounts cited above, either positively or negatively.

D&O and Related Management Liability Classes of Business: For D&O and related management liability classes of business, the assumed loss cost trend was approximately four percent. After evaluating the historical loss cost trends from prior accident years since the early 1990s, in AIG's judgment, it is reasonably likely that actual loss cost trends applicable to the year-end 2006 loss reserve review for these classes will range from negative 11 percent to positive 19 percent, or approximately 15 percent lower or higher than the assumption actually utilized in the year-end 2006 reserve review. A 15 percent change in the assumed loss cost trend for these classes would cause approximately a $625 million increase or a $550 million decrease in the net loss and loss expense reserves for these classes of business. It should be emphasized that the 15 percent deviations are not considered the highest possible deviations that might be expected, but rather what is considered by AIG to reflect a reasonably likely range of potential deviation. Actual loss cost trends for these classes in the early 1990s were negative for several years, including amounts below the negative 11 percent cited above, whereas actual loss cost trends in the late 1990s ran at nearly 50 percent per year for several years, vastly exceeding the 19 percent figure cited above. Because the D&O class of business has exhibited highly volatile loss trends from one accident year to the next, there is the possibility of an exceptionally high deviation.

For D&O and related management liability classes of business, the assumed loss development factors are also an important assumption but less critical than for excess casualty. Because these classes are written on a claims made basis, the loss reporting and development tail is much shorter than for excess casualty. However, the high severity nature of the claims does create the potential for significant deviations in loss development patterns from one year to the next. After evaluating the historical loss development factors for these classes of business for accident years since the early 1990s, in AIG's judgment, it is reasonably likely that actual loss development factors will range approximately five percent lower or higher than those factors actually utilized in the year-end 2006 loss reserve review for these classes. If the loss development factor assumptions were changed by five percent, the net loss reserves for these classes would be estimated to increase or decrease by approximately $200 million. As noted above for excess casualty, actual historical loss development factors are generally used to project future loss development. However, there can be no assurance that future loss development patterns will be the same as in the past, or that they will not deviate by more than the five percent.

Excess Workers Compensation: For excess workers compensation business, loss costs were trended at six percent per annum. After reviewing actual industry loss trends for the past ten years, in AIG's judgment, it is reasonably likely that actual loss cost trends applicable to the year-end 2006 loss reserve review for excess workers compensation will range five percent lower or higher than this estimated loss trend. A five percent change in the assumed loss cost trend would cause approximately a $350 million increase or a $225 million decrease in the net loss reserves for this business. It should be emphasized that the actual loss cost trend could vary significantly from this assumption, and there can be no assurance that actual loss costs will not deviate, perhaps materially, by greater than five percent.

For excess workers compensation business, the assumed loss development factors are a critical assumption. Excess workers compensation is an extremely long-tail class of business, with a much greater than normal uncertainty as to the appropriate loss development factors for the tail of the loss development. After evaluating the historical loss development factors for prior accident years since the 1980s, in AIG's judgment, it is reasonably likely that actual loss development factors will range approximately 15 percent lower or higher than those factors actually utilized in the year-end 2006 loss reserve review for excess workers compensation. If the loss development factor assumptions were changed by 15 percent, the net loss reserves for excess workers compensation would increase or decrease by approximately $600 million. Given the exceptionally long-tail for this class of business, there is the potential for actual deviations in the loss development tail to exceed the deviations assumed, perhaps materially.

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

However, for primary workers compensation business the loss development factor assumptions are important. Generally, AIG's actual historical workers compensation loss development factors would be expected to provide a reasonably accurate predictor of future loss development. However, workers compensation is a long-tail class of business, and AIG's business reflects a very significant volume of losses particularly in recent accident years due to growth of the business. After evaluating the actual historical loss developments since the 1980s for this business, in AIG's judgment, it is reasonably likely that actual loss development factors will fall within the range of approximately 2.75 percent below to 7.5 percent above those actually utilized in the year-end 2006 loss reserve review. If the loss development factor assumptions were changed by 2.75 percent and 7.5 percent, respectively, the net loss reserves for workers compensation would decrease or increase by approximately $525 million and $1.5 billion, respectively. It should be noted that loss emergence in 2006 for this class was higher than historical averages, resulting in an increase in loss reserves for prior accident years. However, it is too soon to ascertain if this increased emergence represents a new trend in the pattern of loss development. For this class of business, there can be no assurance that actual deviations from the expected loss development factors will not exceed the deviations assumed, perhaps materially.

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

Asbestos and Environmental Reserves

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

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

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

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

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

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

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

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

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

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

To determine the appropriate loss reserve as of December 31, 2006 for its asbestos and environmental exposures, AIG performed a series of top-down and ground-up reserve analyses. In order to ensure it had the most comprehensive analysis possible, AIG engaged a third-party actuary to assist in a review of these exposures, including ground-up estimates for both asbestos reserves and environmental reserves consistent with the 2005 review. Prior to 2005, AIG's reserve analyses for asbestos and environmental exposures was focused around a report year projection of aggregate losses for both asbestos and environmental reserves. Additional tests such as market share analyses were also performed. Ground-up analyses take into account policy-

holder-specific and claim-specific information that has been gathered over many years from a variety of sources. Ground-up studies can thus more accurately assess the exposure to AIG's layers of coverage for each policyholder, and hence for all policyholders in the aggregate, provided a sufficient sample of the policyholders can be modeled in this manner.

In order to ensure its ground-up analyses were comprehensive, AIG staff produced in the 2006 analyses the information required at policy and claim level detail for over 1,000 asbestos defendants and nearly 1,000 environmental defendants. This represented over 95 percent of all accounts for which AIG had received any claim notice of any amount pertaining to asbestos or environmental exposure. AIG did not set any minimum thresholds, such as amount of case reserve outstanding, or paid losses to date, that would have served to reduce the sample size and hence the comprehensiveness of the ground-up analysis. The results of the ground-up analysis for each significant account were examined by AIG's claims staff for reasonableness, for consistency with policy coverage terms, and any claim settlement terms applicable. Adjustments were incorporated accordingly. The results from the universe of modeled accounts, which as noted above reflects the vast majority of AIG's known exposures, were then utilized to estimate the ultimate losses from accounts or exposures that could not be modeled and to determine the appropriate provision for all unreported claims.

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

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

For asbestos, these tests project the expected losses to be reported over the next twenty years, i.e., from 2007 through 2026, based on the actual losses reported through 2006 and the expected future loss emergence for these claims. Three scenarios were tested, with a series of assumptions ranging from more optimistic to more conservative. In the first scenario, all carried asbestos case reserves are assumed to be within ten percent of their ultimate settlement value. The second scenario relies on an actuarial projection of report year development for asbestos claims reported from 1993 to the present to estimate case reserve adequacy as of year-end 2006. The third scenario relies on an actuarial projection of report year claims for asbestos but reflects claims reported from 1989 to the present to estimate case reserve adequacy as of year-end 2006. Based on the results of the prior report years for each of the three scenarios described above, the report year approach then projects forward to the year 2026 the expected future report year losses, based on AIG's estimate of reasonable loss trend assumptions. These calculations are performed on losses gross of reinsurance. The IBNR (including a provision for development of reported claims) on a net basis is based on applying a factor reflecting the expected ratio of net losses to gross losses for future loss emergence.

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

At year-end 2006, AIG considered a number of factors and recent experience in addition to the results of the respective top-down and ground-up analyses performed for asbestos and environmental reserves. AIG considered the significant uncertainty that remains as to AIG's ultimate liability relating to asbestos and environmental claims. This uncertainty is due to several factors including:

- The long latency period between asbestos exposure and disease manifestation and the resulting potential for involvement of multiple policy periods for individual claims;
- The increase in the volume of claims by currently unimpaired plaintiffs;
- Claims filed under the non-aggregate premises or operations section of general liability policies;
- The number of insureds seeking bankruptcy protection and the effect of prepackaged bankruptcies;
- Diverging legal interpretations; and
- With respect to environmental claims, the difficulty in estimating the allocation of remediation cost among various parties.

After carefully considering the results of the ground-up analysis, which AIG updates on an annual basis, as well as all of the above factors, including the recent report year experience, AIG determined its best estimate was to recognize an increase of $256 million in its carried net asbestos reserves, and a decrease of $58 million in its carried net environmental reserves at December 31, 2006. The corresponding changes in gross reserves were an increase of approximately $570 million for asbestos and a decrease of approximately $230 million for environmental, respectively. A minor amount of additional incurred loss emergence pertaining to asbestos was reflected in 2006, primarily attributable to the general reinsurance operations of Transatlantic. The majority of the increase in asbestos reserves resulting from the 2006 review is attributable to higher than expected emergence of claims pertaining to new asbestos policy exposures. A significant portion of this increase pertains to higher layers of excess coverage for certain major asbestos defendants on business written by DBG. Approximately $80 million of the overall $256 million net asbestos reserve increase is attributable to business written by Foreign General, approximately $30 million of which is in turn ceded to DBG. In 2006, Foreign General enhanced its capability to identify asbestos exposures, resulting in the identification of additional asbestos defendants in 2006, as well as higher layers of exposure for certain existing defendants. As described above, the ground up analysis as of 2006 now models over 1,000 asbestos defendants and over 95 percent of all known reported asbestos claims.

The decrease in environmental reserves resulting from the 2006 review is primarily attributable to favorable loss trends in recent report years. These favorable trends resulted in a reduced expectation of unreported claims, i.e., IBNR, for future report years.

Management's Discussion and Analysis of Financial Condition and Results of Operations *Continued*

A summary of reserve activity, including estimates for applicable IBNR, relating to asbestos and environmental claims separately and combined at December 31, 2006, 2005 and 2004 appears in the table below. The vast majority of such claims arise from policies written in 1984 and prior years. The current environmental policies that AIG underwrites on a claims-made basis have been excluded from the table below.

	2006		2005		2004	
(in millions)	Gross	Net	Gross	Net	Gross	Net
Asbestos:						
Reserve for losses and loss expenses at beginning of year	**$ 4,441**	**$1,840**	$2,559	$1,060	$1,235	$ 386
Losses and loss expenses incurred[(a)]	**571**	**267**	2,207[(b)]	903[(b)]	1,595[(b)]	772[(b)]
Losses and loss expenses paid[(a)]	**(548)**	**(218)**	(325)	(123)	(271)	(98)
Reserve for losses and loss expenses at end of year	**$ 4,464**	**$1,889**	$4,441	$1,840	$2,559	$1,060
Environmental:						
Reserve for losses and loss expenses at beginning of year	**$ 926**	**$ 410**	$ 974	$ 451	$ 789	$ 283
Losses and loss expenses incurred[(a)]	**(232)**	**(59)**	47[(c)]	27[(c)]	314[(c)]	234[(c)]
Losses and loss expenses paid[(a)]	**(106)**	**(61)**	(95)	(68)	(129)	(66)
Reserve for losses and loss expenses at end of year	**$ 588**	**$ 290**	$ 926	$ 410	$ 974	$ 451
Combined:						
Reserve for losses and loss expenses at beginning of year	**$ 5,367**	**$2,250**	$3,533	$1,511	$2,024	$ 669
Losses and loss expenses incurred[(a)]	**339**	**208**	2,254[(d)]	930[(d)]	1,909[(d)]	1,006[(d)]
Losses and loss expenses paid[(a)]	**(654)**	**(279)**	(420)	(191)	(400)	(164)
Reserve for losses and loss expenses at end of year	**$ 5,052**	**$2,179**	$5,367	$2,250	$3,533	$1,511

(a) All amounts pertain to policies underwritten in prior years, primarily to policies issued in 1984 and prior.

(b) Includes increases to gross losses and loss expense reserves of $2.0 billion and $1.2 billion in the fourth quarter of 2005 and 2004, respectively, and increases to net losses and loss expense reserves of $843 million and $650 million for the fourth quarter of 2005 and 2004, respectively.

(c) Includes increases to gross losses and loss expense reserves of $56 million and $250 million in the fourth quarter of 2005 and 2004, respectively, and increases to net losses and loss expense reserves of $30 million and $200 million for the fourth quarter of 2005 and 2004, respectively.

(d) Includes increases to gross losses and loss expense reserves of $2.0 billion and $1.5 billion in the fourth quarter of 2005 and 2004, respectively, and increases to net losses and loss expense reserves of $873 million and $850 million for the fourth quarter of 2005 and 2004, respectively.

As indicated in the table above, asbestos loss payments increased significantly in 2006 compared to the prior years, primarily as a result of payments pertaining to settlements that had been negotiated in earlier periods.

The gross and net IBNR included in the reserve for losses and loss expenses, relating to asbestos and environmental claims separately and combined, at December 31, 2006, 2005 and 2004 were estimated as follows:

	2006		2005		2004	
(in millions)	Gross	Net	Gross	Net	Gross	Net
Asbestos	**$3,212**	**$1,469**	$3,401	$1,465	$2,033	$ 876
Environmental	**340**	**173**	586	266	606	284
Combined	**$3,552**	**$1,642**	$3,987	$1,731	$2,639	$1,160

A summary of asbestos and environmental claims count activity for the years ended December 31, 2006, 2005 and 2004 was as follows:

	2006			2005			2004		
	Asbestos	Environmental	Combined	Asbestos	Environmental	Combined	Asbestos	Environmental	Combined
Claims at beginning of year	**7,293**	**9,873**	**17,166**	7,575	8,216	15,791	7,474	8,852	16,326
Claims during year:									
Opened	**643**	**1,383**	**2,026**	854	5,253*	6,107	909	2,592	3,501
Settled	**(150)**	**(155)**	**(305)**	(67)	(219)	(286)	(100)	(279)	(379)
Dismissed or otherwise resolved	**(908)**	**(1,659)**	**(2,567)**	(1,069)	(3,377)	(4,446)	(708)	(2,949)	(3,657)
Claims at end of year	**6,878**	**9,442**	**16,320**	7,293	9,873	17,166	7,575	8,216	15,791

** The opened claims count increased substantially during 2005 compared to 2004 because a court ruling led AIG to report separate opened claims for previously pending cases relating to alleged MTBE exposures that AIG previously had counted in the aggregate as only a single claim on the assumption that the cases would be consolidated into a single federal court proceeding.*

Survival Ratios — Asbestos and Environmental

The following table presents AIG's survival ratios for asbestos and environmental claims for year-end 2006, 2005 and 2004. The survival ratio is derived by dividing the year end carried loss reserve by the average payments for the three most recent calendar years for these claims. Therefore, the survival ratio is a simplistic measure estimating the number of years it would be before the current ending loss reserves for these claims would be paid off using recent year average payments. The December 31, 2006 survival ratio is lower than the ratio at December 31, 2005 because the more recent periods included in the rolling average reflect higher claims payments. Many factors, such as aggressive settlement procedures, mix of business and level of coverage provided, have a significant effect on the amount of asbestos and environmental reserves and payments and the resultant survival ratio. Thus, caution should be exercised in attempting to determine reserve adequacy for these claims based simply on this survival ratio.

AIG's survival ratios for asbestos and environmental claims, separately and combined were based upon a three-year average payment. These ratios for the years ended December 31, 2006, 2005 and 2004 were as follows:

	Gross	Net
2006		
Survival ratios:		
Asbestos	**11.7**	**12.9**
Environmental	**5.3**	**4.5**
Combined	**10.3**	**10.3**
2005		
Survival ratios:		
Asbestos	15.9	19.8
Environmental	6.9	6.2
Combined	13.0	14.2
2004		
Survival ratios:		
Asbestos	10.7	13.5
Environmental	6.5	6.8
Combined	9.1	10.5

Life Insurance & Retirement Services Operations

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

Domestically, AIG's Life Insurance & Retirement Services operations offer a broad range of protection products, such as life insurance and group life and health products, including disability income products and payout annuities, which include single premium immediate annuities, structured settlements and terminal funding annuities. Home service operations include an array of life insurance, accident and health and annuity products sold primarily through career agents. In addition, home service includes a small block of runoff property and casualty coverage. Retirement services include group retirement products, individual fixed and variable annuities sold through banks, broker-dealers and exclusive sales representatives, and annuity runoff operations, which include previously acquired ''closed blocks'' and other fixed and variable annuities largely sold through distribution relationships that have been discontinued.

Overseas, AIG's Life Insurance & Retirement Services operations include insurance and investment-oriented products such as whole and term life, investment linked, universal life and endowments, personal accident and health products, group products including pension, life and health, and fixed and variable annuities.

AIG's Life Insurance & Retirement Services subsidiaries report their operations through the following major internal reporting units and business units:

Foreign Life Insurance & Retirement Services

Japan and Other*

- ALICO
- AIG Star Life
- AIG Edison Life

Asia

- AIA
- Nan Shan
- AIRCO
- Philamlife

Domestic Life Insurance

- AIG American General
- USLIFE
- AGLA

Domestic Retirement Services

- VALIC
- AIG Annuity
- AIG SunAmerica

* Japan and Other consists of all operations in Japan and the operations of ALICO and its subsidiaries worldwide.

Management's Discussion and Analysis of Financial Condition and Results of Operations *Continued*

Life Insurance & Retirement Services Results

Life Insurance & Retirement Services results for 2006, 2005 and 2004 were as follows:

(in millions)	GAAP Premiums	Net Investment Income	Realized Capital Gains (Losses)	Total Revenues	Operating Income
2006					
Foreign Life Insurance & Retirement Services	**$24,036**	**$ 9,173**	**$ 707**	**$33,916**	**$ 6,792**
Domestic Life Insurance	**5,543**	**3,778**	**(215)**	**9,106**	**917**
Domestic Retirement Services	**1,057**	**6,488**	**(404)**	**7,141**	**2,323**
Total	**$30,636**	**$19,439**	**$ 88**	**$50,163**	**$10,032**
2005					
Foreign Life Insurance & Retirement Services	$23,016	$ 8,175	$ 84	$31,275	$ 5,245
Domestic Life Insurance	5,447	3,733	35	9,215	1,495
Domestic Retirement Services	937	6,226	(277)	6,886	2,164
Total	$29,400	$18,134	$(158)	$47,376	$ 8,904
2004					
Foreign Life Insurance & Retirement Services	$21,917	$ 5,834	$ 372	$28,123	$ 4,848
Domestic Life Insurance	5,376	3,459	(120)	8,715	1,023
Domestic Retirement Services	795	5,976	(207)	6,564	2,054
Total	$28,088	$15,269	$ 45	$43,402	$ 7,925

The following table presents the Insurance In-force for Life Insurance & Retirement Services for the years ended December 31, 2006, 2005 and 2004:

	Years Ended December 31,		
(in millions)	**2006**	2005	2004
Foreign	**$1,162,699**	$1,027,682	$1,085,843
Domestic*	**907,901**	825,151	772,251
Total	**$2,070,600**	$1,852,833	$1,858,094

* *Domestic insurance in-force for 2005 includes the effect of the non-renewal of a single large group life case of $36 billion.*

2006 and 2005 Comparison

Life Insurance & Retirement Service revenues increased $2.8 billion in 2006, to $50.2 billion. The increased revenues reflect growth in the underlying global Life Insurance & Retirement Services businesses. Revenues include the positive effect of out of period adjustments related to the accounting for certain interests in unit investment trusts totaling $240 million in 2006. Operating income grew by $1.1 billion from 2005, to $10.0 billion, reflecting higher revenues and out of period reductions of policy benefits expense of $163 million resulting from corrections of par policyholder dividend reserves and allocations between participating and non-participating accounts, both of which were related to remediation efforts. Net investment income increased $1.3 billion, reflecting growth in the underlying global business and the related increased level of invested assets. Realized capital gains increased $246 million in 2006 compared to 2005. In addition, operating income in 2006 includes charges of $125 million for the adverse Superior National arbitration ruling (see Note 12(c) of Notes to Consolidated Financial Statements) and $66 million related to the exiting of the domestic financial institutions credit life business.

2005 and 2004 Comparison

Life Insurance & Retirement Services revenues, including realized capital losses of $158 million, grew $4.0 billion to $47.4 billion. The increase in revenues reflects growth in the underlying global Life Insurance & Retirement Services businesses. Operating income grew $979 million in 2005, reflecting growth in both domestic and overseas operations. In 2005, the Domestic Life Insurance reporting unit performed well in its life insurance and payout annuities businesses, but results were offset by restructuring efforts in both home services and group life/health. The Domestic Retirement Services reporting unit faced a challenging environment in 2005, resulting in lower deposits and increased surrender rates. The Foreign Life Insurance & Retirement Services reporting unit had improved operating income in 2005 helped by higher net investment income, lower acquisition and operating expenses in life insurance and strong growth in annuities, partially offset by lower realized capital gains and higher incurred policy benefit costs.

Foreign Life Insurance & Retirement Services Results

Foreign Life Insurance & Retirement Services results for 2006, 2005 and 2004 were as follows:

(in millions)	GAAP Premiums	Net Investment Income	Realized Capital Gains (Losses)	Total Revenues	Operating Income
2006					
Japan and Other:					
Life insurance[(a)]	**$ 4,769**	**$1,696**	**$ 316**	**$ 6,781**	**$1,725**
Personal accident	**3,957**	**162**	**49**	**4,168**	**1,122**
Group products	**1,740**	**541**	**13**	**2,294**	**272**
Individual fixed annuities	**337**	**1,930**	**28**	**2,295**	**553**
Individual variable annuities	**173**	**325**	**—**	**498**	**60**
Total	**$10,976**	**$4,654**	**$ 406**	**$16,036**	**$3,732**
Asia:					
Life insurance[(b)]	**$10,949**	**$4,188**	**$ 258**	**$15,395**	**$2,516**
Personal accident	**1,561**	**123**	**6**	**1,690**	**337**
Group products	**486**	**107**	**34**	**627**	**178**
Individual fixed annuities	**63**	**97**	**3**	**163**	**27**
Individual variable annuities	**1**	**4**	**—**	**5**	**2**
Total	**$13,060**	**$4,519**	**$ 301**	**$17,880**	**$3,060**
Total Foreign Life Insurance & Retirement Services:					
Life insurance[(a)(b)]	**$15,718**	**$5,884**	**$ 574**	**$22,176**	**$4,241**
Personal accident	**5,518**	**285**	**55**	**5,858**	**1,459**
Group products	**2,226**	**648**	**47**	**2,921**	**450**
Individual fixed annuities	**400**	**2,027**	**31**	**2,458**	**580**
Individual variable annuities	**174**	**329**	**—**	**503**	**62**
Total	**$24,036**	**$9,173**	**$ 707**	**$33,916**	**$6,792**
2005					
Japan and Other:					
Life insurance	$ 4,852	$1,752	$ (52)	$ 6,552	$1,280
Personal accident	3,788	137	(15)	3,910	1,051
Group products	1,473	535	(34)	1,974	191
Individual fixed annuities	292	1,672	29	1,993	390
Individual variable annuities	97	767	—	864	47
Total	$10,502	$4,863	$ (72)	$15,293	$2,959
Asia:					
Life insurance	$10,779	$3,056	$ 146	$13,981	$1,907
Personal accident	1,214	118	(15)	1,317	241
Group products	452	78	25	555	131
Individual fixed annuities	69	56	—	125	8
Individual variable annuities	—	4	—	4	(1)
Total	$12,514	$3,312	$ 156	$15,982	$2,286
Total Foreign Life Insurance & Retirement Services:					
Life insurance	$15,631	$4,808	$ 94	$20,533	$3,187
Personal accident	5,002	255	(30)	5,227	1,292
Group products	1,925	613	(9)	2,529	322
Individual fixed annuities	361	1,728	29	2,118	398
Individual variable annuities	97	771	—	868	46
Total	$23,016	$8,175	$ 84	$31,275	$5,245

Management's Discussion and Analysis of Financial Condition and Results of Operations *Continued*

(in millions)	GAAP Premiums	Net Investment Income	Realized Capital Gains (Losses)	Total Revenues	Operating Income
2004					
Japan and Other:					
Life insurance	$ 4,469	$1,371	$(134)	$ 5,706	$1,079
Personal accident	3,307	96	16	3,419	932
Group products	1,229	378	(42)	1,565	133
Individual fixed annuities	312	1,011	4	1,327	236
Individual variable annuities	68	142	—	210	13
Total	$ 9,385	$2,998	$(156)	$12,227	$2,393
Asia:					
Life insurance	$10,469	$2,676	$ 497	$13,642	$2,098
Personal accident	994	83	17	1,094	260
Group products[c]	986	53	14	1,053	90
Individual fixed annuities	83	23	—	106	7
Individual variable annuities	—	1	—	1	—
Total	$12,532	$2,836	$ 528	$15,896	$2,455
Total Foreign Life Insurance & Retirement Services:					
Life insurance	$14,938	$4,047	$ 363	$19,348	$3,177
Personal accident	4,301	179	33	4,513	1,192
Group products[c]	2,215	431	(28)	2,618	223
Individual fixed annuities	395	1,034	4	1,433	243
Individual variable annuities	68	143	—	211	13
Total	$21,917	$5,834	$ 372	$28,123	$4,848

(a) Includes the effect of out of period adjustments related to the accounting for certain interests in unit investment trusts. For 2006, the effect was an increase of $32 million in both net investment income and operating income.

(b) Includes the effect of out of period adjustments related to the accounting for certain interests in unit investment trusts. For 2006, the effect was an increase of $208 million and $137 million in net investment income and operating income, respectively. Operating income also includes an out of period reduction in participating policyholder dividend reserves of $163 million, primarily as a result of tax remediation adjustments.

(c) Revenues include approximately $640 million of premiums from a single reinsurance transaction involving terminal funding business, which is offset by a similar increase of benefit reserves.

AIG transacts business in most major foreign currencies and therefore premiums reported in U.S. dollars vary by volume and from changes in foreign currency translation rates. The following table summarizes the effect of changes in foreign currency exchange rates on the growth of the Foreign Life Insurance & Retirement Services GAAP premiums for the year ended December 31, 2006 and 2005:

	2006	2005
Growth in original currency*	**6.4%**	2.5%
Foreign exchange effect	**(2.0)**	2.5
Growth as reported in U.S. dollars	**4.4%**	5.0%

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

Japan and Other

2006 and 2005 Comparison

Total revenues for Japan and Other increased $743 million in 2006, to $16.0 billion, compared to 2005. Operating income grew $773 million, due to growth in the underlying retirement services businesses and realized capital gains of $406 million. The 2006 results for the reporting unit were negatively affected by the weakening of the Japanese Yen against the U.S. dollar during 2006. In addition, operating income was negatively affected by the continued runoff of the older, higher margin in-force business of AIG Star Life and AIG Edison Life.

Life insurance GAAP premiums declined in 2006 compared to 2005 primarily due to the effect of foreign exchange. Foreign exchange negatively affected GAAP premiums by approximately $250 million, most notably as a result of the weakening in the Japanese Yen. Life insurance operating income grew $445 million, primarily due to an increase of $368 million of realized capital gains. Life insurance growth improved due to an increase in single premium life insurance sales in Japan as a result of further bank deregulation effective in December 2005. The expansion of the bank distribution platform for single premium life insurance products adds to the existing multiple distribution platforms in Japan, where AIG remains the leading foreign insurance provider.

Personal accident revenues grew $258 million or 7 percent resulting in operating income growth of $71 million or 7 percent. Personal accident operating income includes the effect of higher terminations of certain accident and health policies in Japan which increased expenses by $54 million in 2006. The higher terminations are a result of a change in the Japanese tax regulations that reduced the tax deduction for premiums. AIG's Japanese operations have experienced lower sales and higher terminations of these contracts. DAC related to these accident

and health policies in force at December 31, 2006 totaled $214 million. In response to the tax law change, AIG has introduced new products, both life and health, to meet the needs of clients in that market. AIG continues to believe that the effect of future policy terminations will not be material to AIG's consolidated financial condition or results of operations.

Revenues from group products increased in 2006 by $320 million, to $2.3 billion, resulting in an increase in operating income of $81 million to $272 million. Fixed annuity reserves continued to grow due to positive net flows, but demand for U.S. dollar fixed annuities has slowed due to a weaker Japanese Yen. The individual fixed annuity revenues grew $302 million to $2.3 billion resulting in an increase in operating income of $163 million to $553 million. Growth in variable annuity deposits has accelerated compared to 2005 due to new product offerings and stronger equity markets, resulting in higher fees and policy charges included in GAAP premiums. Variable annuity revenues declined in 2006 compared to 2005 due to lower policyholder trading gains which comprise the entirety of variable annuity net investment income. Policyholder trading gains are offset by an equal increase in policy benefits expense, as all investment returns for these variable annuities accrue to the benefit of the policyholder.

2005 and 2004 Comparison

In 2005, total revenues for the Japan and Other reporting unit grew $3.1 billion to $15.3 billion, including policyholder trading gains of $1.3 billion. Operating income grew $566 million to $3.0 billion. Compared to 2004, results reported in U.S. dollars were negatively affected by foreign exchange, particularly the weakening of the Japanese Yen to the U.S. dollar. In addition, Japan and Other operating income was negatively affected by the runoff of older higher margin in-force business of AIG Star Life and AIG Edison Life. Life insurance operating income grew primarily due to lower realized capital losses and higher GAAP premiums. Personal accident operating income continued to report stable profit margins and grew $119 million to $1.05 billion. Group operating income grew to $191 million on strong growth in ALICO operations outside of Japan. Individual fixed annuities operating income grew to $390 million, primarily from strong growth of net flows that increased underlying reserves in Japan. Individual fixed annuity operating income for 2005 included a charge of $47 million related to the unwinding of certain businesses in Chile that were sold in 2006. Individual variable annuities operating income grew to $47 million on higher average reserves. Net investment income for individual variable annuities grew to $767 million in 2005 and represents policyholder trading gains (losses) that are offset by an equal amount in incurred policy losses and benefits.

Asia

2006 and 2005 Comparison

Revenues for Asia grew $1.9 billion in 2006 to $17.9 billion. Operating income grew $774 million, to $3.1 billion, including realized capital gains of $301 million. Revenues and operating income in 2006 include $208 million and $137 million, respectively, from out of period adjustments related to certain investments in unit trusts. GAAP premiums grew 4 percent in 2006 compared to 2005. The GAAP premium growth rate was negatively affected by the continuing trend towards investment-oriented products in Asia as only a portion of policy charges collected from the customers are reported as GAAP premiums. AIG's Life Insurance operations in Asia have responded to this trend by offering a wide array of investment linked products, with multiple fund choices but with minimal investment guarantees.

Operating income benefited in 2006 from an out of period reduction in participating policyholder dividend reserves of $163 million, primarily as a result of tax remediation adjustments and a correction to expense allocations between participating and non-participating accounts. Certain participating policyholder dividend reserves are determined on an after tax basis and as a result any change in the local tax provision will have a partially offsetting, but not equal, effect on participating policyholder dividend reserves. The amount of the offsetting effect depends on the level of participation required by law or regulation in that specific country or by the participation level provided for in the underlying contracts. In 2005, operating income for Asia included a charge of $137 million related to an increase in participating policyholder dividends as a result of the settlement of a tax dispute in Singapore. Life insurance revenues grew $1.4 billion to $15.4 billion in 2006, including realized capital gains of $258 million and policyholder trading gains of $552 million, helped by strong growth in investment linked products throughout Asia. Operating income grew $609 million, including adjustments in 2006 and 2005 for participating policyholder dividend reserves mentioned above. Operating income includes the Life Insurance & Retirement Services segment's equal share of the results of AIG Credit Card Company (Taiwan), which amounted to a loss of $47 million in 2006 compared to a gain of $26 million in 2005. Personal accident revenues grew 28 percent to $1.7 billion, reflecting increased focus on risk based accident and health products. The growth in revenues resulted in operating income of $337 million for the year, an increase of 40 percent over 2005. Group products revenues increased $72 million from 2005, to $627 million, resulting in operating income growth of $47 million to $178 million.

2005 and 2004 Comparison

In 2005, revenues were essentially unchanged at $16.0 billion on lower realized capital gains that declined $372 million, due to lower gains on derivatives that did not qualify for hedge accounting. Operating income declined in 2005 by $169 million due to the decrease in realized capital gains and an increase in liabilities for participating policyholder dividends of $137 million as a result of the settlement of a tax dispute in Singapore. Life insurance GAAP premiums grew $310 million to $10.8 billion. Life insurance operating income did not grow in 2005 due to the effect of the additional par policy dividend reserves previously noted and

lower realized capital gains. Personal accident operating income declined primarily due to realized capital losses in 2005 compared to realized capital gains in 2004. Group products GAAP premiums dropped in 2005 compared to 2004. 2004 GAAP premiums included premiums of approximately $640 million from a single reinsurance transaction involving terminal funding business, which is offset by a similar increase in benefit reserves.

Domestic Life Insurance Results

Domestic Life Insurance results, presented on a sub-product basis for 2006, 2005 and 2004 were as follows:

(in millions)	GAAP Premiums	Net Investment Income	Realized Capital Gains (Losses)	Total Revenues	Operating Income (Loss)
2006					
Life insurance[a]	**$2,127**	**$1,377**	**$ (83)**	**$3,421**	**$ 654**
Home service	**790**	**630**	**(38)**	**1,382**	**282**
Group life/health	**995**	**213**	**(8)**	**1,200**	**(159)**
Payout annuities[b]	**1,582**	**1,004**	**(51)**	**2,535**	**76**
Individual fixed annuities	**4**	**77**	**(8)**	**73**	**8**
Individual annuities — runoff[c]	**45**	**477**	**(27)**	**495**	**56**
Total	**$5,543**	**$3,778**	**$(215)**	**$9,106**	**$ 917**
2005					
Life insurance[a]	$2,041	$1,352	$ 98	$3,491	$ 874
Home service	801	605	(2)	1,404	282
Group life/health	1,079	201	(1)	1,279	69
Payout annuities[b]	1,473	912	(34)	2,351	128
Individual fixed annuities	3	47	—	50	7
Individual annuities — runoff[c]	50	616	(26)	640	135
Total	$5,447	$3,733	$ 35	$9,215	$1,495
2004					
Life insurance[a]	$1,821	$1,228	$ (94)	$2,955	$ 612
Home service	812	608	(18)	1,402	290
Group life/health	1,195	182	—	1,377	(131)
Payout annuities[b]	1,484	801	(8)	2,277	124
Individual fixed annuities	4	22	3	29	1
Individual annuities — runoff[c]	60	618	(3)	675	127
Total	$5,376	$3,459	$(120)	$8,715	$1,023

(a) Effective January 1, 2006, the broker-dealer operations of the Domestic Life Insurance companies are being reported and managed within the Asset Management segment. Included in GAAP premiums and Total Revenues were revenues of $102 million and $96 million, respectively, for 2005 and 2004.

(b) GAAP Premiums and Total Revenues include structured settlements, single premium immediate annuities and terminal funding annuities.

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

The following table reflects periodic Domestic Life insurance sales by product for 2006, 2005 and 2004, respectively:

Domestic Life Insurance

(in millions)	**2006**	2005	2004
Periodic Premium Sales By Product*:			
Universal life	**$334**	$271	$201
Variable universal life	**56**	44	79
Term life	**240**	229	215
Whole life/other	**13**	10	13
Total	**$643**	$554	$508

* *Periodic premium represents premium from new business expected to be collected over a one-year period.*

2006 and 2005 Comparison

GAAP premiums for Domestic Life Insurance were $5.5 billion in 2006, a 2 percent increase compared to 2005. Overall, periodic life insurance sales grew by 16 percent, compared to 2005, reflecting increased growth from the independent distribution platform. During the second half of 2006, certain universal life products were re-priced and underwriting standards were tightened, which could affect future periodic life insurance sales. GAAP premiums from AGLA, AIG's home service business, declined slightly in 2006 as the reduction of premium in-force from normal lapses and maturities exceeded sales growth for the period. GAAP premiums for group life/health for 2006 declined over the prior year primarily due to restructuring efforts in certain product lines, including the financial institutions credit life business and the employer benefits business. The GAAP premium growth from payout annuities for 2006 reflects increased sales of single premium annuities and structured settlements when compared to 2005. At December 31, 2006, AIG effectively exited the financial institutions credit business through a third party indemnity reinsurance agreement. The transaction is expected to close in the first quarter of 2007, subject to normal closing requirements, including regulatory approval. GAAP premiums in 2006 related to this business were approximately $100 million.

Domestic Life Insurance operating income of $917 million declined by 39 percent in 2006 compared to 2005 due to several significant transactions, including a $125 million charge resulting from the loss of the Superior National arbitration. For a further discussion of the Superior National arbitration see Note 12(c) of Notes to Consolidated Financial Statements. In addition, Domestic Life operating income was negatively affected by a $55 million accrual related to other litigation and a $66 million loss related to exiting the financial institutions credit business.

Life insurance operating income decreased by $220 million or 25 percent for 2006 due to a $45 million decrease in partnership income, $30 million in litigation-related charges and realized capital losses that offset growth in the underlying business. Home service operating income was flat compared with 2005 due to increased net investment income from partnerships and lower acquisition costs and catastrophe losses, partially offset by a DAC unlocking charge of $11 million and higher realized capital losses. Group life/health operating income for 2006 was lower than 2005 primarily due to the $125 million Superior National charge and the $66 million loss associated with the exit from the financial institutions credit business. The group life/health lines operating income was also affected by a $25 million charge for litigation reserves. Payout annuities operating income declined for 2006 due to lower calls and tenders on fixed maturity securities. In addition, various methodologies and assumptions were enhanced for payout annuity reserves, resulting in a $24 million increase to the payout annuity reserves. Individual annuities — runoff operating income is down from 2005 due to the decline in the block of business and the related DAC unlocking charge of $30 million to reflect lower in-force amounts.

2005 and 2004 Comparison

The Domestic Life Insurance operations in 2005 had continued growth in term and universal life sales with good performance from the independent distribution channels. GAAP premiums for life insurance grew 12 percent in 2005 reflecting consistently strong sales from the independent distribution platform. Payout annuities declined slightly due to the low interest rate environment and the competitive market conditions for structured settlement and single premiums individual annuity business. Home service GAAP premiums were essentially flat in this slow growth business. The group life/health GAAP premiums declined by $116 million, or 10 percent, primarily due to the non-renewal of several accounts where pricing was unacceptable and loss experience was higher than anticipated.

Domestic Life Insurance operating income of $1.5 billion increased 46 percent in 2005 resulting from increased realized capital gains, higher partnership income and growth in the underlying business compared to 2004. Life insurance operating income was up 43 percent in 2005 compared to 2004 due in part to growth in the underlying business, improved mortality results and higher realized capital gains, offset by higher losses from partnership investments in synthetic fuel production facilities. Home service operating income declined as a result of a reduction in premiums in-force and higher insurance and acquisitions expenses, combined with an increase in losses related to hurricanes. Group life/health operating income was affected by the non-renewal of cases where acceptable margins could not be achieved. Operating income in 2004 includes a $178 million charge related to a workers compensation quota share reinsurance agreement with Superior National. In addition, in 2004, as part of the business review of group life/health, approximately $68 million was incurred for reserve strengthening and allowances for receivables. Payout annuities operating income increased 3 percent as growth in the business base was offset by higher realized capital losses. Individual annuities runoff operating income increased in 2005 primarily as a result of lower operating expenses offset by higher realized capital losses when compared to 2004.

Management's Discussion and Analysis of Financial Condition and Results of Operations *Continued*

Domestic Retirement Services Results

Domestic Retirement Services results, presented on a sub-product basis for 2006, 2005 and 2004 were as follows:

(in millions)	GAAP Premiums	Net Investment Income	Realized Capital Gains (Losses)	Total Revenue	Operating Income
2006					
Group retirement products	**$ 386**	**$2,279**	**$(144)**	**$2,521**	**$1,017**
Individual fixed annuities	**122**	**3,581**	**(257)**	**3,446**	**1,036**
Individual variable annuities	**531**	**202**	**5**	**738**	**193**
Individual annuities — runoff*	**18**	**426**	**(8)**	**436**	**77**
Total	**$1,057**	**$6,488**	**$(404)**	**$7,141**	**$2,323**
2005					
Group retirement products	$ 351	$2,233	$ (67)	$2,517	$1,055
Individual fixed annuities	97	3,346	(214)	3,229	858
Individual variable annuities	467	217	4	688	189
Individual annuities — runoff*	22	430	—	452	62
Total	$ 937	$6,226	$(277)	$6,886	$2,164
2004					
Group retirement products	$ 313	$2,201	$(111)	$2,403	$ 987
Individual fixed annuities	55	3,078	(78)	3,055	851
Individual variable annuities	407	239	(17)	629	176
Individual annuities — runoff*	20	458	(1)	477	40
Total	$ 795	$5,976	$(207)	$6,564	$2,054

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

2006 and 2005 Comparison

Domestic Retirement Services total deposits decreased slightly for 2006 compared to 2005. The decrease in total deposits reflects lower fixed annuity sales that continued to face increased competition from bank deposit products and money market funds offering very competitive short-term rates in the flat yield curve environment. This was partially offset by substantially higher individual variable annuity sales and group mutual fund deposits. Individual variable annuity deposits grew 29 percent in 2006 from 2005, reflecting growth in products with living benefit guarantee features. Group retirement deposits grew 6 percent in 2006, reflecting 51 percent growth in group mutual fund sales partially offset by a 1 percent sales drop in annuity deposits. Over time, this will result in a gradual reduction in overall profit margins of this business driven by the growth in the lower-margin mutual fund products relative to the annuity products. Fixed annuity surrender rates increased in 2006 compared to 2005 due to products coming out of their surrender charge period and the increased competition from banks. Individual fixed annuity net flows for 2006 were negative $2.7 billion compared to positive net flows of $1.3 billion in 2005, reflecting both the lower deposits and higher surrenders, caused by the flat or inverted yield curve.

Total domestic retirement service operating income for 2006 of $2.3 billion increased 7 percent from 2005. Group retirement products total revenues were flat in 2006 primarily due to improvements in partnership income and variable annuity fees being offset by increased capital losses. The flat revenues, coupled with higher amortization of deferred acquisition costs related to internal replacements of existing contracts into new contracts, resulted in a 4 percent decrease in group retirement operating income. Total revenues for individual fixed annuities were up 7 percent in 2006 and operating income was up 21 percent primarily driven by higher partnership and yield enhancement income. Individual variable annuity total revenues were up 7 percent in 2006, primarily driven by higher variable annuity fees resulting from the increase in the equity markets. Offsetting somewhat the growth in total revenues was an increase in DAC amortization resulting from increased surrender activity in the first half of 2006, with operating income up 2 percent for the year. In 2006, the individual annuities runoff operating income increased $15 million even though the underlying reserves decreased. The higher income in 2006 was primarily due to increased net spreads as a result of higher investment yields partially offset by increased realized capital losses and lower volumes due to the continued runoff of the business.

2005 and 2004 Comparison

The Domestic Retirement Services businesses faced a challenging environment in 2005, as deposits declined approximately 18 percent from 2004. The decrease in AIG's individual variable annuity product sales in 2005 was largely attributable to significant variable annuity sales declines at several of AIG's largest distribution firms due to lackluster equity markets, more intense industry competition with regard to living benefit product features and heightened compliance procedures over selling practices. AIG's introduction of more competitive guaranteed minimum withdrawal features was delayed until late in the fourth quarter of 2005 due to filing delays associated with the restatements. During 2005, the interest yield curve flattened and, as a result, competing bank products such as certificates of deposit and other

money market instruments with shorter durations than AIG's individual fixed annuity products became more attractive.

Total Domestic Retirement Services operating income for 2005 of $2.2 billion increased 5 percent compared to 2004 operating income of $2.1 billion. Total revenues for the group retirement products increased 5 percent in 2005 compared to 2004 while operating income increased 7 percent, primarily due to higher variable annuity fee income and lower realized capital losses. Individual fixed annuity total revenues were up 6 percent in 2005 primarily due to an increase in net investment income, partially offset by higher realized capital losses. Operating income for individual fixed annuities increased primarily due to the increase in net investment income from growth in average reserves and higher surrender charges, partially offset by the higher level of realized capital losses. Individual variable annuities total revenues were up 9 percent in 2005, primarily driven by higher variable annuity fees resulting from the increase in the equity markets in the fourth quarter of 2004 and an increase in realized capital gains. The 7 percent growth in individual variable annuities income was consistent with the overall growth in reserves. In 2005, the individual annuities runoff operating income increased $22 million even though the underlying reserves decreased. The higher income in 2005 was due to lower interest crediting rates and lower DAC amortization due to lower surrenders.

Domestic Retirement Services Supplemental Data

The following table presents deposits for 2006, 2005 and 2004:

(in millions)	**2006**	2005	2004
Group retirement products:			
Annuities	**$ 5,464**	$ 5,532	$ 5,555
Mutual funds	**1,361**	904	947
Individual fixed annuities	**5,330**	6,861	9,713
Individual variable annuities	**4,266**	3,319	4,126
Individual fixed annuities — runoff	**56**	67	77
Total	**$16,477**	$16,683	$20,418

The following table presents the amount of reserves by surrender charge category as of December 31, 2006:

(in millions)	Group Retirement Products*	Individual Fixed Annuities	Individual Variable Annuities
Zero or no surrender charge	$42,741	$10,187	$11,467
0% — 2%	6,921	4,503	4,869
Greater than 2% — 4%	4,573	6,422	4,830
Greater than 4%	2,842	28,109	9,836
Non-Surrenderable	877	3,464	91
Total	$57,954	$52,685	$31,093

** Excludes mutual funds.*

In 2006, surrender rates increased for individual fixed annuities, group retirement products and individual variable annuities. The increase in surrender rate for fixed annuities continues to be driven by the shape of the yield curve and general aging of the in-force block; however, less than 20 percent of the individual fixed annuity reserves as of December 31, 2006 were available to be surrendered without charge. Surrender rates for group retirement products increased only slightly as a result of successful retention efforts. In 2006, new products were introduced to retain assets and AIG has retained or attracted over $1 billion in assets. Individual variable annuity surrender rates for 2006 primarily reflect higher shock-lapses that occur following expiration of the surrender charge period on certain 3-year and 7-year contracts, although the trend moderated during the year. Reflecting a widespread industry phenomenon, this lapse rate, much of which was anticipated when the products were issued, has recently been affected by investor demand to exchange existing policies for new-generation contracts with living benefits or lower fees. In addition, the high lapse rates are in part due to the surrenders within certain acquired blocks of business.

A further increase in the level of surrenders in any of these businesses or in the individual fixed annuities runoff block could accelerate the amortization of DAC and negatively affect fee income earned on assets under management.

The following table presents the net flows by line of business for 2006, 2005 and 2004:

	Net Flows[a]		
(in millions)	**2006**	2005	2004
Group retirement products[b]	**$ 467**	$ 628	$ 1,706
Individual fixed annuities	**(2,697)**	1,288	5,936
Individual variable annuities	**(114)**	(336)	1,145
Individual fixed annuities — runoff	**(1,009)**	(818)	(714)
Total	**$(3,353)**	$ 762	$ 8,073

(a) Net flows are defined as deposits received less benefits, surrenders, withdrawals and death benefits.

(b) Includes mutual funds.

The combination of lower deposits and higher surrenders in the individual fixed annuity and individual fixed annuity-runoff blocks, which include closed blocks of business from acquired companies or terminated distribution relationships, resulted in negative net flows for 2006. The continuation of the current interest rate and competitive environment could prolong this trend.

Life Insurance & Retirement Services Net Investment Income and Realized Capital Gains (Losses)

The following table summarizes the components of net investment income for 2006, 2005 and 2004:

(in millions)	**2006**	2005	2004
Domestic			
Fixed maturities, including short term investments	**$ 9,089**	$ 9,060	$ 8,646
Equity securities	**32**	10	27
Interest on mortgage, policy and collateral loans	**798**	728	669
Partnership income — excluding Synfuels	**505**	359	293
Partnership income (loss) — Synfuels	**(107)**	(143)	(121)
Unit investment trusts	**5**	—	—
Other[a]	**49**	56	(20)
Total investment income	**10,371**	10,070	9,494
Investment expenses	**105**	111	59
Net investment income	**$10,266**	$ 9,959	$ 9,435
Foreign			
Fixed maturities, including short term investments	**$ 6,845**	$ 5,995	$ 5,002
Equity securities	**339**	300	182
Interest on mortgage, policy and collateral loans	**455**	448	426
Partnership income	**94**	57	20
Unit investment trusts[b]	**310**	—	—
Other[a]	**312**	423	237
Total investment income before policyholder trading gains (losses)	**8,355**	7,223	5,867
Policyholder trading gains (losses)[c]	**1,053**	1,177	196
Total investment income	**9,408**	8,400	6,063
Investment expenses	**235**	225	229
Net investment income	**$ 9,173**	$ 8,175	$ 5,834
Total			
Fixed maturities, including short term investments	**$15,934**	$15,055	$13,648
Equity securities	**371**	310	209
Interest on mortgage, policy and collateral loans	**1,253**	1,176	1,095
Partnership income — excluding Synfuels	**599**	416	313
Partnership income (loss) — Synfuels	**(107)**	(143)	(121)
Unit investment trusts[b]	**315**	—	—
Other[a]	**361**[c]	479	217
Total investment income before policyholder trading gains (losses)	**$18,726**	$17,293	$15,361
Policyholder trading gains (losses)[c]	**1,053**	1,177	196
Total investment income	**19,779**	18,470	15,557
Investment expenses	**340**	336	288
Net investment income[d]	**$19,439**	$18,134	$15,269

(a) Other net investment income includes real estate income, income on non-partnership invested assets, securities lending and Life Insurance & Retirement Services' equal share of the results of AIG Credit Card Company (Taiwan).

(b) Includes the effect of out of period adjustments relating to the accounting for certain interests in unit investment trusts. For 2006, the effect was an increase of $240 million.

(c) Relates principally to assets held in various trading securities accounts that do not qualify for separate account treatment under SOP 03-1. These amounts are offset by an equal change included in incurred policy losses and benefits.

(d) Includes call and tender income.

The following table summarizes Domestic Life Insurance & Retirement Services partnership income (losses) by sub-product line for 2006, 2005 and 2004:

(in millions)	**2006**	2005	2004
Domestic Life — excluding Synfuels:			
Life insurance	**$ 67**	$ 136	$ 43
Home service	**13**	(1)	8
Subtotal	**80**	135	51
Domestic Life — Synfuels:			
Life insurance	**(73)**	(97)	(74)
Home service	**(34)**	(46)	(47)
Subtotal	**(107)**	(143)	(121)
Total Domestic Life	**(27)**	(8)	(70)
Retirement Services:			
Group retirement products	**178**	89	95
Individual fixed annuities	**247**	135	147
Total Retirement Services	**425**	224	242
Total	**$ 398**	$ 216	$ 172

2006 and 2005 Comparison

Net investment income increased 7 percent for 2006 compared to 2005 as income from fixed maturity and equity securities increased as levels of invested assets grew. Net investment income in 2006 also included out of period adjustments relating to the accounting for certain interests in unit investment trusts of $240 million. Partially offsetting this growth were lower policyholder trading gains (losses) in 2006. Net Investment income for certain operations include investments in structured notes linked to emerging market sovereign debt that incorporates both interest rate risk and currency risk. In addition, period to period comparisons of investment income for some lines of business are affected by yield enhancement activity, particularly partnership income as shown in the above table. See also Insurance and Asset Management Invested Assets herein.

AIG generates income tax credits as a result of investing in synthetic fuel production (synfuels) related to the investment loss shown in the above table and records those benefits in its provision for income taxes. The amounts of those income tax credits were $127 million, $203 million and $160 million for 2006, 2005 and 2004, respectively. For a further discussion of the effect of fluctuating domestic crude oil prices on synfuel tax credits, see Note 12(c) of Notes to Consolidated Financial Statements.

2005 and 2004 Comparison

The growth in net investment income in 2005 compared to 2004 reflects growth in general account reserves and surplus for both Foreign and Domestic Life Insurance & Retirement Services companies. Also, net investment income was positively affected by the compounding of previously earned and reinvested net investment income along with the addition of new cash flow from operations available for investment. The global flattening of the yield curve put additional pressure on yields and spreads, which was partially offset with income generated from other investment sources, including income from partnerships.

The following table summarizes realized capital gains (losses) by major category for 2006, 2005 and 2004:

(in millions)	**2006**	2005	2004
Domestic Life Insurance:			
Sales of fixed maturities	**$ (33)**	$ 65	$ (4)
Sales of equity securities	**17**	18	7
Other:			
Foreign exchange transactions	**(6)**	11	—
Derivatives instruments	**25**	65	8
Other-than-temporary decline	**(192)**	(119)	(98)
Other	**(26)**	(5)	(33)
Total Domestic Life Insurance	**$(215)**	$ 35	$(120)
Domestic Retirement Services:			
Sales of fixed maturities	**$ 1**	$(106)	$ 107
Sales of equity securities	**31**	115	30
Other:			
Foreign exchange transactions	**(13)**	—	—
Derivatives instruments	**(33)**	(12)	(14)
Other-than-temporary decline	**(368)**	(267)	(305)
Other	**(22)**	(7)	(25)
Total Domestic Retirement Services	**$(404)**	$(277)	$(207)
Foreign Life Insurance & Retirement Services:			
Sales of fixed maturities	**$(209)**	$ 191	$ 223
Sales of equity securities	**459**	281	295
Other:			
Foreign exchange transactions	**106**	40	(382)
Derivatives instruments	**276**	(599)	248
Other-than-temporary decline	**(81)**	(39)	(38)
Other*	**156**	210	26
Total Foreign Life Insurance & Retirement Services	**$ 707**	$ 84	$ 372
Total	**$ 88**	$(158)	$ 45

** Net of allocations to participating policyholders of $88 million, $109 million and $65 million for 2006, 2005 and 2004, respectively.*

Realized capital gains (losses) include normal portfolio transactions as well as derivative gains (losses) for transactions that did not qualify for hedge accounting treatment under FAS 133, transactional foreign exchange gains and losses and other-than-temporary declines in the value of investments. Realized capital gains (losses) for derivatives in Foreign Life Insurance & Retirement Services are related primarily to hedging of fixed income instruments denominated in a currency other than the functional currency of the respective country to such functional currency. The related currency gain or loss of the available for sale fixed income instrument is deferred until the date of the sale.

Deferred Policy Acquisition Costs

DAC for Life Insurance & Retirement Services products arises from the deferral of those costs that vary with, and are directly related to, the acquisition of new or renewal business. Policy acquisition costs for life insurance products are generally deferred and amortized over the premium paying period of the policy. Policy acquisition costs that relate to universal life and investment-type products, including variable and fixed annuities (investment-oriented products), are deferred and amortized, with interest, as appropriate, in relation to the historical and future incidence of estimated gross profits to be realized over the estimated lives of the contracts. Total acquisition costs deferred increased $310 million over 2005 and were generally in line with growth in new business. Total DAC amortization expense, excluding VOBA, grew $432 million over 2005 with each year's amortization expense level at approximately 14 percent of the opening DAC balance. Amortization expense includes the effects of current period realized capital gains and losses for investment type products. With respect to investment-oriented products, AIG's policy is to adjust amortization assumptions for DAC when estimates of current or future gross profits to be realized from these contracts are revised. With respect to variable annuities sold domestically (representing the vast majority of AIG's variable annuity business), the assumption for the long-term annual net growth rate of the equity markets used in the determination of DAC amortization is approximately ten percent. A methodology referred to as ''reversion to the mean'' is used to maintain this long-term net growth rate assumption, while giving consideration to short-term variations in equity markets. Estimated gross profits include investment income and gains and losses less interest required on policyholder reserves, as well as other charges in the contract less actual mortality and expenses. Current experience and changes in the expected future gross profits are analyzed to determine the effect on the amortization of DAC. The projection of estimated gross profits requires significant management judgment. The assumptions with respect to the current and projected gross profits are reviewed and analyzed quarterly and are adjusted accordingly.

The following table summarizes the major components of the changes in DAC and Value of Business Acquired (VOBA) for 2006 and 2005:

	2006			2005		
(in millions)	DAC	VOBA	Total	DAC	VOBA	Total
Domestic Life Insurance & Retirement Services:						
Balance at beginning of year[(a)]	**$ 9,599**	**$ 869**	**$10,468**	$ 8,214	$ 836	$ 9,050
Acquisition costs deferred	**1,832**	**—**	**1,832**	1,840	—	1,840
Amortization (charged) or credited to operating income:						
Related to realized capital gains (losses)	**77**	**16**	**93**	45	3	48
Related to unlocking future assumptions	**(40)**	**(5)**	**(45)**	(15)	—	(15)
All other amortization[(b)]	**(1,387)**	**(81)**	**(1,468)**	(1,399)	(85)	(1,484)
Related to change in unrealized gains (losses) on securities	**744**	**34**	**778**	904	112	1,016
Increase (decrease) due to foreign exchange	**(1)**	**—**	**(1)**	10	3	13
Balance at end of year	**$10,824**	**$ 833**	**$11,657**	$ 9,599	$ 869	$10,468
Foreign Life Insurance & Retirement Services:						
Balance at beginning of year[(a)]	**$16,360**	**$1,278**	**$17,638**	$14,349	$1,681	$16,030
Acquisition costs deferred	**4,991**	**—**	**4,991**	4,673	—	4,673
Amortization (charged) or credited to operating income:						
Related to realized capital gains (losses)	**4**	**1**	**5**	(1)	(1)	(2)
Related to unlocking future assumptions	**87**	**15**	**102**	93	—	93
All other amortization	**(2,214)**	**(185)**	**(2,399)**	(1,764)	(204)	(1,968)
Related to change in unrealized gains (losses) on securities	**(127)**	**(5)**	**(132)**	(47)	8	(39)
Increase (decrease) due to foreign exchange	**904**	**44**	**948**	(943)	(206)	(1,149)
Balance at end of year	**$20,005**	**$1,148**	**$21,153**	$16,360	$1,278	$17,638
Total Life Insurance & Retirement Services:						
Balance at beginning of year[(a)]	**$25,959**	**$2,147**	**$28,106**	$22,563	$2,517	$25,080
Acquisition costs deferred	**6,823**	**—**	**6,823**	6,513	—	6,513
Amortization (charged) or credited to operating income:						
Related to realized capital gains (losses)	**81**	**17**	**98**	44	2	46
Related to unlocking future assumptions	**47**	**10**	**57**	78	—	78
All other amortization	**(3,601)**	**(266)**	**(3,867)**	(3,163)	(289)	(3,452)
Related to change in unrealized gains (losses) on securities	**617**	**29**	**646**	857	120	977
Increase (decrease) due to foreign exchange	**903**	**44**	**947**	(933)	(203)	(1,136)
Balance at end of year	**$30,829**	**$1,981**	**$32,810**	$25,959	$2,147	$28,106

(a) In 2006, sales inducement assets were reclassified to Other assets in the consolidated balance sheet. All periods have been adjusted to reflect this reclassification.

(b) In 2006, all other amortization for Domestic Life Insurance & Retirement Services includes $136 million of negative amortization related to changes in estimates from conversion of actuarial systems, which is substantially offset by related adjustments in incurred policy losses and benefits in the consolidated statement of income.

AIG's variable annuity earnings will be affected by changes in market returns because separate account revenues, primarily composed of mortality and expense charges and asset management fees, are a function of asset values.

DAC for both insurance-oriented and investment-oriented products as well as retirement services products is reviewed for recoverability, which involves estimating the future profitability of current business. This review also involves significant management judgment. If the actual emergence of future profitability were to be substantially lower than estimated, AIG's results of operations could be significantly affected in future periods.

Financial Services Operations

AIG's Financial Services subsidiaries engage in diversified activities including aircraft and equipment leasing, capital markets, consumer finance and insurance premium finance.

Financial Services Results

Financial Services results for 2006, 2005 and 2004 were as follows:

(in millions)	**2006**	2005	2004
Revenues[(a)]:			
Aircraft Leasing[(b)]	**$ 4,143**	$ 3,578	$ 3,136
Capital Markets[(c)(d)]	**(186)**	3,260	1,278
Consumer Finance[(e)]	**3,819**	3,613	2,978
Other	**234**	74	103
Total	**$ 8,010**	$ 10,525	$ 7,495
Operating income (loss)[(a)]:			
Aircraft Leasing	**$ 639**	$ 679	$ 642
Capital Markets[(d)]	**(873)**	2,661	662
Consumer Finance[(f)]	**761**	876	786
Other, including intercompany adjustments[(g)]	**(3)**	60	90
Total	**$ 524**	$ 4,276	$ 2,180

(a) Includes the effect of hedging activities that did not qualify for hedge accounting treatment under FAS 133, including the related foreign exchange gains and losses. For 2006, 2005 and 2004, respectively, the effect was $(1.8) billion, $2.0 billion and $(122) million in both revenues and operating income for Capital Markets. These amounts result primarily from interest rate and foreign currency derivatives that are economically hedging available for sale securities and borrowings. For 2004, the effect was $(27) million in operating income for Aircraft Leasing. During 2006 and 2005, Aircraft Leasing derivative gains and losses were reported as part of AIG's Other category, and were not reported in Aircraft Leasing operating income.

(b) Revenues are primarily aircraft lease rentals from ILFC.

(c) Revenues, shown net of interest expense of $3.2 billion, $3.0 billion and $2.3 billion, in 2006, 2005 and 2004, respectively, were primarily from hedged financial positions entered into in connection with counterparty transactions and the effect of hedging activities that did not qualify for hedge accounting treatment under FAS 133 described in (a) above.

(d) Certain transactions entered into by AIGFP generate tax credits and benefits which are included in income taxes in the consolidated statement of income. The amounts of such tax credits and benefits for the years ended December 31, 2006, 2005 and 2004, respectively, are $50 million, $67 million and $107 million.

(e) Revenues are primarily finance charges.

(f) Includes catastrophe-related losses of $62 million recorded in the third quarter of 2005 resulting from hurricane Katrina, which were reduced by $35 million in 2006 due to the reevaluation of the remaining estimated losses.

(g) Includes specific reserves recorded during 2006 in the amount of $42 million related to two commercial lending transactions.

Financial Services operating income decreased in 2006 compared to 2005 and increased in 2005 compared to 2004, due primarily to the effect of hedging activities that did not qualify for hedge accounting under FAS 133. AIG is reinstituting hedge accounting in the first quarter of 2007 for AIGFP and later in 2007 for the balance of the Financial Services operations.

Aircraft Leasing

AIG's Aircraft Leasing operations represent the operations of ILFC, which generates its revenues primarily from leasing new and used commercial jet aircraft to foreign and domestic airlines. Revenues also result from the remarketing of commercial jets for ILFC's own account, and remarketing and fleet management services for airlines and financial institutions. ILFC finances its purchases of aircraft primarily through the issuance of a variety of debt instruments. The composite borrowing rates at December 31, 2006 and 2005 were 5.17 percent and 4.61 percent, respectively. The composite borrowing rates did not reflect the benefit of economically hedging ILFC's floating rate and foreign currency denominated debt using interest rate and foreign currency derivatives. These derivatives are effective economic hedges; however, since hedge accounting under FAS 133 was not applied, the benefits of using derivatives to hedge these exposures were not reflected in ILFC's borrowing rates.

ILFC's sources of revenue are principally from scheduled and charter airlines and companies associated with the airline industry. The airline industry is sensitive to changes in economic conditions and is cyclical and highly competitive. Airlines and related companies may be affected by political or economic instability, terrorist activities, changes in national policy, competitive pressures on certain air carriers, fuel prices and shortages, labor stoppages, insurance costs, recessions, world health issues and other political or economic events adversely affecting world or regional trading markets.

ILFC is exposed to operating loss and liquidity strain through nonperformance of aircraft lessees, through owning aircraft which it would be unable to sell or re-lease at acceptable rates at lease expiration and, in part, through committing to purchase aircraft which it would be unable to lease.

ILFC's revenues and operating income may be adversely affected by the volatile competitive environment in which its customers operate. ILFC manages the risk of nonperformance by its lessees with security deposit requirements, repossession rights, overhaul requirements and close monitoring of industry conditions through its marketing force. However, there can be no assurance that ILFC would be able to successfully manage the risks relating to the effect of possible future deterioration in the airline industry. Approximately 90 percent of ILFC's fleet is leased to non-U.S. carriers, and the fleet, comprised of the most efficient aircraft in the airline industry, continues to be in high demand from such carriers.

ILFC typically contracts to re-lease aircraft before the end of the existing lease term. For aircraft returned before the end of the lease term, ILFC has generally been able to re-lease such aircraft within two to six months of its return. As a lessor, ILFC considers an aircraft ''idle'' or ''off lease'' when the aircraft is not subject to a signed lease agreement or signed letter of intent. ILFC had one aircraft off lease at December 31, 2006, and all new aircraft scheduled for delivery through 2007 have been leased.

Management formally reviews regularly, and no less frequently than quarterly, issues affecting ILFC's fleet, including events and circumstances that may cause impairment of aircraft values. Management evaluates aircraft in the fleet as necessary based on

these events and circumstances in accordance with Statement of Financial Accounting Standards No. 144, ''Accounting for the Impairment or Disposal of Long-Lived Assets'' (FAS 144). ILFC has not recognized any impairment related to its fleet in 2006, 2005 and 2004. ILFC has been able to re-lease the aircraft without diminution in lease rates that would result in an impairment under FAS 144.

Aircraft Leasing Results

2006 and 2005 Comparison

ILFC's operating income decreased in 2006 compared to 2005 by $40 million, or 6 percent. Rental revenues increased by $536 million or 16 percent, driven by a larger aircraft fleet, increased utilization and higher lease rates. During 2006, ILFC's fleet subject to operating leases increased by 78 airplanes to a total of 824. The increase in rental revenues was offset in part by increases in depreciation expense and interest expense, charges related to bankrupt airlines, as well as the settlement of a tax dispute in Australia related to the restructuring of ownership of aircraft. Depreciation expense increased by $200 million, or 14 percent, in line with the increase in the size of the aircraft fleet. Interest expense increased by $317 million, or 28 percent, driven by rising cost of funds, a weaker U.S. dollar against the Euro and the British Pound and additional borrowings funding aircraft purchases. As noted above, ILFC's interest expense did not reflect the benefit of hedging these exposures. Gains or losses on derivatives for ILFC are reported in AIG's Other category.

2005 and 2004 Comparison

ILFC's operating income increased in 2005 compared to 2004 by $37 million, or 6 percent. Rental revenues increased by $499 million, or 17 percent, driven by a larger aircraft fleet and increased utilization. During 2005, ILFC's fleet subject to operating leases increased by 79 airplanes to a total of 746. The increase in rental revenues was offset in part by increases in depreciation expense, interest expense, leasing-related costs and other reserves. Depreciation expense increased by $111 million, or 9 percent, in line with the increase in the size of the aircraft fleet. Interest expense increased by $132 million, or 13 percent, driven by rising cost of funds and additional borrowings funding aircraft purchases.

Capital Markets

Capital Markets represents the operations of AIGFP, which engages as principal in a wide variety of financial transactions, including standard and customized financial products involving commodities, credit, currencies, energy, equities and rates. AIGFP also invests in a diversified portfolio of securities and principal investments and engages in borrowing activities involving issuing standard and structured notes and other securities, and entering into GIAs.

As Capital Markets is a transaction-oriented operation, current and past revenues and operating results may not provide a basis for predicting future performance. AIG's Capital Markets operations derive substantially all their revenues from hedged financial positions entered into in connection with counterparty transactions rather than from speculative transactions. AIGFP also participates as a dealer in a wide variety of financial derivatives transactions. AIGFP economically hedges the market risks arising from its transactions, although hedge accounting under FAS 133 was not being applied during 2006, 2005 and 2004 to any of the derivatives and related assets and liabilities. Accordingly, revenues and operating income were exposed to volatility resulting from differences in the timing of revenue recognition between the derivatives and the hedged assets and liabilities. Revenues and operating income of the Capital Markets operations and the percentage change in these amounts for any given period are also significantly affected by the number, size and profitability of transactions entered into by these subsidiaries during that period relative to those entered into during the prior period. Generally, the realization of transaction revenues as measured by the receipt of funds is not a significant reporting event as the gain or loss on AIGFP's trading transactions is currently reflected in operating income as the fair values change from period to period.

Derivative transactions are entered into in the ordinary course of AIGFP operations. Derivatives are recorded at fair value, determined by reference to the mark to market value of the derivative or their estimated fair value where market prices are not readily available. The resulting aggregate unrealized gains or losses from the derivatives are reflected in the consolidated income statement. Where AIGFP cannot verify significant model inputs to observable market data and cannot verify the model value to market transactions, AIGFP values the contract at the transaction price at inception and, consequently, records no initial gain or loss in accordance with Emerging Issues Task Force Issue No. 02-03, ''Issues Involved in Accounting for Derivative Contracts Held for Trading Purposes and Contracts Involved in Energy Trading and Risk Management Activities'' (EITF 02-03). Such initial gain or loss is recognized over the life of the transaction. AIGFP periodically reevaluates its revenue recognition under EITF 02-03 based on the observability of market parameters. The mark to fair value of derivative transactions is reflected in the consolidated balance sheet in the captions ''Unrealized gain on swaps, options and forward transactions'' and ''Unrealized loss on swaps, options and forward transactions.'' Unrealized gains represent the present value of the aggregate of each net receivable, by counterparty, and the unrealized losses represent the present value of the aggregate of each net payable, by counterparty, as of December 31, 2006. These amounts will change from one period to the next due to changes in interest rates, currency rates, equity and commodity prices and other market variables, as well as cash movements, execution of new transactions and the maturing of existing transactions.

Spread income on investments and borrowings is recorded on an accrual basis over the life of the transaction. Investments are classified as securities available for sale and are carried at fair value with the resulting unrealized gains or losses reflected in accumulated other comprehensive income. U.S. dollar denominated borrowings are carried at cost, while borrowings in any currency other than the U.S. dollar result in unrealized foreign

exchange gains or losses reported in income. AIGFP hedges the economic exposure on its investments and borrowings on a portfolio basis using derivatives and other financial instruments. While these hedges are highly effective economic hedges, they did not qualify for hedge accounting treatment under FAS 133 through 2006. The change in the fair value of the derivatives used to hedge these economic exposures is therefore included in Other income, while the offsetting change in fair value of the hedged investments and borrowings is not recognized in income. AIG is reinstituting hedge accounting in the first quarter of 2007 for AIGFP.

To the extent the Financial Services subsidiaries, other than AIGFP, use derivatives to economically hedge their assets or liabilities with respect to their future cash flows, and such hedges did not qualify for hedge accounting treatment under FAS 133, the changes in fair value of such derivatives were recorded in realized capital gains (losses) or other income. Amounts recorded in realized capital gains (losses) are reported as part of AIG's Other category.

Capital Markets Results

2006 and 2005 Comparison

Capital Markets operating income in 2006 decreased by $3.53 billion compared to 2005. Improved results, primarily from increased transaction flow in AIGFP's credit, commodity index, energy and equity products, were more than offset by the loss resulting from the effect of derivatives not qualifying for hedge accounting treatment under FAS 133. This loss was $1.82 billion in 2006 compared to a gain of $2.01 billion in 2005, a decrease of $3.83 billion. A large part of the net loss on AIGFP's derivatives recognized in 2006 was due to the weakening of the U.S. dollar, primarily against the British Pound and Euro, resulting in a decrease in the fair value of the foreign currency derivatives hedging AIGFP's available for sale securities. The majority of the net gain on AIGFP's derivatives in 2005 was due to the strengthening of the U.S. dollar, primarily against the British Pound and Euro, which increased the fair value of the foreign currency derivatives hedging available for sale securities. To a lesser extent, the net gain in 2005 was due to the decrease in long-term U.S. interest rates, which increased the fair value of derivatives hedging AIGFP's assets and liabilities.

Financial market conditions in 2006 were characterized by a general flattening of interest rate yield curves across fixed income markets globally, tightening of credit spreads, higher equity valuations and a weaker U.S. dollar.

The most significant component of Capital Markets operating expenses is compensation, which was approximately $544 million, $481 million and $497 million in 2006, 2005 and 2004, respectively. The amount of compensation was not affected by gains and losses arising from derivatives not qualifying for hedge accounting treatment under FAS 133.

AIG elected to early adopt FAS 155, ''Accounting for Certain Hybrid Financial Instruments'' (FAS 155), in 2006 and AIGFP elected to apply the fair value option to its structured notes and other financial liabilities containing embedded derivatives outstanding as of January 1, 2006. The cumulative effect of the adoption of FAS 155 on these instruments at January 1, 2006 was a pre-tax loss of $29 million. The effect of these hybrid financial instruments reflected in AIGFP's operating income in 2006 was a pretax loss of $287 million, largely offset by gains on economic hedge positions also reflected in AIGFP's operating income.

2005 and 2004 Comparison

Capital Markets operating income in 2005 increased by $2 billion compared to 2004, primarily due to a gain related to derivatives not qualifying for hedge accounting treatment of $2.01 billion in 2005 compared to a loss of $122 million in 2004. The majority of the net gain on AIGFP's derivatives recognized in 2005 was due to the strengthening of the U.S. dollar against the Euro and British Pound, which resulted in an increase in the fair value of the foreign currency derivatives hedging available for sale securities. To a lesser extent, the net gain was also due to the fall in long-term U.S. interest rates, which resulted in an increase in the fair value of AIGFP's interest rate derivatives hedging its assets and liabilities. The majority of the net loss on AIGFP's derivatives recognized in 2004 was due to the weakening of the U.S. dollar against the Euro and British Pound, which resulted in a decrease in the fair value of the foreign currency derivatives hedging available for sale securities. This loss was partially offset by an increase in the fair value of its interest rate derivatives hedging its assets and liabilities as a result of the decrease in long-term U.S. interest rates.

Financial market conditions in 2005 compared to 2004 were characterized by a general flattening of interest rate yield curves across fixed income markets globally, some tightening of credit spreads, higher equity valuations and a stronger U.S. dollar. AIGFP's 2005 results were adversely affected by customer uncertainty surrounding the negative actions of the rating agencies and the investigations, as well as the negative effect on its structured notes business of AIG being unable to fully access the capital markets during 2005.

Capital Markets operating income was also negatively affected in 2004 by the costs of the PNC settlement.

Consumer Finance

AIG's consumer finance operations in North America are principally conducted through AGF. Effective January 2, 2007, AGF expanded its operations into the United Kingdom through the acquisition of Ocean Finance and Mortgages Limited, a finance broker for home owner loans in the United Kingdom. AGF derives a substantial portion of its revenues from finance charges assessed on outstanding real estate loans, secured and unsecured non-real estate loans and retail sales finance receivables. The real estate loans are comprised principally of first lien and some second lien mortgages on residential real estate generally having a maximum term of 360 months, and are considered nonconforming. The real estate loans may be closed-end accounts or open-end home equity lines of credit and may be fixed rate or adjustable rate products. AGF does not offer mortgage products

with borrower payment options that allow for negative amortization of the principal balance. The secured non-real estate loans are secured by consumer goods, automobiles or other personal property. Both secured and unsecured non-real estate loans and retail sales finance receivables generally have a maximum term of 60 months. The core of AGF's originations is sourced through its branches. However, a significant volume of real estate loans is also originated through broker relationships, and to lesser extents, through correspondent relationships and direct mail solicitations. In the first quarter of 2006, two wholly owned subsidiaries of AGF discontinued originating real estate loans through an arrangement with AIG Federal Savings Bank, a federally chartered thrift, and began originating such loans under their own state licenses.

AIG's foreign consumer finance operations are principally conducted through AIGCFG. AIGCFG operates primarily in emerging and developing markets. AIGCFG has operations in Argentina, China, Hong Kong, Mexico, Philippines, Poland, Taiwan and Thailand. Certain of the AIGCFG operations are owned in part or in whole by Life Insurance subsidiaries. Accordingly, the financial results of those companies are shared between Financial Services and Life Insurance & Retirement Services according to their ownership percentages. While products vary by market, the businesses generally provide credit cards, unsecured and secured non-real estate loans, term deposits, savings accounts, retail sales finance and real estate loans. AIGCFG originates finance receivables through its branches and direct solicitation. AIGCFG also originates finance receivables indirectly through relationships with retailers, auto dealers, and independent agents.

Consumer Finance Results

2006 and 2005 Comparison

Consumer Finance operating income decreased to $761 million, or 13 percent, in 2006 compared to 2005. Operating income from domestic consumer finance operations declined as a result of decreased originations and purchases of real estate loans and margin compression resulting from increased interest rates and flattened yield curves. The foreign operations operating income decreased primarily due to the credit deterioration in the Taiwan credit card market.

Domestically, the U.S. housing market deteriorated throughout 2006 and ended the year fairly weak compared to recent years. As a result, the real estate loan portfolio decreased slightly during 2006 due to lower refinancing activity. This lower refinancing activity also caused a significant decrease in originations and whole loan sales in AGF's mortgage banking operation, which resulted in a substantial reduction of revenue and operating income compared to the prior year. However, softening home prices (reducing the equity customers are able to extract from their homes when refinancing) and higher mortgage rates contributed to customers utilizing non-real estate loans, which increased 10 percent compared to 2005. Retail sales finance receivables also increased 23 percent due to increased marketing efforts and customer demand. Higher revenue resulting from portfolio growth was more than offset by higher interest expense. AGF's short-term borrowing rates were 5.14 percent in 2006 compared to 3.58 percent in 2005. AGF's long-term borrowing rates were 5.05 percent in 2006 compared to 4.41 percent in 2005. AGF's net charge-off ratio improved to 0.95 percent in 2006 from 1.19 percent in 2005. The improvement in the net charge-off ratio in 2006 was primarily due to positive economic fundamentals. The U.S. economy continued to expand during the year, and the unemployment rate remained low, which improved the credit quality of AGF's portfolio. AGF's delinquency ratio remained relatively low, although it increased to 2.06 percent at December 31, 2006 from 1.93 percent at December 31, 2005. AGF reduced the hurricane Katrina portion of its allowance for finance receivable losses to $15 million at December 31, 2006 after the reevaluation of its remaining estimated losses. AGF's allowance ratio was 2.01 percent at December 31, 2006 compared to 2.20 percent at December 31, 2005.

Revenues from the foreign consumer finance operations increased by approximately 19 percent in 2006 compared to 2005. Loan growth, particularly in Poland and Argentina, was the primary driver behind the higher revenues. Higher revenues were more than offset, however, by AIGCFG's $47 million share of the allowance for losses related to industry-wide credit deterioration in the Taiwan credit card market, increased cost of funds, and higher operating expenses in connection with expansion into new markets and distribution channels and new product promotions, resulting in lower operating income for 2006 compared to 2005.

2005 and 2004 Comparison

Revenues and operating income from the Consumer Finance operations improved in 2005, both domestically and internationally.

Domestically, the relatively low interest rate environment contributed to a high level of mortgage refinancing activity. AGF's real estate loans increased 21 percent during 2005 compared to 2004. AGF's short-term borrowing rates rose to 3.58 percent in 2005 compared to 2.68 percent in 2004. AGF's long-term borrowing rates were 4.41 percent in 2005 compared to 4.28 percent in 2004. Despite high energy costs, the U.S. economy continued to expand during 2005, improving consumer credit quality. Both AGF's net charge-off ratio and delinquency ratio improved in 2005 compared to 2004. AGF's net charge-off ratio improved to 1.19 percent in 2005 from 1.60 percent in 2004. The improvement in the net charge-off ratio in 2005 was primarily due to the improving economy and a higher proportion of average net receivables that were real estate loans. AGF's delinquency ratio at December 31, 2005 was 1.93 percent compared to 2.31 percent at December 31, 2004. However, AGF incurred charges of approximately $62 million for the estimated effect of hurricane Katrina on customers in the Gulf Coast areas affected by the storm. At December 31, 2005, AGF's allowance ratio was 2.20 percent compared to 2.26 percent at December 31, 2004.

Foreign consumer finance operations performed well, as the operations in Poland and Argentina recorded improved growth in operating income. The Hong Kong businesses experienced improved loan and earnings growth in a strengthening economy.

Asset Management Operations

AIG's Asset Management operations comprise a wide variety of investment-related services and investment products. Such services and products are offered to individuals and institutions both domestically and overseas, and are primarily comprised of Spread-Based Investment Businesses, Institutional Asset Management and Brokerage Services and Mutual Funds.

The revenues and operating income for this segment are subject to variability because they are affected by the general conditions in the equity and credit markets. In addition, realized gains and performance fees are contingent upon various fund closings, maturity levels and market conditions.

Spread-Based Investment Business

In prior years, the sale of GICs to investors, both domestically and overseas, was AIG's primary institutional Spread-Based Investment Business. During 2005, AIG launched its MIP and its asset management subsidiaries, primarily SunAmerica Life, ceased writing new GIC business. The GIC business will continue to run off for the foreseeable future while the MIP business is expected to grow.

Institutional Asset Management

AIG's Institutional Asset Management business provides an array of investment products and services globally to institutional investors, AIG subsidiaries and affiliates and high net worth investors. These products and services include traditional equity and fixed income investment management and a full range of alternative asset classes. Delivery of AIG's Institutional Asset Management products and services is accomplished via a global network of operating subsidiaries comprising AIGGIG. The primary operating entities within this group are AIG Global Investment Corp., AIG Global Real Estate Investment Corp. and AIG Private Bank. AIG Private Bank offers banking, trading and investment management services to private client and high net worth individuals and institutions globally.

Within the alternative investment asset class, AIGGIG offers hedge and private equity fund-of-funds, direct investments and distressed debt investments. Within the structured fixed income and equity product asset class, AIGGIG offers various forms of structured and credit linked notes, various forms of collateralized debt obligations and other investment strategies aimed at achieving superior returns or capital preservation. In addition, Institutional Asset Management's product offerings include various forms of principal protected and liability management structures.

Brokerage Services and Mutual Funds

AIG's Brokerage Services and Mutual Funds business provides mutual fund and broker-dealer related services to retail investors, group trusts and corporate accounts through an independent network of financial advisors. The AIG Advisor Group, Inc., a subsidiary of AIG Retirement Services, Inc., is comprised of several broker-dealer entities that provide these services to clients primarily in the U.S. marketplace. SAAMCo manages, advises and/or administers retail mutual funds, as well as the underlying assets of variable annuities sold by AIG SunAmerica and VALIC to individuals and groups throughout the United States.

Other

Included in the Other category for Asset Management is income or loss from partnerships. Partnership assets consist of investments in a diversified portfolio of private equity funds, affordable housing partnerships and hedge fund investments.

Asset Management Results

Asset Management results for 2006, 2005 and 2004 were as follows:

(in millions)	**2006**	2005	2004
Revenues:			
Spread-Based Investment Business	**$3,554**	$3,547	$3,192
Institutional Asset Management	**1,670**	1,195	1,049
Brokerage Services and Mutual Funds	**293**	257	249
Other	**297**	326	224
Total	**$5,814**	$5,325	$4,714
Operating income:			
Spread-Based Investment Business[(a)]	**$ 947**	$1,185	$1,328
Institutional Asset Management[(b)(c)]	**1,031**	686	515
Brokerage Services and Mutual Funds	**87**	66	70
Other	**281**	316	212
Total	**$2,346**	$2,253	$2,125

(a) Includes the effect of hedging activities that did not qualify for hedge accounting treatment under FAS 133, including the related foreign exchange gains and losses. For 2004, the effect was a gain of $313 million in operating income. During 2006 and 2005, these derivative gains and losses were reported as part of AIG's Other category, and were not reported in Asset Management operating income.

(b) Includes the full results of certain AIG managed private equity and real estate funds that are consolidated pursuant to FIN 46(R), ''Consolidation of Variable Interest Entities''. Also includes $346 million, $261 million and $195 million for 2006, 2005 and 2004, respectively, of third-party limited partner earnings offset in minority interest expense on the consolidated statement of income which is not a component of operating income.

(c) Includes the full results of certain AIG managed partnerships that are consolidated effective January 1, 2006 pursuant to EITF 04-5, ''Determining Whether a General Partner, or the General Partners as a Group, Controls a Limited Partnership or Similar Entity When the Limited Partners Have Certain Rights''. For 2006, operating income includes $252 million of third-party limited partner earnings offset in minority interest expense which is not a component of operating income.

2006 and 2005 Comparison

Asset Management operating income increased 4 percent in 2006 compared to 2005 on revenues that increased 9 percent.

Operating income related to the Spread-Based Investment Business declined 20 percent in 2006 compared to 2005 due primarily to the continued runoff of GIC balances and spread compression related to increases in short-term interest rates. A significant portion of the remaining GIC portfolio consists of floating rate obligations. AIG has entered into hedges to manage against increases in short-term interest rates. AIG believes these hedges are economically effective, but they did not qualify for hedge accounting treatment under FAS 133. Income or loss from these hedges are classified as realized capital gains or losses and are included in AIG's Other category. The decline in operating income was partially offset by improved partnership income, particularly during the fourth quarter of 2006. Partnership income is primarily derived from alternative investments and is affected by performance in the equity markets. Thus, revenues, operating income and cash flow attributable to GICs will vary among reporting periods. Commencing with transactions initiated in the first quarter of 2007, AIG is reinstituting hedge accounting for derivative transactions related to the MIP.

During 2005, the MIP replaced the GIC program as AIG's principal spread-based investment activity. While the MIP showed strong growth in operating income, AIG does not expect that the income growth in the MIP will offset the runoff in the GIC portfolio for the foreseeable future, because the asset mix under the MIP does not include the alternative investments utilized in the GIC program.

The MIP was initially launched in the Euromarkets in September 2005 through AIG's $10 billion Euro medium term note program. Through December 31, 2006, AIG has issued the equivalent of $5.3 billion for the MIP in the Euromarkets and the U.S. public and private markets.

Operating income related to Institutional Asset Management increased 50 percent in 2006 to $1.0 billion compared to 2005, primarily due to an increase of $337 million in gains on certain VIEs and partnerships. These gains are offset in minority interest expense, which is not a component of operating income. AIG's unaffiliated client assets under management, including both retail mutual funds and institutional accounts, increased 21 percent from year-end 2005 to $75 billion, resulting in higher management fee income. Increased realized capital gains on real estate investments from 2005 also contributed to the increase in operating income. The growth in Institutional Asset Management revenues and operating income were driven by contributions from all asset classes globally. Partially offsetting this growth were lower performance-based fees on private equity investments, and higher expenses related to the planned expansion of marketing and distribution capabilities, combined with technology and operational infrastructure-related enhancements.

2005 and 2004 Comparison

Asset Management operating income increased in 2005 compared to 2004 as a result of growth in institutional assets under management, and the associated fee revenue, along with strong realized gains on sales of real estate investments and performance fees earned on various private equity investments. The increase in operating income was achieved despite the runoff of the existing GIC portfolio and the delay in the MIP. The decline in GIC operating income compared to 2004 reflects tighter spreads in the GIC portfolio, partially offset by improved partnership returns. Spread compression occurred as the base portfolio yield declined due to an increase in the cost of funds in the short-term floating rate portion of the GIC portfolio, only partially offset by increased investment income from the floating rate assets backing the portfolio.

Other Operations

The operating loss of AIG's Other category for the years ended December 31, 2006, 2005 and 2004 was as follows:

(in millions)	**2006**	2005	2004
Other Operating Income (Loss):			
Equity earnings in unconsolidated entities	**$ 193**	$ (124)	$ 157
Interest expense	**(859)**	(541)	(435)
Unallocated corporate expenses	**(555)**	(413)	(316)
Compensation expense — SICO Plans	**(108)**	(205)	(62)
Compensation expense — Starr tender offer	**(54)**	—	—
Realized capital gains (losses)	**(295)**	505	94
Regulatory settlement costs	**—**	(1,644)	—
Other miscellaneous, net	**(23)**	(113)	—
Total Other	**$(1,701)**	$(2,535)	$ (562)

2006 and 2005 Comparison

Operating loss for AIG's Other category declined to $1.7 billion in 2006 compared to $2.5 billion in 2005, largely due to regulatory settlement costs of $1.6 billion in 2005 as described under Item 3. Legal Proceedings. Interest expense grew in 2006 as a result of increased borrowings by the parent holding company. Unallocated corporate expenses increased $142 million due to increases in general corporate expenses primarily resulting from ongoing efforts to improve internal controls, higher stock compensation expenses and expenses relating to executive departures in 2005 and 2006. AIG expects these compensation expenses to continue to increase as these improvement efforts progress. Operating income in 2006 also includes realized capital losses of $295 million, primarily reflecting the effect of hedging activities in the Financial Services and Asset Management segments that did not qualify for hedge accounting treatment under FAS 133. Also reflected in Other operating loss in 2006 is an out of period charge of $61 million with respect to the SICO Plans and a one-time charge related to the Starr tender offer of $54 million. For a further discussion of these items, see Note 16 of Notes to Consolidated Financial Statements. These declines were partially

offset by increased equity earnings in certain unconsolidated subsidiaries.

2005 and 2004 Comparison

AIG's Other operating loss was $2.5 billion in 2005 compared to $562 million in 2004, reflecting the $1.6 billion of regulatory settlement costs in 2005. In addition, AIG's equity in certain partially owned subsidiaries includes $312 million and $96 million in catastrophe losses in 2005 and 2004, respectively.

Capital Resources and Liquidity

At December 31, 2006, AIG had total consolidated shareholders' equity of $101.68 billion and total consolidated borrowings of $148.68 billion. At that date, $131.55 billion of such borrowings were not guaranteed by AIG, were matched borrowings by AIG or AIGFP, or represented liabilities connected to trust preferred stock.

In 2007, AIG expects to issue capital securities in one or more series. The proceeds will be used to repurchase shares of common stock or to otherwise improve the efficiency of AIG's capital structure.

Borrowings

At December 31, 2006, AIG's net borrowings were $17.13 billion after reflecting amounts that were matched borrowings by AIG and AIGFP, amounts not guaranteed by AIG and liabilities connected to trust preferred stock. The following table summarizes borrowings outstanding at December 31, 2006 and 2005:

(in millions)	**2006**	2005
AIG's net borrowings	**$ 17,126**	$ 10,425
Liabilities connected to trust preferred stock	**1,440**	1,391
AIG MIP matched notes and bonds payable	**5,468**	—
Series AIGFP matched notes and bonds payable	**72**	—
AIGFP		
GIAs	**20,664**	20,811
Matched notes and bonds payable	**35,776**	24,950
Hybrid financial instrument liabilities*	**8,856**	—
Borrowings not guaranteed by AIG	**59,277**	52,272
Total	**$148,679**	$109,849

* *Represents structured notes issued by AIGFP that are accounted for using the fair value option.*

Borrowings issued or guaranteed by AIG and those borrowings not guaranteed by AIG at December 31, 2006 and 2005 were as follows:

(in millions)	**2006**	2005
AIG borrowings:		
Notes and bonds payable	**$ 8,915**	$ 4,607
Loans and mortgages payable	**841**	814
AIG MIP matched notes and bonds payable	**5,468**	—
Series AIGFP matched notes and bonds payable	**72**	—
Total AIG Borrowing	**15,296**	5,421
Borrowings guaranteed by AIG:		
AIGFP		
GIAs	**20,664**	20,811
Notes and bonds payable	**37,528**	26,463
Hybrid financial instrument liabilities[(a)]	**8,856**	—
Total	**67,048**	47,274
AIG Funding, Inc. commercial paper	**4,821**	2,694
AGC Notes and bonds payable	**797**	797
Liabilities connected to trust preferred stock	**1,440**	1,391
Total borrowings issued or guaranteed by AIG	**89,402**	57,577
Borrowings not guaranteed by AIG:		
ILFC		
Commercial paper	**2,747**	2,615
Notes and bonds payable[(b)]	**26,591**	23,715
Total	**29,338**	26,330
AGF		
Commercial paper	**4,328**	3,423
Notes and bonds payable	**19,595**	18,719
Total	**23,923**	22,142
AIGCFG		
Commercial paper	**227**	476
Loans and mortgages payable	**1,453**	1,047
Total	**1,680**	1,523
AIG Finance Taiwan Limited commercial paper	**26**	—
Other Subsidiaries	**1,065**	927
Variable Interest Entity debt:		
A.I. Credit	**880**	—
AIGGIG	**55**	140
AIG Global Real Estate Investment	**2,052**	977
AIG SunAmerica	**203**	233
ALICO	**55**	—
Total	**3,245**	1,350
Total borrowings not guaranteed by AIG	**59,277**	52,272
Total Debt	**$148,679**	$109,849

(a) Represents structured notes issued by AIGFP that are accounted for using the fair value option.

(b) Includes borrowings under Export Credit Facility of $2.7 billion and $2.6 billion, at December 31, 2006 and 2005, respectively.

The debt activity, excluding commercial paper of $12.15 billion and VIE debt of $3.25 billion, for the year ended December 31, 2006 was as follows:

(in millions)	Balance at December 31, 2005	Issuances	Maturities and Repayments	Effect of Foreign Exchange	Other Changes	**Balance at December 31, 2006**
AIG						
Notes and bonds payable	$ 4,607	$ 5,262	$ (1,096)	$ 142	$ —	**$ 8,915**
Loans and mortgages payable	814	1,348	(1,325)	3	1	**841**
AIG MIP matched notes and bonds payable	—	5,371	—	98	(1)	**5,468**
Series AIGFP matched notes and bonds payable	—	72	—	—	—	**72**
AIGFP						
GIAs	20,811	12,265	(12,432)	20	—	**20,664**
Notes and bonds payable and hybrid financial instrument liabilities	26,463	32,115	(12,532)	299	39	**46,384**
AGC notes and bonds payable	797	—	—	—	—	**797**
Liabilities connected to trust preferred stock	1,391	—	—	—	49	**1,440**
ILFC notes and bonds payable	23,715	6,406	(3,843)	535	(222)	**26,591**
AGF notes and bonds payable	18,719	3,620	(3,065)	296	25	**19,595**
AIGCFG loans and mortgages payable	1,047	3,067	(2,711)	58	(8)	**1,453**
Other subsidiaries	927	344	(350)	4	140	**1,065**
Total	$ 99,291	$69,870	$ (37,354)	$ 1,455	$ 23	**$ 133,285**

AIG (Parent Company)

AIG intends to continue its customary practice of issuing debt securities from time to time to meet its financing needs and those of certain of its subsidiaries for general corporate purposes, as well as for the MIP. In July 2006, AIG filed and had declared effective a post-effective amendment to its universal shelf registration statement to sell up to $25.1 billion of debt securities, preferred and common stock and other securities.

In October 2006, AIG established a medium term note program under its shelf registration statement providing for the issuance of up to $25.1 billion of AIG debt securities. The proceeds from the issuance of these debt securities may be used (i) by AIG for general corporate purposes, (ii) by AIGFP as it would use the proceeds from its own borrowings as discussed below or (iii) to fund the MIP. As of December 31, 2006, $1.8 billion principal amount of notes were outstanding under the medium term note program, of which (i) $749 million was used for AIG's general corporate purposes, (ii) $72 million was used by AIGFP and (iii) $1.0 billion was used to fund the MIP. The maturity dates of these notes range from 2011 to 2046. To the extent deemed appropriate, AIG may enter into swap transactions to manage its effective borrowing with respect to these notes.

AIG also maintains a Euro medium term note program under which an aggregate nominal amount of up to $10.0 billion of notes may be outstanding at any one time. The program provides that additional notes may be issued to replace matured or redeemed notes. As of December 31, 2006, the equivalent of $5.7 billion of notes were outstanding under the program, of which $3.7 billion were used to fund the MIP and the remainder was used for AIG's general corporate purposes. The aggregate amount outstanding includes $249 million resulting from foreign exchange translation into U.S. dollars, of which $151 million relates to notes issued by AIG for general corporate purposes and $98 million relates to notes issued to fund the MIP. AIG has hedged the currency exposure arising from foreign currency denominated notes by effectively economically hedging that exposure, although such hedges did not qualify for hedge accounting treatment under FAS 133. In 2007, through February 15, AIG issued the equivalent of $194 million under the Euro program to fund the MIP.

In 2006, AIG issued in Rule 144A/Regulation S offerings $3 billion principal amount of senior notes, of which $1.0 billion was exchanged by AIG for substantially identical notes that are registered under the Securities Act. The proceeds from the sale of $2.25 billion of these notes were used for AIG's general corporate purposes and $750 million was used to fund the MIP. In 2007, through February 15, AIG issued in Rule 144A offerings an aggregate of $750 million principal amount of senior notes, of which $500 million was used to fund the MIP and $250 million was used for AIG's general corporate purposes.

In November 2006, AIG filed a shelf registration statement in Japan, providing for the issuance of up to Japanese Yen 300 billion principal amount of senior notes. In December 2006, AIG issued the equivalent of $429 million under the Japanese shelf registration statement, the proceeds of which were used for AIG's general corporate purposes.

In November 2006, AIG established an Australian dollar debt program under which senior notes with an aggregate amount of up to 5 billion Australian dollars may be outstanding at any one time. The program provides that additional notes may be issued to replace matured or redeemed notes. Although as of December 31, 2006 there were no outstanding notes under the Australian program, AIG intends to use the program opportunistically to fund the MIP or for AIG's general corporate purposes.

In March 2006, AIG borrowed a total of $1.3 billion on an unsecured basis pursuant to loan agreements with third-party banks, of which $700 million remained outstanding on Decem-

ber 31, 2006; $500 million was repaid in February 2007, and the balance matures in March 2007.

AIGFP

AIGFP uses the proceeds from the issuance of notes and bonds and GIA borrowings to invest in a diversified portfolio of securities and derivative transactions. The borrowings may also be temporarily invested in securities purchased under agreements to resell. AIGFP's notes and bonds include structured debt instruments whose payment terms are linked to one or more financial or other indices (such as an equity index or commodity index or another measure that is not considered to be clearly and closely related to the debt instrument). These notes contain embedded derivatives that otherwise would be required to be accounted for separately under FAS 133. Upon AIG's early adoption of FAS 155, AIGFP elected the fair value option for these notes. The notes that are accounted for using the fair value option are reported separately under hybrid financial instrument liabilities. AIG guarantees the obligations of AIGFP under AIGFP's notes and bonds and GIA borrowings. See Operating Review — Financial Services Operations, Liquidity and Derivatives herein.

In June 2006, AIGFP sold an aggregate of $2.0 billion principal amount of senior, floating rate notes in Rule 144A offerings, of which $1.0 billion matures in 2007 and $1.0 billion matures in 2008. AIGFP also has a Euro medium term note program under which an aggregate nominal amount of up to $10.0 billion of notes may be outstanding at any one time. The program provides that additional notes may be issued to replace matured or redeemed notes. As of December 31, 2006, $5.66 billion of notes were outstanding under the program, including $575 million resulting from foreign exchange translation into U.S. dollars. AIGFP's Rule 144A Notes and the notes issued under this program are guaranteed by AIG and are included in AIGFP's Notes and Bonds Payable in the preceding table of borrowings.

AIG Funding

AIG Funding, Inc. (AIG Funding), issues commercial paper that is guaranteed by AIG in order to help fulfill the short-term cash requirements of AIG and its subsidiaries. The issuance of AIG Funding's commercial paper, including the guarantee by AIG, is subject to the approval of AIG's Board of Directors or the Finance Committee of the Board if it exceeds certain pre-approved limits.

As backup for the commercial paper program and for other general corporate purposes, AIG and AIG Funding maintain revolving credit facilities, which, as of December 31, 2006, had an aggregate of $5.8 billion available to be drawn and which are summarized below under Revolving Credit Facilities.

ILFC

ILFC fulfills its short-term cash requirements through operating cash flows and the issuance of commercial paper. The issuance of commercial paper is subject to the approval of ILFC's Board of Directors and is not guaranteed by AIG. ILFC maintains syndicated revolving credit facilities which, as of December 31, 2006, aggregated $6.5 billion and which are summarized below under Revolving Credit Facilities. These facilities are used as back up for ILFC's maturing debt and other obligations.

As a well-known seasoned issuer, ILFC has filed an automatic shelf registration statement with the SEC allowing ILFC immediate access to the U.S. public debt markets. For 2006, $1.90 billion of debt securities were issued under this registration statement and $3.52 billion were issued under a prior registration statement. In addition, ILFC has a Euro medium term note program for $7.0 billion, under which $4.28 billion in notes were sold through December 31, 2006. Notes issued under the Euro medium term note program are included in ILFC Notes and bonds payable in the preceding table of borrowings. The foreign exchange adjustment for the foreign currency denominated debt was $733 million at December 31, 2006 and $197 million at December 31, 2005. ILFC has substantially eliminated the currency exposure arising from foreign currency denominated notes by economically hedging the portion of the note exposure not already offset by Euro-denominated operating lease payments, although such hedges did not qualify for hedge accounting treatment under FAS 133.

ILFC had a $4.3 billion Export Credit Facility for use in connection with the purchase of approximately 75 aircraft delivered through 2001. This facility was guaranteed by various European Export Credit Agencies. The interest rate varies from 5.75 percent to 5.90 percent on these amortizing ten-year borrowings depending on the delivery date of the aircraft. At December 31, 2006, ILFC had $1.0 billion outstanding under this facility. The debt is collateralized by a pledge of the shares of a subsidiary of ILFC, which holds title to the aircraft financed under the facility.

In May 2004, ILFC entered into a similarly structured Export Credit Facility for up to a maximum of $2.64 billion for Airbus aircraft to be delivered through May 31, 2005. The facility was subsequently increased to $3.64 billion and extended to include aircraft to be delivered through May 31, 2007. The facility becomes available as the various European Export Credit Agencies provide their guarantees for aircraft based on a six-month forward-looking calendar, and the interest rate is determined through a bid process. At December 31, 2006, ILFC had $1.7 billion outstanding under this facility. Borrowings with respect to these facilities are included in ILFC's Notes and bonds payable in the preceding table of borrowings.

From time to time, ILFC enters into funded financing agreements. As of December 31, 2006, ILFC had a total of $1.2 billion outstanding, which has varying maturities through February 2012. The interest rates are LIBOR-based, with spreads ranging from 0.30 percent to 1.625 percent.

In December of 2005, ILFC issued two tranches of junior subordinated debt totaling $1.0 billion to underlie trust preferred securities issued by a trust sponsored by ILFC. Both tranches mature on December 21, 2065, but each tranche has a different call option. The $600 million tranche has a call date of December 21, 2010 and the $400 million tranche has a call date of December 21, 2015. The tranche with the 2010 call date has a fixed interest rate of 5.90 percent for the first five years. The tranche with the 2015 call date has a fixed interest rate of 6.25 percent for the first ten years.

Both tranches have interest rate adjustments if the call option is not exercised. If the call option is not exercised, the new interest rate will be a floating quarterly reset rate based on the initial credit spread plus the highest of (i) 3-month LIBOR, (ii) 10-year constant maturity treasury and (iii) 30-year constant maturity treasury.

The proceeds of ILFC's debt financing are primarily used to purchase flight equipment, including progress payments during the construction phase. The primary sources for the repayment of this debt and the interest expense thereon are the cash flow from operations, proceeds from the sale of flight equipment and the rollover and refinancing of the prior debt. AIG does not guarantee the debt obligations of ILFC. See also Operating Review — Financial Services Operations and Liquidity herein.

AGF

AGF fulfills its short-term cash requirements through the issuance of commercial paper. The issuance of commercial paper is subject to the approval of AGF's Board of Directors and is not guaranteed by AIG. AGF maintains committed syndicated revolving credit facilities which, as of December 31, 2006, aggregated to $4.25 billion and which are summarized below under Revolving Credit Facilities. The facilities can be used for general corporate purposes and to provide backup for AGF's commercial paper programs.

AGF issued $3.62 billion during 2006 and $5.51 billion during 2005 of notes and bonds ranging in maturities from two to 25 years. As of December 31, 2006, notes and bonds aggregating $19.59 billion were outstanding with maturity dates ranging from 2007 to 2031 at interest rates ranging from 1.94 percent to 8.45 percent. To the extent deemed appropriate, AGF may enter into swap transactions to manage its effective borrowing with respect to these notes and bonds. As a well-known seasoned issuer, AGF has filed an automatic shelf registration statement with the SEC allowing AGF immediate access to the U.S. public debt markets. At December 31, 2006, AGF had the corporate authority to issue up to $13.4 billion of debt securities under its shelf registration statements.

In January 2007, AGF issued junior subordinated debentures in an aggregate principal amount of $350 million that mature in January 2067. The debentures underlie a series of trust preferred securities sold by a trust sponsored by AGF in a Rule 144A/ Regulation S offering. AGF can redeem the debentures at par beginning in January 2017 and until that time will pay a fixed rate of interest. If AGF does not redeem the debentures in January 2017, the interest rate changes to a floating rate, which will reset based on 3-month LIBOR.

AGF's funding sources include a medium term note program, private placement debt, retail note issuances, securitizations of finance receivables that AGF accounts for as on-balance-sheet secured financings and bank financings. In addition, AGF has become an established issuer of long-term debt in the international capital markets.

In addition to debt refinancing activities, proceeds from the collection of finance receivables may be used to pay the principal and interest on AGF's debt. AIG does not guarantee any of the debt obligations of AGF. See also Operating Review — Financial Services Operations and Liquidity herein.

AIGCFG

AIGCFG has a variety of funding mechanisms for its various markets, including: retail and wholesale deposits; short-term and long-term bank loans and intercompany subordinated debt. AIG Credit Card Company (Taiwan), a consumer finance business in Taiwan, has issued commercial paper for the funding of its own operations. AIG does not guarantee any borrowings for AIGCFG businesses, including this commercial paper.

Revolving Credit Facilities

AIG, ILFC and AGF maintain the following committed, unsecured revolving credit facilities in order to support their respective commercial paper programs and for general corporate purposes.

AIG, ILFC and AGF expect to replace or extend these credit facilities on or prior to their expiration. Some of the facilities, as noted below, contain a ''term-out option'' allowing for the conversion by the borrower of any outstanding loans at expiration into one-year term loans.

(in millions) Facility	Size	Borrower(s)	Available Amount **December 31, 2006**	Expiration	One-Year Term-Out Option
AIG:					
364-Day Syndicated Facility	$1,625	AIG AIG Funding[a] AIG Capital Corporation[a]	**$1,625**	July 2007	Yes
5-Year Syndicated Facility	1,625	AIG AIG Funding[a] AIG Capital Corporation[a]	**1,625**	July 2011	No
364-Day Bilateral Facility	3,200	AIG[b] AIG Funding	**505**	November 2007	Yes
364-Day Intercompany Facility[c]	2,000	AIG	**2,000**	October 2007	Yes
Total AIG	$8,450		**$5,755**		
ILFC:					
5-Year Syndicated Facility	$2,500	ILFC	**$2,500**	October 2011	No
5-Year Syndicated Facility	2,000	ILFC	**2,000**	October 2010	No
5-Year Syndicated Facility	2,000	ILFC	**2,000**	October 2009	No
Total ILFC	$6,500		**$6,500**		
AGF:					
364-Day Syndicated Facility	$2,125	American General Finance Corporation American General Finance, Inc.[d]	**$2,125**	July 2007	Yes
5-Year Syndicated Facility	2,125	American General Finance Corporation	**2,125**	July 2010	No
Total AGF	$4,250		**$4,250**		

(a) Guaranteed by AIG.

(b) This facility can be drawn in the form of loans or letters of credit. All drawn amounts shown above are in the form of letters of credit.

(c) Subsidiaries of AIG are the lenders on this facility.

(d) American General Finance, Inc. is an eligible borrower for up to $400 million only.

Credit Ratings

The cost and availability of unsecured financing for AIG and its subsidiaries are generally dependent on their short-term and long-term debt ratings. The following table presents the credit ratings of AIG and certain of its subsidiaries as of February 28, 2007. In parentheses, following the initial occurrence in the table of each rating, is an indication of that rating's relative rank within the agency's rating categories. That ranking refers only to the generic or major rating category and not to the modifiers appended to the rating by the rating agencies to denote relative position within such generic or major category.

	Short-term Debt			Senior Long-term Debt		
	Moody's	S&P	Fitch	Moody's[a]	S&P[b]	Fitch[c]
AIG	P-1 (1st of 3)	A-1+ (1st of 6)	F1+ (1st of 5)	Aa2 (2nd of 9)	AA (2nd of 8)	AA (2nd of 9)
AIG Financial Products Corp.[d]	P-1	A-1+	—	Aa2	AA	—
AIG Funding, Inc.[d]	P-1	A-1+	F1+	—	—	—
ILFC	P-1	A-1+	F1 (1st of 5)	A1 (3rd of 9)	AA-[e] (2nd of 8)	A+ (3rd of 9)
American General Finance Corporation	P-1	A-1 (1st of 6)	F1	A1	A+ (3rd of 8)	A+
American General Finance, Inc.	P-1	A-1	F1	—	—	A+

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

(b) Standard & Poor's, a division of the McGraw-Hill Companies (S&P). S&P ratings may be modified by the addition of a plus or minus sign to show relative standing within the major rating categories.

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

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

(e) Negative rating outlook. A negative outlook by S&P indicates that a rating may be lowered, but is not necessarily a precursor of a ratings change. The outlook on all other credit ratings in the table is stable.

These credit ratings are current opinions of the rating agencies. As such, they may be changed, suspended or withdrawn at any time by the rating agencies as a result of changes in, or unavailability of, information or based on other circumstances. Ratings may also be withdrawn at AIG management's request. This discussion of ratings is not a complete list of ratings of AIG and its subsidiaries. See Item 1A. Risk Factors for more information regarding the credit ratings of AIG and its subsidiaries and certain risks related thereto.

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

AIG believes that any of its own or its subsidiaries' contractual obligations that are subject to ''ratings triggers'' or financial covenants relating to ''ratings triggers'' would not have a material adverse effect on its financial condition or liquidity. Ratings downgrades could also trigger the application of termination provisions in certain of AIG's contracts, principally agreements entered into by AIGFP and assumed reinsurance contracts entered into by Transatlantic.

It is estimated that, as of the close of business on February 15, 2007, based on AIGFP's outstanding municipal GIAs and financial derivatives transactions as of such date, a downgrade of AIG's long-term senior debt ratings to 'Aa3' by Moody's or 'AA–' by S&P would permit counterparties to call for approximately $864 million of collateral. Further, additional downgrades could result in requirements for substantial additional collateral, which could have a material effect on how AIGFP manages its liquidity. The actual amount of additional collateral that AIGFP would be required to post to counterparties in the event of such downgrades depends on market conditions, the fair value of the outstanding affected transactions and other factors prevailing at the time of the downgrade. Additional obligations to post collateral would increase the demand on AIGFP's liquidity.

Contractual Obligations and Other Commercial Commitments

The maturity schedule of contractual obligations of AIG and its consolidated subsidiaries at December 31, 2006 was as follows:

(in millions)	Total Payments	Payments due by Period: Less Than One Year	1-3 Years	3+-5 Years	Over Five Years
Borrowings[a]	$ 133,285	$ 34,670	$ 29,949	$ 30,483	$ 38,183
Interest payments on borrowings	44,090	4,960	8,130	5,445	25,555
Loss reserves[b]	79,999	22,000	24,399	11,600	22,000
Insurance and investment contract liabilities[c]	577,730	16,023	27,728	39,376	494,603
GIC liabilities[d]	56,042	19,399	23,209	3,889	9,545
Aircraft purchase commitments	19,042	5,442	7,079	2,155	4,366
Operating leases	2,763	626	802	581	754
Total	$ 912,951	$103,120	$121,296	$ 93,529	$595,006

(a) Excludes commercial paper and obligations included as debt pursuant to FASB Interpretation No. 46, ''Consolidation of Variable Interest Entities'' (FIN 46R), and includes hybrid financial instrument liabilities recorded at fair value. See also Note 9 of Notes to Consolidated Financial Statements.

(b) Represents future loss and loss adjustment expense payments estimated based on historical loss development payment patterns.

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

(d) Represents guaranteed maturities under GICs.

The maturity schedule of other commercial commitments of AIG and its consolidated subsidiaries at December 31, 2006 was as follows:

	Total Amounts Committed	Amount of Commitment Expiration: Less Than One Year	1-3 Years	3+-5 Years	Over Five Years
Letters of credit:					
Life Insurance & Retirement Services	$ 185	$ 21	$ 28	$ —	$ 136
Parent Company[a]	641	522	1	118	—
DBG	198	198	—	—	—
Standby letters of credit:					
Capital Markets	1,739	1,427	104	40	168
Guarantees:					
Life Insurance & Retirement Services[b]	2,100	113	423	7	1,557
Aircraft Leasing	161	—	52	—	109
Asset Management	246	23	53	—	170
Other commercial commitments[c]:					
Capital Markets[d]	15,946	5,127	2,313	2,640	5,866
Aircraft Leasing[e]	344	—	—	—	344
Life Insurance & Retirement Services[f]	4,896	1,119	1,730	1,177	870
Asset Management[g]	1,310	896	255	91	68
Life Settlement	203	—	203	—	—
DBG[h]	1,588	690	603	295	—
Parent Company	193	56	137	—	—
Total	$ 29,750	$ 10,192	$ 5,902	$ 4,368	$ 9,288

(a) Represents reimbursement obligations under letters of credit issued by commercial banks.

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

(c) Excludes commitments with respect to pension plans. The annual pension contribution for 2007 is expected to be approximately $95 million for U.S. and non-U.S. plans. See also Note 15 of Notes to Consolidated Financial Statements.

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

(e) Primarily in connection with options to acquire aircraft.

(f) Primarily AIG SunAmerica commitments to invest in partnerships.

(g) Includes commitments to invest in limited partnerships, private equity and hedge funds and real estate.

(h) Primarily commitments to invest in limited partnerships.

Special Purpose Vehicles and Off Balance Sheet Arrangements

AIG transacts with special purpose vehicles (SPVs) in the ordinary course of business. Many of these SPVs are included in the consolidated financial statements but some are off balance sheet.

AIG has guidelines with respect to the formation of and investment in SPVs and off balance sheet arrangements. In addition, AIG has expanded the responsibility of its Complex Structured Financial Transaction Committee (CSFT) to include the review of any transaction that could subject AIG to heightened legal, reputational, regulatory, accounting or other risk. See Item 9A. Controls and Procedures — Management's Report on Internal Control Over Financial Reporting for a further discussion of the CSFT.

For additional information related to AIG's activities with respect to VIEs and certain guarantees, see Notes 1 and 18 of Notes to Consolidated Financial Statements.

Shareholders' Equity

AIG's consolidated shareholders' equity increased during 2006 and 2005 as follows:

(in millions)	**2006**	2005
Beginning of year	**$ 86,317**	$79,673
Net income	**14,048**	10,477
Unrealized appreciation (depreciation) of investments, net of tax	**1,735**	(1,978)
Cumulative translation adjustment, net of tax	**936**	(540)
Dividends to shareholders	**(1,690)**	(1,615)
Other*	**331**	300
End of year	**$101,677**	$86,317

* *Reflects the effects of employee stock transactions and in 2006 also reflects the cumulative effect of accounting changes, including the adoption of FAS 158. See Note 1(hh) of Notes to Consolidated Financial Statements.*

AIG has in the past reinvested most of its unrestricted earnings in its operations and believes such continued reinvestment in the future will be adequate to meet any foreseeable capital needs. However, AIG may choose from time to time to raise additional funds through the issuance of additional securities.

In February 2007, AIG's Board of Directors adopted a new dividend policy, to take effect with the dividend to be declared in the second quarter of 2007, providing that under ordinary circumstances, AIG's plan will be to increase its common stock dividend by approximately 20 percent annually.

Share Repurchases

During 2006, AIG did not purchase any shares of its common stock under its existing share repurchase authorization. At December 31, 2006, an additional 36,542,700 shares could be purchased under the then current authorization by AIG's Board of Directors. In February 2007, AIG's Board of Directors increased the repurchase program by authorizing the repurchase of shares with an aggregate purchase price of $8 billion. AIG or its subsidiaries from time to time may buy shares of its common stock in the open market for general corporate purposes, including to satisfy its obligations under various employee benefit plans. During 2006, ILFC purchased 17,000 shares of AIG common stock at an average cost of $72.18 per share to satisfy its obligations under an employee benefit plan. See Capital Resources and Liquidity — Liquidity for a discussion of possible share repurchases in 2007.

Dividends from Insurance Subsidiaries

Payments of dividends to AIG by its insurance subsidiaries are subject to certain restrictions imposed by regulatory authorities. With respect to AIG's domestic insurance subsidiaries, the payment of any dividend requires formal notice to the insurance department in which the particular insurance subsidiary is domiciled. Under the laws of many states, an insurer may pay a dividend without prior approval of the insurance regulator when the amount of the dividend is below certain regulatory thresholds. Other foreign jurisdictions may restrict the ability of AIG's foreign insurance subsidiaries to pay dividends. The most significant foreign insurance regulatory jurisdictions include Bermuda, Japan, Hong Kong, Taiwan, the United Kingdom, Thailand and Singapore. Largely as a result of the restrictions, approximately 90 percent of consolidated shareholders' equity was restricted from immediate transfer to AIG parent at December 31, 2006. See Regulation and Supervision herein. AIG cannot predict how recent regulatory investigations may affect the ability of its regulated subsidiaries to pay dividends. To AIG's knowledge, no AIG company is currently on any regulatory or similar ''watch list'' with regard to solvency. See also Liquidity herein, Note 12 of Notes to Consolidated Financial Statements and Item 1A. Risk Factors — Liquidity.

Regulation and Supervision

AIG's insurance subsidiaries, in common with other insurers, are subject to regulation and supervision by the states and jurisdictions in which they do business. In the U.S., the NAIC has developed Risk-Based Capital (RBC) requirements. RBC relates an individual insurance company's statutory surplus to the risk inherent in its overall operations.

In preparing both its 2004 and 2005 audited statutory financial statements for its Domestic General Insurance companies, AIG agreed with the relevant state regulatory authorities on the statutory accounting treatment of the various items requiring adjustment or restatement. With respect to the 2004 audited statutory financial statements, these adjustments and restatements reduced previously reported General Insurance statutory surplus at December 31, 2004 by approximately $3.5 billion, to approximately $20.6 billion. With respect to the 2005 audited statutory financial statements, the state regulators permitted the Domestic General Insurance companies to record a $724 million reduction to opening statutory surplus as of January 1, 2005.

AIG's insurance subsidiaries file financial statements prepared in accordance with statutory accounting practices prescribed or

permitted by domestic and foreign insurance regulatory authorities. The principal differences between statutory financial statements and financial statements prepared in accordance with U.S. GAAP for domestic companies are that statutory financial statements do not reflect DAC, some bond portfolios may be carried at amortized cost, assets and liabilities are presented net of reinsurance, policyholder liabilities are valued using more conservative assumptions and certain assets are non-admitted.

In connection with the filing of the 2005 statutory financial statements for AIG's Domestic General Insurance companies, AIG agreed with the relevant state insurance regulators on the statutory accounting treatment of various items. The regulatory authorities have also permitted certain of the domestic and foreign insurance subsidiaries to support the carrying value of their investments in certain non-insurance and foreign insurance subsidiaries by utilizing the AIG audited consolidated financial statements to satisfy the requirement that the U.S. GAAP-basis equity of such entities be audited. In addition, the regulatory authorities have permitted the Domestic General Insurance companies to utilize audited financial statements prepared on a basis of accounting other than U.S. GAAP to value investments in joint ventures, limited partnerships and hedge funds. AIG has received similar permitted practices authorizations from insurance regulatory authorities in connection with the 2006 statutory financial statements. These permitted practices did not affect the Domestic General Insurance companies' compliance with minimum regulatory capital requirements.

Statutory capital of each company continued to exceed minimum company action level requirements following the adjustments, but AIG nonetheless contributed an additional $750 million of capital into American Home effective September 30, 2005 and contributed a further $2.25 billion of capital in February 2006 for a total of approximately $3 billion of capital into Domestic General Insurance subsidiaries effective December 31, 2005. To enhance their current capital positions, AIG suspended dividends from the DBG companies from the fourth quarter 2005 through 2006, but AIG expects dividend payments will resume in the first quarter of 2007. AIG believes it has the capital resources and liquidity to fund any necessary statutory capital contributions.

As discussed above, various regulators have commenced investigations into certain insurance business practices. In addition, the OTS and other regulators routinely conduct examinations of AIG and its subsidiaries, including AIG's consumer finance operations. AIG cannot predict the ultimate effect that these investigations and examinations, or any additional regulation arising therefrom, might have on its business. Federal, state or local legislation may affect AIG's ability to operate and expand its various financial services businesses, and changes in the current laws, regulations or interpretations thereof may have a material adverse effect on these businesses.

AIG's U.S. operations are negatively affected under guarantee fund assessment laws which exist in most states. As a result of operating in a state which has guarantee fund assessment laws, a solvent insurance company may be assessed for certain obligations arising from the insolvencies of other insurance companies which operated in that state. AIG generally records these assessments upon notice. Additionally, certain states permit at least a portion of the assessed amount to be used as a credit against a company's future premium tax liabilities. Therefore, the ultimate net assessment cannot reasonably be estimated. The guarantee fund assessments net of credits for 2006, 2005 and 2004, respectively, were $97 million, $124 million and $118 million.

AIG is also required to participate in various involuntary pools (principally workers compensation business) which provide insurance coverage for those not able to obtain such coverage in the voluntary markets. This participation is also recorded upon notification, as these amounts cannot reasonably be estimated.

A substantial portion of AIG's General Insurance business and a majority of its Life Insurance & Retirement Services business are conducted in foreign countries. The degree of regulation and supervision in foreign jurisdictions varies. Generally, AIG, as well as the underwriting companies operating in such jurisdictions, must satisfy local regulatory requirements. Licenses issued by foreign authorities to AIG subsidiaries are subject to modification and revocation. Thus, AIG's insurance subsidiaries could be prevented from conducting future business in certain of the jurisdictions where they currently operate. AIG's international operations include operations in various developing nations. Both current and future foreign operations could be adversely affected by unfavorable political developments up to and including nationalization of AIG's operations without compensation. Adverse effects resulting from any one country may affect AIG's results of operations, liquidity and financial condition depending on the magnitude of the event and AIG's net financial exposure at that time in that country.

Foreign insurance operations are individually subject to local solvency margin requirements that require maintenance of adequate capitalization, which AIG complies with by country. In addition, certain foreign locations, notably Japan, have established regulations that can result in guarantee fund assessments. These have not had a material effect on AIG's financial condition or results of operations.

Liquidity

AIG manages liquidity at both the subsidiary and parent company levels. At December 31, 2006, AIG's consolidated invested assets, primarily held by its subsidiaries, included $26.8 billion in cash and short-term investments. Consolidated net cash provided from operating activities in 2006 amounted to $6.8 billion. At the parent company level, liquidity management activities are conducted in a manner to preserve and enhance funding stability, flexibility, and diversity through the full range of potential operating environments and market conditions. AIG's primary sources of cash flow are dividends and other payments from its regulated and unregulated subsidiaries, as well as issuances of debt securities. Primary uses of cash flow are for debt service, subsidiary funding and shareholder dividend payments. Management believes that AIG's liquid assets, cash provided by operations and access to the capital markets will enable it to meet its anticipated cash requirements, including the funding of increased

dividends under AIG's new dividend policy and repurchases of common stock.

Insurance Operations

The liquidity of the combined insurance operations is derived both domestically and abroad. The combined insurance operating cash flow is derived from two sources, underwriting operations and investment operations. Cash flow from underwriting operations includes periodic premium collections, including policyholders' contract deposits, and paid loss recoveries, less reinsurance premiums, losses, benefits, and acquisition and operating expenses. Generally, there is a time lag from when premiums are collected and, when as a result of the occurrence of events specified in the policy, the losses and benefits are paid. Investment cash flow is primarily derived from interest and dividends received and includes realized capital gains net of realized capital losses.

In addition to the combined insurance operating cash flow, AIG's insurance operations held $11.2 billion in cash and short-term investments at December 31, 2006. Operating cash flow and the cash and short-term balances held provided AIG's insurance operations with a significant amount of liquidity. This liquidity is available, among other things, to purchase predominately high quality and diversified fixed income securities and, to a lesser extent, marketable equity securities, and to provide mortgage loans on real estate, policy loans, and collateral loans. This cash flow coupled with proceeds of approximately $126 billion from the maturities, sales and redemptions of fixed income securities and from the sale of equity securities was used to purchase approximately $161 billion of fixed income securities and marketable equity securities during 2006.

See also Operating Review — General Insurance Operations — General Insurance Net Investment Income and Life Insurance & Retirement Services Operations — Life Insurance & Retirement Services Net Investment Income and Realized Capital Gains (Losses) herein.

General Insurance

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

Life Insurance & Retirement Services

Life Insurance & Retirement Services operating cash flow is derived from underwriting and investment activities. If a substantial portion of the Life Insurance & Retirement Services operations bond portfolio diminished significantly in value and/or defaulted, AIG might need to liquidate other portions of its Life Insurance & Retirement Services investment portfolio and/or arrange financing. Potential events causing such a liquidity strain could be the result of economic collapse of a nation or region in which Life Insurance & Retirement Services operations exist, nationalization, terrorist acts, or other economic or political upheaval. In addition, a significant rise in interest rates leading to a major increase in policyholder surrenders could also create a liquidity strain.

Financial Services

AIG's major Financial Services operating subsidiaries consist of AIGFP, ILFC, AGF and AIGCFG. Sources of funds considered in meeting the liquidity needs of AIGFP's operations include GIAs, issuance of long-term and short-term debt, proceeds from maturities, sales of securities available for sale and securities and spot commodities leased or sold under repurchase agreements. ILFC, AGF and AIGCFG utilize the commercial paper markets, bank loans and bank credit facilities as sources of liquidity. ILFC and AGF also fund in the domestic and international capital markets without reliance on any guarantee from AIG. An additional source of liquidity for ILFC is the use of export credit facilities. AIGCFG also uses wholesale and retail bank deposits as sources of funds. On occasion, AIG has provided equity capital to ILFC, AGF and AIGCFG and provides intercompany loans to AIGCFG.

Asset Management

Asset Management operating cash flow is derived primarily from investment income in connection with domestic and foreign GICs and from the collection of various forms of investment management fees, brokerage commissions and custody fees earned from affiliated and unaffiliated clients. Investment management fees are typically asset-based fees collected on a periodic basis, while brokerage commissions and custody fees are more transaction driven and received on a continual basis. Asset Management also derives cash from the realization of gains earned through its investment partnership holdings and collects various forms of incentive management fees. These incentive management fees, which are typically based on the appreciation and/or realization of gains on managed assets, are generally received in the form of carried interest earned from sponsored funds managed on behalf of clients. Asset Management's spread-based investment business derives cash from the investment income and the sale of invested assets backing these contract liabilities.

AIGGIG incurs expenses with associated cash outflows from the operation of its business, including costs related to portfolio management and related back and middle office costs. In addition, cash is used in association with investment warehousing activities wherein AIGGIG funds and holds an investment for the benefit of a future investment vehicle.

Cash needs for the spread-based investment business are principally the result of GIC maturities. Significant blocks of the GIC portfolio will mature over the next five years. AIG utilizes asset liability matching to control liquidity risks associated with

this business. In addition, AIG believes that its products incorporate certain restrictions which encourage persistency, limiting the magnitude of unforeseen surrenders in the GIC portfolio.

Liquidity for Asset Management operations can be affected by significant credit or geopolitical events that might cause a delay in fund closings, securitizations or an inability of AIG's clients to fund their capital commitments. AIGGIG has relied upon AIG from time to time in order to fund certain liquidity requirements associated with investment warehousing. In addition, AIG Global Real Estate maintains several external credit lines in order to fund its ongoing property development and construction related activities.

AIG (Parent Company)

The liquidity of the parent company is principally derived from its subsidiaries. The primary sources of cash flow are dividends and other payments from its regulated and unregulated subsidiaries, as well as issuance of debt securities. Primary uses of cash flow are for debt service, subsidiary funding, shareholder dividend payments and purchases of outstanding shares of common stock. In 2006, AIG Parent collected $2.1 billion in dividends and other payments from subsidiaries and issued $6.6 billion in debt securities excluding MIP and Series AIGFP debt. AIG Parent also made interest payments totaling $232 million, made $2.9 billion in capital contributions to subsidiaries (principally $2.3 billion to DBG), and paid $1.6 billion in dividends to shareholders in 2006. No share repurchases were made by AIG Parent in 2006.

AIG funds its short-term working capital needs through commercial paper issued by AIG Funding. As of December 31, 2006, AIG Funding had $4.8 billion of commercial paper outstanding with an average maturity of 28 days. As additional liquidity, AIG and AIG Funding maintain revolving credit facilities that, as of December 31, 2006, had an aggregate of $5.8 billion available to be drawn, which are summarized above under Revolving Credit Facilities.

At the parent company level, liquidity management activities are conducted in a manner intended to preserve and enhance funding stability, flexibility, and diversity through the full range of potential operating environments and market conditions. Assessing liquidity risk involves forecasting of cash inflows/outflows on both a short- and long-term basis. Corporate Treasury is responsible for formulating the parent company's liquidity and contingency planning efforts, as well as for execution of AIG's specific funding activities. Through active liquidity management, AIG seeks to retain stable, reliable and cost-effective funding sources. In addition to current liquidity requirements, factors which affect funding decisions include market conditions, prevailing interest rates and the desired maturity profile of liabilities. The objectives of contingency planning are to ensure maintenance of appropriate liquidity during normal and stress periods, to measure and project funding requirements during periods of stress, and to manage access to funding sources. Diversification of funding sources is an important element of AIG's liquidity risk management approach.

AIG's liquidity could be impaired by an inability to access the capital markets or by unforeseen significant outflows of cash. This situation may arise due to circumstances that AIG may be unable to control, such as a general market disruption or an operational problem that affects third parties or AIG. Regulatory and other legal restrictions may limit AIG's ability to transfer funds freely, either to or from its subsidiaries. In particular, many of AIG's subsidiaries, including its insurance subsidiaries, are subject to laws and regulations that authorize regulatory bodies to block or reduce the flow of funds to the parent holding company, or that prohibit such transfers altogether in certain circumstances. These laws and regulations may hinder AIG's ability to access funds that it may need to make payments on its obligations. Because of the wide geographic profile of AIG's regulated subsidiaries, management believes that these cash flows represent a diversified source of liquidity for AIG. For a further discussion of the regulatory environment in which AIG subsidiaries operate and other issues affecting AIG's liquidity, see Item 1A. Risk Factors.

Invested Assets

AIG's investment strategy is to invest primarily in high quality securities while maintaining diversification to avoid significant exposure to issuer, industry and/or country concentrations.

Management's Discussion and Analysis of Financial Condition and Results of Operations *Continued*

The following tables summarize the composition of AIG's invested assets by segment, at December 31, 2006 and 2005:

(in millions)	General Insurance	Life Insurance & Retirement Services	Financial Services	Asset Management	Other	Total
2006						
Fixed maturities:						
Bonds available for sale, at fair value	$ 67,994	$287,360	$ 1,357	$30,680	$ —	$387,391
Bonds held to maturity, at amortized cost	21,437	—	—	—	—	21,437
Bond trading securities, at fair value	1	1,995	—	7,041	—	9,037
Equity securities:						
Common stocks available for sale, at fair value	4,245	8,711	—	226	80	13,262
Common and preferred stocks trading, at fair value	350	13,705	—	366	—	14,421
Preferred stocks available for sale, at fair value	1,884	650	5	—	—	2,539
Mortgage loans on real estate, net of allowance	13	12,852	95	4,107	—	17,067
Policy loans	1	7,458	2	48	(8)	7,501
Collateral and guaranteed loans, net of allowance	3	733	2,301	729	84	3,850
Financial services assets:						
Flight equipment primarily under operating leases, net of accumulated depreciation	—	—	39,875	—	—	39,875
Securities available for sale, at fair value	—	—	47,205	—	—	47,205
Trading securities, at fair value	—	—	5,031	—	—	5,031
Spot commodities	—	—	220	—	—	220
Unrealized gain on swaps, options and forward transactions	—	—	19,252	—	—	19,252
Trading assets	—	—	2,468	—	—	2,468
Securities purchased under agreements to resell, at contract value	—	—	33,702	—	—	33,702
Finance receivables, net of allowance	—	—	29,573	—	—	29,573
Securities lending collateral, at fair value	5,376	50,099	76	13,755	—	69,306
Other invested assets	9,207	14,263	2,212	15,823	609	42,114
Short-term investments, at cost	3,281	6,893	1,245	13,825	5	25,249
Total investments and financial services assets as shown on the balance sheet	113,792	404,719	184,619	86,600	770	790,500
Cash	334	672	390	186	8	1,590
Investment income due and accrued	1,363	4,364	23	326	1	6,077
Real estate, net of accumulated depreciation	570	698	17	75	26	1,386
Total invested assets*	$116,059	$410,453	$185,049	$87,187	$805	$799,553

* *At December 31, 2006, approximately 68 percent and 32 percent of invested assets were held in domestic and foreign investments, respectively.*

(in millions)	General Insurance	Life Insurance & Retirement Services	Financial Services	Asset Management	Other	Total
2005						
Fixed maturities:						
Bonds available for sale, at fair value	$50,870	$273,165	$ 1,307	$34,174	$ —	$359,516
Bonds held to maturity, at amortized cost	21,528	—	—	—	—	21,528
Bond trading securities, at fair value	—	1,073	—	3,563	—	4,636
Equity securities:						
Common stocks available for sale, at fair value	4,505	7,436	—	227	59	12,227
Common stocks trading, at fair value	425	8,122	—	412	—	8,959
Preferred stocks available for sale, at fair value	1,632	760	10	—	—	2,402
Mortgage loans on real estate, net of allowance	14	10,247	71	3,968	—	14,300
Policy loans	2	6,987	2	48	—	7,039
Collateral and guaranteed loans, net of allowance	3	1,172	1,719	578	98	3,570
Financial services assets:						
Flight equipment primarily under operating leases, net of accumulated depreciation	—	—	36,245	—	—	36,245
Securities available for sale, at fair value	—	—	37,511	—	—	37,511
Trading securities, at fair value	—	—	6,499	—	—	6,499
Spot commodities	—	—	92	—	—	92
Unrealized gain on swaps, options and forward transactions	—	—	18,695	—	—	18,695
Trading assets	—	—	1,204	—	—	1,204
Securities purchased under agreements to resell, at contract value	—	28	14,519	—	—	14,547
Finance receivables, net of allowance	—	—	27,995	—	—	27,995
Securities lending collateral, at fair value	4,931	42,991	—	11,549	—	59,471
Other invested assets	6,350	9,847	2,758	12,096	21	31,072
Short-term investments, at cost	2,482	5,855	1,382	5,619	4	15,342
Total investments and financial services assets as shown on the balance sheet	92,742	367,683	150,009	72,234	182	682,850
Cash	305	989	331	196	76	1,897
Investment income due and accrued	1,232	4,073	18	402	2	5,727
Real estate, net of accumulated depreciation	525	659	17	73	19	1,293
Total invested assets*	$94,804	$373,404	$150,375	$72,905	$279	$691,767

* *At December 31, 2005, approximately 70 percent and 30 percent of invested assets were held in domestic and foreign investments, respectively.*

General Insurance Invested Assets

In AIG's General Insurance business, the duration of liabilities for long-tail casualty lines is greater than other lines. As differentiated from the Life Insurance & Retirement Services companies, the focus is not on asset-liability matching, but on preservation of capital and growth of surplus.

Fixed income holdings of the Domestic General Insurance companies are comprised primarily of tax-exempt securities, which provide attractive risk-adjusted after-tax returns. These high quality municipal investments have an average rating of high AA.

Fixed income assets held in Foreign General Insurance are of high quality and short to intermediate duration, averaging 4.2 years compared to 7.2 years for those in Domestic General Insurance.

While reserves are invested in conventional fixed income securities in Domestic General Insurance, a modest portion of surplus is allocated to large capitalization, high-dividend, public equity strategies and to alternative investments, including private equity and hedge funds. These investments have provided a combination of added diversification and attractive long-term returns.

General Insurance invested assets grew by $21.3 billion, or 22 percent, during 2006 as bond holdings grew by $17 billion, or 24 percent. Listed equity holdings remained essentially flat at $6.5 billion.

Life Insurance & Retirement Services Invested Assets

With respect to Life Insurance & Retirement Services, AIG's investment strategy is to produce cash flows greater than maturing insurance liabilities. AIG actively manages the asset-liability relationship in its foreign operations, as it has been doing throughout AIG's history, even though certain territories lack qualified long-term investments or certain local regulatory authorities may impose investment restrictions. For example, in several Southeast Asian countries, the duration of investments is shorter than the effective maturity of the related policy liabilities. Therefore, there is risk that the reinvestment of the proceeds at

the maturity of the initial investments may be at a yield below that of the interest required for the accretion of the policy liabilities. Additionally, there exists a future investment risk associated with certain policies currently in-force which will have premium receipts in the future. That is, the investment of these future premium receipts may be at a yield below that required to meet future policy liabilities.

In 2006, new money investment rates generally increased in the U.S., Japan and Taiwan, and were generally unchanged in Thailand. In regard to in-force business, management focus is required in both the investment and product management process to maintain an adequate yield to match the interest necessary to support future policy liabilities. Business strategies continue to evolve to maintain profitability of the overall business. In some countries, new products are being introduced with minimal investment guarantees resulting in a shift toward investment linked savings products and away from traditional savings products with higher guarantees.

The investment of insurance cash flows and reinvestment of the proceeds of matured securities and coupons requires active management of investment yields while maintaining satisfactory investment quality and liquidity.

AIG may use alternative investments in certain foreign jurisdictions where interest rates remain low and there are limited long-dated bond markets, including equities, real estate and foreign currency denominated fixed income instruments to extend the duration or increase the yield of the investment portfolio to more closely match the requirements of the policyholder liabilities and DAC recoverability. This strategy has been effectively used in Japan and more recently by Nan Shan in Taiwan. In Japan, foreign assets, excluding those matched to foreign liabilities, were approximately 30 percent of statutory assets, which is below the maximum allowable percentage under current local regulation. Foreign assets comprised approximately 32 percent of Nan Shan's invested assets at December 31, 2006, slightly below the maximum allowable percentage under current local regulation. The majority of Nan Shan's in-force policy portfolio is traditional life and endowment insurance products with implicit interest rate guarantees. New business with lower interest rate guarantees are gradually reducing the overall interest requirements, but asset portfolio yields have declined faster due to the prolonged low interest rate environment. As a result, although the investment margins for a large block of in-force policies are negative, the block remains profitable because the mortality and expense margins presently exceed the negative investment spread. In response to the low interest rate environment and the volatile exchange rate of the NT dollar, Nan Shan is emphasizing new products with lower implied guarantees, including participating endowments and investment linked products. Although the risks of a continued low interest rate environment coupled with a volatile NT dollar could increase net liabilities and require additional capital to maintain adequate local solvency margins, Nan Shan currently believes it has adequate resources to meet all future policy obligations.

AIG actively manages the asset-liability relationship in its domestic operations. This relationship is more easily managed through the availability of qualified long-term investments.

A number of guaranteed benefits, such as living benefits or guaranteed minimum death benefits, are offered on certain variable life and variable annuity products. AIG manages its exposure resulting from these long-term guarantees through reinsurance or capital market hedging instruments.

AIG invests in equities for various reasons, including diversifying its overall exposure to interest rate risk. Available for sale bonds and equity securities are subject to declines in fair value. Such declines in fair value are presented in unrealized appreciation or depreciation of investments, net of taxes, as a component of Accumulated other comprehensive income. Declines that are determined to be other-than-temporary are reflected in income in the period in which the intent to hold the securities to recovery no longer exists. See Valuation of Invested Assets herein. Generally, insurance regulations restrict the types of assets in which an insurance company may invest. When permitted by regulatory authorities and when deemed necessary to protect insurance assets, including invested assets, from adverse movements in foreign currency exchange rates, interest rates and equity prices, AIG and its insurance subsidiaries may enter into derivative transactions as end users to hedge their exposures. For a further discussion of AIG's use of derivatives, see Risk Management — Credit Risk Management — Derivatives herein.

In certain jurisdictions, significant regulatory and/or foreign governmental barriers exist which may not permit the immediate free flow of funds between insurance subsidiaries or from the insurance subsidiaries to AIG parent. For a discussion of these restrictions, see Item 1. Business — Regulation.

Life Insurance & Retirement Services invested assets grew by $37.0 billion, or 10 percent, during 2006 as bond holdings grew by $15.1 billion, or 6 percent, and listed equity holdings grew by $6.7 billion, or 41 percent. For a discussion of credit risk exposures, see Risk Management — Credit Risk Management herein.

Financial Services Invested Assets

ILFC

The cash used for the purchase of flight equipment is derived primarily from the proceeds of ILFC's debt financings. The primary sources for the repayment of this debt and the related interest expense are ILFC's cash flow from operations, proceeds from the sale of flight equipment and the rollover and refinancing of the prior debt. During 2006, ILFC acquired flight equipment costing $6.0 billion. For a further discussion of ILFC's borrowings, see Operating Review — Financial Services Operations — Aircraft Leasing and Capital Resources — Borrowings herein.

At December 31, 2006, ILFC had committed to purchase 254 new aircraft deliverable from 2007 through 2015 for an estimated aggregate purchase price of $19.0 billion. As of February 22, 2007, ILFC has entered into leases for all of the new aircraft to be delivered in 2007, and 64 of 171 of the new aircraft to be delivered subsequent to 2007. ILFC will be required to find customers for any aircraft currently on order and any aircraft to be

ordered, and it must arrange financing for portions of the purchase price of such equipment. ILFC has been successful to date both in placing its new aircraft on lease or under sales contract and obtaining adequate financing, but there can be no assurance that such success will continue in future environments.

Capital Markets

Capital Markets derivative transactions are carried at market value or at estimated fair value when market prices are not readily available. AIGFP reduces its economic risk exposure through similarly valued offsetting transactions including swaps, trading securities, options, forwards and futures. The estimated fair values of these transactions represent assessments of the present value of expected future cash flows. These transactions would be exposed to liquidity risk if AIGFP were required to sell or close out the transactions prior to maturity. AIG believes that the effect of any such event would not be significant to AIG's financial condition or its overall liquidity. For a further discussion on the use of derivatives by Capital Markets, see Operating Review — Financial Services Operations — Capital Markets and Risk Management — Derivatives herein and Note 19 of Notes to Consolidated Financial Statements.

AIGFP uses the proceeds from the issuance of notes and bonds and GIAs to invest in a diversified portfolio of securities, including securities available for sale, at market, and derivative transactions. The funds may also be invested in securities purchased under agreements to resell. The proceeds from the disposal of the aforementioned securities available for sale and securities purchased under agreements to resell are used to fund the maturing GIAs or other AIGFP financings, or invest in new assets. For a further discussion of AIGFP's borrowings, see Capital Resources — Borrowings herein.

Securities available for sale is predominately a diversified portfolio of high grade fixed income securities, where the individual securities have varying degrees of credit risk. At December 31, 2006, the average credit rating of this portfolio was in the AA+ category or the equivalent thereto as determined through rating agencies or internal review. AIGFP has also entered into credit derivative transactions to economically hedge its credit risk associated with $128 million of these securities. Securities deemed below investment grade at December 31, 2006 amounted to approximately $340 million in fair value, representing 0.7 percent of the total AIGFP securities available for sale. There have been no significant downgrades through February 15, 2007. If its securities available for sale portfolio were to suffer significant default and the collateral held declined significantly in value with no replacement or the credit default swap counterparty failed to perform, AIGFP could have a liquidity strain. AIG guarantees AIGFP's payment obligations, including its debt obligations.

AIGFP's exposure management objective is to minimize interest rate, currency, commodity and equity risks associated with its securities available for sale. That is, when AIGFP purchases a security for its securities available for sale investment portfolio, it simultaneously enters into an offsetting internal hedge such that the payment terms of the hedging transaction offset the payment terms of the investment security, which achieves the economic result of converting the return on the underlying security to U.S. dollar LIBOR plus or minus a spread based on the underlying profit on each security on the initial trade date. The market risk associated with such internal hedges is managed on a portfolio basis, with third-party hedging transactions executed as necessary. As hedge accounting treatment was not achieved in 2006, the unrealized gains and losses on the derivative transactions with unaffiliated third parties were reflected in operating income. The unrealized gains and losses on the underlying securities available for sale resulting from changes in interest rates and currency rates and commodity and equity prices were included in Accumulated other comprehensive income, or in operating income, as appropriate. When a security is sold, the realized gain or loss with respect to this security is then included in operating income.

Securities purchased under agreements to resell are treated as collateralized financing transactions. AIGFP takes possession of or obtains a security interest in securities purchased under agreements to resell.

AIGFP owns inventories in certain commodities in which it trades, and may reduce the exposure to market risk through the use of swaps, forwards, futures, and option contracts. Physical commodities held in AIGFP's wholly owned broker-dealer subsidiary are recorded at fair value. All other commodities are recorded at the lower of cost or market value.

Trading securities, at fair value, and securities and spot commodities sold but not yet purchased, at fair value, are marked to market daily with the unrealized gain or loss being recognized in income at that time. These trading securities are purchased and sold as necessary to meet the risk management objectives of Capital Markets operations.

The gross unrealized gains and gross unrealized losses of Capital Markets operations included in the financial services assets and liabilities at December 31, 2006 were as follows:

(in millions)	Gross Unrealized Gains	Gross Unrealized Losses
Securities available for sale, at fair value[(a)]	$ 1,575	$ 282
Unrealized gain/loss on swaps, options and forward transactions[(b)]	19,252	11,401

(a) See Note 8(i) of Notes to Consolidated Financial Statements.

(b) These amounts are also presented as the respective balance sheet amounts.

The senior management of AIG defines the policies and establishes general operating parameters for Capital Markets operations. AIG's senior management has established various oversight committees to monitor on an ongoing basis the various financial market, operational and credit risks attendant to the Capital Markets operations. The senior management of AIGFP reports the results of its operations to and reviews future strategies with AIG's senior management.

AIGFP actively manages the exposures to limit potential losses, while maximizing the rewards afforded by these business opportu-

nities. In doing so, AIGFP must continually manage a variety of exposures, including credit, market, liquidity, operational and legal risks.

Consumer Finance

AIG's Consumer Finance operations provide a wide variety of consumer finance products, including real estate and other consumer loans, credit card loans, retail sales finance and credit-related insurance to customers both domestically and overseas, particularly in emerging markets. These products are funded through a combination of deposits and various borrowings, including commercial paper and medium-term notes. AIG's Consumer Finance operations are exposed to credit risk and risk of loss resulting from adverse fluctuations in interest rates. Over half of the finance receivables are real estate loans which are substantially collateralized by the related properties.

With respect to credit losses, the allowance for losses is maintained at a level considered adequate to absorb anticipated credit losses existing in that portfolio as of the balance sheet date.

Asset Management Invested Assets

Asset Management invested assets are primarily comprised of assets supporting AIG's spread-based investment business, which includes AIG's MIP and domestic GIC programs as well as AIG's foreign spread-based business. Asset Management invested assets also include assets attributable to certain consolidated partnerships and variable interest entities. A portion of these consolidated assets is offset by minority interest liabilities attributable to unaffiliated investor entities in AIG-sponsored investment vehicles.

The spread-based investment business strategy is to produce cash flows greater than maturing liabilities. The asset-liability relationship is managed actively, leveraging the organization's experience in the Life Insurance & Retirement Services segment. Margins are emphasized while maintaining satisfactory investment quality and liquidity. The invested assets are predominantly fixed income securities for the spread-based investment business.

Asset Management invested assets grew by $14.3 billion, or 20 percent during 2006, although aggregate Asset Management fixed income investments remained essentially flat at $37.7 billion. The growth in invested assets was primarily attributable to increases in short-term investments, securities lending collateral and real estate investments. These increases were primarily driven by continued growth of the MIP and AIG's foreign spread-based business, and the growth of AIG's institutional Asset Management business. These increases were partially offset by the decrease in assets associated with the runoff of the domestic GIC program.

Valuation of Invested Assets

AIG has the ability to hold any fixed maturity security to its stated maturity, including those fixed maturity securities classified as available for sale. Therefore, the decision to sell any such fixed maturity security classified as available for sale reflects the judgment of AIG's management that the security sold is unlikely to provide, on a relative value basis, as attractive a return in the future as alternative securities entailing comparable risks. With respect to distressed securities, the sale decision reflects management's judgment that the risk-discounted anticipated ultimate recovery is less than the value achievable on sale.

Traded Securities

The valuation of AIG's investment portfolio involves obtaining a market value for each security. The source for the fair value is generally from market exchanges or dealer quotations, with the exception of nontraded securities. AIG considers nontraded securities to mean certain fixed income investments, certain structured securities, direct private equities, limited partnerships, and hedge funds.

Nontraded Securities

The aggregate carrying value of AIG's nontraded securities at December 31, 2006 was approximately $67 billion. The methodology used to estimate fair value of nontraded fixed income investments is by reference to traded securities with similar attributes and using a matrix pricing methodology. This methodology takes into account such factors as the issuer's industry, the security's rating and tenor, its coupon rate, its position in the capital structure of the issuer, and other relevant factors. The change in fair value is recognized as a component of Accumulated other comprehensive income, net of tax.

For certain structured securities, the carrying value is based on an estimate of the security's future cash flows pursuant to the requirements of Emerging Issues Task Force Issue No. 99-20, ''Recognition of Interest Income and Impairment on Purchased and Retained Beneficial Interests in Securitized Financial Assets.'' The change in carrying value is recognized in income.

Hedge funds and limited partnerships in which AIG holds in the aggregate less than a five percent interest are carried at fair value. The change in fair value is recognized as a component of Accumulated other comprehensive income, net of tax.

With respect to hedge funds and limited partnerships in which AIG holds in the aggregate a five percent or greater interest, or less than a five percent interest but where AIG has more than a minor influence over the operations of the investee, AIG accounts for these investments using the equity method. The changes in such net asset values are included in operating income.

AIG obtains the fair value of its investments in limited partnerships and hedge funds from information provided by the general partner or manager of each of these investments, the accounts of which generally are audited on an annual basis.

Each of these investment categories is regularly tested to determine if impairment in value exists. Various valuation techniques are used with respect to each category in this determination.

Portfolio Review

AIG periodically evaluates its securities for other-than-temporary impairments in valuation. As a matter of policy, the determination that a security has incurred an other-than-temporary decline in value and the amount of any loss recognition requires the judgment of AIG's management and a continual review of its investments. See Note 1(e) of Notes to Consolidated Financial Statements for further information on AIG's policy.

Once a security has been identified as other-than-temporarily impaired, the amount of such impairment is determined by reference to that security's contemporaneous market price and recorded as a charge to earnings.

As a result of these policies, AIG recorded, in realized capital gains (losses), other-than-temporary impairment pretax losses of $944 million, $598 million and $684 million in 2006, 2005 and 2004, respectively. Just over half of other-than-temporary impairment charges in 2006 were a result of the decision not to hold these investment securities until they fully recover in value. The writedowns recorded in 2005 and 2004 were primarily the result of adverse changes in the creditworthiness of the issuer.

No impairment charge with respect to any one single credit was significant to AIG's consolidated financial condition or results of operations, and no individual impairment loss exceeded 1.0 percent of consolidated net income for 2006.

Excluding the other-than-temporary impairments noted above, the changes in fair value for AIG's available for sale portfolio, which constitutes the vast majority of AIG's investments, were recorded in Accumulated other comprehensive income as unrealized gains or losses, net of tax.

At December 31, 2006, aggregate pretax unrealized gains were $17.5 billion, while the pretax unrealized losses with respect to investment grade bonds, non-investment grade bonds and equity securities were $3.6 billion, $134 million and $159 million, respectively. Aging of the pretax unrealized losses with respect to these securities, distributed as a percentage of cost relative to unrealized loss (the extent by which the fair value is less than amortized cost or cost), including the number of respective items, was as follows:

	Less than or equal to 20% of Cost[a]			Greater than 20% to 50% of Cost[a]			Greater than 50% of Cost[a]			Total		
Aging *(dollars in millions)*	Cost[a]	Unrealized Loss	Items	Cost[a]	Unrealized Loss	Items	Cost[a]	Unrealized Loss	Items	Cost[a]	Unrealized Loss[b]	Items
Investment grade bonds												
0-6 months	$ 28,869	$ 376	3,941	$ 74	$17	9	$ —	$ —	—	$ 28,943	$ 393	3,950
7-12 months	37,835	777	4,876	—	—	—	—	—	—	37,835	777	4,876
>12 months	82,945	2,377	10,640	10	4	5	—	—	—	82,955	2,381	10,645
Total	$149,649	$3,530	19,457	$ 84	$21	14	$ —	$ —	—	$149,733	$3,551	19,471
Below investment grade bonds												
0-6 months	$ 1,828	$ 56	341	$ 3	$ 1	5	$ 1	$ 1	4	$ 1,832	$ 58	350
7-12 months	1,043	28	146	3	1	4	—	—	—	1,046	29	150
>12 months	1,085	47	201	—	—	—	—	—	—	1,085	47	201
Total	$ 3,956	$ 131	688	$ 6	$ 2	9	$ 1	$ 1	4	$ 3,963	$ 134	701
Total bonds												
0-6 months	$ 30,697	$ 432	4,282	$ 77	$18	14	$ 1	$ 1	4	$ 30,775	$ 451	4,300
7-12 months	38,878	805	5,022	3	1	4	—	—	—	38,881	806	5,026
>12 months	84,030	2,424	10,841	10	4	5	—	—	—	84,040	2,428	10,846
Total	$153,605	$3,661	20,145	$ 90	$23	23	$ 1	$ 1	4	$153,696	$3,685	20,172
Equity securities												
0-6 months	$ 2,042	$ 86	1,309	$ 68	$20	54	$ 1	$ —	3	$ 2,111	$ 106	1,366
7-12 months	566	36	309	56	16	72	1	1	3	623	53	384
>12 months	—	—	—	—	—	—	—	—	—	—	—	—
Total	$ 2,608	$ 122	1,618	$124	$36	126	$ 2	$ 1	6	$ 2,734	$ 159	1,750

(a) For bonds, represents amortized cost.

(b) As more fully described above, upon realization, certain realized losses will be charged to participating policyholder accounts, or realization will result in a current decrease in the amortization of DAC.

At December 31, 2006, the fair value of AIG's fixed maturities and equity securities aggregated $496.0 billion. At December 31, 2006, aggregate unrealized gains after taxes for fixed maturity and equity securities were $11.4 billion. At December 31, 2006, the aggregate unrealized losses after taxes of fixed maturity and equity securities were approximately $2.5 billion.

The effect on net income of unrealized losses after taxes will be mitigated upon realization because certain realized losses will be charged to participating policyholder accounts, or realization will result in current decreases in the amortization of certain DAC.

At December 31, 2006, unrealized losses for fixed maturity securities and equity securities did not reflect any significant industry concentrations.

The amortized cost of fixed maturities available for sale in an unrealized loss position at December 31, 2006, by contractual maturity, is shown below:

(in millions)	Amortized Cost
Due in one year or less	$ 6,139
Due after one year through five years	31,839
Due after five years through ten years	51,084
Due after ten years	64,634
Total	$153,696

For the year ended December 31, 2006, the pretax realized losses incurred with respect to the sale of fixed maturities and equity securities were $1.3 billion. The aggregate fair value of securities sold was $43 billion, which was approximately 97 percent of amortized cost. The average period of time that securities sold at a loss during the year ended December 31, 2006 were trading continuously at a price below book value was approximately four months. See Risk Management — Investments herein for an additional discussion of investment risks associated with AIG's investment portfolio.

Risk Management

Overview

AIG believes that strong risk management practices and a sound internal control environment are fundamental to its continued success and profitable growth. Failure to manage risk properly could expose AIG to significant losses, regulatory issues and a damaged reputation.

The major risks to which AIG is exposed include the following:

- *Insurance risk* — the potential loss resulting from ultimate claims and expenses exceeding held reserves.
- *Credit risk* — the potential loss arising from an obligor's inability or unwillingness to meet its obligations to AIG.
- *Market risk* — the potential loss arising from adverse fluctuations in interest rates, foreign currencies, equity and commodity prices, and their levels of volatility.
- *Operational risk* — the potential loss resulting from inadequate or failed internal processes, people, and systems, or from external events.

AIG senior management establishes the framework, principles and guidelines for risk management. The business executives are responsible for establishing and implementing risk management processes and responding to the individual needs and issues within their business, including risk concentrations within their business segments.

Corporate Risk Management

AIG's major risks are addressed at the corporate level through the Enterprise Risk Management Department (ERM). ERM is headed by AIG's Chief Risk Officer (CRO) and is responsible for assisting AIG's business leaders, executive management and the Board of Directors to identify, assess, quantify, manage and mitigate the risks incurred by AIG. An important goal of ERM is to ensure that once appropriate governance, authorities, procedures and policies have been established, aggregated risks do not result in inappropriate concentrations.

Senior management defines the policies, has established general operating parameters for its global businesses and has established various oversight committees to monitor the risks attendant to its businesses:

- The Credit Risk Committee (CRC) is responsible for (i) approving credit risk policies and procedures for use throughout AIG; (ii) delegating credit authority to business unit credit officers and select business unit managers; (iii) approving transaction requests and limits for corporate, sovereign and cross-border credit exposures that exceed the delegated authorities; (iv) establishing and maintaining AIG's risk rating process for corporate, financial and sovereign obligors; and (v) regular reviews of credit risk exposures in the portfolios of all credit-incurring business units.
- The Financial Risk Committee (FRC) oversees AIG's market risk exposures to interest rates, foreign exchange and equity prices and provides strategic direction for AIG's asset-liability management. The FRC meets monthly and acts as a central mechanism for AIG senior management to review comprehensive information on AIG's financial exposures and to exercise broad control over these exposures.
- The Foreign Exchange Committee (FEC) monitors trends in foreign exchange rates, reviews AIG's foreign exchange exposures, and provides recommendations on foreign currency asset allocation and remittance hedging.
- The Derivatives Review Committee (DRC) provides an independent review of any proposed derivative transaction or program not otherwise managed by AIGFP. The DRC examines, among other things, the nature and purpose of the derivative transaction, its potential credit exposure, if any, and the estimated benefits.
- The Complex Structured Finance Transaction Committee (CSFTC) has the authority and responsibility to review and approve proposed transactions that could subject AIG to heightened legal, reputational, accounting, or regulatory risk (CSFTs). The CSFTC provides guidance to and monitors the activities of transaction review committees (TRCs) which have been established in all major business units. TRCs have the responsibility to identify, review and refer CSFTs to the CSFTC.

Credit Risk Management

Credit risk is one of AIG's largest single business risks and AIG devotes considerable resources, expertise and controls to managing its credit exposures. Credit risk is defined as the risk that AIG's customers or counterparties are unable or unwilling to repay their contractual obligations when they come due. Credit risk may also be manifested: (i) through the downgrading of credit ratings of counterparties whose credit instruments AIG may be holding, or, in some cases, insuring, causing the value of the assets to decline or insured risks to rise and (ii) as cross-border risk where a country (sovereign government risk) or one or more non-sovereign obligors within a country are unable to repay an obligation or are unable to provide foreign exchange to service a credit or equity exposure incurred by another AIG business unit located outside that country.

AIG's credit risks are managed at the corporate level by the Credit Risk Management Department (CRM) whose primary role is to support and supplement the work of the CRC. CRM is headed by AIG's Chief Credit Officer (CCO), who reports to AIG's CRO. AIG's CCO is primarily responsible for the development and maintenance of credit risk policies and procedures approved by the CRC. In discharging this function CRM has the following responsibilities:

- Manage the approval process for all requests for credit limits, program limits and transactions.
- Approve delegated credit authorities to CRM credit executives and business unit credit officers.
- Aggregate globally all credit exposure data by counterparty, country and industry and report risk concentrations regularly to the CRC.
- Administer regular portfolio credit reviews of all investment, derivative and credit-incurring business units.
- Develop methodologies for quantification and assessment of credit risks, including the establishment and maintenance of AIG's internal risk rating process.
- Approve appropriate credit reserves and methodologies at the business unit and enterprise levels.

AIG closely monitors and controls its company-wide credit risk concentrations and attempts to avoid unwanted or excessive risk accumulations, whether funded or unfunded. To minimize the level of credit risk in certain circumstances, AIG may require collateral, guarantees and/or reinsurance support such as letters of credit.

AIG defines its aggregate credit exposures to a counterparty as the sum of its fixed maturities, loans, derivatives (mark to market), deposits (in the case of financial institutions) and the specified credit equivalent exposure to certain insurance products which embody credit risk.

The following table presents AIG's largest credit exposures at December 31, 2006 as a percentage of total shareholders' equity.

Category	Risk Rating[a]	Credit Exposure as a percentage of Total Shareholders' Equity
Investment Grade:		
10 largest combined	AA (weighted average)[b]	73.5%
Single largest non-sovereign (financial institution)	AA	7.4
Single largest corporate	AAA	5.6
Single largest sovereign	AA–	14.3
Non-Investment Grade:		
Single largest sovereign	BB	1.4
Single largest non-sovereign	BB	0.6

(a) Risk rating is based on external ratings, or equivalent, based on AIG's internal risk rating process.

(b) Six are highly-rated financial institutions and three are investment-grade rated sovereigns; none is rated lower than BBB+ or its equivalent.

AIG closely controls its aggregate cross-border exposures to avoid excessive concentrations in any one country or regional group of countries. AIG defines its cross-border exposure to include both cross-border credit exposures and its large cross-border investments in its own international subsidiaries. Nine countries had cross-border exposures in excess of 10 percent of total shareholders' equity; seven are AAA-rated and two are AA-rated.

In addition, AIG closely monitors its industry concentrations, the risks of which are often mitigated by the breadth and scope of AIG's international operations.

- AIG's single largest industry credit exposure is to the highly-rated global financial institutions sector, accounting for 72 percent of total shareholders' equity at December 31, 2006.
- AIG's other industry credit concentrations in excess of 10 percent of total shareholders' equity at December 31, 2006 exist to the following industries (in descending order by approximate size):
  - global telecommunications companies;
  - U.S. residential mortgages;
  - global life insurance carriers;
  - U.S.-based regional financial institutions;
  - U.S. commercial mortgages;
  - global reinsurance firms; and
  - global securities firms.

The CRC reviews quarterly concentration reports in all categories listed above as well as credit trends by risk ratings. The CRC may adjust limits to provide reasonable assurance that AIG does not incur excessive levels of credit risk and that AIG's credit risk profile is properly calibrated across business units.

Market Risk Management

AIG seeks to minimize market risks by matching the market risks in its assets with the market risks in its liabilities. Nevertheless, AIG does have net exposure to market risks, primarily within its insurance businesses. These asset-liability exposures are predominantly structural in nature, and not the result of speculative positioning to take advantage of short-term market opportunities. The Market Risk Management Department (MRM), which reports to the CRO, is responsible for control and oversight of market risks in all aspects of AIG's financial services, insurance, and investment activities.

AIG's market exposures arise from the following:

- AIG is a globally diversified enterprise with capital deployed in a variety of currencies. Capital deployed in AIG's overseas businesses, when converted into U.S. dollars for financial reporting purposes, constitutes a ''long foreign currency/short U.S. dollar'' market exposure on AIG's balance sheet. Similarly, overseas earnings denominated in foreign currency also represent a ''long foreign currency/short U.S. dollar'' market exposure on AIG's income statement.
- Much of AIG's domestic capital is invested in fixed income or equity securities, leading to exposures to U.S. yields and equity markets.
- Several of AIG's Foreign Life subsidiaries operate in developing markets where maturities on longer-term life insurance liabilities exceed the maximum maturities of available local currency assets.

AIG analyzes market risk using various statistical techniques including Value at Risk (VaR). VaR is a summary statistical measure that uses the estimated volatility and correlation of market factors to calculate the maximum loss that could occur over a defined period of time given a certain probability. VaR measures not only the size of individual exposures but also the interaction between different market exposures, thereby providing a portfolio approach to measuring market risk. Substantially similar VaR methodologies are used to determine capital requirements for market risk within AIG's economic capital framework.

While VaR models are relatively sophisticated, their results are limited by the assumptions and parameters used in these models. AIG believes that statistical models alone do not provide a reliable method of monitoring and controlling market risk. Therefore, such models are tools and do not substitute for the experience or judgment of senior management.

Insurance, Asset Management and Non-Trading Financial Services VaR

AIG has performed one comprehensive VaR analysis across all of its non-trading businesses, and a separate VaR analysis for its trading business at AIGFP. The comprehensive VaR is categorized by AIG business segment (General Insurance, Life Insurance & Retirement Services, Financial Services and Asset Management) and also by market risk factor (interest rate, currency and equity).

For the insurance segments, assets included are invested assets (excluding real estate and investment income due and accrued), and liabilities included are reserve for losses and loss expenses, reserve for unearned premiums, future policy benefits for life and accident and health insurance contracts and other policyholders' funds. For financial services companies, loans and leases represent the majority of assets represented in the VaR calculation, while bonds and notes issued represent the majority of liabilities.

AIG calculated the VaR with respect to net fair values as of December 31, 2006 and 2005. The VaR number represents the maximum potential loss as of those dates that could be incurred with a 95 percent confidence (i.e., only five percent of historical scenarios show losses greater than the VaR figure) within a one-month holding period. AIG uses the historical simulation methodology that entails repricing all assets and liabilities under explicit changes in market rates within a specific historical time period. AIG uses the most recent three years of historical market information for interest rates, foreign exchange rates, and equity index prices. For each scenario, each transaction was repriced. Segment and AIG-wide scenario values are then calculated by netting the values of all the underlying assets and liabilities.

The following table presents the year-end, average, high and low VaRs on a diversified basis and of each component of market risk for each of AIG's non-trading investments as of December 31, 2006 and 2005. The diversified VaR is usually smaller than the sum of its components due to correlation effects.

		For the Year Ended December 31, 2006				For the Year Ended December 31, 2005		
(in millions)	As of December 31	Average	High	Low	As of December 31	Average	High	Low
Total AIG Non-Trading								
Market risk:								
Diversified	**$ 5,073**	**$ 5,209**	**$ 5,783**	**$ 4,852**	$ 5,186	$5,353	$5,543	$5,186
Interest rate	**4,577**	**4,962**	**5,765**	**4,498**	4,869	4,963	5,223	4,707
Currency	**686**	**641**	**707**	**509**	667	622	667	532
Equity	**1,873**	**1,754**	**1,873**	**1,650**	1,650	2,113	2,358	1,650
General Insurance:								
Market risk:								
Diversified	**$ 1,717**	**$ 1,697**	**$ 1,776**	**$ 1,617**	$ 1,617	$1,585	$1,672	$1,396
Interest rate	**1,541**	**1,635**	**1,717**	**1,541**	1,717	1,746	1,931	1,563
Currency	**212**	**162**	**212**	**119**	130	125	139	111
Equity	**573**	**551**	**573**	**535**	535	651	727	535
Life Insurance & Retirement Services:								
Market risk:								
Diversified	**$ 4,574**	**$ 4,672**	**$ 5,224**	**$ 4,307**	$ 4,307	$4,710	$5,088	$4,307
Interest rate	**4,471**	**4,563**	**5,060**	**4,229**	4,277	4,425	4,715	4,277
Currency	**568**	**538**	**592**	**459**	538	515	556	441
Equity	**1,293**	**1,228**	**1,299**	**1,133**	1,133	1,396	1,559	1,133
Non-Trading Financial Services:								
Market risk:								
Diversified	**$ 125**	**$ 165**	**$ 252**	**$ 125**	$ 252	$ 161	$ 252	$ 85
Interest rate	**127**	**166**	**249**	**127**	249	165	249	85
Currency	**11**	**8**	**11**	**7**	10	7	10	4
Equity	**1**	**1**	**2**	**1**	2	2	2	1
Asset Management:								
Market risk:								
Combined	**$ 64**	**$ 144**	**$ 190**	**$ 64**	$ 186	$ 148	$ 186	$ 113
Interest rate	**63**	**145**	**192**	**63**	189	137	189	101
Currency	**3**	**4**	**7**	**3**	4	2	4	2
Equity	**8**	**9**	**13**	**8**	13	75	178	13

AIG's total VaR declined from $5.2 billion at the end of 2005 to $5.1 billion at the end of 2006, even as the diversified VaR in each of the Insurance segments grew modestly. Two factors contributed to the decline in total VaR. A reduction in interest rate volatility in many currencies moderated AIG's interest rate risk profile, and higher correlations between the long asset duration exposure in U.S. fixed income and long liability duration exposures in many emerging markets provided a greater diversification benefit during 2006. Lower VaR figures in both the Financial Services and Asset Management segments during 2006 were the result of a combination of closer duration matching and a reduction of interest rate volatility.

Operational Risk Management

AIG has established a corporate-level Operational Risk Management Department (ORM) to oversee AIG's operational risk management practices. The Director of ORM reports to the CRO. ORM is responsible for establishing the framework, principles and guidelines for operational risk management. This framework also utilizes the risk management efforts of AIG's compliance, legal and regulatory and internal audit functions. ORM also manages compliance with the requirements of the Sarbanes-Oxley Act of 2002.

Each business is responsible for implementing the components of AIG's operational risk management program to ensure that effective operational risk management practices are utilized throughout AIG. These components include governance, risk and control self assessment, risk event data analysis, and key risk indicators. The program currently incorporates the following:

- *Governance*

Strong governance sets the appropriate tone to enable effective management of the risks inherent in each of AIG's businesses, as well as aid in the management of reputational risk. Each AIG business is responsible for maintaining appropriate governance over its management of operational risk. This respon-

sibility includes developing and implementing policies, procedures, management oversight processes, and other governance-related activities consistent with AIG's overall operational risk management process.

- *Risk and Control Self Assessment*

AIG's operational risk management program includes a self assessment process. The self assessment process is used to identify key operational risks in a business and evaluate the effectiveness of existing controls to mitigate those risks, as well as develop corrective action plans for identified deficiencies.

Insurance Risk Management

Reinsurance

AIG uses reinsurance programs for its general insurance risks as follows: (i) facultative to cover large individual exposures; (ii) quota share treaties to cover specific books of business; (iii) excess of loss treaties to cover large losses; and (iv) catastrophe treaties to cover certain catastrophes including earthquake, flood, wind and terror. AIG's Reinsurance Security Department conducts periodic detailed assessments of the reinsurance markets and current and potential reinsurers, both foreign and domestic. Such assessments may include, but are not limited to, identifying if a reinsurer is appropriately licensed and has sufficient financial capacity, and evaluating the local economic environment in which a foreign reinsurer operates.

AIG enters into intercompany reinsurance transactions, primarily through AIRCO, for its General Insurance and Life Insurance & Retirement Services operations. AIG enters into these transactions as a sound and prudent business practice in order to maintain underwriting control and spread insurance risk among AIG's various legal entities. AIG generally obtains letters of credit from third-party financial institutions in order to obtain statutory recognition of these intercompany reinsurance transactions. At December 31, 2006, approximately $4.0 billion of letters of credit were outstanding to cover intercompany reinsurance transactions with AIRCO or other General Insurance subsidiaries.

Although reinsurance arrangements do not relieve AIG subsidiaries from their direct obligations to insureds, an efficient and effective reinsurance program substantially limits AIG's exposure to potentially significant losses. AIG continually evaluates the reinsurance markets and the relative attractiveness of various arrangements for coverage, including structures such as catastrophe bonds, insurance risk securitizations and ''sidecar'' and similar vehicles.

Effective July 15, 2006, Lexington and Concord Re Limited (Concord Re), a ''sidecar'' reinsurer that was established exclusively to reinsure Lexington, entered into a quota share reinsurance agreement covering the U.S. commercial property insurance business written by Lexington. Concord Re was capitalized with approximately $730 million through the issuance of equity securities and loans from third party investors. AIG and its subsidiaries invest in a wide variety of investment vehicles managed by third parties where AIG has no control over investment decisions. Accordingly, there can be no assurance that such vehicles do not, or will not, hold securities of Concord Re.

Reinsurance Recoverable

The Reinsurance Security Department reviews the nature of the risks ceded to reinsurers and the requirements for credit risk mitigants. For example, in AIG's treaty reinsurance contracts, AIG frequently includes provisions that require a reinsurer to post collateral when a referenced event occurs. Furthermore, AIG limits its unsecured exposure to reinsurers through the use of credit triggers, which include, but are not limited to, insurer financial strength rating downgrades, declines in policyholders surplus below predetermined levels or reaching maximum limits of reinsurance recoverable. In addition, AIG's CRC reviews all reinsurer exposures and credit limits and approves most large reinsurer credit limits that represent actual or potential credit concentrations. AIG believes that no exposure to a single reinsurer represents an inappropriate concentration of risk to AIG, nor is AIG's business substantially dependent upon any single reinsurance contract.

AIG's consolidated general reinsurance assets amounted to $21.8 billion at December 31, 2006. AIG manages the credit risk in its reinsurance relationships by transacting with reinsurers that it considers financially sound, and when necessary AIG holds substantial collateral in the form of funds, securities and/or irrevocable letters of credit. This collateral can be drawn on for amounts that remain unpaid beyond specified time periods on an individual reinsurer basis. At December 31, 2006, approximately 54 percent of the general reinsurance assets were from unauthorized reinsurers. Many of these balances were collateralized, permitting statutory recognition. Additionally, with the approval of insurance regulators, AIG posted approximately $2 billion of letters of credit issued by commercial banks in favor of certain Domestic General Insurance companies to permit those companies statutory recognition of balances otherwise uncollateralized at December 31, 2006. The remaining 46 percent of the general reinsurance assets were from authorized reinsurers. The terms authorized and unauthorized pertain to regulatory categories, not creditworthiness. At December 31, 2006, approximately 85 percent of the balances with respect to authorized reinsurers are from reinsurers rated A (excellent) or better, as rated by A.M. Best, or A (strong) or better, as rated by S&P. These ratings are measures of financial strength.

The following table provides information for each reinsurer representing in excess of five percent of AIG's general reinsurance assets at December 31, 2006.

(in millions)	S&P Rating	A.M. Best Rating	Gross Reinsurance Assets	Percent of General Reinsurance Assets, Net	Collateral Held[(a)]	Uncollateralized Reinsurance Assets
Reinsurer:						
Swiss Reinsurance Group	AA-	A+	$2,032	9.3%	$339	$1,693
Berkshire Hathaway Insurance Group	AAA	A++	$1,575	7.2%	$144	$1,431
Munich Reinsurance Group	AA-	A+	$1,268	5.8%	$341	$ 927
Lloyd's Syndicates — Lloyd's of London[(b)]	A	A	$1,250	5.7%	$101	$1,149

(a) Excludes collateral held in excess of applicable treaty balances.

(b) Excludes Equitas gross reinsurance assets that are unrated, which are less than five percent of AIG's general reinsurance assets.

At December 31, 2006, consolidated general reinsurance assets of $21.8 billion include reinsurance recoverables for paid losses and loss expenses of $1.0 billion and $17.3 billion with respect to the ceded reserve for losses and loss expenses, including ceded losses IBNR (ceded reserves) and $3.5 billion of ceded reserve for unearned premiums. The ceded reserve for losses and loss expenses represent the accumulation of estimates of ultimate ceded losses including provisions for ceded IBNR and loss expenses. The methods used to determine such estimates and to establish the resulting ceded reserves involve significant judgment in projecting the frequency and severity of losses over multiple years and are continually reviewed and updated by management. Any adjustments thereto are reflected in income currently. It is AIG's belief that the ceded reserves for losses and loss expenses at December 31, 2006 were representative of the ultimate losses recoverable. In the future, as the ceded reserves continue to develop to ultimate amounts, the ultimate loss recoverable may be greater or less than the reserves currently ceded.

AIG maintains an allowance for estimated unrecoverable reinsurance of $536 million. The allowance was reduced substantially during 2006, as uncollectible amounts due from individual reinsurers were charged off against the allowance, primarily as a result of the balance sheet reconciliation remediation process; in addition, a portion of the allowance was reclassified to align it with the related receivable. The reduction for charge offs was partially offset by additional provisions totaling $147 million during 2006. At December 31, 2006, AIG had no significant reinsurance recoverables due from any individual reinsurer that was financially troubled (i.e., liquidated, insolvent, in receivership or otherwise subject to formal or informal regulatory restriction).

Segment Risk Management

Other than as described above, AIG manages its business risk oversight activities through its business segments.

Insurance Operations

AIG's multiple insurance businesses conducted on a global basis expose AIG to a wide variety of risks with different time horizons. These risks are managed throughout the organization, both centrally and locally, through a number of procedures, including: (i) pre-launch approval of product design, development and distribution; (ii) underwriting approval processes and authorities; (iii) exposure limits with ongoing monitoring; (iv) modeling and reporting of aggregations and limit concentrations at multiple levels (policy, line of business, product group, country, individual/group, correlation and catastrophic risk events); (v) compliance with financial reporting and capital and solvency targets; (vi) extensive use of reinsurance, both internal and third-party; and (vii) review and establishment of reserves.

AIG has two major categories of insurance risks as follows:

- *General Insurance* — risks covered include property, casualty, fidelity/surety, management liability and mortgage insurance. Risks in the general insurance segment are managed through aggregations and limitations of concentrations at multiple levels: policy, line of business, correlation and catastrophic risk events.
- *Life Insurance & Retirement Services* — risks include mortality and morbidity in the insurance-oriented products and insufficient cash flows to cover contract liabilities in the retirement savings-oriented products. In the Life Insurance & Retirement Services segment, risk is aggregated and limited by individual/group, product group, country and catastrophic risk events.

AIG closely manages insurance risk by overseeing and controlling the nature and geographic location of the risks in each line of business underwritten, the terms and conditions of the underwriting and the premiums charged for taking on the risk. Concentrations of risk primarily arise from external events, such as wind, flood, earthquake, terrorism and pandemics, which are analyzed using various modeling techniques.

AIG is a major purchaser of reinsurance for its insurance operations. The use of reinsurance facilitates insurance risk management (retention, volatility, concentrations) and capital planning locally (branch and subsidiary). Pooling of AIG's reinsurance risks enables AIG to purchase reinsurance more efficiently at a consolidated level, manage global counterparty risk and relationships and manage global catastrophe risks, both for the General Insurance and Life Insurance & Retirement Services businesses.

General Insurance

In General Insurance, underwriting risks are managed through the application approval process, exposure limitations as well as through exclusions, coverage limits and reinsurance. The risks covered by AIG are managed through limits on delegated under-

writing authority, the use of sound underwriting practices, pricing procedures and the use of actuarial analysis as part of the determination of overall adequacy of provisions for insurance contract liabilities.

A primary goal of AIG in managing its General Insurance operations is to achieve an underwriting profit. To achieve this goal, AIG must be disciplined in its risk selection, and premiums must be adequate and terms and conditions appropriate to cover the risk accepted.

Catastrophe Exposures

The nature of AIG's business exposes it to various catastrophic risk events in which multiple losses across multiple lines of business can occur in any calendar year. In order to control this exposure, AIG uses a combination of techniques, including setting aggregate limits in key business units, monitoring and modeling accumulated exposures and purchasing catastrophe reinsurance to supplement its other reinsurance protections.

Natural disasters such as hurricanes, earthquakes and other catastrophes have the potential to adversely affect AIG's operating results. Other risks, such as an outbreak of a pandemic disease, such as the Avian Influenza A Virus (H5N1), could adversely affect AIG's business and operating results to an extent that may be only partially offset by reinsurance programs.

AIG evaluates catastrophic events and assesses the probability of occurrence and magnitude of catastrophic events through the use of state-of-the-art industry recognized models, among other techniques. AIG supplements these models by periodically monitoring the risk exposure of AIG's worldwide General Insurance operations and adjusting such models accordingly. Following is an overview of modeled losses associated with the more significant natural perils, which includes exposures for DBG, Personal Lines, Foreign General (other than Ascot), HSB and 21st Century. Transatlantic and Ascot utilize a different model, and their combined results are presented separately below. The modeled results assume that all reinsurers fulfill their obligations to AIG in accordance with their terms.

It is important to recognize that there is no standard methodology to project the possible losses from total property and workers compensation exposures. Further, there are no industry standard assumptions to be utilized in projecting these losses. The use of different methodologies and assumptions could materially change the projected losses. Therefore, these modeled losses may not be comparable to estimates made by other companies.

These estimates are inherently uncertain and may not reflect AIG's maximum exposures to these events. It is highly likely that AIG's losses will vary, perhaps significantly, from these estimates.

The modeled results provided in the table below were based on the aggregate exceedence probability (AEP) losses which represent total property and workers compensation losses that may occur in any single year from one or more natural events. The model, which has been updated to reflect 2005 catastrophes, generally used exposure data as of mid-year 2006 and the current reinsurance program structure. The values provided were based on 100-year return period losses, which have a one percent likelihood of being exceeded in any single year. Thus, the model projects that there is a one percent probability that AIG could incur in any year losses in excess of the modeled amounts for these perils.

(in millions)	Gross	Net of Reinsurance	Net, After Income Taxes	Percentage of Total Shareholders' Equity at December 31, 2006
Natural Peril:				
Earthquake	$3,676	$2,474	$1,608	1.6%
Tropical Cyclone*	$4,780	$3,196	$2,077	2.0%

** Includes hurricanes, typhoons and other wind-related events.*

The combined earthquake and tropical cyclone 100-year return period modeled losses for Ascot and Transatlantic together are estimated to be $1.1 billion, on a gross basis, $761 million, net of reinsurance, and $494 million, net after income taxes, or 0.5 percent of total shareholders' equity at December 31, 2006.

In addition, AIG evaluates potential single event earthquake and hurricane losses that may be incurred. The single events utilized are a subset of potential events identified and utilized by Lloyd's[1] and referred to as Realistic Disaster Scenarios (RDSs). The purpose of this analysis is to utilize these RDSs to provide a reference frame and place into context the model results. However, it is important to note that the specific events used for this analysis do not necessarily represent the worst case loss that AIG could incur from this type of an event in these regions. The losses associated with the RDSs are included in the table below.

Single event modeled property and workers compensation losses to AIG's worldwide portfolio of risk for key geographic areas. Gross values represent AIG's liability after the application of policy limits and deductibles, and net values represent losses after all reinsurance is applied.

(in millions)	Gross	Net of Reinsurance
Natural Peril:		
Miami Hurricane	$4,493	$2,798
San Francisco Earthquake	4,029	2,613
Northeast Hurricane	3,711	2,592
Los Angeles Earthquake	3,508	2,440
Gulf Coast Hurricane	2,609	1,717
Japanese Earthquake	553	150
European Windstorm	230	83
Japanese Typhoon	178	143

(1) Lloyd's Realistic Disaster Scenarios, Scenario Specifications, April 2006

The specific international RDS events do not necessarily correspond to AIG's international exposures. As a result, AIG runs its own simulations where statistical return period losses associated with the written exposure specific to AIG provide the basis for monitoring risk. Based on these simulations, the 100-year return period for Japanese Earthquake is $296 million gross, and $120 million net, the 100-year return period for European Windstorm is $269 million gross, and $80 million net, and the 100-year return period for Japanese Typhoon is $306 million gross, and $252 million net.

ACTUAL RESULTS IN ANY PERIOD ARE LIKELY TO VARY, PERHAPS MATERIALLY, FROM THE MODELED SCENARIOS, AND THE OCCURRENCE OF ONE OR MORE SEVERE EVENTS COULD HAVE A MATERIAL ADVERSE EFFECT ON AIG'S FINANCIAL CONDITION, RESULTS OF OPERATIONS AND LIQUIDITY.

Measures Implemented to Control Hurricane and Earthquake Catastrophic Risk

Catastrophic risk from the earthquake and hurricane perils is proactively managed through reinsurance programs, and aggregate accumulation monitoring. Catastrophe reinsurance is purchased by AIG from financially sound reinsurers. Recoveries under this program, along with other non-catastrophic reinsurance protections, are reflected in the net values provided in the tables above. In addition to catastrophic reinsurance programs, hurricane and earthquake exposures are controlled by periodically monitoring aggregate exposures. The aggregate exposures are calculated by compiling total liability within AIG defined hurricane and earthquake catastrophe risk zones and therefore represent the maximum that could be lost in any individual zone. These aggregate accumulations are tracked over time in order to monitor both long and short term trends. AIG's major property writers, Lexington and AIG private client group, have also implemented catastrophe-related underwriting procedures and manage their books at an account level. Lexington individually models most accounts prior to binding in order to specifically quantify catastrophic risk for each account.

Terrorism

Exposure to loss from terrorist attack is controlled by limiting the aggregate accumulation of workers compensation and property insurance that is underwritten within defined target locations. Modeling is used to provide projections of probable maximum loss by target location based upon the actual exposures of AIG policyholders.

Terrorism risk is monitored to manage AIG's exposure. AIG shares its exposures to terrorism risks under the Terrorism Risk Insurance Act (TRIA). During 2006, AIG's deductible under TRIA was approximately $3.3 billion, with a 10 percent share of certified terrorism losses in excess of the deductible. As of January 1, 2007, the deductible increased to approximately $4.0 billion, with a 15 percent share of certified terrorism losses in excess of the deductible. Without an extension by Congress, TRIA will sunset at December 31, 2007. Should TRIA not be renewed, AIG would expect to reassess and modify its underwriting guidelines and retention levels as appropriate.

Life Insurance & Retirement Services

In Life Insurance & Retirement Services, the primary risks are (i) underwriting, which represents the exposure to loss resulting from the actual policy experience emerging adversely in comparison to the assumptions made in the product pricing associated with mortality, morbidity, termination and expenses; and (ii) investment risk which represents the exposure to loss resulting from the cash flows from the invested assets being less than the cash flows required to meet the obligations of the expected policy and contract liabilities and the necessary return on investments. AIG businesses manage these risks through exposure limitations and the active management of the asset-liability relationship in their operations. The emergence of significant adverse experience would require an adjustment to DAC and benefit reserves that could have a material adverse effect on AIG's consolidated results of operations for a particular period.

AIG's Foreign Life Insurance & Retirement Services companies generally limit their maximum underwriting exposure on life insurance of a single life to approximately $1.7 million of coverage. AIG's Domestic Life Insurance & Retirement Services companies limit their maximum underwriting exposure on life insurance of a single life to $10 million of coverage in certain circumstances by using yearly renewable term reinsurance. In Life Insurance & Retirement Services, the reinsurance programs provide risk mitigation per policy, per individual life and group covers and for catastrophic risk events.

Pandemic Influenza

The potential for a pandemic influenza outbreak has received much recent attention. While outbreaks of the Avian Flu continue to occur among poultry or wild birds in a number of countries in Asia, Europe, including the U.K., and Africa, transmission to humans has been rare to date. If the virus mutates to a form that can be transmitted from human to human, it has the potential to spread rapidly worldwide. If such an outbreak were to take place, early quarantine and vaccination could be critical to containment.

The contagion and mortality rates of any mutated H5N1 virus that can be transmitted from human to human are highly speculative. AIG continues to monitor the developing facts. A significant global outbreak could have a material adverse effect on Life Insurance & Retirement Services operating results and liquidity from increased mortality and morbidity rates. AIG continues to analyze its exposure to this serious threat and has engaged an external risk management firm to model loss scenarios associated with an outbreak of Avian Flu. Using a 1 in 100-year return period, AIG estimates its after-tax net losses under its life insurance policies due to Avian Flu at less than 1 percent of consolidated shareholders' equity as of December 31, 2006. This estimate was calculated over a 3-year period, although the majority of the losses would be incurred in the first year. The modeled losses calculated were based on 2005 policy data representing approximately 90 percent of AIG's individual life, group life and credit life books of business, net of reinsurance. This estimate does not include claims that could be made under other policies, such as business interruption or general liability

policies, and does not reflect estimates for losses resulting from disruption of AIG's own business operations that may arise out of such a pandemic. The model used to generate this estimate has only recently been developed. The reasonableness of the model and its underlying assumptions cannot readily be verified by reference to comparable historical events. As a result, AIG's actual losses from a pandemic influenza outbreak are likely to vary significantly from those predicted by the model.

Investments

AIG's fixed maturity investments totaled $417.9 billion at December 31, 2006, compared to $385.7 billion at December 31, 2005. AIG's investment strategies are tailored to the specific business needs of each operating unit based on considerations that include the local market, liability duration and cash flow characteristics, rating agency and regulatory capital considerations, legal investment limitations, tax optimization, diversification and credit limits. These strategies are intended to produce a reasonably stable and predictable return throughout the economic cycle, without undue risk or volatility.

At December 31, 2006, approximately 57 percent of the fixed maturities investments were domestic securities. Approximately 39 percent of such domestic securities were rated AAA by one or more of the principal rating agencies. Approximately five percent were below investment grade or not rated.

A significant portion of the foreign fixed income portfolio is rated by Moody's, S&P or similar foreign rating services. Rating services are not available in all overseas locations. The CRC closely reviews the credit quality of the foreign portfolio's non-rated fixed income investments. At December 31, 2006, approximately 20 percent of the foreign fixed income investments were either rated AAA or, on the basis of AIG's internal analysis, were equivalent from a credit standpoint to securities so rated. Approximately five percent were below investment grade or not rated at that date. A large portion of the foreign fixed income portfolio is sovereign fixed maturity securities supporting the policy liabilities in the country of issuance.

The credit ratings of fixed maturity investments, other than those of AIGFP, at December 31, 2006 were:

	2006
AAA	31%
AA	26
A	23
BBB	14
Below investment grade	4
Non-rated	2
Total	100%

AIG uses asset-liability matching as a management tool worldwide in the life insurance business to determine the composition of the invested assets and appropriate marketing strategies. AIG's objective is to maintain a matched asset-liability structure. However, in certain markets, the absence of long-dated fixed income instruments may preclude a matched asset-liability position in those markets. In addition, AIG may occasionally determine that it is economically advantageous to be temporarily in an unmatched position.

Financial Services

AIG's Financial Services subsidiaries engage in diversified activities including aircraft and equipment leasing, capital markets, consumer finance and insurance premium finance.

Aircraft Leasing

AIG's Aircraft Leasing operations represent the operations of ILFC, which generates its revenues primarily from leasing new and used commercial jet aircraft to scheduled and charter airlines and companies associated with the airline industry. Risks inherent in this business, and which are managed at the business unit level, include: (i) the risk that there will be no market for the aircraft acquired; (ii) the risk that aircraft cannot be placed with lessees; (iii) the risk of nonperformance by lessees; and (iv) the risk that aircraft and related assets cannot be disposed of at the time and in a manner desired.

Capital Markets

The Capital Markets operations of AIG are conducted primarily through AIGFP, which engages as principal in standard and customized interest rate, currency, equity, commodity, energy and credit products with top-tier corporations, financial institutions, governments, agencies, institutional investors and high-net-worth individuals throughout the world.

The senior management of AIG defines the policies and establishes general operating parameters for Capital Markets operations. AIG's senior management has established various oversight committees to monitor on an ongoing basis the various financial market, operational and credit risk attendant to the Capital Markets operations. The senior management of AIGFP reports the results of its operations to and reviews future strategies with AIG's senior management.

AIGFP actively manages its exposures to limit potential losses, while maximizing the rewards afforded by these business opportunities. In doing so, AIGFP must continually manage a variety of exposures including credit, market, liquidity, operational and legal risks.

AIGFP enters into credit derivative transactions in the ordinary course of its business. The majority of AIGFP's credit derivatives require AIGFP to provide credit protection on a designated portfolio of loans or debt securities. AIGFP provides such credit protection on a ''second loss'' basis, under which AIGFP's payment obligations arise only after credit losses in the designated portfolio exceed a specified threshold amount or level of ''first losses.'' The threshold amount of credit losses that must be realized before AIGFP has any payment obligation is negotiated by AIGFP for each transaction to provide that the likelihood of any payment obligation by AIGFP under each transaction is remote, even in severe recessionary market scenarios.

In certain cases, the credit risk associated with a designated portfolio is tranched into different layers of risk, which are then analyzed and rated by the credit rating agencies. Typically, there

will be an equity layer covering the first credit losses in respect of the portfolio up to a specified percentage of the total portfolio, and then successive layers that are rated, generally a BBB-rated layer, an A-rated layer, an AA-rated layer, and one or more AAA-rated layers. In transactions that are rated, the risk layer or tranche that is immediately junior to the threshold level above which AIGFP's payment obligation would generally arise is rated AAA by the rating agencies. In transactions that are not rated, AIGFP applies the same risk criteria for setting the threshold level for its payment obligations. Therefore, the risk layer assumed by AIGFP with respect to the designated portfolio in these transactions is often called the ''super senior'' risk layer, defined as the layer of credit risk senior to a risk layer that has been rated AAA by the credit rating agencies, or if the transaction is not rated, equivalent thereto.

AIGFP continually monitors the underlying portfolios to determine whether the credit loss experience for any particular portfolio has caused the likelihood of AIGFP having a payment obligation under the transaction to be greater than super senior risk. AIGFP maintains the ability opportunistically to economically hedge specific securities in a portfolio and thereby further limit its exposure to loss and has hedged outstanding transactions in this manner on occasion. At December 31, 2006, the notional amount with respect to the Capital Markets credit derivative portfolio (including the super senior transactions) was $483.6 billion.

Financial Services securities available for sale is predominately a diversified portfolio of high grade fixed income securities. At December 31, 2006, the average credit rating of this portfolio was in the AA+ category or the equivalent thereto as determined through rating agencies or internal review. AIGFP has also entered into credit derivative transactions to economically hedge its credit risk associated with $128 million of these securities. Securities deemed below investment grade at December 31, 2006 amounted to approximately $340 million in fair value representing 0.7 percent of the total AIGFP securities available for sale. There have been no significant downgrades through February 15, 2007. If its securities available for sale portfolio were to suffer significant default and the collateral held declined significantly in value with no replacement or the credit default swap counterparty failed to perform, AIGFP could have a liquidity strain. AIG guarantees AIGFP's payment obligations, including its debt obligations.

AIGFP's management objective is to minimize interest rate, currency, commodity and equity risks associated with its securities available for sale. That is, when AIGFP purchases a security for its securities available for sale investment portfolio, it simultaneously enters into an offsetting internal hedge such that the payment terms of the hedging transaction offset the payment terms of the investment security, which achieves the economic result of converting the return on the underlying security to U.S. dollar LIBOR plus or minus a spread based on the underlying profit on each security on the initial trade date. The market risk associated with such internal hedges is managed on a portfolio basis, with third-party hedging transactions executed as necessary. These hedging activities did not qualify for hedge accounting treatment under FAS 133.

Securities purchased under agreements to resell are treated as collateralized financing transactions. AIGFP takes possession of or obtains a security interest in securities purchased under agreements to resell.

A counterparty may default on any obligation to AIG, including a derivative contract. Credit risk is a consequence of extending credit and/or carrying trading and investment positions. Credit risk exists for a derivative contract when that contract has a positive fair value to AIG. The maximum potential exposure will increase or decrease during the life of the derivative commitments as a function of maturity and market conditions. To help manage this risk, AIGFP's credit department operates within the guidelines set by the CRC. Transactions which fall outside these pre-established guidelines require the specific approval of the CRC. It is also AIG's policy to establish reserves for potential credit impairment when necessary.

In addition, AIGFP utilizes various credit enhancements, including letters of credit, guarantees, collateral, credit triggers, credit derivatives and margin agreements to reduce the credit risk relating to its outstanding financial derivative transactions. AIGFP requires credit enhancements in connection with specific transactions based on, among other things, the creditworthiness of the counterparties, and the transaction's size and maturity. Furthermore, AIGFP generally seeks to enter into agreements that have the benefit of set-off and close-out netting provisions. These provisions provide that, in the case of an early termination of a transaction, AIGFP can set-off its receivables from a counterparty against its payables to the same counterparty arising out of all covered transactions. As a result, where a legally enforceable netting agreement exists, the fair value of the transaction with the counterparty represents the net sum of estimated positive fair values. The fair value of AIGFP's interest rate, currency, commodity and equity swaps, options, swaptions, and forward commitments, futures, and forward contracts approximated $19.25 billion at December 31, 2006 and $18.70 billion at December 31, 2005. Where applicable, these amounts have been determined in accordance with the respective close-out netting provisions.

AIGFP independently evaluates the counterparty credit quality by reference to ratings from rating agencies or, where such ratings are not available, by internal analysis consistent with the risk rating policies of the CRC. In addition, AIGFP's credit approval process involves pre-set counterparty and country credit exposure limits and, for particularly credit-intensive transactions, requires approval from the CRC. AIG estimates that the average credit rating of Capital Markets derivatives counterparties, measured by reference to the fair value of its derivative portfolio as a whole, is equivalent to the AA rating category.

At December 31, 2006 and 2005, the distribution by counterparty credit quality with respect to the fair value of Capital Markets derivatives portfolios was as follows:

	Percentage of Total Fair Value	
	2006	2005
Counterparty credit quality:		
AAA	**28%**	24%
AA	**41**	43
A	**19**	21
BBB	**11**	9
Below investment grade	**1**	3
Total	**100%**	100%

Capital Markets Trading VaR

AIGFP maintains a very conservative market risk profile and minimizes risk in interest rates, equities, commodities and foreign exchange. Market exposures in option implied volatilities, correlations and basis risks are also minimized over time but those are the main types of market risks that AIGFP manages. As a result, AIGFP's operating income due to changes in market prices and rates is generally a very small percentage of its overall operating income.

AIGFP's minimal reliance on market risk driven revenue is reflected in its VaR. AIGFP's VaR calculation is based on the interest rate, equity, commodity and foreign exchange risk arising from its portfolio. Because the market risk with respect to securities available for sale, at market, is substantially hedged, segregation of the financial instruments into trading and other than trading was not deemed necessary.

In the calculation of VaR for AIGFP, AIG uses the historical simulation methodology that entails repricing all transactions under explicit changes in market rates within a specific historical time period. AIGFP attempts to secure reliable and independent current market prices, such as published exchange prices, external subscription services such as Bloomberg or Reuters, or third-party broker quotes. When such prices are not available, AIGFP uses an internal methodology which includes extrapolation from observable and verifiable prices nearest to the dates of the transactions. Historically, actual results have not deviated from these models in any material respect.

AIGFP reports its VaR using a 95 percent confidence interval and a one-day holding period, facilitating risk comparison with AIGFP's trading peers and reflecting the fact that market risks can be actively assumed and offset in AIGFP's trading portfolio.

The following table presents the year-end, average, high, and low VaRs on a diversified basis and of each component of market risk for Capital Markets operations for the years 2006 and 2005. The diversified VaR is usually smaller than the sum of its components due to correlation effects.

		For the Year Ended December 31, 2006				For the Year Ended December 31, 2005		
(in millions)	As of December 31	Average	High	Low	As of December 31	Average	High	Low
Total AIG trading market risk:								
Diversified	$4	$4	$7	$3	$5	$4	$7	$3
Interest rate	2	2	3	1	2	2	3	1
Currency	1	1	3	1	1	1	1	—
Equity	3	3	4	2	3	2	5	—
Commodity	3	3	4	2	2	2	3	1

* *In 2006, VaR calculations were changed from a 30-day holding period to a one-day holding period. Accordingly, the 2005 VaR amounts have been restated to reflect this change.*

Consumer Finance

AIG's Consumer Finance operations provide a wide variety of consumer finance products, including real estate and other consumer loans, credit card loans, retail sales finance and credit-related insurance to customers both domestically and overseas, particularly in emerging markets. Consumer Finance operations include AGF as well as AIGCFG. AGF provides a wide variety of consumer finance products, including real estate loans, non-real estate loans, retail sales finance and credit-related insurance to customers in the United States, Puerto Rico and the U.S. Virgin Islands. AIGCFG, through its subsidiaries, is engaged in developing a multi-product consumer finance business with an emphasis on emerging markets.

Many of AGF's borrowers are non-prime or sub-prime. Current economic conditions, such as interest rate and employment levels, can have a direct effect on the borrowers' ability to repay these loans. AGF manages the credit risk inherent in its portfolio by using credit scoring models at the time of credit applications, established underwriting criteria, and, in certain cases, individual loan reviews. AGF monitors the quality of the finance receivables portfolio and determines the appropriate level of the allowance for losses through its Credit Strategy and Policy Committee. This Committee bases its conclusions on quantitative analyses, qualitative factors, current economic conditions and trends, and each Committee member's experience in the consumer finance industry. Through 2006, the credit quality of AGF's finance receivables continued to be strong. However, declines in the strength of the U.S. housing market or economy may adversely affect the future credit quality of these receivables.

AIGCFG monitors the quality of its finance receivable portfolio and determines the appropriate level of the allowance for losses through several internal committees. These committees base their

conclusions on quantitative analysis, qualitative factors, current economic conditions and trends, political and regulatory implications, competition and the judgment of the committees' members.

AIG's Consumer Finance operations are exposed to credit risk and risk of loss resulting from adverse fluctuations in interest rates and payment defaults. Credit loss exposure is managed through a combination of underwriting controls, mix of finance receivables, collateral and collection efficiency. Large product programs are subject to CRC approval.

Over half of the finance receivables are real estate loans which are collateralized by the related properties. With respect to credit losses, the allowance for losses is maintained at a level considered adequate to absorb anticipated credit losses existing in that portfolio as of the balance sheet date.

Asset Management

AIG's Asset Management operations are exposed to various forms of credit, market and operational risks. Asset Management complies with AIG's corporate risk management guidelines and framework and is subject to periodic reviews by the CRC. In addition, transactions are referred to the Asset Management investment committees for approval of investment decisions.

The majority of the credit and market risk exposures within Asset Management results from the spread-based investment business and the investment activities of AIG Global Real Estate Investment Corp.

In the spread-based investment businesses, GIC and MIP, the primary risk is investment risk, which represents the exposure to loss resulting from the cash flows from the invested assets being less than the cash flows required to meet the obligations of the liabilities and the necessary return on investments. Credit risk is also a significant component of the investment strategy for these businesses. Market risk is taken in the form of duration and convexity risk. While AIG generally maintains a matched asset-liability relationship, it may occasionally determine that it is economically advantageous to be in an unmatched duration position. The risks in the spread-based businesses are managed through exposure limitations, active management of the investment portfolios and close oversight of the asset-liability relationship.

Within AIG Global Real Estate Investment Corp., AIG is exposed to the general conditions in global real estate markets and the credit markets. Such exposure can subject Asset Management to delays in real estate sales, additional carrying costs and in turn affect operating results within the segment. These risks are mitigated through the underwriting process, transaction and contract terms and conditions and portfolio diversification by type of project, sponsor, real estate market and country. AIG's exposure to real estate investments is monitored on an ongoing basis by the Asset Management real estate investment committee.

Economic Capital

Since mid 2005, AIG has been developing a firm-wide economic capital model to improve decision making and to enhance shareholder value. Economic Capital is the amount of capital the organization, its segments, profit centers, products or transactions require to cover potential, unexpected losses within a confidence level consistent with the risk profile selected by management. The Economic Capital requirement can then be compared with the economic capital resources available to AIG.

The Economic Capital requirement is driven by exposures to risks and correlations among various types of risks. As a global financial conglomerate, AIG is exposed to various risks including underwriting, financial and operational risks. The Economic Capital initiative has modeled these risks into five major categories: property & casualty insurance risk, life insurance risk, market risk, credit risk and operational risk. Within each risk category, there are sub-risks that have been modeled in greater detail. The Economic Capital initiative also analyzes and includes diversification benefits within and across risk categories and business segments.

A primary objective of the Economic Capital initiative is to develop a comprehensive framework to discuss capital and performance on a risk-adjusted basis internally with AIG management and externally with the investment community, credit providers, regulators and rating agencies. Economic Capital analysis provides a framework to validate AIG's capital adequacy, to measure more precisely capital efficiency at various levels throughout the organization, to allocate capital consistently among AIG's businesses, to quantify the specific areas of diversification benefits and to assess relative economic value added by a business, product or transaction to AIG as a whole. The Economic Capital initiative will also be a component in developing a more efficient capital structure. Other key areas of Economic Capital applications include strategic decision-making for mergers, acquisitions and divestitures, risk retention, reinsurance and hedging strategies and product development and pricing.

During 2006, AIG developed a methodology framework that incorporates financial services industry best practices, maintains consistency with regulatory frameworks and reflects AIG's distinct global business and management strategies. By utilizing stochastic simulation techniques, where appropriate, AIG enhanced existing models or developed new ones through a collaborative effort among business executives, actuaries, finance specialists and risk professionals. Initial assessments of Economic Capital were made and AIG began reviewing its economic capital model methodology with the rating agencies.

The initial assessments were made at the corporate, segment and major business unit level, and detailed analyses of selected businesses and products were undertaken. AIG also developed assessments of diversification benefits across lines of business, geographic regions and risk categories. Given the breadth and global nature of AIG's businesses, these benefits were found to be significant.

The initial assessments have provided useful insight into the overall capital strength of the corporation and its segments and, to date, the initiative has introduced guidance concerning processes to assess economic risk and returns for selected issues, including funding and investment strategies for the MIP, product development, pricing, hedging for living benefits in the variable annuity business and asset-liability management strategies for life insurance products, particularly in Asian markets.

Throughout 2007, AIG will continue to enhance the methodology to provide assurance regarding the completeness and relevance of the model's results. AIG will continue discussions with the rating agencies concerning its enterprise risk management processes and the results of its new economic capital model for their consideration in the rating process. AIG's analysis and conclusions concerning the economic capital support of its segments and major business units will be further extended to include consideration for capital availability and mobility. The framework and process will increasingly provide assistance in management's decision-making concerning capital management and capital allocation, mergers, acquisitions and divestitures, risk retention, reinsurance and hedging strategies and product development and pricing.

Recent Accounting Standards

At the March 2004 meeting, the Emerging Issues Task Force (EITF) reached a consensus with respect to Issue No. 03-1, ''The Meaning of Other-Than-Temporary Impairment and Its Application to Certain Investments.'' On September 30, 2004, the FASB issued FASB Staff Position (FSP) EITF Issue 03-1-1, Effective Date of Paragraphs 10-20 of EITF Issue No. 03-1, ''The Meaning of Other-Than-Temporary Impairment and its Application to Certain Investments.'' In November 2005, the FASB issued FSP FAS 115-1, ''The Meaning of Other-Than-Temporary Impairment and Its Application to Certain Investments,'' which replaces the measurement and recognition guidance set forth in Issue No. 03-1 and codifies certain existing guidance on impairment.

At the June 2005 meeting, the EITF reached a consensus with respect to Issue No. 04-5, ''Determining Whether a General Partner, or the General Partners as a Group, Controls a Limited Partnership or Similar Entity When the Limited Partners have Certain Rights.''

On June 29, 2005, the FASB issued Statement 133 Implementation Issues No. B38, ''Embedded Derivatives: Evaluation of Net Settlement with Respect to the Settlement of a Debt Instrument through Exercise of an Embedded Put Option or Call Option'' and No. B39, ''Application of Paragraph 13(b) to Call Options That are Exercisable Only by the Debtor.''

On September 19, 2005, the FASB issued Statement of Position 05-1, ''Accounting by Insurance Enterprises for Deferred Acquisition Costs in Connection with Modifications or Exchanges of Insurance Contracts.''

On February 16, 2006, the FASB issued FAS No. 155, ''Accounting for Certain Hybrid Financial Instruments.''

On January 17, 2007, the FASB issued Statement 133 Implementation Issue No. B40, ''Embedded Derivatives: Application of Paragraph 13(b) to Securitized Interests in Prepayable Financial Assets'' (Issue B40).

On March 27, 2006, the FASB issued FASB FTB 85-4-1, ''Accounting for Life Settlement Contracts by Third-Party Investors'' (FSP 85-4-1), an amendment of FTB 85-4, ''Accounting for Purchases of Life Insurance.''

On April 13, 2006, the FASB issued FSP FIN 46(R)-6, ''Determining the Variability to be Considered in Applying FASB Interpretation No. 46(R).''

On July 13, 2006, the FASB issued FIN 48, ''Accounting for Uncertainty in Income Taxes — an interpretation of FASB Statement No. 109'' (FIN 48).

Effective January 1, 2006, AIG adopted the fair value recognition provisions of Statement of FAS No. 123R ''Share-Based Payments'' (FAS 123R). For further discussion of this recent accounting standard and its application to AIG, see Note 14 of Notes to Consolidated Financial Statements.

In September 2006, the FASB issued FAS No. 157, ''Fair Value Measurements'' (FAS 157).

In September 2006, the FASB issued FAS No. 158, ''Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans, an amendment of FASB Statements No. 87, 88, 106 and 132(R)'' (FAS 158).

In February 2007, the FASB issued FAS No. 159, ''The Fair Value Option for Financial Assets and Financial Liabilities'' (FAS 159).

For further discussion of these recent accounting standards and their application to AIG, see Note 1(hh) of Notes to Consolidated Financial Statements.

Item 7A.
Quantitative and Qualitative Disclosures About Market Risk

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

Item 8.
Financial Statements and Supplementary Data

American International Group, Inc. and Subsidiaries
Index to Financial Statements and Schedules

Report of Independent Registered Public Accounting Firm

To the Board of Directors and Shareholders of American International Group, Inc.:

We have completed integrated audits of American International Group, Inc.'s consolidated financial statements and of its internal control over financial reporting as of December 31, 2006, in accordance with the standards of the Public Company Accounting Oversight Board (United States). Our opinions, based on our audits, are presented below.

Consolidated Financial Statements and Financial Statement Schedules

In our opinion, the consolidated financial statements listed in the accompanying index present fairly, in all material respects, the financial position of American International Group, Inc. and its subsidiaries (AIG) at December 31, 2006 and 2005, and the results of their operations and their cash flows for each of the three years in the period ended December 31, 2006 in conformity with accounting principles generally accepted in the United States of America. In addition, in our opinion, the financial statement schedules listed in the accompanying index present fairly, in all material respects, the information set forth therein when read in conjunction with the related consolidated financial statements. These financial statements and financial statement schedules are the responsibility of AIG's management. Our responsibility is to express an opinion on these financial statements and financial statement schedules based on our audits. We conducted our audits of these statements in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit of financial statements includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

As described in Notes 1, 14 and 15 to the consolidated financial statements, AIG changed its accounting for certain hybrid financial instruments, life settlement contracts and share based compensation as of January 1, 2006, and certain employee benefit plans as of December 31, 2006.

Internal Control Over Financial Reporting

Also, we have audited management's assessment, included in Management's Report on Internal Control Over Financial Reporting appearing under Item 9A, that AIG did not maintain effective internal control over financial reporting as of December 31, 2006 because of the effect of the material weakness relating to controls over income tax accounting, based on criteria established in *Internal Control — Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). AIG's management is responsible for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting. Our responsibility is to express opinions on management's assessment and on the effectiveness of AIG's internal control over financial reporting based on our audit.

We conducted our audit of internal control over financial reporting in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material respects. An audit of internal control over financial reporting includes obtaining an understanding of internal control over financial reporting, evaluating management's assessment, testing and evaluating the design and operating effectiveness of internal control, and performing such other procedures as we consider necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinions.

A company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (i) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (ii) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (iii) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

A material weakness is a control deficiency, or a combination of control deficiencies, that results in more than a remote likelihood that a material misstatement of the annual or interim financial statements will not be prevented or detected. As of December 31, 2006, a material weakness relating to the controls over income tax accounting has been identified and included in management's assessment.

Controls over income tax accounting: AIG did not maintain effective controls over the determination and reporting of certain components of the provision for income taxes and related income tax balances. Specifically, AIG did not maintain effective controls to review and monitor the accuracy of the components of the income tax provision calculations and related income tax balances and to monitor the differences between the income tax basis and the financial reporting basis of assets and liabilities to effectively

Report of Independent Registered Public Accounting Firm *Continued*

reconcile the differences to the deferred income tax balances. These control deficiencies resulted in adjustments to income tax expense, income taxes payable and deferred income tax asset and liability accounts in the 2006 annual and interim consolidated financial statements. Furthermore, these control deficiencies could result in a material misstatement of the annual or interim AIG consolidated financial statements that would not be prevented or detected. Accordingly, AIG management has concluded that these control deficiencies constitute a material weakness.

This material weakness was considered in determining the nature, timing, and extent of audit tests applied in our audit of the 2006 consolidated financial statements, and our opinion regarding the effectiveness of AIG's internal control over financial reporting does not affect our opinion on those consolidated financial statements.

In our opinion, management's assessment that AIG did not maintain effective internal control over financial reporting as of December 31, 2006 is fairly stated, in all material respects, based on criteria established in *Internal Control — Integrated Framework* issued by the COSO. Also, in our opinion, because of the effect of the material weakness described above on the achievement of the objectives of the control criteria, AIG has not maintained effective internal control over financial reporting as of December 31, 2006, based on criteria established in *Internal Control — Integrated Framework* issued by the COSO.

PricewaterhouseCoopers LLP
New York, New York
March 1, 2007

Consolidated Balance Sheet

December 31, *(in millions)*	**2006**	2005
Assets:		
Investments and financial services assets:		
Fixed maturities:		
Bonds available for sale, at fair value (amortized cost: 2006 — $377,698; 2005 — $349,612) (includes hybrid financial instruments: 2006 — $522)	**$ 387,391**	$359,516
Bonds held to maturity, at amortized cost (fair value: 2006 — $22,154; 2005 — $22,047)	**21,437**	21,528
Bond trading securities, at fair value (cost: 2006 — $9,016; 2005 — $4,623)	**9,037**	4,636
Equity securities:		
Common stocks available for sale, at fair value (cost: 2006 — $10,662; 2005 — $10,125)	**13,262**	12,227
Common and preferred stocks trading, at fair value (cost: 2006 — $12,734; 2005 — $7,746)	**14,421**	8,959
Preferred stocks available for sale, at fair value (cost: 2006 — $2,485; 2005 — $2,282)	**2,539**	2,402
Mortgage loans on real estate, net of allowance (2006 — $55; 2005 — $54)	**17,067**	14,300
Policy loans	**7,501**	7,039
Collateral and guaranteed loans, net of allowance (2006 — $9; 2005 — $10)	**3,850**	3,570
Financial services assets:		
Flight equipment primarily under operating leases, net of accumulated depreciation (2006 — $8,835; 2005 — $7,419)	**39,875**	36,245
Securities available for sale, at fair value (cost: 2006 — $45,912; 2005 — $37,572)	**47,205**	37,511
Trading securities, at fair value	**5,031**	6,499
Spot commodities	**220**	92
Unrealized gain on swaps, options and forward transactions	**19,252**	18,695
Trading assets	**2,468**	1,204
Securities purchased under agreements to resell, at contract value	**33,702**	14,547
Finance receivables, net of allowance (2006 — $737; 2005 — $670) (includes finance receivables held for sale: 2006 — $1,124; 2005 — $1,110)	**29,573**	27,995
Securities lending collateral, at fair value (which approximates cost)	**69,306**	59,471
Other invested assets	**42,114**	31,072
Short-term investments, at cost (approximates fair value)	**25,249**	15,342
Total investments and financial services assets	**790,500**	682,850
Cash	**1,590**	1,897
Investment income due and accrued	**6,077**	5,727
Premiums and insurance balances receivable, net of allowance (2006 — $756; 2005 — $871)	**17,789**	15,333
Reinsurance assets, net of allowance (2006 — $536; 2005 — $999)	**23,355**	24,978
Deferred policy acquisition costs	**37,235**	32,154
Investments in partially owned companies	**1,101**	1,158
Real estate and other fixed assets, net of accumulated depreciation (2006 — $5,525; 2005 — $4,990)	**4,381**	3,641
Separate and variable accounts	**72,655**	63,797
Goodwill	**8,628**	8,093
Other assets	**16,103**	13,423
Total assets	**$ 979,414**	$853,051

See Accompanying Notes to Consolidated Financial Statements.

Consolidated Balance Sheet *Continued*

December 31, *(in millions, except share data)*	**2006**	2005
Liabilities:		
Reserve for losses and loss expenses	**$ 79,999**	$ 77,169
Unearned premiums	**26,271**	24,243
Future policy benefits for life and accident and health insurance contracts	**122,230**	108,807
Policyholders' contract deposits	**244,658**	227,027
Other policyholders' funds	**10,238**	10,870
Commissions, expenses and taxes payable	**5,305**	4,769
Insurance balances payable	**3,789**	3,564
Funds held by companies under reinsurance treaties	**2,602**	4,174
Income taxes payable	**9,546**	6,288
Financial services liabilities:		
Borrowings under obligations of guaranteed investment agreements	**20,664**	20,811
Securities sold under agreements to repurchase, at contract value	**22,710**	11,047
Trading liabilities	**3,141**	2,546
Hybrid financial instrument liabilities, at fair value	**8,856**	—
Securities and spot commodities sold but not yet purchased, at market value	**4,076**	5,975
Unrealized loss on swaps, options and forward transactions	**11,401**	12,740
Trust deposits and deposits due to banks and other depositors	**5,249**	4,877
Commercial paper	**8,208**	6,514
Notes, bonds, loans and mortgages payable	**87,602**	71,313
Commercial paper	**4,821**	2,694
Notes, bonds, loans and mortgages payable	**17,088**	7,126
Liabilities connected to trust preferred stock	**1,440**	1,391
Separate and variable accounts	**72,655**	63,797
Securities lending payable	**70,198**	60,409
Minority interest	**7,778**	5,124
Other liabilities (includes hybrid financial instruments: 2006 — $111)	**27,021**	23,273
Total liabilities	**877,546**	766,548
Preferred shareholders' equity in subsidiary companies	**191**	186
Commitments and Contingent Liabilities (See Note 12)		
Shareholders' equity:		
Common stock, $2.50 par value; 5,000,000,000 shares authorized; shares issued 2006 and 2005 — 2,751,327,476	**6,878**	6,878
Additional paid-in capital	**2,590**	2,339
Retained earnings	**84,996**	72,330
Accumulated other comprehensive income (loss)	**9,110**	6,967
Treasury stock, at cost; 2006 — 150,131,273; 2005 — 154,680,704 shares of common stock (including 119,278,644 and 119,271,176 shares, respectively, held by subsidiaries)	**(1,897)**	(2,197)
Total shareholders' equity	**101,677**	86,317
Total liabilities, preferred shareholders' equity in subsidiary companies and shareholders' equity	**$ 979,414**	$853,051

See Accompanying Notes to Consolidated Financial Statements.

Consolidated Statement of Income

Years Ended December 31, *(in millions, except per share data)*	**2006**	2005	2004
Revenues:			
Premiums and other considerations	**$ 74,083**	$70,209	$66,625
Net investment income	**25,292**	22,165	18,465
Realized capital gains (losses)	**106**	341	44
Other income	**13,713**	16,190	12,532
Total revenues	**113,194**	108,905	97,666
Benefits and expenses:			
Incurred policy losses and benefits	**59,706**	63,558	58,212
Insurance acquisition and other operating expenses	**31,801**	30,134	24,609
Total benefits and expenses	**91,507**	93,692	82,821
Income before income taxes, minority interest and cumulative effect of accounting changes	**21,687**	15,213	14,845
Income taxes:			
Current	**5,489**	2,587	2,645
Deferred	**1,048**	1,671	1,762
Total income taxes	**6,537**	4,258	4,407
Income before minority interest and cumulative effect of accounting changes	**15,150**	10,955	10,438
Minority interest	**(1,136)**	(478)	(455)
Income before cumulative effect of accounting changes	**14,014**	10,477	9,983
Cumulative effect of accounting changes, net of tax	**34**	—	(144)
Net income	**$ 14,048**	$10,477	$ 9,839
Earnings per common share:			
Basic			
Income before cumulative effect of accounting changes	**$ 5.38**	$ 4.03	$ 3.83
Cumulative effect of accounting changes, net of tax	**0.01**	—	(0.06)
Net income	**$ 5.39**	$ 4.03	$ 3.77
Diluted			
Income before cumulative effect of accounting changes	**$ 5.35**	$ 3.99	$ 3.79
Cumulative effect of accounting changes, net of tax	**0.01**	—	(0.06)
Net income	**$ 5.36**	$ 3.99	$ 3.73
Average shares outstanding:			
Basic	**2,608**	2,597	2,606
Diluted	**2,623**	2,627	2,637

See Accompanying Notes to Consolidated Financial Statements.

Consolidated Statement of Shareholders' Equity

Years Ended December 31, (in millions, except share and per share data)	Amounts 2006	Amounts 2005	Amounts 2004	Shares 2006	Shares 2005	Shares 2004
Common stock:						
Balance, beginning and end of year	**$ 6,878**	$ 6,878	$ 6,878	**2,751,327,476**	2,751,327,476	2,751,327,476
Additional paid-in capital:						
Balance, beginning of year	**2,339**	2,094	2,028			
Excess of cost over proceeds of common stock issued under stock plans	**(128)**	(91)	(105)			
Other	**379**	336	171			
Balance, end of year	**2,590**	2,339	2,094			
Retained earnings:						
Balance, beginning of year	**72,330**	63,468	54,384			
Cumulative effect of accounting changes, net of tax	**308**	—	—			
Adjusted balance, beginning of year	**72,638**	63,468	54,384			
Net income	**14,048**	10,477	9,839			
Dividends to common shareholders ($0.65, $0.63 and $0.29 per share, respectively)	**(1,690)**	(1,615)	(755)			
Balance, end of year	**84,996**	72,330	63,468			
Accumulated other comprehensive income (loss):						
Unrealized appreciation (depreciation) of investments, net of tax:						
Balance, beginning of year	**8,348**	10,326	9,070			
Unrealized appreciation (depreciation) of investments, net of reclassification adjustments	**2,574**	(3,577)	1,868			
Income tax benefit (expense)	**(839)**	1,599	(612)			
Balance, end of year	**10,083**	8,348	10,326			
Foreign currency translation adjustments, net of tax:						
Balance, beginning of year	**(1,241)**	(701)	(1,524)			
Translation adjustment	**1,283**	(926)	993			
Income tax benefit (expense)	**(347)**	386	(170)			
Balance, end of year	**(305)**	(1,241)	(701)			
Net derivative gains (losses) arising from cash flow hedging activities:						
Balance, beginning of year	**(25)**	(53)	(103)			
Net deferred gains on cash flow hedges, net of reclassification adjustments	**13**	35	83			
Deferred income tax expense	**(15)**	(7)	(33)			
Balance, end of year	**(27)**	(25)	(53)			
Retirement plan liabilities adjustment, net of taxes:						
Balance, beginning of year	**(115)**	(128)	(106)			
Minimum pension liability adjustment	**80**	81	(100)			
Deferred income tax benefit (expense)	**(74)**	(68)	78			
Adjustment to initially apply FAS 158, net of tax	**(532)**	—	—			
Balance, end of year	**(641)**	(115)	(128)			
Accumulated other comprehensive income (loss), end of year	**9,110**	6,967	9,444			
Treasury stock, at cost:						
Balance, beginning of year	**(2,197)**	(2,211)	(1,397)	**(154,680,704)**	(154,904,286)	(142,880,430)
Cost of shares acquired	**(20)**	(176)	(1,083)	**(288,365)**	(2,654,272)	(16,426,114)
Issued under stock plans	**291**	173	263	**4,579,913**	2,625,227	4,310,733
Other	**29**	17	6	**257,883**	252,627	91,525
Balance, end of year	**(1,897)**	(2,197)	(2,211)	**(150,131,273)**	(154,680,704)	(154,904,286)
Total shareholders' equity, end of year	**$101,677**	$86,317	$79,673			

See Accompanying Notes to Consolidated Financial Statements.

Consolidated Statement of Cash Flows

Years Ended December 31, *(in millions)*	2006	2005	2004
Summary:			
Net cash provided by operating activities	**$ 6,829**	$ 25,382	$ 29,414
Net cash used in investing activities	**(67,040)**	(62,500)	(92,596)
Net cash provided by financing activities	**59,790**	37,169	64,217
Effect of exchange rate changes on cash	**114**	(163)	52
Change in cash	**(307)**	(112)	1,087
Cash at beginning of year	**1,897**	2,009	922
Cash at end of year	**$ 1,590**	$ 1,897	$ 2,009
Cash flows from operating activities:			
Net income	**$ 14,048**	$ 10,477	$ 9,839
Adjustments to reconcile net income to net cash provided by operating activities:			
Noncash revenues, expenses, gains and losses included in income:			
Net gains on sales of securities available for sale and other assets	**(763)**	(1,218)	(1,003)
Foreign exchange transaction (gains) losses	**1,795**	(3,330)	1,231
Net unrealized (gains) losses on non-AIGFP derivative assets and liabilities	**(713)**	878	(648)
Equity in income of partially owned companies and other invested assets	**(3,990)**	(1,421)	(1,279)
Amortization of deferred policy acquisition costs	**11,578**	10,693	9,815
Amortization of premium and discount on securities	**699**	207	502
Depreciation expenses, principally flight equipment	**2,374**	2,200	2,035
Provision for finance receivable losses	**495**	435	389
Impairment losses	**944**	598	684
Changes in operating assets and liabilities:			
General and life insurance reserves	**13,173**	27,299	22,818
Premiums and insurance balances receivable and payable — net	**(1,214)**	192	(953)
Reinsurance assets	**1,665**	(5,365)	1,032
Capitalization of deferred policy acquisition costs	**(15,363)**	(14,454)	(13,334)
Investment income due and accrued	**(235)**	(171)	(916)
Funds held under reinsurance treaties	**(1,612)**	770	361
Other policyholders' funds	**(953)**	518	962
Income taxes payable	**2,003**	1,543	1,356
Commissions, expenses and taxes payable	**408**	140	(16)
Other assets and liabilities — net	**331**	2,966	1,943
Bonds, common and preferred stocks trading, at fair value	**(7,851)**	(5,448)	(3,189)
Trading assets and liabilities — net	**(668)**	2,272	(4,783)
Trading securities, at fair value	**1,339**	(3,753)	1,254
Spot commodities	**(128)**	442	(289)
Net unrealized (gain) loss on swaps, options and forward transactions	**(1,482)**	934	2,302
Securities purchased under agreements to resell	**(19,154)**	11,725	(5,427)
Securities sold under agreements to repurchase	**11,645**	(12,534)	5,688
Securities and spot commodities sold but not yet purchased, at market value	**(1,899)**	571	(269)
Finance receivables held for sale — originations and purchases	**(10,786)**	(13,070)	(6,504)
Sales of finance receivables — held for sale	**10,602**	12,821	5,784
Other, net	**541**	(1,535)	29
Total adjustments	**(7,219)**	14,905	19,575
Net cash provided by operating activities	**$ 6,829**	$ 25,382	$ 29,414

See Accompanying Notes to Consolidated Financial Statements.

Consolidated Statement of Cash Flows *Continued*

Years Ended December 31, *(in millions)*	**2006**	2005	2004
Cash flows from investing activities:			
Proceeds from (payments for)			
Sales and maturities of fixed maturity securities available for sale	**$ 112,899**	$ 140,076	$ 115,625
Sales of equity securities available for sale	**12,475**	11,661	12,246
Proceeds from fixed maturity securities held to maturity	**205**	46	226
Sales of flight equipment	**697**	573	1,219
Sales or distributions of other invested assets	**14,087**	14,899	8,361
Payments received on mortgage, policy, collateral and guaranteed loans	**5,165**	3,679	1,928
Principal payments received on finance receivables held for investment	**12,586**	12,461	10,780
Purchases of fixed maturity securities available for sale	**(146,465)**	(175,657)	(159,229)
Purchases of equity securities available for sale	**(14,482)**	(13,273)	(13,361)
Purchases of fixed maturity securities held to maturity	**(197)**	(3,333)	(10,512)
Purchases of flight equipment	**(6,009)**	(6,193)	(4,860)
Purchases of other invested assets	**(16,040)**	(15,059)	(11,764)
Mortgage, policy, collateral and guaranteed loans issued	**(7,438)**	(5,310)	(2,180)
Finance receivables held for investment — originations and purchases	**(13,830)**	(17,276)	(16,416)
Change in securities lending collateral	**(9,835)**	(10,301)	(19,777)
Net additions to real estate, fixed assets, and other assets	**(1,097)**	(941)	(643)
Net change in short-term investments	**(9,716)**	760	(2,542)
Net change in non-AIGFP derivative assets and liabilities	**(45)**	688	(1,697)
Net cash used in investing activities	**(67,040)**	(62,500)	(92,596)
Cash flows from financing activities:			
Proceeds from (payments for)			
Policyholders' contract deposits	**54,195**	50,229	54,550
Policyholders' contract withdrawals	**(41,866)**	(35,797)	(24,497)
Change in other deposits	**1,269**	(957)	2,519
Change in commercial paper	**2,952**	(476)	3,738
Notes, bonds, loans and mortgages payable, and hybrid financial instrument liabilities issued	**58,763**	53,624	31,488
Repayments on notes, bonds, loans and mortgages payable, and hybrid financial instrument liabilities	**(24,047)**	(40,767)	(24,638)
Issuance of guaranteed investment agreements	**12,265**	13,437	11,469
Maturities of guaranteed investment agreements	**(12,433)**	(10,861)	(8,314)
Change in securities lending payable	**9,789**	10,437	19,777
Redemption of subsidiary company preferred stock	**—**	(100)	(200)
Issuance of treasury stock	**163**	82	158
Cash dividends paid to shareholders	**(1,638)**	(1,421)	(730)
Acquisition of treasury stock	**(20)**	(176)	(1,083)
Other, net	**398**	(85)	(20)
Net cash provided by financing activities	**$ 59,790**	$ 37,169	$ 64,217
Supplementary disclosure of cash flow information:			
Cash paid during the period for:			
Interest	**$ 6,539**	$ 4,883	$ 4,281
Taxes	**$ 4,693**	$ 2,593	$ 3,060
Non-cash activities:			
Interest credited to policyholder accounts included in financing activities	**$ 10,746**	$ 9,782	$ 6,859

See accompanying Notes to Consolidated Financial Statements.

Consolidated Statement of Comprehensive Income

Years Ended December 31, *(in millions)*	**2006**	2005	2004
Net income	**$14,048**	$10,477	$ 9,839
Other comprehensive income (loss):			
Unrealized (depreciation) appreciation of investments — net of reclassification adjustments	**2,574**	(3,577)	1,868
Deferred income tax benefit (expense) on above changes	**(839)**	1,599	(612)
Foreign currency translation adjustments	**1,283**	(926)	993
Deferred income tax benefit (expense) on above changes	**(347)**	386	(170)
Net derivative gains arising from cash flow hedging activities — net of reclassification adjustments	**13**	35	83
Deferred income tax expense on above changes	**(15)**	(7)	(33)
Retirement plan liabilities adjustment	**80**	81	(100)
Deferred income tax benefit (expense) on above changes	**(74)**	(68)	78
Other comprehensive income (loss)	**2,675**	(2,477)	2,107
Comprehensive income	**$16,723**	$ 8,000	$11,946

See Accompanying Notes to Consolidated Financial Statements.

Index of Notes to Consolidated Financial Statements

Notes to Consolidated Financial Statements

1. Summary of Significant Accounting Policies

Basis of Presentation

The consolidated financial statements include the accounts of AIG and its majority owned subsidiaries. AIG consolidates subsidiaries in which it holds a controlling financial interest. Entities that AIG does not consolidate but of which it holds 20 percent to 50 percent of the voting rights and/or has the ability to exercise significant influence are accounted for under the equity method.

Certain of AIG's foreign subsidiaries included in the consolidated financial statements report on a fiscal year ending November 30. The effect on AIG's consolidated financial condition and results of operations of all material events occurring after November 30 and prior to the applicable balance sheet date has been recorded.

The accompanying consolidated financial statements have been prepared in accordance with U.S. generally accepted accounting principles (GAAP). All material intercompany accounts and transactions have been eliminated.

Description of Business

See Note 2 herein for a description of AIG's businesses.

Use of Estimates

AIG considers its most critical accounting estimates to be those with respect to reserves for losses and loss expenses, future policy benefits for life and accident and health contracts, recoverability of deferred policy acquisition costs (DAC), estimated gross profits for investment-oriented products, fair value determinations for certain Capital Markets assets and liabilities, other-than-temporary declines in the value of investments and flight equipment recoverability.

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting periods. Actual results could differ, possibly materially, from those estimates.

Revisions and Reclassifications

It was determined during 2006 that for certain deferred sales inducement assets, the asset and related amortization expense had historically been reported within deferred policy acquisition costs on the consolidated balance sheet and income statement. Under Statement of Position 03-1, ''Accounting and Reporting by Insurance Enterprises for Certain Nontraditional Long-Duration Contracts and for Separate Accounts'' (SOP 03-1), such assets should be classified separately from DAC and the amortization reported in benefit expense. Accordingly, the December 31, 2005 consolidated balance sheet reflects a revision of $1.1 billion from DAC to other assets, and the consolidated income statement includes a revision from acquisition expense to policy benefit expense of $153 million and $149 million in the years ended December 31, 2005 and 2004, respectively, to conform to the current year's presentation. This revision did not have any effect on consolidated pre-tax income, net income or shareholders' equity.

In 2006 AIG determined that certain products that were historically reported as separate account assets under SOP 03-1 should have been reported as general account assets. Accordingly, AIG revised the classification of approximately $2.7 billion of assets from separate account assets in prior years to general account assets, and the same amount of liabilities from separate account liabilities to policyholders' contract deposits at December 31, 2006. As a result, Net investment income and Incurred policy losses and benefits each increased approximately $258 million for the earnings on the general account assets that accrue directly to the benefit of the policyholders. This revision did not have any effect on consolidated income before income taxes, net income, or shareholders' equity for any period presented.

Certain reclassifications and format changes have been made to prior year amounts to conform to the current year presentation.

Accounting Policies

(a) Revenue Recognition and Expenses:

Premiums and other Considerations: Premiums for short duration contracts and considerations received from retailers in connection with the sale of extended service contracts are earned primarily on a pro rata basis over the term of the related coverage. The reserve for unearned premium includes the portion of premiums written and other considerations relating to the unexpired terms of coverage. Premiums for long duration insurance products and life contingent annuities are recognized as revenues when due. Estimates for premiums due but not yet collected are accrued. Consideration for universal life and investment-type products consist of policy charges for the cost of insurance, administration, and surrenders during the period. Policy charges collected with respect to future services are deferred and recognized in a manner similar to DAC related to such products.

Net Investment Income: Net investment income represents income primarily from the following sources in AIG's insurance operations:

- Accrued interest income, as well as amortization and accretion of premiums and discounts on bonds.
- Dividend income and distributions from common and preferred stock and other investments when receivable.
- Unrealized gains and losses from investments in trading securities and hybrid financial instruments.
- Earnings from hedge funds and limited partnership investments accounted for under the equity method.
- The difference between the carrying amount of a life settlement contract and the life insurance proceeds of the underlying life insurance policy recorded in income upon the death of the insured.

1. Summary of Significant Accounting Policies

Continued

Realized Capital Gains (Losses): Realized capital gains and losses are determined principally by specific identification. The realized capital gains and losses are generated primarily from the following sources (in AIG's insurance operations and Other category):

- Sales of fixed maturity securities, equity securities, real estate, investments in joint ventures and limited partnerships and other types of investments.
- Reductions to the cost basis of fixed maturities, equity securities and other invested assets for other-than-temporary impairments.
- Changes in fair value of derivatives used for other than hedging activities.
- Exchange gains and losses resulting from foreign currency transactions.

Other Income: Other income includes income from flight equipment, finance charges on consumer loans and income generated from asset management activities and from the operations of AIGFP.

Income from flight equipment under operating leases is recognized over the life of the lease as rentals become receivable under the provisions of the lease or, in the case of leases with varying payments, under the straight-line method over the noncancelable term of the lease. In certain cases, leases provide for additional payments contingent on usage. Rental income is recognized at the time such usage occurs less a provision for future contractual aircraft maintenance. Gains and losses on flight equipment are recognized when flight equipment is sold and the risk of ownership of the equipment is passed to the new owner.

Finance charges on consumer loans are recognized as revenue using the interest method. Revenue ceases to be accrued when contractual payments are not received for four consecutive months for loans and retail sales contracts, and for six months for revolving retail accounts and private label receivables. Extension fees, late charges, and prepayment penalties are recognized as revenue when received.

Income generated with respect to asset management operations is generally recognized as revenues as services are performed. Certain costs incurred in the sale of mutual funds are deferred and subsequently amortized.

Income generated from the operations of AIGFP includes the following:

- Accrued interest income and expense, as well as amortization and accretion of premiums and discounts on bonds.
- Dividend income and distributions from common and preferred stock and other investments when receivable.
- Changes in the fair value of derivatives. In certain instances, no initial gain or loss is recognized in accordance with Emerging Issues Task Force Issue No. 02-3, ''Issues Involved in Accounting for Derivative Contracts held for Trading Purposes and Contracts Involved in Energy Trading and Risk Management Activities'' (EITF 02-3). The initial gain or loss is recognized over the life of the transactions and as observable market data becomes available.
- Unrealized gains and losses from trading securities, commodities sold, but not yet purchased, futures and hybrid financial instruments.
- Realized gains and losses from the sale of available for sale securities and investments in private equities, joint ventures and limited partnerships.
- Exchange gains and losses resulting from foreign currency transactions.
- Reductions to the cost basis of equity securities for other-than-temporary impairments.
- Earnings from hedge funds and limited partnership investments accounted for under the equity method.

Incurred policy losses and benefits: Incurred policy losses for short duration insurance contracts consist of the estimated ultimate cost of settling claims incurred within the reporting period, including incurred but not reported claims, plus the changes in estimates of current and prior period losses resulting from the continuous review process. Benefits for long duration insurance contracts consist of benefits paid and changes in future policy benefits liabilities. Benefits for universal life and investment-type products primarily consists of interest credited to policy account balances and benefit payments made in excess of policy account balances.

(b) Foreign Currency: Financial statement accounts expressed in foreign currencies are translated into U.S. dollars in accordance with Statement of Financial Accounting Standards (FAS) 52, ''Foreign Currency Translation'' (FAS 52). Under FAS 52, functional currency assets and liabilities are translated into U.S. dollars generally using current rates of exchange prevailing at the balance sheet date of each respective subsidiary and the related translation adjustments are recorded as a separate component of other comprehensive income, net of any related taxes, in consolidated shareholders' equity. Functional currencies are generally the currencies of the local operating environment. Income statement accounts expressed in functional currencies are translated using average exchange rates. The adjustments resulting from translation of financial statements of foreign entities operating in highly inflationary economies are recorded in income. Exchange gains and losses resulting from foreign currency transactions are recorded in income currently.

(c) Income Taxes: Deferred tax assets and liabilities are recorded for the effects of temporary differences between the tax basis of an asset or liability and its reported amount in the consolidated financial statements. AIG assesses its ability to realize deferred tax assets primarily based on the earnings history, future earnings potential, the reversal of taxable temporary differences, and the tax planning strategies available to the legal entities recognizing deferred tax assets, in accordance with FAS 109, ''Accounting for Income Taxes.'' See Note 3 herein for a further discussion of income taxes.

(d) Contingencies: Amounts are accrued for the financial resolution of claims that have either been asserted or are deemed probable of assertion if, in the opinion of management, it is both probable that a liability has been incurred and the amount

1. Summary of Significant Accounting Policies

Continued

of the liability can be reasonably estimated. In many cases, it is not possible to determine whether a liability has been incurred or to estimate the ultimate or minimum amount of that liability until years after the contingency arises, in which case no accrual is made until that time.

(e) Investments in Fixed Maturities and Equity Securities: Bonds held to maturity are principally owned by the insurance subsidiaries and are carried at amortized cost where AIG has the ability and positive intent to hold these securities until maturity.

Where AIG may not have the positive intent to hold bonds until maturity and such securities are not designated as trading, these securities are considered to be available for sale and carried at current fair values.

Premiums and discounts arising from the purchase of bonds are treated as yield adjustments over their estimated lives, until maturity, or call date, if applicable.

Bond trading securities are carried at current fair values.

Common and preferred stocks are carried at current fair values.

AIG may also enter into dollar roll agreements. These are agreements to sell mortgage-backed securities and to repurchase substantially similar securities at a specified price and date in the future. At December 31, 2006, 2005 and 2004, there were no dollar roll agreements outstanding.

Unrealized gains and losses from available for sale investments in equity and fixed maturity securities are reflected as a separate component of other comprehensive income, net of deferred income taxes currently. Unrealized gains and losses from investments in trading securities are reflected in income currently. Investments in fixed maturities and equity securities are recorded on a trade date basis.

AIG evaluates its investments for impairment. As a matter of policy, the determination that a security has incurred an other-than-temporary decline in value and the amount of any loss recognition requires the judgment of AIG's management and a continual review of its investments.

In general, a security is considered a candidate for other-than-temporary impairment if it meets any of the following criteria:

- Trading at a significant (25 percent or more) discount to par or amortized cost (if lower) for an extended period of time (nine months or longer);
- The occurrence of a discrete credit event resulting in the debtor defaulting or seeking bankruptcy or insolvency protection or voluntary reorganization; or
- The probability of non-realization of a full recovery on its investment, irrespective of the occurrence of one of the foregoing events.

At each balance sheet date, AIG evaluates its securities holdings in an unrealized loss position. Where AIG does not intend to hold such securities until they have fully recovered their carrying value, based on the circumstances present at the date of evaluation, AIG records the unrealized loss in income. If events or circumstances change, such as unexpected changes in the creditworthiness of the obligor, unanticipated changes in interest rates, tax laws, statutory capital positions and liquidity events, among others, AIG revisits its intent. Further, if a loss is recognized from a sale subsequent to a balance sheet date pursuant to these unexpected changes in circumstances, the loss is recognized in the period in which the intent to hold the securities to recovery no longer existed.

In periods subsequent to the recognition of an other-than-temporary impairment loss for debt securities, AIG generally amortizes the discount or reduced premium over the remaining life of the security in a prospective manner based on the amount and timing of future estimated cash flows.

(f) Mortgage Loans on Real Estate — net, Policy, Collateral and Guaranteed Loans — net: Mortgage loans on real estate, policy, collateral and guaranteed loans are carried at unpaid principal balances. Interest income on such loans is accrued as earned.

Impairment of mortgage loans on real estate and collateral loans is based upon certain risk factors and when collection of all amounts due under the contractual term is not probable. This impairment is generally measured based on the present value of expected future cash flows discounted at the loan's effective interest rate subject to the fair value of underlying collateral if the loan is collateral dependent. Interest income on such impaired loans is recognized as cash is received.

There is no allowance for policy loans, as these loans serve to reduce the death benefit paid when the death claim is made and the balances are effectively collateralized by the cash surrender value of the policy.

(g) Financial Services — Flight Equipment: Flight equipment is stated at cost, net of accumulated depreciation. Major additions, modifications and interest are capitalized. Normal maintenance and repairs, airframe and engine overhauls and compliance with return conditions of flight equipment on lease are provided by and paid for by the lessee. Under the provisions of most leases for certain airframe and engine overhauls, the lessee is reimbursed for certain costs incurred up to but not exceeding contingent rentals paid to AIG by the lessee. AIG provides a charge to income for such reimbursements based upon the expected reimbursements during the life of the lease. Depreciation and amortization are computed on the straight-line basis to a residual value of approximately 15 percent over the estimated useful lives of the related assets but not exceeding 25 years. Aircraft in the fleet are evaluated, as necessary, based on these events and circumstances in accordance with FAS No. 144, ''Accounting for the Impairment or Disposal of Long-Lived Assets'' (FAS 144). FAS 144 requires that long-lived assets be reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. Recoverability of assets is measured by comparing the carrying amount of an asset to future undiscounted net cash flows expected to be generated by the asset. These evaluations for impairment are significantly affected by estimates of future revenues and other factors which involve some amount of uncertainty.

1. Summary of Significant Accounting Policies

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This caption also includes deposits for aircraft to be purchased. At the time the assets are retired or disposed of, the cost and associated accumulated depreciation and amortization are removed from the related accounts and the difference, net of proceeds, is recorded as a gain or loss in Other income.

(h) Financial Services — Securities Available for Sale, at fair value: These securities are held to meet long-term investment objectives and are accounted for as available for sale, carried at current fair values and recorded on a trade-date basis. This portfolio is hedged using interest rate, foreign exchange, commodity and equity derivatives. The market risk associated with such hedges is managed on a portfolio basis, with third party hedging transactions executed as necessary. As hedge accounting treatment is not achieved in accordance with FAS 133, ''Accounting for Derivative Instruments and Hedging Activities'' (FAS 133), the unrealized gains and losses on these securities resulting from changes in interest rates, currency rates and equity prices are recorded in Other comprehensive income in consolidated shareholders' equity while the unrealized gains and losses on the related economic hedges are reflected in Other income.

(i) Financial Services — Trading Securities, at fair value: Trading securities are held to meet short-term investment objectives, including hedging securities. These securities are recorded on a trade-date basis and carried at current fair values. Unrealized gains and losses are reflected in Other income currently.

(j) Financial Services — Spot Commodities: Spot commodities held in AIGFP's wholly owned broker-dealer subsidiary are recorded at fair value. All other commodities are recorded at the lower of cost or market value. Spot commodities are recorded on a trade-date basis. The exposure to market risk may be reduced through the use of forwards, futures and option contracts. Lower of cost or fair value reductions in commodity positions and unrealized gains and losses in related derivatives are reflected in Other income currently.

(k) Financial Services — Unrealized Gain and Unrealized Loss on Swaps, Options and Forward Transactions: Interest rate, currency, equity and commodity swaps, swaptions, options and forward transactions are accounted for as derivatives recorded on a trade-date basis and are carried at current market values or estimated fair values when market prices are not available. Unrealized gains and losses are reflected in income currently, where appropriate. In certain instances, when income is not recognized at inception of the contract under EITF 02-03, income is recognized over the life of the contract and as observable market data becomes available. Estimated fair values are based on the use of valuation models that utilize, among other things, current interest, foreign exchange, equity, commodity and volatility rates. AIG attempts to secure reliable and independent current market prices, such as published exchange prices, external subscription services' prices such as Bloomberg or Reuters or third-party broker quotes for use in its models. When such prices are not available, AIG uses an internal methodology which includes interpolation and extrapolation from observable and verifiable prices nearest to the dates of the transactions. These valuations represent an assessment of the present values of expected future cash flows of these transactions and reflect market and credit risk. The portfolio's discounted cash flows are evaluated with reference to current market conditions, maturities within the portfolio, and other relevant factors. Based upon this evaluation, it is determined what offsetting transactions, if any, are necessary to reduce the market risk of the portfolio. AIG manages its market risk with a variety of transactions, including swaps, trading securities, futures and forward contracts and other transactions as appropriate. Because of the limited liquidity of some of these instruments, the recorded values of these transactions may be different from the values that might be realized if AIG were to sell or close out the transactions prior to maturity. AIG believes that such differences are not significant to its financial condition or liquidity. Such differences would be immediately recognized in income when the transactions were sold or closed out prior to maturity.

(l) Financial Services — Trading Assets and Trading Liabilities: Trading assets and trading liabilities include option premiums paid and received and receivables from and payables to counterparties which relate to unrealized gains and losses on futures, forwards, and options and balances due from and due to clearing brokers and exchanges.

(m) Financial Services — Securities Purchased (Sold) Under Agreements to Resell (Repurchase), at contract value: Purchases of securities under agreements to resell and sales of securities under agreements to repurchase are accounted for as collateralized borrowing or lending transactions and are recorded at their contracted resale or repurchase amounts, plus accrued interest. AIG's policy is to take possession of or obtain a security interest in securities purchased under agreements to resell.

AIG minimizes the credit risk that counterparties to transactions might be unable to fulfill their contractual obligations by monitoring customer credit exposure and collateral value and generally requiring additional collateral to be deposited with AIG when deemed necessary.

(n) Financial Services — Finance Receivables: Finance receivables, which are net of unearned finance charges, are held for both investment purposes and for sale. Finance receivables held for investment purposes are carried at amortized cost which includes accrued finance charges on interest bearing finance receivables, unamortized deferred origination costs, and unamortized net premiums and discounts on purchased finance receivables. The allowance for finance receivable losses is established through the provision for finance receivable losses charged to expense and is maintained at a level considered adequate to absorb estimated credit losses in the existing portfolio. The portfolio is periodically evaluated on a pooled basis and factors such as economic conditions, portfolio composition, and loss and delinquency experience are considered in the evaluation of the allowance.

1. Summary of Significant Accounting Policies

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Direct costs of originating loans, net of nonrefundable points and fees, are deferred and included in the carrying amount of the related loans. The amount deferred is recognized as an adjustment to finance charge revenues, using the interest method.

Finance receivables originated and intended for sale in the secondary market are carried at the lower of cost or market value, as determined by aggregate outstanding commitments from investors or current investor yield requirements. AGF recognizes net unrealized losses through a valuation allowance by charges to income.

(o) Securities Lending Collateral and Securities Lending Payable, at fair value: AIG's insurance and asset management operations lend their securities and primarily take cash as collateral with respect to the securities lent. Invested collateral consists primarily of floating rate bonds. Income earned on invested collateral, net of interest payable to the collateral provider, is recorded in net investment income.

The fair value of securities pledged under securities lending arrangements was $69 billion and $59 billion as of December 31, 2006 and 2005, respectively. These securities are included in bonds available for sale in AIG's consolidated balance sheet.

(p) Other Invested Assets: Other invested assets consist primarily of investments by AIG's insurance operations in hedge funds and limited partnerships.

Hedge funds and limited partnerships in which AIG holds in the aggregate less than a five percent interest are reported at fair value. The change in fair value is recognized as a component of Other comprehensive income.

With respect to hedge funds and limited partnerships in which AIG holds in the aggregate a five percent or greater interest or less than a five percent interest but where AIG has more than a minor influence over the operations of the investee, AIG's carrying value is its share of the net asset value of the funds or the partnerships. The changes in such net asset values, accounted for under the equity method, are recorded in earnings through net investment income.

AIG obtains the fair values of its investments in limited partnerships and hedge funds from information provided by the general partner or manager of each of these investments, the accounts of which generally are audited on an annual basis.

Also included in other invested assets are real estate held for investment, aircraft asset investments held by non-financial services subsidiaries and investments in life settlement contracts. See Notes 8(g) and 8(h) herein for further information.

(q) Short-term Investments: Short-term investments consist of interest bearing cash equivalents, time deposits, and investments with original maturities within one year, such as commercial paper.

(r) Cash: Cash represents cash on hand and non-interest bearing demand deposits.

(s) Reinsurance Assets: Reinsurance assets include the balances due from reinsurance and insurance companies under the terms of AIG's reinsurance agreements for paid and unpaid losses and loss expenses, ceded unearned premiums and ceded future policy benefits for life and accident and health insurance contracts and benefits paid and unpaid. Amounts related to paid and unpaid losses, benefits and loss expenses with respect to these reinsurance agreements are substantially collateralized.

(t) Deferred Policy Acquisition Costs:

General Insurance: Acquisition costs represent those costs, including commissions, premium taxes and other underwriting expenses, that vary with and are primarily related to the acquisition of new business. These costs are deferred and amortized over the period in which the related premiums written are earned. DAC is grouped consistent with the manner in which the insurance contracts are acquired, serviced and measured for profitability and is reviewed for recoverability based on the profitability of the underlying insurance contracts. Investment income is not anticipated in the recoverability of deferred policy acquisition costs.

Life Insurance & Retirement Services: Acquisition costs represent those costs, including commissions, underwriting and marketing expenses, that vary with, and are primarily related to, the acquisition of new business. Policy acquisition costs for traditional life insurance products are generally deferred and amortized over the premium paying period in accordance with FAS 60, ''Accounting and Reporting by Insurance Enterprises'' (FAS 60). Policy acquisition costs and policy issuance costs related to universal life, participating life, and investment-type products (investment-oriented products) are deferred and amortized, with interest, in relation to the incidence of estimated gross profits to be realized over the estimated lives of the contracts in accordance with FAS 97, ''Accounting and Reporting by Insurance Enterprises for Certain Long-Duration Contracts and for Realized Gains and Losses from the Sale of Investments'' (FAS 97). Estimated gross profits are composed of net interest income, net realized investment gains and losses, fees, surrender charges, expenses, and mortality and morbidity gains and losses. If estimated gross profits change significantly, DAC is recalculated using the new assumptions. Any resulting adjustment is included in current earnings as an adjustment to DAC. DAC is grouped consistent with the manner in which the insurance contracts are acquired, serviced and measured for profitability and is reviewed for recoverability based on the profitability (both current and projected future) of the underlying insurance contracts.

The DAC for investment-oriented products is also adjusted with respect to estimated gross profits as a result of changes in the net unrealized gains or losses on debt and equity securities available for sale. That is, as debt and equity securities available for sale are carried at aggregate fair value, an adjustment is made to DAC equal to the change in amortization that would have been recorded if such securities had been sold at their stated aggregate fair value and the proceeds reinvested at current yields. The change in this adjustment, net of tax, is included with the change in net unrealized gains/losses on debt and equity

1. Summary of Significant Accounting Policies

Continued

securities available for sale that is credited or charged directly to other comprehensive income. DAC has been decreased by $720 million at December 31, 2006 and decreased by $1.14 billion at December 31, 2005 for this adjustment. See also Note 4 herein.

Value of Business Acquired (VOBA) is determined at the time of acquisition and is reported on the consolidated balance sheet with DAC. This value is based on present value of future pre-tax profits discounted at current yields applicable at time of purchase. For products accounted under FAS 60, VOBA is amortized over the life of the business similar to that for DAC based on the assumptions at purchase. For FAS 97 products, VOBA is amortized in relation to the estimated gross profits to date for each period. As of December 31, 2006, there have been no impairments of VOBA.

(u) Investments in Partially Owned Companies: At December 31, 2006, AIG's significant investments in partially owned companies included its 19.4 percent interest in Allied World Assurance Holdings, Ltd., its 26 percent interest in Tata AIG Life Insurance Company, Ltd., its 26 percent interest in Tata AIG General Insurance Company, Ltd. and its 24.5 percent interest in The Fuji Fire and Marine Insurance Co., Ltd. This balance sheet caption also includes investments in less significant partially owned companies. The amounts of dividends received from unconsolidated entities where AIG's ownership interest is less than 50 percent were $28 million, $146 million and $22 million in 2006, 2005 and 2004, respectively. The undistributed earnings of unconsolidated entities where AIG's ownership interest is less than 50 percent were $300 million, $179 million and $445 million as of December 31, 2006, 2005 and 2004, respectively.

(v) Real Estate and Other Fixed Assets: The costs of buildings and furniture and equipment are depreciated principally on a straight-line basis over their estimated useful lives (maximum of 40 years for buildings and ten years for furniture and equipment). Expenditures for maintenance and repairs are charged to income as incurred; expenditures for betterments are capitalized and depreciated.

AIG periodically assesses the carrying value of its real estate for purposes of determining any asset impairment.

Also included in Real Estate and Other Fixed Assets are capitalized software costs, which represent costs directly related to obtaining, developing or upgrading internal use software. Such costs are capitalized and amortized using the straight-line method over a period generally not to exceed five years.

(w) Separate and Variable Accounts: Separate and variable accounts represent funds for which investment income and investment gains and losses accrue directly to the policyholders who predominantly bear the investment risk. Each account has specific investment objectives, and the assets are carried at fair value. The assets of each account are legally segregated and are not subject to claims which arise out of any other business of AIG. The liabilities for these accounts are generally equal to the account assets.

(x) Goodwill and Intangible Assets: Goodwill is the excess of cost over the fair value of net assets acquired. Goodwill is reviewed for impairment on an annual basis, or more frequently if circumstances indicate that a possible impairment has occurred. The assessment of impairment involves a two-step process whereby an initial assessment for potential impairment is performed, followed by a measurement of the amount of impairment, if any. Impairment testing is performed using the fair value approach, which requires the use of estimates and judgment, at the ''reporting unit'' level. A reporting unit is the operating segment, or a business that is one level below the operating segment if discrete financial information is prepared and regularly reviewed by management at that level. The determination of a reporting unit's fair value is based on management's best estimate, which generally considers the unit's market-based earning multiples of peer companies and expected future earnings. If the carrying value of a reporting unit's goodwill exceeds its fair value, the excess is recognized as an impairment and recorded as a charge against net income. No impairment has been recorded by AIG in 2006, 2005 or 2004. Changes in the carrying amount of goodwill result from foreign currency translation adjustments and other purchase price adjustments.

(y) Other Assets: Other assets consist of prepaid expenses, including deferred advertising costs, sales inducement assets and derivatives assets at fair value, other than derivatives in AIGFP, and other deferred charges.

Generally, advertising costs are expensed as incurred except for certain direct response stand-alone cost pools, which are deferred over the expected future benefit period in accordance with Statement of Position 93-7, ''Reporting on Advertising Costs.'' In instances where AIG can demonstrate that its customers have responded specifically to direct-response advertising, whose primary purpose is to elicit sales to customers and where it can be shown that such advertising results in probable future economic benefits, the advertising costs are capitalized. Deferred advertising costs are amortized on a cost-pool by cost-pool basis over the expected economic future benefit period and are reviewed regularly for recoverability. Deferred advertising costs amounted to $1.05 billion and $915 million at December 31, 2006 and 2005, respectively. The amount of expense amortized into earnings was $359 million, $272 million and $244 million, for 2006, 2005, and 2004, respectively.

AIG offers sales inducements, which include enhanced crediting rates or bonus payments to contract holders (bonus interest) on certain annuity and investment contract products. Sales inducements provided to the contractholder are recognized as part of the liability for policyholders' contract deposits on the consolidated balance sheet. Such amounts are deferred and amortized over the life of the contract using the same methodology and assumptions used to amortize DAC. To qualify for such accounting treatment, the bonus interest must be explicitly identified in the contract at inception, and AIG must demonstrate that such amounts are incremental to amounts AIG credits on similar contracts without bonus interest, and are higher than the contract's expected ongoing crediting rates for periods after the bonus period. The deferred bonus interest and other deferred

1. Summary of Significant Accounting Policies

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sales inducement assets amounted to $1.3 billion and $1.1 billion at December 31, 2006 and 2005, respectively. The amortization expense associated with these assets is reported within Incurred policy losses and benefits expense on the consolidated statement of income. Such amortization expense totaled $135 million, $127 million and $104 million for the years ended December 31, 2006, 2005 and 2004, respectively.

See Note 19 herein for a discussion of derivatives.

(z) Reserve for Losses and Loss Expenses: Losses and loss expenses are charged to income as incurred. The reserve for losses and loss expenses represents the accumulation of estimates for unpaid reported losses and includes provisions for losses incurred but not reported. The methods of determining such estimates and establishing resulting reserves, including amounts relating to allowances for estimated unrecoverable reinsurance, are reviewed and updated. If the estimate of reserves is determined to be inadequate or redundant, the increase or decrease is reflected in income. AIG discounts its loss reserves relating to workers compensation business written by its U.S. domiciled subsidiaries as permitted by the domiciliary statutory regulatory authorities.

(aa) Future Policy Benefits for Life and Accident and Health Contracts: The liabilities for future policy benefits and policyholders' contract deposits are established using assumptions described in Note 6 herein.

(bb) Other Policyholders' Funds: Other policyholders' funds are reported at cost and include any policyholders' funds on deposit which encompasses premium deposits and similar items.

(cc) Financial Services — Securities and Spot Commodities Sold but not yet Purchased, at market value: Securities and spot commodities sold but not yet purchased represent sales of securities and spot commodities not owned at the time of sale. The obligations arising from such transactions are recorded on a trade-date basis and carried at fair value. Also included are obligations under gold leases, which are accounted for as a debt host with an embedded gold derivative.

(dd) Short- and Long-Term Borrowings: AIG's funding is principally obtained from medium term and long-term borrowings and commercial paper. Commercial paper, when issued at a discount, is recorded at the proceeds received and accreted to its par value. Long-term borrowings are carried at the principal amount borrowed, net of unamortized discounts or premiums. See Note 9 herein for additional information.

(ee) Liabilities Connected to Trust Preferred Stock: Liabilities connected to trust preferred stock principally relates to outstanding securities issued by American General Corporation (AGC), a wholly owned subsidiary of AIG. Cash distributions on such preferred stock are accounted for as interest expense.

(ff) Other Liabilities: Other liabilities consist of other funds on deposit, derivatives liabilities at fair value, other than derivatives in AIGFP, and other payables. See Note 19 herein for a discussion of Derivatives. AIG has entered into certain insurance and reinsurance contracts, primarily in its general insurance segment, that do not contain sufficient insurance risk to be accounted for as insurance or reinsurance. Accordingly, these transactions are recorded based upon deposit accounting, and the premiums received, after deduction for certain related expenses, are recorded as deposits within Other liabilities on the consolidated balance sheet. Net proceeds of these deposits are invested and generate net investment income. As amounts are paid, consistent with the underlying contracts, the deposit liability is reduced.

(gg) Preferred Shareholders' Equity in Subsidiary Companies: Preferred shareholders' equity in subsidiary companies relates principally to outstanding preferred stock or interest of ILFC, a wholly owned subsidiary of AIG. Cash distributions on such preferred stock or interest are accounted for as interest expense.

(hh) Recent Accounting Standards:

Accounting Changes

FSP FAS 115-1, ''The Meaning of Other-Than-Temporary Impairment and Its Application to Certain Investments,'' replaces the measurement and recognition guidance set forth in EITF Issue No. 03-1 and codifies certain existing guidance on impairment and accretion of income in periods subsequent to an other-than-temporary impairment, where appropriate. AIG's adoption of FSP FAS 115-1 on January 1, 2006 did not have a material effect on AIG's consolidated financial condition or results of operations.

In December 2004, the FASB issued FAS 123, ''Share-Based Payment'' (FAS 123R). FAS 123R and its related interpretive guidance replaces FAS 123, ''Accounting for Stock-Based Compensation'' (FAS 123), which superseded Accounting Principles Board Opinion No. 25, ''Accounting for Stock Issued to Employees'' (APB 25) and amended FAS 95, ''Statement of Cash Flows.'' FAS 123, as originally issued in 1995, established as preferable a fair-value-based method of accounting for share-based payment transactions with employees. On January 1, 2003, AIG adopted the recognition provisions of FAS 123. See also Note 14 herein. AIG adopted the provisions of the revised FAS 123R and its related interpretive guidance on January 1, 2006.

For its service-based awards under the 1999 Stock Option Plan, 2002 Stock Incentive Plan and 1996 Employee Stock Purchase Plan, AIG recognizes compensation on a straight-line basis over the scheduled vesting period. Unrecognized unvested compensation expense for stock option awards granted under APB 25 (i.e., before January 1, 2003) will be recognized from January 1, 2006 to the vesting date. However, for the SICO Plans, the AIG Deferred Compensation Profit Participant Plan (AIG DCPPP) and the AIG Partners Plan, which contain both performance and service conditions, AIG recognizes compensation utilizing a graded vesting expense attribution method. The effect of this approach is to recognize compensation cost over the requisite service period for each separately vesting tranche of the award.

AIG's share-based plans generally provide for accelerated vesting after the participant turns 65 and retires. For awards

1. Summary of Significant Accounting Policies

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granted after January 1, 2006, compensation expense is recognized ratably from the date of grant through the shorter of age 65 or the vesting period. This change did not have a material effect on AIG's consolidated financial position or results of operations. Awards granted prior to January 1, 2006 will continue to be recognized over the vesting period with accelerated expense recognition upon an actual retirement. Starr International Company, Inc. (SICO) compensation expense for participants retiring after age 65 had been reflected in prior years' results consistent with vested status under the SICO Plans.

At the June 2005 meeting, the FASB's Emerging Issues Task Force (EITF) reached a consensus with respect to Issue No. 04-5, ''Determining Whether a General Partner, or the General Partners as a Group, Controls a Limited Partnership or Similar Entity When the Limited Partners Have Certain Rights'' (EITF 04-5). EITF 04-5 addresses what rights held by the limited partner(s) preclude consolidation in circumstances in which the sole general partner would consolidate the limited partnership in accordance with generally accepted accounting principles absent the existence of the rights held by the limited partner(s). Based on that consensus, the EITF 04-5 also agreed to amend the consensus in Issue No. 96-16, ''Investor's Accounting for an Investee When the Investor Has a Majority of the Voting Interest but the Minority Shareholders Have Certain Approval or Veto Rights.'' The guidance in this Issue was effective after June 29, 2005 for general partners of all new limited partnerships formed and for existing limited partnerships for which the partnership agreements are modified. For general partners in all other limited partnerships, the guidance in this Issue was effective beginning January 1, 2006. The effect of the adoption of this EITF Issue was not material to AIG's consolidated financial condition or results of operations.

On June 29, 2005, the FASB issued Statement 133 Implementation Issue No. B38, ''Embedded Derivatives: Evaluation of Net Settlement with Respect to the Settlement of a Debt Instrument through Exercise of an Embedded Put Option or Call Option.'' This implementation guidance relates to the potential settlement of the debtor's obligation to the creditor that would occur upon exercise of the put option or call option, which meets the net settlement criterion in FAS 133. The effective date of the implementation guidance was January 1, 2006. The adoption of this guidance did not have a material effect on AIG's consolidated financial condition or results of operations.

On June 29, 2005, the FASB issued Statement 133 Implementation Issue No. B39, ''Application of Paragraph 13(b) to Call Options That Are Exercisable Only by the Debtor.'' The conditions in FAS 133 paragraph 13(b) do not apply to an embedded call option in a hybrid instrument containing a debt host contract if the right to accelerate the settlement of the debt can be exercised only by the debtor (issuer/borrower). This guidance does not apply to other embedded derivative features that may be present in the same hybrid instrument. The effective date of the implementation guidance was January 1, 2006. The adoption of this guidance did not have a material effect on AIG's consolidated financial condition or results of operations.

On February 16, 2006, the FASB issued FAS 155, ''Accounting for Certain Hybrid Financial Instruments'' (FAS 155), an amendment of FAS 140 and FAS 133. FAS 155 allows AIG to include changes in fair value in earnings on an instrument-by-instrument basis for any hybrid financial instrument that contains an embedded derivative that would otherwise be required to be bifurcated and accounted for separately under FAS 133. The election to measure the hybrid instrument at fair value is irrevocable at the acquisition or issuance date.

AIG elected to early adopt FAS 155 as of January 1, 2006, and apply FAS 155 fair value measurement to certain structured note liabilities and structured investments in AIG's available for sale portfolio that existed at December 31, 2005. The effect of this adoption resulted in an $11 million after-tax ($18 million pre-tax) decrease to opening retained earnings as of January 1, 2006, representing the difference between the fair value of these hybrid financial instruments and the prior carrying value as of December 31, 2005. The effect of adoption on after-tax gross gains and losses was $218 million ($336 million pre-tax) and $229 million ($354 million pre-tax), respectively.

In connection with AIG's early adoption of FAS 155, structured note liabilities of $8.9 billion, other structured liabilities in conjunction with equity derivative transactions of $111 million, and hybrid financial instruments of $522 million at December 31, 2006 are now carried at fair value. The effect on earnings for 2006, for changes in the fair value of hybrid financial instruments, was a pre-tax loss of $313 million, of which $287 million is reflected in Other income and is largely offset by gains on economic hedge positions which are also reflected in operating income, and $26 million is reflected in Net investment income.

In January 2007, the FASB issued Statement 133 Implementation Issue No. B40, ''Embedded Derivatives: Application of Paragraph 13(b) to Securitized Interests in Prepayable Financial Assets'' (Issue B40). Issue B40 provides guidance for when prepayment risk needs to be considered in determining whether mortgage-backed and other asset-backed securities contain an embedded derivative requiring bifurcation. Effective with AIG's adoption of FAS 155 beginning January 1, 2006, AIG has been treating derivatives embedded in securitized interests in prepayable financial assets in accordance with the guidance in Issue B40. Therefore, the adoption of this guidance did not have a material effect on AIG's consolidated financial condition or results of operations.

On March 27, 2006, the FASB issued FSP FTB 85-4-1, ''Accounting for Life Settlement Contracts by Third-Party Investors'' (FSP 85-4-1), an amendment of FTB 85-4, ''Accounting for Purchases of Life Insurance.'' Life settlements are designed to assist life insurance policyholders in monetizing the existing value of life insurance policies. FSP 85-4-1 allows AIG to measure life settlement contracts using either the investment method or fair value method. The election is made on an instrument-by-instrument basis and is irrevocable. AIG elected to early adopt FSP 85-4-1 as of January 1, 2006 using the investment method for pre-existing investments held at December 31, 2005. The effect of this adoption resulted in a $319 million after-tax ($487 million pre-tax)

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increase to opening retained earnings. See Note 8(h) herein for additional disclosures related to life settlement contracts.

On April 13, 2006, the FASB issued FSP FIN 46(R)-6, ''Determining the Variability to be Considered in Applying FASB Interpretation No. 46(R)'' (FIN 46(R)-6 or FSP). The FSP affects the identification of which entities are variable interest entities (VIEs) through a ''by design'' approach in identifying and measuring the variable interests of the VIE and its primary beneficiary. The requirements became effective beginning in the third quarter of 2006 and are to be applied to all new VIEs with which AIG becomes involved. The new requirements need not be applied to entities that have previously been analyzed under FIN 46(R) unless a reconsideration event occurs. The adoption of this guidance did not have a material effect on AIG's consolidated financial condition or results of operations.

In September 2006, the FASB issued FAS 158, ''Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans — an amendment of FASB Statements No. 87, 88, 106 and 132(R)'' (FAS 158). FAS 158 requires AIG to prospectively recognize the over funded or under funded status of defined benefit postretirement plans as an asset or liability in AIG's consolidated balance sheet and to recognize changes in that funded status in the year in which the changes occur through Other Comprehensive Income. FAS 158 also requires AIG to measure the funded status of plans as of the date of its year-end balance sheet, with limited exceptions. AIG adopted FAS 158 for the year ending December 31, 2006. The cumulative effect, net of deferred income taxes, on AIG's consolidated balance sheet at December 31, 2006 was a net reduction in shareholders' equity through a charge to Accumulated other comprehensive income of $532 million, with a corresponding net decrease of $538 million in total assets, and a net decrease of $6 million in total liabilities. See Note 15 herein for additional information on the adoption of FAS 158.

Future Application of Accounting Standards

On September 19, 2005, the AICPA issued Statement of Position 05-1, ''Accounting by Insurance Enterprises for Deferred Acquisition Costs in Connection with Modifications or Exchanges of Insurance Contracts'' (SOP 05-1). SOP 05-1 provides guidance on accounting for DAC on internal replacements of insurance and investment contracts other than those specifically described in FAS 97. SOP 05-1 defines an internal replacement as a modification in product benefits, features, rights, or coverage that occurs by the exchange of a contract for a new contract, or by amendment, endorsement, or rider to a contract, or by the election of a feature or coverage within a contract.

The effective date of the implementation guidance is January 1, 2007. Upon implementation, AIG expects to record a decrease to opening retained earnings of approximately $100 million, net of tax, to reflect changes in unamortized DAC, VOBA, unearned revenue liabilities and deferred sales inducement assets. This adjustment will reflect changes including the cumulative effect of a shorter expected amortization period for deferred items related to certain group life and health insurance contracts and the effect on the estimated gross profits of investment-oriented products related to previously anticipated future internal replacements. AIG does not expect the implementation of SOP 05-1 to have a material effect on its consolidated financial condition or its consolidated results of operations, although operating income for the Life Insurance & Retirement Services segment will be negatively affected.

On July 13, 2006, the FASB issued FASB Interpretation No. 48, ''Accounting for Uncertainty in Income Taxes — an interpretation of FASB Statement No. 109'' (FIN 48), which clarifies the accounting for uncertainty in income tax positions. FIN 48 prescribes a recognition threshold and measurement attribute for the financial statement recognition and measurement of an income tax position taken or expected to be taken in a tax return. FIN 48 also provides guidance on derecognition, classification, interest and penalties, accounting in interim periods, and additional disclosures. The effective date of this implementation guidance is January 1, 2007, with the cumulative effect of the change in accounting principles recorded as an adjustment to opening retained earnings. AIG does not expect the implementation of FIN 48 to be material to its consolidated financial condition.

In September 2006, the FASB issued FAS 157, ''Fair Value Measurements'' (FAS 157). FAS 157 defines fair value, establishes a framework for measuring fair value and expands disclosures about fair value measurements. FAS 157 is effective for financial statements issued for fiscal years beginning after November 15, 2007. AIG is currently assessing the effect of implementing this guidance.

In February 2007, the FASB issued FAS 159, ''The Fair Value Option for Financial Assets and Financial Liabilities'' (FAS 159). FAS 159 permits entities to choose to measure at fair value many financial instruments and certain other items that are not currently required to be measured at fair value. Subsequent changes in fair value for designated items will be required to be reported in earnings in the current period. FAS 159 also establishes presentation and disclosure requirements for similar types of assets and liabilities measured at fair value. FAS 159 is effective for financial statements issued for fiscal years beginning after November 15, 2007. AIG is currently assessing the effect of implementing this guidance, which depends on the nature and extent of items elected to be measured at fair value, upon initial application of the standard on January 1, 2008.

2. Segment Information

AIG identifies its reportable segments by product line consistent with its management structure. These segments and their respective operations are as follows:

General Insurance: AIG's General Insurance subsidiaries are multiple line companies writing substantially all lines of commercial property and casualty insurance and various personal lines both domestically and abroad. AIG's principal General Insurance operations are as follows:

2. Segment Information

Continued

Domestic Brokerage Group (DBG) writes substantially all classes of business insurance in the U.S. and Canada, accepting such business mainly from insurance brokers.

Transatlantic Holdings, Inc. (Transatlantic) subsidiaries offer reinsurance on both a treaty and facultative basis to insurers in the U.S. and abroad. Transatlantic structures programs for a full range of property and casualty products with an emphasis on specialty risks.

AIG's Personal Lines operations provide automobile insurance through AIG Direct, a mass marketing operation, Agency Auto Division and 21st Century Insurance Group (21st Century), as well as a broad range of coverages for high net-worth individuals through the AIG Private Client Group.

Mortgage Guaranty operations provide guaranty insurance primarily on conventional first mortgage loans on single family dwellings and condominiums.

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

Each of the General Insurance sub-segments is comprised of groupings of major products and services as follows: DBG is comprised of domestic commercial insurance products and services; Transatlantic is comprised of reinsurance products and services sold to other general insurance companies; Personal Lines are comprised of general insurance products and services sold to individuals; Mortgage Guaranty is comprised of products insuring against losses arising under certain loan agreements; and Foreign General is comprised of general insurance products sold overseas.

Life Insurance & Retirement Services: AIG's Life Insurance & Retirement Services subsidiaries offer a wide range of insurance and retirement savings products both domestically and abroad. Insurance-oriented products consist of individual and group life, payout annuities (including structured settlements), endowment and accident and health policies. Retirement savings products consist generally of fixed and variable annuities.

AIG's principal overseas Life Insurance & Retirement Services operations are American Life Insurance Company (ALICO), American International Assurance Company, Limited, together with American International Assurance Company (Bermuda) Limited (AIA), Nan Shan Life Insurance Company, Ltd. (Nan Shan), The Philippine American Life and General Insurance Company (PhilamLife), AIG Edison Life Insurance Company (AIG Edison Life) and AIG Star Life Insurance Co. Ltd. (AIG Star Life). In 2006, the major internal reporting units for the Foreign Life operations were realigned to better reflect the current management structure. PhilamLife and other Life operations were classified as a reporting unit in 2005. In 2006, PhilamLife is included with AIA, AIRCO and Nan Shan in the Asia internal reporting unit and other operations are included with ALICO, AIG Star Life and AIG Edison Life in the Japan and Other reporting unit. Prior period amounts have been reclassified to conform to the current period presentation.

AIG's principal Domestic Life Insurance & Retirement Services operations are American General Life Insurance Company (AG Life), The United States Life Insurance Company in the City of New York (USLIFE), American General Life and Accident Insurance Company (AGLA and, collectively with AG Life and USLIFE, the Domestic Life Insurance internal reporting unit), AIG Annuity Insurance Company (AIG Annuity), The Variable Annuity Life Insurance Company (VALIC) and AIG Retirement Services, Inc (AIG SunAmerica and, collectively with AIG Annuity and VALIC, the Domestic Retirement Services internal reporting unit).

American International Reinsurance Company (AIRCO) acts primarily as an internal reinsurance company for AIG's insurance operations.

Life Insurance & Retirement Services is comprised of two major groupings of products and services: insurance-oriented products and services and retirement savings products and services.

Financial Services: AIG's Financial Services subsidiaries engage in diversified financial products and services including aircraft and equipment leasing, capital markets transactions, consumer finance and insurance premium finance.

AIG's Aircraft Leasing operations represent the operations of International Lease Finance Corporation (ILFC), which generates its revenues primarily from leasing new and used commercial jet aircraft to domestic and foreign airlines. Revenues also result from the remarketing of commercial jets for its own account, and remarketing and fleet management services for airlines and for financial institutions.

AIG's Capital Markets operations are conducted through AIGFP. As Capital Markets is a transaction-oriented operation, current and past revenues and operating results may not provide a basis for predicting future performance.

AIG's Capital Markets operations derive substantially all their revenues from hedged financial positions entered in connection with counterparty transactions rather than from speculative transactions. These subsidiaries participate in the derivatives and financial transactions dealer markets conducting, primarily as principal, an interest rate, currency, equity, commodity, energy and credit products business.

Consumer Finance operations include American General Finance Inc. (AGF) as well as AIG Consumer Finance Group Inc. (AIGCFG). AGF and AIGCFG provide a wide variety of consumer finance products, including non-conforming real estate mortgages, consumer loans, retail sales finance and credit-related insurance to customers both domestically and overseas, particularly in emerging markets.

Asset Management: AIG's Asset Management operations comprise a wide variety of investment-related services and investment products including institutional and retail asset management, broker-dealer services and institutional spread-based investment business. Such services and products are offered to individuals and institutions both domestically and overseas.

2. Segment Information

Continued

The following table summarizes the operations by major operating segment for the years ended December 31, 2006, 2005 and 2004:

	Operating Segments							
(in millions)	General Insurance	Life Insurance & Retirement Services	Financial Services	Asset Management	Other[a]	Total	Consolidation and Elimination	Consolidated
2006								
Revenues[b]	**$ 49,206**	**$ 50,163**	**$ 8,010**	**$ 5,814**	**$ (295)**	**$ 112,898**	**$ 296**	**$113,194**
Interest expense	**23**	**74**	**6,216**	**105**	**533**	**6,951**	**—**	**6,951**
Operating income (loss) before minority interest	**10,412**	**10,032**	**524**	**2,346**	**(1,701)**	**21,613**	**74**	**21,687**
Income taxes (benefits)	**2,351**	**2,861**	**(23)**	**606**	**716**	**6,511**	**26**	**6,537**
Depreciation expense	**274**	**268**	**1,655**	**13**	**164**	**2,374**	**—**	**2,374**
Capital expenditures	**375**	**711**	**6,278**	**835**	**244**	**8,443**	**—**	**8,443**
Identifiable assets	**167,004**	**534,977**	**206,845**	**97,913**	**105,279**	**1,112,018**	**(132,604)**	**979,414**
2005								
Revenues[b]	$ 45,174	$ 47,376	$ 10,525	$ 5,325	$ 505	$ 108,905	$ —	$108,905
Interest expense	7	83	5,279	11	293	5,673	—	5,673
Operating income (loss) before minority interest	2,315	8,904	4,276	2,253	(2,535)[c]	15,213	—	15,213
Income taxes (benefits)	140	2,155	1,366	718	(121)	4,258	—	4,258
Depreciation expense	273	268	1,447	43	169	2,200	—	2,200
Capital expenditures	417	590	6,300	25	194	7,526	—	7,526
Identifiable assets	150,667	480,622	166,488	81,080	92,835	971,692	(118,641)	853,051
2004								
Revenues[b]	$ 41,961	$ 43,402	$ 7,495	$ 4,714	$ 94	$ 97,666	$ —	$ 97,666
Interest expense	9	63	4,041	8	306	4,427	—	4,427
Operating income (loss) before minority interest	3,177	7,925	2,180	2,125	(562)	14,845	—	14,845
Income taxes (benefits)	616	2,525	654	753	(141)	4,407	—	4,407
Depreciation expense	251	262	1,366	19	137	2,035	—	2,035
Capital expenditures	350	480	4,481	11	207	5,529	—	5,529
Identifiable assets	131,658	447,841	165,995	80,075	79,752	905,321	(104,314)	801,007

(a) *Includes AIG Parent and other operations which are not required to be reported separately. The following table presents the operating loss for AIG's Other category for the years ended December 31, 2006, 2005 and 2004:*

For the Years Ended December 31, *(in millions)*	**2006**	2005	2004
Operating income (loss):			
Equity earnings in unconsolidated entities*	**$ 193**	$ (124)	$ 157
Interest expense	**(859)**	(541)	(435)
Unallocated corporate expenses	**(555)**	(413)	(316)
Compensation expense — SICO Plans	**(108)**	(205)	(62)
Compensation expense — Starr tender offer	**(54)**	—	—
Realized capital gains (losses)	**(295)**	505	94
Regulatory settlement costs	**—**	(1,644)	—
Other miscellaneous, net	**(23)**	(113)	—
Total Other	**$ (1,701)**	$ (2,535)	$ (562)

* *Includes current year catastrophe-related losses from unconsolidated entities of $312 million and $96 million for 2005 and 2004, respectively. There were no significant catastrophe-related losses in 2006.*

(b) *Represents the sum of General Insurance net premiums earned, Life Insurance & Retirement Services GAAP premiums, net investment income, Financial Services interest, lease and finance charges, Asset Management net investment income from spread-based products and advisory and management fees, and realized capital gains (losses).*

(c) *Includes settlement costs of $1.64 billion as described in Note 12(a) Litigation and Investigations herein.*

2. Segment Information

Continued

The following table summarizes AIG's General Insurance operations by major internal reporting unit for the years ended December 31, 2006, 2005 and 2004:

	General Insurance							
(in millions)	Domestic Brokerage Group	Transatlantic	Personal Lines	Mortgage Guaranty	Foreign General	Total Reportable Segment	Consolidation and Elimination	Total General Insurance
2006								
Revenues[a][b]	**$ 27,445**	**$ 4,050**	**$4,871**	**$ 877**	**$11,973**	**$ 49,216**	**$ (10)**	**$ 49,206**
Losses & loss expenses incurred	**16,622**	**2,463**	**3,306**	**349**	**5,312**	**28,052**	**—**	**28,052**
Underwriting expenses	**4,838**	**998**	**1,133**	**200**	**3,573**	**10,742**	**—**	**10,742**
Operating income[b][c][d]	**5,985**	**589**	**432**	**328**	**3,088**	**10,422**	**(10)**	**10,412**
Depreciation expense	**100**	**2**	**52**	**5**	**115**	**274**	**—**	**274**
Capital expenditures	**125**	**2**	**94**	**11**	**143**	**375**	**—**	**375**
Identifiable assets	**104,866**	**14,268**	**5,391**	**3,604**	**43,879**	**172,008**	**(5,004)**	**167,004**
2005								
Revenues[a]	$ 25,206	$ 3,766	$4,848	$ 655	$10,684	$ 45,159	$ 15	$ 45,174
Losses & loss expenses incurred	21,328	2,877	3,566	139	5,181	33,091	—	33,091
Underwriting expenses	4,524	928	1,087	153	3,076	9,768	—	9,768
Operating income (loss)[c][d][e]	(646)[f]	(39)	195	363	2,427	2,300	15	2,315
Depreciation expense	114	2	48	4	105	273	—	273
Capital expenditures	119	2	94	6	196	417	—	417
Identifiable assets	95,829	12,365	5,245	3,165	39,044	155,648	(4,981)	150,667
2004								
Revenues[a]	$ 23,332	$ 3,990	$4,488	$ 660	$ 9,473	$ 41,943	$ 18	$ 41,961
Losses & loss expenses incurred	18,808	2,755	3,211	142	5,441	30,357	—	30,357
Underwriting expenses	3,747	953	920	119	2,688	8,427	—	8,427
Operating income[c]	777	282	357	399	1,344	3,159	18	3,177
Depreciation expense	122	3	29	3	94	251	—	251
Capital expenditures	115	2	92	7	134	350	—	350
Identifiable assets	81,754	10,605	5,159	2,826	36,055	136,399	(4,741)	131,658

(a) Represents the sum of General Insurance net premiums earned, net investment income and realized capital gains (losses).

(b) Includes the effect of out of period adjustments related to the accounting for certain interests in unit investment trusts. For DBG, the effect was an increase of $66 million in both revenues and operating income and for Foreign General, the effect was an increase of $424 million in both revenues and operating income.

(c) There were no significant catastrophe-related losses in 2006. Catastrophe-related losses for 2005 and 2004 by reporting unit were:

	2005		2004	
(in millions)	Insurance Related Losses	Net Reinstatement Premium Cost	Insurance Related Losses	Net Reinstatement Premium Cost
Reporting Unit:				
DBG	$1,747	$122	$ 582	$ —
Transatlantic	463	45	215	—
Personal Lines	112	2	25	—
Mortgage Guaranty	10	—	—	—
Foreign General	293	94	232	—
Total	$2,625	$263	$1,054	$ —

(d) Includes additional losses incurred and net reinstatement premiums related to prior year catastrophes of $199 million and $277 million in 2006 and 2005, respectively.

(e) Includes the fourth quarter 2005 increase in net reserves of approximately $1.8 billion resulting from the annual review of General Insurance loss and loss adjustment reserves.

(f) Includes $291 million of expenses related to changes in estimates for uncollectible reinsurance and other premium balances, and $100 million of accrued expenses in connection with certain workers compensation insurance policies written between 1985 and 1996.

2. Segment Information

Continued

The following table summarizes AIG's Life Insurance & Retirement Services operations by major internal reporting unit for the years ended December 31, 2006, 2005 and 2004:

	Life Insurance & Retirement Services						
(in millions)	Japan and Other[a]	Asia[b]	Domestic Life Insurance[c]	Domestic Retirement Services[d]	Total Reportable Segment	Consolidation and Elimination	Total Life Insurance & Retirement Services
2006							
Revenues:[e][f]							
Insurance-oriented products	**$ 13,243**	**$ 17,712**	**$ 8,538**	**$ —**	**$ 39,493**	**$ —**	**$ 39,493**
Retirement savings products	**2,793**	**168**	**568**	**7,141**	**10,670**	**—**	**10,670**
Total revenues	**16,036**	**17,880**	**9,106**	**7,141**	**50,163**	**—**	**50,163**
Operating income[f]	**3,732**	**3,060**	**917**	**2,323**	**10,032**	**—**	**10,032**
Depreciation expense	**101**	**70**	**63**	**34**	**268**	**—**	**268**
Capital expenditures	**342**	**260**	**71**	**38**	**711**	**—**	**711**
Identifiable assets	**136,127**	**109,148**	**103,628**	**192,885**	**541,788**	**(6,811)**	**534,977**
2005							
Revenues:[e]							
Insurance-oriented products	$ 12,436	$ 15,853	$ 8,525	$ —	$ 36,814	$ —	$ 36,814
Retirement savings products	2,857	129	690	6,886	10,562	—	10,562
Total revenues	15,293	15,982	9,215	6,886	47,376	—	47,376
Operating income	2,959	2,286	1,495	2,164	8,904	—	8,904
Depreciation expense	91	81	65	31	268	—	268
Capital expenditures	153	340	71	26	590	—	590
Identifiable assets	115,487	87,816	99,597	185,383	488,283	(7,661)	480,622
2004							
Revenues:[e]							
Insurance-oriented products	$ 10,690	$ 15,789	$ 8,011	$ —	$ 34,490	$ —	$ 34,490
Retirement savings products	1,537	107	704	6,564	8,912	—	8,912
Total revenues	12,227	15,896	8,715	6,564	43,402	—	43,402
Operating income	2,393	2,455	1,023	2,054	7,925	—	7,925
Depreciation expense	104	59	62	37	262	—	262
Capital expenditures	308	96	47	29	480	—	480
Identifiable assets	104,060	76,025	91,538	183,092	454,715	(6,874)	447,841

(a) *Revenues and operating income include realized capital gains (losses) of $406 million, $(72) million and $(156) million for 2006, 2005 and 2004, respectively. Includes the effect of hedging activities that did not qualify for hedge accounting treatment under FAS 133 and the application of FAS 52, which were $191 million, $(462) million and $(300) million for 2006, 2005 and 2004, respectively.*

(b) *Revenues in 2004 include approximately $640 million of premium from a single reinsurance transaction involving terminal funding pension business, which is offset by a similar increase in benefit reserves. Revenues and operating income include realized capital gains (losses) of $301 million, $156 million and $528 million for 2006, 2005 and 2004, respectively. Includes the effect of hedging activities that did not qualify for hedge accounting treatment under FAS 133 and the application of FAS 52, which were $191 million, $(97) million and $166 million for 2006, 2005 and 2004, respectively.*

(c) *Includes the life operations of AIG Life Insurance Company and American International Life Assurance Company of New York. Operating income in 2006 included charges of $125 million resulting from the adverse Superior National arbitration ruling and $66 million related to the exiting of the domestic financial institutions credit life business. Operating income in 2004 included a $178 million charge related to a workers compensation quota share reinsurance agreement with Superior National. See Note 12(c) herein for additional information. In addition, in 2004, as part of the business review of group life/health, approximately $68 million was incurred for reserve strengthening and allowances for receivables. Revenues and operating income include realized capital gains (losses) of $(215) million, $35 million and $(120) million for 2006, 2005 and 2004, respectively. Includes the effect of hedging activities that did not qualify for hedge accounting treatment under FAS 133 and the application of FAS 52, which were $19 million, $76 million and $8 million for 2006, 2005 and 2004, respectively.*

(d) *Revenues and operating income include realized capital gains (losses) of $(404) million, $(277) million and $(207) million for 2006, 2005 and 2004, respectively. Includes the effect of hedging activities that did not qualify for hedge accounting treatment under FAS 133 and the application of FAS 52, which were $(46) million, $(12) million and $(14) million for 2006, 2005 and 2004, respectively.*

(e) *Represents the sum of Life Insurance & Retirement Services GAAP premiums, net investment income and realized capital gains (losses).*

(f) *Includes the effect of out of period adjustments related to the accounting for certain interests in unit investment trusts. For 2006 the effect was an increase of $240 million in revenues and $169 million in operating income.*

2. Segment Information

Continued

The following table summarizes AIG's Financial Services operations by major internal reporting unit for the years ended December 31, 2006, 2005 and 2004:

	Financial Services						
(in millions)	Aircraft Leasing	Capital Markets[a]	Consumer Finance	Other[b]	Total Reportable Segment	Consolidation and Elimination	Total Financial Services
2006							
Revenues[c][d][e]	**$ 4,143**	**$ (186)**	**$ 3,819**	**$ 626**	**$ 8,402**	**$ (392)**	**$ 8,010**
Interest expense[d]	**1,442**	**3,215**	**1,303**	**319**	**6,279**	**(63)**	**6,216**
Operating income (loss)[e]	**639**	**(873)**	**761[f]**	**(3)**	**524**	**—**	**524**
Depreciation expense	**1,584**	**19**	**41**	**11**	**1,655**	**—**	**1,655**
Capital expenditures	**6,012**	**15**	**52**	**199**	**6,278**	**—**	**6,278**
Identifiable assets	**41,975**	**121,243**	**32,702**	**16,786**	**212,706**	**(5,861)**	**206,845**
2005							
Revenues[c][d][e]	$ 3,578	$ 3,260	$ 3,613	$ 387	$ 10,838	$ (313)	$ 10,525
Interest expense[d]	1,125	3,033	1,005	316	5,479	(200)	5,279
Operating income[e]	679	2,661	876[f]	60	4,276	—	4,276
Depreciation expense	1,384	20	38	5	1,447	—	1,447
Capital expenditures	6,193	3	54	50	6,300	—	6,300
Identifiable assets	37,515	90,090	30,704	14,872	173,181	(6,693)	166,488
2004							
Revenues[c][d][e]	$ 3,136	$ 1,278	$ 2,978	$ 835	$ 8,227	$ (732)	$ 7,495
Interest expense[d]	993	2,300	705	144	4,142	(101)	4,041
Operating income[e]	642	662	786	90	2,180	—	2,180
Depreciation expense	1,273	42	33	18	1,366	—	1,366
Capital expenditures	4,400	29	35	17	4,481	—	4,481
Identifiable assets	33,997	98,303	26,560	13,985	172,845	(6,850)	165,995

(a) Certain transactions entered into by AIGFP generate tax credits and benefits which are included in income taxes in the consolidated statement of income. The amount of such tax credits and benefits for the years ended December 31, 2006, 2005 and 2004 were $50 million, $67 million, and $107 million, respectively.

(b) Operating loss in 2006 includes specific reserves of $42 million related to two commercial lending transactions.

(c) Represents primarily the sum of aircraft lease rentals from ILFC, AIGFP hedged financial positions entered into in connection with counterparty transactions, the effect of hedging activities that did not qualify for hedge accounting treatment under FAS 133, including the related foreign exchange gains and losses, and finance charges from consumer finance operations.

(d) Interest expense for the Capital Markets business is included in Revenues above and in Other income on the Consolidated Statement of Income.

(e) Includes the effect of hedging activities that did not qualify for hedge accounting treatment under FAS 133, including the related foreign exchange gains and losses. For 2006, 2005 and 2004, respectively, the effect was $(1.82) billion, $2.01 billion and $(122) million in both revenues and operating income for Capital Markets. These amounts result primarily from interest rate and foreign currency derivatives that are economically hedging available for sale securities and borrowings. For 2004, the effect was $(27) million in operating income for Aircraft Leasing. During 2006 and 2005, Aircraft Leasing derivative gains and losses were reported as part of AIG's Other category, and were not reported in Aircraft Leasing's operating income.

(f) Includes catastrophe-related losses of $62 million recorded in 2005 resulting from hurricane Katrina, which were reduced by $35 million in 2006 as a result of reevaluation of the remaining estimated losses.

2. Segment Information

Continued

A substantial portion of AIG's operations is conducted in countries other than the United States and Canada. The following table summarizes AIG's operations by major geographic segment. Allocations have been made on the basis of the location of operations and assets.

	Geographic Segments			
(in millions)	Domestic[a]	Far East	Other Foreign	Consolidated
2006				
Revenues[b]	**$57,986**	**$33,795**	**$21,413**	**$113,194**
Real estate and other fixed assets, net of accumulated depreciation	**2,432**	**1,082**	**867**	**4,381**
Flight equipment primarily under operating leases, net of accumulated depreciation[c]	**39,875**	**—**	**—**	**39,875**
2005				
Revenues[b]	$59,858	$32,036	$17,011	$108,905
Real estate and other fixed assets, net of accumulated depreciation	1,905	929	807	3,641
Flight equipment primarily under operating leases, net of accumulated depreciation[c]	36,245	—	—	36,245
2004				
Revenues[b]	$53,827	$27,761	$16,078	$ 97,666
Real estate and other fixed assets, net of accumulated depreciation	1,777	894	834	3,505
Flight equipment primarily under operating leases, net of accumulated depreciation[c]	32,130	—	—	32,130

(a) Including revenues from General Insurance operations in Canada of $691 million, $638 million and $549 million in 2006, 2005 and 2004, respectively.

(b) Represents the sum of General Insurance net premiums earned, Life Insurance & Retirement Services GAAP premiums, net investment income, Financial Services interest, lease and finance charges, Asset Management net investment income with respect to spread-based products and advisory and management fees, and realized capital gains (losses).

(c) Approximately 90 percent of ILFC's fleet is operated by foreign airlines.

3. Federal Income Taxes

AIG and its eligible U.S. subsidiaries file a consolidated U.S. federal income tax return. Life Insurance subsidiaries of American General Corporation (AGC) also file a consolidated U.S. federal income tax return and will not be included in AIG's consolidated federal income tax return until 2007. Other U.S. entities included in the consolidated financial statements also file separate U.S. federal income tax returns. Subsidiaries operating outside the U.S. are taxed, and income tax expense is recorded, based on applicable U.S. and foreign statutes.

U.S. federal income taxes have not been provided on $1.3 billion of undistributed earnings of certain U.S. subsidiaries that are not included in the consolidated AIG U.S. federal income tax return because tax planning strategies are available, and would be utilized, to eliminate the tax liability related to these earnings. U.S. federal income taxes have not been provided on the undistributed earnings of certain non-U.S. subsidiaries to the extent that such earnings have been reinvested abroad for an indefinite period of time. At December 31, 2006, the cumulative amount of undistributed earnings in these subsidiaries approximated $17.6 billion. Determining the deferred tax liability that would arise if these earnings were not permanently reinvested abroad is not practicable.

A component of life insurance surplus accumulated prior to 1984 is not taxable unless it exceeds certain statutory limitations or is distributed to shareholders. The American Jobs Creation Act of 2004 amended the federal income tax law to permit life insurance companies to distribute amounts from their policyholders' surplus accounts in 2005 and 2006 without incurring federal income tax on the distributions. In 2005 and 2006, AIG made distributions and eliminated the aggregate balance of $945 million from its policyholders' surplus accounts.

A Revenue Agent's Report proposing to assess additional taxes for the years 1997 to 1999 has been issued to AIG and a Letter of Protest contesting the proposed assessments has been filed with the Internal Revenue Service (IRS). A draft settlement agreed to in substance has been received from the IRS for years 1997 to 1999. Settlement has been reached with the IRS for years prior to 1997 although AIG has reserved the right to timely claim refunds for items related to the restatements of AIG's 2004 and prior financial statements during 2005.

In addition, for the years ended September 30, 1993 and 1994, a Notice of Deficiency assessing additional taxes has been issued to AIG Retirement Services Inc., which has filed a petition for redetermination with the United States Tax Court challenging the Notice. Revenue Agents' Reports for the years ended September 30, 1995 and 1996 and for the period from September 30, 1997 to December 31, 1998 have also been issued to AIG Retirement Services Inc., and Letters of Protest contesting the proposed assessments have been filed with the IRS. Similarly, SunAmerica Life Insurance Company (SunAmerica Life) has also received a proposed assessment and has filed a protest for the year ended December 31, 1999.

3. Federal Income Taxes

Continued

It is management's belief that there are substantial arguments in support of the positions taken by AIG, AIG Retirement Services Inc., and SunAmerica Life in their Letters of Protest and Tax Court litigation. Although the final outcome of any issues raised in connection with these years is uncertain, AIG believes that any tax obligation, including interest thereon, would not be material to AIG's consolidated financial condition, results of operations or liquidity.

AGC's tax years through 1999 have been audited and settled with the IRS. Although a Revenue Agent's Report has not yet been issued to AGC for years ended December 31, 2000, 2001 and 2002, AIG has received a notice of proposed adjustment for certain items during that period from the IRS.

The pretax components of U.S. and foreign income reflect the locations in which such pretax income was generated. The pretax U.S. and foreign income was as follows for the years ended December 31, 2006, 2005 and 2004:

(in millions)	**2006**	2005	2004
U.S.	**$ 9,862**	$ 6,103	$ 6,069
Foreign	**11,825**	9,110	8,776
Total	**$21,687**	$15,213	$14,845

The U.S. federal income tax rate was 35 percent for 2006, 2005 and 2004. Actual tax expense on income differs from the ''expected'' amount computed by applying the federal income tax rate because of the following:

	2006		2005		2004	
Years Ended December 31, *(dollars in millions)*	Amount	Percent of Pretax Income	Amount	Percent of Pretax Income	Amount	Percent of Pretax Income
U.S. federal income tax at statutory rate	**$7,591**	**35.0%**	$5,325	35.0%	$5,197	35.0%
Adjustments:						
Tax exempt interest	**(718)**	**(3.3)**	(566)	(3.7)	(440)	(2.9)
Partnerships and joint ventures	**(265)**	**(1.2)**	(85)	(0.5)	(27)	(0.2)
Synthetic fuel and other tax credits	**(196)**	**(0.9)**	(296)	(1.9)	(310)	(2.1)
Effect of foreign operations	**(132)**	**(0.6)**	(253)	(1.7)	(11)	(0.1)
Dividends received deduction	**(102)**	**(0.5)**	(117)	(0.8)	(83)	(0.6)
State income taxes	**59**	**0.3**	86	0.6	23	0.2
Nondeductible compensation	**61**	**0.3**	83	0.5	20	0.1
Penalties	**3**	**—**	76	0.5	28	0.2
Other	**236**	**1.0**	5	—	10	0.1
Actual income tax expense	**$6,537**	**30.1%**	$4,258	28.0%	$4,407	29.7%
Foreign and U.S. components of actual income tax expense:						
Foreign:						
Current	**$2,725**		$ 974		$1,104	
Deferred	**933**		426		561	
U.S.:						
Current	**2,764**		1,613		1,541	
Deferred	**115**		1,245		1,201	
Total	**$6,537**		$4,258		$4,407	

3. Federal Income Taxes

Continued

The components of the net deferred tax liability as of December 31, 2006 and 2005 were as follows:

(in millions)	**2006**	2005
Deferred tax assets:		
Loss reserve discount	**$ 1,969**	$ 2,242
Unearned premium reserve reduction	**1,352**	1,042
Loan loss and other reserves	**1,054**	419
Investment in foreign subsidiaries and joint ventures	**420**	349
Adjustment to life policy reserves	**3,584**	3,170
Accruals not currently deductible, and other	**1,420**	1,189
Total deferred tax assets	**9,799**	8,411
Deferred tax liabilities:		
Deferred policy acquisition costs	**10,396**	7,573
Flight equipment, fixed assets and intangible assets	**4,377**	3,196
Unrealized appreciation of investments	**3,370**	4,025
Other	**508**	224
Total deferred tax liabilities	**18,651**	15,018
Net deferred tax liability	**$ 8,852**	$ 6,607

AIG has recorded alternative minimum tax credit carry forwards of $222 million and $192 million at December 31, 2006 and 2005, respectively. The alternative minimum tax credits do not expire.

4. Deferred Policy Acquisition Costs

The following reflects the policy acquisition costs deferred for amortization against future income and the related amortization charged to income for General Insurance and Life Insurance & Retirement Services operations:

Years Ended December 31, *(in millions)*	**2006**	2005	2004
General Insurance operations:			
Balance at beginning of year	**$ 4,048**	$ 3,998	$ 3,619
Acquisition costs deferred	**8,115**	7,480	6,617
Amortization expense	**(7,866)**	(7,365)	(6,301)
Increase (decrease) due to foreign exchange	**58**	(65)	63
Balance at end of year	**$ 4,355**	$ 4,048	$ 3,998
Life Insurance & Retirement Services operations:			
Balance at beginning of year	**$28,106**	$25,080	$21,822
Acquisition costs deferred	**6,823**	6,513	6,266
Amortization expense	**(3,712)**	(3,328)	(3,514)
Change in net unrealized gains (losses) on securities	**646**	977	(198)
Increase (decrease) due to foreign exchange	**947**	(1,136)	704
Subtotal	**$32,810**	$28,106	$25,080
Consolidation and elimination	**70**	—	—
Balance at end of year	**$32,880**	$28,106	$25,080
Total deferred policy acquisition costs	**$37,235**	$32,154	$29,078

Included in the above table is the VOBA, an intangible asset recorded during purchase accounting, which is amortized in a manner similar to DAC. Amortization of VOBA was $239 million, $291 million and $407 million while the unamortized balance was $1.98 billion, $2.14 billion and $2.52 billion for 2006, 2005 and 2004, respectively. The percentage of the unamortized balance of VOBA at 2006 expected to be amortized for 2007 through 2012 by year is: 11.3 percent, 10.0 percent, 8.8 percent, 7.3 percent and 6.0 percent, respectively, with 56.6 percent being amortized after five years. These projections are based on current estimates for investment, persistency, mortality, and morbidity assumptions. The DAC amortization charged to income includes the increase or decrease of amortization for FAS 97-related realized capital gains (losses), primarily in the Domestic Retirement Services business. For 2006, 2005 and 2004, respectively, the rate of amortization expense decreased by $98 million, $46 million and $41 million.

There were no impairments of DAC or VOBA for the years ended December 31, 2006, 2005 and 2004.

5. Reinsurance

In the ordinary course of business, AIG's General Insurance and Life Insurance companies place reinsurance with other insurance companies in order to provide greater diversification of AIG's business and limit the potential for losses arising from large risks. In addition, AIG's General Insurance subsidiaries assume reinsurance from other insurance companies.

General Reinsurance: General reinsurance is effected under reinsurance treaties and by negotiation on individual risks. Certain of these reinsurance arrangements consist of excess of loss contracts which protect AIG against losses over stipulated amounts. Ceded premiums are considered prepaid reinsurance premiums and are recognized as a reduction of premiums earned over the contract period in proportion to the protection received. Amounts recoverable from general reinsurers are estimated in a manner consistent with the claims liabilities associated with the reinsurance and presented as a component of reinsurance assets. Assumed reinsurance premiums are earned primarily on a pro-rata basis over the terms of the reinsurance contracts.

General Insurance premiums written and earned were comprised of the following:

Years Ended December 31, *(in millions)*	**2006**	2005	2004
Premiums written:			
Direct	**$ 49,609**	$ 46,689	$ 44,692
Assumed	**6,671**	6,036	7,354
Ceded	**(11,414)**	(10,853)	(11,423)
Total	**$ 44,866**	$ 41,872	$ 40,623
Premiums earned:			
Direct	**$ 47,973**	$ 45,794	$ 43,109
Assumed	**6,449**	5,921	7,094
Ceded	**(10,971)**	(10,906)	(11,666)
Total	**$ 43,451**	$ 40,809	$ 38,537

For the years ended December 31, 2006, 2005 and 2004, reinsurance recoveries, which reduced loss and loss expenses incurred, amounted to $8.3 billion, $20.7 billion and $12.1 billion, respectively.

Life Insurance: Life reinsurance is effected principally under yearly renewable term treaties. The premiums with respect to these treaties are considered prepaid reinsurance premiums and are recognized as a reduction of premiums earned over the contract period in proportion to the protection provided. Amounts recoverable from life reinsurers are estimated in a manner consistent with the assumptions used for the underlying policy benefits and are presented as a component of reinsurance assets.

Life Insurance & Retirement Services premiums were comprised of the following:

Years Ended December 31, *(in millions)*	**2006**	2005	2004
Gross premiums	**$32,117**	$30,717	$29,202
Ceded premiums	**(1,481)**	(1,317)	(1,114)
Premiums	**$30,636**	$29,400	$28,088

Life Insurance recoveries, which reduced death and other benefits, approximated $806 million, $770 million and $779 million, respectively, for the years ended December 31, 2006, 2005 and 2004.

Life Insurance in force ceded to other insurance companies was as follows:

Years Ended December 31, *(in millions)*	**2006**	2005	2004
Life Insurance in force ceded	**$408,970**	$365,082	$344,036

Life Insurance assumed represented 0.1 percent, 0.8 percent and 0.7 percent of gross Life Insurance in force at December 31, 2006, 2005 and 2004, respectively, and Life Insurance & Retirement Services premiums assumed represented 0.1 percent, 0.3 percent and 2.5 percent of gross GAAP premiums for the years ended December 31, 2006, 2005 and 2004, respectively.

Supplemental information for gross loss and benefit reserves net of ceded reinsurance at December 31, 2006 and 2005 follows:

(in millions)	As Reported	Net of Reinsurance
2006		
Reserve for losses and loss expenses	**$ (79,999)**	**$ (62,630)**
Future policy benefits for life and accident and health insurance contracts	**(122,230)**	**(120,656)**
Reserve for unearned premiums	**(26,271)**	**(22,759)**
Reinsurance assets	**23,355**	—
2005		
Reserve for losses and loss expenses	$ (77,169)	$ (57,476)
Future policy benefits for life and accident and health insurance contracts	(108,807)	(107,420)
Reserve for unearned premiums	(24,243)	(21,174)
Reinsurance assets	24,978	—

AIRCO acts primarily as an internal reinsurance company for AIG's insurance operations. This facilitates insurance risk management (retention, volatility, concentrations) and capital planning locally (branch and subsidiary). It also allows AIG to pool its insurance risks and purchase reinsurance more efficiently at a consolidated level, manage global counterparty risk and relationships and manage global life catastrophe risks.

AIG's Domestic Life Insurance & Retirement Services operations utilize internal and third-party reinsurance relationships to

5. Reinsurance

Continued

manage insurance risks and to facilitate capital management strategies. Pools of highly-rated third-party reinsurers are utilized to manage net amounts at risk in excess of retention limits. AIG's Domestic Life Insurance companies also cede excess, non-economic reserves carried on a statutory-basis only on certain term and universal life insurance policies and certain fixed annuities to an offshore affiliate.

AIG generally obtains letters of credit in order to obtain statutory recognition of its intercompany reinsurance transactions. For this purpose, AIG has a $2.5 billion syndicated letter of credit facility outstanding as of December 31, 2006, all of which relates to life intercompany reinsurance transactions.

AIG is also a party to a 364-day bilateral revolving credit facility for an aggregate amount of $3.2 billion. The facility can be drawn in the form of letters of credit with terms of up to eight years. As of December 31, 2006, approximately $2.69 billion principal amount of letters of credit are outstanding under this facility, of which approximately $1.3 billion relates to life intercompany reinsurance transactions. AIG has also obtained approximately $201 million of letters of credit on a bilateral basis.

Reinsurance Security: AIG's third party reinsurance arrangements do not relieve AIG from its direct obligation to its insureds. Thus, a credit exposure exists with respect to both general and life reinsurance ceded to the extent that any reinsurer fails to meet the obligations assumed under any reinsurance agreement. AIG holds substantial collateral as security under related reinsurance agreements in the form of funds, securities, and/or letters of credit. A provision has been recorded for estimated unrecoverable reinsurance. AIG has been largely successful in prior recovery efforts.

AIG evaluates the financial condition of its reinsurers and establishes limits per reinsurer through AIG's Credit Risk Committee. AIG believes that no exposure to a single reinsurer represents an inappropriate concentration of risk to AIG, nor is AIG's business substantially dependent upon any single reinsurer.

6. Reserve for Losses and Loss Expenses and Future Life Policy Benefits and Policyholders' Contract Deposits

The following analysis provides a reconciliation of the activity in the reserve for losses and loss expenses:

Years Ended December 31, *(in millions)*	**2006**	2005	2004
At beginning of year:			
Reserve for losses and loss expenses	**$ 77,169**	$ 61,878	$ 51,871
Reinsurance recoverable	**(19,693)**	(14,624)	(15,643)
Total	**57,476**	47,254	36,228
Foreign exchange effect	**741**	(628)	524
Acquisition[(a)]	**55**	—	—
Losses and loss expenses incurred:			
Current year	**27,805**	28,426	26,793
Prior years, other than accretion of discount	**(53)**	4,680[(b)]	3,187[(c)]
Prior years, accretion of discount	**300**	(15)	377
Total	**28,052**	33,091	30,357
Losses and loss expenses paid:			
Current year	**8,368**	7,331	7,692
Prior years	**15,326**	14,910	12,163
Total	**23,694**	22,241	19,855
At end of year:			
Net reserve for losses and loss expenses	**62,630**	57,476	47,254
Reinsurance recoverable	**17,369**	19,693	14,624
Total	**$ 79,999**	$ 77,169	$ 61,878

(a) Reflects the opening balance with respect to the acquisition of the Central Insurance Co., Ltd. in the third quarter of 2006.

(b) Includes fourth quarter charge of $1.8 billion resulting from the annual review of General Insurance loss and loss adjustment reserves.

(c) Includes fourth quarter charge of $850 million attributable to the change in estimate for asbestos and environmental exposures.

The analysis of the future policy benefits and policyholders' contract deposits liabilities follows:

Years Ended December 31, *(in millions)*	**2006**	2005*
Future policy benefits:		
Long duration contracts	**$121,364**	$107,877
Short duration contracts	**866**	930
Total	**$122,230**	$108,807

** 2005 amounts have been reclassified to conform to 2006 presentation.*

6. Reserve for Losses and Loss Expenses and Future Life Policy Benefits and Policyholders' Contract Deposits

Continued

Years Ended December 31, *(in millions)*	**2006**	2005*
Policyholders' contract deposits:		
Annuities	**$144,599**	$142,057
GICs	**34,746**	39,705
Universal life products	**22,632**	18,682
Variable investment contracts	**14,289**	8,373
Variable products	**14,264**	7,799
Corporate life products	**2,083**	2,077
Other investment contracts	**12,045**	8,334
Total	**$244,658**	$227,027

Long duration contract liabilities included in future policy benefits, as presented in the preceding table, result from life products. Short duration contract liabilities are primarily accident and health products. The liability for future life policy benefits has been established based upon the following assumptions:

- Interest rates (exclusive of immediate/terminal funding annuities), which vary by territory, year of issuance and products, range from 1.0 percent to 12.5 percent within the first 20 years. Interest rates on immediate/terminal funding annuities are at a maximum of 11.5 percent and grade to not greater than 6.0 percent.
- Mortality and surrender rates are based upon actual experience by geographical area modified to allow for variations in policy form. The weighted average lapse rate, including surrenders, for individual and group life approximated 7.4 percent.
- The portions of current and prior net income and of current unrealized appreciation of investments that can inure to the benefit of AIG are restricted in some cases by the insurance contracts and by the local insurance regulations of the countries in which the policies are in force.
- Participating life business represented approximately 19 percent of the gross insurance in force at December 31, 2006 and 34 percent of gross GAAP premiums in 2006. The amount of annual dividends to be paid is determined locally by the boards of directors. Provisions for future dividend payments are computed by jurisdiction, reflecting local regulations.

The liability for policyholders' contract deposits has been established based on the following assumptions:

- Interest rates credited on deferred annuities, which vary by territory and year of issuance, range from 1.2 percent to, including bonuses, 12.0 percent. Less than 1.0 percent of the liabilities are credited at a rate greater than 9.0 percent. Current declared interest rates are generally guaranteed to remain in effect for a period of one year though some are guaranteed for longer periods. Withdrawal charges generally range from zero percent to 20.0 percent grading to zero over a period of zero to 19 years.
- Domestically, guaranteed investment contracts (GICs) have market value withdrawal provisions for any funds withdrawn other than benefit responsive payments. Interest rates credited generally range from 2.6 percent to 9.0 percent. The vast majority of these GICs mature within five years. Overseas, interest rates credited on GICs generally range from 1.2 percent to 5.2 percent and maturities range from one to five years.
- Interest rates on corporate life insurance products are guaranteed at 4.0 percent and the weighted average rate credited in 2006 was 5.2 percent.
- The universal life funds have credited interest rates of 1.5 percent to 7.0 percent and guarantees ranging from 1.5 percent to 5.5 percent depending on the year of issue. Additionally, universal life funds are subject to surrender charges that amount to 12.2 percent of the aggregate fund balance grading to zero over a period not longer than 20 years.
- For variable products and investment contracts, policy values are expressed in terms of investment units. Each unit is linked to an asset portfolio. The value of a unit increases or decreases based on the value of the linked asset portfolio. The current liability at any time is the sum of the current unit value of all investment units plus any liability for guaranteed minimum death or withdrawal benefits. A portion of these liabilities are classified in the Spread-Based Investment Business for segment reporting purposes.

Certain products are subject to experience adjustments. These include group life and group medical products, credit life contracts, accident and health insurance contracts/riders attached to life policies and, to a limited extent, reinsurance agreements with other direct insurers. Ultimate premiums from these contracts are estimated and recognized as revenue, and the unearned portions of the premiums recorded as liabilities. Experience adjustments vary according to the type of contract and the territory in which the policy is in force and are subject to local regulatory guidance.

7. Statutory Financial Data

Statutory surplus and net income for General Insurance, Life Insurance & Retirement Services operations in accordance with regulatory accounting practices were as follows:

Years Ended December 31, *(in millions)*	2006	2005	2004
Statutory surplus[(a)]:			
General Insurance	**$32,665**	$24,508	$20,632
Life Insurance & Retirement Services	**35,058**	30,739	28,609
Statutory net income[(a)(b)]:			
General Insurance[(c)]	**8,010**	1,713	3,028
Life Insurance & Retirement Services[(a)]	**5,088**	4,762	4,474

(a) Statutory surplus and net income with respect to foreign operations are estimated as of November 30. The basis of presentation for branches of AIA is the Hong Kong statutory filing basis. The basis of presentation for branches of ALICO is the U.S. statutory filing basis. AIG Star Life, AIG Edison Life, Nan Shan and Philamlife are estimated based on their respective local country filing basis.

(b) Includes realized capital gains and losses and taxes.

(c) Includes catastrophe losses, net of tax, of $1.9 billion and $660 million in 2005 and 2004, respectively.

AIG's insurance subsidiaries file financial statements prepared in accordance with statutory accounting practices prescribed or permitted by domestic and foreign insurance regulatory authorities. The differences between statutory financial statements and financial statements prepared in accordance with U.S. GAAP vary between domestic and foreign by jurisdiction. The principal differences are that statutory financial statements do not reflect DAC, some bond portfolios may be carried at amortized cost, assets and liabilities are presented net of reinsurance, policyholder liabilities are valued using more conservative assumptions and certain assets are non-admitted.

Statutory capital of each company continued to exceed minimum company action level requirements following the adjustments, but AIG nonetheless contributed an additional $750 million of capital into American Home Assurance Company (American Home) effective September 30, 2005 and contributed a further $2.25 billion of capital in February 2006 for a total of approximately $3 billion of capital into Domestic General Insurance subsidiaries effective December 31, 2005.

8. Investment Information

Insurance Operations

(a) Statutory Deposits: Cash and securities with carrying values of $16.5 billion and $11.8 billion were deposited by AIG's insurance subsidiaries under requirements of regulatory authorities as of December 31, 2006 and 2005, respectively.

(b) Net Investment Income: An analysis of net investment income follows:

Years Ended December 31, *(in millions)*	2006	2005	2004
Fixed maturities	**$19,078**	$17,685	$15,884
Equity securities	**1,693**	1,730	621
Short-term investments	**719**	494	177
Interest on mortgage, policy and collateral loans	**1,253**	1,177	1,096
Other invested assets	**3,551**	1,905	1,444
Total investment income	**26,294**	22,991	19,222
Investment expenses	**1,002**	826	757
Net investment income	**$25,292**	$22,165	$18,465

8. Investment Information

Continued

(c) Realized Gains and Losses:

The realized capital gains (losses) and increase (decrease) in unrealized appreciation of AIG's consolidated available for sale investments were as follows:

Years Ended December 31, *(in millions)*	2006	2005	2004
Realized capital gains (losses):			
Fixed maturities*	$(1,069)	$ (108)	$ 178
Equity securities*	679	588	541
Other gains (losses)	496	(139)	(675)
Realized capital gains (losses)	$ 106	$ 341	$ 44
Increase (decrease) in unrealized appreciation of investments:			
Fixed maturities	$ (198)	$(4,656)	$1,436
Equity securities	432	850	445
Other investments	986	2,138	(283)
Capital Markets investments	1,354	(1,909)	270
Increase (decrease) in unrealized appreciation	$ 2,574	$(3,577)	$1,868

** Includes other-than-temporary impairments.*

Net unrealized gains included in the Consolidated Income Statement from investment securities classified as trading securities for 2006, 2005 and 2004 were $938 million, $1.1 billion and $269 million, respectively.

The gross realized gains and gross realized losses on AIG's consolidated available for sale securities were as follows:

	2006		2005		2004	
(in millions)	Gross Realized Gains	Gross Realized Losses	Gross Realized Gains	Gross Realized Losses	Gross Realized Gains	Gross Realized Losses
Fixed maturities	$ 711	$ 1,780	$1,586	$1,694	$1,560	$1,382
Equity securities	1,111	454	930	409	774	379
Preferred stocks	22	—	101	34	173	27
Total	$ 1,844	$ 2,234	$2,617	$2,137	$2,507	$1,788

(d) Fair Value of Investment Securities:

The amortized cost and estimated fair value of securities available for sale and held to maturity for the Insurance and Asset Management segments at December 31, 2006 and December 31, 2005 follows:

	December 31, 2006				December 31, 2005			
(in millions)	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
Available for sale:[a][b]								
U.S. government and government sponsored entities	$ 5,386	$ 106	$ 130	$ 5,362	$ 7,848	$ 124	$ 94	$ 7,878
States[b][c]	59,785	1,056	210	60,631	49,116	853	315	49,654
Foreign governments	62,153	5,428	436	67,145	57,509	4,881	665	61,725
Corporate debt	249,839	6,519	2,627	253,731	235,139	7,770	2,650	240,259
Total bonds	$377,163	$13,109	$3,403	$386,869	$349,612	$13,628	$3,724	$359,516
Equity securities	13,147	2,813	159	15,801	12,407	2,479	257	14,629
Total	$390,310	$15,922	$3,562	$402,670	$362,019	$16,107	$3,981	$374,145
Held to maturity:[a]								
Bonds — States[c]	$ 21,437	$ 731	$ 14	$ 22,154	$ 21,528	$ 552	$ 33	$ 22,047

(a) At December 31, 2006 and 2005, fixed maturities held by AIG that were below investment grade or not rated totaled $21.24 billion and $20.54 billion, respectively.

(b) In 2006, excludes hybrid financial instruments with an estimated fair value of $522 million at December 31, 2006.

(c) Including municipalities and political subdivisions.

8. Investment Information

Continued

The following table presents the amortized cost and estimated fair values of fixed maturity securities available for sale and held to maturity at December 31, 2006, by contractual maturity. Actual maturities may differ from contractual maturities because certain borrowers have the right to call or prepay certain obligations with or without call or prepayment penalties.

	Available for Sale		Held to Maturity	
(in millions)	Amortized Cost	Estimated Fair Value	Amortized Cost	Estimated Fair Value
Due in one year or less	$ 12,730	$ 12,925	$ 66	$ 68
Due after one year through five years	78,800	80,349	430	444
Due after five years through ten years	139,579	141,994	17,516	18,092
Due after ten years	146,054	151,601	3,425	3,550
Total available for sale*	$377,163	$386,869	$ 21,437	$ 22,154

* *Contractual maturities include mortgage backed securities with an amortized cost and estimated fair value of $48.2 billion and $48.1 billion, respectively. Such securities have been allocated to the contractual maturities based on estimated future cash flows.*

(e) Non-Income Producing Invested Assets: At December 31, 2006, non-income producing invested assets were insignificant.

(f) Gross Unrealized Losses and Estimated Fair Values on Investments:

The following table summarizes the gross unrealized losses and cost basis on securities available for sale, aggregated by major investment category and length of time that individual securities have been in a continuous unrealized loss position, at December 31, 2006 and 2005.

	Less than 12 Months		12 Months or More		Total	
(in millions)	Cost[a]	Unrealized Losses	Cost[a]	Unrealized Losses	Cost[a]	Unrealized Losses
2006						
Bonds[b]	**$ 60,591**	**$1,197**	**$82,252**	**$2,206**	**$142,843**	**$3,403**
Equity securities	**2,734**	**159**	**—**	**—**	**2,734**	**159**
Total	**$ 63,325**	**$1,356**	**$82,252**	**$2,206**	**$145,577**	**$3,562**
2005						
Bonds[b]	$121,631	$2,715	$21,160	$1,009	$142,791	$3,724
Equity securities	3,894	246	97	11	3,991	257
Total	$125,525	$2,961	$21,257	$1,020	$146,782	$3,981

(a) For bonds, represents amortized cost.

(b) Primarily relates to the corporate debt category.

8. Investment Information

Continued

As of December 31, 2006, AIG held 20,172 and 1,750 of individual bond and stock investments, respectively, that were in an unrealized loss position, of which 10,846 individual investments were in an unrealized loss position continuously for 12 months or more.

AIG recorded other-than-temporary impairment losses of approximately $944 million, $598 million and $684 million in realized capital gains (losses) in 2006, 2005 and 2004, respectively. See Note 1(e) herein for AIG's other-than-temporary impairment accounting policy.

(g) Other Invested Assets: Other invested assets as of December 31, 2006 were $42.1 billion, consisting primarily of hedge funds and limited partnerships. Approximately $5.3 billion relates to available for sale investments carried at fair value, with unrealized gains and losses recorded in a separate component of Other comprehensive income, net of deferred taxes, with almost all of the remaining investments being accounted for on the equity method of accounting. All of the investments are subject to impairment testing (see Note 1(e) herein). The gross unrealized loss on the investments accounted for as available for sale as of December 31, 2006 was $167 million, the majority of which represents investments that have been in a continuous unrealized loss position for less than 12 months.

Other invested assets at December 31, 2006, also includes approximately $1.8 billion of aircraft asset investments held by non-financial services subsidiaries.

(h) Investments in Life Settlement Contracts: In June 2006, AIG restructured its ownership of life settlement contracts with no effect on the economic substance of these investments. At the same time, AIG paid $610 million to its former co-investors to acquire all the remaining interests in life settlement contracts held in previously non-consolidated trusts. The life insurers for a small portion of these newly consolidated life settlement contracts include AIG subsidiaries. As a result, amounts related to life insurance issued by AIG subsidiaries are eliminated in consolidation.

At December 31, 2006, the carrying value of AIG's life settlement contracts was $1.1 billion, and is included in Other invested assets on the consolidated balance sheet. These investments are monitored for impairment on a contract by contract basis quarterly. During 2006, income recognized on life settlement contracts previously held in non-consolidated trusts was $38 million, and is included in net investment income on the consolidated statement of income. Further information regarding life settlement contracts as of December 31, 2006 is as follows:

(dollars in millions)

Remaining Life Expectancy of Insureds	Number of Contracts	Carrying Value	Face Value (Death Benefits)
0 – 1 year	4	$ 6	$ 8
1 – 2 years	23	10	15
2 – 3 years	61	58	88
3 – 4 years	123	108	188
4 – 5 years	135	79	170
Thereafter	1,453	829	3,197
Total	1,799	$1,090	$3,666

As of December 31, 2006, the anticipated life insurance premiums required to keep the life settlement contracts in force, payable in the ensuing twelve months ending December 31, 2007 and the four succeeding years ending December 31, 2011 are $77 million, $81 million, $85 million, $86 million, and $87 million, respectively.

Financial Services

(i) Economic Hedging of Securities Available for Sale: AIGFP follows a policy of minimizing interest rate, currency, commodity, and equity risks associated with securities available for sale by entering into internal offsetting positions, on a security by security basis within its derivatives portfolio, thereby offsetting a significant portion of the unrealized appreciation and depreciation. In addition, to reduce its credit risk, AIGFP has entered into credit derivative transactions with respect to $128 million of securities available for sale to economically hedge its credit risk. As previously discussed, these economic offsets did not meet the hedge accounting requirements of FAS 133 and, therefore, are recorded in Other income in the Consolidated Statement of Income.

8. Investment Information

Continued

(j) Fair Value of Fixed Maturities and Unrealized Appreciation of Investments — Capital Markets

The amortized cost and estimated fair value of Capital Markets securities available for sale at December 31, 2006 and 2005 were as follows:

	December 31, 2006				December 31, 2005			
(in millions)	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
Securities available for sale:								
Corporate and bank debt	**$40,194**	**$1,257**	**$265**	**$41,186**	$30,690	$386	$783	$30,293
Foreign governments	**706**	**33**	**1**	**738**	825	5	31	799
Asset-backed and collateralized	**2,731**	**170**	**6**	**2,895**	3,522	202	42	3,682
U.S. government and government sponsored entities	**2,281**	**115**	**10**	**2,386**	2,535	209	7	2,737
Total	**$45,912**	**$1,575**	**$282**	**$47,205**	$37,572	$802	$863	$37,511

The amortized cost and estimated fair values of Capital Markets securities available for sale at December 31, 2006, by contractual maturity, are shown below. Actual maturities may differ from contractual maturities because certain borrowers have the right to call or prepay certain obligations with or without call or prepayment penalties.

(in millions)	Amortized Cost	Estimated Fair Value
Securities available for sale:		
Due in one year or less	$ 1,235	$ 1,336
Due after one year through five years	7,509	7,746
Due after five years through ten years	10,570	11,023
Due after ten years	23,867	24,204
Asset-backed and collateralized	2,731	2,896
Total securities available for sale	$45,912	$47,205

The following table summarizes the gross unrealized losses and cost basis on Capital Markets securities available for sale, aggregated by length of time that individual securities have been in a continuous unrealized loss position, at December 31, 2006 and 2005.

	Less than 12 Months		12 Months or More		Total	
(in millions)	Cost	Gross Unrealized Losses	Cost	Gross Unrealized Losses	Cost	Gross Unrealized Losses
2006						
Securities available for sale	**$ 9,065**	**$ 60**	**$ 1,788**	**$222**	**$10,853**	**$282**
2005						
Securities available for sale	$15,676	$713	$ 1,280	$150	$16,956	$863

8. Investment Information

Continued

(k) Finance Receivables:

Finance receivables, net of unearned finance charges, were as follows:

Years Ended December 31, *(in millions)*	**2006**	2005
Real estate loans	**$20,321**	$20,407
Non-real estate loans	**4,506**	3,831
Retail sales finance	**3,092**	2,522
Credit card loans	**1,413**	1,498
Other loans	**978**	407
Total finance receivables	**30,310**	28,665
Allowance for losses	**(737)**	(670)
Finance receivables, net	**$29,573**	$27,995

9. Debt Outstanding

At December 31, 2006, AIG's net borrowings were $17.13 billion after reflecting amounts not guaranteed by AIG, amounts that were matched borrowings by AIG and AIGFP and liabilities connected to trust preferred stock. The following table summarizes borrowings outstanding at December 31, 2006 and 2005:

(in millions)	**2006**	2005
AIG's net borrowings	**$ 17,126**	$ 10,425
Liabilities connected to trust preferred stock	**1,440**	1,391
AIG Matched Investment Program matched notes and bonds payable	**5,468**	—
Series AIGFP matched notes and bonds payable	**72**	—
AIGFP:		
GIAs	**20,664**	20,811
Matched notes and bonds payable	**35,776**	24,950
Hybrid financial instrument liabilities[(a)]	**8,856**	—
Borrowings not guaranteed by AIG[(b)]	**59,277**	52,272
Total debt[(c)]	**$148,679**	$109,849

(a) Represents structured notes issued by AIGFP that are accounted for under the fair value option.

(b) Includes commercial paper not guaranteed by AIG.

(c) Total debt in 2006 includes commercial paper of $12.15 billion and $3.25 billion of debt related to VIEs required to be consolidated under the provisions of FIN 46R.

9. Debt Outstanding

Continued

Total debt at December 31, 2006 is shown below with year of payment due in each of the next five years and thereafter.

(in millions)	Total[(a)]	2007	2008	2009	2010	2011	Thereafter
AIG:							
Notes and bonds payable	$ 8,915	$ 165	$ 1,322	$ —	$ 498	$ 420	$ 6,510
Loans and mortgages payable	841	744	—	—	—	—	97
AIG Matched Investment Program matched notes and bonds payable	5,468	—	—	750	755	2,909	1,054
Series AIGFP matched notes and bonds payable	72	—	—	—	—	—	72
Total AIG[(a)]	15,296	909	1,322	750	1,253	3,329	7,733
AIGFP:							
GIAs	20,664	6,962	2,145	953	920	478	9,206
Notes and bonds payable	37,528	15,835	5,139	3,475	323	8,145	4,611
Hybrid financial instrument liabilities[(b)]	8,856	2,082	1,288	392	1,687	566	2,841
Total AIGFP	67,048	24,879	8,572	4,820	2,930	9,189	16,658
AGC Notes and bonds payable	797	—	—	—	499	—	298
Liabilities connected to trust preferred stock	1,440	—	—	—	—	—	1,440
ILFC[(c)]:							
Notes and bonds payable	22,773	3,347	3,865	3,145	3,465	3,488	5,463
Export credit facility[(d)]	2,659	482	482	430	317	227	721
Bank financings	1,159	75	25	471	103	160	325
Total ILFC	26,591	3,904	4,372	4,046	3,885	3,875	6,509
AGF Notes and bonds payable[(c)]	19,595	4,415	2,512	2,279	2,711	2,797	4,881
AIGCFG Loans and mortgages payable[(c)]	1,453	358	450	645	—	—	—
Other subsidiaries[(c)]	1,065	205	55	126	15	—	664
Total	$133,285	$34,670	$17,283	$12,666	$11,293	$19,190	$38,183

(a) Excludes $12.15 billion of commercial paper and $3.25 billion of debt related to VIEs required to be consolidated under the provisions of FIN 46R.

(b) Represents structured notes issued by AIGFP that are accounted for under the fair value option.

(c) AIG does not guarantee these borrowings.

(d) Reflects future minimum payment for ILFC's borrowing under the Export Credit Facility.

9. Debt Outstanding

Continued

At December 31, 2006, long-term borrowings were $98.68 billion and short-term borrowings were $34.6 billion, excluding $3.25 billion with respect to VIE debt required to be consolidated under the provisions of FIN 46R. Long-term borrowings exclude that portion of long-term debt maturing in less than one year.

(a) Commercial Paper:

At December 31, 2006, the commercial paper issued and outstanding was as follows:

(dollars in millions)	Net Book Value	Unamortized Discount and Accrued Interest	Face Amount	Weighted Average Interest Rate	Weighted Average Maturity in Days
ILFC	$ 2,747	$11	$ 2,758	5.30%	28
AGF	4,328	14	4,342	5.30	24
AIG Funding	4,821	18	4,839	5.28	28
AIGCC — Taiwan[(a)]	227	1	228	2.32	48
AIGF — Taiwan[(a)]	26	—	26	2.00	83
Total[(b)]	$12,149	$44	$12,193	—	—

(a) Issued in Taiwan N.T. dollars at prevailing local interest rates.

(b) Excludes $880 million of VIE commercial paper required to be consolidated under the provisions of FIN 46R.

At December 31, 2006, AIG did not guarantee the commercial paper of any of its subsidiaries other than AIG Funding.

(b) AIG Borrowings:

(i) Notes and bonds issued by AIG: In October 2006, AIG established a medium term note program under its shelf registration statement providing for the issuance of up to $25.1 billion of AIG debt securities. The proceeds from the issuance of these debt securities may be used (i) by AIG (ii) by AIGFP as it would use the proceeds from its own borrowings as discussed below or (iii) to fund the Matched Investment Program (MIP). As of December 31, 2006, $1.8 billion principal amount of notes were outstanding under the medium term note program, of which (i) $749 million was used for AIG's general corporate purposes, (ii) $72 million was used by AIGFP and (iii) $1.0 billion was used to fund the MIP. The maturity dates of these notes range from 2011 to 2046. To the extent deemed appropriate, AIG may enter into swap transactions to manage its effective borrowing rate with respect to these notes.

As of December 31, 2006, the equivalent of $5.7 billion of notes were outstanding under AIG's Euro medium term note program, of which the proceeds from $3.7 billion of notes were used to fund the MIP and the remainder was used for AIG's general corporate purposes. AIG has hedged the currency exposure arising from foreign currency denominated notes by economically hedging that exposure, although such hedges did not qualify for hedge accounting treatment under FAS 133.

In 2006, AIG issued in Rule 144A/Regulation S offerings $3 billion principal amount of senior notes, of which $1.0 billion was exchanged by AIG for substantially identical notes that are registered under the Securities Act of 1933 (Securities Act). The proceeds from the sale of $2.25 billion of these notes were used for AIG's general corporate purposes and $750 million were used to fund the MIP.

In November 2006, AIG filed a shelf registration statement in Japan, providing for the issuance of up to Japanese Yen 300 billion principal amount of senior notes in the aggregate. In December 2006, AIG issued the equivalent of $429 million under this shelf registration statement, the proceeds of which were used for AIG's general corporate purposes.

(ii) Notes and bonds issued by SunAmerica Inc. (SAI): As of December 31, 2006, notes and bonds originally issued by SAI aggregating $435 million (net of unamortized discount of $40 million) were outstanding with maturity dates from 2007 to 2097 at interest rates ranging from 5.60 percent to 9.95 percent.

(iii) Redemption of Zero Coupon Convertible Senior Debentures: On November 9, 2006, AIG redeemed all of its outstanding Zero Coupon Convertible Senior Debentures initially issued in 2001 for an aggregate redemption price of $1.07 billion.

(c) AIGFP Borrowings:

(i) Borrowings under Obligations of Guaranteed Investment Agreements: Borrowings under obligations of guaranteed investment agreements (GIAs), which are guaranteed by AIG, are recorded at the amount outstanding under each contract. Obligations may be called at various times prior to maturity at the option of the counterparty. Interest rates on these borrowings are primarily fixed, vary by maturity, and range up to 9.8 percent.

Funds received from GIA borrowings are invested in a diversified portfolio of securities and derivative transactions. At December 31, 2006, the fair value of securities pledged as collateral with respect to these obligations approximated $7.4 billion.

(ii) Notes and Bonds issued by AIGFP:

At December 31, 2006, AIGFP's notes and bonds outstanding, the proceeds of which are invested in a diversified portfolio of securities and derivative transactions, were as follows:

Range of Maturities *(dollars in millions)*	Currency	Range of Interest Rates	U.S. Dollar Carrying Value
2007-2046	U.S. dollar	0.18 - 8.60%	$ 34,788
2007-2011	United Kingdom pound	4.68 - 5.31	4,285
2007-2024	Euro	0.29 - 9.25	3,312
2008-2011	New Zealand dollar	6.30 - 8.35	1,395
2007-2036	Japanese Yen	0.01 - 7.00	1,533
2007-2015	Australian dollar	1.14 - 4.89	392
2007-2024	Swiss francs	0.25 - 1.38	600
2007-2015	Other	2.53 - 3.72	79
Total			$ 46,384

9. Debt Outstanding

Continued

AIGFP economically hedges its notes and bonds. AIG guarantees all of AIGFP's debt.

(iii) Hybrid financial instrument liabilities: AIGFP's notes and bonds include structured debt instruments whose payment terms are linked to one or more financial or other indices (such as an equity index or commodity index or another measure that is not considered to be clearly and closely related to the debt instrument). These notes contain embedded derivatives that otherwise would be required to be accounted for separately under FAS 133. Upon AIG's early adoption of FAS 155, AIGFP elected the fair value option for these notes. The notes that are accounted for using the fair value option are reported separately under hybrid financial instrument liabilities at fair value.

(d) AGC Borrowings: As of December 31, 2006, AGC notes aggregating $797 million were outstanding with maturity dates ranging from 2010 to 2029 at interest rates of up to 7.50 percent. AIG guarantees the notes and bonds of AGC.

(e) Liabilities Connected to Trust Preferred Stock: AGC issued Junior Subordinated Debentures (liabilities) to certain trusts established by AGC, which represent the sole assets of the trusts. The trusts have no independent operations. The trusts issued mandatory redeemable preferred stock to investors. The interest terms and payment dates of the liabilities correspond to those of the preferred stock. AGC's obligations with respect to the liabilities and related agreements, when taken together, constitute a full and unconditional guarantee by AGC of payments due on the preferred securities. AIG guarantees the obligations of AGC with respect to these liabilities and related agreements. The liabilities are redeemable, under certain conditions, at the option of AGC on a proportionate basis.

As of December 31, 2006, the preferred stock outstanding consisted of $300 million liquidation value of 8.5 percent preferred stock issued by American General Capital II in June 2000, $500 million liquidation value of 8.125 percent preferred stock issued by American General Institutional Capital B in March 1997, and $500 million liquidation value of 7.57 percent preferred stock issued by American General Institutional Capital A in December 1996.

(f) ILFC Borrowings:

(i) Notes and Bonds issued by ILFC: As of December 31, 2006, notes aggregating $22.8 billion were outstanding, consisting of $12.8 billion of term notes, $9.0 billion of medium-term notes with maturities ranging from 2007 to 2013 and interest rates ranging from 3.32 percent to 6.62 percent and $1.0 billion of junior subordinated debt as discussed below. Notes aggregating $5.1 billion are at floating interest rates and the remainder are at fixed rates. To the extent deemed appropriate, ILFC may enter into swap transactions to manage its effective borrowing rates with respect to these notes.

As a well-known seasoned issuer, ILFC has filed an automatic shelf registration statement with the Securities and Exchange Commission (SEC) allowing ILFC immediate access to the U.S. public debt markets. During 2006, $1.9 billion of debt securities were issued under this registration statement and $3.52 billion were issued under a prior registration statement. In addition, ILFC has a Euro medium term note program for $7.0 billion, under which $4.28 billion in notes were sold through December 31, 2006. The foreign exchange adjustment for the foreign currency denominated debt was $733 million at December 31, 2006 and $197 million at December 31, 2005. ILFC has substantially eliminated the currency exposure arising from foreign currency denominated notes by economically hedging the portion of the note exposure not already offset by Euro-denominated operating lease payments, although such hedges did not qualify for hedge accounting treatment under FAS 133.

In December 2005, ILFC issued two tranches of junior subordinated debt totaling $1.0 billion to underlie trust preferred securities issued by a trust sponsored by ILFC. Both tranches mature on December 21, 2065, but each tranche has a different call option. The $600 million tranche has a call date of December 21, 2010 and the $400 million tranche has a call date of December 21, 2015. The note with the 2010 call date has a fixed interest rate of 5.90 percent for the first five years. The note with the 2015 call date has a fixed interest rate of 6.25 percent for the first ten years. Both tranches have interest rate adjustments if the call option is not exercised. The new interest rate is a floating quarterly reset rate based on the initial credit spread plus the highest of (i) 3 month LIBOR, (ii) 10-year constant maturity treasury and (iii) 30-year constant maturity treasury.

(ii) Export credit facility: ILFC had a $4.3 billion Export Credit Facility (ECA) for use in connection with the purchase of approximately 75 aircraft delivered through 2001. This facility was guaranteed by various European Export Credit Agencies. The interest rate varies from 5.75 percent to 5.90 percent on these amortizing ten-year borrowings depending on the delivery date of the aircraft. At December 31, 2006, ILFC had $1.0 billion outstanding under this facility. The debt is collateralized by a pledge of the shares of a subsidiary of ILFC, which holds title to the aircraft financed under the facility.

In May 2004, ILFC entered into a similarly structured ECA for up to a maximum of $2.64 billion for Airbus aircraft to be delivered through May 31, 2005. The facility was subsequently increased to $3.64 billion and extended to include aircraft to be delivered through May 31, 2007. The facility becomes available as the various European Export Credit Agencies provide their guarantees for aircraft based on a six-month forward-looking calendar, and the interest rate is determined through a bid process. At December 31, 2006, ILFC had $1.7 billion outstanding under this facility.

(iii) Bank Financings: From time to time, ILFC enters into various bank financings. As of December 31, 2006, the total funded amount was $1.2 billion. The financings mature through 2012.

AIG does not guarantee any of the debt obligations of ILFC.

(g) AGF Borrowings: As of December 31, 2006, notes and bonds aggregating $19.59 billion were outstanding with maturity dates ranging from 2007 to 2031 at interest rates ranging from

9. Debt Outstanding

Continued

1.94 percent to 8.45 percent. To the extent deemed appropriate, AGF may enter into swap transactions to manage its effective borrowing rates with respect to these notes.

As a well-known seasoned issuer, AGF has filed an automatic shelf registration statement with the SEC allowing AGF immediate access to the U.S. public debt markets. At December 31, 2006, AGF had the corporate authority to issue up to $13.4 billion of debt securities registered under the Securities Act using AGF's effective shelf registration statements.

AGF uses the proceeds from the issuance of notes and bonds for the funding of its finance receivables. AIG does not guarantee any of the debt obligations of AGF.

(h) Other Notes, Bonds, Loans and Mortgages Payable at December 31, 2006, consisted of the following:

(in millions)	Uncollateralized Notes/Bonds/Loans Payable	Collateralized Loans and Mortgages Payable
AIGCFG	$1,453	$ —
AIG	841	—
Other subsidiaries	774	291
Total	$3,068	$291

(i) Revolving Credit Facilities of AIG, ILFC and AGF: AIG, ILFC and AGF maintain the following committed, unsecured revolving credit facilities in order to support their respective commercial paper programs and for general corporate purposes. AIG, ILFC and AGF each expects to replace or extend these credit facilities on or prior to their expiration. Some of the facilities, as noted below, contain a ''term-out option'' allowing for the conversion by the borrower of any outstanding loans at expiration into one-year term loans.

(in millions) Facility	Size	Borrower(s)	Available Amount December 31, 2006	Expiration	One-Year Term-Out Option
AIG:					
364-Day Syndicated Facility	$ 1,625	AIG AIG Funding[a] AIG Capital Corporation[a]	**$ 1,625**	July 2007	Yes
5-Year Syndicated Facility	1,625	AIG AIG Funding[a] AIG Capital Corporation[a]	**1,625**	July 2011	No
364-Day Bilateral Facility	3,200	AIG AIG Funding	**505**[b]	November 2007	Yes
364-Day Intercompany Facility[c]	2,000	AIG	**2,000**	October 2007	Yes
Total AIG	8,450		**5,755**		
ILFC:					
5-Year Syndicated Facility	2,500	ILFC	**2,500**	October 2011	No
5-Year Syndicated Facility	2,000	ILFC	**2,000**	October 2010	No
5-Year Syndicated Facility	2,000	ILFC	**2,000**	October 2009	No
Total ILFC	6,500		**6,500**		
AGF:					
364-Day Syndicated Facility	2,125	American General Finance Corporation American General Finance, Inc.[d]	**2,125**	July 2007	Yes
5-Year Syndicated Facility	2,125	American General Finance Corporation	**2,125**	July 2010	No
Total AGF	$ 4,250		**$ 4,250**		

(a) Guaranteed by AIG.

(b) This facility can be drawn in the form of loans or letters of credit. All drawn amounts shown above are in the form of letters of credit.

(c) Subsidiaries of AIG are the lenders on this facility.

(d) American General Finance, Inc. is an eligible borrower for up to $400 million only.

(j) Interest Expense for All Indebtedness: Total interest expense for all indebtedness, net of capitalized interest, aggregated $6.95 billion in 2006, $5.7 billion in 2005 and $4.4 billion in 2004. Capitalized interest was $59 million in 2006, $64 million in 2005 and $59 million in 2004. Cash distributions on the preferred shareholders' equity in subsidiary companies of ILFC and liabilities connected to trust preferred stock of AGC subsidiaries are accounted for as interest expense in the consolidated statement of income. The cash distributions for ILFC were approximately $5 million, $5 million and $4 million for the years ended December 31, 2006, 2005 and 2004, respectively. The cash distributions for AGC subsidiaries were approximately $107 million, $112 million and $123 million for the years ended December 31, 2006, 2005 and 2004, respectively.

10. Preferred Shareholders' Equity in Subsidiary Companies

As of December 31, 2006, preferred shareholders' equity in subsidiary companies represents preferred stocks issued by ILFC, a wholly owned subsidiary of AIG.

At December 31, 2006, the preferred stock consists of 1,000 shares of market auction preferred stock (MAPS) in two series (Series A and B) of 500 shares each. Each of the MAPS shares has a liquidation value of $100,000 per share and is not convertible. The dividend rate, other than the initial rate, for each dividend period for each series is reset approximately every seven weeks (49 days) on the basis of orders placed in an auction. During 2006, ILFC extended each of the MAPS dividend periods for three years. At December 31, 2006, the dividend rate for Series A MAPS was 4.70 percent and the dividend rate for Series B MAPS was 5.59 percent.

11. Shareholders' Equity and Earnings Per Share

Shareholders' Equity

AIG parent depends on its subsidiaries for cash flow in the form of loans, advances, reimbursement for shared expenses, and dividends. AIG's insurance subsidiaries are subject to regulatory restrictions on the amount of dividends which can be remitted to AIG parent. These restrictions vary by state. For example, unless permitted by the New York Superintendent of Insurance, general insurance companies domiciled in New York may not pay dividends to shareholders which in any twelve month period exceed the lesser of ten percent of the company's statutory policyholders' surplus or 100 percent of its ''adjusted net investment income,'' as defined. Generally, less severe restrictions applicable to both General and Life Insurance companies exist in most of the other states in which AIG's insurance subsidiaries are domiciled. Certain foreign jurisdictions have restrictions which could delay or limit the remittance of dividends. There are also various local restrictions limiting cash loans and advances to AIG by its subsidiaries. Largely as a result of the restrictions, approximately 90 percent of consolidated shareholders' equity was restricted from immediate transfer to AIG parent at December 31, 2006.

At December 31, 2006, there were 6,000,000 shares of AIG's $5 par value serial preferred stock authorized, issuable in series, none of which were outstanding.

11. Shareholders' Equity and Earnings Per Share

Continued

Earnings Per Share

Basic earnings per share are based on the weighted average number of common shares outstanding, retroactively adjusted to reflect all stock dividends and stock splits. Diluted earnings per share are based on those shares used in basic earnings per share plus shares that would have been outstanding assuming issuance of common shares for all dilutive potential common shares outstanding, retroactively adjusted to reflect all stock dividends and stock splits.

The computation of earnings per share for December 31, 2006, 2005 and 2004 was as follows:

Years Ended December 31, *(in millions, except per share data)*	**2006**	2005	2004
Numerator for earnings per share:			
Income before cumulative effect of accounting changes	**$14,014**	$10,477	$9,983
Cumulative effect of accounting changes, net of tax	**34**	—	(144)
Net income applicable to common stock for basic EPS	**$14,048**	$10,477	$9,839
Interest on contingently convertible bonds, net of tax[(a)]	**10**	11	11
Net income applicable to common stock for diluted EPS	**$14,058**	$10,488	$9,850
Cumulative effect of accounting changes, net of tax	**(34)**	—	144
Income before cumulative effect of accounting changes applicable to common stock for diluted EPS	**$14,024**	$10,488	$9,994
Denominator for earnings per share:			
Weighted-average shares outstanding used in the computation of EPS:			
Common stock issued	**2,751**	2,751	2,751
Common stock in treasury	**(153)**	(155)	(146)
Deferred shares	**10**	1	1
Weighted-average shares outstanding — basic	**2,608**	2,597	2,606
Incremental shares from potential common stock:			
Weighted-average number of shares arising from outstanding employee stock plans (treasury stock method)[(b)]	**7**	21	22
Contingently convertible bonds[(a)]	**8**	9	9
Weighted-adjusted average shares outstanding — diluted[(b)]	**2,623**	2,627	2,637
Earnings per share:			
Basic:			
Income before cumulative effect of accounting changes	**$ 5.38**	$ 4.03	$ 3.83
Cumulative effect of accounting changes, net of tax	**0.01**	—	(0.06)
Net income	**$ 5.39**	$ 4.03	$ 3.77
Diluted:			
Income before cumulative effect of accounting changes	**$ 5.35**	$ 3.99	$ 3.79
Cumulative effect of accounting changes, net of tax	**0.01**	—	(0.06)
Net income	**$ 5.36**	$ 3.99	$ 3.73

(a) Assumes conversion of contingently convertible bonds due to the adoption of EITF Issue No. 04-8 ''Accounting Issues Related to Certain Features of Contingently Convertible Debt and the Effect on Diluted Earnings per Share.''

(b) Certain shares arising from employee stock plans were not included in the computation of diluted earnings per share where the exercise price of the options exceeded the average market price and would have been antidilutive. The number of shares excluded were 13 million, 19 million and 7 million for 2006, 2005 and 2004, respectively.

12. Commitments, Contingencies and Guarantees

In the normal course of business, various commitments and contingent liabilities are entered into by AIG and certain of its subsidiaries. In addition, AIG guarantees various obligations of certain subsidiaries.

(a) Litigation and Investigations

Litigation Arising from Operations. AIG and its subsidiaries, in common with the insurance and financial services industries in general, are subject to litigation, including claims for punitive damages, in the normal course of their business. In AIG's insurance operations, litigation arising from claims settlement activities is generally considered in the establishment of AIG's reserve for losses and loss expenses. However, in certain circumstances, AIG provides disclosure because of the size or nature of the potential liability to AIG. The potential for increasing jury awards and settlements makes it difficult to assess the ultimate outcome of such litigation.

12. Commitments, Contingencies and Guarantees

Continued

Litigation Arising from Insurance Operations — Caremark. AIG and certain of its subsidiaries have been named defendants in two putative class actions in state court in Alabama that arise out of the 1999 settlement of class and derivative litigation involving Caremark Rx, Inc. (Caremark). An excess policy issued by a subsidiary of AIG with respect to the 1999 litigation was expressly stated to be without limit of liability. In the current actions, plaintiffs allege that the judge approving the 1999 settlement was misled as to the extent of available insurance coverage and would not have approved the settlement had he known of the existence and/or unlimited nature of the excess policy. They further allege that AIG, its subsidiaries, and Caremark are liable for fraud and suppression for misrepresenting and/or concealing the nature and extent of coverage. In their complaint, plaintiffs request compensatory damages for the 1999 class in the amount of $3.2 billion, plus punitive damages. AIG and its subsidiaries deny the allegations of fraud and suppression and have asserted, *inter alia,* that information concerning the excess policy was publicly disclosed months prior to the approval of the settlement. AIG and its subsidiaries further assert that the current claims are barred by the statute of limitations and that plaintiffs' assertions that the statute was tolled cannot stand against the public disclosure of the excess coverage. Plaintiffs, in turn, have asserted that the disclosure was insufficient to inform them of the nature of the coverage and did not start the running of the statute of limitations. The trial court is currently considering, under standards mandated by the Alabama Supreme Court, whether a class action can be certified. AIG cannot reasonably estimate either the likelihood of its prevailing in these actions or the potential damages in the event liability is determined.

Litigation Arising from Insurance Operations — Gunderson. A subsidiary of AIG has been named as a defendant in a putative class action lawsuit in the 14th Judicial District Court for the State of Louisiana. The *Gunderson* complaint alleges failure to comply with certain provisions of the Louisiana Any Willing Provider Act (the Act) relating to discounts taken by defendants on bills submitted by Louisiana medical providers and hospitals that provided treatment or services to workers compensation claimants and seeks monetary penalties and injunctive relief. On July 20, 2006, the court denied defendants' motion for summary judgment and granted plaintiffs' partial motion for summary judgment, holding that the AIG subsidiary was a ''group purchaser'' and, therefore, potentially subject to liability under the Act. On November 28, 2006, the court issued an order certifying a class of providers and hospitals. In an unrelated action also arising under the Act, a Louisiana appellate court ruled that the district court lacked jurisdiction to adjudicate the claims at issue. In response, defendants in *Gunderson* filed an exception for lack of subject matter jurisdiction. On January 19, 2007, the court denied the motion, holding that it has jurisdiction over the putative class claims. The AIG subsidiary is appealing the class certification ruling and intends to seek an appeal from the jurisdictional ruling. While AIG believes that it has meritorious defenses to plaintiffs' claims, it cannot currently estimate the likelihood of prevailing in this action or reasonably estimate the likely damages, if any.

2006 Regulatory Settlements. In February 2006, AIG reached a resolution of claims and matters under investigation with the United States Department of Justice (DOJ), SEC, the Office of the New York Attorney General (NYAG) and the New York State Department of Insurance (DOI). AIG recorded an after-tax charge of $1.15 billion relating to these settlements in the fourth quarter of 2005.

The settlements resolved investigations conducted by the SEC, NYAG and DOI in connection with the accounting, financial reporting and insurance brokerage practices of AIG and its subsidiaries, as well as claims relating to the underpayment of certain workers compensation premium taxes and other assessments. These settlements did not, however, resolve investigations by regulators from other states into insurance brokerage practices related to contingent commissions and other broker-related conduct, such as alleged bid rigging. Nor did the settlements resolve any obligations that AIG may have to state guarantee funds in connection with any of these matters.

As a result of these settlements, AIG made payments or placed amounts in escrow in 2006 totaling approximately $1.64 billion, $225 million of which represented fines and penalties. Amounts held in escrow totaling $699 million, including interest thereon, are included in other assets at December 31, 2006. At that date, approximately $314 million of the funds were escrowed for settlement of claims resulting from the underpayment by AIG of its residual market assessments for workers compensation. The National Workers Compensation Reinsurance Pool on behalf of its participant members and various states have communicated to AIG that they may assert claims with respect to the underpayment of such assessments. AIG cannot currently estimate whether the amount ultimately required to settle these claims will exceed the funds escrowed for this purpose.

The remaining escrowed funds, which amounted to $385 at December 31, 2006, are set aside for settlements with certain AIG policyholders specified in the settlements who claimed to have been harmed by AIG's insurance brokerage practices. Any funds remaining at the end of the escrow period will be used to resolve claims asserted by policyholders relating to such insurance brokerage practices, including those described in Private Litigation below.

In addition to the escrowed funds, the $800 million was deposited into a fund under the supervision of the SEC as part of the settlements to be available to resolve claims asserted against AIG by investors including, the shareholder lawsuits described herein.

At the current time, AIG cannot predict the outcome of the matters described above, or estimate any potential additional cost related to these matters.

Also, as part of the settlements, AIG has agreed to retain, for a period of three years, an independent consultant who will conduct a review that will include, among other things, the adequacy of AIG's internal control over financial reporting, the policies, procedures and effectiveness of AIG's regulatory, compli-

12. Commitments, Contingencies and Guarantees

Continued

ance and legal functions and the remediation plan that AIG has implemented as a result of its own internal review.

Private Litigation

Securities Actions. Beginning in October 2004, a number of putative securities fraud class action suits were filed against AIG and consolidated as *In re American International Group, Inc. Securities Litigation.* Subsequently, a separate, though similar, securities fraud action was also brought against AIG by certain Florida pension funds. The lead plaintiff in the class action is a group of public retirement systems and pension funds benefiting Ohio state employees, suing on behalf of themselves and all purchasers of AIG's publicly traded securities between October 28, 1999 and April 1, 2005. The named defendants are AIG and a number of present and former AIG officers and directors, as well as Starr, SICO, General Reinsurance Corporation, and PricewaterhouseCoopers LLP (PwC), among others. The lead plaintiff alleges, among other things, that AIG: (1) concealed that it engaged in anti-competitive conduct through alleged payment of contingent commissions to brokers and participation in illegal bid-rigging; (2) concealed that it used ''income smoothing'' products and other techniques to inflate its earnings; (3) concealed that it marketed and sold ''income smoothing'' insurance products to other companies; and (4) misled investors about the scope of government investigations. In addition, the lead plaintiff alleges that AIG's former Chief Executive Officer manipulated AIG's stock price. The lead plaintiff asserts claims for violations of Sections 11 and 15 of the Securities Act, Section 10(b) of the Exchange Act, and Rule 10b-5 promulgated thereunder, Section 20(a) of the Exchange Act, and Section 20A of the Exchange Act. In April 2006, the court denied the defendants' motions to dismiss the second amended class action complaint and the Florida complaint. In December 2006, a third amended class action complaint was filed, which does not differ substantially from the prior complaint. Fact and class discovery is currently ongoing.

ERISA Action. Between November 30, 2004 and July 1, 2005, several ERISA actions were filed on behalf of purported class of participants and beneficiaries of three pension plans sponsored by AIG or its subsidiaries. A consolidated complaint filed on September 26, 2005 alleges a class period between September 30, 2000 and May 31, 2005 and names as defendants AIG, the members of AIG's Retirement Board and the Administrative Boards of the plans at issue, and four present or former members of AIG's Board of Directors. The factual allegations in the complaint are essentially identical to those in the securities actions described above. Plaintiffs allege that defendants violated duties under ERISA by allowing the plans to offer AIG stock as a permitted investment, when defendants allegedly knew it was not a prudent investment, and by failing to provide participants with accurate information about AIG stock. AIG's motion to dismiss was denied by order dated December 12, 2006. Discovery will be consolidated with proceedings in the securities actions.

Derivative Actions — Southern District of New York. Between October 25, 2004 and July 14, 2005, seven separate derivative actions were filed in the Southern District of New York, five of which were consolidated into a single action. The New York derivative complaint contains nearly the same types of allegations made in the securities fraud and ERISA actions described above. The named defendants include current and former officers and directors of AIG, as well as Marsh & McLennan Companies, Inc. (Marsh), SICO, Starr, ACE Limited and subsidiaries (ACE), General Reinsurance Corporation, PwC, and certain employees or officers of these entity defendants. Plaintiffs assert claims for breach of fiduciary duty, gross mismanagement, waste of corporate assets, unjust enrichment, insider selling, auditor breach of contract, auditor professional negligence and disgorgement from AIG's former Chief Executive Officer and Chief Financial Officer of incentive-based compensation and AIG share proceeds under Section 304 of the Sarbanes-Oxley Act, among others. Plaintiffs seek, among other things, compensatory damages, corporate governance reforms, and a voiding of the election of certain AIG directors. AIG's Board of Directors has appointed a special committee of independent directors (special committee) to review the matters asserted in the operative consolidated derivative complaint. The court has approved agreements staying the derivative case pending in the Southern District of New York while the special committee performs its work. The current stay extends until March 14, 2007.

Derivative Actions — Delaware Chancery Court. From October 2004 to April 2005, AIG shareholders filed five derivative complaints in the Delaware Chancery Court. All of these derivative lawsuits have been consolidated into a single action. The amended consolidated complaint names 43 defendants (not including nominal defendant AIG) who, like the New York consolidated derivative litigation, are current and former officers and directors of AIG, as well as other entities and certain of their current and former employees and directors. The factual allegations, legal claims and relief sought in Delaware action are similar to those alleged in the New York derivative actions, except that plaintiffs in the Delaware derivative action assert claims only under state law. The court has approved agreements staying the derivative case pending in the Delaware Chancery Court while the special committee performs its work. The current stay extends until March 14, 2007.

An additional derivative lawsuit was filed in the Delaware Chancery Court in December 2002 against twenty directors and executives of AIG as well as against AIG as a nominal defendant, alleges, among other things, that the directors of AIG breached the fiduciary duties of loyalty and care by approving the payment of commissions to Starr and of rental and service fees to SICO and the executives breached their duty of loyalty by causing AIG to enter into contracts with Starr and SICO and their fiduciary duties by usurping AIG's corporate opportunity. The complaint further alleges that the Starr agencies did not provide any services that AIG was not capable of providing itself, and that the diversion of commissions to these entities was solely for the benefit of Starr's owners. The complaint also alleged that the service fees and rental payments made to SICO and its subsidiaries were improper.

12. Commitments, Contingencies and Guarantees

Continued

Under the terms of a stipulation approved by the Court on February 16, 2006, the claims against the outside independent directors were dismissed with prejudice, while the claims against the other directors were dismissed without prejudice. On October 31, 2005, Messrs. Greenberg, Matthews and Smith, SICO and Starr filed motions to dismiss the amended complaint. In an opinion dated June 21, 2006, the Court denied defendants' motion to dismiss, except with respect to plaintiff's challenge to payments made to Starr before January 1, 2000. On July 21, 2006, plaintiff filed its second amended complaint, which alleges that, between January 1, 2000 and May 31, 2005, individual defendants breached their duty of loyalty by causing AIG to enter into contracts with Starr and SICO and breached their fiduciary duties by usurping AIG's corporate opportunity. Starr is charged with aiding and abetting breaches of fiduciary duty and unjust enrichment for its acceptance of the fees. SICO is no longer named as a defendant. Discovery is currently ongoing.

Policyholder Actions. After the NYAG filed its complaint against insurance broker Marsh, policyholders brought multiple federal antitrust and Racketeer Influenced and Corrupt Organizations Act (RICO) class actions in jurisdictions across the nation against insurers and brokers, including AIG and a number of its subsidiaries, alleging that the insurers and brokers engaged in a broad conspiracy to allocate customers, steer business, and rig bids. These actions, including 18 complaints filed in different federal courts naming AIG or an AIG subsidiary as a defendant, were consolidated by the judicial panel on multi-district litigation and transferred to the United States District Court for the District of New Jersey for coordinated pretrial proceedings. The consolidated actions have proceeded in that court in two parallel actions, *In re Insurance Brokerage Antitrust Litigation* (the *Commercial Complaint*) and *In re Employee Benefit Insurance Brokerage Antitrust Litigation* (the *Employee Benefits Complaint*, and together with the *Commercial Complaint,* the multi-district litigation).

The plaintiffs in the *Commercial Complaint* are nineteen corporations, individuals and public entities that contracted with the broker defendants for the provision of insurance brokerage services for a variety of insurance needs. The broker defendants are alleged to have placed insurance coverage on the plaintiffs' behalf with a number of insurance companies named as defendants, including AIG subsidiaries. The *Commercial Complaint* also named ten brokers and fourteen other insurers (one of which has since settled) as defendants. The *Commercial Complaint* alleges that defendants engaged in a widespread conspiracy to allocate customers through ''bid-rigging'' and ''steering'' practices. The *Commercial Complaint* also alleges that the insurer defendants permitted brokers to place business with AIG subsidiaries through wholesale intermediaries affiliated with or owned by those same brokers rather than placing the business with AIG subsidiaries directly. Finally, the *Commercial Complaint* alleges that the insurer defendants entered into agreements with broker defendants that tied insurance placements to reinsurance placements in order to provide additional compensation to each broker. Plaintiffs assert that the defendants violated the Sherman Antitrust Act, RICO, the antitrust laws of 48 states and the District of Columbia, and are liable under common law breach of fiduciary duty and unjust enrichment theories. Plaintiffs seek treble damages plus interest and attorneys' fees as a result of the alleged RICO and Sherman Act violations.

The plaintiffs in the *Employee Benefits Complaint* are nine individual employees and corporate and municipal employers alleging claims on behalf of two separate nationwide purported classes: an employee class and an employer class that acquired insurance products from the defendants from August 26, 1994 to the date of any class certification. The *Employee Benefits Complaint* names AIG, as well as eleven brokers and five other insurers, as defendants. The activities alleged in the *Employee Benefits Complaint,* with certain exceptions, track the allegations of contingent commissions, bid-rigging and tying made in the *Commercial Complaint.*

On October 3, 2006, Judge Hochberg of the District of New Jersey reserved in part and denied in part motions filed by the insurer defendants and broker defendants to dismiss the multi-district litigation. The Court also ordered the plaintiffs in both actions to file supplemental statements of particularity to elaborate on the allegations in their complaints. Plaintiffs filed their supplemental statements on October 25, 2006, and the AIG defendants, along with other insurer and broker defendants in the two consolidated actions, filed renewed motions to dismiss on November 30, 2006. Briefing has been completed on the renewed motions to dismiss, as well as plaintiffs' motion for class certification in both cases. On February 16, 2007, Chief Judge Brown of the District of New Jersey transferred the multi-district litigation to himself. Oral argument on the renewed motions to dismiss has been scheduled before Chief Judge Brown on March 1, 2007. Fact discovery in the multi-district litigation proceeding is ongoing.

A number of complaints making allegations similar to those in the *Commercial Complaint* have been filed against AIG and other defendants in state and federal courts around the country. The defendants have thus far been successful in having the federal actions transferred to the District of New Jersey and consolidated into the multi-district litigation. The AIG defendants have also sought to have state court actions making similar allegations stayed pending resolution of the multi-district litigation proceeding. In one state court action pending in Florida, the trial court recently decided not to grant an additional stay, but instead to allow the case to proceed.

Litigation Relating to 21st Century. Shortly after the announcement in late January 2007 of AIG's offer to acquire the outstanding shares of 21st Century not already owned by AIG and its subsidiaries, two related class actions were filed in the Superior Court of California, Los Angeles County, against AIG, 21st Century, and the individual members of 21st Century's Board of Directors, two of whom are current executive officers of AIG. The actions were filed purportedly on behalf of the minority shareholders of 21st Century and assert breaches of fiduciary duty in connection with the AIG proposal. The complaints allege that the proposed per share price is unfair and seek preliminary

12. Commitments, Contingencies and Guarantees

Continued

and permanent injunctive relief to enjoin the consummation of the proposed transaction.

SICO. In July, 2005, SICO filed a complaint against AIG in the Southern District of New York, claiming that AIG had refused to provide SICO access to certain artwork and asked the court to order AIG immediately to release the property to SICO. AIG filed an answer denying SICO's allegations and setting forth defenses to SICO's claims. In addition, AIG filed counterclaims asserting breach of contract, unjust enrichment, conversion, breach of fiduciary duty, a constructive trust and declaratory judgment, relating to SICO's breach of its commitment to use its AIG shares only for the benefit of AIG and AIG employees. Fact and expert discovery has been substantially concluded and briefing on SICO's motion for summary judgment is underway.

Regulatory Investigations. Regulators from several states have commenced investigations into insurance brokerage practices related to contingent commissions and other industry-wide practices as well as other broker-related conduct, such as alleged bid-rigging. In addition, various federal and state regulatory agencies are reviewing certain transactions and practices of AIG and its subsidiaries in connection with industry-wide and other inquiries. AIG has cooperated, and will continue to cooperate, in producing documents and other information in response to subpoenas and other requests.

Wells Notices. AIG understands that some of its employees have received Wells notices in connection with previously disclosed SEC investigations of certain of AIG's transactions or accounting practices. Under SEC procedures, a Wells notice is an indication that the SEC staff has made a preliminary decision to recommend enforcement action that provides recipients with an opportunity to respond to the SEC staff before a formal recommendation is finalized. It is possible that additional current and former employees could receive similar notices in the future as the regulatory investigations proceed.

Effect on AIG

In the opinion of AIG management, AIG's ultimate liability for the unresolved litigation and investigation matters referred to above is not likely to have a material adverse effect on AIG's consolidated financial condition, although it is possible that the effect would be material to AIG's consolidated results of operations for an individual reporting period.

(b) Commitments

Flight Equipment

At December 31, 2006, ILFC had committed to purchase 254 new aircraft deliverable from 2007 through 2015 at an estimated aggregate purchase price of $19.0 billion. ILFC will be required to find customers for any aircraft acquired, and it must arrange financing for portions of the purchase price of such equipment.

Minimum future rental income on noncancelable operating leases of flight equipment which have been delivered at December 31, 2006 was as follows:

(in millions)	
2007	$ 3,663
2008	3,220
2009	2,682
2010	2,271
2011	1,800
Remaining years after 2011	4,011
Total	$17,647

Flight equipment is leased, under operating leases, with remaining terms ranging from 1 to 13 years.

Lease Commitments

AIG and its subsidiaries occupy leased space in many locations under various long-term leases and have entered into various leases covering the long-term use of data processing equipment.

At December 31, 2006, the future minimum lease payments under operating leases were as follows:

(in millions)	
2007	$ 626
2008	461
2009	341
2010	274
2011	307
Remaining years after 2011	754
Total	$2,763

Rent expense approximated $657 million, $597 million, and $568 million for the years ended December 31, 2006, 2005, and 2004, respectively.

Other Commitments

On June 27, 2005, AIG entered into an agreement pursuant to which AIG agrees, subject to certain conditions, to make any payment that is not promptly paid with respect to the benefits accrued by certain employees of AIG and its subsidiaries under the SICO Plans (as discussed in Note 16 herein).

(c) Contingencies

Loss Reserves

Although AIG regularly reviews the adequacy of the established reserve for losses and loss expenses, there can be no assurance that AIG's ultimate loss reserves will not develop adversely and materially exceed AIG's current loss reserves. Estimation of ultimate net losses, loss expenses and loss reserves is a complex process for long-tail casualty lines of business, which include excess and umbrella liability, directors and officers liability (D&O), professional liability, medical malpractice, workers compensation, general liability, products liability and related classes, as well as for asbestos and environmental exposures. Generally, actual historical loss development factors are used to project

12. Commitments, Contingencies and Guarantees

Continued

future loss development. However, there can be no assurance that future loss development patterns will be the same as in the past. Moreover, any deviation in loss cost trends or in loss development factors might not be discernible for an extended period of time subsequent to the recording of the initial loss reserve estimates for any accident year. Thus, there is the potential for reserves with respect to a number of years to be significantly affected by changes in loss cost trends or loss development factors that were relied upon in setting the reserves. These changes in loss cost trends or loss development factors could be attributable to changes in inflation, in labor and material costs or in the judicial environment, or in other social or economic phenomena affecting claims.

Superior National. On December 30, 2004, an arbitration panel issued its ruling in connection with a 1998 workers compensation quota share reinsurance agreement under which Superior National Insurance Company, among others, was reinsured by USLIFE, a subsidiary of AGC. In its 2-1 ruling, the arbitration panel refused to rescind the contract as requested by USLIFE. Instead, the panel reformed the contract to reduce USLIFE's participation by ten percent. Further, the arbitration ruling established a second phase of arbitration for USLIFE to present its challenges to certain cessions to the contract. The second phase has now been completed, and the arbitration panel has issued two awards resolving the issues presented in phase two in favor of the cedents. USLIFE has filed a petition to vacate all of the arbitration awards from both phases of the arbitration in California federal court. In addition, USLIFE is pursuing certain insurance recoverables in connection with the contract. As a result of the ruling AIG increased its reserves by $125 million in the fourth quarter to $478 million. AIG believes that the reserves should be adequate to fund unpaid claims.

Synthetic Fuel Tax Credits. AIG generates income tax credits as a result of investing in synthetic fuel production. Tax credits generated from the production and sale of synthetic fuel under the Internal Revenue Code are subject to an annual phase-out provision that is based on the average wellhead price of domestic crude oil. The price range within which the tax credits are phased-out was originally established in 1980 and is adjusted annually for inflation. Depending on the price of domestic crude oil for a particular year, all or a portion of the tax credits generated in that year might be eliminated. AIG evaluates the production levels of its synthetic fuel production facilities in light of the risk of phase-out of the associated tax credits. As a result of fluctuating domestic crude oil prices, AIG evaluates and adjusts production levels when appropriate in light of this risk. Regardless of oil prices, the tax credits expire after 2007.

(d) Guarantees

AIG and certain of its subsidiaries become parties to derivative financial instruments with market risk resulting from both dealer and end-user activities and to reduce currency, interest rate, equity and commodity exposures. These instruments are carried at their estimated fair values in the consolidated balance sheet. The vast majority of AIG's derivative activity is transacted by AIGFP. See also Note 19 herein.

AIG has issued unconditional guarantees with respect to the prompt payment, when due, of all present and future payment obligations and liabilities of AIGFP arising from transactions entered into by AIGFP.

SAI Deferred Compensation Holdings, Inc., a wholly owned subsidiary of AIG, has established a deferred compensation plan for registered representatives of certain AIG subsidiaries, pursuant to which participants have the opportunity to invest deferred commissions and fees on a notional basis. The value of the deferred compensation fluctuates with the value of the deferred investment alternatives chosen. AIG has provided a full and unconditional guarantee of the obligations of SAI Deferred Compensation Holdings, Inc. to pay the deferred compensation under the plan.

13. Fair Value of Financial Instruments

Statement of Financial Accounting Standards No. 107, ''Disclosures about Fair Value of Financial Instruments'' (FAS 107), requires disclosure of fair value information about financial instruments, as defined therein, for which it is practicable to estimate such fair value. In the measurement of the fair value of certain financial instruments, where quoted market prices are not available, other valuation techniques are utilized. These fair value estimates are derived using internally developed valuation methodologies based on available and observable market information. FAS 107 excludes certain financial instruments, including those related to insurance contracts and lease contracts.

The following methods and assumptions were used by AIG in estimating the fair value of the financial instruments presented:

Cash and short-term investments: The carrying amounts approximate fair values.

Fixed maturity securities: Fair values were generally based upon quoted market prices. For certain fixed maturity securities for which market prices were not readily available, fair values were estimated using values obtained from independent pricing services.

Equity securities: Fair values were based on quoted market prices. Where market prices were not readily available, fair values were estimated using quoted market prices of comparable investments.

Mortgage loans on real estate, policy and collateral loans: Where practical, the fair values of loans on real estate and collateral loans were estimated using discounted cash flow calculations based upon AIG's current incremental lending rates for similar type loans. The fair values of the policy loans were not calculated as AIG believes it would have to expend excessive costs for the benefits derived.

Trading assets and trading liabilities: Fair values approximate the carrying values.

13. Fair Value of Financial Instruments

Continued

Finance receivables: Fair values were estimated using discounted cash flow calculations based upon the weighted average rates currently being offered for similar finance receivables.

Securities lending collateral and securities lending payable: The contract values of these financial instruments approximate fair value.

Spot commodities: Fair values are based on current market prices.

Unrealized gains and losses on swaps, options and forward transactions: Fair values were based on the use of valuation models that utilize, among other things, current interest, foreign exchange commodity, equity and volatility rates, as applicable.

Securities purchased (sold) under agreements to resell (repurchase), at contract value: As these securities (obligations) are short-term in nature, the contract values approximate fair values.

Other invested assets: Consisting principally of hedge funds and limited partnerships. Fair values are determined based on the net asset values provided by the general partner or manager of each investment.

Policyholders' contract deposits: Fair values were estimated using discounted cash flow calculations based upon interest rates currently being offered for similar contracts with maturities consistent with those remaining for the contracts being valued.

GIAs: Fair values of AIG's obligations under investment type agreements were estimated using discounted cash flow calculations based on interest rates currently being offered for similar agreements with maturities consistent with those remaining for the agreements being valued.

Securities and spot commodities sold but not yet purchased: The carrying amounts for the securities and spot commodities sold but not yet purchased approximate fair values. Fair values for spot commodities sold short were based on current market prices.

Trust deposits and deposits due to banks and other depositors: To the extent certain amounts are not demand deposits or certificates of deposit which mature in more than one year, fair values were not calculated as AIG believes it would have to expend excessive costs for the benefits derived.

Commercial paper: The carrying amount approximates fair value.

Notes, bonds, loans and mortgages: Where practical, the fair values of these obligations were estimated using discounted cash flow calculations based upon AIG's current incremental borrowing rates for similar types of borrowings with maturities consistent with those remaining for the debt being valued.

13. Fair Value of Financial Instruments

Continued

The carrying values and fair values of AIG's financial instruments at December 31, 2006 and 2005 were as follows:

(in millions)	2006 Carrying Value[a]	2006 Fair Value	2005 Carrying Value[a]	2005 Fair Value
Assets:				
Fixed maturities	**$417,865**	**$418,582**	$385,680	$386,199
Equity securities	**30,222**	**30,222**	23,588	23,588
Mortgage loans on real estate, policy and collateral loans	**28,418**	**28,655**	24,909	26,352
Securities available for sale	**47,205**	**47,205**	37,511	37,511
Trading securities	**5,031**	**5,031**	6,499	6,499
Spot commodities	**220**	**220**	92	96
Unrealized gain on swaps, options and forward transactions	**19,252**	**19,252**	18,695	18,695
Trading assets	**2,468**	**2,468**	1,204	1,204
Securities purchased under agreements to resell	**33,702**	**33,702**	14,547	14,547
Finance receivables, net of allowance	**29,573**	**26,712**	27,995	27,528
Securities lending collateral	**69,306**	**69,306**	59,471	59,471
Other invested assets[b]	**40,330**	**40,637**	29,186	29,408
Short-term investments	**25,249**	**25,249**	15,342	15,342
Cash	**1,590**	**1,590**	1,897	1,897
Liabilities:				
Policyholders' contract deposits	**244,658**	**239,964**	227,027	223,244
Borrowings under obligations of guaranteed investment agreements	**20,664**	**20,684**	20,811	22,373
Securities sold under agreements to repurchase	**22,710**	**22,710**	11,047	11,047
Trading liabilities	**3,141**	**3,141**	2,546	2,546
Hybrid financial instrument liabilities	**8,856**	**8,856**	—	—
Securities and spot commodities sold but not yet purchased	**4,076**	**4,076**	5,975	5,975
Unrealized loss on swaps, options and forward transactions	**11,401**	**11,401**	12,740	12,740
Trust deposits and deposits due to banks and other depositors	**5,249**	**5,261**	4,877	5,032
Commercial paper	**13,029**	**13,029**	9,208	9,208
Notes, bonds, loans and mortgages payable	**104,690**	**106,494**	78,439	79,518
Securities lending payable	**70,198**	**70,198**	60,409	60,409

(a) The carrying value of all other financial instruments approximates fair value.
(b) Excludes aircraft asset investments held by non-Financial Services subsidiaries.

14. Stock Compensation Plans

At December 31, 2006, AIG employees could be awarded compensation pursuant to six different stock-based compensation plan arrangements: *(i)* AIG 1999 Stock Option Plan, as amended (1999 Plan); *(ii)* AIG 1996 Employee Stock Purchase Plan, as amended (1996 Plan); *(iii)* AIG 2002 Stock Incentive Plan, as amended (2002 Plan) under which AIG has issued time-vested restricted stock units (RSUs) and performance restricted stock units (performance RSUs); *(iv)* SICO's Deferred Compensation Profit Participation Plans (SICO Plans); *(v)* AIG's 2005-2006 Deferred Compensation Profit Participation Plan (AIG DCPPP) and *(vi)* the AIG Partners Plan. The AIG DCPPP was adopted as a replacement for the SICO Plans for the 2005-2006 period, and the AIG Partners Plan replaces the AIG DCPPP. Stock-based compensation earned under the AIG DCPPP and the AIG Partners Plan is issued as awards under the 2002 Plan. AIG currently settles share option exercises and other share awards to participants through the issuance of shares it has previously acquired and holds in its treasury account, except for share awards made by SICO, which are settled by SICO.

At December 31, 2006, AIG's non-employee directors received stock-based compensation in two forms, options granted pursuant to the 1999 Plan and grants of AIG common stock with delivery deferred until retirement from the Board, pursuant to the AIG Director Stock Plan, which was approved by the shareholders at the 2004 Annual Meeting of Shareholders.

From January 1, 2003 through December 31, 2005, AIG accounted for share-based payment transactions with employees under FAS No. 123, ''Accounting for Stock-Based Compensation.'' Share-based employee compensation expense from option awards was not recognized in the statement of income in prior periods. Effective January 1, 2006, AIG adopted the fair value recognition provisions of FAS 123R. FAS 123R requires that companies use a fair value method to value share-based payments and recognize the related compensation expense in net earnings. AIG adopted FAS 123R using the modified prospective application method, and accordingly, financial statement amounts for the prior periods presented have not been restated to reflect the fair value method of expensing share-based compensation under FAS 123R. The modified prospective application method provides for the recognition of the fair value with respect to share-based compensation

14. Stock Compensation Plans

Continued

for shares subscribed for or granted on or after January 1, 2006 and all previously granted but unvested awards as of January 1, 2006.

The adoption of FAS 123R resulted in share-based compensation expense of approximately $17 million during 2006, related to awards which were accounted for under the provisions of Accounting Principles Board Opinion No. 25, ''Accounting for Stock Issued to Employees.'' FAS 123R also requires AIG to estimate forfeitures in calculating the expense relating to share-based compensation, rather than recognizing these forfeitures and corresponding reductions in expense as they occur. The pre-tax cumulative effect of adoption, recognized as a reduction in stock-based compensation of $46 million, was recorded as a cumulative effect of an accounting change, net of tax. FAS 123R requires AIG to reflect the cash savings resulting from excess tax benefits in its financial statements as cash flow from financing activities, rather than as cash flow from operating activities as in prior periods. The amount of this excess tax benefit for 2006 was $27.9 million.

Included in AIG's consolidated statement of income for the year ended December 31, 2006 was pre-tax share-based compensation expense of $353 million ($326 million after tax).

The effect of the adoption of FAS 123R on the consolidated statements of income and cash flows for the year ended December 31, 2006 was as follows:

(in millions, except per share data)	Pre-adoption of FAS 123R	Effect of Adoption of FAS 123R	Including Effect of Adoption of FAS 123R
Income before income taxes, minority interest and cumulative effect of an accounting change	$21,704	$ (17)	$21,687
Provision for income taxes	$ 6,539	$ (2)	$ 6,537
Income before minority interest and cumulative effect of an accounting change	$15,165	$ (15)	$15,150
Cumulative effect of an accounting change, net of tax	$ —	$ 34	$ 34
Net income	$14,029	$ 19	$14,048
Net cash provided by (used in) operating activities	$ 6,857	$ (28)	$ 6,829
Net cash provided by financing activities	$59,762	$ 28	$59,790
Basic earnings per share	$ 5.38	$0.01	$ 5.39
Diluted earnings per share	$ 5.35	$0.01	$ 5.36

14. Stock Compensation Plans

Continued

Included in share-based compensation expense of $353 million for 2006 was a one-time compensation cost of approximately $54 million related to the Starr tender offer and various out of period adjustments totalling $61 million, primarily relating to stock-splits and other miscellaneous items for the SICO Plans, offset by a $46 million pre-tax adjustment for the cumulative effect of the adoption of FAS 123R. See Note 16 herein for a discussion of the Starr tender offer.

If AIG had adopted the FAS 123 provisions for recognizing compensation expense commencing at the date of grant of the awards, the effect would not have been material to net income or basic or diluted earnings per share for 2005.

1999 Stock Option Plan

The 1999 Plan provides that options to purchase a maximum of 45,000,000 shares of common stock can be granted to certain key employees and members of the Board of Directors at prices not less than fair market value at the date of grant.

The 1999 Plan was approved by the shareholders at the 2000 Annual Meeting of Shareholders, with certain amendments approved at the 2003 Annual Meeting of Shareholders. The 1999 Plan superseded the 1991 Employee Stock Option Plan (the 1991 Plan), although outstanding options granted under the 1991 Plan continue in-force until exercise or expiration. The maximum number of shares that may be granted to any employee in any one year under the 1999 Plan is 900,000. Options granted under the 1999 Plan generally vest over four years (25 percent vesting per year) and expire 10 years from the date of grant.

At December 31, 2006, there were 19,615,911 shares reserved for future grants under the 1999 Plan and 28,021,943 shares reserved for issuance under the 1999 and 1991 Plans.

Deferrals

At December 31, 2006, AIG was obligated to issue 8,382,632 shares in connection with previous exercises of options with delivery deferred.

Valuation Methodology

In 2004, AIG developed a binomial lattice model to calculate the fair value of stock option grants. In prior years, a Black-Scholes model was used. A more detailed description of the valuation methodology is provided below.

The following weighted average assumptions were used for stock options granted in 2006 and 2005:

	2006	2005
Expected annual dividend yield[(a)]	**0.92%**	0.71%
Expected volatility[(b)]	**23.50%**	27.3%
Risk-free interest rate[(c)]	**4.61%**	4.17%
Expected term[(d)]	**7 years**	7 years

(a) The dividend yield is based on the dividend yield over the twelve month period prior to the grant date.

(b) In 2006, expected volatility is the average of historical volatility (based on seven years of daily stock price changes) and the implied volatility of actively traded options on AIG shares and in 2005, expected volatility is the historical volatility based on five years of daily stock price changes.

(c) The interest rate curves used in the valuation model were the U.S. Treasury STRIP rates with terms from 3 months to 10 years.

(d) The contractual term of the option is generally 10 years with an expected term of 7 years calculated based on an analysis of historical employee exercise behavior and employee turnover (post-vesting terminations). The early exercise rate is a function of time elapsed since the grant. Fifteen years of historical data were used to estimate the early exercise rate.

Additional information with respect to AIG's stock option plans at December 31, 2006, and changes for the year then ended, were as follows:

Options:	Shares	Weighted Average Exercise Price
Outstanding at beginning of year	52,545,425	$ 54.84
Granted	1,621,910	$70.51
Exercised*	(5,329,026)	$27.97
Forfeited or expired	(1,182,589)	$70.76
Outstanding at end of year	47,655,720	$57.99
Options exercisable at end of year	39,383,670	$56.81
Weighted average fair value per share of options granted		$23.41

** Includes options with respect to 2,067,643 shares exercised with delivery deferred, resulting in obligations to issue 1,527,613 shares.*

14. Stock Compensation Plans

Continued

The following table presents information about stock options outstanding at December 31, 2006:

Options Outstanding					Options Exercisable			
Range of Exercise Prices	Number Outstanding	Weighted Average Remaining Contractual Life	Weighted Average Exercise Price	Aggregate Intrinsic Values (in millions)	Number Exercisable (vested)	Weighted Average Remaining Contractual Life	Weighted Average Exercise Price	Aggregate Intrinsic Values (in millions)
$24.55-$26.45	3,077,376	0.82	$24.67	$144	3,077,376	0.82	$24.67	$144
$31.02-$41.51	5,198,823	1.58	36.91	181	5,198,823	1.58	36.91	181
$43.31-$53.40	6,665,147	3.83	48.59	154	5,900,494	3.53	48.80	135
$54.11-$59.99	8,314,413	4.07	57.86	115	6,780,399	3.01	57.52	96
$60.13-$63.95	8,766,329	5.94	62.33	82	7,547,511	5.77	62.12	72
$64.01-$69.63	8,034,276	6.82	65.45	50	4,948,364	5.75	65.53	30
$70.35-$98.00	7,599,356	5.53	81.36	1	5,930,703	4.40	84.06	—
Total	47,655,720	4.60	$57.99	$727	39,383,670	3.81	$56.81	$658

Vested and expected-to-vest options as of December 31, 2006, included in the table above, totaled 45,382,149, with a weighted average exercise price of $57.42, a weighted average contractual life of 4.33 years and an aggregate intrinsic value of $720 million.

As of December 31, 2006, total unrecognized compensation cost (net of expected forfeitures) was $133 million and $3 million related to non-vested share-based compensation awards granted under the 1999 Plan and the 1996 Plan, respectively, with blended weighted average periods of 1.44 years and 0.41 years, respectively. The cost of awards outstanding under these plans at December 31, 2006 is expected to be recognized over approximately three years and one year, respectively, for the 1999 Plan and the 1996 Plan.

The intrinsic value of options exercised during 2006 was approximately $215 million. The fair value of options vesting during 2006 was approximately $97 million. AIG received $104 million and $65 million in cash during 2006 and 2005, respectively, from the exercise of stock options. The tax benefits realized as a result of stock option exercises were $35 million and $20 million for 2006 and 2005, respectively.

2002 Stock Incentive Plan

The 2002 Plan was adopted at the 2002 Annual Meeting of shareholders and amended and restated by the AIG Board of Directors on September 18, 2002. The 2002 Plan provides that equity-based or equity-related awards with respect to shares of common stock can be issued to employees in any year up to a maximum of that number of shares equal to (a) 1,000,000 shares plus (b) the number of shares available but not issued in the prior calendar year. The maximum award that a grantee may receive under the 2002 Plan per year is rights with respect to 250,000 shares. During 2006 and 2005, 6,836,785 RSUs, including performance RSUs, and 3,055,835 RSUs, respectively, were granted by AIG. There were 4,488,458 shares reserved for issuance in connection with future awards at December 31, 2006. Substantially all RSUs granted to date under the 2002 Plan other than performance RSUs granted under the AIG DCPPP and the AIG Partners Plan vest on the fourth anniversary of the date of grant.

Director Stock Awards

The methodology used for valuing employee stock options is also used to value director stock options. Director stock options vest one year after the grant date, but are otherwise the same as employee stock options. Options with respect to 40,000 shares and 32,500 shares were granted during 2006 and 2005, respectively.

AIG also granted 14,000 shares and 6,250 shares, with delivery deferred, to directors during 2006 and 2005, respectively, under the Director Stock Plan. At December 31, 2006, there were 71,000 shares reserved for future grants under the Director Stock Plan.

Employee Stock Purchase Plan

AIG's 1996 Plan provides that eligible employees (those employed at least one year) may receive privileges to purchase up to an aggregate of 10,000,000 shares of AIG common stock, at a price equal to 85 percent of the fair market value on the date of the grant of the purchase privilege. Purchase privileges are granted quarterly and are limited to the number of whole shares that can be purchased on an annual basis by an amount equal to the lesser of 10 percent of an employee's annual salary or $10,000.

SICO Plans

The SICO Plans provide that shares of AIG common stock currently held by SICO are set aside for the benefit of the participant and distributed upon retirement. The SICO Board of Directors currently may permit an early payout of shares under certain circumstances. Prior to payout, the participant is not entitled to vote, dispose of or receive dividends with respect to such shares, and shares are subject to forfeiture under certain

14. Stock Compensation Plans

Continued

conditions, including but not limited to the participant's termination of employment with AIG prior to normal retirement age.

Historically, SICO's Board of Directors could elect to pay a participant cash in lieu of shares of AIG common stock. On December 9, 2005, SICO notified participants that essentially all subsequent distributions would be made only in shares, and not cash. As of that date, AIG modified its accounting for the SICO Plans from variable to fixed measurement accounting. Variable measurement accounting is used for those few awards for which cash elections had been made prior to March 2005. The SICO Plans are also described in Note 16 herein.

Although none of the costs of the various benefits provided under the SICO Plans have been paid by AIG, AIG has recorded compensation expense for the deferred compensation amounts paid to AIG employees by SICO, with an offsetting amount credited to additional paid-in capital reflecting amounts deemed contributed by SICO.

As of December 9, 2005, there were 12,650,292 non-vested AIG shares under the SICO Plans with a weighted-average fair value per share of $61.92. As of December 31, 2006, there were 11,443,772 non-vested AIG shares under the SICO Plans with a weighted-average fair value per share of $61.72.

A significant portion of the awards under the SICO Plans vest upon retirement when or after the participant reaches age 65. The portion of the awards for which early payout is available vest on the applicable payout date.

AIG DCPPP

Effective September 21, 2005, AIG adopted the AIG DCPPP, which provides equity-based compensation to key AIG employees, including senior executive officers. The AIG DCPPP was modeled on the SICO Plans.

The AIG DCPPP contingently allocates a fixed number of shares to each participant if AIG's cumulative adjusted earnings per share, as determined by AIG's Compensation Committee, for 2005 and 2006 exceed that for 2003 and 2004. The performance period is September 21, 2005 to December 31, 2006. At the end of the performance period, common shares are contingently allocated. The service period and related vesting consists of three pre-retirement tranches and a final retirement tranche at age 65.

At December 31, 2006, there were units representing 4,590,622 shares granted to participants.

AIG Partners Plan

On June 26, 2006, AIG's Compensation Committee approved two grants under the AIG Partners Plan. The first grant has a performance period which runs from January 1, 2006 through December 31, 2007. The second grant has a performance period which runs from January 1, 2007 through December 31, 2008. Both grants vest 50 percent on the fourth and sixth anniversaries of the first day of the related performance period. In addition, the Compensation Committee approved the performance metrics for the two grants prior to the date of grant. The measurement of the grants is deemed to have occurred on June 26, 2006 when there was mutual understanding of the key terms and conditions of the grants. Consistent with this treatment: a) 1,068,605 performance RSUs for the first grant and 2,488,865 performance RSUs for the second grant and b) unrecognized compensation of $49 million for the first grant and $137 million for the second grant are included in the related disclosure tables. Performance RSUs related to the first grant are excluded from AIG's diluted shares calculation because an insufficient amount of time has elapsed to conclusively determine that the performance metric will be achieved at the end of the related performance period. Because the performance period for the second grant does not begin until January 1, 2007, compensation expense for the second grant is not included in AIG's 2006 results and diluted shares calculation.

Valuation

The fair value of each award granted under the 2002 Plan, the AIG DCPPP, the AIG Partners Plan, and the SICO Plans is based on the closing price of AIG stock on the date of grant.

The following table presents a summary of shares relating to outstanding awards unvested under the foregoing plans as of December 31, 2006, and changes for the year then ended:

	Number of Shares					Weighted Average Grant-Date Fair Value				
	2002 Plan	AIG DCPPP	AIG Partners Plan	Total 2002 Plan	SICO Plans	2002 Plan	AIG DCPPP	AIG Partners Plan	Total 2002 Plan	SICO Plans
Unvested at January 1, 2006	4,322,265	4,898,880	—	9,221,145	12,650,292	$63.63	$52.55	$ —	$57.74	$61.92
Granted	3,198,885	—	3,637,900	6,836,785	—	70.04	—	56.49	62.83	—
Vested	(130,185)	—	—	(130,185)	(794,814)	61.44	—	—	61.44	65.68
Forfeited	(209,370)	(308,258)	(30,860)	(548,488)	(411,706)	62.53	59.40	56.22	60.41	60.38
Unvested at December 31, 2006	7,181,595	4,590,622	3,607,040	15,379,257	11,443,772	$66.56	$52.09	$56.50	$59.88	$61.72

14. Stock Compensation Plans

Continued

The total unrecognized compensation cost (net of expected forfeitures) related to non-vested share-based compensation awards granted under the 2002 Plan, the AIG DCPPP, the AIG Partners Plan and the SICO Plans at December 31, 2006 and the blended weighted-average period over which that cost is expected to be recognized at December 31, 2006 are as follows:

	Unrecognized Compensation Cost *(in millions)*	Blended Weighted-Average Period
2002 Plan	$322	1.79 years
AIG DCPPP	$208	4.49 years
AIG Partners Plan	$191	2.37 years
Total 2002 Plan	$721	2.72 years
SICO Plans	$301	5.95 years

The total cost for awards outstanding as of December 31, 2006 under the 2002 Plan, the AIG DCPPP, the AIG Partners Plan, and the SICO Plans is expected to be recognized over approximately 4 years, 11 years, 6 years and 23 years, respectively.

15. Employee Benefits

(a) Pension Plans: Employees of AIG, its subsidiaries and certain affiliated companies, including employees in foreign countries, are generally covered under various funded, unfunded and insured pension plans. Eligibility for participation in the various plans is based on either completion of a specified period of continuous service or date of hire, subject to age limitations. Some AIG subsidiaries provide retirement benefits through defined benefit plans, others employ defined contribution plans and some use both.

AIG's U.S. retirement plan is a qualified, noncontributory defined benefit plan which is subject to the provisions of ERISA. All employees of AIG and most of its subsidiaries and affiliates who are regularly employed in the United States, including certain U.S. citizens employed abroad on a U.S. dollar payroll, and who have attained age 21 and completed twelve months of continuous service are eligible to participate in this plan. An employee with 5 or more years of plan participation is entitled to pension benefits beginning at normal retirement at age 65. Benefits are based upon a percentage of average final compensation multiplied by years of credited service limited to 44 years of credited service. The average final compensation is subject to certain limitations. Employees may elect certain options with respect to receipt of their pension benefits including a joint and survivor annuity. An employee with 10 or more years of plan participation may retire early from age 55 to 64. An early retirement factor is applied resulting in a reduced benefit. If an employee terminates with less than five years of continuous service, the employee forfeits the right to receive any pension benefits accumulated to that time. Annual funding requirements are determined based on the ''projected unit credit'' cost method, which attributes a pro rata portion of the total projected benefit payable at normal retirement to each year of credited service.

The HSB Group Inc. (HSB) retirement plan was merged into the AIG U.S. retirement plan effective April 1, 2001. Benefits for HSB participants were changed effective January 1, 2005 to be substantially similar to the AIG U.S. retirement plan benefits subject to a grandfathering agreement.

21st Century sponsors its own benefit plans for its eligible employees. Assets, obligations and costs with respect to 21st Century's plans are included herein. The assumptions used in its plans were not significantly different from those used by AIG in AIG's U.S. plans.

The AIG Excess Retirement Income Plan provides a benefit equal to the reduction in benefits payable under the AIG U.S. retirement plan as a result of federal tax limitations on compensation and benefits payable thereunder. AIG has adopted a Supplemental Executive Retirement Plan (Supplemental Plan) to provide additional retirement benefits to designated executives. Under the Supplemental Plan, an annual benefit accrues at a percentage of final average pay multiplied by each year of credited service, not greater than 60 percent of final average pay, reduced by any benefits from the current and any predecessor retirement plans (including the AIG Excess Retirement Income Plan and any comparable plans), Social Security, if any, and from any qualified pension plan of prior employers. Currently, each of these plans is unfunded. AGC and HSB have adopted similar supplemental type plans. These plans are also unfunded.

Where non-U.S. retirement plans are defined benefit plans, they are generally either based on the employees' years of credited service and compensation in the years preceding retirement, or on points accumulated based on the employee's job grade and other factors during each year of service.

AIG is in the process of spinning off the assets and liabilities in the AIG U.S. retirement plan attributable to employees of Starr and The Starr Foundation. The accumulated benefit obligation of the employees in these two entities was computed as of December 31, 2005. At December 31, 2005, the AIG U.S. retirement plan was funded at an amount slightly greater than the accumulated benefit obligation. In the first quarter of 2007, AIG will transfer assets of approximately $32 million, which is the equivalent of the present value of the December 31, 2005 accumulated benefit (adjusted for interest and benefit payments through the transfer date) attributable to the employees in those entities. Consistent with this arrangement, the amounts shown in the financial statements and footnote exclude liabilities and assets for employees of Starr.

(b) Postretirement Plans: In addition to AIG's defined benefit pension plans, AIG and its subsidiaries provide a postretirement benefit program for medical care and life insurance in the U.S. and in certain non-U.S. countries. Eligibility in the various plans is generally based upon completion of a specified period of eligible service and attaining a specified age. Overseas, benefits vary by geographic location.

AIG's U.S. postretirement medical and life insurance benefits are based upon the employee electing immediate retirement and having a minimum of ten years of service. Retirees who reached

15. Employee Benefits

Continued

age 65 by May 1, 1989 and their dependents participate in the medical plan at no cost. Employees who retired after May 1, 1989 and prior to January 1, 1993 pay 50 percent of the active employee premium. Retiree contributions are subject to adjustment annually. Other cost sharing features of the medical plan include deductibles, coinsurance and Medicare coordination and a lifetime maximum benefit of $2.0 million. The maximum life insurance benefit prior to age 70 is $32,500, with a maximum of $25,000 thereafter.

Effective January 1, 1993, both plans' provisions were amended. Employees who retire after January 1, 1993 are required to pay the actual cost of the medical benefits premium reduced by a credit of a certain amount, based on years of service at retirement. The life insurance benefit varies by age at retirement from $5,000 for retirement at ages 55 through 59; $10,000 for retirement at ages 60 through 64; and $15,000 for retirement at ages 65 and over.

(c) Voluntary Savings Plans: AIG sponsors a voluntary savings plan for domestic employees (the AIG Incentive Savings plan), which provides for salary reduction contributions by employees and matching contributions by AIG of up to seven percent of annual salary depending on the employees' years of service. Contributions are funded currently.

(d) Postemployment Benefits: AIG provides certain benefits to inactive employees who are not retirees. Certain of these benefits are insured and expensed currently; other expenses are provided for currently. Such uninsured expenses include long-term disability benefits, medical and life insurance continuation, and COBRA medical subsidies.

(e) Benefit Obligations: The measurement date for some of the non-U.S. defined benefit pension and postretirement plans is November 30, consistent with the fiscal year end of the sponsoring companies. For all other plans, accumulated benefit obligations represent the present value of pension benefits earned as of December 31, 2006 based on service and compensation as of December 31, 2006. Projected benefit obligations for defined benefit plans represent the present value of pension benefits earned as of December 31, 2006 projected for estimated salary increases to an assumed date with respect to retirement, termination, disability or death. Projected benefit obligations for postretirement plans represent the present value of postretirement medical and life insurance benefits deemed earned as of December 31, 2006 projected for estimated salary and medical claim rate increases to an assumed date with respect to retirement, termination, disability, or death.

The accumulated benefit obligations with respect to both non-U.S. and U.S. pension benefit plans as of December 31, 2006 and 2005 were as follows:

(in millions)	**2006***	2005
Non-U.S. pension benefit plans	**$1,384**	$ 1,210
U.S. pension benefit plans	**$2,689**	$ 2,704

* *As of November 30, 2006 for non-U.S. plans of sponsoring companies with a fiscal year-end date of November 30, 2006.*

15. Employee Benefits

Continued

The following table sets forth the change in the projected benefit obligation of the defined benefit pension plans, including the supplemental plans, and postretirement benefit plans as of December 31, 2006 and 2005:

	Pension			Postretirement		
(in millions)	Non-U.S. Plans	U.S. Plans[a]	Total	Non-U.S. Plans	U.S. Plans	Total
2006[b]						
Change in projected benefit obligation:						
Benefit obligation at beginning of year	**$1,351**	**$3,131**	**$4,482**	**$43**	**$205**	**$248**
Service cost	**78**	**130**	**208**	**4**	**6**	**10**
Interest cost	**36**	**169**	**205**	**2**	**11**	**13**
Participant contributions	**1**	**—**	**1**	**—**	**—**	**—**
Actuarial (gain) loss	**(40)**	**(245)**	**(285)**	**5**	**(1)**	**4**
Plan amendments and mergers	**—**	**—**	**—**	**—**	**47**	**47**
Benefits paid:						
AIG assets	**(28)**	**(10)**	**(38)**	**(1)**	**(16)**	**(17)**
Plan assets	**(27)**	**(84)**	**(111)**	**—**	**—**	**—**
Effect of foreign currency fluctuation	**71**	**—**	**71**	**—**	**—**	**—**
Other[c]	**136**	**(12)**	**124**	**—**	**—**	**—**
Benefit obligation at end of year	**$1,578**	**$3,079**	**$4,657**	**$53**	**$252**	**$305**
2005						
Change in projected benefit obligation:						
Benefit obligation at beginning of year	$1,376	$2,750	$4,126	$35	$243	$278
Service cost	71	111	182	4	5	9
Interest cost	32	153	185	2	11	13
Participant contributions	1	—	1	—	—	—
Actuarial (gain) loss	77	241	318	3	(38)	(35)
Plan amendments, mergers and new material plans	43	(29)	14	—	—	—
Benefits paid:						
AIG assets	(28)	(11)	(39)	(1)	(16)	(17)
Plan assets	(29)	(84)	(113)	—	—	—
Effect of foreign currency fluctuation	(184)	—	(184)	1	—	1
Other	(8)	—	(8)	(1)	—	(1)
Benefit obligation at end of year	$1,351	$3,131	$4,482	$43	$205	$248

(a) Includes excess retirement income type plans and supplemental executive retirement type plans.

(b) As of November 30, 2006 for non-U.S. plans of sponsoring companies with fiscal year-end date of November 30, 2006.

(c) With respect to AIG's non-U.S. plan obligations, $100 million of this increase is the result of the reclassification of the Swiss plans. The Swiss plans were previously categorized as defined contribution plans since insurance companies have guaranteed the risks associated with these plans. However, the cost of paying for these guarantees is now viewed as a liability for the company in Switzerland. Therefore, the Swiss plans are treated as defined benefit plans. $45 million of the increase is due to the inclusion of new plans during 2006.

The weighted average assumptions used to determine the benefit obligations at December 31, 2006 and 2005 are as follows:

	Pension		Postretirement	
	Non-U.S. Plans	U.S. Plans	Non-U.S. Plans	U.S. Plans
2006*				
Discount rate	**2.25 - 10.75%**	**6.00%**	**4.00 - 5.75%**	**6.00%**
Rate of compensation increase	**1.50 - 10.00%**	**4.25%**	**3.00%**	**4.25%**
2005				
Discount rate	1.75 - 12.00%	5.50%	4.50 - 5.50%	5.50%
Rate of compensation increase	1.50 - 10.00%	4.25%	2.50 - 3.00%	4.25%

** At November 30, 2006 for non-U.S. plans of sponsoring companies with a fiscal year-end date of November 30, 2006.*

15. Employee Benefits

Continued

The benefit obligations for non-U.S. plans reflect those assumptions that were most appropriate for the local economic environments of each of the subsidiaries providing such benefits.

To measure the obligations at December 31, 2006 for AIG's U.S. plans, an 8.0 percent annual rate of increase in the per capita cost of covered medical benefits for pre-age-65 retirees, a 6.7 percent annual rate of increase in the per capita cost of covered medical benefits for post-age-65 retirees and a 10.0 percent annual rate of increase in the per capita cost of retiree prescription drug coverage were used for 2007. These rates were assumed to decrease gradually to 5.0 percent in 2013 and remain at that level thereafter.

To measure the obligations at December 31, 2005 for AIG's U.S. plans, a 9.0 percent annual rate of increase in the per capita cost of covered medical benefit for pre-age-65 retirees, a 7.0 percent annual rate of increase in the per capita cost of covered medical benefits for post-age-65 retirees and an 11.0 percent annual rate of increase in the per capita cost of retiree prescription drug coverage was used for 2006.

The assumed range for 2007 with respect to the annual rates of increase in the per capita cost of covered healthcare benefits of AIG's non-U.S. plans is 6.0 to 8.0 percent. These rates are assumed to decrease gradually to 4.0 to 6.0 percent over the next three years and remain at that level thereafter.

A one percent point change in the assumed healthcare cost trend rate would have the following effect on AIG's postretirement benefit obligations at December 31, 2006* and 2005:

	One Percent Increase		One Percent Decrease	
(in millions)	**2006**	2005	**2006**	2005
Non-U.S. plans	**$10**	$ 8	**$(7)**	$(6)
U.S. plans	**$ 3**	$(2)	**$(3)**	$ 2

* *At November 30, 2006, for non-U.S. plans with a fiscal year-end date of November 30, 2006.*

Discount Rate Methodology

The projected benefit cash flows under the AIG Retirement Plan were discounted using the spot rates derived from the Citigroup Pension Discount Curve as of December 31, 2006 and December 31, 2005 and an equivalent single discount rate was derived resulting in the same liability. This single discount rate was rounded to the nearest 25 basis points, namely 6.0 percent and 5.5 percent as of December 31, 2006 and December 31, 2005, respectively. The rates applied to other U.S. plans were not significantly different from those discussed above.

Japan represents over 62 percent of the liabilities of the non-U.S. pension plans. The discount rate for Japan was selected by reference to the published Moody's/S&P AA Corporate Bond Universe at the measurement date having regard to the duration of the plans' liabilities.

The mortality assumption used to determine the obligations for the U.S. plans as of December 31, 2006 and December 31, 2005 was based on the RP2000 White Collar Combined Mortality Table projected to 2006. The mortality assumptions for AIG's non-U.S. plans vary by country. There was a change in the mortality table assumption for Ireland, Japan, Taiwan and United Kingdom as of December 31, 2006 (November 30, 2006 for non-U.S. plans of sponsoring companies with a fiscal year-end date of November 30, 2006). The assumptions used are expected to reasonably anticipate future mortality experience. No other significant changes have been made for the December 31, 2006 obligations (November 30, 2006 obligations for non-U.S. plans of sponsoring companies with a fiscal year-end date of November 30, 2006).

(f) Funded Status: The funded status of the AIG defined benefit plans is a comparison of the projected benefit obligations to the assets related to the respective plan, if any. Effective December 31, 2006, AIG has adopted FAS 158 ''Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans'' — an amendment of FASB Statements No. 87, 88, 106 and 132(R). All amounts shown are pre-tax, unless noted otherwise.

15. Employee Benefits

Continued

The following table sets forth the funded status of the plans, reconciled to the amount reported on the consolidated balance sheet at December 31, 2006 (these assets and liabilities were not reported on the consolidated balance sheet at December 31, 2005):

	Pension			Postretirement[b]		
(in millions)	Non-U.S. Plans[a]	U.S. Plans	Total	Non-U.S. Plans	U.S. Plans	Total
2006						
Fair value of plan assets	**$ 850**	**$2,760**	**$ 3,610**	**$ —**	**$ —**	**$ —**
Less projected benefit obligations	**1,578**	**3,079**	**4,657**	**53**	**252**	**305**
Funded status at end of year	**$ (728)**	**$ (319)**	**$(1,047)**	**$(53)**	**$(252)**	**$(305)**
Amounts recognized in the consolidated balance sheet:						
Assets	**$ 18**	**$ —**	**$ 18**	**$ —**	**$ —**	**$ —**
Liabilities	**(746)**	**(319)**	**(1,065)**	**(53)**	**(252)**	**(305)**
Total amounts recognized	**$ (728)**	**$ (319)**	**$(1,047)**	**$(53)**	**$(252)**	**$(305)**
Amounts recognized in Accumulated other comprehensive income:						
Net loss	**$ 256**	**$ 687**	**$ 943**	**$ 7**	**$ 3**	**$ 10**
Prior service cost (credit)	**(72)**	**(20)**	**(92)**	**—**	**22**	**22**
Total amounts recognized	**$ 184**	**$ 667**	**$ 851**	**$ 7**	**$ 25**	**$ 32**
2005						
Fair value of plan assets	$ 699	$2,561	$ 3,260	$ —	$ —	$ —
Less projected benefit obligations	1,351	3,130	4,481	43	205	248
Funded status at end of year	$ (652)	$ (569)	$(1,221)	$(43)	$(205)	$(248)
Amounts not yet recognized:						
Actuarial (gains)/losses[c]	303	1,093	1,396	3	5	8
Prior service cost	(79)	(23)	(102)	—	(32)	(32)
Transition obligations	1	—	1	—	—	—
Net amount recognized	$ (427)	$ 501	$ 74	$(40)	$(232)	$(272)
Composition of net amount recognized:						
Prepaid benefit cost	$ 24	$ 670	$ 694	$ —	$ —	$ —
Accrued benefit cost	(590)	(217)	(807)	(40)	(232)	(272)
Intangible asset	3	6	9	—	—	—
Accumulated other comprehensive income	136	42	178	—	—	—
Net amount recognized	$ (427)	$ 501	$ 74	$(40)	$(232)	$(272)

(a) A significant portion of these plans, particularly those in Japan, are not required by local regulation to be funded currently. With respect to the funded status of these Japanese plans, the projected benefit obligation amounts to approximately $414 million and $410 million of which approximately $379 million and $360 million has been recognized at November 30, 2006 and December 31, 2005, respectively.

(b) AIG does not currently fund postretirement benefits.

(c) Actuarial (gains)/losses are amounts included in the projected benefit obligations but not yet recognized in the financial statements.

15. Employee Benefits

Continued

The following table sets forth the effect of FAS 158 on the consolidated balance sheet at December 31, 2006:

(in millions)	Pre-adoption of FAS 158	Effect of Adoption of FAS 158	Including Effect of Adoption of FAS 158
Prepaid assets (pensions)	$ 550	$(532)	$ 18
Intangible assets (pensions)	6	(6)	—
Total assets	979,952	(538)	979,414
Liability for pension benefits[(a)]	1,140	230	1,370
Net deferred tax liability	9,088	(236)	8,852
Total liabilities	877,552	(6)	877,546
Accumulated other comprehensive income, net of tax	9,642	(532)	9,110
Total liabilities, preferred shareholders' equity in subsidiary companies and shareholders' equity	$979,952	$(538)	$979,414

(a) Included in Other liabilities in the consolidated balance sheet.

Defined benefit pension plan obligations where the projected benefit obligation was in excess of the related plan assets at December 31, 2006 and 2005 were as follows:

	2006*		2005	
(in millions)	Non-U.S. Plans	U.S. Plans	Non-U.S. Plans	U.S. Plans
Projected benefit obligation	$1,486	$3,079	$1,284	$3,130
Accumulated benefit obligation	1,323	2,689	1,163	2,704
Fair value of plan assets	740	2,760	610	2,561

** At November 30, 2006 for non-U.S. plans of sponsoring companies with fiscal year-end date of November 30, 2006.*

Defined benefit pension plan obligations where the accumulated benefit obligation was in excess of the related plan assets at December 31, 2006 and 2005 were as follows:

	2006*		2005	
(in millions)	Non-U.S. Plans	U.S. Plans	Non-U.S. Plans	U.S. Plans
Projected benefit obligation	$1,465	$240	$1,281	$268
Accumulated benefit obligation	1,311	204	1,161	224
Fair value of plan assets	723	11	607	9

** At November 30, 2006 for non-U.S. plans of sponsoring companies with fiscal year-end date of November 30, 2006.*

15. Employee Benefits

Continued

(g) Plan Assets:

The following table sets forth the change in plan assets as of December 31, 2006 and 2005:

	Pension			Postretirement		
(in millions)	Non-U.S. Plans	U.S. Plans	Total	Non-U.S. Plans	U.S. Plans	Total
2006[a]						
Change in plan assets:						
Fair value of plan assets, at beginning of year	**$699**	**$2,561**	**$3,260**	**$—**	**$ —**	**$ —**
Actual return on plan assets, net of expenses	**33**	**282**	**315**	**—**	**—**	**—**
AIG contributions	**69**	**11**	**80**	**1**	**16**	**17**
Participant contributions	**1**	**—**	**1**	**—**	**—**	**—**
Benefits paid:						
AIG assets	**(28)**	**(10)**	**(38)**	**(1)**	**(16)**	**(17)**
Plan assets	**(27)**	**(84)**	**(111)**	**—**	**—**	**—**
Effect of foreign currency fluctuation	**41**	**—**	**41**	**—**	**—**	**—**
Other[b]	**62**	**—**	**62**	**—**	**—**	**—**
Fair value of plan assets, end of year	**$850**	**$2,760**	**$3,610**	**$—**	**$ —**	**$ —**
2005						
Change in plan assets:						
Fair value of plan assets, at beginning of year	$624	$2,247	$2,871	$—	$ —	$ —
Actual return on plan assets, net of expenses	101	113	214	—	—	—
AIG contributions	95	298	393	1	16	17
Participant contributions	1	—	1	—	—	—
Benefits paid:						
AIG assets	(28)	(11)	(39)	(1)	(16)	(17)
Plan assets	(29)	(84)	(113)	—	—	—
Effect of foreign currency fluctuation	(85)	—	(85)	—	—	—
Other	20	(2)	18	—	—	—
Fair value of plan assets, end of year	$699	$2,561	$3,260	$—	$ —	$ —

(a) As of November 30, 2006 for non-U.S. plans of sponsoring companies with fiscal year-end date of November 30, 2006.

(b) With respect to AIG's non-U.S. plan assets $80 million of this increase resulted from the reclassification of the Swiss plans. For further discussion of the Swiss plans see the preceding discussion in Note 15(e).

The asset allocation percentage by major asset class for AIG's plans at December 31, 2006 and 2005, and the target allocation for 2007 follow:

	Non-U.S. Plans-Allocation			U.S. Plans-Allocation		
	Target 2007	**Actual 2006***	Actual 2005	Target 2007	**Actual 2006**	Actual 2005
Asset class:						
Equity securities	0-75%	**47%**	46%	20-70%	**64%**	59%
Debt securities	0-100	**32**	27	20-70	**26**	34
Other	0-100	**21**	27	5-25	**10**	7
Total		**100%**	100%		**100%**	100%

** At November 30, 2006 for non-U.S. plans of sponsoring companies with fiscal year-end of November 30, 2006.*

Other includes cash, insurance contracts and real estate asset classes.

Included in equity securities for the U.S. plans at December 31, 2006 and 2005 were 55,680 and 602,680 shares of AIG common stock, with values of $4.0 million and $41.1 million, respectively.

The investment strategy with respect to AIG's pension plan assets is designed to achieve investment returns that will fully fund the pension plan over the long term, while limiting the risk of under funding over shorter time periods.

The expected rate of return with respect to AIG's domestic pension plan was 8.0 percent for years ended December 31, 2006 and 2005. These rates of return are an aggregation of

15. Employee Benefits

Continued

expected returns within each asset category. The return with respect to each asset class considers both historical returns and the future expectations for such returns.

(h) Expected Cash Flows: With respect to AIG's U.S. pension plan, the actuarially prepared funding amount ranges from the minimum amount AIG would be required to contribute to the maximum amount that would be deductible for U.S. tax purposes. This range is generally not determined until the fourth quarter with respect to the contribution year. Contributed amounts in excess of the minimum amounts are deemed voluntary. Amounts in excess of the maximum amount would be subject to an excise tax and may not be deductible under the Internal Revenue Code. Supplemental and excess plans' payments and postretirement plan payments are deductible when paid.

AIG contributed $80 million during 2006 to its U.S. and non-U.S. pension plans. The annual pension contribution for 2007 is expected to be approximately $95 million for U.S. and non-U.S. plans.

The expected future benefit payments, net of participants' contributions, with respect to the defined benefit pension plans and other postretirement benefit plans, are as follows:

	Pension		Postretirement	
(in millions)	Non-U.S. Plans	U.S. Plans	Non-U.S. Plans	U.S. Plans
2007	$ 67	$108	$1	$ 20
2008	71	117	1	21
2009	80	126	1	22
2010	79	136	1	20
2011	83	148	1	21
2012-2016	440	944	3	116

(i) Components of net periodic benefit cost and other amounts recognized in other comprehensive income:

The following table presents the components of net periodic benefit cost recognized in income and other amounts recognized in other comprehensive income with respect to the defined benefit pension plans and other postretirement benefit plans for the year ended December 31, 2006 (no amounts were recognized in other comprehensive income for the years ended 2005 and 2004):

	Pensions			Postretirement		
(in millions)	Non-U.S. Plans	U.S. Plans	Total	Non-U.S. Plans	U.S. Plans	Total
2006						
Components of net periodic benefit cost:						
Service cost	**$ 78**	**$ 130**	**$ 208**	**$ 4**	**$ 6**	**$10**
Interest cost	**36**	**169**	**205**	**2**	**11**	**13**
Expected return on assets	**(28)**	**(201)**	**(229)**	**—**	**—**	**—**
Amortization of prior service cost	**(9)**	**(3)**	**(12)**	**—**	**(6)**	**(6)**
Amortization of transitional obligation	**1**	**—**	**1**	**—**	**—**	**—**
Recognition of net actuarial (gains)/losses	**16**	**75**	**91**	**—**	**—**	**—**
Other	**1**	**6**	**7**	**—**	**—**	**—**
Net periodic benefit cost	**$ 95**	**$ 176**	**$ 271**	**$ 6**	**$11**	**$17**
Total recognized in other comprehensive income	**$ 38**	**$ 24**	**$ 62**	**$ —**	**$ —**	**$ —**
Total recognized in net periodic benefit cost and other comprehensive income	**$133**	**$ 200**	**$ 333**	**$ 6**	**$11**	**$17**
2005						
Components of net periodic benefit cost:						
Service cost	$ 71	$ 111	$ 182	$ 4	$ 5	$ 9
Interest cost	32	153	185	2	11	13
Expected return on assets	(21)	(180)	(201)	—	—	—
Amortization of prior service cost	(10)	(3)	(13)	—	(6)	(6)
Amortization of transitional obligation	1	—	1	—	—	—
Recognition of net actuarial (gains)/losses	21	55	76	—	—	—
Other	7	1	8	—	—	—
Net periodic benefit cost	$101	$ 137	$ 238	$ 6	$10	$16
2004						
Components of net periodic benefit cost:						
Service cost	$ 59	$ 101	$ 160	$ 3	$ 6	$ 9
Interest cost	33	147	180	2	14	16
Expected return on assets	(22)	(170)	(192)	—	—	—
Amortization of prior service cost	(8)	—	(8)	—	(7)	(7)
Amortization of transitional obligation	2	—	2	—	—	—
Recognition of net actuarial (gains)/losses	15	53	68	11	2	13
Other*	(24)	—	(24)	3	—	3
Net periodic benefit cost	$ 55	$ 131	$ 186	$19	$15	$34

* *The reduction resulted from transferring to the Japanese government certain Japanese plan obligations approximating $50 million reduced by approximately $26 million loss incurred with respect to the settlement of those obligations.*

For the U.S. plans, the estimated net loss, prior service credit and transition obligation for the defined benefit pension plans that will be amortized from Accumulated other comprehensive income into net periodic benefit cost over the next fiscal year are $37 million, $3 million and $0 million, respectively. For the non-U.S. plans, the estimated net loss, prior service credit and transition obligation for the defined benefit pension plans that will be amortized from Accumulated other comprehensive income into net periodic benefit cost over the next fiscal year are $11 million, $10 million and $1 million, respectively. The estimated net loss, prior service credit and transition obligation for the other defined benefit postretirement plans that will be amortized from Accumulated other comprehensive income into net periodic benefit cost over the next fiscal year will be less than $5 million in the aggregate.

15. Employee Benefits

Continued

The weighted average assumptions used to determine the net periodic benefit costs for the years ended December 31, 2006, 2005 and 2004 were as follows:

	Pension		Postretirement	
	Non-U.S. Plans*	U.S. Plans	Non-U.S. Plans*	U.S. Plans
2006				
Discount rate	**1.75-12.00%**	**5.50%**	**4.50-5.50%**	**5.50%**
Rate of compensation increase	**1.50-10.00%**	**4.25%**	**2.50-3.00%**	**4.25%**
Expected return on assets	**2.50-13.50%**	**8.00%**	**N/A**	**N/A**
2005				
Discount rate	1.75-12.00%	5.75%	4.50-6.00%	5.75%
Rate of compensation increase	1.50-10.00%	4.25%	3.00%	4.25%
Expected return on assets	2.15-13.50%	8.00%	N/A	N/A
2004				
Discount rate	2.00-8.00%	6.00%	5.50-6.00%	6.00%
Rate of compensation increase	1.50-7.00%	4.25%	5.50%	4.25%
Expected return on assets	2.50-10.00%	8.25%	N/A	N/A

* *The benefit obligations for non-U.S. plans reflect those assumptions that were most appropriate for the local economic environments of the subsidiaries providing such benefits.*

AIG's postretirement plans provide benefits primarily in the form of defined employer contributions rather than defined employer benefits. Changes in the assumed healthcare cost trend rate do not have a material effect on postretirement expense.

16. Benefits Provided by Starr International Company, Inc. and C.V. Starr & Co., Inc.

SICO has provided a series of two-year Deferred Compensation Profit Participation Plans (SICO Plans) to certain AIG employees. The SICO Plans came into being in 1975 when the voting shareholders and Board of Directors of SICO, a private holding company whose principal asset is AIG common stock, decided that a portion of the capital value of SICO should be used to provide an incentive plan for the current and succeeding managements of all American International companies, including AIG.

None of the costs of the various benefits provided under the SICO Plans has been paid by AIG, although AIG has recorded a charge to reported earnings for the deferred compensation amounts paid to AIG employees by SICO, with an offsetting amount credited to additional paid-in capital reflecting amounts deemed contributed by SICO. The SICO Plans provide that shares currently owned by SICO are set aside by SICO for the benefit of the participant and distributed upon retirement. The SICO Board of Directors currently may permit an early payout of units under certain circumstances. Prior to payout, the participant is not entitled to vote, dispose of or receive dividends with respect to such shares, and shares are subject to forfeiture under certain conditions, including but not limited to the participant's voluntary termination of employment with AIG prior to normal retirement age. Under the SICO Plans, SICO's Board of Directors may elect to pay a participant cash in lieu of shares of AIG common stock. Following notification from SICO to participants in the SICO Plans that it will settle specific future awards under the SICO Plans with shares rather than cash, AIG modified its accounting for the SICO Plans from variable to fixed measurement accounting. AIG gave effect to this change in settlement method beginning on December 9, 2005, the date of SICO's notice to participants in the SICO Plans. See also Note 12(b) Commitments herein.

Compensation expense in 2006 included various out of period adjustments totaling $61 million, primarily relating to stock-splits and other miscellaneous items for the SICO plans. See also Note 14 herein.

In January 2006, C.V. Starr & Co., Inc. (Starr) completed its tender offer to purchase Starr interests from AIG employees. In conjunction with AIG's adoption of FAS 123R, Starr is considered to be an ''economic interest holder'' in AIG. As a result, compensation expense of $54 million was recorded in 2006 results with respect to the Starr tender offer.

As a result of its changing relationship with Starr and SICO, AIG has established new executive compensation plans to replace the SICO plans and investment opportunities previously provided by Starr. See Note 14 for a description of these plans.

Compensation expense with respect to the SICO Plans aggregated $108 million, $205 million and $62 million for 2006, 2005 and 2004, respectively.

17. Ownership and Transactions With Related Parties

(a) Ownership: According to the Schedule 13D filed on November 20, 2006 by Starr, SICO, Edward E. Matthews, Maurice R. Greenberg, the Maurice R. and Corinne P. Greenberg Family Foundation, Inc., the Universal Foundation, Inc. and the Maurice R. and Corinne P. Greenberg Joint Tenancy Company, LLC, these reporting persons could be deemed to beneficially own 365,923,844 shares of common stock at that date. Based on the shares of common stock outstanding as of January 31, 2007, this ownership would represent approximately 14 percent of the

17. Ownership and Transactions With Related Parties

Continued

voting stock of AIG. Although these reporting persons have made filings under Section 16 of the Exchange Act, reporting sales of shares of common stock, no amendment to the Schedule 13D has been filed to report a change in ownership subsequent to November 20, 2006.

(b) Transactions with Related Parties: Prior to the termination of their agency relationships with Starr during 2006, AIG and its subsidiaries paid commissions to Starr and its subsidiaries for the production and management of insurance business in the ordinary course of business. Payment for the production of insurance business to Starr aggregated approximately $47 million in 2006, $214 million in 2005, and $205 million in 2004. AIG also received approximately $4 million in 2006, $23 million in 2005, and $24 million in 2004 from Starr and paid none in 2006, approximately $20,000 in 2005, and $39,000 in 2004 to Starr in rental fees and none in 2006 and 2005 and $262,000 in 2004 for services. AIG also received none in 2006, approximately $2 million in 2005, and $1 million in 2004, respectively, from SICO and paid none in 2006 and approximately $1 million in each of the years 2005 and 2004 to SICO as reimbursement for services rendered at cost. AIG also paid to SICO $2 million in 2006, $3 million in 2005, and $4 million in 2004 in rental fees. There are no significant receivables from/payables to related parties at December 31, 2006.

18. Variable Interest Entities

FIN 46R clarifies the consolidation accounting for certain entities in which equity investors do not have the characteristics of a controlling financial interest or do not have sufficient equity that is at risk which would allow the entity to finance its activities without additional subordinated financial support. FIN 46R recognizes that consolidation based on majority voting interest should not apply to certain types of entities that are defined as VIEs. A VIE is consolidated by its primary beneficiary, which is the party that absorbs a majority of the expected losses or a majority of the expected residual returns of the VIE, or both.

AIG, in the normal course of business, is involved with various VIEs. In some cases, AIG has participated to varying degrees in the design of the entity. AIG's involvement in VIEs varies from being a passive investor to managing and structuring the activities of the VIE. AIG engages in transactions with VIEs to manage its investment needs, obtain funding as well as facilitate client needs through AIGGIC and AIGFP. AIG purchases debt securities (rated and unrated) and equity interests issued by VIEs, makes loans and provides other credit support to VIEs, enters into insurance and reinsurance transactions with VIEs, enters into leasing arrangements with VIEs, enters into derivative transactions with VIEs through AIGFP and acts as the collateral manager of VIEs through AIGGIC and AIGFP. Obligations to outside interest holders in VIEs consolidated by AIG are reported as liabilities in the consolidated financial statements. These interest holders generally have recourse only to the assets and cash flows of the VIEs and do not have recourse to AIG, except where AIG has provided a guarantee to the VIE's interest holders.

AIG determines whether an entity is a VIE, who the variable interest holders are, and which party is the primary beneficiary of the VIE by performing an analysis of the design of the VIE that includes a review of, among other factors, its capital structure, contractual relationships and terms, nature of the entity's operations and purpose, nature of the entity's interests issued, AIG's interests in the entity which either create or absorb variability and related party relationships. AIG consolidates a VIE in situations where all of AIG's interests in the VIE, when combined, absorb a majority of the expected losses or a majority of the expected residual returns of the VIE.

In addition to the VIEs that are consolidated in accordance with FIN 46R, the Company has significant variable interests in certain other VIEs that are not consolidated because the Company is not the primary beneficiary. AIG applies quantitative and qualitative measures in identifying significant variable interests.

Entities for which AIG is the primary beneficiary and consolidates or where AIG has a significant variable interest are as follows:

SunAmerica Affordable Housing Partnerships

SunAmerica Affordable Housing Partners, Inc. (SAAHP) organizes limited partnerships (investment partnerships) that are considered to be VIEs, and that are consolidated by AIG. The investment partnerships invest as limited partners in operating partnerships that develop and operate affordable housing qualifying for federal tax credits and a few market rate properties across the United States. The general partners in the operating partnerships are almost exclusively unaffiliated third-party developers. AIG does not normally consolidate an operating partnership if the general partner is an unaffiliated person. Through approximately 1,150 partnerships, SAAHP has invested in developments with approximately 155,000 apartment units nationwide, and has syndicated over $6 billion in partnership equity since 1991 to other investors who will receive, among other benefits, tax credits under certain sections of the Internal Revenue Code. AIG Retirement Services, Inc. functions as the general partner in certain investment partnerships and acts both as a credit enhancer in certain transactions, through differing structures with respect to funding development costs for the operating partnerships, and as guarantor that investors will receive the tax benefits projected at the time of syndication. AIG Retirement Services, Inc. consolidates these investment partnerships as a result of the guarantee provided to the investors. As part of their incentive compensation, certain key SAAHP employees have been awarded residual cash flow interests in the partnerships, subject to certain vesting requirements. The operating income of SAAHP is reported, along with other SunAmerica partnership income, as a component of AIG's Asset Management segment.

Asset Management

In certain instances, AIGGIC acts as the collateral manager or general partner of an investment fund, collateralized debt obliga-

18. Variable Interest Entities

Continued

tion (CDO), collateralized loan obligation (CLO), private equity fund or hedge fund. Such entities are typically registered investment companies or qualify for the specialized investment company accounting in accordance with the AICPA Investment Company Audit and Accounting Guide. In CDO and CLO transactions, AIG establishes a trust or other special purpose entity that purchases a portfolio of assets such as bank loans, corporate debt, or non-performing credits and issues trust certificates or debt securities that represent interests in the portfolio of assets. These transactions can be cash-based or synthetic and are actively or passively managed. For investment partnerships, hedge funds and private equity funds, AIG acts as the general partner or manager of the fund and is responsible for carrying out the investment mandate of the VIE. Often, AIG's insurance operations participate in these AIG managed structures as a passive investor in the debt or equity issued by the VIE. Typically, AIG does not provide any guarantees to the investors in the VIE.

AIGGIC is an investor in various real estate investments. These investments are typically with unaffiliated third-party developers via a partnership or limited liability company structure. Some of these entities are VIEs. The activities of these VIEs principally consists of the development or redevelopment of all major types of commercial (retail, office, industrial, logistics parks, mixed use, etc.) and residential real estate. AIG's involvement varies from being a passive equity investor to actively managing the activities of the VIE.

Investment Activities

As part of its investment activities, AIG's insurance operations invest in obligations which include debt and equity securities and interests issued by VIEs. These investments include investments in AIG sponsored and non-sponsored investment funds, hedge funds, private equity funds, and structured financing arrangements. The investments in these VIEs allow AIG's insurance entities to purchase assets permitted by insurance regulations while maximizing their return on these assets. AIG's insurance operations typically are not involved in the design or establishment of the VIE, nor do they actively participate in the management of the VIE.

AIGFP

The variable interests that AIGFP may hold in VIEs include debt securities, equity interests, loans, derivative instruments and other credit support arrangements. Transactions associated with VIEs include an asset-backed commercial paper conduit, asset securitizations, collateralized debt obligations, investment vehicles and other structured financial transactions. AIGFP engages in these transactions to facilitate client needs for investment purposes and to obtain funding.

AIGFP invests in preferred securities issued by VIEs. Additionally, AIGFP establishes VIEs that issue preferred interests to third parties and uses the proceeds to provide financing to AIGFP subsidiaries. In certain instances, AIGFP consolidates these VIEs.

AIGFP is the primary beneficiary of an asset-backed commercial paper conduit with which it entered into several total return swaps covering all the conduit's assets that absorb the majority of the expected losses of the entity. The assets of the conduit serve as collateral for the conduit's obligations. AIGFP is also the primary beneficiary of several structured financing transactions in which AIGFP holds the first loss position either by investing in the equity of the VIE or implicitly through a lending or derivative arrangement.

In certain instances, AIGFP enters into liquidity facilities with various SPEs where AIGFP provides liquidity to the SPE in the form of a guarantee, derivative, or a letter of credit and does not consolidate the VIE. AIGFP also executes various swap and option transactions with VIEs. Such contractual arrangements are done in the ordinary course of business. Typically, interest rate derivatives such as interest rate swaps and options executed with VIEs are not deemed to be variable interests or significant variable interests because the underlying is an observable market interest rate and AIGFP as the derivative counterparty to the VIE is senior to the debt and equity holders.

Asset Management and Insurance Activities

AIG uses VIEs in connection with certain guaranteed investment contract programs written by its Life Insurance & Retirement Services subsidiaries (GIC Programs). In the GIC Programs, AIG's Life Insurance subsidiaries (principally SunAmerica Life) provide guaranteed investment contracts to VIEs in which AIG does not have a direct variable interest, as defined under FIN 46R, in the entity. The VIE issues notes or bonds which are sold to third-party institutional investors. Neither AIG nor the insurance company issuing the GICs has any direct obligation to the investors in the notes or bonds. The proceeds from the securities issued by the VIE are invested by the VIE in the GICs. The insurance company subsidiaries use the proceeds to invest in a diversified portfolio of securities, primarily investment grade bonds. Both the assets and the liabilities of the insurance companies arising from these GIC Programs are presented in AIG's consolidated balance sheet. Thus, at December 31, 2006, approximately $32 billion of policyholders' contract deposits represented liabilities from issuances of GICs included in these GIC Programs.

Assets held by VIEs which are currently consolidated because AIG is the primary beneficiary (except for those VIEs where AIG also owns a majority voting interest), approximated $9.1 billion at December 31, 2006. These consolidated assets are reflected in AIG's consolidated balance sheet as Investments and Financial services assets.

Assets of VIEs where AIG has a significant variable interest and does not consolidate the VIE because AIG is not the primary beneficiary, approximated at $130.1 billion December 31, 2006. Although expected losses are not expected to be material, AIG's maximum exposure to loss from its involvement with these unconsolidated VIEs approximates $38.7 billion at December 31, 2006. For this purpose, maximum loss is considered to be the notional amount of credit lines, guarantees and other credit support, and liquidity facilities, the notional amounts of credit

18. Variable Interest Entities

Continued

default swaps and certain total return swaps, and the amount invested in the debt or equity issued by the VIE.

19. Derivatives

Derivatives are financial arrangements among two or more parties with returns linked to or ''derived'' from some underlying equity, debt, commodity or other asset, liability, or index. Derivative payments may be based on interest rates and exchange rates and/or prices of certain securities, commodities, or financial or commodity indices or other variables. Collateral is required, at the discretion of AIG, on certain transactions based on the creditworthiness of the counterparty.

AIG carries all derivatives in the consolidated balance sheet at fair value. The changes in fair value of the derivative transactions of AIGFP are presented as a component of AIG's operating income. However, in certain instances, when income is not recognized up front under EITF 02-03, income is recognized over the life of the contract, where appropriate.

The discussion below relates to the derivative activities of AIG (other than those of AIGFP) that qualify for hedge accounting treatment under FAS 133.

For derivatives designated as hedges, on the date the derivative contract is entered into, AIG designates the derivative as: *(i)* a hedge of the subsequent changes in the fair value of a recognized asset or liability or of an unrecognized firm commitment (''fair value'' hedge); *(ii)* a hedge of a forecasted transaction, or the variability of cash flows to be received or paid related to a recognized asset or liability (''cash flow'' hedge); or *(iii)* a hedge of a net investment in a foreign operation. Fair value and cash flow hedges may involve foreign currencies (''foreign currency hedges''). The gain or loss in the fair value of a derivative that is appropriately and contemporaneously documented, designated and is highly effective as a fair value hedge is recorded in current period earnings, along with the loss or gain on the hedged item attributable to the hedged risk. The gain or loss in the fair value of a derivative that is appropriately and contemporaneously documented, designated and is highly effective as a cash flow hedge is recorded in other comprehensive income, until earnings are affected by the variability of cash flows in the hedged item. Of the amount deferred in Other comprehensive income at December 31, 2006, AIG does not expect a material amount to be reclassified into earnings over the next twelve months. The portion of the gain or loss in the fair value of a derivative in a cash flow hedge that represents hedge ineffectiveness is recognized immediately in current period earnings. The amount of ineffectiveness was not material for 2006, 2005 and 2004. The gain or loss in the fair value of a derivative that is appropriately and contemporaneously documented, designated and is highly effective as a hedge of a net investment in a foreign operation is recorded in the foreign currency translation adjustments account within other comprehensive income. Changes in the fair value of derivatives used for other than hedging activities are reported in current period earnings (principally in realized capital gains and losses for AIG's insurance operations). AIG had no hedges that were considered fair value hedges or net investment hedges at December 31, 2006. At December 31, 2006, AIG's hedge accounting was limited to cash flow hedge accounting primarily related to the hedge of forecasted transactions.

AIG assesses, both at the hedge's inception and on an ongoing basis, whether the derivatives used in hedging transactions are highly effective in offsetting changes in fair values or cash flows of hedged items.

As of January 1, 2006 and December 31, 2006, the related balance of accumulated derivative net loss arising from cash flow hedges, net of tax, was $25 million and $28 million, respectively. Of the change in accumulated derivative net loss $3 million represents current period reclassifications to operating income.

In addition to hedging activities, AIG also uses derivative instruments with respect to investment operations, which include, among other things, credit default swaps, and purchasing investments with embedded derivatives, such as equity linked notes and convertible bonds. All changes in the fair value of these derivatives are recorded in earnings. AIG bifurcates an embedded derivative where: *(i)* the economic characteristics of the embedded instruments are not clearly and closely related to those of the remaining components of the financial instrument; *(ii)* the contract that embodies both the embedded derivative instrument and the host contract is not remeasured at fair value; and *(iii)* a separate instrument with the same terms as the embedded instrument meets the definition of a derivative under FAS 133.

The overwhelming majority of AIG's derivatives activities are conducted by AIGFP. AIGFP becomes a party to derivative financial instruments in the normal course of business and to reduce currency, interest rate, commodity, and equity exposures. Such instruments are reflected in the consolidated financial statements and are carried at a market or a fair value, whichever is appropriate. The recorded estimated fair values of such instruments may be different from the values that might be realized if AIGFP was required to sell or close out the transactions prior to maturity.

AIGFP, in the ordinary course of operations and as principal, structures and enters into derivative transactions to meet the needs of counterparties who may be seeking to hedge certain aspects of such counterparties' operations or obtain a desired financial exposure. AIGFP also enters into derivative transactions to hedge the financial exposures arising from its counterparty transactions. Such derivative transactions include interest rate, currency, commodity, credit and equity swaps, swaptions, and forward commitments. Interest rate swap transactions generally involve the exchange of fixed and floating rate interest payment obligations without the exchange of the underlying notional amounts. AIGFP typically becomes a principal in the exchange of interest payments between the parties and, therefore, is exposed to counterparty credit risk and may be exposed to loss, if counterparties default. Currency, commodity, and equity swaps are similar to interest rate swaps, but involve the exchange of specific currencies or cashflows based on the underlying commodity, equity securities or indices. Also, they may involve the exchange of notional amounts at the beginning and end

19. Derivatives

Continued

of the transaction. Swaptions are options where the holder has the right but not the obligation to enter into a swap transaction or cancel an existing swap transaction. At December 31, 2006, the aggregate notional amount of AIGFP's outstanding swap transactions approximated $1,456 billion, primarily related to interest rate swaps of approximately $1,058 billion.

Notional amount represents a standard of measurement of the volume of swaps business of Capital Markets operations. Notional amount is not a quantification of market risk or credit risk and is not recorded on the consolidated balance sheet. Notional amounts generally represent those amounts used to calculate contractual cash flows to be exchanged and are not paid or received, except for certain contracts such as currency swaps.

The timing and the amount of cash flows relating to Capital Markets foreign exchange forwards and exchange traded futures and options contracts are determined by each of the respective contractual agreements.

The following table presents the contractual and notional amounts by maturity and type of derivative of Capital Markets derivatives portfolio at December 31, 2006 and 2005:

	Remaining Life of Notional Amount*					
(in millions)	One Year	Two Through Five Years	Six Through Ten Years	After Ten Years	**Total 2006**	Total 2005
Capital Markets interest rate, currency and equity swaps and swaptions:						
Notional amount:						
Interest rate swaps	$380,704	$505,317	$149,573	$22,685	**$1,058,279**	$ 837,389
Currency swaps	59,656	111,571	36,438	10,426	**218,091**	211,519
Swaptions, equity and commodity swaps	65,402	64,467	30,319	19,852	**180,040**	175,097
Total	$505,762	$681,355	$216,330	$52,963	**$1,456,410**	$1,224,005

** Notional amount is not representative of either market risk or credit risk and is not recorded in the consolidated balance sheet.*

Futures and forward contracts are contracts that obligate the holder to sell or purchase foreign currencies, commodities or financial indices in which the seller/purchaser agrees to make/take delivery at a specified future date of a specified instrument, at a specified price or yield. Options are contracts that allow the holder of the option to purchase or sell the underlying commodity, currency or index at a specified price and within, or at, a specified period of time. As a writer of options, AIGFP generally receives an option premium and then manages the risk of any unfavorable change in the value of the underlying commodity, currency or index by entering into offsetting transactions with third-party market participants. Risks arise as a result of movements in current market prices from contracted prices, and the potential inability of the counterparties to meet their obligations under the contracts. At December 31, 2006, the contractual amount of Capital Markets futures, forward and option contracts approximated $520.2 billion.

The following table presents Capital Markets futures, forward and option contracts portfolio by maturity and type of derivative at December 31, 2006 and 2005:

	Remaining Life					
(in millions)	One Year	Two Through Five Years	Six Through Ten Years	After Ten Years	**Total 2006**	Total 2005
Futures, forward and options contracts:						
Exchange traded futures and options contracts contractual amount	$ 25,798	$1,473	$ —	$ —	**$ 27,271**	$ 25,298
Over the counter forward contracts contractual amount	484,524	6,903	1,486	—	**492,913**	295,778
Total	$510,322	$8,376	$1,486	$ —	**$520,184**	$321,076

AIGFP enters into credit derivative transactions in the ordinary course of its business. The majority of AIGFP's credit derivatives require AIGFP to provide credit protection on a designated portfolio of loans or debt securities. AIGFP provides such credit protection on a ''second loss'' basis, under which AIGFP's payment obligations arise only after credit losses in the designated portfolio exceed a specified threshold amount or level of ''first losses.'' The threshold amount of credit losses that must be realized before AIGFP has any payment obligation is negotiated by AIGFP for each transaction to provide that the likelihood of any payment obligation by AIGFP under each transaction is remote, even in severe recessionary market scenarios. At December 31, 2006 and 2005, the notional amounts of this credit derivatives portfolio (including the super senior transactions) were $483.6 billion and $387.2 billion, respectively.

19. Derivatives

Continued

AIG and its subsidiaries also use derivatives and other instruments as part of its financial risk management programs. Interest rate derivatives (such as interest rate swaps) are used to manage interest rate risk associated with its investments in fixed income securities, commercial paper issuances, medium- and long-term note offerings, and other interest rate sensitive assets and liabilities. In addition, foreign exchange derivatives (principally cross currency swaps, forwards and options) are used to economically hedge non-U.S. dollar denominated debt, net capital exposures and foreign exchange transactions. The derivatives are effective economic hedges of the exposures they are meant to offset.

20. Variable Life and Annuity Contracts

AIG follows American Institute of Certified Public Accountants Statement of Position 03-1 (SOP 03-1), which requires recognition of a liability for guaranteed minimum death benefits and other living benefits related to variable annuity and variable life contracts as well as certain disclosures for these products.

AIG reports variable contracts through separate and variable accounts when investment income and investment gains and losses accrue directly to, and investment risk is borne by, the contract holder (traditional variable annuities), and the separate account qualifies for separate account treatment under SOP 03-1. In some foreign jurisdictions, separate accounts are not legally insulated from general account creditors and therefore do not qualify for separate account treatment under SOP 03-1. In such cases, the variable contracts are reported as general account contracts. AIG also reports variable annuity and life contracts through separate and variable accounts, or general accounts when not qualified for separate account reporting, where AIG contractually guarantees to the contract holder (variable contracts with guarantees) either *(a)* total deposits made to the contract less any partial withdrawals plus a minimum return (and in minor instances, no minimum returns) (Net Deposits Plus a Minimum Return) or *(b)* the highest contract value attained, typically on any anniversary date minus any subsequent withdrawals following the contract anniversary (Highest Contract Value Attained). These guarantees include benefits that are payable in the event of death, annuitization, or, in other instances, at specified dates during the accumulation period. Such benefits are referred to as guaranteed minimum death benefits (GMDB), guaranteed minimum income benefits (GMIB), and guaranteed minimum withdrawal benefit (GMWB), or guaranteed minimum account value benefits (GMAV), respectively. For AIG, GMDB is by far the most widely offered benefit.

The assets supporting the variable portion of both traditional variable annuities and variable contracts with guarantees are carried at fair value and reported as summary total separate and variable account assets with an equivalent summary total reported for liabilities when the separate account qualifies for separate account treatment under SOP 03-1. Assets for separate accounts that do not qualify for separate account treatment are reported as trading account assets, and liabilities are included in the respective policyholder liability account of the general account. Amounts assessed against the contract holders for mortality, administrative, and other services are included in revenue and changes in liabilities for minimum guarantees are included in incurred policy losses and benefits in the Consolidated Statement of Income. Separate and variable account net investment income, net investment gains and losses, and the related liability changes are offset within the same line item in the Consolidated Statement of Income for those accounts that qualify for separate account treatment under SOP 03-1. Net investment income and gains and losses on trading accounts for contracts that do not qualify for separate account treatment under SOP 03-1 are reported in net investment income and are offset by an equal amount reported in incurred policy losses and benefits.

The vast majority of AIG's exposure on guarantees made to variable contract holders arises from GMDB. Details concerning AIG's GMDB exposures as of December 31, 2006 and 2005 are as follows:

(dollars in billions)	Net Deposits Plus a Minimum Return	Highest Contract Value Attained
2006		
Account value[(a)]	**$64**	**$15**
Amount at risk[(b)]	**6**	**1**
Average attained age of contract holders by product	**38-70 years**	**56-71 years**
Range of guaranteed minimum return rates	**0-10%**	
2005		
Account value[(a)]	$59	$13
Amount at risk[(b)]	7	1
Average attained age of contract holders by product	51-70 years	57-70 years
Range of guaranteed minimum return rates	0-10%	

(a) Included in Policyholders' contract deposits in the Consolidated Balance Sheet.

(b) Represents the amount of death benefit currently in excess of Account value.

The following summarizes GMDB liabilities for guarantees on variable contracts reflected in the general account.

(in millions)	**2006**	2005
Balance at January 1	**$442**	$485
Reserve increase	**35**	33
Benefits paid	**(71)**	(76)
Balance at December 31	**$406**	$442

The GMDB liability is determined each period end by estimating the expected value of death benefits in excess of the projected account balance and recognizing the excess ratably over the accumulation period based on total expected assessments. AIG regularly evaluates estimates used and adjusts the additional liability balance, with a related charge or credit to benefit

20. Variable Life and Annuity Contracts

Continued

expense, if actual experience or other evidence suggests that earlier assumptions should be revised.

The following assumptions and methodology were used to determine the domestic and foreign GMDB liability as of December 31, 2006:

- Data used was up to 5,000 stochastically generated investment performance scenarios.
- Mean investment performance assumptions ranged from 0 percent to approximately ten percent depending on the block of business.
- Volatility assumptions ranged from 10 percent to 30 percent depending on the block of business.
- Mortality was assumed at between 60 percent and 102 percent of various life and annuity mortality tables.
- For domestic contracts, lapse rates vary by contract type and duration and ranged from zero percent to 40 percent. For Japan, lapse rates ranged from zero percent to 20 percent depending on the type of contract.
- For domestic contracts, the discount rate ranged from 3.25 percent to 11 percent. For Japan, the discount rate ranged from zero percent to seven percent.

In addition to GMDB, AIG's contracts currently include to a lesser extent GMIB. The GMIB liability is determined each period end by estimating the expected value of the annuitization benefits in excess of the projected account balance at the date of annuitization and recognizing the excess ratably over the accumulation period based on total expected assessments. AIG regularly evaluates estimates used and adjusts the additional liability balance, with a related charge or credit to benefit expense, if actual experience or other evidence suggests that earlier assumptions should be revised. As of December 31, 2006, most of AIG's GMIB exposure was transferred via reinsurance agreements. Contracts with GMIB not reinsured have account values of $21 million with a corresponding reserve of less than $4 million.

AIG contracts currently include a minimal amount of GMAV and GMWB. GMAV and GMWB are considered to be derivatives and are recognized at fair value through earnings. AIG enters into derivative contracts to partially hedge the economic exposure that arises from GMAV and GMWB.

21. Quarterly Financial Information (Unaudited)

The following quarterly financial information for each of the three months ended March 31, June 30, September 30 and December 31, 2006 and 2005 is unaudited. However, in the opinion of management, all adjustments (consisting only of normal recurring adjustments) necessary for a fair statement of the results of operations for such periods, have been made.

Consolidated Statements of Income

	Three Months Ended							
	March 31,		June 30,		September 30,		December 31,	
(in millions, except per share data)	**2006**	2005	**2006**	2005	**2006**	2005[a]	**2006**	2005[b]
Revenues	**$27,259**	$27,202	**$26,743**	$27,903	**$29,199**	$26,408	**$29,993**	$27,392
Income before income taxes, minority interest and cumulative effect of an accounting change	**4,793**	5,649	**5,241**	6,701	**6,301**	2,547	**5,352**	316
Income before cumulative effect of an accounting change	**3,161**	3,799	**3,190**	4,489	**4,224**	1,745	**3,439**	444
Net income	**$ 3,195**	$ 3,799	**$ 3,190**	$ 4,489	**$ 4,224**	$ 1,745	**$ 3,439**	$ 444
Earnings per common share:								
Basic								
Income before cumulative effect of an accounting change	**$ 1.21**	$ 1.46	**$ 1.23**	$ 1.73	**$ 1.62**	$ 0.67	**$ 1.32**	$ 0.17
Cumulative effect of an accounting change, net of tax	**0.01**	—	**—**	—	**—**	—	**—**	—
Net income	**$ 1.22**	$ 1.46	**$ 1.23**	$ 1.73	**$ 1.62**	$ 0.67	**$ 1.32**	$ 0.17
Diluted								
Income before cumulative effect of an accounting change	**$ 1.21**	$ 1.45	**$ 1.21**[c]	$ 1.71	**$ 1.61**	$ 0.66[c]	**$ 1.31**	$ 0.17
Cumulative effect of an accounting change, net of tax	**0.01**	—	**—**	—	**—**	—	**—**	—
Net income	**$ 1.22**	$ 1.45	**$ 1.21**[c]	$ 1.71	**$ 1.61**	$ 0.66[c]	**$ 1.31**	$ 0.17
Average shares outstanding:								
Basic	**2,605**	2,597	**2,606**	2,596	**2,607**	2,597	**2,610**	2,597
Diluted	**2,624**	2,624	**2,625**	2,623	**2,626**	2,624	**2,622**	2,626

(a) The third quarter of 2005 included catastrophe losses of approximately $2.4 billion.

(b) The fourth quarter of 2005 included catastrophe losses of $841 million, regulatory settlement costs of approximately $1.6 billion, and an increase in net reserves of approximately $1.8 billion resulting from the annual review of General Insurance loss and loss adjustment reserves.

(c) Diluted earnings per common share were $1.216 for the quarter ended June 30, 2006, and $0.666 for the quarter ended September 30, 2005 using the discrete period weighted average shares outstanding for the respective periods.

22. Information Provided in Connection With Outstanding Debt

The following condensed consolidating financial statements are provided in compliance with Regulation S-X of the SEC.

(a) AGC is a holding company and a wholly owned subsidiary of AIG. AIG provides a full and unconditional guarantee of all outstanding debt of AGC.

American General Corporation (AGC):
Condensed Consolidating Balance Sheet

(in millions)	American International Group, Inc. Guarantor	AGC Issuer	Other Subsidiaries	Eliminations	Consolidated AIG
December 31, 2006					
Assets:					
Invested assets	**$ 7,346**	**$ —**	**$797,976**	**$ (14,822)**	**$790,500**
Cash	**76**	**—**	**1,514**	**—**	**1,590**
Carrying value of subsidiaries and partially owned companies, at equity	**109,125**	**27,967**	**8,436**	**(144,427)**	**1,101**
Other assets	**3,989**	**2,622**	**181,561**	**(1,949)**	**186,223**
Total assets	**$120,536**	**$30,589**	**$989,487**	**$(161,198)**	**$979,414**
Liabilities:					
Insurance liabilities	**$ 21**	**$ —**	**$495,135**	**$ (64)**	**$495,092**
Debt	**15,157**	**2,136**	**146,206**	**(14,820)**	**148,679**
Other liabilities	**3,681**	**3,508**	**228,068**	**(1,482)**	**233,775**
Total liabilities	**18,859**	**5,644**	**869,409**	**(16,366)**	**877,546**
Preferred shareholders' equity in subsidiary companies	**—**	**—**	**191**	**—**	**191**
Total shareholders' equity	**101,677**	**24,945**	**119,887**	**(144,832)**	**101,677**
Total liabilities, preferred shareholders' equity in subsidiary companies and shareholders' equity	**$120,536**	**$30,589**	**$989,487**	**$(161,198)**	**$979,414**
December 31, 2005					
Assets:					
Invested assets	$ 122	$ —	$696,424	$ (13,696)	$682,850
Cash	190	—	1,707	—	1,897
Carrying value of subsidiaries and partially owned companies, at equity	90,723	27,027	15,577	(132,169)	1,158
Other assets	4,332	2,577	161,564	(1,327)	167,146
Total assets	$ 95,367	$29,604	$875,272	$(147,192)	$853,051
Liabilities:					
Insurance liabilities	$ 408	$ —	$460,271	$ (56)	$460,623
Debt	5,329	2,087	114,490	(12,057)	109,849
Other liabilities	3,313	4,110	191,707	(3,054)	196,076
Total liabilities	9,050	6,197	766,468	(15,167)	766,548
Preferred shareholders' equity in subsidiary companies	—	—	186	—	186
Total shareholders' equity	86,317	23,407	108,618	(132,025)	86,317
Total liabilities, preferred shareholders' equity in subsidiary companies and shareholders' equity	$ 95,367	$29,604	$875,272	$(147,192)	$853,051

22. Information Provided in Connection With Outstanding Debt

Continued

Condensed Consolidating Statement of Income

(in millions)	American International Group, Inc. Guarantor	AGC Issuer	Other Subsidiaries	Eliminations	Consolidated AIG
Year Ended December 31, 2006					
Operating income	**$ (786)**	**$ 122**	**$22,351**	**$ —**	**$21,687**
Equity in undistributed net income of consolidated subsidiaries	**13,308**	**1,263**	**—**	**(14,571)**	**—**
Dividend income from consolidated subsidiaries	**1,689**	**602**	**—**	**(2,291)**	**—**
Income taxes (benefits)	**197**	**(131)**	**6,471**	**—**	**6,537**
Minority interest	**—**	**—**	**(1,136)**	**—**	**(1,136)**
Cumulative effect of an accounting change	**34**	**—**	**—**	**—**	**34**
Net income (loss)	**$14,048**	**$2,118**	**$14,744**	**$(16,862)**	**$14,048**
Year Ended December 31, 2005					
Operating income	$(1,569)	$ (200)	$16,982	$ —	$15,213
Equity in undistributed net income of consolidated subsidiaries	10,156	2,530	—	(12,686)	—
Dividend income from consolidated subsidiaries	1,958	—	—	(1,958)	—
Income taxes (benefits)	68	(92)	4,282	—	4,258
Minority interest	—	—	(478)	—	(478)
Net income (loss)	$10,477	$2,422	$12,222	$(14,644)	$10,477
Year Ended December 31, 2004					
Operating income	$ 161	$ 90	$14,594	$ —	$14,845
Equity in undistributed net income of consolidated subsidiaries	8,602	2,048	—	(10,650)	—
Dividend income from consolidated subsidiaries	1,939	65	—	(2,004)	—
Income taxes (benefits)	863	31	3,513	—	4,407
Minority interest	—	—	(455)	—	(455)
Cumulative effect of an accounting change	—	—	(144)	—	(144)
Net income (loss)	$ 9,839	$2,172	$10,482	$(12,654)	$ 9,839

22. Information Provided in Connection With Outstanding Debt

Continued

Condensed Consolidating Statements of Cash Flow

(in millions)	American International Group, Inc. Guarantor	AGC Issuer	Other Subsidiaries	Consolidated AIG
Year Ended December 31, 2006				
Net cash provided by operating activities	**$ (590)**	**$ 258**	**$ 7,161**	**$ 6,829**
Cash flows from investing:				
Invested assets disposed	**3,831**	**—**	**154,283**	**158,114**
Invested assets acquired	**(8,298)**	**—**	**(215,759)**	**(224,057)**
Other	**(3,176)**	**(67)**	**2,146**	**(1,097)**
Net cash used in investing activities	**(7,643)**	**(67)**	**(59,330)**	**(67,040)**
Cash flows from financing activities:				
Issuance of debt	**12,038**	**—**	**61,942**	**73,980**
Repayments of debt	**(2,417)**	**—**	**(34,063)**	**(36,480)**
Other	**(1,502)**	**(191)**	**23,983**	**22,290**
Net cash provided by (used in) financing activities	**8,119**	**(191)**	**51,862**	**59,790**
Effect of exchange rate changes on cash	**—**	**—**	**114**	**114**
Change in cash	**(114)**	**—**	**(193)**	**(307)**
Cash at beginning of year	**190**	**—**	**1,707**	**1,897**
Cash at end of year	**$ 76**	**$ —**	**$ 1,514**	**$ 1,590**
Year Ended December 31, 2005				
Net cash provided by operating activities	$ 1,854	$ 805	$ 22,723	$ 25,382
Cash flows from investing:				
Invested assets disposed	—	—	184,843	184,843
Invested assets acquired	(598)	—	(245,804)	(246,402)
Other	(1,083)	(247)	389	(941)
Net cash used in investing activities	(1,681)	(247)	(60,572)	(62,500)
Cash flows from financing activities:				
Issuance of debt	2,101	—	64,960	67,061
Repayments of debt	(607)	(398)	(51,099)	(52,104)
Other	(1,494)	(160)	23,866	22,212
Net cash provided by (used in) financing activities	—	(558)	37,727	37,169
Effect of exchange rate changes on cash	—		(163)	(163)
Change in cash	173	—	(285)	(112)
Cash at beginning of year	17	—	1,992	2,009
Cash at end of year	$ 190	$ —	$ 1,707	$ 1,897
Year Ended December 31, 2004				
Net cash provided by operating activities	$ 1,390	$ 839	$ 27,185	$ 29,414
Cash flows from investing:				
Invested assets disposed	502	—	149,883	150,385
Invested assets acquired	(107)	—	(242,231)	(242,338)
Other	251	(408)	(486)	(643)
Net cash used in investing activities	646	(408)	(92,834)	(92,596)
Cash flows from financing activities:				
Issuance of debt	—	—	46,695	46,695
Repayments of debt	(400)	(349)	(32,203)	(32,952)
Other	(1,638)	(82)	52,194	50,474
Net cash provided by (used in) financing activities	(2,038)	(431)	66,686	64,217
Effect of exchange rate changes on cash	—		52	52
Change in cash	(2)	—	1,089	1,087
Cash at beginning of year	19	—	903	922
Cash at end of year	$ 17	$ —	$ 1,992	$ 2,009

22. Information Provided in Connection With Outstanding Debt

Continued

(b) AIG Liquidity Corp. is a wholly owned subsidiary of AIG. AIG provides a full and unconditional guarantee of all obligations of AIG Liquidity Corp., which commenced operations in 2003.

AIG Liquidity Corp.:
Condensed Consolidating Balance Sheet

(in millions)	American International Group, Inc. Guarantor	AIG Liquidity Corp.	Other Subsidiaries	Eliminations	Consolidated AIG
December 31, 2006					
Assets:					
Invested assets	**$ 7,346**	**$ ***	**$ 797,976**	**$ (14,822)**	**$790,500**
Cash	**76**	****	**1,514**	**—**	**1,590**
Carrying value of subsidiaries and partially owned companies, at equity	**109,125**	**—**	**36,403**	**(144,427)**	**1,101**
Other assets	**3,989**	****	**184,183**	**(1,949)**	**186,223**
Total assets	**$120,536**	**$ ***	**$1,020,076**	**$(161,198)**	**$979,414**
Liabilities:					
Insurance liabilities	**$ 21**	**$ —**	**$ 495,135**	**$ (64)**	**$495,092**
Debt	**15,157**	****	**148,342**	**(14,820)**	**148,679**
Other liabilities	**3,681**	****	**231,576**	**(1,482)**	**233,775**
Total liabilities	**18,859**	**$ ***	**$ 875,053**	**$ (16,366)**	**$877,546**
Preferred shareholders' equity in subsidiary companies	**—**	**—**	**191**	**—**	**191**
Total shareholders' equity	**101,677**	****	**144,832**	**(144,832)**	**101,677**
Total liabilities, preferred shareholders' equity in subsidiary companies and shareholders' equity	**$120,536**	**$ ***	**$1,020,076**	**$(161,198)**	**$979,414**
December 31, 2005					
Assets:					
Invested assets	$ 122	$ *	$ 696,424	$ (13,696)	$682,850
Cash	190	*	1,707	—	1,897
Carrying value of subsidiaries and partially owned companies, at equity	90,723	—	42,604	(132,169)	1,158
Other assets	4,332	*	164,141	(1,327)	167,146
Total assets	$ 95,367	$ *	$ 904,876	$(147,192)	$853,051
Liabilities:					
Insurance liabilities	$ 408	$ —	$ 460,271	$ (56)	$460,623
Debt	5,329	*	116,577	(12,057)	109,849
Other liabilities	3,313	*	195,817	(3,054)	196,076
Total liabilities	9,050	*	772,665	(15,167)	766,548
Preferred shareholders' equity in subsidiary companies	—	—	186	—	186
Total shareholders' equity	86,317	*	132,025	(132,025)	86,317
Total liabilities, preferred shareholders' equity in subsidiary companies and shareholders' equity	$ 95,367	$ *	$ 904,876	$(147,192)	$853,051

** Amounts significantly less than $1 million.*

22. Information Provided in Connection With Outstanding Debt

Continued

Condensed Consolidating Statement of Income

(in millions)	American International Group, Inc. Guarantor	AIG Liquidity Corp.	Other Subsidiaries	Eliminations	Consolidated AIG
Year Ended December 31, 2006					
Operating Income	**$ (786)**	**$ ***	**$22,473**	**$ —**	**$21,687**
Equity in undistributed net income of consolidated subsidiaries	**13,308**	**—**	**1,263**	**(14,571)**	**—**
Dividend income from consolidated subsidiaries	**1,689**	**—**	**602**	**(2,291)**	**—**
Income taxes (benefits)	**197**	*****	**6,340**	**—**	**6,537**
Minority interest	**—**	**—**	**(1,136)**	**—**	**(1,136)**
Cumulative effect of an accounting change	**34**	*****	**—**	**—**	**34**
Net income (loss)	**$14,048**	**$ ***	**$16,862**	**$(16,862)**	**$14,048**
Year Ended December 31, 2005					
Operating Income	$ (1,569)	$ *	$16,782	$ —	$15,213
Equity in undistributed net income of consolidated subsidiaries	10,156	—	2,530	(12,686)	—
Dividend income from consolidated subsidiaries	1,958	*	—	(1,958)	—
Income taxes (benefits)	68	—	4,190	—	4,258
Minority interest	—	—	(478)	—	(478)
Net income (loss)	$10,477	$ *	$14,644	$(14,644)	$10,477
Year Ended December 31, 2004					
Operating Income	$ 161	$ *	$14,684	$ —	$14,845
Equity in undistributed net income of consolidated subsidiaries	8,602	—	2,048	(10,650)	—
Dividend income from consolidated subsidiaries	1,939	—	65	(2,004)	—
Income taxes (benefits)	863	*	3,544	—	4,407
Minority interest	—	—	(455)	—	(455)
Cumulative effect of an accounting change	—	—	(144)	—	(144)
Net income (loss)	$ 9,839	$ *	$12,654	$(12,654)	$ 9,839

** Amounts significantly less than $1 million.*

22. Information Provided in Connection With Outstanding Debt

Continued

Condensed Consolidating Statements of Cash Flow

(in millions)	American International Group, Inc. Guarantor	AIG Liquidity Corp.	Other Subsidiaries	Consolidated AIG
Year Ended December 31, 2006				
Net cash provided by operating activities	**$ (590)**	**$ ***	**$ 7,419**	**$ 6,829**
Cash flows from investing activities:				
Invested assets disposed	**3,831**	**—**	**154,283**	**158,114**
Invested assets acquired	**(8,298)**	**—**	**(215,759)**	**(224,057)**
Other	**(3,176)**	*****	**2,079**	**(1,097)**
Net cash used in investing activities	**(7,643)**	*****	**(59,397)**	**(67,040)**
Cash flows from financing activities:				
Issuance of debt	**12,038**	**—**	**61,942**	**73,980**
Repayments of debt	**(2,417)**	**—**	**(34,063)**	**(36,480)**
Other	**(1,502)**	*****	**23,792**	**22,290**
Net cash provided by (used in) financing activities	**8,119**	*****	**51,671**	**59,790**
Effect of exchange rate changes on cash	**—**	**—**	**114**	**114**
Change in cash	**(114)**	*****	**(193)**	**(307)**
Cash at beginning of year	**190**	**—**	**1,707**	**1,897**
Cash at end of year	**$ 76**	**$ ***	**$ 1,514**	**$ 1,590**
Year Ended December 31, 2005				
Net cash provided by operating activities	$ 1,854	$ *	$ 23,528	$ 25,382
Cash flows from investing activities:				
Invested assets disposed	—	—	184,843	184,843
Invested assets acquired	(598)	—	(245,804)	(246,402)
Other	(1,083)	*	142	(941)
Net cash used in investing activities	(1,681)	*	(60,819)	(62,500)
Cash flows from financing activities:				
Issuance of debt	2,101	—	64,960	67,061
Repayments of debt	(607)	—	(51,497)	(52,104)
Other	(1,494)	*	23,706	22,212
Net cash provided by (used in) financing activities	—	*	37,169	37,169
Effect of exchange rate changes on cash	—	—	(163)	(163)
Change in cash	173	*	(285)	(112)
Cash at beginning of year	17	—	1,992	2,009
Cash at end of year	$ 190	$ *	$ 1,707	$ 1,897
Year Ended December 31, 2004				
Net cash provided by operating activities	$ 1,390	$ *	$ 28,024	$ 29,414
Cash flows from investing activities:				
Invested assets disposed	502	—	149,883	150,385
Invested assets acquired	(107)	—	(242,231)	(242,338)
Other	251	*	(894)	(643)
Net cash used in investing activities	646	*	(93,242)	(92,596)
Cash flows from financing activities:				
Issuance of debt	—	—	46,695	46,695
Repayments of debt	(400)	—	(32,552)	(32,952)
Other	(1,638)	*	52,112	50,474
Net cash provided by (used in) financing activities	(2,038)	*	66,255	64,217
Effect of exchange rate changes on cash	—	—	52	52
Change in cash	(2)	*	1,089	1,087
Cash at beginning of year	19	—	903	922
Cash at end of year	$ 17	$ *	$ 1,992	$ 2,009

** Amounts significantly less than $1 million.*

23. Cash Flows

As part of its remediation activities during 2006, AIG determined that certain non-cash activities and adjustments, including the effects of changes in foreign exchange translation on assets and liabilities, previously were misclassified within the operating, investing and financing sections of the Consolidated Statement of Cash Flows. The more significant line items revised include the change in General and life insurance reserves and DAC within operating activities; Purchases of fixed maturity securities within investing activities; and Proceeds from notes, bonds, loans and mortgages payable, and hybrid financial instrument liabilities within financing activities. After evaluating the effect of these items during the third quarter of 2006, AIG has revised the previous periods presented below to conform to the 2006 presentation:

(in millions)	Year Ended December 31, 2005	Year Ended December 31, 2004
Cash flows from operating activities — As previously reported	$ 25,138	$ 30,716
Revisions	244	(1,302)
Cash flows from operating activities — As revised	$ 25,382	$ 29,414
Cash flows from investing activities — As previously reported	$(57,321)	$(97,115)
Revisions	(5,179)	4,519
Cash flows from investing activities — As revised	$(62,500)	$(92,596)
Cash flows from financing activities — As previously reported	$ 32,999	$ 66,494
Revisions	4,170	(2,277)
Cash flows from financing activities — As revised	$ 37,169	$ 64,217
Effect of exchange rate changes on cash — As previously reported	$ (928)	$ 992
Revisions	765	(940)
Effect of exchange rate changes on cash — As revised	$ (163)	$ 52

There was no effect on ending cash balances.

Part II – Other Information

Item 9.
Changes in and Disagreements With Accountants on Accounting and Financial Disclosure

There have been no changes in accountants during the twenty-four months ended December 31, 2006.

Item 9A.
Controls and Procedures

Evaluation of Disclosure Controls and Procedures

In connection with the preparation of this Annual Report on Form 10-K, an evaluation was carried out by AIG's management, with the participation of AIG's Chief Executive Officer and Chief Financial Officer, of the effectiveness of AIG's disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934 (Exchange Act)) as of December 31, 2006. Disclosure controls and procedures are designed to ensure that information required to be disclosed in reports filed or submitted under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in SEC rules and forms and that such information is accumulated and communicated to management, including the Chief Executive Officer and Chief Financial Officer, to allow timely decisions regarding required disclosures.

During the evaluation of disclosure controls and procedures as of December 31, 2005 conducted during the preparation of AIG's financial statements to be included in the Annual Report on Form 10-K for the year ended December 31, 2005, three material weaknesses in internal control over financial reporting were identified, relating to controls over certain balance sheet reconciliations, controls over the accounting for certain derivative transactions and controls over income tax accounting. As a result, AIG's Chief Executive Officer and Chief Financial Officer concluded that, as of December 31, 2005, AIG's disclosure controls and procedures were ineffective.

Under the direction of its Chief Executive Officer and Chief Financial Officer, AIG continued to implement its plans to remediate the material weaknesses, and adjusted these plans as appropriate.

AIG's remediation efforts were governed by a Steering Committee, under the direction of AIG's Chief Risk Officer and also including AIG's Chief Executive Officer, Chief Financial Officer and Comptroller. The status of remediation of each material weakness was reviewed with the Audit Committee and this Committee was advised of issues encountered and key decisions reached by AIG management relating to the remediation efforts.

As of December 31, 2006 and as described under Remediation of Material Weaknesses in Internal Control Over Financial Reporting below, the material weaknesses relating to the controls over certain balance sheet reconciliations and the controls over the accounting for certain derivative transactions were remediated, and the material weakness relating to the controls over income tax accounting was not fully remediated.

As a result of the remaining material weakness in internal control over financial reporting relating to income tax accounting, described more fully below, AIG's Chief Executive Officer and Chief Financial Officer concluded that, as of December 31, 2006, AIG's disclosure controls and procedures were ineffective.

Notwithstanding the existence of this remaining material weakness, AIG believes that the consolidated financial statements in this Annual Report on Form 10-K fairly present, in all material respects, AIG's financial condition as of December 31, 2006 and 2005, and results of its operations and cash flows for the years ended December 31, 2006, 2005 and 2004, in conformity with U.S. generally accepted accounting principles (GAAP).

Management's Report on Internal Control Over Financial Reporting

Management of AIG is responsible for establishing and maintaining adequate internal control over financial reporting. AIG's internal control over financial reporting is a process, under the supervision of AIG's Chief Executive Officer and Chief Financial Officer, designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of AIG's financial statements for external purposes in accordance with GAAP.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions or that the degree of compliance with the policies or procedures may deteriorate.

AIG management conducted an assessment of the effectiveness of AIG's internal control over financial reporting as of December 31, 2006 based on the criteria established in *Internal Control — Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO).

A material weakness is a control deficiency, or a combination of control deficiencies, that results in more than a remote likelihood that a material misstatement of AIG's annual or interim financial statements will not be prevented or detected. AIG management has concluded that, as of December 31, 2006, the material weakness relating to the controls over income tax accounting was not fully remediated.

Controls over income tax accounting: AIG did not maintain effective controls over the determination and reporting of certain components of the provision for income taxes and related income tax balances. Specifically, AIG did not maintain effective controls to review and monitor the accuracy of the components of the income tax provision calculations and related income tax balances and to monitor the differences between the income tax basis and the financial reporting basis of assets and liabilities to effectively reconcile the differences to the deferred income tax balances. These control deficiencies resulted in adjustments to income tax expense, income taxes payable and deferred income tax asset and liability accounts in the 2006 annual and interim consolidated financial statements. Furthermore, these control deficiencies could result in a material misstatement of the annual or interim

AIG consolidated financial statements that would not be prevented or detected. Accordingly, AIG management has concluded that these control deficiencies constitute a material weakness.

As a result of the material weakness in internal control over financial reporting described above, AIG management has concluded that, as of December 31, 2006, AIG's internal control over financial reporting was not effective based on the criteria in *Internal Control — Integrated Framework* issued by the COSO.

Management's assessment of the effectiveness of AIG's internal control over financial reporting as of December 31, 2006 has been audited by PricewaterhouseCoopers LLP, an independent registered public accounting firm, as stated in their report, which is included in this Annual Report on Form 10-K.

Remediation of Material Weaknesses in Internal Control Over Financial Reporting

Throughout 2006 and continuing in 2007, AIG has been actively engaged in the implementation of remediation efforts to address the three material weaknesses in existence at December 31, 2005. These remediation efforts, outlined below, are specifically designed to address the material weaknesses identified by AIG management. As a result of its assessment of the effectiveness of internal control over financial reporting, AIG management determined that as of December 31, 2006, two material weaknesses, relating to the controls over certain balance sheet reconciliations and the controls over the accounting for certain derivative transactions, had been remediated, but the material weakness relating to the controls over income tax accounting had not been remediated.

Controls over certain balance sheet reconciliations: As of December 31, 2005, AIG did not maintain effective controls to ensure the accuracy of certain balance sheet accounts in certain key segments of AIG's operations, principally in the Domestic Brokerage Group (DBG). Specifically, accounting personnel did not perform timely reconciliations and did not properly resolve reconciling items for premium receivables, reinsurance recoverables and intercompany accounts.

During 2006, AIG management developed and implemented a corporate-wide accounting policy on balance sheet reconciliations, which augments the corporate guidelines on balance sheet reconciliations that were released in 2005. The policy requires all reporting units to perform timely reconciliations of their balance sheet accounts including the resolution of reconciling items and the evaluation of exposure.

AIG reporting units, including DBG, have been performing reconciliations of their accounts consistent with this policy. Implementation of the new policy was supplemented with dedicated training sessions, a self-assessment process and the continued addition of qualified staff to monitor on-going compliance with the new policy.

AIG continues to develop further enhancements to its controls over certain balance sheet reconciliations. Based upon the significant actions taken and the testing and evaluation of the effectiveness of the controls, AIG management has concluded that remediation of the material weakness in AIG's controls over certain balance sheet reconciliations had been achieved as of December 31, 2006.

Controls over the accounting for certain derivative transactions: As of December 31, 2005, AIG did not maintain effective controls over accounting for certain derivative transactions and related assets and liabilities under FAS 133. In particular, AIG did not maintain effective controls over the evaluation and documentation of whether certain derivative transactions qualified under GAAP for hedge accounting.

During 2006, AIG management implemented effective controls over accounting for derivative transactions. An important element of this implementation was the hiring in key staff positions of additional professionals with expertise in derivatives and hedge accounting.

AIG management has established a new corporate team with the responsibility and authority for overseeing and monitoring the application of hedge accounting throughout AIG. This team, staffed with accounting and quantitative professionals with extensive experience in dealing with derivative accounting matters, is responsible to ensure that the application of hedge accounting by AIG or its subsidiaries is in compliance with FAS 133 and AIG's accounting policies. As part of this activity, both enhancements to existing systems and investments in new applications were made to automate certain processes with respect to the application of hedge accounting and to reduce reliance on manual procedures.

Based upon the significant actions taken and the testing and evaluation of the effectiveness of the controls, AIG management has concluded that remediation of the material weakness in AIG's controls over the accounting for certain derivative transactions had been achieved as of December 31, 2006.

Continuing Remediation

Controls over income tax accounting: As of December 31, 2005, AIG did not maintain effective controls over the determination and reporting of certain components of the provision for income taxes and related income tax balances. During 2006, AIG management took the following actions to remediate this material weakness:

- Continued focus on implementing and testing of standard key controls globally,
- Continued focus on reconciling, evaluating and monitoring of historical balance sheet income tax accounts as well as more detailed financial statement exposure analysis,
- Implementation of a global income tax accounting reporting tool,
- Hiring of additional qualified staff including a new Director of Taxes, as well as Tax Managers and Tax Accountants at designated business units and Corporate, and
- Development and dissemination of income tax accounting training and education programs at the Corporate and business unit levels utilizing site visits and training conferences.

Notwithstanding these significant efforts towards remediation of the material weakness in controls over income tax accounting, implementation and testing of the standard key controls, as well

as procedures and processes, were not completed within all business units as of December 31, 2006. As a result, the effectiveness and sustainability of controls and processes could not be assured as of that date.

Furthermore, during 2006, the reconciliation, evaluation and monitoring of historical balance sheet income tax accounts identified errors in the income tax balances. The errors identified to date were not material; therefore, they were recorded and disclosed in the period in which they were identified. AIG has not completed the necessary reconciliation and evaluation of all historical balance sheet income tax accounts; accordingly, additional work is required in the analysis of the remaining prior year balances. AIG cannot predict the outcome of the review and analysis described above or estimate the potential adjustments related to these remediation activities. However, in the opinion of AIG management and based upon information currently known, resolution of these historical balance sheet income tax accounts is not likely to have a material adverse effect on AIG's consolidated financial condition, but it is possible that the effect could be material to AIG's consolidated results of operations for an individual reporting period.

Remediation of the material weakness in controls over income tax accounting requires completing the implementation of key controls in the applicable AIG business units and testing them after they are in place to validate their effectiveness and sustainability. Due to the nature of these requirements and the need to complete the reconciliation of certain historical balances, no assurance can be given as to the specific timing of the remediation of this material weakness. AIG management continues to assign the highest priority to AIG's remediation efforts in this area, with the goal of remediating this material weakness by year-end 2007.

While the material weakness in controls over income tax accounting was not remediated, due to the substantive alternative procedures performed and compensating controls in place, AIG believes that the consolidated financial statements present fairly in all material respects AIG's financial condition as of December 31, 2006 and 2005, and results of its operations and cash flows for the years ended December 31, 2006, 2005 and 2004, in conformity with GAAP.

AIG recognizes that improvement in its internal controls over financial reporting and consolidation processes, as well as those over investment accounting, is essential. Over time, AIG intends to reduce its reliance on the manual controls that have been established. AIG is currently developing new systems and processes which will allow it to rely on front end detection and preventative controls which will be more sustainable over the long term. AIG recognizes that, to accomplish its goals, further strengthening and investing are needed in financial personnel, as well as in systems and processes. AIG is committed to making the investments necessary to make these improvements.

Changes in Internal Controls over Financial Reporting

Changes in AIG's internal control over financial reporting during the quarter ended December 31, 2006 that have materially affected, or are reasonably likely to materially affect, AIG's internal control over financial reporting have been described above.

Item 9B.
Other Information

None.

Part III

Item 10.
Directors, Executive Officers and Corporate Governance

Except for the information provided in Part I under the heading ''Directors and Executive Officers of AIG'', this item, including information regarding AIG's audit committee and audit committee financial expert, any material changes to the procedures by which security holders may recommend nominees to AIG's board of directors, if any, and information relating to AIG's code of ethics that applies to its directors, executive officers and senior financial officers, is omitted because a definitive proxy statement which involves the election of directors will be filed with the SEC not later than 120 days after the close of the fiscal year pursuant to Regulation 14A.

Item 11.
Executive Compensation

This item is omitted because a definitive proxy statement which involves the election of directors will be filed with the SEC not later than 120 days after the close of the fiscal year pursuant to Regulation 14A.

Item 12.
Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters

This item is omitted because a definitive proxy statement which involves the election of directors will be filed with the SEC not later than 120 days after the close of the fiscal year pursuant to Regulation 14A.

Item 13.
Certain Relationships and Related Transactions, and Director Independence

This item is omitted because a definitive proxy statement which involves the election of directors will be filed with the SEC not later than 120 days after the close of the fiscal year pursuant to Regulation 14A.

Item 14.
Principal Accountant Fees and Services

This item is omitted because a definitive proxy statement which involves the election of directors will be filed with the SEC not later than 120 days after the close of the fiscal year pursuant to Regulation 14A.

Part IV

Item 15.
Exhibits and Financial Statement Schedules

(a) Financial Statements and Schedules. See accompanying Index to Financial Statements.

(b) Exhibits. See accompanying Exhibit Index.

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, as amended, the Registrant has duly caused this Annual Report on Form 10-K to be signed on its behalf by the undersigned, thereunto duly authorized, in the City of New York and State of New York, on the 1st of March, 2007.

AMERICAN INTERNATIONAL GROUP, INC.

By /s/ MARTIN J. SULLIVAN
(Martin J. Sullivan, President and Chief Executive Officer)

KNOW ALL PERSONS BY THESE PRESENTS, that each person whose signature appears below constitutes and appoints Martin J. Sullivan and Steven J. Bensinger, and each of them severally, his or her true and lawful attorney-in-fact, with full power of substitution and resubstitution, to sign in his or her name, place and stead, in any and all capacities, to do any and all things and execute any and all instruments that such attorney may deem necessary or advisable under the Securities Exchange Act of 1934, as amended, and any rules, regulations and requirements of the U.S. Securities and Exchange Commission in connection with this Annual Report on Form 10-K and any and all amendments hereto, as fully for all intents and purposes as he or she might or could do in person, and hereby ratifies and confirms all said attorneys-in-fact and agents, each acting alone, and his or her substitute or substitutes, may lawfully do or cause to be done by virtue hereof.

Pursuant to the requirements of the Securities Exchange Act of 1934, as amended, this Annual Report on Form 10-K has been signed below by the following persons in the capacities indicated on the 1st of March, 2007.

Signature	Title
/s/ MARTIN J. SULLIVAN (Martin J. Sullivan)	President, Chief Executive Officer and Director (Principal Executive Officer)
/s/ STEVEN J. BENSINGER (Steven J. Bensinger)	Executive Vice President and Chief Financial Officer (Principal Financial Officer)
/s/ DAVID L. HERZOG (David L. Herzog)	Senior Vice President and Comptroller (Principal Accounting Officer)
/s/ MARSHALL A. COHEN (Marshall A. Cohen)	Director
/s/ MARTIN S. FELDSTEIN (Martin S. Feldstein)	Director
/s/ ELLEN V. FUTTER (Ellen V. Futter)	Director
/s/ STEPHEN L. HAMMERMAN (Stephen L. Hammerman)	Director
/s/ RICHARD C. HOLBROOKE (Richard C. Holbrooke)	Director
/s/ FRED H. LANGHAMMER (Fred H. Langhammer)	Director

Signature	Title
/s/ George L. Miles, Jr. (George L. Miles, Jr.)	Director
/s/ Morris W. Offit (Morris W. Offit)	Director
/s/ James F. Orr III (James F. Orr III)	Director
/s/ Virginia M. Rometty (Virginia M. Rometty)	Director
/s/ Michael H. Sutton (Michael H. Sutton)	Director
/s/ Edmund S.W. Tse (Edmund S.W. Tse)	Director
/s/ Robert B. Willumstad (Robert B. Willumstad)	Director
/s/ Frank G. Zarb (Frank G. Zarb)	Director

EXHIBIT INDEX

Exhibit Number	Description	Location
2	Plan of acquisition, reorganization, arrangement, liquidation or succession	
	Agreement and Plan of Merger, dated as of May 11, 2001, among American International Group, Inc., Washington Acquisition Corporation and American General Corporation	Incorporated by reference to Exhibit 2.1(i)(a) to AIG's Registration Statement on Form S-4 (File No. 333-62688).
3(i)(a)	Restated Certificate of Incorporation of AIG	Incorporated by reference to Exhibit 3(i) to AIG's Annual Report on Form 10-K for the year ended December 31, 1996 (File No. 1-8787).
3(i)(b)	Certificate of Amendment of Certificate of Incorporation of AIG, filed June 3, 1998	Incorporated by reference to Exhibit 3(i) to AIG's Quarterly Report on Form 10-Q for the quarter ended June 30, 1998 (File No. 1-8787).
3(i)(c)	Certificate of Merger of SunAmerica Inc. with and into AIG, filed December 30, 1998 and effective January 1, 1999	Incorporated by reference to Exhibit 3(i) to AIG's Annual Report on Form 10-K for the year ended December 31, 1998 (File No. 1-8787).
3(i)(d)	Certificate of Amendment of Certificate of Incorporation of AIG, filed June 5, 2000	Incorporated by reference to Exhibit 3(i)(c) to AIG's Registration Statement on Form S-4 (File No. 333-45828).
3(ii)	Amended and Restated By-laws of AIG	Incorporated by reference to Exhibit 3(ii) to AIG's Current Report on Form 8-K filed with the SEC on January 19, 2007 (File No. 1-8787).
4	Instruments defining the rights of security holders, including indentures	Certain instruments defining the rights of holders of long-term debt securities of AIG and its subsidiaries are omitted pursuant to Item 601(b)(4)(iii) of Regulation S-K. AIG hereby undertakes to furnish to the Commission, upon request, copies of any such instruments.
9	Voting Trust Agreement	None.
10	Material contracts*	
	(1) AIG 1969 Employee Stock Option Plan and Agreement Form	Filed as exhibit to AIG's Registration Statement (File No. 2-44043) and incorporated herein by reference.
	(2) AIG 1972 Employee Stock Option Plan	Filed as exhibit to AIG's Registration Statement (File No. 2-44702) and incorporated herein by reference.
	(3) AIG 1972 Employee Stock Purchase Plan	Filed as exhibit to AIG's Registration Statement (File No. 2-44043) and incorporated herein by reference.
	(4) AIG 1984 Employee Stock Purchase Plan	Filed as exhibit to AIG's Registration Statement (File No. 2-91945) and incorporated herein by reference.
	(5) AIG Amended and Restated 1996 Employee Stock Purchase Plan	Filed as exhibit to AIG's Definitive Proxy Statement dated April 4, 2003 (File No. 1-8787) and incorporated herein by reference.
	(6) AIG 2003 Japan Employee Stock Purchase Plan	Incorporated by reference to Exhibit 4 to AIG's Registration Statement on Form S-8 (File No. 333-111737).
	(7) AIG 1977 Stock Option and Stock Appreciation Rights Plan	Filed as exhibit to AIG's Registration Statement (File No. 2-59317) and incorporated herein by reference.
	(8) AIG 1982 Employee Stock Option Plan	Filed as exhibit to AIG's Registration Statement (File No. 2-78291) and incorporated herein by reference.
	(9) AIG 1987 Employee Stock Option Plan	Filed as exhibit to AIG's Definitive Proxy Statement dated April 6, 1987 (File No. 0-4652) and incorporated herein by reference.
	(10) AIG 1991 Employee Stock Option Plan	Filed as exhibit to AIG's Definitive Proxy Statement dated April 4, 1997 (File No. 1-8787) and incorporated herein by reference.

** All material contracts are management contracts or compensatory plans or arrangements, except items (66), (67), (68) and (69).*

Exhibit Number		Description	Location
	(11)	AIG Amended and Restated 1999 Stock Option Plan	Filed as exhibit to AIG's Definitive Proxy Statement dated April 4, 2003 (File No. 1-8787) and incorporated herein by reference.
	(12)	Form of Stock Option Grant Agreement under the AIG Amended and Restated 1999 Stock Option Plan	Incorporated by reference to Exhibit 10(a) to AIG's Quarterly Report on Form 10-Q for the quarter ended September 30, 2004 (File No. 1-8787).
	(13)	AIG Amended and Restated 2002 Stock Incentive Plan	Incorporated by reference to Exhibit 4(a) to AIG's Registration Statement on Form S-8 (File No. 333-101967).
	(14)	Form of Restricted Stock Unit Award Agreement under the AIG Amended and Restated 2002 Stock Incentive Plan	Incorporated by reference to Exhibit 10(b) to AIG's Quarterly Report on Form 10-Q for the quarter ended September 30, 2004 (File No. 1-8787).
	(15)	AIG Executive Deferred Compensation Plan	Incorporated by reference to Exhibit 4(a) to AIG's Registration Statement on Form S-8 (File No. 333-101640).
	(16)	AIG Supplemental Incentive Savings Plan	Incorporated by reference to Exhibit 4(b) to AIG's Registration Statement on Form S-8 (File No. 333-101640).
	(17)	AIG Director Stock Plan	Filed as an exhibit to AIG's Definitive Proxy Statement dated April 5, 2004 (File No. 1-8787) and incorporated herein by reference.
	(18)	AIG Chief Executive Officer Annual Compensation Plan	Filed as an exhibit to AIG's Definitive Proxy Statement dated April 5, 2004 (File No. 1-8787) and incorporated herein by reference.
	(19)	AIRCO 1972 Employee Stock Option Plan	Incorporated by reference to AIG's Joint Proxy Statement and Prospectus (File No. 2-61994).
	(20)	AIRCO 1977 Stock Option and Stock Appreciation Rights Plan	Incorporated by reference to AIG's Joint Proxy Statement and Prospectus (File No. 2-61994).
	(21)	Purchase Agreement between AIA and Mr. E.S.W. Tse	Incorporated by reference to Exhibit 10(l) to AIG's Annual Report on Form 10-K for the year ended December 31, 1997 (File No. 1-8787).
	(22)	Retention and Employment Agreement between AIG and Jay S. Wintrob	Incorporated by reference to Exhibit 10(m) to AIG's Annual Report on Form 10-K for the year ended December 31, 1998 (File No. 1-8787).
	(23)	SunAmerica Inc. 1988 Employee Stock Plan	Incorporated by reference to Exhibit 4(a) to AIG's Registration Statement on Form S-8 (File No. 333-70069).
	(24)	SunAmerica 1997 Employee Incentive Stock Plan	Incorporated by reference to Exhibit 4(b) to AIG's Registration Statement on Form S-8 (File No. 333-70069).
	(25)	SunAmerica Nonemployee Directors' Stock Option Plan	Incorporated by reference to Exhibit 4(c) to AIG's Registration Statement on Form S-8 (File No. 333-70069).
	(26)	SunAmerica 1995 Performance Stock Plan	Incorporated by reference to Exhibit 4(d) to AIG's Registration Statement on Form S-8 (File No. 333-70069).
	(27)	SunAmerica Inc. 1998 Long-Term Performance-Based Incentive Plan For the Chief Executive Officer	Incorporated by reference to Exhibit 4(e) to AIG's Registration Statement on Form S-8 (File No. 333-70069).
	(28)	SunAmerica Inc. Long-Term Performance-Based Incentive Plan Amended and Restated 1997	Incorporated by reference to Exhibit 4(f) to AIG's Registration Statement on Form S-8 (File No. 333-70069).
	(29)	SunAmerica Five Year Deferred Cash Plan	Incorporated by reference to Exhibit 4(a) to AIG's Registration Statement on Form S-8 (File No. 333-31346).
	(30)	SunAmerica Executive Savings Plan	Incorporated by reference to Exhibit 4(b) to AIG's Registration Statement on Form S-8 (File No. 333-31346).

Exhibit Number		Description	Location
	(31)	HSB Group, Inc. 1995 Stock Option Plan	Incorporated by reference to Exhibit 10(iii)(f) to HSB's Annual Report on Form 10-K for the year ended December 31, 1999 (File No. 1-13135).
	(32)	HSB Group, Inc. 1985 Stock Option Plan	Incorporated by reference to Exhibit 10(iii)(a) HSB's Quarterly Report on Form 10-Q for the quarter ended September 30, 1998 (File No. 1-13135).
	(33)	HSB Group, Inc. Employee's Thrift Incentive Plan	Incorporated by reference to Exhibit 4(i)(c) to The Hartford Steam Boiler Inspection and Insurance Company's Registration Statement on Form S-8 (File No. 33-36519).
	(34)	American General Corporation 1984 Stock and Incentive Plan	Incorporated by reference to Exhibit 10.1 to American General Corporation's Quarterly Report on Form 10-Q for the quarter ended June 30, 1998 (File No. 1-7981).
	(35)	Amendment to American General Corporation 1984 Stock and Incentive Plan (January 2000)	Incorporated by reference to Exhibit 10.2 to American General Corporation's Annual Report on Form 10-K for the year ended December 31, 1999 (File No. 1-7981).
	(36)	American General Corporation 1994 Stock and Incentive Plan (January 2000)	Incorporated by reference to Exhibit 10.2 to American General Corporation's Quarterly Report on Form 10-Q for the quarter ended June 30, 1998 (File No. 1-7981).
	(37)	Amendment to American General Corporation 1994 Stock and Incentive Plan (January 1999)	Incorporated by reference to Exhibit 10.4 to American General Corporation's Annual Report on Form 10-K for the year ended December 31, 1999 (File No. 1-7981).
	(38)	Amendment to American General Corporation 1994 Stock and Incentive Plan (January 2000)	Incorporated by reference to Exhibit 10.5 to American General Corporation's Annual Report on Form 10-K for the year ended December 31, 1999 (File No. 1-7981).
	(39)	Amendment to American General Corporation 1994 Stock and Incentive Plan (November 2000)	Incorporated by reference to Exhibit 10.1 to American General Corporation's Quarterly Report on Form 10-Q for the quarter ended September 30, 2000 (File No. 1-7981).
	(40)	American General Corporation 1997 Stock and Incentive Plan	Incorporated by reference to Exhibit 10.3 to American General Corporation's Quarterly Report on Form 10-Q for the quarter ended June 30, 1998 (File No. 1-7981).
	(41)	Amendment to American General Corporation 1997 Stock and Incentive Plan (January 1999)	Incorporated by reference to Exhibit 10.7 to American General Corporation's Annual Report on Form 10-K for the year ended December 31, 1999 (File No. 1-7981).
	(42)	Amendment to American General Corporation 1997 Stock and Incentive Plan (November 2000)	Incorporated by reference to Exhibit 10.2 to American General Corporation's Quarterly Report on Form 10-Q for the quarter ended September 30, 2000 (File No. 1-7981).
	(43)	American General Corporation 1999 Stock and Incentive Plan	Incorporated by reference to Exhibit 10.4 to American General Corporation's Annual Report on Form 10-K for the year ended December 31, 1998 (File No. 1-7981).
	(44)	Amendment to American General Corporation 1999 Stock and Incentive Plan (January 1999)	Incorporated by reference to Exhibit 10.9 to American General Corporation's Annual Report on Form 10-K for the year ended December 31, 1999 (File No. 1-7981).
	(45)	Amendment to American General Corporation 1999 Stock and Incentive Plan (November 2000)	Incorporated by reference to Exhibit 10.3 to American General Corporation's Quarterly Report on Form 10-Q for the quarter ended September 30, 2000 (File No. 1-7981).
	(46)	Amended and Restated American General Corporation Deferred Compensation Plan (12/11/00)	Incorporated by reference to Exhibit 10.13 to American General Corporation's Annual Report on Form 10-K for the year ended December 31, 2000 (File No. 1-7981).
	(47)	Amended and Restated Restoration of Retirement Income Plan for Certain Employees Participating in the Restated American General Retirement Plan (Restoration of Retirement Income Plan) (12/31/98)	Incorporated by reference to Exhibit 10.14 to American General Corporation's Annual Report on Form 10-K for the year ended December 31, 2000 (File No. 1-7981).
	(48)	Amended and Restated American General Supplemental Thrift Plan (12/31/98)	Incorporated by reference to Exhibit 10.15 to American General Corporation's Annual Report on Form 10-K for the year ended December 31, 2000 (File No. 1-7981).

Exhibit Number		Description	Location
	(49)	American General Employees' Thrift and Incentive Plan (restated July 1, 2001)	Incorporated by reference to Exhibit 4(a) to AIG's Registration Statement on Form S-8 (File No. 333-68640).
	(50)	American General Agents' and Managers' Thrift and Incentive Plan (restated July 1, 2001)	Incorporated by reference to Exhibit 4(b) to AIG's Registration Statement on Form S-8 (File No. 333-68640).
	(51)	CommLoCo Thrift Plan (restated July 1, 2001)	Incorporated by reference to Exhibit 4(c) to AIG's Registration Statement on Form S-8 (File No. 333-68640).
	(52)	Western National Corporation 1993 Stock and Incentive Plan, as amended	Incorporated by reference to Exhibit 10.18 to Western National Corporation's Annual Report on Form 10-K for the year ended December 31, 1995 (File No. 1-12540).
	(53)	USLIFE Corporation 1991 Stock Option Plan, as amended	Incorporated by reference to USLIFE Corporation's Quarterly Report on Form 10-Q for the quarter ended September 30, 1995 (File No. 1-5683).
	(54)	Employment Agreement, Amendment to Employment Agreement, and Split-Dollar Agreement, including Assignment of Life Insurance Policy as Collateral, with Rodney O. Martin, Jr.	Incorporated by reference to Exhibit 10(xx) to AIG's Annual Report on Form 10-K for the year ended December 31, 2002 (File No. 1-8787).
	(55)	Employment Arrangements with Richard W. Scott	
		(a) Employment Agreement	Incorporated by reference to Exhibit 10.3 to American General Corporation's Quarterly Report on Form 10-Q for the quarter ended March 31, 2000 (File No. 1-7981).
		(b) Change in Control Severance Agreement	Incorporated by reference to Exhibit 10.32 to American General Corporation's Annual Report on Form 10-K for the year ended December 31, 1999 (File No. 1-7981).
		(c) Amendment to Employment Arrangements	Incorporated by reference to Exhibit 10(zz)(iii) to AIG's Annual Report on Form 10-K for the year ended December 31, 2003 (File No. 1-8787).
	(56)	Letter from AIG to Martin J. Sullivan, dated March 16, 2005	Incorporated by reference to Exhibit 10.1 to AIG's Current Report on Form 8-K filed with the SEC on March 17, 2005 (File No. 1-8787).
	(57)	Letter from AIG to Steven J. Bensinger, dated March 16, 2005	Incorporated by reference to Exhibit 10.3 to AIG's Current Report on Form 8-K filed with the SEC on March 17, 2005 (File No. 1-8787).
	(58)	Employment Agreement between AIG and Martin J. Sullivan, dated as of June 27, 2005	Incorporated by reference to Exhibit 10(1) to AIG's Quarterly Report on Form 10-Q for the quarter ended March 31, 2005 (File No. 1-8787).
	(59)	Employment Agreement between AIG and Steven J. Bensinger, dated as of June 27, 2005	Incorporated by reference to Exhibit 10(3) to AIG's Quarterly Report on Form 10-Q for the quarter ended March 31, 2005 (File No. 1-8787).
	(60)	Executive Severance Plan, effective as of June 27, 2005	Incorporated by reference to Exhibit 10(4) to AIG's Quarterly Report on Form 10-Q for the quarter ended March 31, 2005 (File No. 1-8787).
	(61)	Assurance Agreement, by AIG in favor of eligible employees, dated as of June 27, 2005, relating to certain obligations of Starr International Company, Inc.	Incorporated by reference to Exhibit 10(6) to AIG's Quarterly Report on Form 10-Q for the quarter ended March 31, 2005 (File No. 1-8787).
	(62)	2005/2006 Deferred Compensation Profit Participation Plan	Incorporated by reference to Exhibit 10.1 to AIG's Current Report on Form 8-K filed with the SEC on September 26, 2005 (File No. 1-8787).
	(63)	Summary of Director Compensation	Incorporated by reference to Exhibit 10.1 to AIG's Current Report on Form 8-K filed with the SEC on November 22, 2005 (File No. 1-8787).
	(64)	AIG 2005 Senior Partners Plan	Incorporated by reference to Exhibit 10.1 to AIG's Current Report on Form 8-K filed with the SEC on December 20, 2005 (File No. 1-8787).

Exhibit Number	Description	Location
	(65) AIG Special Restricted Stock Unit Award Agreement with Steven J. Bensinger, dated January 6, 2006	Incorporated by reference to Exhibit 10.1 to AIG's Current Report on Form 8-K filed with the SEC on January 9, 2006 (File No. 1-8787).
	(66) Agreement with the United States Department of Justice, dated February 7, 2006	Incorporated by reference to Exhibit 10.1 to AIG's Current Report on Form 8-K filed with the SEC on February 9, 2006 (File No. 1-8787).
	(67) Final Judgment and Consent with the Securities and Exchange Commission, including the related complaint, dated February 9, 2006	Incorporated by reference to Exhibit 10.2 to AIG's Current Report on Form 8-K filed with the SEC on February 9, 2006 (File No. 1-8787).
	(68) Agreement between the Attorney General of the State of New York and AIG and its Subsidiaries, dated January 18, 2006	Incorporated by reference to Exhibit 10.3 to AIG's Current Report on Form 8-K filed with the SEC on February 9, 2006 (File No. 1-8787).
	(69) Stipulation with the State of New York Insurance Department, dated January 18, 2006	Incorporated by reference to Exhibit 10.4 to AIG's Current Report on Form 8-K filed with the SEC on February 9, 2006 (File No. 1-8787).
	(70) AIG Senior Partners Plan (amended and restated)	Incorporated by reference to Exhibit 10.1 to AIG's Current Report on Form 8-K filed with the SEC on July 21, 2006 (File No. 1-8787).
	(71) AIG Partners Plan	Incorporated by reference to Exhibit 10.2 to AIG's Current Report on Form 8-K filed with the SEC on May 22, 2006 (File No. 1-8787).
	(72) AIG Executive Incentive Plan	Incorporated by reference to Exhibit 10.1 to AIG's Current Report on Form 8-K filed with the SEC on May 22, 2006 (File No. 1-8787).
11	Statement re computation of per share earnings	Included in Note 11 of Notes to Consolidated Financial Statements.
12	Statements re computation of ratios	Filed herewith.
13	Annual report to security holders	Not required to be filed.
18	Letter re change in accounting principles	None.
21	Subsidiaries of the Registrant	Filed herewith.
23	Consent of PricewaterhouseCoopers LLP	Filed herewith.
24	Power of attorney	Included on the signature page hereof.
31	Rule 13a-14(a)/15d-14(a) Certifications	Filed herewith.
32	Section 1350 Certifications	Filed herewith.
99	Additional exhibits	None.

Computation of Ratios of Earnings to Fixed Charges

Exhibit 12

Years Ended December 31, *(in millions, except ratios)*	**2006**	2005	2004	2003	2002
Income before income taxes, minority interest and cumulative effect of accounting changes	**$21,687**	$15,213	$14,845	$11,907	$ 7,808
Less — Equity income of less than 50% owned companies	**188**	(129)	164	146	168
Add — Dividends from less than 50% owned companies	**28**	146	22	13	13
	21,527	15,488	14,703	11,774	7,653
Add — Fixed charges	**9,062**	7,663	6,049	5,762	4,893
Less — Capitalized interest	**59**	64	59	52	61
Income before income taxes, minority interest, cumulative effect of accounting changes and fixed charges	**$30,530**	$23,087	$20,693	$17,484	$12,485
Fixed charges:					
Interest costs	**$ 8,843**	$ 7,464	$ 5,860	$ 5,588	$ 4,725
Rental expense*	**219**	199	189	174	168
Total fixed charges	**$ 9,062**	$ 7,663	$ 6,049	$ 5,762	$ 4,893
Ratio of earnings to fixed charges	**3.37**	3.01	3.42	3.03	2.55
Secondary Ratio					
Interest credited to GIC and GIA policy and contract holders	**$ (5,128)**	$ (4,760)	$ (3,674)	$ (3,578)	$ (2,702)
Total fixed charges excluding interest credited to GIC and GIA policy and contract holders	**$ 3,934**	$ 2,903	$ 2,375	$ 2,184	$ 2,191
Secondary ratio of earnings to fixed charges	**6.46**	6.31	7.17	6.37	4.47

** The proportion deemed representative of the interest factor.*

The secondary ratio is disclosed for the convenience of fixed income investors and the rating agencies that serve them and is more comparable to the ratios disclosed by all issuers of fixed income securities. The secondary ratio removes interest credited to guaranteed investment contract (GIC) policyholders and guaranteed investment agreement (GIA) contractholders. Such interest expenses are also removed from earnings used in this calculation. GICs and GIAs are entered into by AIG's insurance subsidiaries, principally SunAmerica Life Insurance Company and AIG Financial Products Corp. and its subsidiaries, respectively. The proceeds from GICs and GIAs are invested in a diversified portfolio of securities, primarily investment grade bonds. The assets acquired yield rates greater than the rates on the related policyholders obligation or contract, with the intent of earning a profit from the spread.

Subsidiaries of Registrant

Exhibit 21

	Jurisdiction of Incorporation or Organization	Percentage of Voting Securities held by Immediate Parent[1]
American International Group, Inc.[2]	Delaware	[3]
AIG Capital Corporation	Delaware	100
AIG Capital India Private Limited	India	99[4]
AIG Global Asset Management Company (India) Private Limited	India	99[5]
AIG Consumer Finance Group, Inc.	Delaware	100
AIG Bank Polska S.A.	Poland	99.92
AIG Credit S.A.	Poland	100
Compania Financiera Argentina S.A.	Argentina	100
AIG Equipment Finance Holdings, Inc.	Delaware	100
AIG Commercial Equipment Finance, Inc.	Delaware	100
AIG Commercial Equipment Finance Company Canada	Canada	100
AIG Rail Services, Inc.	Delaware	100
AIG Finance Holdings, Inc.	New York	100
AIG Finance (Hong Kong) Limited	Hong Kong	100
AIG Global Asset Management Holdings Corp.	Delaware	100
AIG Asset Management Services, Inc.	Delaware	100
Brazos Capital Management, L.P.	Delaware	100
AIG Capital Partners, Inc.	Delaware	100
AIG Equity Sales Corp.	New York	100
AIG Global Investment Corp.	New Jersey	100
AIG Securities Lending Corp.	Delaware	100
AIG Global Real Estate Investment Corp.	Delaware	100
International Lease Finance Corporation	California	67.23[6]
AIG Credit Corp.	Delaware	100
A.I. Credit Consumer Discount Corp.	Pennsylvania	100
A.I. Credit Corp.	New Hampshire	100
AICCO, Inc.	Delaware	100
AICCO, Inc.	California	100
AIG Credit Corp. of Canada	Canada	100
Imperial Premium Funding, Inc.	Delaware	100
AIG Egypt Insurance Company, S.A.E.	Egypt	89.98
AIG Federal Savings Bank	USA	100
AIG Financial Advisor Services, Inc.	Delaware	100
AIG Financial Advisor Services (Europe), S.A.	Luxembourg	100
AIG Financial Products Corp.	Delaware	100
AIG Matched Funding Corp.	Delaware	100
Banque AIG	France	90[7]
AIG Funding, Inc.	Delaware	100
AIG Global Trade & Political Risk Insurance Company	New Jersey	100
AIG Israel Insurance Company Ltd.	Israel	100
AIG Life Holdings (International) LLC	Delaware	100
AIG Star Life Insurance Co., Ltd.	Japan	100
American International Reinsurance Company, Ltd.	Bermuda	100
AIG Life Edison Insurance Company	Japan	90[8]
American International Assurance Company, Limited	Hong Kong	100
American International Assurance Company (Australia) Limited	Australia	100
American International Assurance Company (Bermuda) Limited	Bermuda	100
American International Assurance Co. (Vietnam) Limited	Vietnam	100
Tata AIG Life Insurance Company Limited	India	26
Nan Shan Life Insurance Company, Ltd.	Taiwan	95
AIG Life Insurance Company	Delaware	79[9]
AIG Life Insurance Company of Puerto Rico	Puerto Rico	100
AIG Life Insurance Company (Switzerland) Ltd.	Switzerland	100
AIG Liquidity Corp.	Delaware	100

Subsidiaries of Registrant *Continued*

	Jurisdiction of Incorporation or Organization	Percentage of Voting Securities held by Immediate Parent[1]
AIG Private Bank Ltd.	Switzerland	100
AIG Property Casualty Insurance Group, Inc.	Delaware	100
AIG Commercial Insurance Group, Inc.	Delaware	100
AIG Aviation, Inc.	Georgia	100
AIG Casualty Company	Pennsylvania	100
AIG Risk Management, Inc.	New York	100
AIU Insurance Company	New York	52[10]
American Home Assurance Company	New York	100
AIG Domestic Claims, Inc.	Delaware	50[11]
AIG Hawaii Insurance Company	Hawaii	100
American Pacific Insurance Company	Hawaii	100
American International Insurance Company	New York	50[12]
AIG Advantage Insurance Company	Minnesota	100
American International Insurance Company of California	California	100
American International Insurance Company of New Jersey	New Jersey	100
American International Realty Corp.	Delaware	31.5[13]
Pine Street Real Estate Holdings Corp.	New Hampshire	31.47[14]
Transatlantic Holdings, Inc.	Delaware	33.34[15]
Transatlantic Reinsurance Company	New York	100
Putnam Reinsurance Company	New York	100
Trans Re Zurich	Switzerland	100
American International Surplus Lines Agency, Inc.	New Jersey	100
Audubon Insurance Company	Louisiana	100
Agency Management Corporation	Louisiana	100
The Gulf Agency, Inc.	Alabama	100
Audubon Indemnity Company	Mississippi	100
Commerce and Industry Insurance Company	New York	100
Commerce and Industry Insurance Company of Canada	Canada	100
The Insurance Company of the State of Pennsylvania	Pennsylvania	100
Landmark Insurance Company	California	100
National Union Fire Insurance Company of Pittsburgh, Pa	Pennsylvania	100
American International Specialty Lines Insurance Company	Alaska	70[16]
Lexington Insurance Company	Delaware	70[17]
AIG Centennial Insurance Company	Pennsylvania	100
AIG Auto Insurance Company of New Jersey	New Jersey	100
AIG Preferred Insurance Company	Pennsylvania	100
AIG Premier Insurance Company	Pennsylvania	100
AIG Indemnity Insurance Company	Pennsylvania	100
JI Accident & Fire Insurance Co. Ltd.	Japan	50
National Union Fire Insurance Company of Louisiana	Louisiana	100
National Union Fire Insurance Company of Vermont	Vermont	100
21st Century Insurance Group	California	33.03[18]
21st Century Casualty Company	California	100
21st Century Insurance Company	California	100
21st Century Insurance Company of the Southwest	Texas	100
Starr Excess Liability Insurance Company, Ltd.	Delaware	100
Starr Liability Insurance International Ltd.	Ireland	100
New Hampshire Insurance Company	Pennsylvania	100
AI Network Corporation	Delaware	100
AIG Europe, S.A.	France	70.48[19]
American International Pacific Insurance Company	Colorado	100
American International South Insurance Company	Pennsylvania	100
Granite State Insurance Company	Pennsylvania	100
Illinois National Insurance Co.	Illinois	100

Subsidiaries of Registrant *Continued*

	Jurisdiction of Incorporation or Organization	Percentage of Voting Securities held by Immediate Parent[1]
New Hampshire Indemnity Company, Inc.	Pennsylvania	100
AIG National Insurance Company, Inc.	New York	100
New Hampshire Insurance Services, Inc.	New Hampshire	100
Risk Specialists Companies, Inc.	Delaware	100
AIG Marketing, Inc.	Delaware	100
American International Insurance Company of Delaware	Delaware	100
Hawaii Insurance Consultants, Inc.	Hawaii	100
AIG Retirement Services, Inc.	Delaware	100
SunAmerica Life Insurance Company	Arizona	100
SunAmerica Investments, Inc.	Georgia	70[20]
AIG Advisor Group, Inc.	Maryland	100
Advantage Capital Corporation	New York	100
American General Securities Incorporated	Texas	100
FSC Securities Corporation	Delaware	100
Royal Alliance Associates, Inc.	Delaware	100
SunAmerica Securities, Inc.	Delaware	100
AIG SunAmerica Life Assurance Company	Arizona	100
AIG SunAmerica Asset Management Corp.	Delaware	100
AIG SunAmerica Capital Services, Inc.	Delaware	100
First SunAmerica Life Insurance Company	New York	100
AIG Technologies, Inc.	New Hampshire	100
AIG Trading Group, Inc.	Delaware	100
AIG International, Inc.	Delaware	100
AIGTI, Inc.	Delaware	100
AIU Holdings, LLC	Delaware	100
AIG Central Europe & CIS Insurance Holdings Corporation	Delaware	100
AIG Bulgaria Insurance and Reinsurance Company EAD	Bulgaria	100
AIG Czech Republic pojistovna, as	Czech Republic	100
AIG Kazakhstan Insurance Company, S.A.	Kazakhstan	88.87
AIG Memsa, Inc.	Delaware	100
AIG Hayleys Investment Holdings (Private) Ltd.	Sri Lanka	80
Hayleys AIG Insurance Company, Ltd.	Sri Lanka	100
AIG Iraq	Delaware	100
AIG Lebanon, S.A.L	Lebanon	100
AIG Libya, Inc.	Libya	100
AIG Sigora A.S	Turkey	100
Tata AIG General Insurance Company Limited	India	26
AIU Africa Holdings, Inc.	Delaware	100
AIG Kenya Insurance Company, Limited	Kenya	100
AIU North America, Inc.	New York	100
American General Corporation	Texas	100
AGC Life Insurance Company	Missouri	100
AIG Life Holdings (Canada), ULC	Canada	100
AIG Assurance Canada	Canada	100
AIG Life Insurance Company of Canada	Canada	100
AIG Life of Bermuda, Ltd.	Bermuda	100
American General Life and Accident Insurance Company	Tennessee	100
American General Life Insurance Company	Texas	100
AIG Annuity Insurance Company	Texas	100
AIG Enterprise Services, LLC	Delaware	100
American General Annuity Service Corporation	Texas	100
American General Life Companies, LLC	Delaware	100
American General Property Insurance Company	Tennessee	51.85[21]

Subsidiaries of Registrant *Continued*

	Jurisdiction of Incorporation or Organization	Percentage of Voting Securities held by Immediate Parent[1]
American General Property Insurance Company of Florida	Florida	100
The United State Life Insurance Company in the City of New York	New York	100
The Variable Annuity Life Insurance Company	Texas	100
VALIC Retirement Services Company	Texas	100
American General Assurance Company	Illinois	100
American General Indemnity Company	Illinois	100
American General Bancassurance Services, Inc.	Illinois	100
American General Finance, Inc.	Indiana	100
American General Auto Finance, Inc.	Delaware	100
American General Finance Corporation	Indiana	100
Merit Life Insurance Co.	Indiana	100
MorEquity, Inc.	Nevada	100
Wilmington Finance, Inc.	Delaware	100
Yosemite Insurance Company	Indiana	100
CommoLoCo, Inc.	Puerto Rico	100
American General Financial Services of Alabama, Inc.	Delaware	100
American General Investment Management Corporation	Delaware	100
American General Realty Investment Corporation	Texas	100
Knickerbocker Corporation	Texas	100
American International Life Assurance Company of New York	New York	77.52[22]
American International Underwriters Corporation	New York	100
American International Underwriters Overseas, Ltd.	Bermuda	100
A.I.G. Colombia Seguros Generales S.A.	Colombia	100
AIG Brasil Companhia de Seguros	Brazil	50
AIG Direct Marketing Company Ltd.	Taiwan	100
Central Insurance Company Limited	Taiwan	100
AIG Europe (Ireland) Limited	Ireland	100
AIG Europe (UK) Limited	England	100
AIG General Insurance (Thailand) Company Limited	Thailand	100
AIG General Insurance (Vietnam) Company Limited	Vietnam	100
AIG MEMSA Insurance Company Ltd.	United Arab Emirates	100
AIG Takaful B.S.C.	Bahrain	100
American International Insurance Company of Puerto Rico	Puerto Rico	100
American International Underwriters GmBH	Germany	100
La Meridional Compania Argentina de Seguros	Argentina	100
La Seguridad de Centroamerica Compania de Seguros S.A.	Guatemala	100
Richmond Insurance Company Limited	Bermuda	100
Underwriters Adjustment Company	Panama	100
American Life Insurance Company	Delaware	100
AIG Life (Bulgaria) Z.D.A.D.	Bulgaria	100
ALICO, S.A.	France	100
First American Polish Life Insurance and Reinsurance Company, S.A.	Poland	100
Inversiones Interamericana S.A. (Chile)	Chile	100
Pharaonic American Life Insurance Company	Egypt	71.63
Unibanco AIG Seguros S.A.	Brazil	47.80[23]
American Security Life Insurance Company, Ltd.	Lichtenstein	100
Delaware American Life Insurance Company	Delaware	100
HSB Group, Inc.	Delaware	100
The Hartford Steam Boiler Inspection and Insurance Company	Connecticut	100
The Hartford Steam Boiler Inspection and Insurance Company of Connecticut	Connecticut	100
HSB Engineering Insurance Limited	England	100
The Boiler Inspection and Insurance Company of Canada	Canada	100
Mt. Mansfield Company, Inc.	Vermont	100
The Philippine American Life and General Insurance Company	Philippines	99.78

Subsidiaries of Registrant *Continued*

	Jurisdiction of Incorporation or Organization	Percentage of Voting Securities held by Immediate Parent[1]
Pacific Union Assurance Company	California	100
Philam Equitable Life Assurance Company, Inc.	Philippines	95.31
Philam Insurance Company, Inc.	Philippines	100
United Guaranty Corporation	North Carolina	36.31[24]
A.I.G. Mortgage Holdings Israel, Ltd.	Israel	82.12
E.M.I.-Ezer Mortgage Insurance Company, Limited	Israel	100
AIG United Guaranty Agenzia DI Assicurazione S.R.L	Italy	100
AIG United Guaranty Insurance (Asia) Limited	Hong Kong	100
AIG United Guaranty Re, Ltd.	Ireland	100
United Guaranty Insurance Company	North Carolina	100
United Guaranty Mortgage Insurance Company	North Carolina	100
United Guaranty Mortgage Insurance Company Canada	Canada	100
United Guaranty Mortgage Insurance Company of North Carolina	North Carolina	100
United Guaranty Partners Insurance Company	Vermont	80
United Guaranty Residential Insurance Company	North Carolina	75.03[25]
United Guaranty Credit Insurance Company	North Carolina	100
United Guaranty Insurance Company of North Carolina	North Carolina	100
United Guaranty Mortgage Indemnity Company	North Carolina	100
United Guaranty Residential Insurance Company of North Carolina	North Carolina	100
United Guaranty Services, Inc.	North Carolina	100

(1) Percentages include directors' qualifying shares.

(2) All subsidiaries listed are consolidated in the accompanying financial statements. Certain subsidiaries have been omitted from the tabulation. The omitted subsidiaries, when considered in the aggregate as a single subsidiary, do not constitute a significant subsidiary.

(3) The common stock is owned approximately 14.1 percent by C.V. Starr & Co., Inc., Edward E. Matthews, Maurice R. and Corinne P. Greenberg Joint Tenancy Company, LLC, Starr International Company, Inc., The Maurice R. Greenberg and Corinne P. Greenberg Family Foundation, Inc. and the Universal Foundation, Inc.

(4) Also owned 1 percent by AIG Global Investment Corp.

(5) Also owned 1 percent by AIG Capital Corporation.

(6) Also owned 32.77 percent by National Union Fire Insurance Company of Pittsburgh, Pa.

(7) Also owned 10 percent by AIG Matched Funding Corp.

(8) Also owned 10 percent by a subsidiary of American Life Insurance Company.

(9) Also owned 21 percent by Commerce and Industry Insurance Company.

(10) Also owned 8 percent by The Insurance Company of the State of Pennsylvania, 32 percent by National Union Fire Insurance Company of the Pittsburgh, Pa., and 8 percent by AIG Casualty Company.

(11) Also owned 50 percent by The Insurance Company of the State of Pennsylvania.

(12) Also owned 25 percent by Commerce and Industry Insurance Company and 25 percent by AIU Insurance Company.

(13) Also owned by 11 other AIG subsidiaries.

(14) Also owned by 11 other AIG Subsidiaries.

(15) Also owned 25.85 percent by AIG.

(16) Also owned 20 percent by the Insurance Company of the State of Pennsylvania and 10 percent by AIG Casualty Company.

(17) Also owned 20 percent by the Insurance Company of the State of Pennsylvania and 10 percent by AIG Casualty Company.

(18) Also owned 16.85 percent by American Home Assurance Company, 6.34 percent by Commerce and Industry Insurance Company and 6.34 percent by New Hampshire Insurance Company.

(19) 100 percent held together with AIG companies.

(20) Also owned 30 percent by AIG Retirement Services, Inc.

(21) Also owned 48.15 percent by American General Life and Accident Insurance Company.

(22) Also owned 22.48 percent by American Home Assurance Company.

(23) Also owned 1.7 percent by American International Underwriters Overseas, Ltd. and 0.48 percent by American Home Assurance Company.

(24) Also owned 45.88 percent by National Union Fire Insurance Company of Pittsburgh, Pa., 16.95% by New Hampshire Insurance Company and 0.86 percent by The Insurance Company of the State of Pennsylvania.

(25) Also owned 24.97 percent by United Guaranty Residential Insurance Company of North Carolina.

Consent of Independent Registered Public Accounting Firm

Exhibit 23

We hereby consent to the incorporation by reference in the Registration Statements on Form S-8 and Form S-3 (No. 2-45346, No. 2-75875, No. 2-78291, No. 2-91945, No. 33-18073, No. 33-57250, No. 333-48639, No. 333-58095, No. 333-70069, No. 333-83813, No. 333-31346, No. 333-39976, No. 333-45828, No. 333-50198, No. 333-52938, No. 333-68640, No. 333-74187, No. 333-101640, No. 333-101967, No. 333-108466, No. 333-111737, No. 333-115911, No. 333-106040 and No. 333-132561) of American International Group, Inc. of our report dated March 1, 2007, relating to the financial statements, financial statement schedules, management's assessment of the effectiveness of internal control over financial reporting and the effectiveness of internal control over financial reporting, which appears in this Annual Report on Form 10-K.

PricewaterhouseCoopers LLP

New York, New York
March 1, 2007

Exhibit 31

CERTIFICATIONS

I, Martin J. Sullivan, certify that:

1. I have reviewed this Annual Report on Form 10-K of American International Group, Inc.;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:

(a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

(b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

(c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

(d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):

(a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

(b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: March 1, 2007

/s/ Martin J. Sullivan

Martin J. Sullivan
President and Chief Executive Officer

CERTIFICATIONS

I, Steven J. Bensinger, certify that:

1. I have reviewed this Annual Report on Form 10-K of American International Group, Inc.;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:

(a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

(b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

(c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

(d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):

(a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

(b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: March 1, 2007

/s/ Steven J. Bensinger

Steven J. Bensinger
Executive Vice President and Chief Financial Officer

Exhibit 32

CERTIFICATION

In connection with this Annual Report on Form 10-K of American International Group, Inc. (the ''Company'') for the year ended December 31, 2006, as filed with the Securities and Exchange Commission on the date hereof (the ''Report''), I, Martin J. Sullivan, President and Chief Executive Officer of the Company, certify, pursuant to 18 U.S.C. Section 1350, that to my knowledge:

(1) The Report fully complies with the requirements of Section 13(a) or 15(d), as applicable, of the Securities Exchange Act of 1934; and

(2) The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Date: March 1, 2007

/s/ MARTIN J. SULLIVAN

Martin J. Sullivan
President and Chief Executive Officer

The foregoing certification is being furnished solely pursuant to 18 U.S.C. Section 1350 and is not being filed as part of the Report or as a separate disclosure document.

CERTIFICATION

In connection with this Annual Report on Form 10-K of American International Group, Inc. (the ''Company'') for the year ended December 31, 2006, as filed with the Securities and Exchange Commission on the date hereof (the ''Report''), I, Steven J. Bensinger, Executive Vice President and Chief Financial Officer of the Company, certify, pursuant to 18 U.S.C. Section 1350, that to my knowledge:

(1) The Report fully complies with the requirements of Section 13(a) or 15(d), as applicable, of the Securities Exchange Act of 1934; and

(2) The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Date: March 1, 2007

/s/ Steven J. Bensinger

Steven J. Bensinger
Executive Vice President and Chief Financial Officer

The foregoing certification is being furnished solely pursuant to 18 U.S.C. Section 1350 and is not being filed as part of the Report or as a separate disclosure document.

Summary Of Investments – Other than Investments in Related Parties

Schedule I

At December 31, 2006 *(in millions)*	Cost*	Fair Value	Amount at which shown in the Balance Sheet
Fixed maturities:			
Bonds:			
United States government and government agencies and authorities	$ 5,415	$ 5,391	$ 5,391
States, municipalities and political subdivisions	81,236	82,802	82,085
Foreign governments	62,708	67,698	67,698
Public utilities	14,687	15,012	15,012
All other corporate	244,105	247,679	247,679
Total bonds	408,151	418,582	417,865
Total fixed maturities	408,151	418,582	417,865
Equity securities:			
Common stocks:			
Public utilities	286	372	372
Banks, trust and insurance companies	1,796	2,596	2,596
Industrial, miscellaneous and all other	21,292	24,692	24,692
Total common stocks	23,374	27,660	27,660
Preferred stocks	2,507	2,562	2,562
Total equity securities	25,881	30,222	30,222
Mortgage loans on real estate, policy and collateral loans	28,418	28,655	28,418
Financial services assets:			
Flight equipment primarily under operating leases, net of accumulated depreciation	39,875	–	39,875
Securities available for sale, at market value	45,912	47,205	47,205
Trading securities, at market value	–	5,031	5,031
Spot commodities	–	220	220
Unrealized gain on swaps, options and forward transactions	–	19,252	19,252
Trading assets	–	2,468	2,468
Securities purchased under agreements to resell, at contract value	33,702	–	33,702
Finance receivables, net of allowance	29,573	26,712	29,573
Securities lending collateral, at market value (approximates cost)	69,306	69,306	69,306
Other invested assets (approximates market value)	42,114	42,421	42,114
Short-term investments, at cost (approximates fair value)	25,249	25,249	25,249
Total investments	–	–	$790,500

* *Original cost of equity securities and, as to fixed maturities, original cost reduced by repayments and adjusted for amortization of premiums or accrual of discounts.*

Condensed Financial Information of Registrant
Balance Sheet – Parent Company Only

Schedule II

December 31, *(in millions)*	**2006**	2005
Assets:		
Cash	**$ 76**	$ 190
Invested assets	**7,346**	122
Carrying value of subsidiaries and partially-owned companies, at equity	**109,125**	90,723
Premiums and insurance balances receivable – net	**222**	186
Other assets	**3,767**	4,146
Total assets	**120,536**	95,367
Liabilities:		
Insurance balances payable	**21**	408
Due to affiliates – net	**1,841**	3,250
Notes and bonds payable	**8,917**	4,607
Loans payable	**700**	722
AIG MIP matched notes and bonds payable	**5,468**	—
Series AIGFP matched notes and bonds payable	**72**	—
Other liabilities	**1,840**	63
Total liabilities	**18,859**	9,050
Shareholders' equity:		
Common stock	**6,878**	6,878
Additional paid-in capital	**2,590**	2,339
Retained earnings	**84,996**	72,330
Accumulated other comprehensive income	**9,110**	6,967
Treasury stock	**(1,897)**	(2,197)
Total shareholders' equity	**101,677**	86,317
Total liabilities and shareholders' equity	**$ 120,536**	$95,367

See Accompanying Notes to Financial Statements – Parent Company Only.

Statement of Income – Parent Company Only

Years Ended December 31, *(in millions)*	**2006**	2005	2004
Agency income (loss)	**$ 9**	$ 3	$ (8)
Financial services income	**531**	507	578
Asset management income (loss)	**34**	(3)	(11)
Dividend income from consolidated subsidiaries:			
Cash	**1,689**	1,958	1,938
Other	**–**	–	1
Dividend income from partially-owned companies	**11**	127	11
Equity in undistributed net income of consolidated subsidiaries and partially-owned companies	**13,308**	10,156	8,602
Other income (expenses) – net	**(1,371)**	(2,203)	(409)
Cumulative effect of an accounting change	**34**	–	–
Income before income taxes	**14,245**	10,545	10,702
Income taxes	**197**	68	863
Net income	**$ 14,048**	$10,477	$ 9,839

See Accompanying Notes to Financial Statements – Parent Company Only.

Condensed Financial Information of Registrant — *Continued*

Schedule II

Statement of Cash Flows — Parent Company Only

Years Ended December 31, *(in millions)*	**2006**	2005	2004
Cash flows from operating activities:			
Net income	**$14,048**	$10,477	$ 9,839
Adjustments to reconcile net income to net cash provided by operating activities:			
Noncash revenues, expenses, gains and losses included in income:			
Equity in undistributed net income of consolidated subsidiaries and partially-owned companies	**(13,308)**	(10,156)	(8,602)
Change in premiums and insurance balances receivable and payable — net	**(423)**	15	(12)
Foreign exchange transaction (gains) losses	**232**	—	—
Other — net	**(1,139)**	1,518	165
Total adjustments	**(14,638)**	(8,623)	(8,449)
Net cash provided by (used in) operating activities	**(590)**	1,854	1,390
Cash flows from investing activities:			
Purchase of investments	**(8,298)**	—	(107)
Sale of investments	**3,417**	—	200
Change in short-term investments	**414**	(598)	302
Contributions to subsidiaries and investments in partially-owned companies	**(3,017)**	(966)	270
Other — net	**(159)**	(117)	(19)
Net cash used in investing activities	**(7,643)**	(1,681)	646
Cash flows from financing activities:			
Notes, bonds and loans issued	**12,038**	2,101	—
Repayments of notes, bonds and loans	**(2,417)**	(607)	(400)
Issuance of treasury stock	**163**	82	158
Cash dividends paid to shareholders	**(1,638)**	(1,421)	(730)
Acquisition of treasury stock	**(20)**	(176)	(1,083)
Other — net	**(7)**	21	17
Net cash (used in) provided by financing activities	**8,119**	—	(2,038)
Change in cash	**(114)**	173	(2)
Cash at beginning of year	**190**	17	19
Cash at end of year	**$ 76**	$ 190	$ 17

NOTES TO FINANCIAL STATEMENTS — PARENT COMPANY ONLY

(1) Agency operations conducted in New York through the North American Division of AIU are included in the financial statements of the parent company.

(2) Certain accounts have been reclassified in the 2005 and 2004 financial statements to conform to their 2006 presentation.

(3) ''Equity in undistributed net income of consolidated subsidiaries and partially-owned companies'' in the accompanying Statement of Income — Parent Company Only — includes equity in income of the minority-owned insurance operations.

Supplementary Insurance Information

Schedule III

At December 31, 2006, 2005 and 2004 and for the years then ended

Segment *(in millions)*	Deferred Policy Acquisition Costs	Reserves for Losses and Loss Expenses, Future Policy Benefits[a]	Reserve for Unearned Premiums	Policy and Contract Claims[b]	Premium Revenue	Net Investment Income	Losses and Loss Expenses Incurred, Benefits	Amortization of Deferred Policy Acquisition Costs	Other Operating Expenses	Net Premiums Written
2006										
General Insurance	**$ 4,355**	**$ 79,999**	**$ 26,271**	**$ –**	**$ 43,451**	**$ 5,696**	**$ 28,052**	**$ 7,866**	**$ 2,876**	**$ 44,866**
Life Insurance & Retirement Services	**32,810**	**122,230**	**–**	**2,788**	**30,636**	**19,439**	**31,505**	**3,712**	**4,914**	**–**
Other	**70**	**–-**	**–**	**–**	**(4)**	**157**	**149**	**–**	**–**	**–**
	$ 37,235	**$ 202,229**	**$ 26,271**	**$ 2,788**	**$ 74,083**	**$ 25,292**	**$ 59,706**	**$ 11,578**	**$ 7,790**	**$ 44,866**
2005										
General Insurance	$ 4,048	$ 77,169	$24,243	$ –	$40,809	$ 4,031	$33,091	$ 7,365	$2,403	$41,872
Life Insurance & Retirement Services	28,106	108,807	–	2,473	29,400	18,134	30,467	3,328	4,677	–
	$32,154	$185,976	$24,243	$2,473	$70,209	$22,165	$63,558	$10,693	$7,080	$41,872
2004										
General Insurance	$ 3,998	$ 61,878	$23,400	$ –	$38,537	$ 3,196	$30,357	$ 6,301	$2,126	$40,623
Life Insurance & Retirement Services	25,080	104,740	–	2,435	28,088	15,269	27,855	3,514	4,108	–
	$ 29,078	$ 166,618	$ 23,400	$ 2,435	$ 66,625	$ 18,465	$ 58,212	$ 9,815	$ 6,234	$ 40,623

(a) Reserves for losses and loss expenses with respect to the General Insurance operations are net of discounts of $2.26 billion, $2.11 billion and $1.55 billion at December 31, 2006, 2005 and 2004, respectively.

(b) Reflected in insurance balances payable on the accompanying consolidated balance sheet.

Reinsurance

At December 31, 2006, 2005 and 2004 and for the years then ended

Schedule IV

(dollars in millions)	Gross Amount	Ceded to Other Companies	Assumed from Other Companies	Net Amount	Percent of Amount Assumed to Net
2006					
Life Insurance in-force	**$2,069,617**	**$408,970**	**$ 983**	**$1,661,630**	**0.1%**
Premiums:					
General Insurance	**$ 49,609**	**$ 11,414**	**$ 6,671**	**$ 44,866**	**14.9%**
Life Insurance & Retirement Services	**32,097**	**1,481**	**20**	**30,636***	**0.1**
Total premiums	**$ 81,706**	**$ 12,895**	**$ 6,691**	**$ 75,502**	**8.9%**
2005					
Life Insurance in-force	$1,838,337	$365,082	$14,496	$1,487,751	1.0%
Premiums:					
General Insurance	$ 46,689	$ 10,853	$ 6,036	$ 41,872	14.4%
Life Insurance & Retirement Services	30,637	1,317	80	29,400*	0.3
Total premiums	$ 77,326	$ 12,170	$ 6,116	$ 71,272	8.6%
2004					
Life Insurance in-force	$1,844,189	$344,036	$13,905	$1,514,058	0.9%
Premiums:					
General Insurance	$ 44,692	$ 11,423	$ 7,354	$ 40,623	18.1%
Life Insurance & Retirement Services	28,486	1,114	716	28,088*	2.5
Total premiums	$ 73,178	$ 12,537	$ 8,070	$ 68,711	11.7%

** Includes accident and health premiums of $7.11 billion, $6.51 billion and $5.63 billion in 2006, 2005 and 2004, respectively.*

Valuation and Qualifying Accounts

For the years ended December 31, 2006, 2005 and 2004

Schedule V

(in millions)	Balance, Beginning of Year	Additions: Charged to Costs and Expenses	Additions: Charge offs	Other Changes[a][b]	Balance, End of Year
2006					
Allowance for mortgage loans	**$ 54**	**$ 6**	**$ —**	**$ (5)**	**$ 55**
Allowance for collateral and guaranteed loans	**10**	**11**	**(11)**	**(1)**	**9**
Allowance for finance receivables	**670**	**495**	**(534)**	**106**	**737**
Allowance for premiums and insurances balances receivable	**871**	**240**	**(481)**	**126**	**756**
Allowance for reinsurance assets	**999**	**147**	**(381)**	**(229)**	**536**
Overhaul reserve[c]	**142**	**249**	**—**	**(146)**	**245**
2005					
Allowance for mortgage loans	$ 65	$ 1	$ (19)	$ 7	$ 54
Allowance for collateral and guaranteed loans	18	—	(7)	(1)	10
Allowance for finance receivables	571	435	(414)	78	670
Allowance for premiums and insurances balances receivable	561	418	(104)	(4)	871
Allowance for reinsurance assets	846	185	(49)	17	999
Overhaul reserve[c]	68	260	—	(186)	142
2004					
Allowance for mortgage loans	$ 68	$ 11	$ (9)	$ (5)	$ 65
Allowance for collateral and guaranteed loans	15	4	(2)	1	18
Allowance for finance receivables	562	389	(443)	63	571
Allowance for premiums and insurances balances receivable	485	147	(25)	(46)	561
Allowance for reinsurance assets	569	276	(11)	12	846
Overhaul reserve[c]	69	164	—	(165)	68

(a) Includes recoveries of amounts previously charged off and reclassifications to/from other accounts.

(b) Amounts for Overhaul reserve represent reimbursements to lessees for overhauls performed and amounts transferred to buyers for aircraft sold.

(c) Included in Other liabilities on the Consolidated Balance Sheet.

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

Form 10-Q

(Mark One)

☑ QUARTERLY REPORT UNDER SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended March 31, 2007

or

☐ TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the transition period from to

Commission File Number 1-8787

American International Group, Inc.

(Exact name of registrant as specified in its charter)

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

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

Former name, former address and former fiscal year, if changed since last report: None

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

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of accelerated filer and large accelerated filer in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer ☑ Accelerated filer ☐ Non-accelerated filer ☐

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes ☐ No ☑

As of April 30, 2007, there were 2,594,237,019 shares outstanding of the registrant's common stock.

TABLE OF CONTENTS

Part I – FINANCIAL INFORMATION

ITEM 1. Financial Statements (unaudited)

CONSOLIDATED BALANCE SHEET

(in millions) (unaudited)

	March 31, 2007	December 31, 2006
Assets:		
Investments and financial services assets:		
Fixed maturities:		
Bonds available for sale, at fair value (amortized cost: 2007 – $380,104; 2006 – $377,698) (includes hybrid financial instruments: 2007 – $568; 2006 – $522)	**$390,141**	$387,391
Bonds held to maturity, at amortized cost (fair value: 2007 – $22,066; 2006 – $22,154)	**21,414**	21,437
Bond trading securities, at fair value (cost: 2007 – $8,883; 2006 – $9,016)	**8,845**	9,037
Equity securities:		
Common stocks available for sale, at fair value (cost: 2007 – $10,791; 2006 – $10,662)	**14,457**	13,262
Common and preferred stocks trading, at fair value (cost: 2007 – $13,742; 2006 – $12,734)	**15,756**	14,421
Preferred stocks available for sale, at fair value (cost: 2007 – $2,625; 2006 – $2,485)	**2,703**	2,539
Mortgage loans on real estate, net of allowance (2007 – $57; 2006 – $55)	**18,228**	17,067
Policy loans	**7,521**	7,501
Collateral and guaranteed loans, net of allowance (2007 – $7; 2006 – $9)	**4,840**	3,850
Financial services assets:		
Flight equipment primarily under operating leases, net of accumulated depreciation (2007 – $9,233; 2006 – $8,835)	**41,345**	39,875
Securities available for sale, at fair value (cost: 2007 – $46,313; 2006 – $45,912)	**47,643**	47,205
Trading securities, at fair value	**5,369**	5,031
Spot commodities	**73**	220
Unrealized gain on swaps, options and forward transactions	**16,547**	19,252
Trade receivables	**3,883**	4,317
Securities purchased under agreements to resell, at contract value	**31,775**	31,853
Finance receivables, net of allowance (2007 – $707; 2006 – $737) (includes finance receivables held for sale: 2007 – $983; 2006 – $1,124)	**29,508**	29,573
Securities lending collateral, at fair value (which approximates cost)	**74,827**	69,306
Other invested assets	**44,167**	42,114
Short-term investments, at cost (approximates fair value)	**25,866**	25,249
Total investments and financial services assets	**804,908**	790,500
Cash	**1,702**	1,590
Investment income due and accrued	**6,170**	6,077
Premiums and insurance balances receivable, net of allowance (2007 – $777; 2006 – $756)	**19,731**	17,789
Reinsurance assets, net of allowance (2007 – $498; 2006 – $536)	**23,130**	23,355
Deferred policy acquisition costs	**37,691**	37,235
Investments in partially owned companies	**1,179**	1,101
Real estate and other fixed assets, net of accumulated depreciation (2007 – $5,612; 2006 – $5,525)	**4,898**	4,381
Separate and variable accounts	**73,971**	72,655
Goodwill	**8,687**	8,628
Other assets	**17,680**	16,103
Total assets	**$999,747**	$979,414

See Accompanying Notes to Consolidated Financial Statements.

CONSOLIDATED BALANCE SHEET *(continued)*

(in millions, except share data) (unaudited)

	March 31, 2007	December 31, 2006
Liabilities:		
Reserve for losses and loss expenses	**$ 81,135**	$ 79,999
Unearned premiums	**27,135**	26,271
Future policy benefits for life and accident and health insurance contracts	**123,806**	122,230
Policyholders' contract deposits	**246,301**	246,615
Other policyholders' funds	**8,476**	8,281
Commissions, expenses and taxes payable	**6,053**	5,305
Insurance balances payable	**4,537**	3,789
Funds held by companies under reinsurance treaties	**2,446**	2,602
Income taxes payable	**10,992**	9,546
Financial services liabilities:		
Borrowings under obligations of guaranteed investment agreements	**19,771**	20,664
Securities sold under agreements to repurchase, at contract value	**17,581**	19,677
Trade payables	**7,546**	6,174
Hybrid financial instrument liabilities, at fair value	**8,459**	8,856
Securities and spot commodities sold but not yet purchased, at market value	**4,056**	4,076
Unrealized loss on swaps, options and forward transactions	**9,679**	11,401
Trust deposits and deposits due to banks and other depositors	**4,245**	5,249
Commercial paper	**9,228**	8,208
Notes, bonds, loans and mortgages payable	**91,186**	87,602
Commercial paper	**4,149**	4,821
Notes, bonds, loans and mortgages payable	**19,185**	17,088
Junior subordinated debt	**3,793**	—
Liabilities connected to trust preferred stock	**1,440**	1,440
Separate and variable accounts	**73,971**	72,655
Securities lending payable	**75,913**	70,198
Minority interest	**8,166**	7,778
Other liabilities (includes hybrid financial instruments: 2007 – $42; 2006 – $111)	**27,343**	27,021
Total liabilities	**896,592**	877,546
Preferred shareholders' equity in subsidiary companies	**100**	191
Commitments and Contingent Liabilities (See Note 6)		
Shareholders' equity:		
Common stock, $2.50 par value; 5,000,000,000 shares authorized; shares issued 2007 and 2006 – 2,751,327,476	**6,878**	6,878
Additional paid-in capital	**2,674**	2,590
Payments advanced to purchase shares	**(2,851)**	—
Retained earnings	**88,493**	84,996
Accumulated other comprehensive income (loss)	**9,854**	9,110
Treasury stock, at cost; 2007 – 151,556,041; 2006 – 150,131,273 shares of common stock	**(1,993)**	(1,897)
Total shareholders' equity	**103,055**	101,677
Total liabilities, preferred shareholders' equity in subsidiary companies and shareholders' equity	**$999,747**	$979,414

See Accompanying Notes to Consolidated Financial Statements.

CONSOLIDATED STATEMENT OF INCOME

(in millions, except per share data) (unaudited)

	Three Months Ended March 31,	
	2007	2006
Revenues:		
Premiums and other considerations	**$19,642**	$18,270
Net investment income	**7,124**	5,971
Realized capital gains (losses)	**(70)**	169
Other income	**3,949**	2,868
Total revenues	**30,645**	27,278
Benefits and expenses:		
Incurred policy losses and benefits	**16,146**	15,089
Insurance acquisition and other operating expenses	**8,327**	7,396
Total benefits and expenses	**24,473**	22,485
Income before income taxes, minority interest and cumulative effect of an accounting change	**6,172**	4,793
Income taxes	**1,726**	1,435
Income before minority interest and cumulative effect of an accounting change	**4,446**	3,358
Minority interest	**(316)**	(197)
Income before cumulative effect of an accounting change	**4,130**	3,161
Cumulative effect of an accounting change, net of tax	**—**	34
Net income	**$ 4,130**	$ 3,195
Earnings per common share:		
Basic		
Income before cumulative effect of an accounting change	**$ 1.58**	$ 1.21
Cumulative effect of an accounting change, net of tax	**—**	0.01
Net income	**$ 1.58**	$ 1.22
Diluted		
Income before cumulative effect of an accounting change	**$ 1.58**	$ 1.21
Cumulative effect of an accounting change, net of tax	**—**	0.01
Net income	**$ 1.58**	$ 1.22
Dividends declared per common share	**$ 0.165**	$ 0.150
Average shares outstanding:		
Basic	**2,612**	2,605
Diluted	**2,621**	2,624

See Accompanying Notes to Consolidated Financial Statements.

CONSOLIDATED STATEMENT OF CASH FLOWS

(in millions) (unaudited)

	Three Months Ended March 31,	
	2007	2006
Summary:		
Net cash provided by operating activities	**$ 8,633**	$ 3,848
Net cash used in investing activities	**(16,863)**	(18,107)
Net cash provided by financing activities	**8,352**	13,587
Effect of exchange rate changes on cash	**(10)**	23
Change in cash	**112**	(649)
Cash at beginning of period	**1,590**	1,897
Cash at end of period	**$ 1,702**	$ 1,248
Cash flows from operating activities:		
Net income	**$ 4,130**	$ 3,195
Adjustments to reconcile net income to net cash provided by operating activities:		
Noncash revenues, expenses, gains and losses included in income:		
Net gains on sales of securities available for sale and other assets	**(250)**	(210)
Foreign exchange transaction (gains) losses	**305**	214
Net unrealized (gains) losses on non-AIGFP derivative assets and liabilities	**61**	(370)
Equity in income of partially owned companies and other invested assets	**(1,329)**	(480)
Amortization of deferred policy acquisition costs	**2,921**	2,635
Amortization of premium and discount on securities	**38**	390
Depreciation expenses, principally flight equipment	**646**	554
Provision for finance receivable losses	**87**	160
Impairment losses	**467**	226
Changes in operating assets and liabilities:		
General and life insurance reserves	**4,190**	4,483
Premiums and insurance balances receivable and payable – net	**(1,192)**	(2,245)
Reinsurance assets	**223**	121
Capitalization of deferred policy acquisition costs	**(3,750)**	(4,252)
Investment income due and accrued	**(109)**	(6)
Funds held under reinsurance treaties	**(158)**	21
Other policyholders' funds	**223**	(459)
Income taxes payable	**1,076**	744
Commissions, expenses and taxes payable	**661**	170
Other assets and liabilities – net	**774**	(1,967)
Bonds, common and preferred stocks trading, at fair value	**(1,260)**	(1,596)
Trade receivables and payables – net	**1,805**	(168)
Trading securities, at fair value	**(337)**	149
Spot commodities	**147**	(138)
Net unrealized (gain) loss on swaps, options and forward transactions	**962**	2
Securities purchased under agreements to resell	**78**	2,302
Securities sold under agreements to repurchase	**(2,100)**	(1,604)
Securities and spot commodities sold but not yet purchased, at market value	**(20)**	454
Finance receivables held for sale – originations and purchases	**(2,433)**	(2,267)
Sales of finance receivables – held for sale	**2,573**	2,671
Other, net	**204**	1,119
Total adjustments	**4,503**	653
Net cash provided by operating activities	**$ 8,633**	$ 3,848

See Accompanying Notes to Consolidated Financial Statements.

CONSOLIDATED STATEMENT OF CASH FLOWS *(continued)*

(in millions) (unaudited)

	Three Months Ended March 31,	
	2007	2006
Cash flows from investing activities:		
Proceeds from (payments for)		
Sales and maturities of fixed maturity securities available for sale	**$ 30,145**	$ 27,456
Sales of equity securities available for sale	**2,112**	3,627
Proceeds from fixed maturity securities held to maturity	**18**	9
Sales of flight equipment	**27**	159
Sales or distributions of other invested assets	**2,698**	2,352
Payments received on mortgage, policy, collateral and guaranteed loans	**658**	168
Principal payments received on finance receivables held for investment	**3,349**	3,076
Purchases of fixed maturity securities available for sale	**(34,273)**	(34,331)
Purchases of equity securities available for sale	**(2,436)**	(4,020)
Purchases of fixed maturity securities held to maturity	**(9)**	(16)
Purchases of flight equipment	**(1,917)**	(1,897)
Purchases of other invested assets	**(4,586)**	(3,320)
Acquisitions of new businesses, net of cash acquired	**(584)**	—
Mortgage, policy, collateral and guaranteed loans issued	**(2,326)**	(1,525)
Finance receivables held for investment – originations and purchases	**(3,409)**	(3,401)
Change in securities lending collateral	**(5,521)**	(3,496)
Net additions to real estate, fixed assets, and other assets	**(259)**	(248)
Net change in short-term investments	**(588)**	(2,676)
Net change in non-AIGFP derivative assets and liabilities	**38**	(24)
Net cash used in investing activities	**$ (16,863)**	$ (18,107)
Cash flows from financing activities:		
Proceeds from (payments for)		
Policyholders' contract deposits	**$ 14,080**	$ 13,469
Policyholders' contract withdrawals	**(14,682)**	(10,191)
Change in other deposits	**(1,340)**	(427)
Change in commercial paper	**279**	4,250
Notes, bonds, loans and mortgages payable, and hybrid financial instrument liabilities issued	**19,186**	9,403
Repayments on notes, bonds, loans and mortgages payable, and hybrid financial instrument liabilities	**(14,549)**	(6,835)
Issuance of junior subordinated debt	**3,740**	—
Issuance of guaranteed investment agreements	**979**	3,546
Maturities of guaranteed investment agreements	**(1,775)**	(2,846)
Change in securities lending payable	**5,716**	3,550
Issuance of treasury stock	**52**	34
Payments advanced to purchase shares	**(3,000)**	—
Acquisition of treasury stock	**(16)**	(2)
Cash dividends paid to shareholders	**(430)**	(390)
Other, net	**112**	26
Net cash provided by financing activities	**$ 8,352**	$ 13,587
Supplementary disclosure of cash flow information:		
Cash paid during the period for:		
Interest	**$ 1,901**	$ 1,263
Taxes	**$ 640**	$ 460
Non-cash financing activities:		
Interest credited to policyholder accounts	**$ 2,879**	$ 2,741
Treasury stock acquired using payments advanced to purchase shares	**$ 149**	—
Non-cash investing activities:		
Debt assumed on acquisitions	**$ 1,208**	—

See Accompanying Notes to Consolidated Financial Statements.

CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME

(in millions) (unaudited)

	Three Months Ended March 31,	
	2007	2006
Net income	**$ 4,130**	$ 3,195
Other comprehensive income (loss):		
Unrealized (depreciation) appreciation of investments – net of reclassification adjustments	**1,309**	(2,599)
Deferred income tax benefit (expense) on above changes	**(458)**	1,100
Foreign currency translation adjustments	**(165)**	550
Deferred income tax benefit (expense) on above changes	**28**	(290)
Net derivative gains arising from cash flow hedging activities – net of reclassification adjustments	**1**	4
Deferred income tax expense on above changes	**27**	13
Change in pension and postretirement unrecognized periodic benefit (cost)	**3**	(3)
Deferred income tax benefit (expense) on above changes	**(1)**	(33)
Other comprehensive income (loss)	**744**	(1,258)
Comprehensive income	**$ 4,874**	$ 1,937

See Accompanying Notes to Consolidated Financial Statements.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited)*

1. Financial Statement Presentation

These unaudited condensed consolidated financial statements do not include certain financial information required by U.S. generally accepted accounting principles (GAAP) for complete financial statements and should be read in conjunction with the audited consolidated financial statements and the related notes included in the Annual Report on Form 10-K of American International Group, Inc. (AIG) for the year ended December 31, 2006 (2006 Annual Report on Form 10-K).

In the opinion of management, these consolidated financial statements contain the normal recurring adjustments necessary for a fair statement of the results presented herein. All material intercompany accounts and transactions have been eliminated.

Certain reclassifications and format changes have been made to prior period amounts to conform to the current period presentation.

2. Segment Information

AIG identifies its reportable segments by product line consistent with its management structure. These segments are General Insurance, Life Insurance & Retirement Services, Financial Services and Asset Management.

In order to better align financial reporting with the manner in which AIG's chief operating decision makers have managed their businesses, for the three months ended March 31, 2007, AIG realigned certain products among reportable segments and major internal reporting units. AIG also began reporting realized capital gains and losses for the Financial Services and Asset Management segments in the results of these segments. Historically, realized capital gains and losses were included in the Other category. There has been no change in AIG's management structure or in its reportable segments. All prior period amounts presented in the tables below have been revised to conform to the current year's presentation of these items.

The following table summarizes the operations by the major operating segments:

Operating Segments *(in millions)*	Three Months Ended March 31, **2007**	2006
Revenues[(a)]:		
General Insurance[(b)]	**$12,903**	$11,656
Life Insurance & Retirement Services[(c)]	**13,682**	12,850
Financial Services[(d)(e)]	**2,201**	1,666
Asset Management[(f)]	**1,908**	1,139
Other	**102**	90
Consolidation and eliminations	**(151)**	(123)
Consolidated	**$30,645**	$27,278
Operating income (loss)[(a)(g)]:		
General Insurance	**$ 3,096**	$ 2,331
Life Insurance & Retirement Services	**2,281**	2,630
Financial Services[(e)]	**292**	(108)
Asset Management	**994**	449
Other[(h)]	**(499)**	(509)
Consolidation and eliminations	**8**	–
Consolidated	**$ 6,172**	$ 4,793

(a) Includes the effect of hedging activities that did not qualify for hedge accounting treatment under Statement of Financial Accounting Standards No. 133, "Accounting for Derivative Instruments and Hedging Activities" (FAS 133) or for which hedge accounting was not applied, including the related foreign exchange gains and losses. For the first three months of 2007 and 2006, respectively, the effect was $(452) million and $(212) million in both revenues and operating income. These amounts result primarily from interest rate and foreign currency derivatives that are hedging investments and borrowings.

(b) Represents the sum of General Insurance net premiums earned, net investment income and realized capital gains (losses).

(c) Represents the sum of Life Insurance & Retirement Services premiums and other considerations, net investment income and realized capital gains (losses). Included in realized capital gains (losses) and operating income is the effect of hedging activities that did not qualify for hedge accounting treatment under FAS 133, which were $(123) million and $352 million for the first three months of 2007 and 2006, respectively, and the application of Statement of Financial Accounting Standards No. 52 "Foreign Currency Translation" (FAS 52), which were $123 million and $4 million for the first three months of 2007 and 2006, respectively.

(d) Represents interest, lease and finance charges.

(e) Includes the effect of hedging activities that did not qualify for hedge accounting treatment under FAS 133 or for which hedge accounting was not applied, including the related foreign exchange gains and losses. For the three months ended March 31, 2007 and 2006, respectively, the effect was $(160) million, and $(619) million in both revenues and operating income. These amounts result primarily from interest rate and foreign currency derivatives that are effective economic hedges of investments and borrowings. In the first quarter of 2007, AIG began applying hedge accounting for certain transactions, primarily in its Capital Markets operations.

(f) Represents net investment income with respect to spread-based products and management and advisory fees.

(g) Represents income before income taxes, minority interest and cumulative effect of an accounting change.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

2. Segment Information *(continued)*

(h) Includes AIG parent and other operations which are not required to be reported separately. The following table presents the operating loss for AIG's Other category:

(in millions)	Three Months Ended March 31, 2007	2006
Other operating income (loss):		
Equity earnings in unconsolidated entities	**$ 41**	$ 19
Interest expense	**(252)**	(183)
Unallocated corporate expenses	**(162)**	(184)
Compensation expense — SICO Plans	**(10)**	(76)
Compensation expense — Starr tender offer	**–**	(54)
Realized capital gains (losses)	**(78)**	(5)
Other miscellaneous, net	**(38)**	(26)
Total Other	**$(499)**	$(509)

The following table summarizes AIG's General Insurance operations by major internal reporting unit:

General Insurance *(in millions)*	Three Months Ended March 31, 2007	2006
Revenues:		
Domestic Brokerage Group	**$ 7,091**	$ 6,561
Transatlantic	**1,096**	1,016
Personal Lines	**1,213**	1,215
Mortgage Guaranty	**248**	198
Foreign General	**3,262**	2,664
Reclassifications and eliminations	**(7)**	2
Total General Insurance	**$12,903**	$11,656
Operating Income*:		
Domestic Brokerage Group	**$ 1,929**	$ 1,305
Transatlantic	**151**	141
Personal Lines	**106**	101
Mortgage Guaranty	**8**	109
Foreign General	**909**	673
Reclassifications and eliminations	**(7)**	2
Total General Insurance	**$ 3,096**	$ 2,331

* *Includes additional losses incurred and net reinstatement premiums related to prior year catastrophes of $35 million and $99 million for the three months ended March 31, 2007 and 2006, respectively.*

The following table summarizes AIG's Life Insurance & Retirement Services operations by major internal reporting unit:

Life Insurance & Retirement Services *(in millions)*	Three Months Ended March 31, 2007	2006
Revenues:		
Foreign:		
Japan and Other	**$ 4,770**	$ 4,264
Asia	**4,491**	4,460
Domestic:		
Domestic Life Insurance	**2,521**	2,367
Domestic Retirement Services	**1,900**	1,759
Total Life Insurance & Retirement Services	**$13,682**	$12,850
Operating Income:		
Foreign:		
Japan and Other	**$ 913**	$ 978
Asia	**371**	708
Domestic:		
Domestic Life Insurance	**345**	366
Domestic Retirement Services	**652**	578
Total Life Insurance & Retirement Services	**$ 2,281**	$ 2,630

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

2. Segment Information *(continued)*

The following table summarizes AIG's Financial Services operations by major internal reporting unit:

Financial Services *(in millions)*	Three Months Ended March 31, **2007**	2006
Revenues:		
Aircraft Leasing[(a)]	**$1,058**	$1,012
Capital Markets[(b)(c)]	**228**	(300)
Consumer Finance[(d)(e)]	**883**	925
Other, including intercompany adjustments	**32**	29
Total Financial Services	**$2,201**	$1,666
Operating income (loss):		
Aircraft Leasing[(a)]	**$ 164**	$ 176
Capital Markets[(b)(c)]	**68**	(470)
Consumer Finance[(d)(e)]	**36**	176
Other, including intercompany adjustments	**24**	10
Total Financial Services	**$ 292**	$ (108)

(a) Revenues are primarily aircraft lease rentals from International Lease Finance Corporation (ILFC). Both revenues and operating income include the effect of hedging activities that did not qualify for hedge accounting treatment under FAS 133, including the related foreign exchange gains and losses. For the three months ended March 31, 2007 and 2006, the effect was $(37) million and $45 million, respectively. These amounts result primarily from interest rate and foreign currency derivatives that are effective economic hedges of borrowings.

(b) Revenues, shown net of interest expense of $1.1 billion and $639 million in the first three months of 2007 and 2006, respectively, were primarily from hedged financial positions entered into in connection with counterparty transactions. Both revenues and operating income include the effect of hedging activities that did not qualify for hedge accounting treatment under FAS 133 or for which hedge accounting was not applied, including the related foreign exchange gains and losses. For the three months ended March 31, 2007 and 2006, the effect was $(85) million and $(678) million, respectively.

(c) Certain transactions entered into by AIGFP generate tax credits and benefits which are included in income taxes in the consolidated statement of income. The amounts of such tax credits and benefits for the three months ended March 31, 2007 and 2006 were $17 million and $18 million, respectively.

(d) Revenues are primarily finance charges. Both revenues and operating income include the effect of hedging activities that did not qualify for hedge accounting treatment under FAS 133, including the related foreign exchange gains and losses. For the three months ended March 31, 2007 and 2006, the effect was $(36) million and $3 million, respectively. These amounts result primarily from interest rate and foreign currency derivatives that are effective economic hedges of borrowings.

(e) The three months ended March 31, 2007 includes a pre-tax charge of $128 million ($83 million after tax) in connection with domestic consumer finance's mortgage banking activities.

3. Shareholders' Equity and Earnings Per Share (EPS)

Earnings Per Share

Basic EPS of AIG is calculated using the weighted average number of common shares outstanding. Diluted EPS is based on those shares used in basic EPS plus shares that would have been outstanding assuming issuance of common shares for all potentially dilutive common shares outstanding.

The following table presents the computation of basic and diluted EPS:

(in millions, except per share data)	Three Months Ended March 31, **2007**	2006
Numerator for basic earnings per share:		
Income before cumulative effect of an accounting change	**$4,130**	$3,161
Cumulative effect of an accounting change, net of tax	**–**	34
Net income applicable to common stock for basic EPS	**$4,130**	$3,195
Interest on contingently convertible bonds, net of tax[(a)]	**–**	3
Net income applicable to common stock for diluted EPS	**$4,130**	$3,198
Cumulative effect of an accounting change, net of tax	**–**	(34)
Income before cumulative effect of an accounting change applicable to common stock for diluted EPS	**$4,130**	$3,164
Denominator for earnings per share:		
Weighted-average shares outstanding used in the computation of EPS:		
Common stock issued	**2,751**	2,751
Common stock in treasury	**(150)**	(154)
Deferred shares	**11**	8
Weighted-average shares outstanding – basic	**2,612**	2,605
Incremental shares from potential common stock:		
Weighted-average number of shares arising from outstanding employee stock plans (treasury stock method)[(b)]	**9**	10
Contingently convertible bonds[(a)]	**–**	9
Weighted average shares outstanding – diluted[(b)]	**2,621**	2,624

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

3. Shareholders' Equity and Earnings Per Share (EPS) *(continued)*

(in millions, except per share data)	Three Months Ended March 31, **2007**	2006
Earnings per share:		
Basic:		
Income before cumulative effect of an accounting change	**$ 1.58**	$ 1.21
Cumulative effect of an accounting change, net of tax	**–**	0.01
Net income	**$ 1.58**	$ 1.22
Diluted:		
Income before cumulative effect of an accounting change	**$ 1.58**	$ 1.21
Cumulative effect of an accounting change, net of tax	**–**	0.01
Net income	**$ 1.58**	$ 1.22

(a) Assumes conversion of contingently convertible bonds due to the adoption of Emerging Issues Task Force Issue No. 04-8 "Accounting Issues Related to Certain Features of Contingently Convertible Debt and the Effect on Diluted Earnings per Share."

(b) Certain shares arising from employee stock plans were not included in the computation of diluted earnings per share where the exercise price of the options exceeded the average market price and would have been antidilutive. The number of shares excluded was 7 million for both the three months ended March 31, 2007 and 2006.

Shareholders' Equity

From time to time, AIG may buy shares of its common stock for general corporate purposes, including to satisfy its obligations under various employee benefit plans. At December 31, 2006, an additional 36,542,700 shares could be purchased under the then current authorization by AIG's Board of Directors. In February 2007, AIG's Board of Directors increased the repurchase program by authorizing the repurchase of shares with an aggregate purchase price of $8 billion. During March 2007, AIG made open market share repurchases and entered into a $3 billion structured share repurchase arrangement. A total of 2,470,499 shares were repurchased during March 2007. The portion of the payment advanced by AIG under the structured share repurchase arrangement that had not yet been utilized to repurchase shares at March 31, 2007, amounting to $2.85 billion, has been recorded as a component of shareholders' equity under the caption Payments advanced to purchase shares. Purchases have continued since March 31, 2007, with an additional 6,643,052 shares purchased during April 2007, and purchases are anticipated to occur throughout 2007. All shares repurchased are recorded as treasury stock at cost.

The quarterly dividend per common share, commencing with the dividend declared in May 2006 and paid on September 15, 2006, was $0.165.

The following table summarizes the changes in retained earnings:

(in millions)	Three Months Ended March 31, **2007**	2006
Retained earnings:		
Balance at beginning of year	**$84,996**	$72,330
Cumulative effect of accounting changes, net of tax	**(203)**	308
Adjusted balance, beginning of year	**84,793**	72,638
Net income	**4,130**	3,195
Dividends to shareholders	**(430)**	(400)
Balance, end of period	**$88,493**	$75,433

4. Benefits Provided by Starr International Company, Inc. and C.V. Starr & Co., Inc.

Starr International Company, Inc. (SICO) has provided a series of two-year Deferred Compensation Profit Participation Plans (SICO Plans) to certain AIG employees. The SICO Plans came into being in 1975 when the voting shareholders and Board of Directors of SICO, a private holding company whose principal asset is AIG common stock, decided that a portion of the capital value of SICO should be used to provide an incentive plan for the current and succeeding managements of all American International companies, including AIG.

None of the costs of the various benefits provided under the SICO Plans has been paid by AIG, although AIG has recorded a charge to reported earnings for the deferred compensation amounts paid to AIG employees by SICO, with an offsetting amount credited to additional paid-in capital reflecting amounts deemed contributed by SICO. The SICO Plans provide that shares currently owned by SICO are set aside by SICO for the benefit of the participant and distributed upon retirement. The SICO Board of Directors currently

may permit an early payout of units under certain circumstances. Prior to payout, the participant is not entitled to vote, dispose of or receive dividends with respect to such shares, and shares are subject to forfeiture under certain conditions, including but not limited to the participant's voluntary termination of employment with AIG prior to normal retirement age. Under the SICO Plans, SICO's Board of Directors may elect to pay a participant cash in lieu of shares of AIG common stock. Following notification from SICO to participants in the SICO Plans that it will settle specific future awards under the SICO Plans with shares rather than cash, AIG modified its accounting for the SICO Plans from variable to fixed measurement accounting. AIG gave effect to this change in settlement method beginning on December 9, 2005, the date of SICO's notice to participants in the SICO Plans. See also Note 6(b) "Commitments" herein.

In January 2006, C.V. Starr & Co., Inc. (Starr) completed its tender offer to purchase Starr interests from AIG employees. In conjunction with AIG's adoption of FAS 123R, Starr is considered to be an "economic interest holder" in AIG. As a result, compensation expense of $54 million was included in the first three months of 2006 with respect to the Starr tender offer.

Compensation expense with respect to the SICO Plans aggregated $10 million and $76 million for the first three months of 2007 and 2006, respectively. Compensation expense in 2006 included various out of period adjustments totaling $61 million, primarily relating to stock splits and other miscellaneous items for the SICO plans.

5. Ownership

According to the Schedule 13D filed on March 20, 2007 by Starr, SICO, Edward E. Matthews, Maurice R. Greenberg, the Maurice R. and Corinne P. Greenberg Family Foundation, Inc., the Universal Foundation, Inc., the Maurice R. and Corinne P. Greenberg Joint Tenancy Company, LLC and the C.V. Starr & Co., Inc. Trust, these reporting persons could be deemed to beneficially own 354,987,261 shares of AIG's common stock at that date. Based on the shares of AIG's common stock outstanding as of April 30, 2007, this ownership would represent approximately 14 percent of the voting stock of AIG. Although these reporting persons have made filings under Section 16 of the Exchange Act, reporting sales of shares of common stock, no amendment to the Schedule 13D has been filed to report a change in ownership subsequent to March 20, 2007.

6. Commitments, Contingencies and Guarantees

In the normal course of business, various commitments and contingent liabilities are entered into by AIG and certain of its subsidiaries. In addition, AIG guarantees various obligations of certain subsidiaries.

(a) Litigation and Investigations

Litigation Arising from Operations. AIG and its subsidiaries, in common with the insurance and financial services industries in general, are subject to litigation, including claims for punitive damages, in the normal course of their business. In AIG's insurance operations, litigation arising from claims settlement activities is generally considered in the establishment of AIG's reserve for losses and loss expenses. However, in certain circumstances, AIG provides disclosure because of the size or nature of the potential liability to AIG. The potential for increasing jury awards and settlements makes it difficult to assess the ultimate outcome of such litigation.

Litigation Arising from Insurance Operations — Caremark. AIG and certain of its subsidiaries have been named defendants in two putative class actions in state court in Alabama that arise out of the 1999 settlement of class and derivative litigation involving Caremark Rx, Inc. (Caremark). The plaintiffs in the second-filed action have intervened in the first-filed action, and the second-filed action has been dismissed. An excess policy issued by a subsidiary of AIG with respect to the 1999 litigation was expressly stated to be without limit of liability. In the current actions, plaintiffs allege that the judge approving the 1999 settlement was misled as to the extent of available insurance coverage and would not have approved the settlement had he known of the existence and/or unlimited nature of the excess policy. They further allege that AIG, its subsidiaries, and Caremark are liable for fraud and suppression for misrepresenting and/or concealing the nature and extent of coverage. In their complaint, plaintiffs request compensatory damages for the 1999 class in the amount of $3.2 billion, plus punitive damages. AIG and its subsidiaries deny the allegations of fraud and suppression and have asserted, *inter alia,* that information concerning the excess policy was publicly disclosed months prior to the approval of the settlement. AIG and its subsidiaries further assert that the current claims are barred by the statute of limitations and that plaintiffs' assertions that the statute was tolled cannot stand against the public disclosure of the excess coverage. Plaintiffs, in turn, have asserted that the disclosure was insufficient to inform them of the nature of the coverage and did not start the running of the statute of limitations. The trial court is currently considering, under standards mandated by the Alabama Supreme Court, whether a class action can be certified and whether the defendants in the case brought by the intervenors should be dismissed. AIG cannot reasonably estimate either the likelihood of its prevailing in these actions or the potential damages in the event liability is determined.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

6. Commitments, Contingencies and Guarantees *(continued)*

Litigation Arising from Insurance Operations — Gunderson. A subsidiary of AIG has been named as a defendant in a putative class action lawsuit in the 14th Judicial District Court for the State of Louisiana. The *Gunderson* complaint alleges failure to comply with certain provisions of the Louisiana Any Willing Provider Act (the Act) relating to discounts taken by defendants on bills submitted by Louisiana medical providers and hospitals that provided treatment or services to workers compensation claimants and seeks monetary penalties and injunctive relief. On July 20, 2006, the court denied defendants' motion for summary judgment and granted plaintiffs' partial motion for summary judgment, holding that the AIG subsidiary was a "group purchaser" and, therefore, potentially subject to liability under the Act. On November 28, 2006, the court issued an order certifying a class of providers and hospitals. In an unrelated action also arising under the Act, a Louisiana appellate court ruled that the district court lacked jurisdiction to adjudicate the claims at issue. In response, defendants in *Gunderson* filed an exception for lack of subject matter jurisdiction. On January 19, 2007, the court denied the motion, holding that it has jurisdiction over the putative class claims. The AIG subsidiary is appealing the class certification ruling and is seeking an appeal from the jurisdictional ruling. While AIG believes that it has meritorious defenses to plaintiffs' claims, it cannot currently estimate the likelihood of prevailing in this action or reasonably estimate the likely damages, if any.

2006 Regulatory Settlements. In February 2006, AIG reached a resolution of claims and matters under investigation with the United States Department of Justice (DOJ), SEC, the Office of the New York Attorney General (NYAG) and the New York State Department of Insurance (DOI). AIG recorded an after-tax charge of $1.15 billion relating to these settlements in the fourth quarter of 2005.

The settlements resolved investigations conducted by the SEC, NYAG and DOI in connection with the accounting, financial reporting and insurance brokerage practices of AIG and its subsidiaries, as well as claims relating to the underpayment of certain workers compensation premium taxes and other assessments. These settlements did not, however, resolve investigations by regulators from other states into insurance brokerage practices related to contingent commissions and other broker-related conduct, such as alleged bid rigging. Nor did the settlements resolve any obligations that AIG may have to state guarantee funds in connection with any of these matters.

As a result of these settlements, AIG made payments or placed amounts in escrow in 2006 totaling approximately $1.64 billion, $225 million of which represented fines and penalties. Amounts held in escrow totaling $380 million, including interest thereon, are included in other assets at March 31, 2007. At that date, approximately $317 million of the funds were escrowed for settlement of claims resulting from the underpayment by AIG of its residual market assessments for workers compensation. The National Workers Compensation Reinsurance Pool on behalf of its participant members and various states have communicated to AIG that they may assert claims with respect to the underpayment of such assessments. In addition, the National Association of Insurance Commissioners has formed a Settlement Review Working Group, which has commenced its own investigation into the underpayment of such assessments, directed by the State of Indiana. AIG cannot currently estimate whether the amount ultimately required to settle these claims will exceed the funds escrowed for this purpose.

The remaining escrowed funds, which amounted to $63 million at March 31, 2007, are set aside for settlements with certain AIG policyholders specified in the settlements who claimed to have been harmed by AIG's insurance brokerage practices. During the first three months of 2007, approximately $323 million was paid out from escrow in exchange for releasing AIG and its subsidiaries from any alleged liability relating to such brokerage practices. Any funds remaining at the end of the escrow period will be used to resolve claims asserted by policyholders relating to such insurance brokerage practices, including those described in Private Litigation below.

In addition to the escrowed funds, $800 million was deposited into a fund under the supervision of the SEC as part of the settlements to be available to resolve claims asserted against AIG by investors including, the shareholder lawsuits described herein.

At the current time, AIG cannot predict the outcome of the matters described above, or estimate any potential additional cost related to these matters.

Also, as part of the settlements, AIG has agreed to retain, for a period of three years, an independent consultant who will conduct a review that will include, among other things, the adequacy of AIG's internal control over financial reporting, the policies, procedures and effectiveness of AIG's regulatory, compliance and legal functions and the remediation plan that AIG has implemented as a result of its own internal review.

Private Litigation

Securities Actions. Beginning in October 2004, a number of putative securities fraud class action suits were filed against AIG and consolidated as *In re American International Group, Inc. Securities Litigation*. Subsequently, a separate, though similar, securities fraud action was also brought against AIG by certain Florida pension funds. The lead plain-

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

6. Commitments, Contingencies and Guarantees *(continued)*

tiff in the class action is a group of public retirement systems and pension funds benefiting Ohio state employees, suing on behalf of themselves and all purchasers of AIG's publicly traded securities between October 28, 1999 and April 1, 2005. The named defendants are AIG and a number of present and former AIG officers and directors, as well as Starr, SICO, General Reinsurance Corporation, and PricewaterhouseCoopers LLP (PwC), among others. The lead plaintiff alleges, among other things, that AIG: (1) concealed that it engaged in anti-competitive conduct through alleged payment of contingent commissions to brokers and participation in illegal bid-rigging; (2) concealed that it used "income smoothing" products and other techniques to inflate its earnings; (3) concealed that it marketed and sold "income smoothing" insurance products to other companies; and (4) misled investors about the scope of government investigations. In addition, the lead plaintiff alleges that AIG's former Chief Executive Officer manipulated AIG's stock price. The lead plaintiff asserts claims for violations of Sections 11 and 15 of the Securities Act, Section 10(b) of the Exchange Act, and Rule 10b-5 promulgated thereunder, Section 20(a) of the Exchange Act, and Section 20A of the Exchange Act. In April 2006, the court denied the defendants' motions to dismiss the second amended class action complaint and the Florida complaint. In December 2006, a third amended class action complaint was filed, which does not differ substantially from the prior complaint. Fact and class discovery is currently ongoing.

ERISA Action. Between November 30, 2004 and July 1, 2005, several ERISA actions were filed on behalf of purported class of participants and beneficiaries of three pension plans sponsored by AIG or its subsidiaries. A consolidated complaint filed on September 26, 2005 alleges a class period between September 30, 2000 and May 31, 2005 and names as defendants AIG, the members of AIG's Retirement Board and the Administrative Boards of the plans at issue, and four present or former members of AIG's Board of Directors. The factual allegations in the complaint are essentially identical to those in the securities actions described above. Plaintiffs allege that defendants violated duties under ERISA by allowing the plans to offer AIG stock as a permitted investment, when defendants allegedly knew it was not a prudent investment, and by failing to provide participants with accurate information about AIG stock. AIG's motion to dismiss was denied by order dated December 12, 2006. Discovery will be consolidated with proceedings in the securities actions.

Derivative Actions — Southern District of New York. Between October 25, 2004 and July 14, 2005, seven separate derivative actions were filed in the Southern District of New York, five of which were consolidated into a single action. The New York derivative complaint contains nearly the same types of allegations made in the securities fraud and ERISA actions described above. The named defendants include current and former officers and directors of AIG, as well as Marsh & McLennan Companies, Inc. (Marsh), SICO, Starr, ACE Limited and subsidiaries (ACE), General Reinsurance Corporation, PwC, and certain employees or officers of these entity defendants. Plaintiffs assert claims for breach of fiduciary duty, gross mismanagement, waste of corporate assets, unjust enrichment, insider selling, auditor breach of contract, auditor professional negligence and disgorgement from AIG's former Chief Executive Officer and Chief Financial Officer of incentive-based compensation and AIG share proceeds under Section 304 of the Sarbanes-Oxley Act, among others. Plaintiffs seek, among other things, compensatory damages, corporate governance reforms, and a voiding of the election of certain AIG directors. AIG's Board of Directors has appointed a special committee of independent directors (special committee) to review the matters asserted in the operative consolidated derivative complaint. The court has approved an agreement staying the derivative case pending in the Southern District of New York. The current stay extends until July 13, 2007.

Derivative Actions — Delaware Chancery Court. From October 2004 to April 2005, AIG shareholders filed five derivative complaints in the Delaware Chancery Court. All of these derivative lawsuits have been consolidated into a single action. The amended consolidated complaint names 43 defendants (not including nominal defendant AIG) who, like the New York consolidated derivative litigation, are current and former officers and directors of AIG, as well as other entities and certain of their current and former employees and directors. The factual allegations, legal claims and relief sought in Delaware action are similar to those alleged in the New York derivative actions, except that plaintiffs in the Delaware derivative action assert claims only under state law. The court has approved an agreement that AIG be realigned as plaintiff. AIG has until June 13, 2007 to file an amended complaint, and the special committee has until June 13, 2007 to file a motion to terminate the litigation with respect to certain defendants.

An additional derivative lawsuit was filed in the Delaware Chancery Court in December 2002 against twenty directors and executives of AIG as well as against AIG as a nominal defendant, alleges, among other things, that the directors of AIG breached the fiduciary duties of loyalty and care by approving the payment of commissions to Starr and of rental and service fees to SICO and the executives breached their duty of loyalty by causing AIG to enter into contracts with Starr and SICO and their fiduciary duties by usurping AIG's corporate opportunity. The complaint further alleges that the Starr agencies did not provide any services that AIG

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

6. Commitments, Contingencies and Guarantees *(continued)*

was not capable of providing itself, and that the diversion of commissions to these entities was solely for the benefit of Starr's owners. The complaint also alleged that the service fees and rental payments made to SICO and its subsidiaries were improper. Under the terms of a stipulation approved by the Court on February 16, 2006, the claims against the outside independent directors were dismissed with prejudice, while the claims against the other directors were dismissed without prejudice. On October 31, 2005, Messrs. Greenberg, Matthews and Smith, SICO and Starr filed motions to dismiss the amended complaint. In an opinion dated June 21, 2006, the Court denied defendants' motion to dismiss, except with respect to plaintiff's challenge to payments made to Starr before January 1, 2000. On July 21, 2006, plaintiff filed its second amended complaint, which alleges that, between January 1, 2000 and May 31, 2005, individual defendants breached their duty of loyalty by causing AIG to enter into contracts with Starr and SICO and breached their fiduciary duties by usurping AIG's corporate opportunity. Starr is charged with aiding and abetting breaches of fiduciary duty and unjust enrichment for its acceptance of the fees. SICO is no longer named as a defendant. On April 20, 2007, the individual defendants and Starr filed a motion seeking leave of the Court to assert a cross-claim against AIG and a third-party complaint against PwC and the directors previously dismissed from the action, as well as certain other AIG officers and employees. Discovery is currently ongoing.

Policyholder Actions. After the NYAG filed its complaint against insurance broker Marsh, policyholders brought multiple federal antitrust and Racketeer Influenced and Corrupt Organizations Act (RICO) class actions in jurisdictions across the nation against insurers and brokers, including AIG and a number of its subsidiaries, alleging that the insurers and brokers engaged in a broad conspiracy to allocate customers, steer business, and rig bids. These actions, including 18 complaints filed in different federal courts naming AIG or an AIG subsidiary as a defendant, were consolidated by the judicial panel on multi-district litigation and transferred to the United States District Court for the District of New Jersey for coordinated pretrial proceedings. The consolidated actions have proceeded in that court in two parallel actions, *In re Insurance Brokerage Antitrust Litigation* (the *Commercial Complaint*) and *In re Employee Benefit Insurance Brokerage Antitrust Litigation* (the *Employee Benefits Complaint,* and together with the *Commercial Complaint,* the multi-district litigation).

The plaintiffs in the *Commercial Complaint* are nineteen corporations, individuals and public entities that contracted with the broker defendants for the provision of insurance brokerage services for a variety of insurance needs. The broker defendants are alleged to have placed insurance coverage on the plaintiffs' behalf with a number of insurance companies named as defendants, including AIG subsidiaries. The *Commercial Complaint* also named ten brokers and fourteen other insurers (one of which has since settled) as defendants. The *Commercial Complaint* alleges that defendants engaged in a widespread conspiracy to allocate customers through "bid-rigging" and "steering" practices. The *Commercial Complaint* also alleges that the insurer defendants permitted brokers to place business with AIG subsidiaries through wholesale intermediaries affiliated with or owned by those same brokers rather than placing the business with AIG subsidiaries directly. Finally, the *Commercial Complaint* alleges that the insurer defendants entered into agreements with broker defendants that tied insurance placements to reinsurance placements in order to provide additional compensation to each broker. Plaintiffs assert that the defendants violated the Sherman Antitrust Act, RICO, the antitrust laws of 48 states and the District of Columbia, and are liable under common law breach of fiduciary duty and unjust enrichment theories. Plaintiffs seek treble damages plus interest and attorneys' fees as a result of the alleged RICO and Sherman Act violations.

The plaintiffs in the *Employee Benefits Complaint* are nine individual employees and corporate and municipal employers alleging claims on behalf of two separate nationwide purported classes: an employee class and an employer class that acquired insurance products from the defendants from August 26, 1994 to the date of any class certification. The *Employee Benefits Complaint* names AIG, as well as eleven brokers and five other insurers, as defendants. The activities alleged in the *Employee Benefits Complaint,* with certain exceptions, track the allegations of contingent commissions, bid-rigging and tying made in the *Commercial Complaint.*

On October 3, 2006, Judge Hochberg of the District of New Jersey reserved in part and denied in part motions filed by the insurer defendants and broker defendants to dismiss the multi-district litigation. The Court also ordered the plaintiffs in both actions to file supplemental statements of particularity to elaborate on the allegations in their complaints. Plaintiffs filed their supplemental statements on October 25, 2006, and the AIG defendants, along with other insurer and broker defendants in the two consolidated actions, filed renewed motions to dismiss on November 30, 2006. On February 16, 2007, the case was transferred to Judge Garrett E. Brown, Chief Judge of the District of New Jersey. On April 5, 2007, Chief Judge Brown granted the defendants' renewed motions to dismiss the *Commercial Complaint* and *Employee Benefits Complaint* with respect to the antitrust and RICO claims. The claims were dismissed without prejudice and the plaintiffs were given 30 days, later extended to 45 days, to file amended complaints. On April 11, 2007, the Court stayed all proceedings, including all discovery, that are part of the

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

6. Commitments, Contingencies and Guarantees *(continued)*

multi-district litigation until any renewed motions to dismiss the amended complaints are resolved.

A number of complaints making allegations similar to those in the *Commercial Complaint* have been filed against AIG and other defendants in state and federal courts around the country. The defendants have thus far been successful in having the federal actions transferred to the District of New Jersey and consolidated into the multi-district litigation. The AIG defendants have also sought to have state court actions making similar allegations stayed pending resolution of the multi-district litigation proceeding. In one state court action pending in Florida, the trial court recently decided not to grant an additional stay, but instead to allow the case to proceed.

Litigation Relating to 21st Century. Shortly after the announcement in late January 2007 of AIG's offer to acquire the outstanding shares of 21st Century not already owned by AIG and its subsidiaries, two related class actions were filed in the Superior Court of California, Los Angeles County, against AIG, 21st Century, and the individual members of 21st Century's Board of Directors, two of whom are current executive officers of AIG. The actions were filed purportedly on behalf of the minority shareholders of 21st Century and assert breaches of fiduciary duty in connection with the AIG proposal. The complaints allege that the proposed per share price is unfair and seek preliminary and permanent injunctive relief to enjoin the consummation of the proposed transaction.

SICO. In July, 2005, SICO filed a complaint against AIG in the Southern District of New York, claiming that AIG had refused to provide SICO access to certain artwork and asked the court to order AIG immediately to release the property to SICO. AIG filed an answer denying SICO's allegations and setting forth defenses to SICO's claims. In addition, AIG filed counterclaims asserting breach of contract, unjust enrichment, conversion, breach of fiduciary duty, a constructive trust and declaratory judgment, relating to SICO's breach of its commitment to use its AIG shares only for the benefit of AIG and AIG employees. Fact and expert discovery has been substantially concluded and briefing on SICO's motion for summary judgment is underway.

Regulatory Investigations. Regulators from several states have commenced investigations into insurance brokerage practices related to contingent commissions and other industry-wide practices as well as other broker-related conduct, such as alleged bid-rigging. In addition, various federal and state regulatory agencies are reviewing certain transactions and practices of AIG and its subsidiaries in connection with industry-wide and other inquiries. AIG has cooperated, and will continue to cooperate, in producing documents and other information in response to subpoenas and other requests.

Wells Notices. AIG understands that some of its employees have received Wells notices in connection with previously disclosed SEC investigations of certain of AIG's transactions or accounting practices. Under SEC procedures, a Wells notice is an indication that the SEC staff has made a preliminary decision to recommend enforcement action that provides recipients with an opportunity to respond to the SEC staff before a formal recommendation is finalized. It is possible that additional current and former employees could receive similar notices in the future as the regulatory investigations proceed.

Effect on AIG

In the opinion of AIG management, AIG's ultimate liability for the unresolved litigation and investigation matters referred to above is not likely to have a material adverse effect on AIG's consolidated financial condition, although it is possible that the effect would be material to AIG's consolidated results of operations for an individual reporting period.

(b) Commitments

Flight Equipment

At March 31, 2007, ILFC had committed to purchase 224 new aircraft deliverable from 2007 through 2015 at an estimated aggregate purchase price of $17.2 billion. ILFC will be required to find customers for any aircraft acquired, and it must arrange financing for portions of the purchase price of such equipment.

Other Commitments

On June 27, 2005, AIG entered into an agreement pursuant to which AIG agrees, subject to certain conditions, to make any payment that is not promptly paid with respect to the benefits accrued by certain employees of AIG and its subsidiaries under the SICO Plans (as discussed in Note 4 herein).

(c) Contingencies

Loss Reserves

Although AIG regularly reviews the adequacy of the established reserve for losses and loss expenses, there can be no assurance that AIG's ultimate loss reserves will not develop adversely and materially exceed AIG's current loss reserves. Estimation of ultimate net losses, loss expenses and loss reserves is a complex process for long-tail casualty lines of business, which include excess and umbrella liability, directors and officers liability (D&O), professional liability, medical malpractice, workers compensation, general liability, products liability and related classes, as well as for asbestos

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

6. Commitments, Contingencies and Guarantees *(continued)*

and environmental exposures. Generally, actual historical loss development factors are used to project future loss development. However, there can be no assurance that future loss development patterns will be the same as in the past. Moreover, any deviation in loss cost trends or in loss development factors might not be discernible for an extended period of time subsequent to the recording of the initial loss reserve estimates for any accident year. Thus, there is the potential for reserves with respect to a number of years to be significantly affected by changes in loss cost trends or loss development factors that were relied upon in setting the reserves. These changes in loss cost trends or loss development factors could be attributable to changes in inflation, in labor and material costs or in the judicial environment, or in other social or economic phenomena affecting claims.

Synthetic Fuel Tax Credits. AIG generates income tax credits as a result of investing in synthetic fuel production. Tax credits generated from the production and sale of synthetic fuel under the Internal Revenue Code are subject to an annual phase-out provision that is based on the average wellhead price of domestic crude oil. The price range within which the tax credits are phased-out was originally established in 1980 and is adjusted annually for inflation. Depending on the price of domestic crude oil for a particular year, all or a portion of the tax credits generated in that year might be eliminated. AIG evaluates the production levels of its synthetic fuel production facilities in light of the risk of phase-out of the associated tax credits. As a result of fluctuating domestic crude oil prices, AIG evaluates and adjusts production levels when appropriate in light of this risk. Regardless of oil prices, the tax credits expire after 2007.

(d) Guarantees

AIG and certain of its subsidiaries become parties to derivative financial instruments with market risk resulting from both dealer and end-user activities and to reduce currency, interest rate, equity and commodity exposures. These instruments are carried at their estimated fair values in the consolidated balance sheet. The vast majority of AIG's derivative activity is transacted by AIG Financial Products Corp. and AIG Trading Group Inc. and their respective subsidiaries (collectively, AIGFP). See Note 19 of AIG's 2006 Annual Report on Form 10-K.

AIG has issued unconditional guarantees with respect to the prompt payment, when due, of all present and future payment obligations and liabilities of AIGFP arising from transactions entered into by AIGFP.

SAI Deferred Compensation Holdings, Inc., a wholly owned subsidiary of AIG, has established a deferred compensation plan for registered representatives of certain AIG subsidiaries, pursuant to which participants have the opportunity to invest deferred commissions and fees on a notional basis. The value of the deferred compensation fluctuates with the value of the deferred investment alternatives chosen. AIG has provided a full and unconditional guarantee of the obligations of SAI Deferred Compensation Holdings, Inc. to pay the deferred compensation under the plan.

7. Employee Benefits

The following table presents the components of the net periodic benefit costs with respect to pensions and other postretirement benefits:

	Pensions			Postretirement		
(in millions)	Non-U.S. Plans	U.S. Plans	Total	Non-U.S. Plans	U.S. Plans	Total
Three Months Ended March 31, 2007						
Components of net periodic benefit cost:						
Service cost	**$ 23**	**$ 30**	**$ 53**	**$ 1**	**$ 2**	**$ 3**
Interest cost	**12**	**45**	**57**	**1**	**4**	**5**
Expected return on assets	**(9)**	**(53)**	**(62)**	**–**	**–**	**–**
Amortization of prior service cost	**(2)**	**(1)**	**(3)**	**–**	**–**	**–**
Amortization of net loss	**2**	**9**	**11**	**–**	**–**	**–**
Net periodic benefit cost	**$ 26**	**$ 30**	**$ 56**	**$ 2**	**$ 6**	**$ 8**
Three Months Ended March 31, 2006						
Components of net periodic benefit cost:						
Service cost	$ 19	$ 31	$ 50	$ 1	$ 1	$ 2
Interest cost	9	40	49	1	3	4
Expected return on assets	(7)	(48)	(55)	–	–	–
Amortization of prior service cost	(2)	(1)	(3)	–	(2)	(2)
Recognized actuarial loss	4	19	23	–	–	–
Net periodic benefit cost	$ 23	$ 41	$ 64	$ 2	$ 2	$ 4

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

8. Recent Accounting Standards

Accounting Changes

SOP 05-1

On September 19, 2005, the AICPA issued Statement of Position 05-1, "Accounting by Insurance Enterprises for Deferred Acquisition Costs in Connection with Modifications or Exchanges of Insurance Contracts" (SOP 05-1). SOP 05-1 provides guidance on accounting for internal replacements of insurance and investment contracts other than those specifically described in FAS 97, "Accounting and Reporting by Insurance Enterprises for Certain Long-Duration Contracts and for Realized Gains and Losses from the Sale of Investments" (FAS 97). SOP 05-1 defines an internal replacement as a modification in product benefits, features, rights, or coverage that occurs by the exchange of a contract for a new contract, or by amendment, endorsement, or rider to a contract, or by the election of a feature or coverage within a contract. Internal replacements that result in a substantially changed contract are accounted for as a termination.

The provisions of SOP 05-1 became effective as of January 1, 2007. On the date of adoption, AIG recorded a cumulative effect reduction of $82 million, net of tax, to the opening balance of retained earnings to reflect changes in unamortized DAC, value of business acquired, deferred sales inducement assets, unearned revenue liabilities and future policy benefits for life and accident and health insurance contracts. This adjustment primarily reflects a shorter expected life related to certain group life and health insurance contracts and the effect on the gross profits of investment-oriented products related to previously anticipated future internal replacements. This cumulative effect adjustment affected only the Life Insurance & Retirement Services segment.

FIN 48

On July 13, 2006, the FASB issued FASB Interpretation No. 48, "Accounting for Uncertainty in Income Taxes — an interpretation of FASB Statement No. 109" (FIN 48), which clarifies the accounting for uncertainty in income tax positions. FIN 48 prescribes a recognition threshold and measurement attribute for the financial statement recognition and measurement of an income tax position taken or expected to be taken in a tax return. FIN 48 also provides guidance on derecognition, classification, interest and penalties, accounting in interim periods, and additional disclosures. AIG adopted the provisions of FIN 48 on January 1, 2007. As a result of the adoption of FIN 48, AIG recognized a $71 million increase in the liability for unrecognized tax benefits, which was accounted for as a decrease to opening retained earnings as of January 1, 2007.

As of the date of adoption and after recognizing the effect of the increase in the liability noted above, the total amount of AIG's unrecognized tax benefit, excluding interest and penalties, is $1.138 billion. Included in this balance are $407 million of tax positions, the disallowance of which would not affect the annual effective income tax rate. Accordingly, the amount of unrecognized tax benefit that, if recognized, would favorably affect the effective tax rate is $731 million.

Interest and penalties related to unrecognized tax benefits are recognized in income tax expense. At January 1, 2007, AIG had accrued $176 million for the payment of interest (net of the federal benefit) and penalties. At March 31, 2007, there has been no material change in the amount of unrecognized tax benefits and related interest and penalties.

Interest income related to potential tax benefits emanating from prior restatements has not been recognized because this amount is not currently estimable. In addition, certain tax benefits emanating from compensation deductions have not been recognized because of existing uncertainty with respect to the documentation supporting these tax benefits.

AIG continually evaluates proposed adjustments by taxing authorities. At March 31, 2007, such proposed adjustments would not result in a material change to its consolidated financial condition. However, AIG believes that it is reasonably possible that the balance of the unrecognized tax benefits could decrease by $0 to $150 million by the end of 2007 due to settlements or expiration of statutes.

Listed below are the tax years that remain subject to examination by major tax jurisdiction:

Major Tax Jurisdictions	Open Tax Years
United States	1991-2006
Hong Kong	1997-2006
Malaysia	1999-2006
Singapore	1993-2006
Thailand	2001-2006
Taiwan	2000-2006
Japan	2000-2006
United Kingdom	2003-2006
France	2003-2006
Korea	2001-2006

FSP 13-2

On July 13, 2006, the FASB issued FASB Staff Position (FSP) No. 13-2, "Accounting for a Change or Projected Change in the Timing of Cash Flows Relating to Income Taxes Generated by a Leveraged Lease Transaction" (FSP 13-2). FSP 13-2 addresses how a change or projected change in the timing of cash flows relating to income taxes generated

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

8. Recent Accounting Standards *(continued)*

by a leveraged lease transaction affects the accounting for the lease by the lessor, and directs that the tax assumptions be consistent with any FIN 48 uncertain tax position related to the lease. FSP 13-2 is effective for fiscal years beginning after December 15, 2006. Upon adoption, AIG recorded a $50 million decrease in the opening balance of retained earnings, net of tax, as of January 1, 2007 to reflect the cumulative effect of this change in accounting. The adoption of this guidance is not expected to have a material effect on the Company's results of operations in 2007.

As a result of the adoptions of SOP 05-1, FIN 48 and FSP 13-2, AIG recorded a total decrease to opening retained earnings of $203 million.

Future Application of Accounting Standards

FAS 157

In September 2006, the FASB issued FAS No. 157, "Fair Value Measurements" (FAS 157). FAS 157 defines fair value, establishes a framework for measuring fair value and expands disclosures about fair value measurements. FAS 157 is effective January 1, 2008. AIG is currently assessing the effect of implementing this guidance.

FAS 159

In February 2007, the FASB issued FAS No. 159, "The Fair Value Option for Financial Assets and Financial Liabilities" (FAS 159). FAS 159 permits entities to choose to measure at fair value many financial instruments and certain other items that are not currently required to be measured at fair value. Subsequent changes in fair value for designated items will be required to be reported in earnings in the current period. FAS 159 also establishes presentation and disclosure requirements for similar types of assets and liabilities measured at fair value. FAS 159 is effective January 1, 2008. AIG is currently assessing the effect of implementing this guidance, which depends on the nature and extent of items elected to be measured at fair value upon initial application of the standard on January 1, 2008.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

9. Information Provided in Connection with Outstanding Debt

The following condensed consolidating financial statements are provided in compliance with Regulation S-X of the Securities and Exchange Commission.

(a) American General Corporation (AGC) is a holding company and a wholly owned subsidiary of AIG. AIG provides a full and unconditional guarantee of all outstanding debt of AGC.

American General Corporation:

Condensed Consolidating Balance Sheet

(in millions)	American International Group, Inc. (As Guarantor)	AGC	Other Subsidiaries	Eliminations	Consolidated AIG
March 31, 2007					
Assets:					
Investments and financial services assets	**$ 10,529**	**$ –**	**$ 813,303**	**$ (18,924)**	**$804,908**
Cash	**47**	**–**	**1,655**	**–**	**1,702**
Carrying value of subsidiaries and partially owned companies, at equity	**113,412**	**28,145**	**9,396**	**(149,774)**	**1,179**
Other assets	**4,693**	**2,669**	**186,519**	**(1,923)**	**191,958**
Total assets	**$128,681**	**$30,814**	**$1,010,873**	**$ (170,621)**	**$999,747**
Liabilities:					
Insurance liabilities	**$ 16**	**$ –**	**$ 499,951**	**$ (78)**	**$499,889**
Debt	**21,354**	**2,136**	**150,907**	**(17,186)**	**157,211**
Other liabilities	**4,256**	**3,239**	**235,176**	**(3,179)**	**239,492**
Total liabilities	**25,626**	**5,375**	**886,034**	**(20,443)**	**896,592**
Preferred shareholders' equity in subsidiary companies	**–**	**–**	**100**	**–**	**100**
Total shareholders' equity	**103,055**	**25,439**	**124,739**	**(150,178)**	**103,055**
Total liabilities, preferred shareholders' equity in subsidiary companies and shareholders' equity	**$128,681**	**$30,814**	**$1,010,873**	**$ (170,621)**	**$999,747**
December 31, 2006					
Assets:					
Investments and financial services assets	$ 7,346	$ –	$797,976	$ (14,822)	$790,500
Cash	76	–	1,514	–	1,590
Carrying value of subsidiaries and partially owned companies, at equity	109,125	27,967	8,436	(144,427)	1,101
Other assets	3,989	2,622	181,561	(1,949)	186,223
Total assets	$120,536	$30,589	$989,487	$ (161,198)	$979,414
Liabilities:					
Insurance liabilities	$ 21	$ –	$495,135	$ (64)	$495,092
Debt	15,157	2,136	146,206	(14,820)	148,679
Other liabilities	3,681	3,508	228,068	(1,482)	233,775
Total liabilities	18,859	5,644	869,409	(16,366)	877,546
Preferred shareholders' equity in subsidiary companies	–	–	191	–	191
Total shareholders' equity	101,677	24,945	119,887	(144,832)	101,677
Total liabilities, preferred shareholders' equity in subsidiary companies and shareholders' equity	$120,536	$30,589	$989,487	$ (161,198)	$979,414

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

9. Information Provided in Connection with Outstanding Debt *(continued)*

Condensed Consolidating Statement of Income

(in millions)	American International Group, Inc. (As Guarantor)	AGC	Other Subsidiaries	Eliminations	Consolidated AIG
Three Months Ended March 31, 2007					
Operating income (loss)	**$ (261)**	**$ (73)**	**$6,506**	**$ –**	**$6,172**
Equity in undistributed net income of consolidated subsidiaries	**3,244**	**151**	**–**	**(3,395)**	**–**
Dividend income from consolidated subsidiaries	**1,286**	**440**	**–**	**(1,726)**	**–**
Income taxes	**139**	**8**	**1,579**	**–**	**1,726**
Minority interest	**–**	**–**	**(316)**	**–**	**(316)**
Net income (loss)	**$4,130**	**$510**	**$4,611**	**$(5,121)**	**$4,130**
Three Months Ended March 31, 2006					
Operating income (loss)	$ (286)	$ (38)	$5,117	$ –	$4,793
Equity in undistributed net income of consolidated subsidiaries	3,260	359	–	(3,619)	–
Dividend income from consolidated subsidiaries	187	304	–	(491)	–
Income taxes (benefits)	–	(13)	1,448	–	1,435
Minority interest	–	–	(197)	–	(197)
Cumulative effect of an accounting change, net of tax	34	–	–	–	34
Net income (loss)	$3,195	$638	$3,472	$(4,110)	$3,195

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

9. Information Provided in Connection with Outstanding Debt *(continued)*

Condensed Consolidating Statement of Cash Flow

(in millions)	American International Group, Inc. (As Guarantor)	AGC	Other Subsidiaries	Consolidated AIG
Three Months Ended March 31, 2007				
Net cash provided by operating activities	**$ 261**	**$ 48**	**$ 8,324**	**$ 8,633**
Cash flows from investing:				
Invested assets disposed	**170**	**–**	**38,875**	**39,045**
Invested assets acquired	**(3,520)**	**–**	**(52,129)**	**(55,649)**
Other	**349**	**–**	**(608)**	**(259)**
Net cash used in investing activities	**(3,001)**	**–**	**(13,862)**	**(16,863)**
Cash flows from financing activities:				
Issuance of debt	**6,831**	**–**	**17,353**	**24,184**
Repayments of debt	**(728)**	**–**	**(15,596)**	**(16,324)**
Payments advanced to purchase shares	**(3,000)**	**–**	**–**	**(3,000)**
Cash dividends paid to shareholders	**(430)**	**–**	**–**	**(430)**
Other	**38**	**(48)**	**3,932**	**3,922**
Net cash provided by (used in) financing activities	**2,711**	**(48)**	**5,689**	**8,352**
Effect of exchange rate changes on cash	**–**	**–**	**(10)**	**(10)**
Change in cash	**(29)**	**–**	**141**	**112**
Cash at beginning of period	**76**	**–**	**1,514**	**1,590**
Cash at end of period	**$ 47**	**$ –**	**$ 1,655**	**$ 1,702**
Three Months Ended March 31, 2006				
Net cash (used in) provided by operating activities	$ (956)	$ 45	$ 4,759	$ 3,848
Cash flows from investing:				
Invested assets disposed	1,269	–	35,578	36,847
Invested assets acquired	–	–	(54,706)	(54,706)
Other	(2,283)	–	2,035	(248)
Net cash used in investing activities	(1,014)	–	(17,093)	(18,107)
Cash flows from financing activities:				
Issuance of debt	2,407	–	14,792	17,199
Repayments of debt	(145)	(1)	(9,535)	(9,681)
Cash dividends paid to shareholders	(390)	–	–	(390)
Other	33	(44)	6,470	6,459
Net cash provided by (used in) financing activities	1,905	(45)	11,727	13,587
Effect of exchange rate changes on cash	–	–	23	23
Change in cash	(65)	–	(584)	(649)
Cash at beginning of period	190	–	1,707	1,897
Cash at end of period	$ 125	$ –	$ 1,123	$ 1,248

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

9. Information Provided in Connection with Outstanding Debt *(continued)*

(b) AIG Liquidity Corp. is a wholly owned subsidiary of AIG. AIG provides a full and unconditional guarantee of all obligations of AIG Liquidity Corp.

AIG Liquidity Corp.:

Condensed Consolidating Balance Sheet

(in millions)	American International Group, Inc. (As Guarantor)	AIG Liquidity Corp.	Other Subsidiaries	Eliminations	Consolidated AIG
March 31, 2007					
Assets:					
Investments and financial services assets	**$ 10,529**	**$***	**$ 813,303**	**$ (18,924)**	**$804,908**
Cash	**47**	*****	**1,655**	**–**	**1,702**
Carrying value of subsidiaries and partially owned companies, at equity	**113,412**	**–**	**37,541**	**(149,774)**	**1,179**
Other assets	**4,693**	*****	**189,188**	**(1,923)**	**191,958**
Total assets	**$128,681**	**$***	**$1,041,687**	**$ (170,621)**	**$999,747**
Liabilities:					
Insurance liabilities	**$ 16**	**$–**	**$ 499,951**	**$ (78)**	**$499,889**
Debt	**21,354**	*****	**153,043**	**(17,186)**	**157,211**
Other liabilities	**4,256**	*****	**238,415**	**(3,179)**	**239,492**
Total liabilities	**25,626**	*****	**891,409**	**(20,443)**	**896,592**
Preferred shareholders' equity in subsidiary companies	**–**	**–**	**100**	**–**	**100**
Total shareholders' equity	**103,055**	*****	**150,178**	**(150,178)**	**103,055**
Total liabilities, preferred shareholders' equity in subsidiary companies and shareholders' equity	**$128,681**	**$***	**$1,041,687**	**$ (170,621)**	**$999,747**
December 31, 2006:					
Assets:					
Investments and financial services assets	$ 7,346	$*	$ 797,976	$ (14,822)	$790,500
Cash	76	*	1,514	–	1,590
Carrying value of subsidiaries and partially owned companies, at equity	109,125	–	36,403	(144,427)	1,101
Other assets	3,989	*	184,183	(1,949)	186,223
Total assets	$120,536	$*	$1,020,076	$ (161,198)	$979,414
Liabilities:					
Insurance liabilities	$ 21	$–	$ 495,135	$ (64)	$495,092
Debt	15,157	*	148,342	(14,820)	148,679
Other liabilities	3,681	*	231,576	(1,482)	233,775
Total liabilities	18,859	*	875,053	(16,366)	877,546
Preferred shareholders' equity in subsidiary companies	–	–	191	–	191
Total shareholders' equity	101,677	*	144,832	(144,832)	101,677
Total liabilities, preferred shareholders' equity in subsidiary companies and shareholders' equity	$120,536	$*	$1,020,076	$ (161,198)	$979,414

**Amounts significantly less than $1 million.*

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

9. Information Provided in Connection with Outstanding Debt *(continued)*

Condensed Consolidating Statement of Income

(in millions)	American International Group, Inc. (As Guarantor)	AIG Liquidity Corp.	Other Subsidiaries	Eliminations	Consolidated AIG
Three Months Ended March 31, 2007					
Operating income (loss)	**$ (261)**	**$ ***	**$6,433**	**$ –**	**$6,172**
Equity in undistributed net income of consolidated subsidiaries	**3,244**	**–**	**151**	**(3,395)**	**–**
Dividend income from consolidated subsidiaries	**1,286**	**–**	**440**	**(1,726)**	**–**
Income taxes	**139**	*****	**1,587**	**–**	**1,726**
Minority interest	**–**	**–**	**(316)**	**–**	**(316)**
Net income (loss)	**$ 4,130**	**$ ***	**$5,121**	**$(5,121)**	**$4,130**
Three Months Ended March 31, 2006					
Operating income (loss)	$ (286)	$ *	$5,079	$ –	$4,793
Equity in undistributed net income of consolidated subsidiaries	3,260	–	359	(3,619)	–
Dividend income from consolidated subsidiaries	187	–	304	(491)	–
Income taxes	–	*	1,435	–	1,435
Minority interest	–	–	(197)	–	(197)
Cumulative effect of an accounting change, net of tax	34	–	–	–	34
Net income (loss)	$ 3,195	$ *	$4,110	$(4,110)	$3,195

**Amounts significantly less than $1 million.*

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

9. Information Provided in Connection with Outstanding Debt *(continued)*

Condensed Consolidating Statement of Cash Flow

(in millions)	American International Group, Inc. (As Guarantor)	AIG Liquidity Corp.	Other Subsidiaries	Consolidated AIG
Three Months Ended March 31, 2007				
Net cash provided by operating activities	**$ 261**	**$***	**$ 8,372**	**$ 8,633**
Cash flows from investing:				
Invested assets disposed	**170**	**–**	**38,875**	**39,045**
Invested assets acquired	**(3,520)**	**–**	**(52,129)**	**(55,649)**
Other	**349**	*****	**(608)**	**(259)**
Net cash used in investing activities	**(3,001)**	*****	**(13,862)**	**(16,863)**
Cash flows from financing activities:				
Issuance of debt	**6,831**	**–**	**17,353**	**24,184**
Repayments of debt	**(728)**	**–**	**(15,596)**	**(16,324)**
Payments advanced to purchase shares	**(3,000)**	**–**	**–**	**(3,000)**
Cash dividends paid to shareholders	**(430)**	**–**	**–**	**(430)**
Other	**38**	*****	**3,884**	**3,922**
Net cash provided by financing activities	**2,711**	*****	**5,641**	**8,352**
Effect of exchange rate changes on cash	**–**	**–**	**(10)**	**(10)**
Change in cash	**(29)**	*****	**141**	**112**
Cash at beginning of period	**76**	**–**	**1,514**	**1,590**
Cash at end of period	**$ 47**	**$***	**$ 1,655**	**$ 1,702**
Three Months Ended March 31, 2006				
Net cash (used in) provided by operating activities	$ (956)	$*	$ 4,804	$ 3,848
Cash flows from investing:				
Invested assets disposed	1,269	–	35,578	36,847
Invested assets acquired	–	–	(54,706)	(54,706)
Other	(2,283)	*	2,035	(248)
Net cash used in investing activities	(1,014)	*	(17,093)	(18,107)
Cash flows from financing activities:				
Issuance of debt	2,407	–	14,792	17,199
Repayments of debt	(145)	–	(9,536)	(9,681)
Cash dividends paid to shareholders	(390)	–	–	(390)
Other	33	*	6,426	6,459
Net cash provided by financing activities	1,905	*	11,682	13,587
Effect of exchange rate changes on cash	–	–	23	23
Change in cash	(65)	*	(584)	(649)
Cash at beginning of period	190	–	1,707	1,897
Cash at end of period	$ 125	$*	$ 1,123	$ 1,248

**Amounts significantly less than $1 million.*

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

10. Derivatives and Hedge Accounting

Derivatives, as defined in FAS 133, are financial arrangements among two or more parties with returns linked to or ''derived'' from some underlying equity, debt, commodity or other asset, liability, or foreign exchange rate or other index or the occurence of a specified payment event. Derivative payments may be based on interest rates, exchange rates, prices of certain securities, commodities, or financial or commodity indices or other variables. Collateral is required on certain transactions based on the creditworthiness of the counterparty.

Unless subject to a scope exclusion, AIG carries all derivatives on the Consolidated Balance Sheet at fair value. The changes in fair value of the derivative transactions of AIGFP are presented as a component of AIG's operating income. Gains or losses on derivative transactions for AIG other than those of AIGFP, and only the effective portion of those held as cash flow hedges, are presented in realized capital gains (losses). However, in certain instances, when significant inputs into model valuations are not supported by observable market data, income is not recognized at inception under EITF 02-03, and instead income is recognized over the life of the contract when those inputs become sufficiently observable.

AIG also uses derivatives and other instruments as part of its financial risk management programs. AIG applies hedge accounting to certain derivative instruments used to hedge interest rate and foreign exchange risk arising from assets, liabilities, and forecasted transactions. These derivative financial instruments are included in Other assets or Other liabilities for derivative activities of AIG other than those of AIGFP, and in Unrealized gain or loss on swaps, options and forward transactions for those of AIGFP.

AIG designates the derivative as: *(i)* a hedge of the changes in the fair value of a recognized asset or liability or of an unrecognized firm commitment (''fair value'' hedge); *(ii)* a hedge of a forecasted transaction, or the variability of cash flows to be received or paid related to a recognized asset or liability (''cash flow'' hedge); or *(iii)* a hedge of a net investment in a foreign operation (''net investment'' hedge). Fair value and cash flow hedges may involve hedges of foreign currencies exposure (''foreign currency'' hedge).

The change in fair value of a derivative that qualifies under the requirements of FAS 133 as a fair value hedge is recorded in current period earnings, along with the gain or loss on the hedged item attributable to the risk being hedged. The effective portion of the change in the fair value of a derivative that qualifies under the requirements of FAS 133 as a cash flow hedge is recorded in Accumulated other comprehensive income (loss), until earnings are affected by the variability of cash flows in the hedged item. The effective portion of the change in the fair value of a derivative that qualifies under the requirements of FAS 133 as a net investment hedge is recorded in the foreign currency translation adjustments account reported within Accumulated other comprehensive income (loss). Changes in the fair value of the hedging instrument measured as ineffectiveness are reported in current period earnings. AIG had no hedges that were designated as net investment hedges at March 31, 2007.

AIG performs and documents an initial prospective assessment of hedge effectiveness to demonstrate that the hedge is expected to be highly effective in future periods. Subsequently, on a regular basis, AIG performs a prospective hedge effectiveness assessment to demonstrate the continued expectation that the hedge will be highly effective in future periods and a retrospective hedge effectiveness assessment to demonstrate that the hedge was effective in the most recent period. AIG does not utilize the short cut method or equivalent methods for its ongoing assessment of hedge effectiveness.

Upon the discontinuance of hedge accounting, the derivatives are carried on the Consolidated Balance Sheet at fair value, with changes in fair value recognized currently in earnings. The carrying value of the hedged recognized asset or liability under a fair value hedge is no longer adjusted for changes in its fair value due to the hedged risk, and the cumulative adjustment to its carrying value is amortized into income over the remaining life of the hedged item. Provided the hedged forecasted transaction is still probable of occurrence, the changes in fair value of derivatives recorded in Other comprehensive income (loss) related to discontinued cash flow hedges are released into the Consolidated Statement of Income when AIG's earnings are affected by the variability in cash flows of the hedged item.

Upon the discontinuance of hedge accounting because it is no longer probable that the forecasted transactions will occur by the end of the specified time period or the hedged item no longer meets the definition of a firm commitment, the derivatives continue to be carried on the Consolidated Balance Sheet at fair value, with changes in fair value recognized currently in earnings. Any asset or liability associated with a recognized firm commitment is derecognized from

10. Derivatives and Hedge Accounting *(continued)*

the Consolidated Balance Sheet and recorded currently in earnings. Deferred gains and losses of a derivative recorded in Other comprehensive income (loss) pursuant to the cash flow hedge of a forecasted transaction are recognized immediately in earnings. AIG had no hedges for firm commitments or forecasted transactions at March 31, 2007.

For the first three months of 2007, the preponderance of the derivative transactions that were designated for hedge accounting were at AIGFP. AIGFP designated interest rate swaps as fair value hedges of the benchmark interest rate risk on its interest bearing financial assets and liabilities, and in particular, on its fixed rate available for sale debt securities and fixed rate borrowings. AIGFP also designated its foreign currency forwards as hedging its foreign currency denominated available for sale debt securities for changes in spot foreign exchange rates. AIG designated interest rate swaps and cross currency swaps as either fair value or cash flow hedges of certain of the borrowings of AIG parent.

Fair Value Hedges

AIG designates and accounts for the following as fair value hedges when they have met the requirements of FAS 133: (i) interest rate swaps to hedge issued fixed rate debt against changes in fair value due to changes in the benchmark interest rate; (ii) foreign currency swaps to hedge issued foreign currency debt against changes in fair value due to changes in the benchmark interest rate and/or spot foreign exchange rates; (iii) interest rate swaps to hedge fixed rate investments including available for sale debt securities against changes in fair value due to changes in the benchmark interest rate; and (iv) foreign currency forwards to hedge foreign currency investment securities classified as available for sale against changes in fair value due to changes in the spot foreign exchange rates.

During the three months ended March 31, 2007, AIG recognized a net gain of $2 million in Other income related to the ineffective portion of its hedging instruments, and a net loss of $54 million in Other income related to the portion of the hedging instruments related to the passage of time excluded from the assessment of hedge ineffectiveness. The amount recognized in Realized gains and losses for hedge ineffectiveness and the change in the hedging instrument's forward points excluded from the assessment of hedge ineffectiveness during the three months ended March 31, 2007 were each less than $1 million.

Cash Flow Hedges

AIG designates and accounts for the following as cash flow hedges, when they have met the requirements of FAS 133: (i) interest rate swaps to hedge issued floating rate debt against changes in its cash flows attributable to changes in the benchmark interest rate; (ii) foreign currency swaps to hedge issued foreign currency fixed rate debt against changes in its cash flows attributable to changes in the forward foreign exchange rates; and (iii) foreign currency swaps to hedge issued foreign currency floating rate debt against changes in its cash flows attributable to changes in the benchmark interest rate and spot foreign exchange rates.

The portion of the gain or loss in the fair value of a derivative instrument in a cash flow hedge that represents hedge ineffectiveness is recognized immediately in current period earnings. The amounts recognized during the three months ended March 31, 2007 were less than $1 million. There were no amounts recognized in 2006. All components of each derivative's gain or loss were included in the assessment of hedge ineffectiveness.

At March 31, 2007, $2 million of the deferred net gain (loss) on derivative instruments in Accumulated other comprehensive income (loss) is expected to be reclassified to earnings during the 12 months ending March 31, 2008. For the first three months ended March 31, 2007, there were no instances in which AIG reclassified amounts from Other comprehensive income to earnings as a result of a discontinuance of a cash flow hedge because it was probable the original forecasted transaction would not occur at the end of the specified time period.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

11. Cash Flows

As part of its remediation activities during 2006, AIG determined that certain non-cash activities and adjustments, including the effects of changes in foreign exchange translation on assets and liabilities, previously were misclassified within the operating, investing and financing sections of the Consolidated Statement of Cash flows. The more significant line items revised include the change in General and life insurance reserves and DAC within operating activities; Purchases of fixed maturity securities within investing activities; and Proceeds from notes, bonds, loans and mortgages payable, and hybrid financial instrument liabilities within financing activities. After evaluating the effect of these items during the third quarter of 2006, AIG revised the previous periods presented in its September 30, 2006 consolidated financial statements included in that quarter's Form 10-Q to conform to the 2006 presentation.

Subsequent to that revision, additional revisions were made, primarily relating to certain elements of realized capital gains and the effect of reclassifying certain policyholders' account balances from Other policyholder funds to Policyholders' contract deposits.

The effect of these revisions on the Consolidated Statement of Cash flows for the three months ended March 31, 2006 is presented below:

(in millions)	Originally Reported March 31, 2006	Revisions Third Quarter 2006	As Revised Third Quarter 2006	Additional Revisions	As Revised
For the three months ended March 31, 2006					
Cash flows from operating activities	$ 3,066	$ 1,076	$ 4,142	$(294)	$ 3,848
Cash flows from investing activities	(19,937)	1,724	(18,213)	106	(18,107)
Cash flows from financing activities	15,672	(2,273)	13,399	188	13,587
Effect of exchange rate changes on cash	550	(527)	23	—	23

ITEM 2. Management's Discussion and Analysis of Financial Condition and Results of Operations

Management's Discussion and Analysis of Financial Condition and Results of Operations is designed to provide the reader a narrative with respect to AIG's operations, financial condition and liquidity and certain other significant matters.

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Cautionary Statement Regarding Projections and Other Information About Future Events

This Quarterly Report on Form 10-Q and other publicly available documents may include, and AIG's officers and representatives may from time to time make, projections concerning financial information and statements concerning future economic performance and events, plans and objectives relating to management, operations, products and services, and assumptions underlying these projections and statements. These projections and statements are not historical facts but instead represent only AIG's belief regarding future events, many of which, by their nature, are inherently uncertain and outside AIG's control. These projections and statements may address, among other things, the status and potential future outcome of the current regulatory and civil proceedings against AIG and their potential effect on AIG's businesses, financial position, results of operations, cash flows and liquidity, the effect of credit rating changes on AIG's businesses and competitive position, the unwinding and resolving of various relationships between AIG and SICO and AIG's strategy for growth, product development, market position, financial results and reserves. It is possible that AIG's actual results and financial condition may differ, possibly materially, from the anticipated results and financial condition indicated in these projections and statements. Factors that could cause AIG's actual results to differ, possibly materially, from those in the specific projections and statements are discussed throughout this Management's Discussion and Analysis of Financial Condition and Results of Operations and in Item 1A. Risk Factors of AIG's Annual Report on Form 10-K for the year ended December 31, 2006 (2006 Annual Report on Form 10-K). AIG is not under any obligation (and expressly disclaims any such obligations) to update or alter any projection or other statement, whether written or oral, that may be made from time to time, whether as a result of new information, future events or otherwise.

In addition to reviewing AIG's results for the first three months of 2007, this Management's Discussion and Analysis supplements and updates the information and discussion included in the 2006 Annual Report on Form 10-K. Throughout this Management's Discussion and Analysis of Financial Condition and Results of Operations, AIG presents its operations in the way it believes will be most meaningful. Statutory loss ratios and combined ratios are presented in accordance with accounting principles prescribed by insurance regulatory authorities because these are standard measures of performance filed with insurance regulatory authorities and used for analysis in the insurance industry and thus allow more meaningful comparisons with AIG's insurance competitors. AIG has also incorporated into this discussion cross-references to additional information included in this Quarterly Report on Form 10-Q and in its 2006 Annual Report on Form 10-K to assist readers seeking related information on a particular subject.

Overview of Operations and Business Results

AIG identifies its reportable segments by product or service line, consistent with its management structure. AIG's segments are General Insurance, Life Insurance & Retirement Services, Financial Services and Asset Management. AIG's operations in 2007 and 2006 were conducted by its subsidiaries through these segments. Through these segments, AIG provides insurance, financial and investment products and services to both businesses and individuals in more than 130 countries and jurisdictions. This geographic, product and service diversification is one of AIG's major strengths and sets it apart from its competitors. AIG's Other category consists of items not allocated to AIG's operating segments.

AIG's subsidiaries serve commercial, institutional and individual customers through an extensive property-casualty and life insurance and retirement services network. In the United States, AIG companies are the largest underwriters of commercial and industrial insurance and are among the largest life insurance and retirement services operations as well. AIG's Financial Services businesses include commercial aircraft and equipment leasing, capital markets operations and consumer finance, both in the United States and abroad. AIG also provides asset management services to institutions and individuals. As part of its spread-based business activities, AIG issues various debt instruments in the public and private markets.

Outlook

The commercial property and casualty insurance industry has historically experienced cycles of price erosion followed by rate strengthening as a result of catastrophes or other significant losses that affect the overall capacity of the industry to provide coverage. Despite industry price erosion in commercial lines, AIG expects to continue to identify profitable opportunities and build attractive new general insurance businesses as a result of AIG's broad product line and extensive distribution networks in the U.S. and abroad. Workers compensation remains under considerable pricing pressure, as statutory rates continue to decline. Rates for excess casualty, D&O and certain other lines of insurance also continue to decline due to competitive pressures. There can be no assurance that price erosion will not become more widespread or that AIG's profitability will not deteriorate from current levels in major commercial lines; however, AIG seeks to mitigate this risk by constantly seeking out profitable opportunities across its diverse product lines and distribution networks.

In Japan, the National Tax Authority in cooperation with the Life Insurance Association of Japan is reviewing the tax treatment for increasing term life insurance, which may affect the amount of premiums that qualify as tax deductions for business owners. As a result of this review, AIG's life insurance companies in Japan suspended the sale of increasing term life insurance and other corporate tax products from early April 2007. This action will have an adverse effect on life insurance sales. AIG companies in Japan have taken several measures aimed at increasing sales of other products in the Japanese market, especially sales of U.S. dollar life insurance products.

In March 2007, the U.S. Treasury Department published proposed new regulations that, if adopted in their current form, would limit the ability of U.S. taxpayers to claim foreign tax credits in certain circumstances under the Internal Revenue Code. Should the proposed regulations be adopted in their current form, they would limit AIG's ability to claim foreign tax credits in connection with certain structured transactions entered into by AIGFP, resulting in a material adverse effect on AIGFP's operating results.

The operating results of AIG's consumer finance operations in the United States may be affected by further deterioration in the credit quality of loans originated to non-prime borrowers, the evolving changes in the regulatory environment and a slower residential housing market.

See also Management's Discussion and Analysis of Financial Condition and Results of Operations — Outlook in the 2006 Annual Report on Form 10-K.

Consolidated Results

The following table summarizes AIG's consolidated revenues, income before income taxes, minority interest and cumulative effect of an accounting change and net income:

(in millions)	Three Months Ended March 31, **2007**	2006	Percentage Increase/ (Decrease)
Total revenues	**$30,645**	$27,278	12%
Income before income taxes, minority interest and cumulative effect of an accounting change	**6,172**	4,793	29
Net income	**$ 4,130**	$ 3,195	29%

Revenues for the first three months of 2007 increased from the same period of 2006 as revenues grew in each of AIG's operating segments.

AIG's income before income taxes, minority interest and cumulative effect of an accounting change increased in the first three months of 2007 compared to the same period of 2006 as growth in the General Insurance, Financial Services and Asset Management segments were partially offset by a decline in the Life Insurance & Retirement Services segment. Financial Services results reflect the reinstitution of hedge accounting in the Capital Markets operation.

During the first quarter of 2007, AIG recorded certain out of period adjustments. These adjustments collectively decreased pre-tax operating income by $192 million and net income by $254 million. The adjustments are comprised principally of a $129 million increase to tax expense related to the remediation of the material weakness in controls over income tax accounting, and $130 million in pre-tax charges and write-offs related to other remediation activities ($97 million after tax).

The effective tax rate decreased from 29.9 percent for the first three months of 2006 to 28.0 percent for the first three months of 2007, primarily due to the recognition of $175 million of tax benefits associated with the SICO Plans for which the compensation expense had been recognized in prior years.

Results for the first three months of 2006 were negatively affected by the compensation expense relating to the Starr tender offer ($54 million before and after tax) and an additional allowance for losses in AIG Credit Card Company (Taiwan) ($88 million before tax and $57 million after tax). Results in the first three months of 2006 were also negatively affected by certain out of period adjustments of $61 million (before and after tax) of expenses related to the SICO Plans, $59 million ($38 million after tax) of expenses related to deferred advertising costs in General Insurance, a decrease of $300 million ($145 million after tax) in revenues related to the remediation of the 2006 material weakness in accounting for certain derivative transactions under FAS 133, and a $126 million of income tax expense as part of the ongoing remediation of the material weakness in controls over income tax accounting.

Segment Results

The following table summarizes the operations of each principal segment. (See also Note 2 of Notes to Consolidated Financial Statements.)

(in millions)	**Three Months Ended March 31, 2007**	2006	Percentage Increase/ (Decrease)
Revenues[(a)]:			
General Insurance[(b)]	**$12,903**	$11,656	11%
Life Insurance & Retirement Services[(c)]	**13,682**	12,850	6
Financial Services[(d)(e)]	**2,201**	1,666	32
Asset Management[(f)]	**1,908**	1,139	68
Other	**102**	90	13
Consolidation and eliminations	**(151)**	(123)	–
Consolidated	**$30,645**	$27,278	12%
Operating income (loss)[(a)(g)]:			
General Insurance	**$ 3,096**	$ 2,331	33%
Life Insurance & Retirement Services	**2,281**	2,630	(13)
Financial Services[(e)]	**292**	(108)	–
Asset Management	**994**	449	121
Other	**(499)**	(509)	–
Consolidation and eliminations	**8**	–	–
Consolidated	**$ 6,172**	$ 4,793	29%

(a) Includes the effect of hedging activities that did not qualify for hedge accounting treatment under FAS 133 or for which hedge accounting was not applied, including the related foreign exchange gains and losses. For the first three months of 2007 and 2006, respectively, the effect was $(452) million and $(212) million in revenues and operating income. These amounts result primarily from interest rate and foreign currency derivatives that are hedging investments and borrowings.

(b) Represents the sum of General Insurance net premiums earned, net investment income and realized capital gains (losses).

(c) Represents the sum of Life Insurance & Retirement Services premiums and other considerations, net investment income and realized capital gains (losses). Included in realized capital gains (losses) and operating income is the effect of hedging activities that did not qualify for hedge accounting treatment under

FAS 133 which were $(123) million and $352 million for the first three months of 2007 and 2006, respectively, and the application of FAS 52, which were $123 million and $4 million for the first three months of 2007 and 2006, respectively.

(d) Represents interest, lease and finance charges.

(e) Includes the effect of hedging activities that did not qualify for hedge accounting treatment under FAS 133 or for which hedge accounting was not applied, including the related foreign exchange gains and losses. For the three months ended March 31, 2007 and 2006, respectively, the effect was $(160) million, and $(619) million in both revenues and operating income. These amounts result primarily from interest rate and foreign currency derivatives that are effective economic hedges of investments and borrowings. In the first quarter of 2007, AIG began applying hedge accounting for certain transactions, primarily in its Capital Markets operations.

(f) Represents net investment income with respect to spread-based products and management and advisory fees.

(g) Represents income before income taxes, minority interest and cumulative effect of an accounting change.

General Insurance

AIG's General Insurance operations provide property and casualty products and services throughout the world. The increase in General Insurance operating income in the first three months of 2007 compared to the same period of 2006 was primarily attributable to improved underwriting results for DBG and higher net investment income.

Life Insurance & Retirement Services

AIG's Life Insurance & Retirement Services operations provide insurance, financial and investment products throughout the world. Foreign operations provided approximately 56 percent and 64 percent of AIG's Life Insurance & Retirement Services operating income for the first three months of 2007 and 2006, respectively. This decline resulted principally from realized capital losses in the first three months of 2007.

Life Insurance & Retirement Services total revenues increased in the first three months of 2007 compared to the same period of 2006, reflecting growth in premiums and net investment income partially offset by decreased realized capital gains (losses). Operating income decreased in the first three months of 2007 compared to the same period of 2006 due to realized capital gains (losses). Realized capital losses included in revenues and operating income were $256 million in the first three months of 2007 compared to realized capital gains of $216 million in the same period of 2006. Foreign Life operations' results for 2007 also included an out of period charge of $50 million related to balance sheet reconciliation remediation, a $37 million charge for additional claim expense resulting from a continuing industry-wide regulatory review of claims in Japan and a $10 million charge related to the adoption of SOP 05-1. Domestic Life Insurance operating income declined from the prior year primarily due to a $22 million charge related to the adoption of SOP 05-1 along with lower realized capital gains. Domestic Retirement Services operating results increased in the first three months of 2007 compared to the same period of 2006 due to higher premiums and other considerations along with lower realized capital losses.

Financial Services

AIG's Financial Services subsidiaries engage in diversified activities including aircraft and equipment leasing, capital markets, consumer finance and insurance premium finance.

Financial Services operating income increased in the first three months of 2007 compared to the same period of 2006 primarily due to differences in the accounting treatment for hedging activities. In the first three months of 2007, AIGFP applied hedge accounting to certain of its interest rate swaps and foreign currency forward contracts hedging its investments and borrowings. As a result, AIGFP was able to recognize in earnings the change in the fair value on the hedged items attributable to the hedged risks offsetting the gains and losses on the derivatives designated as hedges. In 2006, AIGFP did not apply hedge accounting under FAS 133 to any of its derivatives or related assets and liabilities.

In the first three months of 2007, the domestic consumer finance operations recorded a pre-tax charge of $128 million in connection with its mortgage banking activities.

Asset Management

AIG's Asset Management operations include institutional and retail asset management, broker-dealer services and institutional spread-based investment businesses. The Matched Investment Program (MIP) has replaced the GIC program as AIG's principal institutional spread-based investment activity.

Asset Management operating income increased in the first three months of 2007 compared to the same period of 2006 due primarily to growth in the Spread-Based Investment and Institutional Asset Management businesses. Other revenues and operating income for Asset Management also increased from a year ago due to higher income from partnerships. Gains and losses arising from the consolidation of certain partnerships, private equity investments and real estate funds are included in operating income, but are offset in minority interest expense, which is not a component of operating income.

Capital Resources

In March 2007, AIG issued $3.7 billion of junior subordinated debentures in three series of securities. The proceeds from the sales are being used to repurchase shares of AIG's common stock.

At March 31, 2007, AIG had total consolidated shareholders' equity of $103.1 billion and total consolidated borrowings of $157.2 billion. At that date, $140.3 billion of such borrowings were not guaranteed by AIG, were matched borrowings by AIG Parent or AIGFP, or represented junior subordinated debt or liabilities connected to trust preferred stock.

In February 2007, AIG's Board of Directors increased its share repurchase program by authorizing the repurchase of shares with an aggregate purchase price of $8 billion. Share repurchases during 2007 are described under Capital Resources and Liquidity — Share Repurchases and in Item 2. of Part II of this Quarterly Report on Form 10-Q.

Liquidity

AIG manages liquidity at both the subsidiary and parent company levels. At March 31, 2007, AIG's consolidated invested assets, primarily held by its subsidiaries, included $27.6 billion in cash and short-term investments. Consolidated net cash provided from operating activities in the first three months of 2007 amounted to $8.6 billion. Management believes that AIG's liquid assets, cash provided by operations and access to the capital markets will enable it to meet its anticipated cash requirements, including the funding of increased dividends under AIG's new dividend policy and repurchases of common stock.

Critical Accounting Estimates

AIG considers its most critical accounting estimates to be those relating to reserves for losses and loss expenses, future policy benefits for life and accident and health contracts, recoverability of DAC, estimated gross profits for investment-oriented products, fair value determinations for certain Capital Markets assets and liabilities, other-than-temporary declines in the value of investments and flight equipment recoverability. These accounting estimates require the use of assumptions about matters, some of which are highly uncertain at the time of estimation. To the extent actual experience differs from the assumptions used, AIG's results of operations would be directly affected.

Throughout this Management's Discussion and Analysis of Financial Condition and Results of Operations, AIG's critical accounting estimates are discussed in detail. The major categories for which assumptions are developed and used to establish each critical accounting estimate are highlighted below.

Reserves for Losses and Loss Expenses (General Insurance):

- *Loss trend factors:* used to establish expected loss ratios for subsequent accident years based on premium rate adequacy and the projected loss ratio with respect to prior accident years.
- *Expected loss ratios for the latest accident year:* in this case, accident year 2006 for the year-end 2006 loss reserve analysis. For low-frequency, high-severity classes such as excess casualty, expected loss ratios generally are utilized for at least the three most recent accident years.
- *Loss development factors:* used to project the reported losses for each accident year to an ultimate amount.
- *Reinsurance recoverable on unpaid losses:* the expected recoveries from reinsurers on losses that have not yet been reported and/or settled.

Future Policy Benefits for Life and Accident and Health Contracts (Life Insurance & Retirement Services):

- *Interest rates:* which vary by geographical region, year of issuance and products.
- *Mortality, morbidity and surrender rates:* based upon actual experience by geographical region modified to allow for variation in policy form, risk classification and distribution channel.

Estimated Gross Profits (Life Insurance & Retirement Services):

- *Estimated gross profits:* to be realized over the estimated duration of the contracts (investment-oriented products) affect the carrying value of DAC, unearned revenue liability and associated amortization patterns under FAS 97 and Sales Inducement Assets under Statement of Position 03-1, "Accounting and Reporting by Insurance Enterprises for Certain Nontraditional Long-Duration Contracts and for Separate Accounts" (SOP 03-1). Estimated gross profits include investment income and gains and losses on investments less required interest, actual mortality and other expenses.

Deferred Policy Acquisition Costs (Life Insurance & Retirement Services):

- *Recoverability:* based on current and future expected profitability, which is affected by interest rates, foreign exchange rates, mortality experience, and policy persistency.

Deferred Policy Acquisition Costs (General Insurance):

- *Recoverability and eligibility:* based upon the current terms and profitability of the underlying insurance contracts.

Fair Value Determinations Of Certain Assets And Liabilities (Financial Services):

- *Valuation models:* utilizing factors, such as market liquidity and current interest, foreign exchange and volatility rates.
- *Market price data:* AIG attempts to secure reliable and independent current market price data, such as published exchange rates from external subscription services such as Bloomberg or Reuters or third-party broker quotes for use in its models. When such data is not available, AIG uses an internal methodology, which includes interpolation and extrapolation from verifiable recent prices.

Other-Than-Temporary Declines In The Value Of Investments:
A security is considered a candidate for other-than-temporary impairment if it meets any of the following criteria:

- Trading at a significant (25 percent or more) discount to par or amortized cost (if lower) for an extended period of time (nine months or longer);
- The occurrence of a discrete credit event resulting in the debtor defaulting or seeking bankruptcy or insolvency protection or voluntary reorganization; or
- The probability of non-realization of a full recovery on its investment, irrespective of the occurrence of one of the foregoing events.

At each balance sheet date, AIG evaluates its securities holdings in an unrealized loss position. Where AIG does not intend to hold such securities until they have fully recovered their carrying value, based on the circumstances present at the date of evaluation, AIG records the unrealized loss in income. If events or circumstances change, such as unexpected changes in the creditworthiness of the obligor, unanticipated changes in interest rates, tax laws, statutory capital positions and unforeseen liquidity events, among others, AIG revisits its intent. Further, if a loss is recognized from a sale subsequent to a balance sheet date pursuant to these unexpected changes in circumstances, the loss is recognized in the period in which the intent to hold the securities to recovery no longer existed.

In periods subsequent to the recognition of an other-than-temporary impairment loss for debt securities, AIG amortizes the discount or reduced premium over the remaining life of the security in a prospective manner based on the amount and timing of estimated future cash flows.

Flight Equipment — Recoverability (Financial Services):

- *Expected undiscounted future net cash flows:* based upon current lease rates, projected future lease rates and estimated terminal values of each aircraft based on third party information.

Operating Review

General Insurance Operations

AIG's General Insurance subsidiaries are multiple line companies writing substantially all lines of property and casualty insurance and various personal lines both domestically and abroad.

Domestic General Insurance operations are comprised of DBG, Reinsurance, Personal Lines and Mortgage Guaranty businesses.

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

Transatlantic subsidiaries offer reinsurance capacity on both a treaty and facultative basis both in the U.S. and abroad. Transatlantic structures programs for a full range of property and casualty products with an emphasis on specialty risk.

AIG's Personal Lines operations provide automobile insurance through AIG Direct, a mass marketing operation, the Agency Auto Division and 21st Century, as well as a broad range of coverages for high net-worth individuals through the AIG Private Client Group.

The main business of the UGC subsidiaries is the issuance of residential mortgage guaranty insurance on conventional first lien mortgages for the purchase or refinance of one to four family residences. UGC subsidiaries also write second-lien and private student loan guaranty insurance.

AIG's Foreign General Insurance group accepts risks primarily underwritten through American International Underwriters (AIU), a marketing unit consisting of wholly owned agencies and insurance companies. The Foreign General Insurance group also includes business written by AIG's foreign-based insurance subsidiaries.

General Insurance Results

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

(in millions, except ratios)	Three Months Ended March 31, 2007	2006	Percentage Increase/ (Decrease)
Net premiums written:			
Domestic General			
DBG	**$ 6,009**	$ 5,860	**3%**
Transatlantic	**984**	914	**8**
Personal Lines	**1,229**	1,198	**3**
Mortgage Guaranty	**266**	197	**35**
Foreign General[(a)]	**3,618**	3,086	**17**
Total	**$12,106**	$11,255	**8%**
Net premiums earned:			
Domestic General			
DBG	**$ 5,981**	$ 5,769	**4%**
Transatlantic	**965**	908	**6**
Personal Lines	**1,155**	1,159	**–**
Mortgage Guaranty	**210**	166	**27**
Foreign General[(a)]	**2,908**	2,468	**18**
Total	**$11,219**	$10,470	**7%**
Net investment income:			
Domestic General			
DBG	**$ 1,033**	$ 745	**39%**
Transatlantic	**116**	102	**14**
Personal Lines	**57**	57	**–**
Mortgage Guaranty	**37**	32	**16**
Foreign General	**319**	182	**75**
Reclassifications and Eliminations	**1**	–	**–**
Total	**$ 1,563**	$ 1,118	**40%**
Realized capital gains (losses)	**$ 121**	$ 68	**78%**
Operating Income[(b)]:			
Domestic General			
DBG	**$ 1,929**	$ 1,305	**48%**
Transatlantic	**151**	141	**7**
Personal Lines	**106**	101	**5**
Mortgage Guaranty	**8**	109	**(93)**
Foreign General[(c)]	**909**	673	**35**
Reclassifications and Eliminations	**(7)**	2	**–**
Total	**$ 3,096**	$ 2,331	**33%**
Statutory underwriting profit (loss)[(b)(e)]:			
Domestic General			
DBG	**$ 784**	$ 484	**62%**
Transatlantic	**16**	30	**(47)**
Personal Lines	**33**	40	**(18)**
Mortgage Guaranty	**(42)**	70	**–**
Foreign General[(c)]	**402**	333	**21**
Total	**$ 1,193**	$ 957	**25%**
Domestic General[(b)]:			
Loss Ratio	**68.9**	71.5	
Expense Ratio	**21.1**	20.3	
Combined Ratio	**90.0**	91.8	
Foreign General[(b)]:			
Loss Ratio[(a)]	**50.6**	50.7	
Expense Ratio[(c)(d)]	**28.6**	28.6	
Combined ratio	**79.2**	79.3	
Consolidated[(c)]:			
Loss Ratio	**64.2**	66.7	
Expense Ratio	**23.3**	22.5	
Combined Ratio	**87.5**	89.2	

(a) Income statement accounts expressed in non-functional currencies are translated into U.S. dollars using average exchange rates.

(b) Includes additional losses incurred and net reinstatement premiums related to prior year catastrophes of $35 million and $99 million in the first three months of 2007 and 2006, respectively.

(c) Includes the results of wholly owned Foreign General agencies.

(d) Includes amortization of advertising costs.

(e) Statutory underwriting profit (loss) is a measure that U.S. domiciled insurance companies are required to report to their regulatory authorities. The following table reconciles statutory underwriting profit (loss) to operating income for General Insurance:

(in millions)	Domestic Brokerage Group	Transatlantic	Personal Lines	Mortgage Guaranty	Foreign General	Reclassifications and Eliminations	Total
Three Months Ended March 31, 2007:							
Statutory underwriting profit (loss)	**$ 784**	**$ 16**	**$ 33**	**$ (42)**	**$ 402**	**$ –**	**$ 1,193**
Increase (decrease) in DAC	**35**	**4**	**15**	**12**	**153**	**–**	**219**
Net investment income	**1,033**	**116**	**57**	**37**	**319**	**1**	**1,563**
Realized capital gains (losses)	**77**	**15**	**1**	**1**	**35**	**(8)**	**121**
Operating income (loss)	**$ 1,929**	**$ 151**	**$106**	**$ 8**	**$ 909**	**$ (7)**	**$ 3,096**
Three Months Ended March 31, 2006:							
Statutory underwriting profit (loss)	$ 484	$ 30	$ 40	$ 70	$ 333	$ –	$ 957
Increase (decrease) in DAC	29	3	5	7	144	–	188
Net investment income	745	102	57	32	182	–	1,118
Realized capital gains (losses)	47	6	(1)	–	14	2	68
Operating income (loss)	$ 1,305	$ 141	$101	$109	$ 673	$ 2	$ 2,331

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

	Three Months Ended March 31,	
	2007	2006
Growth in original currency*	**6.2%**	6.0%
Foreign exchange effect	**1.4**	(1.7)
Growth as reported in U.S. dollars	**7.6%**	4.3%

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

General Insurance operating income increased in the first three months of 2007 compared to the same period of 2006 due to growth in net premiums, a reduction in incurred losses and growth in net investment income. The combined ratio improved to 87.5, a reduction of 1.7 points from 2006, including an improvement in the loss ratio of 2.5 points. Prior year development reduced incurred losses by $131 million in the first three months of 2007, compared to an increase of $35 million in the first three months of 2006, representing 1.5 points of the overall reduction. The loss ratio for accident year 2007 recorded in the first quarter of 2007 was 1.0 point lower than the loss ratio recorded in the first quarter of 2006 for accident year 2006, despite an increase in Mortgage Guaranty losses in the 2007 period. The downward cycle in the U.S. housing market is not expected to improve until residential inventories return to a more normal level, and AIG expects that this downward cycle will continue to adversely affect UGC's loss ratios for the foreseeable future. Domestic General net premiums written increased as submission activity increased due to the strength of AIG's capacity, commitment during challenging market conditions and diverse product offerings. Foreign General also contributed to the increase in net premiums written, reflecting growth from both established and new distribution channels.

General Insurance net investment income increased in the first three months of 2007 to $1.6 billion. Interest and dividend income increased $195 million for the first three months of 2007 compared to the same period of 2006 as fixed maturities and equity securities increased by $13.9 billion and the yield remained consistent at 4.6 percent. Income from partnership investments increased $182 million for the first three months of 2007 compared to the year ago period, primarily due to improved returns on underlying investments and higher levels of invested assets, which increased by $900 million. See also Capital Resources and Liquidity — Liquidity and Invested Assets herein.

In order to better align financial reporting with the manner in which AIG's chief operating decision makers have managed their businesses, for the three months ended March 31, 2007, the foreign aviation business, which was historically reported in DBG, is now being reported as part of Foreign General and the oil rig and marine businesses, which were historically reported in Foreign General, are now being reported as part of DBG. Prior period amounts have been revised to conform to the current presentation.

DBG Results

DBG's operating income increased in the first three months of 2007 compared to the first three months of 2006. The improvement is also reflected in the combined ratio, which declined 4.6 points in the first three months of 2007 compared to the first three months of 2006 primarily due to an improvement in the loss ratio of 5.3 points. The loss ratio for accident year 2007 recorded in the first quarter of 2007 was

2.5 points lower than the loss ratio recorded in the first quarter of 2006 for accident year 2006. Prior year development reduced incurred losses by $87 million in the first three months of 2007 compared to an increase of $74 million in the first three months of 2006, accounting for 2.7 points of the improvement.

DBG's net premiums written increased 3 percent in the first three months of 2007 compared to the same period of 2006 due to the strength of AIG's capacity, commitment during challenging market conditions, diverse product offerings and the acquisition of TravelGuard, which markets accident and health products. Ceded premiums as a percentage of gross written premiums increased to 24 percent in the first three months of 2007 compared to 22 percent in the first three months of 2006, primarily due to additional reinsurance for property risks to manage catastrophe exposures.

DBG's expense ratio increased to 19.2 in the first three months of 2007 compared to 18.5 in the same period of 2006, primarily due to changes in the mix of business towards products with lower loss ratios and higher expense ratios.

DBG's net investment income increased in the first three months of 2007 compared to the same period of 2006, as interest income increased $120 million on growth in the bond portfolio resulting from investment of operating cash flows and capital contributions. Income from partnership investments increased $155 million in the first three months of 2007 compared to the same period of 2006, primarily due to improved returns on the underlying investments.

Transatlantic Results

Transatlantic's net premiums written and net premiums earned increased in the first three months of 2007 compared to the same period of 2006 due primarily to increased writings in domestic operations. Underwriting results were adversely affected by European windstorm losses, only partially offset by lower adverse development for the first three months of 2007 compared to the same period in 2006, resulting in an overall decline in statutory underwriting profit for the 2007 period. Operating income, however, increased in the first three months of 2007 compared to the same period of 2006 as increased net investment income and realized capital gains more than offset the decline in underwriting results.

Personal Lines Results

The modest increase in Personal Lines operating income in the first three months of 2007 compared to the same period of 2006 reflects a reduction in the loss ratio of 1.6 points. Favorable development of prior accident years reduced incurred losses by $29 million in the first three months of 2007 compared to a decrease of $19 million in the same period of 2006, accounting for 0.9 points of the decrease in the loss ratio. The loss ratio for the first three months of 2007 also improved 0.7 points compared to the same period in 2006, primarily due to favorable loss trends and growth in the Private Client Group, partially offset by increased losses in 21st Century. The improvement in the loss ratio was partially offset by an increase in the expense ratio of 1.4 points, primarily due to increased acquisition expenses by 21st Century along with growth in the Private Client Group, investments in human resources and technology, and lower average premiums.

The increase in net premiums written was driven by continued growth in the Private Client Group. 21st Century and AIG Direct net premiums written grew modestly at 3.6 percent and 2.4 percent, respectively, while Agency Auto declined 8.4 percent.

Mortgage Guaranty Results

The significant decline in Mortgage Guaranty operating income in the first quarter of 2007 compared to the same period in 2006 was due primarily to unfavorable loss experience in both the domestic first and second-lien businesses as a result of the continued softening in the U.S. housing market. Losses on UGC's subprime business were not significant. However the third-party originated second-lien product continued to perform poorly, resulting in $61 million of losses incurred in the first quarter of 2007. UGC's consolidated loss ratio for the quarter was 92.2 compared to a loss ratio of 30.4 for the same period in 2006. Prior year development increased incurred losses by $31 million in the first three months of 2007 compared to a reduction of $12 million in the first three months of 2006, accounting for 22 points of the increase in the loss ratio. The downward cycle in the U.S. housing market is not expected to improve until residential inventories return to a more normal level, and AIG expects that this downward cycle will continue to adversely affect UGC's operating results for the foreseeable future.

Net premiums written increased 35 percent in the first quarter of 2007 compared to the first quarter of 2006 as growth in the European markets resulted in a 189 percent increase in international premiums. In addition, second-lien premiums increased 49 percent due to higher renewal premiums on the domestic second-lien business. Although UGC discontinued accepting new business for the poorly performing third-party originated second-lien product in the fourth quarter of 2006, UGC will continue to receive renewal premiums on the existing portfolio for the life of the loans, estimated to be three to five years. The expense ratio of 21.7 in the first quarter of 2007 declined from 22.7 in the year ago quarter as premium growth offset expenses related to UGC's international expansion and additional operational resources in the second-lien and private education loan businesses.

Foreign General Insurance Results

Foreign General's operating income increased in the first three months of 2007 compared to the same period of 2006 due to increases in net investment income and statutory underwriting profit and the effect of changes in the exchange rates of the Euro and Sterling.

Net premiums written increased 17 percent (13 percent in original currency) in the first three months of 2007 compared to the same period of 2006, reflecting growth in commercial and consumer lines driven by new business from both established and new distribution channels, including a wholly owned insurance company in Vietnam and Central Insurance Co., Ltd. in Taiwan, and by greater retention of commercial lines accounts on renewal. Consumer lines in Latin America and commercial lines in Europe, the Far East and the U.K., also contributed to the increase. Net premiums written by the Lloyd's syndicate Ascot were essentially unchanged from the same period in 2006 as increased premiums due to rate increases were offset by decreased premiums due to loss of market share and higher reinsurance costs.

The loss ratio in the first three months of 2007 was essentially flat compared to the first quarter of 2006. Favorable loss development from prior accident years was relatively consistent in both periods. The 2007 loss ratio was negatively affected by an increase in personal accident losses in the Far East and an increase in severe but non-catastrophic losses, which were more than offset by reduced adverse development relating to the 2005 hurricanes.

The expense ratio was unchanged in the first three months of 2007 compared to the same period of 2006. The 2006 expense ratio reflected an out of period adjustment for amortization of deferred advertising costs which increased the first quarter 2006 expense ratio by 1.7 points. The comparable increase in the expense ratio in 2007 resulted from growth in certain commercial lines, which have higher acquisition expenses but historically lower loss ratios. AIG expects the expense ratio to increase during the remainder of 2007 as the consumer lines of business, which have higher acquisition costs, increase in significance as a component of net premiums written.

Net investment income increased in the first three months of 2007 compared to the same period of 2006 due to higher interest and dividend income of $56 million as a result of increased cash flows, higher interest rates and the compounding of previously earned and reinvested interest income. Net investment income also reflects increased equity mutual fund income of $52 million related to certain interests in unit investment trusts that AIG began recognizing in the second quarter of 2006, as well as increased equity partnership income.

Reserve for Losses and Loss Expenses

The following table presents the components of the General Insurance gross reserve for losses and loss expenses (loss reserves) as of March 31, 2007 and December 31, 2006 by major line of business on a statutory Annual Statement basis[a]:

(in millions)	**March 31, 2007**	December 31, 2006[b]
Other liability occurrence	**$19,763**	$19,327
Workers compensation	**14,265**	13,612
Other liability claims made	**13,180**	12,513
Auto liability	**6,144**	6,070
International	**6,049**	6,006
Property	**4,766**	5,499
Reinsurance	**3,108**	2,979
Medical malpractice	**2,332**	2,347
Products liability	**2,181**	2,239
Accident and health	**1,817**	1,693
Commercial multiple peril	**1,744**	1,651
Aircraft	**1,688**	1,629
Fidelity/surety	**1,234**	1,148
Other	**2,864**	3,286
Total	**$81,135**	$79,999

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

[b] Allocations among various lines were revised from the previous presentation.

AIG's gross reserve for losses and loss expenses represents the accumulation of estimates of ultimate losses, including IBNR and loss expenses. The methods used to determine loss reserve estimates and to establish the resulting reserves are continually reviewed and updated by management. Any adjustments resulting therefrom are reflected in operating income currently. Because loss reserve estimates are subject to the outcome of future events, changes in estimates are unavoidable given that loss trends vary and time is often required for changes in trends to be recognized and confirmed. Reserve changes that increase previous estimates of ultimate cost are referred to as unfavorable or adverse development or reserve strengthening. Reserve changes that decrease previous estimates of ultimate cost are referred to as favorable development.

At March 31, 2007, General Insurance net loss reserves increased $1.40 billion from the prior year-end to $64.03 billion. The net loss reserves represent loss reserves reduced by reinsurance recoverables, net of an allowance for unrecoverable reinsurance and applicable discount for future investment income.

The following table classifies the components of the General Insurance net loss reserves by business unit:

(in millions)	**March 31, 2007**	December 31, 2006
DBG[(a)]	**$45,014**	$44,119
Transatlantic	**6,407**	6,207
Personal Lines[(b)]	**2,373**	2,440
Mortgage Guaranty	**544**	460
Foreign General[(c)]	**9,696**	9,404
Total Net Loss Reserve	**$64,034**	$62,630

(a) At March 31, 2007 and December 31, 2006, respectively, DBG loss reserves include approximately $3.30 billion and $3.33 billion ($3.60 billion and $3.66 billion, respectively, before discount), related to business written by DBG but ceded to American International Reinsurance Company Limited (AIRCO) and reported in AIRCO's statutory filings. DBG loss reserves also include approximately $574 million and $535 million related to business included in American International Underwriters Overseas, Ltd.'s (AIUO) statutory filings at March 31, 2007 and December 31, 2006, respectively.

(b) At March 31, 2007 and December 31, 2006, respectively, Personal Lines loss reserves include $844 million and $861 million related to business ceded to DBG and reported in DBG's statutory filings.

(c) At March 31, 2007 and December 31, 2006, respectively, Foreign General loss reserves include approximately $2.80 billion and $2.75 billion related to business reported in DBG's statutory filings.

The DBG net loss reserve of $45.0 billion is comprised principally of the business of AIG subsidiaries participating in the American Home Assurance Company (American Home)/ National Union Fire Insurance Company of Pittsburgh, Pa. (National Union) pool (11 companies) and the surplus lines pool (Lexington, Starr Excess Liability Insurance Company and Landmark Insurance Company).

DBG cedes a quota share percentage of its other liability occurrence and products liability occurrence business to AIRCO. The quota share percentage ceded was 15 percent for the first quarter 2007 and 20 percent for the year 2006 and covered all business written in these years for these lines by participants in the American Home/National Union pool. AIRCO's loss reserves relating to these quota share cessions from DBG are recorded on a discounted basis. As of March 31, 2007, AIRCO carried a discount of approximately $300 million applicable to the $3.60 billion in undiscounted reserves it assumed from the American Home/National Union pool via this quota share cession. AIRCO also carries approximately $488 million in net loss reserves relating to Foreign General insurance business. These reserves are carried on an undiscounted basis.

The companies participating in the American Home/National Union pool have maintained a participation in the business written by AIU for decades. As of March 31, 2007, these AIU reserves carried by participants in the American Home/National Union pool totaled approximately $2.80 billion. The remaining Foreign General reserves are carried by AIUO, AIRCO, and other smaller AIG subsidiaries domiciled outside the United States. Statutory filings in the U.S. by AIG companies reflect all the business written by U.S. domiciled entities only, and therefore exclude business written by AIUO, AIRCO, and all other internationally domiciled subsidiaries. The total reserves carried at March 31, 2007 by AIUO and AIRCO were approximately $4.70 billion and $3.79 billion, respectively. AIRCO's $3.79 billion in total general insurance reserves consist of approximately $3.30 billion from business assumed from the American Home/National Union pool and an additional $488 million relating to Foreign General Insurance business.

Discounting of Reserves

At March 31, 2007, AIG's overall General Insurance net loss reserves reflects a loss reserve discount of $2.26 billion, including tabular and non-tabular calculations. The tabular workers compensation discount is calculated using a 3.5 percent interest rate and the 1979-81 Decennial Mortality Table. The non-tabular workers compensation discount is calculated separately for companies domiciled in New York and Pennsylvania, and follows the statutory regulations for each state. For New York companies, the discount is based on a five percent interest rate and the companies' own payout patterns. For Pennsylvania companies, the statute has specified discount factors for accident years 2001 and prior, which are based on a six percent interest rate and an industry payout pattern. For accident years 2002 and subsequent, the discount is based on the yield of U.S. Treasury securities ranging from one to twenty years and the company's own payout pattern, with the future expected payment for each year using the interest rate associated with the corresponding Treasury security yield for that time period. The discount is comprised of the following: $662 million – tabular discount for workers compensation in DBG; $1.30 billion – non-tabular discount for workers compensation in DBG; and, $300 million – non-tabular discount for other liability occurrence and products liability occurrence in AIRCO. The total undiscounted workers compensation loss reserve carried by DBG is approximately $11.8 billion as of March 31, 2007. The other liability occurrence and products liability occurrence business in AIRCO that is assumed from DBG is discounted based on the yield of U.S. Treasury securities ranging from one to twenty years and the DBG payout pattern for this business. The undiscounted reserves assumed by AIRCO from DBG totaled approximately $3.60 billion at March 31, 2007.

Quarterly Reserving Process

Management believes that the General Insurance net loss reserves are adequate to cover General Insurance net losses and loss expenses as of March 31, 2007. While AIG regularly reviews the adequacy of established loss reserves, there can be no assurance that AIG's ultimate loss reserves will not develop adversely and materially exceed AIG's loss reserves as of March 31, 2007. In the opinion of management, such adverse development and resulting increase in reserves is not likely to have a material adverse effect on AIG's consolidated

financial condition, although it could have a material adverse effect on AIG's consolidated results of operations for an individual reporting period.

The following table presents the reconciliation of net loss reserves:

(in millions)	Three Months Ended March 31, **2007**	2006
Net reserve for losses and loss expenses at beginning of year	**$62,630**	$57,476
Foreign exchange effect	**(38)**	117
Losses and loss expenses incurred:		
Current year	**7,215**	6,841
Prior years, other than accretion of discount	**(131)**	35
Prior years, accretion of discount	**116**	101
Losses and loss expenses incurred	**7,200**	6,977
Losses and loss expenses paid	**5,758**	5,678
Net reserve for losses and loss expenses at end of period	**$64,034**	$58,892

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

(in millions)	Three Months Ended March 31, **2007**	2006
Prior Accident Year Development by Reporting Unit:		
DBG	**$ (87)**	$ 74
Personal Lines	**(29)**	(19)
Mortgage Guaranty	**31**	(12)
Foreign General	**(64)**	(43)
Subtotal	**(149)**	—
Transatlantic	**18**	35
Prior years, other than accretion of discount	**$ (131)**	$ 35

(in millions)	Calendar Year **2007**	2006
Prior Accident Year Development by Accident Year:		
2006	**$ (178)**	
2005	**(31)**	$ (74)
2004	**(47)**	(124)
2003	**(9)**	(87)
2002	**18**	66
2001 & prior	**116**	254
Prior years, other than accretion of discount	**$ (131)**	$ 35

In determining the quarterly loss development from prior accident years, AIG conducts analyses to determine the change in estimated ultimate loss for each accident year for each profit center. For example, if loss emergence for a profit center is different than expected for certain accident years, the actuaries examine the indicated effect such emergence would have on the reserves of that profit center. In some cases, the higher or lower than expected emergence may result in no clear change in the ultimate loss estimate for the accident years in question, and no adjustment would be made to the profit center's reserves for prior accident years. In other cases, the higher or lower than expected emergence may result in a larger change, either favorable or unfavorable, than the difference between the actual and expected loss emergence. Such additional analyses were conducted for each profit center, as appropriate, in the first quarter of 2007 to determine the loss development from prior accident years for the first quarter of 2007. As part of its quarterly reserving process, AIG also considers notices of claims received with respect to emerging issues, such as those related to stock option backdating.

In the first three months of 2007, net loss development from prior accident years was favorable by approximately $131 million, including approximately $36 million of adverse development pertaining to the major hurricanes in 2004 and 2005; and $18 million of adverse development from the general reinsurance operations of Transatlantic; and excluding approximately $116 million from accretion of loss reserve discount. Excluding catastrophes and Transatlantic, as well as accretion of discount, net loss development in the first three months of 2007 from prior accident years was favorable by approximately $185 million. The overall favorable development of $131 million consisted of approximately $265 million of favorable development from accident years 2003 through 2006, partially offset by approximately $134 million of adverse development from accident years 2002 and prior. For the first three months of 2007, most classes of AIG's business continued to experience favorable development for accident years 2003 through 2006. The adverse development from accident years 2002 and prior reflected development from excess casualty within DBG and from Transatlantic. This adverse development from accident years 2002 and prior in the first three months of 2007 pertaining to excess casualty and to Transatlantic was significantly lower than the amounts of adverse development from these accident years observed during the first three months of 2006.

In the first three months of 2006, net adverse loss development from prior accident years was approximately $35 million, including approximately $98 million pertaining to catastrophes in 2004 and 2005 and $35 million from the general reinsurance operations of Transatlantic, but excluding approximately $101 million pertaining to accretion of loss reserve discount applicable to accident years 2005 and prior. Excluding catastrophes and Transatlantic, as well as accretion of discount, net loss development from prior accident years in the first three months of 2006 was favorable by approximately $98 million. The overall adverse development of $35 million consisted of approximately $285 million of favorable development from accident years 2003 through 2005, offset by approximately $320 million of adverse development from accident years 2002 and prior. Most classes of business throughout AIG experienced favorable development from accident years 2003 through 2005, other than the adverse development of $98 million pertaining to the 2004 and

2005 hurricanes. The adverse development from accident years 2002 and prior was primarily attributable to excess casualty business within DBG, and to Transatlantic, with a much smaller amount attributable to excess workers compensation business within DBG.

Asbestos and Environmental Reserves

The estimation of loss reserves relating to asbestos and environmental claims on insurance policies written many years ago is subject to greater uncertainty than other types of claims due to inconsistent court decisions as well as judicial interpretations and legislative actions that in some cases have tended to broaden coverage beyond the original intent of such policies and in others have expanded theories of liability.

As described more fully in the 2006 Annual Report on Form 10-K, AIG's reserves relating to asbestos and environmental claims reflect a comprehensive ground up analysis. In the first three months of 2007, AIG maintained the ultimate loss estimates for asbestos and environmental claims resulting from the recently completed reserve analyses. A minor amount of favorable incurred loss development pertaining to asbestos was reflected in the first three months of 2007, as depicted in the table that follows. This minor development is primarily attributable to one large settlement.

A summary of reserve activity, including estimates for applicable IBNR, relating to asbestos and environmental claims separately and combined:

	Three Months Ended March 31,			
	2007		2006	
(in millions)	**Gross**	**Net**	Gross	Net
Asbestos:				
Reserve for losses and loss expenses at beginning of year	**$4,464**	**$1,889**	$4,441	$1,840
Losses and loss expenses incurred*	**(11)**	**(17)**	5	2
Losses and loss expenses paid*	**(199)**	**(128)**	(149)	(54)
Reserve for losses and loss expenses at end of period	**$4,254**	**$1,744**	$4,297	$1,788
Environmental:				
Reserve for losses and loss expenses at beginning of year	**$ 588**	**$ 290**	$ 926	$ 410
Losses and loss expenses incurred*	**–**	**–**	–	–
Losses and loss expenses paid*	**(15)**	**(9)**	(21)	(9)
Reserve for losses and loss expenses at end of period	**$ 573**	**$ 281**	$ 905	$ 401
Combined:				
Reserve for losses and loss expenses at beginning of year	**$5,052**	**$2,179**	$5,367	$2,250
Losses and loss expenses incurred*	**(11)**	**(17)**	5	2
Losses and loss expenses paid*	**(214)**	**(137)**	(170)	(63)
Reserve for losses and loss expenses at end of period	**$4,827**	**$2,025**	$5,202	$2,189

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

The gross and net IBNR included in the reserve for losses and loss expenses, relating to asbestos and environmental claims separately and combined, were estimated as follows:

	Three Months Ended March 31,			
	2007		2006	
(in millions)	**Gross**	**Net**	Gross	Net
Asbestos	**$3,191**	**$1,436**	$3,314	$1,425
Environmental	**329**	**161**	572	256
Combined	**$3,520**	**$1,597**	$3,886	$1,681

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

	Three Months Ended March 31,					
	2007			2006		
	Asbestos	**Environmental**	**Combined**	Asbestos	Environmental	Combined
Claims at beginning of year	**6,878**	**9,442**	**16,320**	7,293	9,873	17,166
Claims during year:						
Opened	**200**	**411**	**611**	286	388	674
Settled	**(32)**	**(13)**	**(45)**	(37)	(42)	(79)
Dismissed or otherwise resolved	**(246)**	**(389)**	**(635)**	(295)	(296)	(591)
Claims at end of period	**6,800**	**9,451**	**16,251**	7,247	9,923	17,170

Survival Ratios — Asbestos and Environmental

The table below presents AIG's survival ratios for asbestos and environmental claims at March 31, 2007 and 2006. The survival ratio is derived by dividing the current carried loss reserve by the average payments for the three most recent calendar years for these claims. Therefore, the survival ratio is a simplistic measure estimating the number of years it would be before the current ending loss reserves for these claims would be paid off using recent year average payments. The March 31, 2007 survival ratio is lower than the ratio at March 31, 2006 because the more recent periods included in the rolling average reflect higher claims payments. In addition, AIG's survival ratio for asbestos claims was negatively affected in the first quarter of 2007 as a result of a large settlement. Many factors, such as aggressive settlement procedures, mix of business and level of coverage provided, have a significant effect on the amount of asbestos and environmental reserves and payments and the resultant survival ratio. Thus, caution should be exercised in attempting to determine reserve adequacy for these claims based simply on this survival ratio.

AIG's survival ratios for asbestos and environmental claims, separately and combined were based upon a three-year average payment. These ratios at March 31, 2007 and 2006 were as follows:

(number of years)	**Gross**	**Net**
2007		
Survival ratios:		
Asbestos	10.3	9.9
Environmental	5.5	4.4
Combined	9.4	8.4
2006		
Survival ratios:		
Asbestos	14.7	17.8
Environmental	7.1	6.4
Combined	12.4	13.5

Life Insurance & Retirement Services Operations

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

Domestically, AIG's Life Insurance & Retirement Services operations offer a broad range of protection products, such as life insurance and group life and health products, including disability income products and payout annuities, which include single premium immediate annuities, structured settlements and terminal funding annuities. Home service operations include an array of life insurance, accident and health and annuity products sold primarily through career agents. In addition, home service includes a small block of runoff property and casualty coverage. Retirement services include group retirement products, individual fixed and variable annuities sold through banks, broker-dealers and exclusive sales representatives, and annuity runoff operations, which include previously acquired "closed blocks" and other fixed and variable annuities largely sold through distribution relationships that have been discontinued.

Overseas, AIG's Life Insurance & Retirement Services operations include insurance and investment-oriented products such as whole and term life, investment linked, universal life and endowments, personal accident and health products, group products including pension, life and health, and fixed and variable annuities.

AIG's Life Insurance & Retirement Services subsidiaries report their operations through the following major internal reporting units and business units:

Foreign Life Insurance & Retirement Services

Japan and Other*

- ALICO
- AIG Star Life
- AIG Edison Life

Asia

- AIA
- Nan Shan
- AIRCO
- Philamlife

Domestic Life Insurance

- AIG American General
- USLIFE
- AGLA

Domestic Retirement Services

- VALIC
- AIG Annuity
- AIG SunAmerica

**Japan and Other consists of all operations in Japan and the operations of ALICO and its subsidiaries worldwide.*

Life Insurance & Retirement Services Results

Life Insurance & Retirement Services results were as follows:

(in millions)	Premiums and Other Considerations	Net Investment Income	Realized Capital Gains (Losses)	Total Revenues	Operating Income
Three months ended March 31, 2007					
Foreign Life Insurance & Retirement Services	**$6,613**	**$2,883**	**$(235)**	**$ 9,261**	**$1,284**
Domestic Life Insurance	**1,528**	**1,005**	**(12)**	**2,521**	**345**
Domestic Retirement Services	**284**	**1,625**	**(9)**	**1,900**	**652**
Total	**$8,425**	**$5,513**	**$(256)**	**$13,682**	**$2,281**
Three months ended March 31, 2006					
Foreign Life Insurance & Retirement Services	$6,117	$2,255	$ 352	$ 8,724	$1,686
Domestic Life Insurance	1,426	933	8	2,367	366
Domestic Retirement Services	257	1,646	(144)	1,759	578
Total	$7,800	$4,834	$ 216	$12,850	$2,630
Percentage Increase/(Decrease) from Prior Year:					
Foreign Life Insurance & Retirement Services	8%	28%	–%	6%	(24)%
Domestic Life Insurance	7	8	–	7	(6)
Domestic Retirement Services	11	(1)	94	8	13
Total	8%	14%	–%	6%	(13)%

The following table presents the Insurance In-force for Life Insurance & Retirement Services:

(in millions)	**March 31, 2007**	December 31, 2006
Foreign	**$1,158,107**	$ 1,162,699
Domestic	**924,440**	907,901
Total	**$2,082,547**	$ 2,070,600

Life Insurance & Retirement Services operating results for the first three months of 2007 reflect growth in premium and net investment income offset by realized capital losses. Realized capital losses reduced revenues and operating income by $256 million in the first three months of 2007 while realized capital gains increased revenues and operating income by $216 million in the same period of 2006. Realized capital losses in the Foreign Life operations in 2007 included losses related to derivatives that do not qualify for hedge accounting treatment and losses related to the decline in value of securities deemed to be other-than-temporary.

Operating results in the first three months of 2007 includes a charge of $32 million as a result of the adoption of SOP 05-1 which generally requires DAC related to group contracts to be amortized over a shorter duration than in prior periods, and also requires that DAC be expensed at the time a policy is terminated and cannot be re-capitalized if that policy is reinstated. The effect of SOP 05-1 was most significant to the group products line in the Domestic Life operations and was a significant factor in the decline of operating income for Domestic Life in the first three months of 2007 compared to the same period of 2006.

The growth in Domestic Retirement Services operating income in the first quarter of 2007 compared to the same period last year was driven by higher premiums and other considerations and lower realized capital losses. Although Domestic Retirement Services had realized capital losses of $144 million in the first three months of 2006 compared to a loss of $9 million in the same period of 2007, the effect of those losses in 2006 was partially offset by a corresponding reduction of $26 million in amortization of DAC.

In order to better align financial reporting with the manner in which AIG's chief operating decision makers have managed their businesses, for the three months ended March 31, 2007, revenues and operating income related to foreign investment contacts, which were historically reported as a component of the Spread-Based Investment Business in the Asset Management segment, are now being reported as part of Foreign Life Insurance & Retirement Services. Prior period amounts have been revised to conform to the current presentation.

Foreign Life Insurance & Retirement Services Results

Foreign Life Insurance & Retirement Services results were as follows:

(in millions)	Premiums and Other Considerations	Net Investment Income	Realized Capital Gains (Losses)	Total Revenues	Operating Income
Three months ended March 31, 2007					
Japan and Other:					
Life insurance	**$1,216**	**$ 550**	**$ (18)**	**$1,748**	**$ 352**
Personal accident	**1,028**	**50**	**2**	**1,080**	**289**
Group products	**575**	**150**	**5**	**730**	**73**
Individual fixed annuities	**116**	**546**	**(35)**	**627**	**147**
Individual variable annuities	**91**	**494**	**–**	**585**	**52**
Total	**$3,026**	**$1,790**	**$ (46)**	**$4,770**	**$ 913**
Asia:					
Life insurance	**$2,951**	**$1,007**	**$(150)**	**$3,808**	**$ 300**
Personal accident	**445**	**33**	**(10)**	**468**	**79**
Group products	**178**	**24**	**(26)**	**176**	**(10)**
Individual fixed annuities	**12**	**28**	**(2)**	**38**	**2**
Individual variable annuities	**1**	**1**	**(1)**	**1**	**–**
Total	**$3,587**	**$1,093**	**$(189)**	**$4,491**	**$ 371**
Total Foreign Life Insurance & Retirement Services:					
Life insurance	**$4,167**	**$1,557**	**$(168)**	**$5,556**	**$ 652**
Personal accident	**1,473**	**83**	**(8)**	**1,548**	**368**
Group products	**753**	**174**	**(21)**	**906**	**63**
Individual fixed annuities	**128**	**574**	**(37)**	**665**	**149**
Individual variable annuities	**92**	**495**	**(1)**	**586**	**52**
Total	**$6,613**	**$2,883**	**$(235)**	**$9,261**	**$1,284**
Three months ended March 31, 2006					
Japan and Other:					
Life insurance	$1,171	$ 456	$ 121	$1,748	$ 448
Personal accident	944	38	18	1,000	287
Group products	430	153	9	592	77
Individual fixed annuities	79	476	3	558	138
Individual variable annuities	61	305	–	366	28
Total	$2,685	$1,428	$ 151	$4,264	$ 978
Asia:					
Life insurance	$2,911	$ 756	$ 160	$3,827	$ 562
Personal accident	362	26	9	397	76
Group products	143	24	31	198	64
Individual fixed annuities	16	20	1	37	5
Individual variable annuities	–	1	–	1	1
Total	$3,432	$ 827	$ 201	$4,460	$ 708
Total Foreign Life Insurance & Retirement Services:					
Life insurance	$4,082	$1,212	$ 281	$5,575	$1,010
Personal accident	1,306	64	27	1,397	363
Group products	573	177	40	790	141
Individual fixed annuities	95	496	4	595	143
Individual variable annuities	61	306	–	367	29
Total	$6,117	$2,255	$ 352	$8,724	$1,686
Percentage Increase/(Decrease) from Prior Year:					
Japan and Other:					
Life insurance	4%	21%	–%	–%	(21)%
Personal accident	9	32	(89)	8	1
Group products	34	(2)	(44)	23	(5)
Individual fixed annuities	47	15	–	12	7
Individual variable annuities	49	62	–	60	86
Total	13%	25%	–%	12%	(7)%
Asia:					
Life insurance	1%	33%	–%	–%	(47)%
Personal accident	23	27	–	18	4
Group products	24	–	–	(11)	–
Individual fixed annuities	(25)	40	–	3	(60)
Individual variable annuities	–	–	–	–	–
Total	5%	32%	–%	1%	(48)%

(in millions)	Premiums and Other Considerations	Net Investment Income	Realized Capital Gains (Losses)	Total Revenues	Operating Income
Total Foreign Life Insurance & Retirement Services:					
Life insurance	2%	28%	–%	–%	(35)%
Personal accident	13	30	–	11	1
Group products	31	(2)	–	15	(55)
Individual fixed annuities	35	16	–	12	4
Individual variable annuities	51	62	–	60	79
Total	8%	28%	–%	6%	(24)%

AIG transacts business in most major foreign currencies and therefore premiums reported in U.S. dollars vary by volume and from changes in foreign currency translation rates. The following table summarizes the effect of changes in foreign currency exchange rates on the growth of the Foreign Life Insurance & Retirement Services premiums and other considerations:

	Three Months Ended March 31,	
	2007	2006
Growth in original currency*	**5.2%**	7.1%
Foreign exchange effect	**2.9**	(4.0)
Growth as reported in U.S. dollars	**8.1%**	3.1%

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

Japan and Other

Total revenues for the first three months of 2007 increased compared to the same period of 2006, primarily due to higher premium and net investment income partially offset by a decline in realized capital gains. Operating income growth decreased in the first three months of 2007 compared to the first three months of 2006 due to lower realized capital gains. In addition, a $37 million provision, including $25 million for personal accident, for additional claim expense was established in Japan as a result of a continuing industry-wide regulatory review of claims. That review is expected to be completed in late 2007.

Life insurance premiums and other considerations increased modestly in the first three months of 2007 compared to the same period of 2006. In Japan, increased fees and policy charges related to interest sensitive universal life and U.S. dollar life insurance products were partially offset by the runoff of the acquired blocks of business in AIG Star Life and AIG Edison Life. In Europe, growth in premiums and other considerations was enhanced by the foreign exchange effect. The growth in net investment income included higher partnership income, equity in unit investment trusts and growth in underlying invested assets. Life insurance operating income declined in the first three months of 2007 compared to the same period last year due to lower realized capital gains and an $11 million provision for additional claim expense resulting from the continuing industry-wide regulatory review of claims in Japan.

Personal accident premiums and other considerations continue to grow. New business in Japan has been adversely affected by increased competition and lower sales of tax-related products. Net investment income increased in the first three months of 2007 compared to the same period last year primarily due to higher invested assets and increased partnership income. Operating income growth in the first three months of 2007 was affected by lower realized capital gains, the $25 million provision for additional claim expenses and $15 million of higher expenses related to the termination of certain tax-related products in Japan. Loss ratios remained stable for this business which continues to enjoy relatively high margins.

Group products premiums and other considerations reflected growth for the first three months of 2007 compared to the same period last year primarily due to sales of credit and pension business in Europe. Net investment income declined from first quarter 2006 primarily due to the decline in interest rates in Brazil which adversely affected the pension business results. Operating income for the first quarter of 2007 declined from the same period last year primarily due to the decline in net investment income and lower realized capital gains.

Individual fixed annuities' premium and other considerations growth reflects higher surrender charges from U.S. dollar contracts in Japan where a weak yen makes it attractive for certain policyholders to lock in foreign exchange gains in excess of surrender charges. Net investment income increased due to higher average investment yields and higher assets under management. Management implemented a new investment strategy during the quarter to enhance future investment yields which resulted in realized capital losses in the current quarter as a small portion of the existing bond portfolio was sold and reinvested in higher yielding assets. The positive effect on operating income for the realized capital losses was $13 million, primarily related to lower DAC amortization. Operating income increased for the first three months of 2007 compared to the first three months of 2006 primarily due to growth in reserves and surrender charges.

Individual variable annuity assets under management, particularly in Europe, continued to grow due to new product offerings and stronger equity markets. The fees generated from the growth in assets under management increased premiums and operating income for the first three months of 2007 compared to the same period last year. Net investment income grew in the first three months of 2007 compared to the same period of 2006 due to increased policyholder trad-

ing gains which comprise the entirety of variable annuity net investment income. Policyholder trading gains are offset by an equal increase in policy benefits expense, as all investment returns for these variable annuities accrue to the benefit of the policyholder.

Asia

Total revenues for the first three months of 2007 were up slightly from last year's levels, while the growth in operating income fell compared to the same period of 2006. Net realized capital losses recorded in the current period compared to net realized capital gains recorded in the same period last year greatly influenced the low growth rate in total revenues and caused the decline in operating income. The net realized capital losses recorded in the current period were driven primarily by the mark to market of derivatives that did not qualify for hedge accounting treatment under FAS 133 along with the write-down of U.S. dollar bonds held in Singapore and Thailand where the decline in the value of those bonds when measured in the local currency was determined to be other than temporary. Premiums and other considerations grew in the current period reflecting a continued trend toward investment-oriented products where only a portion of policy charges collected from policyholders are reported as premium. Net investment income grew in the current period in line with the growth in underlying invested assets. Higher income from interests in unit investment trusts and higher policyholder trading gains, which are offset by an equal charge to incurred policy losses and benefits, also contributed to the growth.

Life insurance premiums and other considerations were flat in the first three months of 2007 compared to the same period of 2006, due to the shift in product mix from traditional life insurance products to investment-oriented products as mentioned above. Net investment income grew in the current period compared to the same period of 2006, due primarily to the growth in the underlying invested assets and in part due to earnings on certain interests in unit investment trusts along with higher policyholder trading gains. Operating income decreased in the first three months of 2007 compared to the same period last year, due mainly to the change in net realized capital gains (losses) which more than offset the growth in other sources of earnings. Operating income for the first three months of 2007 included a $50 million charge related to balance sheet reconciliation remediation activity. Operating income results for the first three months of 2006 included a $40 million loss from the Life Insurance & Retirement Services segment's share of the loss of AIG Credit Card Company (Taiwan).

Personal accident reported growth in total revenues and operating income for the first three months of 2007 compared to the same period in 2006. The higher revenues resulted from an increased focus on risk based accident and health products particularly in Korea and Taiwan. Operating earnings reflect the combined effect of premium growth and stable loss ratios that were partially offset by net realized capital losses.

Group products premiums and other considerations grew in the first three months of 2007 compared to the same period of 2006. The increase reflects the new business written in China, where AIG received approval to write group insurance in the second quarter of 2006, improved sales due to promotional activities in Thailand, and new business written in Hong Kong. Operating income declined in the first three months of 2007 compared to the same period of 2006, due in part to the net realized capital losses incurred and higher incurred policy losses and benefits of $13 million due to a 2007 out of period reserve charge.

Individual fixed annuity premiums declined in the first three months of 2007 compared to the same period of 2006, due primarily to the erosion of market share in Korea as a result of competition from higher yielding bank products.

Domestic Life Insurance Results

Domestic Life Insurance results, presented by sub-product were as follows:

(in millions)	Premiums and Other Considerations[a]	Net Investment Income	Realized Capital Gains (Losses)	Total Revenues	Operating Income (Loss)
Three months ended March 31, 2007					
Life insurance	$ 578	$ 372	$ (3)	$ 947	$187
Home service	195	161	(2)	354	82
Group life/health	229	53	(1)	281	3
Payout annuities[a]	512	289	(6)	795	51
Individual fixed annuities	2	27	–	29	4
Individual annuities – runoff[b]	12	103	–	115	18
Total	$ 1,528	$1,005	$ (12)	$2,521	$345

(in millions)	Premiums and Other Considerations[a]	Net Investment Income	Realized Capital Gains (Losses)	Total Revenues	Operating Income (Loss)
Three months ended March 31, 2006					
Life insurance	$ 516	$ 338	$ 62	$ 916	$240
Home service	200	158	(23)	335	59
Group life/health	246	54	(1)	299	19
Payout annuities	450	237	(18)	669	22
Individual fixed annuities	1	15	(2)	14	(2)
Individual annuities – runoff[b]	13	131	(10)	134	28
Total	$ 1,426	$ 933	$ 8	$2,367	$366
Percentage Increase/(Decrease) from Prior Year:					
Life insurance	12%	10%	–%	3%	(22)%
Home service	(3)	2	91	6	39
Group life/health	(7)	(2)	–	(6)	(84)
Payout annuities	14	22	67	19	132
Individual fixed annuities	100	80	–	107	–
Individual annuities – runoff[b]	(8)	(21)	–	(14)	(36)
Total	7%	8%	–%	7%	(6)%

(a) Premiums and other considerations include structured settlements, single premium immediate annuities and terminal funding annuities.
(b) Primarily represents runoff annuity business sold through discontinued distribution relationships.

The following table reflects periodic Domestic Life insurance sales by product:

Domestic Life Insurance

(in millions)	Three Months Ended March 31, **2007**	2006	Percentage Increase/ (Decrease)
Periodic premium sales by product*:			
Universal life	**$51**	$136	(62)%
Variable universal life	**13**	9	44
Term life	**55**	60	(8)
Whole life/other	**2**	3	(33)
Total	**$121**	$208	(42)%

** Periodic premium represents premium from new business expected to be collected over a one-year period.*

Premiums and other considerations for Domestic Life Insurance in the first three months of 2007 increased compared to the same period of 2006, primarily due to the growth in life insurance business in force. Periodic life insurance sales declined compared to the first three months of 2006 as a result of re-pricing certain universal life products and tightening of underwriting standards during the second half of 2006. In the first quarter of 2007, the Domestic Life Insurance operating unit acquired Matrix Direct, a leading direct marketer of life insurance, which will further expand its already broad distribution network. Premiums and other considerations for the home service segment declined compared to the same period in 2006 as the reduction in premium in force from normal lapses and maturities exceeded sales growth. Premiums and other considerations for group life/health for the first three months of 2007 declined over the same period of 2006, primarily due to exiting the financial institutions credit life business and tightened pricing and underwriting in the group employer lines. Premiums and other considerations growth from payout annuities for the first three months of 2007 reflects increased sales of structured settlements and terminal funding compared to the same period of 2006.

Domestic Life Insurance operating income declined in the first three months of 2007 compared to the same period of 2006, primarily due to a $22 million charge related to the adoption of SOP 05-1 and an increase in realized capital losses, offset by growth in the underlying business and increases in net investment income.

Life insurance operating income decreased for the first three months of 2007 compared to the first three months of 2006 primarily due to increased realized capital losses and higher policyholder benefits, partially offset by growth in the underlying business and increased partnership income. Home service operating income increased due to lower realized capital losses. Group life/health lines operating income decreased due to a charge of $16 million resulting from the adoption of SOP 05-1. Payout annuities operating income increased for the first three months of 2007 due to growth in the business, lower realized capital losses and an increase in calls and tenders on fixed maturity securities. Individual fixed annuities operating income increased primarily from lower realized capital losses. Individual annuities – runoff operating income is down from the first three months of 2006 due to the decline in the block of business partially offset by lower realized capital losses.

Domestic Retirement Services Results

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

(in millions)	Premiums and Other Considerations	Net Investment Income	Realized Capital Gains (Losses)	Total Revenues	Operating Income
Three months ended March 31, 2007					
Group retirement products	**$ 105**	**$ 570**	**$ (10)**	**$ 665**	**$276**
Individual fixed annuities	**25**	**914**	**(11)**	**928**	**303**
Individual variable annuities	**146**	**42**	**10**	**198**	**52**
Individual annuities – runoff*	**8**	**99**	**2**	**109**	**21**
Total	**$ 284**	**$1,625**	**$ (9)**	**$1,900**	**$652**
Three months ended March 31, 2006					
Group retirement products	$ 94	$ 572	$ (37)	$ 629	$265
Individual fixed annuities	28	917	(100)	845	259
Individual variable annuities	128	52	2	182	46
Individual annuities – runoff*	7	105	(9)	103	8
Total	$ 257	$1,646	$(144)	$1,759	$578
Percentage Increase/(Decrease) from Prior Year:					
Group retirement products	12%	–%	73%	6%	4%
Individual fixed annuities	(11)	–	89	10	17
Individual variable annuities	14	(19)	–	9	13
Individual annuities – runoff*	14	(6)	–	6	163
Total	11%	(1)%	94%	8%	13%

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

Domestic Retirement Services total deposits decreased for the first three months of 2007 compared to the same period of 2006. The decrease in total deposits primarily reflects lower fixed annuity sales that continued to face increased competition from bank deposit products and money market funds offering very competitive short-term rates in the flat yield curve environment. Individual variable annuity deposits declined slightly in the first three months of 2007 compared to the same period in 2006, due to discontinuing a proprietary product in a major bank. Absent the loss of this product, deposits would have increased 2 percent. Group retirement deposits declined in the first three months of 2007 as a result of higher external mutual fund conversions in the prior year period partially offset by an increase in variable annuity deposits. Over time, AIG expects that mutual fund sales will result in a gradual reduction in overall profit margins of this business driven by the growth in the lower-margin mutual fund products relative to the annuity products. Group retirement surrenders increased as a result of a few large group mutual fund surrenders in the first three months of 2007 compared to the same period last year. Fixed annuity surrender rates increased in the first three months of 2007 compared to the same period in 2006 due to products coming out of their surrender charge period and increased competition from banks. Individual fixed annuity net flows for the first three months of 2007 declined compared to the same period of 2006, reflecting both the lower deposits and higher surrenders, caused by the flat or inverted yield curve.

Total Domestic Retirement Services operating income for the first three months of 2007 increased over the same period of 2006. Group retirement products total revenues increased in the first three months of 2007 compared to the same period in 2006, primarily due to lower realized capital losses and an increase in fee income, primarily driven by higher variable annuity fees and other advisory fees. The higher revenues, partially offset by higher amortization of DAC related to the increase in surrenders and internal replacements of existing contracts into new contracts and general account spread compression, resulted in an increase in group retirement operating income over the first three months of 2006. Total revenues and operating income for individual fixed annuities were up in the first three months of 2007 compared to the first three months of 2006 primarily driven by lower realized capital losses, partially offset by higher amortization of DAC as a result of lower realized capital losses and increased early duration surrenders. Individual variable annuity total revenues increased in the first three months of 2007 compared to the first three months of 2006, primarily driven by higher variable annuity fees resulting from the increase in the equity markets in 2006 and increases in realized capital gains partially offset by lower investment income. The higher revenues, partially offset by higher amortization of DAC, resulted in the increase in individual variable annuity operating income. Individual annuities – runoff operating income increased in the first three months of 2007 over the same period of 2006 even though the underlying reserves decreased. The higher income was primarily due to lower realized capital losses and increased net spreads as a result of higher investment yields partially offset by lower volumes due to the continued runoff of the business.

Domestic Retirement Services Supplemental Data

The following table presents deposits*:

(in millions)	Three Months Ended March 31, 2007	2006
Group retirement products:		
Annuities	**$1,418**	$1,396
Mutual funds	**465**	545
Individual fixed annuities	**1,231**	1,541
Individual variable annuities	**1,008**	1,027
Individual fixed annuities – runoff	**14**	15
Total	**$4,136**	$4,524

** Excludes internal replacements.*

The following table presents Domestic Retirement Services reserves by surrender charge category as of March 31, 2007:

(in millions)	Group Retirement Products*	Individual Fixed Annuities	Individual Variable Annuities
Zero or no surrender charge	$43,889	$10,513	$11,721
0% - 2%	6,323	4,406	5,022
Greater than 2% - 4%	3,732	6,395	4,960
Greater than 4%	3,523	27,579	9,640
Non-Surrenderable	879	3,446	89
Total	$58,346	$52,339	$31,432

** Excludes mutual funds of $6.9 billion.*

Surrender rates increased for individual fixed annuities and group retirement products for the first three months of 2007 compared to the same period of the prior year. The increase in the surrender rate for fixed annuities continues to be driven by the shape of the yield curve and general aging of the in-force block; however, less than 21 percent of the individual fixed annuity reserves as of March 31, 2007 were available to be surrendered without charge. Surrender rates for group retirement products increased as a result of an increase in mutual fund and annuity surrenders. New products have been introduced to retain assets and AIG has retained or attracted over $293 million in assets in the first three months of 2007. Individual variable annuity surrender rates were higher in the first three months of 2006 reflecting higher shock-lapses that occur following expiration of the surrender charge period on certain 3-year and 7-year contracts.

A further increase in the level of surrenders in any of these businesses or in the individual fixed annuities runoff block could accelerate the amortization of DAC and negatively affect fee income earned on assets under management.

The following table presents the net flows[a] by line of business:

(in millions)	Three Months Ended March 31, 2007	2006
Group retirement products[b]	**$ (102)**	$ 441
Individual fixed annuities	**(837)**	(146)
Individual variable annuities	**(103)**	(133)
Individual fixed annuities – runoff	**(263)**	(228)
Total	**$(1,305)**	$ (66)

(a) Net flows are defined as deposits received less benefits, surrenders, withdrawals and death benefits.
(b) Includes mutual funds.

The combination of lower deposits and higher surrenders in the individual fixed annuity and individual fixed annuity – runoff blocks, which include closed blocks of business from acquired companies or terminated distribution relationships, resulted in negative net flows for the first three months of 2007. The continuation of the current interest rate and competitive environment could prolong this trend.

Life Insurance & Retirement Services Net Investment Income and Realized Capital Gains (Losses)

The following table summarizes the components of Net investment income:

(in millions)	Three Months Ended March 31, 2007	2006
Foreign Life Insurance & Retirement Services:		
Fixed maturities, including short-term investments	**$2,076**	$1,655
Equity securities	**64**	71
Interest on mortgage, policy and collateral loans	**146**	108
Partnership income	**48**	17
Unit investment trusts	**86**	–
Other[a]	**64**	69
Total investment income before policyholder trading gains (losses)	**2,484**	1,920
Policyholder trading gains (losses)[b]	**475**	390
Total investment income	**2,959**	2,310
Investment expenses	**76**	55
Net investment income	**$2,883**	$2,255
Domestic Life Insurance:		
Fixed maturities, including short-term investments	**$ 911**	$ 870
Equity securities	**(1)**	2
Interest on mortgage, policy and collateral loans	**100**	85
Partnership income – excluding Synfuels	**27**	10
Partnership income (loss) – Synfuels	**(33)**	(37)
Unit investment trusts	**2**	–
Other[a]	**14**	14
Total investment income	**1,020**	944
Investment expenses	**15**	11
Net investment income	**$1,005**	$ 933
Domestic Retirement Services:		
Fixed maturities, including short-term investments	**$1,400**	$1,438
Equity securities	**3**	3
Interest on mortgage, policy and collateral loans	**121**	104
Partnership income – excluding Synfuels	**130**	131
Unit investment trusts	**–**	–
Other[a]	**(12)**	(17)
Total investment income before policyholder trading gains (losses)	**1,642**	1,659
Investment expenses	**17**	13
Net investment income	**$1,625**	$1,646
Total:		
Fixed maturities, including short-term investments	**$4,387**	$3,963
Equity securities	**66**	76
Interest on mortgage, policy and collateral loans	**367**	297
Partnership income – excluding Synfuels	**205**	158
Partnership income (loss) – Synfuels	**(33)**	(37)
Unit investment trusts	**88**	–
Other[a]	**66**	66

(in millions)	Three Months Ended March 31, 2007	2006
Total investment income before policyholder trading gains (losses)	**5,146**	4,523
Policyholder trading gains (losses)[(b)]	**475**	390
Total investment income	**5,621**	4,913
Investment expenses	**108**	79
Net investment income[(c)]	**$5,513**	$4,834

(a) Other includes real estate income, income on non-partnership invested assets, securities lending and Foreign Life Insurance & Retirement Services' equal share of the results of AIG Credit Card Company (Taiwan).

(b) Relates principally to assets held in various trading securities accounts that do not qualify for separate account treatment under SOP 03-1. These amounts are offset by an equal change included in incurred policy losses and benefits.

(c) Includes call and tender income.

Net investment income increased for the first three months of 2007 compared to the same period of 2006. Fixed maturities income rose as the underlying invested asset base grew. Yield enhancement activity, including partnership income, increased for the first three months of 2007 compared to the same period last year. The first quarter 2007 results included $88 million in earnings on certain interests in unit investment trusts, of which $41 million was allocated to policyholder accounts through incurred policy losses and benefits. Policyholder trading gains (losses) increased in the first three months of 2007 compared to the same period last year. These gains have no effect on operating income because there is an equal charge to incurred policy losses and benefits to offset these results. Net investment income for certain operations include investments in structured notes linked to emerging market sovereign debt that incorporates both interest rate risk and currency risk. In addition, period to period comparisons of investment income for some lines of business are affected by yield enhancement activity, particularly partnership income as shown in the above table. See also Insurance and Asset Management Invested Assets herein.

AIG generates income tax credits as a result of investing in synthetic fuel production (synfuels) related to the investment loss shown in the above table and records those benefits in its provision for income taxes. The amounts of those income tax credits were $51 million and $40 million for the first three months of 2007 and 2006, respectively. For a further discussion of the effect of fluctuating domestic crude oil prices on synfuel tax credits, see Note 6(c) of Notes to Consolidated Financial Statements.

The following table summarizes Realized capital gains (losses) by major category:

(in millions)	Three Months Ended March 31, 2007	2006
Foreign Life Insurance & Retirement Services:		
Sales of fixed maturities	**$ (20)**	$ (21)
Sales of equity securities	**32**	151
Other:		
Foreign exchange transactions	**115**	5
Derivatives instruments	**(117)**	259
Other-than-temporary decline	**(331)**	(41)
Other*	**86**	(1)
Total Foreign Life Insurance & Retirement Services	**(235)**	352
Domestic Life Insurance:		
Sales of fixed maturities	**$ 19**	$ (22)
Sales of equity securities	**1**	2
Other:		
Foreign exchange transactions	**2**	(1)
Derivatives instruments	**(11)**	87
Other-than-temporary decline	**(19)**	(54)
Other	**(4)**	(4)
Total Domestic Life Insurance	**$ (12)**	$ 8
Domestic Retirement Services:		
Sales of fixed maturities	**$ 19**	$ (47)
Sales of equity securities	**11**	14
Other:		
Foreign exchange transactions	**6**	–
Derivatives instruments	**5**	6
Other-than-temporary decline	**(42)**	(92)
Other	**(8)**	(25)
Total Domestic Retirement Services	**$ (9)**	$(144)
Total:		
Sales of fixed maturities	**$ 18**	$ (90)
Sales of equity securities	**44**	167
Other:		
Foreign exchange transactions	**123**	4
Derivative instruments	**(123)**	352
Other-than-temporary decline	**(392)**	(187)
Other	**74**	(30)
Total:	**$(256)**	$ 216

** Includes losses of $71 million and gains of $67 million allocated to participating policyholders for the first three months of 2007 and 2006, respectively.*

Realized capital gains (losses) include normal portfolio transactions as well as derivative gains (losses) for transactions that did not qualify for hedge accounting treatment under FAS 133, foreign exchange gains and losses and other-than-temporary declines in the value of investments. Realized capital losses in the Foreign Life operations in the first three months of 2007 include losses of $117 million related to derivatives that did not qualify for hedge accounting treatment compared to a gain of $259 million in the same period of 2006. Derivatives in the Foreign Life operations are primarily used to economically hedge cash flows related to U.S. dollar bonds back to the respective currency of the country, principally in Taiwan, Thailand, and Singapore. The corresponding foreign exchange gain or loss of the economically hedged bond is deferred in Other comprehensive income until sold or deemed to be other than temporary. In the first quarter of 2007, Foreign Life operations incurred losses of $331 million for the decline in the value of securities deemed to be other than temporarily impaired. A significant portion of those losses was related to the decline in value of U.S. dollar bonds held in Thailand and Singapore reflecting the depreciation of the U.S. dollar against the local currency.

Deferred Policy Acquisition Costs

DAC for Life Insurance & Retirement Services products arises from the deferral of those costs that vary with, and are directly related to, the acquisition of new or renewal business. Policy acquisition costs for life insurance products are generally deferred and amortized over the premium paying period of the policy. Policy acquisition costs that relate to universal life and investment-type products, including variable and fixed annuities (investment-oriented products), are deferred and amortized, with interest, as appropriate, in relation to the historical and future incidence of estimated gross profits to be realized over the estimated lives of the contracts. Total acquisition costs deferred decreased $69 million in the first three months of 2007 compared to the first three months of 2006 due to lower sales in the Domestic Life business. Total DAC amortization expense, excluding VOBA, increased $127 million compared to the first three months of 2006 with each period's annualized amortization expense level at approximately 13 percent of the opening DAC balance.

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

(in millions)	Three Months Ended March 31,					
	2007			2006		
	DAC	**VOBA**	**Total**	DAC	VOBA	Total
Foreign Life Insurance & Retirement Services						
Balance at beginning of year	**$20,005**	**$1,148**	**$21,153**	$16,360	$1,278	$17,638
Acquisition costs deferred	**1,227**	**–**	**1,227**	1,205	–	1,205
Amortization charged to income or credited to operating income:						
Related to realized capital gains (losses)	**19**	**–**	**19**	1	–	1
Related to unlocking future assumptions	**11**	**–**	**11**	17	–	17
All other amortization	**(623)**	**(27)**	**(650)**	(537)	(44)	(581)
Change in unrealized gains (losses) on securities	**(11)**	**1**	**(10)**	5	(4)	1
Increase (decrease) due to foreign exchange	**(158)**	**(27)**	**(185)**	474	41	515
Other*	**(59)**	**(1)**	**(60)**	–	–	–
Balance at end of period	**$20,411**	**$1,094**	**$21,505**	$17,525	$1,271	$18,796
Domestic Life Insurance						
Balance at beginning of year	**$ 5,448**	**$ 558**	**$ 6,006**	$ 4,625	$ 559	$ 5,184
Acquisition costs deferred	**234**	**–**	**234**	310	–	310
Amortization charged to income or credited to operating income:						
Related to realized capital gains (losses)	**–**	**–**	**–**	(8)	2	(6)
Related to unlocking future assumptions	**(1)**	**2**	**1**	–	–	–
All other amortization	**(164)**	**(13)**	**(177)**	(160)	(9)	(169)
Change in unrealized gains (losses) on securities	**19**	**2**	**21**	434	39	473
Increase (decrease) due to foreign exchange	**5**	**–**	**5**	(1)	–	(1)
Other*	**(64)**	**–**	**(64)**	–	–	–
Balance at end of period	**$ 5,477**	**$ 549**	**$ 6,026**	$ 5,200	$ 591	$ 5,791
Domestic Retirement Services						
Balance at beginning of year	**$ 5,376**	**$ 275**	**$ 5,651**	$ 4,974	$ 310	$ 5,284
Acquisition costs deferred	**169**	**–**	**169**	184	–	184
Amortization charged to income or credited to operating income:						
Related to realized capital gains (losses)	**(10)**	**–**	**(10)**	22	4	26
Related to unlocking future assumptions	**2**	**–**	**2**	2	–	2
All other amortization	**(204)**	**(15)**	**(219)**	(180)	(17)	(197)
Change in unrealized gains (losses) on securities	**(84)**	**10**	**(74)**	563	50	613
Increase (decrease) due to foreign exchange	**–**	**–**	**–**	–	–	–
Balance at end of period	**$ 5,249**	**$ 270**	**$ 5,519**	$ 5,565	$ 347	$ 5,912
Total Life Insurance & Retirement Services						
Balance at beginning of year	**$30,829**	**$1,981**	**$32,810**	$25,959	$2,147	$28,106
Acquisition costs deferred	**1,630**	**–**	**1,630**	1,699	–	1,699
Amortization charged to income or credited to operating income:						
Related to realized capital gains (losses)	**9**	**–**	**9**	15	6	21
Related to unlocking future assumptions	**12**	**2**	**14**	19	–	19
All other amortization	**(991)**	**(55)**	**(1,046)**	(877)	(70)	(947)
Change in unrealized gains (losses) on securities	**(76)**	**13**	**(63)**	1,002	85	1,087
Increase (decrease) due to foreign exchange	**(153)**	**(27)**	**(180)**	473	41	514
Other*	**(123)**	**(1)**	**(124)**	–	–	–
Balance at end of period	**$31,137**	**$1,913**	**$33,050**	$28,290	$2,209	$30,499

** Represents the cumulative effect of the adoption of SOP 05-1.*

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

Financial Services Operations

AIG's Financial Services subsidiaries engage in diversified activities including aircraft and equipment leasing, capital markets, consumer finance and insurance premium finance. (See also Note 2 of Notes to Consolidated Financial Statements.)

Financial Services Results

Financial Services results were as follows:

(in millions)	Three Months Ended March 31, 2007	2006	Percentage Increase/ (Decrease)
Revenues:			
Aircraft Leasing[(a)]	**$1,058**	$1,012	5%
Capital Markets[(b)(c)]	**228**	(300)	–
Consumer Finance[(d)(e)]	**883**	925	(5)
Other, including intercompany adjustments	**32**	29	10
Total	**$2,201**	$1,666	32%
Operating income (loss):			
Aircraft Leasing[(a)]	**$ 164**	$ 176	(7)%
Capital Markets[(b)(c)]	**68**	(470)	–
Consumer Finance[(d)(e)]	**36**	176	(80)
Other, including intercompany adjustments	**24**	10	140
Total	**$ 292**	$ (108)	–%

(a) Revenues are primarily aircraft lease rentals from ILFC. Both revenues and operating income include the effect of hedging activities that did not qualify for hedge accounting treatment under FAS 133, including the related foreign exchange gains and losses. For the first three months of 2007 and 2006, the effect was $(37) million and $45 million, respectively. These amounts result primarily from interest rate and foreign currency derivatives that are effective economic hedges of borrowings.

(b) Revenues, shown net of interest expense of $1.1 billion and $639 million in the first three months of 2007 and 2006, respectively, were primarily from hedged financial positions entered into in connection with counterparty transactions. Both revenues and operating income include the effect of hedging activities that did not qualify for hedge accounting treatment under FAS 133 or for which hedge accounting was not applied, including the related foreign exchange gains and losses. For the first three months of 2007 and 2006, the effect was $(85) million and $(678) million, respectively.

(c) Certain transactions entered into by AIGFP generate tax credits and benefits which are included in income taxes in the consolidated statement of income. The amounts of such tax credits and benefits for the first three months of 2007 and 2006 were $17 million and $18 million, respectively.

(d) Revenues are primarily finance charges. Both revenues and operating income include the effect of hedging activities that did not qualify for hedge accounting treatment under FAS 133, including the related foreign exchange gains and losses. For the first three months of 2007 and 2006, the effect was $(36) million and $3 million, respectively. These amounts result primarily from interest rate and foreign currency derivatives that are effective economic hedges of borrowings.

(e) The three months ended March 31, 2007 includes a pre-tax charge of $128 million in connection with domestic consumer finance's mortgage banking activities.

Financial Services operating income increased in the first three months of 2007 compared to the same period of 2006 primarily due to differences in the accounting treatment for hedging activities. In the first three months of 2007, AIGFP began applying hedge accounting to certain of its interest rate swaps and foreign currency forward contracts hedging its investments and borrowings. As a result of the application of hedge accounting, AIGFP recognized in earnings the change in the fair value on the hedged items attributable to the hedged risks offsetting the gains and losses on the derivatives designated as hedges. Prior to 2007, hedge accounting under FAS 133 was not being applied to any of the derivatives and related assets and liabilities. Accordingly, revenues and operating income were exposed to volatility resulting from differences in the timing of revenue recognition between the derivatives and the hedged assets and liabilities.

Beginning in the first quarter of 2007, derivative gains and losses and foreign exchange transaction gains and losses for Financial Services entities other than AIGFP, which were previously reported as part of AIG's Other category, are now included in Financial Services revenues and operating income. For the first three months of 2007, the amount included in both Financial Services revenues and operating income was a loss of $67 million. All prior periods have been revised to conform to the current presentation.

Aircraft Leasing

AIG's Aircraft Leasing operations represent the operations of ILFC, which generates its revenues primarily from leasing new and used commercial jet aircraft to foreign and domestic airlines. Revenues also result from the remarketing of commercial jets for ILFC's own account, and remarketing and fleet management services for airlines and financial institutions. ILFC finances its aircraft purchases primarily through the issuance of debt instruments. ILFC economically hedges its floating rate and foreign currency denominated debt using interest rate and foreign currency derivatives. These derivatives are effective economic hedges; however, since hedge accounting under FAS 133 was not applied, the benefits of using derivatives to hedge these exposures are not reflected in ILFC's corporate borrowing rates. The composite borrowing rates at March 31, 2007 and 2006 were 5.19 percent and 4.77 percent, respectively. ILFC has begun to apply hedge accounting in the second quarter of 2007.

ILFC typically contracts to re-lease aircraft before the end of the existing lease term. For aircraft returned before the end of the lease term, ILFC has generally been able to re-lease such aircraft within two to six months of its return. As a lessor, ILFC considers an aircraft "idle" or "off lease" when the aircraft is not subject to a signed lease agreement or signed letter of intent. ILFC had one aircraft off lease at March 31, 2007, and all new aircraft scheduled for delivery through 2007 have been leased.

Aircraft Leasing Results

ILFC's operating income decreased in the first three months of 2007 compared to the same period of 2006 by $12 million, or 6.8 percent. For the first three months of 2007 and 2006, the effect of hedging activities that did not qualify for hedge accounting treatment under FAS 133, including the related foreign exchange gains and losses, was $(37) million and $45 million, respectively, in both revenues and operating income. Rental revenues increased by $142 million or 15.4 per-

cent, driven by a larger aircraft fleet, increased utilization and higher lease rates. During the first three months of 2007, ILFC's fleet subject to operating leases increased by 32 airplanes to a total of 856. The increase in rental revenues was partially offset by increases in depreciation expense and interest expense. Depreciation expense increased by $42 million, or 11.5 percent, in line with the increase in the size of the aircraft fleet. Interest expense increased by $71 million, or 22.6 percent, driven by rising cost of funds, a weaker U.S. dollar against the Euro and the British Pound and additional borrowings to fund aircraft purchases. As noted above, ILFC's interest expense did not reflect the benefit of hedging these exposures.

Capital Markets

Capital Markets represents the operations of AIGFP, which engages as principal in a wide variety of financial transactions, including standard and customized financial products involving commodities, credit, currencies, energy, equities and rates. AIGFP also invests in a diversified portfolio of securities and principal investments and engages in borrowing activities involving issuing standard and structured notes and other securities, and entering into GIAs.

Beginning in 2007, AIGFP applied hedge accounting under FAS 133 to certain of its interest rate swaps and foreign currency forward contracts hedging its investments and borrowings. As a result, AIGFP recognized in earnings the change in the fair value on the hedged items attributable to the hedged risks offsetting the gains and losses on the derivatives designated as hedges. Prior to 2007, AIGFP did not apply hedge accounting under FAS 133 to any of its derivatives or related assets and liabilities.

Capital Markets Results

Capital Markets operating income increased in the first three months of 2007 by $538 million compared to the same period of 2006, primarily due to differences in its accounting treatment for hedging activities. In the first three months of 2007, AIGFP began applying hedge accounting under FAS 133 to certain of its interest rate swaps and foreign currency forward contracts hedging its investments and borrowings. As a result, AIGFP recognized in earnings the change in the fair value on the hedged items attributable to the hedged risks offsetting the gains and losses on the derivatives designated as hedges. In the first three months of 2007, AIGFP recognized a net loss of $85 million related to hedging activities for which hedge accounting was not applied compared to a net loss of $678 million in the first three months of 2006. The net loss recognized for the first three months of 2007 included a $166 million reduction in fair value at March 31, 2007 of certain derivatives that are an integral part of, and economically hedge, the structured transactions potentially affected by the proposed guidance by the U.S. Treasury Department discussed above in Overview of Operations and Business — Outlook. This valuation adjustment effectively reverses the cumulative gains resulting from movements in market interest rates on the derivatives since their inception through March 31, 2007. While these derivatives were economically hedging the preferred interests in the structured transactions, for accounting purposes the preferred interests were accounted for either at amortized cost, or as available for sale debt securities. Accordingly, no changes in market value on these securities have been recognized in income. The net loss on AIGFP's derivatives recognized in the first three months of 2006 was partially due to an out of period charge of $300 million related to the remediation of the material weakness in accounting for certain derivative transactions under FAS 133. The remainder of the net loss reflected the effect of increases in U.S. interest rates resulting in a decrease in the fair value of the interest rate derivatives hedging AIGFP's assets and liabilities. The improved results in the first three months of 2007 were partially offset by reduced transaction flow in AIGFP's equity, commodity and interest rate products.

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

The most significant component of Capital Markets operating expenses is compensation, which was $123 million and $136 million in the first three months of 2007 and 2006, respectively. The amount of compensation was not affected by gains and losses arising from derivatives not qualifying for hedge accounting treatment under FAS 133.

AIG elected to early adopt FAS 155, "Accounting for Certain Hybrid Financial Instruments" (FAS 155), in 2006 and AIGFP elected to apply the fair value option to certain structured notes and other financial liabilities containing embedded derivatives outstanding as of January 1, 2006. The cumulative effect of the adoption of FAS 155 on these instruments at January 1, 2006 was a pre-tax loss of $29 million. The effect of these hybrid financial instruments reflected in AIGFP's operating income in the first three months of 2007 and 2006 was a pre-tax loss of $166 million and a pre-tax gain of $9 million, respectively. These amounts were largely offset by gains and losses on economic hedge positions also reflected in AIGFP's operating income.

Consumer Finance

AIG's consumer finance operations in North America are principally conducted through American General Finance, Inc. (AGF). Effective January 2, 2007, AGF expanded its operations into the United Kingdom through the acquisition of Ocean Finance and Mortgages Limited, a finance broker for home owner loans in the United Kingdom. AGF derives a substantial portion of its revenues from finance charges assessed on outstanding real estate loans, secured and un-

secured non-real estate loans and retail sales finance receivables. The real estate loans are comprised principally of first lien mortgages on residential real estate generally having a maximum term of 360 months, and are considered non-conforming. The real estate loans may be closed-end accounts or open-end home equity lines of credit and are principally fixed rate products. AGF does not offer mortgage products with borrower payment options that allow for negative amortization of the principal balance. The secured non-real estate loans are secured by consumer goods, automobiles or other personal property. Both secured and unsecured non-real estate loans and retail sales finance receivables generally have a maximum term of 60 months. The majority of AGF's originations is sourced through its branches. However, a significant volume of real estate loans is also originated through broker relationships, and to lesser extents, through correspondent relationships and direct mail solicitations.

AGF also conducts mortgage banking activities through its centralized real estate operations. It originates residential real estate loans, the majority of which are sold to investors on a servicing-released basis. These loans are collateralized by first and second-liens on one to four family properties and are originated largely through broker relationships and to a lesser extent are originated directly to consumers or through correspondent relationships. From July 2003 through February 2006, these loans were originated through an arrangement with AIG Federal Savings Bank, a federally chartered thrift. The origination relationship was terminated in the first quarter of 2006. Since then, all new loans were originated directly by AGF subsidiaries under their own state licenses.

AIG's foreign consumer finance operations are principally conducted through AIGCFG. AIGCFG operates primarily in emerging and developing markets. AIGCFG has operations in Argentina, China, Hong Kong, Mexico, Philippines, Poland, Taiwan and Thailand and most recently began operations in India through the acquisition of a majority interest in a sales finance lending operation. In addition, AIGCFG expanded its distribution channels in Thailand by acquiring in the first quarter of 2007 an 80 percent interest in a company with a network of over 130 branches for secured consumer lending. Certain of the AIGCFG operations are partly or wholly owned by life insurance subsidiaries of AIG. Accordingly, the financial results of those companies are allocated between Financial Services and Life Insurance & Retirement Services according to their ownership percentages. While products vary by market, the businesses generally provide credit cards, unsecured and secured non-real estate loans, term deposits, savings accounts, retail sales finance and real estate loans. AIGCFG originates finance receivables through its branches and direct solicitation. AIGCFG also originates finance receivables indirectly through relationships with retailers, auto dealers, and independent agents.

Consumer Finance Results

Consumer Finance operating income decreased by $140 million, or 79.5 percent, in the first three months of 2007 compared to the same period of 2006. Included in operating income is the effect of hedging activities that did not qualify for hedge accounting treatment under FAS 133, including the related foreign exchange gains and losses on the related hedged items, of $(36) million and $3 million in the first three months of 2007 and 2006, respectively.

The operating income for the first three months of 2007 from the domestic consumer finance operations, which includes the operations of AGF and AIG Federal Savings Bank, decreased by $184 million or 93 percent from the same period of 2006. In light of evolving market and regulatory developments affecting non-prime mortgage lending, AIG's domestic consumer finance operations are in ongoing discussions with the Office of Thrift Supervision relating to loans originated in the name of AIG Federal Savings Bank during the period from the beginning of July 2003 to the beginning of May 2006. Management expects that the application of underwriting criteria developed in consideration of regulatory guidance issued by the banking agencies will result in significant costs to the domestic consumer finance operations. At this time, management's best estimate of these costs is $128 million pre-tax, and a charge for this amount has been included in Consumer Finance operating income for the three months ended March 31, 2007.

First quarter domestic consumer finance revenues and operating income also declined from the prior year partially due to the change in fair value of the derivatives hedging borrowings for which hedge accounting was not applied during either period. During the first three months of 2007, AGF recorded a net loss of $36 million on its derivatives for which hedge accounting was not applied, including the related foreign exchange losses, compared to a net gain of $1 million for the same period of 2006. Additionally, for the first quarter of 2007, domestic results were adversely affected by the slower housing market, higher interest rates on most long-term fixed rate loans and evolving changes in the regulatory environment which resulted in lower real estate loan originations. For the first three months of 2007, results from mortgage banking activities also included a $25 million increase in AGF's warranty reserve which covers its obligations to repurchase loans sold to third-party investors should there be a first payment default or breach of representations and warranties. Although mortgage loan originations declined in the first quarter of 2007, the softening of home price appreciation (reducing the equity customers may be able to extract from their homes by refinancing) and higher mortgage loan rates contributed to an increase in non-real estate loans of 11 percent at March 31, 2007 compared to March 31, 2006. Retail sales finance receivables also increased 23 percent compared to March 31, 2006 due to increased marketing efforts and customer demand. AGF's results for the first three

months of 2007 also included $65 million from a favorable out of court settlement.

The credit quality of AGF's finance receivables during the first three months of 2007 remained stable. Its net charge-off ratio increased to 0.97 percent compared to 0.88 percent in the same period in 2006, which reflected $6 million of non-recurring recoveries that were recorded in the first quarter of 2006. AGF's delinquency ratio remained relatively low, although it increased by 31 basis points to 2.05 percent at March 31, 2007 compared to March 31, 2006. AGF's allowance for finance receivables losses as a percentage of outstanding receivables was 1.99 percent at March 31, 2007 compared to 2.10 percent at March 31, 2006. The allowance for finance receivables losses includes an allowance for catastrophe-related losses relating to hurricane Katrina of $12 million at March 31, 2007 compared to $56 million at March 31, 2006.

AGF's interest expense increased by $47 million or 18 percent as both its short-term and long-term borrowing rates increased in the first three months of 2007 compared to the same period of 2006. Its short-term borrowing rates averaged 5.42 percent in the first three months of 2007 compared to 4.59 percent in the same period of 2006, while long-term borrowing rates averaged 5.19 percent in the first quarter of 2007 compared to 4.84 percent in the first quarter of 2006.

Revenues from the foreign consumer finance operations increased by approximately 17 percent in the first three months of 2007 compared to the same period of 2006. Loan growth, particularly in Poland and Argentina, was the primary driver behind the higher revenues. Operating income in the first quarter of 2006 reflects AIGCFG's $44 million share of the allowance for losses related to industry-wide credit deterioration in the Taiwan credit card market.

Asset Management Operations

AIG's Asset Management operations comprise a wide variety of investment-related services and investment products. Such services and products are offered to individuals and institutions both domestically and overseas, and are primarily comprised of Spread-Based Investment Businesses, Institutional Asset Management and Brokerage Services and Mutual Funds.

The revenues and operating income for this segment are affected by the general conditions in the equity and credit markets. In addition, realized gains and performance fees are contingent upon various fund closings, maturity levels and market conditions.

Spread-Based Investment Business

In prior years, the sale of GICs to investors, both domestically and overseas, was AIG's primary institutional Spread-Based Investment Business. During 2005, AIG launched its MIP and its asset management subsidiaries, primarily SunAmerica Life, ceased writing new GIC business. The GIC business will continue to run off for the foreseeable future while the MIP business is expected to grow.

Institutional Asset Management

AIG's Institutional Asset Management business provides an array of investment products and services globally to institutional investors, AIG subsidiaries and affiliates and high net worth investors. These products and services include traditional equity and fixed income investment management and a full range of alternative asset classes. Delivery of AIG's Institutional Asset Management products and services is accomplished via a global network of operating subsidiaries comprising AIG Global Asset Management Holdings Corp. and its subsidiaries and affiliated companies (collectively, AIGGIG). The primary operating entities within this group are AIG Global Investment Corp., AIG Global Real Estate Investment Corp. and AIG Private Bank. AIG Private Bank offers banking, trading and investment management services to private client and high net worth individuals and institutions globally.

Within the alternative investment asset class, AIGGIG offers hedge and private equity fund-of-funds, direct investments and distressed debt investments. Within the structured fixed income and equity product asset class, AIGGIG offers various forms of structured and credit linked notes, various forms of collateralized debt obligations and other investment strategies aimed at achieving superior returns or capital preservation. In addition, Institutional Asset Management's product offerings include various forms of principal protected and liability management structures.

Brokerage Services and Mutual Funds

AIG's Brokerage Services and Mutual Funds business provides mutual fund and broker-dealer related services to retail investors, group trusts and corporate accounts through an independent network of financial advisors. The AIG Advisor Group, Inc., a subsidiary of AIG Retirement Services, Inc., is comprised of several broker-dealer entities that provide these services to clients primarily in the U.S. marketplace. AIG SunAmerica Asset Management Corp. manages, advises and/or administers retail mutual funds, as well as the underlying assets of variable annuities sold by AIG SunAmerica and VALIC to individuals and groups throughout the United States.

Other

Included in the Other category for Asset Management is income or loss from certain SunAmerica sponsored partnerships and partnership investments. Partnership assets consist of investments in a diversified portfolio of private equity

funds, affordable housing partnerships and hedge fund investments.

Asset Management Results

Asset Management results were as follows:

(in millions)	Three Months Ended March 31, **2007**	2006	Percentage Increase/ (Decrease)
Revenues:			
Spread-Based Investment Business	**$1,015**	$ 675	50%
Institutional Asset Management	**668**	326	105
Brokerage Services and Mutual Funds	**78**	73	7
Other	**147**	65	126
Total	**$1,908**	$1,139	68%
Operating income:			
Spread-Based Investment Business	**$ 491**	$ 207	137%
Institutional Asset Management*	**333**	158	111
Brokerage Services and Mutual Funds	**26**	23	13
Other	**144**	61	136
Total	**$ 994**	$ 449	121%

** Includes a total of $228 million and $96 million for the three months ended March 31, 2007 and 2006, respectively, of income from certain AIG managed partnerships, private equity and real estate funds that are consolidated. Such income is offset in minority interest expense, which is not a component of operating income, on the consolidated statement of income.*

Asset Management revenues and operating income increased significantly in the first three months of 2007 compared to the same period of 2006 due primarily to growth in the Spread-Based Investment and Institutional Asset Management businesses. Other revenues and operating income for Asset Management also increased significantly from a year ago due to higher income from partnerships.

Beginning in the first quarter of 2007, derivative gains and losses and foreign exchange transaction gains and losses, which were previously reported as part of AIG's Other category, are now included in Asset Management revenues and operating income. For the first three months of 2007, the amount included in both Asset Management revenues and operating income was a loss of $20 million. All prior periods have been revised to conform to the current presentation.

Spread-Based Investment Business Results

Operating income related to the Spread-Based Investment Business increased in the first three months of 2007 compared to the same period of 2006 due to a significant increase in partnership income associated with the Domestic GIC program. Partnership income in the first quarter of 2007 included a distribution from a single partnership of $164 million, which became available after a five-year restriction on capital withdrawals. Also contributing to the increase in operating income of the Spread-Based Investment Business were increases in operating income generated by hedge funds and affordable housing partnerships. Partnership income is primarily derived from alternative investments and is affected by performance in the equity markets. Thus, revenues, operating income and cash flows attributable to GICs will vary from reporting period to reporting period.

Offsetting this growth in operating income was the continued runoff of GIC balances. A significant portion of the remaining GIC portfolio consists of floating rate obligations. AIG has entered into hedges to manage against increases in short-term interest rates. AIG believes these hedges are economically effective, but they did not qualify for hedge accounting treatment under FAS 133. Income or loss from these hedges are classified as realized capital gains or losses in the Asset Management segment results.

The following table illustrates the anticipated runoff of the domestic GIC portfolio at March 31, 2007:

(in billions)	Less Than One Year	1-3 Years	3+-5 Years	Over Five Years	Total
Domestic GICs	$6.4	$13.5	$2.7	$6.6	$29.2

MIP operating income, which is reported in the Spread-Based Investment Business, improved during the first three months of 2007 compared to the same period of 2006. During 2005, the MIP replaced the GIC program as AIG's principal spread-based investment activity. Despite the growth in MIP operating income, AIG does not expect that the income growth in the MIP will offset the runoff in the GIC portfolio for the foreseeable future because the asset mix under the MIP does not include the alternative investments utilized in the GIC program. Through March 31, 2007, AIG has issued the equivalent of $7.5 billion of securities to fund the MIP in the Euromarkets and the U.S. public and private markets. Commencing with transactions initiated in the first quarter of 2007, AIG applied hedge accounting for certain derivative transactions related to the MIP.

In order to better align financial reporting with the manner in which AIG's chief operating decision makers have managed their businesses, for the three months ended March 31, 2007, revenues and operating income related to foreign investment contracts, which were historically reported as a component of the Spread-Based Investment Business, are now being reported in the Life Insurance & Retirement Services segment. All prior periods have been revised to conform to the current presentation.

Institutional Asset Management Results

Operating income for Institutional Asset Management increased significantly in the first three months of 2007 compared to the same period of 2006, primarily due to an increase in carried interest and realized capital gains related to hedge funds as well as private equity and real estate partnerships. The increase in carried interest was driven by higher

valuations of portfolio investments and is generally associated with improved performance in the equity markets. Operating income also reflects higher gains on certain consolidated investments and partnerships; however, these gains are offset in minority interest expense, which is not a component of operating income, on the Consolidated Statement of Income.

AIG's unaffiliated client assets under management, including both retail mutual funds and institutional accounts, increased 17 percent from March 31, 2006 to $76.5 billion at March 31, 2007, resulting in higher management fee income. The growth in Institutional Asset Management revenues and operating income were driven by contributions from all asset classes globally.

While unaffiliated client assets under management and the resulting management fees continue to increase, the growth in operating income has trailed the growth in revenues due to higher fund-related expenses as well as sales and infrastructure enhancements. The fund-related expenses are associated with AIG Global Asset Management Holdings Corp. and its subsidiaries and affiliated companies (collectively, AIGGIG) purchasing and carrying investments on its balance sheet in anticipation of future fund launches. AIGGIG held over $2.3 billion in warehoused investments as of March 31, 2007. It is anticipated that these expenses will be recovered from fund entities in future periods. The sales and infrastructure enhancements are associated with AIG's planned expansion of marketing and distribution capabilities, combined with technology and operational infrastructure-related improvements.

Other Operations

The operating loss of AIG's Other category was as follows:

(in millions)	Three Months Ended March 31, **2007**	2006
Other operating income (loss):		
Equity earnings in unconsolidated entities	**$ 41**	$ 19
Interest expense	**(252)**	(183)
Unallocated corporate expenses	**(162)**	(184)
Compensation expense – SICO Plans	**(10)**	(76)
Compensation expense – Starr tender offer	**–**	(54)
Realized capital gains (losses)	**(78)**	(5)
Other miscellaneous, net	**(38)**	(26)
Total Other	**$(499)**	$(509)

The operating loss for AIG's Other category declined in the first three months of 2007 compared to the same period of 2006. Increased earnings from unconsolidated entities and lower unallocated corporate expenses were offset by higher interest expenses in the first three months of 2007 resulting from increased borrowings at the parent company. The operating loss in the first three months of 2006 included an out of period charge of $61 million related to the SICO Plans and a one-time charge related to the Starr tender offer of $54 million. Realized capital losses for the first three months of 2007 increased from the same period of 2006 due to foreign exchange losses on foreign denominated debt issued by AIG parent.

Beginning in the first quarter of 2007, derivative gains and losses and foreign exchange transaction gains and losses for Asset Management and Financial Services entities (other than AIGFP) are now included in Asset Management and Financial Services revenues and operating income. These amounts were previously reported as part of AIG's Other category. All prior periods have been revised to conform to the current presentation.

Capital Resources and Liquidity

At March 31, 2007, AIG had total consolidated shareholders' equity of $103.1 billion and total consolidated borrowings of $157.2 billion. At that date, $140.3 billion of such borrowings were not guaranteed by AIG, were matched borrowings by AIG or AIGFP, or represented junior subordinated debt or liabilities connected to trust preferred stock.

Borrowings

At March 31, 2007, AIG's net borrowings were $16.9 billion, excluding amounts that were matched borrowings by AIG and AIGFP, amounts not guaranteed by AIG, junior subordinated debt and liabilities connected to trust preferred stock. The following table summarizes borrowings outstanding:

(in millions)	**March 31, 2007**	December 31, 2006
AIG's net borrowings	**$ 16,853**	$ 17,126
Junior subordinated debt	**3,793**	–
Liabilities connected to trust preferred stock	**1,440**	1,440
MIP matched notes and bonds payable	**7,672**	5,468
Series AIGFP matched notes and bonds payable	**97**	72
AIGFP		
GIAs	**19,771**	20,664
Matched notes and bonds payable	**38,379**	35,776
Hybrid financial instrument liabilities*	**8,459**	8,856
Borrowings not guaranteed by AIG	**60,747**	59,277
Total	**$157,211**	$148,679

** Represents structured notes issued by AIGFP that are accounted for using the fair value option.*

Borrowings issued or guaranteed by AIG and subsidiary borrowings not guaranteed by AIG were as follows:

(in millions)	**March 31, 2007**	December 31, 2006
AIG borrowings:		
Notes and bonds payable	**$ 9,792**	$ 8,915
Junior subordinated debt	**3,793**	–
Loans and mortgages payable	**152**	841
MIP matched notes and bonds payable	**7,672**	5,468
Series AIGFP matched notes and bonds payable	**97**	72
Total AIG Borrowings	**21,506**	15,296
Borrowings guaranteed by AIG:		
AIGFP		
GIAs	**19,771**	20,664
Notes and bonds payable	**40,342**	37,528
Hybrid financial instrument liabilities[(a)]	**8,459**	8,856
Total	**68,572**	67,048
AIG Funding, Inc. commercial paper	**4,149**	4,821
AGC Notes and bonds payable	**797**	797
Liabilities connected to trust preferred stock	**1,440**	1,440
Total borrowings issued or guaranteed by AIG	**96,464**	89,402

(in millions)	**March 31, 2007**	December 31, 2006
Borrowings not guaranteed by AIG:		
ILFC		
Commercial paper	**3,762**	2,747
Junior subordinated debt	**999**	999
Notes and bonds payable[(b)]	**25,826**	25,592
Total	**30,587**	29,338
AGF		
Commercial paper	**4,251**	4,328
Junior subordinated debt	**346**	–
Notes and bonds payable	**19,346**	19,595
Total	**23,943**	23,923
AIGCFG		
Commercial paper	**306**	227
Loans and mortgages payable	**1,387**	1,453
Total	**1,693**	1,680
AIG Finance Taiwan Limited commercial paper	**29**	26
Other Subsidiaries	**1,849**	1,065
Borrowings of consolidated investments:		
A.I. Credit	**880**	880
AIGGIG	**55**	55
AIG Global Real Estate Investment	**1,485**	2,052
AIG SunAmerica	**201**	203
ALICO	**25**	55
Total	**2,646**	3,245
Total borrowings not guaranteed by AIG	**60,747**	59,277
Total Debt	**$157,211**	$148,679

(a) Represents structured notes issued by AIGFP that are accounted for using the fair value option.

(b) Includes borrowings under Export Credit Facility of $2.7 billion at March 31, 2007 and December 31, 2006.

The debt activity, excluding commercial paper of $12.50 billion and borrowings of consolidated investments of $2.65 billion, for the three months ended March 31, 2007 was as follows:
(in millions)

	Balance at December 31, 2006	Issuances	Maturities and Repayments	Effect of Foreign Exchange	Other Changes	**Balance at March 31, 2007**
AIG						
Notes and bonds payable	$ 8,915	$ 850	$ –	$ 11	$ 16	**$ 9,792**
Junior subordinated debt	–	3,740	–	53	–	**3,793**
Loans and mortgages payable	841	13	(702)	–	–	**152**
MIP matched notes and bonds payable	5,468	2,216	–	(14)	2	**7,672**
Series AIGFP matched notes and bonds payable	72	25	–	–	–	**97**
AIGFP						
GIAs	20,664	979	(1,775)	–	(97)	**19,771**
Notes and bonds payable and hybrid financial instrument liabilities	46,384	12,563	(10,298)	5	147	**48,801**
AGC notes and bonds payable	797	–	–	–	–	**797**
Liabilities connected to trust preferred stock	1,440	–	–	–	–	**1,440**
ILFC notes and bonds payable	25,592	702	(533)	63	2	**25,826**
ILFC junior subordinated debt	999	–	–	–	–	**999**
AGF notes and bonds payable	19,595	1,117	(1,603)	39	198	**19,346**
AGF junior subordinated debt	–	346	–	–	–	**346**
AIGCFG loans and mortgages payable	1,453	1,196	(1,188)	3	(77)	**1,387**
Other subsidiaries	1,065	109	(104)	(3)	782	**1,849**
Total	$133,285	$23,856	$(16,203)	$ 157	$ 973	**$ 142,068**

AIG (Parent Company)

AIG intends to continue its customary practice of issuing debt securities from time to time to meet its financing needs and those of certain of its subsidiaries for general corporate purposes, as well as for the MIP. As of March 31, 2007, AIG had up to $18.6 billion of debt securities, preferred and common stock and other securities registered under its universal shelf registration statement and available for issuance from time to time.

AIG maintains a medium term note program under its shelf registration statement. As of March 31, 2007, approximately $2.75 billion principal amount of notes were outstanding under the medium term note program, of which $750 million was used for AIG's general corporate purposes, $97 million was used by AIGFP and $1.9 billion was used to fund the MIP. The maturity dates of these notes range from 2011 to 2047. To the extent deemed appropriate, AIG may enter into swap transactions to manage its effective borrowing with respect to these notes.

AIG also maintains a Euro medium term note program under which an aggregate nominal amount of up to $10.0 billion of notes may be outstanding at any one time. As of March 31, 2007, the equivalent of $6.5 billion of notes were outstanding under the program, of which $4.5 billion were used to fund the MIP and the remainder was used for AIG's general corporate purposes. The aggregate amount outstanding includes $255 million resulting from foreign exchange translation into U.S. dollars, of which $171 million relates to notes issued by AIG for general corporate purposes and $84 million relates to notes issued to fund the MIP.

During the first quarter of 2007, AIG issued in Rule 144A offerings an aggregate of $1.35 billion principal amount of senior notes, of which $500 million was used to fund the MIP and $850 million was used for AIG's general corporate purposes.

AIG maintains a shelf registration statement in Japan, providing for the issuance of up to Japanese Yen 300 billion principal amount of senior notes, of which the equivalent of $425 million was outstanding as of March 31, 2007, the proceeds of which were used for AIG's general corporate purposes. AIG also maintains an Australian dollar debt program under which senior notes with an aggregate principal amount of up to 5 billion Australian dollars may be outstanding at any one time. Although as of March 31, 2007 there were no outstanding notes under the Australian program, AIG intends to use the program opportunistically to fund the MIP or for AIG's general corporate purposes.

In March 2007, AIG issued $3.7 billion of junior subordinated debentures in three series. The proceeds from the issuance are being used to repurchase shares of AIG's common stock. This issuance consisted of: $1 billion aggregate principal amount of Series A-1 6.25 percent junior subordinated debentures (U.S. Dollar Debentures); British Pound 750 million aggregate principal amount of Series A-2 5.75 percent junior subordinated debentures (Sterling Debentures); and Euro 1 billion aggregate principal amount of Series A-3 4.875 percent junior subordinated debentures (Euro Debentures and together with the U.S. Dollar Debentures and Sterling Debentures, the Debentures). Subject to the applicable Replacement Capital Covenant (RCC) described below, the U.S. Dollar Debentures are scheduled for repayment in

2037 and have a final maturity in 2087, and the Sterling and Euro Debentures are scheduled for repayment in 2037 and have a final maturity in 2067. The Debentures are redeemable by AIG prior to those times at make-whole redemption prices. In addition, the Sterling and Euro Debentures are redeemable by AIG at par beginning in 2017.

In connection with each series of Debentures, AIG entered into an RCC for the benefit of the holders of AIG's 6.25 percent Notes Due 2036. The RCCs provide that AIG will not repay, redeem, or purchase the U.S. Dollar Debentures on or before March 15, 2067, or the Sterling and Euro Debentures on or before March 15, 2047, unless it has received qualifying proceeds from the sale of replacement capital securities.

Also, in the first quarter of 2007, AIG repaid the remaining $700 million of bank term loans that were borrowed by AIG in March 2006.

AIG began applying hedge accounting for certain AIG parent transactions in the first quarter of 2007.

AIGFP

AIGFP uses the proceeds from the issuance of notes and bonds and GIA borrowings to invest in a diversified portfolio of securities and derivative transactions. The borrowings may also be temporarily invested in securities purchased under agreements to resell. AIGFP's notes and bonds include structured debt instruments whose payment terms are linked to one or more financial or other indices (such as an equity index or commodity index or another measure that is not considered to be clearly and closely related to the debt instrument). These notes contain embedded derivatives that otherwise would be required to be accounted for separately under FAS 133. Upon AIG's early adoption of FAS 155, AIGFP elected the fair value option for these notes. The notes that are accounted for using the fair value option are reported separately under hybrid financial instrument liabilities. AIG guarantees the obligations of AIGFP under AIGFP's notes and bonds and GIA borrowings. See Operating Review — Financial Services Operations, Liquidity and Derivatives herein.

AIGFP has a Euro medium term note program under which an aggregate nominal amount of up to $10.0 billion of notes may be outstanding at any one time. As of March 31, 2007, $7.16 billion of notes were outstanding under the program, including $649 million resulting from foreign exchange translation into U.S. dollars. The notes issued under this program are guaranteed by AIG and are included in AIGFP's Notes and Bonds Payable in the preceding table of borrowings.

AIG Funding

AIG Funding, Inc. (AIG Funding) issues commercial paper that is guaranteed by AIG in order to help fulfill the short-term cash requirements of AIG and its subsidiaries. The issuance of AIG Funding's commercial paper, including the guarantee by AIG, is subject to the approval of AIG's Board of Directors or the Finance Committee of the Board if it exceeds certain pre-approved limits.

As backup for the commercial paper program and for other general corporate purposes, AIG and AIG Funding maintain revolving credit facilities, which, as of March 31, 2007, had an aggregate of $5.5 billion available to be drawn and which are summarized below under Revolving Credit Facilities.

ILFC

ILFC fulfills its short-term cash requirements through operating cash flows and the issuance of commercial paper. The issuance of commercial paper is subject to the approval of ILFC's Board of Directors and is not guaranteed by AIG. ILFC maintains syndicated revolving credit facilities which, as of March 31, 2007, totaled $6.5 billion and which are summarized below under Revolving Credit Facilities. These facilities are used as back up for ILFC's maturing debt and other obligations.

As a well-known seasoned issuer, ILFC has filed an automatic shelf registration statement with the SEC allowing ILFC immediate access to the U.S. public debt markets. At March 31, 2007, $2.50 billion of debt securities were issued under this registration statement and $5.82 billion were issued under a prior registration statement. In addition, ILFC has a Euro medium term note program for $7.0 billion, under which $4.28 billion in notes were sold through March 31, 2007. Notes issued under the Euro medium term note program are included in ILFC Notes and bonds payable in the preceding table of borrowings. The foreign exchange adjustment for the foreign currency denominated debt was $796 million at March 31, 2007 and $733 million at December 31, 2006. ILFC has substantially eliminated the currency exposure arising from foreign currency denominated notes by economically hedging the portion of the note exposure not already offset by Euro-denominated operating lease payments, although such hedges did not qualify for hedge accounting treatment under FAS 133.

ILFC had a $4.3 billion Export Credit Facility for use in connection with the purchase of approximately 75 aircraft delivered through 2001. This facility was guaranteed by various European Export Credit Agencies. The interest rate varies from 5.75 percent to 5.90 percent on these amortizing ten-year borrowings depending on the delivery date of the aircraft. At March 31, 2007, ILFC had $0.9 billion outstanding under this facility. The debt is collateralized by a pledge of the

shares of a subsidiary of ILFC, which holds title to the aircraft financed under the facility.

In May 2004, ILFC entered into a similarly structured Export Credit Facility for up to a maximum of $2.64 billion for Airbus aircraft to be delivered through May 31, 2005. The facility was subsequently increased to $3.64 billion and extended to include aircraft to be delivered through May 31, 2007. The facility becomes available as the various European Export Credit Agencies provide their guarantees for aircraft based on a six-month forward-looking calendar, and the interest rate is determined through a bid process. At March 31, 2007, ILFC had $1.8 billion outstanding under this facility. Borrowings with respect to these facilities are included in ILFC's Notes and bonds payable in the preceding table of borrowings.

From time to time, ILFC enters into funded financing agreements. As of March 31, 2007, ILFC had a total of $1.2 billion outstanding, which has varying maturities through February 2012. The interest rates are LIBOR-based, with spreads ranging from 0.30 percent to 1.625 percent.

The proceeds of ILFC's debt financing are primarily used to purchase flight equipment, including progress payments during the construction phase. The primary sources for the repayment of this debt and the interest expense thereon are the cash flow from operations, proceeds from the sale of flight equipment and the rollover and refinancing of the prior debt. AIG does not guarantee the debt obligations of ILFC. See also Operating Review — Financial Services Operations and Liquidity herein.

AGF

AGF fulfills most of its short-term cash borrowing requirements through the issuance of commercial paper. The issuance of commercial paper is subject to the approval of AGF's Board of Directors and is not guaranteed by AIG. AGF maintains committed syndicated revolving credit facilities which, as of March 31, 2007, totaled $4.25 billion and which are summarized below under Revolving Credit Facilities. The facilities can be used for general corporate purposes and to provide backup for AGF's commercial paper programs.

As of March 31, 2007, notes and bonds aggregating $19.69 billion were outstanding with maturity dates ranging from 2007 to 2067 at interest rates ranging from 1.94 percent to 8.45 percent. To the extent deemed appropriate, AGF may enter into swap transactions to manage its effective borrowing with respect to these notes and bonds. As a well-known seasoned issuer, AGF has filed an automatic shelf registration statement with the SEC allowing AGF immediate access to the U.S. public debt markets. At March 31, 2007, AGF had the corporate authorization to issue up to $12.5 billion of debt securities under its shelf registration statements.

In January 2007, AGF issued junior subordinated debentures in an aggregate principal amount of $350 million that mature in January 2067. The debentures underlie a series of trust preferred securities sold by a trust sponsored by AGF in a Rule 144A/Regulation S offering. AGF can redeem the debentures at par beginning in January 2017.

AGF's funding sources include a medium term note program, private placement debt, retail note issuances, bank financing and securitizations of finance receivables that AGF accounts for as on-balance-sheet secured financings. In addition, AGF has become an established issuer of long-term debt in the international capital markets.

In addition to debt refinancing activities, proceeds from the collection of finance receivables are used to fund cash needs including the payment of principal and interest on AGF's debt. AIG does not guarantee any of the debt obligations of AGF. See also Operating Review — Financial Services Operations and Liquidity herein.

AIGCFG

AIGCFG has a variety of funding mechanisms for its various markets, including retail and wholesale deposits, short-term and long-term bank loans, and intercompany subordinated debt. AIG Credit Card Company (Taiwan), a consumer finance business in Taiwan, and AIG Finance (Thailand) PLC have issued commercial paper for the funding of their respective operations. AIG does not guarantee any borrowings for AIGCFG businesses, including this commercial paper.

Revolving Credit Facilities

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

(in millions)

Facility	Size	Borrower(s)	Available Amount **March 31, 2007**	Expiration	One-Year Term-Out Option
AIG:					
364-Day Syndicated Facility	$1,625	AIG/AIG Funding[(a)] AIG Capital Corporation[(a)]	**$1,625**	July 2007	Yes
5-Year Syndicated Facility	1,625	AIG/AIG Funding[(a)] AIG Capital Corporation[(a)]	**1,625**	July 2011	No
364-Day Bilateral Facility[(b)]	3,200	AIG/AIG Funding	**211**	November 2007	Yes
364-Day Intercompany Facility[(c)]	2,000	AIG	**2,000**	October 2007	Yes
Total AIG	$8,450		**$5,461**		
ILFC:					
5-Year Syndicated Facility	$2,500	ILFC	**$2,500**	October 2011	No
5-Year Syndicated Facility	2,000	ILFC	**2,000**	October 2010	No
5-Year Syndicated Facility	2,000	ILFC	**2,000**	October 2009	No
Total ILFC	$6,500		**$6,500**		
AGF:					
364-Day Syndicated Facility	$2,125	American General Finance Corporation American General Finance, Inc.[(d)]	**$2,125**	July 2007	Yes
5-Year Syndicated Facility	2,125	American General Finance Corporation	**2,125**	July 2010	No
Total AGF	$4,250		**$4,250**		

(a) Guaranteed by AIG.
(b) This facility can be drawn in the form of loans or letters of credit. All drawn amounts shown above are in the form of letters of credit.
(c) Subsidiaries of AIG are the lenders on this facility.
(d) American General Finance, Inc. is an eligible borrower for up to $400 million only.

Credit Ratings

The cost and availability of unsecured financing for AIG and its subsidiaries are generally dependent on their short-term and long-term debt ratings. The following table presents the credit ratings of AIG and certain of its subsidiaries as of April 30, 2007. In parentheses, following the initial occurrence in the table of each rating, is an indication of that rating's relative rank within the agency's rating categories. That ranking refers only to the generic or major rating category and not to the modifiers appended to the rating by the rating agencies to denote relative position within such generic or major category.

	Short-term Debt			Senior Long-term Debt		
	Moody's	S&P	Fitch	Moody's[(a)]	S&P[(b)]	Fitch[(c)]
AIG	P-1 (1st of 3)	A-1+ (1st of 6)	F1+ (1st of 5)	Aa2 (2nd of 9)	AA (2nd of 8)	AA (2nd of 9)
AIG Financial Products Corp.[(d)]	P-1	A-1+	—	Aa2	AA	—
AIG Funding, Inc.[(d)]	P-1	A-1+	F1+	—	—	—
ILFC	P-1	A-1+	F1 (1st of 5)	A1 (3rd of 9)	AA-[(e)](2nd of 8)	A+ (3rd of 9)
American General Finance Corporation	P-1	A-1 (1st of 6)	F1	A1	A+ (3rd of 8)	A+
American General Finance, Inc.	P-1	A-1	F1	—	—	A+

(a) Moody's Investors Service (Moody's). Moody's appends numerical modifiers 1, 2 and 3 to the generic rating categories to show relative position within rating categories.
(b) Standard & Poor's, a division of the McGraw-Hill Companies (S&P). S&P ratings may be modified by the addition of a plus or minus sign to show relative standing within the major rating categories.
(c) Fitch Ratings (Fitch). Fitch ratings may be modified by the addition of a plus or minus sign to show relative standing within the major rating categories.
(d) AIG guarantees all obligations of AIG Financial Products Corp. and AIG Funding, Inc.
(e) Negative rating outlook. A negative outlook by S&P indicates that a rating may be lowered, but is not necessarily a precursor of a ratings change. The outlook on all other credit ratings in the table is stable.

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

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

AIG believes that any of its own or its subsidiaries' contractual obligations that are subject to "ratings triggers" or financial covenants relating to "ratings triggers" would not have a material adverse effect on its financial condition or liquidity. Ratings downgrades could also trigger the application of termination provisions in certain of AIG's contracts, principally agreements entered into by AIGFP and assumed reinsurance contracts entered into by Transatlantic.

It is estimated that, as of the close of business on April 30, 2007, based on AIGFP's outstanding municipal GIAs and financial derivatives transactions as of such date, a downgrade of AIG's long-term senior debt ratings to 'Aa3' by Moody's or 'AA–' by S&P would permit counterparties to call for approximately $902 million of collateral. Further, additional downgrades could result in requirements for substantial additional collateral, which could have a material effect on how AIGFP manages its liquidity. The actual amount of additional collateral that AIGFP would be required to post to counterparties in the event of such downgrades depends on market conditions, the fair value of the outstanding affected transactions and other factors prevailing at the time of the downgrade. Additional obligations to post collateral would increase the demand on AIGFP's liquidity.

Contractual Obligations and Other Commercial Commitments

The maturity schedule of AIG's contractual obligations at March 31, 2007 was as follows:

		Payments due by Period			
(in millions)	Total Payments	Less Than One Year	1-3 Years	3+-5 Years	Over Five Years
Borrowings[(a)]	$142,068	$35,916	$ 34,260	$ 34,865	$ 37,027
Interest payments on borrowings	80,102	5,204	8,535	6,166	60,197
Loss reserves[(b)]	81,135	22,312	24,747	11,764	22,312
Insurance and investment contract liabilities[(c)]	593,578	22,560	34,274	41,429	495,315
GIC liabilities[(d)]	36,224	5,495	17,240	3,000	10,489
Aircraft purchase commitments	17,177	3,249	7,185	2,377	4,366
Total	$950,284	$94,736	$126,241	$ 99,601	$629,706

(a) Excludes commercial paper and obligations included as debt pursuant to FASB Interpretation No. 46, "Consolidation of Variable Interest Entities" (FIN 46R), and includes hybrid financial instrument liabilities recorded at fair value.

(b) Represents future loss and loss adjustment expense payments estimated based on historical loss development payment patterns.

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

(d) Represents guaranteed maturities under GICs.

The maturity schedule of other commercial commitments of AIG and its consolidated subsidiaries at March 31, 2007 was as follows:

(in millions)	Total Amounts Committed	Amount of Commitment Expiration: Less Than One Year	1-3 Years	3+-5 Years	Over Five Years
Letters of credit:					
Life Insurance & Retirement Services	$ 185	$ 17	$ 4	$ 22	$ 142
DBG	191	191	—	—	—
Standby letters of credit:					
Capital Markets	1,728	1,452	72	42	162
Parent Company[(a)]	739	620	1	118	—
Guarantees:					
Life Insurance & Retirement Services[(b)]	2,170	76	44	537	1,513
Aircraft Leasing	201	—	51	28	122
Asset Management	515	292	53	—	170
General Insurance	40	40	—	—	—
Other commercial commitments[(c)]:					
Capital Markets[(d)]	16,161	5,323	1,948	2,684	6,206
Aircraft Leasing[(e)]	344	—	—	—	344
Other Financial Services companies	12	8	—	—	4
Life Insurance & Retirement Services[(f)]	5,149	1,347	1,687	1,124	991
Asset Management[(g)]	1,410	1,003	243	126	38
General Insurance companies[(h)]	1,982	692	880	389	21
Parent and other companies	318	112	181	25	—
Total	$ 31,145	$11,173	$5,164	$5,095	$9,713

(a) Represents reimbursement obligations under letters of credit issued by commercial banks.

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

(c) Excludes commitments with respect to pension plans. The annual pension contribution for 2007 is expected to be approximately $95 million for U.S. and non-U.S. plans.

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

(e) Primarily in connection with options to acquire aircraft.

(f) Primarily AIG SunAmerica commitments to invest in partnerships.

(g) Includes commitments to invest in limited partnerships, private equity and hedge funds and real estate.

(h) Primarily commitments to invest in limited partnerships.

Shareholders' Equity

AIG's consolidated shareholders' equity increased during the first three months of 2007 and twelve months of 2006 as follows:

(in millions)	**March 31, 2007**	**December 31, 2006**
Beginning of year	**$101,677**	$86,317
Net income	**4,130**	14,048
Unrealized appreciation (depreciation) of investments, net of tax	**851**	1,735
Cumulative translation adjustment, net of tax	**(137)**	936
Dividends to shareholders	**(430)**	(1,690)
Payments advanced to purchase shares	**(2,851)**	—
Other*	**(185)**	331
End of period	**$103,055**	$101,677

** Reflects the effects of employee stock transactions and cumulative effect of accounting changes.*

AIG has in the past reinvested most of its unrestricted earnings in its operations and believes such continued reinvestment in the future will be adequate to meet any foreseeable capital needs. However, AIG may choose from time to time to raise additional funds through the issuance of additional securities.

In February 2007, AIG's Board of Directors adopted a new dividend policy, to take effect with the dividend to be declared in the second quarter of 2007, providing that under ordinary circumstances, AIG's plan will be to increase its common stock dividend by approximately 20 percent annually. The payment of any dividend, however, is at the discretion of AIG's Board of Directors, and the future payment of dividends will depend on various factors, including the performance of AIG's businesses, AIG's consolidated financial position, results of operations and liquidity and the existence of investment opportunities.

Share Repurchases

From time to time, AIG may buy shares of its common stock for general corporate purposes, including to satisfy its obligations under various employee benefit plans. In February 2007, AIG's Board of Directors increased its share repurchase program by authorizing the repurchase of shares with an aggregate purchase price of $8 billion. During March 2007, AIG made open market share repurchases and entered into a $3 billion structured share repurchase arrangement. A total of 2,470,499 shares were repurchased during March 2007. The portion of the payment advanced by AIG under the structured share repurchase arrangement that had not yet been utilized to repurchase shares at March 31, 2007, amounting to $2.85 billion, has been recorded as a component of shareholders' equity under the caption Payments advanced to purchase shares. Purchases have continued since March 31, 2007, with an additional 6,643,052 shares purchased during April 2007, and purchases are anticipated to occur throughout 2007. All shares repurchased are recorded as treasury stock at cost.

Liquidity

AIG manages liquidity at both the subsidiary and parent company levels. At March 31, 2007, AIG's consolidated invested assets, primarily held by its subsidiaries, included $27.6 billion in cash and short-term investments. Consolidated net cash provided from operating activities in the first three months of 2007 amounted to $8.6 billion. At the parent company level, liquidity management activities are conducted in a manner to preserve and enhance funding stability, flexibility, and diversity through the full range of potential operating environments and market conditions. AIG's primary sources of cash flow are dividends and other payments from its regulated and unregulated subsidiaries, as well as issuances of debt securities. Primary uses of cash flow are for debt service, subsidiary funding, shareholder dividend payments and common stock repurchases. Management believes that AIG's liquid assets, cash provided by operations and access to the capital markets will enable it to meet its anticipated cash requirements, including the funding of increased dividends under AIG's new dividend policy and repurchases of common stock.

In the first three months of 2007, AIG parent collected $1.3 billion in dividends and other payments from subsidiaries, principally from DBG companies, issued $4.6 billion of debt securities and retired $700 million of debt, excluding MIP and Series AIGFP debt. AIG parent also advanced $3 billion for a structured share repurchase arrangement. AIG parent made interest payments totaling $16 million, made $82 million in capital contributions to subsidiaries, and paid $430 million in dividends to shareholders in the first three months of 2007.

AIG funds its short-term working capital needs through commercial paper issued by AIG Funding. As of March 31, 2007, AIG Funding had $4.1 billion of commercial paper outstanding with an average maturity of 35 days. As additional liquidity, AIG parent and AIG Funding maintain revolving credit facilities that, as of March 31, 2007, had an aggregate of $5.5 billion available to be drawn, which are summarized above under Revolving Credit Facilities.

Invested Assets

AIG's investment strategy is to invest primarily in high quality securities while maintaining diversification to avoid significant exposure to issuer, industry and/or country concentrations.

The following tables summarize the composition of AIG's invested assets by segment.

(in millions)	General Insurance	Life Insurance & Retirement Services	Financial Services	Asset Management	Other	Total
March 31, 2007						
Fixed maturities:						
Bonds available for sale, at fair value	$ 69,508	$289,383	$ 1,369	$29,881	$ –	$390,141
Bonds held to maturity, at amortized cost	21,414	–	–	–	–	21,414
Bond trading securities, at fair value	–	8,845	–	–	–	8,845
Equity securities:						
Common stocks available for sale, at fair value	4,424	9,713	–	238	82	14,457
Common and preferred stocks trading, at fair value	395	15,361	–	–	–	15,756
Preferred stocks available for sale, at fair value	1,950	746	7	–	–	2,703
Mortgage loans on real estate, net of allowance	12	13,833	111	4,272	–	18,228
Policy loans	2	7,478	2	48	(9)	7,521
Collateral and guaranteed loans, net of allowance	3	782	3,190	781	84	4,840
Financial services assets:						
Flight equipment primarily under operating leases, net of accumulated depreciation	–	–	41,345	–	–	41,345
Securities available for sale, at fair value	–	–	47,643	–	–	47,643
Trading securities, at fair value	–	–	5,369	–	–	5,369
Spot commodities	–	–	73	–	–	73
Unrealized gain (loss) on swaps, options and forward transactions	–	–	17,198	–	(651)	16,547
Trade receivables	–	–	3,883	–	–	3,883
Securities purchased under agreements to resell, at contract value	–	–	31,775	–	–	31,775
Finance receivables, net of allowance	–	5	29,503	–	–	29,508
Securities lending collateral, at fair value	6,012	53,886	80	14,849	–	74,827
Other invested assets	9,909	14,836	2,927	15,892	603	44,167
Short-term investments, at cost	3,575	16,712	1,367	4,092	120	25,866
Total investments and financial services assets as shown on the balance sheet	117,204	431,580	185,842	70,053	229	804,908
Cash	427	772	341	157	5	1,702
Investment income due and accrued	1,290	4,513	22	344	1	6,170
Real estate, net of accumulated depreciation	565	894	24	76	21	1,580
Total invested assets*	$119,486	$437,759	$186,229	$70,630	$ 256	$814,360

** At March 31, 2007, approximately 68 percent and 32 percent of invested assets were held in domestic and foreign investments, respectively.*

(in millions)	General Insurance	Life Insurance & Retirement Services	Financial Services	Asset Management	Other	Total
December 31, 2006						
Fixed maturities:						
Bonds available for sale, at fair value	$67,994	$288,540	$ 1,357	$ 29,500	$ –	$ 387,391
Bonds held to maturity, at amortized cost	21,437	–	–	–	–	21,437
Bond trading securities, at fair value	1	9,036	–	–	–	9,037
Equity securities:						
Common stocks available for sale, at fair value	4,245	8,711	–	226	80	13,262
Common stocks trading, at fair value	350	14,071	–	–	–	14,421
Preferred stocks available for sale, at fair value	1,884	650	5	–	–	2,539
Mortgage loans on real estate, net of allowance	13	12,852	95	4,107	–	17,067
Policy loans	1	7,458	2	48	(8)	7,501
Collateral and guaranteed loans, net of allowance	3	733	2,301	729	84	3,850
Financial services assets:						
Flight equipment primarily under operating leases, net of accumulated depreciation	–	–	39,875	–	–	39,875
Securities available for sale, at fair value	–	–	47,205	–	–	47,205
Trading securities, at fair value	–	–	5,031	–	–	5,031
Spot commodities	–	–	220	–	–	220
Unrealized gain on swaps, options and forward transactions	–	–	19,252	–	–	19,252
Trade receivables	–	–	4,317	–	–	4,317
Securities purchased under agreements to resell, at contract value	–	–	31,853	–	–	31,853
Finance receivables, net of allowance	–	–	29,573	–	–	29,573
Securities lending collateral, at fair value	5,376	50,099	76	13,755	–	69,306
Other invested assets	9,207	14,263	2,212	15,823	609	42,114
Short-term investments, at cost	3,281	14,520	1,245	6,198	5	25,249
Total investments and financial services assets as shown on the balance sheet	113,792	420,933	184,619	70,386	770	790,500
Cash	334	740	390	118	8	1,590
Investment income due and accrued	1,363	4,364	23	326	1	6,077
Real estate, net of accumulated depreciation	570	698	17	75	26	1,386
Total invested assets*	$116,059	$426,735	$ 185,049	$ 70,905	$805	$ 799,553

** At December 31, 2006, approximately 68 percent and 32 percent of invested assets were held in domestic and foreign investments, respectively.*

As a result of AIG's periodic evaluation of its securities for other-than-temporary impairments in value, AIG recorded, in realized capital gains (losses), other-than-temporary impairment pre-tax losses of $467 million and $226 million in the first three months of 2007 and 2006, respectively. The majority of the losses in the first three months of 2007 related to the Foreign Life operations and reflected a decline in value of U.S. dollar bonds held in Thailand and Singapore due to the depreciation of the U.S. dollar against the local currency.

No impairment charge with respect to any one single credit was significant to AIG's consolidated financial condition or results of operations, and no individual impairment loss exceeded 1.0 percent of consolidated net income for the first three months of 2007.

At March 31, 2007, aggregate pre-tax unrealized gains were $17.9 billion, while the pre-tax unrealized losses with respect to investment grade bonds, non-investment grade bonds and equity securities were $2.6 billion, $79 million and $116 million, respectively. Aging of the pre-tax unrealized losses with respect to these securities, distributed as a percentage of cost relative to unrealized loss (the extent by which the fair value is less than amortized cost or cost), including the number of respective items, was as follows:

	Less than or equal to 20% of Cost			Greater than 20% to 50% of Cost			Greater than 50% of Cost			Total		
Aging *(dollars in millions)*	Cost[a]	Unrealized Loss	Items	Cost[a]	Unrealized Loss	Items	Cost[a]	Unrealized Loss	Items	Cost[a]	Unrealized Loss[b]	Items
Investment grade bonds												
0-6 months	$ 44,008	$ 533	5,413	$ 83	$22	10	$ —	$ —	—	$ 44,091	$ 555	5,423
7-12 months	13,094	151	1,710	20	5	1	—	—	—	13,114	156	1,711
>12 months	84,288	1,900	12,961	61	5	16	—	—	—	84,349	1,905	12,977
Total	$141,390	$2,584	20,084	$164	$32	27	$ —	$ —	—	$141,554	$2,616	20,111
Below investment grade bonds												
0-6 months	$ 2,273	$ 19	703	$ 3	$ 1	5	$ 2	$ 1	5	$ 2,278	$ 21	713
7-12 months	361	6	47	2	—	2	—	—	—	363	6	49
>12 months	1,696	52	208	—	—	—	—	—	—	1,696	52	208
Total	$ 4,330	$ 77	958	$ 5	$ 1	7	$ 2	$ 1	5	$ 4,337	$ 79	970
Total bonds												
0-6 months	$ 46,281	$ 552	6,116	$ 86	$23	15	$ 2	$ 1	5	$ 46,369	$ 576	6,136
7-12 months	13,455	157	1,757	22	5	3	—	—	—	13,477	162	1,760
>12 months	85,984	1,952	13,169	61	5	16	—	—	—	86,045	1,957	13,185
Total	$145,720	$2,661	21,042	$169	$33	34	$ 2	$ 1	5	$145,891	$2,695	21,081
Equity securities												
0-6 months	$ 1,831	$ 72	1,454	$ 69	$21	115	$ 2	$ —	8	$ 1,902	$ 93	1,577
7-12 months	261	12	159	35	10	43	1	1	24	297	23	226
>12 months	—	—	—	—	—	—	—	—	—	—	—	—
Total	$ 2,092	$ 84	1,613	$104	$31	158	$ 3	$ 1	32	$ 2,199	$ 116	1,803

(a) For bonds, represents amortized cost.

(b) As more fully described above, upon realization, certain realized losses will be charged to participating policyholder accounts, or realization will result in a current decrease in the amortization of DAC.

At March 31, 2007, the fair value of AIG's fixed maturities and equity securities aggregated $501.6 billion. At March 31, 2007, aggregate unrealized gains after taxes for fixed maturity and equity securities were $11.6 billion. At March 31, 2007, the aggregate unrealized losses after taxes of fixed maturity and equity securities were approximately $1.8 billion.

The effect on net income of unrealized losses after taxes will be mitigated upon realization because certain realized losses will be charged to participating policyholder accounts, or realization will result in current decreases in the amortization of certain DAC.

At March 31, 2007, unrealized losses for fixed maturity securities and equity securities did not reflect any significant industry concentrations.

The amortized cost of fixed maturities available for sale in an unrealized loss position at March 31, 2007, by contractual maturity, is shown below:

(in millions)	Amortized Cost
Due in one year or less	$ 6,525
Due after one year through five years	28,993
Due after five years through ten years	48,604
Due after ten years	61,769
Total	$145,891

For the three months ended March 31, 2007, the pre-tax realized losses incurred with respect to the sale of fixed maturities and equity securities were $255 million. The aggregate fair value of securities sold was $7.3 billion, which was approximately 97 percent of amortized cost. The average period of time that securities sold at a loss during the three months ended March 31, 2007 were trading continuously at a price below book value was approximately four months.

Risk Management

AIG believes that strong risk management practices and a sound internal control environment are fundamental to its continued success and profitable growth. Through its extensive global operations, AIG is exposed to a number of major risks, including insurance, credit, market and operational risks. AIG senior management establishes the framework, principles and guidelines for risk management. AIG business executives are responsible for establishing and implementing risk management processes and responding to the individual needs and issues within their businesses, including risk concentrations within their business segments.

For a complete discussion of AIG's risk management program, see Management's Discussion and Analysis of Financial Condition and Results of Operations in the 2006 Annual Report on Form 10-K.

Insurance, Asset Management and Non-Trading Financial Services VaR

AIG has performed one comprehensive Value at Risk (VaR) analysis across all of its non-trading businesses, and a separate VaR analysis for its trading business at AIGFP. The comprehensive VaR is categorized by AIG business segment (General Insurance, Life Insurance & Retirement Services, Financial Services and Asset Management) and also by market risk factor (interest rate, currency and equity).

AIG calculated the VaR with respect to net fair values as of March 31, 2007 and December 31, 2006. The VaR number represents the maximum potential loss as of those dates that could be incurred with a 95 percent confidence and a one-month holding period.

The following table presents the period-end, average, high and low VaRs on a diversified basis and of each component of market risk for each of AIG's non-trading investments. The diversified VaR is usually smaller than the sum of its components due to correlation effects.

	2007				2006			
		Three months ended March 31,				Year ended December 31,		
(in millions)	As of March 31,	Average	High	Low	As of December 31,	Average	High	Low
Total AIG Non-Trading								
Market risk:								
Diversified	**$5,129**	**$5,101**	**$5,129**	**$5,073**	$5,073	$5,209	$5,783	$4,852
Interest rate	**4,659**	**4,618**	**4,659**	**4,577**	4,577	4,962	5,765	4,498
Currency	**685**	**685**	**686**	**685**	686	641	707	509
Equity	**1,956**	**1,914**	**1,956**	**1,873**	1,873	1,754	1,873	1,650
General Insurance:								
Market risk:								
Diversified	**$1,543**	**$1,630**	**$1,717**	**$1,543**	$1,717	$1,697	$1,776	$1,617
Interest rate	**1,470**	**1,506**	**1,541**	**1,470**	1,541	1,635	1,717	1,541
Currency	**205**	**208**	**212**	**205**	212	162	212	119
Equity	**587**	**580**	**587**	**573**	573	551	573	535
Life Insurance & Retirement Services:								
Market risk:								
Diversified	**$4,688**	**$4,631**	**$4,688**	**$4,574**	$4,574	$4,672	$5,224	$4,307
Interest rate	**4,552**	**4,511**	**4,552**	**4,471**	4,471	4,563	5,060	4,229
Currency	**583**	**575**	**583**	**568**	568	538	592	459
Equity	**1,325**	**1,309**	**1,325**	**1,293**	1,293	1,228	1,299	1,133
Non-Trading Financial Services:								
Market risk:								
Diversified	**$ 85**	**$ 105**	**$ 125**	**$ 85**	$ 125	$ 165	$ 252	$ 125
Interest rate	**76**	**101**	**127**	**76**	127	166	249	127
Currency	**12**	**11**	**12**	**11**	11	8	11	7
Equity	**1**	**1**	**1**	**1**	1	1	2	1
Asset Management:								
Market risk:								
Diversified	**$ 43**	**$ 53**	**$ 64**	**$ 43**	$ 64	$ 144	$ 190	$ 64
Interest rate	**37**	**50**	**63**	**37**	63	145	192	63
Currency	**2**	**2**	**3**	**2**	3	4	7	3
Equity	**11**	**10**	**11**	**8**	8	9	13	8

AIG's total Non-Trading VaR for the first three months of 2007 was largely unchanged from the total Non-Trading VaR at the end of 2006. VaR increases resulting from business growth during the first three months of 2007 were offset by a reduction in interest rate volatility in many currencies.

Capital Markets Trading VaR

AIGFP maintains a very conservative market risk profile and minimizes risk in interest rates, equities, commodities and foreign exchange. Market exposures in option implied volatilities, correlations and basis risks are also minimized over time but those are the main types of market risks that AIGFP manages.

AIGFP's minimal reliance on market risk driven revenue is reflected in its VaR. Because the market risk with respect to securities available for sale, at market, is substantially hedged, segregation of the financial instruments into trading and other than trading was not deemed necessary.

AIGFP reports its VaR using a 95 percent confidence interval and a one-day holding period.

The following table presents the period-end, average, high, and low VaRs (based on daily observations) on a diversified basis and of each component of market risk for Capital Markets operations. The diversified VaR is usually smaller than the sum of its components due to correlation effects.

	2007				2006			
		Three months ended March 31,				Year ended December 31,		
(in millions)	As of March 31,	Average	High	Low	As of December 31,	Average	High	Low
Total AIG trading market risk:								
Diversified	**$4**	**$5**	**$6**	**$4**	$4	$4	$7	$3
Interest rate	**2**	**2**	**3**	**2**	2	2	3	1
Currency	**1**	**1**	**1**	**1**	1	1	3	1
Equity	**2**	**3**	**4**	**2**	3	3	4	2
Commodity	**3**	**4**	**5**	**3**	3	3	4	2

ITEM 3. Quantitative and Qualitative Disclosures About Market Risk

Included in Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations.

ITEM 4. Controls and Procedures

In connection with the preparation of this Form 10-Q, an evaluation was carried out by AIG's management, with the participation of AIG's Chief Executive Officer and Chief Financial Officer, of the effectiveness of AIG's disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934 (Exchange Act)). Disclosure controls and procedures are designed to ensure that information required to be disclosed in reports filed or submitted under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in SEC rules and forms and that such information is accumulated and communicated to management, including the Chief Executive Officer and Chief Financial Officer, to allow timely decisions regarding required disclosures. Based on its evaluation, and in light of the previously identified material weakness in internal control over financial reporting, as of December 31, 2006, relating to controls over income tax accounting described in the 2006 Annual Report on Form 10-K, AIG's Chief Executive Officer and Chief Financial Officer concluded that, as of March 31, 2007, AIG's disclosure controls and procedures were ineffective. In addition, there has been no change in AIG's internal control over financial reporting (as defined in Rule 13a-15(f) under the Exchange Act) that occurred during the quarter ended March 31, 2007 that has materially affected, or is reasonably likely to materially affect, AIG's internal control over financial reporting.

Part II

ITEM 2. Unregistered Sales of Equity Securities and Use of Proceeds

The table below provides information with respect to purchases of AIG Common stock during the three months ended March 31, 2007.

Period	Total Number of Shares Purchased[1]	Average Price Paid per Share	Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs	Maximum Number of Shares that May Yet Be Purchased Under the Plans or Programs at End of Month[2]
January 1 - 31	–	$ –	–	36,542,700
February 1 - 28	–	–	–	[2]
March 1 - 31	2,470,499	66.54	2,470,499	[2]
Total	2,470,499	$66.54	2,470,499	

(1) Does not include 34,839 shares delivered or attested to in satisfaction of the exercise price by holders of AIG employee stock options exercised during the three months ended March 31, 2007.

(2) In July 2002, AIG announced that its Board of Directors had authorized the purchase of up to 10 million shares of AIG common stock. In February 2003, AIG announced that the Board had expanded the existing program through the authorization of an additional 50 million shares. In February 2007, AIG's Board of Directors increased the repurchase program by authorizing the repurchase of shares with an aggregate purchase price of $8 billion. A balance of $7.84 billion remained for purchases under the program as of March 31, 2007, although $2.85 billion of that amount has been advanced by AIG to purchase shares under the program. The purchase program has no set expiration or termination date.

ITEM 6. Exhibits

See accompanying Exhibit Index.

SIGNATURE

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

AMERICAN INTERNATIONAL GROUP, INC.
(Registrant)

/s/ STEVEN J. BENSINGER

Steven J. Bensinger
Executive Vice President and Chief Financial Officer

/s/ DAVID L. HERZOG

David L. Herzog
Senior Vice President and Comptroller
(Principal Accounting Officer)

Dated: May 10, 2007

EXHIBIT INDEX

Exhibit Number	Description	Location
11	Statement re computation of per share earnings	Included in Note (3) of Notes to Consolidated Financial Statements.
12	Statement re computation of ratios	Filed herewith.
31	Rule 13a-14(a)/15d-14(a) Certifications	Filed herewith.
32	Section 1350 Certifications	Filed herewith.

Exhibit 12

American International Group, Inc.
Computation of Ratios of Earnings to Fixed Charges

(in millions, except ratios)	Three Months Ended March 31, **2007**	2006
Income before income taxes, minority interest and cumulative effect of an accounting change	**$ 6,172**	$ 4,793
Less – Equity income of less than 50% owned persons	**42**	20
Add – Dividends from less than 50% owned persons	**—**	3
	6,130	4,776
Add – Fixed charges	**2,672**	1,948
Less – Capitalized interest	**11**	15
Income before income taxes, minority interest, cumulative effect of an accounting change and fixed charges	**$ 8,791**	$ 6,709
Fixed charges:		
Interest costs	**$ 2,612**	$ 1,896
Rental expense*	**60**	52
Total fixed charges	**$ 2,672**	$ 1,948
Ratio of earnings to fixed charges	**3.29**	3.44
Secondary Ratio		
Interest credited to GIC and GIA policy and contract holders	**$ (1,579)**	$ (1,090)
Total fixed charges excluding interest credited to GIC and GIA policy and contract holders	**$ 1,093**	$ 858
Secondary ratio of earnings to fixed charges	**6.60**	6.55

** The proportion deemed representative of the interest factor.*

The secondary ratio is disclosed for the convenience of fixed income investors and the rating agencies that serve them and is more comparable to the ratios disclosed by all issuers of fixed income securities. The secondary ratio removes interest credited to guaranteed investment contract (GIC) policyholders and guaranteed investment agreement (GIA) contractholders. Such interest expenses are also removed from income before income taxes, minority interest and cumulative effect of an accounting change used in this calculation. GICs and GIAs are entered into by AIG's insurance subsidiaries, principally Sun America Life Insurance Company and AIG Financial Products Corp. and its subsidiaries, respectively. The proceeds from GICs and GIAs are invested in a diversified portfolio of securities, primarily investment grade bonds. The assets acquired yield rates greater than the rates on the related policyholders obligation or agreement, with the intent of earning operating income from the spread.

Exhibit 31

CERTIFICATIONS

I, Martin J. Sullivan, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q of American International Group, Inc.;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:

(a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

(b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

(c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

(d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):

(a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

(b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

/s/ MARTIN J. SULLIVAN

Martin J. Sullivan
President and Chief Executive Officer

Date: May 10, 2007

CERTIFICATIONS

I, Steven J. Bensinger, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q of American International Group, Inc.;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:

(a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

(b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

(c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

(d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):

(a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

(b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

/s/ STEVEN J. BENSINGER

Steven J. Bensinger
Executive Vice President and Chief Financial Officer

Date: May 10, 2007

Exhibit 32

CERTIFICATION

In connection with the Quarterly Report on Form 10-Q of American International Group, Inc. (the "Company") for the quarter ended March 31, 2007, as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, Martin J. Sullivan, President and Chief Executive Officer of the Company, certify, pursuant to 18 U.S.C. Section 1350, that to my knowledge:

1. The Report fully complies with the requirements of Section 13(a) or 15(d), as applicable, of the Securities Exchange Act of 1934; and

2. The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

/s/ MARTIN J. SULLIVAN

Martin J. Sullivan
President and Chief Executive Officer

Date: May 10, 2007

The foregoing certification is being furnished solely pursuant to 18 U.S.C. Section 1350 and is not being filed as part of the Report or as a separate disclosure document.

CERTIFICATION

In connection with the Quarterly Report on Form 10-Q of American International Group, Inc. (the "Company") for the quarter ended March 31, 2007, as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, Steven J. Bensinger, Executive Vice President and Chief Financial Officer of the Company, certify, pursuant to 18 U.S.C. Section 1350, that to my knowledge:

1. The Report fully complies with the requirements of Section 13(a) or 15(d), as applicable, of the Securities Exchange Act of 1934; and

2. The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

/s/ STEVEN J. BENSINGER

Steven J. Bensinger
Executive Vice President and Chief Financial Officer

Date: May 10, 2007

The foregoing certification is being furnished solely pursuant to 18 U.S.C. Section 1350 and is not being filed as part of the Report or as a separate disclosure document.

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

Form 10-Q

(Mark One)

☑ QUARTERLY REPORT UNDER SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended June 30, 2007

or

☐ TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the transition period from to

Commission File Number 1-8787

American International Group, Inc.

(Exact name of registrant as specified in its charter)

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

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

Former name, former address and former fiscal year, if changed since last report: None

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

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of accelerated filer and large accelerated filer in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer ☑ Accelerated filer ☐ Non-accelerated filer ☐

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes ☐ No ☑

As of July 31, 2007, there were 2,564,389,291 shares outstanding of the registrant's common stock.

TABLE OF CONTENTS

Part I – FINANCIAL INFORMATION

ITEM 1. Financial Statements (unaudited)

CONSOLIDATED BALANCE SHEET

(in millions) (unaudited)

	June 30, 2007	December 31, 2006
Assets:		
Investments and financial services assets:		
Fixed maturities:		
Bonds available for sale, at fair value (amortized cost: 2007 – $383,451; 2006 – $377,698) (includes hybrid financial instruments: 2007 – $767; 2006 – $522)	**$ 388,717**	$387,391
Bonds held to maturity, at amortized cost (fair value: 2007 – $21,614; 2006 – $22,154)	**21,389**	21,437
Bond trading securities, at fair value (cost: 2007 – $9,264; 2006 – $9,016)	**9,261**	9,037
Equity securities:		
Common stocks available for sale, at fair value (cost: 2007 – $12,320; 2006 – $10,662)	**17,372**	13,262
Common and preferred stocks trading, at fair value (cost: 2007 – $15,101; 2006 – $12,734)	**17,479**	14,421
Preferred stocks available for sale, at fair value (cost: 2007 – $2,574; 2006 – $2,485)	**2,609**	2,539
Mortgage loans on real estate, net of allowance (2007 – $57; 2006 – $55)	**18,701**	17,067
Policy loans	**7,607**	7,501
Collateral and guaranteed loans, net of allowance (2007 – $3; 2006 – $9)	**5,054**	3,850
Financial services assets:		
Flight equipment primarily under operating leases, net of accumulated depreciation (2007 – $9,670; 2006 – $8,835)	**42,232**	39,875
Securities available for sale, at fair value (cost: 2007 – $46,508; 2006 – $45,912)	**48,166**	47,205
Trading securities, at fair value	**4,567**	5,031
Spot commodities	**93**	220
Unrealized gain on swaps, options and forward transactions	**18,120**	19,252
Trade receivables	**7,138**	4,317
Securities purchased under agreements to resell, at contract value	**31,595**	31,853
Finance receivables, net of allowance (2007 – $736; 2006 – $737) (includes finance receivables held for sale: 2007 – $608; 2006 – $1,124)	**30,027**	29,573
Securities lending collateral, at fair value (which approximates cost)	**81,079**	69,306
Other invested assets	**49,887**	42,114
Short-term investments, at cost (approximates fair value)	**27,736**	25,249
Total investments and financial services assets	**828,829**	790,500
Cash	**1,635**	1,590
Investment income due and accrued	**6,118**	6,077
Premiums and insurance balances receivable, net of allowance (2007 – $776; 2006 – $756)	**20,147**	17,789
Reinsurance assets, net of allowance (2007 – $521; 2006 – $536)	**23,541**	23,355
Deferred policy acquisition costs	**39,694**	37,235
Investments in partially owned companies	**1,176**	1,101
Real estate and other fixed assets, net of accumulated depreciation (2007 – $5,616; 2006 – $5,525)	**5,060**	4,381
Separate and variable accounts	**78,618**	72,655
Goodwill	**8,590**	8,628
Other assets	**20,458**	16,103
Total assets	**$1,033,866**	$979,414

See Accompanying Notes to Consolidated Financial Statements.

CONSOLIDATED BALANCE SHEET *(continued)*

(in millions, except share data) (unaudited)

	June 30, 2007	December 31, 2006
Liabilities:		
Reserve for losses and loss expenses	**$ 82,079**	$ 79,999
Unearned premiums	**28,019**	26,271
Future policy benefits for life and accident and health insurance contracts	**126,584**	122,230
Policyholders' contract deposits	**247,526**	246,615
Other policyholders' funds	**8,562**	8,281
Commissions, expenses and taxes payable	**6,144**	5,305
Insurance balances payable	**5,765**	3,789
Funds held by companies under reinsurance treaties	**2,407**	2,602
Income taxes payable	**8,996**	9,546
Financial services liabilities:		
Borrowings under obligations of guaranteed investment agreements	**19,451**	20,664
Securities sold under agreements to repurchase, at contract value	**19,459**	19,677
Trade payables	**8,324**	6,174
Hybrid financial instrument liabilities, at fair value	**8,155**	8,856
Securities and spot commodities sold but not yet purchased, at market value	**4,297**	4,076
Unrealized loss on swaps, options and forward transactions	**12,841**	11,401
Trust deposits and deposits due to banks and other depositors	**4,290**	5,249
Commercial paper	**10,057**	8,208
Notes, bonds, loans and mortgages payable	**93,998**	87,602
Commercial paper	**4,468**	4,821
Notes, bonds, loans and mortgages payable	**23,156**	17,088
Junior subordinated debt	**4,585**	–
Liabilities connected to trust preferred stock	**1,440**	1,440
Separate and variable accounts	**78,618**	72,655
Securities lending payable	**82,219**	70,198
Minority interest	**9,290**	7,778
Other liabilities (includes hybrid financial instruments: 2007 – $208; 2006 – $111)	**28,706**	27,021
Total liabilities	**929,436**	877,546
Preferred shareholders' equity in subsidiary companies	**100**	191
Commitments and Contingent Liabilities (See Note 6)		
Shareholders' equity:		
Common stock, $2.50 par value; 5,000,000,000 shares authorized; shares issued 2007 and 2006 – 2,751,327,476	**6,878**	6,878
Additional paid-in capital	**2,708**	2,590
Payments advanced to purchase shares	**(2,336)**	–
Retained earnings	**92,251**	84,996
Accumulated other comprehensive income (loss)	**8,187**	9,110
Treasury stock, at cost; 2007 – 171,309,237; 2006 – 150,131,273 shares of common stock	**(3,358)**	(1,897)
Total shareholders' equity	**104,330**	101,677
Total liabilities, preferred shareholders' equity in subsidiary companies and shareholders' equity	**$1,033,866**	$979,414

See Accompanying Notes to Consolidated Financial Statements.

CONSOLIDATED STATEMENT OF INCOME

(in millions, except per share data) (unaudited)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2007	2006	**2007**	2006
Revenues:				
Premiums and other considerations	**$19,533**	$18,326	**$39,175**	$36,596
Net investment income	**7,853**	6,145	**14,977**	12,116
Net realized capital gains (losses)	**(28)**	(214)	**(98)**	(45)
Other income	**3,792**	2,597	**7,741**	5,465
Total revenues	**31,150**	26,854	**61,795**	54,132
Benefits and expenses:				
Incurred policy losses and benefits	**16,221**	14,066	**32,367**	29,155
Insurance acquisition and other operating expenses	**8,601**	7,547	**16,928**	14,943
Total benefits and expenses	**24,822**	21,613	**49,295**	44,098
Income before income taxes, minority interest and cumulative effect of an accounting change	**6,328**	5,241	**12,500**	10,034
Income taxes	**1,679**	1,688	**3,405**	3,123
Income before minority interest and cumulative effect of an accounting change	**4,649**	3,553	**9,095**	6,911
Minority interest	**(372)**	(363)	**(688)**	(560)
Income before cumulative effect of an accounting change	**4,277**	3,190	**8,407**	6,351
Cumulative effect of an accounting change, net of tax	**–**	–	**–**	34
Net income	**$ 4,277**	$ 3,190	**$ 8,407**	$ 6,385
Earnings per common share:				
Basic				
Income before cumulative effect of an accounting change	**$ 1.64**	$ 1.23	**$ 3.22**	$ 2.44
Cumulative effect of an accounting change, net of tax	**–**	–	**–**	0.01
Net income	**$ 1.64**	$ 1.23	**$ 3.22**	$ 2.45
Diluted				
Income before cumulative effect of an accounting change	**$ 1.64**	$ 1.21	**$ 3.21**	$ 2.42
Cumulative effect of an accounting change, net of tax	**–**	–	**–**	0.01
Net income	**$ 1.64**	$ 1.21	**$ 3.21**	$ 2.43
Dividends declared per common share	**$ 0.200**	$ 0.165	**$ 0.365**	$ 0.315
Average shares outstanding:				
Basic	**2,602**	2,606	**2,607**	2,606
Diluted	**2,613**	2,625	**2,621**	2,624

See Accompanying Notes to Consolidated Financial Statements.

CONSOLIDATED STATEMENT OF CASH FLOWS

(in millions) (unaudited)

	Six Months Ended June 30,	
	2007	2006
Summary:		
Net cash provided by operating activities	**$ 15,071**	$ 5,265
Net cash used in investing activities	**(37,873)**	(33,930)
Net cash provided by financing activities	**22,866**	28,861
Effect of exchange rate changes on cash	**(19)**	47
Change in cash	**45**	243
Cash at beginning of period	**1,590**	1,897
Cash at end of period	**$ 1,635**	$ 2,140
Cash flows from operating activities:		
Net income	**$ 8,407**	$ 6,385
Adjustments to reconcile net income to net cash provided by operating activities:		
Noncash revenues, expenses, gains and losses included in income:		
Net gains on sales of securities available for sale and other assets	**(732)**	(226)
Foreign exchange transaction (gains) losses	**639**	915
Net unrealized (gains) losses on non-AIGFP derivative assets and liabilities	**(123)**	(770)
Equity in income of partially owned companies and other invested assets	**(2,747)**	(1,410)
Amortization of deferred policy acquisition costs	**5,976**	5,607
Amortization of premium and discount on securities	**41**	39
Depreciation expenses, principally flight equipment	**1,337**	1,137
Provision for finance receivable losses	**229**	245
Impairment losses	**884**	596
Changes in operating assets and liabilities:		
General and life insurance reserves	**8,202**	7,290
Premiums and insurance balances receivable and payable – net	**(941)**	(1,229)
Reinsurance assets	**434**	707
Capitalization of deferred policy acquisition costs	**(7,678)**	(8,346)
Investment income due and accrued	**(46)**	(5)
Funds held under reinsurance treaties	**(210)**	(953)
Other policyholders' funds	**339**	(233)
Income taxes payable	**(225)**	885
Commissions, expenses and taxes payable	**724**	291
Other assets and liabilities – net	**832**	(1,475)
Bonds, common and preferred stocks trading, at fair value	**(2,962)**	(2,921)
Trade receivables and payables – net	**(925)**	20
Trading securities, at fair value	**465**	1,334
Spot commodities	**127**	(705)
Net unrealized (gain) loss on swaps, options and forward transactions	**1,317**	(425)
Securities purchased under agreements to resell	**258**	1,174
Securities sold under agreements to repurchase	**(226)**	(4,390)
Securities and spot commodities sold but not yet purchased, at market value	**221**	(248)
Finance receivables held for sale – originations and purchases	**(3,652)**	(4,911)
Sales of finance receivables – held for sale	**4,168**	5,250
Other, net	**938**	1,637
Total adjustments	**6,664**	(1,120)
Net cash provided by operating activities	**$ 15,071**	$ 5,265

See Accompanying Notes to Consolidated Financial Statements.

CONSOLIDATED STATEMENT OF CASH FLOWS *(continued)*

(in millions) (unaudited)

	Six Months Ended June 30,	
	2007	2006
Cash flows from investing activities:		
Proceeds from (payments for)		
Sales and maturities of fixed maturity securities available for sale	**$ 64,754**	$ 60,229
Sales of equity securities available for sale	**4,187**	7,231
Proceeds from fixed maturity securities held to maturity	**133**	313
Sales of flight equipment	**28**	256
Sales or distributions of other invested assets	**6,185**	8,021
Payments received on mortgage, policy, collateral and guaranteed loans	**2,047**	1,876
Principal payments received on finance receivables held for investment	**6,430**	6,297
Purchases of fixed maturity securities available for sale	**(73,274)**	(69,849)
Purchases of equity securities available for sale	**(5,852)**	(8,178)
Purchases of fixed maturity securities held to maturity	**(129)**	(323)
Purchases of flight equipment	**(3,883)**	(4,171)
Purchases of other invested assets	**(10,688)**	(8,118)
Acquisitions of new businesses, net of cash acquired	**(655)**	—
Mortgage, policy, collateral and guaranteed loans issued	**(4,408)**	(4,420)
Finance receivables held for investment – originations and purchases	**(7,387)**	(7,053)
Change in securities lending collateral	**(11,772)**	(9,261)
Net additions to real estate, fixed assets, and other assets	**(466)**	(388)
Net change in short-term investments	**(3,023)**	(6,529)
Net change in non-AIGFP derivative assets and liabilities	**(100)**	137
Net cash used in investing activities	**$ (37,873)**	$ (33,930)
Cash flows from financing activities:		
Proceeds from (payments for)		
Policyholders' contract deposits	**$ 28,774**	$ 25,119
Policyholders' contract withdrawals	**(28,189)**	(20,440)
Change in other deposits	**(1,271)**	313
Change in commercial paper	**1,424**	2,971
Notes, bonds, loans and mortgages payable, and hybrid financial instrument liabilities issued	**40,931**	22,333
Repayments on notes, bonds, loans and mortgages payable, and hybrid financial instrument liabilities	**(30,282)**	(10,481)
Issuance of junior subordinated debt	**4,490**	—
Issuance of guaranteed investment agreements	**4,186**	6,841
Maturities of guaranteed investment agreements	**(4,655)**	(6,469)
Change in securities lending payable	**12,021**	9,345
Issuance of treasury stock	**180**	63
Payments advanced to purchase shares	**(4,000)**	—
Acquisition of treasury stock	**(16)**	(4)
Cash dividends paid to shareholders	**(859)**	(780)
Other, net	**132**	50
Net cash provided by financing activities	**$ 22,866**	$ 28,861
Supplementary disclosure of cash flow information:		
Cash paid during the period for:		
Interest	**$ 3,744**	$ 2,805
Taxes	**$ 3,524**	$ 2,100
Non-cash financing activities:		
Interest credited to policyholder accounts	**$ 5,932**	$ 4,653
Treasury stock acquired using payments advanced to purchase shares	**$ 1,664**	—
Non-cash investing activities:		
Debt assumed on acquisitions	**$ 1,654**	$ —

See Accompanying Notes to Consolidated Financial Statements.

CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME (LOSS)

(in millions) (unaudited)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2007	2006	**2007**	2006
Net income	**$ 4,277**	$ 3,190	**$ 8,407**	$ 6,385
Other comprehensive income (loss):				
Unrealized (depreciation) appreciation of investments – net of reclassification adjustments	**(2,161)**	(5,734)	**(852)**	(8,333)
Deferred income tax benefit (expense) on above changes	**598**	1,743	**140**	2,843
Foreign currency translation adjustments	**(164)**	520	**(329)**	1,070
Deferred income tax benefit (expense) on above changes	**7**	(59)	**35**	(349)
Net derivative gains arising from cash flow hedging activities – net of reclassification adjustments	**61**	4	**62**	8
Deferred income tax benefit (expense) on above changes	**(22)**	(16)	**5**	(3)
Change in pension and postretirement unrecognized periodic benefit (cost)	**15**	—	**18**	(3)
Deferred income tax benefit (expense) on above changes	**(1)**	34	**(2)**	1
Other comprehensive income (loss)	**(1,667)**	(3,508)	**(923)**	(4,766)
Comprehensive income (loss)	**$ 2,610**	$ (318)	**$ 7,484**	$ 1,619

See Accompanying Notes to Consolidated Financial Statements.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited)*

1. Summary of Significant Accounting Policies

Basis of Presentation

These unaudited condensed consolidated financial statements do not include certain financial information required by U.S. generally accepted accounting principles (GAAP) for complete financial statements and should be read in conjunction with the audited consolidated financial statements and the related notes included in the Annual Report on Form 10-K of American International Group, Inc. (AIG) for the year ended December 31, 2006 (2006 Annual Report on Form 10-K).

In the opinion of management, these consolidated financial statements contain the normal recurring adjustments necessary for a fair statement of the results presented herein. All material intercompany accounts and transactions have been eliminated.

Certain reclassifications and format changes have been made to prior period amounts to conform to the current period presentation.

Out of period adjustments

During the three and six-month periods ended June 30, 2007, AIG recorded the effects of certain out of period adjustments which reduced net income by $139 million and $373 million, respectively, and diluted earnings per share by $0.05 per share and $0.14 per share, respectively.

During the three and six-month periods ended June 30, 2006, AIG recorded the effects of certain out of period adjustments which increased (decreased) net income by $279 million and $(67) million, respectively, and diluted earnings per share by $0.11 per share and $(0.03) per share, respectively.

Recent Accounting Standards

Accounting Changes

SOP 05-1

On September 19, 2005, the American Institute of Certified Public Accountants (AICPA) issued Statement of Position 05-1, "Accounting by Insurance Enterprises for Deferred Acquisition Costs in Connection with Modifications or Exchanges of Insurance Contracts" (SOP 05-1). SOP 05-1 provides guidance on accounting for internal replacements of insurance and investment contracts other than those specifically described in Statement of Financial Accounting Standards (FAS) No. 97, "Accounting and Reporting by Insurance Enterprises for Certain Long-Duration Contracts and for Realized Gains and Losses from the Sale of Investments" (FAS 97). SOP 05-1 defines an internal replacement as a modification in product benefits, features, rights, or coverage that occurs by the exchange of a contract for a new contract, or by amendment, endorsement, or rider to a contract, or by the election of a feature or coverage within a contract. Internal replacements that result in a substantially changed contract are accounted for as a termination and a replacement contract.

The provisions of SOP 05-1 became effective as of January 1, 2007. On the date of adoption, AIG recorded a cumulative effect reduction of $82 million, net of tax, to the opening balance of retained earnings to reflect changes in unamortized deferred policy acquisition costs (DAC), value of business acquired, deferred sales inducement assets, unearned revenue liabilities and future policy benefits for life and accident and health insurance contracts. This adjustment primarily reflects a shorter expected life related to certain group life and health insurance contracts and the effect on the gross profits of investment-oriented products related to previously anticipated future internal replacements. This cumulative effect adjustment affected only the Life Insurance & Retirement Services segment.

FIN 48

On July 13, 2006, the Financial Accounting Standards Board (FASB) issued FASB Interpretation No. 48, "Accounting for Uncertainty in Income Taxes – an interpretation of FASB Statement No. 109" (FIN 48), which clarifies the accounting for uncertainty in income tax positions. FIN 48 prescribes a recognition threshold and measurement attribute for the financial statement recognition and measurement of an income tax position taken or expected to be taken in a tax return. FIN 48 also provides guidance on derecognition, classification, interest and penalties, accounting in interim periods, and additional disclosures. AIG adopted the provisions of FIN 48 on January 1, 2007. As a result of the adoption of FIN 48, AIG recognized a $71 million increase in the liability for unrecognized tax benefits, which was accounted for as a decrease to opening retained earnings as of January 1, 2007.

As of the date of adoption and after recognizing the effect of the increase in the liability noted above, the total amount of AIG's unrecognized tax benefit, excluding interest and penalties, was $1.138 billion. Included in this balance are $407 million related to tax positions the disallowance of which would not affect the annual effective income tax rate. Accordingly, the amount of unrecognized tax benefit that, if recognized, would favorably affect the effective tax rate is $731 million.

At June 30, 2007, AIG's unrecognized tax benefit, excluding interest and penalties, was $1.274 billion which includes $577 million related to tax positions the disallowance of which would not affect the annual effective income tax rate. Accordingly, the amount of unrecognized tax benefit

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

1. Summary of Significant Accounting Policies *(continued)*

that, if recognized, would favorably affect the effective tax rate was $697 million.

Interest and penalties related to unrecognized tax benefits are recognized in income tax expense. At January 1, 2007 and June 30, 2007, AIG had accrued $176 million and $203 million, respectively, for the payment of interest (net of the federal benefit) and penalties.

Neither reserves for uncertain tax positions attributable to prior restatements (including various other remediation-related adjustments) nor the corresponding interest income have been recognized because such amounts are not currently estimable. In addition, certain tax benefits from compensation deductions have not been recognized because of existing uncertainty with respect to the documentation supporting these tax benefits.

AIG continually evaluates proposed adjustments by taxing authorities. At June 30, 2007, such proposed adjustments would not result in a material change to AIG's consolidated financial condition. However, AIG believes that it is reasonably possible that the balance of the unrecognized tax benefits could decrease by $0 to $150 million by the end of 2007 due to settlements or expiration of statutes.

Listed below are the tax years that remain subject to examination by major tax jurisdiction:

Major Tax Jurisdictions	Open Tax Years
United States	1991-2006
Hong Kong	1997-2006
Malaysia	1999-2006
Singapore	1993-2006
Thailand	2001-2006
Taiwan	2000-2006
Japan	2000-2006
United Kingdom	2003-2006
France	2003-2006
Korea	2001-2006

FSP 13-2

On July 13, 2006, the FASB issued FASB Staff Position (FSP) No. 13-2, "Accounting for a Change or Projected Change in the Timing of Cash Flows Relating to Income Taxes Generated by a Leveraged Lease Transaction" (FSP 13-2). FSP 13-2 addresses how a change or projected change in the timing of cash flows relating to income taxes generated by a leveraged lease transaction affects the accounting for the lease by the lessor, and directs that the tax assumptions be consistent with any FIN 48 uncertain tax position related to the lease. FSP 13-2 is effective for fiscal years beginning after December 15, 2006. Upon adoption, AIG recorded at January 1, 2007, a $50 million decrease in the opening balance of retained earnings, net of tax, as of January 1, 2007 to reflect the cumulative effect of this change in accounting. The adoption of this guidance is not expected to have a material effect on the Company's results of operations in 2007.

As a result of the adoptions of SOP 05-1, FIN 48 and FSP 13-2, AIG recorded a total decrease to opening retained earnings of $203 million as of January 1, 2007.

Future Application of Accounting Standards

FAS 157

In September 2006, the FASB issued FAS No. 157, "Fair Value Measurements" (FAS 157). FAS 157 defines fair value, establishes a framework for measuring fair value and expands disclosure requirements regarding fair value measurements. FAS 157 will be effective January 1, 2008. AIG is currently assessing the effect of implementing this guidance.

FAS 159

In February 2007, the FASB issued FAS No. 159, "The Fair Value Option for Financial Assets and Financial Liabilities" (FAS 159). FAS 159 permits entities to choose to measure at fair value many financial instruments and certain other items that are not currently required to be measured at fair value. Subsequent changes in fair value for designated items will be required to be reported in earnings in the current period. FAS 159 also establishes presentation and disclosure requirements for similar types of assets and liabilities measured at fair value. FAS 159 will be effective January 1, 2008. AIG is currently assessing the effect of implementing this guidance, which depends on the nature and extent of items elected to be measured at fair value upon initial application of the standard on January 1, 2008.

SOP 07-1

In June 2007, the AICPA issued Statement of Position No. 07-1 (SOP 07-1), "Clarification of the Scope of the Audit and Accounting Guide 'Audits of Investment Companies' and Accounting by Parent Companies and Equity Method Investors for Investments in Investment Companies." SOP 07-1 amends the guidance for whether an entity may apply the provisions of the Audit and Accounting Guide, "Audits of Investment Companies" (the Guide). Investment companies that are subject to the Guide must report all investments at fair value regardless of the nature of the investment or the level of ownership. SOP 07-1 also establishes new requirements for whether a parent company can retain specialized investment company accounting in its consolidated financial statements for subsidiaries and equity method investees that are covered by the Guide. SOP 07-1 will be effective on January 1, 2008. AIG is currently assessing the effect of implementing this guidance.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

2. Segment Information

AIG identifies its reportable segments by product line consistent with its management structure. These segments are General Insurance, Life Insurance & Retirement Services, Financial Services and Asset Management.

In order to better align financial reporting with the manner in which AIG's chief operating decision makers have managed their businesses, commencing in the first quarter of 2007, AIG realigned certain products among reportable segments and major internal reporting units. AIG also began reporting net realized capital gains and losses for the Financial Services and Asset Management segments in the results of these segments. Historically, net realized capital gains and losses were included in the Other category. There has been no change in AIG's management structure or in its reportable segments. All prior period amounts presented in the tables below have been revised to conform to the current year's presentation of these items.

The following table summarizes AIG's operations by major operating segment:

Operating Segments *(in millions)*	Three Months Ended June 30, **2007**	2006	Six Months Ended June 30, **2007**	2006
Revenues[a]:				
General Insurance[b][c]	**$12,928**	$12,167	**$25,831**	$23,823
Life Insurance & Retirement Services[c][d]	**14,023**	11,911	**27,705**	24,761
Financial Services[e][f]	**2,123**	1,246	**4,324**	2,912
Asset Management[g]	**1,989**	1,515	**3,897**	2,654
Other	**263**	138	**394**	228
Consolidation and eliminations	**(176)**	(123)	**(356)**	(246)
Consolidated	**$31,150**	$26,854	**$61,795**	$54,132
Operating income (loss)[a][h]:				
General Insurance[c]	**$ 2,976**	$ 2,863	**$ 6,072**	$ 5,194
Life Insurance & Retirement Services[c]	**2,620**	2,381	**4,901**	5,011
Financial Services[f]	**47**	(530)	**339**	(638)
Asset Management	**1,128**	785	**2,122**	1,234
Other[i]	**(460)**	(258)	**(930)**	(767)
Consolidation and eliminations	**17**	–	**(4)**	–
Consolidated	**$ 6,328**	$ 5,241	**$12,500**	$10,034

(a) Includes gains (losses) from hedging activities that did not qualify for hedge accounting treatment under FAS No. 133, "Accounting for Derivative Instruments and Hedging Activities" (FAS 133), including the related foreign exchange gains and losses. For the three-month periods ended June 30, 2007 and 2006, respectively, the effect was $(430) million and $(1.08) billion in both revenues and operating income. For the six-month periods ended June 30, 2007 and 2006, respectively, the effect was $(882) million and $(1.30) billion in both revenues and operating income. These amounts result primarily from interest rate and foreign currency derivatives that are hedging investments and borrowings. These gains (losses) for the three and six months ended June 30, 2007 include out of period charges of $431 million and $326 million, respectively, including a $380 million charge in both periods to reverse net gains recognized on transfers of available for sale securities among legal entities consolidated within AIG Financial Products Corp. and AIG Trading Group Inc. and their respective subsidiaries (collectively, AIGFP). The first six months of 2006 include an out of period charge of $300 million related to the remediation of the material weakness in accounting for certain derivative transactions under FAS 133.

(b) Represents the sum of General Insurance net premiums earned, net investment income and net realized capital gains (losses).

(c) Includes the effect of an out of period adjustment in the second quarter of 2006 related to the accounting for certain interests in unit investment trusts (UCITS). For the three and six-month periods ended June 30, 2006, the effect was an increase of $432 million and $405 million, respectively, in both revenues and operating income for General Insurance and an increase of $221 million and $203 million, respectively, in revenues and $144 million and $132 million, respectively, in operating income for Life Insurance & Retirement Services.

(d) Represents the sum of Life Insurance & Retirement Services premiums and other considerations, net investment income and net realized capital gains (losses). Included in net realized capital gains (losses) and operating income are gains (losses) from hedging activities that did not qualify for hedge accounting treatment under FAS 133, which were $41 million and $73 million for the three-month periods ended June 30, 2007 and 2006, respectively, and $(82) million and $425 million for the six-month periods ended June 30, 2007 and 2006, respectively. Also included in net realized capital gains (losses) was the application of FAS No. 52 "Foreign Currency Translation" (FAS 52), the effects of which were $(24) million and $(94) million for the three-month periods ended June 30, 2007 and 2006, respectively, and $99 million and $(90) million for the six-month periods ended June 30, 2007 and 2006, respectively.

(e) Primarily represents interest, lease and finance charges.

(f) Includes gains (losses) from hedging activities that did not qualify for hedge accounting treatment under FAS 133, including the related foreign exchange gains and losses. For the three-month periods ended June 30, 2007 and 2006, respectively, the effect was $(443) million, and $(1.1) billion in both revenues and operating income. For the six-month periods ended June 30, 2007 and 2006, respectively, the effect was $(603) million and $(1.8) billion in both revenues and operating income. These amounts result primarily from interest rate and foreign currency derivatives that are effective economic hedges of investments and borrowings. The second quarter and the first six months of 2007 include the out of period charges of $431 million and $326 million, respectively, as discussed above. The first six months of 2006 include an out of period charge of $300 million as discussed above. In the first quarter of 2007, AIG began applying hedge accounting for certain transactions, primarily in its Capital Markets operations. In the second quarter of 2007, American General Finance, Inc. (AGF) and International Lease Finance Corporation (ILFC) began applying hedge accounting to most of their derivatives hedging interest rate and foreign exchange risks associated with their floating rate and foreign currency denominated borrowings.

(g) Represents net investment income with respect to spread-based products and management and advisory fees.

(h) Represents income before income taxes, minority interest and cumulative effect of an accounting change.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

2. Segment Information *(continued)*

(i) Includes AIG parent and other operations which are not required to be reported separately. The following table presents the operating loss for AIG's Other category:

(in millions)	Three Months Ended June 30, 2007	Three Months Ended June 30, 2006	Six Months Ended June 30, 2007	Six Months Ended June 30, 2006
Other operating income (loss):				
Equity earnings in unconsolidated entities	**$ 50**	$ 111	**$ 91**	$ 130
Interest expense	**(302)**	(223)	**(554)**	(406)
Unallocated corporate expenses	**(200)**	(64)	**(362)**	(248)
Compensation expense — SICO Plans	**(10)**	(14)	**(20)**	(90)
Compensation expense — Starr tender offer	**—**	—	**—**	(54)
Net realized capital gains (losses)	**22**	(49)	**(27)**	(54)
Other miscellaneous, net	**(20)**	(19)	**(58)**	(45)
Total Other	**$(460)**	$(258)	**$(930)**	$(767)

The following table summarizes AIG's General Insurance operations by major internal reporting unit:

General Insurance *(in millions)*	Three Months Ended June 30, 2007	Three Months Ended June 30, 2006	Six Months Ended June 30, 2007	Six Months Ended June 30, 2006
Revenues:				
Domestic Brokerage Group	**$ 6,904**	$ 6,587	**$13,995**	$13,148
Transatlantic	**1,069**	1,015	**2,165**	2,031
Personal Lines	**1,223**	1,223	**2,436**	2,438
Mortgage Guaranty	**257**	212	**505**	410
Foreign General[(a)]	**3,475**	3,130	**6,737**	5,794
Reclassifications and eliminations	**–**	–	**(7)**	2
Total General Insurance	**$12,928**	$12,167	**$25,831**	$23,823
Operating Income (loss)[(b)]:				
Domestic Brokerage Group	**$ 1,904**	$ 1,474	**$ 3,833**	$ 2,779
Transatlantic	**168**	143	**319**	284
Personal Lines	**118**	118	**224**	219
Mortgage Guaranty	**(81)**	107	**(73)**	216
Foreign General[(a)(c)]	**867**	1,021	**1,776**	1,694
Reclassifications and eliminations	**–**	–	**(7)**	2
Total General Insurance	**$ 2,976**	$ 2,863	**$ 6,072**	$ 5,194

(a) The three and six-month periods ended June 30, 2006, include the effect of an out of period UCITS adjustment in the second quarter of 2006 which was an increase of $412 million and $386 million, respectively, in both revenues and operating income.

(b) Includes additional losses incurred and net reinstatement premiums related to prior year catastrophes of $18 million and $(51) million for the three-month periods ended June 30, 2007 and 2006, respectively. Such losses and premiums were $53 million and $48 million for the six-month periods ended June 30, 2007 and 2006, respectively.

(c) Includes losses incurred and net reinstatement premiums related to current year catastrophes of $68 million in both the three and six-month periods ended June 30, 2007.

The following table summarizes AIG's Life Insurance & Retirement Services operations by major internal reporting unit:

Life Insurance & Retirement Services *(in millions)*	Three Months Ended June 30, 2007	Three Months Ended June 30, 2006	Six Months Ended June 30, 2007	Six Months Ended June 30, 2006
Revenues:				
Foreign:				
Japan and Other	**$ 4,863**	$ 3,812	**$ 9,633**	$ 8,076
Asia*	**5,019**	4,303	**9,510**	8,763
Domestic:				
Domestic Life Insurance	**2,359**	2,222	**4,880**	4,589
Domestic Retirement Services	**1,782**	1,574	**3,682**	3,333
Total Life Insurance & Retirement Services	**$14,023**	$11,911	**$27,705**	$24,761
Operating Income:				
Foreign:				
Japan and Other	**$ 810**	$ 975	**$ 1,723**	$ 1,953
Asia*	**844**	764	**1,215**	1,472
Domestic:				
Domestic Life Insurance	**368**	235	**713**	601
Domestic Retirement Services	**598**	407	**1,250**	985
Total Life Insurance & Retirement Services	**$ 2,620**	$ 2,381	**$ 4,901**	$ 5,011

* *Includes the effect of an out of period UCITS adjustment in the second quarter of 2006. For the three and six-month periods ended June 30, 2006, the effect was an increase of $221 million and $203 million, respectively, in revenues and $144 million and $132 million, respectively, in operating income.*

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

2. Segment Information *(continued)*

The following table summarizes AIG's Financial Services operations by major internal reporting unit:

Financial Services *(in millions)*	Three Months Ended June 30, **2007**	2006	Six Months Ended June 30, **2007**	2006
Revenues:				
Aircraft Leasing[(a)]	**$1,173**	$1,051	**$2,231**	$ 2,063
Capital Markets[(b)(c)]	**(67)**	(788)	**161**	(1,088)
Consumer Finance[(d)(e)]	**949**	942	**1,832**	1,867
Other, including intercompany adjustments	**68**	41	**100**	70
Total Financial Services	**$2,123**	$1,246	**$4,324**	$ 2,912
Operating income (loss):				
Aircraft Leasing[(a)]	**$ 207**	$ 198	**$ 371**	$ 374
Capital Markets[(b)(c)]	**(255)**	(952)	**(187)**	(1,422)
Consumer Finance[(d)(e)]	**75**	202	**111**	378
Other, including intercompany adjustments	**20**	22	**44**	32
Total Financial Services	**$ 47**	$ (530)	**$ 339**	$ (638)

(a) Revenues are primarily aircraft lease rentals from ILFC. Both revenues and operating income include gains (losses) from hedging activities that did not qualify for hedge accounting treatment under FAS 133, including the related foreign exchange gains and losses. For the three-month periods ended June 30, 2007 and 2006, the effect was $24 million and $10 million, respectively. For the six-month periods ended June 30, 2007 and 2006, the effect was $(13) million and $55 million, respectively. These amounts result primarily from interest rate and foreign currency derivatives that are effective economic hedges of borrowings. In the second quarter of 2007, ILFC began applying hedge accounting to most of its derivatives hedging interest rate and foreign exchange risks associated with its floating rate and foreign currency denominated borrowings.

(b) Revenues, shown net of interest expense of $805 million and $633 million for the three-month periods ended June 30, 2007 and 2006, respectively, and $1.9 billion and $1.3 billion for the six-month periods ended June 30, 2007 and 2006, respectively, were primarily from hedged financial positions entered into in connection with counterparty transactions. Both revenues and operating income include gains (losses) from hedging activities that did not qualify for hedge accounting treatment under FAS 133, including the related foreign exchange gains and losses. For the three-month periods ended June 30, 2007 and 2006, the effect was $(528) million and $(1.2) billion, respectively. For the six-month periods ended June 30, 2007 and 2006, the effect was $(613) million and $(1.8) billion, respectively. The second quarter and the first six months of 2007 include out of period charges of $431 million and $326 million, respectively, including a $380 million charge in both periods to reverse net gains recognized on transfers of available for sale securities among legal entities consolidated within AIGFP. The first six months of 2006 include an out of period charge of $300 million related to the remediation of the material weakness in accounting for certain derivative transactions under FAS 133. In the first quarter of 2007, AIGFP began applying hedge accounting for certain transactions.

(c) Certain transactions entered into by AIGFP generate tax credits and benefits which are included in income taxes in the consolidated statement of income. The amounts of such tax credits and benefits for the three-month periods ended June 30, 2007 and 2006 were $18 million and $8 million, respectively. The amounts of such tax credits and benefits for the six-month periods ended June 30, 2007 and 2006 were $35 million and $26 million, respectively.

(d) Revenues are primarily finance charges. Both revenues and operating income include gains (losses) from hedging activities that did not qualify for hedge accounting treatment under FAS 133, including the related foreign exchange gains and losses. For the three-month periods ended June 30, 2007 and 2006, the effect was $20 million and $5 million, respectively. For the six-month periods ended June 30, 2007 and 2006, the effect was $(15) million and $8 million, respectively. These amounts result primarily from interest rate and foreign currency derivatives that are effective economic hedges of borrowings. In the second quarter of 2007, AGF began applying hedge accounting to most of its derivatives hedging interest rate and foreign exchange risks associated with its floating rate and foreign currency denominated borrowings.

(e) The three-month and six-month periods ended June 30, 2007 included pre-tax charges of $50 million and $178 million, respectively, in connection with domestic consumer finance's mortgage banking activities.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

3. Shareholders' Equity and Earnings Per Share

Earnings Per Share (EPS)

Basic EPS of AIG is calculated using the weighted average number of common shares outstanding. Diluted EPS is based on those shares used in basic EPS plus shares that would have been outstanding assuming issuance of common shares for all potentially dilutive common shares outstanding.

The following table presents the computation of basic and diluted EPS:

	Three Months Ended June 30,		Six Months Ended June 30,	
(in millions, except per share data)	**2007**	2006	**2007**	2006
Numerator for earnings per share:				
Income before cumulative effect of an accounting change	**$4,277**	$3,190	**$8,407**	$6,351
Cumulative effect of an accounting change, net of tax	**–**	–	**–**	34
Net income applicable to common stock for basic EPS	**$4,277**	$3,190	**$8,407**	$6,385
Interest on contingently convertible bonds, net of tax[(a)]	**–**	3	**–**	6
Net income applicable to common stock for diluted EPS	**$4,277**	$3,193	**$8,407**	$6,391
Cumulative effect of an accounting change, net of tax	**–**	–	**–**	(34)
Income before cumulative effect of an accounting change applicable to common stock for diluted EPS	**$4,277**	$3,193	**$8,407**	$6,357
Denominator for earnings per share:				
Weighted average shares outstanding used in the computation of EPS:				
Common stock issued	**2,751**	2,751	**2,751**	2,751
Common stock in treasury	**(161)**	(153)	**(156)**	(153)
Deferred shares	**12**	8	**12**	8
Weighted average shares outstanding – basic	**2,602**	2,606	**2,607**	2,606
Incremental shares from potential common stock:				
Weighted average number of shares arising from outstanding employee stock plans (treasury stock method)[(b)]	**11**	10	**14**	9
Contingently convertible bonds[(a)]	**–**	9	**–**	9
Weighted average shares outstanding – diluted[(b)]	**2,613**	2,625	**2,621**	2,624
Earnings per share:				
Basic:				
Income before cumulative effect of an accounting change	**$ 1.64**	$ 1.23	**$ 3.22**	$ 2.44
Cumulative effect of an accounting change, net of tax	**–**	–	**–**	0.01
Net income	**$ 1.64**	$ 1.23	**$ 3.22**	$ 2.45
Diluted:				
Income before cumulative effect of an accounting change	**$ 1.64**	$ 1.21	**$ 3.21**	$ 2.42
Cumulative effect of an accounting change, net of tax	**–**	–	**–**	0.01
Net income	**$ 1.64**	$ 1.21	**$ 3.21**	$ 2.43

(a) Assumes conversion of contingently convertible bonds due to the adoption of Emerging Issues Task Force Issue No. 04-8 "Accounting Issues Related to Certain Features of Contingently Convertible Debt and the Effect on Diluted Earnings per Share."

(b) Certain shares arising from employee stock plans were not included in the computation of diluted earnings per share where the exercise price of the options exceeded the average market price for the period and would have been antidilutive. The number of shares excluded was 7 million and 15 million for the six-month periods ended June 30, 2007 and 2006, respectively.

Shareholders' Equity

From time to time, AIG may buy shares of its common stock for general corporate purposes, including to satisfy its obligations under various employee benefit plans. In February 2007, AIG's Board of Directors increased AIG's share repurchase program by authorizing the repurchase of shares with an aggregate purchase price of $8 billion. During March 2007, AIG entered into a $3 billion structured share repurchase arrangement, and in May 2007 AIG entered into an additional $1 billion structured share repurchase arrangement. A total of 24,491,961 shares were repurchased during the first six months of 2007. The portion of the payments advanced by AIG under the structured share repurchase arrangements that had not yet been utilized to repurchase shares at June 30, 2007, amounting to $2.34 billion, has been recorded as a component of shareholders' equity under the caption Payments advanced to purchase shares. Purchases have continued subsequent to June 30, 2007, with an additional 24,501,510 shares purchased from July 1 through August 6, 2007. All shares repurchased are recorded as treasury stock at cost.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

The quarterly dividend per common share, commencing with the dividend declared in May 2007 and payable on September 21, 2007, was $0.20.

The following table summarizes the changes in retained earnings during the first six months of 2007:

(in millions)	June 30, 2007
Retained earnings:	
Balance at beginning of year	$ 84,996
Cumulative effect of accounting changes, net of tax	(203)
Adjusted balance, beginning of year	84,793
Net income	8,407
Dividends to shareholders	(949)
Balance, end of period	$ 92,251

4. Benefits Provided by Starr International Company, Inc. and C.V. Starr & Co., Inc.

Starr International Company, Inc. (SICO) has provided a series of two-year Deferred Compensation Profit Participation Plans (SICO Plans) to certain AIG employees. The SICO Plans came into being in 1975 when the voting shareholders and Board of Directors of SICO, a private holding company whose principal asset is AIG common stock, decided that a portion of the capital value of SICO should be used to provide an incentive plan for the current and succeeding managements of all American International companies, including AIG.

None of the costs of the various benefits provided under the SICO Plans has been paid by AIG, although AIG has recorded a charge to reported earnings for the deferred compensation amounts paid to AIG employees by SICO, with an offsetting amount credited to additional paid-in capital reflecting amounts deemed contributed by SICO. The SICO Plans provide that shares currently owned by SICO are set aside by SICO for the benefit of the participant and distributed upon retirement. The SICO Board of Directors currently may permit an early payout of units under certain circumstances. Prior to payout, the participant is not entitled to vote, dispose of or receive dividends with respect to such shares, and shares are subject to forfeiture under certain conditions, including but not limited to the participant's voluntary termination of employment with AIG prior to normal retirement age. Under the SICO Plans, SICO's Board of Directors may elect to pay a participant cash in lieu of shares of AIG common stock. Following notification from SICO to participants in the SICO Plans that it will settle specific future awards under the SICO Plans with shares rather than cash, AIG modified its accounting for the SICO Plans from variable to fixed measurement accounting. AIG gave effect to this change in settlement method beginning on December 9, 2005, the date of SICO's notice to participants in the SICO Plans. See also Note 6(b) ''Commitments'' herein.

In January 2006, C.V. Starr & Co., Inc. (Starr) completed its tender offer to purchase Starr interests from AIG employees. In conjunction with AIG's adoption of FAS No. 123R ''Share-Based Payments'' (FAS 123R), Starr is considered to be an ''economic interest holder'' in AIG. As a result, compensation expense of $54 million was included in the first six months of 2006 with respect to the Starr tender offer.

Compensation expense with respect to the SICO Plans aggregated $10 million and $14 million for the three-month periods ended June 30, 2007 and 2006, respectively, and $20 million and $90 million for the six-month periods ended June 30, 2007 and 2006, respectively. Compensation expense for the first six months of 2006 included various out of period adjustments totaling $61 million, primarily relating to stock splits and other miscellaneous items for the SICO plans.

5. Ownership

According to the Schedule 13D filed on March 20, 2007 by Starr, SICO, Edward E. Matthews, Maurice R. Greenberg, the Maurice R. and Corinne P. Greenberg Family Foundation, Inc., the Universal Foundation, Inc., the Maurice R. and Corinne P. Greenberg Joint Tenancy Company, LLC and the C.V. Starr & Co., Inc. Trust, these reporting persons could be deemed to beneficially own 354,987,261 shares of AIG's common stock at that date. Based on the shares of AIG's common stock outstanding as of July 31, 2007, this ownership would represent approximately 14 percent of the voting stock of AIG. Although these reporting persons have made filings under Section 16 of the Securities Exchange Act of 1934 (Exchange Act), reporting sales of shares of common stock, no amendment to the Schedule 13D has been filed to report a change in ownership subsequent to March 20, 2007.

6. Commitments, Contingencies and Guarantees

In the normal course of business, various commitments and contingent liabilities are entered into by AIG and certain of its

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

6. Commitments, Contingencies and Guarantees *(continued)*

subsidiaries. In addition, AIG guarantees various obligations of certain subsidiaries.

(a) Litigation and Investigations

Litigation Arising from Operations. AIG and its subsidiaries, in common with the insurance and financial services industries in general, are subject to litigation, including claims for punitive damages, in the normal course of their business. In AIG's insurance operations, litigation arising from claims settlement activities is generally considered in the establishment of AIG's reserve for losses and loss expenses. However, in certain circumstances, AIG provides disclosure because of the size or nature of the potential liability to AIG. The potential for increasing jury awards and settlements makes it difficult to assess the ultimate outcome of such litigation.

Litigation Arising from Insurance Operations — Caremark. AIG and certain of its subsidiaries have been named defendants in two putative class actions in state court in Alabama that arise out of the 1999 settlement of class and derivative litigation involving Caremark Rx, Inc. (Caremark). The plaintiffs in the second-filed action have intervened in the first-filed action, and the second-filed action has been dismissed. An excess policy issued by a subsidiary of AIG with respect to the 1999 litigation was expressly stated to be without limit of liability. In the current actions, plaintiffs allege that the judge approving the 1999 settlement was misled as to the extent of available insurance coverage and would not have approved the settlement had he known of the existence and/or unlimited nature of the excess policy. They further allege that AIG, its subsidiaries, and Caremark are liable for fraud and suppression for misrepresenting and/or concealing the nature and extent of coverage. In their complaint, plaintiffs request compensatory damages for the 1999 class in the amount of $3.2 billion, plus punitive damages. AIG and its subsidiaries deny the allegations of fraud and suppression and have asserted, *inter alia*, that information concerning the excess policy was publicly disclosed months prior to the approval of the settlement. AIG and its subsidiaries further assert that the current claims are barred by the statute of limitations and that plaintiffs' assertions that the statute was tolled cannot stand against the public disclosure of the excess coverage. Plaintiffs, in turn, have asserted that the disclosure was insufficient to inform them of the nature of the coverage and did not start the running of the statute of limitations. The trial court is currently considering, under standards mandated by the Alabama Supreme Court, whether a class action can be certified and whether the defendants in the case brought by the intervenors should be dismissed. AIG cannot reasonably estimate either the likelihood of its prevailing in these actions or the potential damages in the event liability is determined.

Litigation Arising from Insurance Operations — Gunderson. A subsidiary of AIG has been named as a defendant in a putative class action lawsuit in the 14th Judicial District Court for the State of Louisiana. The *Gunderson* complaint alleges failure to comply with certain provisions of the Louisiana Any Willing Provider Act (the Act) relating to discounts taken by defendants on bills submitted by Louisiana medical providers and hospitals that provided treatment or services to workers compensation claimants and seeks monetary penalties and injunctive relief. On July 20, 2006, the court denied defendants' motion for summary judgment and granted plaintiffs' partial motion for summary judgment, holding that the AIG subsidiary was a "group purchaser" and, therefore, potentially subject to liability under the Act. On November 28, 2006, the court issued an order certifying a class of providers and hospitals. In an unrelated action also arising under the Act, a Louisiana appellate court ruled that the district court lacked jurisdiction to adjudicate the claims at issue. In response, defendants in *Gunderson* filed an exception for lack of subject matter jurisdiction. On January 19, 2007, the court denied the motion, holding that it has jurisdiction over the putative class claims. The AIG subsidiary is appealing the class certification ruling and is seeking an appeal from the jurisdictional ruling. While AIG believes that it has meritorious defenses to plaintiffs' claims, it cannot currently estimate the likelihood of prevailing in this action or reasonably estimate the likely damages, if any.

2006 Regulatory Settlements. In February 2006, AIG reached a resolution of claims and matters under investigation with the United States Department of Justice (DOJ), the Securities and Exchange Commission (SEC), the Office of the New York Attorney General (NYAG) and the New York State Department of Insurance (DOI). AIG recorded an after-tax charge of $1.15 billion relating to these settlements in the fourth quarter of 2005.

The settlements resolved investigations conducted by the SEC, NYAG and DOI in connection with the accounting, financial reporting and insurance brokerage practices of AIG and its subsidiaries, as well as claims relating to the underpayment of certain workers compensation premium taxes and other assessments. These settlements did not, however, resolve investigations by regulators from other states into insurance brokerage practices related to contingent commissions and other broker-related conduct, such as alleged bid rigging. Nor did the settlements resolve any obligations that AIG may have to state guarantee funds in connection with any of these matters.

As a result of these settlements, AIG made payments or placed amounts in escrow in 2006 totaling approximately

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

6. Commitments, Contingencies and Guarantees *(continued)*

$1.64 billion, $225 million of which represented fines and penalties. Amounts held in escrow totaling $341 million, including interest thereon, are included in other assets at June 30, 2007. At that date, approximately $322 million of the funds were escrowed for settlement of claims resulting from the underpayment by AIG of its residual market assessments for workers compensation. The National Workers Compensation Reinsurance Pool, on behalf of its participant members, has filed a lawsuit against AIG with respect to the underpayment of such assessments. The National Association of Insurance Commissioners has formed a Settlement Review Working Group directed by the State of Indiana, which has commenced its own investigation into the underreporting of workers compensation premium. In addition, similar lawsuits filed by the Attorney General of the State of Minnesota, the Minnesota Workers Compensation Reinsurance Association and the Minnesota Workers Compensation Insurers Association are pending. AIG cannot currently estimate whether the amount ultimately required to settle these claims will exceed the funds escrowed or otherwise accrued for this purpose.

The remaining escrowed funds, which amounted to $19 million at June 30, 2007, are set aside for settlements for certain specified AIG policyholders. During the first six months of 2007, approximately $366 million was paid out from escrow in exchange for releasing AIG and its subsidiaries from any alleged liability relating to, among other things, brokerage practices alleged in the NYAG settlement. Any funds remaining at the end of the escrow period can be used to resolve claims asserted by policyholders relating to such insurance brokerage practices, including those described in Private Litigation below.

In addition to the escrowed funds, $800 million was deposited into a fund under the supervision of the SEC as part of the settlements to be available to resolve claims asserted against AIG by investors, including the shareholder lawsuits described herein.

At the current time, AIG cannot predict the outcome of the matters described above, or estimate any potential additional cost related to these matters.

Also, as part of the settlements, AIG agreed to retain, for a period of three years, an independent consultant to conduct a review that will include, among other things, the adequacy of AIG's internal control over financial reporting, the policies, procedures and effectiveness of AIG's regulatory, compliance and legal functions and the remediation plan that AIG has implemented as a result of its own internal review.

Private Litigation

Securities Actions. Beginning in October 2004, a number of putative securities fraud class action suits were filed against AIG and consolidated as *In re American International Group, Inc. Securities Litigation*. Subsequently, a separate, though similar, securities fraud action was also brought against AIG by certain Florida pension funds. The lead plaintiff in the class action is a group of public retirement systems and pension funds benefiting Ohio state employees, suing on behalf of themselves and all purchasers of AIG's publicly traded securities between October 28, 1999 and April 1, 2005. The named defendants are AIG and a number of present and former AIG officers and directors, as well as Starr, SICO, General Reinsurance Corporation, and PricewaterhouseCoopers LLP (PwC), among others. The lead plaintiff alleges, among other things, that AIG: (1) concealed that it engaged in anti-competitive conduct through alleged payment of contingent commissions to brokers and participation in illegal bid-rigging; (2) concealed that it used "income smoothing" products and other techniques to inflate its earnings; (3) concealed that it marketed and sold "income smoothing" insurance products to other companies; and (4) misled investors about the scope of government investigations. In addition, the lead plaintiff alleges that AIG's former Chief Executive Officer manipulated AIG's stock price. The lead plaintiff asserts claims for violations of Sections 11 and 15 of the Securities Act of 1933, Section 10(b) of the Exchange Act, and Rule 10b-5 promulgated thereunder, Section 20(a) of the Exchange Act, and Section 20A of the Exchange Act. In April 2006, the court denied the defendants' motions to dismiss the second amended class action complaint and the Florida complaint. In December 2006, a third amended class action complaint was filed, which does not differ substantially from the prior complaint. Fact and class discovery is currently ongoing.

ERISA Action. Between November 30, 2004 and July 1, 2005, several Employee Retirement Income Security Act of 1974 (ERISA) actions were filed on behalf of purported class of participants and beneficiaries of three pension plans sponsored by AIG or its subsidiaries. A consolidated complaint filed on September 26, 2005 alleges a class period between September 30, 2000 and May 31, 2005 and names as defendants AIG, the members of AIG's Retirement Board and the Administrative Boards of the plans at issue, and four present or former members of AIG's Board of Directors. The factual allegations in the complaint are essentially identical to those in the securities actions described above. Plaintiffs allege that defendants violated duties under ERISA by allowing the plans to offer AIG stock as a permitted investment, when defendants allegedly knew it was not a prudent investment, and by failing to provide participants with accurate information about AIG stock. AIG's motion to dismiss was denied by

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

6. Commitments, Contingencies and Guarantees *(continued)*

order dated December 12, 2006. AIG filed an answer on February 12, 2007, denying plaintiffs' allegations of wrongdoing and asserting affirmative defenses to plaintiffs' claims. Discovery was consolidated with proceedings in the securities actions and is ongoing.

Derivative Actions — Southern District of New York. Between October 25, 2004 and July 14, 2005, seven separate derivative actions were filed in the Southern District of New York, five of which were consolidated into a single action. The New York derivative complaint contains nearly the same types of allegations made in the securities fraud and ERISA actions described above. The named defendants include current and former officers and directors of AIG, as well as Marsh & McLennan Companies, Inc. (Marsh), SICO, Starr, ACE Limited and subsidiaries (ACE), General Reinsurance Corporation, PwC, and certain employees or officers of these entity defendants. Plaintiffs assert claims for breach of fiduciary duty, gross mismanagement, waste of corporate assets, unjust enrichment, insider selling, auditor breach of contract, auditor professional negligence and disgorgement from AIG's former Chief Executive Officer and Chief Financial Officer of incentive-based compensation and AIG share proceeds under Section 304 of the Sarbanes-Oxley Act, among others. Plaintiffs seek, among other things, compensatory damages, corporate governance reforms, and a voiding of the election of certain AIG directors. AIG's Board of Directors has appointed a special committee of independent directors (special committee) to review the matters asserted in the operative consolidated derivative complaint. The court has approved an agreement staying the derivative case pending in the Southern District of New York. The current stay extends until September 14, 2007.

Derivative Actions — Delaware Chancery Court. From October 2004 to April 2005, AIG shareholders filed five derivative complaints in the Delaware Chancery Court. All of these derivative lawsuits have been consolidated into a single action. The amended consolidated complaint names 43 defendants (not including nominal defendant AIG) who, like the New York consolidated derivative litigation, are current and former officers and directors of AIG, as well as other entities and certain of their current and former employees and directors. The factual allegations, legal claims and relief sought in Delaware action are similar to those alleged in the New York derivative actions, except that plaintiffs in the Delaware derivative action assert claims only under state law. Earlier in 2007, the Court approved an agreement that AIG be realigned as plaintiff, and, on June 13, 2007, acting on the direction of the special committee, AIG filed an amended complaint against former directors and officers Maurice R. Greenberg and Howard I. Smith, alleging breach of fiduciary duty and indemnification. Also on June 13, 2007, the special committee filed a motion to terminate the litigation as to certain defendants, while taking no action as to others. Defendants Greenberg and Smith filed answers to AIG's complaint and brought third-party complaints against certain current and former AIG directors and officers, PwC and Regulatory Insurance Services, Inc. Certain defendants have subsequently filed motions to dismiss plaintiff's complaint, as well as defendants Greenberg and Smith's third-party complaints. Both plaintiff and defendant Smith have served initial discovery requests; however, certain defendants have sought to stay discovery pending the resolution of the motions to dismiss. Such motions are currently before the Court.

In December 2002, a derivative lawsuit was filed in the Delaware Chancery Court against twenty directors and executives of AIG as well as against AIG as a nominal defendant that alleges, among other things, that the directors of AIG breached the fiduciary duties of loyalty and care by approving the payment of commissions to Starr and of rental and service fees to SICO and the executives breached their duty of loyalty by causing AIG to enter into contracts with Starr and SICO and their fiduciary duties by usurping AIG's corporate opportunity. The complaint further alleges that the Starr agencies did not provide any services that AIG was not capable of providing itself, and that the diversion of commissions to these entities was solely for the benefit of Starr's owners. The complaint also alleged that the service fees and rental payments made to SICO and its subsidiaries were improper. Under the terms of a stipulation approved by the Court on February 16, 2006, the claims against the outside independent directors were dismissed with prejudice, while the claims against the other directors were dismissed without prejudice. On October 31, 2005, Messrs. Greenberg, Matthews and Smith, SICO and Starr filed motions to dismiss the amended complaint. In an opinion dated June 21, 2006, the Court denied defendants' motion to dismiss, except with respect to plaintiff's challenge to payments made to Starr before January 1, 2000. On July 21, 2006, plaintiff filed its second amended complaint, which alleges that, between January 1, 2000 and May 31, 2005, individual defendants breached their duty of loyalty by causing AIG to enter into contracts with Starr and SICO and breached their fiduciary duties by usurping AIG's corporate opportunity. Starr is charged with aiding and abetting breaches of fiduciary duty and unjust enrichment for its acceptance of the fees. SICO is no longer named as a defendant. On April 20, 2007, the individual defendants and Starr filed a motion seeking leave of the Court to assert a cross-claim against AIG and a third-party complaint against PwC and the directors previously dismissed from the action, as well as certain other AIG officers and employees. On June 13, 2007, the Court denied the individual defendants' motion to file a third-party complaint, but granted the proposed cross-claim against AIG. On June 27,

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

6. Commitments, Contingencies and Guarantees *(continued)*

2007, Starr filed its cross-claim against AIG, alleging one count that includes contribution, unjust enrichment and set-off. On July 16, 2007, AIG filed its answer and motion to dismiss Starr's cross-claim to the extent it seeks contribution by Starr and/or the individual defendants. That motion is currently before the Court. Document discovery and depositions are currently ongoing.

Policyholder Actions. After the NYAG filed its complaint against insurance broker Marsh, policyholders brought multiple federal antitrust and Racketeer Influenced and Corrupt Organizations Act (RICO) class actions in jurisdictions across the nation against insurers and brokers, including AIG and a number of its subsidiaries, alleging that the insurers and brokers engaged in a broad conspiracy to allocate customers, steer business, and rig bids. These actions, including 23 complaints filed in different federal courts naming AIG or an AIG subsidiary as a defendant, were consolidated or will be consolidated by the judicial panel on multi-district litigation and transferred to the United States District Court for the District of New Jersey for coordinated pretrial proceedings. The consolidated actions have proceeded in that court in two parallel actions, *In re Insurance Brokerage Antitrust Litigation* (the *First Commercial Complaint*) and *In re Employee Benefit Insurance Brokerage Antitrust Litigation* (the *First Employee Benefits Complaint*, and together with the *First Commercial Complaint*, the multi-district litigation).

The plaintiffs in the *First Commercial Complaint* are nineteen corporations, individuals and public entities that contracted with the broker defendants for the provision of insurance brokerage services for a variety of insurance needs. The broker defendants are alleged to have placed insurance coverage on the plaintiffs' behalf with a number of insurance companies named as defendants, including AIG subsidiaries. The *First Commercial Complaint* also named ten brokers and fourteen other insurers as defendants (two of which have since settled). The *First Commercial Complaint* alleges that defendants engaged in a widespread conspiracy to allocate customers through "bid-rigging" and "steering" practices. The *First Commercial Complaint* also alleges that the insurer defendants permitted brokers to place business with AIG subsidiaries through wholesale intermediaries affiliated with or owned by those same brokers rather than placing the business with AIG subsidiaries directly. Finally, the *First Commercial Complaint* alleges that the insurer defendants entered into agreements with broker defendants that tied insurance placements to reinsurance placements in order to provide additional compensation to each broker. Plaintiffs assert that the defendants violated the Sherman Antitrust Act, RICO, the antitrust laws of 48 states and the District of Columbia, and are liable under common law breach of fiduciary duty and unjust enrichment theories. Plaintiffs seek treble damages plus interest and attorneys' fees as a result of the alleged RICO and Sherman Antitrust Act violations.

The plaintiffs in the *First Employee Benefits Complaint* are nine individual employees and corporate and municipal employers alleging claims on behalf of two separate nationwide purported classes: an employee class and an employer class that acquired insurance products from the defendants from August 26, 1994 to the date of any class certification. The *First Employee Benefits Complaint* names AIG, as well as eleven brokers and five other insurers, as defendants. The activities alleged in the *First Employee Benefits Complaint*, with certain exceptions, track the allegations of contingent commissions, bid-rigging and tying made in the *First Commercial Complaint*.

On October 3, 2006, Judge Hochberg of the District of New Jersey reserved in part and denied in part motions filed by the insurer defendants and broker defendants to dismiss the multi-district litigation. The Court also ordered the plaintiffs in both actions to file supplemental statements of particularity to elaborate on the allegations in their complaints. Plaintiffs filed their supplemental statements on October 25, 2006, and the AIG defendants, along with other insurer and broker defendants in the two consolidated actions, filed renewed motions to dismiss on November 30, 2006. On February 16, 2007, the case was transferred to Judge Garrett E. Brown, Chief Judge of the District of New Jersey. On April 5, 2007, Chief Judge Brown granted the defendants' renewed motions to dismiss the *First Commercial Complaint* and *First Employee Benefits Complaint* with respect to the antitrust and RICO claims. The claims were dismissed without prejudice and the plaintiffs were given 30 days, later extended to 45 days, to file amended complaints. On April 11, 2007, the Court stayed all proceedings, including all discovery, that are part of the multi-district litigation until any renewed motions to dismiss the amended complaints are resolved.

A number of complaints making allegations similar to those in the *First Commercial Complaint* have been filed against AIG and other defendants in state and federal courts around the country. The defendants have thus far been successful in having the federal actions transferred to the District of New Jersey and consolidated into the multi-district litigation. The AIG defendants have also sought to have state court actions making similar allegations stayed pending resolution of the multi-district litigation proceeding. In one state court action pending in Florida, the trial court recently decided not to grant an additional stay, but instead to allow the case to proceed. The parties in that case are currently awaiting the trial court's ruling on the defendants' motions to dismiss the complaint.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

6. Commitments, Contingencies and Guarantees *(continued)*

Plaintiffs filed amended complaints in both *In re Insurance Brokerage Antitrust Litigation* (the *Second Commercial Complaint*) and *In re Employee Benefit Insurance Brokerage Antitrust Litigation* (the *Second Employee Benefits Complaint*) along with revised particularized statements in both actions on May 22, 2007. The allegations in the *Second Commercial Complaint* and the *Second Employee Benefits Complaint* are substantially similar to the allegations in the *First Commercial Complaint and First Employee Benefits Complaint,* respectively. The complaints also attempt to add several new parties and delete others; the *Second Commercial Complaint* adds two new plaintiffs and twenty seven new defendants (including three new AIG defendants), and the *Second Employee Benefits Complaint* adds eight new plaintiffs and nine new defendants (including two new AIG defendants). The defendants filed motions to dismiss the amended complaints and to strike the newly added parties, and the parties are currently awaiting the court's ruling on the motions.

Litigation Relating to 21st Century. Shortly after the announcement in late January 2007 of AIG's offer to acquire the outstanding shares of 21st Century Insurance Group (21st Century) not already owned by AIG and its subsidiaries, two related class actions were filed in the Superior Court of California, Los Angeles County, against AIG, 21st Century, and the individual members of 21st Century's Board of Directors, two of whom are current executive officers of AIG. The actions were filed purportedly on behalf of the minority shareholders of 21st Century and assert breaches of fiduciary duty in connection with the AIG proposal. The complaints allege that the proposed per share price is unfair and seek preliminary and permanent injunctive relief to enjoin the consummation of the proposed transaction. On May 23, 2007, a third action was filed alleging breaches of fiduciary duty by the same defendants based upon their entering into the merger agreement and taking steps to complete the contemplated merger, and seeking injunctive relief comparable to that sought in the first two complaints. All three actions have been consolidated under the caption *In re 21st Century Shareholder Litigation*. Plaintiffs have stated an intention to file a consolidated amended complaint.

SICO. In July, 2005, SICO filed a complaint against AIG in the Southern District of New York, claiming that AIG had refused to provide SICO access to certain artwork and asked the court to order AIG immediately to release the property to SICO. AIG filed an answer denying SICO's allegations and setting forth defenses to SICO's claims. In addition, AIG filed counterclaims asserting breach of contract, unjust enrichment, conversion, breach of fiduciary duty, a constructive trust and declaratory judgment, relating to SICO's breach of its commitment to use its AIG shares only for the benefit of AIG and AIG employees. Fact and expert discovery has been substantially concluded and SICO's motion for summary judgment is pending.

Regulatory Investigations. Regulators from several states have commenced investigations into insurance brokerage practices related to contingent commissions and other industry-wide practices as well as other broker-related conduct, such as alleged bid-rigging. In addition, various federal and state regulatory agencies are reviewing certain transactions and practices of AIG and its subsidiaries in connection with industry-wide and other inquiries. AIG has cooperated, and will continue to cooperate, in producing documents and other information in response to subpoenas and other requests.

Wells Notices. AIG understands that some of its employees have received Wells notices in connection with previously disclosed SEC investigations of certain of AIG's transactions or accounting practices. Under SEC procedures, a Wells notice is an indication that the SEC staff has made a preliminary decision to recommend enforcement action that provides recipients with an opportunity to respond to the SEC staff before a formal recommendation is finalized. It is possible that additional current and former employees could receive similar notices in the future as the regulatory investigations proceed.

Effect on AIG

In the opinion of AIG management, AIG's ultimate liability for the unresolved litigation and investigation matters referred to above is not likely to have a material adverse effect on AIG's consolidated financial condition, although it is possible that the effect would be material to AIG's consolidated results of operations for an individual reporting period.

(b) Commitments

Flight Equipment

At June 30, 2007, ILFC had committed to purchase 246 new aircraft deliverable from 2007 through 2017 at an estimated aggregate purchase price of $20.9 billion. ILFC will be required to find customers for any aircraft acquired, and it must arrange financing for portions of the purchase price of such equipment.

Other Commitments

In the normal course of business, AIG enters into commitments to invest in limited partnerships, private equities and hedge funds and to purchase and develop real estate in the U.S. and abroad. These commitments totaled $6.73 billion at June 30, 2007.

On June 27, 2005, AIG entered into an agreement pursuant to which AIG agrees, subject to certain conditions, to

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

6. Commitments, Contingencies and Guarantees *(continued)*

make any payment that is not promptly paid with respect to the benefits accrued by certain employees of AIG and its subsidiaries under the SICO Plans (as discussed in Note 4 herein).

(c) Contingencies

Loss Reserves. Although AIG regularly reviews the adequacy of the established reserve for losses and loss expenses, there can be no assurance that AIG's ultimate loss reserves will not develop adversely and materially exceed AIG's current loss reserves. Estimation of ultimate net losses, loss expenses and loss reserves is a complex process for long-tail casualty lines of business, which include excess and umbrella liability, directors and officers liability (D&O), professional liability, medical malpractice, workers compensation, general liability, products liability and related classes, as well as for asbestos and environmental exposures. Generally, actual historical loss development factors are used to project future loss development. However, there can be no assurance that future loss development patterns will be the same as in the past. Moreover, any deviation in loss cost trends or in loss development factors might not be discernible for an extended period of time subsequent to the recording of the initial loss reserve estimates for any accident year. Thus, there is the potential for reserves with respect to a number of years to be significantly affected by changes in loss cost trends or loss development factors that were relied upon in setting the reserves. These changes in loss cost trends or loss development factors could be attributable to changes in inflation, in labor and material costs or in the judicial environment, or in other social or economic phenomena affecting claims.

Synthetic Fuel Tax Credits. AIG generates income tax credits as a result of investing in synthetic fuel production. Tax credits generated from the production and sale of synthetic fuel under the Internal Revenue Code are subject to an annual phase-out provision that is based on the average wellhead price of domestic crude oil. The price range within which the tax credits are phased-out was originally established in 1980 and is adjusted annually for inflation. Depending on the price of domestic crude oil for a particular year, all or a portion of the tax credits generated in that year might be eliminated. AIG evaluates the production levels of its synthetic fuel production facilities in light of the risk of phase-out of the associated tax credits. As a result of fluctuating domestic crude oil prices, AIG evaluates and adjusts production levels when appropriate in light of this risk. Under current legislation, the opportunity to generate additional tax credits from the production and sale of synthetic fuel expires on December 31, 2007.

Lease Transactions. On June 27, 2007, field agents at the Internal Revenue Service issued three Notices of Proposed Adjustment (NOPAs) relating to a series of lease transactions by an AIG subsidiary. In the NOPAs, the field agents asserted that the leasing transactions were "lease-in lease-out" transactions described in Revenue Ruling 2002-69 and proposed adjustments to taxable income of approximately $81 million in the aggregate for the years 1998 and 1999. AIG cannot currently estimate the effect, if any, of the resolution of these matters.

(d) Guarantees

AIG and certain of its subsidiaries become parties to derivative financial instruments with market risk resulting from both dealer and end-user activities and to reduce currency, interest rate, equity and commodity exposures. These instruments are carried at their estimated fair values in the consolidated balance sheet. The vast majority of AIG's derivative activity is transacted by AIGFP. See Note 9 below and see Note 19 to the consolidated financial statements in the 2006 Annual Report on Form 10-K.

AIG has issued unconditional guarantees with respect to the prompt payment, when due, of all present and future payment obligations and liabilities of AIGFP arising from transactions entered into by AIGFP.

SAI Deferred Compensation Holdings, Inc., a wholly owned subsidiary of AIG, has established a deferred compensation plan for registered representatives of certain AIG subsidiaries, pursuant to which participants have the opportunity to invest deferred commissions and fees on a notional basis. The value of the deferred compensation fluctuates with the value of the deferred investment alternatives chosen. AIG has provided a full and unconditional guarantee of the obligations of SAI Deferred Compensation Holdings, Inc. to pay the deferred compensation under the plan.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

7. Employee Benefits

The following table presents the components of the net periodic benefit costs with respect to pensions and other postretirement benefits:

	Pensions			Postretirement		
(in millions)	Non-U.S. Plans	U.S. Plans	Total	Non-U.S. Plans	U.S. Plans	Total
Three Months Ended June 30, 2007						
Components of net periodic benefit cost:						
Service cost	**$ 21**	**$ 30**	**$ 51**	**$ 2**	**$ 3**	**$ 5**
Interest cost	**12**	**44**	**56**	**–**	**4**	**4**
Expected return on assets	**(9)**	**(54)**	**(63)**	**–**	**–**	**–**
Amortization of prior service cost	**(3)**	**–**	**(3)**	**–**	**(1)**	**(1)**
Amortization of net loss	**3**	**9**	**12**	**–**	**–**	**–**
Settlement loss	**1**	**–**	**1**	**–**	**–**	**–**
Net periodic benefit cost	**$ 25**	**$ 29**	**$ 54**	**$ 2**	**$ 6**	**$ 8**
Three Months Ended June 30, 2006						
Components of net periodic benefit cost:						
Service cost	$ 18	$ 31	$ 49	$ 1	$ 2	$ 3
Interest cost	8	41	49	–	2	2
Expected return on assets	(7)	(49)	(56)	–	–	–
Amortization of prior service cost	(2)	–	(2)	–	(1)	(1)
Recognized actuarial loss	4	19	23	–	–	–
Net periodic benefit cost	$ 21	$ 42	$ 63	$ 1	$ 3	$ 4
Six Months Ended June 30, 2007						
Components of net periodic benefit cost:						
Service cost	**$ 44**	**$ 60**	**$ 104**	**$ 3**	**$ 5**	**$ 8**
Interest cost	**24**	**89**	**113**	**1**	**8**	**9**
Expected return on assets	**(18)**	**(107)**	**(125)**	**–**	**–**	**–**
Amortization of prior service cost	**(5)**	**(1)**	**(6)**	**–**	**(1)**	**(1)**
Amortization of net loss	**5**	**18**	**23**	**–**	**–**	**–**
Settlement loss	**1**	**–**	**1**	**–**	**–**	**–**
Net periodic benefit cost	**$ 51**	**$ 59**	**$ 110**	**$ 4**	**$ 12**	**$ 16**
Six Months Ended June 30, 2006						
Components of net periodic benefit cost:						
Service cost	$ 37	$ 62	$ 99	$ 2	$ 3	$ 5
Interest cost	17	81	98	1	5	6
Expected return on assets	(14)	(97)	(111)	–	–	–
Amortization of prior service cost	(4)	(1)	(5)	–	(3)	(3)
Recognized actuarial loss	8	38	46	–	–	–
Net periodic benefit cost	$ 44	$ 83	$ 127	$ 3	$ 5	$ 8

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

8. Information Provided in Connection with Outstanding Debt

The following condensed consolidating financial statements are provided in compliance with Regulation S-X of the Securities and Exchange Commission.

- **American General Corporation (AGC) is a holding company and a wholly owned subsidiary of AIG. AIG provides a full and unconditional guarantee of all outstanding debt of AGC.**
- **AIG Liquidity Corp. is a wholly owned subsidiary of AIG. AIG provides a full and unconditional guarantee of all obligations of AIG Liquidity Corp.**
- **AIG Program Funding, Inc. is a wholly owned subsidiary of AIG. AIG provides a full and unconditional guarantee of all obligations of AIG Program Funding, Inc., which was established in 2007.**

Condensed Consolidating Balance Sheet

(in millions)	American International Group, Inc. (As Guarantor)	AGC	AIG Liquidity Corp.	AIG Program Funding, Inc.	Other Subsidiaries	Eliminations	Consolidated AIG
June 30, 2007							
Assets:							
Investments and financial services assets	**$ 14,368**	**$ –**	**$ –**	**$ –**	**$ 832,421**	**$ (17,960)**	**$ 828,829**
Cash	**36**	**–**	**–**	**–**	**1,599**	**–**	**1,635**
Carrying value of subsidiaries and partially owned companies, at equity	**116,412**	**27,670**	**–**	**–**	**11,896**	**(154,802)**	**1,176**
Other assets	**5,201**	**2,673**	**–**	**–**	**194,403**	**(51)**	**202,226**
Total assets	**$136,017**	**$30,343**	**$ –**	**$ –**	**$1,040,319**	**$ (172,813)**	**$1,033,866**
Liabilities:							
Insurance liabilities	**$ 23**	**$ –**	**$ –**	**$ –**	**$ 507,129**	**$ (66)**	**507,086**
Debt	**26,454**	**2,136**	**–**	**–**	**154,213**	**(17,493)**	**165,310**
Other liabilities	**5,210**	**3,143**	**–**	**–**	**248,725**	**(38)**	**257,040**
Total liabilities	**31,687**	**5,279**	**–**	**–**	**910,067**	**(17,597)**	**929,436**
Preferred shareholders' equity in subsidiary companies	**–**	**–**	**–**	**–**	**100**	**–**	**100**
Total shareholders' equity	**104,330**	**25,064**	**–**	**–**	**130,152**	**(155,216)**	**104,330**
Total liabilities, preferred shareholders' equity in subsidiary companies and shareholders' equity	**$136,017**	**$30,343**	**$ –**	**$ –**	**$1,040,319**	**$ (172,813)**	**$1,033,866**
December 31, 2006							
Assets:							
Investments and financial services assets	$ 7,346	$ –	$*	$ –	$ 797,976	$ (14,822)	$ 790,500
Cash	76	–	*	–	1,514	–	1,590
Carrying value of subsidiaries and partially owned companies, at equity	109,125	27,967	–	–	8,436	(144,427)	1,101
Other assets	3,989	2,622	*	–	181,561	(1,949)	186,223
Total assets	$120,536	$30,589	$*	$ –	$ 989,487	$ (161,198)	$ 979,414

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

(in millions)	American International Group, Inc. (As Guarantor)	AGC	AIG Liquidity Corp.	AIG Program Funding, Inc.	Other Subsidiaries	Eliminations	Consolidated AIG
Liabilities:							
Insurance liabilities	$ 21	$ –	$ –	$ –	$ 495,135	$ (64)	$ 495,092
Debt	15,157	2,136	*	–	146,206	(14,820)	148,679
Other liabilities	3,681	3,508	*	–	228,068	(1,482)	233,775
Total liabilities	18,859	5,644	*	$ –	869,409	(16,366)	877,546
Preferred shareholders' equity in subsidiary companies	–	–	–	–	191	–	191
Total shareholders' equity	101,677	24,945	*	–	119,887	(144,832)	101,677
Total liabilities, preferred shareholders' equity in subsidiary companies and shareholders' equity	$120,536	$30,589	$ *	$ –	$ 989,487	$ (161,198)	$ 979,414

**Less than $1 million.*

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

8. Information Provided in Connection with Outstanding Debt *(continued)*

Condensed Consolidating Statement of Income

(in millions)	American International Group, Inc. (As Guarantor)	AGC	AIG Liquidity Corp.	AIG Program Funding, Inc.	Other Subsidiaries	Eliminations	Consolidated AIG
Three Months Ended June 30, 2007							
Operating income (loss)	**$ (282)**	**$ (13)**	**$ ***	**$ –**	**$ 6,623**	**$ –**	**$ 6,328**
Equity in undistributed net income of consolidated subsidiaries	**3,605**	**340**	**–**	**–**	**–**	**(3,945)**	**–**
Dividend income from consolidated subsidiaries	**879**	**218**	**–**	**–**	**–**	**(1,097)**	**–**
Income taxes	**(75)**	**(15)**	*****	**–**	**1,769**	**–**	**1,679**
Minority interest	**–**	**–**	**–**	**–**	**(372)**	**–**	**(372)**
Net income (loss)	**$4,277**	**$ 560**	**$ ***	**$ –**	**$ 4,482**	**$ (5,042)**	**$ 4,277**
Three Months Ended June 30, 2006							
Operating income (loss)	$ (436)	$ (48)	$ *	$ –	$ 5,725	$ –	$ 5,241
Equity in undistributed net income of consolidated subsidiaries	3,507	309	–	–	–	(3,816)	–
Dividend income from consolidated subsidiaries	380	154	–	–	–	(534)	–
Income taxes (benefits)	261	(17)	*	–	1,444	–	1,688
Minority interest	–	–	–	–	(363)	–	(363)
Net income (loss)	$3,190	$ 432	$ *	$ –	$ 3,918	$ (4,350)	$ 3,190
Six Months Ended June 30, 2007							
Operating income (loss)	**$ (543)**	**$ (86)**	**$ ***	**$ –**	**$13,129**	**$ –**	**$12,500**
Equity in undistributed net income of consolidated subsidiaries	**6,849**	**491**	**–**	**–**	**–**	**(7,340)**	**–**
Dividend income from consolidated subsidiaries	**2,165**	**658**	**–**	**–**	**–**	**(2,823)**	**–**
Income taxes	**64**	**(7)**	*****	**–**	**3,348**	**–**	**3,405**
Minority interest	**–**	**–**	**–**	**–**	**(688)**	**–**	**(688)**
Net income (loss)	**$8,407**	**$1,070**	**$ ***	**$ –**	**$ 9,093**	**$(10,163)**	**$ 8,407**
Six Months Ended June 30, 2006							
Operating income (loss)	$ (722)	$ (86)	$ *	$ –	$10,842	$ –	$10,034
Equity in undistributed net income of consolidated subsidiaries	6,767	668	–	–	–	(7,435)	–
Dividend income from consolidated subsidiaries	567	458	–	–	–	(1,025)	–
Income taxes (benefits)	261	(30)	*	–	2,892	–	3,123
Minority interest	–	–	–	–	(560)	–	(560)
Cumulative effect of an accounting change, net of tax	34	–	–	–	–	–	34
Net income (loss)	$6,385	$1,070	$ *	$ –	$ 7,390	$ (8,460)	$ 6,385

**Less than $1 million.*

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

8. Information Provided in Connection with Outstanding Debt *(continued)*

Condensed Consolidating Statement of Cash Flow

(in millions)	American International Group, Inc. (As Guarantor)	AGC	AIG Liquidity Corp.	AIG Program Funding, Inc.	Other Subsidiaries	Consolidated AIG
Six Months Ended June 30, 2007						
Net cash provided by operating activities	**$ 743**	**$ 172**	**$ ***	**$ –**	**$ 14,156**	**$ 15,071**
Cash flows from investing:						
Invested assets disposed	**–**	**–**	**–**	**–**	**83,764**	**83,764**
Invested assets acquired	**(6,973)**	**–**	**–**	**–**	**(114,198)**	**(121,171)**
Other	**(242)**	**(76)**	*****	**–**	**(148)**	**(466)**
Net cash used in investing activities	**(7,215)**	**(76)**	*****	**–**	**(30,582)**	**(37,873)**
Cash flows from financing activities:						
Issuance of debt	**11,931**	**–**	**–**	**–**	**39,100**	**51,031**
Repayments of debt	**(793)**	**–**	**–**	**–**	**(34,144)**	**(34,937)**
Payments advanced to purchase shares	**(4,000)**	**–**	**–**	**–**	**—**	**(4,000)**
Cash dividends paid to shareholders	**(859)**	**–**	**–**	**–**	**—**	**(859)**
Other	**153**	**(96)**	*****	**–**	**11,574**	**11,631**
Net cash provided by (used in) financing activities	**6,432**	**(96)**	*****	**–**	**16,530**	**22,866**
Effect of exchange rate changes on cash	**–**	**–**	**–**	**–**	**(19)**	**(19)**
Change in cash	**(40)**	**–**	*****	**–**	**85**	**45**
Cash at beginning of period	**76**	**–**	**–**	**–**	**1,514**	**1,590**
Cash at end of period	**$ 36**	**$ –**	**$ ***	**$ –**	**$ 1,599**	**$ 1,635**
Six Months Ended June 30, 2006						
Net cash (used in) provided by operating activities	$ (3,465)	$ 112	$ *	$ –	$ 8,618	$ 5,265
Cash flows from investing:						
Invested assets disposed	–	–	–	–	84,360	84,360
Invested assets acquired	(905)	–	–	–	(116,997)	(117,902)
Other	(718)	(17)	*	–	347	(388)
Net cash used in investing activities	(1,623)	(17)	*	–	(32,290)	(33,930)
Cash flows from financing activities:						
Issuance of debt	5,816	–	–	–	26,329	32,145
Repayments of debt	(145)	–	–	–	(16,805)	(16,950)
Cash dividends paid to shareholders	(780)	–	–	–	—	(780)
Other	60	(95)	*	–	14,481	14,446
Net cash provided by (used in) financing activities	4,951	(95)	*	–	24,005	28,861
Effect of exchange rate changes on cash	–	–	–	–	47	47
Change in cash	(137)	–	*	–	380	243
Cash at beginning of period	190	–	–	–	1,707	1,897
Cash at end of period	$ 53	$ –	$ *	$ –	$ 2,087	$ 2,140

**Less than $1 million.*

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

9. Derivatives and Hedge Accounting

AIG uses derivatives and other instruments as part of its financial risk management programs and as part of its investment operations. AIGFP also transacts in derivatives as a dealer.

Derivatives, as defined in FAS 133, are financial arrangements among two or more parties with returns linked to or "derived" from some underlying equity, debt, commodity or other asset, liability, or foreign exchange rate or other index or the occurrence of a specified payment event. Derivative payments may be based on interest rates, exchange rates, prices of certain securities, commodities, or financial or commodity indices or other variables. Collateral is required on certain transactions based on the creditworthiness of the counterparty.

Unless subject to a scope exclusion, AIG carries all derivatives on the consolidated balance sheet at fair value. The changes in fair value of the derivative transactions of AIGFP are presented as a component of AIG's operating income.

AIGFP

AIGFP, in the ordinary course of operations and as principal, structures and enters into derivative transactions to meet the needs of counterparties who may be seeking to hedge certain aspects of such counterparties' operations or obtain a desired financial exposure. AIGFP also enters into derivative transactions to mitigate risk in its exposures (interest rates, currencies, commodities and equities) arising from such transactions. Such instruments are carried at market or fair value, whichever is appropriate, and are reflected on the balance sheet in "Unrealized gain on swaps, options and forward transactions" and "Unrealized loss on swaps, options and forward contracts."

Beginning in the first quarter of 2007, AIGFP designated certain interest rate swaps as fair value hedges of the benchmark interest rate risk on certain of its interest bearing financial assets and liabilities. In these hedging relationships, AIG is hedging its fixed rate available for sale securities and fixed rate borrowings. AIGFP also designated foreign currency forward contracts as fair value hedges for changes in spot foreign exchange rates of the non-U.S. dollar denominated available for sale debt securities. Under these strategies, all or portions of individual or multiple derivatives may be designated against a single hedged item.

At inception of each hedging relationship, AIGFP performs and documents its prospective assessments of hedge effectiveness to demonstrate that the hedge is expected to be highly effective. For hedges of interest rate risk, AIGFP uses regression to demonstrate the hedge is highly effective, while it uses the periodic dollar offset method for its foreign currency hedges. AIGFP uses the periodic dollar offset method to assess whether its hedging relationships were highly effective on a retrospective basis. The prospective and retrospective assessments are updated on a daily basis. The passage of time component of the hedging instruments is excluded from the assessment of hedge effectiveness and measurement of hedge ineffectiveness. AIGFP does not utilize the shortcut, match terms or equivalent methods.

The change in fair value of the derivative that qualifies under the requirements of FAS 133 as a fair value hedge is recorded in current period earnings along with the gain or loss on the hedged item for the hedged risk. For interest rate hedges, the adjustments to the carrying value of the hedged items are amortized into income using the effective yield method over the remaining life of the hedged item. Amounts excluded from the assessment of hedge effectiveness are recognized in current period earnings.

For the three and six months ended June 30, 2007, AIGFP recognized a net loss of less than $1 million and a net gain of $2 million in earnings, respectively, representing hedge ineffectiveness, and also recognized a net loss of $157 million and $211 million, respectively, related to the portion of the hedging instruments excluded from the assessment of hedge effectiveness. All these amounts are reflected in Other income. AIGFP did not apply hedge accounting in 2006.

Other Derivative Users

AIG and its subsidiaries (other than AIGFP) also use derivatives and other instruments as part of their financial risk management programs. Interest rate derivatives (such as interest rate swaps) are used to manage interest rate risk associated with investments in fixed income securities, commercial paper issuances, medium- and long-term note offerings, and other interest rate sensitive assets and liabilities. In addition, foreign exchange derivatives (principally cross currency swaps, forwards and options) are used to economically mitigate risk associated with non-U.S. dollar denominated debt, net capital exposures and foreign exchange transactions. The derivatives are effective economic hedges of the exposures they are meant to offset.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

9. Derivatives and Hedge Accounting *(continued)*

In 2007, AIG and its subsidiaries other than AIGFP designated certain derivatives as either fair value or cash flow hedges of their debt. The fair value hedges included (i) interest rate swaps that were designated as hedges of the change in the fair value of fixed rate debt attributable to changes in the benchmark interest rate and (ii) foreign currency swaps designated as hedges of the change in fair value of foreign currency denominated debt attributable to changes in foreign exchange rates and/or the benchmark interest rate. With respect to the cash flow hedges, (i) interest rate swaps were designated as hedges of the changes in cash flows on floating rate debt attributable to changes in the benchmark interest rate, and (ii) foreign currency swaps were designated as hedges of changes in cash flows on foreign currency denominated debt attributable to changes in the benchmark interest rate and foreign exchange rates.

AIG assesses, both at the hedge's inception and on an ongoing basis, whether the derivatives used in hedging transactions are highly effective in offsetting changes in fair values or cash flows of hedged items. Regression analysis is employed to assess the effectiveness of these hedges both on a prospective and retrospective basis. AIG does not utilize the shortcut, match terms or equivalent methods.

The change in fair value of derivatives designated and effective as fair value hedges along with the gain or loss on the hedged item are recorded in net realized capital gains (losses). Upon discontinuation of hedge accounting, the cumulative adjustment to the carrying value of the hedged item resulting from changes in the benchmark interest rate is amortized into income using the effective yield method over the remaining life of the hedged item. Amounts excluded from the assessment of hedge effectiveness are recognized in current period earnings. During both the three and six months ended June 30, 2007, AIG recognized a gain of less than $1 million in earnings related to the ineffective portion of the hedging instruments. AIG also recognized a loss of $8 million related to the change in the hedging instruments forward points excluded from the assessment of hedge effectiveness.

The effective portion of the change in fair value of a derivative qualifying as a cash flow hedge is recorded in Accumulated other comprehensive income (loss), until earnings are affected by the variability of cash flows in the hedged item. The ineffective portion of these hedges is recorded in net realized capital gains (losses). During the three and six months ended June 30, 2007, AIG recognized a loss of less than $1 million and a gain of less than $1 million, respectively, in earnings representing hedge ineffectiveness. At June 30, 2007, $10 million of the deferred net gain in Accumulated other comprehensive income is expected to be recognized in earnings during the next 12 months. All components of the derivatives' gains and losses were included in the assessment of hedge effectiveness. There were no instances of the discontinuation of hedge accounting in 2007.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

10. Cash Flows

As part of its remediation activities during 2006, AIG determined that certain non-cash activities and adjustments, including the effects of changes in foreign exchange translation on assets and liabilities, previously were misclassified within the operating, investing and financing sections of the Consolidated Statement of Cash flows. The more significant line items revised include the change in General and life insurance reserves and DAC within operating activities; Purchases of fixed maturity securities within investing activities; and Proceeds from notes, bonds, loans and mortgages payable, and hybrid financial instrument liabilities within financing activities. After evaluating the effect of these items during the third quarter of 2006, AIG revised the previous periods presented in its September 30, 2006 consolidated financial statements included in that quarter's Quarterly Report on Form 10-Q to conform to the revised presentation.

Subsequent to that revision, additional revisions were made in 2006, primarily relating to certain elements of net realized capital gains and the effect of reclassifying certain policyholders' account balances from Other policyholder funds to Policyholders' contract deposits.

The effect of these revisions on the Consolidated Statement of Cash flows for the six months ended June 30, 2006 is presented below:

(in millions)	Originally Reported June 30, 2006	Revisions Third Quarter 2006	As Revised Third Quarter 2006	Additional Revisions	As Revised
Cash flows from operating activities	$ 6,978	$ (355)	$ 6,623	$(1,358)	$ 5,265
Cash flows from investing activities	(40,048)	5,682	(34,366)	436	(33,930)
Cash flows from financing activities	32,243	(4,304)	27,939	922	28,861
Effect of exchange rate changes on cash	1,070	(1,023)	47	—	47

ITEM 2. Management's Discussion and Analysis of Financial Condition and Results of Operations

Management's Discussion and Analysis of Financial Condition and Results of Operations is designed to provide the reader a narrative with respect to AIG's operations, financial condition and liquidity and certain other significant matters.

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Cautionary Statement Regarding Projections and Other Information About Future Events

This Quarterly Report on Form 10-Q and other publicly available documents may include, and AIG's officers and representatives may from time to time make, projections concerning financial information and statements concerning future economic performance and events, plans and objectives relating to management, operations, products and services, and assumptions underlying these projections and statements. These projections and statements are not historical facts but instead represent only AIG's belief regarding future events, many of which, by their nature, are inherently uncertain and outside AIG's control. These projections and statements may address, among other things, the status and potential future outcome of the current regulatory and civil proceedings against AIG and their potential effect on AIG's businesses, financial position, results of operations, cash flows and liquidity, the effect of credit rating changes on AIG's businesses and competitive position, the unwinding and resolving of various relationships between AIG and SICO and AIG's strategy for growth, product development, market position, financial results and reserves. It is possible that AIG's actual results and financial condition may differ, possibly materially, from the anticipated results and financial condition indicated in these projections and statements. Factors that could cause AIG's actual results to differ, possibly materially, from those in the specific projections and statements are discussed throughout this Management's Discussion and Analysis of Financial Condition and Results of Operations and in Item 1A. Risk Factors of AIG's Annual Report on Form 10-K for the year ended December 31, 2006 (2006 Annual Report on Form 10-K). AIG is not under any obligation (and expressly disclaims any such obligations) to update or alter any projection or other statement, whether written or oral, that may be made from time to time, whether as a result of new information, future events or otherwise.

In addition to reviewing AIG's results for the first six months of 2007, this Management's Discussion and Analysis of Financial Condition and Results of Operations supplements and updates the information and discussion included in the 2006 Annual Report on Form 10-K. Throughout this Management's Discussion and Analysis, AIG presents its operations in the way it believes will be most meaningful. Statutory loss ratios and combined ratios are presented in accordance with accounting principles prescribed by insurance regulatory authorities because these are standard measures of performance filed with insurance regulatory authorities and used for analysis in the insurance industry and thus allow more meaningful comparisons with AIG's insurance competitors. AIG has also incorporated into this discussion cross-references to additional information included in this Quarterly Report on Form 10-Q and in the 2006 Annual Report on Form 10-K to assist readers seeking related information on a particular subject.

Overview of Operations and Business Results

AIG identifies its reportable segments by product or service line, consistent with its management structure. AIG's segments are General Insurance, Life Insurance & Retirement Services, Financial Services and Asset Management. AIG's operations in 2007 and 2006 were conducted by its subsidiaries through these segments. Through these segments, AIG provides insurance, financial and investment products and services to both businesses and individuals in more than 130 countries and jurisdictions. This geographic, product and service diversification is one of AIG's major strengths and sets it apart from its competitors. AIG's Other category consists of items not allocated to AIG's operating segments.

AIG's subsidiaries serve commercial, institutional and individual customers through an extensive property-casualty and life insurance and retirement services network. In the United States, AIG companies are the largest underwriters of commercial and industrial insurance and are among the largest life insurance and retirement services operations as well. AIG's Financial Services businesses include commercial aircraft and equipment leasing, capital markets operations and consumer finance, both in the United States and abroad. AIG also provides asset management services to institutions and individuals. As part of its spread-based business activities, AIG issues various debt instruments in the public and private markets.

Outlook

The following paragraphs supplement and update the information and discussion included in Management's Discussion and Analysis of Financial Condition and Results of Operations — Outlook, in the 2006 Annual Report on Form 10-K to reflect developments in or affecting AIG's business during 2007.

The commercial property and casualty insurance industry has historically experienced cycles of price erosion followed by rate strengthening as a result of catastrophes or other significant losses that affect the overall capacity of the industry to provide coverage. Despite industry price erosion in commercial lines, AIG expects to continue to identify profitable opportunities and build attractive new general insurance businesses as a result of AIG's broad product line and extensive distribution networks in the U.S. and abroad.

Workers compensation remains under considerable pricing pressure, as statutory rates continue to decline. Rates for excess casualty, D&O and certain other lines of insurance also continue to decline due to competitive pressures. There can be no assurance that price erosion will not become more widespread or that AIG's profitability will not deteriorate from current levels in major commercial lines; however, AIG seeks to mitigate this risk by constantly seeking out profitable opportunities across its diverse product lines and distribution networks.

In AIG's Foreign Retirement Services business, the continued weak yen has resulted in higher than normal surrenders and that trend, if prolonged, could further accelerate the amortization of deferred acquisition costs (DAC). Similarly, in the Domestic Retirement Services business, the flat yield curve and the age of the in-force blocks of individual fixed annuities could result in an acceleration of surrender activity as early as 2008.

In Japan, the National Tax Authority in cooperation with the Life Insurance Association of Japan is reviewing the tax treatment for increasing term life insurance, which may affect the amount of premiums that qualify as tax deductions for business owners. As a result of this review, AIG's life insurance companies in Japan suspended the sale of increasing term life insurance from early April 2007. This action will have an adverse effect on life insurance sales in the second half of 2007. AIG companies in Japan have taken several measures aimed at increasing sales of other products in the Japanese market, in particular sales of U.S. dollar life insurance products.

In March 2007, the U.S. Treasury Department published proposed new regulations that, if adopted in their current form, would limit the ability of U.S. taxpayers to claim foreign tax credits in certain circumstances under the Internal Revenue Code. Should the proposed regulations be adopted in their current form, they would limit AIG's ability to claim foreign tax credits in connection with certain structured transactions entered into by AIG Financial Products Corp. and AIG Trading Group Inc. and their respective subsidiaries (collectively, AIGFP), resulting in a material adverse effect on AIGFP's operating results.

The U.S. residential mortgage market is experiencing serious disruption due to deterioration in the credit quality of loans originated to non-prime and subprime borrowers,

evolving changes in the regulatory environment and a slower residential housing market. AIG participates in the U.S. residential mortgage market in several ways: American General Finance, Inc. (AGF) extends first and second-lien mortgage loans to buyers and owners of residential housing; United Guaranty Corporation (UGC) provides mortgage guaranty insurance for first and second-lien residential mortgages; AIG insurance and financial services subsidiaries invest in mortgage-backed securities and collateralized debt obligations (CDOs) in which the underlying collateral is composed in whole or in part of residential mortgage loans; and AIGFP provides credit protection through credit default swaps on certain senior tranches of such CDOs. The operating results of AIG's consumer finance and mortgage guaranty operations in the United States have been and are likely to continue to be adversely affected by the factors referred to above. The downward cycle in the U.S. housing market is not expected to improve until residential inventories return to a more normal level and the mortgage credit market stabilizes. AIG expects that this downward cycle will continue to adversely affect UGC's operating results for the foreseeable future, although UGC is beginning to experience improved credit quality trends on new production. The effect of the downward cycle in the U.S. housing market on AIG's other operations, investment portfolio and overall consolidated financial position, is not expected to be material due to AIG's disciplined underwriting and active risk management, as well as the high credit ratings for assets collateralized by subprime and non-prime mortgages and the structural protections against loss afforded AIG by its senior position in the investments and exposures that it holds.

In recent quarters, AIG's returns from partnerships and other alternative investments have been particularly strong, driven by favorable equity market performance and credit conditions. These returns may vary significantly from period to period. AIG believes that the particularly strong performance in recent periods is not indicative of the returns to be expected from this asset class in future periods.

Consolidated Results

The following table summarizes AIG's consolidated revenues, income before income taxes, minority interest and cumulative effect of an accounting change and net income:

(in millions)	Three Months Ended June 30, **2007**	2006	Percentage Increase/ (Decrease)	Six Months Ended June 30, **2007**	2006	Percentage Increase/ (Decrease)
Total revenues	**$31,150**	$26,854	16%	**$61,795**	$54,132	14%
Income before income taxes, minority interest and cumulative effect of an accounting change	**6,328**	5,241	21	**12,500**	10,034	25
Net income	**$ 4,277**	$ 3,190	34%	**$ 8,407**	$ 6,385	32%

AIG's consolidated revenues for the three and six-month periods ended June 30, 2007 increased compared to the same periods in 2006 as revenues increased in each of AIG's operating segments.

AIG's consolidated income before income taxes, minority interest and cumulative effect of an accounting change increased in the three and six-month periods ended June 30, 2007 compared to the same periods in 2006. During the three months ended June 30, 2007, growth was experienced in all operating segments compared to the same period in 2006. For the six months ended June 30, 2007 operating income grew in all operating segments with the exception of Life Insurance & Retirement Services, which declined marginally due to higher net realized capital losses. Operating income for the three and six-month periods ended June 30, 2007 reflects significant increases from the comparable periods in 2006 related to differences in the accounting treatment for hedging activities. In the first six months of 2007, AIGFP applied hedge accounting to certain of its interest rate swaps and foreign currency forward contracts hedging its investments and borrowings. As a result, AIGFP was able to recognize in earnings the change in the fair value on the hedged items attributable to the hedged risks, offsetting the gains and losses on the derivatives designated as hedges. In 2006, AIGFP did not apply hedge accounting under FAS 133 to any of its derivatives or related assets and liabilities.

During the three months ended June 30, 2007, AIG recorded certain out of period adjustments. These adjustments collectively decreased pre-tax operating income in that quarter by $334 million and net income by $139 million. The adjustments were comprised of a charge of $431 million ($280 million after tax) in Capital Markets, including $380 million ($247 million after tax) to reverse net gains on transfers of investment securities among legal entities consolidated within AIGFP into Accumulated other comprehensive income; a $78 million decrease in income tax expense related to the remediation of the material weakness in controls over income tax accounting; $27 million ($18 million after tax) of net realized capital gains relating to foreign exchange; and $70 million of additional income primarily relating to other remediation activities ($45 million after tax).

For the six months ended June 30, 2007, out of period adjustments collectively decreased pre-tax operating income by $495 million ($373 million after tax). The adjustments were comprised of a charge of $380 million ($247 million after tax) discussed above; $51 million of additional income tax expense related to the aforementioned remediation

activities; $74 million ($48 million after tax) of net realized capital gains related to foreign exchange; and $189 million ($123 million after tax) of additional expense, primarily relating to other remediation activities.

During the second quarter of 2006, as part of its remediation efforts, AIG identified and recorded an out of period adjustment related to the accounting for UCITS in accordance with FIN 46(R), "Consolidation of Variable Interest Entities" and APB Opinion No. 18, "The Equity Method of Accounting for Investments in Common Stock." These investments had previously been accounted for as available for sale securities, with changes in market values being reflected in Accumulated other comprehensive income, net of deferred income taxes. Beginning with the second quarter of 2006, the changes in market values are included in Net investment income. For the three and six-month periods ended June 30, 2006, the effect on the Consolidated Statement of Comprehensive Income (Loss) was decreases of $576 million and $537 million, respectively, in Unrealized appreciation (depreciation) of investments — net of reclassification adjustments, and increases of $202 million and $188 million, respectively, in the related Deferred income tax benefit (expense). For the three and six-month periods ended June 30, 2006, the effect on the Consolidated Statement of Income was increases of $653 million and $608 million, respectively, in Net investment income, increases of $77 million and $71 million, respectively, in Incurred policy losses and benefits, related to certain participating policyholder funds, and increases in Income taxes of $202 and $188 million, respectively. There was no effect on Total shareholders' equity at June 30, 2006.

In the second quarter of 2006, AIG recorded other out of period adjustments of $85 million ($55 million after tax) of interest income related to interest earned on deposit contracts and $199 million ($150 million after tax) of expenses related to the remediation of a material weakness in controls over certain balance sheet reconciliations and other remediation-related activities.

For the six months ended June 30, 2006, out of period adjustments collectively increased pre-tax operating income by $23 million and reduced net income by $67 million. The adjustments were comprised of $537 million ($349 million after tax) of additional investment income related to the accounting for UCITS; $300 million ($145 million after tax) of charges related to the remediation of a material weakness in accounting for certain derivative transactions under FAS 133; $126 million of additional income tax expense related to the aforementioned remediation activities; $85 million ($55 million after tax) of interest income related interest earned on deposit contracts; $61 million (before and after tax) of expenses related to the Starr International Company, Inc. (SICO) Deferred Compensation Profit Participation Plans (SICO Plans); $59 million ($38 million after tax) of expenses related to deferred advertising costs; and $179 million ($101 million after tax) of additional expense, primarily related to other remediation activities.

Results for the first six months of 2006 were also negatively affected by a one-time charge relating to the C.V. Starr & Co., Inc. (Starr) tender offer ($54 million before and after tax) and an additional allowance for losses in AIG Credit Card Company (Taiwan) ($88 million before and after tax), both of which were recorded in first quarter of 2006.

Since March 31, 2006, through its continued remediation efforts, AIG identified additional out of period adjustments relating to the three and six months ended June 30, 2006 that increased (decreased) net income by $(45) million and $76 million, respectively. These items primarily relate to AIG's ongoing remediation of internal controls over accounting for UCITS and reconciliation of balance sheet accounts.

The effective income tax rate decreased from 30.1 percent for the full year of 2006 to 26.5 percent and 27.2 percent for the three and six-month periods ended June 30, 2007, respectively, primarily due to the benefits from remediation adjustments and the recognition of tax benefits associated with the SICO Plans for which the compensation expense had been recognized in prior years. Such tax benefits amounted to $97 million and $143 million, respectively, for the three and six-month periods ended June 30, 2007.

Segment Results

The following table summarizes AIG's operations by major operating segment. (See also Note 2 of Notes to Consolidated Financial Statements.)

(in millions)	Three Months Ended June 30, **2007**	2006	Percentage Increase/ (Decrease)	Six Months Ended June 30, **2007**	2006	Percentage Increase/ (Decrease)
Revenues[a]:						
General Insurance[b][c]	**$12,928**	$12,167	6%	**$25,831**	$23,823	8%
Life Insurance & Retirement Services[c][d]	**14,023**	11,911	18	**27,705**	24,761	12
Financial Services[e][f]	**2,123**	1,246	70	**4,324**	2,912	48
Asset Management[g]	**1,989**	1,515	31	**3,897**	2,654	47
Other	**263**	138	91	**394**	228	73
Consolidation and eliminations	**(176)**	(123)	—	**(356)**	(246)	—
Consolidated	**$31,150**	$26,854	16%	**$61,795**	$54,132	14%
Operating income (loss)[a][h]:						
General Insurance[c]	**$ 2,976**	$ 2,863	4%	**$ 6,072**	$ 5,194	17%
Life Insurance & Retirement Services[c]	**2,620**	2,381	10	**4,901**	5,011	(2)
Financial Services[f]	**47**	(530)	–	**339**	(638)	–
Asset Management	**1,128**	785	44	**2,122**	1,234	72
Other	**(460)**	(258)	—	**(930)**	(767)	—
Consolidation and eliminations	**17**	—	—	**(4)**	—	—
Consolidated	**$ 6,328**	$ 5,241	21%	**$12,500**	$10,034	25%

(a) Includes gains (losses) from hedging activities that did not qualify for hedge accounting treatment under FAS 133, "Accounting for Derivative Instruments and Hedging Activities" (FAS 133), including the related foreign exchange gains and losses. For the three-month periods ended June 30, 2007 and 2006, respectively, the effect was $(430) million and $(1.08) billion in both revenues and operating income. For the six-month periods ended June 30, 2007 and 2006, respectively, the effect was $(882) million and $(1.30) billion in both revenues and operating income. These amounts result primarily from interest rate and foreign currency derivatives that are hedging investments and borrowings. These gains (losses) for the three and six months ended June 30, 2007 include out of period charges of $431 million and $326 million, respectively, including a $380 million charge in both periods to reverse net gains recognized on transfers of available for sale securities among legal entities consolidated within AIGFP. The first six months of 2006 include an out of period charge of $300 million related to the remediation of the material weakness in accounting for certain derivative transactions under FAS 133.

(b) Represents the sum of General Insurance net premiums earned, net investment income and net realized capital gains (losses).

(c) Includes the effect of an out of period UCITS adjustment in the second quarter of 2006. For the three and six-month periods ended June 30, 2006, the effect was an increase of $432 million and $405 million, respectively, in both revenues and operating income for General Insurance and an increase of $221 million and $203 million, respectively, in revenues and $144 million and $132 million, respectively, in operating income for Life Insurance & Retirement Services.

(d) Represents the sum of Life Insurance & Retirement Services premiums and other considerations, net investment income and net realized capital gains (losses). Included in net realized capital gains (losses) and operating income are gains (losses) from hedging activities that did not qualify for hedge accounting treatment under FAS 133, which were $41 million and $73 million for the three-month periods ended June 30, 2007 and 2006, respectively, and $(82) million and $425 million for the six-month periods ended June 30, 2007 and 2006, respectively. Also included in net realized capital gains (losses) was the application of FAS 52, the effects of which were $(24) million and $(94) million for the three-month periods ended June 30, 2007 and 2006, respectively, and $99 million and $(90) million for the six-month periods ended June 30, 2007 and 2006, respectively.

(e) Primarily represents interest, lease and finance charges.

(f) Includes gains (losses) from hedging activities that did not qualify for hedge accounting treatment under FAS 133, including the related foreign exchange gains and losses. For the three-month periods ended June 30, 2007 and 2006, respectively, the effect was $(443) million, and $(1.1) billion in both revenues and operating income. For the six-month periods ended June 30, 2007 and 2006, respectively, the effect was $(603) million and $(1.8) billion in both revenues and operating income. These amounts result primarily from interest rate and foreign currency derivatives that are effective economic hedges of investments and borrowings. The second quarter and the first six months of 2007 include the out of period charges of $431 million and $326 million, respectively, as discussed above. The first six months of 2006 include an out of period charge of $300 million as discussed above. In the first quarter of 2007, AIG began applying hedge accounting for certain transactions, primarily in its Capital Markets operations. In the second quarter of 2007, AGF and ILFC began applying hedge accounting to most of their derivatives hedging interest rate and foreign exchange risks associated with their floating rate and foreign currency denominated borrowings.

(g) Represents net investment income with respect to spread-based products and management and advisory fees.

(h) Represents income before income taxes, minority interest and cumulative effect of an accounting change.

General Insurance

AIG's General Insurance operations provide property and casualty products and services throughout the world. Foreign operations provided approximately 29 percent and 36 percent of General Insurance operating income for the three months ended June 30, 2007 and 2006, respectively, and approximately 29 percent and 33 percent for the six months ended June 30, 2007 and 2006, respectively. The increase in General Insurance operating income in the three and six-month periods ended June 30, 2007 compared to the same periods in 2006 was primarily attributable to improved underwriting results for the Domestic Brokerage Group (DBG) and higher net investment income, partially offset by losses from the Mortgage Guaranty business.

Life Insurance & Retirement Services

AIG's Life Insurance & Retirement Services operations provide insurance, financial and investment products throughout the world. Foreign operations provided approximately 63 percent and 73 percent of Life Insurance & Retirement Services operating income for the three months ended June 30, 2007 and 2006, respectively, and approximately 60 percent and 68 percent for the six months ended June 30, 2007 and 2006, respectively. Operating income for the three months ended June 30, 2007 grew compared to the same period in 2006 primarily due to higher income from partnerships, credit-linked notes and call and

tender activity (other yield enhancement income) and growth in the underlying business. For the six months ended June 30, 2007, operating income declined 2 percent compared to the same period in 2006 due to charges related to balance sheet reconciliation remediation, an industry-wide claims review in Japan, the effect of SOP 05-1 and realized capital losses.

Financial Services

AIG's Financial Services subsidiaries engage in diversified activities including aircraft and equipment leasing, capital markets, consumer finance and insurance premium finance.

Financial Services operating income increased in the three and six-month periods ended June 30, 2007 compared to the same periods of 2006 primarily due to differences in the accounting treatment for hedging activities. In the first quarter of 2007, AIGFP applied hedge accounting to certain of its interest rate swaps and foreign currency forward contracts hedging its investments and borrowings. In the second quarter of 2007, AGF and International Lease Finance Corporation (ILFC) began applying hedge accounting to most of their derivatives hedging interest rate and foreign currency denominated borrowings. Prior to 2007, hedge accounting under FAS 133 was not being applied to any of AIG's derivatives and related assets and liabilities. Accordingly, revenues and operating income were exposed to volatility resulting from differences in the timing of revenue recognition between the derivatives and the hedged assets and liabilities.

In the second quarter and first six months of 2007, the domestic consumer finance operations recorded pre-tax charges of $50 million and $178 million, respectively, representing the estimated cost of implementing the Supervisory Agreement entered into with the Office of Thrift Supervision (OTS), which are discussed in the Consumer Finance results of operations section.

Asset Management

AIG's Asset Management operations include institutional and retail asset management, broker-dealer services and institutional spread-based investment businesses. The Matched Investment Program (MIP) has replaced the GIC program as AIG's principal institutional spread-based investment activity.

Asset Management operating income increased for the three-month period ended June 30, 2007 compared to the same period in 2006 primarily due to higher investment gains, including a realized capital gain of $398 million on the sale of a portion of AIG's investment in Blackstone Group, LP in connection with its initial public offering. Asset Management operating income increased for the six-month period ended June 30, 2007 compared to the same period in 2006 due to the aforementioned investment gains as well as growth in both the Spread-Based Investment business and the Institutional Asset Management business. Gains and losses arising from the consolidation of certain partnerships, private equity investments and real estate funds are included in Operating income, but are offset in Minority interest expense, which is not a component of operating income.

Capital Resources

In the first six months of 2007, AIG issued $4.49 billion of junior subordinated debentures in four series of securities. Substantially all of the proceeds from these sales, net of expenses, are being used to repurchase shares of AIG's common stock.

At June 30, 2007, AIG had total consolidated shareholders' equity of $104.3 billion and total consolidated borrowings of $165.3 billion. At that date, $148.1 billion of such borrowings were not guaranteed by AIG, were matched borrowings by AIG Parent or AIGFP, or represented junior subordinated debt or liabilities connected to trust preferred stock.

In February 2007, AIG's Board of Directors increased AIG's share repurchase program by authorizing the repurchase of shares with an aggregate purchase price of $8 billion. Share repurchases during 2007 are described under Capital Resources and Liquidity — Share Repurchases and in Item 2. of Part II of this Quarterly Report on Form 10-Q.

Liquidity

AIG manages liquidity at both the subsidiary and parent company levels. At June 30, 2007, AIG's consolidated invested assets, primarily held by its subsidiaries, included $29.4 billion in cash and short-term investments. Consolidated net cash provided from operating activities in the first six months of 2007 amounted to $15.1 billion. Management believes that AIG's liquid assets, cash provided by operations and access to the capital markets will enable it to meet its anticipated cash requirements, including the funding of increased dividends under AIG's new dividend policy and repurchases of common stock.

Critical Accounting Estimates

AIG considers its most critical accounting estimates to be those relating to reserves for losses and loss expenses, future policy benefits for life and accident and health contracts, recoverability of DAC, estimated gross profits for investment-oriented products, fair value determinations for certain Capital Markets assets and liabilities, other-than-temporary declines in the value of investments and flight equipment recoverability. These accounting estimates require the use of assumptions about matters, some of which are highly uncertain at the time of estimation. To the extent actual experience differs from the assumptions used, AIG's results of operations would be directly affected.

Throughout this Management's Discussion and Analysis of Financial Condition and Results of Operations, AIG's

critical accounting estimates are discussed in detail. The major categories for which assumptions are developed and used to establish each critical accounting estimate are highlighted below.

Reserves for Losses and Loss Expenses (General Insurance):

- *Loss trend factors:* used to establish expected loss ratios for subsequent accident years based on premium rate adequacy and the projected loss ratio with respect to prior accident years.
- *Expected loss ratios for the latest accident year:* in this case, accident year 2007 for the loss reserve analyses updated through June 30, 2007. For low-frequency, high-severity classes such as excess casualty, expected loss ratios generally are utilized for at least the three most recent accident years.
- *Loss development factors:* used to project the reported losses for each accident year to an ultimate amount.
- *Reinsurance recoverable on unpaid losses:* the expected recoveries from reinsurers on losses that have not yet been reported and/or settled.

Future Policy Benefits for Life and Accident and Health Contracts (Life Insurance & Retirement Services):

- *Interest rates:* which vary by geographical region, year of issuance and products.
- *Mortality, morbidity and surrender rates:* based upon actual experience by geographical region modified to allow for variation in policy form, risk classification and distribution channel.

Estimated Gross Profits (Life Insurance & Retirement Services):

- *Estimated gross profits:* to be realized over the estimated duration of the contracts (investment-oriented products) affect the carrying value of DAC, unearned revenue liability and associated amortization patterns under FAS 97 and Sales Inducement Assets under Statement of Position 03-1, "Accounting and Reporting by Insurance Enterprises for Certain Nontraditional Long-Duration Contracts and for Separate Accounts" (SOP 03-1). Estimated gross profits include investment income and gains and losses on investments less required interest, actual mortality and other expenses.

Deferred Policy Acquisition Costs (Life Insurance & Retirement Services):

- *Recoverability:* based on current and future expected profitability, which is affected by interest rates, foreign exchange rates, mortality experience, and policy persistency.

Deferred Policy Acquisition Costs (General Insurance):

- *Recoverability and eligibility:* based upon the current terms and profitability of the underlying insurance contracts.

Fair Value Determinations Of Certain Assets And Liabilities (Financial Services):

- *Valuation models:* utilizing factors, such as market liquidity and current interest, foreign exchange and volatility rates.
- *Market price data:* AIG attempts to secure reliable and independent current market price data, such as published exchange rates from external subscription services such as Bloomberg or Reuters or third-party broker quotes for use in its models. When such data is not available, AIG uses an internal methodology, which includes interpolation and extrapolation from verifiable recent prices.

Other-Than-Temporary Declines In The Value Of Investments:

A security is considered a candidate for other-than-temporary impairment if it meets any of the following criteria:

- Trading at a significant (25 percent or more) discount to par or amortized cost (if lower) for an extended period of time (nine months or longer);
- The occurrence of a discrete credit event resulting in the debtor defaulting or seeking bankruptcy or insolvency protection or voluntary reorganization; or
- The probability of non-realization of a full recovery on its investment, irrespective of the occurrence of one of the foregoing events.

At each balance sheet date, AIG evaluates its securities holdings in an unrealized loss position. Where AIG does not intend to hold such securities until they have fully recovered their carrying value, based on the circumstances present at the date of evaluation, AIG records the unrealized loss in income. If events or circumstances change, such as unexpected changes in the creditworthiness of the obligor, unanticipated changes in interest rates, tax laws, statutory capital positions and unforeseen liquidity events, among others, AIG revisits its intent. Further, if a loss is recognized from a sale subsequent to a balance sheet date pursuant to these unexpected changes in circumstances, the loss is recognized in the period in which the intent to hold the securities to recovery no longer exists.

In periods subsequent to the recognition of an other-than-temporary impairment loss for debt securities, AIG amortizes the discount or reduced premium over the remaining life of the security in a prospective manner based on the amount and timing of estimated future cash flows.

Flight Equipment — Recoverability (Financial Services):

- *Expected undiscounted future net cash flows:* based upon current lease rates, projected future lease rates and estimated terminal values of each aircraft based on third party information.

Operating Review

General Insurance Operations

AIG's General Insurance subsidiaries are multiple line companies writing substantially all lines of property and casualty insurance and various personal lines both domestically and abroad.

Domestic General Insurance operations are comprised of DBG, Reinsurance, Personal Lines and Mortgage Guaranty businesses.

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

Transatlantic Holdings, Inc. (Transatlantic) subsidiaries offer reinsurance capacity on both a treaty and facultative basis both in the U.S. and abroad. Transatlantic structures programs for a full range of property and casualty products with an emphasis on specialty risk.

AIG's Personal Lines operations provide automobile insurance through AIG Direct, a mass marketing operation, the Agency Auto Division and 21st Century, as well as a broad range of coverages for high net worth individuals through the AIG Private Client Group.

The main business of the UGC subsidiaries is the issuance of residential mortgage guaranty insurance on conventional first-lien mortgages for the purchase or refinance of one to four family residences. UGC subsidiaries also write second-lien and private student loan guaranty insurance.

AIG's Foreign General Insurance group accepts risks primarily underwritten through American International Underwriters (AIU), a marketing unit consisting of wholly owned agencies and insurance companies. The Foreign General Insurance group also includes business written by AIG's foreign-based insurance subsidiaries.

General Insurance Results

General Insurance operating income is comprised of statutory underwriting results, changes in DAC, net investment income and net realized capital gains and losses.

Operating income, as well as net premiums written, net premiums earned, net investment income and net realized capital gains (losses) and statutory ratios were as follows:

(in millions, except ratios)	Three Months Ended June 30, **2007**	2006	Percentage Increase/ (Decrease)	Six Months Ended June 30, **2007**	2006	Percentage Increase/ (Decrease)
Net premiums written:						
Domestic General						
DBG	**$ 6,439**	$ 6,476	(1)%	**$12,448**	$12,336	1%
Transatlantic[(a)]	**983**	914	8	**1,967**	1,828	8
Personal Lines	**1,203**	1,180	2	**2,432**	2,378	2
Mortgage Guaranty	**272**	193	41	**538**	390	38
Foreign General[(a)]	**3,242**	2,871	13	**6,860**	5,957	15
Total	**$12,139**	$11,634	4%	**$24,245**	$22,889	6%
Net premiums earned:						
Domestic General						
DBG	**$ 5,996**	$ 5,818	3%	**$11,977**	$11,587	3%
Transatlantic[(a)]	**948**	909	4	**1,913**	1,817	5
Personal Lines	**1,168**	1,167	–	**2,323**	2,326	–
Mortgage Guaranty	**221**	179	23	**431**	345	25
Foreign General[(a)]	**3,030**	2,605	16	**5,938**	5,073	17
Total	**$11,363**	$10,678	6%	**$22,582**	$21,148	7
Net investment income:						
Domestic General						
DBG	**$ 984**	$ 813	21%	**$ 2,017**	$ 1,558	29
Transatlantic	**119**	108	10	**235**	210	12
Personal Lines	**57**	55	4	**114**	112	2
Mortgage Guaranty	**39**	36	8	**76**	68	12
Foreign General[(b)]	**427**	602	(29)	**746**	784	(5)
Reclassifications and Eliminations	**2**	–	–	**3**	–	–
Total	**$ 1,628**	$ 1,614	1%	**$ 3,191**	$ 2,732	17%
Net realized capital gains (losses)	**$ (63)**	$ (125)	(50)%	**$ 58**	$ (57)	–%
Operating Income (loss)[(c)]:						
Domestic General						
DBG	**$ 1,904**	$ 1,474	29%	**$ 3,833**	$ 2,779	38%
Transatlantic	**168**	143	17	**319**	284	12
Personal Lines	**118**	118	–	**224**	219	2
Mortgage Guaranty	**(81)**	107	–	**(73)**	216	–
Foreign General[(b)(d)(e)]	**867**	1,021	(15)	**1,776**	1,694	5
Reclassifications and Eliminations	**–**	–	–	**(7)**	2	–
Total	**$ 2,976**	$ 2,863	4%	**$ 6,072**	$ 5,194	17%
Statutory underwriting profit (loss)[(c)(f)]:						
Domestic General						
DBG	**$ 946**	$ 641	48%	**$ 1,730**	$ 1,125	54%
Transatlantic	**37**	33	12	**53**	63	(16)
Personal Lines	**56**	53	6	**89**	93	(4)
Mortgage Guaranty	**(126)**	73	–	**(168)**	143	–
Foreign General[(d)(e)]	**371**	423	(12)	**773**	756	2
Total	**$ 1,284**	$ 1,223	5%	**$ 2,477**	$ 2,180	14%
Domestic General[(c)]:						
Loss Ratio	**68.2**	68.6		**68.5**	70.1	
Expense Ratio	**19.6**	19.8		**20.3**	20.0	
Combined Ratio	**87.8**	88.4		**88.8**	90.1	
Foreign General[(c)]:						
Loss Ratio[(a)(e)]	**52.1**	47.1		**51.4**	48.9	
Expense Ratio[(d)]	**33.3**	33.3		**30.8**	30.8	
Combined ratio	**85.4**	80.4		**82.2**	79.7	
Consolidated[(d)]:						
Loss Ratio	**63.9**	63.4		**64.0**	65.0	
Expense Ratio	**23.2**	23.1		**23.3**	22.8	
Combined Ratio	**87.1**	86.5		**87.3**	87.8	

(a) Income statement accounts expressed in non-functional currencies are translated into U.S. dollars using average exchange rates.

(b) The three and six-month periods ended June 30, 2006 include increases of $412 million and $386 million, respectively, relating to an out of period UCITS adjustment recorded in the second quarter of 2006.

(c) Includes additional losses incurred and net reinstatement premiums related to prior year catastrophes of $18 million and $(51) million in the three-month periods ended June 30, 2007 and 2006, respectively, and $53 million and $48 million in the six-month periods ended June 30, 2007 and 2006, respectively.

(d) Includes the results of wholly owned Foreign General agencies.

(e) Includes losses incurred and net reinstatement premiums related to current year catastrophes of $68 million in both the three and six-month periods ended June 30, 2007.

(f) Statutory underwriting profit (loss) is a measure that U.S. domiciled insurance companies are required to report to their regulatory authorities. The following table reconciles statutory underwriting profit (loss) to operating income for General Insurance:

(in millions)	Domestic Brokerage Group	Transatlantic	Personal Lines	Mortgage Guaranty	Foreign General	Reclassifications and Eliminations	Total
Three Months Ended June 30, 2007:							
Statutory underwriting profit (loss)	**$ 946**	**$ 37**	**$ 56**	**$(126)**	**$ 371**	**$ –**	**$ 1,284**
Increase (decrease) in DAC	**50**	**10**	**7**	**9**	**51**	**–**	**127**
Net investment income	**984**	**119**	**57**	**39**	**427**	**2**	**1,628**
Net realized capital gains (losses)	**(76)**	**2**	**(2)**	**(3)**	**18**	**(2)**	**(63)**
Operating income (loss)	**$1,904**	**$168**	**$118**	**$ (81)**	**$ 867**	**$ —**	**$ 2,976**
Three Months Ended June 30, 2006:							
Statutory underwriting profit (loss)	$ 641	$ 33	$ 53	$ 73	$ 423	$ –	$ 1,223
Increase (decrease) in DAC	64	4	9	1	73	–	151
Net investment income	813	108	55	36	602	–	1,614
Net realized capital gains (losses)	(44)	(2)	1	(3)	(77)	–	(125)
Operating income (loss)	$1,474	$143	$118	$ 107	$1,021	$ –	$ 2,863
Six Months Ended June 30, 2007:							
Statutory underwriting profit (loss)	**$1,730**	**$ 53**	**$ 89**	**$(168)**	**$ 773**	**$ –**	**$ 2,477**
Increase (decrease) in DAC	**85**	**14**	**22**	**21**	**204**	**–**	**346**
Net investment income	**2,017**	**235**	**114**	**76**	**746**	**3**	**3,191**
Net realized capital gains (losses)	**1**	**17**	**(1)**	**(2)**	**53**	**(10)**	**58**
Operating income (loss)	**$3,833**	**$319**	**$224**	**$ (73)**	**$1,776**	**$ (7)**	**$ 6,072**
Six Months Ended June 30, 2006:							
Statutory underwriting profit (loss)	$1,125	$ 63	$ 93	$ 143	$ 756	$ –	$ 2,180
Increase (decrease) in DAC	93	7	14	8	217	–	339
Net investment income	1,558	210	112	68	784	–	2,732
Net realized capital gains (losses)	3	4	–	(3)	(63)	2	(57)
Operating income (loss)	$2,779	$284	$219	$ 216	$1,694	$ 2	$ 5,194

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

	Three Months Ended June 30,		Six Months Ended June 30,	
	2007	2006	**2007**	2006
Growth in original currency*	**3.3%**	9.7%	**4.7%**	7.9%
Foreign exchange effect	**1.0**	(0.4)	**1.2**	(1.1)
Growth as reported in U.S. dollars	**4.3%**	9.3%	**5.9%**	6.8%

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

Quarterly General Insurance Results

General Insurance operating income increased in the three months ended June 30, 2007 compared to the same period in 2006. The 2007 combined ratio increased to 87.1, an increase of 0.6 points over 2006, including an increase in the loss ratio of 0.5 points. Prior year development and increases in the loss reserve discount reduced incurred losses by $212 million and $248 million for the three months ended June 30, 2007 and 2006, respectively, accounting for 0.5 points of the increase. The loss ratio for accident year 2007 recorded in the three months ended June 30, 2007 was substantially the same as the loss ratio recorded in the three months ended June 30, 2006 for accident year 2006, despite a $68 million loss from the June 2007 U.K. floods and an increase in Mortgage Guaranty losses in the 2007 period. The downward cycle in the U.S. housing market is not expected to improve until residential inventories return to a more normal level, and AIG expects that this downward cycle will continue to adversely affect UGC's loss ratios for the foreseeable future. Net premiums written increased for the three months ended June 30, 2007 compared to the same period in 2006, driven by Foreign General growth from both established and new distribution channels and the effect of changes in foreign currency exchange rates.

General Insurance net investment income was essentially unchanged for the three months ended June 30, 2007 compared to the same period in 2006. Interest and dividend income increased $138 million for the second quarter of 2007 compared to the same period in 2006 as investment in fixed maturities and equity securities increased by $11.9 billion and the yield on interest earning investments remained consistent at 4.6 percent. Income from partnership investments increased $120 million for the three months ended June 30, 2007 compared to the same period in 2006, primarily due to improved returns on underlying investments. Other investment income decreased $250 million, primarily

due to the effect of the $432 million out of period adjustment related to the accounting for UCITS recorded in 2006.

Year-to-Date General Insurance Results

General Insurance operating income increased for the first six months of 2007 compared to the same period in 2006 due to growth in net investment income and an increase in underwriting profit, which is reflected in the combined ratio. The combined ratio improved to 87.3, a reduction of 0.5 points from 2006, including an improvement in the loss ratio of 1.0 point. Prior year development and increases in the loss reserve discount reduced incurred losses by $343 million and $213 million for the first six months of 2007 and 2006, respectively, accounting for 0.5 points of the improvement in the loss ratio. The loss ratio for accident year 2007 recorded in the first six months of 2007 was 0.5 points lower than the loss ratio recorded in the first six months of 2006 for accident year 2006, despite the loss from the June 2007 U.K. floods and an increase in Mortgage Guaranty losses in the 2007 period.

General Insurance net premiums written increased in the first six months of 2007 compared to the same period in 2006, reflecting growth in Foreign General from both established and new distribution channels, the effect of changes in foreign currency exchange rates, and growth in Mortgage Guaranty, primarily from international business.

General Insurance net investment income increased in the first six months of 2007 to $3.2 billion. Interest and dividend income increased $333 million for the first six months of 2007 compared to the same period of 2006 as fixed maturities and equity securities increased by $11.9 billion and the yield remained consistent at 4.6 percent. Income from partnership investments increased $302 million for the first six months of 2007 compared to the same period in 2006, primarily due to improved returns on underlying investments and higher levels of invested assets, which increased by $1.3 billion. Other investment income decreased by $154 million, which reflects the effect of the $405 million out of period UCITS adjustment recorded in 2006. See also Capital Resources and Liquidity — Liquidity and Invested Assets herein.

In order to better align financial reporting with the manner in which AIG's chief operating decision makers have managed their businesses, commencing in the first quarter of 2007, the foreign aviation business, which was historically reported in DBG, is now being reported as part of Foreign General, and the oil rig and marine businesses, which were historically reported in Foreign General, are now being reported as part of DBG. Prior period amounts have been revised to conform to the current presentation.

Quarterly DBG Results

DBG's operating income increased in the three months ended June 30, 2007 compared to the same period of 2006. The improvement is also reflected in the combined ratio, which declined 3.9 points in the three months ended June 30, 2007 compared to the same period of 2006 primarily due to an improvement in the loss ratio of 3.8 points. The loss ratio for accident year 2007 recorded in the three months ended June 30, 2007 was 2.4 points lower than the loss ratio recorded in the same period of 2006 for accident year 2006. Prior year development and increases in the loss reserve discount reduced incurred losses by $190 million and $106 million for the three months ended June 30, 2007 and 2006, respectively, accounting for 1.4 points of the improvement.

DBG's net premiums written declined for the three months ended June 30, 2007 compared to the same period in 2006 due to an increase in ceded premiums and declines in premium rates in casualty lines of business. These declines were partially offset by the renewal of a property reinsurance treaty in 2007 at rates lower than the expiring treaty, resulting in a $52 million increase in net premiums written. Ceded premiums as a percentage of gross written premiums increased to 26 percent for the three months ended June 30, 2007 compared to 24 percent in the same period in 2006, primarily due to additional reinsurance for property risks to manage catastrophe exposures.

DBG's expense ratio decreased to 17.5 for the three months ended June 30, 2007 compared to 17.7 in the same period in 2006, primarily due to a decrease in charges related to remediation of the material weakness in balance sheet reconciliations which included a $32 million out of period charge in the second quarter of 2006. This decline was partially offset by increases in expenses for marketing initiatives in 2007.

DBG's net investment income increased for the three months ended June 30, 2007 compared to the same period in 2006, as interest income increased $95 million for the three months ended June 30, 2007, on growth in the bond portfolio resulting from investment of operating cash flows and capital contributions. Income from partnership investments increased $44 million for the three months ended June 30, 2007 compared to the same period in 2006, primarily due to improved returns on the underlying investments.

Year-to-date DBG Results

DBG's operating income increased for the first six months of 2007 compared to the same period in 2006. The improvement is also reflected in the combined ratio, which declined 4.3 points in the first six months of 2007 compared to the same period in 2006, primarily due to an improvement

in the loss ratio of 4.5 points. The loss ratio for accident year 2007 recorded for the first six months of 2007 was 2.5 points lower than the loss ratio recorded in the same period of 2006 for accident year 2006. Prior year development and increases in the loss reserve discount reduced incurred losses by $277 million and $32 million for the three months ended June 30, 2007 and 2006, respectively, accounting for 2.0 points of the improvement.

DBG's net premiums written increased in the first six months of 2007 compared to the same period of 2006 due to the strength of AIG's capacity, commitment during challenging market conditions, diverse product offerings and the acquisition of TravelGuard, which markets accident and health products. Ceded premiums as a percentage of gross written premiums increased to 25 percent in the first six months of 2007 compared to 23 percent for the same period in 2006, primarily due to additional reinsurance for property risks to manage catastrophe exposures.

DBG's expense ratio increased to 18.3 for the first six months in 2007 compared to 18.1 in the same period of 2006, due to increases in operating expenses for marketing initiatives and operations as well as changes in the mix of business towards products with lower loss ratios and higher expense ratios.

DBG's net investment income increased for the first six months of 2007 compared to the same period in 2006, as interest income increased $225 million for the six months ended June 30, 2007, on growth in the bond portfolio resulting from investment of operating cash flows and capital contributions. Income from partnership investments increased $199 million for the first six months of 2007 compared to the same period in 2006, primarily due to improved returns on the underlying investments.

Quarterly Transatlantic Results

Transatlantic's net premiums written and net premiums earned increased for the three months ended June 30, 2007 compared to the same period in 2006 due primarily to increased writings in domestic and international operations. Statutory underwriting profit increased due to improved underwriting results from European operations for the three months ended June 30, 2007 compared to the same period in 2006. Operating income increased for the three months ended June 30, 2007 compared to the same period in 2006 due to increased net investment income and improved underwriting results.

Year-to-date Transatlantic Results

Transatlantic's net premiums written and net premiums earned increased for the first six months of 2007 compared to the same period in 2006 due primarily to increased writings in domestic operations. Statutory underwriting profit was adversely affected by European windstorm and flood losses and storms in Australia, partially offset by lower net adverse development for the six months ended June 30, 2007 compared to the same period in 2006, resulting in an overall decline in statutory underwriting profit for the 2007 period. Operating income increased for the first six months of 2007 compared to the same period in 2006 as increased net investment income and net realized capital gains more than offset the decline in underwriting results.

Quarterly Personal Lines Results

Personal Lines operating income in the three months ended June 30, 2007 compared to the same period of 2006 was unchanged, and reflected a reduction in the loss ratio of 0.5 points. The loss ratio for accident year 2007 recorded for the three months ended June 30, 2007 was 1.5 points lower than the loss ratio recorded for the same period in 2006 for accident year 2006. Prior year development reduced incurred losses by $32 million and $43 million for the three months ended June 30, 2007 and 2006, respectively, increasing the 2007 loss ratio by 1.0 point relative to the 2006 loss ratio. The improvement in the accident year loss ratio is primarily due to favorable loss trends and growth in the Private Client Group. The improvement in the loss ratio along with a decrease in the expense ratio of 0.26 points resulted in an overall improvement of the combined ratio of 0.73 points.

Net premiums written increased 1.9 percent for the three months ended June 30, 2007 compared to the same period in 2006 due to continued growth in the Private Client Group, partially offset by an 11 percent reduction in Agency Auto.

On May 15, 2007, AIG and 21st Century Insurance Group entered into a definitive merger agreement providing that AIG will acquire the 21st Century shares it does not currently own at a price of $22.00 per share in cash, for a total purchase price of approximately $813 million. AIG already owns, through its subsidiaries, approximately 60.8 percent of the outstanding shares of 21st Century. Upon completion of the transaction, 21st Century will become a wholly owned subsidiary of AIG.

The merger is expected to be completed in the third quarter of 2007, subject to customary conditions and approvals. The exact time is dependent on the review and clearance of necessary filings with the SEC, which are in process. The transaction is subject to the affirmative vote of the holders of the majority of the outstanding shares of 21st Century. AIG has agreed to vote or cause to be voted all of its and its subsidiaries' 21st Century shares in favor of the merger.

Year-to-date Personal Lines Results

The modest increase in Personal Lines operating income in the first six months of 2007 compared to the same period of 2006 reflects a reduction in the loss ratio of 1.0 point. The loss ratio for accident year 2007 recorded for the first six

months of 2007 was 1.0 point lower than the loss ratio recorded in the same period of 2006 for accident year 2006. Prior year development reduced incurred losses by $61 million and $62 million for the six months ended June 30, 2007 and 2006, respectively, resulting in a negligible change in the loss ratio between the periods. The improvement in the accident year loss ratio was primarily due to favorable loss trends and growth in the Private Client Group, partially offset by increased losses in 21st Century. The improvement in the loss ratio was partially offset by an increase in the expense ratio of 0.6 points, primarily due to increased acquisition expenses in connection with the 21st Century merger, growth in the Private Client Group, and reduced premium writings in Agency Auto.

Net premiums written increased 2.3 percent for the first six months of 2007 compared to the same period in 2006 due to continued growth in the Private Client Group and a modest increase in the Direct business, partially offset by a 10 percent reduction in Agency Auto.

Quarterly Mortgage Guaranty Results

The significant decline in Mortgage Guaranty operating income for the three months ended June 30, 2007 compared to the same period in 2006 was due primarily to unfavorable loss experience in both the domestic first and second-lien businesses as a result of the continued softening in the U.S. housing market. Losses incurred were up significantly across all lines of the domestic Mortgage Guaranty business. UGC's consolidated loss ratio for the three months ended June 30, 2007 was 129.9 compared to a loss ratio of 33.1 for the same period in 2006. Prior year development reduced incurred losses by $4 million and $52 million for the three months ended June 30, 2007 and 2006, respectively, increasing the 2007 loss ratio by 27.6 points relative to the 2006 loss ratio.

Net premiums written increased 41 percent in the three months ended June 30, 2007 compared to the same period in 2006 as international premiums were up $50 million, accounting for 26 points of the increase in net premiums written. In addition, first-lien premiums increased by $23 million due to increased use of mortgage insurance for credit enhancement and improved persistency. Although UGC discontinued accepting new business for the poorly performing third-party originated second-lien product in the fourth quarter of 2006, UGC will continue to receive renewal premiums on the existing portfolio for the life of the loans, estimated to be three to five years. The expense ratio of 22.4 in the three months ended June 30, 2007 declined from 24.7 in the same period of 2006 as premium growth offset expenses related to UGC's international expansion and additional operational resources in the second-lien and private education loan businesses.

UGC's domestic mortgage net risk in force totaled $25.9 billion as of June 30, 2007 with a 60-day delinquency ratio of 2.5 percent (based on number of policies, consistent with mortgage insurance industry practice). A significant portion of the mortgage risk is secured by first liens on single family, owner-occupied properties.

Year-to-date Mortgage Guaranty Results

The significant decline in Mortgage Guaranty operating income in the first six months of 2007 compared to the same period in 2006 was due primarily to the unfavorable loss experience in both the domestic first and second-lien businesses. The third-party originated second-lien product continued to perform poorly. UGC's consolidated loss ratio for the first six months was 111.5 compared to a loss ratio of 31.8 for the same period in 2006. Prior year development increased incurred losses by $27 million in the first six months of 2007 compared to a reduction of $65 million for the same period in 2006, accounting for 25 points of the increase in the loss ratio.

Net premiums written increased 38 percent in the first six months of 2007 compared to the same period in 2006 as international premiums grew $85 million, accounting for 22 points of the increase in net premiums written. In addition, domestic first-lien premiums increased $36 million for the six months ended June 30, 2007 compared to the same period in 2006 due to the increased use of mortgage insurance for credit enhancement as well as improved persistency. The expense ratio of 22.1 in the first six months of 2007 declined from 23.7 for the same period in 2006 as premium growth offset expenses related to UGC's international expansion and additional operational resources in the second-lien and private education loan businesses.

Quarterly Foreign General Insurance Results

Foreign General's operating income decreased in the three months ended June 30, 2007 compared to the same period in 2006 due to decreases in statutory underwriting profit and net investment income, partially offset by increases due to the effect of changes in the currency exchange rates of the Euro and the British Pound. Statutory underwriting profit decreased due to a $68 million loss from the June 2007 U.K. floods. Net investment income in the prior year quarter included the $412 million out of period UCITS adjustment.

Net premiums written increased 13 percent (9 percent in original currency) for the three months ended June 30, 2007 compared to the same period in 2006, reflecting growth in commercial and consumer lines driven by new business from both established and new distribution channels, including Central Insurance Co. Ltd. in Taiwan, and by greater retention of commercial lines accounts on renewal. Growth in consumer lines in Latin America and Europe and commercial lines in Europe and the U.K. also contributed to

the increase. Net premiums written also increased by one percent compared to the same period in 2006 due to decreases in the use of reinsurance. Net premiums written by the Lloyd's syndicate Ascot increased for the three months ended June 30, 2007 compared to the same period in 2006. Net premiums written for Aviation declined due to rate decreases resulting from increased market competition.

The loss ratio increased 5 points for the three months ended June 30, 2007 compared to the same period in 2006. The 2007 loss ratio increased 2.2 points due to the losses from the U.K. floods and increased 0.6 points due to higher asbestos and environmental reserves relating to one case. The 2007 and 2006 loss ratios benefited from favorable loss development on prior accident years, by 0.8 points and 2.7 points, respectively.

The expense ratio was unchanged for the three months ended June 30, 2007 compared to the same period in 2006. The 2006 expense ratio reflected a profit commission adjustment in Ascot which increased the second quarter 2006 expense ratio by 1.2 points. The comparable increase in the expense ratio in 2007 resulted from higher commission costs and higher operating expenses due to new business initiatives and the cost of realigning certain legal entities through which Foreign General operates. AIG expects the expense ratio to increase during the remainder of 2007 due to the underlying seasonality of renewals and as the consumer lines of business, which have higher acquisition costs, increase in significance as a component of net premiums written.

Net investment income decreased for the three months ended June 30, 2007 compared to the same period in 2006, as the 2006 period included the out of period UCITS adjustment, which more than offset underlying growth of $237 million in net investment income. Net investment income for the second quarter of 2007 reflected higher interest rates, strong cash flows and increased equity mutual fund and partnership income. Equity mutual fund income was $130 million higher than the same quarter last year reflecting the strong performance in the equity markets, and partnership income was $69 million higher than prior year quarter due to strong infrastructure fund performance in Africa, Europe and Latin America.

Year-to-date Foreign General Insurance Results

Foreign General's operating income increased in the first six months of 2007 compared to the same period in 2006, due to the effect of changes in the currency exchange rates of the Euro and the British Pound and increased net realized capital gains.

Net premiums written increased 15 percent (11 percent in original currency) for the six months ended June 30, 2007 compared to the same period in 2006, reflecting growth in commercial and consumer lines driven by new business from both established and new distribution channels, including a wholly owned insurance company in Vietnam and Central Insurance Co., Ltd. in Taiwan, and by greater retention of commercial lines accounts on renewal. Growth in consumer lines in Latin America and commercial lines in Europe and the U.K. also contributed to the increase. Net premiums written also increased by one percent from the same period in 2006 due to decreases in the use of reinsurance.

The loss ratio increased 2.5 points for the six months ended June 30, 2007 compared to the same period in 2006. The 2007 loss ratio increased 1.1 points due to the losses from the U.K. floods and increased 0.7 points due to severe but non-catastrophic losses. The 2007 and 2006 loss ratios benefited from favorable loss development on prior accident years by 1.5 points and 2.1 points, respectively.

The expense ratio was unchanged in the six months ended June 30, 2007 compared to the same period in 2006. The expense ratio for 2006 increased by 1.5 points due to a profit commission charge in Ascot and an out of period charge for amortization of deferred advertising costs. This increase in the 2006 expense ratio was offset by higher commission costs and higher operating expenses due to new business initiatives and the realignment costs mentioned above.

Net investment income decreased for the six months ended June 30, 2007 compared to the same period in 2006, as the 2006 period reflected the out of period UCITS adjustment, which more than offset underlying growth of $348 million in net investment income. Net investment income for the first six months of 2007 reflected higher interest rates, strong cash flows and increased equity mutual fund and partnership income. Equity mutual fund income increased $156 million for the six months ended June 30, 2007 compared to the same period in 2006 reflecting strong performance in the equity markets and partnership income increased $94 million for the six months ended June 30, 2007 compared to the same period in 2006 due to strong infrastructure fund performance in Africa, Europe and Latin America.

Reserve for Losses and Loss Expenses

The following table presents the components of the General Insurance gross reserve for losses and loss expenses (loss reserves) as of June 30, 2007 and December 31, 2006 by major line of business on a statutory Annual Statement basis[a]:

(in millions)	**June 30, 2007**	December 31, 2006[b]
Other liability occurrence	**$19,961**	$19,327
Workers compensation	**14,502**	13,612
Other liability claims made	**13,470**	12,513
Auto liability	**6,137**	6,070
International	**6,100**	6,006
Property	**4,629**	5,499
Reinsurance	**3,152**	2,979
Medical malpractice	**2,330**	2,347
Products liability	**2,181**	2,239
Accident and health	**1,851**	1,693
Commercial multiple peril	**1,744**	1,651
Aircraft	**1,698**	1,629
Fidelity/surety	**1,248**	1,148
Other	**3,076**	3,286
Total	**$82,079**	$79,999

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

[b] *Allocations among various lines were revised from the previous presentation.*

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

At June 30, 2007, General Insurance net loss reserves were $65.20 billion, an increase of $2.57 billion from the prior year-end. The net loss reserves represent loss reserves reduced by reinsurance recoverables, net of an allowance for unrecoverable reinsurance and applicable discount for future investment income.

The following table classifies the components of the General Insurance net loss reserves by business unit:

(in millions)	**June 30, 2007**	December 31, 2006
DBG[a]	**$45,650**	$44,119
Transatlantic	**6,451**	6,207
Personal Lines[b]	**2,304**	2,440
Mortgage Guaranty	**718**	460
Foreign General[c]	**10,074**	9,404
Total Net Loss Reserve	**$65,197**	$62,630

(a) *At June 30, 2007 and December 31, 2006, respectively, DBG loss reserves include approximately $3.23 billion and $3.33 billion ($3.50 billion and $3.66 billion, respectively, before discount), related to business written by DBG but ceded to American International Reinsurance Company Limited (AIRCO) and reported in AIRCO's statutory filings. DBG loss reserves also include approximately $601 million and $535 million related to business included in American International Underwriters Overseas, Ltd.'s (AIUO) statutory filings at June 30, 2007 and December 31, 2006, respectively.*

(b) *At June 30, 2007 and December 31, 2006, respectively, Personal Lines loss reserves include $826 million and $861 million related to business ceded to DBG and reported in DBG's statutory filings.*

(c) *At June 30, 2007 and December 31, 2006, respectively, Foreign General loss reserves include approximately $2.90 billion and $2.75 billion related to business reported in DBG's statutory filings.*

The DBG net loss reserve of $45.7 billion is comprised principally of the business of AIG subsidiaries participating in the American Home Assurance Company (American Home)/ National Union Fire Insurance Company of Pittsburgh, Pa. (National Union) pool (11 companies) and the surplus lines pool (Lexington, Starr Excess Liability Insurance Company and Landmark Insurance Company).

DBG cedes a quota share percentage of its other liability occurrence and products liability occurrence business to AIRCO. The quota share percentage ceded was 15 percent for the six months ended June 30, 2007 and 20 percent for the year 2006 and covered all business written in these years for these lines by participants in the American Home/ National Union pool. AIRCO's loss reserves relating to these quota share cessions from DBG are recorded on a discounted basis. As of June 30, 2007, AIRCO carried a discount of approximately $270 million applicable to the $3.50 billion in undiscounted reserves it assumed from the American Home/ National Union pool via this quota share cession. AIRCO also carries approximately $503 million in net loss reserves relating to Foreign General insurance business. These reserves are carried on an undiscounted basis.

The companies participating in the American Home/ National Union pool have maintained a participation in the business written by AIU for decades. As of June 30, 2007, these AIU reserves carried by participants in the American Home/National Union pool totaled approximately $2.90 billion. The remaining Foreign General reserves are carried by AIUO, AIRCO, and other smaller AIG subsidiaries domiciled outside the United States. Statutory filings in the U.S. by AIG companies reflect all the business written by

U.S. domiciled entities only, and therefore exclude business written by AIUO, AIRCO, and all other internationally domiciled subsidiaries. The total reserves carried at June 30, 2007 by AIUO and AIRCO were approximately $4.57 billion and $3.73 billion, respectively. AIRCO's $3.73 billion in total general insurance reserves consist of approximately $3.23 billion from business assumed from the American Home/National Union pool and an additional $503 million relating to Foreign General Insurance business.

Discounting of Reserves

At June 30, 2007, AIG's overall General Insurance net loss reserves reflect a loss reserve discount of $2.39 billion, including tabular and non-tabular calculations. The tabular workers compensation discount is calculated using a 3.5 percent interest rate and the 1979-81 Decennial Mortality Table. The non-tabular workers compensation discount is calculated separately for companies domiciled in New York and Pennsylvania, and follows the statutory regulations for each state. For New York companies, the discount is based on a five percent interest rate and the companies' own payout patterns. For Pennsylvania companies, the statute has specified discount factors for accident years 2001 and prior, which are based on a six percent interest rate and an industry payout pattern. For accident years 2002 and subsequent, the discount is based on the yield of U.S. Treasury securities ranging from one to twenty years and the company's own payout pattern, with the future expected payment for each year using the interest rate associated with the corresponding Treasury security yield for that time period. The discount is comprised of the following: $726 million – tabular discount for workers compensation in DBG; $1.39 billion – non-tabular discount for workers compensation in DBG; and, $270 million – non-tabular discount for other liability occurrence and products liability occurrence in AIRCO. The total undiscounted workers compensation loss reserve carried by DBG is approximately $12.2 billion as of June 30, 2007. The other liability occurrence and products liability occurrence business in AIRCO that is assumed from DBG is discounted based on the yield of U.S. Treasury securities ranging from one to twenty years and the DBG payout pattern for this business. The undiscounted reserves assumed by AIRCO from DBG totaled approximately $3.50 billion at June 30, 2007.

Quarterly Reserving Process

Management believes that the General Insurance net loss reserves are adequate to cover General Insurance net losses and loss expenses as of June 30, 2007. While AIG regularly reviews the adequacy of established loss reserves, there can be no assurance that AIG's ultimate loss reserves will not develop adversely and materially exceed AIG's loss reserves as of June 30, 2007. In the opinion of management, such adverse development and resulting increase in reserves is not likely to have a material adverse effect on AIG's consolidated financial condition, although it could have a material adverse effect on AIG's consolidated results of operations for an individual reporting period.

The following table presents the reconciliation of net loss reserves:

	Three Months Ended June 30,		Six Months Ended June 30,	
(in millions)	**2007**	2006	**2007**	2006
Net reserve for losses and loss expenses at beginning of period	**$64,034**	$58,892	**$62,630**	$57,476
Foreign exchange effect	**252**	370	**214**	487
Losses and loss expenses incurred:				
Current year	**7,334**	6,911	**14,549**	13,752
Prior years, other than accretion of discount	**(120)**	(248)	**(268)**	(213)
Prior years, accretion of discount	**12**	101	**128**	202
Losses and loss expenses incurred	**7,226**	6,764	**14,409**	13,741
Losses and loss expenses paid	**6,315**	5,812	**12,056**	11,490
Net reserve for losses and loss expenses at end of period	**$65,197**	$60,214	**$65,197**	$60,214

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

	Three Months Ended June 30,		Six Months Ended June 30,	
(in millions)	**2007**	2006	**2007**	2006
Prior Accident Year Development by Reporting Unit:				
DBG	**$ (65)**	$ (106)	**$ (152)**	$ (32)
Personal Lines	**(32)**	(43)	**(61)**	(62)
Mortgage Guaranty	**(4)**	(52)	**27**	(64)
Foreign General	**(4)**	(77)	**(68)**	(120)
Subtotal	**(105)**	(278)	**(254)**	(278)
Transatlantic	**18**	30	**36**	65
Asbestos settlements*	**(33)**	–	**(50)**	–
Prior years, other than accretion of discount	**$ (120)**	$ (248)	**$ (268)**	$ (213)

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

(in millions)	Calendar Year 2007	2006
Prior Accident Year Development by Accident Year:		
2006	**$ (454)**	
2005	**(165)**	$ (302)
2004	**(136)**	(259)
2003	**15**	(214)
2002	**112**	61
2001 & prior	**360**	501
Prior years, other than accretion of discount	**$ (268)**	$ (213)

In determining the quarterly loss development from prior accident years, AIG conducts analyses to determine the change in estimated ultimate loss for each accident year for each profit center. For example, if loss emergence for a profit center is different than expected for certain accident years, the actuaries examine the indicated effect such emergence would have on the reserves of that profit center. In some cases, the higher or lower than expected emergence may result in no clear change in the ultimate loss estimate for the accident years in question, and no adjustment would be made to the profit center's reserves for prior accident years. In other cases, the higher or lower than expected emergence may result in a larger change, either favorable or unfavorable, than the difference between the actual and expected loss emergence. Such additional analyses were conducted for each profit center, as appropriate, in the second quarter of 2007 to determine the loss development from prior accident years for the second quarter of 2007. As part of its quarterly reserving process, AIG also considers notices of claims received with respect to emerging issues, such as those related to stock option backdating. Also as part of the quarterly reserving process, beginning with the second quarter of 2007, AIG updated its analysis of the loss reserve discount pertaining to workers compensation reserves. Historically, this review was only performed at year end. As a result of the updated analysis in the second quarter of 2007, AIG increased its loss reserve discount for workers compensation by approximately $155 million in the second quarter of 2007, bringing the total increase in loss reserve discount for workers compensation for the first six months of 2007 to approximately $185 million.

2007 Net Loss Development

In the three months ended June 30, 2007, net loss development from prior accident years was favorable by approximately $120 million, including approximately $18 million of adverse development from the general reinsurance operations of Transatlantic; and excluding approximately $12 million from accretion of loss reserve discount. Excluding Transatlantic, as well as accretion of discount, net loss development in the three months ended June 30, 2007 from prior accident years was favorable by approximately $138 million. The overall favorable development of $120 million consisted of approximately $475 million of favorable development from accident years 2003 through 2006, partially offset by approximately $355 million of adverse development from accident years 2002 and prior. For the three months ended June 30, 2007, most classes of AIG's business continued to experience favorable development for accident years 2003 through 2006. The majority of the adverse development from accident years 2002 and prior was related to developments from excess casualty business within DBG and from Transatlantic.

In the first six months of 2007, net loss development from prior accident years was favorable by approximately $268 million, including approximately $36 million of adverse development from the general reinsurance operations of Transatlantic; and excluding approximately $128 million from accretion of loss reserve discount. Excluding Transatlantic, as well as accretion of discount, net loss development in the first six months of 2007 from prior accident years was favorable by approximately $304 million. The overall favorable development of $268 million consisted of approximately $740 million of favorable development from accident years 2003 through 2006, partially offset by approximately $472 million of adverse development from accident years 2002 and prior. For the first six months of 2007, most classes of AIG's business continued to experience favorable development for accident years 2003 through 2006. The majority of the adverse development from accident years 2002 and prior was related to development from excess casualty business within DBG and from Transatlantic.

2006 Net Loss Development

In the second quarter of 2006, net loss development from prior accident years was favorable by approximately $248 million. This reflects approximately $63 million of favorable development pertaining to catastrophes in 2005, partially offset by adverse development of approximately $30 million from Transatlantic. Excluding catastrophes and Transatlantic, as well as accretion of discount of approximately $101 million, net loss development from prior accident years in the second quarter of 2006 was favorable by approximately $215 million. The overall favorable development of $248 million consisted of approximately $490 million of favorable development from accident years 2003 through 2005, partially offset by approximately $242 million of adverse development from accident years 2002 and prior. For the three months ended June 30, 2006, most classes of AIG's business experienced favorable development for accident years 2003 through 2005. The adverse development from accident years 2002 and prior reflected development from excess casualty business within DBG, and to a much lesser extent from excess workers compensation business within DBG, as well as development from Transatlantic.

In the first six months of 2006, net loss development from prior accident years was favorable by approximately $213 million. This reflects approximately $35 million of

adverse development pertaining to catastrophes in 2004 and 2005 and approximately $65 million of adverse development from Transatlantic. Excluding catastrophes and Transatlantic, as well as accretion of discount of approximately $202 million, net loss development from prior accident years in the first six months of 2006 was favorable by approximately $313 million. The $213 million of overall net favorable development was comprised of approximately $775 million of favorable development from accident years 2003 through 2005, partially offset by approximately $562 million of adverse development from accident years 2002 and prior. For the first six months of 2006, most classes of AIG's business experienced favorable development for accident years 2003 through 2005. The adverse development from accident years 2002 and prior reflected development from excess casualty business within DBG, and to a lesser extent from excess workers compensation business within DBG, as well as development from Transatlantic.

Asbestos and Environmental Reserves

The estimation of loss reserves relating to asbestos and environmental claims on insurance policies written many years ago is subject to greater uncertainty than other types of claims due to inconsistent court decisions as well as judicial interpretations and legislative actions that in some cases have tended to broaden coverage beyond the original intent of such policies and in others have expanded theories of liability.

As described more fully in the 2006 Annual Report on Form 10-K, AIG's reserves relating to asbestos and environmental claims reflect a comprehensive ground up analysis. In the first six months of 2007, one large asbestos settlement resulted in a minor amount of adverse incurred loss development, which was more than offset, on a net basis, by the favorable $50 million effect of several other settlements.

A summary of reserve activity, including estimates for applicable IBNR, relating to asbestos and environmental claims separately and combined:

	Six Months Ended June 30,			
	2007		2006	
(in millions)	**Gross**	**Net**	Gross	Net
Asbestos:				
Reserve for losses and loss expenses at beginning of year	**$4,464**	**$1,889**	$4,441	$1,840
Losses and loss expenses incurred*	**10**	**(25)**	(1)	4
Losses and loss expenses paid*	**(454)**	**(268)**	(277)	(96)
Reserve for losses and loss expenses at end of period	**$4,020**	**$1,596**	$4,163	$1,748
Environmental:				
Reserve for losses and loss expenses at beginning of year	**$ 588**	**$ 290**	$ 926	$ 410
Losses and loss expenses incurred*	**–**	**(1)**	1	–
Losses and loss expenses paid*	**(54)**	**(31)**	(55)	(33)
Reserve for losses and loss expenses at end of period	**$ 534**	**$ 258**	$ 872	$ 377
Combined:				
Reserve for losses and loss expenses at beginning of year	**$5,052**	**$2,179**	$5,367	$2,250
Losses and loss expenses incurred*	**10**	**(26)**	–	4
Losses and loss expenses paid*	**(508)**	**(299)**	(332)	(129)
Reserve for losses and loss expenses at end of period	**$4,554**	**$1,854**	$5,035	$2,125

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

The gross and net IBNR included in the reserve for losses and loss expenses, relating to asbestos and environmental claims separately and combined, were estimated as follows:

	Six Months Ended June 30,			
	2007		2006	
(in millions)	**Gross**	**Net**	Gross	Net
Asbestos	**$3,011**	**$1,279**	$3,100	$1,351
Environmental	**316**	**148**	562	241
Combined	**$3,327**	**$1,427**	$3,662	$1,592

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

	Six Months Ended June 30,					
	2007			2006		
	Asbestos	**Environmental**	**Combined**	Asbestos	Environmental	Combined
Claims at beginning of year	**6,878**	**9,442**	**16,320**	7,293	9,873	17,166
Claims during year:						
Opened	**300**	**695**	**995**	453	900	1,353
Settled	**(66)**	**(59)**	**(125)**	(73)	(83)	(156)
Dismissed or otherwise resolved	**(544)**	**(899)**	**(1,443)**	(493)	(893)	(1,386)
Claims at end of period	**6,568**	**9,179**	**15,747**	7,180	9,797	16,977

Survival Ratios — Asbestos and Environmental

The table below presents AIG's survival ratios for asbestos and environmental claims at June 30, 2007 and 2006. The survival ratio is derived by dividing the current carried loss reserve by the average payments for the three most recent calendar years for these claims. Therefore, the survival ratio is a simplistic measure estimating the number of years it would be before the current ending loss reserves for these claims would be paid off using recent year average payments. The June 30, 2007 survival ratio is lower than the ratio at June 30, 2006 because the more recent periods included in the rolling average reflect higher claims payments. In addition, AIG's survival ratio for asbestos claims was negatively affected by the favorable settlements described above, which reduced gross and net asbestos survival ratios at June 30, 2007 by approximately 1.7 years and 4.1 years, respectively. Many factors, such as aggressive settlement procedures, mix of business and level of coverage provided, have a significant effect on the amount of asbestos and environmental reserves and payments and the resultant survival ratio. Thus, caution should be exercised in attempting to determine reserve adequacy for these claims based simply on this survival ratio.

AIG's survival ratios for asbestos and environmental claims, separately and combined were based upon a three-year average payment. These ratios at June 30, 2007 and 2006 were as follows:

(number of years)	**Gross**	**Net**
2007		
Survival ratios:		
Asbestos	8.5	7.4
Environmental	5.0	4.0
Combined	7.8	6.6
2006		
Survival ratios:		
Asbestos	13.2	15.9
Environmental	6.3	5.5
Combined	11.1	11.9

Life Insurance & Retirement Services Operations

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

Domestically, AIG's Life Insurance & Retirement Services operations offer a broad range of protection products, such as life insurance and group life and health products, including disability income products and payout annuities, which include single premium immediate annuities, structured settlements and terminal funding annuities. Home service operations include an array of life insurance, accident and health and annuity products sold primarily through career agents. Retirement services include group retirement products, individual fixed and variable annuities sold through banks, broker-dealers and exclusive sales representatives, and annuity runoff operations, which include previously acquired "closed blocks" and other fixed and variable annuities largely sold through distribution relationships that have been discontinued.

Overseas, AIG's Life Insurance & Retirement Services operations include insurance and investment-oriented products such as whole and term life, investment linked, universal life and endowments, personal accident and health products, group products including pension, life and health, and fixed and variable annuities.

AIG's Life Insurance & Retirement Services subsidiaries report their operations through the following major internal reporting units and business units:

Foreign Life Insurance & Retirement Services

Japan and Other

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

Asia

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

Domestic Life Insurance

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

Domestic Retirement Services

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

Life Insurance & Retirement Services Results

Life Insurance & Retirement Services results were as follows:

(in millions)	Premiums and Other Considerations	Net Investment Income	Net Realized Capital Gains (Losses)	Total Revenues	Operating Income
Three months ended June 30, 2007					
Foreign Life Insurance & Retirement Services	**$ 6,503**	**$ 3,361**	**$ 18**	**$ 9,882**	**$1,654**
Domestic Life Insurance	**1,369**	**1,006**	**(16)**	**2,359**	**368**
Domestic Retirement Services	**298**	**1,765**	**(281)**	**1,782**	**598**
Total	**$ 8,170**	**$ 6,132**	**$(279)**	**$14,023**	**$2,620**
Three months ended June 30, 2006					
Foreign Life Insurance & Retirement Services*	$ 5,981	$ 1,970	$ 164	$ 8,115	$1,739
Domestic Life Insurance	1,404	893	(75)	2,222	235
Domestic Retirement Services	263	1,557	(246)	1,574	407
Total	$ 7,648	$ 4,420	$(157)	$11,911	$2,381
Percentage Increase/(Decrease) from Prior Year:					
Foreign Life Insurance & Retirement Services	9%	71%	—%	22%	(5)%
Domestic Life Insurance	(2)	13	—	6	57
Domestic Retirement Services	13	13	—	13	47
Total	7%	39%	—%	18%	10%
Six months ended June 30, 2007					
Foreign Life Insurance & Retirement Services	**$13,116**	**$ 6,244**	**$(217)**	**$19,143**	**$2,938**
Domestic Life Insurance	**2,897**	**2,011**	**(28)**	**4,880**	**713**
Domestic Retirement Services	**582**	**3,390**	**(290)**	**3,682**	**1,250**
Total	**$16,595**	**$11,645**	**$(535)**	**$27,705**	**$4,901**
Six months ended June 30, 2006					
Foreign Life Insurance & Retirement Services*	$12,098	$ 4,225	$ 516	$16,839	$3,425
Domestic Life Insurance	2,830	1,826	(67)	4,589	601
Domestic Retirement Services	520	3,203	(390)	3,333	985
Total	$15,448	$ 9,254	$ 59	$24,761	$5,011
Percentage Increase/(Decrease) from Prior Year:					
Foreign Life Insurance & Retirement Services	8%	48%	—%	14%	(14)%
Domestic Life Insurance	2	10	—	6	19
Domestic Retirement Services	12	6	—	10	27
Total	7%	26%	—%	12%	(2)%

** Includes the effect of an out of period UCITS adjustment in the second quarter of 2006. For the three and six-month periods ended June 30, 2006, the effect was an increase of $221 million and $203 million, respectively, in net investment income and $144 million and $132 million, respectively, in operating income.*

The following table presents the Insurance In-force for Life Insurance & Retirement Services:

(in millions)	**June 30, 2007**	December 31, 2006
Foreign	**$1,195,315**	$1,162,699
Domestic	**946,598**	907,901
Total	**$2,141,913**	$2,070,600

Life Insurance & Retirement Services total revenues for the three and six-month periods ended June 30, 2007 reflect growth in premiums and other considerations and net investment income offset by realized capital losses. Realized capital losses reduced revenues by $279 million and $535 million in the three and six-month periods ended June 30, 2007, respectively, while net realized capital losses decreased revenues by $157 million in the three months ended June 30, 2006 and net realized capital gains increased revenues by $59 million in the six months ended June 30, 2006. Net realized capital losses in 2007 were primarily related to the decline in value of securities deemed to be other-than-temporary that AIG no longer intends to hold to recovery.

Operating income for the first six months of 2007 includes a charge of $48 million related to SOP 05-1 which generally requires DAC related to group contracts to be amortized over a shorter duration than in prior periods, and also requires that DAC be expensed at the time a policy is terminated and prohibits recapitalization if that policy is reinstated. The effect of SOP 05-1 was most significant to the group products line in the Domestic Life operations.

Operating income for the six months ended June 30, 2007 also included a $62 million charge for additional benefit expense resulting from a continuing industry-wide review of claims in Japan and a $50 million charge related to balance sheet reconciliation remediation activities. Operating income for the six months ended June 30, 2006 included an increase of $132 million for an out of period adjustment related to the accounting for UCITS.

Policyholder trading gains (losses) for the three and six months ended June 30, 2007 increased significantly compared to the same periods in 2006. The three and six months ended June 30, 2007 included policyholder trading gains of $784 million and $1.3 billion, respectively, compared to losses of $321 million and gains of $69 million for the three and six months ended June 30, 2006, respectively. Policyholder trading gains (losses) are offset by an equal charge to incurred policy losses and benefits expense, as these investment returns accrue to the benefit of the policyholder. The trend in policyholder trading gains (losses) generally reflects the trend in equity markets.

In order to better align financial reporting with the manner in which AIG's chief operating decision makers have managed their businesses, commencing in the first quarter of 2007, revenues and operating income related to foreign investment contracts, which were historically reported as a component of the Asset Management segment, are now being reported as part of Foreign Life Insurance & Retirement Services. Prior period amounts have been revised to conform to the current presentation.

Foreign Life Insurance & Retirement Services Results

Foreign Life Insurance & Retirement Services results were as follows:

(in millions)	Premiums and Other Considerations	Net Investment Income	Net Realized Capital Gains (Losses)	Total Revenues	Operating Income
Three months ended June 30, 2007					
Japan and Other:					
Life insurance	**$ 1,350**	**$ 641**	**$ 33**	**$ 2,024**	**$ 438**
Personal accident	**1,041**	**52**	**–**	**1,093**	**243**
Group products	**539**	**201**	**1**	**741**	**63**
Individual fixed annuities	**101**	**546**	**(129)**	**518**	**34**
Individual variable annuities	**102**	**385**	**–**	**487**	**32**
Total	**$ 3,133**	**$1,825**	**$ (95)**	**$ 4,863**	**$ 810**
Asia:					
Life insurance	**$ 2,755**	**$1,451**	**$ 108**	**$ 4,314**	**$ 717**
Personal accident	**446**	**35**	**2**	**483**	**82**
Group products	**151**	**21**	**(7)**	**165**	**26**
Individual fixed annuities	**17**	**28**	**9**	**54**	**18**
Individual variable annuities	**1**	**1**	**1**	**3**	**1**
Total	**$ 3,370**	**$1,536**	**$ 113**	**$ 5,019**	**$ 844**
Total Foreign Life Insurance & Retirement Services:					
Life insurance	**$ 4,105**	**$2,092**	**$ 141**	**$ 6,338**	**$1,155**
Personal accident	**1,487**	**87**	**2**	**1,576**	**325**
Group products	**690**	**222**	**(6)**	**906**	**89**
Individual fixed annuities	**118**	**574**	**(120)**	**572**	**52**
Individual variable annuities	**103**	**386**	**1**	**490**	**33**
Total	**$ 6,503**	**$3,361**	**$ 18**	**$ 9,882**	**$1,654**
Three months ended June 30, 2006					
Japan and Other:					
Life insurance	$ 1,238	$ 343	$ 113	$ 1,694	$ 454
Personal accident	1,006	42	22	1,070	279
Group products	410	93	2	505	63
Individual fixed annuities	78	432	27	537	148
Individual variable annuities	62	(56)	–	6	31
Total	$ 2,794	$ 854	$ 164	$ 3,812	$ 975

Foreign Life Insurance & Retirement Services Results (continued)

(in millions)	Premiums and Other Considerations	Net Investment Income	Net Realized Capital Gains (Losses)	Total Revenues	Operating Income
Asia:					
Life insurance*	$ 2,700	$1,038	$ 26	$ 3,764	$ 688
Personal accident	374	29	3	406	76
Group products	97	22	(30)	89	(7)
Individual fixed annuities	16	26	1	43	6
Individual variable annuities	–	1	–	1	1
Total	$ 3,187	$1,116	$ –	$ 4,303	$ 764
Total Foreign Life Insurance & Retirement Services:					
Life insurance*	$ 3,938	$1,381	$ 139	$ 5,458	$1,142
Personal accident	1,380	71	25	1,476	355
Group products	507	115	(28)	594	56
Individual fixed annuities	94	458	28	580	154
Individual variable annuities	62	(55)	–	7	32
Total	$ 5,981	$1,970	$ 164	$ 8,115	$1,739
Percentage Increase/(Decrease) from Prior Year:					
Japan and Other:					
Life insurance	9%	87%	–%	19%	(4)%
Personal accident	3	24	–	2	(13)
Group products	31	116	–	47	–
Individual fixed annuities	29	26	–	(4)	(77)
Individual variable annuities	65	–	–	–	3
Total	12%	114%	–%	28%	(17)%
Asia:					
Life insurance	2%	40%	–%	15%	4%
Personal accident	19	21	–	19	8
Group products	56	(5)	–	85	–
Individual fixed annuities	6	8	–	26	–
Individual variable annuities	–	–	–	–	–
Total	6%	38%	–%	17%	10%
Total Foreign Life Insurance & Retirement Services:					
Life insurance	4%	51%	–%	16%	1%
Personal accident	8	23	–	7	(8)
Group products	36	93	–	53	59
Individual fixed annuities	26	25	–	(1)	(66)
Individual variable annuities	66	–	–	–	3
Total	9%	71%	–%	22%	(5)%
Six months ended June 30, 2007					
Japan and Other:					
Life insurance	**$ 2,566**	**$1,191**	**$ 15**	**$ 3,772**	**$ 790**
Personal accident	**2,069**	**102**	**2**	**2,173**	**532**
Group products	**1,114**	**351**	**6**	**1,471**	**136**
Individual fixed annuities	**217**	**1,092**	**(164)**	**1,145**	**181**
Individual variable annuities	**193**	**879**	**–**	**1,072**	**84**
Total	**$ 6,159**	**$3,615**	**$(141)**	**$ 9,633**	**$1,723**
Asia:					
Life insurance	**$ 5,706**	**$2,458**	**$ (42)**	**$ 8,122**	**$1,017**
Personal accident	**891**	**68**	**(8)**	**951**	**161**
Group products	**329**	**45**	**(33)**	**341**	**16**
Individual fixed annuities	**29**	**56**	**7**	**92**	**20**
Individual variable annuities	**2**	**2**	**–**	**4**	**1**
Total	**$ 6,957**	**$2,629**	**$ (76)**	**$ 9,510**	**$1,215**
Total Foreign Life Insurance & Retirement Services:					
Life insurance	**$ 8,272**	**$3,649**	**$ (27)**	**$11,894**	**$1,807**
Personal accident	**2,960**	**170**	**(6)**	**3,124**	**693**
Group products	**1,443**	**396**	**(27)**	**1,812**	**152**
Individual fixed annuities	**246**	**1,148**	**(157)**	**1,237**	**201**
Individual variable annuities	**195**	**881**	**–**	**1,076**	**85**
Total	**$13,116**	**$6,244**	**$(217)**	**$19,143**	**$2,938**

Foreign Life Insurance & Retirement Services Results (continued)

(in millions)	Premiums and Other Considerations	Net Investment Income	Net Realized Capital Gains (Losses)	Total Revenues	Operating Income
Six months ended June 30, 2006					
Japan and Other:					
Life insurance	$ 2,409	$ 799	$ 234	$ 3,442	$ 902
Personal accident	1,950	80	40	2,070	566
Group products	840	246	11	1,097	140
Individual fixed annuities	157	908	30	1,095	286
Individual variable annuities	123	249	–	372	59
Total	$ 5,479	$2,282	$ 315	$ 8,076	$1,953
Asia:					
Life insurance*	$ 5,611	$1,794	$ 186	$ 7,591	$1,250
Personal accident	736	55	12	803	152
Group products	240	46	1	287	57
Individual fixed annuities	32	46	2	80	11
Individual variable annuities	–	2	–	2	2
Total	$ 6,619	$1,943	$ 201	$ 8,763	$1,472
Total Foreign Life Insurance & Retirement Services:					
Life insurance*	$ 8,020	$2,593	$ 420	$11,033	$2,152
Personal accident	2,686	135	52	2,873	718
Group products	1,080	292	12	1,384	197
Individual fixed annuities	189	954	32	1,175	297
Individual variable annuities	123	251	–	374	61
Total	$12,098	$4,225	$ 516	$16,839	$3,425
Percentage Increase/(Decrease) from Prior Year:					
Japan and Other:					
Life insurance	7%	49%	–%	10%	(12)%
Personal accident	6	28		5	(6)
Group products	33	43		34	(3)
Individual fixed annuities	38	20	–	5	(37)
Individual variable annuities	57	–	–	–	42
Total	12%	58%	–%	19%	(12)%
Asia:					
Life insurance	2%	37%	–%	7%	(19)%
Personal accident	21	24	–	18	6
Group products	37	(2)	–	19	(72)
Individual fixed annuities	(9)	22	–	15	82
Individual variable annuities	–	–	–	–	(50)
Total	5%	35%	–%	9%	(17)%
Total Foreign Life Insurance & Retirement Services:					
Life insurance	3%	41%	–%	8%	(16)%
Personal accident	10	26	–	9	(3)
Group products	34	36	–	31	(23)
Individual fixed annuities	30	20	–	5	(32)
Individual variable annuities	59	–	–	–	39
Total	8%	48%	–%	14%	(14)%

** Includes the effect of an out of period UCITS adjustment in the second quarter of 2006. For the three and six-month periods ended June 30, 2006 the effect was an increase of $221 million and $203 million, respectively, in net investment income and $144 million and $132 million, respectively, in operating income.*

AIG transacts business in most major foreign currencies and therefore premiums reported in U.S. dollars vary both by volume and as a result of changes in foreign currency translation rates. The following table summarizes the effect of changes in foreign currency exchange rates on the growth of the Foreign Life Insurance & Retirement Services premiums and other considerations:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2007	2006	**2007**	2006
Growth in original currency*	**7.8%**	6.8%	**6.5%**	7.3%
Foreign exchange effect	**0.9**	(3.1)	**1.9**	(4.2)
Growth as reported in U.S. dollars	**8.7%**	3.7%	**8.4%**	3.1%

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

Quarterly Japan and Other Results

Total revenues for the three-month period ended June 30, 2007 increased compared to the same period in 2006, primarily due to higher premiums and net investment income partially offset by a decline in net realized capital gains. Operating income decreased for the three months ended June 30, 2007 compared to the same period in 2006 due to net realized capital losses and additional benefit expenses of $25 million related to the continuing industry-wide regulatory review of unpaid benefits in Japan which is expected to be completed in late 2007.

Life insurance premiums and other considerations increased in the three months ended June 30, 2007 compared to the same period in 2006 due to strong sales in Japan of increasing term products that have tax benefits for corporate clients. Sales of these products ceased in April pending an industry-wide review by the National Tax Authority. In Japan, increased fees and policy charges related to interest sensitive universal life and U.S. dollar life insurance products were partially offset by the runoff of the acquired blocks of business in AIG Star Life and AIG Edison Life. In Europe, growth in premiums and other considerations was enhanced by the effect of changes in foreign exchange rates. The growth in net investment income was due to higher partnership income and equity income from unit investment trusts. Life insurance operating income declined for the three months ended June 30, 2007 compared to the same period in 2006 due to net realized capital losses, partially offset by the growth in net investment income.

Personal accident premiums and other considerations continue to grow. Strong growth in Europe has offset the declines in Japan, which has been adversely affected by increased competition and lower sales of tax-related products. When compared to the same period in 2006, net investment income increased primarily due to higher invested assets and increased partnership income. Operating income declined for the three months ended June 30, 2007 compared to the same period in 2006 due to lower net realized capital gains, additional benefit expenses related to the continuing industry-wide regulatory review, higher DAC amortization related to SOP 05-1, and higher expenses related to the termination of certain tax-related products in Japan. Loss ratios remained stable for this business which continues to enjoy relatively high margins.

Group products premiums and other considerations reflected growth for the three months ended June 30, 2007 compared to the same period in 2006 primarily due to rapidly growing credit business in Europe and higher fee income from pension business in Brazil. Net investment income increased over the same period last year as policyholder trading gains were higher. Operating income was flat compared to the same period in 2006 as improvements in Europe from increased production of credit business were offset by lower realized capital gains.

Individual fixed annuities premiums and other considerations growth reflects higher surrender charges from U.S. dollar contracts in Japan where a weak yen makes it attractive for certain policyholders to lock in foreign exchange gains in excess of surrender charges. Surrender charges were $33 million and $18 million for the three months ended June 30, 2007 and 2006, respectively. Net investment income increased due to higher average investment yields and higher assets under management. Operating income declined in the three months ended June 30, 2007 compared to the same period in 2006 due to net realized capital losses in 2007 compared to net realized capital gains in 2006. The net realized capital losses offset increased earnings from higher assets under management, higher surrender charge income and higher positive DAC unlocking of $9 million.

Individual variable annuity assets under management continued to grow, particularly in Europe, due to new product offerings and strong equity markets. The fees generated from the growth in assets under management increased premiums and operating income for the three months ended June 30, 2007 compared to the same period in 2006. Net investment income grew in the three months ended June 30, 2007 compared to the same period in 2006 due to increased policyholder trading gains which comprise the entirety of variable annuity net investment income.

Year-to-date Japan and Other Results

Total revenues for the first six months of 2007 increased compared to the same period in 2006, primarily due to higher premiums and net investment income partially offset by net realized capital losses. Operating income decreased in the first six months of 2007 compared to the same period in 2006 due to net realized capital losses. In addition, a $62 million provision for additional benefit expense was established in Japan as a result of a continuing industry-wide regulatory review of claims.

Life insurance premiums and other considerations increased in the first six months of 2007 compared to the same period in 2006. In Japan, increased fees and policy charges related to interest sensitive universal life and U.S. dollar life insurance products, as well as strong sales of increasing term products with tax benefits for corporate clients, were partially offset by the runoff of the acquired blocks of business in AIG Star Life and AIG Edison Life. In Europe, growth in premiums and other considerations was enhanced by the effect of changes in foreign exchange rates. The growth in net investment income was due to higher income from partnerships and other yield enhancement income, equity income from UCITS, higher policyholder trading gains and growth in underlying invested assets. Life

insurance operating income declined in the first six months of 2007 compared to the same period in 2006 due to net realized capital losses which offset the benefits of higher net investment income, lower acquisition costs and lower benefit costs.

Personal accident premiums and other considerations growth in Japan has been adversely affected by increased competition and lower sales of tax-related products. Net investment income increased in the first six months of 2007 compared to the same period in 2006 primarily due to higher income from invested assets and increased partnership income. Operating income in the first six months of 2007 was affected by lower realized capital gains, the $46 million provision for additional benefit expenses, $34 million of expenses related to the termination of certain tax-related products in Japan and a $12 million charge related to the effect of SOP 05-1. Loss ratios remained stable for this business which continues to enjoy relatively high margins.

Group products premiums and other considerations reflected growth for the first six months in 2007 compared to the same period of 2006 primarily due to credit business growth in Europe. Net investment income increased from the first six months of 2006 primarily related to higher policyholder trading gains. Operating income for the first six months of 2007 declined slightly from the same period in 2006 primarily due to SOP 05-1 and higher benefit expense in Japan.

Individual fixed annuities premiums and other considerations growth reflects higher surrender charges from U.S. dollar contracts in Japan where a weak yen makes it attractive for certain policyholders to lock in foreign exchange gains in excess of surrender charges. Surrender charges were $86 million and $42 million for the six months ended June 30, 2007 and 2006, respectively. Net investment income increased due to higher average investment yields, assets under management and partnership income. In the first half of 2007, AIG implemented a new investment strategy to enhance future investment yields that resulted in realized capital losses as a small portion of the existing bond portfolio was sold and reinvested in higher yielding assets. These actions resulted in net realized capital losses for the first six months of 2007 compared to net realized capital gains in 2006, which offsets the positive effect of higher assets under management.

Individual variable annuity assets under management continued to grow particularly in Europe, due to new product offerings and favorable market conditions. The fees generated from the growth in assets under management increased premiums and other considerations and operating income for the first six months of 2007 compared to the same period in 2006. Net investment income grew for the first six months of 2007 compared to the same period in 2006 due to increased policyholder trading gains which comprise the entirety of variable annuity net investment income.

Quarterly Asia Results

Total revenues for the three months ended June 30, 2007 increased from the same period in 2006. Premiums and other considerations growth reflects a continued trend toward investment-oriented products where only a portion of policy charges are reported as premiums. Net investment income increased, primarily due to higher policyholder trading gains. Net investment income and operating income for the three months ended June 30, 2006 included out of period income related to unit investment trusts of $221 million and $144 million, respectively. Net realized capital gains were higher than the same period in 2006. Operating income for the three months ended June 30, 2007 improved over the same period in 2006 primarily due to growth in premiums and other considerations, higher investment returns and net realized capital gains.

Life insurance premiums and other considerations were up slightly in the three months ended June 30, 2007 compared to the same period in 2006. The shift in product mix from traditional life insurance products to investment-oriented products as mentioned above dampens the growth rate. Net investment income grew in the current period compared to the same period in 2006, due primarily to the growth in the underlying invested assets, higher partnership income and higher policyholder trading gains. Net investment income and operating income for the three months ended June 30, 2006 included out of period income related to unit investment trusts of $221 million and $144 million, respectively. Operating income increased for the three months ended June 30, 2007 compared to the same period in 2006, due primarily to higher realized capital gains, partnership income and the positive effect of SOP 05-1.

Personal accident premiums and other considerations increased primarily due to growth in Korea and the favorable effect of changes in foreign exchange rates. The primary focus in Asia has been on risk-based individual and rider accident and health (A&H) products particularly in Korea and Taiwan. Operating earnings reflect the combined effect of premium growth and stable loss ratios and also include a benefit resulting from SOP 05-1.

Group products premiums and other considerations grew in the three months ended June 30, 2007 compared to the same period in 2006, reflecting higher pension management fees and improved sales in Thailand, Hong Kong and Singapore. Operating income improved compared to the same period last year primarily due to lower realized capital losses and increased business in force.

Individual fixed annuities total revenues and operating income were higher for the three months ended June 30, 2007 compared to the same period in 2006 resulting from net

realized capital gains. Production for the three months ended June 30, 2007 increased compared to the same period in 2006, mostly due to the launch of a coupon product in Korea which pays periodic interest to policyholders based upon their election.

Year-to-date Asia Results

Total revenues for the first six months of 2007 were higher than in 2006, while operating income fell compared to the same period in 2006 due to net realized capital losses in 2007 compared to net realized capital gains in 2006. Premiums and other considerations grew moderately compared to the same period in 2006 reflecting a continued trend toward investment-oriented products where only a portion of policy charges are reported as premium. Net investment income grew due to higher policyholder trading gains, higher income from interests in unit investment trusts, and growth in underlying invested assets. Net investment income and operating income for the six months ended June 30, 2006 included out of period income related to unit investment trusts of $203 million and $132 million, respectively. Net realized capital losses in the current period compared to net realized capital gains in the same period last year also influenced the growth rate in total revenues and caused the decline in operating income. The net realized capital losses in the current period were driven primarily by the mark to market of derivatives that do not qualify for hedge accounting treatment under FAS 133 and the other-than-temporary decline in value of U.S. dollar bonds held in Singapore and Thailand.

Life insurance premiums and other considerations were up slightly in the first six months of 2007 compared to the same period in 2006, benefiting from improved sales in Thailand and the favorable effect of foreign exchange rates, partially offset by the shift in product mix from traditional life insurance products to investment-oriented products as mentioned above. Net investment income grew in the current period compared to the same period in 2006, due primarily to higher policyholder trading gains, the growth in the underlying invested assets and earnings on certain interests in unit investment trusts. Operating income decreased in the first six months of 2007 compared to the same period in 2006, due mainly to net realized capital losses which more than offset the growth in other sources of earnings. Operating income for the first six months of 2007 includes a $50 million charge related to balance sheet reconciliation remediation activity.

Personal accident revenues grew for the first six months of 2007 compared to the same period in 2006 primarily due to higher premiums and other considerations particularly in Korea and Taiwan. Operating earnings reflect the combined effect of premium growth and stable loss ratios that were partially offset by realized capital losses. In addition, results for the first six months of 2007 include a $6 million positive effect related to SOP 05-1.

Group products premiums and other considerations grew in the first six months of 2007 compared to the same period in 2006. The increase reflected higher pension management fees and improved sales, particularly in Thailand, Hong Kong and Singapore, in the first six months of 2007 compared to the same period in 2006. Operating income declined in the first six months of 2007 compared to the same period in 2006 primarily due to realized capital losses and higher incurred policy losses and benefits of $13 million due to a 2007 out of period reserve charge.

Individual fixed annuities total revenues increased in the first six months of 2007 compared to the same period in 2006, due primarily to higher net investment income on underlying assets and higher realized capital gains. Production for the six months ended June 30, 2007 was flat compared to the same period in 2006 due to increased competition in Korea.

Domestic Life Insurance Results

Domestic Life Insurance results, presented by sub-product were as follows:

(in millions)	Premiums and Other Considerations	Net Investment Income	Net Realized Capital Gains (Losses)	Total Revenues	Operating Income (Loss)
Three months ended June 30, 2007					
Life insurance	$ 603	$ 402	$ 43	$1,048	$262
Home service	192	158	(11)	339	66
Group life/health	197	51	(4)	244	1
Payout annuities[(a)]	364	276	(35)	605	17
Individual fixed annuities	2	24	–	26	8
Individual annuities – runoff[(b)]	11	95	(9)	97	14
Total	$1,369	$1,006	$ (16)	$2,359	$368
Three months ended June 30, 2006					
Life insurance	$ 557	$ 313	$ (29)	$ 841	$148
Home service	197	145	(10)	332	66
Group life/health	241	52	(3)	290	(8)
Payout annuities	397	244	(18)	623	12
Individual fixed annuities	–	19	(1)	18	8
Individual annuities – runoff[(b)]	12	120	(14)	118	9
Total	$1,404	$ 893	$ (75)	$2,222	$235
Percentage Increase/(Decrease) from Prior Year:					
Life insurance	8%	28%	–%	25%	77%
Home service	(3)	9	–	2	–
Group life/health	(18)	(2)	–	(16)	–
Payout annuities	(8)	13	–	(3)	42
Individual fixed annuities	–	26	–	44	–
Individual annuities – runoff[(b)]	(8)	(21)	–	(18)	56
Total	(2)%	13%	–%	6%	57%
Six months ended June 30, 2007					
Life insurance	$1,181	$ 774	$ 40	$1,995	$449
Home service	387	319	(13)	693	148
Group life/health	426	104	(5)	525	4
Payout annuities[(a)]	876	565	(41)	1,400	68
Individual fixed annuities	4	51	–	55	12
Individual annuities – runoff[(b)]	23	198	(9)	212	32
Total	$2,897	$2,011	$ (28)	$4,880	$713
Six months ended June 30, 2006					
Life insurance	$1,073	$ 651	$ 33	$1,757	$388
Home service	397	303	(33)	667	125
Group life/health	487	106	(4)	589	11
Payout annuities	847	481	(36)	1,292	34
Individual fixed annuities	1	34	(3)	32	6
Individual annuities – runoff[(b)]	25	251	(24)	252	37
Total	$2,830	$1,826	$ (67)	$4,589	$601
Percentage Increase/(Decrease) from Prior Year:					
Life insurance	10%	19%	–%	14%	16%
Home service	(3)	5	–	4	18
Group life/health	(13)	(2)	–	(11)	(64)
Payout annuities	3	17	–	8	–
Individual fixed annuities	–	50	–	72	–
Individual annuities – runoff[(b)]	(8)	(21)	–	(16)	(14)
Total	2%	10%	–%	6%	19%

(a) Premiums and other considerations include structured settlements, single premium immediate annuities and terminal funding annuities.
(b) Primarily represents runoff annuity business sold through discontinued distribution relationships.

Domestic Life Insurance

Quarterly Domestic Life Results

Domestic Life Insurance premiums and other considerations declined in the three months ended June 30, 2007 compared to the same period in 2006, primarily due to the exiting of the financial institutions credit life business within the group life/health segment as of the end of 2006 and lower sales of payout annuities. These declines were partially offset by growth in the life insurance business in force. Premiums and other considerations for the home service segment declined in

the three months ended June 30, 2007 compared to the same period in 2006 as the reduction in premium in force from normal lapses and maturities exceeded sales growth. Premiums and other considerations from payout annuities decreased for the three-month period ended June 30, 2007 compared to the same period in 2006 reflecting decreased sales of single premium immediate annuities, which were affected by the re-pricing of this product line in the second half of 2006.

Domestic Life Insurance operating income increased in the three months ended June 30, 2007 compared to the same period in 2006. The increase was primarily driven by higher partnership income, lower realized capital losses and overall growth in the in-force business. Financial results for the three months ended June 30, 2007 also benefited from a $15 million decrease in certain litigation accruals due to favorable developments from the related matters and were adversely affected by a $17 million increase in DAC amortization related to SOP 05-1.

Life insurance operating income increased for the three months ended June 30, 2007 compared to the same period in 2006, primarily due to higher partnership income, increased net realized capital gains, a $15 million release of litigation related reserves and growth in the underlying business, partially offset by higher policyholder benefits. Home service operating income for the three months ended June 30, 2007 was unchanged from the prior period in 2006 as higher net investment income from foreign denominated emerging market bonds offset the effect of the decline in premiums and other considerations. Group life/health operating income from the three months ended June 30, 2007 improved compared to the same period in 2006, as 2006 results included the effect of a $24 million litigation accrual. Results for the three months ended June 30, 2007 included a $12 million charge related to SOP 05-1. Payout annuities operating income increased for the three months ended June 30, 2007 due to growth in reserves offset by higher realized capital losses. Individual fixed annuities operating income remained unchanged as growth in net investment income was offset by higher interest credited and acquisition expenses. Individual annuities — runoff operating income increased for three months ended June 30, 2007 due to lower realized capital losses compared to same period in 2006.

Year-to-date Domestic Life Results

Domestic Life Insurance premiums and other considerations increased during the first six months of 2007 compared to the same period in 2006. The increase was primarily due to the growth in life insurance business in force and payout annuities. Premiums and other considerations for the home service segment declined compared to the same period in 2006 as the reduction in premiums in force from normal lapses and maturities exceeded sales growth. Premiums and other considerations for group life/health for the first six months of 2007 declined compared to the same period in 2006, primarily due to the exiting of the financial institutions credit life business as of the end of 2006 and tightened pricing and underwriting in the group employer lines. Premiums and other considerations growth from payout annuities for the first six months of 2007 reflects increased sales of structured settlements and terminal funding annuities compared to the same period in 2006.

Domestic Life Insurance operating income increased in the first six months of 2007 compared to the same period in 2006, primarily due to increases in net investment income, lower realized capital losses, growth in the underlying business and a $15 million reduction of certain litigation accruals due to favorable developments on the related matters. Operating income for the six-month period ended June 30, 2006 included a $25 million charge for litigation accruals. The financial results for the six months ended June 30, 2007 were also affected by a $39 million charge related to SOP 05-1.

Life insurance operating income increased for the first six months of 2007 compared to the same period in 2006 primarily due to higher net investment income, increased realized capital gains and a reduction of the aforementioned litigation-related accrual, partially offset by higher policyholder benefits. Home service operating income increased due to lower realized capital losses and higher net investment income offset by the decline in premiums and other considerations. Group life/health lines operating income decreased due to a charge of $28 million resulting from SOP 05-1 partially offset by lower operating expenses. The operating income for the six-month period ended June 30, 2006 included a $25 million charge for litigation accruals. Payout annuities operating income increased for the first six months of 2007 due to growth in the business and an increase in call and tender income on fixed maturity securities. Individual fixed annuities operating income increased primarily from higher net investment income. Individual annuities — runoff operating income decreased from the first six months in 2006 due to the reduction in the block of business partially offset by lower realized capital losses.

The following table reflects periodic Domestic Life Insurance sales by product:

(in millions)	Three Months Ended June 30, 2007	Three Months Ended June 30, 2006	Percentage Increase/ (Decrease)	Six Months Ended June 30, 2007	Six Months Ended June 30, 2006	Percentage Increase/ (Decrease)
Periodic premium sales by product*:						
Universal life	**$47**	$107	(56)%	**$98**	$243	(60)%
Variable universal life	**12**	18	(33)	**25**	27	(7)
Term life	**57**	63	(10)	**112**	123	(9)
Whole life/other	**3**	3	—	**5**	6	(17)
Total	**$119**	$191	(38)%	**$240**	$399	(40)%

** Periodic premium represents premium from new business expected to be collected over a one-year period.*

Periodic life insurance sales declined for the three and six-month periods ended June 30, 2007 compared to the same periods in 2006 primarily as a result of the re-pricing of certain universal life and term products and the tightening of underwriting standards during the second half of 2006.

Domestic Retirement Services Results

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

(in millions)	Premiums and Other Considerations	Net Investment Income	Net Realized Capital Gains (Losses)	Total Revenues	Operating Income
Three months ended June 30, 2007					
Group retirement products	**$112**	**$ 641**	**$(103)**	**$ 650**	**$ 265**
Individual fixed annuities	**26**	**981**	**(158)**	**849**	**261**
Individual variable annuities	**155**	**43**	**(17)**	**181**	**53**
Individual annuities — runoff*	**5**	**100**	**(3)**	**102**	**19**
Total	**$298**	**$1,765**	**$(281)**	**$1,782**	**$ 598**
Three months ended June 30, 2006					
Group retirement products	$ 96	$ 539	$ (76)	$ 559	$ 192
Individual fixed annuities	35	861	(152)	744	160
Individual variable annuities	130	50	(7)	173	41
Individual annuities — runoff*	2	107	(11)	98	14
Total	$263	$1,557	$(246)	$1,574	$ 407
Percentage Increase/(Decrease) from Prior Year:					
Group retirement products	17%	19%	–%	16%	38%
Individual fixed annuities	(26)	14	–	14	63
Individual variable annuities	19	(14)	–	5	29
Individual annuities — runoff*	–	(7)	–	4	36
Total	13%	13%	–%	13%	47%
Six months ended June 30, 2007					
Group retirement products	**$217**	**$1,211**	**$(113)**	**$1,315**	**$ 541**
Individual fixed annuities	**51**	**1,895**	**(169)**	**1,777**	**564**
Individual variable annuities	**301**	**85**	**(7)**	**379**	**105**
Individual annuities — runoff*	**13**	**199**	**(1)**	**211**	**40**
Total	**$582**	**$3,390**	**$(290)**	**$3,682**	**$1,250**
Six months ended June 30, 2006					
Group retirement products	$190	$1,111	$(113)	$1,188	$ 457
Individual fixed annuities	63	1,778	(252)	1,589	419
Individual variable annuities	258	102	(5)	355	87
Individual annuities — runoff*	9	212	(20)	201	22
Total	$520	$3,203	$(390)	$3,333	$ 985
Percentage Increase/(Decrease) from Prior Year:					
Group retirement products	14%	9%	–%	11%	18%
Individual fixed annuities	(19)	7	–	12	35
Individual variable annuities	17	(17)	–	7	21
Individual annuities — runoff*	44	(6)	–	5	82
Total	12%	6%	–%	10%	27%

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

Quarterly Domestic Retirement Services Results

Total Domestic Retirement Services operating income for the three months ended June 30, 2007 increased compared to the same period in 2006. Group retirement products total revenues increased in the three months ended June 30, 2007 compared to the same period in 2006, primarily due to higher

income from partnerships, credit-linked notes and other yield enhancement income and an increase in variable annuity fees resulting from the increase in the equity markets. Group retirement products operating income increased for the three months ended June 30, 2007 driven by higher revenues related to partnerships and other yield enhancement income, partially offset by higher amortization of DAC. DAC amortization increases were related to the increase in surrenders and policy changes adding guaranteed minimum withdrawal benefit riders to existing contracts. Total revenues for individual fixed annuities increased in the three months ended June 30, 2007 compared to the same period in 2006 primarily driven by higher partnership and yield enhancement income. Individual fixed annuities operating income increased for the three months ended June 30, 2007 driven by higher revenues, partially offset by higher amortization of DAC resulting from an increase in early duration surrenders. Individual variable annuities total revenues increased in the three months ended June 30, 2007 compared to the same period in 2006, driven by higher fees primarily from the increase in the equity markets. Individual variable annuity fees also increased due to an increased number of contracts sold with living benefit features. The higher revenues, as well as decreased death benefits, were partially offset by higher amortization of DAC and higher net realized capital losses, and resulted in an increase in individual variable annuity operating income. Partnership investments of $166 million were transferred to support the variable annuity line of business commencing in the second quarter of 2007. Although not significant to individual variable annuities in 2007, partnership income is expected to become more significant in future periods. Individual annuities — runoff operating income increased for the three months ended June 30, 2007 over the same period in 2006 even though the underlying reserves decreased. The higher income was primarily due to lower realized capital losses, partially offset by lower volumes due to the continued runoff of the business.

Year-to-date Domestic Retirement Services Results

Total Domestic Retirement Services operating income for the first six months of 2007 increased over the same period in 2006. Group retirement products total revenues increased in the first six months of 2007 compared to the same period in 2006, primarily due to higher partnership and yield enhancement income and an increase in variable annuity fees. Group retirement products income increased for the six months in 2007 driven by higher revenues related to income from partnerships and other yield enhancement income, partially offset by higher amortization of DAC. DAC amortization increases were related to the increase in surrenders and policy changes adding guaranteed minimum withdrawal benefit riders to existing contracts. Total revenues and operating income for individual fixed annuities increased in the first six months of 2007 compared to the first six months in 2006 primarily driven by higher partnership and yield enhancement income and lower realized capital losses, partially offset by higher amortization of DAC as a result of lower realized capital losses and increased early duration surrenders. Individual variable annuities total revenues increased in the first six months of 2007 compared to the first six months in 2006, primarily driven by higher variable annuity fees resulting from the increase in the equity markets. Additionally, more contracts sold with living benefit features also contributed to higher individual variable annuity fees. The higher revenues as well as decreased death benefits, partially offset by higher amortization of DAC, resulted in the increase in individual variable annuities operating income. Individual annuities — runoff operating income increased in the first six months of 2007 over the same period of 2006 even though the underlying reserves decreased. The higher income was primarily due to lower realized capital losses and increased net spreads as a result of higher investment yields, partially offset by lower volumes due to the continued runoff of the business.

Domestic Retirement Services Supplemental Data

The following table presents deposits*:

	Three Months Ended June 30,		Six Months Ended June 30,	
(in millions)	**2007**	2006	**2007**	2006
Group retirement products:				
Annuities	**$1,463**	$1,352	**$2,881**	$2,748
Mutual funds	**330**	256	**795**	801
Individual fixed annuities	**1,633**	1,194	**2,864**	2,735
Individual variable annuities	**1,204**	1,148	**2,212**	2,175
Individual fixed annuities – runoff	**13**	14	**27**	29
Total	**$4,643**	$3,964	**$8,779**	$8,488

** Excludes internal replacements.*

Domestic Retirement Services total deposits increased for the three months ended June 30, 2007 compared to the same period in 2006 with all three primary product lines showing improved results. Group retirement deposits increased 12 percent in the three months ended June 30, 2007 compared to the same period in 2006 as a result of an increase in group annuity deposits and group mutual funds. Over time, AIG expects that group mutual fund sales will result in a gradual reduction in overall profit margins of this business due to the growth in the lower-margin mutual fund products relative to the annuity products. Individual fixed annuity deposits increased 37 percent for the three months ended June 30, 2007 compared to the same period in 2006, as several large bank distributors increased their focus on fixed annuities in the second quarter of 2007. Individual variable annuity deposits increased 5 percent for the three months ended June 30, 2007 compared to the same period in 2006. Individual fixed annuity surrenders increased in the three months ended June 30, 2007 compared to the same period in 2006 due to policies coming out of their surrender charge periods and increased competition from banks. AIG expects this trend to continue into the next year as a significant amount of business comes out of its surrender charge period.

Individual fixed annuity net flows for the three months ended June 30, 2007 improved compared to the same period in 2006, reflecting the higher deposits discussed above. Individual variable annuities net flows for the three months ended June 30, 2007 declined compared to the same period in 2006 due to higher surrender amounts resulting from market growth, while the surrender rate remained relatively constant.

Domestic Retirement Services total deposits increased for the first six months of 2007 compared to the same period in 2006. The increase in total deposits primarily reflects higher deposits from group annuities, individual fixed annuities and individual variable annuities. Group retirement deposits increased 4 percent in the first six months of 2007 compared to the same period in 2006 as a result of an increase in group variable annuity deposits, partially offset by slightly lower deposits in group fixed annuities and group mutual funds. Although individual fixed annuity sales continued to face increased competition from bank deposit products and money market funds offering very competitive short-term rates in the flat yield curve environment, individual fixed annuity deposits increased 5 percent for the six months ended June 30, 2007 compared to the same period in 2006. Individual variable annuity deposits increased slightly in the first six months of 2007 compared to the same period in 2006 despite the discontinuation of a major bank proprietary product. Group retirement surrenders increased as a result of normal maturing of the business and due to a few large group surrenders in the first three months of 2007 compared to the same period last year. Individual fixed annuity surrender rates increased in the first six months of 2007 compared to the same period in 2006 due to policies coming out of their surrender charge period and increased competition from banks. Individual fixed annuities net flows for the first six months of 2007 declined compared to the same period in 2006, reflecting the higher surrenders discussed above, partially offset by slightly higher deposits.

The following table presents Domestic Retirement Services reserves by surrender charge category as of June 30, 2007:

(in millions)	Group Retirement Products*	Individual Fixed Annuities	Individual Variable Annuities
Zero or no surrender charge	$45,361	$10,813	$12,591
0% - 2%	6,734	4,068	5,424
Greater than 2% - 4%	3,872	6,665	5,589
Greater than 4%	3,241	27,182	9,355
Non-Surrenderable	877	3,442	92
Total	$60,085	$52,170	$33,051

** Excludes mutual funds of $7.6 billion.*

Surrender rates increased for group retirement products and individual fixed annuities for the first six months of 2007 compared to the same period in 2006. Surrender rates for group retirement products increased as a result of an increase in mutual fund and group annuity surrenders. New products have been introduced to retain assets and AIG has retained or attracted over $795 million in assets in the first six months of 2007. The increase in the surrender rate for fixed annuities continues to be driven by a relatively flat yield curve and the general aging of the in-force block; however, less than 21 percent of the individual fixed annuity reserves as of June 30, 2007 were available to be surrendered without charge. Individual variable annuities surrender rates were lower in the first six months of 2007 compared to the same period in 2006.

An increase in the level of surrenders in any of these businesses or in the individual fixed annuities runoff block could accelerate the amortization of DAC and negatively affect fee income earned on assets under management.

The following table presents the net flows[a] by line of business:

	Three Months Ended June 30,		Six Months Ended June 30,	
(in millions)	**2007**	2006	**2007**	2006
Group retirement products[b]	**$ 236**	$ 194	**$ 134**	$ 635
Individual fixed annuities	**(675)**	(873)	**(1,512)**	(1,019)
Individual variable annuities	**18**	88	**(85)**	(45)
Individual fixed annuities – runoff	**(229)**	(258)	**(492)**	(486)
Total	**$(650)**	$(849)	**$(1,955)**	$ (915)

(a) Net flows are defined as deposits received less benefits, surrenders, withdrawals and death benefits.
(b) Includes mutual funds.

Higher surrenders in the group retirement and individual fixed annuity blocks, offset somewhat by increased deposits on both blocks, resulted in negative net flows for the first six months of 2007. The continuation of the current interest rate and competitive environment could prolong this trend.

Life Insurance & Retirement Services Net Investment Income and Net Realized Capital Gains (Losses)

The following table summarizes the components of Net investment income:

(in millions)	Three Months Ended June 30, 2007	Three Months Ended June 30, 2006	Six Months Ended June 30, 2007	Six Months Ended June 30, 2006
Foreign Life Insurance & Retirement Services:				
Fixed maturities, including short-term investments	**$2,099**	$1,831	**$ 4,208**	$3,486
Equity securities	**101**	95	**165**	166
Interest on mortgage, policy and collateral loans	**114**	111	**227**	219
Partnership income	**38**	23	**86**	40
Unit investment trusts[(a)]	**235**	184	**321**	184
Other[(b)]	**78**	114	**142**	183
Total investment income before policyholder trading gains (losses)	**2,665**	2,358	**5,149**	4,278
Policyholder trading gains (losses)[(c)]	**784**	(321)	**1,259**	69
Total investment income	**3,449**	2,037	**6,408**	4,347
Investment expenses	**88**	67	**164**	122
Net investment income	**$3,361**	$1,970	**$ 6,244**	$4,225
Domestic Life Insurance:				
Fixed maturities, including short-term investments	**$ 870**	$ 829	**$ 1,781**	$1,699
Equity securities	**(1)**	–	**(2)**	2
Interest on mortgage, policy and collateral loans	**102**	84	**202**	169
Partnership income — excluding Synfuels	**60**	2	**87**	12
Partnership income (loss) — Synfuels	**(42)**	(22)	**(75)**	(59)
Unit investment trusts	**2**	–	**4**	–
Other[(b)]	**26**	16	**40**	30
Total investment income	**1,017**	909	**2,037**	1,853
Investment expenses	**11**	16	**26**	27
Net investment income	**$1,006**	$ 893	**$ 2,011**	$1,826
Domestic Retirement Services:				
Fixed maturities, including short-term investments	**$1,364**	$1,390	**$ 2,764**	$2,828
Equity securities	**21**	2	**24**	5
Interest on mortgage, policy and collateral loans	**135**	111	**256**	215
Partnership income — excluding Synfuels	**253**	70	**383**	201
Other[(b)]	**4**	(3)	**(8)**	(20)
Total investment income before policyholder trading gains (losses)	**1,777**	1,570	**3,419**	3,229
Investment expenses	**12**	13	**29**	26
Net investment income	**$1,765**	$1,557	**$ 3,390**	$3,203
Total:				
Fixed maturities, including short-term investments	**$4,333**	$4,050	**$ 8,753**	$8,013
Equity securities	**121**	97	**187**	173
Interest on mortgage, policy and collateral loans	**351**	306	**685**	603
Partnership income — excluding Synfuels	**351**	95	**556**	253
Partnership income (loss) — Synfuels	**(42)**	(22)	**(75)**	(59)
Unit investment trusts[(a)]	**237**	184	**325**	184
Other[(b)]	**108**	127	**174**	193
Total investment income before policyholder trading gains (losses)	**5,459**	4,837	**10,605**	9,360
Policyholder trading gains (losses)[(c)]	**784**	(321)	**1,259**	69
Total investment income	**6,243**	4,516	**11,864**	9,429
Investment expenses	**111**	96	**219**	175
Net investment income[(d)]	**$6,132**	$4,420	**$11,645**	$9,254

(a) Includes the effect of an out of period UCITS adjustment in the second quarter of 2006. For the three and six-month periods ended June 30, 2006 the effect was an increase of $221 million and $203 million, respectively, in net investment income and $144 million and $132 million, respectively, in operating income.

(b) Other includes real estate income, income on non-partnership invested assets, securities lending and Foreign Life Insurance & Retirement Services' equal share of the results of AIG Credit Card Company (Taiwan).

(c) Relates principally to assets held in various trading securities accounts that do not qualify for separate account treatment under SOP 03-1. These amounts are offset by an equal change included in incurred policy losses and benefits.

(d) Includes call and tender income.

Net investment income increased for the three and six-month periods ended June 30, 2007 compared to the same periods in 2006. Fixed maturities income rose as the underlying invested asset base grew. Yield enhancement activity increased over the same period in 2006. Earnings on certain interests in unit investment trusts allocated to policyholder accounts through incurred policy losses and benefits for the current quarter and year-to-date include earnings of $148 million and

$189 million, respectively, compared to $64 million for both the second quarter and first six months in 2006, respectively. Policyholder trading gains (losses) increased for both the quarter and year-to-date compared to the same period in 2006 and generally follow the trend of equity markets in the respective periods. Net investment income for certain operations include investments in structured notes linked to emerging market sovereign debt that incorporates both interest rate risk and currency risk. For 2007, these investments generated income of $23 million and $45 million for the three and six-month periods ended June 30, 2007, respectively, compared to losses of $51 million and $32 million for the same periods in 2006. In addition, period to period comparisons of investment income for some investment activities, particularly partnership income, are affected by yield enhancement activity, as shown in the above table.

See also Insurance and Asset Management Invested Assets herein.

AIG generates income tax credits as a result of investing in synthetic fuel production (synfuels) related to the investment loss shown in the above table and records those benefits in its provision for income taxes. The amounts of those income tax credits were $118 million and $61 million for the first six months of 2007 and 2006, respectively. For a further discussion of the effect of fluctuating domestic crude oil prices on synfuel tax credits, see Note 6(c) of Notes to Consolidated Financial Statements.

The following table summarizes Net realized capital gains (losses) by major category:

	Three Months Ended June 30,		Six Months Ended June 30,	
(in millions)	**2007**	2006	**2007**	2006
Foreign Life Insurance & Retirement Services:				
Sales of fixed maturities	**$ (25)**	$(125)	**$ (45)**	$(146)
Sales of equity securities	**180**	250	**212**	401
Other:				
Foreign exchange transactions	**(25)**	(95)	**90**	(90)
Derivatives instruments	**52**	87	**(65)**	346
Other-than-temporary decline	**(131)**	(4)	**(462)**	(45)
Other*	**(33)**	51	**53**	50
Total Foreign Life Insurance & Retirement Services	**$ 18**	$ 164	**$(217)**	$ 516
Domestic Life Insurance:				
Sales of fixed maturities	**$ (58)**	$ (39)	**$ (39)**	$ (61)
Sales of equity securities	**4**	4	**5**	6
Other:				
Foreign exchange transactions	**–**	1	**2**	–
Derivatives instruments	**41**	28	**30**	115
Other-than-temporary decline	**(49)**	(61)	**(68)**	(115)
Other	**46**	(8)	**42**	(12)
Total Domestic Life Insurance	**$ (16)**	$ (75)	**$ (28)**	$ (67)
Domestic Retirement Services:				
Sales of fixed maturities	**$ (79)**	$ (41)	**$ (60)**	$ (88)
Sales of equity securities	**5**	17	**16**	31
Other:				
Foreign exchange transactions	**1**	–	**7**	–
Derivatives instruments	**(52)**	(42)	**(47)**	(36)
Other-than-temporary decline	**(144)**	(169)	**(186)**	(261)
Other	**(12)**	(11)	**(20)**	(36)
Total Domestic Retirement Services	**$(281)**	$(246)	**$(290)**	$(390)
Total:				
Sales of fixed maturities	**$(162)**	$(205)	**$(144)**	$(295)
Sales of equity securities	**189**	271	**233**	438
Other:				
Foreign exchange transactions	**(24)**	(94)	**99**	(90)
Derivative instruments	**41**	73	**(82)**	425
Other-than-temporary decline	**(324)**	(234)	**(716)**	(421)
Other	**1**	32	**75**	2
Total:	**$(279)**	$(157)	**$(535)**	$ 59

** Includes gains of $66 million and losses of $19 million allocated to participating policyholders for the three-month periods ended June 30, 2007 and 2006, respectively, and losses of $5 million and gains of $48 million for the first six months of 2007 and 2006, respectively.*

Net realized capital gains (losses) include normal portfolio transactions as well as derivative gains (losses) for transactions that did not qualify for hedge accounting treatment under FAS 133, foreign exchange gains and losses and other-than-temporary declines in the value of investments. Net realized capital losses in the Foreign Life operations in the first six months of 2007 include losses of $65 million related to derivatives that did not qualify for hedge accounting treatment compared to a gain of $346 million in the same period in 2006. Derivatives in the Foreign Life operations are primarily used to economically hedge cash flows related to U.S. dollar bonds back to the

respective currency of the country, principally in Taiwan, Thailand, and Singapore. The corresponding foreign exchange gain or loss with respect to the economically hedged bond is deferred in Accumulated other comprehensive income until the bond is sold or deemed to be other than temporarily impaired. In the first six months of 2007, Foreign Life operations incurred losses of $462 million for the decline in the value of securities deemed to be other than temporarily impaired. A significant portion of those losses was related to the decline in value of U.S. dollar bonds held in Thailand and Singapore reflecting the depreciation of the U.S. dollar against the local currencies.

Deferred Policy Acquisition Costs, Sales Inducement Assets and Future Policy Benefit Reserves

DAC for Life Insurance & Retirement Services products arises from the deferral of those costs that vary with, and are directly related to, the acquisition of new or renewal business. Policy acquisition costs for life insurance products are generally deferred and amortized over the premium paying period of the policy. Policy acquisition costs that relate to universal life and investment-type products, including variable and fixed annuities (investment-oriented products), are deferred and amortized, with interest, as appropriate, in relation to the historical and future incidence of estimated gross profits to be realized over the estimated lives of the contracts. Total acquisition costs deferred decreased $118 million in the first six months of 2007 compared to the first six months in 2006 primarily due to lower Domestic Life sales. Total amortization expense increased $79 million compared to the first six months in 2006. Annualized amortization expense levels for 2007 and 2006 are approximately 12 percent and 14 percent, respectively, of the opening DAC balance.

The following table summarizes the major components of the changes in DAC/Value of Business Acquired (VOBA) and Sales Inducement Assets (SIA):

	Six Months Ended June 30,					
(in millions)	**2007**			2006		
	DAC/VOBA	**SIA**	**Total**	DAC/VOBA	SIA	Total
Foreign Life Insurance & Retirement Services						
Balance at beginning of year	**$21,153**	**$ 404**	**$21,557**	$17,638	$ 192	$17,830
Acquisition costs deferred	**2,510**	**60**	**2,570**	2,479	34	2,513
Amortization charged to income or credited to operating income:						
Related to net realized capital gains (losses)	**45**	**1**	**46**	1	—	1
Related to unlocking future assumptions	**30**	**2**	**32**	28	—	28
All other amortization	**(1,344)**	**2**	**(1,342)**	(1,292)	(14)	(1,306)
Change in unrealized gains (losses) on securities	**531**	**7**	**538**	81	—	81
Increase (decrease) due to foreign exchange	**(230)**	**1**	**(229)**	936	9	945
Other *	**(78)**	**—**	**(78)**	—	—	—
Balance at end of period	**$22,617**	**$ 477**	**$23,094**	$19,871	$ 221	$20,092
Domestic Life Insurance						
Balance at beginning of year	**$ 6,006**	**$ 46**	**$ 6,052**	$ 5,184	$ 31	$ 5,215
Acquisition costs deferred	**442**	**10**	**452**	617	10	627
Amortization charged to income or credited to operating income:						
Related to net realized capital gains (losses)	**4**	**—**	**4**	17	—	17
All other amortization	**(344)**	**(3)**	**(347)**	(350)	(1)	(351)
Change in unrealized gains (losses) on securities	**230**	**—**	**230**	717	—	717
Increase (decrease) due to foreign exchange	**45**	**—**	**45**	20	—	20
Other *	**(64)**		**(64)**	—	—	—
Balance at end of period	**$ 6,319**	**$ 53**	**$ 6,372**	$ 6,205	$ 40	$ 6,245
Domestic Retirement Services						
Balance at beginning of year	**$ 5,651**	**$ 887**	**$ 6,538**	$ 5,284	$ 871	$ 6,155
Acquisition costs deferred	**376**	**101**	**477**	360	117	477
Amortization charged to income or credited to operating income:						
Related to net realized capital gains (losses)	**52**	**12**	**64**	72	12	84
Related to unlocking future assumptions	**2**	**—**	**2**	(1)	—	(1)
All other amortization	**(445)**	**(79)**	**(524)**	(394)	(64)	(458)
Change in unrealized gains (losses) on securities	**318**	**64**	**382**	1,099	190	1,289
Balance at end of period	**$ 5,954**	**$ 985**	**$ 6,939**	$ 6,420	$1,126	$ 7,546

(in millions)	Six Months Ended June 30,					
	2007			2006		
	DAC/VOBA	**SIA**	**Total**	DAC/VOBA	SIA	Total
Total Life Insurance & Retirement Services						
Balance at beginning of year	**$32,810**	**$1,337**	**$34,147**	$28,106	$1,094	$29,200
Acquisition costs deferred	**3,328**	**171**	**3,499**	3,456	161	3,617
Amortization charged to income or credited to operating income:						
Related to net realized capital gains (losses)	**101**	**13**	**114**	90	12	102
Related to unlocking future assumptions	**32**	**2**	**34**	27	—	27
All other amortization	**(2,133)**	**(80)**	**(2,213)**	(2,036)	(79)	(2,115)
Change in unrealized gains (losses) on securities	**1,079**	**71**	**1,150**	1,897	190	2,087
Increase (decrease) due to foreign exchange	**(185)**	**1**	**(184)**	956	9	965
Other *	**(142)**	**—**	**(142)**	—	—	—
Balance at end of period	**$34,890**	**$1,515**	**$36,405**	$32,496	$1,387	$33,883

** Primarily represents the cumulative effect of adoption of SOP 05-1.*

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

Future Policy Benefit Reserves

Periodically, the net benefit reserves (policy benefit reserves less DAC) established for life and retirement services companies are tested to ensure that, including consideration of future expected premium payments, they are adequate to provide for future policyholder benefit obligations. The assumptions used to perform the tests are current best-estimate assumptions as to policyholder mortality, morbidity, terminations, company maintenance expenses and invested asset returns. For long duration traditional business, a "lock-in" principle applies, whereby the assumptions used to calculate the benefit reserves and DAC are set when a policy is issued and do not change with changes in actual experience. These assumptions include margins for adverse deviation in the event that actual experience might deviate from these assumptions. For business in force outside of North America, 46 percent of total policyholder benefit liabilities at June 30, 2007 resulted from traditional business where the lock-in principle applies. In most foreign locations, guarantees have been made to pay benefits to policyholders for many decades into the future.

As experience changes over time, the best-estimate assumptions are updated to reflect the observed changes. Because of the long-term nature of many of AIG's liabilities subject to the lock-in principle, small changes in certain of the assumptions may cause large changes in the degree of reserve adequacy that exists. In particular, changes in estimates of future invested asset return assumptions have a large effect on the degree of reserve adequacy that exists.

Taiwan

Beginning in calendar year 2000, the yield available on Taiwanese 10-year government bonds dropped from approximately 6 percent to approximately 2.5 percent at June 30, 2007. Yields on most other invested assets have correspondingly dropped over the same period of time. Current sales are focused on products such as a) variable separate account products which do not contain interest rate guarantees, b) participating products which contain very low implied interest rate guarantees, and c) A&H policies and riders.

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

- Observed historical mortality improvement trends have been projected to 2014;
- Morbidity, expense and termination rates have been updated to reflect recent experience;
- Taiwan government bond rates are expected to remain at current levels for 10 years and gradually increase to best estimate assumptions of a market consensus view of long-term interest rate expectations. Foreign assets are assumed to comprise 35 percent of invested assets, resulting in a composite long-term investment assumption of approximately 4.7 percent; and
- The currently permitted practice of offsetting positive mortality experience with negative interest margins, thus eliminating the need for mortality dividends, will continue.

Future results of the reserve adequacy tests are uncertain given the long-term nature of the business and the volatility inherent in actual investment yields. The inability to achieve assumed investment returns could accelerate DAC amortization and necessitate reserve strengthening.

Financial Services Operations

AIG's Financial Services subsidiaries engage in diversified activities including aircraft and equipment leasing, capital markets, consumer finance and insurance premium finance.

Financial Services Results

Financial Services results were as follows:

(in millions)	Three Months Ended June 30, **2007**	2006	Percentage Increase/ (Decrease)	Six Months Ended June 30, **2007**	2006	Percentage Increase/ (Decrease)
Revenues:						
Aircraft Leasing[(a)]	**$1,173**	$1,051	12%	**$ 2,231**	$ 2,063	8%
Capital Markets[(b)(c)]	**(67)**	(788)	–	**161**	(1,088)	–
Consumer Finance[(d)(e)]	**949**	942	1	**1,832**	1,867	(2)
Other, including intercompany adjustments	**68**	41	66	**100**	70	43
Total	**$2,123**	$1,246	70%	**$ 4,324**	$ 2,912	48%
Operating income (loss):						
Aircraft Leasing[(a)]	**$ 207**	$ 198	5%	**$ 371**	$ 374	(1)%
Capital Markets[(b)(c)]	**(255)**	(952)	–	**(187)**	(1,422)	–
Consumer Finance[(d)(e)]	**75**	202	(63)	**111**	378	(71)
Other, including intercompany adjustments	**20**	22	(9)	**44**	32	38
Total	**$ 47**	$ (530)	–%	**$ 339**	$ (638)	–%

(a) Revenues are primarily aircraft lease rentals from ILFC. Both revenues and operating income include gains (losses) from hedging activities that did not qualify for hedge accounting treatment under FAS 133, including the related foreign exchange gains and losses. For the three-month periods ended June 30, 2007 and 2006, the effect was $24 million and $10 million, respectively. For the six-month periods ended June 30, 2007 and 2006, the effect was $(13) million and $55 million, respectively. These amounts result primarily from interest rate and foreign currency derivatives that are effective economic hedges of borrowings. In the second quarter of 2007, ILFC began applying hedge accounting to most of its derivatives hedging interest rate and foreign exchange risks associated with its floating rate and foreign currency denominated borrowings.

(b) Revenues, shown net of interest expense of $805 million and $633 million for the three-month periods ended June 30, 2007 and 2006, respectively, and $1.9 billion and $1.3 billion for the six-month periods ended June 30, 2007 and 2006, respectively, were primarily from hedged financial positions entered into in connection with counterparty transactions. Both revenues and operating income include gains (losses) from hedging activities that did not qualify for hedge accounting treatment under FAS 133, including the related foreign exchange gains and losses. For the three-month periods ended June 30, 2007 and 2006, the effect was $(528) million and $(1.2) billion, respectively. For the six-month periods ended June 30, 2007 and 2006, the effect was $(613) million and $(1.8) billion, respectively. The second quarter and the first six months of 2007 include out of period charges of $431 million and $326 million, respectively, including a $380 million charge in both periods to reverse net gains recognized on transfers of available for sale securities among legal entities consolidated within AIGFP. The first six months of 2006 include an out of period charge of $300 million related to the remediation of the material weakness in accounting for certain derivative transactions under FAS 133. In the first quarter of 2007, AIGFP began applying hedge accounting for certain transactions.

(c) Certain transactions entered into by AIGFP generate tax credits and benefits which are included in income taxes in the consolidated statement of income. The amounts of such tax credits and benefits for the three-month periods ended June 30, 2007 and 2006 were $18 million and $8 million, respectively. The amounts of such tax credits and benefits for the six-month periods ended June 30, 2007 and 2006 were $35 million and $26 million, respectively.

(d) Revenues are primarily finance charges. Both revenues and operating income include gains (losses) from hedging activities that did not qualify for hedge accounting treatment under FAS 133, including the related foreign exchange gains and losses. For the three-month periods ended June 30, 2007 and 2006, the effect was $20 million and $5 million, respectively. For the six-month periods ended June 30, 2007 and 2006, the effect was $(15) million and $8 million, respectively. These amounts result primarily from interest rate and foreign currency derivatives that are effective economic hedges of borrowings. In the second quarter of 2007, AGF began applying hedge accounting to most of its derivatives hedging interest rate and foreign exchange risks associated with its floating rate and foreign currency denominated borrowings.

(e) The three-month and six-month periods ended June 30, 2007 included pre-tax charges of $50 million and $178 million, respectively, in connection with domestic consumer finance's mortgage banking activities.

Financial Services operating income increased in the three and six-month periods ended June 30, 2007 compared to the same periods in 2006 primarily due to differences in the accounting treatment for hedging activities. In the first quarter of 2007, AIGFP began applying hedge accounting to certain of its interest rate swaps and foreign currency forward contracts hedging its investments and borrowings. In the second quarter of 2007, AGF and ILFC began applying hedge accounting to most of their derivatives hedging interest rate and foreign exchange risks associated with their floating rate and foreign currency denominated borrowings. During 2006, hedge accounting under FAS 133 was not being applied to any of the derivatives and related assets and liabilities. Accordingly, revenues and operating income were exposed to volatility resulting from differences in the timing of revenue recognition between the derivatives and the related hedged assets and liabilities.

The second quarter and the first six months of 2007 included out of period charges of $431 million and $326 million, respectively, of which $380 million was to reverse net gains recognized on transfers of available for sale securities among legal entities consolidated within AIGFP.

The first six months of 2006 included an out of period charge of $300 million related to the remediation of the material weakness in accounting for certain derivative transactions under FAS 133.

Beginning in the first quarter of 2007, net realized capital gains and losses, including derivative gains and losses and foreign exchange transaction gains and losses for Financial Services entities other than AIGFP, which were previously reported as part of AIG's Other category, are now included in Financial Services revenues and operating income. For the three and six-month periods ended June 30, 2007, the amount included in both Financial Services revenues and operating income was a gain of $63 million and a loss of $4 million, respectively. All prior periods have been revised to conform to the current presentation.

Aircraft Leasing

AIG's Aircraft Leasing operations represent the operations of ILFC, which generates its revenues primarily from leasing new and used commercial jet aircraft to foreign and domestic airlines. Revenues also result from the remarketing of commercial jets for ILFC's own account, and remarketing and fleet management services for airlines and financial institutions. ILFC finances its aircraft purchases primarily through the issuance of debt instruments. ILFC hedges the majority of its floating rate and foreign currency denominated debt using interest rate and foreign currency derivatives. Starting in the second quarter of 2007, ILFC began applying hedge accounting to most of its derivatives. All of ILFC's derivatives are effective economic hedges; however, since hedge accounting under FAS 133 was not applied prior to April 2, 2007, the benefits of using derivatives to hedge these exposures are not reflected in ILFC's 2006 corporate borrowing rate. The composite borrowing rates at June 30, 2007 and 2006 were 5.25 percent and 5.01 percent, respectively.

ILFC typically contracts to re-lease aircraft before the end of the existing lease term. For aircraft returned before the end of the lease term, ILFC has generally been able to re-lease such aircraft within two to six months of its return. As a lessor, ILFC considers an aircraft "idle" or "off lease" when the aircraft is not subject to a signed lease agreement or signed letter of intent. ILFC had no aircraft off lease at June 30, 2007, and all new aircraft scheduled for delivery through 2007 have been leased.

Quarterly Aircraft Leasing Results

ILFC's operating income increased in the three months ended June 30, 2007 compared to the same period of 2006 by $9 million, or 5 percent. Rental revenues increased by $136 million or 14 percent, driven by a larger aircraft fleet and higher lease rates. During the three months ended June 30, 2007, ILFC's fleet subject to operating leases increased by 38 airplanes to a total of 894. The increase in rental revenues was partially offset by increases in depreciation and interest expense. During the second quarter of 2007, ILFC did not sell any aircraft compared to three aircraft sold in the same period in 2006, resulting in a decrease in revenues of $18 million from the comparative period. Depreciation expense increased by $49 million, or 13 percent, in line with the increase in the size of the aircraft fleet. Interest expense increased by $71 million, or 21 percent, driven by rising cost of funds, a weaker U.S. dollar against the Euro and the British Pound and additional borrowings to fund aircraft purchases. As noted above, ILFC's interest expense did not reflect the benefit of hedging these exposures in 2006. For the three-month periods ended June 30, 2007 and 2006, the gains from hedging activities that did not qualify for hedge accounting treatment under FAS 133, including the related foreign exchange gains and losses, were $24 million and $10 million, respectively, in both revenues and operating income.

Year-to-date Aircraft Leasing Results

ILFC's operating income decreased in the first six months of 2007 compared to the same period of 2006 by $3 million, or 1 percent. Rental revenues increased by $273 million or 14 percent, driven by a larger aircraft fleet and higher lease rates. During the first six months of 2007, ILFC's fleet subject to operating leases increased by 70 airplanes to a total of 894. The increase in rental revenues was partially offset by increases in depreciation and interest expense. During the first six months of 2007, ILFC sold one aircraft compared to six aircraft sold in the same period in 2006, resulting in a decrease in revenues of $35 million compared to the same period in 2006. Depreciation expense increased by $92 million, or 12 percent, in line with the increase in the size of the aircraft fleet. Interest expense increased by $142 million, or 22 percent, driven by rising cost of funds, a weaker U.S. dollar against the Euro and the British Pound and additional borrowings to fund aircraft purchases. ILFC's interest expense did not reflect the benefit of hedging these exposures in the first quarter of 2007 and in 2006. For the first six months of 2007 and 2006, the gains (losses) from hedging activities that did not qualify for hedge accounting treatment under FAS 133, including the related foreign exchange gains and losses, were $(13) million and $55 million, respectively, in both revenues and operating income.

Capital Markets

Capital Markets represents the operations of AIGFP, which engages as principal in a wide variety of financial transactions, including standard and customized financial products involving commodities, credit, currencies, energy, equities and rates. AIGFP also invests in a diversified portfolio of securities and principal investments and engages in borrowing activities involving issuing standard and

structured notes and other securities, and entering into guaranteed investment agreements (GIAs).

Beginning in 2007, AIGFP applied hedge accounting under FAS 133 to certain of its interest rate swaps and foreign currency forward contracts hedging its investments and borrowings. As a result, AIGFP recognized in earnings the change in the fair value on the hedged items attributable to the hedged risks offsetting the gains and losses on the derivatives designated as hedges. Prior to 2007, AIGFP did not apply hedge accounting under FAS 133 to any of its derivatives or related assets and liabilities.

Since 1998, AIGFP has written super senior (AAA+) protection through credit default swaps, a portion of which is exposed to CDOs of residential mortgage-backed securities and other asset-backed securities. At June 30, 2007, the notional amount of this credit derivative portfolio was $465 billion, including $64 billion from transactions with mixed collateral that include U.S. subprime mortgages. As of August 6, 2007, all of AIGFP's super senior exposures continued to have tranches below AIGFP's attachment point which have been explicitly rated AAA or would have been rated AAA had they been rated. AIGFP's portfolio of credit default swaps is carefully structured, undergoes regular monitoring, modeling and analysis and contains significant protection through collateral subordination. In addition, in December 2005, AIGFP stopped committing to writing super senior protection for CDOs that included any subprime collateral. For a further description of AIGFP's risk management practices in its credit default swaps business, see Management's Discussion and Analysis of Financial Condition and Results of Operations — Risk Management — Segment Risk Management — Financial Services in the 2006 Annual Report on Form 10-K.

Quarterly Capital Markets Results

Capital Markets operating income increased in the three months ended June 30, 2007 by $697 million compared to the same period in 2006. During the second quarter of 2007, AIGFP experienced increased transaction flow in its equity, credit and currency products.

In addition, AIGFP recognized a net loss of $528 million related to hedging activities that did not qualify for hedge accounting treatment under FAS 133, compared to a net loss of $1.2 billion for the same period in 2006. The net loss in the second quarter of 2007 includes out of period charges of $431 million, including a charge of $380 million to reverse net gains recognized in previous periods on transfers of available for sale securities among legal entities consolidated within AIGFP. The net loss also reflects the effect of increases in U.S. interest rates and the slight weakening of the U.S. Dollar on derivatives hedging AIGFP's assets and liabilities.

Financial market conditions in the three months ended June 30, 2007 were characterized by sizable increases in global interest rates, increases in credit spreads, higher equity valuations and a slightly weaker U.S. dollar.

The most significant component of Capital Markets operating expenses is compensation, which was $153 million and $129 million in the three-month periods ended June 30, 2007 and 2006, respectively. The amount of compensation was not affected by gains and losses arising from derivatives not qualifying for hedge accounting treatment under FAS 133.

AIG elected to early adopt FAS 155, "Accounting for Certain Hybrid Financial Instruments" (FAS 155) in 2006 and AIGFP elected to apply the fair value option to certain structured notes and other financial liabilities containing embedded derivatives outstanding as of January 1, 2006. AIGFP recognized a gain of $196 million in the second quarter of 2007 and a loss of $98 million in the second quarter of 2006 on hybrid financial instruments for which it applied the fair value option under FAS 155. These amounts were largely offset by gains and losses on economic hedge positions also reflected in AIGFP's operating income.

Year-to-date Capital Markets Results

Capital Markets operating income increased in the first six months of 2007 by $1.2 billion compared to the same period in 2006, as AIGFP experienced higher transaction flow in the first six months of 2007 in its equity and commodity products. AIGFP also recognized a net loss of $613 million related to hedging activities that did not qualify for hedge accounting treatment under FAS 133, compared to a net loss of $1.8 billion for the same period in 2006. The first six months of 2007 included out of period charges of $326 million, as noted above, and a $166 million reduction in fair value at March 31, 2007 of certain derivatives that are an integral part of, and economically hedge, the structured transactions potentially affected by the proposed regulations issued by the U.S. Treasury Department discussed above in Overview of Operations and Business — Outlook. The net loss on AIGFP's derivatives recognized in the first six months of 2006 included an out of period charge of $300 million related to the remediation of the material weakness in accounting for certain derivative transactions under FAS 133. The net loss also reflects the effect of increases in U.S. interest rates and a weakening of the U.S. Dollar on derivatives hedging AIGFP's assets and liabilities.

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

The most significant component of Capital Markets operating expenses is compensation, which was $276 million and $265 million in the first six months of 2007 and 2006, respectively. The amount of compensation was not affected

by gains and losses arising from derivatives not qualifying for hedge accounting treatment under FAS 133.

AIGFP recognized a gain of $30 million in the first six months of 2007 and a loss of $89 million in the first six months of 2006 on hybrid financial instruments for which it applied the fair value option under FAS 155. These amounts were largely offset by gains and losses on economic hedge positions also reflected in AIGFP's operating income.

Consumer Finance

AIG's consumer finance operations in North America are principally conducted through AGF. On January 2, 2007, AGF expanded its operations into the United Kingdom through the acquisition of Ocean Finance and Mortgages Limited, a finance broker for home owner loans in the United Kingdom. AGF derives a substantial portion of its revenues from finance charges assessed on outstanding real estate loans, secured and unsecured non-real estate loans and retail sales finance receivables. The real estate loans are comprised principally of first-lien mortgages on residential real estate generally having a maximum term of 360 months, and are considered non-conforming. The real estate loans may be closed-end accounts or open-end home equity lines of credit and are principally fixed rate products. AGF does not offer mortgage products with borrower payment options that allow for negative amortization of the principal balance. The secured non-real estate loans are secured by consumer goods, automobiles or other personal property. Both secured and unsecured non-real estate loans and retail sales finance receivables generally have a maximum term of 60 months. The majority of AGF's finance receivables are sourced through its branches. However, a significant volume of real estate loans is also sourced through broker relationships, and to lesser extents, through correspondent relationships and direct mail solicitations.

AGF also conducts mortgage banking activities through its centralized real estate operations. It originates residential real estate loans, the majority of which are sold to investors on a servicing-released basis. These loans are collateralized by first and second-liens on one to four family properties and are originated largely through broker relationships and to a lesser extent are originated directly to consumers or through correspondent relationships. These real estate loans usually have maximum original terms of 360 months and generally have higher credit quality than the real estate loans sourced through its branches. These real estate loans are generally considered non-conforming and include fixed, adjustable and hybrid adjustable loans. From July 2003 through February 2006, these loans were originated through an arrangement with AIG Federal Savings Bank (AIG Bank), a federally chartered thrift. The origination relationship was terminated in the first quarter of 2006. Since then, all new loans have been originated directly by AGF subsidiaries under their own state licenses.

On June 7, 2007, AIG's domestic consumer finance operations, consisting of AIG Bank, AGF's mortgage banking subsidiary Wilmington Finance, Inc. (WFI) and AGF entered into a Supervisory Agreement with the Office of Thrift Supervision (OTS). The Supervisory Agreement pertains to certain mortgage loans originated in the name of AIG Bank from July 2003 through early May 2006 pursuant to a servicing agreement between WFI and AIG Bank, which was terminated in February 2006. Pursuant to the terms of the Supervisory Agreement, AIG Bank, WFI and AGF agreed to implement a financial remediation program whereby certain borrowers may be provided loans on more affordable terms and/or reimbursement of certain fees. The Supervisory Agreement also requires AGF to engage the services of an external consultant to monitor, evaluate and periodically report to the OTS with respect to the matters covered by the Supervisory Agreement. Separately, the domestic consumer finance operations also committed to donate $15 million to certain not-for-profit organizations to support their efforts to promote financial literacy and credit counseling.

Management's best estimate of the cost of implementing the financial remediation plan contemplated by the Supervisory Agreement, including the $15 million donation, was $178 million at June 30, 2007. A charge in the amount of $128 million was recorded in the first quarter of 2007 while the remaining $50 million was recorded in the second quarter of 2007 at the time the terms of the Supervisory Agreement were finalized. As the estimate is based on judgments and assumptions made by management, the actual cost of implementing the financial remediation plan may differ from this estimate.

AIG's foreign consumer finance operations are principally conducted through AIG Consumer Finance Group, Inc. (AIGCFG). AIGCFG operates primarily in emerging and developing markets. AIGCFG has operations in Argentina, China, Hong Kong, Mexico, Philippines, Poland, Taiwan and Thailand and most recently began operations in India through the acquisition of a majority interest in a sales finance lending operation during the first quarter of 2007 and the acquisition of a mortgage lending operation in the second quarter of 2007. In addition, AIGCFG expanded its distribution channels in Thailand by acquiring in the first quarter of 2007 an 80 percent interest in a company with a network of over 130 branches for secured consumer lending. Certain of the AIGCFG operations are partly or wholly owned by life insurance subsidiaries of AIG. Accordingly, the financial results of those companies are allocated between Financial Services and Life Insurance & Retirement Services according to their ownership percentages. While products vary by market, the businesses generally provide credit cards, unsecured and secured non-real estate loans, term deposits, savings accounts, retail sales finance and real estate loans. AIGCFG originates finance receivables through its branches and direct solicitation. AIGCFG also originates finance

receivables indirectly through relationships with retailers, auto dealers, and independent agents.

Quarterly Consumer Finance Results

Consumer Finance operating income decreased by $127 million, or 63 percent, in the three months ended June 30, 2007 compared to the same period in 2006.

The operating income from the domestic consumer finance operations, which include the operations of AGF and AIG Bank, decreased by $127 million, or 68 percent, for the three months ended June 30, 2007 compared to the same period in 2006. Pursuant to the terms of the Supervisory Agreement, as discussed above, a charge of $50 million was recorded in the second quarter of 2007. Additionally, for the three months ended June 30, 2007, domestic results were adversely affected by the slower housing market, higher interest rates on most long-term fixed rate loans and evolving changes in the regulatory environment which resulted in lower originations for both investment and held for sale real estate loans. For the three months ended June 30, 2007, results from mortgage banking activities included lower net gains on sales of real estate loans held for sale as well as an $11 million increase in the provision for AGF's warranty reserve compared to the same period in 2006, which covers its obligations to repurchase loans sold to third-party investors should there be a first payment default or breach of representations and warranties.

AGF's finance receivables totaled $24.9 billion as of June 30, 2007, including $19.2 billion of loans for which some or all of the collateral consisted of real estate, and which were predominantly underwritten with full income verification. As of June 30, 2007, the 60-day delinquency rate for these real estate loans was 1.95 percent (based on outstanding loan balances, consistent with mortgage lending practice). The overall credit quality of AGF's finance receivables during the three months ended June 30, 2007 remained stable. AGF's net charge-off rate increased to 1.02 percent compared to 0.86 percent in the same period in 2006. The 60-day delinquency rate for all finance receivable types increased from 1.75 percent at June 30, 2006 to 2.18 percent at June 30, 2007.

AGF's interest expense increased by $18 million or 6 percent as both its short-term and long-term borrowing rates increased in the three months ended June 30, 2007 compared to the same period in 2006. During the three months ended June 30, 2007, AGF recorded a net gain of $17 million on its derivatives that did not qualify for hedge accounting under FAS 133, including the related foreign exchange losses, compared to a net gain of $2 million for the same period in 2006. Commencing in the second quarter of 2007, AGF began applying hedge accounting.

Revenues from the foreign consumer finance operations increased by approximately 26 percent in the three months ended June 30, 2007 compared to the same period in 2006. Loan growth, particularly in Poland and Argentina, was the primary driver behind the higher revenues.

Year-to-date Consumer Finance Results

Consumer Finance operating income decreased by $267 million, or 71 percent, in the first six months of 2007 compared to the same period of 2006.

The operating income for the first six months of 2007 from the domestic consumer finance operations, which includes the operations of AGF and AIG Bank, decreased by $311 million or 81 percent from the same period of 2006. Pursuant to the terms of the Supervisory Agreement, as discussed above, charges of $178 million were recorded during the first six months of 2007.

Additionally, for the first six months of 2007, domestic results were adversely affected by the slower housing market, higher interest rates on most long-term fixed rate loans and evolving changes in the regulatory environment which resulted in lower originations for both investment and held for sale real estate loans. For the first six months of 2007, results from mortgage banking activities included a $36 million increase in the provision for AGF's warranty reserve compared to the same period in 2006. Although mortgage loan originations declined in the first six months of 2007, the softening of home price appreciation (reducing the equity customers may be able to extract from their homes by refinancing) and higher mortgage loan interest rates contributed to an increase in non-real estate loans of 12 percent at June 30, 2007 compared to June 30, 2006. Retail sales finance receivables also increased 22 percent compared to June 30, 2006 due to increased marketing efforts and customer demand. AGF's results for the first six months of 2007 also included $65 million from a favorable out of court settlement.

The credit quality of AGF's finance receivables during the first six months of 2007 remained stable. Its net charge-off ratio increased to 1.00 percent compared to 0.87 percent in the same period in 2006, which reflected $6 million of non-recurring recoveries that were recorded in the first quarter of 2006. AGF's delinquency ratio remained relatively low, although it increased by 43 basis points to 2.18 percent at June 30, 2007 compared to June 30, 2006. AGF's allowance for finance receivables losses as a percentage of outstanding receivables was 2.04 percent at June 30, 2007 compared to 2.07 percent at June 30, 2006. The allowance for finance receivables losses includes an allowance for catastrophe-related losses relating to hurricane Katrina of $11 million at June 30, 2007 compared to $54 million at June 30, 2006.

AGF's interest expense increased by $64 million or 11 percent as both its short-term and long-term borrowing rates increased in the first six months of 2007 compared to the same period of 2006. Its short-term borrowing rates

averaged 5.40 percent in the first six months of 2007 compared to 4.85 percent in the same period of 2006, while long-term borrowing rates averaged 5.19 percent in the first six months of 2007 compared to 4.89 percent in the first six months of 2006.

For the first six months of 2007, domestic consumer finance revenues and operating income also declined from the prior year, partially due to the change in fair value of the derivatives hedging borrowings which did not qualify for hedge accounting treatment under FAS 133 during either period. During the first six months of 2007, AGF recorded a net loss of $19 million on such derivatives, including the related foreign exchange losses, compared to a net gain of $4 million for the same period in 2006. Commencing in the second quarter of 2007, AGF began applying hedge accounting.

Revenues from the foreign consumer finance operations increased by 22 percent in the first six months of 2007 compared to the same period of 2006. Loan growth, particularly in Poland and Argentina, was the primary driver behind the higher revenues. Operating income in the first six months of 2006 reflects AIGCFG's $44 million share of the allowance for losses related to industry-wide credit deterioration in the Taiwan credit card market.

Asset Management Operations

AIG's Asset Management operations comprise a wide variety of investment-related services and investment products. Such services and products are offered to individuals and institutions both domestically and overseas, and are primarily comprised of Spread-Based Investment Businesses, Institutional Asset Management and Brokerage Services and Mutual Funds.

The revenues and operating income for this segment are affected by the general conditions in the equity and credit markets. In addition, net realized gains and performance fees are contingent upon various fund closings, maturity levels and market conditions.

Spread-Based Investment Business

In prior years, the sale of GICs to investors, both domestically and overseas, was AIG's primary institutional Spread-Based Investment Business. During 2005, AIG launched its MIP and its asset management subsidiaries, primarily SunAmerica Life, ceased writing new GIC business. The GIC business will continue to run off for the foreseeable future while the MIP business is expected to grow.

Institutional Asset Management

AIG's Institutional Asset Management business provides an array of investment products and services globally to institutional investors, AIG subsidiaries and affiliates and high net worth investors. These products and services include traditional equity and fixed income investment management and a full range of alternative asset classes. Delivery of AIG's Institutional Asset Management products and services is accomplished via a global network of operating subsidiaries comprising AIG Global Asset Management Holdings Corp. and its subsidiaries and affiliated companies (collectively, AIG Investments). The primary operating entities within this group are AIG Global Investment Corp., AIG Global Real Estate Investment Corp. and AIG Private Bank. AIG Private Bank offers banking, trading and investment management services to private client and high net worth individuals and institutions globally.

Within the alternative investment asset class, AIG Investments offers hedge and private equity fund-of-funds, direct investments and distressed debt investments. Within the structured fixed income and equity product asset class, AIG Investments offers various forms of structured and credit linked notes, various forms of collateralized debt obligations and other investment strategies aimed at achieving superior returns or capital preservation. In addition, Institutional Asset Management's product offerings include various forms of principal protected and liability management structures.

Brokerage Services and Mutual Funds

AIG's Brokerage Services and Mutual Funds business provides mutual fund and broker-dealer related services to retail investors, group trusts and corporate accounts through an independent network of financial advisors. The AIG Advisor Group, Inc., a subsidiary of AIG Retirement Services, Inc., is comprised of several broker-dealer entities that provide these services to clients primarily in the U.S. marketplace. AIG SunAmerica Asset Management Corp. manages, advises and/or administers retail mutual funds, as well as the underlying assets of variable annuities sold by AIG SunAmerica and VALIC to individuals and groups throughout the United States.

Other

Included in the Other category for Asset Management is income or loss from certain SunAmerica sponsored partnerships and partnership investments. Partnership assets consist of investments in a diversified portfolio of private equity funds, affordable housing partnerships and hedge fund investments.

Asset Management Results

Asset Management results were as follows:

(in millions)	Three Months Ended June 30, **2007**	2006	Percentage Increase/ (Decrease)	Six Months Ended June 30, **2007**	2006	Percentage Increase/ (Decrease)
Revenues:						
Spread-Based Investment Business	**$ 734**	$ 697	5%	**$1,749**	$1,372	27%
Institutional Asset Management	**1,077**	666	62	**1,745**	992	76
Brokerage Services and Mutual Funds	**82**	73	12	**160**	146	10
Other	**96**	79	22	**243**	144	69
Total	**$1,989**	$1,515	31%	**$3,897**	$2,654	47%
Operating income:						
Spread-Based Investment Business	**$ 244**	$ 216	13%	**$ 735**	$ 423	74%
Institutional Asset Management*	**770**	473	63	**1,103**	631	75
Brokerage Services and Mutual Funds	**21**	21	–	**47**	44	7
Other	**93**	75	24	**237**	136	74
Total	**$1,128**	$ 785	44%	**$2,122**	$1,234	72%

** Includes a total of $223 million and $270 million for the three-month periods ended June 30, 2007 and 2006, respectively, and $451 million and $366 million for the six-month periods ended June 30, 2007 and 2006, respectively, of income from certain AIG managed partnerships, private equity and real estate funds that are consolidated. Such income is offset in minority interest expense, which is not a component of operating income, on the consolidated statement of income.*

Asset Management operating income increased in the three-month period ended June 30, 2007 compared to the same period in 2006 primarily due to higher investment gains, including a gain of $398 million from the sale of a portion of AIG's investment in Blackstone Group, LP in connection with its initial public offering. Asset Management operating income increased in the six-month period ended June 30, 2007 compared to the same period in 2006 due to the aforementioned investment gains as well as growth in both the Spread-Based Investment business and the Institutional Asset Management business. Gains and losses arising from the consolidation of certain partnerships, private equity investments and real estate funds are included in operating income, but are offset in minority interest expense, which is not a component of operating income.

Beginning in the first quarter of 2007, net realized capital gains and losses, including derivative gains and losses and foreign exchange transaction gains and losses, which were previously reported as part of AIG's Other category, are now included in Asset Management revenues and operating income. For the three and six-month periods of 2007, the amount included in both Asset Management revenues and operating income was a gain of $352 million and $332 million, respectively. The three and six-month periods of 2006 reflected losses of $8 million and $3 million, respectively. All prior periods have been revised to conform to the current presentation.

Quarterly Spread-Based Investment Business Results

Operating income related to the Spread-Based Investment business increased in the three months ended June 30, 2007 compared to the same period in 2006 due to an increase in partnership income associated with the Domestic GIC program and higher income from hedge funds and private equity partnerships. Partnership income is primarily derived from alternative investments and is affected by performance in the equity markets. Thus, revenues, operating income and cash flows attributable to GICs will vary from reporting period to reporting period.

Offsetting this growth in operating income was the continued runoff of GIC balances. A significant portion of the remaining GIC portfolio consists of floating rate obligations. AIG has entered into hedges to manage against increases in short-term interest rates. AIG believes these hedges are economically effective, but they did not qualify for hedge accounting treatment under FAS 133. Income or loss from these hedges are classified as net realized capital gains or losses in the Asset Management segment results.

The following table illustrates the anticipated runoff of the domestic GIC portfolio at June 30, 2007:

(in billions)	Less Than One Year	1-3 Years	3+-5 Years	Over Five Years	Total
Domestic GICs	$3,879	$12,944	$2,721	$ 6,663	$26,207

MIP operating income, which is reported in the Spread-Based Investment business, declined during the three months ended June 30, 2007 compared to the same period of 2006 primarily due to foreign exchange losses on foreign-denominated debt that, while economically hedged, did not qualify for hedge accounting treatment under FAS 133, including a $36 million out of period loss recorded in the second quarter of 2007.

During 2005, the MIP replaced the GIC program as AIG's principal institutional spread-based investment activity. AIG does not expect that income growth in the MIP will offset the runoff in the GIC portfolio for the foreseeable future because the asset mix under the MIP does not include

the alternative investments utilized in the GIC program. Commencing with transactions initiated in the first quarter of 2007, AIG applied hedge accounting for certain derivative transactions related to the MIP.

Year-to-date Spread-Based Investment Business Results

Operating income related to the Spread-Based Investment business increased in the first six months of 2007 compared to the same period of 2006 due to a significant increase in partnership income associated with the Domestic GIC program and increased returns from hedge funds and private equity partnerships. Partnership income in the first six months of 2007 included a distribution from a single partnership of $164 million, which became available after a five-year restriction on capital withdrawals.

MIP operating income grew in the first six months of 2007 compared to the same period of 2006, reflecting increased issuance activity. Through June 30, 2007, AIG has issued the equivalent of $6.3 billion of securities to fund the MIP in the Euromarkets and the U.S. public and private markets.

In order to better align financial reporting with the manner in which AIG's chief operating decision makers have managed their businesses, commencing in the first quarter of 2007, revenues and operating income related to foreign investment contracts, which were historically reported as a component of the Spread-Based Investment business, are now being reported in the Life Insurance & Retirement Services segment. All prior periods have been revised to conform to the current presentation.

Quarterly Institutional Asset Management Results

Operating income for Institutional Asset Management increased in the three months ended June 30, 2007 compared to the same period of 2006, reflecting the $398 million gain from the sale of a portion of AIG's investment in Blackstone Group, LP in connection with its initial public offering. Operating income for the three months ended June 30, 2007 was negatively affected by a decline in net realized capital gains related to real estate investments, as well as carried interest on private equity investments, which were particularly strong during the same period of 2006. Also negatively affecting operating income was a decrease in carried interest, which was driven by lower valuations of portfolio investments and is generally associated with performance in the equity markets, and lower gains on certain consolidated investments and partnerships. These gains are offset in minority interest expense, which is not a component of operating income, on the Consolidated Statement of Income.

Year-to-date Institutional Asset Management Results

Operating income for Institutional Asset Management increased in the first six months of 2007 compared to the same period of 2006 reflecting the $398 million gain from the sale of a portion of AIG's investment in Blackstone Group, LP in connection with its initial public offering and increased carried interest driven by higher valuations of portfolio investments which are generally associated with improved performance in the equity markets. Operating income also reflects higher gains on certain consolidated investments and partnerships; however, these gains are offset in minority interest expense. Partly offsetting these gains was a decrease in net realized capital gains related to real estate investments as well as increased expenses resulting from investment in sales and infrastructure enhancements.

AIG's unaffiliated client assets under management, including retail mutual funds and institutional accounts, increased 15 percent to $86.5 billion from December 31, 2006 to June 30, 2007, contributing to growth in its base management fees. Additionally, AIG Investments successfully launched several new private equity and real estate funds in the first half of 2007, which provide both a base management fee and the opportunity for future performance fees.

While unaffiliated client assets under management and the resulting management fees continue to increase, the growth in operating income has trailed the growth in revenues due to higher fund-related expenses as well as sales and infrastructure enhancements. The fund-related expenses are associated with investments acquired and held in anticipation of future fund launches. It is anticipated that these expenses will be recovered from fund entities in future periods. The sales and infrastructure enhancements are associated with AIG's planned expansion of marketing and distribution capabilities, combined with technology and operational infrastructure-related improvements.

Other Operations

The operating loss of AIG's Other category was as follows:

	Three Months Ended June 30,		Six Months Ended June 30,	
(in millions)	**2007**	2006	**2007**	2006
Other operating income (loss):				
Equity earnings in unconsolidated entities	**$ 50**	$ 111	**$ 91**	$ 130
Interest expense	**(302)**	(223)	**(554)**	(406)
Unallocated corporate expenses	**(200)**	(64)	**(362)**	(248)
Compensation expense – SICO Plans	**(10)**	(14)	**(20)**	(90)
Compensation expense – Starr tender offer	**–**	–	**–**	(54)
Net realized capital gains (losses)	**22**	(49)	**(27)**	(54)
Other miscellaneous, net	**(20)**	(19)	**(58)**	(45)
Total Other	**$(460)**	$(258)	**$(930)**	$(767)

The operating loss of AIG's Other category increased in the second quarter and first six months of 2007 compared to the comparable periods in 2006, reflecting higher interest expenses resulting from increased borrowings in the parent company, higher unallocated corporate expenses primarily resulting from ongoing efforts to improve internal controls, an increase in a provision for certain foreign payroll tax obligations to $60 million, higher incentive plan costs and lower income from unconsolidated entities.

Operating loss for the first six months of 2006 included an out of period charge of $61 million related to the SICO Plans and a one-time charge related to the Starr tender offer of $54 million.

Beginning in the first quarter of 2007, derivative gains and losses and foreign exchange transaction gains and losses for Asset Management and Financial Services entities (other than AIGFP) are now included in Asset Management and Financial Services revenues and operating income. These amounts were previously reported as part of AIG's Other category. All prior periods have been revised to conform to the current presentation.

Capital Resources and Liquidity

At June 30, 2007, AIG had total consolidated shareholders' equity of $104.3 billion and total consolidated borrowings of $165.3 billion. At that date, $148.1 billion of such borrowings were not guaranteed by AIG, were matched borrowings by AIG or AIGFP, or represented junior subordinated debt or liabilities connected to trust preferred stock.

Borrowings

At June 30, 2007, AIG's net borrowings were $17.2 billion, excluding amounts that were matched borrowings by AIG and AIGFP, amounts not guaranteed by AIG, junior subordinated debt and liabilities connected to trust preferred stock.

The following table summarizes borrowings outstanding:

(in millions)	**June 30, 2007**	December 31, 2006
AIG's net borrowings	**$ 17,225**	$ 17,126
Junior subordinated debt	**4,585**	–
Liabilities connected to trust preferred stock	**1,440**	1,440
MIP matched notes and bonds payable	**11,756**	5,468
Series AIGFP matched notes and bonds payable	**371**	72
AIGFP		
GIAs	**19,451**	20,664
Matched notes and bonds payable	**38,626**	35,776
Hybrid financial instrument liabilities*	**8,155**	8,856
Borrowings not guaranteed by AIG	**63,693**	59,277
Eliminations	**8**	–
Total	**$165,310**	$148,679

** Represents structured notes issued by AIGFP that are accounted for using the fair value option.*

Borrowings issued or guaranteed by AIG and subsidiary borrowings not guaranteed by AIG were as follows:

(in millions)	**June 30, 2007**	December 31, 2006
AIG borrowings:		
Notes and bonds payable	**$ 9,742**	$ 8,915
Junior subordinated debt	**4,585**	–
Loans and mortgages payable	**178**	841
MIP matched notes and bonds payable	**11,756**	5,468
Series AIGFP matched notes and bonds payable	**371**	72
Total AIG Borrowings	**26,632**	15,296
Borrowings guaranteed by AIG:		
AIGFP		
GIAs	**19,451**	20,664
Notes and bonds payable	**40,666**	37,528
Hybrid financial instrument liabilities[(a)]	**8,155**	8,856
Total	**68,272**	67,048
AIG Funding, Inc. commercial paper	**4,468**	4,821
AGC Notes and bonds payable	**797**	797
Liabilities connected to trust preferred stock	**1,440**	1,440
Total borrowings issued or guaranteed by AIG	**101,609**	89,402
Borrowings not guaranteed by AIG:		
ILFC		
Commercial paper	**4,177**	2,747
Junior subordinated debt	**999**	999
Notes and bonds payable[(b)]	**26,951**	25,592
Total	**32,127**	29,338

(in millions)	**June 30, 2007**	December 31, 2006
AGF		
Commercial paper	**4,683**	4,328
Junior subordinated debt	**346**	–
Notes and bonds payable	**19,032**	19,595
Total	**24,061**	23,923
AIGCFG		
Commercial paper	**290**	227
Loans and mortgages payable	**1,506**	1,453
Total	**1,796**	1,680
AIG Finance Taiwan Limited commercial paper	**27**	26
Other Subsidiaries	**741**	672

(in millions)	**June 30, 2007**	December 31, 2006
Borrowings of consolidated investments:		
A.I. Credit	**880**	880
AIG Investments	**1,145**	193
AIG Global Real Estate Investment	**2,712**	2,307
AIG SunAmerica	**195**	203
ALICO	**9**	55
Total	**4,941**	3,638
Total borrowings not guaranteed by AIG	**63,693**	59,277
Eliminations	**8**	–
Total Debt	**$165,310**	$148,679

(a) Represents structured notes issued by AIGFP that are accounted for using the fair value option.

(b) Includes borrowings under Export Credit Facility of $2.8 billion at June 30, 2007 and $2.7 billion at December 31, 2006.

The debt activity, excluding commercial paper of $13.65 billion and borrowings of consolidated investments of $4.94 billion, for the six months ended June 30, 2007 was as follows:

(in millions)

	Balance at December 31, 2006	Issuances	Maturities and Repayments	Effect of Foreign Exchange	Other Changes	**Balance at June 30, 2007**
AIG						
Notes and bonds payable	$ 8,915	$ 850	$ (65)	$ 38	$ 4	**$ 9,742**
Junior subordinated debt	–	4,490	–	95	–	**4,585**
Loans and mortgages payable	841	46	(714)	5	–	**178**
MIP matched notes and bonds payable	5,468	6,320	–	9	(41)	**11,756**
Series AIGFP matched notes and bonds payable	72	298	–	–	1	**371**
AIGFP						
GIAs	20,664	4,186	(4,655)	–	(744)	**19,451**
Notes and bonds payable and hybrid financial instrument liabilities	46,384	24,763	(21,598)	104	(832)	**48,821**
AGC notes and bonds payable	797	–	–	–	–	**797**
Liabilities connected to trust preferred stock	1,440	–	–	–	–	**1,440**
ILFC notes and bonds payable	25,592	3,399	(2,170)	123	7	**26,951**
ILFC junior subordinated debt	999	–	–	–	–	**999**
AGF notes and bonds payable	19,595	1,718	(2,796)	75	440	**19,032**
AGF junior subordinated debt	–	346	–	–	–	**346**
AIGCFG loans and mortgages payable	1,453	1,945	(1,917)	25	–	**1,506**
Other subsidiaries	672	154	(168)	(4)	87	**741**
Eliminations	–	–	–	28	(20)	**8**
Total	$132,892	$48,515	$(34,083)	$ 498	$ (1,098)	**$ 146,724**

AIG (Parent Company)

AIG intends to continue its customary practice of issuing debt securities from time to time to meet its financing needs and those of certain of its subsidiaries for general corporate purposes, as well as for the MIP. As of June 30, 2007, AIG had up to $16.6 billion of debt securities, preferred and common stock and other securities registered and available for issuance under its universal shelf registration statement. In July 2007, AIG's new universal shelf registration statement was declared effective. The new registration statement includes the securities registered on its existing shelf registration statement and results in AIG having up to $22 billion of debt securities, preferred stock and other securities, including up to $16.5 billion of common stock, registered and available for issuance from time to time.

AIG maintains a medium term note program under its shelf registration statement. As of June 30, 2007, approximately $4.1 billion principal amount of notes were outstanding under the medium term note program, of which $749 million was used for AIG's general corporate purposes, $371 million was used by AIGFP and $2.9 billion was used to fund the MIP. The maturity dates of these notes range from 2008 to 2052. To the extent deemed appropriate, AIG may enter into swap transactions to manage its effective borrowing rates with respect to these notes. In connection with AIG's new universal shelf registration statement, in July 2007, AIG increased the size of its medium term note program, allowing AIG to issue from time to time up to $22 billion of its registered debt securities in the form of medium term notes.

AIG also maintains a Euro medium term note program under which, as of June 30, 2007, an aggregate nominal amount of up to $10.0 billion of notes may be outstanding at any one time. As of June 30, 2007, the equivalent of $9.4 billion of notes were outstanding under the program, of which $7.4 billion were used to fund the MIP and the remainder was used for AIG's general corporate purposes. The aggregate amount outstanding includes $284 million resulting from foreign exchange translation into U.S. dollars, of which $198 million relates to notes issued by AIG for general corporate purposes and $86 million relates to notes issued to fund the MIP.

During the first six months of 2007, AIG issued in Rule 144A offerings an aggregate of $1.5 billion principal amount of senior notes, of which $650 million was used to fund the MIP and $850 million was used for AIG's general corporate purposes.

AIG maintains a shelf registration statement in Japan, providing for the issuance of up to Japanese Yen 300 billion principal amount of senior notes, of which the equivalent of $400 million was outstanding as of June 30, 2007, the proceeds of which were used for AIG's general corporate purposes. AIG also maintains an Australian dollar debt program under which senior notes with an aggregate principal amount of up to 5 billion Australian dollars may be outstanding at any one time. Although as of June 30, 2007 there were no outstanding notes under the Australian program, AIG intends to use the program opportunistically to fund the MIP or for AIG's general corporate purposes.

In June 2007, AIG issued $750 million of 6.45 percent Series A-4 junior subordinated debentures (Series A-4 Debentures), the proceeds of which were used for general corporate purposes, including the repurchase of shares of AIG common stock. Subject to the Replacement Capital Covenant (RCC) described below, the Series A-4 Debentures are scheduled for repayment in 2047 and have a final maturity in 2077. The Series A-4 Debentures are redeemable by AIG at par beginning in 2012.

AIG issued three series of junior subordinated debentures in March 2007, which, together with the Series A-4 Debentures, totaled $4.59 billion outstanding as of June 30, 2007. In connection with each Series of junior subordinated debentures, AIG entered into an RCC for the benefit of the holders of AIG's 6.25 percent notes due 2036. The RCCs provide that AIG will not repay, redeem, or purchase the applicable series of junior subordinated debentures on or before a specified date (which, in the case of the Series A-4 Debentures, is June 15, 2057), unless it has received qualifying proceeds from the sale of replacement capital securities.

AIG began applying hedge accounting for certain AIG parent transactions in the first quarter of 2007.

AIGFP

AIGFP uses the proceeds from the issuance of notes and bonds and GIA borrowings to invest in a diversified portfolio of securities and derivative transactions. The borrowings may also be temporarily invested in securities purchased under agreements to resell. AIGFP's notes and bonds include structured debt instruments whose payment terms are linked to one or more financial or other indices (such as an equity index or commodity index or another measure that is not considered to be clearly and closely related to the debt instrument). These notes contain embedded derivatives that otherwise would be required to be accounted for separately under FAS 133. Upon AIG's early adoption of FAS 155, AIGFP elected the fair value option for these notes. The notes that are accounted for using the fair value option are reported separately under hybrid financial instrument liabilities. AIG guarantees the obligations of AIGFP under AIGFP's notes and bonds and GIA borrowings. See Operating Review — Financial Services Operations, Liquidity and Derivatives herein.

AIGFP has a Euro medium term note program under which an aggregate nominal amount of up to $10.0 billion of notes may be outstanding at any one time. As of June 30, 2007, $7.04 billion of notes were outstanding under the program, including $748 million resulting from foreign exchange translation into U.S. dollars. The notes issued under this program are guaranteed by AIG and are included in AIGFP's Notes and Bonds Payable in the preceding table of borrowings.

AIG Funding

AIG Funding, Inc. (AIG Funding) issues commercial paper that is guaranteed by AIG in order to help fulfill the short-term cash requirements of AIG and its subsidiaries. The issuance of AIG Funding's commercial paper, including the guarantee by AIG, is subject to the approval of AIG's Board of Directors or the Finance Committee of the Board if it exceeds certain pre-approved limits.

As backup for the commercial paper program and for other general corporate purposes, AIG and AIG Funding maintain revolving credit facilities, which, as of June 30, 2007, had an aggregate of $5.4 billion available to be drawn and which are summarized below under Revolving Credit Facilities. In July 2007, AIG and AIG Funding renewed their 364-day syndicated revolving credit facility and increased its size by $500 million to $2.125 billion.

ILFC

ILFC fulfills its short-term cash requirements through operating cash flows and the issuance of commercial paper. The issuance of commercial paper is subject to the approval of ILFC's Board of Directors and is not guaranteed by AIG. ILFC maintains syndicated revolving credit facilities which,

as of June 30, 2007, totaled $6.5 billion and which are summarized below under Revolving Credit Facilities. These facilities are used as back up for ILFC's maturing debt and other obligations.

As a well-known seasoned issuer, ILFC has filed an automatic shelf registration statement with the SEC allowing ILFC immediate access to the U.S. public debt markets. At June 30, 2007, $4.35 billion of debt securities were issued under this registration statement and $5.84 billion were issued under a prior registration statement. In addition, ILFC has a Euro medium term note program for $7.0 billion, under which $4.28 billion in notes were outstanding at June 30, 2007. Notes issued under the Euro medium term note program are included in ILFC notes and bonds payable in the preceding table of borrowings. The foreign exchange adjustment for the foreign currency denominated debt was $855 million at June 30, 2007 and $733 million at December 31, 2006. ILFC has substantially eliminated the currency exposure arising from foreign currency denominated notes by economically hedging the portion of the note exposure not already offset by Euro-denominated operating lease payments.

ILFC had a $4.3 billion Export Credit Facility for use in connection with the purchase of approximately 75 aircraft delivered through 2001. This facility was guaranteed by various European Export Credit Agencies. The interest rate varies from 5.75 percent to 5.90 percent on these amortizing ten-year borrowings depending on the delivery date of the aircraft. At June 30, 2007, ILFC had $806 million outstanding under this facility. The debt is collateralized by a pledge of the shares of a subsidiary of ILFC, which holds title to the aircraft financed under the facility.

In May 2004, ILFC entered into a similarly structured Export Credit Facility for up to a maximum of $2.64 billion for Airbus aircraft to be delivered through May 31, 2005. The facility was subsequently increased to $3.64 billion and extended to include aircraft to be delivered through May 31, 2008. The facility becomes available as the various European Export Credit Agencies provide their guarantees for aircraft based on a six-month forward-looking calendar, and the interest rate is determined through a bid process. At June 30, 2007, ILFC had $2.0 billion outstanding under this facility. Borrowings with respect to these facilities are included in ILFC's notes and bonds payable in the preceding table of borrowings.

From time to time, ILFC enters into funded financing agreements. As of June 30, 2007, ILFC had a total of $1.1 billion outstanding, which has varying maturities through February 2012. The interest rates are LIBOR-based, with spreads ranging from 0.30 percent to 1.625 percent.

The proceeds of ILFC's debt financing are primarily used to purchase flight equipment, including progress payments during the construction phase. The primary sources for the repayment of this debt and the interest expense thereon are the cash flow from operations, proceeds from the sale of flight equipment and the rollover and refinancing of the prior debt. AIG does not guarantee the debt obligations of ILFC. See also Operating Review — Financial Services Operations and Liquidity herein.

AGF

AGF fulfills most of its short-term cash borrowing requirements through the issuance of commercial paper. The issuance of commercial paper is subject to the approval of AGF's Board of Directors and is not guaranteed by AIG. AGF maintains committed syndicated revolving credit facilities which, as of June 30, 2007, totaled $4.25 billion and which are summarized below under Revolving Credit Facilities. The facilities can be used for general corporate purposes and to provide backup for AGF's commercial paper programs. In July 2007, AGF resyndicated its 364-day revolving credit facility and increased its size by $500 million to $2.625 billion.

As of June 30, 2007, notes and bonds aggregating $19.03 billion were outstanding with maturity dates ranging from 2007 to 2031 at interest rates ranging from 1.94 percent to 8.45 percent. To the extent deemed appropriate, AGF may enter into swap transactions to manage its effective borrowing rates with respect to these notes and bonds. As a well-known seasoned issuer, AGF filed an automatic shelf registration statement with the SEC allowing AGF immediate access to the U.S. public debt markets. At June 30, 2007, AGF had the corporate authorization to issue up to $12.2 billion of debt securities under its shelf registration statements.

AGF's funding sources include a medium term note program, private placement debt, retail note issuances, bank financing and securitizations of finance receivables that AGF accounts for as on-balance-sheet secured financings. In addition, AGF has become an established issuer of long-term debt in the international capital markets.

In addition to debt refinancing activities, proceeds from the collection of finance receivables are used to fund cash needs including the payment of principal and interest on AGF's debt. AIG does not guarantee any of the debt obligations of AGF. See also Operating Review — Financial Services Operations and Liquidity herein.

AIGCFG

AIGCFG has a variety of funding mechanisms for its various markets, including retail and wholesale deposits, short-term and long-term bank loans, and intercompany subordinated debt. AIG Credit Card Company (Taiwan), a consumer finance business in Taiwan, and AIG Finance (Thailand) PLC have issued commercial paper for the funding of their respective operations. AIG does not guarantee any

borrowings for AIGCFG businesses, including this commercial paper.

Revolving Credit Facilities

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

As of June 30, 2007 (in millions)

Facility	Size	Borrower(s)	Available Amount	Expiration	One-Year Term-Out Option
AIG:					
364-Day Syndicated Facility[(a)]	$1,625	AIG/AIG Funding[(b)] AIG Capital Corporation[(b)]	**$1,625**	July 2007[(a)]	Yes
5-Year Syndicated Facility	1,625	AIG/AIG Funding[(b)] AIG Capital Corporation[(b)]	**1,625**	July 2011	No
364-Day Bilateral Facility[(c)]	3,200	AIG/AIG Funding	**154**	November 2007	Yes
364-Day Intercompany Facility[(d)]	2,000	AIG	**2,000**	October 2007	Yes
Total AIG	$8,450		**$5,404**		
ILFC:					
5-Year Syndicated Facility	$2,500	ILFC	**$2,500**	October 2011	No
5-Year Syndicated Facility	2,000	ILFC	**2,000**	October 2010	No
5-Year Syndicated Facility	2,000	ILFC	**2,000**	October 2009	No
Total ILFC	$6,500		**$6,500**		
AGF:					
364-Day Syndicated Facility[(e)]	$2,125	American General Finance Corporation American General Finance, Inc.[(f)]	**$2,125**	July 2007[(e)]	Yes
5-Year Syndicated Facility	2,125	American General Finance Corporation	**2,125**	July 2010	No
Total AGF	$4,250		**$4,250**		

(a) In July 2007, the size of this facility was increased to $2.125 billion and the expiration was extended to July 2008.
(b) Guaranteed by AIG.
(c) This facility can be drawn in the form of loans or letters of credit. All drawn amounts shown above are in the form of letters of credit.
(d) Subsidiaries of AIG are the lenders on this facility.
(e) In July 2007, the size of this facility was increased to $2.625 billion and the expiration was extended to July 2008.
(f) American General Finance, Inc. is an eligible borrower for up to $400 million only.

Credit Ratings

The cost and availability of unsecured financing for AIG and its subsidiaries are generally dependent on their short-term and long-term debt ratings. The following table presents the credit ratings of AIG and certain of its subsidiaries as of July 31, 2007. In parentheses, following the initial occurrence in the table of each rating, is an indication of that rating's relative rank within the agency's rating categories. That ranking refers only to the generic or major rating category and not to the modifiers appended to the rating by the rating agencies to denote relative position within such generic or major category.

	Short-term Debt			Senior Long-term Debt		
	Moody's	S&P	Fitch	Moody's(a)	S&P(b)	Fitch(c)
AIG	P-1 (1st of 3)	A-1+ (1st of 6)	F1+ (1st of 5)	Aa2 (2nd of 9)	AA (2nd of 8)	AA (2nd of 9)
AIG Financial Products Corp.[(d)]	P-1	A-1+	–	Aa2	AA	–
AIG Funding, Inc.[(d)]	P-1	A-1+	F1+	–	–	–
ILFC	P-1	A-1+	F1(1st of 5)	A1(3rd of 9)	AA-[(e)](2nd of 8)	A+(3rd of 9)
American General Finance Corporation	P-1	A-1(1st of 6)	F1	A1	A+ (3rd of 8)	A+
American General Finance, Inc.	P-1	A-1	F1	–	–	A+

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

(b) Standard & Poor's, a division of the McGraw-Hill Companies (S&P). S&P ratings may be modified by the addition of a plus or minus sign to show relative standing within the major rating categories.

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

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

(e) Negative rating outlook. A negative outlook by S&P indicates that a rating may be lowered, but is not necessarily a precursor of a ratings change. The outlook on all other credit ratings in the table is stable.

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

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

AIG believes that any of its own or its subsidiaries' contractual obligations that are subject to "ratings triggers" or financial covenants relating to "ratings triggers" would not have a material adverse effect on its financial condition or liquidity. Ratings downgrades could also trigger the application of termination provisions in certain of AIG's contracts, principally agreements entered into by AIGFP and assumed reinsurance contracts entered into by Transatlantic.

It is estimated that, as of the close of business on July 31, 2007, based on AIGFP's outstanding municipal GIAs and financial derivatives transactions as of such date, a downgrade of AIG's long-term senior debt ratings to 'Aa3' by Moody's or 'AA–' by S&P would permit counterparties to call for approximately $847 million of collateral. Further, additional downgrades could result in requirements for substantial additional collateral, which could have a material effect on how AIGFP manages its liquidity. The actual amount of additional collateral that AIGFP would be required to post to counterparties in the event of such downgrades depends on market conditions, the fair value of the outstanding affected transactions and other factors prevailing at the time of the downgrade. Additional obligations to post collateral would increase the demand on AIGFP's liquidity.

Contractual Obligations and Other Commercial Commitments

The maturity schedule of AIG's contractual obligations at June 30, 2007 was as follows:

(in millions)	Total Payments	Payments due by Period: Less Than One Year	1-3 Years	3+-5 Years	Over Five Years
Borrowings[(a)]	$146,724	$ 38,307	$ 32,060	$ 34,714	$ 41,643
Interest payments on borrowings	84,018	6,164	10,668	7,338	59,848
Loss reserves[(b)]	82,209	22,607	25,075	11,920	22,607
Insurance and investment contract liabilities[(c)]	606,340	27,737	35,180	41,227	502,196
GIC liabilities[(d)]	32,619	5,235	14,175	3,659	9,550
Aircraft purchase commitments	20,928	890	6,765	2,445	10,828
Total	$972,838	$100,940	$123,923	$101,303	$646,672

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

(b) Represents future loss and loss adjustment expense payments estimated based on historical loss development payment patterns.

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

(d) Represents guaranteed maturities under GICs.

The maturity schedule of other commercial commitments of AIG and its consolidated subsidiaries at June 30, 2007 was as follows:

(in millions)	Total Amounts Committed	Amount of Commitment Expiration: Less Than One Year	1-3 Years	3+-5 Years	Over Five Years
Letters of credit:					
Life Insurance & Retirement Services	$ 185	$ 17	$ 4	$ 22	$ 142
Parent Company[(a)]	753	631	1	121	–
DBG	195	195	–	–	–
Standby letters of credit:					
Capital Markets	1,728	1,458	70	40	160
Guarantees:					
Life Insurance & Retirement Services[(b)]	2,148	75	45	537	1,491
Aircraft Leasing	200	–	51	28	121
Asset Management	410	135	73	32	170
General Insurance	40	40	–	–	–
Other commercial commitments[(c)]:					
Capital Markets[(d)]	17,196	4,556	2,448	3,131	7,061
Aircraft Leasing[(e)]	344	–	–	–	344
Other Financial Services companies	11	8	–	–	3
Life Insurance & Retirement Services[(f)]	5,502	1,418	1,860	1,278	946
Asset Management[(g)]	1,616	1,249	234	116	17
General Insurance companies[(h)]	1,774	607	784	366	17
Parent and other companies	304	139	134	31	–
Total	$32,406	$10,528	$5,704	$5,702	$10,472

(a) Represents reimbursement obligations under letters of credit issued by commercial banks.

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

(c) Excludes commitments with respect to pension plans. The annual pension contribution for 2007 is expected to be approximately $95 million for U.S. and non-U.S. plans.

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

(e) Primarily in connection with options to acquire aircraft.

(f) Primarily AIG SunAmerica commitments to invest in partnerships.

(g) Includes commitments to invest in limited partnerships, private equity and hedge funds and commitments to purchase and develop real estate in the U.S. and abroad.

(h) Primarily commitments to invest in limited partnerships.

Shareholders' Equity

AIG's consolidated shareholders' equity increased during the first six months of 2007 as follows:

(in millions)	June 30, 2007
Beginning of year	**$101,677**
Net income	8,407
Unrealized appreciation (depreciation) of investments, net of tax	(712)
Cumulative translation adjustment, net of tax	(294)
Dividends to shareholders	(949)
Payments advanced to purchase shares	(2,336)
Share repurchase	(1,680)
Other*	217
End of period	**$104,330**

** Reflects the effects of employee stock transactions and cumulative effect of accounting changes.*

AIG has in the past reinvested most of its unrestricted earnings in its operations and believes such continued reinvestment in the future will be adequate to meet any foreseeable capital needs. However, AIG may choose from time to time to raise additional funds through the issuance of additional securities.

In February 2007, AIG's Board of Directors adopted a new dividend policy, which took effect with the dividend declared in the second quarter of 2007, providing that under ordinary circumstances, AIG's plan will be to increase its common stock dividend by approximately 20 percent annually. The payment of any dividend, however, is at the discretion of AIG's Board of Directors, and the future payment of dividends will depend on various factors, including the performance of AIG's businesses, AIG's consolidated financial position, results of operations and liquidity and the existence of investment opportunities.

Share Repurchases

From time to time, AIG may buy shares of its common stock for general corporate purposes, including to satisfy its obligations under various employee benefit plans. In February 2007, AIG's Board of Directors increased AIG's share repurchase program by authorizing the repurchase of shares with an aggregate purchase price of $8 billion. During March 2007, AIG entered into a $3 billion structured share repurchase arrangement and in May 2007, AIG entered into an additional $1 billion structured share repurchase arrangement. A total of 24,491,961 shares were repurchased during the first six months of 2007. The portion of the payments advanced by AIG under the structured share repurchase arrangements that had not yet been utilized to repurchase shares at June 30, 2007, amounting to $2.34 billion, has been recorded as a component of shareholders' equity under the caption, Payments advanced to purchase shares. Purchases have continued subsequent to June 30, 2007, with an additional 24,501,510 shares purchased from July 1 through August 6, 2007. All shares repurchased are recorded as treasury stock at cost.

Liquidity

AIG manages liquidity at both the subsidiary and parent company levels. At June 30, 2007, AIG's consolidated invested assets, primarily held by its subsidiaries, included $29.4 billion in cash and short-term investments. Consolidated net cash provided from operating activities in the first six months of 2007 amounted to $15.1 billion. At the parent company level, liquidity management activities are conducted in a manner to preserve and enhance funding stability, flexibility, and diversity through the full range of potential operating environments and market conditions. AIG's primary sources of cash flow are dividends and other payments from its regulated and unregulated subsidiaries, as well as issuances of debt securities. Primary uses of cash flow are for debt service, subsidiary funding, shareholder dividend payments and common stock repurchases. Management believes that AIG's liquid assets, cash provided by operations and access to the capital markets will enable it to meet its anticipated cash requirements, including the funding of increased dividends under AIG's new dividend policy and repurchases of common stock.

In the first six months of 2007, AIG parent collected $1.8 billion in dividends and other payments from subsidiaries, principally from DBG companies, issued $5.4 billion of debt securities and retired $765 million of debt, excluding MIP and Series AIGFP debt. AIG parent also advanced $4 billion for structured share repurchase arrangements. AIG parent made interest payments totaling $158 million, made $856 million in capital contributions to subsidiaries, and paid $859 million in dividends to shareholders in the first six months of 2007.

AIG parent funds its short-term working capital needs through commercial paper issued by AIG Funding. As of June 30, 2007, AIG Funding had $4.5 billion of commercial paper outstanding with an average maturity of 30 days. As additional liquidity, AIG parent and AIG Funding maintain revolving credit facilities that, as of June 30, 2007, had an aggregate of $5.4 billion available to be drawn, which are summarized above under Revolving Credit Facilities.

Invested Assets

AIG's investment strategy is to invest primarily in high quality securities while maintaining diversification to avoid significant exposure to issuer, industry and/or country concentrations.

The following tables summarize the composition of AIG's invested assets by segment.

(in millions)	General Insurance	Life Insurance & Retirement Services	Financial Services	Asset Management	Other	Total
June 30, 2007						
Fixed maturities:						
Bonds available for sale, at fair value	$ 70,036	$286,825	$ 1,341	$30,515	$ –	$388,717
Bonds held to maturity, at amortized cost	21,388	1	–	–	–	21,389
Bond trading securities, at fair value	–	9,261	–	–	–	9,261
Equity securities:						
Common stocks available for sale, at fair value	4,776	11,800	–	690	106	17,372
Common and preferred stocks trading, at fair value	425	17,054	–	–	–	17,479
Preferred stocks available for sale, at fair value	1,853	748	8	–	–	2,609
Mortgage loans on real estate, net of allowance	12	14,513	113	4,063	–	18,701
Policy loans	2	7,564	2	48	(9)	7,607
Collateral and guaranteed loans, net of allowance	3	771	3,382	824	74	5,054
Financial services assets:						
Flight equipment primarily under operating leases, net of accumulated depreciation	–	–	42,232	–	–	42,232
Securities available for sale, at fair value	–	–	48,166	–	–	48,166
Trading securities, at fair value	–	–	4,567	–	–	4,567
Spot commodities	–	–	93	–	–	93
Unrealized gain (loss) on swaps, options and forward transactions	–	–	18,439	–	(319)	18,120
Trade receivables	–	–	7,138	–	–	7,138
Securities purchased under agreements to resell, at contract value	–	–	31,595	–	–	31,595
Finance receivables, net of allowance	–	5	30,022	–	–	30,027
Securities lending collateral, at fair value	5,912	58,444	113	16,610	–	81,079
Other invested assets	10,687	17,008	3,843	17,473	876	49,887
Short-term investments, at cost	3,780	17,742	2,030	4,241	(57)	27,736
Total investments and financial services assets as shown on the balance sheet	118,874	441,736	193,084	74,464	671	828,829
Cash	413	630	442	143	7	1,635
Investment income due and accrued	1,369	4,419	22	308	–	6,118
Real estate, net of accumulated depreciation	524	898	25	76	30	1,553
Total invested assets*	$121,180	$447,683	$193,573	$74,991	$ 708	$838,135

** At June 30, 2007, approximately 68 percent and 32 percent of invested assets were held in domestic and foreign investments, respectively.*

(in millions)	General Insurance	Life Insurance & Retirement Services	Financial Services	Asset Management	Other	Total
December 31, 2006						
Fixed maturities:						
Bonds available for sale, at fair value	$67,994	$288,540	$ 1,357	$ 29,500	$ –	$ 387,391
Bonds held to maturity, at amortized cost	21,437	–	–	–	–	21,437
Bond trading securities, at fair value	1	9,036	–	–	–	9,037
Equity securities:						
Common stocks available for sale, at fair value	4,245	8,711	–	226	80	13,262
Common stocks trading, at fair value	350	14,071	–	–	–	14,421
Preferred stocks available for sale, at fair value	1,884	650	5	–	–	2,539
Mortgage loans on real estate, net of allowance	13	12,852	95	4,107	–	17,067
Policy loans	1	7,458	2	48	(8)	7,501
Collateral and guaranteed loans, net of allowance	3	733	2,301	729	84	3,850
Financial services assets:						
Flight equipment primarily under operating leases, net of accumulated depreciation	–	–	39,875	–	–	39,875
Securities available for sale, at fair value	–	–	47,205	–	–	47,205
Trading securities, at fair value	–	–	5,031	–	–	5,031
Spot commodities	–	–	220	–	–	220
Unrealized gain on swaps, options and forward transactions	–	–	19,252	–	–	19,252
Trade receivables	–	–	4,317	–	–	4,317
Securities purchased under agreements to resell, at contract value	–	–	31,853	–	–	31,853
Finance receivables, net of allowance	–	–	29,573	–	–	29,573
Securities lending collateral, at fair value	5,376	50,099	76	13,755	–	69,306
Other invested assets	9,207	14,263	2,212	15,823	609	42,114
Short-term investments, at cost	3,281	14,520	1,245	6,198	5	25,249
Total investments and financial services assets as shown on the balance sheet	113,792	420,933	184,619	70,386	770	790,500
Cash	334	740	390	118	8	1,590
Investment income due and accrued	1,363	4,364	23	326	1	6,077
Real estate, net of accumulated depreciation	570	698	17	75	26	1,386
Total invested assets*	$116,059	$426,735	$ 185,049	$ 70,905	$ 805	$ 799,553

** At December 31, 2006, approximately 68 percent and 32 percent of invested assets were held in domestic and foreign investments, respectively.*

Investments in Residential Mortgage-Backed Securities and CDOs

As part of its strategy to diversify its investments, AIG invests in various types of securities, including residential mortgage-backed securities (RMBS) and CDOs. At June 30, 2007, AIG's investment portfolio included such securities with an amortized cost of $98.5 billion and an estimated fair value of $97.9 billion. The gross unrealized gains and gross unrealized losses related to these investments were $134 million and $(747) million, respectively, at June 30, 2007.

AIG's insurance operations held investments in RMBS with an estimated fair value of $94 billion at June 30, 2007, or approximately 11 percent of AIG's total invested assets. In addition, AIGFP held investments totaling $3.6 billion in CDOs which include some level of subprime exposure. AIG's RMBS investments are predominantly in highly-rated tranches that contain substantial protection features through collateral subordination. At June 30, 2007, approximately 91 percent of these investments were rated AAA and approximately 7 percent were rated AA by one or more of the principal rating agencies. AIG's investments rated BBB or below totaled approximately $400 million, or less than 1 percent of AIG's total invested assets at June 30, 2007. As of August 6, 2007, none of AIG's RMBS with some level of subprime collateral had been downgraded as a result of recent rating agency actions, and a small amount of AIG's RMBS investments with subprime collateral had been upgraded. AIG currently intends to hold these securities to full recovery and/or full payment of principal and interest, and therefore expects that any mark to market effect will result in only a temporary adjustment to shareholders' equity.

AIG's underwriting practices for investing in RMBS, other asset-backed securities and CDOs takes into consideration the quality of the originator, the manager, the servicer, security credit ratings, underlying characteristics of the mortgages, borrower characteristics, and the level of credit enhancement in the transaction. AIG's strategy is

typically to invest in securities rated AA or better and create diversification across multiple underlying asset classes.

Other-than-temporary impairments

As a result of AIG's periodic evaluation of its securities for other-than-temporary impairments in value, AIG recorded, in net realized capital gains (losses), other-than-temporary impairment pre-tax losses of $417 million and $370 million in the three-month periods ended June 30, 2007 and 2006, respectively, and $884 million and $596 million in the six-month periods ended June 30, 2007 and 2006, respectively.

AIG no longer intends to hold to recovery certain available-for-sale investments. Approximately 66 percent and 42 percent of the other-than-temporary losses for the three and six-month periods ended June 30, 2007, respectively, relate to changes in interest rates. The balance arises primarily from foreign exchange or issuer-specific events.

The principal causes of the other-than-temporary impairment losses in the three and six-month periods ended June 30, 2007 were as follows:

Three months ended June 30, 2007

- Securities which AIG no longer intends to hold until they have fully recovered their carrying value, totaling $277 million.
- A decline in value of U.S. dollar bonds held by AIG's Foreign Life operations totaling $92 million, due to the depreciation of the U.S. dollar against the local currency.
- Issuer-specific events totaling $9 million and equity securities and partnership investments of $31 million in an unrealized loss position for a continuous 12-month period.

Six months ended June 30, 2007

- Securities which AIG no longer intends to hold until they have fully recovered their carrying value, totaling $371 million.
- A decline in value of U.S. dollar bonds held by AIG's Foreign Life operations totaling $304 million, due to the depreciation of the U.S. dollar against the local currency.
- Issuer-specific events totaling $26 million and equity securities and partnership investments of $147 million in an unrealized loss position for a continuous 12-month period.

No impairment charge with respect to any one single credit was significant to AIG's consolidated financial condition or results of operations, and no individual impairment loss exceeded 1.0 percent of consolidated net income for the first six months of 2007.

An aging of the pre-tax unrealized losses of fixed maturity and equity securities, distributed as a percentage of cost relative to unrealized loss (the extent by which the fair value is less than amortized cost or cost), including the number of respective items, was as follows at June 30, 2007:

	Less than or equal to 20% of Cost			Greater than 20% to 50% of Cost			Greater than 50% of Cost			Total		
Aging *(dollars in millions)*	Cost[a]	Unrealized Loss	Items	Cost[a]	Unrealized Loss	Items	Cost[a]	Unrealized Loss	Items	Cost[a]	Unrealized Loss[b]	Items
Investment grade bonds												
0-6 months	$115,823	$2,154	15,113	$ 60	$14	26	$ —	$ —	—	$115,883	$2,168	15,139
7-12 months	11,966	219	1,216	90	25	7	—	—	—	12,056	244	1,223
>12 months	84,818	3,288	12,661	100	26	20	—	—	—	84,918	3,314	12,681
Total	$212,607	$5,661	28,990	$250	$65	53	$ —	$ —	—	$212,857	$5,726	29,043
Below investment grade bonds												
0-6 months	$ 5,236	$ 104	1,470	$ —	$ —	—	$ —	$ —	—	$ 5,236	$ 104	1,470
7-12 months	444	8	66	—	—	—	—	—	—	444	8	66
>12 months	1,427	88	202	14	3	1	—	—	—	1,441	91	203
Total	$ 7,107	$ 200	1,738	$ 14	$ 3	1	$ —	$ —	—	$ 7,121	$ 203	1,739
Total bonds												
0-6 months	$121,059	$2,258	16,583	$ 60	$14	26	$ —	$ —	—	$121,119	$2,272	16,609
7-12 months	12,410	227	1,282	90	25	7	—	—	—	12,500	252	1,289
>12 months	86,245	3,376	12,863	114	29	21	—	—	—	86,359	3,405	12,884
Total	$219,714	$5,861	30,728	$264	$68	54	$ —	$ —	—	$219,978	$5,929	30,782
Equity securities												
0-6 months	$ 2,389	$ 94	1,555	$ 48	$12	80	$ 3	$ 2	33	$ 2,440	$ 108	1,668
7-12 months	242	12	88	37	10	46	—	—	—	279	22	134
>12 months	—	—	—	—	—		—	—	—	—	—	—
Total	$ 2,631	$ 106	1,643	$ 85	$22	126	$ 3	$ 2	33	$ 2,719	$ 130	1,802

(a) For bonds, represents amortized cost.

(b) The effect on net income of unrealized losses after taxes will be mitigated upon realization because certain realized losses will be charged to participating policyholder accounts, or realization will result in current decreases in the amortization of certain DAC.

At June 30, 2007, the fair value of AIG's fixed maturity and equity securities aggregated $505.2 billion. At June 30, 2007, aggregate pre-tax unrealized gains for fixed maturity and equity securities were $18.0 billion ($11.7 billion after tax). At June 30, 2007, the aggregate pre-tax unrealized losses of fixed maturity and equity securities were $6.1 billion ($3.9 billion after tax).

Additional information about these securities is as follows:

- These securities are trading, in the aggregate, at approximately 97 percent of their current amortized cost.
- Less than 1 percent of these securities are trading at a value which is less than 20 percent of its current cost, or amortized cost.
- Less than 4 percent of the fixed income securities have issuer credit ratings which are below investment grade.

AIG did not consider these investments to be other-than-temporarily impaired at June 30, 2007, as management has the intent and ability to hold these investments until they fully recover in value.

At June 30, 2007, unrealized losses for fixed maturity securities and equity securities did not reflect any significant industry concentrations.

The amortized cost of fixed maturity securities available for sale in an unrealized loss position at June 30, 2007, by contractual maturity, is shown below:

(in millions)	**Amortized Cost**
Due in one year or less	$ 6,384
Due after one year through five years	36,213
Due after five years through ten years	84,052
Due after ten years	93,329
Total	$219,978

For the six months ended June 30, 2007, the pre-tax realized losses incurred with respect to the sale of fixed maturities and equity securities were $598 million. The aggregate fair value of securities sold was $22.2 billion, which was approximately 97 percent of amortized cost. The average period of time that securities sold at a loss during the six months ended June 30, 2007 were trading continuously at a price below book value was approximately seven months.

Risk Management

For a complete discussion of AIG's risk management program, see Management's Discussion and Analysis of Financial Condition and Results of Operations in the 2006 Annual Report on Form 10-K.

Insurance, Asset Management and Non-Trading Financial Services VaR

AIG performs one comprehensive Value at Risk (VaR) analysis across all of its non-trading businesses, and a separate VaR analysis for its trading business at AIGFP. The comprehensive VaR is categorized by AIG business segment (General Insurance, Life Insurance & Retirement Services, Financial Services and Asset Management) and also by market risk factor (interest rate, currency and equity).

AIG calculated the VaR with respect to net fair values as of June 30, 2007 and December 31, 2006. The VaR number represents the maximum potential loss as of those dates that could be incurred with a 95 percent confidence and a one-month holding period.

The following table presents the period-end, average, high and low VaRs on a diversified basis and of each component of market risk for AIG's non-trading businesses. The diversified VaR is usually smaller than the sum of its components due to correlation effects.

	2007				2006			
		Six Months Ended June 30,				Year Ended December 31,		
(in millions)	As of June 30,	Average	High	Low	As of December 31,	Average	High	Low
Total AIG Non-Trading Market Risk:								
Market risk:								
Diversified	**$5,168**	**$5,123**	**$5,168**	**$5,073**	$5,073	$5,209	$5,783	$4,852
Interest rate	**4,625**	**4,621**	**4,659**	**4,577**	4,577	4,962	5,765	4,498
Currency	**727**	**699**	**727**	**685**	686	641	707	509
Equity	**2,109**	**1,979**	**2,109**	**1,873**	1,873	1,754	1,873	1,650
General Insurance:								
Diversified	**$1,892**	**$1,717**	**$1,892**	**$1,543**	$1,717	$1,697	$1,776	$1,617
Interest rate	**1,792**	**1,601**	**1,792**	**1,470**	1,541	1,635	1,717	1,541
Currency	**218**	**212**	**218**	**205**	212	162	212	119
Equity	**626**	**595**	**626**	**573**	573	551	573	535
Life Insurance & Retirement Services:								
Diversified	**$4,670**	**$4,644**	**$4,688**	**$4,574**	$4,574	$4,672	$5,224	$4,307
Interest rate	**4,287**	**4,437**	**4,552**	**4,287**	4,471	4,563	5,060	4,229
Currency	**625**	**592**	**625**	**568**	568	538	592	459
Equity	**1,436**	**1,351**	**1,436**	**1,293**	1,293	1,228	1,299	1,133
Non-Trading Financial Services:								
Diversified	**$ 105**	**$ 105**	**$ 125**	**$ 85**	$ 125	$ 165	$ 252	$ 125
Interest rate	**113**	**105**	**127**	**76**	127	166	249	127
Currency	**12**	**11**	**12**	**11**	11	8	11	7
Equity	**1**	**1**	**1**	**1**	1	1	2	1
Asset Management:								
Diversified	**$ 74**	**$ 60**	**$ 74**	**$ 43**	$ 64	$ 144	$ 190	$ 64
Interest rate	**72**	**57**	**72**	**37**	63	145	192	63
Currency	**2**	**2**	**3**	**2**	3	4	7	3
Equity	**10**	**10**	**11**	**8**	8	9	13	8

Increased equity investment allocation in the Life Insurance & Retirement Services and General Insurance segments, as well as growth in those businesses, contributed to the modest growth in AIG's total Non-Trading VaR during the first six months of 2007. Interest rate and equity volatilities continued to moderate in many markets.

Capital Markets Trading VaR

AIGFP's policy is to maintain a conservative market risk profile and minimize risks in interest rates, equities, commodities and foreign exchange. In addition, AIGFP's primary market exposures in option implied volatilities, correlations and basis risks are closely managed.

AIGFP's minimal reliance on market risk driven revenue is reflected in its VaR. Because the market risk with respect to securities available for sale, at market, is substantially hedged, segregation of the financial instruments into trading and other than trading was not deemed necessary.

AIGFP reports its VaR using a 95 percent confidence interval and a one-day holding period.

The following table presents the period-end, average, high, and low VaRs (based on daily observations) on a diversified basis and of each component of market risk for AIG's Capital Markets operations. The diversified VaR is usually smaller than the sum of its components due to correlation effects.

	2007				2006			
		Six Months Ended June 30,				Year Ended December 31,		
(in millions)	As of June 30,	Average	High	Low	As of December 31,	Average	High	Low
Total AIG trading market risk:								
Diversified	**$5**	**$5**	**$7**	**$4**	$4	$4	$7	$3
Interest rate	**2**	**2**	**3**	**2**	2	2	3	1
Currency	**2**	**1**	**2**	**1**	1	1	3	1
Equity	**2**	**3**	**5**	**2**	3	3	4	2
Commodity	**3**	**4**	**6**	**2**	3	3	4	2

Catastrophe Exposures

The nature of AIG's business exposes it to various catastrophic events in which multiple losses across multiple lines of business can occur in any calendar year. In order to control this exposure, AIG uses a combination of techniques, including setting aggregate limits in key business units, monitoring and modeling accumulated exposures, and purchasing catastrophe reinsurance to supplement its other reinsurance protections.

Natural disasters such as hurricanes, earthquakes and other catastrophes have the potential to adversely affect AIG's operating results. Other risks, such as an outbreak of a pandemic disease, such as the Avian Influenza A Virus (H5N1), could adversely affect AIG's business and operating results to an extent that may be only partially offset by reinsurance programs.

AIG evaluates catastrophic events and assesses the probability of occurrence and magnitude of catastrophic events through the use of industry recognized models, among other techniques. AIG supplements these models by periodically monitoring the exposure risks of AIG's worldwide General Insurance operations and adjusting such models accordingly. Following is an overview of modeled losses associated with the more significant natural perils, which includes exposures for DBG, Personal Lines, Foreign General (other than Ascot), The Hartford Steam Boiler Inspection and Insurance Company and 21st Century. Transatlantic and Ascot utilize a different model, and their combined results are presented separately below. Significant life and A&H exposures have been added to these results as well. The modeled results assume that all reinsurers fulfill their obligations to AIG in accordance with their terms.

It is important to recognize that there is no standard methodology to project the possible losses from total property and workers compensation exposures. Further, there are no industry standard assumptions to be utilized in projecting these losses. The use of different methodologies and assumptions could materially change the projected losses. Therefore, these modeled losses may not be comparable to estimates made by other companies.

These estimates are inherently uncertain and may not reflect AIG's maximum exposures to these events. It is highly likely that AIG's losses will vary, perhaps significantly, from these estimates.

AIG has revised the catastrophe exposure disclosures presented below from that presented in the 2006 Annual Report on Form 10-K to include significant life and A&H exposures to natural perils as well as to update the domestic property exposures to reflect more recent data. The modeled results provided in the table below were based on the aggregate exceedence probability (AEP) losses which represent total property, workers compensation, life, and accident and health losses that may occur in any single year from one or more natural events. The life and A&H data include exposures for United States, Japan, and Taiwan earthquakes. These represent the largest share of life and A&H exposures to earthquake. A&H losses were modeled using December 2006 data, and life losses were modeled using March 2006 data. The updated property exposures were generally modeled with exposure data as of year-end 2006. Lexington commercial lines exposure, which represents the largest share of the modeled losses, was based on data as of April 2007. All reinsurance program structures, including both domestic and international structures, have also been updated. The values provided were based on 100-year return period losses, which have a one percent likelihood of being exceeded in any single year. Thus, the model projects that there is a one percent probability that AIG could incur in any year losses in excess of the modeled amounts for these perils.

(in millions)	Gross	Net of Reinsurance	Net After Income Tax	% of Consolidated Shareholders' Equity at June 30, 2007
Natural Peril:				
Earthquake	$ 4,970	$ 2,705	$ 1,758	1.7%
Tropical Cyclone*	$ 5,546	$ 2,980	$ 1,937	1.9%

** Includes hurricanes, typhoons and other wind-related events.*

The combined earthquake and tropical cyclone 100-year return period modeled losses for Ascot and Transatlantic together are estimated to be $1.1 billion, on a gross basis, $761 million, net of reinsurance, and $494 million, net after income taxes, or 0.5 percent of total shareholders' equity at June 30, 2007.

In addition, AIG evaluates potential single event earthquake and hurricane losses that may be incurred. The single events utilized are a subset of potential events identified and utilized by Lloyd's[(1)] and referred to as Realistic Disaster Scenarios (RDSs). The purpose of this analysis is to utilize these RDSs to provide a reference frame and place into context the model results. However, it is important to note that the specific events used for this analysis do not necessarily represent the worst case loss that AIG could incur from this type of an event in these regions. The losses associated with the RDSs are included in the table below.

Single event modeled property and workers compensation losses to AIG's worldwide portfolio of risk for key geographic areas are set forth below. Gross values represent AIG's liability after the application of policy limits and deductibles, and net values represent losses after reinsurance is applied.

(in millions)	Gross	Net of Reinsurance
Natural Peril:		
San Francisco Earthquake	$ 5,562	$ 3,012
Miami Hurricane	$ 5,375	$ 2,651
Northeast Hurricane	$ 4,755	$ 2,779
Los Angeles Earthquake	$ 4,750	$ 2,614
Gulf Coast Hurricane	$ 3,553	$ 1,797
Japanese Earthquake	$ 843	$ 366
European Windstorm	$ 239	$ 87
Japanese Typhoon	$ 185	$ 149

(1) Lloyd's Realistic Disaster Scenarios, Scenario Specifications, April 2006.

The specific international RDS events do not necessarily correspond to AIG's international property exposures. As a result, AIG runs its own simulations where property statistical return period losses associated with the written exposure specific to AIG provide the basis for monitoring risk.

Based on these simulations, the 100-year return period loss for Japanese Earthquake is $296 million gross, and $120 million net, the 100-year return period loss for European Windstorm is $269 million gross, and $80 million net, and the 100-year return period loss for Japanese Typhoon is $306 million gross, and $252 million net.

Recent market conditions in the U.S. property business have supported growth in this line of business. Consequently, gross modeled catastrophe losses have increased. Associated net exposure has been carefully monitored and controlled through the strategic placement of reinsurance.

ACTUAL RESULTS IN ANY PERIOD ARE LIKELY TO VARY, PERHAPS MATERIALLY, FROM THE MODELED SCENARIOS, AND THE OCCURRENCE OF ONE OR MORE SEVERE EVENTS COULD HAVE A MATERIAL ADVERSE EFFECT ON AIG'S FINANCIAL CONDITION, RESULTS OF OPERATIONS AND LIQUIDITY.

ITEM 3. Quantitative and Qualitative Disclosures About Market Risk

Included in Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations.

ITEM 4. Controls and Procedures

In connection with the preparation of this Quarterly Report on Form 10-Q, an evaluation was carried out by AIG's management, with the participation of AIG's Chief Executive Officer and Chief Financial Officer, of the effectiveness of AIG's disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934 (Exchange Act)). Disclosure controls and procedures are designed to ensure that information required to be disclosed in reports filed or submitted under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in SEC rules and forms and that such information is accumulated and communicated to management, including the Chief Executive Officer and Chief Financial Officer, to allow timely decisions regarding required disclosures. Based on its evaluation, and in light of the previously identified material weakness in internal control over financial reporting, as of December 31, 2006, relating to controls over income tax accounting described in the 2006 Annual Report on Form 10-K, AIG's Chief Executive Officer and Chief Financial Officer concluded that, as of June 30, 2007, AIG's disclosure controls and procedures were ineffective. In addition, there has been no change in AIG's internal control over financial reporting (as defined in Rule 13a-15(f) under the Exchange Act) that occurred during the quarter ended June 30, 2007 that has materially affected, or is reasonably likely to materially affect, AIG's internal control over financial reporting.

Part II – OTHER INFORMATION

ITEM 2. Unregistered Sales of Equity Securities and Use of Proceeds

The table below provides information with respect to purchases of AIG Common stock during the three months ended June 30, 2007.

Period	Total Number of Shares Purchased[1]	Average Price Paid per Share	Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs	Maximum Number of Shares that May Yet Be Purchased Under the Plans or Programs at End of Month[2]
April 1 - 30	6,643,052	$65.92	6,643,052	
May 1 - 31	—	—	—	
June 1 - 30	15,378,410	70.09	15,378,410	
Total	22,021,462	$68.84	22,021,462	

(1) Reflects date of delivery. Does not include 8,061 shares delivered or attested to in satisfaction of the exercise price by holders of AIG employee stock options exercised during the three months ended June 30, 2007.

(2) In February 2007, AIG's Board of Directors increased AIG's share repurchase program by authorizing the repurchase of shares with an aggregate purchase price of $8 billion. A balance of $6.30 billion remained for purchases under the program as of June 30, 2007, although $2.34 billion of that amount has been advanced by AIG to purchase shares under the program. The purchase program has no set expiration or termination date.

ITEM 4. Submission of Matters to a Vote of Security Holders.

At the Annual Meeting of Shareholders held on May 16, 2007, the Shareholders:

(a) Elected fifteen directors as follows:

Nominee	Shares For	Shares Withheld
Marshall A. Cohen	1,863,591,324	479,677,730
Martin S. Feldstein	1,925,930,648	417,338,406
Ellen V. Futter	1,920,091,144	423,177,910
Stephen L. Hammerman	2,316,775,772	26,493,282
Richard C. Holbrooke	1,787,372,289	555,896,765
Fred H. Langhammer	2,303,536,899	39,732,155
George L. Miles, Jr.	2,216,252,110	127,016,944
Morris W. Offit	1,920,016,457	423,252,597
James F. Orr III	2,246,051,541	97,217,513
Virginia M. Rometty	2,306,729,284	36,539,770
Martin J. Sullivan	1,929,344,493	413,924,561
Michael H. Sutton	2,309,868,113	33,400,941
Edmund S.W. Tse	1,929,071,878	414,197,176
Robert B. Willumstad	2,303,916,443	39,352,611
Frank G. Zarb	1,826,711,442	516,557,612

(b) Approved by a vote of 1,778,412,239 shares to 525,833,405 shares, with 39,023,410 abstaining, a proposal to ratify the selection of PricewaterhouseCoopers LLP as the independent registered public accounting firm for 2007.

(c) Approved by a vote of 1,529,091,124 shares to 572,822,919 shares, with 62,808,813 abstaining, and 178,546,198 shares not voting, a proposal to approve the American International Group, Inc. 2007 Stock Incentive Plan.

(d) Rejected by a vote of 554,311,568 shares for and 1,586,624,750 shares against, with 23,818,514 shares abstaining and 178,514,222 shares not voting, a shareholder proposal relating to performance-based stock options.

ITEM 6. Exhibits

See accompanying Exhibit Index.

SIGNATURE

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

AMERICAN INTERNATIONAL GROUP, INC.
(Registrant)

/s/ Steven J. Bensinger

Steven J. Bensinger
Executive Vice President and Chief Financial Officer

/s/ David L. Herzog

David L. Herzog
Senior Vice President and Comptroller
(Principal Accounting Officer)

Dated: August 8, 2007

EXHIBIT INDEX

Exhibit Number	Description	Location
10.1	Form of Option Award Agreement under the AIG 2007 Stock Incentive Plan*	Filed herewith.
10.2	Form of Performance RSU Award Agreement under the AIG 2007 Stock Incentive Plan and the AIG Partners Plan*	Filed herewith.
10.3	Form of Time-Vested RSU Award Agreement*	Filed herewith.
10.4	Form of Time-Vested RSU Award Agreement with early retirement provisions*	Filed herewith.
10.5	Form of Non-Employee Director Deferred Stock Units Award Agreement*	Filed herewith.
10.6	Summary of Director compensation*	Filed herewith.
11	Statement re computation of per share earnings	Included in Note (3) of Notes to Consolidated Financial Statements.
12	Statement re computation of ratios	Filed herewith.
31	Rule 13a-14(a)/15d-14(a) Certifications	Filed herewith.
32	Section 1350 Certifications	Filed herewith.

** These exhibits are management contracts or compensatory plans or arrangements.*

Exhibit 12

American International Group, Inc.
Computation of Ratios of Earnings to Fixed Charges

(in millions, except ratios)	Three Months Ended June 30, 2007	Three Months Ended June 30, 2006	Six Months Ended June 30, 2007	Six Months Ended June 30, 2006
Income before income taxes, minority interest and cumulative effect of an accounting change	**$ 6,328**	$ 5,241	**$12,500**	$10,034
Less – Equity income of less than 50% owned persons	**49**	110	**91**	130
Add – Dividends from less than 50% owned persons	**25**	15	**25**	18
	6,304	5,146	**12,434**	9,922
Add – Fixed charges	**2,442**	2,048	**5,114**	3,996
Less – Capitalized interest	**9**	14	**20**	29
Income before income taxes, minority interest, cumulative effect of an accounting change and fixed charges	**$ 8,737**	$ 7,180	**$17,528**	$13,889
Fixed charges:				
Interest costs	**$ 2,381**	$ 1,995	**$ 4,993**	$ 3,891
Rental expense*	**61**	53	**121**	105
Total fixed charges	**$ 2,442**	$ 2,048	**$ 5,114**	$ 3,996
Ratio of earnings to fixed charges	**3.58**	3.51	**3.43**	3.48
Secondary Ratio				
Interest credited to GIC and GIA policy and contract holders	**$(1,268)**	$(1,097)	**$ (2,847)**	$ (2,187)
Total fixed charges excluding interest credited to GIC and GIA policy and contract holders	**$ 1,174**	$ 951	**$ 2,267**	$ 1,809
Secondary ratio of earnings to fixed charges	**6.36**	6.40	**6.48**	6.47

** The proportion deemed representative of the interest factor.*

The secondary ratio is disclosed for the convenience of fixed income investors and the rating agencies that serve them and is more comparable to the ratios disclosed by all issuers of fixed income securities. The secondary ratio removes interest credited to guaranteed investment contract (GIC) policyholders and guaranteed investment agreement (GIA) contractholders. Such interest expenses are also removed from income before income taxes, minority interest and cumulative effect of an accounting change used in this calculation. GICs and GIAs are entered into by AIG's insurance subsidiaries, principally Sun America Life Insurance Company and AIG Financial Products Corp. and its subsidiaries, respectively. The proceeds from GICs and GIAs are invested in a diversified portfolio of securities, primarily investment grade bonds. The assets acquired yield rates greater than the rates on the related policyholders obligation or agreement, with the intent of earning operating income from the spread.

Exhibit 31

CERTIFICATIONS

I, Martin J. Sullivan, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q of American International Group, Inc.;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:

(a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

(b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

(c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

(d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):

(a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

(b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

/s/ Martin J. Sullivan

Martin J. Sullivan
President and Chief Executive Officer

Date: August 8, 2007

CERTIFICATIONS

I, Steven J. Bensinger, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q of American International Group, Inc.;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:

(a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

(b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

(c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

(d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):

(a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

(b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

/s/ Steven J. Bensinger

Steven J. Bensinger
Executive Vice President and Chief Financial Officer

Date: August 8, 2007

Exhibit 32

CERTIFICATION

In connection with the Quarterly Report on Form 10-Q of American International Group, Inc. (the "Company") for the quarter ended June 30, 2007, as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, Martin J. Sullivan, President and Chief Executive Officer of the Company, certify, pursuant to 18 U.S.C. Section 1350, that to my knowledge:

1. The Report fully complies with the requirements of Section 13(a) or 15(d), as applicable, of the Securities Exchange Act of 1934; and

2. The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

/s/ Martin J. Sullivan

Martin J. Sullivan
President and Chief Executive Officer

Date: August 8, 2007

The foregoing certification is being furnished solely pursuant to 18 U.S.C. Section 1350 and is not being filed as part of the Report or as a separate disclosure document.

CERTIFICATION

In connection with the Quarterly Report on Form 10-Q of American International Group, Inc. (the "Company") for the quarter ended June 30, 2007, as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, Steven J. Bensinger, Executive Vice President and Chief Financial Officer of the Company, certify, pursuant to 18 U.S.C. Section 1350, that to my knowledge:

1. The Report fully complies with the requirements of Section 13(a) or 15(d), as applicable, of the Securities Exchange Act of 1934; and

2. The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

/s/ Steven J. Bensinger

Steven J. Bensinger
Executive Vice President and Chief Financial Officer

Date: August 8, 2007

The foregoing certification is being furnished solely pursuant to 18 U.S.C. Section 1350 and is not being filed as part of the Report or as a separate disclosure document.

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

Form 10-Q

(Mark One)

☑ QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended September 30, 2007

or

☐ TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the transition period from to

Commission File Number 1-8787

American International Group, Inc.

(Exact name of registrant as specified in its charter)

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

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

Former name, former address and former fiscal year, if changed since last report: None

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

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of "accelerated filer and large accelerated filer" in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer ☑ Accelerated filer ☐ Non-accelerated filer ☐

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes ☐ No ☑

As of October 31, 2007, there were 2,536,238,141 shares outstanding of the registrant's common stock.

TABLE OF CONTENTS

Part I – FINANCIAL INFORMATION

ITEM 1. Financial Statements (unaudited)

CONSOLIDATED BALANCE SHEET

(in millions) (unaudited)

	September 30, 2007	December 31, 2006
Assets:		
Investments and financial services assets:		
Fixed maturities:		
Bonds available for sale, at fair value (amortized cost: 2007 – $391,497; 2006 – $377,698) (includes hybrid financial instruments: 2007 – $566; 2006 – $522)	**$ 394,810**	$387,391
Bonds held to maturity, at amortized cost (fair value: 2007 – $22,053; 2006 – $22,154)	**21,576**	21,437
Bond trading securities, at fair value (cost: 2007 – $9,604; 2006 – $10,292)	**9,459**	10,314
Equity securities:		
Common stocks available for sale, at fair value (cost: 2007 – $12,852; 2006 – $10,662)	**18,649**	13,256
Common and preferred stocks trading, at fair value (cost: 2007 – $17,269; 2006 – $13,079)	**19,219**	14,855
Preferred stocks available for sale, at fair value (cost: 2007 – $2,620; 2006 – $2,485)	**2,606**	2,539
Mortgage loans on real estate, net of allowance (2007 – $52; 2006 – $55)	**18,854**	17,067
Policy loans	**7,822**	7,501
Collateral and guaranteed loans, net of allowance (2007 – $4; 2006 – $9)	**4,385**	3,850
Financial services assets:		
Flight equipment primarily under operating leases, net of accumulated depreciation (2007 – $10,105; 2006 – $8,835)	**41,804**	39,875
Securities available for sale, at fair value (cost: 2007 – $46,892; 2006 – $45,912)	**47,805**	47,205
Trading securities, at fair value	**4,874**	5,031
Spot commodities	**115**	220
Unrealized gain on swaps, options and forward transactions	**18,608**	19,252
Trade receivables	**6,548**	4,317
Securities purchased under agreements to resell, at contract value	**37,189**	30,291
Finance receivables, net of allowance (2007 – $775; 2006 – $737) (includes finance receivables held for sale: 2007 – $406; 2006 – $1,124)	**30,640**	29,573
Securities lending collateral, at fair value (cost: 2007 – $87,956; 2006 – $69,306)	**86,108**	69,306
Other invested assets	**51,783**	42,111
Short-term investments, at cost (approximates fair value)	**38,998**	27,483
Total investments and financial services assets	**861,852**	792,874
Cash	**2,249**	1,590
Investment income due and accrued	**6,635**	6,091
Premiums and insurance balances receivable, net of allowance (2007 – $746; 2006 – $756)	**18,199**	17,789
Reinsurance assets, net of allowance (2007 – $658; 2006 – $536)	**23,426**	23,355
Deferred policy acquisition costs	**40,878**	37,235
Investments in partially owned companies	**1,277**	1,101
Real estate and other fixed assets, net of accumulated depreciation (2007 – $5,807; 2006 – $5,525)	**6,093**	4,381
Separate and variable accounts	**78,701**	70,277
Goodwill	**8,909**	8,628
Other assets	**23,886**	16,089
Total assets	**$1,072,105**	$979,410

See Accompanying Notes to Consolidated Financial Statements.

CONSOLIDATED BALANCE SHEET *(continued)*

(in millions, except share data) (unaudited)

	September 30, 2007	December 31, 2006
Liabilities:		
Reserve for losses and loss expenses	**$ 83,608**	$ 79,999
Unearned premiums	**27,909**	26,271
Future policy benefits for life and accident and health insurance contracts	**130,759**	122,230
Policyholders' contract deposits	**254,109**	248,994
Other policyholders' funds	**8,196**	8,281
Commissions, expenses and taxes payable	**6,523**	5,305
Insurance balances payable	**5,304**	3,789
Funds held by companies under reinsurance treaties	**2,456**	2,602
Income taxes payable	**9,288**	9,546
Financial services liabilities:		
Borrowings under obligations of guaranteed investment agreements	**19,495**	20,664
Securities sold under agreements to repurchase, at contract value	**23,368**	19,677
Trade payables	**10,137**	6,174
Hybrid financial instrument liabilities, at fair value	**7,692**	8,856
Securities and spot commodities sold but not yet purchased, at market value	**4,736**	4,076
Unrealized loss on swaps, options and forward transactions	**12,512**	11,401
Trust deposits and deposits due to banks and other depositors	**4,737**	5,249
Commercial paper	**10,120**	8,208
Notes, bonds, loans and mortgages payable	**101,747**	87,816
Commercial paper and extendible commercial notes	**5,845**	4,821
Notes, bonds, loans and mortgages payable	**25,165**	16,874
Junior subordinated debt	**4,681**	–
Liabilities connected to trust preferred stock	**1,440**	1,440
Separate and variable accounts	**78,701**	70,277
Securities lending payable	**88,360**	70,198
Minority interest	**10,395**	7,778
Other liabilities (includes hybrid financial instruments: 2007 – $99; 2006 – $111)	**30,655**	27,016
Total liabilities	**967,938**	877,542
Preferred shareholders' equity in subsidiary companies	**100**	191
Commitments and Contingent Liabilities (See Note 6)		
Shareholders' equity:		
Common stock, $2.50 par value; 5,000,000,000 shares authorized; shares issued 2007 and 2006 – 2,751,327,476	**6,878**	6,878
Additional paid-in capital	**2,818**	2,590
Payments advanced to purchase shares	**(1,275)**	–
Retained earnings	**94,830**	84,996
Accumulated other comprehensive income (loss)	**6,194**	9,110
Treasury stock, at cost; 2007 – 201,311,212; 2006 – 150,131,273 shares of common stock	**(5,378)**	(1,897)
Total shareholders' equity	**104,067**	101,677
Total liabilities, preferred shareholders' equity in subsidiary companies and shareholders' equity	**$1,072,105**	$979,410

See Accompanying Notes to Consolidated Financial Statements.

CONSOLIDATED STATEMENT OF INCOME

(in millions, except per share data) (unaudited)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2007	2006	**2007**	2006
Revenues:				
Premiums and other considerations	**$19,733**	$18,890	**$58,908**	$55,486
Net investment income	**6,172**	6,463	**21,149**	18,579
Net realized capital gains (losses)	**(864)**	(87)	**(962)**	(132)
Other income	**4,795**	3,981	**12,536**	9,446
Total revenues	**29,836**	29,247	**91,631**	83,379
Benefits and expenses:				
Incurred policy losses and benefits	**15,595**	14,963	**47,962**	44,118
Insurance acquisition and other operating expenses	**9,362**	7,983	**26,290**	22,926
Total benefits and expenses	**24,957**	22,946	**74,252**	67,044
Income before income taxes, minority interest and cumulative effect of an accounting change	**4,879**	6,301	**17,379**	16,335
Income taxes	**1,463**	1,943	**4,868**	5,066
Income before minority interest and cumulative effect of an accounting change	**3,416**	4,358	**12,511**	11,269
Minority interest	**(331)**	(134)	**(1,019)**	(694)
Income before cumulative effect of an accounting change	**3,085**	4,224	**11,492**	10,575
Cumulative effect of an accounting change, net of tax	**–**	–	**–**	34
Net income	**$ 3,085**	$ 4,224	**$11,492**	$10,609
Earnings per common share:				
Basic				
Income before cumulative effect of an accounting change	**$ 1.20**	$ 1.62	**$ 4.43**	$ 4.06
Cumulative effect of an accounting change, net of tax	**–**	–	**–**	0.01
Net income	**$ 1.20**	$ 1.62	**$ 4.43**	$ 4.07
Diluted				
Income before cumulative effect of an accounting change	**$ 1.19**	$ 1.61	**$ 4.40**	$ 4.03
Cumulative effect of an accounting change, net of tax	**–**	–	**–**	0.01
Net income	**$ 1.19**	$ 1.61	**$ 4.40**	$ 4.04
Dividends declared per common share	**$ 0.200**	$ 0.165	**$ 0.565**	$ 0.480
Average shares outstanding:				
Basic	**2,576**	2,607	**2,596**	2,607
Diluted	**2,589**	2,626	**2,609**	2,625

See Accompanying Notes to Consolidated Financial Statements.

CONSOLIDATED STATEMENT OF CASH FLOWS

(in millions) (unaudited)

	Nine Months Ended September 30, 2007	2006
Summary:		
Net cash provided by operating activities	**$ 27,056**	$ 4,037
Net cash used in investing activities	**(65,929)**	(52,144)
Net cash provided by financing activities	**39,524**	47,576
Effect of exchange rate changes on cash	**8**	59
Change in cash	**659**	(472)
Cash at beginning of period	**1,590**	1,897
Cash at end of period	**$ 2,249**	$ 1,425
Cash flows from operating activities:		
Net income	**$ 11,492**	$ 10,609
Adjustments to reconcile net income to net cash provided by operating activities:		
Noncash revenues, expenses, gains and losses included in income:		
Net gains on sales of securities available for sale and other assets	**(1,110)**	(407)
Foreign exchange transaction (gains) losses	**1,214**	845
Net unrealized (gains) losses on non-AIGFP derivative assets and liabilities	**(103)**	(441)
Equity in income of partially owned companies and other invested assets	**(3,336)**	(2,655)
Amortization of deferred policy acquisition costs	**9,242**	8,785
Amortization of premium and discount on securities	**491**	100
Depreciation expenses, principally flight equipment	**2,072**	1,743
Provision for finance receivable losses	**391**	329
Impairment losses	**1,413**	766
Changes in operating assets and liabilities:		
General and life insurance reserves	**12,131**	10,507
Premiums and insurance balances receivable and payable – net	**515**	(173)
Reinsurance assets	**561**	614
Capitalization of deferred policy acquisition costs	**(11,897)**	(11,949)
Investment income due and accrued	**(538)**	(486)
Funds held under reinsurance treaties	**(166)**	(1,732)
Other policyholders' funds	**(85)**	(840)
Income taxes payable	**707**	1,905
Commissions, expenses and taxes payable	**1,110**	356
Other assets and liabilities – net	**2,181**	(842)
Bonds, common and preferred stocks trading, at fair value	**(2,546)**	(5,535)
Trade receivables and payables – net	**1,844**	(163)
Trading securities, at fair value	**158**	677
Spot commodities	**105**	(26)
Net unrealized (gain) loss on swaps, options and forward transactions	**2,059**	(966)
Securities purchased under agreements to resell	**(6,898)**	(10,638)
Securities sold under agreements to repurchase	**3,686**	2,384
Securities and spot commodities sold but not yet purchased, at market value	**660**	(330)
Finance receivables held for sale – originations and purchases	**(4,377)**	(7,965)
Sales of finance receivables – held for sale	**5,095**	7,888
Other, net	**985**	1,677
Total adjustments	**15,564**	(6,572)
Net cash provided by operating activities	**$ 27,056**	$ 4,037

See Accompanying Notes to Consolidated Financial Statements.

CONSOLIDATED STATEMENT OF CASH FLOWS *(continued)*

(in millions) (unaudited)

	Nine Months Ended September 30,	
	2007	2006
Cash flows from investing activities:		
Proceeds from (payments for)		
Sales and maturities of fixed maturity securities available for sale	**$ 97,068**	$ 86,579
Sales of equity securities available for sale	**6,700**	9,394
Proceeds from fixed maturity securities held to maturity	**175**	265
Sales of flight equipment	**95**	380
Sales or distributions of other invested assets	**9,298**	11,880
Payments received on mortgage, policy, collateral and guaranteed loans	**3,863**	3,081
Principal payments received on finance receivables held for investment	**9,554**	9,131
Purchases of fixed maturity securities available for sale	**(110,037)**	(106,750)
Purchases of equity securities available for sale	**(8,438)**	(11,032)
Purchases of fixed maturity securities held to maturity	**(154)**	(264)
Purchases of flight equipment	**(3,925)**	(4,860)
Purchases of other invested assets and warehoused investments	**(20,677)**	(12,865)
Mortgage, policy, collateral and guaranteed loans issued	**(6,554)**	(5,793)
Finance receivables held for investment – originations and purchases	**(11,394)**	(9,947)
Change in securities lending collateral	**(18,723)**	(11,917)
Net additions to real estate, fixed assets, and other assets	**(1,004)**	(620)
Net change in short-term investments	**(11,764)**	(8,787)
Net change in non-AIGFP derivative assets and liabilities	**(12)**	(19)
Net cash used in investing activities	**$ (65,929)**	$ (52,144)
Cash flows from financing activities:		
Proceeds from (payments for)		
Policyholders' contract deposits	**$ 46,239**	$ 40,226
Policyholders' contract withdrawals	**(43,220)**	(31,201)
Change in other deposits	**(713)**	753
Change in commercial paper	**2,526**	3,216
Notes, bonds, loans and mortgages payable, and hybrid financial instrument liabilities issued	**61,119**	40,345
Repayments on notes, bonds, loans and mortgages payable, and hybrid financial instrument liabilities	**(42,098)**	(16,851)
Issuance of junior subordinated debt	**4,490**	–
Issuance of guaranteed investment agreements	**6,430**	9,411
Maturities of guaranteed investment agreements	**(7,545)**	(9,480)
Change in securities lending payable	**18,156**	11,855
Issuance of treasury stock	**204**	94
Payments advanced to purchase shares	**(5,000)**	–
Acquisition of treasury stock	**(16)**	(7)
Cash dividends paid to shareholders	**(1,372)**	(1,209)
Other, net	**324**	424
Net cash provided by financing activities	**$ 39,524**	$ 47,576
Supplementary disclosure of cash flow information:		
Cash paid during the period for:		
Interest	**$ 6,190**	$ 4,202
Taxes	**$ 4,044**	$ 3,252
Non-cash financing activities:		
Interest credited to policyholder accounts	**$ 7,553**	$ 7,253
Treasury stock acquired using payments advanced to purchase shares	**$ 3,725**	–
Non-cash investing activities:		
Debt assumed on acquisitions and warehoused investments	**$ 358**	$ –
Liability related to purchase of additional interest in 21st Century	**$ 759**	$ –

See Accompanying Notes to Consolidated Financial Statements.

CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME (LOSS)

(in millions) (unaudited)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2007	2006	**2007**	2006
Net income	**$ 3,085**	$ 4,224	**$11,492**	$10,609
Other comprehensive income (loss):				
Unrealized (depreciation) appreciation of investments – net of reclassification adjustments	**(3,394)**	7,200	**(4,246)**	(1,133)
Deferred income tax benefit (expense) on above changes	**941**	(2,562)	**1,081**	281
Foreign currency translation adjustments	**619**	(115)	**290**	955
Deferred income tax benefit (expense) on above changes	**(109)**	17	**(74)**	(332)
Net derivative gains arising from cash flow hedging activities – net of reclassification adjustments	**(93)**	4	**(31)**	12
Deferred income tax benefit (expense) on above changes	**34**	(1)	**39**	(4)
Change in pension and postretirement unrecognized periodic benefit (cost)	**17**	–	**35**	(3)
Deferred income tax benefit (expense) on above changes	**(8)**	–	**(10)**	1
Other comprehensive income (loss)	**(1,993)**	4,543	**(2,916)**	(223)
Comprehensive income (loss)	**$ 1,092**	$ 8,767	**$ 8,576**	$10,386

See Accompanying Notes to Consolidated Financial Statements.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited)*

1. Summary of Significant Accounting Policies

Basis of Presentation

These unaudited condensed consolidated financial statements do not include certain financial information required by U.S. generally accepted accounting principles (GAAP) for complete financial statements and should be read in conjunction with the audited consolidated financial statements and the related notes included in the Annual Report on Form 10-K of American International Group, Inc. (AIG) for the year ended December 31, 2006 (2006 Annual Report on Form 10-K).

In the opinion of management, these consolidated financial statements contain the normal recurring adjustments necessary for a fair statement of the results presented herein. All material intercompany accounts and transactions have been eliminated.

Revisions and Reclassifications

In the third quarter of 2007, AIG determined that certain products that were historically reported as separate account assets under Statement of Position 03-1, "Accounting and Reporting by Insurance Enterprises for Certain Nontraditional Long-Duration Contracts and for Separate Accounts" (SOP 03-1) should have been reported as general account assets. Accordingly, the December 31, 2006 consolidated balance sheet has been revised to transfer $2.4 billion of assets from separate account assets to general account assets, and the same amount of liabilities from separate account liabilities to policyholders' contract deposits. This revision did not have any effect on consolidated income before income taxes, net income, or shareholders' equity for any period presented.

Certain reclassifications and format changes have been made to prior period amounts to conform to the current period presentation.

Out of period adjustments

During the three and nine-month periods ended September 30, 2007, AIG recorded the effects of certain out of period adjustments, which reduced net income by $35 million and $408 million, respectively, and diluted earnings per share by $0.01 per share and $0.16 per share, respectively.

During the three and nine-month periods ended September 30, 2006, AIG recorded the effects of certain out of period adjustments which increased (decreased) net income by $73 million and $(135) million, respectively, and diluted earnings per share by $0.03 per share and $(0.05) per share, respectively.

Recent Accounting Standards

Accounting Changes

SOP 05-1

On September 19, 2005, the American Institute of Certified Public Accountants (AICPA) issued Statement of Position 05-1, "Accounting by Insurance Enterprises for Deferred Acquisition Costs in Connection with Modifications or Exchanges of Insurance Contracts" (SOP 05-1). SOP 05-1 provides guidance on accounting for internal replacements of insurance and investment contracts other than those specifically described in Statement of Financial Accounting Standards (FAS) No. 97, "Accounting and Reporting by Insurance Enterprises for Certain Long-Duration Contracts and for Realized Gains and Losses from the Sale of Investments" (FAS 97). SOP 05-1 defines an internal replacement as a modification in product benefits, features, rights, or coverage that occurs by the exchange of a contract for a new contract, or by amendment, endorsement, or rider to a contract, or by the election of a feature or coverage within a contract. Internal replacements that result in a substantially changed contract are accounted for as a termination and a replacement contract.

The provisions of SOP 05-1 became effective as of January 1, 2007. On the date of adoption, AIG recorded a cumulative effect reduction of $82 million, net of tax, to the opening balance of retained earnings to reflect changes in unamortized deferred policy acquisition costs (DAC), value of business acquired, deferred sales inducement assets, unearned revenue liabilities and future policy benefits for life and accident and health insurance contracts. This adjustment primarily reflects a shorter expected life related to certain group life and health insurance contracts and the effect on the gross profits of investment-oriented products related to previously anticipated future internal replacements. This cumulative effect adjustment affected only the Life Insurance & Retirement Services segment.

FIN 48

On July 13, 2006, the Financial Accounting Standards Board (FASB) issued FASB Interpretation No. 48, "Accounting for Uncertainty in Income Taxes – an interpretation of FASB Statement No. 109" (FIN 48), which clarifies the accounting for uncertainty in income tax positions. FIN 48 prescribes a recognition threshold and measurement attribute for the financial statement recognition and measurement of an income tax position taken or expected to be taken in a tax return. FIN 48 also provides guidance on derecognition, classification, interest and penalties, accounting in interim periods, and additional disclosures. AIG adopted the provisions of FIN 48 on January 1, 2007. As a result of the adoption of FIN 48, AIG recognized a $71 million increase in the liability for unrecognized tax benefits, which was accounted for as a decrease to opening retained earnings as of January 1, 2007.

As of the date of adoption and after recognizing the effect of the increase in the liability noted above, the total amount of AIG's unrecognized tax benefit, excluding interest and penalties, was $1.138 billion. Included in this balance are $407 million related to tax positions, the disallowance of which would not

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

1. Summary of Significant Accounting Policies *(continued)*

affect the annual effective income tax rate. Accordingly, the amount of unrecognized tax benefit that, if recognized, would favorably affect the effective tax rate is $731 million.

At September 30, 2007, AIG's unrecognized tax benefit, excluding interest and penalties, was $1.139 billion, which includes $447 million related to tax positions the disallowance of which would not affect the annual effective income tax rate. Accordingly, the amount of unrecognized tax benefit that, if recognized, would favorably affect the effective tax rate was $692 million.

Interest and penalties related to unrecognized tax benefits are recognized in income tax expense. At January 1, 2007 and September 30, 2007, AIG had accrued $176 million and $207 million, respectively, for the payment of interest (net of tax benefits) and penalties.

Neither reserves for uncertain tax positions attributable to prior restatements (including various other remediation-related adjustments) nor the corresponding interest income have been recognized because such amounts are not currently estimable. In addition, certain tax benefits from compensation deductions have not been recognized because of existing uncertainty with respect to documentation supporting these tax benefits.

AIG continually evaluates proposed adjustments by taxing authorities. At September 30, 2007, such proposed adjustments would not result in a material change to AIG's consolidated financial condition. However, AIG believes that it is reasonably possible that the balance of the unrecognized tax benefits could decrease by $0 to $100 million within the next twelve months due to settlements or expiration of statutes.

Listed below are the tax years that remain subject to examination by major tax jurisdiction:

Major Tax Jurisdictions	Open Tax Years
United States	1991-2006
Hong Kong	1997-2006
Malaysia	1999-2006
Singapore	1993-2006
Thailand	2001-2006
Taiwan	2000-2006
Japan	2000-2006
United Kingdom	2003-2006
France	2003-2006
Korea	2001-2006

FSP 13-2

On July 13, 2006, the FASB issued FASB Staff Position (FSP) No. 13-2, "Accounting for a Change or Projected Change in the Timing of Cash Flows Relating to Income Taxes Generated by a Leveraged Lease Transaction" (FSP 13-2). FSP 13-2 addresses how a change or projected change in the timing of cash flows relating to income taxes generated by a leveraged lease transaction affects the accounting for the lease by the lessor, and directs that the tax assumptions be consistent with any FIN 48 uncertain tax position related to the lease. FSP 13-2 is effective for fiscal years beginning after December 15, 2006. Upon adoption, AIG recorded a $50 million decrease in the opening balance of retained earnings, net of tax, as of January 1, 2007 to reflect the cumulative effect of this change in accounting. The adoption of this guidance is not expected to have a material effect on AIG's results of operations in 2007.

As a result of the adoptions of SOP 05-1, FIN 48 and FSP 13-2, AIG recorded a total decrease to opening retained earnings of $203 million as of January 1, 2007.

Future Application of Accounting Standards

FAS 157

In September 2006, the FASB issued FAS No. 157, "Fair Value Measurements" (FAS 157). FAS 157 defines fair value, establishes a framework for measuring fair value and expands disclosure requirements regarding fair value measurements. FAS 157 will be effective January 1, 2008. AIG is currently assessing the effect of implementing this guidance.

FAS 159

In February 2007, the FASB issued FAS No. 159, "The Fair Value Option for Financial Assets and Financial Liabilities" (FAS 159). FAS 159 permits entities to choose to measure at fair value many financial instruments and certain other items that are not currently required to be measured at fair value. Subsequent changes in fair value for designated items will be required to be reported in earnings in the current period. FAS 159 also establishes presentation and disclosure requirements for similar types of assets and liabilities measured at fair value. FAS 159 will be effective January 1, 2008. AIG is currently assessing the effect of implementing this guidance, which depends on the nature and extent of items elected to be measured at fair value upon initial application of the standard on January 1, 2008.

SOP 07-1

In June 2007, the AICPA issued Statement of Position No. 07-1 (SOP 07-1), "Clarification of the Scope of the Audit and Accounting Guide 'Audits of Investment Companies' and Accounting by Parent Companies and Equity Method Investors for Investments in Investment Companies." SOP 07-1 amends the guidance for whether an entity may apply the provisions of the Audit and Accounting Guide, "Audits of Investment Companies" (the Guide). Investment companies that are subject to the Guide must report all investments at fair value regardless of the nature of the investment or the level of ownership. SOP 07-1 also establishes new requirements for whether a parent company can retain specialized investment company accounting in its consolidated financial statements for subsidiaries and equity method investees that are covered by the Guide. At the October 17, 2007 Board

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

1. Summary of Significant Accounting Policies *(continued)*

meeting, the FASB decided it would indefinitely defer the effective date of SOP 07-1. AIG understands that a FASB Staff Position will be issued shortly. AIG is currently monitoring any changes to the existing guidance.

2. Segment Information

AIG identifies its reportable segments by product line consistent with its management structure. These segments are General Insurance, Life Insurance & Retirement Services, Financial Services and Asset Management.

In order to better align financial reporting with the manner in which AIG's chief operating decision makers have managed their businesses, commencing in the first quarter of 2007, AIG realigned certain products among reportable segments and major internal reporting units. AIG also began reporting net realized capital gains and losses for the Financial Services and Asset Management segments in the results of these segments. Historically, net realized capital gains and losses were included in the Other category. There has been no change in AIG's management structure or in its reportable segments. All prior period amounts presented in the tables below have been revised to conform to the current year's presentation of these items.

The following table summarizes AIG's operations by major operating segment:

Operating Segments *(in millions)*	Three Months Ended September 30, **2007**	2006	Nine Months Ended September 30, **2007**	2006
Revenues[(a)]:				
General Insurance[(b)]	**$12,758**	$12,615	**$38,589**	$36,438
Life Insurance & Retirement Services[(b)]	**12,632**	12,542	**40,337**	37,303
Financial Services[(c)(d)]	**2,785**	3,011	**7,109**	5,923
Asset Management	**1,824**	993	**5,721**	3,647
Other	**13**	215	**407**	443
Consolidation and eliminations	**(176)**	(129)	**(532)**	(375)
Consolidated	**$29,836**	$29,247	**$91,631**	$83,379
Operating income (loss)[(a)]:				
General Insurance[(b)]	**$ 2,439**	$ 2,625	**$ 8,511**	$ 7,819
Life Insurance & Retirement Services[(b)]	**1,999**	2,472	**6,900**	7,483
Financial Services[(c)(d)]	**669**	1,179	**1,008**	541
Asset Management	**419**	211	**2,541**	1,445
Other[(e)]	**(627)**	(186)	**(1,557)**	(953)
Consolidation and eliminations	**(20)**	–	**(24)**	–
Consolidated	**$ 4,879**	$ 6,301	**$17,379**	$16,335

(a) Includes gains (losses) from hedging activities that did not qualify for hedge accounting treatment under FAS No. 133, "Accounting for Derivative Instruments and Hedging Activities" (FAS 133), including the related foreign exchange gains and losses. For the three-month periods ended September 30, 2007 and 2006, respectively, the effect was $(178) million and $165 million in both revenues and operating income. For the nine-month periods ended September 30, 2007 and 2006, respectively, the effect was $(1.06) billion and $(1.13) billion in both revenues and operating income. These amounts result primarily from interest rate and foreign currency derivatives that are hedging investments and borrowings. These gains (losses) for the three and nine-month periods ended September 30, 2007 include out of period charges of $20 million and $346 million, respectively, including a $380 million charge in the nine months ended September 30, 2007 to reverse net gains recognized on transfers of available for sale securities among legal entities consolidated within AIG Financial Products Corp. and AIG Trading Group Inc. and their respective subsidiaries (collectively, AIGFP). The three and nine-month periods ended September 30, 2006 include an out of period gain of $115 million and a charge of $223 million related to the remediation of the material weakness in accounting for certain derivative transactions under FAS 133.

(b) Includes the effect of out of period adjustments related to the accounting for certain interests in unit investment trusts (UCITS). For the three and nine-month periods ended September 30, 2006, the effect was an increase of $92 million and $472 million, respectively, in both revenues and operating income for General Insurance and an increase of $24 million and $240 million, respectively, in revenues and $24 million and $169 million, respectively, in operating income for Life Insurance & Retirement Services.

(c) Includes gains (losses) from hedging activities that did not qualify for hedge accounting treatment under FAS 133, including the related foreign exchange gains and losses. For the three-month periods ended September 30, 2007 and 2006, respectively, the effect was $353 million, and $581 million in both revenues and operating income. For the nine-month periods ended September 30, 2007 and 2006, respectively, the effect was $(250) million and $(1.2) billion in both revenues and operating income. These amounts result primarily from interest rate and foreign currency derivatives that are effective economic hedges of investments and borrowings. The three and nine-month periods ended September 30, 2007 include out of period charges of $20 million and $346 million, respectively, as discussed above. The three and nine-month periods ended September 30, 2006 include an out of period gain of $115 million and a charge of $223 million as discussed above. In the first quarter of 2007, AIG began applying hedge accounting for certain transactions, primarily in its Capital Markets operations. In the second quarter of 2007, American General Finance, Inc. (AGF) and International Lease Finance Corporation (ILFC) began applying hedge accounting to most of their derivatives hedging interest rate and foreign exchange risks associated with their floating rate and foreign currency denominated borrowings.

(d) For the three and nine-month periods ended September 30, 2007, both revenues and operating income include an unrealized market valuation loss of $352 million on AIGFP's super senior credit default swap portfolio.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

2. Segment Information *(continued)*

(e) Includes AIG parent and other operations which are not required to be reported separately. The following table presents the operating loss for AIG's Other category:

(in millions)	Three Months Ended September 30, 2007	Three Months Ended September 30, 2006	Nine Months Ended September 30, 2007	Nine Months Ended September 30, 2006
Other operating income (loss):				
Equity earnings in unconsolidated entities	**$ 37**	$ 48	**$ 128**	$ 178
Interest expense	**(315)**	(227)	**(869)**	(633)
Unallocated corporate expenses	**(157)**	(89)	**(519)**	(337)
Compensation expense – SICO Plans	**(9)**	(14)	**(29)**	(104)
Compensation expense – Starr tender offer	**–**	–	**–**	(54)
Net realized capital gains (losses)	**(199)**	85	**(226)**	31
Other miscellaneous, net	**16**	11	**(42)**	(34)
Total Other	**$(627)**	$(186)	**$(1,557)**	$(953)

The following table summarizes AIG's General Insurance operations by major internal reporting unit:

General Insurance *(in millions)*	Three Months Ended September 30, 2007	Three Months Ended September 30, 2006	Nine Months Ended September 30, 2007	Nine Months Ended September 30, 2006
Revenues:				
Domestic Brokerage Group	**$ 6,736**	$ 7,182	**$20,731**	$20,330
Transatlantic	**1,088**	1,004	**3,253**	3,035
Personal Lines	**1,252**	1,214	**3,688**	3,652
Mortgage Guaranty	**267**	226	**772**	636
Foreign General*	**3,413**	2,989	**10,150**	8,783
Reclassifications and eliminations	**2**	–	**(5)**	2
Total General Insurance	**$12,758**	$12,615	**$38,589**	$36,438
Operating Income (loss):				
Domestic Brokerage Group	**$ 1,829**	$ 1,543	**$ 5,662**	$ 4,322
Transatlantic	**189**	143	**508**	427
Personal Lines	**28**	133	**252**	352
Mortgage Guaranty	**(216)**	85	**(289)**	301
Foreign General*	**607**	721	**2,383**	2,415
Reclassifications and eliminations	**2**	–	**(5)**	2
Total General Insurance	**$ 2,439**	$ 2,625	**$ 8,511**	$ 7,819

* *Includes the effect of an out of period UCITS adjustment which increased both revenues and operating income by $22 million and $406 million for the three and nine-month periods ended September 30, 2006, respectively.*

The following table summarizes AIG's Life Insurance & Retirement Services operations by major internal reporting unit:

Life Insurance & Retirement Services *(in millions)*	Three Months Ended September 30, 2007	Three Months Ended September 30, 2006	Nine Months Ended September 30, 2007	Nine Months Ended September 30, 2006
Revenues:				
Foreign:				
Japan and Other	**$ 4,315**	$ 4,339	**$13,948**	$12,415
Asia*	**4,695**	4,109	**14,205**	12,872
Domestic:				
Domestic Life Insurance	**2,185**	2,259	**7,065**	6,848
Domestic Retirement Services	**1,437**	1,835	**5,119**	5,168
Total Life Insurance & Retirement Services	**$12,632**	$12,542	**$40,337**	$37,303
Operating Income:				
Foreign:				
Japan and Other	**$ 1,030**	$ 993	**$ 2,753**	$ 2,946
Asia*	**706**	615	**1,921**	2,087
Domestic:				
Domestic Life Insurance	**61**	261	**774**	862
Domestic Retirement Services	**202**	603	**1,452**	1,588
Total Life Insurance & Retirement Services	**$ 1,999**	$ 2,472	**$ 6,900**	$ 7,483

* *Includes the effect of an out of period UCITS adjustment, which increased revenues by $9 million and $208 million and operating income by $9 million and $137 million, respectively, for the three and nine-month periods ended September 30, 2006, respectively.*

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

2. Segment Information *(continued)*

The following table summarizes AIG's Financial Services operations by major internal reporting unit:

Financial Services *(in millions)*	Three Months Ended September 30, **2007**	2006	Nine Months Ended September 30, **2007**	2006
Revenues:				
Aircraft Leasing[(a)]	**$1,237**	$ 950	**$3,468**	$ 3,013
Capital Markets[(b)(c)]	**540**	1,118	**701**	30
Consumer Finance[(d)(e)]	**992**	901	**2,824**	2,768
Other, including intercompany adjustments	**16**	42	**116**	112
Total Financial Services	**$2,785**	$3,011	**$7,109**	$ 5,923
Operating income (loss):				
Aircraft Leasing[(a)]	**$ 254**	$ 47	**$ 625**	$ 421
Capital Markets[(b)(c)]	**370**	965	**183**	(457)
Consumer Finance[(d)(e)]	**69**	151	**180**	529
Other, including intercompany adjustments	**(24)**	16	**20**	48
Total Financial Services	**$ 669**	$1,179	**$1,008**	$ 541

(a) Both revenues and operating income include gains (losses) from hedging activities that did not qualify for hedge accounting treatment under FAS 133, including the related foreign exchange gains and losses. For the three-month periods ended September 30, 2007 and 2006, the effect was $(19) million and $(111) million, respectively. For the nine-month periods ended September 30, 2007 and 2006, the effect was $(32) million and $(56) million, respectively. These amounts result primarily from interest rate and foreign currency derivatives that are effective economic hedges of borrowings. In the second quarter of 2007, ILFC began applying hedge accounting to most of its derivatives hedging interest rate and foreign exchange risks associated with its floating rate and foreign currency denominated borrowings.

(b) Revenues, shown net of interest expense of $1.4 billion and $802 million for the three-month periods ended September 30, 2007 and 2006, respectively, and $3.3 billion and $2.1 billion for the nine-month periods ended September 30, 2007 and 2006, respectively, were primarily from hedged financial positions entered into in connection with counterparty transactions. Both revenues and operating income include gains (losses) from hedging activities that did not qualify for hedge accounting treatment under FAS 133, including the related foreign exchange gains and losses. For the three-month periods ended September 30, 2007 and 2006, the effect was $428 million and $783 million, respectively. For the nine-month periods ended September 30, 2007 and 2006, the effect was $(185) million and $(1.1) billion, respectively. The three and nine-month periods ended September 30, 2007 include out of period charges of $20 million and $346 million, respectively, including a $380 million charge in the nine months ended September 30, 2007 to reverse net gains recognized on transfers of available for sale securities among legal entities consolidated within AIGFP. The three and nine-month periods ended September 30, 2006 include an out of period gain of $115 million and a charge of $223 million, respectively, related to the remediation of the material weakness in accounting for certain derivative transactions under FAS 133. In the first quarter of 2007, AIGFP began applying hedge accounting for certain transactions.

(c) For the three and nine-month periods ended September 30, 2007, both revenues and operating income include an unrealized market valuation loss of $352 million on AIGFP's super senior credit default swap portfolio.

(d) Both revenues and operating income include gains (losses) from hedging activities that did not qualify for hedge accounting treatment under FAS 133, including the related foreign exchange gains and losses. For the three-month periods ended September 30, 2007 and 2006, the effect was $(6) million and $(73) million, respectively. For the nine-month periods ended September 30, 2007 and 2006, the effect was $(21) million and $(65) million, respectively. These amounts result primarily from interest rate and foreign currency derivatives that are effective economic hedges of borrowings. In the second quarter of 2007, AGF began applying hedge accounting to most of its derivatives hedging interest rate and foreign exchange risks associated with its floating rate and foreign currency denominated borrowings.

(e) The nine-month period ended September 30, 2007 includes a pre-tax charge of $178 million in connection with domestic consumer finance's mortgage banking activities.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

3. Shareholders' Equity and Earnings Per Share

Earnings Per Share (EPS)

Basic EPS of AIG is calculated using the weighted average number of common shares outstanding. Diluted EPS is based on those shares used in basic EPS plus shares that would have been outstanding assuming issuance of common shares for all potentially dilutive common shares outstanding.

The following table presents the computation of basic and diluted EPS:

	Three Months Ended September 30,		Nine Months Ended September 30,	
(in millions, except per share data)	**2007**	2006	**2007**	2006
Numerator for earnings per share:				
Income before cumulative effect of an accounting change	**$3,085**	$4,224	**$11,492**	$10,575
Cumulative effect of an accounting change, net of tax	**–**	–	**–**	34
Net income applicable to common stock for basic EPS	**$3,085**	$4,224	**$11,492**	$10,609
Interest on contingently convertible bonds, net of tax[(a)]	**–**	2	**–**	8
Net income applicable to common stock for diluted EPS	**$3,085**	$4,226	**$11,492**	$10,617
Cumulative effect of an accounting change, net of tax	**–**	–	**–**	(34)
Income before cumulative effect of an accounting change applicable to common stock for diluted EPS	**$3,085**	$4,226	**$11,492**	$10,583
Denominator for earnings per share:				
Weighted average shares outstanding used in the computation of EPS:				
Common stock issued	**2,751**	2,751	**2,751**	2,751
Common stock in treasury	**(189)**	(153)	**(168)**	(153)
Deferred shares	**14**	9	**13**	9
Weighted average shares outstanding – basic	**2,576**	2,607	**2,596**	2,607
Incremental shares from potential common stock:				
Weighted average number of shares arising from outstanding employee stock plans (treasury stock method)[(b)]	**13**	10	**13**	9
Contingently convertible bonds[(a)]	**–**	9	**–**	9
Weighted average shares outstanding – diluted[(b)]	**2,589**	2,626	**2,609**	2,625
Earnings per share:				
Basic:				
Income before cumulative effect of an accounting change	**$ 1.20**	$ 1.62	**$ 4.43**	$ 4.06
Cumulative effect of an accounting change, net of tax	**–**	–	**–**	0.01
Net income	**$ 1.20**	$ 1.62	**$ 4.43**	$ 4.07
Diluted:				
Income before cumulative effect of an accounting change	**$ 1.19**	$ 1.61	**$ 4.40**	$ 4.03
Cumulative effect of an accounting change, net of tax	**–**	–	**–**	0.01
Net income	**$ 1.19**	$ 1.61	**$ 4.40**	$ 4.04

(a) Assumes conversion of contingently convertible bonds due to the adoption of Emerging Issues Task Force Issue No. 04-8 "Accounting Issues Related to Certain Features of Contingently Convertible Debt and the Effect on Diluted Earnings per Share."

(b) Certain shares arising from employee stock plans were not included in the computation of diluted earnings per share where the exercise price of the options exceeded the average market price for the period and would have been antidilutive. The number of shares excluded was 7 million and 14 million for the nine-month periods ended September 30, 2007 and 2006, respectively.

Shareholders' Equity

From time to time, AIG may buy shares of its common stock for general corporate purposes, including to satisfy its obligations under various employee benefit plans. In February 2007, AIG's Board of Directors increased AIG's share repurchase program by authorizing the repurchase of shares with an aggregate purchase price of $8 billion. In March 2007, AIG entered into a $3 billion structured share repurchase arrangement and AIG entered into additional $1 billion structured share repurchase arrangements in each of May and September 2007. A total of 55,103,845 shares were repurchased during the first nine months of 2007. The portion of the payments advanced by AIG under the structured share repurchase arrangements that had not yet been utilized to repurchase shares at September 30, 2007, amounting to $1.28 billion, has been recorded as a component of shareholders' equity under the caption Payments advanced to purchase shares. Purchases have continued subsequent to September 30, 2007, with an additional 13,964,098 shares purchased from October 1 through November 5, 2007. All shares repurchased are recorded as treasury stock at cost.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

The quarterly dividend per common share, commencing with the dividend declared in May 2007 and paid on September 21, 2007, was $0.20.

The following table summarizes the changes in retained earnings during the first nine months of 2007:

(in millions)	**September 30, 2007**
Retained earnings:	
Balance at beginning of year	$ 84,996
Cumulative effect of accounting changes, net of tax	(203)
Adjusted balance, beginning of year	84,793
Net income	11,492
Dividends to shareholders	(1,455)
Balance, end of period	$ 94,830

4. Benefits Provided by Starr International Company, Inc. and C.V. Starr & Co., Inc.

Starr International Company, Inc. (SICO) has provided a series of two-year Deferred Compensation Profit Participation Plans (SICO Plans) to certain AIG employees. The SICO Plans came into being in 1975 when the voting shareholders and Board of Directors of SICO, a private holding company whose principal asset is AIG common stock, decided that a portion of the capital value of SICO should be used to provide an incentive plan for the current and succeeding managements of all American International companies, including AIG.

None of the costs of the various benefits provided under the SICO Plans has been paid by AIG, although AIG has recorded a charge to reported earnings for the deferred compensation amounts paid to AIG employees by SICO, with an offsetting amount credited to additional paid-in capital reflecting amounts deemed contributed by SICO. The SICO Plans provide that shares currently owned by SICO are set aside by SICO for the benefit of the participant and distributed upon retirement. The SICO Board of Directors currently may permit an early payout of units under certain circumstances. Prior to payout, the participant is not entitled to vote, dispose of or receive dividends with respect to such shares, and shares are subject to forfeiture under certain conditions, including but not limited to the participant's voluntary termination of employment with AIG prior to normal retirement age. Under the SICO Plans, SICO's Board of Directors may elect to pay a participant cash in lieu of shares of AIG common stock. Following notification from SICO to participants in the SICO Plans that it will settle specific future awards under the SICO Plans with shares rather than cash, AIG modified its accounting for the SICO Plans from variable to fixed measurement accounting. AIG gave effect to this change in settlement method beginning on December 9, 2005, the date of SICO's notice to participants in the SICO Plans. See also Note 6(b) "Commitments" herein.

In January 2006, C.V. Starr & Co., Inc. (Starr) completed its tender offer to purchase Starr interests from AIG employees. In conjunction with AIG's adoption of FAS No. 123R "Share-Based Payments" (FAS 123R), Starr is considered to be an "economic interest holder" in AIG. As a result, compensation expense of $54 million was included in the first nine months of 2006 with respect to the Starr tender offer.

Compensation expense with respect to the SICO Plans aggregated $9 million and $14 million for the three-month periods ended September 30, 2007 and 2006, respectively, and $29 million and $104 million for the nine-month periods ended September 30, 2007 and 2006, respectively. Compensation expense for the first nine months of 2006 included various out of period adjustments totaling $61 million, primarily relating to stock splits and other miscellaneous items for the SICO plans.

5. Ownership

According to the Schedule 13D filed on March 20, 2007 by Starr, SICO, Edward E. Matthews, Maurice R. Greenberg, the Maurice R. and Corinne P. Greenberg Family Foundation, Inc., the Universal Foundation, Inc., the Maurice R. and Corinne P. Greenberg Joint Tenancy Company, LLC and the C.V. Starr & Co., Inc. Trust, these reporting persons could be deemed to beneficially own 354,987,261 shares of AIG's common stock at that date. Based on the shares of AIG's common stock outstanding as of October 31, 2007, this ownership would represent approximately 14 percent of the voting stock of AIG. Although these reporting persons have made filings under Section 16 of the Securities Exchange Act of 1934 (Exchange Act), reporting sales of shares of common stock, no amendment to the Schedule 13D has been filed to report a change in ownership subsequent to March 20, 2007.

6. Commitments, Contingencies and Guarantees

In the normal course of business, various commitments and contingent liabilities are entered into by AIG and certain of its

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

6. Commitments, Contingencies and Guarantees *(continued)*

subsidiaries. In addition, AIG guarantees various obligations of certain subsidiaries.

(a) Litigation and Investigations

Litigation Arising from Operations. AIG and its subsidiaries, in common with the insurance and financial services industries in general, are subject to litigation, including claims for punitive damages, in the normal course of their business. In AIG's insurance operations, litigation arising from claims settlement activities is generally considered in the establishment of AIG's reserve for losses and loss expenses. However, in certain circumstances, AIG provides disclosure because of the size or nature of the potential liability to AIG. The potential for increasing jury awards and settlements makes it difficult to assess the ultimate outcome of such litigation.

Litigation Arising from Insurance Operations – Caremark. AIG and certain of its subsidiaries have been named defendants in two putative class actions in state court in Alabama that arise out of the 1999 settlement of class and derivative litigation involving Caremark Rx, Inc. (Caremark). The plaintiffs in the second-filed action have intervened in the first-filed action, and the second-filed action has been dismissed. An excess policy issued by a subsidiary of AIG with respect to the 1999 litigation was expressly stated to be without limit of liability. In the current actions, plaintiffs allege that the judge approving the 1999 settlement was misled as to the extent of available insurance coverage and would not have approved the settlement had he known of the existence and/or unlimited nature of the excess policy. They further allege that AIG, its subsidiaries, and Caremark are liable for fraud and suppression for misrepresenting and/or concealing the nature and extent of coverage. In their complaint, plaintiffs request compensatory damages for the 1999 class in the amount of $3.2 billion, plus punitive damages. AIG and its subsidiaries deny the allegations of fraud and suppression and have asserted, *inter alia,* that information concerning the excess policy was publicly disclosed months prior to the approval of the settlement. AIG and its subsidiaries further assert that the current claims are barred by the statute of limitations and that plaintiffs' assertions that the statute was tolled cannot stand against the public disclosure of the excess coverage. Plaintiffs, in turn, have asserted that the disclosure was insufficient to inform them of the nature of the coverage and did not start the running of the statute of limitations. The trial court is currently considering, under standards mandated by the Alabama Supreme Court, whether a class action can be certified and whether the defendants in the case brought by the intervenors should be dismissed. AIG cannot reasonably estimate either the likelihood of its prevailing in these actions or the potential damages in the event liability is determined.

Litigation Arising from Insurance Operations – Gunderson. A subsidiary of AIG has been named as a defendant in a putative class action lawsuit in the 14th Judicial District Court for the State of Louisiana. The *Gunderson* complaint alleges failure to comply with certain provisions of the Louisiana Any Willing Provider Act (the Act) relating to discounts taken by defendants on bills submitted by Louisiana medical providers and hospitals that provided treatment or services to workers compensation claimants and seeks monetary penalties and injunctive relief. On July 20, 2006, the court denied defendants' motion for summary judgment and granted plaintiffs' partial motion for summary judgment, holding that the AIG subsidiary was a "group purchaser" and, therefore, potentially subject to liability under the Act. On November 28, 2006, the court issued an order certifying a class of providers and hospitals. In an unrelated action also arising under the Act, a Louisiana appellate court ruled that the district court lacked jurisdiction to adjudicate the claims at issue. In response, defendants in *Gunderson* filed an exception for lack of subject matter jurisdiction. On January 19, 2007, the court denied the motion, holding that it has jurisdiction over the putative class claims. The AIG subsidiary is appealing the class certification ruling and is seeking an appeal from the jurisdictional ruling. AIG believes that it has meritorious defenses to plaintiffs' claims and expects that the ultimate resolution of this matter will not have a material adverse effect on AIG's consolidated financial condition or results of operations for any period.

2006 Regulatory Settlements. In February 2006, AIG reached a resolution of claims and matters under investigation with the United States Department of Justice (DOJ), the Securities and Exchange Commission (SEC), the Office of the New York Attorney General (NYAG) and the New York State Department of Insurance (DOI). AIG recorded an after-tax charge of $1.15 billion relating to these settlements in the fourth quarter of 2005.

The settlements resolved investigations conducted by the SEC, NYAG and DOI in connection with the accounting, financial reporting and insurance brokerage practices of AIG and its subsidiaries, as well as claims relating to the underpayment of certain workers compensation premium taxes and other assessments. These settlements did not, however, resolve investigations by regulators from other states into insurance brokerage practices related to contingent commissions and other broker-related conduct, such as alleged bid rigging. Nor did the settlements resolve any obligations that AIG may have to state guarantee funds in connection with any of these matters.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

6. Commitments, Contingencies and Guarantees *(continued)*

As a result of these settlements, AIG made payments or placed amounts in escrow in 2006 totaling approximately $1.64 billion, $225 million of which represented fines and penalties. Amounts held in escrow totaling $344 million, including interest thereon, are included in other assets at September 30, 2007. At that date, approximately $326 million of the funds were escrowed for settlement of claims resulting from the underpayment by AIG of its residual market assessments for workers compensation. The National Workers Compensation Reinsurance Pool, on behalf of its participant members, has filed a lawsuit against AIG with respect to the underpayment of such assessments. The National Association of Insurance Commissioners has formed a Settlement Review Working Group directed by the State of Indiana, which has commenced its own investigation into the underreporting of workers compensation premium. In addition, similar lawsuits filed by the Attorney General of the State of Minnesota, the Minnesota Workers Compensation Reinsurance Association and the Minnesota Workers Compensation Insurers Association are pending. AIG cannot currently estimate whether the amount ultimately required to settle these claims will exceed the funds escrowed or otherwise accrued for this purpose.

The remaining escrowed funds, which amounted to $18 million at September 30, 2007, are set aside for settlements for certain specified AIG policyholders. During the first nine months of 2007, approximately $367 million was paid out from escrow in exchange for releasing AIG and its subsidiaries from any alleged liability relating to, among other things, brokerage practices alleged in the NYAG settlement. Any funds remaining at the end of the escrow period can be used to resolve claims asserted by policyholders relating to such insurance brokerage practices, including those described in Private Litigation below.

In addition to the escrowed funds, $800 million was deposited into a fund under the supervision of the SEC as part of the settlements to be available to resolve claims asserted against AIG by investors, including the shareholder lawsuits described herein.

Also, as part of the settlements, AIG agreed to retain, for a period of three years, an independent consultant to conduct a review that will include, among other things, the adequacy of AIG's internal control over financial reporting, the policies, procedures and effectiveness of AIG's regulatory, compliance and legal functions and the remediation plan that AIG has implemented as a result of its own internal review.

Other than as described above, at the current time, AIG cannot predict the outcome of the matters described above, or estimate any potential additional costs related to these matters.

Private Litigation

Securities Actions. Beginning in October 2004, a number of putative securities fraud class action suits were filed against AIG and consolidated as *In re American International Group, Inc. Securities Litigation*. Subsequently, a separate, though similar, securities fraud action was also brought against AIG by certain Florida pension funds. The lead plaintiff in the class action is a group of public retirement systems and pension funds benefiting Ohio state employees, suing on behalf of themselves and all purchasers of AIG's publicly traded securities between October 28, 1999 and April 1, 2005. The named defendants are AIG and a number of present and former AIG officers and directors, as well as Starr, SICO, General Reinsurance Corporation, and PricewaterhouseCoopers LLP (PwC), among others. The lead plaintiff alleges, among other things, that AIG: (1) concealed that it engaged in anti-competitive conduct through alleged payment of contingent commissions to brokers and participation in illegal bid-rigging; (2) concealed that it used "income smoothing" products and other techniques to inflate its earnings; (3) concealed that it marketed and sold "income smoothing" insurance products to other companies; and (4) misled investors about the scope of government investigations. In addition, the lead plaintiff alleges that AIG's former Chief Executive Officer manipulated AIG's stock price. The lead plaintiff asserts claims for violations of Sections 11 and 15 of the Securities Act of 1933, Section 10(b) of the Exchange Act, and Rule 10b-5 promulgated thereunder, Section 20(a) of the Exchange Act, and Section 20A of the Exchange Act. In April 2006, the court denied the defendants' motions to dismiss the second amended class action complaint and the Florida complaint. In December 2006, a third amended class action complaint was filed, which does not differ substantially from the prior complaint. Fact and class discovery is currently ongoing.

ERISA Action. Between November 30, 2004 and July 1, 2005, several Employee Retirement Income Security Act of 1974 (ERISA) actions were filed on behalf of purported class of participants and beneficiaries of three pension plans sponsored by AIG or its subsidiaries. A consolidated complaint filed on September 26, 2005 alleges a class period between September 30, 2000 and May 31, 2005 and names as defendants AIG, the members of AIG's Retirement Board and the Administrative Boards of the plans at issue, and four present or former members of AIG's Board of Directors. The factual allegations in the complaint are essentially identical to those in the securities actions described above. Plaintiffs allege that defendants violated duties under ERISA by allowing the plans to offer AIG stock as a permitted investment, when defendants allegedly knew it was not a prudent investment, and by failing to provide participants with accurate information about AIG stock. AIG's motion to dismiss was denied by

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

6. Commitments, Contingencies and Guarantees *(continued)*

order dated December 12, 2006. AIG filed an answer on February 12, 2007, denying plaintiffs' allegations of wrongdoing and asserting affirmative defenses to plaintiffs' claims. AIG expects that the ultimate resolution of this matter will not have a material adverse effect on AIG's consolidated financial condition or results of operations for any period.

Derivative Actions – Southern District of New York. Between October 25, 2004 and July 14, 2005, seven separate derivative actions were filed in the Southern District of New York, five of which were consolidated into a single action. The New York derivative complaint contains nearly the same types of allegations made in the securities fraud and ERISA actions described above. The named defendants include current and former officers and directors of AIG, as well as Marsh & McLennan Companies, Inc. (Marsh), SICO, Starr, ACE Limited and subsidiaries (ACE), General Reinsurance Corporation, PwC, and certain employees or officers of these entity defendants. Plaintiffs assert claims for breach of fiduciary duty, gross mismanagement, waste of corporate assets, unjust enrichment, insider selling, auditor breach of contract, auditor professional negligence and disgorgement from AIG's former Chief Executive Officer and Chief Financial Officer of incentive-based compensation and AIG share proceeds under Section 304 of the Sarbanes-Oxley Act, among others. Plaintiffs seek, among other things, compensatory damages, corporate governance reforms, and a voiding of the election of certain AIG directors. AIG's Board of Directors has appointed a special committee of independent directors (special committee) to review the matters asserted in the operative consolidated derivative complaint. The court has entered an order staying the derivative case in the Southern District of New York pending resolution of the consolidated derivative action in the Delaware Chancery Court (discussed below). The court also has entered an order that termination of certain named defendants from the Delaware derivative action applies to the New York derivative action without further order of the court. On October 17, 2007, plaintiffs and those AIG officer and director defendants against whom the shareholder plaintiffs in the Delaware action are no longer pursuing claims filed a stipulation providing for all claims in the New York action against such defendants to be dismissed with prejudice. Former directors and officers Maurice R. Greenberg and Howard I. Smith have asked the court to refrain from so ordering this stipulation.

Derivative Actions – Delaware Chancery Court. From October 2004 to April 2005, AIG shareholders filed five derivative complaints in the Delaware Chancery Court. All of these derivative lawsuits have been consolidated into a single action. The amended consolidated complaint named 43 defendants (not including nominal defendant AIG) who, like the New York consolidated derivative litigation, were current and former officers and directors of AIG, as well as other entities and certain of their current and former employees and directors. Earlier in 2007, the Court approved an agreement that AIG be realigned as plaintiff, and, on June 13, 2007, acting on the direction of the special committee, AIG filed an amended complaint against former directors and officers Maurice R. Greenberg and Howard I. Smith, alleging breach of fiduciary duty and indemnification. Also on June 13, 2007, the special committee filed a motion to terminate the litigation as to certain defendants, while taking no action as to others. Defendants Greenberg and Smith filed answers to AIG's complaint and brought third-party complaints against certain current and former AIG directors and officers, PwC and Regulatory Insurance Services, Inc. Certain defendants have subsequently filed motions to dismiss plaintiffs' complaint, as well as defendants Greenberg and Smith's third-party complaints. On September 28, 2007, AIG and the shareholder plaintiffs filed a combined amended complaint in which AIG continued to assert claims against defendants Greenberg and Smith and took no position as to the claims asserted by the shareholder plaintiffs in the remainder of the combined amended complaint. In that pleading, the shareholder plaintiffs are no longer pursuing claims against certain AIG officers and directors. The factual allegations, legal claims and relief sought in the Delaware action are similar to those alleged in the New York derivative actions, except that shareholder plaintiffs in the Delaware derivative action assert claims only under state law. Certain defendants have filed motions to dismiss the shareholder plaintiffs' claims. The shareholder plaintiffs have moved to sever their claims to a separate action. AIG has joined that motion to the extent that, among other things, the claims brought by AIG against defendants Greenberg and Smith remain for prosecution in the pending action. AIG also has moved to stay discovery in the Delaware derivative action pending the resolution of the claims against AIG in the New York consolidated securities action. That motion, together with the motion to sever, is currently pending before the court.

In December 2002, a derivative lawsuit was filed in the Delaware Chancery Court against twenty directors and executives of AIG as well as against AIG as a nominal defendant that alleges, among other things, that the directors of AIG breached the fiduciary duties of loyalty and care by approving the payment of commissions to Starr and of rental and service fees to SICO and the executives breached their duty of loyalty by causing AIG to enter into contracts with Starr and SICO and their fiduciary duties by usurping AIG's corporate opportunity. The complaint further alleges that the Starr agencies did not provide any services that AIG was not capable of providing itself, and that the diversion of commissions to these entities was solely for the benefit of Starr's owners. The complaint also alleged that the service fees and rental

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

6. Commitments, Contingencies and Guarantees *(continued)*

payments made to SICO and its subsidiaries were improper. Under the terms of a stipulation approved by the Court on February 16, 2006, the claims against the outside independent directors were dismissed with prejudice, while the claims against the other directors were dismissed without prejudice. On October 31, 2005, Messrs. Greenberg, Matthews and Smith, SICO and Starr filed motions to dismiss the amended complaint. In an opinion dated June 21, 2006, the Court denied defendants' motion to dismiss, except with respect to plaintiff's challenge to payments made to Starr before January 1, 2000. On July 21, 2006, plaintiff filed its second amended complaint, which alleges that, between January 1, 2000 and May 31, 2005, individual defendants breached their duty of loyalty by causing AIG to enter into contracts with Starr and SICO and breached their fiduciary duties by usurping AIG's corporate opportunity. Starr is charged with aiding and abetting breaches of fiduciary duty and unjust enrichment for its acceptance of the fees. SICO is no longer named as a defendant. On April 20, 2007, the individual defendants and Starr filed a motion seeking leave of the Court to assert a cross-claim against AIG and a third-party complaint against PwC and the directors previously dismissed from the action, as well as certain other AIG officers and employees. On June 13, 2007, the Court denied the individual defendants' motion to file a third-party complaint, but granted the proposed cross-claim against AIG. On June 27, 2007, Starr filed its cross-claim against AIG, alleging one count that includes contribution, unjust enrichment and setoff. AIG has filed an answer and moved to dismiss Starr's cross-claim to the extent it seeks affirmative relief, as opposed to a reduction in the judgment amount. Starr has agreed to withdraw its claim for contribution and clarified that it is not seeking any relief on behalf of the individual defendants. AIG's motion to dismiss Starr's claim for affirmative relief is currently pending before the Court. Document discovery and depositions are currently ongoing.

Policyholder Actions. After the NYAG filed its complaint against insurance broker Marsh, policyholders brought multiple federal antitrust and Racketeer Influenced and Corrupt Organizations Act (RICO) class actions in jurisdictions across the nation against insurers and brokers, including AIG and a number of its subsidiaries, alleging that the insurers and brokers engaged in a broad conspiracy to allocate customers, steer business, and rig bids. These actions, including 24 complaints filed in different federal courts naming AIG or an AIG subsidiary as a defendant, were consolidated or will be consolidated by the judicial panel on multidistrict litigation and transferred to the United States District Court for the District of New Jersey for coordinated pretrial proceedings. The consolidated actions have proceeded in that court in two parallel actions, *In re Insurance Brokerage Antitrust Litigation* (the *First Commercial Complaint*) and *In re Employee Benefit Insurance Brokerage Antitrust Litigation* (the *First Employee Benefits Complaint,* and, together with the *First Commercial Complaint*, the multi-district litigation).

The plaintiffs in the *First Commercial Complaint* are nineteen corporations, individuals and public entities that contracted with the broker defendants for the provision of insurance brokerage services for a variety of insurance needs. The broker defendants are alleged to have placed insurance coverage on the plaintiffs' behalf with a number of insurance companies named as defendants, including AIG subsidiaries. The *First Commercial Complaint* also named ten brokers and fourteen other insurers as defendants (two of which have since settled). The *First Commercial Complaint* alleges that defendants engaged in a widespread conspiracy to allocate customers through "bid-rigging" and "steering" practices. The *First Commercial Complaint* also alleges that the insurer defendants permitted brokers to place business with AIG subsidiaries through wholesale intermediaries affiliated with or owned by those same brokers rather than placing the business with AIG subsidiaries directly. Finally, the *First Commercial Complaint* alleges that the insurer defendants entered into agreements with broker defendants that tied insurance placements to reinsurance placements in order to provide additional compensation to each broker. Plaintiffs assert that the defendants violated the Sherman Antitrust Act, RICO, the antitrust laws of 48 states and the District of Columbia, and are liable under common law breach of fiduciary duty and unjust enrichment theories. Plaintiffs seek treble damages plus interest and attorneys' fees as a result of the alleged RICO and Sherman Antitrust Act violations.

The plaintiffs in the *First Employee Benefits Complaint* are nine individual employees and corporate and municipal employers alleging claims on behalf of two separate nationwide purported classes: an employee class and an employer class that acquired insurance products from the defendants from August 26, 1994 to the date of any class certification. The *First Employee Benefits Complaint* names AIG, as well as eleven brokers and five other insurers, as defendants. The activities alleged in the *First Employee Benefits Complaint*, with certain exceptions, track the allegations of contingent commissions, bid-rigging and tying made in the *First Commercial Complaint*.

On October 3, 2006, Judge Hochberg of the District of New Jersey reserved in part and denied in part motions filed by the insurer defendants and broker defendants to dismiss the multi-district litigation. The Court also ordered the plaintiffs in both actions to file supplemental statements of particularity to elaborate on the allegations in their complaints. Plaintiffs filed their supplemental statements on October 25, 2006, and the AIG defendants, along with other insurer and

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

6. Commitments, Contingencies and Guarantees *(continued)*

broker defendants in the two consolidated actions, filed renewed motions to dismiss on November 30, 2006. On February 16, 2007, the case was transferred to Judge Garrett E. Brown, Chief Judge of the District of New Jersey. On April 5, 2007, Chief Judge Brown granted the defendants' renewed motions to dismiss the *First Commercial Complaint* and *First Employee Benefits Complaint* with respect to the antitrust and RICO claims. The claims were dismissed without prejudice and the plaintiffs were given 30 days, later extended to 45 days, to file amended complaints. On April 11, 2007, the Court stayed all proceedings, including all discovery, that are part of the multi-district litigation until any renewed motions to dismiss the amended complaints are resolved.

A number of complaints making allegations similar to those in the *First Commercial Complaint* have been filed against AIG and other defendants in state and federal courts around the country. The defendants have thus far been successful in having the federal actions transferred to the District of New Jersey and consolidated into the multi-district litigation and have petitioned to have a recently filed action transferred to the District of New Jersey for consolidation. The AIG defendants have also sought to have state court actions making similar allegations stayed pending resolution of the multi-district litigation proceeding. In one state court action pending in Florida, the trial court recently decided not to grant an additional stay, but instead to allow the case to proceed. Defendants filed their motions to dismiss, and on September 24, 2007, the court denied the motions with respect to the state antitrust, RICO, and common law claims and granted the motions with respect to both the Florida insurance bad faith claim against AIG (with prejudice) and the punitive damages claim (without prejudice). Discovery in this action is ongoing.

Plaintiffs filed amended complaints in both *In re Insurance Brokerage Antitrust Litigation* (the *Second Commercial Complaint*) and *In re Employee Benefit Insurance Brokerage Antitrust Litigation* (the *Second Employee Benefits Complaint*) along with revised particularized statements in both actions on May 22, 2007. The allegations in the *Second Commercial Complaint* and the *Second Employee Benefits Complaint* are substantially similar to the allegations in the *First Commercial Complaint and First Employee Benefits Complaint*, respectively. The complaints also attempt to add several new parties and delete others; the *Second Commercial Complaint* adds two new plaintiffs and twenty seven new defendants (including three new AIG defendants), and the *Second Employee Benefits Complaint* adds eight new plaintiffs and nine new defendants (including two new AIG defendants). The defendants filed motions to dismiss the amended complaints and to strike the newly added parties. The Court granted (without leave to amend) defendants' motions to dismiss the federal antitrust and RICO claims on August 31, 2007 and September 28, 2007, respectively. The Court declined to exercise supplemental jurisdiction over the state law claims in the *Second Commercial Complaint* and therefore dismissed it in its entirety. The *Second Employee Benefits Complaint* is still before the Court, pending a decision on defendants' motion for summary judgment on the ERISA claims.

On August 24, 2007, the Ohio Attorney General filed a complaint in the Ohio Court of Common Pleas against AIG and a number of its subsidiaries, as well as several other broker and insurer defendants, asserting violation of Ohio's antitrust laws. The complaint, which is similar to the *Second Commercial Complaint*, alleges that AIG and the other broker and insurer defendants conspired to allocate customers, divide markets, and restrain competition in commercial lines of casualty insurance sold through the broker defendant. The complaint seeks treble damages on behalf of Ohio public purchasers of commercial casualty insurance, disgorgement on behalf of both public and private purchasers of commercial casualty insurance, as well as a $500 per day penalty for each day of conspiratorial conduct.

Litigation Relating to 21st Century. Shortly after the announcement in late January 2007 of AIG's offer to acquire the outstanding shares of 21st Century Insurance Group (21st Century) not already owned by AIG and its subsidiaries, two related class actions were filed in the Superior Court of California, Los Angeles County, against AIG, 21st Century, and the individual members of 21st Century's Board of Directors, two of whom are current executive officers of AIG. The actions were filed purportedly on behalf of the minority shareholders of 21st Century and assert breaches of fiduciary duty in connection with the AIG proposal. The complaints alleged that the proposed per share price was unfair and sought preliminary and permanent injunctive relief to enjoin the consummation of the proposed transaction. On May 23, 2007, a third action was filed alleging breaches of fiduciary duty by the same defendants based upon their entering into the merger agreement and taking steps to complete the contemplated merger, and seeking injunctive relief comparable to that sought in the first two complaints. All three actions were consolidated under the caption *In re 21st Century Shareholder Litigation*. On August 14, 2007, the court dismissed the action at the request of the plaintiffs.

SICO. In July, 2005, SICO filed a complaint against AIG in the Southern District of New York, claiming that AIG had refused to provide SICO access to certain artwork and asked the court to order AIG immediately to release the property to SICO. AIG filed an answer denying SICO's allegations and setting forth defenses to SICO's claims. In addition, AIG filed counterclaims asserting breach of contract, unjust en-

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

6. Commitments, Contingencies and Guarantees *(continued)*

richment, conversion, breach of fiduciary duty, a constructive trust and declaratory judgment, relating to SICO's breach of its commitment to use its AIG shares only for the benefit of AIG and AIG employees. Fact and expert discovery has been substantially concluded and SICO's motion for summary judgment is pending.

Regulatory Investigations. Regulators from several states have commenced investigations into insurance brokerage practices related to contingent commissions and other industry-wide practices as well as other broker-related conduct, such as alleged bid-rigging. In addition, various federal and state regulatory agencies are reviewing certain transactions and practices of AIG and its subsidiaries in connection with industry-wide and other inquiries. AIG has cooperated, and will continue to cooperate, in producing documents and other information in response to subpoenas and other requests.

Wells Notices. AIG understands that some of its employees have received Wells notices in connection with previously disclosed SEC investigations of certain of AIG's transactions or accounting practices. Under SEC procedures, a Wells notice is an indication that the SEC staff has made a preliminary decision to recommend enforcement action that provides recipients with an opportunity to respond to the SEC staff before a formal recommendation is finalized. It is possible that additional current and former employees could receive similar notices in the future as the regulatory investigations proceed.

Effect on AIG

In the opinion of AIG management, AIG's ultimate liability for the unresolved litigation and investigation matters referred to above is not likely to have a material adverse effect on AIG's consolidated financial condition, although it is possible that the effect would be material to AIG's consolidated results of operations for an individual reporting period.

(b) Commitments

Flight Equipment

At September 30, 2007, ILFC had committed to purchase 245 new aircraft deliverable from 2007 through 2017 at an estimated aggregate purchase price of $21.0 billion. ILFC will be required to find customers for any aircraft acquired, and it must arrange financing for portions of the purchase price of such equipment.

Other Commitments

In the normal course of business, AIG enters into commitments to invest in limited partnerships, private equities, hedge funds and mutual funds and to purchase and develop real estate in the U.S. and abroad. These commitments totaled $5.98 billion at September 30, 2007.

On June 27, 2005, AIG entered into an agreement pursuant to which AIG agrees, subject to certain conditions, to make any payment that is not promptly paid with respect to the benefits accrued by certain employees of AIG and its subsidiaries under the SICO Plans (as discussed in Note 4 herein).

(c) Contingencies

Loss Reserves. Although AIG regularly reviews the adequacy of the established reserve for losses and loss expenses, there can be no assurance that AIG's ultimate loss reserves will not develop adversely and materially exceed AIG's current loss reserves. Estimation of ultimate net losses, loss expenses and loss reserves is a complex process for long-tail casualty lines of business, which include excess and umbrella liability, directors and officers liability (D&O), professional liability, medical malpractice, workers compensation, general liability, products liability and related classes, as well as for asbestos and environmental exposures. Generally, actual historical loss development factors are used to project future loss development. However, there can be no assurance that future loss development patterns will be the same as in the past. Moreover, any deviation in loss cost trends or in loss development factors might not be discernible for an extended period of time subsequent to the recording of the initial loss reserve estimates for any accident year. Thus, there is the potential for reserves with respect to a number of years to be significantly affected by changes in loss cost trends or loss development factors that were relied upon in setting the reserves. These changes in loss cost trends or loss development factors could be attributable to changes in inflation, in labor and material costs or in the judicial environment, or in other social or economic phenomena affecting claims.

Synthetic Fuel Tax Credits. AIG generates income tax credits as a result of investing in synthetic fuel production. Tax credits generated from the production and sale of synthetic fuel under the Internal Revenue Code are subject to an annual phase-out provision that is based on the average wellhead price of domestic crude oil. The price range within which the tax credits are phased-out was originally established in 1980 and is adjusted annually for inflation. Depending on the price of domestic crude oil for a particular year, all or a portion of the tax credits generated in that year might be eliminated. AIG evaluates the production levels of its synthetic fuel production facilities in light of the risk of phase-out of the associated tax credits. As a result of fluctuating domestic crude oil prices, AIG evaluates and adjusts production levels when appropriate in light of this risk. Recent increases in oil prices have reduced the current estimate of 2007

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

6. Commitments, Contingencies and Guarantees *(continued)*

tax credits. Under current legislation, the opportunity to generate additional tax credits from the production and sale of synthetic fuel expires on December 31, 2007.

Lease Transactions. In June and August, 2007, field agents at the Internal Revenue Service issued Notices of Proposed Adjustment (NOPAs) relating to a series of lease transactions by an AIG subsidiary. In the NOPAs, the field agents asserted that the leasing transactions were "lease-in lease-out" transactions described in Revenue Ruling 2002-69 and proposed adjustments to taxable income of approximately $203 million in the aggregate for the years 1998, 1999, 2001 and 2002.

(d) Guarantees

AIG and certain of its subsidiaries become parties to derivative financial instruments with market risk resulting from both dealer and end-user activities and to reduce currency, interest rate, equity and commodity exposures. These instruments are carried at their estimated fair values in the consolidated balance sheet. The vast majority of AIG's derivative activity is transacted by AIGFP. See Note 9 below and see Note 19 to the consolidated financial statements in the 2006 Annual Report on Form 10-K.

AIG has issued unconditional guarantees with respect to the prompt payment, when due, of all present and future payment obligations and liabilities of AIGFP arising from transactions entered into by AIGFP.

SAI Deferred Compensation Holdings, Inc., a wholly owned subsidiary of AIG, has established a deferred compensation plan for registered representatives of certain AIG subsidiaries, pursuant to which participants have the opportunity to invest deferred commissions and fees on a notional basis. The value of the deferred compensation fluctuates with the value of the deferred investment alternatives chosen. AIG has provided a full and unconditional guarantee of the obligations of SAI Deferred Compensation Holdings, Inc. to pay the deferred compensation under the plan.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

7. Employee Benefits

The following table presents the components of the net periodic benefit costs with respect to pensions and other postretirement benefits:

	Pensions			Postretirement		
(in millions)	Non-U.S. Plans	U.S. Plans	Total	Non-U.S. Plans	U.S. Plans	Total
Three Months Ended September 30, 2007						
Components of net periodic benefit cost:						
Service cost	**$ 22**	**$ 30**	**$ 52**	**$ 1**	**$ 3**	**$ 4**
Interest cost	**12**	**45**	**57**	**1**	**3**	**4**
Expected return on assets	**(9)**	**(53)**	**(62)**	**–**	**–**	**–**
Amortization of prior service cost	**(2)**	**(1)**	**(3)**	**–**		
Amortization of net loss	**2**	**9**	**11**	**–**	**–**	**–**
Amortization of initial net obligation	**1**	**–**	**1**	**–**	**–**	**–**
Settlement loss	**–**	**3**	**3**	**–**	**–**	**–**
Net periodic benefit cost	**$ 26**	**$ 33**	**$ 59**	**$ 2**	**$ 6**	**$ 8**
Three Months Ended September 30, 2006						
Components of net periodic benefit cost:						
Service cost	$ 18	$ 32	$ 50	$ 1	$ 1	$ 2
Interest cost	9	41	50	1	3	4
Expected return on assets	(7)	(48)	(55)	–	–	–
Amortization of prior service cost	(3)	(1)	(4)	–	(2)	(2)
Amortization of transitional liability	1	–	1	–	–	–
Recognized actuarial loss	4	18	22	–	–	–
Net periodic benefit cost	$ 22	$ 42	$ 64	$ 2	$ 2	$ 4
Nine Months Ended September 30, 2007						
Components of net periodic benefit cost:						
Service cost	**$ 66**	**$ 90**	**$ 156**	**$ 4**	**$ 8**	**$ 12**
Interest cost	**36**	**134**	**170**	**2**	**11**	**13**
Expected return on assets	**(27)**	**(160)**	**(187)**	**–**	**–**	**–**
Amortization of prior service cost	**(7)**	**(2)**	**(9)**	**–**	**(1)**	**(1)**
Amortization of net loss	**7**	**27**	**34**	**–**	**–**	**–**
Amortization of initial net obligation	**1**	**–**	**1**	**–**	**–**	**–**
Settlement loss	**1**	**3**	**4**	**–**	**–**	**–**
Net periodic benefit cost	**$ 77**	**$ 92**	**$ 169**	**$ 6**	**$ 18**	**$ 24**
Nine Months Ended September 30, 2006						
Components of net periodic benefit cost:						
Service cost	$ 55	$ 94	$ 149	$ 3	$ 4	$ 7
Interest cost	26	122	148	2	8	10
Expected return on assets	(21)	(145)	(166)	–	–	–
Amortization of prior service cost	(7)	(2)	(9)	–	(5)	(5)
Amortization of transitional liability	1	–	1	–	–	–
Recognized actuarial loss	12	56	68	–	–	–
Net periodic benefit cost	$ 66	$ 125	$ 191	$ 5	$ 7	$ 12

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

8. Information Provided in Connection with Outstanding Debt

The following condensed consolidating financial statements are provided in compliance with Regulation S-X of the Securities and Exchange Commission.

- **AIG Life Holdings (US), Inc. (AIGLH), formerly known as American General Corporation, is a holding company and a wholly owned subsidiary of AIG. AIG provides a full and unconditional guarantee of all outstanding debt of AIGLH.**
- **AIG Liquidity Corp. is a wholly owned subsidiary of AIG. AIG provides a full and unconditional guarantee of all obligations of AIG Liquidity Corp.**
- **AIG Program Funding, Inc. is a wholly owned subsidiary of AIG. AIG provides a full and unconditional guarantee of all obligations of AIG Program Funding, Inc., which was established in 2007.**

Condensed Consolidating Balance Sheet

(in millions)	American International Group, Inc. (As Guarantor)	AIGLH	AIG Liquidity Corp.	AIG Program Funding, Inc.	Other Subsidiaries	Eliminations	Consolidated AIG
September 30, 2007							
Assets:							
Investments and financial services assets	$ 15,718	$ 40	$ –	$ –	$ 865,584	$ (19,490)	$ 861,852
Cash	25	1	–	–	2,223	–	2,249
Carrying value of subsidiaries and partially owned companies, at equity	118,252	24,378	–	–	11,451	(152,804)	1,277
Other assets	4,693	2,650	–	–	199,420	(36)	206,727
Total assets	$138,688	$27,069	$ –	$ –	$1,078,678	$ (172,330)	$1,072,105
Liabilities:							
Insurance liabilities	$ 48	$ –	$ –	$ –	$ 518,879	$ (63)	$ 518,864
Debt	28,758	2,136	–	–	163,878	(18,587)	176,185
Other liabilities	5,815	3,191	–	–	264,348	(465)	272,889
Total liabilities	34,621	5,327	–	–	947,105	(19,115)	967,938
Preferred shareholders' equity in subsidiary companies	–	–	–	–	100	–	100
Total shareholders' equity	104,067	21,742	–	–	131,473	(153,215)	104,067
Total liabilities, preferred shareholders' equity in subsidiary companies and shareholders' equity	$138,688	$27,069	$ –	$ –	$1,078,678	$ (172,330)	$1,072,105

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

(in millions)	American International Group, Inc. (As Guarantor)	AIGLH	AIG Liquidity Corp.	AIG Program Funding, Inc.	Other Subsidiaries	Eliminations	Consolidated AIG
December 31, 2006							
Assets:							
Investments and financial services assets	$ 7,346	$ –	$*	$ –	$ 800,350	$ (14,822)	$ 792,874
Cash	76	–	*	–	1,514	–	1,590
Carrying value of subsidiaries and partially owned companies, at equity	109,125	27,967	–	–	8,436	(144,427)	1,101
Other assets	3,989	2,622	*	–	179,183	(1,949)	183,845
Total assets	$120,536	$30,589	$*	$ –	$ 989,483	$ (161,198)	$ 979,410
Liabilities:							
Insurance liabilities	$ 21	$ –	$ –	$ –	$ 497,514	$ (64)	$ 497,471
Debt	15,157	2,136	*	–	146,206	(14,820)	148,679
Other liabilities	3,681	3,508	*	–	225,685	(1,482)	231,392
Total liabilities	18,859	5,644	*	$ –	869,405	(16,366)	877,542
Preferred shareholders' equity in subsidiary companies	–	–	–	–	191	–	191
Total shareholders' equity	101,677	24,945	*	–	119,887	(144,832)	101,677
Total liabilities, preferred shareholders' equity in subsidiary companies and shareholders' equity	$120,536	$30,589	$*	$ –	$ 989,483	$ (161,198)	$ 979,410

**Less than $1 million.*

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

8. Information Provided in Connection with Outstanding Debt *(continued)*

Condensed Consolidating Statement of Income

(in millions)	American International Group, Inc. (As Guarantor)	AIGLH	AIG Liquidity Corp.	AIG Program Funding, Inc.	Other Subsidiaries	Eliminations	Consolidated AIG
Three Months Ended September 30, 2007							
Operating income (loss)	**$ (587)**	**$ (37)**	**$ ***	**$ –**	**$ 5,503**	**$ –**	**$ 4,879**
Equity in undistributed net income of consolidated subsidiaries	**2,343**	**55**	**–**	**–**	**–**	**(2,398)**	**–**
Dividend income from consolidated subsidiaries	**1,109**	**320**	**–**	**–**	**–**	**(1,429)**	**–**
Income taxes	**(220)**	**256**	*****	**–**	**1,427**	**–**	**1,463**
Minority interest	**–**	**–**	**–**	**–**	**(331)**	**–**	**(331)**
Net income (loss)	**$ 3,085**	**$ 82**	**$ ***	**$ –**	**$ 3,745**	**$ (3,827)**	**$ 3,085**
Three Months Ended September 30, 2006							
Operating income (loss)	$ (215)	$ (49)	$ *	$ –	$ 6,565	$ –	$ 6,301
Equity in undistributed net income of consolidated subsidiaries	4,223	420	–	–	–	(4,643)	–
Dividend income from consolidated subsidiaries	287	134	–	–	–	(421)	–
Income taxes (benefits)	71	(17)	*	–	1,889	–	1,943
Minority interest	–	–	–	–	(134)	–	(134)
Net income (loss)	$ 4,224	$ 522	$ *	$ –	$ 4,542	$ (5,064)	$ 4,224
Nine Months Ended September 30, 2007							
Operating income (loss)	**$ (1,130)**	**$ (123)**	**$ ***	**$ –**	**$18,632**	**$ –**	**$17,379**
Equity in undistributed net income of consolidated subsidiaries	**9,192**	**546**	**–**	**–**	**–**	**(9,738)**	**–**
Dividend income from consolidated subsidiaries	**3,274**	**978**	**–**	**–**	**–**	**(4,252)**	**–**
Income taxes	**(156)**	**249**	*****	**–**	**4,775**	**–**	**4,868**
Minority interest	**–**	**–**	**–**	**–**	**(1,019)**	**–**	**(1,019)**
Net income (loss)	**$11,492**	**$1,152**	**$ ***	**$ –**	**$12,838**	**$(13,990)**	**$11,492**
Nine Months Ended September 30, 2006							
Operating income (loss)	$ (937)	$ (135)	$ *	$ –	$17,407	$ –	$16,335
Equity in undistributed net income of consolidated subsidiaries	10,990	1,088	–	–	–	(12,078)	–
Dividend income from consolidated subsidiaries	854	592	–	–	–	(1,446)	–
Income taxes (benefits)	332	(47)	*	–	4,781	–	5,066
Minority interest	–	–	–	–	(694)	–	(694)
Cumulative effect of an accounting change, net of tax	34	–	–	–	–	–	34
Net income (loss)	$10,609	$1,592	$ *	$ –	$11,932	$(13,524)	$10,609

**Less than $1 million.*

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

8. Information Provided in Connection with Outstanding Debt *(continued)*

Condensed Consolidating Statement of Cash Flows

(in millions)	American International Group, Inc. (As Guarantor)	AIGLH	AIG Liquidity Corp.	AIG Program Funding, Inc.	Other Subsidiaries	Consolidated AIG
Nine Months Ended September 30, 2007						
Net cash provided by operating activities	**$ 1,627**	**$ 375**	**$ ***	**$ –**	**$ 25,054**	**$ 27,056**
Cash flows from investing:						
Invested assets disposed	**782**	**–**	**–**	**–**	**125,971**	**126,753**
Invested assets acquired	**(8,767)**	**–**	**–**	**–**	**(182,911)**	**(191,678)**
Other	**186**	**(220)**	*****	**–**	**(970)**	**(1,004)**
Net cash used in investing activities	**(7,799)**	**(220)**	*****	**–**	**(57,910)**	**(65,929)**
Cash flows from financing activities:						
Issuance of debt	**13,540**	**–**	**–**	**–**	**61,025**	**74,565**
Repayments of debt	**(1,143)**	**–**	**–**	**–**	**(48,500)**	**(49,643)**
Payments advanced to purchase shares	**(2,955)**	**–**	**–**	**–**	**(2,045)**	**(5,000)**
Cash dividends paid to shareholders	**(1,372)**	**–**	**–**	**–**	**–**	**(1,372)**
Other	**(1,949)**	**(154)**	*****	**–**	**23,077**	**20,974**
Net cash provided by (used in) financing activities	**6,121**	**(154)**	*****	**–**	**33,557**	**39,524**
Effect of exchange rate changes on cash	**–**	**–**	**–**	**–**	**8**	**8**
Change in cash	**(51)**	**1**	*****	**–**	**709**	**659**
Cash at beginning of period	**76**	**–**	**–**	**–**	**1,514**	**1,590**
Cash at end of period	**$ 25**	**$ 1**	**$ ***	**$ –**	**$ 2,223**	**$ 2,249**
Nine Months Ended September 30, 2006						
Net cash (used in) provided by operating activities	$ (2,526)	$ 160	$ *	$ –	$ 6,403	$ 4,037
Cash flows from investing:						
Invested assets disposed	2,147	–	–	–	118,563	120,710
Invested assets acquired	(5,555)	–	–	–	(166,679)	(172,234)
Other	790	(17)	*	–	(1,393)	(620)
Net cash used in investing activities	(2,618)	(17)	*	–	(49,509)	(52,144)
Cash flows from financing activities:						
Issuance of debt	7,445	–	–	–	45,527	52,972
Repayments of debt	(1,345)	–	–	–	(24,986)	(26,331)
Cash dividends paid to shareholders	(1,209)	–	–	–	–	(1,209)
Other	91	(143)	*	–	22,196	22,144
Net cash provided by (used in) financing activities	4,982	(143)	*	–	42,737	47,576
Effect of exchange rate changes on cash	–	–	–	–	59	59
Change in cash	(162)	–	*	–	(310)	(472)
Cash at beginning of period	190	–	–	–	1,707	1,897
Cash at end of period	$ 28	$ –	$ *	$ –	$ 1,397	$ 1,425

**Less than $1 million.*

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

9. Derivatives and Hedge Accounting

AIG uses derivatives and other financial instruments as part of its financial risk management programs and as part of its investment operations. AIGFP also transacts in derivatives as a dealer.

Derivatives, as defined in FAS 133, are financial arrangements among two or more parties with returns linked to or "derived" from some underlying equity, debt, commodity or other asset, liability, or foreign exchange rate or other index or the occurrence of a specified payment event. Derivative payments may be based on interest rates, exchange rates, prices of certain securities, commodities, or financial or commodity indices or other variables.

Unless subject to a scope exclusion, AIG carries all derivatives on the consolidated balance sheet at fair value. The changes in fair value of the derivative transactions of AIGFP are presented as a component of AIG's operating income.

AIGFP

AIGFP, in the ordinary course of operations and as principal, structures and enters into derivative transactions to meet the needs of counterparties who may be seeking to hedge certain aspects of such counterparties' operations or obtain a desired financial exposure. AIGFP also enters into derivative transactions to mitigate risk in its exposures (interest rates, currencies, commodities, credit and equities) arising from such transactions. Such instruments are carried at market or fair value, whichever is appropriate, and are reflected on the balance sheet in "Unrealized gain on swaps, options and forward transactions" and "Unrealized loss on swaps, options and forward contracts."

Beginning in the first quarter of 2007, AIGFP designated certain interest rate swaps as fair value hedges of the benchmark interest rate risk on certain of its interest bearing financial assets and liabilities. In these hedging relationships, AIG is hedging its fixed rate available for sale securities and fixed rate borrowings. AIGFP also designated foreign currency forward contracts as fair value hedges for changes in spot foreign exchange rates of the non-U.S. dollar denominated available for sale debt securities. Under these strategies, all or portions of individual or multiple derivatives may be designated against a single hedged item.

At inception of each hedging relationship, AIGFP performs and documents its prospective assessments of hedge effectiveness to demonstrate that the hedge is expected to be highly effective. For hedges of interest rate risk, AIGFP uses regression to demonstrate the hedge is highly effective, while it uses the periodic dollar offset method for its foreign currency hedges. AIGFP uses the periodic dollar offset method to assess whether its hedging relationships were highly effective on a retrospective basis. The prospective and retrospective assessments are updated on a daily basis. The passage of time component of the hedging instruments and the forward points on foreign currency hedges are excluded from the assessment of hedge effectiveness and measurement of hedge ineffectiveness. AIGFP does not utilize the shortcut, matched terms or equivalent methods.

The change in fair value of the derivative that qualifies under the requirements of FAS 133 as a fair value hedge is recorded in current period earnings along with the gain or loss on the hedged item for the hedged risk. For interest rate hedges, the adjustments to the carrying value of the hedged items are amortized into income using the effective yield method over the remaining life of the hedged item. Amounts excluded from the assessment of hedge effectiveness are recognized in current period earnings.

For the three and nine months ended September 30, 2007, AIGFP recognized net losses of $5 million and $3 million in earnings, respectively, representing hedge ineffectiveness, and also recognized net losses of $152 million and $363 million, respectively, related to the portion of the hedging instruments excluded from the assessment of hedge effectiveness. All these amounts are reflected in Other income. AIGFP did not apply hedge accounting in 2006.

Other Derivative Users

AIG and its subsidiaries (other than AIGFP) also use derivatives and other instruments as part of their financial risk management programs. Interest rate derivatives (such as interest rate swaps) are used to manage interest rate risk associated with investments in fixed income securities, commercial paper issuances, medium and long-term note offerings, and other interest rate sensitive assets and liabilities. In addition, foreign exchange derivatives (principally cross currency swaps, forwards and options) are used to economically mitigate risk associated with non-U.S. dollar denominated debt, net capital exposures and foreign exchange transactions. The derivatives are effective economic hedges of the exposures they are meant to offset.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

9. Derivatives and Hedge Accounting *(continued)*

In 2007, AIG and its subsidiaries other than AIGFP designated certain derivatives as either fair value or cash flow hedges of their debt. The fair value hedges included (i) interest rate swaps that were designated as hedges of the change in the fair value of fixed rate debt attributable to changes in the benchmark interest rate and (ii) foreign currency swaps designated as hedges of the change in fair value of foreign currency denominated debt attributable to changes in foreign exchange rates and/or the benchmark interest rate. With respect to the cash flow hedges, (i) interest rate swaps were designated as hedges of the changes in cash flows on floating rate debt attributable to changes in the benchmark interest rate, and (ii) foreign currency swaps were designated as hedges of changes in cash flows on foreign currency denominated debt attributable to changes in the benchmark interest rate and foreign exchange rates.

AIG assesses, both at the hedge's inception and on an ongoing basis, whether the derivatives used in hedging transactions are highly effective in offsetting changes in fair values or cash flows of hedged items. Regression analysis is employed to assess the effectiveness of these hedges both on a prospective and retrospective basis. AIG does not utilize the shortcut, matched terms or equivalent methods.

The change in fair value of derivatives designated and effective as fair value hedges along with the gain or loss on the hedged item are recorded in net realized capital gains (losses). Upon discontinuation of hedge accounting, the cumulative adjustment to the carrying value of the hedged item resulting from changes in the benchmark interest rate is amortized into income using the effective yield method over the remaining life of the hedged item. Amounts excluded from the assessment of hedge effectiveness are recognized in current period earnings. During both the three and nine months ended September 30, 2007, AIG recognized a loss of less than $1 million in earnings related to the ineffective portion of the hedging instruments. During the three and nine months ended September 30, 2007, AIG also recognized losses of $45 million and $53 million, respectively, related to the change in the hedging instruments forward points excluded from the assessment of hedge effectiveness.

The effective portion of the change in fair value of a derivative qualifying as a cash flow hedge is recorded in Accumulated other comprehensive income (loss), until earnings are affected by the variability of cash flows in the hedged item. The ineffective portion of these hedges is recorded in net realized capital gains (losses). During both the three and nine months ended September 30, 2007, AIG recognized losses of $1 million in earnings representing hedge ineffectiveness. At September 30, 2007, $10 million of the deferred net loss in Accumulated other comprehensive income is expected to be recognized in earnings during the next 12 months. All components of the derivatives' gains and losses were included in the assessment of hedge effectiveness. There were no instances of the discontinuation of hedge accounting in 2007.

10. Cash Flows

As part of its ongoing remediation activities, AIG has made certain revisions to the Consolidated Statement of Cash Flows, primarily relating to certain elements of net realized capital gains, the effect of reclassifying certain policyholders' account balances from Other policyholder funds to Policyholders' contract deposits, the elimination of certain intercompany balances and revisions related to separate account assets. Accordingly, AIG revised the previous periods presented to conform to the revised presentation.

The revisions and their effect on the Consolidated Statement of Cash Flows for the nine months ended September 30, 2006 are presented below:

(in millions)	Originally Reported September 30, 2006	Revisions	As Revised
Cash flows from operating activities	$ 6,004	$(1,967)	$ 4,037
Cash flows from investing activities	(51,400)	(744)	(52,144)
Cash flows from financing activities	44,865	2,711	47,576
Effect of exchange rate changes on cash	59	—	59
Change in cash	(472)	—	(472)

ITEM 2. Management's Discussion and Analysis of Financial Condition and Results of Operations

Management's Discussion and Analysis of Financial Condition and Results of Operations is designed to provide the reader a narrative with respect to AIG's operations, financial condition and liquidity and certain other significant matters.

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Cautionary Statement Regarding Projections and Other Information About Future Events

This Quarterly Report on Form 10-Q and other publicly available documents may include, and AIG's officers and representatives may from time to time make, projections concerning financial information and statements concerning future economic performance and events, plans and objectives relating to management, operations, products and services, and assumptions underlying these projections and statements. These projections and statements are not historical facts but instead represent only AIG's belief regarding future events, many of which, by their nature, are inherently uncertain and outside AIG's control. These projections and statements may address, among other things, the status and potential future outcome of the current regulatory and civil proceedings against AIG and their potential effect on AIG's businesses, financial position, results of operations, cash flows and liquidity, the effect of credit rating changes on AIG's businesses and competitive position, the unwinding and resolving of various relationships between AIG and SICO and AIG's strategy for growth, product development, market position, financial results and reserves. It is possible that AIG's actual results and financial condition may differ, possibly materially, from the anticipated results and financial condition indicated in these projections and statements. Factors that could cause AIG's actual results to differ, possibly materially, from those in the specific projections and statements are discussed throughout this Management's Discussion and Analysis of Financial Condition and Results of Operations and in Item 1A. Risk Factors of AIG's Annual Report on Form 10-K for the year ended December 31, 2006 (2006 Annual Report on Form 10-K). AIG is not under any obligation (and expressly disclaims any such obligations) to update or alter any projection or other statement, whether written or oral, that may be made from time to time, whether as a result of new information, future events or otherwise.

In addition to reviewing AIG's results for the first nine months of 2007, this Management's Discussion and Analysis of Financial Condition and Results of Operations supplements and updates the information and discussion included in the 2006 Annual Report on Form 10-K. Throughout this Management's Discussion and Analysis of Financial Condition and Results of Operations, AIG presents its operations in the way it believes will be most meaningful. Statutory loss ratios and combined ratios are presented in accordance with accounting principles prescribed by insurance regulatory authorities because these are standard measures of performance filed with insurance regulatory authorities and used for analysis in the insurance industry and thus allow more meaningful comparisons with AIG's insurance competitors. AIG has also incorporated into this discussion cross-references to additional information included in this Quarterly Report on Form 10-Q and in the 2006 Annual Report on Form 10-K to assist readers seeking related information on a particular subject.

Overview of Operations and Business Results

AIG identifies its reportable segments by product or service line, consistent with its management structure. AIG's segments are General Insurance, Life Insurance & Retirement Services, Financial Services and Asset Management. AIG's operations in 2007 and 2006 were conducted by its subsidiaries through these segments. Through these segments, AIG provides insurance, financial and investment products and services to both businesses and individuals in more than 130 countries and jurisdictions. This geographic, product and service diversification is one of AIG's major strengths and sets it apart from its competitors. AIG's Other category consists of items not allocated to AIG's operating segments.

AIG's subsidiaries serve commercial, institutional and individual customers through an extensive property-casualty and life insurance and retirement services network. In the United States, AIG companies are the largest underwriters of commercial and industrial insurance and are among the largest life insurance and retirement services operations as well. AIG's Financial Services businesses include commercial aircraft and equipment leasing, capital markets operations and consumer finance, both in the United States and abroad. AIG also provides asset management services to institutions and individuals. As part of its spread-based business activities, AIG issues various debt instruments in the public and private markets.

Outlook

The following paragraphs supplement and update the information and discussion included in Management's Discussion and Analysis of Financial Condition and Results of Operations – Outlook, in the 2006 Annual Report on Form 10-K to reflect developments in or affecting AIG's business during 2007.

The commercial property and casualty insurance industry has historically experienced cycles of price erosion followed by rate strengthening as a result of catastrophes or other significant losses that affect the overall capacity of the industry to provide coverage. Despite industry price erosion in commercial lines, AIG expects to continue to identify profitable opportunities and build attractive new general insurance businesses as a result of AIG's broad product line and extensive distribution networks in the U.S. and abroad. In October 2007, for example, AIG expanded its Foreign General insurance operations in Germany through the acquisition of Württembergische and Badische Versicherungs-Aktiengesellschaft.

Workers compensation remains under considerable pricing pressure, as statutory rates continue to decline. Rates for aviation, excess casualty, D&O and certain other lines of insurance also continue to decline due to competitive pressures. AIG also expects further price erosion for its foreign commercial lines during 2008. There can be no assurance that price erosion will not become more widespread or that AIG's profitability will not deteriorate from current levels in major commercial lines; however, AIG seeks to mitigate this risk by constantly seeking out profitable opportunities across its diverse product lines and distribution networks.

AIG has commenced a realignment of its Foreign General insurance operations, many of which were historically conducted through branches of U.S. companies. On December 1, 2007, Landmark Insurance Company Limited, a U.K. subsidiary, will assume all of the insurance liabilities of the U.K. branch of New Hampshire Insurance Company and will change its name to AIG U.K. Ltd.

In AIG's Foreign Retirement Services business, the continued weak yen has resulted in higher than normal surrenders and that trend, if prolonged, could further accelerate the amortization of deferred acquisition costs (DAC). Similarly, in the Domestic Retirement Services business, the competitive environment and the age of the in-force blocks of individual fixed annuities could result in ongoing heightened surrender activity.

In Japan, the National Tax Authority in cooperation with the Life Insurance Association of Japan is reviewing the tax treatment for increasing term life insurance, which may affect the amount of premiums that qualify as tax deductions for business owners. As a result of this review, AIG's life insurance companies in Japan suspended the sale of increasing term life insurance from early April 2007. This action had an adverse effect on life insurance sales in the third quarter of 2007 and AIG expects that trend to continue for the remainder of the year. AIG companies in Japan have taken several measures aimed at increasing sales of other

products in the Japanese market, in particular sales of U.S. dollar life insurance products.

In Japan, full deregulation of banks with respect to insurance product sales will become effective in December 2007. AIG expects that it will be able to leverage its existing bank relationships and innovative product expertise to expand sales of both life and accident and health products beginning in 2008.

During the third quarter of 2007, the Internal Revenue Service proposed to change the treatment of the dividends-received deduction on separate account assets held in connection with variable annuity contracts. This proposal was withdrawn later in the quarter for additional study. Should this change be adopted, AIG does not expect it would have a material effect on AIG's consolidated financial position or results of operations for any period.

In March 2007, the U.S. Treasury Department published proposed new regulations that, if adopted in their current form, would limit the ability of U.S. taxpayers to claim foreign tax credits in certain circumstances under the Internal Revenue Code. Should the proposed regulations be adopted in their current form, they would limit AIG's ability to claim foreign tax credits in connection with certain structured transactions entered into by AIG Financial Products Corp. and AIG Trading Group Inc. and their respective subsidiaries (collectively, AIGFP), resulting in a material adverse effect on AIGFP's operating results.

The ongoing disruption in the structured finance markets and the recent downgrades by rating agencies continue to adversely affect AIG's estimates of the fair value of the super senior credit derivatives written by AIGFP. Although it remains difficult to estimate the fair value of these derivatives due to continuing limitations on the availability of market observable data, AIG's best estimate of the further decline in the fair value of AIGFP's super senior credit derivatives since September 30, 2007 is approximately $550 million as of October 31, 2007. The fair value of these derivatives is expected to fluctuate, perhaps materially, in response to changing market conditions, and AIG's estimates of the value of AIGFP's super senior credit derivative portfolio at future dates could therefore be materially different from current estimates. AIG continues to believe that it is highly unlikely that AIGFP will be required to make payments with respect to these derivatives.

The U.S. residential mortgage market is experiencing serious disruption due to credit quality deterioration in a significant portion of loans originated, particularly to non-prime and subprime borrowers, evolving changes in the regulatory environment, a slower residential housing market, increased cost of borrowings for mortgage participants and illiquid credit markets. AIG participates in the U.S. residential mortgage market in several ways: American General Finance, Inc. (AGF) originates principally first-lien mortgage loans and to a lesser extent second-lien mortgage loans to buyers and owners of residential housing; United Guaranty Corporation (UGC) provides first loss mortgage guaranty insurance for high loan-to-value first and second-lien residential mortgages; AIG insurance and financial services subsidiaries invest in mortgage-backed securities and collateralized debt obligations (CDOs) in which the underlying collateral is composed in whole or in part of residential mortgage loans; and AIGFP provides credit protection through credit default swaps on certain super senior tranches of CDOs that have AAA underlying or subordinate layers. The operating results of AIG's consumer finance and mortgage guaranty operations in the United States have been and are likely to continue to be adversely affected by the factors referred to above. The downward cycle in the U.S. housing market is not expected to improve until residential inventories return to a more normal level and the mortgage credit market stabilizes. AIG expects that this downward cycle will continue to adversely affect UGC's operating results for the foreseeable future and will result in a significant operating loss for UGC in 2008. The effect of the downward cycle in the U.S. housing market on AIG's other operations, investment portfolio and overall consolidated financial position could be material if the market disruption continues and expands beyond the U.S. residential mortgage markets, although AIG seeks to mitigate the risks to its business by disciplined underwriting and active risk management.

In recent quarters, AIG's returns from partnerships and other alternative investments were particularly strong, driven by favorable equity market performance and credit conditions. These returns may vary from period to period and declined significantly in the most recent quarter. AIG believes that the particularly strong performance in certain prior periods is not indicative of the returns to be expected from this asset class in future periods.

As part of an ongoing project to increase the standardization of AIG actuarial systems and processes throughout the world, adjustments reflecting certain changes in actuarial estimates for future policy benefits and DAC have been recognized in the Life Insurance & Retirement Services segment results during 2006 and 2007. AIG expects further adjustments over time as these new systems and processes are implemented.

AIG has recorded out of period quarterly adjustments in the last two years due to the remediation of control deficiencies. As AIG continues its remediation activities, AIG expects to record additional out of period adjustments.

Consolidated Results

The following table summarizes AIG's consolidated revenues, income before income taxes, minority interest and cumulative effect of an accounting change and net income:

(in millions)	Three Months Ended September 30, **2007**	2006	Percentage Increase/ (Decrease)	Nine Months Ended September 30, **2007**	2006	Percentage Increase/ (Decrease)
Total revenues	**$29,836**	$29,247	2%	**$91,631**	$83,379	10%
Income before income taxes, minority interest and cumulative effect of an accounting change	**4,879**	6,301	(23)	**17,379**	16,335	6
Net income	**$ 3,085**	$ 4,224	(27)%	**$11,492**	$10,609	8%

AIG's consolidated revenues increased slightly for the three months ended September 30, 2007 compared to the same period in 2006. AIG's consolidated income before income taxes, minority interest and cumulative effect of an accounting change decreased for the three-month period ended September 30, 2007 compared to the same period in 2006 primarily due to higher Net realized capital losses and the operating loss in the Mortgage Guaranty business. Net realized capital losses included other-than-temporary declines of $529 million and foreign currency related losses of $361 million.

AIG's consolidated revenues increased for the nine-month period ended September 30, 2007 compared to the same period in 2006 as revenues increased in each of the operating segments. Operating income increased in all segments with the exception of Life Insurance & Retirement Services, which declined due to an increase in Net realized capital losses compared to the same period in 2006.

Operating income for the three and nine-month periods ended September 30, 2007 was significantly affected by the change in accounting treatment for hedging activities. In the first nine months of 2007, AIGFP applied hedge accounting to certain of its interest rate swaps and foreign currency forward contracts hedging its investments and borrowings. As a result, AIGFP recognized in earnings the change in the fair value on the hedged items attributable to the hedged risks, offsetting the gains and losses on the derivatives designated as hedges. In 2006, AIGFP did not apply hedge accounting under FAS 133 to any of its assets and liabilities.

During the three months ended September 30, 2007, AIG recorded certain out of period adjustments. These adjustments collectively decreased pre-tax operating income in that quarter by $33 million and net income by $35 million. The adjustments were primarily comprised of a net charge of $49 million ($32 million after tax) in Capital Markets, a $14 million increase in income tax expense related to the remediation of the material weakness in controls over income tax accounting and an increase to operating income of $16 million ($11 million after tax) primarily related to other remediation activities.

For the nine months ended September 30, 2007, out of period adjustments collectively decreased pre-tax operating income by $536 million ($408 million after tax). The adjustments were comprised of a charge of $380 million ($247 million after tax) to reverse net gains on transfers of investment securities among legal entities consolidated within AIGFP and a corresponding increase to Accumulated other comprehensive income; $58 million of additional income tax expense related to the aforementioned remediation activities; $71 million ($46 million after tax) of net realized capital gains related to foreign exchange; and $227 million ($149 million after tax) of additional expense, primarily relating to other remediation activities.

During the three months ended September 30, 2006, out of period adjustments collectively increased pre-tax operating income by $293 million and net income by $73 million. The adjustments were comprised of an increase in income primarily related to the remediation of the material weakness in accounting for certain derivative transactions under FAS 133 totalling $151 million ($23 million after tax); increases in bad debt expense of $225 million ($146 million after tax) and earned premiums of $99 million ($65 million after tax), both of which relate to balance sheet reconciliations; an increase in partnership income of $121 million ($79 million after tax), which relates to improved valuation information; a further increase in income from certain investments in unit investment trusts (UCITS) of $116 million ($75 million after tax), as described below; other favorable remediation adjustments of $31 million ($16 million after tax) and an increase in income tax expense of $39 million relating to AIG's ongoing remediation of internal controls over income tax accounting. See also the discussion of AIG's reportable segments in Management's Discussion & Analysis of Financial Condition and Results of Operations.

For the nine months ended September 30, 2006, out of period adjustments collectively increased pre-tax operating income by $173 million and reduced net income by $135 million. The adjustments were comprised of $642 million ($417 million after tax) of additional investment income related to the accounting for UCITS; $194 million ($127 million after tax) of charges primarily related to the remediation of the material weakness in accounting for certain derivative transactions under FAS 133; $239 million of additional income tax expense related to the aforementioned remediation activities; $85 million ($55 million after tax) of interest income related to interest earned on deposit contracts; $61 million (before and after tax) of expenses related to the Starr International Company,

Inc. (SICO) Deferred Compensation Profit Participation Plans (SICO Plans); $59 million ($38 million after tax) of expenses related to deferred advertising costs; and $240 million ($142 million after tax) of additional expense, primarily related to other remediation activities.

Results for the first nine months of 2006 were also negatively affected by a one-time charge relating to the C.V. Starr & Co., Inc. (Starr) tender offer ($54 million before and after tax) and an additional allowance for losses in AIG Credit Card Company (Taiwan) ($88 million before and after tax), both of which were recorded in first quarter of 2006.

AIG's effective income tax rates for the year ended December 31, 2006 and the three-month period ended September 30, 2007 were 30.1 percent and 30.0 percent, respectively. For the nine-month period ended September 30, 2007, the effective income tax rate declined to 28.0 percent, primarily due to recognition of tax benefits associated with the SICO Plans for which the compensation expense had been recognized in prior years. Such tax benefits amounted to $194 million for the nine-month period ended September 30, 2007.

Segment Results

The following table summarizes AIG's operations by major operating segment. (See also Note 2 of Notes to Consolidated Financial Statements.)

(in millions)	Three Months Ended September 30, **2007**	2006	Percentage Increase/ (Decrease)	Nine Months Ended September 30, **2007**	2006	Percentage Increase/ (Decrease)
Revenues[(a)]:						
General Insurance[(b)]	**$12,758**	$12,615	1%	**$38,589**	$36,438	6%
Life Insurance & Retirement Services[(b)]	**12,632**	12,542	1	**40,337**	37,303	8
Financial Services[(c)(d)]	**2,785**	3,011	(8)	**7,109**	5,923	20
Asset Management	**1,824**	993	84	**5,721**	3,647	57
Other	**13**	215	(94)	**407**	443	(8)
Consolidation and eliminations	**(176)**	(129)	36	**(532)**	(375)	42
Consolidated	**$29,836**	$29,247	2%	**$91,631**	$83,379	10%
Operating income (loss)[(a)]:						
General Insurance[(b)]	**$ 2,439**	$ 2,625	(7)%	**$ 8,511**	$ 7,819	9%
Life Insurance & Retirement Services[(b)]	**1,999**	2,472	(19)	**6,900**	7,483	(8)
Financial Services[(c)(d)]	**669**	1,179	(43)	**1,008**	541	86
Asset Management	**419**	211	99	**2,541**	1,445	76
Other	**(627)**	(186)	237	**(1,557)**	(953)	63
Consolidation and eliminations	**(20)**	–	–	**(24)**	–	–
Consolidated	**$ 4,879**	$ 6,301	(23)%	**$17,379**	$16,335	6%

(a) *Includes gains (losses) from hedging activities that did not qualify for hedge accounting treatment under FAS 133, "Accounting for Derivative Instruments and Hedging Activities" (FAS 133), including the related foreign exchange gains and losses. For the three-month periods ended September 30, 2007 and 2006, respectively, the effect was $(178) million and $165 million in both revenues and operating income. For the nine-month periods ended September 30, 2007 and 2006, respectively, the effect was $(1.06) billion and $(1.13) billion in both revenues and operating income. These amounts result primarily from interest rate and foreign currency derivatives that are hedging investments and borrowings. These gains (losses) for the three and nine months ended September 30, 2007 include out of period charges of $20 million and $346 million, respectively, including a $380 million charge in the nine months ended September 30, 2007 to reverse net gains recognized on transfers of available for sale securities among legal entities consolidated within AIGFP. The three and nine-month periods ended September 30, 2006 include an out of period gain of $115 million and a charge of $223 million related to the remediation of the material weakness in accounting for certain derivative transactions under FAS 133.*

(b) *Includes the effect of out of period UCITS adjustments. For the three and nine-month periods ended September 30, 2006, the effect was an increase of $92 million and $472 million, respectively, in both revenues and operating income for General Insurance and an increase of $24 million and $240 million, respectively, in revenues and $24 million and $169 million, respectively, in operating income for Life Insurance & Retirement Services.*

(c) *Includes gains (losses) from hedging activities that did not qualify for hedge accounting treatment under FAS 133, including the related foreign exchange gains and losses. For the three-month periods ended September 30, 2007 and 2006, respectively, the effect was $353 million, and $581 million in both revenues and operating income. For the nine-month periods ended September 30, 2007 and 2006, respectively, the effect was $(250) million and $(1.2) billion in both revenues and operating income. These amounts result primarily from interest rate and foreign currency derivatives that are effective economic hedges of investments and borrowings. The three and nine-month periods ended September 30, 2007 include out of period charges of $20 million and $346 million, respectively, as discussed above. The three and nine-month periods ended September 30, 2006 include an out of period gain of $115 million and a charge of $223 million as discussed above. In the first quarter of 2007, AIG began applying hedge accounting for certain transactions, primarily in its Capital Markets operations. In the second quarter of 2007, AGF and ILFC began applying hedge accounting to most of their derivatives hedging interest rate and foreign exchange risks associated with their floating rate and foreign currency denominated borrowings.*

(d) *For the three and nine-month periods ended September 30, 2007, both revenues and operating income include an unrealized market valuation loss of $352 million on AIGFP's super senior credit default swap portfolio.*

General Insurance

AIG's General Insurance operations provide property and casualty products and services throughout the world. Foreign operations provided approximately 25 percent and 27 percent of General Insurance operating income for the three months ended September 30, 2007 and 2006, respectively, and approximately 28 percent and 31 percent for the nine months ended September 30, 2007 and 2006, respectively. The decrease in General Insurance operating income in the three-month period ended September 30, 2007 compared to the same period in 2006 was primarily attributable to operating losses from the Mortgage Guaranty business and a decline in operating income in the Foreign

General and Personal Lines businesses, partially offset by improved underwriting results for the Domestic Brokerage Group (DBG) and higher net investment income.

Operating income grew in the nine-month period ended September 30, 2007 compared to the same period of 2006, driven by strength in DBG, partially offset by operating losses from the Mortgage Guaranty business.

Life Insurance & Retirement Services

AIG's Life Insurance & Retirement Services operations provide insurance, financial and investment products throughout the world. Foreign operations provided approximately 87 percent and 65 percent of Life Insurance & Retirement Services operating income for the three months ended September 30, 2007 and 2006, respectively, and approximately 68 percent and 67 percent for the nine months ended September 30, 2007 and 2006, respectively. Operating income for the three months ended September 30, 2007 declined compared to the same period in 2006, primarily due to the securities market volatility which resulted in lower investment income and higher net realized capital losses compared to the same period in 2006. For the nine months ended September 30, 2007, operating income declined 8 percent compared to the same period in 2006 due to charges related to balance sheet reconciliation remediation, an industry-wide claims review in Japan, the effect of SOP 05-1, trading account losses and realized capital losses.

Financial Services

AIG's Financial Services subsidiaries engage in diversified activities including aircraft and equipment leasing, capital markets, consumer finance and insurance premium finance.

Financial Services operating income decreased in the three-month period and increased in the nine-month period ended September 30, 2007 compared to the same periods in 2006 due, in large part, to differences in the accounting treatment for hedging activities. In the first quarter of 2007, AIGFP began applying hedge accounting to certain of its interest rate swaps and foreign currency forward contracts that hedge its investments and borrowings. In the second quarter of 2007, AGF and International Lease Finance Corporation (ILFC) began applying hedge accounting to most of their derivatives that hedge interest rate and foreign currency denominated borrowings. Prior to 2007, hedge accounting under FAS 133 was not being applied to any of AIG's derivatives and related assets and liabilities. Accordingly, revenues and operating income were exposed to volatility resulting from differences in the timing of revenue recognition between the derivatives and the hedged assets and liabilities. During the three and nine-month periods ended September 30, 2007 operating income was also adversely affected by an unrealized market valuation loss of $352 million on AIGFP's super senior credit default swap portfolio.

ILFC generated strong operating income growth for the three and nine-month periods ended September 30, 2007 compared to the same periods in 2006, driven to a large extent by a larger aircraft fleet, higher lease rates and higher utilization.

AGF's operating income decreased in the three and nine months ended September 30, 2007, in large part due to the reduced residential mortgage origination volumes and lower revenues from its mortgage banking activities. Further, in the first nine months of 2007, AGF's mortgage banking operations recorded pre-tax charges of $178 million, representing the estimated cost of implementing the Supervisory Agreement entered into with the Office of Thrift Supervision (OTS), which are discussed in the Consumer Finance results of operations section.

Asset Management

AIG's Asset Management operations include institutional and retail asset management, broker-dealer services and institutional spread-based investment businesses. The Matched Investment Program (MIP) has replaced the GIC program as AIG's principal institutional spread-based investment activity.

Asset Management operating income increased for the three and nine-month periods ended September 30, 2007 compared to the same periods in 2006, primarily due to higher income from consolidated managed partnerships and funds that is entirely offset in Minority interest expense, which is not a component of operating income. Realized capital losses, principally relating to economically effective hedges not qualifying for hedge accounting, also increased for the three months ended September 30, 2007 compared to the same period in 2006. Asset Management operating income also increased for the nine-month period ended September 30, 2007 compared to the same period in 2006 due to increased investment income from consolidated managed partnerships and funds, and a realized capital gain of $398 million on the sale of a portion of AIG's investment in Blackstone Group, LP in connection with its initial public offering, as well as growth in both the Spread-Based Investment business and the Institutional Asset Management business.

Capital Resources

In the first nine months of 2007, AIG issued an aggregate of $4.49 billion of junior subordinated debentures in four series of securities. Substantially all of the proceeds from these sales, net of expenses, are being used to repurchase shares of AIG's common stock.

At September 30, 2007, AIG had total consolidated shareholders' equity of $104.1 billion and total consolidated borrowings of $176.2 billion, of which $20.3 billion represented AIG's net borrowings. At that date, $155.9 billion of total borrowings represented obligations of

AIG's subsidiaries not guaranteed by AIG, matched borrowings by AIG parent or AIGFP, obligations of guaranteed investment agreements, junior subordinated debt, liabilities connected to trust preferred stock and hybrid financial instrument liabilities.

In February 2007, AIG's Board of Directors increased AIG's share repurchase program by authorizing the repurchase of shares with an aggregate purchase price of $8 billion. Share repurchases during 2007 are described under Capital Resources and Liquidity – Share Repurchases and in Item 2. of Part II of this Quarterly Report on Form 10-Q.

Liquidity

AIG manages liquidity at both the subsidiary and parent company levels. At September 30, 2007, AIG's consolidated invested assets, primarily held by its subsidiaries, included $41.2 billion in cash and short-term investments. The increase in cash and short-term investments during the quarter was primarily the result of the steps AIG took to enhance the liquidity of its portfolios in light of the market disruption during the quarter. Consolidated net cash provided from operating activities in the first nine months of 2007 amounted to $27.1 billion. Management believes that AIG's liquid assets, cash provided by operations and access to the capital markets will enable it to meet its anticipated cash requirements, including the funding of increased dividends under AIG's new dividend policy and repurchases of common stock.

Critical Accounting Estimates

AIG considers its most critical accounting estimates to be those relating to reserves for losses and loss expenses, future policy benefits for life and accident and health contracts, recoverability of DAC, estimated gross profits for investment-oriented products, fair value determinations for certain Capital Markets assets and liabilities, other-than-temporary declines in the value of investments and flight equipment recoverability. These accounting estimates require the use of assumptions about matters, some of which are highly uncertain at the time of estimation. To the extent actual experience differs from the assumptions used, AIG's results of operations would be directly affected.

Throughout this Management's Discussion and Analysis of Financial Condition and Results of Operations, AIG's critical accounting estimates are discussed in detail. The major categories for which assumptions are developed and used to establish each critical accounting estimate are highlighted below.

Reserves for Losses and Loss Expenses (General Insurance):

- *Loss trend factors:* used to establish expected loss ratios for subsequent accident years based on premium rate adequacy and the projected loss ratio with respect to prior accident years.
- *Expected loss ratios for the latest accident year:* in this case, accident year 2007 for the loss reserve analyses updated through September 30, 2007. For low-frequency, high-severity classes such as excess casualty, expected loss ratios generally are utilized for at least the three most recent accident years.
- *Loss development factors:* used to project the reported losses for each accident year to an ultimate amount.
- *Reinsurance recoverable on unpaid losses:* the expected recoveries from reinsurers on losses that have not yet been reported and/or settled.

Future Policy Benefits for Life and Accident and Health Contracts (Life Insurance & Retirement Services):

- *Interest rates:* which vary by geographical region, year of issuance and products.
- *Mortality, morbidity and surrender rates:* based upon actual experience by geographical region modified to allow for variation in policy form, risk classification and distribution channel.

Estimated Gross Profits (Life Insurance & Retirement Services):

- *Estimated gross profits:* to be realized over the estimated duration of the contracts (investment-oriented products) affect the carrying value of DAC, unearned revenue liability and associated amortization patterns under FAS 97 and Sales Inducement Assets under SOP 03-1. Estimated gross profits include investment income and gains and losses on investments less required interest, actual mortality and other expenses.

Deferred Policy Acquisition Costs (Life Insurance & Retirement Services):

- *Recoverability:* based on current and future expected profitability, which is affected by interest rates, foreign exchange rates, mortality experience, and policy persistency.

Deferred Policy Acquisition Costs (General Insurance):

- *Recoverability and eligibility:* based upon the current terms and profitability of the underlying insurance contracts.

Fair Value Determinations Of Certain Assets And Liabilities:

- *Market price data:* AIG attempts to secure reliable and independent current market price data, such as published exchange rates from external subscription services such as IDC, Bloomberg or Reuters or third-party broker/dealer quotes for use in its models. When such data is not available, AIG uses an internal methodology, which includes interpolation and extrapolation from verifiable recent prices.

- *Valuation models:* utilizing factors, such as market prices, liquidity, commodity prices, credit spreads, and current interest, foreign exchange and volatility rates.

Other-Than-Temporary Declines In The Value Of Investments:
A security is considered a candidate for other-than-temporary impairment if it meets any of the following criteria:

- Trading at a significant (25 percent or more) discount to par or amortized cost (if lower) for an extended period of time (nine months or longer);
- The occurrence of a discrete credit event resulting in the debtor defaulting or seeking bankruptcy or insolvency protection or voluntary reorganization; or
- The probability of non-realization of a full recovery on its investment, irrespective of the occurrence of one of the foregoing events.

At each balance sheet date, AIG evaluates its securities holdings in an unrealized loss position. Where AIG does not intend to hold such securities until they have fully recovered their carrying value, based on the circumstances present at the date of evaluation, AIG records the unrealized loss in income. If events or circumstances change, such as unexpected changes in the creditworthiness of the obligor, unanticipated changes in interest rates, tax laws, statutory capital positions and unforeseen liquidity events, among others, AIG revisits its intent. Further, if a loss is recognized from a sale subsequent to a balance sheet date pursuant to these unexpected changes in circumstances, the loss is recognized in the period in which the intent to hold the securities to recovery no longer exists.

In periods subsequent to the recognition of an other-than-temporary impairment loss for debt securities, AIG amortizes the discount or reduced premium over the remaining life of the security in a prospective manner based on the amount and timing of estimated future cash flows.

Flight Equipment – Recoverability (Financial Services):

- *Expected undiscounted future net cash flows:* based upon current lease rates, projected future lease rates and estimated terminal values of each aircraft based on third party information.

Allowance for Finance Receivable Losses (Financial Services):

- *Historical defaults and delinquency experience:* utilizing factors, such as delinquency ratio, allowance ratio, charge-off ratio, and charge-off coverage.
- *Portfolio characteristics:* portfolio composition and consideration of the recent changes to underwriting criteria and portfolio seasoning.
- *External factors:* consideration of current economic conditions, including levels of unemployment and personal bankruptcies.
- *Migration analysis:* empirical technique measuring historical movement of like finance receivables through various levels of repayment, delinquency, and loss categories to existing finance receivable pools.

Operating Review

General Insurance Operations

AIG's General Insurance subsidiaries are multiple line companies writing substantially all lines of property and casualty insurance and various personal lines both domestically and abroad.

Domestic General Insurance operations are comprised of DBG, Reinsurance, Personal Lines and Mortgage Guaranty businesses.

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

Transatlantic Holdings, Inc. (Transatlantic) subsidiaries offer reinsurance capacity on both a treaty and facultative basis both in the U.S. and abroad. Transatlantic structures programs for a full range of property and casualty products with an emphasis on specialty risk.

AIG's Personal Lines operations provide automobile insurance through aigdirect.com, the newly formed operation resulting from the merger of AIG Direct and 21st Century, and the Agency Auto Division, as well as a broad range of coverages for high net worth individuals through the AIG Private Client Group.

The main business of the UGC subsidiaries is the issuance of residential mortgage guaranty insurance that covers the first loss for credit defaults on high loan-to-value conventional first-lien mortgages for the purchase or refinance of one to four family residences. UGC subsidiaries also write second-lien and private student loan guaranty insurance.

AIG's Foreign General Insurance group accepts risks primarily underwritten through American International Underwriters (AIU), a marketing unit consisting of wholly owned agencies and insurance companies. The Foreign General Insurance group also includes business written by AIG's foreign-based insurance subsidiaries.

General Insurance Results

General Insurance operating income is comprised of statutory underwriting results, changes in DAC, net investment income and net realized capital gains and losses.

Operating income, as well as net premiums written, net premiums earned, net investment income and net realized capital gains (losses) and statutory ratios were as follows:

(in millions, except ratios)	Three Months Ended September 30, **2007**	2006	Percentage Increase/ (Decrease)	Nine Months Ended September 30, **2007**	2006	Percentage Increase/ (Decrease)
Net premiums written:						
Domestic General						
DBG	**$ 6,012**	$ 6,071	(1)%	**$18,460**	$18,407	–%
Transatlantic	**985**	895	10	**2,952**	2,723	8
Personal Lines	**1,253**	1,162	8	**3,685**	3,540	4
Mortgage Guaranty	**303**	232	31	**841**	622	35
Foreign General	**3,270**	2,864	14	**10,130**	8,821	15
Total	**$11,823**	$11,224	5%	**$36,068**	$34,113	6%
Net premiums earned:						
Domestic General						
DBG	**$ 5,942**	$ 6,276	(5)%	**$17,919**	$17,863	–%
Transatlantic	**960**	895	7	**2,873**	2,712	6
Personal Lines	**1,193**	1,158	3	**3,516**	3,484	1
Mortgage Guaranty	**226**	191	18	**657**	536	23
Foreign General	**3,112**	2,697	15	**9,050**	7,770	16
Total	**$11,433**	$11,217	2%	**$34,015**	$32,365	5%
Net investment income:						
Domestic General						
DBG	**$ 854**	$ 880	(3)%	**$ 2,871**	$ 2,438	18%
Transatlantic	**113**	107	6	**348**	317	10
Personal Lines	**59**	56	5	**173**	168	3
Mortgage Guaranty	**42**	35	20	**118**	103	15
Foreign General[(a)]	**325**	291	12	**1,071**	1,075	–
Reclassifications and Eliminations	**1**	1	–	**4**	1	–
Total	**$ 1,394**	$ 1,370	2%	**$ 4,585**	$ 4,102	12%
Net realized capital gains (losses)	**$ (69)**	$ 28	–%	**$ (11)**	$ (29)	(62)%
Operating Income (loss):						
Domestic General						
DBG	**$ 1,829**	$ 1,543	19%	**$ 5,662**	$ 4,322	31%
Transatlantic	**189**	143	32	**508**	427	19
Personal Lines	**28**	133	(79)	**252**	352	(28)
Mortgage Guaranty	**(216)**	85	–	**(289)**	301	–
Foreign General[(a)]	**607**	721	(16)	**2,383**	2,415	(1)
Reclassifications and Eliminations	**2**	–	–	**(5)**	2	–
Total	**$ 2,439**	$ 2,625	(7)%	**$ 8,511**	$ 7,819	9%
Statutory underwriting profit (loss)[(b)]:						
Domestic General						
DBG	**$ 1,014**	$ 666	52%	**$ 2,744**	$ 1,791	53%
Transatlantic	**53**	34	56	**106**	97	9
Personal Lines	**(40)**	83	–	**49**	176	(72)
Mortgage Guaranty	**(270)**	48	–	**(438)**	191	–
Foreign General	**266**	391	(32)	**1,039**	1,147	(9)
Total	**$ 1,023**	$ 1,222	(16)%	**$ 3,500**	$ 3,402	3%
Domestic General:						
Loss Ratio	**69.2**	67.0		**68.8**	69.0	
Expense Ratio	**21.1**	23.7		**20.5**	21.2	
Combined Ratio	**90.3**	90.7		**89.3**	90.2	
Foreign General:						
Loss Ratio	**52.4**	48.4		**51.7**	48.7	
Expense Ratio	**37.1**	35.0		**32.9**	32.2	
Combined ratio	**89.5**	83.4		**84.6**	80.9	
Consolidated:						
Loss Ratio	**64.7**	62.6		**64.3**	64.1	
Expense Ratio	**25.5**	26.5		**24.0**	24.1	
Combined Ratio	**90.2**	89.1		**88.3**	88.2	

(a) The three and nine-month periods ended September 30, 2006 include increases of $22 million and $406 million, respectively, relating to an out of period UCITS adjustment.

(b) Statutory underwriting profit (loss) is a measure that U.S. domiciled insurance companies are required to report to their regulatory authorities. The following table reconciles statutory underwriting profit (loss) to operating income for General Insurance:

(in millions)	Domestic Brokerage Group	Transatlantic	Personal Lines	Mortgage Guaranty	Foreign General	Reclassifications and Eliminations	Total
Three Months Ended September 30, 2007:							
Statutory underwriting profit (loss)	**$1,014**	**$ 53**	**$ (40)**	**$(270)**	**266**	**$ –**	**$1,023**
Increase (decrease) in DAC	**21**	**8**	**9**	**13**	**40**	**–**	**91**
Net investment income	**854**	**113**	**59**	**42**	**325**	**1**	**1,394**
Net realized capital gains (losses)	**(60)**	**15**	**–**	**(1)**	**(24)**	**1**	**(69)**
Operating income (loss)	**$1,829**	**$189**	**$ 28**	**$(216)**	**607**	**$ 2**	**$2,439**
Three Months Ended September 30, 2006:							
Statutory underwriting profit (loss)	$ 666	$ 34	$ 83	$ 48	$ 391	$ –	$1,222
Increase (decrease) in DAC	(29)	–	(6)	2	38	–	5
Net investment income	880	107	56	35	291	1	1,370
Net realized capital gains (losses)	26	2	–	–	1	(1)	28
Operating income (loss)	$1,543	$143	$133	$ 85	$ 721	$ –	$2,625
Nine Months Ended September 30, 2007:							
Statutory underwriting profit (loss)	**$2,744**	**$106**	**$ 49**	**$(438)**	**1,039**	**$ –**	**$3,500**
Increase (decrease) in DAC	**106**	**22**	**31**	**34**	**244**	**–**	**437**
Net investment income	**2,871**	**348**	**173**	**118**	**1,071**	**4**	**4,585**
Net realized capital gains (losses)	**(59)**	**32**	**(1)**	**(3)**	**29**	**(9)**	**(11)**
Operating income (loss)	**$5,662**	**$508**	**$252**	**$(289)**	**2,383**	**$(5)**	**$8,511**
Nine Months Ended September 30, 2006:							
Statutory underwriting profit (loss)	$1,791	$ 97	$176	$ 191	$1,147	$ –	$3,402
Increase (decrease) in DAC	64	7	8	10	255	–	344
Net investment income	2,438	317	168	103	1,075	1	4,102
Net realized capital gains (losses)	29	6	–	(3)	(62)	1	(29)
Operating income (loss)	$4,322	$427	$352	$ 301	$2,415	$ 2	$7,819

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

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2007	2006	**2007**	2006
Growth in original currency*	**4.3%**	8.5%	**4.6%**	8.1%
Foreign exchange effect	**1.0**	0.3	**1.1**	(0.6)
Growth as reported in U.S. dollars	**5.3%**	8.8%	**5.7%**	7.5%

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

Quarterly General Insurance Results

General Insurance operating income decreased in the three months ended September 30, 2007 compared to the same period in 2006. The 2007 combined ratio increased to 90.2, an increase of 1.1 points over 2006, including an increase in the loss ratio of 2.1 points. The loss ratio for accident year 2007 recorded in the three months ended September 30, 2007 was 4.5 points higher than the loss ratio recorded in the three months ended September 30, 2006 for accident year 2006. Increases in Mortgage Guaranty losses accounted for 3.1 points of the higher accident year loss ratio. The downward cycle in the U.S. housing market is not expected to improve until residential inventories return to a more normal level, and AIG expects that this downward cycle will continue to adversely affect UGC's loss ratios for the foreseeable future.

The higher accident year loss ratio was partially offset by favorable development on prior years and increases in the loss reserve discount, reducing losses by $377 million and $41 million for three months ended September 30, 2007 and 2006, respectively. The three months ended September 30, 2006, included an increase to Other expenses of $225 million in connection with balance sheet reconciliation remediation activities which accounted for 2.0 points of the decrease in the expense ratio in the three months ended September 30, 2007 compared to the same period in 2006. Net premiums written increased for the three months ended September 30, 2007 compared to the same period in 2006, driven by Foreign General growth from both established and new distribution channels and the effect of changes in foreign currency exchange rates.

General Insurance net investment income was essentially unchanged for the three months ended September 30, 2007 compared to the same period in 2006, which included an out of period increase to Net investment income of $213 million related to the accounting for UCITS and additional partnership income arising from improved valuations. Interest and dividend income increased $244 million for the third quarter of 2007 compared to the same period in 2006 as investment in fixed maturities and equity securities increased by $12.0 billion from the investment of operating cash flow and the yield on interest earning investments increased 30 basis points to 4.8 percent. Income from partnership investments increased $10 million for the three months ended September 30, 2007 compared to the same period in 2006, primarily due to improved returns on underlying investments. Other investment income decreased $290 million, primarily due to declining returns on investments in mutual funds and the effect of the $92 million out of period adjustment related to the accounting for UCITS recorded in 2006.

Year-to-Date General Insurance Results

General Insurance operating income increased for the first nine months of 2007 compared to the same period in 2006 due to growth in net investment income and an increase in underwriting profit, driven by an increase in earned premiums as the combined ratio was substantially the same for both periods. The loss ratio for accident year 2007 recorded in the first nine months of 2007 was 1.2 points higher than the loss ratio recorded in the first nine months of 2006 for accident year 2006, primarily due to an increase in Mortgage Guaranty losses in the 2007 period. The higher accident year loss ratio was substantially offset by favorable development on prior years and increases in the loss reserve discount, which combined to reduce losses by $720 million and $255 million in the first nine months of 2007 and 2006, respectively.

General Insurance net premiums written increased in the first nine months of 2007 compared to the same period in 2006, reflecting growth in Foreign General from both established and new distribution channels, the effect of changes in foreign currency exchange rates, and growth in Mortgage Guaranty, primarily from international business.

General Insurance net investment income increased in the first nine months of 2007 to $4.6 billion. Interest and dividend income increased $577 million for the first nine months of 2007 compared to the same period of 2006 as fixed maturities and equity securities increased by $15.3 billion and the yield increased 20 basis points to 4.7 percent. Income from partnership investments increased $312 million for the first nine months of 2007 compared to the same period in 2006, primarily due to improved returns on underlying investments and higher levels of invested assets, which increased by $1.2 billion. Other investment income decreased by $444 million, which reflects the effect of the $472 million out of period UCITS adjustment recorded in 2006. See also Capital Resources and Liquidity and Invested Assets herein.

In order to better align financial reporting with the manner in which AIG's chief operating decision makers have managed their businesses, commencing in the first quarter of 2007, the foreign aviation business, which was historically reported in DBG, is now being reported as part of Foreign General, and the oil rig and marine businesses, which were historically reported in Foreign General, are now being reported as part of DBG. Prior period amounts have been revised to conform to the current presentation.

Quarterly DBG Results

DBG's operating income increased in the three months ended September 30, 2007 compared to the same period of 2006. The improvement is also reflected in the combined ratio, which declined 7.4 points in the three months ended September 30, 2007 compared to the same period of 2006 due to an improvement in the loss ratio of 3.7 points and an improvement in the expense ratio of 3.7 points. Favorable prior year development and increases in the loss reserve discount reduced incurred losses by $353 million and increased incurred losses by $67 million for the three months ended September 30, 2007 and 2006, respectively, accounting for 7.0 points of the improvement. The loss ratio for accident year 2007 recorded in the three months ended September 30, 2007 was 1.6 points higher than the loss ratio recorded in the same period of 2006 for accident year 2006. The expected loss ratios for accident year 2006 were reduced for a number of casualty classes of business in the three-month period ended September 30, 2006, accounting for most of the change in the accident year loss ratio compared to the same period in 2006. Net premiums earned in the three months ended September 30, 2006 included a favorable out of period adjustment of $155 million which reduced the loss ratio by 1.7 points.

DBG's net premiums written declined for the three months ended September 30, 2007 compared to the same period in 2006 due to an increase in ceded premiums and declines in premium rates in casualty lines of business. Ceded premiums as a percentage of gross written premiums increased to 24 percent for the three months ended September 30, 2007 compared to 23 percent in the same period in 2006, primarily due to additional reinsurance for property risks to manage catastrophe exposures.

DBG's expense ratio decreased to 19.2 for the three months ended September 30, 2007 compared to 23.0 in the same period in 2006, primarily due to a decrease in charges related to remediation of the material weakness in balance sheet reconciliations which included a $225 million out of period charge in the third quarter of 2006.

DBG's net investment income decreased for the three months ended September 30, 2007 compared to the same period in 2006, which included out of period increases in partnership and other investment income of $121 million and $70 million, respectively. Interest income increased $139 million for the three months ended September 30, 2007, on growth in the bond portfolio resulting from investment of operating cash flows and capital contributions. Income from partnership investments increased $16 million for the three months ended September 30, 2007 compared to the same period in 2006, primarily due to improved returns on the underlying investments.

Year-to-date DBG Results

DBG's operating income increased for the first nine months of 2007 compared to the same period in 2006 due to growth in both net investment income and underwriting profit. The improvement is also reflected in the combined ratio, which declined 5.2 points in the first nine months of 2007 compared to the same period in 2006, primarily due to an improvement in the loss ratio of 4.2 points. The loss ratio for accident year 2007 recorded for the first nine months of 2007 was 0.5 points lower than the loss ratio recorded in the same period of 2006 for accident year 2006. The loss ratio for accident year 2006 has subsequently improved in each quarter since September 30, 2006. Prior year development and increases in the loss reserve discount reduced incurred losses by $630 million for the nine months ended September 30, 2007 and increased incurred losses by $35 million for the same period in 2006, accounting for 3.7 points of the improvement.

DBG's net premiums written was essentially unchanged in the first nine months of 2007 compared to the same period of 2006. Ceded premiums as a percentage of gross written premiums increased to 25 percent in the first nine months of 2007 compared to 23 percent for the same period in 2006, primarily due to additional reinsurance for property risks to manage catastrophe exposures.

DBG's expense ratio decreased to 18.6 for the first nine months in 2007 compared to 19.7 in the same period of 2006, primarily due to the 2006 charge related to the remediation of the material weakness in internal control over certain balance sheet reconciliations that accounted for 1.6 points of the decline. The decline was partially offset by increases in operating expenses for marketing initiatives and operations as well as changes in the mix of business towards products with lower loss ratios and higher expense ratios.

DBG's net investment income increased for the first nine months of 2007 compared to the same period in 2006, as interest income increased $334 million for the nine months ended September 30, 2007, on growth in the bond portfolio resulting from investment of operating cash flows and capital contributions. Income from partnership investments increased $215 million for the first nine months of 2007 compared to the same period in 2006, primarily due to improved returns on the underlying investments. Other investment income declined $133 million in the first nine months of 2007 compared to the same period in 2006, primarily due to the out of period adjustment of $151 million recorded in the 2006 period.

Quarterly Transatlantic Results

Transatlantic's net premiums written and net premiums earned increased for the three months ended September 30, 2007 compared to the same period in 2006 due primarily to increased writings in domestic and international operations and the strengthening of certain foreign currencies against the U.S. dollar. Statutory underwriting profit increased due to improved underwriting results from domestic operations for the three months ended September 30, 2007 compared to the same period in 2006. Operating income increased for the three months ended September 30, 2007 compared to the same period in 2006 due primarily to increased net investment income, improved underwriting results and increased net realized capital gains.

Year-to-date Transatlantic Results

Transatlantic's net premiums written and net premiums earned increased for the first nine months of 2007 compared to the same period in 2006 due primarily to increased writings in domestic operations. The increase in statutory underwriting profit in the nine months ended September 30, 2007 compared to the same period in 2006 reflects improved underwriting results in Domestic and European operations. Overall, costs from European windstorms and floods and storms in Australia in the nine months ended September 30, 2007 were largely offset by lower estimated net adverse development, related to losses occurring in prior years, compared to the same period of 2006. Operating income increased for the first nine months of 2007 compared to the same period in 2006 due principally to increased net investment income, improved underwriting results and net realized capital gains.

Quarterly Personal Lines Results

Personal Lines operating income for the three months ended September 30, 2007 was $28 million, a decrease of $105 million compared to the same period in 2006, primarily due to a $53 million increase in incurred losses resulting from a change in prior year reserve development, mainly from discontinued businesses, and $28 million of transaction and integration costs related to the acquisition of the minority interest in 21st Century Insurance Group (21st Century), as discussed below. The loss ratio for accident year 2007 recorded for the three months ended September 30, 2007 was 3.21 points higher than the loss ratio for the same period in 2006 primarily due to increasing accident frequency trends in

the direct businesses coupled with a decline in average premium, and increasing loss frequencies in the homeowners line of the Private Client Group segment. Prior year development increased incurred losses by $32 million for the three months ended September 30, 2007 and decreased incurred losses by $21 million for the three months ended September 30, 2006, thereby increasing the 2007 loss ratio by 4.52 points relative to the 2006 loss ratio. The transaction and integration costs related to the 21st Century acquisition increased the expense ratio in the third quarter of 2007 by 2.2 points compared to the same period of 2006.

Net premiums written increased 7.8 percent for the three months ended September 30, 2007 compared to the same period of 2006, which represents the highest growth rate since the third quarter of 2005. This increase resulted from continued growth in the Private Client Group, as well as growth in Agency Auto and the Direct segment.

On September 27, 2007, AIG completed its previously announced acquisition of 21st Century. AIG paid $759 million to acquire the remaining 39.2 percent of the shares of 21st Century that it did not previously own. As a result of the acquisition, the AIG Direct and 21st Century operations will be combined as aigdirect.com. Duplicate positions which exist in both the home office and corporate functions and in the field organization will be eliminated. These positions, as well as the locations scheduled for closing over the next two years, have been identified and will affect about 11 percent of the combined workforce.

Under the purchase method of accounting, the assets and liabilities of 21st Century that were acquired were adjusted to their estimated fair values as of the date of the acquisition, and goodwill of $233 million was recorded. A customer relationship intangible asset, initially valued at $290 million, was also established.

Year-to-date Personal Lines Results

Personal Lines operating income for the nine months of 2007 was $252 million, a decrease of $100 million compared to the same period in 2006, primarily due to $55 million of less favorable reserve development and $31 million of transaction and integration costs related to the 21st Century acquisition. The loss ratio for accident year 2007 recorded for the first nine months of 2007 increased by 0.36 points compared to the same period in 2006 for accident year 2006. Favorable prior year development reduced incurred losses by $29 million and $84 million for the nine months ended September 30, 2007 and 2006, respectively, resulting in a 1.57 point increase in the loss ratio for the first nine months of 2007 compared to the same period of 2006. The 0.9 point increase in the expense ratio was primarily due to the transaction and integration costs associated with the 21st Century acquisition.

Net premiums written increased 4.1 percent for the first nine months of 2007 compared to the same period in 2006 due to continued growth in the Private Client Group and an increase in the aigdirect.com business, partially offset by a reduction in the Agency Auto segment.

Quarterly Mortgage Guaranty Results

Mortgage Guaranty reported an operating loss of $216 million for the three months ended September 30, 2007 compared to operating income of $85 million in the same period in 2006 due to the unfavorable loss experience in both the domestic first and second-lien businesses as continued deterioration in the U.S. housing market increased the frequency and severity of claims. The second-lien product was the major contributor to the operating loss, comprising $206 million of the third quarter 2007 operating loss. UGC's consolidated loss ratio for the third quarter of 2007 was 197.0 compared to a loss ratio of 47.5 in the same period of 2006. Prior year development reduced incurred losses by $27 million and $22 million for the three months ended September 30, 2007 and 2006, respectively, decreasing the 2007 loss ratio by 0.4 points relative to the 2006 loss ratio.

Net premiums written increased 31 percent in the three months ended September 30, 2007 compared to the same period in 2006 as strong growth in the European markets, Canada and Australia led to higher International premiums of $55 million. The increased use of mortgage insurance for credit enhancement, along with improved persistency, led to higher domestic first-lien premiums of $32 million, an increase of 27 percent compared to the 2006 quarter. Although UGC discontinued accepting new business for the poorly performing third-party originated second-lien product in the fourth quarter of 2006, UGC will continue to receive renewal premiums on the existing portfolio for the life of the loans, estimated to be three to five years. The expense ratio of 16.8 points in the three months ended September 30, 2007 declined from 22.5 points in the same period of 2006 as premium growth offset the effect of increased expenses related to UGC's international expansion and the employment of additional operational resources in the second-lien business.

UGC's domestic mortgage risk in force totaled $28.2 billion as of September 30, 2007 and the 60-day delinquency ratio was 3.0 percent (based on number of policies, consistent with mortgage industry practice) compared to domestic mortgage risk in force of $24.2 billion and a delinquency ratio of 2.0 percent at September 30, 2006. Approximately 81 percent of the domestic mortgage risk is secured by first-lien, owner-occupied properties.

Year-to-date Mortgage Guaranty Results

Mortgage Guaranty's operating loss for the first nine months of 2007 was $289 million compared to operating income of

$301 million for the same period in 2006 as the deteriorating U.S. residential housing market adversely affected losses incurred for both the domestic first-lien and second-lien businesses. Domestic first and second-lien losses incurred increased 254 percent and 611 percent respectively, compared to the first nine months of 2006, resulting in year-to-date loss ratios of 87.6 and 343.1, respectively, for the first nine months of 2007. Increases in domestic losses incurred resulted in a consolidated UGC loss ratio of 140.9 for the first nine months of 2007 compared to 37.4 for the same period in 2006. Prior year development had minimal effect on incurred losses in the first nine months of 2007 compared to a reduction of $86 million for the same period in 2006, which accounted for 16 points of the increase in the loss ratio.

Net premiums written increased 35 percent in the nine months ended September 30, 2007 compared to the same period in 2006 primarily due to growth in the International markets, accounting for 22 percent of the increase in net written premiums. In addition the increased use of mortgage insurance for credit enhancement as well as better persistency resulted in an increase in domestic first-lien premiums. The expense ratio for the first nine months of 2007 was 20.2, down from 23.3 in the same period in 2006 as premium growth offset the effect of increased expenses related to UGC's international expansion.

Quarterly Foreign General Insurance Results

Foreign General's operating income decreased in the three months ended September 30, 2007 compared to the same period in 2006 due to decreases in statutory underwriting profit, partially offset by increases in net investment income and the effect of changes in the currency exchange rates of the Euro and the British Pound. Statutory underwriting profit decreased due to lower favorable loss development on prior accident years of $49 million, additional losses from the June 2007 U.K. floods of $23 million and an increase over the 2006 quarter in severe but non-catastrophic losses of $20 million.

Net premiums written increased 14 percent (11 percent in original currency) for the three months ended September 30, 2007 compared to the same period in 2006, reflecting growth in commercial and consumer lines driven by new business from both established and new distribution channels, including Central Insurance Co. Ltd. in Taiwan. Net premiums written for commercial lines in the U.K. and Europe increased due to new business and decreases in the use of reinsurance, partially offset by declines in premium rates. Growth in consumer lines in Latin America, Asia and Europe also contributed to the increase. Net premiums written also increased by one percent compared to the same period in 2006 due to decreases in the use of reinsurance. Net premiums for the Lloyd's syndicate Ascot and Aviation declined due to rate decreases resulting from increased market competition.

The loss ratio increased 4.0 points for the three months ended September 30, 2007 compared to the same period in 2006. The 2007 loss ratio increased a total of 3.3 points due to the losses described above. The lower favorable loss development on prior accident years was primarily due to increases in the allowance for reinsurance. Also, the loss ratio increased due to higher loss frequency for personal accident businesses in Japan.

The expense ratio increased 2.1 points for the three months ended September 30, 2007 compared to the same period in 2006 due to higher operating expenses relating to new business initiatives. In addition, the 2007 expense ratio increased 1.2 points due to accelerated amortization of advertising costs, the cost of realigning certain legal entities through which Foreign General operates and the increased significance of consumer lines of business, which have higher acquisition costs. AIG expects the expense ratio to increase in the fourth quarter of 2007 as a result of expected decreases in net premiums written due to continuing rate pressures in the commercial lines business, the underlying seasonality of renewals and the growth of the consumer lines of business.

Net investment income increased for the three months ended September 30, 2007 compared to the same period of 2006 reflecting higher interest rates and strong cash flows, partially offset by reductions in mutual fund income. Mutual fund income was $61 million lower than the same quarter in 2006 reflecting a weaker performance in the equity markets and income of $22 million from an out of period UCITS adjustment in the year ago quarter.

Year-to-date Foreign General Insurance Results

Foreign General's operating income decreased in the first nine months of 2007 compared to the same period in 2006, due primarily to decreases in statutory underwriting profits. Statutory underwriting profit decreased due to lower favorable loss development on prior accident years of $101 million, losses from the June 2007 U.K. floods of $91 million, and an increase in severe but non-catastrophic losses of $48 million compared to the same period in 2006. Net investment income in the nine months ended September 30, 2006 included income of $406 million from out of period UCITS adjustments.

Net premiums written increased 15 percent (11 percent in original currency) for the nine months ended September 30, 2007 compared to the same period in 2006, reflecting growth in commercial and consumer lines driven by new business from both established and new distribution channels.

The loss ratio increased 3.0 points for the nine months ended September 30, 2007 compared to the same period in 2006. The 2007 loss ratio increased 2.6 points, due to the losses described above.

The expense ratio increased 0.7 points for the nine months ended September 30, 2007 compared to the same period in 2006 due to higher commission costs and higher operating expenses resulting from new business initiatives and the costs to realign certain legal entities.

Net investment income was essentially unchanged in the nine months ended September 30, 2007 compared to the same period of 2006 as the 2006 period included the out of period UCITS adjustments, which more than offset increased investment income of $402 million reflecting higher interest rates, strong cash flows and increased partnership and mutual fund income. Partnership income was $97 million higher than prior year due to strong infrastructure fund performance in Africa, Europe and Latin America. Mutual fund income was $117 million higher than the same period of the prior year reflecting strong performance in the equity markets for the nine month period.

Reserve for Losses and Loss Expenses

The following table presents the components of the General Insurance gross reserve for losses and loss expenses (loss reserves) as of September 30, 2007 and December 31, 2006 by major line of business on a statutory Annual Statement basis[a]:

(in millions)	**September 30, 2007**	December 31, 2006[b]
Other liability occurrence	**$20,296**	$19,327
Workers compensation	**14,994**	13,612
Other liability claims made	**13,546**	12,513
Auto liability	**6,208**	6,070
International	**6,173**	6,006
Property	**4,431**	5,499
Reinsurance	**3,371**	2,979
Medical malpractice	**2,349**	2,347
Products liability	**2,181**	2,239
Accident and health	**1,901**	1,693
Commercial multiple peril	**1,744**	1,651
Aircraft	**1,715**	1,629
Fidelity/surety	**1,248**	1,148
Other	**3,451**	3,286
Total	**$83,608**	$79,999

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

[b] *Allocations among various lines were revised from the previous presentation.*

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

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

At September 30, 2007, General Insurance net loss reserves were $66.94 billion, an increase of $4.31 billion from the prior year-end. The net loss reserves represent loss reserves reduced by reinsurance recoverables, net of an allowance for unrecoverable reinsurance and applicable discount for future investment income.

The following table classifies the components of the General Insurance net loss reserves by business unit:

(in millions)	**September 30, 2007**	December 31, 2006
DBG[a]	**$46,511**	$44,119
Transatlantic	**6,669**	6,207
Personal Lines[b]	**2,313**	2,440
Mortgage Guaranty	**1,016**	460
Foreign General[c]	**10,428**	9,404
Total Net Loss Reserve	**$66,937**	$62,630

(a) *At September 30, 2007 and December 31, 2006, respectively, DBG loss reserves include approximately $3.16 billion and $3.33 billion ($3.40 billion and $3.66 billion, respectively, before discount), related to business written by DBG but ceded to American International Reinsurance Company Limited (AIRCO) and reported in AIRCO's statutory filings. DBG loss reserves also include approximately $573 million and $535 million related to business included in American International Underwriters Overseas, Ltd.'s (AIUO) statutory filings at September 30, 2007 and December 31, 2006, respectively.*

(b) *At September 30, 2007 and December 31, 2006, respectively, Personal Lines loss reserves include $844 million and $861 million related to business ceded to DBG and reported in DBG's statutory filings.*

(c) *At September 30, 2007 and December 31, 2006, respectively, Foreign General loss reserves include approximately $3.05 billion and $2.75 billion related to business reported in DBG's statutory filings.*

The DBG net loss reserve of $46.5 billion is comprised principally of the business of AIG subsidiaries participating in

the American Home Assurance Company (American Home)/ National Union Fire Insurance Company of Pittsburgh, Pa. (National Union) pool (10 companies) and the surplus lines pool (Lexington, AIG Excess Liability Insurance Company and Landmark Insurance Company).

DBG cedes a quota share percentage of its other liability occurrence and products liability occurrence business to AIRCO. The quota share percentage ceded was 15 percent for the nine months ended September 30, 2007 and 20 percent for the year 2006 and covered all business written in these years for these lines by participants in the American Home/National Union pool. AIRCO's loss reserves relating to these quota share cessions from DBG are recorded on a discounted basis. As of September 30, 2007, AIRCO carried a discount of approximately $240 million applicable to the $3.40 billion in undiscounted reserves it assumed from the American Home/National Union pool via this quota share cession. AIRCO also carries approximately $523 million in net loss reserves relating to Foreign General insurance business. These reserves are carried on an undiscounted basis.

The companies participating in the American Home/ National Union pool have maintained a participation in the business written by AIU for decades. As of September 30, 2007, these AIU reserves carried by participants in the American Home/National Union pool totaled approximately $3.05 billion. The remaining Foreign General reserves are carried by AIUO, AIRCO, and other smaller AIG subsidiaries domiciled outside the United States. Statutory filings in the U.S. by AIG companies reflect all the business written by U.S. domiciled entities only, and therefore exclude business written by AIUO, AIRCO, and all other internationally domiciled subsidiaries. The total reserves carried at September 30, 2007 by AIUO and AIRCO were approximately $5.04 billion and $3.69 billion, respectively. AIRCO's $3.69 billion in total general insurance reserves consist of approximately $3.16 billion from business assumed from the American Home/National Union pool and an additional $523 million relating to Foreign General Insurance business.

Discounting of Reserves

At September 30, 2007, AIG's overall General Insurance net loss reserves reflect a loss reserve discount of $2.43 billion, including tabular and non-tabular calculations. The tabular workers compensation discount is calculated using a 3.5 percent interest rate and the 1979-81 Decennial Mortality Table. The non-tabular workers compensation discount is calculated separately for companies domiciled in New York and Pennsylvania, and follows the statutory regulations for each state. For New York companies, the discount is based on a five percent interest rate and the companies' own payout patterns. For Pennsylvania companies, the statute has specified discount factors for accident years 2001 and prior, which are based on a six percent interest rate and an industry payout pattern. For accident years 2002 and subsequent, the discount is based on the yield of U.S. Treasury securities ranging from one to twenty years and the company's own payout pattern, with the future expected payment for each year using the interest rate associated with the corresponding Treasury security yield for that time period. The discount is comprised of the following: $726 million – tabular discount for workers compensation in DBG; $1.46 billion – non-tabular discount for workers compensation in DBG; and, $240 million – non-tabular discount for other liability occurrence and products liability occurrence in AIRCO. The total undiscounted workers compensation loss reserve carried by DBG is approximately $12.7 billion as of September 30, 2007. The other liability occurrence and products liability occurrence business in AIRCO that is assumed from DBG is discounted based on the yield of U.S. Treasury securities ranging from one to twenty years and the DBG payout pattern for this business. The undiscounted reserves assumed by AIRCO from DBG totaled approximately $3.40 billion at September 30, 2007.

Quarterly Reserving Process

Management believes that the General Insurance net loss reserves are adequate to cover General Insurance net losses and loss expenses as of September 30, 2007. While AIG regularly reviews the adequacy of established loss reserves, there can be no assurance that AIG's ultimate loss reserves will not develop adversely and materially exceed AIG's loss reserves as of September 30, 2007. In the opinion of management, such adverse development and resulting increase in reserves is not likely to have a material adverse effect on AIG's consolidated financial condition, although it could have a material adverse effect on AIG's consolidated results of operations for an individual reporting period.

The following table presents the reconciliation of net loss reserves:

	Three Months Ended September 30,		Nine Months Ended September 30,	
(in millions)	**2007**	2006	**2007**	2006
Net reserve for losses and loss expenses at beginning of period	**$65,197**	$60,214	**$62,630**	$57,476
Foreign exchange effect	**224**	34	**438**	521
Acquisition*	**–**	55	**–**	55
Losses and loss expenses incurred:				
Current year	**7,636**	6,957	**22,185**	20,710
Prior years, other than accretion of discount	**(337)**	(41)	**(605)**	(255)
Prior years, accretion of discount	**92**	101	**220**	303
Losses and loss expenses incurred	**7,391**	7,017	**21,800**	20,758
Losses and loss expenses paid	**5,875**	5,807	**17,931**	17,297
Net reserve for losses and loss expenses at end of period	**$66,937**	$61,513	**$66,937**	$61,513

** Reflects the opening balance with respect to the acquisition of the Central Insurance Co., Ltd. in the third quarter of 2006*

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

	Three Months Ended September 30,		Nine Months Ended September 30,	
(in millions)	**2007**	2006	**2007**	2006
Prior Accident Year Development by Reporting Unit:				
DBG	**$ (313)**	$ 67	**$ (465)**	$ 35
Personal Lines	**32**	(21)	**(29)**	(84)
Mortgage Guaranty	**(27)**	(22)	**–**	(86)
Foreign General	**(40)**	(89)	**(108)**	(209)
Subtotal	**(348)**	(65)	**(602)**	(344)
Transatlantic	**11**	24	**47**	89
Asbestos settlements*	**–**	–	**(50)**	–
Prior years, other than accretion of discount	**$ (337)**	$ (41)	**$ (605)**	$ (255)

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

	Calendar Year	
(in millions)	**2007**	2006
Prior Accident Year Development by Accident Year:		
2006	**$ (898)**	
2005	**(373)**	$ (638)
2004	**(248)**	(416)
2003	**143**	(233)
2002	**200**	156
2001 & prior	**571**	876
Prior years, other than accretion of discount	**$ (605)**	$ (255)

In determining the quarterly loss development from prior accident years, AIG conducts analyses to determine the change in estimated ultimate loss for each accident year for each profit center. For example, if loss emergence for a profit center is different than expected for certain accident years, the actuaries examine the indicated effect such emergence would have on the reserves of that profit center. In some cases, the higher or lower than expected emergence may result in no clear change in the ultimate loss estimate for the accident years in question, and no adjustment would be made to the profit center's reserves for prior accident years. In other cases, the higher or lower than expected emergence may result in a larger change, either favorable or unfavorable, than the difference between the actual and expected loss emergence. Such additional analyses were conducted for each profit center, as appropriate, in the third quarter of 2007 to determine the loss development from prior accident years for the third quarter of 2007. As part of its quarterly reserving process, AIG also considers notices of claims received with respect to emerging issues, such as those related to the U.S. mortgage and housing market. Also as part of the quarterly reserving process, beginning with the second quarter of 2007, AIG updated its analysis of the loss reserve discount pertaining to workers compensation reserves. Historically, this review was only performed at year end. As a result of the

updated analysis in the third quarter of 2007, AIG increased its loss reserve discount for workers compensation by approximately $70 million in the third quarter of 2007, bringing the total increase in loss reserve discount for workers compensation for the first nine months of 2007 to approximately $255 million.

2007 Net Loss Development

In the three months ended September 30, 2007, net loss development from prior accident years was favorable by approximately $337 million, including approximately $11 million of adverse development from the general reinsurance operations of Transatlantic; and excluding approximately $92 million from accretion of loss reserve discount. Excluding Transatlantic, as well as accretion of discount, net loss development in the three months ended September 30, 2007 from prior accident years was favorable by approximately $348 million. The overall favorable development of $337 million consisted of approximately $764 million of favorable development from accident years 2004 through 2006, partially offset by approximately $299 million of adverse development from accident years 2002 and prior and $128 million of adverse development from accident year 2003. For the three months ended September 30, 2007, most classes of AIG's business continued to experience favorable development for accident years 2004 through 2006. The majority of the adverse development from accident years 2002 and prior was related to developments from excess casualty business within DBG and from Transatlantic. The adverse development from accident year 2003 was primarily related to developments from excess casualty business within DBG, which represented less than a 1 percent change in the ultimate loss estimate for accident year 2003. In the three months ended September 30, 2007, AIG completed an update of its ground up projections of claims exposure for the D&O and related management liability classes of business. AIG utilizes the ultimate loss estimates resulting from these claims projections as a benchmark in determining the appropriate loss reserves for this business. As a result of the updated claims projections, in addition to the quarterly review of reported loss experience as of September 30, 2007 and other relevant factors, AIG recognized approximately $150 million in favorable loss development from prior accident years for the D&O and related management liability classes of business in the three months ended September 30, 2007. This consisted of approximately $200 million of favorable development from accident years 2004 through 2006, partially offset by approximately $50 million of adverse development from accident years 2002 and prior. The overall favorable development of $337 million reflects this $150 million from the D&O and related management liability classes of business within DBG.

In the first nine months of 2007, net loss development from prior accident years was favorable by approximately $605 million, including approximately $47 million of adverse development from the general reinsurance operations of Transatlantic; and excluding approximately $220 million from accretion of loss reserve discount. Excluding Transatlantic, as well as accretion of discount, net loss development in the first nine months of 2007 from prior accident years was favorable by approximately $652 million. The overall favorable development of $605 million consisted of approximately $1.52 billion of favorable development from accident years 2004 through 2006, partially offset by approximately $771 million of adverse development from accident years 2002 and prior and $143 million of adverse development from accident year 2003. For the first nine months of 2007, most classes of AIG's business continued to experience favorable development for accident years 2004 through 2006. The majority of the adverse development from accident years 2002 and prior was related to development from excess casualty business within DBG and from Transatlantic. The adverse development from accident year 2003 was primarily related to developments from excess casualty business within DBG. The overall favorable development of $605 million includes approximately $200 million pertaining to the D&O and related management liability classes of business within DBG, consisting of approximately $235 million of favorable development from accident years 2004 through 2006, partially offset by approximately $35 million of adverse development from accident years 2002 and prior.

2006 Net Loss Development

In the three months ended September 30, 2006, net loss development from prior accident years was favorable by approximately $41 million, including approximately $43 million of adverse development pertaining to the major hurricanes in 2005 and 2004 and $24 million of adverse development pertaining to the general reinsurance operations of Transatlantic. Excluding catastrophes and Transatlantic, as well as accretion of discount of approximately $101 million, net loss development from prior accident years in the three months ended September 30, 2006 was favorable by approximately $108 million. This overall favorable development of $41 million consisted of approximately $511 million of favorable development from accident years 2003 through 2005, partially offset by approximately $470 million of adverse development from accident years 2002 and prior. For the three months ended September 30, 2006, most classes of business throughout AIG experienced favorable development for accident years 2003 through 2005. The adverse development from accident years 2002 and prior reflected developments from excess casualty, workers compensation, and post-1986 environmental liability classes of business, all within DBG, and from Transatlantic.

In the first nine months of 2006, net loss development from prior accident years was favorable by approximately $255 million, including approximately $80 million of adverse development pertaining to the major hurricanes in 2004 and 2005 and $89 million of adverse development from the general reinsurance operations of Transatlantic, and excluding approximately $303 million from accretion of loss reserve discount. Excluding catastrophes and Transatlantic, as well as accretion of discount, net loss development from prior accident years in the first nine months of 2006 was favorable by approximately $424 million. The overall favorable development of $255 million consisted of approximately $1.29 billion of favorable development from accident years 2003 through 2005, partially offset by approximately $1.03 billion of adverse development from accident years 2002 and prior. For the first nine months of 2006, most classes of business throughout AIG experienced favorable development for accident years 2003 through 2005. The adverse development from accident years 2002 and prior reflected developments from excess casualty, workers compensation, excess workers compensation, and post-1986 environmental liability classes of business, all within DBG, and from Transatlantic.

As a result of the continued favorable experience for accident years 2003 through 2005, the expected loss ratios for accident year 2006 were improved for a number of casualty classes of business in the three months ended September 30, 2006. For those classes of business where the expected loss ratio for accident year 2006 was adjusted in the three months ended September 30, 2006, the revised loss ratio was generally applied to the cumulative 2006 net earned premium for the class. The overall effect on the results for the three months ended September 30, 2006, was approximately a $100 million improvement. This amount represents the application of the revised expected loss ratios to the net premiums earned reported for the first six months of 2006.

Asbestos and Environmental Reserves

The estimation of loss reserves relating to asbestos and environmental claims on insurance policies written many years ago is subject to greater uncertainty than other types of claims due to inconsistent court decisions as well as judicial interpretations and legislative actions that in some cases have tended to broaden coverage beyond the original intent of such policies and in others have expanded theories of liability.

As described more fully in the 2006 Annual Report on Form 10-K, AIG's reserves relating to asbestos and environmental claims reflect a comprehensive ground up analysis. In the first nine months of 2007, one large asbestos settlement, as well as a reduction in estimated reinsurance recoverable, resulted in a minor amount of adverse incurred loss development, which was partially offset, on a net basis, by the favorable $50 million effect of several other settlements.

A summary of reserve activity, including estimates for applicable IBNR, relating to asbestos and environmental claims separately and combined:

	Nine Months Ended September 30,			
	2007		2006	
(in millions)	**Gross**	**Net**	Gross	Net
Asbestos:				
Reserve for losses and loss expenses at beginning of year	**$4,464**	**$1,889**	$4,441	$1,840
Losses and loss expenses incurred*	**19**	**7**	2	7
Losses and loss expenses paid*	**(614)**	**(363)**	(404)	(151)
Reserve for losses and loss expenses at end of period	**$3,869**	**$1,533**	$4,039	$1,696
Environmental:				
Reserve for losses and loss expenses at beginning of year	**$ 588**	**$ 290**	$ 926	$ 410
Losses and loss expenses incurred*	**2**	**(1)**	(3)	–
Losses and loss expenses paid*	**(89)**	**(46)**	(80)	(43)
Reserve for losses and loss expenses at end of period	**$ 501**	**$ 243**	$ 843	$ 367
Combined:				
Reserve for losses and loss expenses at beginning of year	**$5,052**	**$2,179**	$5,367	$2,250
Losses and loss expenses incurred*	**21**	**6**	(1)	7
Losses and loss expenses paid*	**(703)**	**(409)**	(484)	(194)
Reserve for losses and loss expenses at end of period	**$4,370**	**$1,776**	$4,882	$2,063

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

The gross and net IBNR included in the reserve for losses and loss expenses, relating to asbestos and environmental claims separately and combined, were estimated as follows:

	Nine Months Ended September 30,			
	2007		2006	
(in millions)	**Gross**	**Net**	Gross	Net
Asbestos	**$2,743**	**$1,261**	$2,863	$1,312
Environmental	**289**	**127**	567	242
Combined	**$3,032**	**$1,388**	$3,430	$1,554

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

	Nine Months Ended September 30,					
	2007			2006		
	Asbestos	**Environmental**	**Combined**	Asbestos	Environmental	Combined
Claims at beginning of year	**6,878**	**9,442**	**16,320**	7,293	9,873	17,166
Claims during year:						
Opened	**321**	**850**	**1,171**	538	1,032	1,570
Settled	**(113)**	**(101)**	**(214)**	(126)	(120)	(246)
Dismissed or otherwise resolved	**(745)**	**(2,138)**	**(2,883)**	(678)	(1,295)	(1,973)
Claims at end of period	**6,341**	**8,053**	**14,394**	7,027	9,490	16,517

Survival Ratios – Asbestos and Environmental

The table below presents AIG's survival ratios for asbestos and environmental claims at September 30, 2007 and 2006. The survival ratio is derived by dividing the current carried loss reserve by the average payments for the three most recent calendar years for these claims. Therefore, the survival ratio is a simplistic measure estimating the number of years it would be before the current ending loss reserves for these claims would be paid off using recent year average payments. The September 30, 2007 survival ratio is lower than the ratio at September 30, 2006 because the more recent periods included in the rolling average reflect higher claims payments. In addition, AIG's survival ratio for asbestos claims was negatively affected by the favorable settlements described above, which reduced gross and net asbestos survival ratios at September 30, 2007 by approximately 1.4 years and 3.2 years, respectively. Many factors, such as aggressive settlement procedures, mix of business and level of coverage provided, have a significant effect on the amount of asbestos and environmental reserves and payments and the resultant survival ratio. Thus, caution should be exercised in attempting to determine reserve adequacy for these claims based simply on this survival ratio.

AIG's survival ratios for asbestos and environmental claims, separately and combined were based upon a three-year average payment. These ratios at September 30, 2007 and 2006 were as follows:

(number of years)	**Gross**	**Net**
2007		
Survival ratios:		
Asbestos	7.6	6.4
Environmental	4.8	3.8
Combined	7.1	5.8
2006		
Survival ratios:		
Asbestos	11.9	13.6
Environmental	6.5	5.3
Combined	10.4	10.7

Life Insurance & Retirement Services Operations

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

Overseas, AIG's Life Insurance & Retirement Services operations include insurance and investment-oriented products such as whole and term life, investment linked, universal life and endowments, personal accident and health products, group products including pension, life and health, and fixed and variable annuities.

Domestically, AIG's Life Insurance & Retirement Services operations offer a broad range of protection products, such as life insurance and group life and health products, including disability income products and payout annuities, which include single premium immediate annuities, structured settlements and terminal funding annuities. Home service operations include an array of life insurance, accident and health and annuity products sold primarily through career agents. Retirement services include group retirement products, individual fixed and variable annuities sold

through banks, broker-dealers and exclusive sales representatives, and annuity runoff operations, which include previously acquired "closed blocks" and other fixed and variable annuities largely sold through distribution relationships that have been discontinued.

AIG's Life Insurance & Retirement Services subsidiaries report their operations through the following major internal reporting units and business units:

Foreign Life Insurance & Retirement Services

Japan and Other

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

Asia

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

Domestic Life Insurance

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

Domestic Retirement Services

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

Life Insurance & Retirement Services Results

Life Insurance & Retirement Services results were as follows:

(in millions)	Premiums and Other Considerations	Net Investment Income	Net Realized Capital Gains (Losses)	Total Revenues	Operating Income
Three Months Ended September 30, 2007					
Foreign Life Insurance & Retirement Services	**$ 6,505**	**$ 2,367**	**$ 138**	**$ 9,010**	**$1,736**
Domestic Life Insurance	**1,495**	**985**	**(295)**	**2,185**	**61**
Domestic Retirement Services	**300**	**1,471**	**(334)**	**1,437**	**202**
Total	**$ 8,300**	**$ 4,823**	**$ (491)**	**$12,632**	**$1,999**
Three Months Ended September 30, 2006					
Foreign Life Insurance & Retirement Services*	$ 5,987	$ 2,490	$ (29)	$ 8,448	$1,608
Domestic Life Insurance	1,424	958	(123)	2,259	261
Domestic Retirement Services	262	1,597	(24)	1,835	603
Total	$ 7,673	$ 5,045	$ (176)	$12,542	$2,472
Percentage Increase/(Decrease) from Prior Year:					
Foreign Life Insurance & Retirement Services	9%	(5)%	—%	7%	8%
Domestic Life Insurance	5	3	—	(3)	(77)
Domestic Retirement Services	15	(8)	—	(22)	(67)
Total	8%	(4)%	—%	1%	(19)%
Nine Months Ended September 30, 2007					
Foreign Life Insurance & Retirement Services	**$19,621**	**$ 8,611**	**$ (79)**	**$28,153**	**$4,674**
Domestic Life Insurance	**4,392**	**2,996**	**(323)**	**7,065**	**774**
Domestic Retirement Services	**882**	**4,861**	**(624)**	**5,119**	**1,452**
Total	**$24,895**	**$16,468**	**$(1,026)**	**$40,337**	**$6,900**
Nine Months Ended September 30, 2006					
Foreign Life Insurance & Retirement Services*	$18,085	$ 6,715	$ 487	$25,287	$5,033
Domestic Life Insurance	4,254	2,784	(190)	6,848	862
Domestic Retirement Services	782	4,800	(414)	5,168	1,588
Total	$23,121	$14,299	$ (117)	$37,303	$7,483
Percentage Increase/(Decrease) from Prior Year:					
Foreign Life Insurance & Retirement Services	8%	28%	—%	11%	(7)%
Domestic Life Insurance	3	8	—	3	(10)
Domestic Retirement Services	13	1	—	(1)	(9)
Total	8%	15%	—%	8%	(8)%

** Includes the effect of an out of period UCITS adjustment in 2006. For the three and nine-month periods ended September 30, 2006, the effect was increases of $24 million and $240 million, respectively, in net investment income and $24 million and $169 million, respectively, in operating income.*

The following table presents the Insurance In force for Life Insurance & Retirement Services:

(in millions)	**September 30, 2007**	December 31, 2006
Foreign	**$1,237,507**	$1,162,699
Domestic	**964,515**	907,901
Total	**$2,202,022**	$2,070,600

Volatility in the securities markets had a negative effect on Life Insurance & Retirement Services results for the three months ended September 30, 2007, and resulted in lower investment income from partnerships and UCITS and higher net realized capital losses for the quarter compared to last year. This negative effect was partially offset by strong life insurance production in Asia, improved universal life and variable universal life sales in the Domestic Life operations, and improved deposit flows for group retirement products and individual variable annuities in the Domestic Retirement Services business. The fixed annuity business environment remained challenging both domestically and in Japan reflecting a continuation of trends seen throughout the year. Investment income for the three months ended September 30, 2007 reflects a decline of $163 million in income from partnerships, UCITS, mutual funds and hedge funds, particularly in the Domestic Retirement Services business, and $74 million of trading account losses in the U.K. related to variable annuity products. In addition, the decline in Japanese equity markets resulted in higher incurred benefits of $36 million on a closed block of business having guaranteed benefits. The nine-month period ended September 30, 2007 included an increase of $176 million in income from partnerships, UCITS, mutual funds and hedge funds and $88 million of trading account losses in the U.K. associated with the variable annuity products.

Life Insurance & Retirement Services total revenues for the three and nine-month periods ended September 30, 2007 reflect growth in premiums and other considerations and higher realized capital losses. Net investment income grew for

the nine months ended September 30, 2007 but declined for three months then ended compared to the same period in 2006. Net realized capital losses reduced revenues by $491 million and $1.0 billion in the three and nine-month periods ended September 30, 2007, respectively, while net realized capital losses decreased revenues by $176 million and $117 million in the three and nine-month periods ended September 30, 2006, respectively. Net realized capital losses in 2007 were primarily related to the other-than-temporary decline in value of securities that AIG no longer intends to hold to recovery. Net investment income includes policyholder investment income and trading gains and losses (collectively, policyholder trading gains), which are offset by an equal charge to incurred policy losses and benefits expense, as these investment returns accrue to the benefit of the policyholder. Policyholder trading gains generally reflect the trend in equity markets. Policyholder trading gains were $150 million and $2 billion for the three and nine-month periods ended September 30, 2007, respectively, compared to $485 million and $969 million for the three and nine-month periods ended September 30, 2006, respectively. Net investment income for the three and nine-month periods ended September 30, 2006 included an increase of $24 million and $240 million, respectively, for an out of period adjustment related to the accounting for UCITS.

In order to better align financial reporting with the manner in which AIG's chief operating decision makers have managed their businesses, commencing in the first quarter of 2007, revenues and operating income related to foreign investment contracts, which were historically reported as a component of the Asset Management segment, are now being reported as part of Foreign Life Insurance & Retirement Services. Prior period amounts have been revised to conform to the current presentation.

Operating income for the first nine months of 2007 includes the adverse effect of $62 million related to SOP 05-1, a $62 million charge for additional benefits expense and a $50 million charge related to balance sheet reconciliation remediation activities. SOP 05-1 generally requires DAC related to group contracts to be amortized over a shorter duration than in prior periods and also requires that DAC be expensed at the time a policy is terminated. The effect of SOP 05-1 was most significant to the group products line in the Domestic Life operations. The additional benefit expense resulted from a continuing industry-wide review of claims in Japan. In addition, increased charges for DAC related to the conversion of actuarial systems to a common global standard within AIG decreased operating income by $32 million for both the three and nine-month periods ended September 30, 2007, respectively. Operating income for the three and nine-month periods ended September 30, 2006 included an increase of $24 million and $169 million, respectively, for an out of period adjustment related to the accounting for UCITS. Operating income for the three-month period ended September 30, 2007 declined compared to the same period in 2006 due to higher net realized capital losses, lower income from partnerships, UCITS, mutual funds and hedge funds as discussed above, trading account losses in the U.K. and a $14 million charge related to SOP 05-1.

Foreign Life Insurance & Retirement Services Results

Foreign Life Insurance & Retirement Services results were as follows:

(in millions)	Premiums and Other Considerations	Net Investment Income	Net Realized Capital Gains (Losses)	Total Revenues	Operating Income
Three Months Ended September 30, 2007					
Life insurance	**$ 3,992**	**$1,598**	**$ 74**	**$ 5,664**	**$1,048**
Personal accident	**1,519**	**91**	**12**	**1,622**	**353**
Group products	**744**	**162**	**(37)**	**869**	**81**
Individual fixed annuities	**141**	**533**	**89**	**763**	**286**
Individual variable annuities	**109**	**(17)**	**—**	**92**	**(32)**
Total	**$ 6,505**	**$2,367**	**$ 138**	**$ 9,010**	**$1,736**
Three Months Ended September 30, 2006					
Life insurance*	$ 3,837	$1,404	$ (25)	$ 5,216	$ 920
Personal accident	1,398	78	(16)	1,460	362
Group products	589	171	8	768	106
Individual fixed annuities	84	516	4	604	178
Individual variable annuities	79	321	—	400	42
Total	$ 5,987	$2,490	$ (29)	$ 8,448	$1,608
Percentage Increase/(Decrease) from Prior Year:					
Life insurance	4%	14%	—%	9%	14%
Personal accident	9	17	—	11	(2)
Group products	26	(5)	—	13	(24)
Individual fixed annuities	68	3	—	26	61
Individual variable annuities	38	—	—	(77)	—
Total	9%	(5)%	—%	7%	8%
Nine Months Ended September 30, 2007					
Life insurance	**$12,264**	**$5,247**	**$ 47**	**$17,558**	**$2,855**
Personal accident	**4,479**	**261**	**6**	**4,746**	**1,046**
Group products	**2,187**	**558**	**(64)**	**2,681**	**233**
Individual fixed annuities	**387**	**1,681**	**(68)**	**2,000**	**487**
Individual variable annuities	**304**	**864**	**—**	**1,168**	**53**
Total	**$19,621**	**$8,611**	**$ (79)**	**$28,153**	**$4,674**
Nine Months Ended September 30, 2006					
Life insurance*	$11,857	$3,997	$ 395	$16,249	$3,072
Personal accident	4,084	213	36	4,333	1,080
Group products	1,669	463	20	2,152	303
Individual fixed annuities	273	1,470	36	1,779	475
Individual variable annuities	202	572	—	774	103
Total	$18,085	$6,715	$ 487	$25,287	$5,033
Percentage Increase/(Decrease) from Prior Year:					
Life insurance	3%	31%	(88)%	8%	(7)%
Personal accident	10	23	(83)	10	(3)
Group products	31	21	—	25	(23)
Individual fixed annuities	42	14	—	12	3
Individual variable annuities	50	51	—	51	(49)
Total	8%	28%	—%	11%	(7)%

** Includes the effect of an out of period UCITS adjustment in 2006. For the three and nine-month periods ended September 30, 2006, the effect was an increase of $22 million and $237 million, respectively, in net investment income and $22 million and $166 million, respectively, in operating income.*

Foreign Life Insurance & Retirement Services Results (continued)

AIG transacts business in most major foreign currencies and therefore premiums reported in U.S. dollars vary both by volume and as a result of changes in foreign currency translation rates. The following table summarizes the effect of changes in foreign currency exchange rates on the growth of the Foreign Life Insurance & Retirement Services premiums and other considerations:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2007	2006	**2007**	2006
Growth in original currency*	**7.5%**	8.8%	**6.8%**	7.8%
Foreign exchange effect	**1.2**	(0.6)	**1.7**	(3.0)
Growth as reported in U.S. dollars	**8.7%**	8.2%	**8.5%**	4.8%

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

Quarterly Japan and Other Results

(in millions)	Premiums and Other Considerations	Net Investment Income	Net Realized Capital Gains (Losses)	Total Revenues	Operating Income
Three Months Ended September 30, 2007					
Life insurance	**$1,219**	**$ 393**	**$ 81**	**$1,693**	**$ 429**
Personal accident	**1,049**	**48**	**5**	**1,102**	**267**
Group products	**563**	**131**	**(2)**	**692**	**76**
Individual fixed annuities	**137**	**499**	**101**	**737**	**290**
Individual variable annuities	**109**	**(18)**	**—**	**91**	**(32)**
Total	**$3,077**	**$1,053**	**$185**	**$4,315**	**$1,030**
Three Months Ended September 30, 2006					
Life insurance*	$1,199	$ 470	$ 66	$1,735	$ 428
Personal accident	1,004	42	(4)	1,042	292
Group products	449	147	1	597	61
Individual fixed annuities	72	490	4	566	171
Individual variable annuities	78	321	—	399	41
Total	$2,802	$1,470	$ 67	$4,339	$ 993
Percentage Increase/(Decrease) from Prior Year:					
Life insurance	2%	(16)%	23%	(2)%	—%
Personal accident	4	14	—	6	(9)
Group products	25	(11)	—	16	25
Individual fixed annuities	90	2	—	30	70
Individual variable annuities	40	—	—	(77)	—
Total	10%	(28)%	176%	(1)%	4%

** Includes the effect of an out of period UCITS adjustment in 2006. For the three-month period ended September 30, 2006, the effect was an increase of $13 million for both net investment income and operating income.*

Total revenues for the three-month period ended September 30, 2007 declined slightly compared to the same period in 2006, primarily due to securities markets volatility which resulted in lower policyholder trading gains and partnership and mutual fund income. Operating income increased for the three months ended September 30, 2007 compared to the same period in 2006 primarily due to net realized capital gains which more than offset the negative effect of securities markets volatility. The volatility in the securities markets reduced partnership and mutual fund revenues by $89 million, increased incurred policyholder benefits by $36 million related to a closed block of business with guaranteed benefits and resulted in trading account losses of $74 million in the U.K. associated with the variable annuity product.

Life insurance premiums and other considerations increased moderately in the three months ended September 30, 2007 compared to the same period in 2006 reflecting a continuing shift to interest sensitive whole life products in Japan. In addition, first year premium sales in Japan declined due to the suspension of increasing term products pending completion of an industry-wide review by the National Tax Authority. Single premium sales of interest sensitive whole life products in Japan and investment linked products in Europe remained strong. Net investment income declined due to lower policyholder trading gains. Both net investment income and operating income for the three months ended September 30, 2006 included out of period income related to UCITS of $13 million. Life insurance operating income for the three months ended September 30, 2007 was essentially unchanged compared to the same period in 2006 as higher realized capital gains and earnings from growth in new business were offset by the effects of securities market volatility which resulted in a decline in partnership and mutual fund income, and higher incurred benefits of $36 million on a closed block of business with guaranteed benefits.

Personal accident premiums and other considerations continue to grow at a modest rate. Strong growth in Europe was offset by declines in Japan, which has been adversely affected by increased competition and market saturation. When compared to the same period in 2006, net investment income increased due to higher invested assets. Operating income declined for the three months ended September 30, 2007 compared to the same period in 2006 due to changes in actuarial estimates, which decreased operating income in 2007 by $14 million and increased operating income in 2006 by $29 million.

Group products premiums and other considerations increased for the three months ended September 30, 2007 compared to the same period in 2006 primarily due to rapidly growing credit business in Europe and higher fee income from pension business in Brazil. Net investment income declined over the same period last year as policyholder trading gains were negatively affected by the volatile securities market. Operating income increased compared to the same period in 2006 reflecting higher premium revenues.

Individual fixed annuities premiums and other considerations growth reflects higher surrender charges from U.S. dollar contracts in Japan where a weak yen makes it attractive for certain policyholders to lock in foreign exchange gains in excess of surrender charges. Surrender charges were $46 million and $22 million for the three months ended September 30, 2007 and 2006, respectively. Operating income also reflected higher net realized capital gains.

Individual variable annuity deposits declined in Europe due to a change in consumer tax benefits for certain off-shore products, but increased in Japan as the bank distribution base for new products with guarantees is steadily expanding. New on-shore products are being launched in the U.K. to replace declining sales of off-shore products. Net investment income for the three months ended September 30, 2007 declined compared to the same period in 2006 due to lower policyholder trading gains as a result of the volatility in the securities markets. Net investment income in 2007 also included trading account losses of $74 million, offset partially by higher fees generated from the growth in assets under management compared to the same period in 2006.

Year-to-date Japan and Other Results

(in millions)	Premiums and Other Considerations	Net Investment Income	Net Realized Capital Gains (Losses)	Total Revenues	Operating Income
Nine Months Ended September 30, 2007					
Life insurance	**$3,785**	**$1,584**	**$ 96**	**$ 5,465**	**$1,219**
Personal accident	**3,118**	**150**	**7**	**3,275**	**799**
Group products	**1,677**	**482**	**4**	**2,163**	**212**
Individual fixed annuities	**354**	**1,591**	**(63)**	**1,882**	**471**
Individual variable annuities	**302**	**861**	**—**	**1,163**	**52**
Total	**$9,236**	**$4,668**	**$ 44**	**$13,948**	**$2,753**
Nine Months Ended September 30, 2006					
Life insurance *	$3,608	$1,269	$300	$ 5,177	$1,330
Personal accident	2,954	122	36	3,112	858
Group products	1,289	393	12	1,694	201
Individual fixed annuities	229	1,398	34	1,661	457
Individual variable annuities	201	570	—	771	100
Total	$8,281	$3,752	$382	$12,415	$2,946
Percentage Increase/(Decrease) from Prior Year:					
Life insurance	5%	25%	(68)%	6%	(8)%
Personal accident	6	23	(81)	5	(7)
Group products	30	23	(67)	28	5
Individual fixed annuities	55	14	—	13	3
Individual variable annuities	50	51	—	51	(48)
Total	12%	24%	(88)%	12%	(7)%

** Includes the effect of an out of period UCITS adjustment in 2006. For the nine-month period ended September 30, 2006, the effect was an increase of $29 million for both net investment income and operating income.*

Revenues for the first nine months of 2007 increased compared to the same period in 2006, primarily due to higher premiums and other considerations and net investment income partially offset by lower net realized capital gains. Investment income increased due to growth in assets under management and higher policyholder trading gains partially offset by lower partnership and mutual fund income for the nine months ended September 30, 2007. Operating income decreased in the first nine months of 2007 compared to the same period in 2006 due to lower net realized capital gains, trading account losses of $88 million in the U.K. associated with the variable annuity products and $62 million of additional reserve provisions related to the claims review in Japan.

Life insurance premiums and other considerations increased in the first nine months of 2007 compared to the same period in 2006. In Japan, increased fees and policy charges related to interest sensitive whole life and U.S. dollar life insurance products, as well as strong sales of increasing term products earlier in the year, were partially offset by the runoff of the acquired blocks of business in AIG Star Life and AIG Edison Life. In Europe, growth in premiums and other considerations was driven by the growing block of single premium investment-linked products and the positive effect of foreign exchange rates. The growth in net investment income was due to higher partnership income and other yield enhancement income, income from UCITS, higher policyholder trading gains and growth in underlying invested assets. Life insurance operating income declined in the first nine months of 2007 compared to the same period in 2006 due to lower net realized capital gains.

Personal accident premiums and other considerations grew modestly as strong growth in Europe was offset by slower growth in Japan. Net investment income increased in the first nine months of 2007 compared to the same period in 2006 primarily due to higher invested assets and increased partnership income. Operating income in the first nine months of 2007 was affected by lower realized capital gains, a $46 million provision related to the Japan claims review, and $17 million of additional expenses related to the effect of SOP 05-1. The effect of the termination of certain tax-related accident and health products in Japan diminished in the third quarter of 2007 as the renewal cycle of these policies has been completed. Loss ratios remained stable for this business.

Group products premiums and other considerations increased for the first nine months in 2007 compared to the same period in 2006 primarily due to the growing credit business in Europe. Net investment income increased from the first nine months of 2006 primarily due to higher assets under management related to the Brazil pension business. Operating income for the first nine months of 2007 improved over the same period in 2006 primarily due to revenue growth, which was partially offset by a $16 million adverse effect related to SOP 05-1.

Individual fixed annuity deposits declined in the first nine months of 2007 due to the effect of a weak Yen on sales in Japan as well as the market shift to variable annuity products in Japan. Assets under management however

continued to grow. Individual fixed annuities premiums and other considerations growth reflects a shift to front-end load products and higher surrender charges from U.S. dollar contracts in Japan where a weak yen makes it attractive for certain policyholders to lock in foreign exchange gains in excess of surrender charges. Surrender charges were $132 million and $64 million for the nine months ended September 30, 2007 and 2006, respectively. Net investment income increased due to higher average investment yields and growth in assets under management, partially offset by lower partnership income. Operating income declined in 2007 due to realized capital losses in 2007 versus realized capital gains in 2006.

Individual variable annuity deposits declined due to the effect of tax law changes in Europe that reduced tax benefits to policyholders and lower sales in Japan. The fees generated from the growth in assets under management increased premiums and other considerations for the first nine months of 2007 compared to the same period in 2006. Net investment income increased due to higher policyholder trading gains in the first nine months of 2007 compared to the same period in 2006. Operating income declined for the first nine months of 2007 compared to the same period in 2006 primarily due to $88 million of trading account losses.

Quarterly Asia Results

(in millions)	Premiums and Other Considerations	Net Investment Income	Net Realized Capital Gains (Losses)	Total Revenues	Operating Income
Three Months Ended September 30, 2007					
Life insurance	**$2,773**	**$1,205**	**$ (7)**	**$3,971**	**$619**
Personal accident	**470**	**43**	**7**	**520**	**86**
Group products	**181**	**31**	**(35)**	**177**	**5**
Individual fixed annuities	**4**	**34**	**(12)**	**26**	**(4)**
Individual variable annuities	**—**	**1**	**—**	**1**	**—**
Total	**$3,428**	**$1,314**	**$(47)**	**$4,695**	**$706**
Three Months Ended September 30, 2006					
Life insurance *	$2,638	$ 934	$(91)	$3,481	$492
Personal accident	394	36	(12)	418	70
Group products	140	24	7	171	45
Individual fixed annuities	12	26	—	38	7
Individual variable annuities	1	—	—	1	1
Total	$3,185	$1,020	$(96)	$4,109	$615
Percentage Increase/(Decrease) from Prior Year:					
Life insurance	5%	29%	—%	14%	26%
Personal accident	19	19	—	24	23
Group products	29	29	—	4	(89)
Individual fixed annuities	(67)	31	—	(32)	—
Individual variable annuities	—	—	—	—	—
Total	8%	29%	—%	14%	15%

** Includes the effect of an out of period UCITS adjustment in 2006. For the three-month period ended September 30, 2006, the effect was an increase of $9 million for both net investment income and operating income.*

Total revenues for the three months ended September 30, 2007 increased from the same period in 2006. Premiums and other considerations growth reflects a continued trend toward investment-oriented products where only a portion of policy charges are reported as premiums. Net investment income increased due to growth in assets under management, higher equity dividends in Taiwan and higher policyholder trading gains. In Taiwan, it is customary for most companies to declare and distribute dividends in the third quarter of the calendar year. Dividend income for Taiwan was $129 million and $90 million for the three-month periods ended September 30, 2007 and 2006, respectively. Both net investment income and operating income for the three months ended September 30, 2006 included out of period income related to UCITS of $9 million. Operating income for the three months ended September 30, 2007 improved over the same period in 2006 primarily due to growth in premiums and other considerations, higher investment returns and lower net realized capital losses.

Life insurance premiums and other considerations grew modestly in the three months ended September 30, 2007 compared to the same period in 2006, despite strong growth in both first year and single premium business in the quarter. The strong sales growth, principally in Taiwan, Hong Kong, Thailand and Singapore, was primarily from investment-linked products. In Taiwan, the strong sales growth in the third quarter was due to a combination of sales campaigns and anticipation of regulatory changes related to investment-linked products that will be effective in the fourth quarter of 2007. The shift in product mix from traditional life insurance products to investment-oriented products as mentioned above dampens the growth rate of premiums and other considerations. Net investment income increased in the current period compared to the same period in 2006, due

primarily to the growth in the underlying invested assets, higher equity dividends in Taiwan and higher policyholder trading gains. Both net investment income and operating income for the three months ended September 30, 2006 included out of period income related to UCITS of $9 million. Operating income increased for the three months ended September 30, 2007 compared to the same period in 2006 as a result of growth in revenues and lower net realized capital losses.

Personal accident premiums and other considerations increased primarily due to growth in Korea. Operating earnings reflect the combined effect of premium growth and stable loss ratios and include a benefit of $4 million resulting from SOP 05-1.

Group products premiums and other considerations grew in the three months ended September 30, 2007 compared to the same period in 2006, reflecting higher pension management fees and growth in Australia. Operating income declined from the prior year due to realized capital losses, primarily related to hedging activities.

Individual fixed annuities total revenues and operating income were lower for the three months ended September 30, 2007 compared to the same period in 2006 resulting from net realized capital losses. New production for the three months ended September 30, 2007 increased compared to the same period in 2006, primarily due to new products in Korea, although market demand is shifting to variable annuities.

Year-to-date Asia Results

(in millions)	Premiums and Other Considerations	Net Investment Income	Net Realized Capital Gains (Losses)	Total Revenues	Operating Income
Nine Months Ended September 30, 2007					
Life insurance	**$ 8,479**	**$3,663**	**$ (49)**	**$12,093**	**$1,636**
Personal accident	**1,361**	**111**	**(1)**	**1,471**	**247**
Group products	**510**	**76**	**(68)**	**518**	**21**
Individual fixed annuities	**33**	**90**	**(5)**	**118**	**16**
Individual variable annuities	**2**	**3**	**—**	**5**	**1**
Total	**$10,385**	**$3,943**	**$(123)**	**$14,205**	**$1,921**
Nine Months Ended September 30, 2006					
Life insurance*	$ 8,249	$2,728	$ 95	$11,072	$1,742
Personal accident	1,130	91	—	1,221	222
Group products	380	70	8	458	102
Individual fixed annuities	44	72	2	118	18
Individual variable annuities	1	2	—	3	3
Total	$ 9,804	$2,963	$ 105	$12,872	$2,087
Percentage Increase/(Decrease) from Prior Year:					
Life insurance	3%	34%	—%	9%	(6)%
Personal accident	20	22	—	20	11
Group products	34	9	—	13	(79)
Individual fixed annuities	(25)	25	—	—	(11)
Individual variable annuities	100	50	—	67	(67)
Total	6%	33%	—%	10%	(8)%

** Includes the effect of an out of period UCITS adjustment in 2006. For the nine-month period ended September 30, 2006 the effect was an increase of $208 million and $137 million in net investment income and operating income, respectively.*

Revenues for the first nine months of 2007 were higher than the same period in 2006, but operating income declined compared to the same period in 2006 due to net realized capital losses in 2007 compared to net realized capital gains in 2006 and the positive effect from out of period adjustments in 2006. Premiums and other considerations increased over the same period in 2006, reflecting a continued trend toward investment-oriented products where only a portion of policy charges are reported as premium. Sales of investment-linked life products have been particularly strong in Hong Kong, Korea, Singapore, and more recently in Taiwan. Net investment income grew due to higher policyholder trading gains, higher equity dividends in Taiwan of $41 million and growth in underlying invested assets. Net investment income and operating income for the nine months ended September 30, 2006 included out of period income related to UCITS of $208 million and $137 million, respectively. Net realized capital losses in the current period compared to net realized capital gains in the same period in 2006 reduced the growth rate in revenues and

caused the decline in operating income. The net realized capital losses in the current period were driven primarily by the change in fair value of derivatives that do not qualify for hedge accounting treatment under FAS 133.

Life insurance premiums and other considerations were up slightly in the first nine months of 2007 compared to the same period in 2006, benefiting from improved sales in Thailand and the favorable effect of foreign exchange rates, partially offset by the shift in product mix from traditional life insurance products to investment-oriented products as discussed above. Net investment income grew in the current period compared to the same period in 2006, due primarily to higher policyholder trading gains, the growth in the underlying invested assets and higher equity dividends in Taiwan. Operating income decreased in the first nine months of 2007 compared to the same period in 2006, due to net realized capital losses and the positive effect on prior year operating income from the out of period adjustments discussed above. Operating income for the first nine months of 2007 included a $50 million charge related to balance sheet reconciliation remediation activity.

Personal accident revenues grew for the first nine months of 2007 compared to the same period in 2006 primarily due to higher premiums and other considerations particularly in Korea and Taiwan. Operating earnings reflect the combined effect of premium growth and stable loss ratios and a $10 million positive effect related to SOP 05-1.

Group products premiums and other considerations grew in the first nine months of 2007 compared to the same period in 2006 due to higher pension management fees and sales in the first nine months of 2007 compared to the same period in 2006. Operating income declined in the first nine months of 2007 compared to the same period in 2006, primarily due to net realized capital losses resulting from hedging activities and higher incurred policy losses and benefits of $10 million due to a 2007 out of period reserve charge.

Individual fixed annuities total revenues were unchanged in the first nine months of 2007 compared to the same period in 2006, due primarily to higher investment income, offset by lower premiums and other considerations and realized capital losses in 2007 compared to realized capital gains in 2006. Deposits for the nine months ended September 30, 2007 were flat compared to the same period in 2006 due to increased competition and a market shift to variable life products in Korea.

Domestic Life Insurance Results

Quarterly Domestic Life Insurance Results

Domestic Life Insurance results, presented by sub-product were as follows:

(in millions)	Premiums and Other Considerations	Net Investment Income	Net Realized Capital Gains (Losses)	Total Revenues	Operating Income (Loss)
Three Months Ended September 30, 2007					
Life insurance	**$ 586**	**$375**	**$ (253)**	**$ 708**	**$ (56)**
Home service	**189**	**160**	**(29)**	**320**	**52**
Group life/health	**211**	**48**	**(5)**	**254**	**53**
Payout annuities[(a)]	**494**	**287**	**(10)**	**771**	**(13)**
Individual fixed annuities	**2**	**27**	**5**	**34**	**10**
Individual annuities – runoff[(b)]	**13**	**88**	**(3)**	**98**	**15**
Total	**$1,495**	**$985**	**$ (295)**	**$2,185**	**$ 61**
Three Months Ended September 30, 2006					
Life insurance	$ 546	$347	$ (110)	$ 783	$ 97
Home service	196	167	1	364	87
Group life/health	256	55	(1)	310	19
Payout annuities	414	253	(9)	658	25
Individual fixed annuities	2	21	–	23	8
Individual annuities – runoff[(b)]	10	115	(4)	121	25
Total	$1,424	$958	$ (123)	$2,259	$261
Percentage Increase/(Decrease) from Prior Year:					
Life insurance	7%	8%	–%	(10)%	–%
Home service	(4)	(4)	–	(12)	(40)
Group life/health	(18)	(13)	–	(18)	179
Payout annuities	19	13	–	17	–
Individual fixed annuities	–	29	–	48	25
Individual annuities – runoff[(b)]	30	(23)	–	(19)	(40)
Total	5%	3%	–%	(3)%	(77)%

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

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

Domestic Life Insurance premiums and other considerations increased in the three months ended September 30, 2007 compared to the same period in 2006, primarily due to growth in the life insurance business in force, which includes increased policyholder charges related to interest sensitive whole life product sales, and in payout annuity deposits, reflecting increased sales of single premium immediate annuities and terminal funding annuities. The increase was partially offset by the decline in group life/health premiums and other considerations, primarily due to the exiting of the financial institutions credit life business at the end of 2006, and in home service premiums and other considerations, as the reduction in premiums in force from normal lapses and maturities exceeded sales growth. Domestic Life Insurance operating income decreased in the three months ended September 30, 2007 compared to the same period in 2006. The decrease was primarily driven by higher net realized capital losses which consisted of both losses related to the sales of securities and an increase in other-than-temporary declines related to the fixed income portfolio and derivative losses. Operating income also included a $30 million out of period adjustment to increase group annuity reserves for payout annuities in connection with AIG's continuing remediation efforts. These negative effects were partially offset by growth in the life insurance in-force block of business, increased net investment income, continued improvement in profit margins for the home service business and a $52 million increase primarily related to additional reinsurance recoveries related to Superior National. Offsetting these increases was an $18 million increase in DAC amortization related to SOP 05-1.

Year-to-date Domestic Life Insurance Results

(in millions)	Premiums and Other Considerations	Net Investment Income	Net Realized Capital Gains (Losses)	Total Revenues	Operating Income (Loss)
Nine Months Ended September 30, 2007					
Life insurance	**$1,767**	**$1,149**	**$ (213)**	**$2,703**	**$393**
Home service	**576**	**479**	**(42)**	**1,013**	**200**
Group life/health	**637**	**152**	**(10)**	**779**	**57**
Payout annuities[(a)]	**1,370**	**852**	**(51)**	**2,171**	**55**
Individual fixed annuities	**6**	**78**	**5**	**89**	**22**
Individual annuities – runoff[(b)]	**36**	**286**	**(12)**	**310**	**47**
Total	**$4,392**	**$2,996**	**$ (323)**	**$7,065**	**$774**
Nine Months Ended September 30, 2006					
Life insurance	$1,619	$ 998	$ (77)	$2,540	$485
Home service	593	470	(32)	1,031	212
Group life/health	743	161	(5)	899	30
Payout annuities	1,261	734	(45)	1,950	59
Individual fixed annuities	3	55	(3)	55	14
Individual annuities – runoff[(b)]	35	366	(28)	373	62
Total	$4,254	$2,784	$ (190)	$6,848	$862
Percentage Increase/(Decrease) from Prior Year:					
Life insurance	9%	15%	–%	6%	(19)%
Home service	(3)	2	–	(2)	(6)
Group life/health	(14)	(6)	–	(13)	90
Payout annuities	9	16	–	11	(7)
Individual fixed annuities	100	42	–	62	57
Individual annuities – runoff[(b)]	3	(22)	–	(17)	(24)
Total	3%	8%	–%	3%	(10)%

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

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

Domestic Life Insurance premiums and other considerations increased in the first nine months of 2007 compared to the same period in 2006. The increase was primarily due to the growth in life insurance business in force and payout annuity deposits from increased sales of structured settlements and terminal funding annuities, offset by the effect of exiting the financial institutions credit life business at the end of 2006, tightened pricing and underwriting in the group employer lines and the decline in home service premiums and other considerations. Domestic Life Insurance operating income decreased in the first nine months of 2007 compared to the same period in 2006, primarily due to higher net realized capital losses, offset by an increase in life insurance net investment income from higher partnership income and a positive change from foreign denominated emerging market bonds, higher call and tender income for life insurance and payout annuities operations, a $52 million decrease in policy benefits associated with the Superior National workers compensation reinsurance program described above and a $15 million reduction of certain litigation accruals due to favorable developments on the related matters. Life insurance operating income was also adversely affected by higher

mortality in 2007, although mortality was still within normal ranges. The underlying profit margins on payout annuities continue to trail the increase in payout annuity reserves due to interest spread compression from prior period calls. The higher net realized capital losses consisted primarily of an increase in other-than-temporary declines related to the fixed income portfolio and derivative losses. Operating income for the nine-month period ended September 30, 2007 was also adversely affected by a $30 million out of period adjustment to increase payout annuity reserves related to AIG's continuing remediation efforts and a $57 million increase in DAC amortization related to SOP 05-1, $37 million of which was attributable to group life/health operations. Operating income for the nine-month period ended September 30, 2006 included a $25 million charge for litigation accruals in group life/health operations. Individual annuities — runoff net investment income and operating income decreased for the nine-month period ended September 30, 2007 compared to the same period in 2006 consistent with the declining insurance reserves partially offset by lower realized capital losses.

The following table reflects periodic Domestic Life Insurance sales by product:

(in millions)	Three Months Ended September 30, 2007	Three Months Ended September 30, 2006	Percentage Increase/ (Decrease)	Nine Months Ended September 30, 2007	Nine Months Ended September 30, 2006	Percentage Increase/ (Decrease)
Periodic premium sales by product*:						
Universal life	**$52**	$46	13%	**$150**	$289	(48)%
Variable universal life	**19**	15	27	**44**	42	5
Term life	**53**	59	(10)	**165**	182	(9)
Whole life/other	**2**	3	(33)	**7**	9	(22)
Total	**$126**	$123	2%	**$366**	$522	(30)%

** Periodic premium represents premium from new business expected to be collected over a one-year period.*

Periodic life insurance sales increased slightly for the three months ended September 30, 2007 compared to the same period in 2006 primarily as a result of the increase in indexed universal life sales and the sale of a large private placement variable universal life case. Periodic life insurance sales declined for the nine months ended September 30, 2007 compared to the same period in 2006 primarily as a result of the re-pricing of certain universal life and term products and the tightening of underwriting standards during the second half of 2006.

Domestic Retirement Services Results

Quarterly Domestic Retirement Services Results

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

(in millions)	Premiums and Other Considerations	Net Investment Income	Net Realized Capital Gains (Losses)	Total Revenues	Operating Income
Three Months Ended September 30, 2007					
Group retirement products	**$114**	**$510**	**$(116)**	**$508**	**$120**
Individual fixed annuities	**24**	**828**	**(177)**	**675**	**42**
Individual variable annuities	**159**	**38**	**(22)**	**175**	**41**
Individual annuities – runoff*	**3**	**95**	**(19)**	**79**	**(1)**
Total	**$300**	**$1,471**	**$(334)**	**$1,437**	**$202**
Three Months Ended September 30, 2006					
Group retirement products	$94	$563	$(3)	$654	$267
Individual fixed annuities	30	872	(12)	890	275
Individual variable annuities	132	51	8	191	56
Individual annuities – runoff*	6	111	(17)	100	5
Total	$262	$1,597	$(24)	$1,835	$603
Percentage Increase/(Decrease) from Prior Year:					
Group retirement products	21%	(9)%	–%	(22)%	(55)%
Individual fixed annuities	(20)	(5)	–	(24)	(85)
Individual variable annuities	20	(25)	–	(8)	(27)
Individual annuities – runoff*	(50)	(14)	–	(21)	–
Total	15%	(8)%	–%	(22)%	(67)%

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

Total revenues and operating income for each sub-product group included in Domestic Retirement Services declined for the three months ended September 30, 2007 compared to the same period in 2006, primarily due to increased realized capital losses and lower net investment income. Net realized capital losses for group retirement products and individual fixed annuities increased due to an increase in other-than-temporary impairments and sales to reposition assets in

certain investment portfolios. For individual variable annuities, net realized capital losses were higher in 2007 compared to 2006, primarily due to changes in the value of certain product guarantees and related hedges associated with living benefit features. Net investment income decreased in group retirement and individual fixed annuities primarily due to lower income from partnerships. For individual variable annuities, net investment income was lower in 2007 compared to 2006 resulting from lower balances in the guaranteed fixed income option due to policyholder elections and lower partnership income. These declines were partially offset by an overall increase in variable annuity fees resulting from an increase in assets under management. Individual variable annuity fees also increased due to an increased number of contracts with living benefit features. Individual annuities — runoff operating income declined for the three months ended September 30, 2007 compared to the same period in 2006 due to lower net investment income resulting from decreases in the underlying reserves and lower yield enhancement income.

Year-to-date Domestic Retirement Services Results

(in millions)	Premiums and Other Considerations	Net Investment Income	Net Realized Capital Gains (Losses)	Total Revenues	Operating Income
Nine Months Ended September 30, 2007					
Group retirement products	**$331**	**$1,721**	**$(229)**	**$1,823**	**$661**
Individual fixed annuities	**75**	**2,723**	**(346)**	**2,452**	**606**
Individual variable annuities	**460**	**123**	**(29)**	**554**	**146**
Individual annuities – runoff*	**16**	**294**	**(20)**	**290**	**39**
Total	**$882**	**$4,861**	**$(624)**	**$5,119**	**$1,452**
Nine Months Ended September 30, 2006					
Group retirement products	$284	$1,674	$(116)	$1,842	$724
Individual fixed annuities	93	2,650	(264)	2,479	694
Individual variable annuities	390	153	3	546	143
Individual annuities – runoff*	15	323	(37)	301	27
Total	$782	$4,800	$(414)	$5,168	$1,588
Percentage Increase/(Decrease) from Prior Year:					
Group retirement products	17%	3%	–%	(1)%	(9)%
Individual fixed annuities	(19)	3	–	(1)	(13)
Individual variable annuities	18	(20)	–	1	2
Individual annuities – runoff*	7	(9)	–	(4)	44
Total	13%	1%	–%	(1)%	(9)%

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

Revenues and operating income for Domestic Retirement Services for the first nine months of 2007 declined compared to the same period in 2006 primarily due to increased realized capital losses, partially offset by higher net investment income in group retirement products and individual fixed annuities, and an overall increase in variable annuity fees resulting from the increase in assets under management and more individual variable annuity contracts with living benefit features. Net realized capital losses for Domestic Retirement Services increased due to higher other-than-temporary impairments and sales to reposition assets in certain investment portfolios for both group retirement products and individual fixed annuities, as well as from changes in the value of certain individual variable annuity product guarantees and related hedges associated with living benefit features. The increases in net investment income in group retirement products and individual fixed annuities resulted from higher partnership and yield enhancement income, while net investment income for individual variable annuities was lower in 2007 primarily due to policyholders election to shift from the fixed income option to the variable income option. Operating income for group retirement products and individual fixed annuities decreased for the nine months in 2007 driven by the lower revenues and higher expenses, including higher amortization of DAC for both product groups and higher sales inducement costs for individual fixed annuities. DAC amortization increases for group retirement products were related to the increase in surrenders and policy changes adding guaranteed minimum withdrawal benefit riders to existing contracts. DAC amortization and sales inducement cost increases for individual fixed annuities were related to increased surrenders and an approximately $32 million adjustment reflecting certain changes in actuarial estimates from the conversion to a new DAC system, as well as unlocking future assumptions and experience updates.

Individual annuities — runoff operating income increased in the first nine months of 2007 over the same period of 2006 largely due to lower realized capital losses.

Domestic Retirement Services Supplemental Data

The following table presents deposits*:

(in millions)	Three Months Ended September 30, 2007	Three Months Ended September 30, 2006	Nine Months Ended September 30, 2007	Nine Months Ended September 30, 2006
Group retirement products:				
Annuities	**$1,533**	$1,335	**$ 4,414**	$ 4,083
Mutual funds	**501**	284	**1,296**	1,085
Individual fixed annuities	**993**	1,035	**3,857**	3,770
Individual variable annuities	**1,181**	1,059	**3,393**	3,234
Individual fixed annuities – runoff	**13**	13	**40**	42
Total	**$4,221**	$3,726	**$13,000**	$12,214

** Excludes internal replacements.*

Domestic Retirement Services deposits increased for the three months ended September 30, 2007 compared to the same period in 2006. Group retirement deposits increased 26 percent in the three months ended September 30, 2007 compared to the same period in 2006 as a result of an increase in both group annuity deposits and group mutual funds. Over time, AIG expects that group mutual fund sales will result in a gradual reduction in overall profit margins in this business due to the growth in the lower-margin mutual fund products relative to the annuity products. Individual fixed annuity deposits decreased slightly for the three months ended September 30, 2007 compared to the same period in 2006 as a result of increased competition from bank deposit products and money market funds offering competitive short-term rates in the current yield curve environment. Individual variable annuity deposits increased 12 percent for the three months ended September 30, 2007 compared to the same period in 2006.

Individual fixed annuity surrenders increased 19 percent in the three months ended September 30, 2007 over the same period in 2006 due to policies coming out of their surrender charge periods and increased competition from banks. AIG expects this trend to continue into 2008 as a significant amount of business comes out of its surrender charge period. Individual fixed annuity net flows for the three months ended September 30, 2007 declined compared to the same period in 2006, reflecting the higher surrenders discussed above.

Domestic Retirement Services deposits increased for the first nine months of 2007 compared to the same period in 2006. The increase primarily reflects higher deposits from group retirement products, individual fixed annuities and individual variable annuities. Group retirement deposits increased 10 percent in the first nine months of 2007 compared to the same period in 2006 as a result of an increase in both group variable annuity and group mutual funds deposits, partially offset by slightly lower deposits in group fixed annuities. Although individual fixed annuity sales continued to face increased competition from bank deposit products and money market funds offering very competitive short-term rates in the current yield curve environment, individual fixed annuity deposits increased 2 percent for the nine months ended September 30, 2007 compared to the same period in 2006. Individual variable annuity deposits increased 5 percent in the first nine months of 2007 compared to the same period in 2006 despite the discontinuation of a major bank proprietary product.

Group retirement surrenders increased as a result of normal maturing of the business and due to a few large group surrenders in the first three months of 2007 compared to the same period last year. Individual fixed annuity surrenders increased in the first nine months of 2007 compared to the same period in 2006 due to policies coming out of their surrender charge period and increased competition from banks. Individual fixed annuities net flows for the first nine months of 2007 declined compared to the same period in 2006, reflecting the higher surrenders discussed above, partially offset by slightly higher deposits.

The following table presents Domestic Retirement Services reserves by surrender charge category as of September 30, 2007:

(in millions)	Group Retirement Products*	Individual Fixed Annuities	Individual Variable Annuities
Zero or no surrender charge	$46,193	$ 9,763	$13,142
0% - 2%	6,519	2,835	5,597
Greater than 2% - 4%	3,771	7,904	5,598
Greater than 4%	3,191	27,205	9,348
Non-Surrenderable	875	3,429	92
Total	$60,549	$51,136	$33,777

** Excludes mutual funds of $8.2 billion.*

Surrender rates increased for group retirement products and individual fixed annuities for the first nine months of 2007 compared to the same period in 2006. Surrender rates for group retirement products increased as a result of normal maturing of the business and due to a few large group surrenders in the first nine months of 2007 compared to the same period in 2006. New products and strategies have been introduced to retain assets. The increase in the surrender rate for fixed annuities continues to be driven by a relatively flat yield curve and the general aging of the in-force block; however, less than 20 percent of the individual fixed annuity reserves as of September 30, 2007 were available for surrender without charge. Individual variable annuities surrender rates were slightly lower in the first nine months of 2007 compared to the same period in 2006.

An increase in the level of surrenders in any of these businesses or in the individual fixed annuities runoff block could accelerate the amortization of DAC and negatively affect fee income earned on assets under management.

The following table presents the net flows(a) by line of business:

(in millions)	Three Months Ended September 30, **2007**	2006	Nine Months Ended September 30, **2007**	2006
Group retirement products*(b)*	**$ 319**	$ 158	**$ 453**	$ 793
Individual fixed annuities	**(1,535)**	(1,179)	**(3,047)**	(2,198)
Individual variable annuities	**26**	11	**(59)**	(34)
Individual fixed annuities – runoff	**(213)**	(286)	**(705)**	(772)
Total	**$(1,403)**	$(1,296)	**$(3,358)**	$(2,211)

(a) Net flows are defined as deposits received less benefits, surrenders, withdrawals and death benefits.

(b) Includes mutual funds.

Higher surrenders in the group retirement and individual fixed annuity blocks, offset somewhat by increased deposits on both blocks, resulted in negative net flows for the first nine months of 2007. The continuation of the current interest rate and competitive environment would prolong this trend.

Life Insurance & Retirement Services Net Investment Income and Net Realized Capital Gains (Losses)

The following table summarizes the components of Net investment income:

(in millions)	Three Months Ended September 30, 2007	Three Months Ended September 30, 2006	Nine Months Ended September 30, 2007	Nine Months Ended September 30, 2006
Foreign Life Insurance & Retirement Services:				
Fixed maturities, including short-term investments	**$2,031**	$1,720	**$ 5,846**	$ 4,968
Equity securities	**239**	142	**386**	255
Interest on mortgage, policy and collateral loans	**119**	114	**346**	333
Partnership income	**—**	36	**86**	76
Unit investment trusts[(a)]	**(14)**	28	**107**	223
Other[(b)]	**(42)**	26	**89**	91
Total investment income before policyholder income and trading gains (losses)	**2,333**	2,066	**6,860**	5,946
Policyholder investment income and trading gains (losses)[(c)]	**141**	485	**2,017**	969
Total investment income	**2,474**	2,551	**8,877**	6,915
Investment expenses	**107**	61	**266**	200
Net investment income	**$2,367**	$2,490	**$ 8,611**	$ 6,715
Domestic Life Insurance:				
Fixed maturities, including short-term investments	**$ 865**	$ 864	**$ 2,646**	$ 2,563
Equity securities	**3**	1	**1**	3
Interest on mortgage, policy and collateral loans	**110**	88	**312**	257
Partnership income — excluding Synfuels	**26**	24	**113**	36
Partnership income (loss) — Synfuels	**(26)**	(20)	**(101)**	(79)
Unit investment trusts	**(2)**	2	**2**	2
Other[(b)]	**11**	13	**51**	43
Total investment income before policyholder income and trading gains (losses)	**987**	972	**3,024**	2,825
Policyholder investment income and trading gains (losses)[(c)]	**9**	-	**9**	-
Total investment income	**996**	972	**3,033**	2,825
Investment expenses	**11**	14	**37**	41
Net investment income	**$ 985**	$ 958	**$ 2,996**	$ 2,784
Domestic Retirement Services:				
Fixed maturities, including short-term investments	**$1,325**	$1,404	**$ 4,089**	$ 4,232
Equity securities	**4**	5	**28**	10
Interest on mortgage, policy and collateral loans	**141**	113	**397**	328
Partnership income — excluding Synfuels	**6**	79	**389**	280
Other[(b)]	**9**	10	**1**	(10)
Total investment income	**1,485**	1,611	**4,904**	4,840
Investment expenses	**14**	14	**43**	40
Net investment income	**$1,471**	$1,597	**$ 4,861**	$ 4,800
Total:				
Fixed maturities, including short-term investments	**$4,221**	$3,988	**$12,581**	$11,763
Equity securities	**246**	148	**415**	268
Interest on mortgage, policy and collateral loans	**370**	315	**1,055**	918
Partnership income — excluding Synfuels	**32**	139	**588**	392
Partnership income (loss) — Synfuels	**(26)**	(20)	**(101)**	(79)
Unit investment trusts[(a)]	**(16)**	30	**109**	225
Other[(b)]	**(22)**	49	**141**	124
Total investment income before policyholder income and trading gains (losses)	**4,805**	4,649	**14,788**	13,611
Policyholder investment income and trading gains (losses)[(c)]	**150**	485	**2,026**	969
Total investment income	**4,955**	5,134	**16,814**	14,580
Investment expenses	**132**	89	**346**	281
Net investment income[(d)]	**$4,823**	$5,045	**$16,468**	$14,299

(a) Includes the effect of an out of period UCITS adjustment in 2006. For the three and nine-month periods ended September 30, 2006 the effect was an increase of $24 million and $240 million, respectively, in net investment income and $24 million and $169 million, respectively, in operating income.

(b) Other includes real estate income, income on non-partnership invested assets, securities lending and Foreign Life Insurance & Retirement Services' equal share of the results of AIG Credit Card Company (Taiwan).

(c) Relates principally to assets held in various trading securities accounts that do not qualify for separate account treatment under SOP 03-1. These amounts are offset by an equal change included in incurred policy losses and benefits.

(d) Includes call and tender income.

Net investment income decreased for the three-month period ended September 30, 2007 compared to the same period in 2006. Securities market volatility significantly affected the net investment income results for this quarter as partnership and hedge fund income, UCITS and mutual fund income and policyholder trading gains fell below last year's results. Net

investment income increased for the nine-month period ended September 30, 2007 compared to the same period in 2006. Fixed maturities income rose as the underlying invested asset base grew. Yield enhancement activity increased over the same period in 2006. Earnings on certain interests in UCITS for the first nine months of 2007 were lower than the same period in 2006 as results in 2006 included a $240 million out of period adjustment. Policyholder trading gains (losses) increased for the nine months ended September 30, 2007 compared to the same period in 2006 and generally follow the trend of equity markets in the respective periods. Net investment income for certain operations include investments in structured notes linked to emerging market sovereign debt that incorporates both interest rate risk and currency risk. For 2007, these investments generated income of $1 million and $44 million for the three and nine-month periods ended September 30, 2007, respectively, compared to income of $6 million and losses of $22 million for the same periods in 2006. In addition, period to period comparisons of investment income for some investment activities, particularly partnership income, are affected by yield enhancement activity. See also Insurance and Asset Management Invested Assets herein.

AIG generates income tax credits as a result of investing in synthetic fuel production (synfuels) related to the investment loss shown in the above table and records those benefits separately from segment operating results in its consolidated provision for income taxes. The amounts of those income tax credits were $115 million and $79 million for the first nine months of 2007 and 2006, respectively. For a further discussion of the effect of fluctuating domestic crude oil prices on synfuel tax credits, see Note 6(c) of Notes to Consolidated Financial Statements.

The following table summarizes Net realized capital gains (losses) by major category:

	Three Months Ended September 30,		Nine Months Ended September 30,	
(in millions)	**2007**	2006	**2007**	2006
Foreign Life Insurance & Retirement Services:				
Sales of fixed maturities	**$(122)**	$ (28)	**$ (167)**	$(174)
Sales of equity securities	**205**	14	**417**	415
Other:				
Foreign exchange transactions	**247**	133	**337**	43
Derivatives instruments	**(130)**	(219)	**(195)**	127
Other-than-temporary decline	**(90)**	(33)	**(552)**	(78)
Other[(a)]	**28**	104	**81**	154
Total Foreign Life Insurance & Retirement Services	**$ 138**	$ (29)	**$ (79)**	$ 487
Domestic Life Insurance:				
Sales of fixed maturities	**$ (18)**	$ 1	**$ (57)**	$ (60)
Sales of equity securities	**1**	8	**6**	14
Other:				
Foreign exchange transactions	**5**	(6)	**7**	(6)
Derivatives instruments	**(121)**	(98)	**(91)**	17
Other-than-temporary decline	**(96)**	(24)	**(164)**	(139)
Other[(b)]	**(66)**	(4)	**(24)**	(16)
Total Domestic Life Insurance	**$(295)**	$(123)	**$ (323)**	$(190)
Domestic Retirement Services:				
Sales of fixed maturities	**$ (20)**	$ 19	**$ (80)**	$ (69)
Sales of equity securities	**4**	(8)	**20**	23
Other:				
Foreign exchange transactions	**6**	(13)	**13**	(13)
Derivatives instruments	**(34)**	13	**(81)**	(23)
Other-than-temporary decline	**(148)**	(40)	**(334)**	(301)
Other[(b)]	**(142)**	5	**(162)**	(31)
Total Domestic Retirement Services	**$(334)**	$ (24)	**$ (624)**	$(414)
Total:				
Sales of fixed maturities	**$(160)**	$ (8)	**$ (304)**	$(303)
Sales of equity securities	**210**	14	**443**	452
Other:				
Foreign exchange transactions	**258**	114	**357**	24
Derivative instruments	**(285)**	(304)	**(367)**	121
Other-than-temporary decline	**(334)**	(97)	**(1,050)**	(518)
Other	**(180)**	105	**(105)**	107
Total:	**$(491)**	$(176)	**$(1,026)**	$(117)

(a) Includes losses of $16 million and $15 million for the three-month periods ended September 30, 2007 and 2006, respectively, and losses of $21 million and gains of $33 million for the nine months ended September 30, 2007 and 2006, respectively, allocated to participating policyholders.

(b) Includes losses of $71 million and $130 million for Domestic Life Insurance and Domestic Retirement Services, respectively, for the three and nine-month periods ended September 30, 2007, related to sales to reposition assets in certain investment portfolios.

Net realized capital gains (losses) include normal portfolio transactions as well as derivative gains (losses) for transactions that did not qualify for hedge accounting treatment under FAS 133, foreign exchange gains and losses and other-than-temporary declines in the value of investments. In the first nine months of 2007, Life Insurance & Retirement Services operations incurred losses of $1 billion from the decrease in the value of securities deemed to be other than temporarily impaired. These losses were related to both the decline in value of U.S. dollar bonds held in Thailand and Singapore, which reflects the depreciation of the U.S. dollar against local currencies, and a change in management's intent to hold the securities to recovery, in part, due to the recent volatility in the securities markets. Net realized capital losses in the Foreign Life operations in the first nine months of 2007 include losses of $195 million related to derivatives that did not qualify for hedge accounting treatment compared to a gain of $127 million in the same period in 2006. Derivatives in the Foreign Life operations are primarily used to economically hedge cash flows related to U.S. dollar bonds back to the respective currency of the country, principally in Taiwan, Thailand, and Singapore. The corresponding foreign exchange gain or loss with respect to the economically hedged bond is deferred in accumulated other comprehensive income until the bond is sold or deemed to be other than temporarily impaired.

Deferred Policy Acquisition Costs, Sales Inducement Assets and Future Policy Benefit Reserves

DAC for Life Insurance & Retirement Services products arises from the deferral of those costs that vary with, and are directly related to, the acquisition of new or renewal business. Policy acquisition costs for life insurance products are generally deferred and amortized over the premium paying period of the policy. Policy acquisition costs that relate to universal life and investment-type products, including variable and fixed annuities (investment-oriented products), are deferred and amortized, with interest, as appropriate, in relation to the historical and future incidence of estimated gross profits to be realized over the estimated lives of the contracts. Total acquisition costs deferred increased $138 million in the first nine months of 2007 compared to the first nine months in 2006, primarily due to higher production in the Foreign Life operations partially offset by lower Domestic Life sales. Total amortization expense increased $307 million compared to the first nine months in 2006. Annualized amortization expense levels for 2007 and 2006 are approximately 13 percent of the opening DAC balance.

The following table summarizes the major components of the changes in DAC/Value of Business Acquired (VOBA) and Sales Inducement Assets (SIA):

(in millions)	Nine Months Ended September 30,					
	2007			2006		
	DAC/VOBA	**SIA**	**Total**	DAC/VOBA	SIA	Total
Foreign Life Insurance & Retirement Services						
Balance at beginning of year	**$21,153**	**$ 404**	**$21,557**	$17,638	$ 192	$17,830
Acquisition costs deferred	**4,047**	**99**	**4,146**	3,735	79	3,814
Amortization charged to income or credited to operating income:						
Related to net realized capital gains (losses)	**44**	**—**	**44**	3	—	3
Related to unlocking future assumptions	**53**	**4**	**57**	63	—	63
All other amortization	**(2,141)**	**(12)**	**(2,153)**	(1,894)	(16)	(1,910)
Change in unrealized gains (losses) on securities	**558**	**13**	**571**	232	(2)	230
Increase (decrease) due to foreign exchange	**125**	**4**	**129**	554	9	563
Other *	**68**	**—**	**68**	—	96	96
Balance at end of period	**$23,907**	**$ 512**	**$24,419**	$20,331	$ 358	$20,689
Domestic Life Insurance						
Balance at beginning of year	**$ 6,006**	**$ 46**	**$ 6,052**	$ 5,184	$ 31	$ 5,215
Acquisition costs deferred	**656**	**12**	**668**	856	14	870
Amortization charged to income or credited to operating income:						
Related to net realized capital gains (losses)	**8**	**—**	**8**	20	—	20
All other amortization	**(526)**	**(4)**	**(530)**	(529)	(1)	(530)
Change in unrealized gains (losses) on securities	**197**	**—**	**197**	369	—	369
Increase (decrease) due to foreign exchange	**80**	**—**	**80**	20	—	20
Other *	**(64)**	**—**	**(64)**	—	—	—
Balance at end of period	**$ 6,357**	**$ 54**	**$ 6,411**	$ 5,920	$ 44	$ 5,964
Domestic Retirement Services						
Balance at beginning of year	**$ 5,651**	**$ 887**	**$ 6,538**	$ 5,284	$ 871	$ 6,155
Acquisition costs deferred	**553**	**150**	**703**	522	173	695
Amortization charged to income or credited to operating income:						
Related to net realized capital gains (losses)	**96**	**22**	**118**	58	19	77
Related to unlocking future assumptions	**4**	**(17)**	**(13)**	(1)	—	(1)
All other amortization	**(677)**	**(120)**	**(797)**	(572)	(109)	(681)
Change in unrealized gains (losses) on securities	**314**	**62**	**376**	353	(91)	262
Balance at end of period	**$ 5,941**	**$ 984**	**$ 6,925**	$ 5,644	$ 863	$ 6,507
Total Life Insurance & Retirement Services						
Balance at beginning of year	**$32,810**	**$1,337**	**$34,147**	$28,106	$1,094	$29,200
Acquisition costs deferred	**5,256**	**261**	**5,517**	5,113	266	5,379
Amortization charged to income or credited to operating income:						
Related to net realized capital gains (losses)	**148**	**22**	**170**	81	19	100
Related to unlocking future assumptions	**57**	**(13)**	**44**	62	—	62
All other amortization	**(3,344)**	**(136)**	**(3,480)**	(2,995)	(126)	(3,121)
Change in unrealized gains (losses) on securities	**1,069**	**75**	**1,144**	954	(93)	861
Increase (decrease) due to foreign exchange	**205**	**4**	**209**	574	9	583
Other *	**4**	**—**	**4**	—	96	96
Balance at end of period	**$36,205**	**$1,550**	**$37,755**	$31,895	$1,265	$33,160

** Current year primarily represents the cumulative effect of the adoption of SOP 05-1. Prior year represents a balance sheet reclassification.*

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

Future Policy Benefit Reserves

Periodically, the net benefit reserves (policy benefit reserves less DAC) established for Life Insurance & Retirement Services companies are tested to ensure that, including consideration of future expected premium payments, they are adequate to provide for future policyholder benefit obligations. The assumptions used to perform the tests are

current best-estimate assumptions as to policyholder mortality, morbidity, terminations, company maintenance expenses and invested asset returns. For long duration traditional business, a "lock-in" principle applies, whereby the assumptions used to calculate the benefit reserves and DAC are set when a policy is issued and do not change with changes in actual experience. These assumptions include margins for adverse deviation in the event that actual experience might deviate from these assumptions. For business in force outside of North America, 46 percent of total policyholder benefit liabilities at September 30, 2007 resulted from traditional business where the lock-in principle applies. In most foreign locations, guarantees have been made to pay benefits to policyholders for many decades into the future.

As experience changes over time, the best-estimate assumptions are updated to reflect the observed changes. Because of the long-term nature of many of AIG's liabilities subject to the lock-in principle, small changes in certain of the assumptions may cause large changes in the degree of reserve adequacy. In particular, changes in estimates of future invested asset return assumptions have a large effect on the degree of reserve adequacy.

Taiwan

Beginning in 2000, the yield available on Taiwanese 10-year government bonds dropped from approximately 6 percent to approximately 2.6 percent at September 30, 2007. Yields on most other invested assets have correspondingly dropped over the same period. Current sales are focused on products such as:

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

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

- Observed historical mortality improvement trends have been projected to 2014;
- Morbidity, expense and termination rates have been updated to reflect recent experience;
- Taiwan government bond rates are expected to remain at current levels for 10 years and gradually increase to best estimate assumptions of a market consensus view of long-term interest rate expectations. Foreign assets are assumed to comprise 35 percent of invested assets, resulting in a composite long-term investment assumption of approximately 4.8 percent; and
- The currently permitted practice of offsetting positive mortality experience with negative interest margins, thus eliminating the need for mortality dividends, will continue.

Future results of the reserve adequacy tests involve significant management judgment as to mortality, morbidity, expense and termination rates and investment yields. Changes in these assumptions accelerate DAC amortization and necessitate reserve strengthening.

Financial Services Operations

AIG's Financial Services subsidiaries engage in diversified activities including aircraft and equipment leasing, capital markets, consumer finance and insurance premium finance.

Financial Services Results

Financial Services results were as follows:

(in millions)	Three Months Ended September 30, **2007**	2006	Percentage Increase/ (Decrease)	Nine Months Ended September 30, **2007**	2006	Percentage Increase/ (Decrease)
Revenues:						
Aircraft Leasing[(a)]	**$1,237**	$ 950	30 %	**$3,468**	$3,013	15 %
Capital Markets[(b)(c)]	**540**	1,118	(52)	**701**	30	–
Consumer Finance[(d)(e)]	**992**	901	10	**2,824**	2,768	2
Other, including intercompany adjustments	**16**	42	(62)	**116**	112	4
Total	**$2,785**	$3,011	(8) %	**$7,109**	$5,923	20 %
Operating income (loss):						
Aircraft Leasing[(a)]	**$ 254**	$ 47	440 %	**$ 625**	$ 421	48 %
Capital Markets[(b)(c)]	**370**	965	(62)	**183**	(457)	–
Consumer Finance[(d)(e)]	**69**	151	(54)	**180**	529	(66)
Other, including intercompany adjustments	**(24)**	16	(–)	**20**	48	(58)
Total	**$ 669**	$1,179	(43) %	**$1,008**	$ 541	86 %

(a) Both revenues and operating income include gains (losses) from hedging activities that did not qualify for hedge accounting treatment under FAS 133, including the related foreign exchange gains and losses. For the three-month periods ended September 30, 2007 and 2006, the effect was $(19) million and

$(111) million, respectively. For the nine-month periods ended September 30, 2007 and 2006, the effect was $(32) million and $(56) million, respectively. These amounts result primarily from interest rate and foreign currency derivatives that are effective economic hedges of borrowings. In the second quarter of 2007, ILFC began applying hedge accounting to most of its derivatives hedging interest rate and foreign exchange risks associated with its floating rate and foreign currency denominated borrowings.

(b) Revenues, shown net of interest expense of $1.4 billion and $802 million for the three-month periods ended September 30, 2007 and 2006, respectively, and $3.3 billion and $2.1 billion for the nine-month periods ended September 30, 2007 and 2006, respectively, were primarily from hedged financial positions entered into in connection with counterparty transactions. Both revenues and operating income include gains (losses) from hedging activities that did not qualify for hedge accounting treatment under FAS 133, including the related foreign exchange gains and losses. For the three-month periods ended September 30, 2007 and 2006, the effect was $428 million and $783 million, respectively. For the nine-month periods ended September 30, 2007 and 2006, the effect was $(185) million and $(1.1) billion, respectively. The three and nine-month periods ended September 30, 2007 include out of period charges of $20 million and $346 million, respectively, including a $380 million charge in the nine months ended September 30, 2007 to reverse net gains recognized on transfers of available for sale securities among legal entities consolidated within AIGFP. The three and nine-month periods ended September 30, 2006 include an out of period gain of $115 million and a charge of $223 million, respectively, related to the remediation of the material weakness in accounting for certain derivative transactions under FAS 133. In the first quarter of 2007, AIGFP began applying hedge accounting for certain transactions.

(c) For the three and nine-month periods ended September 30, 2007, both revenues and operating income include an unrealized market valuation loss of $352 million on AIGFP's super senior credit default swap portfolio.

(d) Both revenues and operating income include gains (losses) from hedging activities that did not qualify for hedge accounting treatment under FAS 133, including the related foreign exchange gains and losses. For the three-month periods ended September 30, 2007 and 2006, the effect was $(6) million and $(73) million, respectively. For the nine-month periods ended September 30, 2007 and 2006, the effect was $(21) million and $(65) million, respectively. These amounts result primarily from interest rate and foreign currency derivatives that are effective economic hedges of borrowings. In the second quarter of 2007, AGF began applying hedge accounting to most of its derivatives hedging interest rate and foreign exchange risks associated with its floating rate and foreign currency denominated borrowings.

(e) The nine-month period ended September 30, 2007 includes a pre-tax charge of $178 million in connection with domestic consumer finance's mortgage banking activities.

Financial Services operating income decreased in the three-month period and increased in the nine-month period ended September 30, 2007 compared to the same periods in 2006 primarily due to differences in the accounting treatment for hedging activities. In the first quarter of 2007, AIGFP began applying hedge accounting to certain of its interest rate swaps and foreign currency forward contracts hedging its investments and borrowings. In the second quarter of 2007, AGF and ILFC began applying hedge accounting to most of their derivatives hedging interest rate and foreign exchange risks associated with their floating rate and foreign currency denominated borrowings. During 2006, hedge accounting under FAS 133 was not being applied to any of the derivatives and related assets and liabilities. Accordingly, revenues and operating income were exposed to volatility resulting from differences in the timing of revenue recognition between the derivatives and the related hedged assets and liabilities.

The third quarter and the first nine months of 2007 included out of period charges of $49 million and $346 million, respectively, including a $380 million charge in the nine months ended September 30, 2007 to reverse net gains recognized on transfers of available for sale securities among legal entities consolidated within AIGFP. The three and nine-month periods ended September 30, 2006 included an out of period gain of $115 million and a charge of $223 million related to the remediation of the material weakness in internal control over accounting for certain derivative transactions under FAS 133.

Beginning in the first quarter of 2007, net realized capital gains and losses, including derivative gains and losses and foreign exchange transaction gains and losses for Financial Services entities other than AIGFP, which were previously reported as part of AIG's Other category, are now included in Financial Services revenues and operating income. For the three and nine-month periods ended September 30, 2007, the amount included in both Financial Services revenues and operating income was a loss of $66 million and a loss of $70 million, respectively. All prior periods have been revised to conform to the current presentation.

Aircraft Leasing

Aircraft Leasing operations represent the operations of ILFC, which generates its revenues primarily from leasing new and used commercial jet aircraft to foreign and domestic airlines. Revenues also result from the remarketing of commercial aircraft for ILFC's own account, and remarketing and fleet management services for airlines and financial institutions. ILFC finances its aircraft purchases primarily through the issuance of debt instruments. ILFC economically hedges the majority of its floating rate and foreign currency denominated debt using interest rate and foreign currency derivatives. Starting in the second quarter of 2007, ILFC began applying hedge accounting to most of its derivatives. All of ILFC's derivatives are effective economic hedges; however, since hedge accounting under FAS 133 was not applied prior to April 2, 2007, the benefits of using derivatives to hedge these exposures are not reflected in ILFC's 2006 corporate borrowing rate. The composite borrowing rates at September 30, 2007 and 2006 were 5.28 percent and 5.14 percent, respectively.

ILFC typically contracts to re-lease aircraft before the end of the existing lease term. For aircraft returned before the end of the lease term, ILFC has generally been able to re-lease such aircraft within two to six months of its return. As a lessor, ILFC considers an aircraft "idle" or "off lease" when the aircraft is not subject to a signed lease agreement or

signed letter of intent. ILFC had one aircraft off lease at September 30, 2007, and all but two new aircraft scheduled for delivery through 2008 have been leased.

Quarterly Aircraft Leasing Results

ILFC's operating income increased in the three months ended September 30, 2007 compared to the same period of 2006 by $207 million, or 440 percent. Rental revenues increased by $160 million or 15 percent, driven by a larger aircraft fleet, higher lease rates and higher utilization. As of September 30, 2007, ILFC's fleet subject to operating leases consisted of 894 aircraft compared to 818 aircraft as of September 30, 2006. Flight equipment marketing revenues increased by $12 million in the third quarter of 2007 compared to the same period in 2006 due to higher realization on aircraft sales. During the third quarter of 2007, ILFC realized income of $24 million from the sale of its rights against a bankrupt airline. The increase in revenues was partially offset by increases in depreciation and interest expense. Depreciation expense increased by $42 million, or 10 percent, in line with the increase in the size of the aircraft fleet. Interest expense increased by $20 million, or 5 percent, driven by additional borrowings to fund aircraft purchases and the rising cost of funds. As noted above, ILFC's interest expense did not reflect the benefit of hedging these exposures in 2006. For the three-month periods ended September 30, 2007 and 2006, the losses from hedging activities that did not qualify for hedge accounting treatment under FAS 133, including the related foreign exchange gains and losses, were $19 million and $111 million, respectively, in both revenues and operating income.

Year-to-date Aircraft Leasing Results

ILFC's operating income increased in the first nine months of 2007 compared to the same period in 2006 by $204 million, or 48 percent. Rental revenues increased by $432 million or 15 percent, driven by a larger aircraft fleet and higher lease rates. During the first nine months of 2007, ILFC realized income of $24 million from the sale of its rights against a bankrupt airline. The increase in revenues was partially offset by reduced flight equipment marketing revenues and increases in depreciation and interest expense. Flight marketing revenues decreased by $23 million compared to the same period in 2006 due to fewer aircraft sales. Depreciation expense increased by $133 million, or 11 percent, in line with the increase in the size of the aircraft fleet. Interest expense increased by $162 million, or 15 percent, driven by additional borrowings to fund aircraft purchases and the rising cost of funds. ILFC's interest expense did not reflect the benefit of hedging these exposures in the first quarter of 2007 and in 2006. For the first nine months of 2007 and 2006, the losses from hedging activities that did not qualify for hedge accounting treatment under FAS 133, including the related foreign exchange gains and losses, were $32 million and $56 million, respectively, in both revenues and operating income. During the first nine months of 2006, ILFC recorded adjustments related to a tax settlement in Australia, increased credit reserves and lease accruals totaling $37 million.

Capital Markets

Capital Markets represents the operations of AIGFP, which engages as principal in a wide variety of financial transactions, including standard and customized financial products involving commodities, credit, currencies, energy, equities and rates. AIGFP also invests in a diversified portfolio of securities and principal investments and engages in borrowing activities involving the issuance of standard and structured notes and other securities, and entering into guaranteed investment agreements (GIAs).

Beginning in 2007, AIGFP applied hedge accounting under FAS 133 to certain of its interest rate swaps and foreign currency forward contracts hedging its investments and borrowings. As a result, AIGFP recognized in earnings the change in the fair value on the hedged items attributable to the hedged risks offsetting the gains and losses on the derivatives designated as hedges. Prior to 2007, AIGFP did not apply hedge accounting under FAS 133 to any of its derivatives or related assets and liabilities.

Since 1998, AIGFP has written super senior (AAA+) protection through credit default swaps, a portion of which is exposed to CDOs of residential mortgage-backed securities and other asset-backed securities. AIGFP has structured this portfolio to provide protection such that AIGFP is at risk on only the super senior portion related to a diversified portfolio of credits referenced to loans or debt securities. The super senior risk portion is the last tranche to suffer losses after significant subordination. Credit losses would have to erode all tranches junior to the super senior tranche before AIGFP would have any payment obligation. The subordination level required for each transaction is determined based on internal modeling and analysis of the pool of underlying credits. The subordination levels are not dependent on ratings determined by the rating agencies.

At September 30, 2007, the notional amount of this credit derivative portfolio was $513 billion, covering the following asset classes:

(in billions)	Net Notional Exposure
Corporate	$294
European residential mortgages	141
Multi-sector CDO*	78
Total	$513

* *Approximately $63 billion of the multi-sector CDO pools includes some exposure to U.S. subprime mortgages.*

As of October 31, 2007, all of AIGFP's super senior exposures continued to have tranches below AIGFP's

attachment point that have been explicitly rated AAA or, in AIGFP's judgment, would have been rated AAA had they been rated. AIGFP's portfolio of credit default swaps is carefully structured, undergoes regular monitoring, modeling and analysis and contains significant protection through collateral subordination. In addition, in December 2005, AIGFP stopped committing to writing super senior protection for CDOs that included any U.S. subprime collateral, although collateral managers are permitted to substitute collateral in some of the underlying CDOs, in each case subject to certain restrictions.

AIGFP accounts for the super senior credit default swaps in accordance with FAS 133 "Accounting For Derivative Instruments and Hedging Activities" and Emerging Issues Task Force 02-3, "Issues Involved in Accounting for Derivative Contracts Held for Trading Purposes and Contracts Involved in Energy Trading and Risk Management Activities" (EITF 02-3). In accordance with EITF 02-3, AIGFP does not recognize income in earnings at the inception of each transaction because the inputs to value these instruments are not derivable from observable market data. AIGFP values its super senior credit default swaps using internal methodologies that utilize available market observable information and incorporate management estimates and judgments when information is not available. It also employs the Binomial Expansion Technique (BET) model where appropriate to help estimate the fair value of these derivatives. The BET model utilizes credit spreads for the collateral pool obtained from an independent source. The model also utilizes diversity scores, weighted average lives, recovery rates and discount rates. The BET model does not adequately quantify the benefit of certain structural mitigants, such as triggers that accelerate the amortization of the more senior tranches, that AIGFP believes are important to the appropriate valuation of its transactions. AIG believes that the value of these mitigants could range from zero to $50 million, but is not able to reliably estimate their value at this time. Therefore, AIG's estimate of the fair value of AIGFP's super senior credit default swaps as of September 30, 2007 does not attribute value to these features.

The valuation of the super senior credit derivatives has become increasingly challenging given the limitation on the availability of market observable information due to the lack of trading and price transparency in the structured finance market. These market conditions have increased the reliance on management estimates and judgments in arriving at an estimate of fair value for financial reporting purposes. Further, disparities in the valuation methodologies employed by market participants and the varying judgments reached by such participants when assessing volatile markets has increased the likelihood that the various parties to these instruments may arrive at significantly different estimates as to their fair values.

As of October 31, 2007, AIG is aware that estimates made by certain AIGFP counterparties with respect to the fair value of certain AIGFP super senior credit default swaps and the collateral required in connection with such instruments differ significantly from AIGFP's estimates.

For a further description of AIGFP's risk management practices in its credit default swaps business, see Management's Discussion and Analysis of Financial Condition and Results of Operations — Risk Management — Segment Risk Management — Financial Services in the 2006 Annual Report on Form 10-K.

Quarterly Capital Markets Results

Capital Markets operating income decreased in the three months ended September 30, 2007 by $595 million compared to the same period in 2006, primarily due to changes in accounting related to hedging activities that did not qualify for hedge accounting treatment under FAS 133, as described below. During the third quarter of 2007, AIGFP continued to experience good transaction flow in its rates and currency products which contributed to its revenues. AIGFP recognized total net gains of $153 million for the three months ended September 30, 2007 related to credit default swaps and embedded credit derivatives in credit-linked notes. This gain was offset by an unrealized market valuation loss of $352 million related to AIGFP's super senior credit default swap portfolio, principally written on multi-sector CDOs, and an out of period charge of $51 million for a change in the projected timing of income tax cash flows from a series of lease transactions.

The $352 million unrealized market valuation loss represented a decline in the fair value of super senior credit derivatives for the three-month period ended September 30, 2007, resulting from the significant disruption in the structured finance markets. AIG continues to believe that it is highly unlikely that AIGFP will be required to make payments with respect to these derivatives.

Included in the net gains of $153 million recognized by AIGFP was a net unrealized market valuation gain of $131 million on certain credit default swaps and embedded credit derivatives in credit-linked notes for the three and nine-month periods ended September 30, 2007. In these transactions, AIGFP purchased protection at the AAA to BBB-rated risk layers on portfolios of reference obligations that include multi-sector CDO obligations. This gain was driven by the significant widening in credit spreads during the period. Also included were net gains of $22 million for the three and nine-month periods ended September 30, 2007 on credit derivatives on home equity, CMBS and corporate credits.

In addition, in the three months ended September 30, 2007 AIGFP recognized a net gain of $428 million related to hedging activities that did not qualify for hedge accounting

treatment under FAS 133, compared to a net gain of $783 million for the same period in 2006. The net gain in the three months ended September 30, 2007 reflects the effect of decreases in U.S. interest rates and the weakening of the U.S. dollar on derivatives hedging AIGFP's assets and liabilities. The net gain in the third quarter of 2006 included an out of period charge of $115 million related to the remediation of the material weakness in internal control over accounting for certain derivative transactions under FAS 133.

Financial market conditions in the three months ended September 30, 2007 were characterized by decreases in global interest rates, increases in credit spreads, higher equity valuations and a weaker U.S. dollar.

The most significant component of Capital Markets operating expenses is compensation, which was $136 million and $115 million in the three-month periods ended September 30, 2007 and 2006, respectively. The amount of compensation is not affected by gains and losses arising from derivatives not qualifying for hedge accounting treatment under FAS 133. AIG does not currently intend to have the unrealized market valuation gains and losses described above affect the amount of compensation. Accordingly, compensation expense for the three and nine-month periods does not reflect these amounts.

AIG elected to early adopt FAS 155, "Accounting for Certain Hybrid Financial Instruments" (FAS 155) in 2006 and AIGFP elected to apply the fair value option to certain structured notes and other financial liabilities containing embedded derivatives outstanding as of January 1, 2006. AIGFP recognized a gain of $21 million in the third quarter of 2007 and a gain of $85 million in the third quarter of 2006 on hybrid financial instruments for which it applied the fair value option under FAS 155. These amounts were largely offset by gains and losses on economic hedge positions also reflected in AIGFP's operating income.

Year-to-date Capital Markets Results

Capital Markets operating income increased in the first nine months of 2007 by $640 million compared to the same period in 2006, primarily due to changes in accounting related to hedging activities that did not qualify for hedge accounting treatment under FAS 133, as described below. AIGFP experienced higher transaction flow in the first nine months of 2007 in its rates and currency products. Operating income for the first nine months of 2007 also includes a net unrealized market valuation gain of $131 million related to certain credit default swaps purchased against the AAA to BBB-rated risk layers on portfolios of reference obligations and net gains of $35 million on home equity, CMBS and corporate credit derivatives. These gains were offset by the net unrealized market valuation loss of $352 million and the out of period charge of $51 million, discussed above.

In the first nine months of 2007, AIGFP also recognized a net loss of $185 million related to hedging activities that did not qualify for hedge accounting treatment under FAS 133, compared to a net loss of $1.1 billion for the same period in 2006. The first nine months of 2007 included out of period charges of $346 million, as noted above, including a charge of $380 million to reverse net gains recognized in previous periods on transfers of available for sale securities among legal entities consolidated within AIGFP, and a $166 million reduction in fair value at March 31, 2007 of certain derivatives that are an integral part of, and economically hedge, the structured transactions potentially affected by the proposed regulations issued by the U.S. Treasury Department discussed above in Overview of Operations and Business — Outlook. The net loss on AIGFP's derivatives recognized in the first nine months of 2006 included an out of period charge of $223 million related to the remediation of the material weakness in internal control over accounting for certain derivative transactions under FAS 133. The net loss also reflects the effect of increases in U.S. interest rates and a weakening of the U.S. Dollar on derivatives hedging AIGFP's assets and liabilities.

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

Compensation expense was $412 million and $380 million in the first nine months of 2007 and 2006, respectively.

AIGFP recognized a gain of $51 million in the first nine months of 2007 and a loss of $4 million in the first nine months of 2006 on hybrid financial instruments for which it applied the fair value option under FAS 155. These amounts were largely offset by gains and losses on economic hedge positions also reflected in AIGFP's operating income.

Consumer Finance

AIG's consumer finance operations in North America are principally conducted through AGF. AGF derives a substantial portion of its revenues from finance charges assessed on outstanding real estate loans, secured and unsecured non-real estate loans and retail sales finance receivables. The real estate loans are comprised principally of first-lien mortgages on residential real estate generally having a maximum term of 360 months, and are considered non-conforming. The real estate loans may be closed-end accounts or open-end home equity lines of credit and are principally fixed rate products. AGF does not offer mortgage products with borrower payment options that allow for negative amortization of the principal balance. The secured non-real estate loans are secured by consumer goods, automobiles or other personal property. Both secured and unsecured non-real estate loans and retail sales finance receivables generally have a maximum term of 60 months.

The majority of AGF's finance receivables are sourced through its branches. However, a significant volume of real estate loans is also sourced through its centralized real estate operations, which include its mortgage banking activities. These loans are collateralized by first and second liens on one to four-family properties and are originated largely through broker relationships and to a lesser extent are originated through correspondent relationships and directly to consumers. The majority of these loans are sold to investors on a servicing-released basis. These real estate loans usually have maximum original terms of 360 months, are generally considered non conforming and include fixed, adjustable and hybrid-adjustable loans. From July 2003 through May 2006, AGF's centralized real estate operations originated loans through a servicing arrangement with AIG Federal Savings Bank (AIG Bank), a federally chartered thrift. The origination relationship was terminated in the first quarter of 2006. Since then, all new loans have been originated directly by AGF subsidiaries under their own state licenses.

On June 7, 2007, AIG's domestic consumer finance operations, consisting of AIG Bank, AGF's mortgage banking subsidiary Wilmington Finance, Inc. (WFI) and AGF, entered into a Supervisory Agreement with the Office of Thrift Supervision (OTS). The Supervisory Agreement pertains to certain mortgage loans originated in the name of AIG Bank from July 2003 through early May 2006 pursuant to a servicing agreement between WFI and AIG Bank, which was terminated in February 2006. Pursuant to the terms of the Supervisory Agreement, AIG Bank, WFI and AGF have undertaken a financial remediation program whereby certain borrowers may be provided loans on more affordable terms and/or reimbursed for certain fees. Pursuant to the requirements of the Supervisory Agreement, AGF has engaged the services of an external consultant to monitor, evaluate and periodically report to the OTS with respect to the matters covered by the Supervisory Agreement. Separately, the domestic consumer finance operations also committed to donate $15 million to certain not-for-profit organizations to support their efforts to promote financial literacy and credit counseling.

Management's best estimate of the cost of implementing the financial remediation plan contemplated by the Supervisory Agreement, including the $15 million donation, was $178 million at September 30, 2007. A charge in the amount of $128 million was recorded in the first quarter of 2007 while the remaining $50 million was recorded in the second quarter of 2007 at the time the terms of the Supervisory Agreement were finalized. As the estimate is based on judgments and assumptions made by management, the actual cost of implementing the financial remediation plan may differ from this estimate.

AIG's foreign consumer finance operations are principally conducted through AIG Consumer Finance Group, Inc. (AIGCFG). AIGCFG operates primarily in emerging and developing markets. AIGCFG has operations in Argentina, China, Hong Kong, Mexico, Philippines, Poland, Taiwan and Thailand and most recently began operations in India through the acquisition of a majority interest in a sales finance lending operation during the first quarter of 2007 and the acquisition of a mortgage lending operation in the second quarter of 2007. In addition, AIGCFG expanded its distribution channels in Thailand by acquiring in the first quarter of 2007 an 80 percent interest in a company with a network of over 130 branches for secured consumer lending. AIGCFG is continuously exploring expansion opportunities in its existing operations as well as new geographic locations throughout the world. Certain of the AIGCFG operations are partly or wholly owned by life insurance subsidiaries of AIG. Accordingly, the financial results of those companies are allocated between Financial Services and Life Insurance & Retirement Services according to their ownership percentages. While products vary by market, the businesses generally provide credit cards, unsecured and secured non-real estate loans, term deposits, savings accounts, retail sales finance and real estate loans. AIGCFG originates finance receivables through its branches and direct solicitation. AIGCFG also originates finance receivables indirectly through relationships with retailers, auto dealers, and independent agents.

Quarterly Consumer Finance Results

Consumer Finance operating income decreased by $82 million, or 54 percent, in the three months ended September 30, 2007 compared to the same period in 2006.

The operating income from the domestic consumer finance operations, which include the operations of AGF and AIG Bank, decreased by $68 million, or 49 percent, for the three months ended September 30, 2007 compared to the same period in 2006. For the three months ended September 30, 2007, domestic results were adversely affected by the weakening housing market and tighter underwriting guidelines, which resulted in lower originations of real estate loans.

AGF's net finance receivables totaled $25.4 billion at September 30, 2007, an increase of approximately $1 billion compared to the prior year period, including $19.5 billion of real estate secured loans, most of which were underwritten with full income verification. The increase in the net finance receivables resulted in a similar increase in revenues generated from these assets.

AGF's revenues increased $34 million or 5 percent during the three-month period ended September 30, 2007 compared to the same period in 2006. Revenues from AGF's mortgage banking activities decreased $68 million or 87 percent during the three-month period ended September 30, 2007 compared to the same period in 2006. The decrease in revenues was primarily caused by a

significantly reduced origination volume, and to a lesser extent, tighter underwriting guidelines, reduced third party margins and higher warranty reserves, which cover obligations to repurchase loans sold to third-party investors should there be a first payment default or breach of representations and warranties.

AGF's interest expense increased by $9 million or 3 percent as its long-term borrowing rate increased in the three months ended September 30, 2007 compared to the same period in 2006. During the three months ended September 30, 2007, AGF recorded a net loss of $5 million on its derivatives that did not qualify for hedge accounting under FAS 133, including the related foreign exchange losses, compared to a net loss of $67 million for the same period in 2006. Commencing in the second quarter of 2007, AGF began applying hedge accounting.

Revenues from the foreign consumer finance operations increased by approximately 32 percent to $232 million in the three months ended September 30, 2007 compared to the same period in 2006. Loan growth, particularly in Poland, Thailand and Latin America, was the primary driver of the higher revenues. The increase in revenues was more than offset by higher expenses associated with branch expansions, acquisition activities and product promotion campaigns.

Year-to-date Consumer Finance Results

Consumer Finance operating income decreased by $349 million, or 66 percent, in the first nine months of 2007 compared to the same period in 2006.

The operating income for the first nine months of 2007 from the domestic consumer finance operations decreased by $379 million or 72 percent from the same period of 2006. Pursuant to the terms of the Supervisory Agreement, as discussed above, charges of $178 million were recorded during the first nine months of 2007.

Additionally, for the first nine months of 2007, domestic results were adversely affected by the weakening housing market and tighter underwriting guidelines, which resulted in lower originations for real estate loans.

Although mortgage loan originations declined in the first nine months of 2007, the softening of home price appreciation (reducing the equity customers may be able to extract from their homes by refinancing) contributed to an increase in non-real estate loans of 12 percent at September 30, 2007 compared to September 30, 2006. Retail sales finance receivables also increased 19 percent compared to September 30, 2006 due to increased marketing efforts and customer demand. AGF's centralized real estate business segment finance receivables decreased by 2 percent while branch business segment finance receivables increased by 9 percent. AGF's results for the first nine months of 2007 also included a recovery of $65 million from a favorable out of court settlement.

AGF's revenues decreased $69 million or 3 percent for the nine-month period ended September 30, 2007 compared to the same period in 2006. Revenues from AGF's mortgage banking activities decreased $306 million or 152 percent during the nine-month period ended September 30, 2007 compared to the same period in 2006, which also reflects charges relating to the Supervisory Agreement. The decrease in revenues was primarily caused by significantly reduced origination volume, and to a lesser extent, tighter underwriting guidelines, a shift in distribution channels, and higher warranty reserve, which covers AGF's obligations to repurchase loans sold to third-party investors should there be a first payment default or breach of representations and warranties.

AGF's interest expense increased by $73 million or 8 percent as both its short-term and long-term borrowing rates increased in the first nine months of 2007 compared to the same period in 2006. Its short-term borrowing rates averaged 5.40 percent in the first nine months of 2007 compared to 5.06 percent in the same period of 2006, while long-term borrowing rates averaged 5.19 percent in the first nine months of 2007 compared to 4.97 percent in the first nine months of 2006.

For the first nine months of 2007, domestic consumer finance revenues and operating income also declined from the prior year, partially due to the change in fair value of the derivatives hedging borrowings which did not qualify for hedge accounting treatment under FAS 133 during either period. During the first nine months of 2007, AGF recorded a net loss of $24 million on such derivatives, including the related foreign exchange losses, compared to a net loss of $63 million for the same period in 2006.

Revenues from the foreign consumer finance operations increased by 25 percent in the first nine months of 2007 compared to the same period of 2006. Loan growth, particularly in Poland, Thailand and Latin America, was the primary driver of the increased revenues. The increase in revenues were more than offset by higher expenses associated with branch expansions, acquisition activities and product promotion campaigns. Operating income in the first nine months of 2006 reflects AIGCFG's $44 million share of the allowance for losses related to industry-wide credit deterioration in the Taiwan credit card market.

Credit Quality of Finance Receivables

The overall credit quality of AGF's finance receivables portfolio deteriorated modestly due to negative economic fundamentals, a higher proportion of non-real estate loans and retail sales finance loans and the aging of the real estate loan portfolio.

As of September 30, 2007, the 60-day delinquency rate for the entire portfolio increased by 55 basis points to 2.47 percent compared to the same period in 2006, while the 60-day delinquency rate for the real estate loans increased by 63 basis points to 2.22 percent. For the three months ended September 30, 2007, AGF's net charge-off rate increased to 1.15 percent compared to 0.92 percent for the same period in 2006 and for the nine months ended September 30, 2007 increased to 1.05 percent compared to 0.89 percent for the same period in 2006, which reflected $6 million of non-recurring recoveries recorded in the first quarter of 2006.

AGF's allowance for finance receivables losses as a percentage of outstanding receivables was 2.11 percent at September 30, 2007 compared to 1.99 percent at September 30, 2006.

Asset Management Operations

AIG's Asset Management operations comprise a wide variety of investment-related services and investment products. Such services and products are offered to individuals and institutions both domestically and overseas, and are primarily comprised of Spread-Based Investment Businesses, Institutional Asset Management and Brokerage Services and Mutual Funds.

The revenues and operating income for this segment are affected by the general conditions in the equity and credit markets. In addition, net realized gains and performance fees are contingent upon various fund closings, maturity levels and market conditions.

Spread-Based Investment Business

In prior years, the sale of GICs to investors, both domestically and overseas, was AIG's primary institutional Spread-Based Investment Business. During 2005, AIG launched its MIP and its asset management subsidiaries, primarily SunAmerica Life, ceased writing new GIC business. The GIC business will continue to run off for the foreseeable future while the MIP business is expected to grow.

Institutional Asset Management

AIG's Institutional Asset Management business provides an array of investment products and services globally to institutional investors, AIG subsidiaries and affiliates and high net worth investors. These products and services include traditional equity and fixed income investment management and a full range of alternative asset classes. Delivery of AIG's Institutional Asset Management products and services is accomplished via a global network of operating subsidiaries comprising AIG Global Asset Management Holdings Corp. and its subsidiaries and affiliated companies (collectively, AIG Investments). The primary operating entities within this group are AIG Global Investment Corp., AIG Global Real Estate Investment Corp. and AIG Private Bank. AIG Private Bank offers banking, trading and investment management services to private client and high net worth individuals and institutions globally.

Within the alternative investment asset class, AIG Investments offers hedge and private equity fund-of-funds, direct investments and distressed debt investments. Within the structured fixed income and equity product asset class, AIG Investments offers various forms of structured and credit linked notes, various forms of collateralized debt obligations and other investment strategies aimed at achieving superior returns or capital preservation.

From time to time, AIG Investments acquires alternative investments, primarily consisting of direct private equity investments, on a temporary basis, ''warehousing'' such investments until the investment or economic benefit thereof is transferred to a fund or other AIG managed investment product. As a consequence of this warehousing activity, AIG incurs the cost of carrying these investments and consolidates the balance sheet and operating results until the new managed investment product is launched.

Brokerage Services and Mutual Funds

AIG's Brokerage Services and Mutual Funds business provides mutual fund and broker-dealer related services to retail investors, group trusts and corporate accounts through an independent network of financial advisors. The AIG Advisor Group, Inc., a subsidiary of AIG Retirement Services, Inc., is comprised of several broker-dealer entities that provide these services to clients primarily in the U.S. marketplace. AIG SunAmerica Asset Management Corp. manages, advises and/or administers retail mutual funds, as well as the underlying assets of variable annuities sold by AIG SunAmerica and VALIC to individuals and groups throughout the United States.

Other

Included in the Other category for Asset Management is income or loss from certain SunAmerica sponsored partnerships and partnership investments. Partnership assets consist of investments in a diversified portfolio of private equity funds, affordable housing partnerships and hedge fund investments.

Asset Management Results

Asset Management results were as follows:

(in millions)	Three Months Ended September 30, **2007**	2006	Percentage Increase/ (Decrease)	Nine Months Ended September 30, **2007**	2006	Percentage Increase/ (Decrease)
Revenues:						
Spread-Based Investment Business	**$ 555**	$ 552	1%	**$2,304**	$1,924	20%
Institutional Asset Management:						
Institutional Asset Management	**362**	255	42	**1,635**	883	85
Consolidated Managed Partnerships & Funds	**300**	58	417	**765**	422	81
Consolidated Warehouse Investments	**458**	–	–	**465**	–	–
Total Institutional Asset Management	**1,120**	313	258	**2,865**	1,305	120
Brokerage Services and Mutual Funds	**83**	71	17	**243**	217	12
Other	**66**	57	16	**309**	201	54
Total	**$1,824**	$ 993	84%	**$5,721**	$3,647	57%
Operating income:						
Spread-Based Investment Business	**$ 24**	$ 44	(45)%	**$ 759**	$ 467	63%
Institutional Asset Management:						
Institutional Asset Management	**49**	46	7	**737**	311	137
Consolidated Managed Partnerships & Funds	**293**	44	566	**748**	410	82
Consolidated Warehouse Investments*	**(39)**	–	–	**(79)**	–	–
Total Institutional Asset Management	**303**	90	237	**1,406**	721	95
Brokerage Services and Mutual Funds	**27**	23	17	**74**	67	10
Other	**65**	54	20	**302**	190	59
Total	**$ 419**	$ 211	99%	**$2,541**	$1,445	76%

** Includes operating costs as well as the cost of funding these investments.*

Asset Management revenues and operating income increased in the three and nine-month periods ended September 30, 2007 compared to the same periods in 2006 due to the effect of consolidated managed partnerships and funds, consolidated warehouse investments and, for the first nine months of 2007, a gain of $398 million from the sale of a portion of AIG's investment in Blackstone Group, LP in connection with its initial public offering. Income arising from consolidated managed partnerships and funds is included in operating income, but offset in minority interest expense, which is not a component of operating income. Offsetting the increase in revenues is an operating loss due to the effect of consolidating the operating results of warehoused investments for the three and nine-month periods ended September 30, 2007. AIG expects to divest the consolidated warehouse investments through various managed investment products in future periods.

Beginning in the first quarter of 2007, net realized capital gains and losses, including derivative gains and losses and foreign exchange transaction gains and losses, which were previously reported as part of AIG's Other category, are now included in Asset Management revenues and operating income. For the three and nine-month periods of 2007, the amount included in both Asset Management revenues and operating income was a loss of $232 million and a gain of $100 million, respectively. The three and nine-month periods of 2006 reflected losses of $106 million and $109 million, respectively. All prior periods have been revised to conform to the current presentation.

In order to better align financial reporting with the manner in which AIG's chief operating decision makers have managed their businesses, commencing in the first quarter of 2007, revenues and operating income related to foreign investment contracts, which were historically reported as a component of the Spread-Based Investment business, are now being reported in the Life Insurance & Retirement Services segment. All prior periods have been revised to conform to the current presentation.

Quarterly Spread-Based Investment Business Results

Operating income related to the Spread-Based Investment business decreased in the three months ended September 30, 2007 compared to the same period in 2006 due to losses associated with the MIP. MIP operating income decreased during the three months ended September 30, 2007 compared to the same period of 2006 primarily due to foreign exchange losses on foreign-denominated debt that, while economically hedged, did not qualify for hedge accounting treatment under FAS 133, as well as other than temporary write-downs on certain investments and mark to market losses on derivatives that did not qualify for hedge accounting treatment under FAS 133. These losses are partially offset by an increase in partnership income associated with the GIC program and higher income from private equity partnerships. Partnership income is primarily

derived from alternative investments and is affected by performance in the equity and credit markets. Thus, revenues, operating income and cash flows attributable to GICs will vary from reporting period to reporting period.

As anticipated, GIC balances continue to run off. A significant portion of the remaining GIC portfolio consists of floating rate obligations. AIG has entered into hedges to manage against increases in short-term interest rates. AIG believes these hedges are economically effective, but they did not qualify for hedge accounting treatment under FAS 133. Income or loss from these hedges are classified as net realized capital gains or losses in the Asset Management segment results.

The following table illustrates the anticipated runoff of the domestic GIC portfolio at September 30, 2007:

(in billions)	Less Than One Year	1-3 Years	3+-5 Years	Over Five Years	Total
Domestic GICs	$ 4.8	$ 11.9	$ 2.7	$ 6.7	$ 26.1

During 2005, the MIP replaced the GIC program as AIG's principal institutional spread-based investment activity. AIG does not expect that income growth in the MIP will offset the runoff in the GIC portfolio for the foreseeable future because the asset mix under the MIP does not include the alternative investments utilized in the GIC program. Commencing in the first quarter of 2007, AIG applied hedge accounting for certain derivative transactions related to the MIP.

Year-to-date Spread-Based Investment Business Results

Operating income related to the Spread-Based Investment business increased in the first nine months of 2007 compared to the same period in 2006 due to a significant increase in partnership income associated with the Domestic GIC program. Partnership income in the first nine months of 2007 included a distribution from a single partnership of $164 million, which became available after a five-year restriction on capital withdrawals.

MIP operating income decreased in the first nine months of 2007 compared to the same period in 2006, reflecting foreign exchange losses on foreign-denominated debt that, while economically hedged, did not qualify for hedge accounting treatment under FAS 133, as well as other-than-temporary write-downs on certain investments and mark to market losses on derivatives not receiving hedge accounting treatment. Through September 30, 2007, AIG has issued the equivalent of $6.8 billion of securities to fund the MIP in the Euromarkets and the U.S. public and private markets.

Quarterly Institutional Asset Management Results

Operating income for Institutional Asset Management increased in the three months ended September 30, 2007 compared to the same period in 2006, due to higher asset management fees resulting from growth in assets under management; an increase in carried interest, which was driven by higher valuations of portfolio investments and is generally associated with improved equity markets performance; and increased income from consolidated managed partnerships and funds, which are offset in minority interest expense that is not a component of operating income. These increases were partially offset by the effect of consolidating the operating results of various warehoused investments, an increase in distribution expenses related to the launch of several new investment products and the timing of real estate sales compared to the year ago quarter.

Year-to-date Institutional Asset Management Results

Operating income for Institutional Asset Management increased in the first nine months of 2007 compared to the same period in 2006 reflecting the $398 million gain from the sale of a portion of AIG's investment in Blackstone Group, LP in connection with its initial public offering and increased carried interest driven by higher valuations of portfolio investments which are generally associated with improved performance in the equity markets. Operating income also reflects higher income from certain consolidated managed partnerships and funds; however, this income is offset in minority interest expense. Partly offsetting this income was a decrease in net realized capital gains related to real estate investments as well as increased expenses resulting from investment in sales and infrastructure enhancements and the effect of consolidating the operating results of various warehoused investments.

AIG's unaffiliated client assets under management, including retail mutual funds and institutional accounts, increased 24 percent to $93.1 billion from December 31, 2006 to September 30, 2007, contributing to growth in base management fees. Additionally, AIG Investments successfully launched several new private equity and real estate funds in the first nine months of 2007, which provide both a base management fee and the opportunity for future performance fees.

While unaffiliated client assets under management and the resulting management fees continue to increase, the growth in operating income has trailed the growth in revenues due to additional warehousing activities as well as the costs associated with sales and infrastructure enhancements. The sales and infrastructure enhancements are associated with AIG's planned expansion of marketing and distribution capabilities, combined with technology and operational infrastructure-related improvements.

Other Operations

The operating loss of AIG's Other category was as follows:

(in millions)	Three Months Ended September 30, **2007**	2006	Nine Months Ended September 30, **2007**	2006
Other operating income (loss):				
Equity earnings in unconsolidated entities	**$ 37**	$ 48	**$ 128**	$ 178
Interest expense	**(315)**	(227)	**(869)**	(633)
Unallocated corporate expenses*	**(157)**	(89)	**(519)**	(337)
Compensation expense – SICO Plans	**(9)**	(14)	**(29)**	(104)
Compensation expense – Starr tender offer	**–**	–	**–**	(54)
Net realized capital gains (losses)	**(199)**	85	**(226)**	31
Other miscellaneous, net	**16**	11	**(42)**	(34)
Total Other	**$(627)**	$(186)	**$(1,557)**	$(953)

** Includes expenses of corporate staff not attributable to specific business segments, expenses related to efforts to improve internal controls, corporate initiatives and certain compensation plan expenses.*

The operating loss of AIG's Other category increased in the third quarter and first nine months of 2007 compared to the comparable periods in 2006, reflecting higher interest expenses resulting from increased borrowings, higher unallocated corporate expenses and foreign exchange losses on foreign-denominated debt of which a portion is economically hedged, but did not qualify for hedge accounting treatment under FAS 133.

Operating loss for the first nine months of 2006 included an out of period charge of $61 million related to the SICO Plans and a one-time charge related to the Starr tender offer of $54 million.

Beginning in the first quarter of 2007, derivative gains and losses and foreign exchange transaction gains and losses for Asset Management and Financial Services entities (other than AIGFP) are now included in Asset Management and Financial Services revenues and operating income. These amounts were previously reported as part of AIG's Other category. All prior periods have been revised to conform to the current presentation.

Capital Resources and Liquidity

Borrowings

At September 30, 2007, AIG's total borrowings amounted to $176.2 billion as follows:

(in millions)	**September 30, 2007**	December 31, 2006
AIG's net borrowings	**$ 20,299**	$ 17,126
Junior subordinated debt	**4,681**	–
Liabilities connected to trust preferred stock	**1,440**	1,440
MIP matched notes and bonds payable	**12,754**	5,468
Series AIGFP matched notes and bonds payable	**530**	72
AIGFP		
GIAs	**19,495**	20,664
Matched notes and bonds payable	**41,552**	35,776
Hybrid financial instrument liabilities*	**7,692**	8,856
Borrowings not guaranteed by AIG	**67,742**	59,277
Total	**$176,185**	$148,679

** Represents structured notes issued by AIGFP that are accounted for using the fair value option.*

Borrowings issued or guaranteed by AIG and subsidiary borrowings not guaranteed by AIG were as follows:

(in millions)	**September 30, 2007**	December 31, 2006
AIG borrowings:		
Notes and bonds payable	**$ 10,784**	$ 8,915
Junior subordinated debt	**4,681**	–
Loans and mortgages payable	**210**	841
MIP matched notes and bonds payable	**12,754**	5,468
Series AIGFP matched notes and bonds payable	**530**	72
Total AIG Borrowings	**28,959**	15,296
Borrowings guaranteed by AIG:		
AIGFP		
GIAs	**19,495**	20,664
Notes and bonds payable	**44,215**	37,528
Hybrid financial instrument liabilities[(a)]	**7,692**	8,856
Total	**71,402**	67,048
AIG Funding, Inc. commercial paper	**5,845**	4,821
AIGLH Notes and bonds payable	**797**	797
Liabilities connected to trust preferred stock	**1,440**	1,440
Total borrowings issued or guaranteed by AIG	**108,443**	89,402
Borrowings not guaranteed by AIG:		
ILFC		
Commercial paper	**3,818**	2,747
Junior subordinated debt	**999**	999
Notes and bonds payable[(b)]	**26,904**	25,592
Total	**31,721**	29,338
AGF		
Commercial paper	**5,229**	4,328
Junior subordinated debt	**349**	–
Notes and bonds payable	**18,998**	19,595
Total	**24,576**	23,923
AIGCFG		
Commercial paper	**177**	227
Loans and mortgages payable	**1,534**	1,453
Total	**1,711**	1,680

(in millions)	**September 30, 2007**	December 31, 2006
AIG Finance Taiwan Limited commercial paper	**15**	26
Other Subsidiaries	**753**	672
Borrowings of consolidated investments:		
A.I. Credit	**881**	880
AIG Investments	**3,364**	193
AIG Global Real Estate Investment	**4,523**	2,307
AIG SunAmerica	**193**	203
ALICO	**5**	55
Total	**8,966**	3,638
Total borrowings not guaranteed by AIG	**67,742**	59,277
Total Debt	**$176,185**	$148,679

(a) Represents structured notes issued by AIGFP that are accounted for using the fair value option.

(b) Includes borrowings under Export Credit Facility of $2.7 billion at September 30, 2007 and $2.7 billion at December 31, 2006.

The debt activity, excluding commercial paper and extendible commercial notes of $15.08 billion and borrowings of consolidated investments of $8.97 billion, for the nine months ended September 30, 2007 was as follows:

(in millions)

	Balance at December 31, 2006	Issuances	Maturities and Repayments	Effect of Foreign Exchange	Other Changes	**Balance at September 30, 2007**
AIG						
Notes and bonds payable	$ 8,915	$ 1,759	$ (65)	$ 110	$ 65	**$ 10,784**
Junior subordinated debt	–	4,490	–	191	–	**4,681**
Loans and mortgages payable	841	82	(724)	11	–	**210**
MIP matched notes and bonds payable	5,468	6,835	–	94	357	**12,754**
Series AIGFP matched notes and bonds payable	72	457	–	–	1	**530**
AIGFP						
GIAs	20,664	6,430	(7,545)	–	(54)	**19,495**
Notes and bonds payable and hybrid financial instrument liabilities	46,384	36,045	(31,118)	508	88	**51,907**
AIGLH notes and bonds payable	797	–	–	–	–	**797**
Liabilities connected to trust preferred stock	1,440	–	–	–	–	**1,440**
ILFC notes and bonds payable	25,592	3,748	(2,811)	371	4	**26,904**
ILFC junior subordinated debt	999	–	–	–	–	**999**
AGF notes and bonds payable	19,595	3,199	(3,829)	226	(193)	**18,998**
AGF junior subordinated debt	–	346	–	–	3	**349**
AIGCFG loans and mortgages payable	1,453	2,541	(2,510)	50	–	**1,534**
Other subsidiaries	672	21	(30)	(3)	93	**753**
Total	$132,892	$65,953	$(48,632)	$ 1,558	$ 364	**$ 152,135**

AIG (Parent Company)

AIG intends to continue its customary practice of issuing debt securities from time to time to meet its financing needs and those of certain of its subsidiaries for general corporate purposes, as well as for the MIP. As of September 30, 2007, AIG had up to $21.9 billion of debt securities, preferred stock and other securities, and up to $16.5 billion of common stock, registered and available for issuance under its universal shelf registration statement.

AIG maintains a medium term note program under its shelf registration statement. As of September 30, 2007, approximately $4.2 billion principal amount of notes were outstanding under the medium term note program, of which $749 million was used for AIG's general corporate purposes, $529 million was used by AIGFP and $3.0 billion was used to fund the MIP. The maturity dates of these notes range from 2008 to 2052. To the extent deemed appropriate, AIG may enter into swap transactions to manage its effective borrowing rates with respect to these notes.

AIG also maintains a Euro medium term note program under which, as of September 30, 2007, an aggregate nominal amount of up to $20.0 billion of notes may be outstanding at any one time. As of September 30, 2007, the equivalent of $10.9 billion of notes were outstanding under the program, of which $8.4 billion were used to fund the MIP and the remainder was used for AIG's general corporate purposes. The aggregate amount outstanding includes $839 million loss resulting from foreign exchange translation into U.S. dollars, of which $288 million loss relates to notes

issued by AIG for general corporate purposes and $551 million loss relates to notes issued to fund the MIP.

During the first nine months of 2007, AIG issued in Rule 144A offerings an aggregate of $2.0 billion principal amount of senior notes, of which $650 million was used to fund the MIP and $1.4 billion was used for AIG's general corporate purposes.

AIG maintains a shelf registration statement in Japan, providing for the issuance of up to Japanese Yen 300 billion principal amount of senior notes, of which the equivalent of $434 million was outstanding as of September 30, 2007, the proceeds of which were used for AIG's general corporate purposes. AIG also maintains an Australian dollar debt program under which senior notes with an aggregate principal amount of up to 5 billion Australian dollars may be outstanding at any one time. Although as of September 30, 2007 there were no outstanding notes under the Australian program, AIG intends to use the program opportunistically to fund the MIP or for AIG's general corporate purposes.

During the first nine months of 2007, AIG issued an aggregate of $4.49 billion of junior subordinated debentures in four series of securities. Substantially all of the proceeds from these sales, net of expenses, are being used to repurchase shares of AIG's common stock. In connection with each series of junior subordinated debentures, AIG entered into a Replacement Capital Covenant (RCC) for the benefit of the holders of AIG's 6.25 percent senior notes due 2036. The RCCs provide that AIG will not repay, redeem, or purchase the applicable series of junior subordinated debentures on or before a specified date, unless it has received qualifying proceeds from the sale of replacement capital securities.

AIG began applying hedge accounting for certain AIG parent transactions in the first quarter of 2007.

AIGFP

AIGFP uses the proceeds from the issuance of notes and bonds and GIA borrowings to invest in a diversified portfolio of securities and derivative transactions. The borrowings may also be temporarily invested in securities purchased under agreements to resell. AIGFP's notes and bonds include structured debt instruments whose payment terms are linked to one or more financial or other indices (such as an equity index or commodity index or another measure that is not considered to be clearly and closely related to the debt instrument). These notes contain embedded derivatives that otherwise would be required to be accounted for separately under FAS 133. Upon AIG's early adoption of FAS 155, AIGFP elected the fair value option for these notes. The notes that are accounted for using the fair value option are reported separately under hybrid financial instrument liabilities. AIG guarantees the obligations of AIGFP under AIGFP's notes and bonds and GIA borrowings. See Operating Review – Financial Services Operations, Liquidity and Derivatives herein.

AIGFP has a Euro medium term note program under which, as of September 30, 2007, an aggregate nominal amount of up to $20.0 billion of notes may be outstanding at any one time. As of September 30, 2007, $7.18 billion of notes were outstanding under the program, including $899 million loss resulting from foreign exchange translation into U.S. dollars. The notes issued under this program are guaranteed by AIG and are included in AIGFP's Notes and Bonds Payable in the preceding table of borrowings.

AIG Funding

AIG Funding, Inc. (AIG Funding) issues commercial paper that is guaranteed by AIG in order to help fulfill the short-term cash requirements of AIG and its subsidiaries. The issuance of AIG Funding's commercial paper, including the guarantee by AIG, is subject to the approval of AIG's Board of Directors or the Finance Committee of the Board if it exceeds certain pre-approved limits.

As backup for the commercial paper program and for other general corporate purposes, AIG and AIG Funding maintain revolving credit facilities, which, as of September 30, 2007, had an aggregate of $9.2 billion available to be drawn and which are summarized below under Revolving Credit Facilities.

ILFC

ILFC fulfills its short-term cash requirements through operating cash flows and the issuance of commercial paper. The issuance of commercial paper is subject to the approval of ILFC's Board of Directors and is not guaranteed by AIG. ILFC maintains syndicated revolving credit facilities which, as of September 30, 2007, totaled $6.5 billion and which are summarized below under Revolving Credit Facilities. These facilities are used as back up for ILFC's maturing debt and other obligations.

As a well-known seasoned issuer, ILFC has filed an automatic shelf registration statement with the SEC allowing ILFC immediate access to the U.S. public debt markets. At September 30, 2007, $4.65 billion of debt securities had been issued under this registration statement and $5.89 billion had been issued under a prior registration statement. In addition, ILFC has a Euro medium term note program for $7.0 billion, under which $4.28 billion in notes were outstanding at September 30, 2007. Notes issued under the Euro medium term note program are included in ILFC notes and bonds payable in the preceding table of borrowings. The cumulative foreign exchange adjustment loss for the foreign currency denominated debt was $1.1 billion at September 30, 2007 and $733 million at December 31, 2006. ILFC has substantially eliminated the currency exposure arising from foreign currency denominated notes by economically hedging

the portion of the note exposure not already offset by Euro-denominated operating lease payments.

ILFC had a $4.3 billion Export Credit Facility for use in connection with the purchase of approximately 75 aircraft delivered through 2001. This facility was guaranteed by various European Export Credit Agencies. The interest rate varies from 5.75 percent to 5.90 percent on these amortizing ten-year borrowings depending on the delivery date of the aircraft. At September 30, 2007, ILFC had $748 million outstanding under this facility. The debt is collateralized by a pledge of the shares of a subsidiary of ILFC, which holds title to the aircraft financed under the facility.

In May 2004, ILFC entered into a similarly structured Export Credit Facility for up to a maximum of $2.64 billion for Airbus aircraft to be delivered through May 31, 2005. The facility was subsequently increased to $3.64 billion and extended to include aircraft to be delivered through May 31, 2008. The facility becomes available as the various European Export Credit Agencies provide their guarantees for aircraft based on a nine-month forward-looking calendar, and the interest rate is determined through a bid process. At September 30, 2007, ILFC had $1.9 billion outstanding under this facility. Borrowings with respect to these facilities are included in ILFC's notes and bonds payable in the preceding table of borrowings. The debt is collateralized by a pledge of shares of a subsidiary of ILFC, which holds title to the aircraft financed under the facility.

From time to time, ILFC enters into funded financing agreements. As of September 30, 2007, ILFC had a total of $1.1 billion outstanding, which has varying maturities through February 2012. The interest rates are LIBOR-based, with spreads ranging from 0.30 percent to 1.625 percent.

The proceeds of ILFC's debt financing are primarily used to purchase flight equipment, including progress payments during the construction phase. The primary sources for the repayment of this debt and the interest expense thereon are the cash flow from operations, proceeds from the sale of flight equipment and the rollover and refinancing of the prior debt. AIG does not guarantee the debt obligations of ILFC. See also Operating Review – Financial Services Operations and Liquidity herein.

AGF

AGF fulfills most of its short-term cash borrowing requirements through the issuance of commercial paper. The issuance of commercial paper is subject to the approval of AGF's Board of Directors and is not guaranteed by AIG. AGF maintains committed syndicated revolving credit facilities which, as of September 30, 2007, totaled $4.75 billion and which are summarized below under Revolving Credit Facilities. The facilities can be used for general corporate purposes and to provide backup for AGF's commercial paper programs.

As of September 30, 2007, notes and bonds aggregating $19.01 billion were outstanding with maturity dates ranging from 2007 to 2031 at interest rates ranging from 1.94 percent to 8.45 percent. To the extent deemed appropriate, AGF may enter into swap transactions to manage its effective borrowing rates with respect to these notes and bonds. As a well-known seasoned issuer, AGF filed an automatic shelf registration statement with the SEC allowing AGF immediate access to the U.S. public debt markets. At September 30, 2007, AGF had remaining corporate authorization to issue up to $10.8 billion of debt securities under its shelf registration statements.

AGF's funding sources include a medium term note program, private placement debt, retail note issuances, bank financing and securitizations of finance receivables that AGF accounts for as on-balance-sheet secured financings. In addition, AGF has become an established issuer of long-term debt in the international capital markets.

In addition to debt refinancing activities, proceeds from the collection of finance receivables are used to fund cash needs including the payment of principal and interest on AGF's debt. AIG does not guarantee any of the debt obligations of AGF. See also Operating Review – Financial Services Operations and Liquidity herein.

AIGCFG

AIGCFG has a variety of funding mechanisms for its various markets, including retail and wholesale deposits, short-term and long-term bank loans, securitizations and intercompany subordinated debt. AIG Credit Card Company (Taiwan), a consumer finance business in Taiwan, and AIG Retail Bank PLC, a full service consumer bank in Thailand, have issued commercial paper for the funding of their respective operations. AIG does not guarantee any borrowings for AIGCFG businesses, including this commercial paper.

Revolving Credit Facilities

AIG, ILFC and AGF maintain committed, unsecured revolving credit facilities listed on the table below in order to support their respective commercial paper programs and for general corporate purposes. AIG, ILFC and AGF expect to replace or extend these credit facilities on or prior to their expiration. Some of the facilities, as noted below, contain a "term-out option" allowing for the conversion by the

borrower of any outstanding loans at expiration into one-year term loans.

As of September 30, 2007 (in millions)

Facility	Size	Borrower(s)	Available Amount	Expiration	One-Year Term-Out Option
AIG:					
364-Day Syndicated Facility	$ 2,125	AIG/AIG Funding[(a)] AIG Capital Corporation[(a)]	**$2,125**	July 2008	Yes
5-Year Syndicated Facility	1,625	AIG/AIG Funding[(a)] AIG Capital Corporation[(a)]	**1,625**	July 2011	No
364-Day Bilateral Facility[(b)]	3,200	AIG/AIG Funding	**72**	November 2007	Yes
364-Day Intercompany Facility[(c)]	5,335	AIG	**5,335**	September 2008	Yes
Total AIG	$12,285		**$9,157**		
ILFC:					
5-Year Syndicated Facility	$ 2,500	ILFC	**$2,500**	October 2011	No
5-Year Syndicated Facility	2,000	ILFC	**2,000**	October 2010	No
5-Year Syndicated Facility	2,000	ILFC	**2,000**	October 2009	No
Total ILFC	$ 6,500		**$6,500**		
AGF:					
364-Day Syndicated Facility	$ 2,625	American General Finance Corporation American General Finance, Inc.[(d)]	**$2,625**	July 2008	Yes
5-Year Syndicated Facility	2,125	American General Finance Corporation	**2,125**	July 2010	No
Total AGF	$ 4,750		**$4,750**		

(a) Guaranteed by AIG.

(b) This facility can be drawn in the form of loans or letters of credit. All drawn amounts shown above are in the form of letters of credit.

(c) Subsidiaries of AIG are the lenders on this facility.

(d) American General Finance, Inc. is an eligible borrower for up to $400 million only.

Credit Ratings

The cost and availability of unsecured financing for AIG and its subsidiaries are generally dependent on their short-term and long-term debt ratings. The following table presents the credit ratings of AIG and certain of its subsidiaries as of October 31, 2007. In parentheses, following the initial occurrence in the table of each rating, is an indication of that rating's relative rank within the agency's rating categories. That ranking refers only to the generic or major rating category and not to the modifiers appended to the rating by the rating agencies to denote relative position within such generic or major category.

	Short-term Debt			Senior Long-term Debt		
	Moody's	S&P	Fitch	Moody's[(a)]	S&P[(b)]	Fitch[(c)]
AIG	P-1 (1st of 3)	A-1+ (1st of 6)	F1+ (1st of 5)	Aa2 (2nd of 9)	AA (2nd of 8)	AA (2nd of 9)
AIG Financial Products Corp.[(d)]	P-1	A-1+	–	Aa2	AA	–
AIG Funding, Inc.[(d)]	P-1	A-1+	F1+	–	–	–
ILFC	P-1	A-1+	F1 (1st of 5)	A1 (3rd of 9)	AA–[(e)] (2nd of 8)	A+ (3rd of 9)
American General Finance Corporation	P-1	A-1 (1st of 6)	F1	A1	A+ (3rd of 8)	A+
American General Finance, Inc.	P-1	A-1	F1	–	–	A+

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

(b) Standard & Poor's, a division of the McGraw-Hill Companies (S&P). S&P ratings may be modified by the addition of a plus or minus sign to show relative standing within the major rating categories.

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

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

(e) Negative rating outlook. A negative outlook by S&P indicates that a rating may be lowered, but is not necessarily a precursor of a ratings change. The outlook on all other credit ratings in the table is stable.

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

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

AIG believes that any of its own or its subsidiaries' contractual obligations that are subject to "ratings triggers" or financial covenants relating to "ratings triggers" would not have a material adverse effect on its financial condition or liquidity. Ratings downgrades could also trigger the application of termination provisions in certain of AIG's contracts, principally agreements entered into by AIGFP and assumed reinsurance contracts entered into by Transatlantic.

It is estimated that, as of the close of business on October 31, 2007, based on AIGFP's outstanding municipal GIAs and financial derivatives transactions as of such date, a downgrade of AIG's long-term senior debt ratings to 'Aa3' by Moody's or 'AA–' by S&P would permit counterparties to call for approximately $830 million of collateral. Further, additional downgrades could result in requirements for substantial additional collateral, which could have a material effect on how AIGFP manages its liquidity. The actual amount of additional collateral that AIGFP would be required to post to counterparties in the event of such downgrades depends on market conditions, the fair value of the outstanding affected transactions and other factors prevailing at the time of the downgrade. Additional obligations to post collateral would increase the demand on AIGFP's liquidity.

Contractual Obligations and Other Commercial Commitments

The maturity schedule of AIG's contractual obligations at September 30, 2007 was as follows:

		Payments due by Period			
(in millions)	Total Payments	Less Than One Year	1-3 Years	3(+)-5 Years	Over Five Years
Borrowings[(a)]	$152,135	$ 42,513	$ 34,762	$ 31,874	$ 42,986
Interest payments on borrowings	83,122	5,121	10,640	6,833	60,528
Loss reserves[(b)]	83,608	22,992	25,500	12,124	22,992
Insurance and investment contract liabilities[(c)]	620,375	29,495	35,992	41,232	513,656
GIC liabilities[(d)]	31,708	5,895	12,810	3,603	9,400
Aircraft purchase commitments	20,995	840	6,765	2,690	10,700
Total	$991,943	$106,856	$126,469	$ 98,356	$660,262

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

(b) Represents future loss and loss adjustment expense payments estimated based on historical loss development payment patterns.

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

(d) Represents guaranteed maturities under GICs.

The maturity schedule of other commercial commitments of AIG and its consolidated subsidiaries at September 30, 2007 was as follows:

		Amount of Commitment Expiration			
(in millions)	Total Amounts Committed	Less Than One Year	1-3 Years	3(+)-5 Years	Over Five Years
Guarantees:					
Liquidity facilities[(a)]	$ 4,120	$ 181	$ 374	$1,901	$ 1,664
Standby letters of credit	1,727	1,466	68	37	156
Construction guarantees[(b)]	745	—	—	—	745
Guarantees of indebtedness	1,089	46	91	532	420
All other guarantees	662	65	58	64	475
Commitments:					
Investment commitments[(c)]	5,983	1,290	2,842	1,587	264
Commitments to extent credit	907	359	261	257	30
Securities lending commitments	84	47	37	—	—
Letters of credit	1,278	983	27	122	146
Other commercial commitments[(d)(e)]	17,963	7,659	3,716	166	6,422
Total	$34,558	$12,096	$7,474	$4,666	$10,322

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

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

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

(d) Excludes commitments with respect to pension plans. The annual pension contribution for 2007 is expected to be approximately $95 million for U.S. and non-U.S. plans.

(e) Includes options to acquire aircraft.

Shareholders' Equity

AIG's consolidated shareholders' equity increased during the first nine months of 2007 as follows:

(in millions)	**September 30, 2007**
Beginning of year	$101,677
Net income	11,492
Unrealized appreciation (depreciation) of investments, net of tax	(3,165)
Cumulative translation adjustment, net of tax	216
Dividends to shareholders	(1,455)
Payments advanced to purchase shares	(1,275)
Share repurchase	(3,741)
Other*	318
End of period	$104,067

** Reflects the effects of employee stock transactions and cumulative effect of accounting changes.*

AIG has in the past reinvested most of its unrestricted earnings in its operations and believes such continued reinvestment in the future will be adequate to meet any foreseeable capital needs. However, AIG may choose from time to time to raise additional funds through the issuance of additional securities.

In February 2007, AIG's Board of Directors adopted a new dividend policy, which took effect with the dividend declared in the second quarter of 2007, providing that under ordinary circumstances, AIG's plan will be to increase its common stock dividend by approximately 20 percent annually. The payment of any dividend, however, is at the discretion of AIG's Board of Directors, and the future payment of dividends will depend on various factors, including the performance of AIG's businesses, AIG's consolidated financial position, results of operations and liquidity and the existence of investment opportunities.

Share Repurchases

From time to time, AIG may buy shares of its common stock for general corporate purposes, including to satisfy its obligations under various employee benefit plans. In February 2007, AIG's Board of Directors increased AIG's share repurchase program by authorizing the repurchase of shares with an aggregate purchase price of $8 billion. In March 2007, AIG entered into a $3 billion structured share repurchase arrangement and entered into additional $1 billion structured share repurchase arrangements in each of May and September 2007. A total of 55,103,845 shares were repurchased during the first nine months of 2007. The portion of the payments advanced by AIG under the structured share repurchase arrangements that had not yet been utilized to repurchase shares at September 30, 2007, amounting to $1.28 billion, has been recorded as a component of shareholders' equity under the caption, Payments advanced to purchase shares. Purchases have continued subsequent to September 30, 2007, with an additional 13,964,098 shares purchased from October 1 through November 5, 2007. All shares repurchased are recorded as treasury stock at cost.

Liquidity

AIG manages liquidity at both the subsidiary and parent company levels. At September 30, 2007, AIG's consolidated invested assets, primarily held by its subsidiaries, included $41.2 billion in cash and short-term investments. Consolidated net cash provided from operating activities in the first nine months of 2007 amounted to $27.1 billion. At both the subsidiary and parent company level, liquidity management activities are conducted in a manner to preserve and enhance funding stability, flexibility, and diversity through the full range of potential operating environments and market conditions. AIG's primary sources of cash flow are dividends and other payments from its regulated and unregulated subsidiaries, as well as issuances of debt securities. Primary uses of cash flow are for debt service, subsidiary funding, shareholder dividend payments and common stock repurchases. As a result of market disruption in the credit markets during the third quarter of 2007, AIG took prudent steps to enhance the liquidity of its portfolios. Management believes that AIG's liquid assets, cash provided by operations and access to the capital markets will enable it to meet its anticipated cash requirements, including the funding of increased dividends under AIG's current dividend policy and repurchases of common stock.

In the first nine months of 2007, AIG parent collected $2.6 billion in dividends and other payments from subsidiaries, principally from DBG companies, issued $6.2 billion of debt securities and retired $765 million of debt, excluding MIP and Series AIGFP debt. AIG parent also advanced $5 billion for structured share repurchase arrangements. AIG parent made interest payments totaling $376 million, made $1.56 billion in capital contributions to subsidiaries, and paid $1.41 billion in dividends to shareholders in the first nine months of 2007.

AIG parent funds its short-term working capital needs through commercial paper issued by AIG Funding. As of September 30, 2007, AIG Funding had $5.8 billion of commercial paper outstanding with an average maturity of 28 days. As additional liquidity, AIG parent and AIG Funding maintain revolving credit facilities that, as of September 30, 2007, had an aggregate of $9.2 billion available to be drawn, which are summarized above under Revolving Credit Facilities.

Invested Assets

AIG's investment strategy is to invest primarily in high quality securities while maintaining diversification to avoid significant exposure to issuer, industry and/or country concentrations.

The following tables summarize the composition of AIG's invested assets by segment.

(in millions)	General Insurance	Life Insurance & Retirement Services	Financial Services	Asset Management	Other	Total
September 30, 2007						
Fixed maturities:						
Bonds available for sale, at fair value	$ 73,522	$288,945	$ 1,369	$30,974	$ –	$394,810
Bonds held to maturity, at amortized cost	21,357	1	–	218	–	21,576
Bond trading securities, at fair value	–	9,436	–	23	–	9,459
Equity securities:						
Common stocks available for sale, at fair value	5,941	11,895	–	700	113	18,649
Common and preferred stocks trading, at fair value	404	18,779	–	36	–	19,219
Preferred stocks available for sale, at fair value	1,858	739	9	–	–	2,606
Mortgage loans on real estate, net of allowance	11	14,764	127	3,952	–	18,854
Policy loans	2	7,779	2	48	(9)	7,822
Collateral and guaranteed loans, net of allowance	3	821	2,355	1,142	64	4,385
Financial services assets:						
Flight equipment primarily under operating leases, net of accumulated depreciation	–	–	41,804	–	–	41,804
Securities available for sale, at fair value	–	–	47,805	–	–	47,805
Trading securities, at fair value	–	–	4,874	–	–	4,874
Spot commodities	–	–	115	–	–	115
Unrealized gain (loss) on swaps, options and forward transactions	–	–	19,046	–	(438)	18,608
Trade receivables	–	–	6,548	–	–	6,548
Securities purchased under agreements to resell, at contract value	–	–	37,189	–	–	37,189
Finance receivables, net of allowance	–	5	30,635	–		30,640
Securities lending collateral, at fair value	7,291	62,921	171	15,725	–	86,108
Other invested assets	11,009	16,555	2,890	21,058	271	51,783
Short-term investments, at cost	4,698	22,455	8,297	3,614	(66)	38,998
Total investments and financial services assets as shown on the balance sheet	126,096	455,095	203,236	77,490	(65)	861,852
Cash	314	1,054	657	218	6	2,249
Investment income due and accrued	1,418	4,841	23	354	(1)	6,635
Real estate, net of accumulated depreciation	320	909	17	88	229	1,563
Total invested assets[1]	$128,148	$461,899	$203,933[2]	$78,150	$ 169	$872,299

(1) At September 30, 2007, approximately 67 percent and 33 percent of invested assets were held in domestic and foreign investments, respectively.

(2) Excludes $2.5 billion of assets held in an unconsolidated structured investment vehicle sponsored by AIGFP in the second quarter of 2007. As of September 30, 2007, AIGFP's invested assets included $1.0 billion of commercial paper and medium-term notes issued by this entity. In addition, AIGFP owned approximately 11.5 percent of the capital notes issued by this entity.

(in millions)	General Insurance	Life Insurance & Retirement Services	Financial Services	Asset Management	Other	Total
December 31, 2006						
Fixed maturities:						
Bonds available for sale, at fair value	$ 67,994	$288,540	$ 1,357	$29,500	$ –	$387,391
Bonds held to maturity, at amortized cost	21,437	–	–	–	–	21,437
Bond trading securities, at fair value	1	10,313	–	–	–	10,314
Equity securities:						
Common stocks available for sale, at fair value	4,245	8,705	–	226	80	13,256
Common stocks trading, at fair value	350	14,505	–	–	–	14,855
Preferred stocks available for sale, at fair value	1,884	650	5	–	–	2,539
Mortgage loans on real estate, net of allowance	13	12,852	95	4,107	–	17,067
Policy loans	1	7,458	2	48	(8)	7,501
Collateral and guaranteed loans, net of allowance	3	733	2,301	729	84	3,850
Financial services assets:						
Flight equipment primarily under operating leases, net of accumulated depreciation	–	–	39,875	–	–	39,875
Securities available for sale, at fair value	–	–	47,205	–	–	47,205
Trading securities, at fair value	–	–	5,031	–	–	5,031
Spot commodities	–	–	220	–	–	220
Unrealized gain on swaps, options and forward transactions	–	–	19,252	–	–	19,252
Trade receivables	–	–	4,317	–	–	4,317
Securities purchased under agreements to resell, at contract value	–	–	30,291	–	–	30,291
Finance receivables, net of allowance	–	–	29,573	–	–	29,573
Securities lending collateral, at fair value	5,376	50,099	76	13,755	–	69,306
Other invested assets	9,207	14,260	2,212	15,823	609	42,111
Short-term investments, at cost	3,281	15,192	2,807	6,198	5	27,483
Total investments and financial services assets as shown on the balance sheet	113,792	423,307	184,619	70,386	770	792,874
Cash	334	740	390	118	8	1,590
Investment income due and accrued	1,363	4,378	23	326	1	6,091
Real estate, net of accumulated depreciation	570	698	17	75	26	1,386
Total invested assets*	$116,059	$429,123	$185,049	$70,905	$805	$801,941

** At December 31, 2006, approximately 68 percent and 32 percent of invested assets were held in domestic and foreign investments, respectively.*

Investments in Residential Mortgage-Backed Securities and CDOs

As part of its strategy to diversify its investments, AIG invests in various types of securities, including residential mortgage-backed securities (RMBS) and CDOs. At September 30, 2007, AIG's investment portfolio included such securities with an amortized cost of $96.8 billion and an estimated fair value of $94.4 billion. The gross unrealized gains and gross unrealized losses related to these investments were $333 million and $2.7 billion, respectively, at September 30, 2007.

AIG's insurance operations held investments in RMBS with an estimated fair value of $91 billion at September 30, 2007, or approximately 10 percent of AIG's total invested assets. In addition, AIGFP held investments totaling $3.3 billion in CDOs which include some level of subprime exposure. AIG's RMBS investments are predominantly in highly-rated tranches that contain substantial protection features through collateral subordination. At September 30, 2007, approximately 91 percent of these investments were rated AAA and approximately 7 percent were rated AA by one or more of the principal rating agencies. AIG's investments rated BBB or below totaled approximately $500 million, or less than 1 percent of AIG's total invested assets at September 30, 2007. As of October 31, 2007, approximately $598 million of AIG's RMBS backed primarily by subprime collateral had been downgraded as a result of rating agency actions in 2007, approximately $236 million of such investments had been upgraded, $70 million in the third quarter, and approximately $819 million was on watch for downgrade and approximately $30 million on watch for upgrade. AIG currently intends to hold these securities to full recovery and/or full payment of principal and interest, and therefore expects that any mark to market effect will result in only a temporary adjustment to shareholders' equity.

AIG's underwriting practices for investing in RMBS, other asset-backed securities and CDOs takes into consideration the quality of the originator, the manager, the servicer, security credit ratings, underlying characteristics of the mortgages, borrower characteristics, and the level of credit enhancement in the transaction. AIG's strategy is typically to invest in securities rated AA or better and create diversification across multiple underlying asset classes.

Securities lending operations

At September 30, 2007, AIG's securities lending payables totaled $88.4 billion, $14.6 billion of which was one-day tenor, with the balance maturing within the next six months. Collateral held for this program at September 30, 2007 included interest bearing cash equivalents with overnight maturities of $17.4 billion.

Other-than-temporary impairments

As a result of AIG's periodic evaluation of its securities for other-than-temporary impairments in value, AIG recorded, in net realized capital gains (losses), other-than-temporary impairment pre-tax losses of $529 million and $170 million in the three-month periods ended September 30, 2007 and 2006, respectively, and $1.4 billion and $766 million in the nine-month periods ended September 30, 2007 and 2006, respectively.

The principal causes of the other-than-temporary impairment losses in the three and nine-month periods ended September 30, 2007 were as follows:

Three months ended September 30, 2007

- Securities which AIG no longer intends to hold until they have fully recovered their carrying value, totaling $250 million.
- Impairments of $147 million related to certain structured securities, the carrying value of which is based on an estimate of the security's future cash flows pursuant to the requirements of EITF No. 99-20, "Recognition of Interest Income and Impairment on Purchased and Retained Beneficial Interests in Securitized Financial Assets" (EITF No. 99-20).
- Issuer-specific events totaling $104 million and equity securities and partnership investments of $1 million in an unrealized loss position for a continuous 12-month period.
- A decline in value of U.S. dollar bonds held by AIG's Foreign Life operations totaling $27 million, due to the depreciation of the U.S. dollar against the local currency.

Nine months ended September 30, 2007

- Securities which AIG no longer intends to hold until they have fully recovered their carrying value, totaling $621 million.
- A decline in value of U.S. dollar bonds held by AIG's Foreign Life operations totaling $333 million, due to the depreciation of the U.S. dollar against the local currency.
- Issuer-specific events totaling $131 million and equity securities and partnership investments of $148 million in an unrealized loss position for a continuous 12-month period.
- Impairments of $159 million related to certain structured securities, the carrying value of which is based on an estimate of the security's future cash flows pursuant to the requirements of EITF No. 99-20.

No impairment charge with respect to any one single credit was significant to AIG's consolidated financial condition or results of operations, and no individual impairment loss exceeded 1.0 percent of consolidated net income for the first nine months of 2007.

An aging of the pre-tax unrealized losses of fixed maturity and equity securities, distributed as a percentage of cost relative to unrealized loss (the extent by which the fair value is less than amortized cost or cost), including the number of respective items, was as follows at September 30, 2007:

	Less than or equal to 20% of Cost			Greater than 20% to 50% of Cost			Greater than 50% of Cost			Total		
Aging *(dollars in millions)*	Cost[a]	Unrealized Loss	Items	Cost[a]	Unrealized Loss	Items	Cost[a]	Unrealized Loss	Items	Cost[a]	Unrealized Loss[b]	Items
Investment grade bonds												
0-6 months	$138,250	$3,435	12,809	$ 441	$118	45	$20	$13	7	$138,711	$3,566	12,861
7-12 months	35,024	1,299	3,626	503	142	68	—	—	—	35,527	1,441	3,694
>12 months	97,331	3,426	11,744	892	212	41	36	16	3	98,259	3,654	11,788
Total	$270,605	$8,160	28,179	$1,836	$472	154	$56	$29	10	$272,497	$8,661	28,343
Below investment grade bonds												
0-6 months	$ 6,196	$ 167	1,502	$ 37	$ 11	24	$ —	$ —	—	$ 6,233	$ 178	1,526
7-12 months	1,061	43	133	14	4	4	—	—	—	1,075	47	137
>12 months	1,433	77	177	40	9	7	—	—	—	1,473	86	184
Total	$ 8,690	$ 287	1,812	$ 91	$ 24	35	$ —	$ —	—	$ 8,781	$ 311	1,847
Total bonds												
0-6 months	$144,446	$3,602	14,311	$ 478	$129	69	$20	$13	7	$144,944	$3,744	14,387
7-12 months	36,085	1,342	3,759	517	146	72	—	—	—	36,602	1,488	3,831
>12 months	98,764	3,503	11,921	932	221	48	36	16	3	99,732	3,740	11,972
Total	$279,295	$8,447	29,991	$1,927	$496	189	$56	$29	10	$281,278	$8,972	30,190
Equity securities												
0-6 months	$ 4,309	$ 256	2,279	$ 246	$ 65	301	$ 6	$ 5	46	$ 4,561	$ 326	2,626
7-12 months	312	22	109	57	15	40	2	1	13	371	38	162
>12 months	—	—	—	—	—	—	—	—	—	—	—	—
Total[c]	$ 4,621	$ 278	2,388	$ 303	$ 80	341	$ 8	$ 6	59	$ 4,932	$ 364	2,788

(a) For bonds, represents amortized cost.

(b) The effect on net income of unrealized losses after taxes will be mitigated upon realization because certain realized losses will be charged to participating policyholder accounts, or realization will result in current decreases in the amortization of certain DAC.

(c) Beginning in the third quarter of 2007, includes securities lending collateral.

Unrealized gains and losses

At September 30, 2007, the fair value of AIG's fixed maturity and equity securities aggregated $552.9 billion. At September 30, 2007, aggregate pre-tax unrealized gains for fixed maturity and equity securities were $17.6 billion ($11.4 billion after tax).

At September 30, 2007, the aggregate pre-tax unrealized losses of fixed maturity and equity securities were $9.3 billion ($6.07 billion after tax). Additional information about these securities is as follows:

- These securities are trading, in the aggregate, at approximately 97 percent of their current amortized cost.
- Less than 1 percent of these securities are trading at a value which is less than 20 percent of its current cost, or amortized cost.
- Less than 4 percent of the fixed income securities have issuer credit ratings which are below investment grade.

AIG did not consider these securities in an unrealized loss position to be other-than-temporarily impaired at September 30, 2007, as management has the intent and ability to hold these investments until they fully recover in value.

At September 30, 2007, unrealized losses for fixed maturity securities and equity securities did not reflect any significant industry concentrations.

For the three months ended September 30, 2007, unrealized losses related to investment grade bonds increased $2.9 billion ($1.9 billion after tax), reflecting the widening of credit spreads, partially offset by the effects of a decline in risk free interest rates.

The amortized cost of fixed maturity securities available for sale in an unrealized loss position at September 30, 2007, by contractual maturity, is shown below:

(in millions)	Amortized Cost
Due in one year or less	$ 8,291
Due after one year through five years	48,310
Due after five years through ten years	78,136
Due after ten years	146,541
Total	$281,278

For the nine months ended September 30, 2007, the pre-tax realized losses incurred with respect to the sale of fixed maturities and equity securities were $931 million. The aggregate fair value of securities sold was $32.0 billion, which was approximately 96 percent of amortized cost. The average period of time that securities sold at a loss during the nine months ended September 30, 2007 were trading

continuously at a price below book value was approximately five months.

Risk Management

For a complete discussion of AIG's risk management program, see Management's Discussion and Analysis of Financial Condition and Results of Operations in the 2006 Annual Report on Form 10-K.

Insurance, Asset Management and Non-Trading Financial Services VaR

AIG performs one comprehensive Value at Risk (VaR) analysis across all of its non-trading businesses, and a separate VaR analysis for its trading business at AIGFP. The comprehensive VaR is categorized by AIG business segment (General Insurance, Life Insurance & Retirement Services, Financial Services and Asset Management) and also by market risk factor (interest rate, currency and equity).

AIG calculated the VaR with respect to net fair values as of September 30, 2007 and December 31, 2006. The VaR number represents the maximum potential loss as of those dates that could be incurred with a 95 percent confidence and a one-month holding period.

The following table presents the period-end, average, high and low VaRs on a diversified basis and of each component of market risk for AIG's non-trading businesses. The diversified VaR is usually smaller than the sum of its components due to correlation effects.

	2007				2006			
		Nine Months Ended September 30,				Year Ended December 31,		
(in millions)	As of September 30,	Average	High	Low	As of December 31,	Average	High	Low
Total AIG Non-Trading Market Risk:								
Market risk:								
Diversified	**$5,619**	**$5,247**	**$5,619**	**$5,073**	$5,073	$5,209	$5,783	$4,852
Interest rate	**4,757**	**4,655**	**4,757**	**4,577**	4,577	4,962	5,765	4,498
Currency	**762**	**715**	**762**	**685**	686	641	707	509
Equity	**2,350**	**2,072**	**2,350**	**1,873**	1,873	1,754	1,873	1,650
General Insurance:								
Diversified	**$1,668**	**$1,705**	**$1,892**	**$1,543**	$1,717	$1,697	$1,776	$1,617
Interest rate	**1,539**	**1,585**	**1,792**	**1,470**	1,541	1,635	1,717	1,541
Currency	**222**	**214**	**222**	**205**	212	162	212	119
Equity	**675**	**615**	**675**	**573**	573	551	573	535
Life Insurance & Retirement Services:								
Diversified	**$5,126**	**$4,765**	**$5,126**	**$4,574**	$4,574	$4,672	$5,224	$4,307
Interest rate	**4,611**	**4,480**	**4,611**	**4,287**	4,471	4,563	5,060	4,229
Currency	**678**	**613**	**678**	**568**	568	538	592	459
Equity	**1,697**	**1,438**	**1,697**	**1,293**	1,293	1,228	1,299	1,133
Non-Trading Financial Services:								
Diversified	**$ 170**	**$ 122**	**$ 170**	**$ 85**	$ 125	$ 165	$ 252	$ 125
Interest rate	**168**	**121**	**168**	**76**	127	166	249	127
Currency	**12**	**12**	**12**	**11**	11	8	11	7
Equity	**1**	**1**	**1**	**1**	1	1	2	1
Asset Management:								
Diversified	**$ 26**	**$ 51**	**$ 74**	**$ 26**	$ 64	$ 144	$ 190	$ 64
Interest rate	**22**	**48**	**72**	**22**	63	145	192	63
Currency	**5**	**3**	**5**	**2**	3	4	7	3
Equity	**13**	**10**	**13**	**8**	8	9	13	8

Increased equity investment allocation in the Life Insurance & Retirement Services and General Insurance segments, combined with higher volatility in equity markets, contributed to the growth in AIG's total Non-Trading VaR during the first nine months of 2007. Interest rate volatilities continued to moderate in many markets.

Capital Markets Trading VaR

AIGFP's policy is to maintain a conservative market risk profile and minimize risks in interest rates, equities, commodities and foreign exchange. In addition, AIGFP's primary market exposures in option implied volatilities, correlations and basis risks are closely managed.

AIGFP's minimal reliance on market risk driven revenue is reflected in its VaR. Because the market risk with respect to securities available for sale, at market, is substantially hedged, segregation of the financial instruments into trading and other than trading was not deemed necessary.

AIGFP reports its VaR using a 95 percent confidence interval and a one-day holding period.

The following table presents the period-end, average, high, and low VaRs (based on daily observations) on a diversified basis and of each component of market risk for AIG's Capital Markets operations. The diversified VaR is usually smaller than the sum of its components due to correlation effects.

	2007				2006			
		Nine Months Ended September 30,				Year Ended December 31,		
(in millions)	As of September 30,	Average	High	Low	As of December 31,	Average	High	Low
Total AIG trading market risk:								
Diversified	**$6**	**$5**	**$7**	**$4**	$4	$4	$7	$3
Interest rate	**2**	**2**	**3**	**2**	2	2	3	1
Currency	**1**	**1**	**2**	**1**	1	1	3	1
Equity	**3**	**3**	**5**	**2**	3	3	4	2
Commodity	**6**	**4**	**6**	**2**	3	3	4	2

Catastrophe Exposures

The nature of AIG's business exposes it to various catastrophic events in which multiple losses across multiple lines of business can occur in any calendar year. In order to control this exposure, AIG uses a combination of techniques, including setting aggregate limits in key business units, monitoring and modeling accumulated exposures, and purchasing catastrophe reinsurance to supplement its other reinsurance protections.

Natural disasters such as hurricanes, earthquakes and other catastrophes have the potential to adversely affect AIG's operating results. Other risks, such as an outbreak of a pandemic disease, such as the Avian Influenza A Virus (H5N1), could adversely affect AIG's business and operating results to an extent that may be only partially offset by reinsurance programs.

AIG evaluates catastrophic events and assesses the probability of occurrence and magnitude of catastrophic events through the use of industry recognized models, among other techniques. AIG supplements these models by periodically monitoring the exposure risks of AIG's worldwide General Insurance operations and adjusting such models accordingly. Following is an overview of modeled losses associated with the more significant natural perils, which includes exposures for DBG, Personal Lines, Foreign General (other than Ascot), The Hartford Steam Boiler Inspection and Insurance Company and 21st Century. Transatlantic and Ascot utilize a different model, and their combined results are presented separately below. Significant life and A&H exposures have been added to these results as well. The modeled results assume that all reinsurers fulfill their obligations to AIG in accordance with their terms.

It is important to recognize that there is no standard methodology to project the possible losses from total property and workers compensation exposures. Further, there are no industry standard assumptions to be utilized in projecting these losses. The use of different methodologies and assumptions could materially change the projected losses. Therefore, these modeled losses may not be comparable to estimates made by other companies.

These estimates are inherently uncertain and may not reflect AIG's maximum exposures to these events. It is highly likely that AIG's losses will vary, perhaps significantly, from these estimates.

AIG has revised the catastrophe exposure disclosures presented below from that presented in the 2006 Annual Report on Form 10-K to include significant life and A&H exposures to natural perils as well as to update the domestic property exposures to reflect more recent data. The modeled results provided in the table below were based on the aggregate exceedence probability (AEP) losses which represent total property, workers compensation, life, and accident and health losses that may occur in any single year from one or more natural events. The life and A&H data include exposures for United States, Japan, and Taiwan earthquakes. These represent the largest share of life and A&H exposures to earthquake. A&H losses were modeled using December 2006 data, and life losses were modeled using March 2006 data. The updated property exposures were generally modeled with exposure data as of year-end 2006. Lexington commercial lines exposure, which represents the largest share of the modeled losses, was based on data as of April 2007. All reinsurance program structures, including both domestic and international structures, have also been updated. The values provided were based on 100-year return period losses, which have a one percent likelihood of being exceeded in any single year. Thus, the model projects that there is a one percent probability that AIG could incur in any year losses in excess of the modeled amounts for these perils.

(in millions)	Gross	Net of Reinsurance	Net After Income Tax	% of Consolidated Shareholders' Equity at September 30, 2007
Natural Peril:				
Earthquake	$4,970	$2,705	$1,758	1.7%
Tropical Cyclone*	$5,546	$2,980	$1,937	1.9%

** Includes hurricanes, typhoons and other wind-related events.*

The combined earthquake and tropical cyclone 100-year return period modeled losses for Ascot and Transatlantic together are estimated to be $1.1 billion, on a gross basis, $761 million, net of reinsurance, and $494 million, net after income taxes, or 0.5 percent of total shareholders' equity at September 30, 2007.

In addition, AIG evaluates potential single event earthquake and hurricane losses that may be incurred. The single events utilized are a subset of potential events identified and utilized by Lloyd's[(1)] and referred to as Realistic Disaster Scenarios (RDSs). The purpose of this analysis is to utilize these RDSs to provide a reference frame and place into context the model results. However, it is important to note that the specific events used for this analysis do not necessarily represent the worst case loss that AIG could incur from this type of an event in these regions. The losses associated with the RDSs are included in the table below.

Single event modeled property and workers compensation losses to AIG's worldwide portfolio of risk for key geographic areas are set forth below. Gross values represent AIG's liability after the application of policy limits and deductibles, and net values represent losses after reinsurance is applied.

(in millions)	Gross	Net of Reinsurance
Natural Peril:		
San Francisco Earthquake	$5,562	$3,012
Miami Hurricane	$5,375	$2,651
Northeast Hurricane	$4,755	$2,779
Los Angeles Earthquake	$4,750	$2,614
Gulf Coast Hurricane	$3,553	$1,797
Japanese Earthquake	$ 843	$ 366
European Windstorm	$ 239	$ 87
Japanese Typhoon	$ 185	$ 149

(1) Lloyd's Realistic Disaster Scenarios, Scenario Specifications, April 2006.

The specific international RDS events do not necessarily correspond to AIG's international property exposures. As a result, AIG runs its own simulations where property statistical return period losses associated with the written exposure specific to AIG provide the basis for monitoring risk.

Based on these simulations, the 100-year return period loss for Japanese Earthquake is $296 million gross, and $120 million net, the 100-year return period loss for European Windstorm is $269 million gross, and $80 million net, and the 100-year return period loss for Japanese Typhoon is $306 million gross, and $252 million net.

Recent market conditions in the U.S. property business have supported growth in this line of business. Consequently, gross modeled catastrophe losses have increased. Associated net exposure has been carefully monitored and controlled through the strategic placement of reinsurance.

ACTUAL RESULTS IN ANY PERIOD ARE LIKELY TO VARY, PERHAPS MATERIALLY, FROM THE MODELED SCENARIOS, AND THE OCCURRENCE OF ONE OR MORE SEVERE EVENTS COULD HAVE A MATERIAL ADVERSE EFFECT ON AIG'S CONSOLIDATED FINANCIAL CONDITION, RESULTS OF OPERATIONS AND LIQUIDITY.

ITEM 3. Quantitative and Qualitative Disclosures About Market Risk

Included in Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations.

ITEM 4. Controls and Procedures

In connection with the preparation of this Quarterly Report on Form 10-Q, an evaluation was carried out by AIG's management, with the participation of AIG's Chief Executive Officer and Chief Financial Officer, of the effectiveness of AIG's disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934 (Exchange Act)). Disclosure controls and procedures are designed to ensure that information required to be disclosed in reports filed or submitted under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in SEC rules and forms and that such information is accumulated and communicated to management, including the Chief Executive Officer and Chief Financial Officer, to allow timely decisions regarding required disclosures. Based on its evaluation, and in light of the previously identified material weakness in internal control over financial reporting, as of December 31, 2006, relating to controls over income tax accounting described in the 2006 Annual Report on Form 10-K, AIG's Chief Executive Officer and Chief Financial Officer concluded that, as of September 30, 2007, AIG's disclosure controls and procedures were ineffective. In addition, there has been no change in AIG's internal control over financial reporting (as defined in Rule 13a-15(f) under the Exchange Act) that occurred during the quarter ended September 30, 2007 that has materially affected, or is reasonably likely to materially affect, AIG's internal control over financial reporting.

Part II – OTHER INFORMATION

ITEM 2. Unregistered Sales of Equity Securities and Use of Proceeds

The table below provides information with respect to purchases of AIG Common stock during the three months ended September 30, 2007.

Period	Total Number of Shares Purchased[1]	Average Price Paid per Share	Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs	Maximum Number of Shares that May Yet Be Purchased Under the Plans or Programs at End of Month[2]
July 1 - 31	15,956,939	$68.50	15,956,939	
August 1 - 31	9,464,750	67.10	9,464,750	
September 1 - 30	5,190,195	64.09	5,190,195	
Total	30,611,884	$67.32	30,611,884	

(1) Reflects date of delivery. Does not include 42,867 shares delivered or attested to in satisfaction of the exercise price by holders of AIG employee stock options exercised during the three months ended September 30, 2007.

(2) In February 2007, AIG's Board of Directors increased AIG's share repurchase program by authorizing the repurchase of shares with an aggregate purchase price of $8 billion. A balance of $4.3 billion remained for purchases under the program as of September 30, 2007, although $1.28 billion of that amount has been advanced by AIG to purchase shares under the program. The purchase program has no set expiration or termination date.

ITEM 6. Exhibits

See accompanying Exhibit Index.

SIGNATURE

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

AMERICAN INTERNATIONAL GROUP, INC.
(Registrant)

/s/ Steven J. Bensinger

Steven J. Bensinger
Executive Vice President and Chief Financial Officer

/s/ David L. Herzog

David L. Herzog
Senior Vice President and Comptroller
(Principal Accounting Officer)

Dated: November 7, 2007

EXHIBIT INDEX

Exhibit Number	Description	Location
11	Statement re computation of per share earnings	Included in Note (3) of Notes to Consolidated Financial Statements.
12	Statement re computation of ratios	Filed herewith.
31	Rule 13a-14(a)/15d-14(a) Certifications	Filed herewith.
32	Section 1350 Certifications	Filed herewith.

Exhibit 12

American International Group, Inc.
Computation of Ratios of Earnings to Fixed Charges

(in millions, except ratios)	Three Months Ended September 30,		Nine Months Ended September 30,	
	2007	2006	**2007**	2006
Income before income taxes, minority interest and cumulative effect of an accounting change	**$ 4,879**	$ 6,301	**$17,379**	$16,335
Less – Equity income of less than 50% owned persons	**39**	44	**130**	174
Add – Dividends from less than 50% owned persons	**3**	8	**28**	26
	4,843	6,265	**17,277**	16,187
Add – Fixed charges	**3,153**	2,306	**8,267**	6,302
Less – Capitalized interest	**8**	14	**28**	43
Income before income taxes, minority interest, cumulative effect of an accounting change and fixed charges	**$ 7,988**	$ 8,557	**$25,516**	$22,446
Fixed charges:				
Interest costs	**$ 3,093**	$ 2,254	**$ 8,086**	$ 6,145
Rental expense*	**60**	52	**181**	157
Total fixed charges	**$ 3,153**	$ 2,306	**$ 8,267**	$ 6,302
Ratio of earnings to fixed charges	**2.53**	3.71	**3.09**	3.56
Secondary Ratio				
Interest credited to GIC and GIA policy and contract holders	**$(1,949)**	$(1,266)	**$ (4,796)**	$ (3,453)
Total fixed charges excluding interest credited to GIC and GIA policy and contract holders	**$ 1,204**	$ 1,040	**$ 3,471**	$ 2,849
Secondary ratio of earnings to fixed charges	**5.02**	7.01	**5.97**	6.67

** The proportion deemed representative of the interest factor.*

The secondary ratio is disclosed for the convenience of fixed income investors and the rating agencies that serve them and is more comparable to the ratios disclosed by all issuers of fixed income securities. The secondary ratio removes interest credited to guaranteed investment contract (GIC) policyholders and guaranteed investment agreement (GIA) contractholders. Such interest expenses are also removed from income before income taxes, minority interest and cumulative effect of an accounting change used in this calculation. GICs and GIAs are entered into by AIG's insurance subsidiaries, principally Sun America Life Insurance Company and AIG Financial Products Corp. and its subsidiaries, respectively. The proceeds from GICs and GIAs are invested in a diversified portfolio of securities, primarily investment grade bonds. The assets acquired yield rates greater than the rates on the related policyholders obligation or agreement, with the intent of earning operating income from the spread.

Exhibit 31

CERTIFICATIONS

I, Martin J. Sullivan, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q of American International Group, Inc.;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:

(a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

(b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

(c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

(d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):

(a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

(b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

/s/ Martin J. Sullivan

Martin J. Sullivan
President and Chief Executive Officer

Date: November 7, 2007

CERTIFICATIONS

I, Steven J. Bensinger, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q of American International Group, Inc.;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:

(a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

(b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

(c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

(d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):

(a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

(b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

/s/ Steven J. Bensinger

Steven J. Bensinger
Executive Vice President and Chief Financial Officer

Date: November 7, 2007

Exhibit 32

CERTIFICATION

In connection with the Quarterly Report on Form 10-Q of American International Group, Inc. (the "Company") for the quarter ended September 30, 2007, as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, Martin J. Sullivan, President and Chief Executive Officer of the Company, certify, pursuant to 18 U.S.C. Section 1350, that to my knowledge:

1. The Report fully complies with the requirements of Section 13(a) or 15(d), as applicable, of the Securities Exchange Act of 1934; and

2. The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

/s/ Martin J. Sullivan

Martin J. Sullivan
President and Chief Executive Officer

Date: November 7, 2007

The foregoing certification is being furnished solely pursuant to 18 U.S.C. Section 1350 and is not being filed as part of the Report or as a separate disclosure document.

CERTIFICATION

In connection with the Quarterly Report on Form 10-Q of American International Group, Inc. (the ''Company'') for the quarter ended September 30, 2007, as filed with the Securities and Exchange Commission on the date hereof (the ''Report''), I, Steven J. Bensinger, Executive Vice President and Chief Financial Officer of the Company, certify, pursuant to 18 U.S.C. Section 1350, that to my knowledge:

1. The Report fully complies with the requirements of Section 13(a) or 15(d), as applicable, of the Securities Exchange Act of 1934; and

2. The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

/s/ Steven J. Bensinger

Steven J. Bensinger
Executive Vice President and Chief Financial Officer

Date: November 7, 2007

The foregoing certification is being furnished solely pursuant to 18 U.S.C. Section 1350 and is not being filed as part of the Report or as a separate disclosure document.

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

Form 10-K

(Mark One)

☑ ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the fiscal year ended December 31, 2007

or

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

Commission file number 1-8787

American International Group, Inc.

(Exact name of registrant as specified in its charter)

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

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

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

Title of each class	Name of each exchange on which registered
Common Stock, Par Value $2.50 Per Share	New York Stock Exchange
5.75% Series A-2 Junior Subordinated Debentures	New York Stock Exchange
4.875% Series A-3 Junior Subordinated Debentures	New York Stock Exchange
6.45% Series A-4 Junior Subordinated Debentures	New York Stock Exchange
7.70% Series A-5 Junior Subordinated Debentures	New York Stock Exchange
NIKKEI 225® Index Market Index Target-Term Securities® due January 5, 2011	American Stock Exchange

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

Title of each class
None

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

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

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

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

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

Large Accelerated Filer ☑ Accelerated Filer ☐ Non-Accelerated Filer ☐ Smaller Reporting Company ☐
(Do not check if a smaller reporting company)

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).
Yes ☐ No ☑

The aggregate market value of the voting and nonvoting common equity held by nonaffiliates of the registrant computed by reference to the price at which the common equity was last sold as of June 29, 2007 (the last business day of the registrant's most recently completed second fiscal quarter), was approximately $152,287,000,000.

As of January 31, 2008, there were outstanding 2,522,336,771 shares of Common Stock, $2.50 par value per share, of the registrant.

Documents Incorporated by Reference:

Portions of the registrant's definitive proxy statement filed or to be filed with the Securities and Exchange Commission pursuant to Regulation 14A involving the election of directors at the Annual Meeting of Shareholders of the registrant scheduled to be held on May 14, 2008 are incorporated by reference in Part III of this Form 10-K.

Table of Contents

* *Except for the information provided in Part I under the heading ''Directors and Executive Officers of AIG,'' Part III Items 10, 11, 12, 13 and 14 are included in AIG's Definitive Proxy Statement to be used in connection with AIG's Annual Meeting of Shareholders scheduled to be held on May 14, 2008.*

Part I

Item 1.
Business

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

General Insurance

American Home Assurance Company (American Home)

National Union Fire Insurance Company of Pittsburgh, Pa. (National Union)

New Hampshire Insurance Company (New Hampshire)

Lexington Insurance Company (Lexington)

The Hartford Steam Boiler Inspection and Insurance Company (HSB)

Transatlantic Reinsurance Company

United Guaranty Residential Insurance Company

American International Underwriters Overseas, Ltd. (AIUO)

AIU Insurance Company (AIUI)

Life Insurance & Retirement Services

Domestic:

American General Life Insurance Company (AIG American General)

American General Life and Accident Insurance Company (AGLA)

The United States Life Insurance Company in the City of New York (USLIFE)

The Variable Annuity Life Insurance Company (VALIC)

AIG Annuity Insurance Company (AIG Annuity)

AIG SunAmerica Life Assurance Company (AIG SunAmerica)

Foreign:

American Life Insurance Company (ALICO)

AIG Star Life Insurance Co., Ltd. (AIG Star Life)

AIG Edison Life Insurance Company (AIG Edison Life)

American International Assurance Company, Limited, together with American International Assurance Company (Bermuda) Limited (AIA)

American International Reinsurance Company Limited (AIRCO)

Nan Shan Life Insurance Company, Ltd. (Nan Shan)

The Philippine American Life and General Insurance Company (Philamlife)

Financial Services

International Lease Finance Corporation (ILFC)

AIG Financial Products Corp. and AIG Trading Group Inc. and their respective subsidiaries (collectively, AIGFP)

American General Finance, Inc. (AGF)

AIG Consumer Finance Group, Inc. (AIGCFG)

Imperial A.I. Credit Companies (A.I. Credit)

Asset Management

AIG SunAmerica Asset Management Corp. (SAAMCo)

AIG Global Asset Management Holdings Corp. and its subsidiaries and affiliated companies (collectively, AIG Investments)

AIG Private Bank Ltd. (AIG Private Bank)

AIG Global Real Estate Investment Corp. (AIG Global Real Estate)

At December 31, 2007, AIG and its subsidiaries had approximately 116,000 employees.

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

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

**For information on AIG's business segments, see Note 2 to Consolidated Financial Statements.*

The following table presents the general development of the business of AIG on a consolidated basis, the contributions made to AIG's consolidated revenues and operating income and the assets held, in the periods indicated, by its General Insurance, Life Insurance & Retirement Services, Financial Services and Asset Management operations and Other operations. For additional information, see Item 6. Selected Financial Data, Management's Discussion and Analysis of Financial Condition and Results of Operations and Notes 1 and 2 to Consolidated Financial Statements.

Years Ended December 31, *(in millions)*	**2007**	2006[a]	2005[a]	2004[a]	2003[a]
General Insurance operations:					
Gross premiums written	**$ 58,798**	$ 56,280	$ 52,725	$ 52,046	$ 46,938
Net premiums written	**47,067**	44,866	41,872	40,623	35,031
Net premiums earned	**45,682**	43,451	40,809	38,537	31,306
Net investment income[b]	**6,132**	5,696	4,031	3,196	2,566
Net realized capital gains (losses)	**(106)**	59	334	228	(39)
Operating income[b][c][d]	**10,526**	10,412	2,315	3,177	4,502
Year-end identifiable assets	**181,708**	167,004	150,667	131,658	117,511
Statutory measures[e]:					
Statutory underwriting profit (loss)[c][d]	**4,073**	4,408	(2,165)	(564)	1,559
Loss ratio	**65.6**	64.6	81.1	78.8	73.1
Expense ratio	**24.7**	24.5	23.6	21.5	19.6
Combined ratio[d]	**90.3**	89.1	104.7	100.3	92.7
Life Insurance & Retirement Services operations:					
Premiums and other considerations	**33,627**	30,766	29,501	28,167	23,568
Net investment income[b]	**22,341**	20,024	18,677	15,654	13,278
Net realized capital gains (losses)[f]	**(2,398)**	88	(158)	45	362
Operating income[b][f]	**8,186**	10,121	8,965	7,968	6,970
Year-end identifiable assets	**615,386**	550,957	489,331	457,071	380,126
Gross insurance in force at end of year	**2,312,045**	2,070,600	1,852,833	1,858,094	1,583,031
Financial Services operations:					
Interest, lease and finance charges[g][h]	**(1,209)**	7,910	10,523	7,495	6,241
Net realized capital gains (losses)	**(100)**	(133)	154	(45)	123
Operating income (loss)[g][h]	**(9,515)**	383	4,424	2,131	1,302
Year-end identifiable assets	**203,894**	202,485	161,919	161,929	138,613
Asset Management operations:					
Investment income from spread-based products and management, advisory and incentive fees	**6,625**	4,668	4,500	4,179	3,379
Net realized capital gains (losses)	**(1,000)**	(125)	82	60	(754)
Operating income	**1,164**	1,538	1,963	1,947	521
Year-end identifiable assets	**77,274**	78,275	69,584	68,503	56,047
Other operations:					
Net realized capital gains (losses)	**12**	217	(71)	(244)	(134)
All other[i]	**(1,430)**	(984)	(2,383)	(134)	(1,254)
Consolidated:					
Total revenues[j][k]	**110,064**	113,387	108,781	97,823	79,601
Operating income[b][j][k]	**8,943**	21,687	15,213	14,845	11,907
Year-end total assets	**1,060,505**	979,410	853,048	801,007	675,602

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

(b) In 2006, includes the effect of out of period adjustments related to the accounting for certain interests in unit investment trusts (UCITS). The effect was an increase of $490 million in both revenues and operating income for General Insurance and an increase of $240 million and $169 million in revenues and operating income, respectively, for Life Insurance & Retirement Services.

(c) Includes current year catastrophe-related losses of $276 million, $2.89 billion and $1.05 billion in 2007, 2005 and 2004, respectively. There were no significant catastrophe-related losses in 2006 or 2003.

(d) Operating income was reduced by fourth quarter charges of $1.8 billion and $850 million in 2005 and 2004, respectively, resulting from the annual review of General Insurance loss and loss adjustment reserves. In 2006, 2005 and 2004, changes in estimates for asbestos and environmental reserves were $198 million, $873 million and $850 million, respectively.

(e) Calculated on the basis under which the U.S.-domiciled general insurance companies are required to report such measurements to regulatory authorities.

(f) In 2007, 2006, 2005, 2004 and 2003, includes other-than-temporary impairment charges of $2.8 billion, $641 million, $425 million, $441 million and $1.2 billion. See Management's Discussion and Analysis of Financial Condition and Results of Operations — Invested Assets — Other-than-temporary impairments.

(g) Includes gains (losses) from hedging activities that did not qualify for hedge accounting treatment under Statement of Financial Accounting Standards (FAS) No. 133, ''Accounting for Derivative Instruments and Hedging Activities'' (FAS 133), including the related foreign exchange gains and losses. In 2007, 2006, 2005, 2004 and 2003, respectively, the effect was $211 million, $(1.82) billion, $2.01 billion, $(122) million and $(1.01) billion in both revenues and operating income for Capital Markets. These amounts result primarily from interest rate and foreign currency derivatives that are effective economic hedges of investments and borrowings. These gains (losses) in 2007 include a $380 million out of period charge to reverse net gains recognized on transfers of available for sale securities among legal entities consolidated within AIGFP. In 2006, includes an out of period charge of $223 million related to the remediation of the material weakness in internal control over the accounting for certain derivative transactions under FAS 133. In the first quarter of 2007, AIGFP began applying hedge accounting for certain of its interest rate swaps and foreign currency forward contracts hedging its investments and borrowings.

(h) In 2007, both revenues and operating income (loss) include an unrealized market valuation loss of $11.5 billion on AIGFP super senior credit default swap portfolio and an other-than-temporary impairment charge of $643 million on AIGFP's available for sale investment securities. See Management's Discussion and Analysis of Financial Condition and Results of Operations — Invested Assets — Other-than-temporary impairments.

(i) In 2005, includes $1.6 billion of regulatory settlement costs as described under Item 3. Legal Proceedings.

(j) In 2007, 2006, 2005, 2004 and 2003, includes other-than-temporary impairment charges of $4.7 billion, $944 million, $598 million, $684 million and $1.5 billion. Also includes gains (losses) from hedging activities that did not qualify for hedge accounting treatment under FAS 133, including the related foreign exchange gains and losses. In 2007, 2006, 2005, 2004 and 2003, respectively, the effect was $(1.44) billion, $(1.87) billion, $2.02 billion, $385 million and $(1.50) billion in revenues and $(1.44) billion, $(1.87) billion, $2.02 billion, $671 million and $(1.22) billion in operating income. These amounts result primarily from interest rate and foreign currency derivatives that are effective economic hedges of investments and borrowings.

(k) Represents income before income taxes, minority interest and cumulative effect of accounting changes.

General Insurance Operations

AIG's General Insurance subsidiaries write substantially all lines of commercial property and casualty insurance and various personal lines both domestically and abroad. Domestic General Insurance operations are comprised of the Domestic Brokerage Group (DBG), Reinsurance, Personal Lines and Mortgage Guaranty.

AIG is diversified both in terms of classes of business and geographic locations. In General Insurance, workers compensation business is the largest class of business written and represented approximately 15 percent of net premiums written for the year ended December 31, 2007. During 2007, 10 percent and 7 percent of the direct General Insurance premiums written (gross premiums less return premiums and cancellations, excluding reinsurance assumed and before deducting reinsurance ceded) were written in California and New York, respectively. No other state or foreign country accounted for more than five percent of such premiums.

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

DBG

AIG's primary Domestic General Insurance division is DBG. DBG's business in the United States and Canada is conducted through American Home, National Union, Lexington, HSB and certain other General Insurance company subsidiaries of AIG. During 2007, DBG accounted for 51 percent of AIG's General Insurance net premiums written.

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

In addition to writing substantially all classes of business insurance, including large commercial or industrial property insurance, excess liability, inland marine, environmental, workers compensation and excess and umbrella coverages, DBG offers many specialized forms of insurance such as aviation, accident and health, equipment breakdown, directors and officers liability (D&O), difference-in-conditions, kidnap-ransom, export credit and political risk, and various types of professional errors and omissions coverages. Also included in DBG are the operations of AIG Risk Management, which provides insurance and risk management programs for large corporate customers and is a leading provider of customized structured insurance products, and AIG Environmental, which focuses specifically on providing specialty products to clients with environmental exposures. Lexington writes surplus lines for risks on which conventional insurance companies do not readily provide insurance coverage, either because of complexity or because the coverage does not lend itself to conventional contracts. The AIG Worldsource Division introduces and coordinates AIG's products and services to U.S.-based multinational clients and foreign corporations doing business in the U.S.

Reinsurance

The subsidiaries of Transatlantic Holdings, Inc. (Transatlantic) offer reinsurance on both a treaty and facultative basis to insurers in the United States and abroad. Transatlantic structures programs for a full range of property and casualty products with an emphasis on specialty risk. Transatlantic is a public company owned 59.0 percent by AIG and therefore is included in AIG's consolidated financial statements.

Personal Lines

AIG's Personal Lines operations provide automobile insurance through aigdirect.com, the newly formed operation resulting from the 2007 combination of AIG Direct and 21st Century Insurance Group (21st Century) operations, and the Agency Auto Division, as well as a broad range of coverages for high net worth individuals through the AIG Private Client Group.

Mortgage Guaranty

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

Foreign General Insurance

AIG's Foreign General Insurance group accepts risks primarily underwritten through American International Underwriters (AIU), a marketing unit consisting of wholly owned agencies and insurance companies. The Foreign General Insurance group also includes business written by AIG's foreign-based insurance subsidiaries. The Foreign General Insurance group uses various marketing methods and multiple distribution channels to write both commercial and consumer lines insurance with certain refinements for local laws, customs and needs. AIU operates in Asia, the Pacific Rim, Europe, the U.K., Africa, the Middle East and Latin America. During 2007, the Foreign General Insurance group accounted for 28 percent of AIG's General Insurance net premiums written.

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

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

Loss reserves established with respect to foreign business are set and monitored in terms of the currency in which payment is expected to be made. Therefore, no assumption is included for

changes in currency rates. See also Note 1(ff) to Consolidated Financial Statements.

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

The ''Analysis of Consolidated Losses and Loss Expense Reserve Development'' table presents the development of net losses and loss expense reserves for calendar years 1997 through 2007. Immediately following this table is a second table that presents all data on a basis that excludes asbestos and environmental net losses and loss expense reserve development. The opening reserves held are shown at the top of the table for each year end date. The amount of loss reserve discount included in the opening reserve at each date is shown immediately below the reserves held for each year. The undiscounted reserve at each date is thus the sum of the discount and the reserve held.

The upper half of the table presents the cumulative amounts paid during successive years related to the undiscounted opening loss reserves. For example, in the table that excludes asbestos and environmental losses, with respect to the net losses and loss expense reserve of $24.83 billion as of December 31, 2000, by the end of 2007 (seven years later) $33.05 billion had actually been paid in settlement of these net loss reserves. In addition, as reflected in the lower section of the table, the original undiscounted reserve of $26.12 billion was reestimated to be $41.21 billion at December 31, 2007. This increase from the original estimate would generally result from a combination of a number of factors, including reserves being settled for larger amounts than originally estimated. The original estimates will also be increased or decreased as more information becomes known about the individual claims and overall claim frequency and severity patterns. The redundancy (deficiency) depicted in the table, for any particular calendar year, presents the aggregate change in estimates over the period of years subsequent to the calendar year reflected at the top of the respective column heading. For example, the redundancy of $672 million at December 31, 2007 related to December 31, 2006 net losses and loss expense reserves of $62.72 billion represents the cumulative amount by which reserves in 2006 and prior years have developed favorably during 2007.

The bottom of each table below presents the remaining undiscounted and discounted net loss reserve for each year. For example, in the table that excludes asbestos and environmental losses, for the 2002 year end, the remaining undiscounted reserves held as of December 31, 2007 are $13.57 billion, with a corresponding discounted net reserve of $12.57 billion.

The reserves for net losses and loss expenses with respect to Transatlantic and 21st Century are included only in consolidated net losses and loss expenses commencing with the year ended December 31, 1998, the year they were first consolidated in AIG's financial statements. Reserve development for these operations is included only for 1998 and subsequent periods. Thus, the presentation for 1997 and prior year ends is not fully comparable to that for 1998 and subsequent years in the tables below.

Analysis of Consolidated Losses and Loss Expense Reserve Development

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

(in millions)	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006	**2007**
Net Reserves Held	$ 20,901	$ 25,418	$ 25,636	$ 25,684	$ 26,005	$ 29,347	$ 36,228	$ 47,254	$ 57,476	$62,630	**$69,288**
Discount (in Reserves Held)	619	897	1,075	1,287	1,423	1,499	1,516	1,553	2,110	2,264	**2,429**
Net Reserves Held (Undiscounted)	21,520	26,315	26,711	26,971	27,428	30,846	37,744	48,807	59,586	64,894	**71,717**
Paid (Cumulative) as of:											
One year later	5,607	7,205	8,266	9,709	11,007	10,775	12,163	14,910	15,326	14,862	
Two years later	9,754	12,382	14,640	17,149	18,091	18,589	21,773	24,377	25,152		
Three years later	12,939	16,599	19,901	21,930	23,881	25,513	28,763	31,296			
Four years later	15,484	20,263	23,074	26,090	28,717	30,757	33,825				
Five years later	17,637	22,303	25,829	29,473	32,685	34,627					
Six years later	18,806	24,114	28,165	32,421	35,656						
Seven years later	19,919	25,770	30,336	34,660							
Eight years later	21,089	27,309	31,956								
Nine years later	22,177	28,626									
Ten years later	23,096										

(in millions)	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006	**2007**
Net Reserves Held (undiscounted)	$ 21,520	$ 26,315	$ 26,711	$ 26,971	$ 27,428	$ 30,846	$ 37,744	$ 48,807	$ 59,586	$64,894	**$71,717**
Undiscounted Liability as of:											
One year later	21,563	25,897	26,358	26,979	31,112	32,913	40,931	53,486	59,533	64,238	
Two years later	21,500	25,638	27,023	30,696	33,363	37,583	49,463	55,009	60,126		
Three years later	21,264	26,169	29,994	32,732	37,964	46,179	51,497	56,047			
Four years later	21,485	28,021	31,192	36,210	45,203	48,427	52,964				
Five years later	22,405	28,607	33,910	41,699	47,078	49,855					
Six years later	22,720	30,632	38,087	43,543	48,273						
Seven years later	24,209	33,861	39,597	44,475							
Eight years later	26,747	34,986	40,217								
Nine years later	27,765	35,556									
Ten years later	28,104										
Net Redundancy/(Deficiency)	(6,584)	(9,241)	(13,506)	(17,504)	(20,845)	(19,009)	(15,220)	(7,240)	(540)	656	
Remaining Reserves (Undiscounted)	5,008	6,930	8,261	9,815	12,617	15,228	19,139	24,751	34,974	49,376	
Remaining Discount	418	499	591	705	851	1,005	1,155	1,319	1,563	1,937	
Remaining Reserves	4,590	6,431	7,670	9,110	11,766	14,223	17,984	23,432	33,411	47,439	

The following table presents the gross liability (before discount), reinsurance recoverable and net liability recorded at each year end and the reestimation of these amounts as of December 31, 2007:

(in millions)	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006	**2007**
Gross Liability, End of Year	$ 32,049	$ 36,973	$ 37,278	$ 39,222	$ 42,629	$ 48,173	$ 53,387	$ 63,431	$ 79,279	$82,263	**$87,929**
Reinsurance Recoverable, End of Year	10,529	10,658	10,567	12,251	15,201	17,327	15,643	14,624	19,693	17,369	**16,212**
Net Liability, End of Year	21,520	26,315	26,711	26,971	27,428	30,846	37,744	48,807	59,586	64,894	**71,717**
Reestimated Gross Liability	44,844	54,284	60,212	66,308	70,680	72,234	72,944	74,434	80,941	81,695	
Reestimated Reinsurance Recoverable	16,740	18,729	19,995	21,833	22,407	22,379	19,980	18,386	20,816	17,457	
Reestimated Net Liability	28,104	35,555	40,217	44,475	48,273	49,855	52,964	56,048	60,125	64,238	
Cumulative Gross Redundancy/(Deficiency)	(12,795)	(17,311)	(22,934)	(27,086)	(28,051)	(24,061)	(19,557)	(11,003)	(1,662)	568	

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

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

(in millions)	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006	**2007**
Net Reserves Held	$20,113	$ 24,554	$ 24,745	$ 24,829	$ 25,286	$ 28,650	$ 35,559	$45,742	$55,227	$60,451	**$67,597**
Discount (in Reserves Held)	619	897	1,075	1,287	1,423	1,499	1,516	1,553	2,110	2,264	**2,429**
Net Reserves Held (Undiscounted)	20,732	25,451	25,820	26,116	26,709	30,149	37,075	47,295	57,336	62,715	**70,026**
Paid (Cumulative) as of:											
One year later	5,467	7,084	8,195	9,515	10,861	10,632	11,999	14,718	15,047	14,356	
Two years later	9,500	12,190	14,376	16,808	17,801	18,283	21,419	23,906	24,367		
Three years later	12,618	16,214	19,490	21,447	23,430	25,021	28,129	30,320			
Four years later	14,972	19,732	22,521	25,445	28,080	29,987	32,686				
Five years later	16,983	21,630	25,116	28,643	31,771	33,353					
Six years later	18,014	23,282	27,266	31,315	34,238						
Seven years later	18,972	24,753	29,162	33,051							
Eight years later	19,960	26,017	30,279								
Nine years later	20,779	26,832									
Ten years later	21,202										

(in millions)	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006	**2007**
Net Reserves Held (undiscounted)	$20,732	$ 25,451	$ 25,820	$ 26,116	$ 26,709	$ 30,149	$ 37,075	$47,295	$57,336	$62,715	**$70,026**
Undiscounted Liability as of:											
One year later	20,576	24,890	25,437	26,071	30,274	32,129	39,261	51,048	57,077	62,043	
Two years later	20,385	24,602	26,053	29,670	32,438	35,803	46,865	52,364	57,653		
Three years later	20,120	25,084	28,902	31,619	36,043	43,467	48,691	53,385			
Four years later	20,301	26,813	30,014	34,102	42,348	45,510	50,140				
Five years later	21,104	27,314	31,738	38,655	44,018	46,925					
Six years later	21,336	28,345	34,978	40,294	45,201						
Seven years later	21,836	30,636	36,283	41,213							
Eight years later	23,441	31,556	36,889								
Nine years later	24,261	32,113									
Ten years later	24,588										
Net Redundancy/(Deficiency)	(3,856)	(6,662)	(11,069)	(15,097)	(18,492)	(16,776)	(13,065)	(6,090)	(317)	672	
Remaining Reserves (undiscounted)	3,386	5,281	6,610	8,162	10,963	13,572	17,454	23,065	33,286	47,687	
Remaining Discount	418	499	591	705	851	1,005	1,155	1,319	1,563	1,937	
Remaining Reserves	2,968	4,782	6,019	7,457	10,112	12,567	16,299	21,746	31,723	45,750	

The following table presents the gross liability (before discount), reinsurance recoverable and net liability recorded at each year end and the reestimation of these amounts as of December 31, 2007:

(in millions)	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006	**2007**
Gross Liability, End of Year	$29,740	$ 34,474	$ 34,666	$ 36,777	$ 40,400	$ 46,036	$ 51,363	$59,790	$73,808	$77,111	**$83,551**
Reinsurance Recoverable, End of Year	9,008	9,023	8,846	10,661	13,691	15,887	14,288	12,495	16,472	14,396	**13,525**
Net Liability, End of Year	20,732	25,451	25,820	26,116	26,709	30,149	37,075	47,295	57,336	62,715	**70,026**
Reestimated Gross Liability	35,712	45,467	51,801	58,420	63,320	65,217	66,320	68,100	75,028	76,439	
Reestimated Reinsurance Recoverable	11,124	13,354	14,912	17,207	18,119	18,292	16,180	14,715	17,375	14,396	
Reestimated Net Liability	24,588	32,113	36,889	41,213	45,201	46,925	50,140	53,385	57,653	62,043	
Cumulative Gross Redundancy/(Deficiency)	(5,972)	(10,993)	(17,135)	(21,643)	(22,920)	(19,181)	(14,957)	(8,310)	(1,220)	672	

The reserve for losses and loss expenses as reported in AIG's consolidated balance sheet at December 31, 2007 differs from the total reserve reported in the Annual Statements filed with state insurance departments and, where appropriate, with foreign regulatory authorities. The differences at December 31, 2007 relate primarily to reserves for certain foreign operations not required to be reported in the United States for statutory reporting purposes. Further, statutory practices in the United States require reserves to be shown net of applicable reinsurance recoverable.

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

For further discussion regarding net reserves for losses and loss expenses, see Management's Discussion and Analysis of Financial Condition and Results of Operations — Operating Review — General Insurance Operations — Reserve for Losses and Loss Expenses.

Life Insurance & Retirement Services Operations

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

Foreign Life Insurance & Retirement Services

In its Foreign Life Insurance & Retirement Services businesses, AIG operates principally through ALICO, AIG Star Life, AIG Edison Life, AIA, Nan Shan and Philamlife. ALICO is incorporated in Delaware and all of its business is written outside of the United States. ALICO has operations either directly or through subsidiaries in Europe, including the U.K., Latin America, the Caribbean, the Middle East, South Asia and the Far East, with Japan being the largest territory. ALICO also conducts life insurance business through a joint venture in Brazil. AIA operates primarily in China (including Hong Kong), Singapore, Malaysia, Thailand, Korea, Australia, New Zealand, Vietnam, Indonesia and India. The operations in India are conducted through a joint venture, Tata AIG Life Insurance Company Limited. Nan Shan operates in Taiwan. Philamlife is the largest life insurer in the Philippines. AIG Star Life and AIG Edison Life operate in Japan. Operations in foreign countries comprised 79 percent of Life Insurance & Retirement Services Premiums and other considerations and 76 percent of Life Insurance & Retirement Services operating income in 2007.

The Foreign Life Insurance & Retirement Services companies have over 285,000 full and part-time agents, as well as independent producers, and sell their products largely to indigenous persons in local and foreign currencies. In addition to the agency outlets, these companies also distribute their products through direct marketing channels, such as mass marketing, and through brokers and other distribution outlets, such as financial institutions.

Domestic Life Insurance & Retirement Services

AIG's principal Domestic Life Insurance & Retirement Services operations include AGLA, AIG American General, AIG Annuity, USLIFE, VALIC and AIG SunAmerica. These companies utilize multiple distribution channels including independent producers, brokerage, career agents and financial institutions to offer life insurance, annuity and accident and health products and services, as well as financial and other investment products. The Domestic Life Insurance & Retirement Services operations comprised 21 percent of total Life Insurance & Retirement Services Premiums and other considerations and 24 percent of Life Insurance & Retirement Services operating income in 2007.

Reinsurance

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

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

For a further discussion of reinsurance, see Item 1A. Risk Factors — Reinsurance; Management's Discussion and Analysis of Financial Condition and Results of Operations — Risk Management — Reinsurance; and Note 5 to Consolidated Financial Statements.

Insurance Investment Operations

A significant portion of AIG's General Insurance and Life Insurance & Retirement Services revenues are derived from AIG's insurance investment operations.

The following table summarizes the investment results of the insurance operations:

Years Ended December 31, *(in millions)*	Annual Average Cash and Invested Assets: Cash (including short-term investments)[(a)]	Invested Assets[(a)]	Total	Return on Average Cash and Invested Assets[(b)]	Return on Average Invested Assets[(c)]
General Insurance:					
2007	**$ 5,874**	**$117,050**	**$122,924**	**5.0%**	**5.2%**
2006	3,201	102,231	105,432	5.4	5.6
2005	2,450	86,211	88,661	4.5	4.7
2004	2,012	73,338	75,350	4.2	4.4
2003	1,818	59,855	61,673	4.2	4.3
Life Insurance & Retirement Services:					
2007	**$25,926**	**$423,473**	**$449,669**	**5.0%**	**5.3%**
2006	13,698	392,348	406,046	4.9	5.1
2005	11,137	356,839	367,976	5.1	5.2
2004	7,737	309,627	317,364	4.9	5.1
2003	4,680	247,608	252,288	5.3	5.4

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

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

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

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

Financial Services Operations

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

Aircraft Leasing

Aircraft Leasing operations represent the operations of ILFC, which generates its revenues primarily from leasing new and used commercial jet aircraft to foreign and domestic airlines. Revenues also result from the remarketing of commercial jets for ILFC's own account, and remarketing and fleet management services for airlines and financial institutions. See also Note 2 to Consolidated Financial Statements.

Capital Markets

Capital Markets represents the operations of AIGFP, which engages as principal in a wide variety of financial transactions, including standard and customized financial products involving commodities, credit, currencies, energy, equities and rates. The credit products include credit protection written through credit default swaps on super senior risk tranches of diversified pools of loans and debt securities. AIGFP also invests in a diversified portfolio of securities and principal investments and engages in borrowing activities that include issuing standard and structured notes and other securities and entering into guaranteed investment agreements (GIAs).

Consumer Finance

Consumer Finance operations include AGF as well as AIGCFG. AGF provides a wide variety of consumer finance products, including real estate and non-real estate loans, retail sales finance and credit-related insurance to customers in the United States, the U.K., Puerto Rico and the U.S. Virgin Islands. AGF's finance receivables are primarily sourced through its branches, although many of AGF's real estate loans are sourced through its centralized real estate operations, which include AGF's mortgage banking activities. AIGCFG, through its subsidiaries, is engaged in developing a multi-product consumer finance business with an emphasis on emerging and developing markets.

Asset Management Operations

AIG's Asset Management operations comprise a wide variety of investment-related services and investment products. These ser-

vices and products are offered to individuals, pension funds and institutions globally through AIG's Spread-Based Investment business, Institutional Asset Management, and Brokerage Services and Mutual Funds business. Also included in Asset Management operations are the results of certain SunAmerica sponsored partnership investments.

Spread-Based Investment Business

AIG's Spread-Based Investment business includes the results of AIG's proprietary spread-based investment operations, the Matched Investment Program (MIP), which was launched in September of 2005 to replace the Guaranteed Investment Contract (GIC) program, which is in runoff. The MIP is an investment strategy that involves investing in various asset classes with financing provided through third parties. This business uses various risk mitigating strategies designed to hedge interest rate and currency risk associated with underlying investments and related liabilities.

Institutional Asset Management

AIG's Institutional Asset Management business, conducted through AIG Investments, provides an array of investment products and services globally to institutional investors, pension funds, AIG subsidiaries and high net worth investors. These products include traditional equity and fixed income investments, and a wide range of alternative asset classes. These services include investment advisory and subadvisory services, investment monitoring and investment transaction structuring. Within the fixed income and equity asset classes, AIG Investments offers various forms of structured investments aimed at achieving superior returns or capital preservation. Within the alternative asset class, AIG Investments offers hedge and private equity fund-of-funds, direct investments and distressed debt investments.

AIG Global Real Estate provides a wide range of real estate investment and management services for AIG subsidiaries, as well as for third-party institutional investors, high net worth investors and pension funds. Through a strategic network of local real estate ventures, AIG Global Real Estate actively invests in and develops office, industrial, multi-family residential, retail, hotel and resort properties globally.

AIG Private Bank offers banking, trading and investment management services to private clients and institutions globally.

From time to time, AIG Investments acquires alternative investments, primarily consisting of direct controlling equity interests in private enterprises, with the intention of ''warehousing'' such investments until the investment or economic benefit thereof is transferred to a fund or other AIG-managed investment product. During the warehousing period, AIG bears the cost and risks associated with carrying these investments and consolidates them on its balance sheet and records the operating results until the investments are transferred, sold or otherwise divested. Changes in market conditions may negatively affect the fair value of these warehoused investments. Market conditions may impede AIG from launching new investment products for which these warehoused assets are being held, which could result in AIG not recovering its investment upon transfer or divestment. In the event that AIG is unable to transfer or otherwise divest its interest in the warehoused investment to third parties, AIG could be required to hold these investments indefinitely. In certain instances, the consolidated warehoused investments are not wholly owned by AIG. In such cases, AIG shares the risk associated with warehousing the asset with the minority interest investors.

Brokerage Services and Mutual Funds

AIG's Brokerage Services and Mutual Funds business, conducted through AIG Advisor Group, Inc. and AIG SunAmerica Asset Management Corp., provides broker-dealer related services and mutual funds to retail investors, group trusts and corporate accounts through an independent network of financial advisors. AIG Advisor Group, Inc., a subsidiary of AIG Retirement Services, Inc., is comprised of several broker-dealer entities that provide these services to clients primarily in the U.S. marketplace. AIG SunAmerica Asset Management Corp. manages, advises and/or administers retail mutual funds, as well as the underlying assets of variable annuities sold by AIG SunAmerica and VALIC to individuals and groups throughout the United States.

Other Asset Management

Included in Other Asset Management is income or loss from certain AIG SunAmerica sponsored partnerships and partnership investments. Partnership assets consist of investments in a diversified portfolio of private equity funds, affordable housing partnerships and hedge fund investments.

Other Operations

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

AIG has several other subsidiaries that engage in various businesses. Mt. Mansfield Company, Inc. owns and operates the ski slopes, lifts, a school and an inn located in Stowe, Vermont. Also reported in AIG's Other operations are interest expense, expenses of corporate staff not attributable to specific business segments, expenses related to efforts to improve internal controls, corporate initiatives, certain compensation plan expenses and the settlement costs more fully described in Item 3. Legal Proceedings and Note 12(a) to Consolidated Financial Statements.

Additional Investments

AIG's significant investments in partially owned companies (which are accounted for under the equity method) include a 25.4 percent interest in The Fuji Fire and Marine Insurance Co., Ltd., a general insurance company in Japan, a 26.0 percent interest in Tata AIG Life Insurance Company, Ltd. and a 26.0 percent interest

in Tata AIG General Insurance Company, Ltd. in India. Substantially all of AIG's equity interest in Allied World Assurance Holdings, Ltd. was sold by AIG in December 2007. For a discussion of AIG's investments in partially owned companies, see Note 1(s) to Consolidated Financial Statements.

Locations of Certain Assets

As of December 31, 2007, approximately 37 percent of the consolidated assets of AIG were located in foreign countries (other than Canada), including $4.4 billion of cash and securities on deposit with foreign regulatory authorities. Foreign operations and assets held abroad may be adversely affected by political developments in foreign countries, including tax changes, nationalization and changes in regulatory policy, as well as by consequence of hostilities and unrest. The risks of such occurrences and their overall effect upon AIG vary from country to country and cannot easily be predicted. If expropriation or nationalization does occur, AIG's policy is to take all appropriate measures to seek recovery of such assets. Certain of the countries in which AIG's business is conducted have currency restrictions which generally cause a delay in a company's ability to repatriate assets and profits. See also Notes 1 and 2 to Consolidated Financial Statements and Item 1A. Risk Factors — Foreign Operations.

Regulation

AIG's operations around the world are subject to regulation by many different types of regulatory authorities, including insurance, securities, investment advisory, banking and thrift regulators in the United States and abroad. The regulatory environment can have a significant effect on AIG and its business. AIG's operations have become more diverse and consumer-oriented, increasing the scope of regulatory supervision and the possibility of intervention. Although AIG cannot predict the scope or effect of such regulation on its business, AIG expects further regulation of its domestic consumer finance operations as a result of the current disruption of the U.S. residential mortgage market. In addition, the investigations into financial accounting practices that led to two restatements of AIG's consolidated financial statements have heightened regulatory scrutiny of AIG worldwide.

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

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

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

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

AIG has taken various steps to enhance the capital positions of the Domestic General Insurance companies. AIG entered into capital maintenance agreements with the Domestic General Insurance companies that set forth procedures through which AIG will provide ongoing capital support. Also, in order to allow the Domestic General Insurance companies to record as an admitted asset at December 31, 2007 certain reinsurance ceded to non-U.S. reinsurers (which has the effect of increasing the statutory surplus of such Domestic General Insurance companies), AIG obtained and entered into reimbursement agreements for approximately $1.8 billion of letters of credit issued by several commercial banks in favor of certain Domestic General Insurance companies.

In the U.S., Risk-Based Capital (RBC) is designed to measure the adequacy of an insurer's statutory surplus in relation to the risks inherent in its business. Thus, inadequately capitalized general and life insurance companies may be identified. The U.S. RBC formula develops a risk-adjusted target level of statutory

surplus by applying certain factors to various asset, premium and reserve items. Higher factors are applied to more risky items and lower factors are applied to less risky items. Thus, the target level of statutory surplus varies not only as a result of the insurer's size, but also based on the risk profile of the insurer's operations.

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

The statutory surplus of each of AIG's Domestic General Insurance and Life Insurance subsidiaries exceeded their RBC target levels as of December 31, 2007.

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

A substantial portion of AIG's General Insurance business and a majority of its Life Insurance business is carried on in foreign countries. The degree of regulation and supervision in foreign jurisdictions varies. Generally, AIG, as well as the underwriting companies operating in such jurisdictions, must satisfy local regulatory requirements. Licenses issued by foreign authorities to AIG subsidiaries are subject to modification or revocation by such authorities, and these subsidiaries could be prevented from conducting business in certain of the jurisdictions where they currently operate. In the past, AIG has been allowed to modify its operations to conform with new licensing requirements in most jurisdictions.

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

See Management's Discussion and Analysis of Financial Condition and Results of Operations — Capital Resources and Liquidity — Regulation and Supervision and Note 15 to Consolidated Financial Statements.

Competition

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

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

Directors and Executive Officers of AIG

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

Except as hereinafter noted, each of the executive officers has, for more than five years, occupied an executive position with AIG or companies that are now its subsidiaries. Other than the employment contracts between AIG and Messrs. Sullivan and Bensinger, there are no other arrangements or understandings between any executive officer and any other person pursuant to which the executive officer was elected to such position. From January 2000 until joining AIG in May 2004, Dr. Frenkel served as Chairman of Merrill Lynch International, Inc. Prior to joining AIG in September 2006, Ms. Kelly served as Executive Vice President and General Counsel of MCI/WorldCom. Previously, she was Senior Vice President and General Counsel of Sears, Roebuck and Co. from 1999 to 2003. From June 2004 until joining AIG in May 2007, Mr. Kaslow was a managing partner of QuanStar Group, LLC (an advisory services firm), and, from January 2002 until May 2004, Mr. Kaslow was Senior Executive Vice President of Human Resources for Vivendi Universal (an entertainment and telecommunications company).

Set forth below is information concerning the directors and executive officers of AIG as of February 28, 2008.

Name	Title	Age	Served as Director or Officer Since
Stephen F. Bollenbach	Director	65	2008
Marshall A. Cohen	Director	72	1992
Martin S. Feldstein	Director	68	1987
Ellen V. Futter	Director	58	1999
Stephen L. Hammerman	Director	69	2005
Richard C. Holbrooke	Director	66	2001
Fred H. Langhammer	Director	64	2006
George L. Miles, Jr.	Director	66	2005
Morris W. Offit	Director	71	2005
James F. Orr III	Director	64	2006
Virginia M. Rometty	Director	50	2006
Martin J. Sullivan	Director, President and Chief Executive Officer	53	2002
Michael H. Sutton	Director	67	2005
Edmund S. W. Tse	Director, Senior Vice Chairman – Life Insurance	70	1996
Robert B. Willumstad	Director and Chairman	62	2006
Frank G. Zarb	Director	73	2001
Jacob A. Frenkel	Vice Chairman – Global Economic Strategies	64	2004
Frank G. Wisner	Vice Chairman – External Affairs	69	1997
Steven J. Bensinger	Executive Vice President and Chief Financial Officer	53	2002
Anastasia D. Kelly	Executive Vice President, General Counsel and Senior Regulatory and Compliance Officer	58	2006
Rodney O. Martin, Jr.	Executive Vice President – Life Insurance	55	2002
Kristian P. Moor	Executive Vice President – Domestic General Insurance	48	1998
Win J. Neuger	Executive Vice President and Chief Investment Officer	58	1995
Robert M. Sandler	Executive Vice President – Domestic Personal Lines	65	1980
Nicholas C. Walsh	Executive Vice President – Foreign General Insurance	57	2005
Jay S. Wintrob	Executive Vice President – Retirement Services	50	1999
William N. Dooley	Senior Vice President – Financial Services	55	1992
David L. Herzog	Senior Vice President and Comptroller	48	2005
Andrew J. Kaslow	Senior Vice President and Chief Human Resources Officer	57	2007
Robert E. Lewis	Senior Vice President and Chief Risk Officer	56	1993
Brian T. Schreiber	Senior Vice President – Strategic Planning	42	2002

Item 1A.
Risk Factors

Casualty Insurance Underwriting and Reserves

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

Credit Market Environment

AIG's businesses may continue to be adversely affected by the current disruption in the global credit markets and repricing of credit risk. During the second half of 2007, disruption in the global credit markets, coupled with the repricing of credit risk, and the U.S. housing market deterioration created increasingly difficult conditions in the financial markets. These conditions have resulted in greater volatility, less liquidity, widening of credit spreads and a lack of price transparency in certain markets. These conditions continue to adversely affect Mortgage Guaranty's results of operations and the fair value of the AIGFP super senior credit default swap portfolio and contribute to higher levels of finance receivables delinquencies at AGF and to the severe and rapid decline in the fair value of certain investment securities, particularly those backed by U.S. residential mortgage loans. It is difficult to predict how long these conditions will exist and how AIG's markets, products and businesses will continue to be adversely affected. Accordingly, these conditions could adversely affect AIG's consolidated financial condition or results of operations in future periods. In addition, litigation and regulatory or governmental investigations and inquiries have been commenced against AIG related to these events and AIG may become subject to further litigation and regulatory or governmental scrutiny as a result of these events.

Risk Management

AIG is exposed to a number of significant risks, and AIG's risk management processes and controls may not be fully effective in mitigating AIG's risk exposures in all market conditions and to all types of risk. The major risks to which AIG is exposed include: credit risk, market risk, operational risk, liquidity risk and insurance risk. AIG has devoted significant resources to the development and implementation of risk management processes and controls across AIG's operations, including by establishing review and oversight committees to monitor risks, setting limits and identifying risk mitigating strategies and techniques. Nonetheless, these procedures may not be fully effective in mitigating risk exposure in all market conditions, some of which change rapidly and severely. A failure of AIG's risk management processes or the ineffectiveness of AIG's risk mitigating strategies and techniques could adversely affect, perhaps materially, AIG's consolidated results of operations, liquidity or financial condition, result in regulatory action or litigation or damage AIG's reputation. See Management's Discussion and Analysis of Financial Condition and Results of Operations — Risk Management.

Liquidity

AIG's liquidity could be impaired by an inability to access the capital markets or by unforeseen significant outflows of cash. This situation may arise due to circumstances that AIG may be unable to control, such as a general market disruption or an operational problem that affects third parties or AIG. In addition, this situation may arise due to circumstances specific to AIG, such as a decline in its credit ratings. AIG depends on dividends, distributions and other payments from its subsidiaries to fund dividend payments and to fund payments on AIG's obligations, including debt obligations. Regulatory and other legal restrictions may limit AIG's ability to transfer funds freely, either to or from its subsidiaries. In particular, many of AIG's subsidiaries, including AIG's insurance subsidiaries, are subject to laws and regulations that authorize regulatory bodies to block or reduce the flow of funds to the parent holding company, or that prohibit such transfers altogether in certain circumstances. These laws and regulations may hinder AIG's ability to access funds that AIG may need to make payments on its obligations. See also Item 1. Business — Regulation.

Some of AIG's investments are relatively illiquid and would be difficult to sell, or to sell at acceptable prices, if AIG required cash in amounts greater than its customary needs. AIG's investments in certain securities, including certain structured securities, direct private equities, limited partnerships, hedge funds, mortgage loans, flight equipment, finance receivables and real estate are relatively illiquid. These asset classes represented approximately 23 percent of the carrying value of AIG's total cash and invested assets as of December 31, 2007. In addition, the current disruption in the credit markets has affected the liquidity of other AIG portfolios

including the residential mortgage-backed securities portfolio. If AIG requires significant amounts of cash on short notice in excess of normal cash requirements or is required to post or return collateral in connection with its investment portfolio, derivative transactions or securities lending activities, then AIG may have difficulty selling these investments or terminating these transactions in a timely manner or may be forced to sell or terminate them for less than what AIG might otherwise have been able to, or both. Although AIGFP has no current intent to do so, if AIGFP sells or closes out its derivative transactions prior to maturity, the effect could be significant to AIG's overall liquidity.

AIG's liquidity may be adversely affected by requirements to post collateral. Certain of the credit default swaps written by AIGFP contain collateral posting requirements. The amount of collateral required to be posted for most of these transactions is determined based on the value of the security or loan referenced in the documentation for the credit default swap. Continued declines in the values of these referenced securities or loans will increase the amount of collateral AIGFP must post which could impair AIG's liquidity.

See also Management's Discussion and Analysis of Financial Condition and Results of Operations — Capital Resources and Liquidity — Liquidity.

Investment Concentration

Concentration of AIG's investment portfolios in any particular segment of the economy may have adverse effects. Any concentration of AIG's investment portfolios in any particular industry, group of related industries, asset classes, such as residential mortgage-backed securities and other asset-backed securities, or geographic sector could have an adverse effect on the investment portfolios and consequently on AIG's consolidated results of operations or financial condition. While AIG seeks to mitigate this risk by having a broadly diversified portfolio, events or developments that have a negative effect on any particular industry, asset class, group of related industries or geographic region may have a greater adverse effect on the investment portfolios to the extent that the portfolios are concentrated. Further, AIG's ability to sell assets relating to such particular groups of related assets may be limited if other market participants are seeking to sell at the same time.

Credit Ratings

Ratings actions regarding AIG could adversely affect AIG's business and its consolidated results of operations. Following AIG's filing with the SEC on February 11, 2008 of a Current Report on Form 8-K regarding the valuation of AIGFP's super senior credit default swap portfolio and reporting the conclusion by AIG's independent auditors that AIG had a material weakness in internal control over financial reporting and oversight relating to this valuation, the following credit rating actions were taken:

- Standard & Poor's, a division of The McGraw-Hill Companies, Inc. (S&P) affirmed its 'AA' counterparty credit ratings on AIG and its 'AA+' counterparty credit and financial strength ratings on AIG's core subsidiaries, but revised the rating outlook to negative. In addition, S&P revised its rating outlook on ILFC's corporate credit rating (AA-) to negative. A negative ratings outlook by S&P indicates that a rating may be lowered, but is not necessarily a precursor of a ratings change.
- Moody's Investors Service (Moody's) changed its rating outlook for AIG and its subsidiaries that have substantial exposure to the U.S. subprime mortgage market or whose ratings rely on significant explicit or implicit support from AIG to negative. Moody's rates AIG 'Aa2' and nearly all of its insurance subsidiaries either 'Aa1' or 'Aa2'. A negative ratings outlook by Moody's indicates that a rating may be lowered, but is not necessarily a precursor of a ratings change.
- Fitch Ratings (Fitch) placed AIG's and its subsidiaries' long-term debt ratings (AA), including ILFC (A+) and AGF (A+), on Rating Watch Negative. Rating Watch Negative indicates that a rating has been placed on active rating watch status. Fitch indicated that it expects to resolve the Rating Watch after it reviews AIG's 2007 audited financial statements.
- A.M. Best Company (A.M. Best) placed most of its financial strength and issuer credit ratings on AIG's domestic Life Insurance and Retirement Services (A++) and Domestic General Insurance subsidiaries (including Transatlantic) (A+), as well as AIG's issuer credit rating (AA), under review with negative implications. A.M. Best indicated that following a detailed review of AIG's 2007 audited financial statements and further discussion with AIG management, it will re-evaluate the ''under review'' rating status.

Financial strength and credit ratings by the major ratings agencies are an important factor in establishing the competitive position of insurance companies and other financial institutions and affect the availability and cost of borrowings. Financial strength ratings measure an insurance company's ability to meet its obligations to contract holders and policyholders, help to maintain public confidence in a company's products, facilitate marketing of products and enhance a company's competitive position. Credit ratings measure a company's ability to repay its obligations and directly affect the cost and availability to that company of unsecured financing. AIG's ratings have historically provided it with a competitive advantage. However, a ratings downgrade could adversely affect AIG's business and its consolidated results of operations in a number of ways, including:

- increasing AIG's interest expense;
- reducing AIGFP's ability to compete in the structured products and derivatives businesses;
- reducing the competitive advantage of AIG's insurance subsidiaries, which may result in reduced product sales;
- adversely affecting relationships with agents and sales representatives;
- in the case of a downgrade of AGF or ILFC, increasing their interest expense and reducing their ability to compete in their respective businesses; and
- triggering the application of a termination provision in certain of AIG's contracts, principally agreements entered into by AIGFP and assumed reinsurance contracts entered into by Transatlantic.

In the event of a downgrade of AIG, AIG would be required to post additional collateral. It is estimated that, as of the close of business on February 14, 2008, based on AIG's outstanding municipal GIAs and financial derivatives transactions as of such date, a further downgrade of AIG's long-term senior debt ratings to Aa3 by Moody's or AA- by S&P would permit counterparties to call for approximately $1.39 billion of additional collateral. Further, additional downgrades could result in requirements for substantial additional collateral, which could have a material effect on how AIG manages its liquidity. For a further discussion of AIG's credit ratings and the potential effect of posting collateral on AIG's liquidity, see Management's Discussion and Analysis of Financial Condition and Results of Operations — Capital Resources and Liquidity — Credit Ratings and — Liquidity.

Catastrophe Exposures

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

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

Reinsurance

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

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

Adjustments to Life Insurance & Retirement Services Deferred Policy Acquisition Costs

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

DAC for both insurance-oriented and investment-oriented products as well as retirement services products is reviewed for recoverability, which involves estimating the future profitability of current business. This review involves significant management judgment. If the actual emergence of future profitability were to be substantially lower than estimated, AIG could be required to accelerate its DAC amortization and such acceleration could adversely affect AIG's results of operations. See also Management's Discussion and Analysis of Financial Condition and Results of Operations — Critical Accounting Estimates and Notes 1 and 6 to Consolidated Financial Statements.

Use of Estimates

If actual experience differs from management's estimates used in the preparation of financial statements, AIG's consolidated results of operations or financial condition could be adversely affected. The preparation of financial statements in conformity with accounting principles generally accepted in the United States requires the application of accounting policies that often involve a significant degree of judgment. AIG considers that its accounting policies that are most dependent on the application of estimates and assumptions, and therefore viewed as critical accounting estimates, are those described in Management's Discussion and Analysis of Financial Condition and Results of Operations — Critical Accounting Estimates. These accounting estimates require the use of assumptions, some of which are highly uncertain at the time of estimation. For example, recent market volatility and declines in liquidity have made it more difficult to value certain of AIG's invested assets and the obligations and collateral relating to certain financial instruments issued or held by AIG, such as

AIGFP's super senior credit default swap portfolio. To the extent actual experience differs from the assumptions used, AIG's consolidated results of operations or financial condition would be directly affected, perhaps materially.

Legal Proceedings

Significant legal proceedings may adversely affect AIG's results of operations. AIG is party to numerous legal proceedings and regulatory or governmental investigations. It is possible that the effect of these unresolved matters could be material to AIG's consolidated results of operations for an individual reporting period. For a discussion of these unresolved matters, see Item 3. Legal Proceedings.

Foreign Operations

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

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

Regulation

AIG is subject to extensive regulation in the jurisdictions in which it conducts its businesses. AIG's operations around the world are subject to regulation by different types of regulatory authorities, including insurance, securities, investment advisory, banking and thrift regulators in the United States and abroad. AIG's operations have become more diverse and consumer-oriented, increasing the scope of regulatory supervision and the possibility of intervention. In particular, AIG's consumer lending business is subject to a broad array of laws and regulations governing lending practices and permissible loan terms, and AIG would expect increased regulatory oversight relating to this business.

The regulatory environment could have a significant effect on AIG and its businesses. Among other things, AIG could be fined, prohibited from engaging in some of its business activities or subject to limitations or conditions on its business activities. Significant regulatory action against AIG could have material adverse financial effects, cause significant reputational harm or harm business prospects. New laws or regulations or changes in the enforcement of existing laws or regulations applicable to clients may also adversely affect AIG and its businesses.

A Material Weakness

A material weakness in internal control over financial reporting and oversight relating to the AIGFP valuation of its super senior credit default swap portfolio could adversely affect the accuracy or timing of future regulatory filings. AIG's management has concluded that a material weakness relating to the internal control over financial reporting and oversight relating to the fair value valuation of the AIGFP super senior credit default swap portfolio existed as of December 31, 2007. Until remediated, this weakness could adversely affect the accuracy or timing of future filings with the SEC and other regulatory authorities. A discussion of this material weakness and AIG's remediation efforts can be found in Item 9A. Controls and Procedures — Management's Report on Internal Control Over Financial Reporting.

Employee Error and Misconduct

Employee error and misconduct may be difficult to detect and prevent and may result in significant losses. Losses may result from, among other things, fraud, errors, failure to document transactions properly or to obtain proper internal authorization or failure to comply with regulatory requirements.

There have been a number of highly publicized cases involving fraud or other misconduct by employees in the financial services industry in recent years, and AIG runs the risk that employee misconduct could occur. It is not always possible to deter or prevent employee misconduct and the controls that AIG has in place to prevent and detect this activity may not be effective in all cases.

Aircraft Suppliers

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

Item 1B.
Unresolved Staff Comments

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

Item 2.
Properties

AIG and its subsidiaries operate from approximately 2,100 offices in the United States, 6 offices in Canada and numerous offices in approximately 100 foreign countries. The offices in Greensboro and Winston-Salem, North Carolina; Springfield, Illinois; Amarillo, Ft. Worth, Houston and Lewisville, Texas; Wilmington, Delaware; San Juan, Puerto Rico; Tampa, Florida; Livingston, New Jersey; Evansville, Indiana; Nashville, Tennessee; 70 Pine Street, 72 Wall Street and 175 Water Street in New York, New York; and offices in more than 30 foreign countries and jurisdictions including Bermuda, Chile, Hong Kong, the Philippines, Japan, the U.K., Singapore, Malaysia, Switzerland, Taiwan and Thailand are located in buildings owned by AIG and its subsidiaries. The remainder of the office space utilized by AIG subsidiaries is leased.

Item 3.
Legal Proceedings

General

AIG and its subsidiaries, in common with the insurance industry in general, are subject to litigation, including claims for punitive damages, in the normal course of their business. See also Note 12(a) to Consolidated Financial Statements, as well as the discussion and analysis of Reserve for Losses and Loss Expenses under Operating Review — General Insurance Operations in Management's Discussion and Analysis of Financial Condition and Results of Operations.

Litigation Arising from Operations. AIG and its subsidiaries, in common with the insurance and financial services industries in general, are subject to litigation, including claims for punitive damages, in the normal course of their business. In AIG's insurance operations, litigation arising from claims settlement activities is generally considered in the establishment of AIG's reserve for losses and loss expenses. However, the potential for increasing jury awards and settlements makes it difficult to assess the ultimate outcome of such litigation.

Litigation Arising from Insurance Operations — Caremark. AIG and certain of its subsidiaries have been named defendants in two putative class actions in state court in Alabama that arise out of the 1999 settlement of class and derivative litigation involving Caremark Rx, Inc. (Caremark). The plaintiffs in the second-filed action have intervened in the first-filed action, and the second-filed action has been dismissed. An excess policy issued by a subsidiary of AIG with respect to the 1999 litigation was expressly stated to be without limit of liability. In the current actions, plaintiffs allege that the judge approving the 1999 settlement was misled as to the extent of available insurance coverage and would not have approved the settlement had he known of the existence and/or unlimited nature of the excess policy. They further allege that AIG, its subsidiaries, and Caremark are liable for fraud and suppression for misrepresenting and/or concealing the nature and extent of coverage. In addition, the intervenor-plaintiffs allege that various lawyers and law firms who represented parties in the underlying class and derivative litigation (the ''Lawyer Defendants'') are also liable for fraud and suppression, misrepresentation, and breach of fiduciary duty. The complaints filed by the plaintiffs and the intervenor-plaintiffs request compensatory damages for the 1999 class in the amount of $3.2 billion, plus punitive damages. AIG and its subsidiaries deny the allegations of fraud and suppression and have asserted that information concerning the excess policy was publicly disclosed months prior to the approval of the settlement. AIG and its subsidiaries further assert that the current claims are barred by the statute of limitations and that plaintiffs' assertions that the statute was tolled cannot stand against the public disclosure of the excess coverage. The plaintiffs and intervenor-plaintiffs, in turn, have asserted that the disclosure was insufficient to inform them of the nature of the coverage and did not start the running of the statute of limitations. On November 26, 2007, the trial court issued an order that dismissed the intervenors' complaint against the Lawyer Defendants and entered a final judgment in favor of the Lawyer Defendants. The intervenors are appealing the dismissal of the Lawyer Defendants and have requested a stay of all trial court proceedings pending the appeal. If the motion to stay is granted, no further proceedings at the trial court level will occur until the appeal is resolved. If the motion to stay is denied, the next step will be to proceed with class discovery so that the trial court can determine, under standards mandated by the Alabama Supreme Court, whether the action should proceed as a class action. AIG cannot reasonably estimate either the likelihood of its prevailing in these actions or the potential damages in the event liability is determined.

Litigation Arising from Insurance Operations — Gunderson. A subsidiary of AIG has been named as a defendant in a putative class action lawsuit in the 14th Judicial District Court for the State of Louisiana (Gunderson). The *Gunderson* complaint alleges failure to comply with certain provisions of the Louisiana Any Willing Provider Act (the Act) relating to discounts taken by defendants on bills submitted by Louisiana medical providers and hospitals that provided treatment or services to workers compensation claimants and seeks monetary penalties and injunctive relief. On July 20, 2006, the court denied defendants' motion for summary judgment and granted plaintiffs' partial motion for summary judgment, holding that the AIG subsidiary was a ''group purchaser'' and, therefore, potentially subject to liability under the Act. On November 28, 2006, the court issued an order certifying a class of providers and hospitals. In an unrelated action also arising under the Act, a Louisiana appellate court ruled that the district court lacked jurisdiction to adjudicate the claims at issue. In response, defendants in *Gunderson* filed an exception for lack of subject matter jurisdiction. On January 19, 2007, the court denied the motion, holding that it has jurisdiction over the putative class claims. The AIG subsidiary appealed the class certification and jurisdictional rulings. While the appeal was pending, the AIG subsidiary settled the lawsuit. On January 25, 2008, plaintiffs and the AIG subsidiary agreed to resolve the lawsuit on a class-wide basis for approximately $29 million. The court has preliminarily approved the settlement and will hold a final approval hearing on May 29, 2008. In the event that the settlement is not finally approved, AIG believes that it has meritorious defenses to

plaintiffs' claims and expects that the ultimate resolution of this matter will not have a material adverse effect on AIG's consolidated financial condition or results of operations for any period.

2006 Regulatory Settlements. In February 2006, AIG reached a resolution of claims and matters under investigation with the United States Department of Justice (DOJ), the Securities and Exchange Commission (SEC), the Office of the New York Attorney General (NYAG) and the New York State Department of Insurance (DOI). AIG recorded an after-tax charge of $1.15 billion relating to these settlements in the fourth quarter of 2005.

The settlements resolved investigations conducted by the SEC, NYAG and DOI in connection with the accounting, financial reporting and insurance brokerage practices of AIG and its subsidiaries, as well as claims relating to the underpayment of certain workers compensation premium taxes and other assessments. These settlements did not, however, resolve investigations by regulators from other states into insurance brokerage practices related to contingent commissions and other broker-related conduct, such as alleged bid rigging. Nor did the settlements resolve any obligations that AIG may have to state guarantee funds in connection with any of these matters.

As a result of these settlements, AIG made payments or placed amounts in escrow in 2006 totaling approximately $1.64 billion, $225 million of which represented fines and penalties. Amounts held in escrow totaling $347 million, including interest thereon, are included in other assets at December 31, 2007. At that date, approximately $330 million of the funds were escrowed for settlement of claims resulting from the underpayment by AIG of its residual market assessments for workers compensation. On May 24, 2007, The National Workers Compensation Reinsurance Pool, on behalf of its participant members, filed a lawsuit against AIG with respect to the underpayment of such assessments. On August 6, 2007, the court denied AIG's motion seeking to dismiss or stay the complaint or in the alternative, to transfer to the Southern District of New York. On December 26, 2007, the court denied AIG's motion to dismiss the complaint. AIG filed its answer on January 22, 2008. On February 5, 2008, following agreement of the parties, the court entered an order staying all proceedings through March 3, 2008. In addition, a similar lawsuit filed by the Minnesota Workers Compensation Reinsurance Association and the Minnesota Workers Compensation Insurers Association is pending. On August 6, 2007, AIG moved to dismiss the complaint and that motion is under review. A purported class action was filed in South Carolina Federal Court on January 25, 2008 against AIG and certain of its subsidiaries, on behalf of a class of employers that obtained workers compensation insurance from AIG companies and allegedly paid inflated premiums as a result of AIG's alleged underreporting of workers compensation premiums. AIG cannot currently estimate whether the amount ultimately required to settle these claims will exceed the funds escrowed or otherwise accrued for this purpose.

AIG has settled litigation that was filed by the Minnesota Attorney General with respect to claims by the Minnesota Department of Revenue and the Minnesota Special Compensation Fund.

The National Association of Insurance Commissioners has formed a Market Analysis Working Group directed by the State of Indiana, which has commenced its own investigation into the underreporting of workers compensation premiums. In early 2008, AIG was informed that the Market Analysis Working Group had been disbanded in favor of a multi-state targeted market conduct exam focusing on worker's compensation insurance.

The remaining escrowed funds, which amounted to $17 million at December 31, 2007, are set aside for settlements for certain specified AIG policyholders. As of February 20, 2008, eligible policyholders entitled to receive approximately $359 million (or 95 percent) of the excess casualty fund had opted to receive settlement payments in exchange for releasing AIG and its subsidiaries from liability relating to certain insurance brokerage practices. Amounts remaining in the excess casualty fund may be used by AIG to settle claims from other policyholders relating to such practices through February 29, 2008 (originally set for January 31, 2008 and later extended), after which they will be distributed pro rata to participating policyholders.

In addition to the escrowed funds, $800 million was deposited into a fund under the supervision of the SEC as part of the settlements to be available to resolve claims asserted against AIG by investors, including the shareholder lawsuits described herein.

Also, as part of the settlements, AIG agreed to retain, for a period of three years, an independent consultant to conduct a review that will include, among other things, the adequacy of AIG's internal control over financial reporting, the policies, procedures and effectiveness of AIG's regulatory, compliance and legal functions and the remediation plan that AIG has implemented as a result of its own internal review.

Other than as described above, at the current time, AIG cannot predict the outcome of the matters described above, or estimate any potential additional costs related to these matters.

Private Litigation

Securities Actions. Beginning in October 2004, a number of putative securities fraud class action suits were filed against AIG and consolidated as *In re American International Group, Inc. Securities Litigation.* Subsequently, a separate, though similar, securities fraud action was also brought against AIG by certain Florida pension funds. The lead plaintiff in the class action is a group of public retirement systems and pension funds benefiting Ohio state employees, suing on behalf of themselves and all purchasers of AIG's publicly traded securities between October 28, 1999 and April 1, 2005. The named defendants are AIG and a number of present and former AIG officers and directors, as well as C.V. Starr & Co., Inc. (Starr), Starr International Company, Inc. (SICO), General Reinsurance Corporation, and PricewaterhouseCoopers LLP (PwC), among others. The lead plaintiff alleges, among other things, that AIG: (1) concealed that it engaged in anti-competitive conduct through alleged payment of contingent commissions to brokers and participation in illegal bid-rigging; (2) concealed that it used ''income smoothing'' products and other techniques to inflate its earnings; (3) concealed that it marketed and sold ''income smoothing'' insurance products to other companies; and (4) misled investors about the scope of

government investigations. In addition, the lead plaintiff alleges that AIG's former Chief Executive Officer manipulated AIG's stock price. The lead plaintiff asserts claims for violations of Sections 11 and 15 of the Securities Act of 1933, Section 10(b) of the Exchange Act, and Rule 10b-5 promulgated thereunder, Section 20(a) of the Exchange Act, and Section 20A of the Exchange Act. In April 2006, the court denied the defendants' motions to dismiss the second amended class action complaint and the Florida complaint. In December 2006, a third amended class action complaint was filed, which does not differ substantially from the prior complaint. Fact and class discovery is currently ongoing. On February 20, 2008, the lead plaintiff filed a motion for class certification.

ERISA Action. Between November 30, 2004 and July 1, 2005, several Employee Retirement Income Security Act of 1974 (ERISA) actions were filed on behalf of purported class of participants and beneficiaries of three pension plans sponsored by AIG or its subsidiaries. A consolidated complaint filed on September 26, 2005 alleges a class period between September 30, 2000 and May 31, 2005 and names as defendants AIG, the members of AIG's Retirement Board and the Administrative Boards of the plans at issue, and four present or former members of AIG's Board of Directors. The factual allegations in the complaint are essentially identical to those in the securities actions described above. The parties have reached an agreement in principle to settle this matter for an amount within AIG's insurance coverage limits.

Securities Action — Oregon State Court. On February 27, 2008, The State of Oregon, by and through the Oregon State Treasurer, and the Oregon Public Employee Retirement Board, on behalf of the Oregon Public Employee Retirement Fund, filed a lawsuit against American International Group, Inc. for damages arising out of plaintiffs' purchase of AIG common stock at prices that allegedly were inflated. Plaintiffs allege, among other things, that AIG: (1) made false and misleading statements concerning its accounting for a $500 million transaction with General Re; (2) concealed that it marketed and misrepresented its control over off-shore entities in order to improve financial results; (3) improperly accounted for underwriting losses as investment losses in connection with transactions involving CAPCO Reinsurance Company, Ltd. and Union Excess; (4) misled investors about the scope of government investigations; and (5) engaged in market manipulation through its then Chairman and CEO Maurice R. Greenberg. The complaint asserts claims for violations of Oregon Securities Law, and seeks compensatory damages in an amount in excess of $15 million, and prejudgement interest and costs and fees.

Derivative Actions — Southern District of New York. On November 20, 2007, two purported shareholder derivative actions were filed in the Southern District of New York naming as defendants the then-current directors of AIG and certain senior officers of AIG and its subsidiaries. Plaintiffs assert claims for breach of fiduciary duty, waste of corporate assets and unjust enrichment, as well as violations of Section 10(b) of the Exchange Act and Rule 10b-5 promulgated thereunder, and Section 20(a) of the Exchange Act, among other things, in connection with AIG's public disclosures regarding its exposure to what the lawsuits describe as the subprime market crisis. The actions were consolidated as *In re American International Group, Inc. 2007 Derivative Litigation*. On February 15, 2008, plaintiffs filed a consolidated amended complaint alleging the same causes of action.

Between October 25, 2004 and July 14, 2005, seven separate derivative actions were filed in the Southern District of New York, five of which were consolidated into a single action. The New York derivative complaint contains nearly the same types of allegations made in the securities fraud and ERISA actions described above. The named defendants include current and former officers and directors of AIG, as well as Marsh & McLennan Companies, Inc. (Marsh), SICO, Starr, ACE Limited and subsidiaries (ACE), General Reinsurance Corporation, PwC, and certain employees or officers of these entity defendants. Plaintiffs assert claims for breach of fiduciary duty, gross mismanagement, waste of corporate assets, unjust enrichment, insider selling, auditor breach of contract, auditor professional negligence and disgorgement from AIG's former Chief Executive Officer and Chief Financial Officer of incentive-based compensation and AIG share proceeds under Section 304 of the Sarbanes-Oxley Act, among others. Plaintiffs seek, among other things, compensatory damages, corporate governance reforms, and a voiding of the election of certain AIG directors. AIG's Board of Directors has appointed a special committee of independent directors (special committee) to review the matters asserted in the operative consolidated derivative complaint. The court has entered an order staying the derivative case in the Southern District of New York pending resolution of the consolidated derivative action in the Delaware Chancery Court (discussed below). The court also has entered an order that termination of certain named defendants from the Delaware derivative action applies to the New York derivative action without further order of the court. On October 17, 2007, plaintiffs and those AIG officer and director defendants against whom the shareholder plaintiffs in the Delaware action are no longer pursuing claims filed a stipulation providing for all claims in the New York action against such defendants to be dismissed with prejudice. Former directors and officers Maurice R. Greenberg and Howard I. Smith have asked the court to refrain from so ordering this stipulation.

Derivative Actions — Delaware Chancery Court. From October 2004 to April 2005, AIG shareholders filed five derivative complaints in the Delaware Chancery Court. All of these derivative lawsuits were consolidated into a single action as *In re American International Group, Inc. Consolidated Derivative Litigation*. The amended consolidated complaint named 43 defendants (not including nominal defendant AIG) who, like the New York consolidated derivative litigation, were current and former officers and directors of AIG, as well as other entities and certain of their current and former employees and directors. The factual allegations, legal claims and relief sought in the Delaware action are similar to those alleged in the New York derivative actions, except that shareholder plaintiffs in the Delaware derivative action assert claims only under state law. Earlier in 2007, the Court approved an agreement that AIG be realigned as plaintiff, and, on June 13,

2007, acting on the direction of the special committee, AIG filed an amended complaint against former directors and officers Maurice R. Greenberg and Howard I. Smith, alleging breach of fiduciary duty and indemnification. Also on June 13, 2007, the special committee filed a motion to terminate the litigation as to certain defendants, while taking no action as to others. Defendants Greenberg and Smith filed answers to AIG's complaint and brought third-party complaints against certain current and former AIG directors and officers, PwC and Regulatory Insurance Services, Inc. On September 28, 2007, AIG and the shareholder plaintiffs filed a combined amended complaint in which AIG continued to assert claims against defendants Greenberg and Smith and took no position as to the claims asserted by the shareholder plaintiffs in the remainder of the combined amended complaint. In that pleading, the shareholder plaintiffs are no longer pursuing claims against certain AIG officers and directors. In November 2007, the shareholder plaintiffs moved to sever their claims to a separate action. AIG joined the motion to the extent that, among other things, the claims against defendants Greenberg and Smith would remain in prosecution in the pending action. In addition, a number of parties, including AIG, filed motions to stay discovery. On February 12, 2008, the court granted AIG's motion to stay discovery pending the resolution of claims against AIG in the New York consolidated securities action. The court also denied plaintiff's motion to sever and directed the parties to coordinate a briefing schedule for the motions to dismiss.

A separate derivative lawsuit was filed in December 2002 in the Delaware Chancery Court against twenty directors and executives of AIG as well as against AIG as a nominal defendant that alleges, among other things, that the directors of AIG breached the fiduciary duties of loyalty and care by approving the payment of commissions to Starr and of rental and service fees to SICO and the executives breached their duty of loyalty by causing AIG to enter into contracts with Starr and SICO and their fiduciary duties by usurping AIG's corporate opportunity. The complaint further alleges that the Starr agencies did not provide any services that AIG was not capable of providing itself, and that the diversion of commissions to these entities was solely for the benefit of Starr's owners. The complaint also alleged that the service fees and rental payments made to SICO and its subsidiaries were improper. Under the terms of a stipulation approved by the Court on February 16, 2006, the claims against the outside independent directors were dismissed with prejudice, while the claims against the other directors were dismissed without prejudice. On October 31, 2005, defendants Greenberg, Matthews, Smith, SICO and Starr filed motions to dismiss the amended complaint. In an opinion dated June 21, 2006, the Court denied defendants' motion to dismiss, except with respect to plaintiff's challenge to payments made to Starr before January 1, 2000. On July 21, 2006, plaintiff filed its second amended complaint, which alleges that, between January 1, 2000 and May 31, 2005, individual defendants breached their duty of loyalty by causing AIG to enter into contracts with Starr and SICO and breached their fiduciary duties by usurping AIG's corporate opportunity. Starr is charged with aiding and abetting breaches of fiduciary duty and unjust enrichment for its acceptance of the fees. SICO is no longer named as a defendant. On April 20, 2007, the individual defendants and Starr filed a motion seeking leave of the Court to assert a cross-claim against AIG and a third-party complaint against PwC and the directors previously dismissed from the action, as well as certain other AIG officers and employees. On June 13, 2007, the Court denied the individual defendants' motion to file a third-party complaint, but granted the proposed cross-claim against AIG. On June 27, 2007, Starr filed its cross-claim against AIG, alleging one count that includes contribution, unjust enrichment and setoff. AIG has filed an answer and moved to dismiss Starr's cross-claim to the extent it seeks affirmative relief, as opposed to a reduction in the judgment amount. On November 15, 2007, the court granted AIG's motion to dismiss the cross-claim by Starr to the extent that it sought affirmative relief from AIG. On November 21, 2007, shareholder plaintiffs submitted a motion for leave to file their Third Amended Complaint in order to add Thomas Tizzio as a defendant. On February 14, 2008, the court granted this motion and allowed Mr. Tizzio until April 2008 to take additional discovery. Document discovery and depositions are otherwise complete.

Policyholder Actions. After the NYAG filed its complaint against insurance broker Marsh, policyholders brought multiple federal antitrust and Racketeer Influenced and Corrupt Organizations Act (RICO) class actions in jurisdictions across the nation against insurers and brokers, including AIG and a number of its subsidiaries, alleging that the insurers and brokers engaged in a broad conspiracy to allocate customers, steer business, and rig bids. These actions, including 24 complaints filed in different federal courts naming AIG or an AIG subsidiary as a defendant, were consolidated by the judicial panel on multi-district litigation and transferred to the United States District Court for the District of New Jersey for coordinated pretrial proceedings. The consolidated actions have proceeded in that court in two parallel actions, *In re Insurance Brokerage Antitrust Litigation* (the *First Commercial Complaint*) and *In re Employee Benefit Insurance Brokerage Antitrust Litigation* (the *First Employee Benefits Complaint,* and, together with the *First Commercial Complaint,* the multi-district litigation).

The plaintiffs in the *First Commercial Complaint* are nineteen corporations, individuals and public entities that contracted with the broker defendants for the provision of insurance brokerage services for a variety of insurance needs. The broker defendants are alleged to have placed insurance coverage on the plaintiffs' behalf with a number of insurance companies named as defendants, including AIG subsidiaries. The *First Commercial Complaint* also named ten brokers and fourteen other insurers as defendants (two of which have since settled). The *First Commercial Complaint* alleges that defendants engaged in a widespread conspiracy to allocate customers through ''bid-rigging'' and ''steering'' practices. The *First Commercial Complaint* also alleges that the insurer defendants permitted brokers to place business with AIG subsidiaries through wholesale intermediaries affiliated with or owned by those same brokers rather than placing the business with AIG subsidiaries directly. Finally, the *First Commercial Complaint* alleges that the insurer defendants entered into agreements with broker defendants that tied insurance placements to reinsurance placements in order to provide additional

compensation to each broker. Plaintiffs assert that the defendants violated the Sherman Antitrust Act, RICO, the antitrust laws of 48 states and the District of Columbia, and are liable under common law breach of fiduciary duty and unjust enrichment theories. Plaintiffs seek treble damages plus interest and attorneys' fees as a result of the alleged RICO and Sherman Antitrust Act violations.

The plaintiffs in the *First Employee Benefits Complaint* are nine individual employees and corporate and municipal employers alleging claims on behalf of two separate nationwide purported classes: an employee class and an employer class that acquired insurance products from the defendants from August 26, 1994 to the date of any class certification. The *First Employee Benefits Complaint* names AIG, as well as eleven brokers and five other insurers, as defendants. The activities alleged in the *First Employee Benefits Complaint,* with certain exceptions, track the allegations of contingent commissions, bid-rigging and tying made in the *First Commercial Complaint.*

On October 3, 2006, Judge Hochberg of the District of New Jersey reserved in part and denied in part motions filed by the insurer defendants and broker defendants to dismiss the multi-district litigation. The Court also ordered the plaintiffs in both actions to file supplemental statements of particularity to elaborate on the allegations in their complaints. Plaintiffs filed their supplemental statements on October 25, 2006, and the AIG defendants, along with other insurer and broker defendants in the two consolidated actions, filed renewed motions to dismiss on November 30, 2006. On February 16, 2007, the case was transferred to Judge Garrett E. Brown, Chief Judge of the District of New Jersey. On April 5, 2007, Chief Judge Brown granted the defendants' renewed motions to dismiss the *First Commercial Complaint* and *First Employee Benefits Complaint* with respect to the antitrust and RICO claims. The claims were dismissed without prejudice and the plaintiffs were given 30 days, later extended to 45 days, to file amended complaints. On April 11, 2007, the Court stayed all proceedings, including all discovery, that are part of the multi-district litigation until any renewed motions to dismiss the amended complaints are resolved.

A number of complaints making allegations similar to those in the *First Commercial Complaint* have been filed against AIG and other defendants in state and federal courts around the country. The defendants have thus far been successful in having the federal actions transferred to the District of New Jersey and consolidated into the multi-district litigation. The AIG defendants have also sought to have state court actions making similar allegations stayed pending resolution of the multi-district litigation proceeding. In one state court action pending in Florida, the trial court recently decided not to grant an additional stay, but instead to allow the case to proceed. Defendants filed their motions to dismiss, and on September 24, 2007, the court denied the motions with respect to the state antitrust, RICO, and common law claims and granted the motions with respect to both the Florida insurance bad faith claim against AIG (with prejudice) and the punitive damages claim (without prejudice). Discovery in this action is ongoing.

Plaintiffs filed amended complaints in both *In re Insurance Brokerage Antitrust Litigation* (the *Second Commercial Complaint*) and *In re Employee Benefit Insurance Brokerage Antitrust Litigation* (the *Second Employee Benefits Complaint*) along with revised particularized statements in both actions on May 22, 2007. The allegations in the *Second Commercial Complaint* and the *Second Employee Benefits Complaint* are substantially similar to the allegations in the *First Commercial Complaint and First Employee Benefits Complaint,* respectively. The complaints also attempt to add several new parties and delete others; the *Second Commercial Complaint* adds two new plaintiffs and twenty seven new defendants (including three new AIG defendants), and the *Second Employee Benefits Complaint* adds eight new plaintiffs and nine new defendants (including two new AIG defendants). The defendants filed motions to dismiss the amended complaints and to strike the newly added parties. The Court granted (without leave to amend) defendants' motions to dismiss the federal antitrust and RICO claims on August 31, 2007 and September 28, 2007, respectively. The Court declined to exercise supplemental jurisdiction over the state law claims in the *Second Commercial Complaint* and therefore dismissed it in its entirety. On January 14, 2008, the court granted defendants' motion for summary judgment on the ERISA claims in the Second Employee Benefits Complaint and subsequently dismissed the remaining state law claims without prejudice, thereby dismissing the Second Employee Benefits Complaint in its entirety. On February 12, 2008, plaintiffs filed a notice of appeal to the United States Court of Appeals for the Third Circuit with respect to the dismissal of the Second Employee Benefits Complaint. Plaintiffs previously appealed the dismissal of the Second Commercial Complaint to the United States Court of Appeals for the Third Circuit on October 10, 2007. Several similar actions that were consolidated before Chief Judge Brown are still pending in the District Court. Those actions are currently stayed pending a decision by the court on whether they will proceed during the appeal of the dismissal of the Second Commercial Complaint and the Second Employee Benefits Complaint.

On August 24, 2007, the Ohio Attorney General filed a complaint in the Ohio Court of Common Pleas against AIG and a number of its subsidiaries, as well as several other broker and insurer defendants, asserting violation of Ohio's antitrust laws. The complaint, which is similar to the *Second Commercial Complaint,* alleges that AIG and the other broker and insurer defendants conspired to allocate customers, divide markets, and restrain competition in commercial lines of casualty insurance sold through the broker defendant. The complaint seeks treble damages on behalf of Ohio public purchasers of commercial casualty insurance, disgorgement on behalf of both public and private purchasers of commercial casualty insurance, as well as a $500 per day penalty for each day of conspiratorial conduct. AIG, along with other co-defendants, moved to dismiss the complaint on November 16, 2007. Discovery is stayed in the case pending a ruling on the motion to dismiss or until May 15, 2008, whichever occurs first.

SICO. In July, 2005, SICO filed a complaint against AIG in the Southern District of New York, claiming that AIG had refused to provide SICO access to certain artwork and asked the court to order AIG immediately to release the property to SICO. AIG filed

an answer denying SICO's allegations and setting forth defenses to SICO's claims. In addition, AIG filed counterclaims asserting breach of contract, unjust enrichment, conversion, breach of fiduciary duty, a constructive trust and declaratory judgment, relating to SICO's breach of its commitment to use its AIG shares only for the benefit of AIG and AIG employees. Fact and expert discovery has been concluded and SICO's motion for summary judgment is pending.

Regulatory Investigations. Regulators from several states have commenced investigations into insurance brokerage practices related to contingent commissions and other industry wide practices as well as other broker-related conduct, such as alleged bid-rigging. In addition, various federal, state and foreign regulatory and governmental agencies are reviewing certain transactions and practices of AIG and its subsidiaries in connection with industry wide and other inquiries. AIG has cooperated, and will continue to cooperate, in producing documents and other information in response to subpoenas and other requests. On January 29, 2008, AIG reached settlement agreements with nine states and the District of Columbia. The settlement agreements call for AIG to pay a total of $12.5 million to be allocated among the ten jurisdictions and also require AIG to continue to maintain certain producer compensation disclosure and ongoing compliance initiatives. AIG will also continue to cooperate with these states in their ongoing investigations. AIG has not admitted liability under the settlement agreements and continues to deny the allegations. Nevertheless, AIG agreed to settle in order to avoid the expense and uncertainty of protracted litigation. The settlement agreements, which remain subject to court approvals, were reached with the Attorneys General of the States of Florida, Hawaii, Maryland, Michigan, Oregon, Texas and West Virginia, the Commonwealths of Massachusetts and Pennsylvania, and the District of Columbia, the Florida Department of Financial Services, and the Florida Office of Insurance Regulation. The agreement with the Texas Attorney General also settles allegations of anticompetitive conduct relating to AIG's relationship with Allied World Assurance Company and includes an additional settlement payment of $500,000 related thereto.

Wells Notices. AIG understands that some of its employees have received Wells notices in connection with previously disclosed SEC investigations of certain of AIG's transactions or accounting practices. Under SEC procedures, a Wells notice is an indication that the SEC staff has made a preliminary decision to recommend enforcement action that provides recipients with an opportunity to respond to the SEC staff before a formal recommendation is finalized. It is possible that additional current and former employees could receive similar notices in the future as the regulatory investigations proceed.

Effect on AIG

In the opinion of AIG management, AIG's ultimate liability for the unresolved litigation and investigation matters referred to above is not likely to have a material adverse effect on AIG's consolidated financial condition, although it is possible that the effect would be material to AIG's consolidated results of operations for an individual reporting period.

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

There were no matters submitted to a vote of security holders during the fourth quarter of 2007.

Part II

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

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

The following table presents the high and low closing sales prices and the dividends paid per share of AIG's common stock on the New York Stock Exchange Composite Tape, for each quarter of 2007 and 2006:

	2007			2006		
	High	Low	Dividends Paid	High	Low	Dividends Paid
First quarter	**$72.15**	**$66.77**	**$0.165**	$70.83	$65.35	$0.150
Second quarter	**72.65**	**66.49**	**0.165**	66.54	58.67	0.150
Third quarter	**70.44**	**61.64**	**0.200**	66.48	57.76	0.165
Fourth quarter	**70.11**	**51.33**	**0.200**	72.81	66.30	0.165

The approximate number of holders of common stock as of January 31, 2008, based upon the number of record holders, was 56,500.

Subject to the dividend preference of any of AIG's serial preferred stock that may be outstanding, the holders of shares of common stock are entitled to receive such dividends as may be declared by AIG's Board of Directors from funds legally available therefor.

In February 2007, AIG's Board of Directors adopted a new dividend policy, which took effect with the dividend that was declared in the second quarter of 2007. Under ordinary circumstances, AIG's plan is to increase its common stock dividend by approximately 20 percent annually. The payment of any dividend, however, is at the discretion of AIG's Board of Directors, and the future payment of dividends will depend on various factors, including the performance of AIG's businesses, AIG's consolidated financial condition, results of operations and liquidity and the existence of investment opportunities.

For a discussion of certain restrictions on the payment of dividends to AIG by some of its insurance subsidiaries, see Note 14 to Consolidated Financial Statements.

The following table summarizes AIG's stock repurchases for the three-month period ended December 31, 2007:

Period	Total Number of Shares Purchased[(a)(b)]	Average Price Paid per Share	Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs	Maximum Number of Shares that May Yet Be Purchased Under the Plans or Programs at End of Month[(b)]
October 1 - 31, 2007	13,964,098	$66.12	13,964,098	
November 1 - 30, 2007	5,709,067	61.56	5,709,067	
December 1 - 31, 2007	1,584,199	55.58	1,584,199	
Total	21,257,364	$64.11	21,257,364	

(a) Reflects date of delivery. Does not include 49,583 shares delivered or attested to in satisfaction of the exercise price by holders of AIG employee stock options exercised during the three months ended December 31, 2007 or 23,300 shares purchased by ILFC to satisfy obligations under employee benefit plans.

(b) In February 2007, AIG's Board of Directors increased AIG's share repurchase program by authorizing the repurchase of shares with an aggregate purchase price of $8 billion. In November 2007, AIG's Board of Directors authorized the repurchase of an additional $8 billion in common stock. A balance of $10.9 billion remained for purchases under the program as of December 31, 2007, although $912 million of that amount has been advanced by AIG to purchase shares under the program and an additional $1 billion was required to be advanced in January 2008 to meet commitments that existed at December 31, 2007.

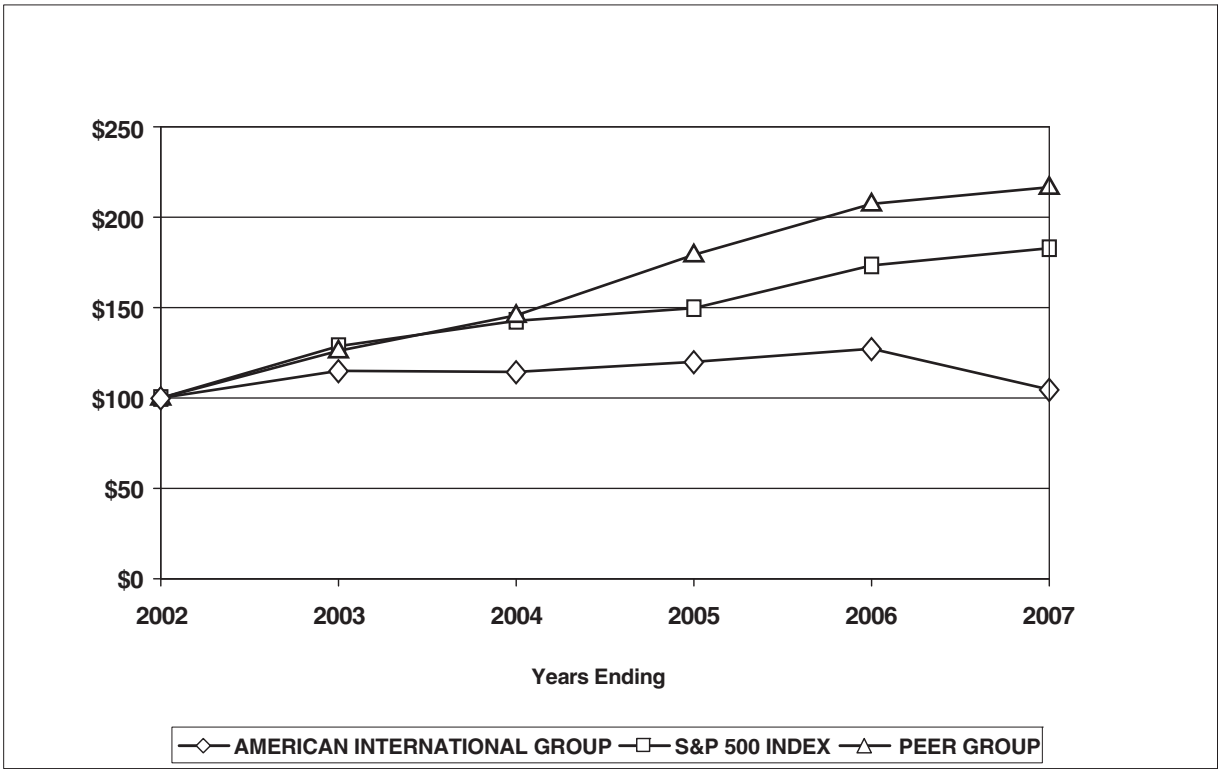
AIG does not expect to purchase additional shares under its share repurchase program for the foreseeable future, other than to meet commitments that existed at December 31, 2007.

AIG's table of equity compensation plans previously approved by security holders and equity compensation plans not previously approved by security holders will be included in AIG's Definitive Proxy Statement in connection with its 2008 Annual Meeting of Shareholders, which will be filed with the SEC within 120 days of AIG's fiscal year end.

Performance Graph

The following Performance Graph compares the cumulative total shareholder return on AIG common stock for a five-year period (December 31, 2002 to December 31, 2007) with the cumulative total return of the Standard & Poor's 500 stock index (which includes AIG) and a peer group of companies consisting of nine insurance companies to which AIG compares its business and operations: ACE Limited, Aflac Incorporated, The Chubb Corporation, The Hartford Financial Services Group, Inc., Lincoln National Corporation, MetLife, Inc., Prudential Financial, Inc., The Travelers Companies, Inc. (formerly The St. Paul Travelers Companies, Inc.) and XL Capital Ltd.

FIVE-YEAR CUMULATIVE TOTAL SHAREHOLDER RETURNS
Value of $100 Invested on December 31, 2002



	As of December 31,					
	2002	2003	2004	2005	2006	2007
AIG	$100.00	$115.02	$114.43	$119.98	$127.24	**$104.67**
S&P 500	100.00	128.68	142.69	149.70	173.34	**182.86**
Peer Group	100.00	126.10	145.73	179.22	207.37	**216.60**

Item 6.
Selected Financial Data

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

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

Years Ended December 31, *(in millions, except per share data)*	**2007**	2006[a]	2005[a]	2004[a]	2003[a]
Revenues[b][c][d]:					
Premiums and other considerations	**$ 79,302**	$ 74,213	$ 70,310	$ 66,704	$ 54,874
Net investment income	**28,619**	26,070	22,584	19,007	16,024
Net realized capital gains (losses)	**(3,592)**	106	341	44	(442)
Unrealized market valuation losses on AIGFP super senior credit default swap portfolio	**(11,472)**	—	—	—	—
Other income	**17,207**	12,998	15,546	12,068	9,145
Total revenues	**110,064**	113,387	108,781	97,823	79,601
Benefits and expenses:					
Incurred policy losses and benefits	**66,115**	60,287	64,100	58,600	46,362
Insurance acquisition and other operating expenses	**35,006**	31,413	29,468	24,378	21,332
Total benefits and expenses	**101,121**	91,700	93,568	82,978	67,694
Income before income taxes, minority interest and cumulative effect of accounting changes[b][c][d][e][f]	**8,943**	21,687	15,213	14,845	11,907
Income taxes	**1,455**	6,537	4,258	4,407	3,556
Income before minority interest and cumulative effect of accounting changes	**7,488**	15,150	10,955	10,438	8,351
Minority interest	**(1,288)**	(1,136)	(478)	(455)	(252)
Income before cumulative effect of accounting changes	**6,200**	14,014	10,477	9,983	8,099
Cumulative effect of accounting changes, net of tax	**—**	34	—	(144)	9
Net income	**6,200**	14,048	10,477	9,839	8,108
Earnings per common share:					
Basic					
Income before cumulative effect of accounting changes	**2.40**	5.38	4.03	3.83	3.10
Cumulative effect of accounting changes, net of tax	**—**	0.01	—	(0.06)	—
Net income	**2.40**	5.39	4.03	3.77	3.10
Diluted					
Income before cumulative effect of accounting changes	**2.39**	5.35	3.99	3.79	3.07
Cumulative effect of accounting changes, net of tax	**—**	0.01	—	(0.06)	—
Net income	**2.39**	5.36	3.99	3.73	3.07
Dividends declared per common share	**0.77**	0.65	0.63	0.29	0.24
Year-end balance sheet data:					
Total assets	**1,060,505**	979,410	853,048	801,007	675,602
Long-term borrowings[g]	**162,935**	135,316	100,314	86,653	73,881
Commercial paper and extendible commercial notes	**13,114**	13,363	9,535	10,246	6,468
Total liabilities	**964,604**	877,542	766,545	721,135	606,180
Shareholders' equity	**$ 95,801**	$101,677	$ 86,317	$ 79,673	$ 69,230

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

(b) In 2007, 2006, 2005, 2004 and 2003, includes other-than-temporary impairment charges of $4.7 billion, $944 million, $598 million, $684 million and $1.5 billion, respectively. Also includes gains (losses) from hedging activities that did not qualify for hedge accounting treatment under FAS 133, including the related foreign exchange gains and losses. In 2007, 2006, 2005, 2004 and 2003, respectively, the effect was $(1.44) billion, $(1.87) billion, $2.02 billion, $385 million and $(1.50) billion in revenues and $(1.44) billion, $(1.87) billion, $2.02 billion, $671 million and $(1.22) billion in operating income. These amounts result primarily from interest rate and foreign currency derivatives that are effective economic hedges of investments and borrowings. These gains (losses) in 2007 include a $380 million out of period charge to reverse net gains recognized on transfers of available for sale securities among legal entities consolidated within AIGFP. The gains (losses) in 2006 include an out of period charge of $223 million related to the remediation of the material weakness in internal control over the accounting for certain derivative transactions under FAS 133. In the first quarter of 2007, AIG began applying hedge accounting for certain transactions, primarily in its Capital Markets operations. In the second quarter of 2007, AGF and ILFC began applying hedge accounting to most of their derivatives hedging interest rate and foreign exchange risks associated with their floating rate and foreign currency denominated borrowings.

(c) In 2006, includes the effect of out of period adjustments related to the accounting for UCITS. The effect was an increase of $490 million in both revenues and operating income for General Insurance and an increase of $240 million and $169 million in revenues and operating income, respectively, for Life Insurance & Retirement Services.

(d) In 2007, includes an unrealized market valuation loss of $11.5 billion on AIGFP's super senior credit default swap portfolio and an other-than-temporary impairment charge of $643 million on AIGFP's available for sale investment securities reported in other income.

(e) Includes current year catastrophe-related losses of $276 million in 2007, $3.28 billion in 2005 and $1.16 billion in 2004. There were no significant catastrophe-related losses in 2006 and 2003.

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

(g) Includes that portion of long-term debt maturing in less than one year. See also Note 11 to Consolidated Financial Statements.

Management's Discussion and Analysis of Financial Condition and Results of Operations

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

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

Cautionary Statement Regarding Projections and Other Information About Future Events

This Annual Report on Form 10-K and other publicly available documents may include, and AIG's officers and representatives may from time to time make, projections concerning financial information and statements concerning future economic performance and events, plans and objectives relating to management, operations, products and services, and assumptions underlying these projections and statements. These projections and statements are not historical facts but instead represent only AIG's belief regarding future events, many of which, by their nature, are inherently uncertain and outside AIG's control. These projections and statements may address, among other things, the status and potential future outcome of the current regulatory and civil proceedings against AIG and their potential effect on AIG's businesses, financial condition, results of operations, cash flows and liquidity, AIG's exposures to subprime mortgages, monoline insurers and the residential real estate market and AIG's strategy for growth, product development, market position, financial results and reserves. It is possible that AIG's actual results and financial condition may differ, possibly materially, from the anticipated results and financial condition indicated in these projections and statements. Factors that could cause AIG's actual results to differ, possibly materially, from those in the specific projections and statements are discussed throughout this Management's Discussion and Analysis of Financial Condition and Results of Operations and in Item 1A. Risk Factors of this Annual Report on Form 10-K. AIG is not under any obligation (and expressly disclaims any such obligations) to update or alter any projection or other statement, whether written or oral, that may be made from time to time, whether as a result of new information, future events or otherwise.

Overview of Operations and Business Results

AIG identifies its reportable segments by product or service line, consistent with its management structure. AIG's major product and service groupings are General Insurance, Life Insurance & Retirement Services, Financial Services and Asset Management. Through these operating segments, AIG provides insurance, financial and investment products and services to both businesses and individuals in more than 130 countries and jurisdictions. This geographic, product and service diversification is one of AIG's major strengths and sets it apart from its competitors. AIG's Other category consists of items not allocated to AIG's operating segments.

AIG's subsidiaries serve commercial, institutional and individual customers through an extensive property-casualty and life insurance and retirement services network. In the United States, AIG companies are the largest underwriters of commercial and industrial insurance and are among the largest life insurance and retirement services operations as well. AIG's Financial Services businesses include commercial aircraft and equipment leasing, capital markets operations and consumer finance, both in the United States and abroad. AIG also provides asset management services to institutions and individuals. As part of its Spread-Based Investment activities, and to finance its operations, AIG issues various debt instruments in the public and private markets.

AIG's operating performance reflects implementation of various long-term strategies and defined goals in its various operating segments. A primary goal of AIG in managing its General Insurance operations is to achieve an underwriting profit. To achieve this goal, AIG must be disciplined in its risk selection, and premiums must be adequate and terms and conditions appropriate to cover the risks accepted and expenses incurred.

AIG has commenced a realignment to simplify its Foreign General Insurance operations, many of which were historically conducted through branches of U.S. companies. On October 8, 2007, AIU Insurance Company announced the conversion of its existing China branches into AIG General Insurance Company China Limited, the first non-Chinese owned general insurance company established in China. This subsidiary assumed the existing business portfolio, assets and liabilities of the China branches. On October 15, 2007, AIG General Insurance (Taiwan) Co., Ltd. (AIGGI Taiwan) announced the completion of its merger with AIU Insurance Company Taiwan Branch. On December 1, 2007, Landmark Insurance Company Limited, a U.K. subsidiary, assumed all of the insurance liabilities of the U.K. branch of New Hampshire Insurance Company and changed its name to AIG U.K. Ltd. On January 1, 2008, AIU Insurance Company ceased participating in the Domestic General Insurance pooling arrangement. These ongoing simplification efforts are expected to result in better utilization of capital and a lower effective tax rate.

A central focus of AIG operations in recent years has been the development and expansion of distribution channels. In 2007, AIG continued to expand its distribution channels, which now include banks, credit card companies, television-media home shopping, affinity groups, direct response, worksite marketing and e-commerce.

AIG patiently builds relationships in markets around the world where it sees long-term growth opportunities. For example, the fact that AIG has the only wholly owned foreign life insurance operations in China, operating in 19 cities, is the result of relationships developed over nearly 30 years. AIG's more recent extensions of operations into India, Vietnam, Russia and other emerging markets reflect the same growth strategy. Moreover, AIG believes in investing in the economies and infrastructures of these countries and growing with them. When AIG companies enter a new jurisdiction, they typically offer basic protection and savings products. As the economies evolve, AIG's products evolve with them, to more sophisticated and investment-oriented models.

Growth for AIG may be generated internally as well as through acquisitions which both fulfill strategic goals and offer adequate return on capital. In October 2007, AIG expanded its Foreign General Insurance operations in Germany through the acquisition of Württembergische und Badische Versicherungs-AG (WüBA). In January 2007, American General Finance, Inc. (AGF) expanded its operations into the U.K. through the acquisition of Ocean Finance and Mortgages Limited, a finance broker for home owner loans in the U.K.

Outlook

General Trends

In mid-2007, the U.S. residential mortgage market began to experience serious disruption due to credit quality deterioration in a significant portion of loans originated, particularly to non-prime and subprime borrowers; evolving changes in the regulatory environment; a slower residential housing market; increased cost of borrowings for mortgage participants; and illiquid credit markets.

AIG participates in the U.S. residential mortgage market in several ways: AGF originates principally first-lien mortgage loans and to a lesser extent second-lien mortgage loans to buyers and owners of residential housing; United Guaranty Corporation (UGC) provides first loss mortgage guaranty insurance for high loan-to-value first- and second-lien residential mortgages; AIG insurance and financial services subsidiaries invest in mortgage-backed securities and CDOs, in which the underlying collateral is composed in whole or in part of residential mortgage loans; and AIGFP provides credit protection through credit default swaps on certain super senior tranches of collateralized debt obligations (CDOs), a significant majority of which have AAA underlying or subordinate layers.

Disruption in the U.S. residential mortgage market may also increase claim activity in the financial institution segment of AIG's D&O and professional liability classes of business. However, based on its review of information currently available, AIG believes overall loss activity for the broader D&O and professional liability classes is likely to remain within or near the levels observed during the last several years, which include losses related to stock options backdating as well as to the U.S. residential mortgage market.

The operating results of AIG's consumer finance and mortgage guaranty operations in the United States have been and are likely

to continue to be adversely affected by the factors referred to above. The downward cycle in the U.S. housing market is not expected to improve until residential inventories return to a more normal level and the mortgage credit market stabilizes. AIG expects that this downward cycle will continue to adversely affect UGC's operating results for the foreseeable future and will result in a significant operating loss for UGC in 2008. AIG also incurred substantial unrealized market valuation losses in 2007, particularly in the fourth quarter, on AIGFP's super senior credit default swap portfolio and substantial other-than-temporary impairment charges on AIG's Insurance and Financial Services available for sale securities. The results from AIG's operations with exposure to the U.S. residential mortgage market will be highly dependent on future market conditions. Continuing market deterioration will cause AIG to report additional unrealized market valuation losses and impairment charges.

The ongoing effect of the downward cycle in the U.S. housing market on AIG's other operations, investment portfolio and overall consolidated financial condition could be material if the market disruption continues and expands beyond the residential mortgage markets, although AIG seeks to mitigate the risks to its business by disciplined underwriting and active risk management.

Globally, heightened regulatory scrutiny of financial services companies in many jurisdictions has the potential to affect future financial results through higher compliance costs. This is particularly true in the United States, where Federal and state authorities have commenced various investigations of the financial services industry, and in Japan and Southeast Asia, where financial institutions have received remediation orders affecting consumer and policyholder rights.

In certain quarters, AIG's returns from partnerships and other alternative investments were particularly strong, driven by favorable equity market performance and credit conditions. These returns may vary from period to period and AIG believes that the particularly strong performance in certain prior periods is not indicative of the returns to be expected from this asset class in future periods.

AIG has recorded out of period adjustments in the last two years due to the remediation of control deficiencies. As AIG continues its remediation activities, AIG expects to continue to incur expenses related to these activities and to record additional out of period adjustments, although all known errors have been corrected.

General Insurance

The commercial property and casualty insurance industry has historically experienced cycles of price erosion followed by rate strengthening as a result of catastrophes or other significant losses that affect the overall capacity of the industry to provide coverage. As premium rates decline, AIG will generally experience higher current accident year loss ratios, as the written premiums are earned. Despite industry price erosion in commercial lines, AIG expects to continue to identify profitable opportunities and build attractive new general insurance businesses as a result of AIG's broad product line and extensive distribution networks in the United States and abroad.

Workers compensation remains under considerable pricing pressure, as statutory rates continue to decline. Rates for aviation, excess casualty, D&O and certain other lines of insurance also continue to decline due to competitive pressures. Rates for commercial property lines are also declining following another year of relatively low catastrophe losses. Further price erosion is expected in 2008 for the commercial lines; AIG seeks to mitigate the decline by constantly seeking out profitable opportunities across its diverse product lines and distribution networks while maintaining a commitment to underwriting discipline. There can be no assurance that price erosion will not become more widespread or that AIG's profitability will not deteriorate from current levels in major commercial lines.

In Foreign General Insurance, opportunities for growth exist in the consumer lines due to increased demand in emerging markets and the trend toward privatization of health insurance. In commercial lines, the late 2007 acquisition of WüBa enhances AIG's insurance offerings to small and medium sized companies in Europe.

Through operations in Bahrain designed to comply with Islamic law, AIG is tapping into a growing market. Islamic insurance, called Takaful, is an alternative to conventional insurance based on the concept of mutual assistance through pooling of resources.

The Personal Lines automobile marketplace remains challenging with rates declining steadily, increased spending on commissions and advertising and favorable liability frequency trends slowing, while severity in both liability and physical damage are expected to increase. In addition to the deteriorating underwriting cycle, a generally weakening economy leads to slower growth in automobile insurance exposure units and values. The Personal Lines business is focused on consolidation and improving operational efficiencies to reduce costs, as well as enhancing rating algorithms and creating a new aigdirect.com brand, as a result of the 2007 combination of AIG Direct and 21st Century Insurance Group (21st Century) operations, to support growth. The high net worth market continues to provide opportunities for growth as a result of AIG's innovative products and services specifically designed for that market.

Losses caused by catastrophes can fluctuate widely from year to year, making comparisons of results more difficult. With respect to catastrophe losses, AIG believes that it has taken appropriate steps, such as careful exposure selection and adequate reinsurance coverage, to reduce the effect of possible future losses. The occurrence of one or more catastrophic events of higher than anticipated frequency or severity, such as a terrorist attack, earthquake or hurricane, that causes insured losses, however, could have a material adverse effect on AIG's results of operations, liquidity or financial condition.

Life Insurance & Retirement Services

Disruption in the U.S. residential mortgage and credit markets had a significant adverse effect on Life Insurance & Retirement Services operating results in 2007 and will continue to be a key factor in 2008 and beyond, especially in the U.S.-based operations. The volatility in operating results will be further magnified by the continuing market shift to variable products with living benefits

and the adoption of FAS No. 157, ''Fair Value Measurements'' (FAS 157). Life Insurance & Retirement Services elected the fair value option under FAS No. 159, ''The Fair Value Option for Financial Assets and Financial Liabilities'' (FAS 159), for two products beginning January 1, 2008 - a closed block of single premium variable life business in Japan and an investment-linked life insurance product sold principally in Asia. After adoption on January 1, 2008, subsequent changes in fair value for these products will be reported in operating income. The adoption of FAS 159 for these products is expected to result in a decrease to opening 2008 retained earnings of approximately $600 million. For a description of these accounting standards, see Note 1 to Consolidated Financial Statements.

Life Insurance & Retirement Services uses various derivative instruments to hedge cash flows related to certain foreign currencies and fixed income related instruments. Although these derivatives are purchased to mitigate the economic effect of movements in foreign exchange rates and interest rates, reported earnings may be volatile due to certain hedges not qualifying for hedge accounting under FAS 133. The change in fair value of derivative instruments is reported in net realized capital gains (losses). Life Insurance & Retirement Services engages in hedging programs that use derivatives and other instruments to hedge the guaranteed living benefits associated with variable products. Nevertheless, short-term market movements will vary from long-term expectations underlying the product pricing assumptions and may cause volatility in reported earnings. The inclusion of risk margins in the valuation of embedded derivatives under FAS 157 will increase earnings volatility as differences emerge between the change in fair value of embedded derivatives and the change in fair value of hedging instruments. As variable products with guaranteed living benefits continue to grow, the reported earnings volatility associated with these programs will likely increase.

Life Insurance & Retirement Services may continue to experience volatility in net realized capital gains (losses) due to other-than-temporary impairment writedowns of the fair value of investments, primarily related to the significant disruption in the residential mortgage and credit markets and foreign currency related losses.

In Japan, given AIG's multi-channel, multi-product strategy, AIG expects its Life Insurance & Retirement Services operations to exceed industry growth in the long term, although downward pressure on earnings growth rates is anticipated due to the difficult market conditions. Market conditions remain challenging as a result of increased competition due to new market entrants, the increasing financial strength of the domestic companies as the economy has recovered, the effect of additional regulatory oversight, changes to the tax deductibility of insurance premiums and the regulatory claims review which has negatively affected consumer perceptions of the industry. While the market shift to variable products with living benefits will constrain fixed annuity sales, AIG is positioned to grow annuity sales overall with its annuity products designed to meet the needs of consumers in a range of market conditions. In addition, AIG expects that the planned integration of AIG Star Life and AIG Edison Life, which is anticipated to be completed in 2009, will provide enhanced distribution opportunities and operational efficiencies pending regulatory approval.

Full deregulation of banks in Japan with respect to insurance product sales became effective in December 2007, and AIG expects that it will be able to leverage its existing bank relationships and innovative product expertise to expand sales of both life and accident and health products in 2008. Deregulation of Japan Post is also expected to provide additional growth opportunities during 2008 and beyond.

Although the Japanese Yen strengthened in the fourth quarter of 2007, historical volatility of Japanese Yen-dollar exchange rates has resulted in higher than normal surrenders, and if that trend returns, an acceleration of the amortization of deferred policy acquisition costs could occur.

Outside of Japan, ALICO continues to execute its strategy of diversifying distribution channels and developing new products. In particular, ALICO's Central and Eastern European operations performed well and demographic and economic conditions in these countries provide excellent opportunities for continued growth.

AIG's operations in China continue to expand, but AIG expects competition in China to remain strong. AIG's success in China will depend on its ability to execute its growth strategy. Key growth strategies in 2008 include expansion of sales and service centers, increased bank distribution and entering into strategic alliances with key partners. In Southeast Asia, AIG's operations are focused on growing market share and profits in Singapore, Malaysia, Thailand and Hong Kong with products focused on the life savings-oriented consumer along with high net worth consumers through the newly formed Wealth Management Group.

Domestically, AIG plans to continue expansion of its Life Insurance & Retirement Services businesses through direct marketing and independent agent distribution channels. The aging population in the United States provides a growth opportunity for a variety of products, including longevity, guaranteed income and supplemental accident and health products. Certain other demographic groups that have traditionally been underserved provide additional growth opportunities. The Domestic Life Insurance operations showed positive momentum in the second half of 2007 resulting from new products and expanded distribution. Domestic group life/health operations continue to face competitors with greater scale in group benefits.

The fixed annuities business experienced a difficult year as surrenders increased in 2007 due to both an increasing number of policies coming out of their surrender charge period and increased competition from bank deposit products. While surrenders are expected to continue to be higher than normal, the current interest rate environment should provide opportunities for improvements in net flows during 2008. AIG believes that improvement in net flows in the individual variable annuity market will be driven by variable annuity products with living benefits while the group retirement products will continue to experience a shift from group annuities to lower margin mutual fund products.

Since the beginning of 2000, the yield available on Taiwanese 10-year government bonds dropped from approximately 6 percent to less than 3 percent at December 31, 2007. Yields on most

other invested assets have correspondingly dropped over the same period. New regulatory capital requirements being developed in Taiwan, combined with growth opportunities in bancassurance and variable annuities with living benefits, may potentially create a need for capital contributions in 2008 and beyond to support local solvency requirements.

Financial Services

Within Financial Services, demand for International Lease Finance Corporation (ILFC's) modern, fuel efficient aircraft remains strong, and ILFC plans to increase its fleet by purchasing 73 aircraft in 2008. However, ILFC's margins may be adversely affected by increases in interest rates. AIG Financial Products Corp. and AIG Trading Group Inc. and their respective subsidiaries (collectively, AIGFP) expect opportunities for growth across their product segments, but AIGFP is a transaction-oriented business, and its operating results will depend to a significant extent on actual transaction flow, which is affected by market conditions and other variables outside its control. AIG continues to explore opportunities to expand its Consumer Finance operations into new domestic and foreign markets.

The ongoing disruption in the U.S. residential mortgage and credit markets and the recent downgrades of residential mortgage-backed securities and CDO securities by rating agencies continue to adversely affect the fair value of the super senior credit default swap portfolio written by AIGFP. AIG expects that continuing limitations on the availability of market observable data will affect AIG's determinations of the fair value of these derivatives, including by preventing AIG, for the foreseeable future, from recognizing the beneficial effect of the differential between credit spreads used to price a credit default swap and spreads implied from prices of the CDO bonds referenced by such swap. The fair value of these derivatives is expected to continue to fluctuate, perhaps materially, in response to changing market conditions, and AIG's estimates of the value of AIGFP's super senior credit derivative portfolio at future dates could therefore be materially different from current estimates. AIG continues to believe that the unrealized market valuation losses recorded on the AIGFP super senior credit default swap portfolio are not indicative of the losses AIGFP may realize over time. Under the terms of most of these credit derivatives, losses to AIG would generally result from the credit impairment of the referenced CDO bonds that AIG would acquire in satisfying its swap obligations. Based upon its most current analyses, AIG believes that any credit impairment losses realized over time by AIGFP will not be material to AIG's consolidated financial condition, although it is possible that such realized losses could be material to AIG's consolidated results of operations for an individual reporting period. Except to the extent of any such credit impairment losses, AIG expects the unrealized market valuation losses to reverse over the remaining life of the super senior credit default swap portfolio.

Approximately $379 billion of the $527 billion in notional exposure on AIGFP's super senior credit default swap portfolio as of December 31, 2007 were written to facilitate regulatory capital relief for financial institutions primarily in Europe. AIG expects that the majority of these transactions will be terminated within the next 12 to 18 months by AIGFP's counterparties as they implement models compliant with the new Basel II Accord. As of February 26, 2008, $54 billion in notional exposures have either been terminated or are in the process of being terminated. AIGFP was not required to make any payments as part of these terminations and in certain cases was paid a fee upon termination. In light of this experience to date and after other comprehensive analyses, AIG did not recognize an unrealized market valuation adjustment for this regulatory capital relief portfolio for the year ended December 31, 2007. AIG will continue to assess the valuation of this portfolio and monitor developments in the marketplace. There can be no assurance that AIG will not recognize unrealized market valuation losses from this portfolio in future periods. These transactions contributed approximately $210 million to AIGFP's revenues in 2007. If AIGFP is not successful in replacing the revenues generated by these transactions, AIGFP's operating results could be materially adversely affected. For additional information on the AIGFP super senior credit default swap portfolio, see Risk Management — Segment Risk Management — Financial Services — Capital Markets Derivative Transactions and Note 8 to Consolidated Financial Statements.

In March 2007, the U.S. Treasury Department published proposed regulations that, had they been adopted in 2007, would have had the effect of limiting the ability of AIG to claim foreign tax credits with respect to certain transactions entered into by AIGFP. AIGFP is no longer a participant in those transactions and therefore, the proposed regulations, if adopted in their current form in 2008 or subsequent years, would not be expected to have any material effect on AIG's ability to claim foreign tax credits.

Effective January 1, 2008, AIGFP elected to apply the fair value option to all eligible assets and liabilities, other than equity method investments. The adoption of FAS 159 with respect to elections made by AIGFP is currently being evaluated for the effect of recently issued draft guidance by the FASB, anticipated to be issued in final form in early 2008, and its potential effect on AIG's consolidated financial statements.

Asset Management

In the Spread-Based Investment business, the Guaranteed Investment Contract (GIC) portfolio continues to run off and was replaced by the Matched Investment Program (MIP). The results from domestic GICs and the MIP have been adversely affected by the ongoing disruption in the credit markets, the weakening U.S. dollar and declining interest rates. The MIP is exposed to credit and market risk in the form of investments in, among other asset classes, U.S. residential mortgage-backed securities, asset-backed securities, commercial mortgage-backed securities and single name corporate credit default swaps entered into by the MIP. In addition, earnings volatility for the MIP may arise from investments in bank loans that are held for future collateralized loan obligations to be managed by AIG Investments. The value of the investments may fluctuate materially from period to period due to market movements, which may result in realized and unrealized net losses. Although it is difficult to estimate future movements in these markets, effective hedges exist to mitigate the effect of

interest rate and foreign currency exchange rate disruptions. Reported results may be volatile due to certain hedges not qualifying for hedge accounting treatment.

In the Institutional Asset Management business, carried interest, computed in accordance with each fund's governing agreement, is based on the investment's performance over the life of each fund. Unrealized carried interest is recognized based on each fund's performance as of the balance sheet date. Future fund performance may negatively affect previously recognized carried interest.

For a description of important factors that may affect the operations and initiatives described above, see Item 1A. Risk Factors.

Consolidated Results

The following table summarizes AIG's consolidated revenues, income before income taxes, minority interest and cumulative effect of accounting changes and net income for the years ended December 31, 2007, 2006 and 2005:

Years Ended December 31, *(in millions)*	2007	2006	2005	Percentage Increase/(Decrease) 2007 vs. 2006	2006 vs. 2005
Total revenues	**$110,064**	$113,387	$108,781	(3)%	4%
Income before income taxes, minority interest and cumulative effect of accounting changes	**8,943**	21,687	15,213	(59)	43
Net income	**$ 6,200**	$ 14,048	$ 10,477	(56)%	34%

Effect of Credit Market Events in the Fourth Quarter of 2007

AIG reported a net loss of $8.4 billion before tax ($5.2 billion after tax) in the fourth quarter of 2007 as a result of severe credit market disruption. Contributing to this loss was an $11.5 billion pre-tax charge for the unrealized market valuation loss on AIGFP's super senior credit default swap portfolio. Net realized capital losses totaled $2.6 billion before tax in the fourth quarter of 2007, arising primarily from other-than-temporary impairment charges in AIG's investment portfolio, with an additional $643 million impairment charge related to Financial Services securities available for sale reported in other income. Also contributing to the operating loss for the fourth quarter was an operating loss of $348 million before tax from Mortgage Guaranty from continued deterioration in the U.S. residential housing market.

2007 and 2006 Comparison

AIG's consolidated revenues decreased in 2007 compared to 2006 as growth in Premiums and other considerations and Net investment income in the General Insurance and Life Insurance & Retirement Services segments were more than offset by higher Net realized capital losses compared to 2006 and an unrealized market valuation loss of $11.5 billion on AIGFP's super senior credit default swap portfolio recorded in other income. Net realized capital losses of $3.6 billion in 2007 included other-than-temporary impairment charges of the fair value of investments of $4.1 billion, primarily related to the significant disruption in the residential mortgage and credit markets, and foreign currency related losses of $500 million. Similarly, AIG recorded in other income, other-than-temporary impairment charges of $643 million related to its Financial Services securities available for sale reported in other income. Total other-than-temporary impairment charges in 2006 were $944 million. See Invested Assets — Other-than-temporary impairments herein.

Income before income taxes, minority interest and cumulative effect of accounting changes declined in 2007 due to the losses described above, partially offset by the favorable effects in 2007 of the application of hedge accounting under Statement of Financial Accounting Standards No. 133, ''Accounting for Derivative Instruments and Hedging Activities'' (FAS 133). In 2007, AIGFP applied hedge accounting to certain of its interest rate swaps and foreign currency forward contracts hedging its investments and borrowings. As a result, AIGFP recognized in earnings the change in the fair value of the hedged items attributable to the hedged risks, substantially offsetting the gains and losses on the derivatives designated as hedges. In 2006, AIGFP did not apply hedge accounting to any of its assets and liabilities.

2006 and 2005 Comparison

The increase in revenues in 2006 compared to 2005 was primarily attributable to the growth in Premiums and other considerations and Net investment income in the General Insurance and Life Insurance & Retirement Services segments. Revenues in the Financial Services segment declined as a result of the effect of hedging activities for AIGFP that did not qualify for hedge accounting treatment under FAS 133, decreasing revenues by $1.8 billion in 2006 and increasing revenues by $2.0 billion in 2005.

Income before income taxes, minority interest and cumulative effect of accounting changes increased in 2006 compared to 2005, reflecting higher General Insurance and Life Insurance & Retirement Services operating income. These increases were partially offset by lower Financial Services operating income reflecting the effects of hedging activities that did not qualify for hedge accounting treatment under FAS 133. Results in 2005 reflected the negative effect of $3.3 billion (pre-tax) in catastrophe-related losses incurred that year. Net income in 2005 also reflected the charges related to regulatory settlements, as described in Item 3. Legal Proceedings, and the fourth quarter

charge resulting from the annual review of General Insurance loss and loss adjustment reserves.

Remediation

Throughout 2007 and 2006, as part of its continuing remediation efforts, AIG recorded out of period adjustments which are detailed below. In addition, certain revisions were made to the Consolidated Statement of Cash Flows.

2007 Adjustments

During 2007, out of period adjustments collectively decreased pre-tax operating income by $372 million ($399 million after tax). The adjustments were comprised of a charge of $380 million ($247 million after tax) to reverse net gains on transfers of investment securities among legal entities consolidated within AIGFP and a corresponding increase to accumulated other comprehensive income (loss); $156 million of additional income tax expense related to the successful remediation of the material weakness in internal control over income tax accounting; $142 million ($92 million after tax) of additional expense related to insurance reserves and DAC in connection with improvements in internal control over financial reporting and consolidation processes; $42 million ($29 million after tax) of additional expense, primarily related to other remediation activities; and $192 million ($125 million after tax) of net realized capital gains related to foreign exchange.

2006 Adjustments

During 2006, out of period adjustments collectively increased pre-tax operating income by $313 million ($65 million after tax). The adjustments were comprised of $773 million ($428 million after tax) of additional investment income related to the accounting for certain interests in unit investment trusts (UCITS); $300 million ($145 million after tax) of charges primarily related to the remediation of the material weakness in internal control over the accounting for certain derivative transactions under FAS 133; $58 million of additional income tax expense related to the remediation of the material weakness in internal control over income tax accounting; $85 million ($55 million after tax) of interest income related to interest earned on deposit contracts; $61 million (before and after tax) of expenses related to the Starr International Company, Inc. (SICO) Deferred Compensation Profit Participation Plans (SICO Plans); $59 million ($38 million after tax) of expenses related to deferred advertising costs; and $125 million ($116 million after tax) of additional expense, primarily related to other remediation activities.

Results in 2006 were also negatively affected by a one-time charge relating to the C.V. Starr & Co., Inc. (Starr) tender offer ($54 million before and after tax) and an additional allowance for losses in AIG Credit Card Company (Taiwan) ($88 million before and after tax), both of which were recorded in first quarter of 2006.

Cash Flows

As part of its ongoing remediation activities, AIG has made certain revisions to the Consolidated Statement of Cash Flows, primarily relating to the effect of reclassifying certain policyholders' account balances, the elimination of certain intercompany balances and revisions related to separate account assets. Accordingly, AIG revised the previous periods presented to conform to the revised presentation. See Note 24 to Consolidated Financial Statements for further information.

Income Taxes

The effective tax rate declined from 30.1 percent in 2006 to 16.3 percent in 2007, primarily due to the unrealized market valuation losses on AIGFP's super senior credit default swap portfolio and other-than-temporary impairment charges. These losses, which are taxed at a U.S. tax rate of 35 percent and are included in the calculation of income tax expense, reduced AIG's overall effective tax rate. In addition, other tax benefits, including tax exempt interest and effects of foreign operations are proportionately larger in 2007 than in 2006 due to the decline in pre-tax income in 2007. Furthermore, tax deductions taken in 2007 for SICO compensation plans for which the expense had been recognized in prior years also reduced the effective tax rate in 2007. AIG has now completed its claims for tax refunds attributable to adjustments made for 2004 and prior financial statements. Refund claims for tax years 1991-1996 were filed with the Internal Revenue Service in June 2007. Claims for tax years 1997-2004 will be filed before September 2008.

AIG expects to receive cash tax benefits in 2008 as a result of the unrealized market valuation losses on AIGFP's super senior credit default swap portfolio, whether AIG is in a regular or alternative minimum tax position.

Management's Discussion and Analysis of Financial Condition and Results of Operations *Continued*

The following table summarizes the net effect of catastrophe-related losses for the years ended December 31, 2007 and 2005. There were no significant catastrophe-related losses for the year ended December 31, 2006.

(in millions)	**2007**	2005
Pretax	**$276**	$3,280*
Net of tax and minority interest	**$177**	2,109

** Includes $312 million in catastrophe-related losses from partially owned companies.*

Segment Results

The following table summarizes AIG's operations by reporting segment for the years ended December 31, 2007, 2006 and 2005. See also Note 2 to Consolidated Financial Statements.

				Percentage Increase/(Decrease)	
(in millions)	**2007**	2006[a]	2005[a]	2007 vs. 2006	2006 vs. 2005
Revenues[b]:					
General Insurance[c]	**$ 51,708**	$ 49,206	$ 45,174	5%	9%
Life Insurance & Retirement Services[c][d]	**53,570**	50,878	48,020	5	6
Financial Services[e][f]	**(1,309)**	7,777	10,677	—	(27)
Asset Management	**5,625**	4,543	4,582	24	(1)
Other	**457**	483	344	(5)	40
Consolidation and eliminations	**13**	500	(16)	(97)	—
Total	**$110,064**	$113,387	$108,781	(3)%	4%
Operating Income (loss)[b][g]:					
General Insurance[c]	**$ 10,526**	$ 10,412	$ 2,315	1%	350%
Life Insurance & Retirement Services[c][d]	**8,186**	10,121	8,965	(19)	13
Financial Services[e][f]	**(9,515)**	383	4,424	—	(91)
Asset Management	**1,164**	1,538	1,963	(24)	(22)
Other[h]	**(2,140)**	(1,435)	(2,765)	—	—
Consolidation and eliminations	**722**	668	311	8	115
Total	**$ 8,943**	$ 21,687	$ 15,213	(59)%	43%

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

(b) In 2007, 2006 and 2005, includes other-than-temporary impairment charges of $4.7 billion, $944 million and $598 million, respectively. Also includes gains (losses) from hedging activities that did not qualify for hedge accounting treatment under FAS 133, including the related foreign exchange gains and losses. In 2007, 2006, and 2005, respectively, the effect was $(1.44) billion, $(1.87) billion and $2.02 billion in both revenues and operating income. These amounts result primarily from interest rate and foreign currency derivatives that are effective economic hedges of investments and borrowings. These gains (losses) in 2007 include a $380 million out of period charge to reverse net gains recognized on transfers of available for sale securities among legal entities consolidated within AIGFP. The gains (losses) in 2006 include an out of period charge of $223 million related to the remediation of the material weakness in internal control over the accounting for certain derivative transactions under FAS 133.

(c) In 2006, includes the effect of out of period adjustments related to the accounting for UCITS. In 2006, the effect was an increase of $490 million in both revenues and operating income for General Insurance and an increase of $240 million and $169 million in revenues and operating income, respectively, for Life Insurance & Retirement Services.

(d) In 2007, 2006 and 2005, includes other-than-temporary impairment charges of $2.8 billion, $641 million and $425 million, respectively, for Life Insurance & Retirement Services.

(e) Includes gains (losses) from hedging activities that did not qualify for hedge accounting treatment under FAS 133, including the related foreign exchange gains and losses. In 2007, 2006 and 2005, respectively, the effect was $104 million, $(1.97) billion, and $2.19 billion in both revenues and operating income. These amounts result primarily from interest rate and foreign currency derivatives that are effective economic hedges of investments and borrowings. The years ended December 31, 2007 and 2006 include out of period charges of $380 million and $223 million, respectively, as discussed in footnote (b). In the first quarter of 2007, AIG began applying hedge accounting for certain transactions, primarily in its Capital Markets operations. In the second quarter of 2007, AGF and ILFC began applying hedge accounting to most of their derivatives hedging interest rate and foreign exchange risks associated with their floating rate and foreign currency denominated borrowings.

(f) In 2007, both revenues and operating income (loss) include an unrealized market valuation loss of $11.5 billion on AIGFP's super senior credit default swap portfolio and an other-than-temporary impairment charge of $643 million on AIGFP's available for sale investment securities recorded in other income.

(g) Includes current year catastrophe-related losses of $276 million in 2007 and $3.28 billion in 2005. There were no significant catastrophe-related losses in 2006.

(h) In 2005, includes current year catastrophe-related losses from unconsolidated entities of $312 million.

General Insurance

AIG's General Insurance operations provide property and casualty products and services throughout the world. Revenues in the General Insurance segment represent net premiums earned, net investment income and net realized capital gains (losses). The increase in General Insurance operating income in 2007 compared to 2006 was driven by strength in the Domestic Brokerage Group (DBG), partially offset by operating losses from the Mortgage Guaranty business and a decrease in Personal Lines operating income.

Life Insurance & Retirement Services

AIG's Life Insurance & Retirement Services operations provide insurance, financial and investment-oriented products throughout the world. Revenues in the Life Insurance & Retirement Services operations represent premiums and other considerations, net investment income and net realized capital gains (losses). Foreign operations contributed approximately 76 percent, 68 percent and 59 percent of AIG's Life Insurance & Retirement Services operating income in 2007, 2006 and 2005, respectively.

Life Insurance & Retirement Services operating income declined in 2007 compared to 2006 primarily due to higher net realized capital losses in 2007. In addition, operating income in 2007 was negatively affected by charges related to remediation activity in Asia; an industry wide regulatory claims review in Japan; the effect of Statement of Position 05-1, ''Accounting by Insurance Enterprises for Deferred Acquisition Costs in Connection with Modifications or Exchanges of Insurance Contracts'' (SOP 05-1), which was adopted in 2007; and investment losses where a FAS 115 trading election was made (trading account).

Financial Services

AIG's Financial Services subsidiaries engage in diversified activities including aircraft and equipment leasing, capital markets, consumer finance and insurance premium finance. Revenues in the Financial Services segment include interest, realized and unrealized gains and losses, including the unrealized market valuation losses on AIGFP's super senior credit default swap portfolio, lease and finance charges.

Financial Services reported an operating loss in 2007 compared to operating income in 2006, primarily due to an unrealized market valuation loss of $11.5 billion on AIGFP's super senior credit default swap portfolio, an other-than-temporary impairment charge of $643 million on AIGFP's investment portfolio of CDOs of asset-backed securities (ABS) and a decline in operating income for AGF. AGF's operating income declined in 2007 compared to 2006 due to reduced residential mortgage origination volume, lower revenues from its mortgage banking activities and increases in the provision for finance receivable losses. In 2007, AGF's mortgage banking operations recorded a pre-tax charge of $178 million, representing the estimated cost of implementing the Supervisory Agreement entered into with the Office of Thrift Supervision (OTS), which is discussed in the Consumer Finance results of operations section.

Operating income for ILFC increased in 2007 compared to 2006, driven to a large extent by a larger aircraft fleet, higher lease rates and higher utilization.

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

Asset Management

AIG's Asset Management operations include institutional and retail asset management, broker-dealer services and spread-based investment businesses. Revenues in the Asset Management segment represent investment income with respect to spread-based products and management, advisory and incentive fees.

Asset Management operating income decreased in 2007 compared to 2006, due to realized capital losses on interest rate and foreign currency hedge positions not qualifying for hedge accounting and other-than-temporary impairment charges on fixed income investments due primarily to disruptions in the U.S. credit markets. These decreases were partially offset by higher partnership income from the Spread-Based Investment business, increased gains on real estate investments and a gain on the sale of a portion of AIG's investment in Blackstone Group, L.P. in connection with its initial public offering.

Capital Resources

At December 31, 2007, AIG had total consolidated shareholders' equity of $95.8 billion and total consolidated borrowings of $176.0 billion. At that date, $67.9 billion of such borrowings were subsidiary borrowings not guaranteed by AIG.

In 2007, AIG issued an aggregate of $5.6 billion of junior subordinated debentures in five series of securities. Substantially all of the proceeds from these sales, net of expenses, were used to repurchase shares of AIG's common stock. A total of 76,361,209 shares were repurchased during 2007.

In February 2007, AIG's Board of Directors increased AIG's share repurchase program by authorizing the repurchase of shares with an aggregate purchase price of $8 billion. In November 2007, AIG's Board of Directors authorized the repurchase of an additional $8 billion in common stock. At February 15, 2008, $10.25 billion was available for repurchase under the aggregate authorization. AIG did not purchase shares of its common stock under its common stock repurchase authorization during 2006. AIG does not expect to purchase additional shares under its share repurchase program for the foreseeable future, other than pursuant to commitments that existed at December 31, 2007.

Liquidity

AIG manages liquidity at both the subsidiary and parent company levels. At December 31, 2007, AIG's consolidated invested assets, primarily held by its subsidiaries, included $65.6 billion in cash and short-term investments. Consolidated net cash provided from operating activities in 2007 amounted to $35.2 billion. At both the subsidiary and parent company level, liquidity management activities are intended to preserve and enhance funding stability, flexibility, and diversity through a wide range of potential operating environments and market conditions. AIG's primary sources of cash flow are dividends and other payments from its regulated and unregulated subsidiaries, as well as issuances of debt securities. Primary uses of cash flow are for debt service, subsidiary funding, shareholder dividend payments and common stock repurchases. As a result of disruption in the credit markets during 2007, AIG took steps to enhance the liquidity of its portfolios, including increasing the liquidity of the collateral in the securities lending program. Management believes that AIG's liquid assets, cash provided by operations and access to the capital markets will enable it to meet its anticipated cash requirements, including the funding of increased dividends under AIG's new dividend policy.

Critical Accounting Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires the application of accounting policies that often involve a significant degree of judgment. AIG considers that its accounting policies that are most dependent on the application of estimates and assumptions, and therefore viewed as critical accounting estimates, to be those relating to reserves for losses and loss expenses, future policy benefits for life and accident and health contracts, recoverability of DAC, estimated gross profits for investment-oriented products, fair value measurements of certain financial assets and liabilities, other-than-temporary impairments, the allowance for finance receivable losses and flight equipment recoverability. These accounting estimates require the use of assumptions about matters, some of which are highly uncertain at the time of estimation. To the extent actual experience differs from the assumptions used, AIG's results of operations would be directly affected.

Throughout this Management's Discussion and Analysis of Financial Condition and Results of Operations, AIG's critical accounting estimates are discussed in detail. The major categories for which assumptions are developed and used to establish each critical accounting estimate are highlighted below.

Reserves for Losses and Loss Expenses (General Insurance):

- *Loss trend factors:* used to establish expected loss ratios for subsequent accident years based on premium rate adequacy and the projected loss ratio with respect to prior accident years.
- *Expected loss ratios for the latest accident year:* in this case, accident year 2007 for the year-end 2007 loss reserve analysis. For low-frequency, high-severity classes such as excess casualty, expected loss ratios generally are utilized for at least the three most recent accident years.
- *Loss development factors:* used to project the reported losses for each accident year to an ultimate amount.
- *Reinsurance recoverable on unpaid losses:* the expected recoveries from reinsurers on losses that have not yet been reported and/or settled.

Future Policy Benefits for Life and Accident and Health Contracts (Life Insurance & Retirement Services):

- *Interest rates:* which vary by geographical region, year of issuance and products.
- *Mortality, morbidity and surrender rates:* based upon actual experience by geographical region modified to allow for variation in policy form, risk classification and distribution channel.

Deferred Policy Acquisition Costs (Life Insurance & Retirement Services):

- *Recoverability:* based on current and future expected profitability, which is affected by interest rates, foreign exchange rates, mortality experience and policy persistency.

Deferred Policy Acquisition Costs (General Insurance):

- *Recoverability:* based upon the current terms and profitability of the underlying insurance contracts.

Estimated Gross Profits (Life Insurance & Retirement Services):

- *Estimated gross profits:* to be realized over the estimated duration of the contracts (investment-oriented products) affect the carrying value of DAC, unearned revenue liability and associated amortization patterns under FAS 97, ''Accounting and Reporting by Insurance Enterprises for Certain Long-Duration Contracts and for Realized Gains and Losses from the Sale of Investments'' (FAS 97); and Sales Inducement Assets under American Institute of Certified Public Accountants (AICPA) Statement of Position (SOP) 03-1, ''Accounting and Reporting by Insurance Enterprises for Certain Nontraditional Long-Duration Contracts and for Separate Accounts'' (SOP 03-1). Estimated gross profits include investment income and gains and losses on investments less required interest, actual mortality and other expenses.

Fair Value Measurements of Financial Instruments:

AIG measures financial instruments in its trading and available for sale securities portfolios, together with securities sold but not yet purchased, certain hybrid financial instruments, and derivative assets and liabilities at fair value. The fair value of a financial instrument is the amount that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date.

The degree of judgment used in measuring the fair value of financial instruments generally correlates with the level of pricing observability. Financial instruments with quoted prices in active markets generally have more pricing observability and less judgment is used in measuring fair value. Conversely, financial instruments traded in other than active markets or that do not have quoted prices have less observability and are measured at fair value using valuation models or other pricing techniques that

require more judgment. Pricing observability is affected by a number of factors, including the type of financial instrument, whether the financial instrument is new to the market and not yet established, the characteristics specific to the transaction and general market conditions.

AIG maximizes the use of observable inputs and minimizes the use of unobservable inputs when measuring fair value. AIG obtains market price data to value financial instruments whenever such information is available. Market price data generally is obtained from market exchanges or dealer quotations. The types of instruments valued based on market price data include G-7 government and agency securities, equities listed in active markets, investments in publicly traded mutual funds with quoted market prices and listed derivatives.

AIG estimates the fair value of fixed income instruments not traded in active markets by referring to traded securities with similar attributes and using a matrix pricing methodology. This methodology considers such factors as the issuer's industry, the security's rating and tenor, its coupon rate, its position in the capital structure of the issuer, and other relevant factors. The types of fixed income instruments not traded in active markets include non-G-7 government securities, municipal bonds, certain hybrid financial instruments, most investment-grade and high-yield corporate bonds, and most mortgage- and asset-backed products.

AIG initially estimates the fair value of equity instruments not traded in active markets by reference to the transaction price. This valuation is adjusted only when changes to inputs and assumptions are corroborated by evidence such as transactions in similar instruments, completed or pending third-party transactions in the underlying investment or comparable entities, subsequent rounds of financing, recapitalizations and other transactions across the capital structure, offerings in the equity capital markets, and changes in financial ratios or cash flows.

For equity and fixed income instruments that are not traded in active markets or that are subject to transfer restrictions, valuations are adjusted to reflect illiquidity and/or non-transferability, and such adjustments generally are based on available market evidence. In the absence of such evidence, management's best estimate is used.

AIG obtains the fair value of its investments in limited partnerships and hedge funds from information provided by the general partner or manager of the investments, the financial statements of which generally are audited annually.

Derivative assets and liabilities can be exchange-traded or traded over the counter (OTC). AIG generally values exchange-traded derivatives within portfolios using models that calibrate to market clearing levels and eliminate timing differences between the closing price of the exchange-traded derivatives and their underlying instruments.

OTC derivatives are valued using market transactions and other market evidence whenever possible, including market-based inputs to models, model calibration to market clearing transactions, broker or dealer quotations or alternative pricing sources with reasonable levels of price transparency. When models are used, the selection of a particular model to value an OTC derivative depends on the contractual terms of, and specific risks inherent in, the instrument as well as the availability of pricing information in the market. AIG generally uses similar models to value similar instruments. Valuation models require a variety of inputs, including contractual terms, market prices and rates, yield curves, credit curves, measures of volatility, prepayment rates and correlations of such inputs. For OTC derivatives that trade in liquid markets, such as generic forwards, swaps and options, model inputs can generally be verified and model selection does not involve significant management judgment.

Certain OTC derivatives trade in less liquid markets with limited pricing information, and the determination of fair value for these derivatives is inherently more difficult. When AIG does not have corroborating market evidence to support significant model inputs and cannot verify the model to market transactions, transaction price is initially used as the best estimate of fair value. Accordingly, when a pricing model is used to value such an instrument, the model is adjusted so that the model value at inception equals the transaction price. Subsequent to initial recognition, AIG updates valuation inputs when corroborated by evidence such as similar market transactions, third-party pricing services and/or broker or dealer quotations, or other empirical market data. When appropriate, valuations are adjusted for various factors such as liquidity, bid/offer spreads and credit considerations. Such adjustments are generally based on available market evidence. In the absence of such evidence, management's best estimate is used.

AIGFP employs a modified version of the Binomial Expansion Technique (BET) model to value its super senior credit default swap portfolio, including maturity-shortening puts that allow the holders of the notes issued by certain multi-sector CDOs to treat the notes as short-term eligible 2a-7 investments under the Investment Company Act of 1940 (2a-7 Puts). The BET model utilizes default probabilities derived from credit spreads implied from market prices for the individual securities included in the underlying collateral pools securing the CDOs, as well as diversity scores, weighted average lives, recovery rates and discount rates. The determination of some of these inputs requires the use of judgment and estimates, particularly in the absence of market observable data. AIGFP also employs a Monte Carlo simulation to assist in quantifying the effect on the valuation of the CDOs of the unique aspects of the CDO's structure such as triggers that divert cash flows to the most senior part of the capital structure. In the final determination of fair value, AIGFP also considers the price estimates for the super senior CDO notes provided by third parties, including counterparties to these transactions, and makes adjustments when deemed necessary. See also Risk Management, Segment Risk Management, Financial Services — Capital Markets Derivative Transactions and Note 8 to Consolidated Financial Statements.

Other-Than-Temporary Impairments:

AIG evaluates its investments for impairment such that a security is considered a candidate for other-than-temporary impairment if it meets any of the following criteria:

- Trading at a significant (25 percent or more) discount to par, amortized cost (if lower) or cost for an extended period of time (nine consecutive months or longer);

- The occurrence of a discrete credit event resulting in (i) the issuer defaulting on a material outstanding obligation; (ii) the issuer seeking protection from creditors under the bankruptcy laws or any similar laws intended for court supervised reorganization of insolvent enterprises; or (iii) the issuer proposing a voluntary reorganization pursuant to which creditors are asked to exchange their claims for cash or securities having a fair value substantially lower than par value of their claims; or
- AIG may not realize a full recovery on its investment, regardless of the occurrence of one of the foregoing events.

The above criteria also consider circumstances of a rapid and severe market valuation decline, such as that experienced in current credit markets, in which AIG could not reasonably assert that the recovery period would be temporary (severity losses).

In light of the recent significant disruption in the U.S. residential mortgage and credit markets, particularly in the fourth quarter, AIG has recognized an other-than-temporary impairment charge (severity loss) of $2.2 billion (including $643 million related to AIGFP's available for sale investment securities recorded in other income), primarily from certain residential mortgage-backed securities and other structured securities. Even while retaining their investment grade ratings, such securities were priced at a severe discount to cost. Notwithstanding AIG's intent and ability to hold such securities indefinitely, and despite structures which indicate that a substantial amount of the securities should continue to perform in accordance with their original terms, AIG concluded that it could not reasonably assert that the recovery period would be temporary.

At each balance sheet date, AIG evaluates its securities holdings with unrealized losses. When AIG does not intend to hold such securities until they have recovered their cost basis, AIG records the unrealized loss in income. If a loss is recognized from a sale subsequent to a balance sheet date pursuant to changes in circumstances, the loss is recognized in the period in which the intent to hold the securities to recovery no longer existed.

In periods subsequent to the recognition of an other-than-temporary impairment charge for fixed maturity securities, which is not credit or foreign exchange related, AIG generally accretes into income the discount or amortizes the reduced premium resulting from the reduction in cost basis over the remaining life of the security.

Allowance for Finance Receivable Losses (Financial Services):

- *Historical defaults and delinquency experience:* utilizing factors, such as delinquency ratio, allowance ratio, charge-off ratio, and charge-off coverage.
- *Portfolio characteristics:* portfolio composition and consideration of the recent changes to underwriting criteria and portfolio seasoning.
- *External factors:* consideration of current economic conditions, including levels of unemployment and personal bankruptcies.
- *Migration analysis:* empirical technique measuring historical movement of similar finance receivables through various levels of repayment, delinquency, and loss categories to existing finance receivable pools.

Flight Equipment Recoverability (Financial Services):

- *Expected undiscounted future net cash flows:* based upon current lease rates, projected future lease rates and estimated terminal values of each aircraft based on third-party information.

Operating Review

General Insurance Operations

AIG's General Insurance subsidiaries write substantially all lines of commercial property and casualty insurance and various personal lines both domestically and abroad.

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

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

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

GAAP provides for the recognition of certain acquisition expenses at the same time revenues are earned, the accounting principle of matching. Therefore, acquisition expenses are deferred and amortized over the period the related net premiums written are earned. DAC is reviewed for recoverability, and such review requires management judgment. The most comparable GAAP measure to statutory underwriting profit is income before income taxes, minority interest and cumulative effect of an accounting change. A table reconciling statutory underwriting profit to income before income taxes, minority interest and cumulative effect of an accounting change is contained in footnote (d) to the following table. See also Critical Accounting Estimates herein and Notes 1 and 6 to Consolidated Financial Statements.

AIG, along with most general insurance companies, uses the loss ratio, the expense ratio and the combined ratio as measures of underwriting performance. The loss ratio is the sum of losses and loss expenses incurred divided by net premiums earned. The expense ratio is statutory underwriting expenses divided by net premiums written. These ratios are relative measurements that describe, for every $100 of net premiums earned or written, the cost of losses and statutory expenses, respectively. The combined ratio is the sum of the loss ratio and the expense ratio. The combined ratio presents the total cost per $100 of premium production. A combined ratio below 100 demonstrates underwriting profit; a combined ratio above 100 demonstrates underwriting loss.

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

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

General Insurance Results

General Insurance operating income is comprised of statutory underwriting profit (loss), changes in DAC, net investment income and net realized capital gains and losses. Operating income, as well as net premiums written, net premiums earned, net investment income and net realized capital gains (losses) and statutory ratios in 2007, 2006 and 2005 were as follows:

				Percentage Increase/(Decrease)	
(in millions, except ratios)	**2007**	2006	2005	2007 vs. 2006	2006 vs. 2005
Net premiums written:					
Domestic General Insurance					
DBG	**$24,112**	$ 24,312	$ 23,104	(1)%	5%
Transatlantic	**3,953**	3,633	3,466	9	5
Personal Lines	**4,808**	4,654	4,653	3	—
Mortgage Guaranty	**1,143**	866	628	32	38
Foreign General Insurance	**13,051**	11,401	10,021	14	14
Total	**$47,067**	$ 44,866	$ 41,872	5%	7%
Net premiums earned:					
Domestic General Insurance					
DBG	**$23,849**	$ 23,910	$ 22,567	—%	6%
Transatlantic	**3,903**	3,604	3,385	8	6
Personal Lines	**4,695**	4,645	4,634	1	—
Mortgage Guaranty	**886**	740	533	20	39
Foreign General Insurance	**12,349**	10,552	9,690	17	9
Total	**$45,682**	$ 43,451	$ 40,809	5%	6%
Net investment income[(a)]:					
Domestic General Insurance					
DBG	**$ 3,879**	$ 3,411	$ 2,403	14%	42%
Transatlantic	**470**	435	343	8	27
Personal Lines	**231**	225	217	3	4
Mortgage Guaranty	**158**	140	123	13	14
Intercompany adjustments and eliminations — net	**6**	1	1	500	—
Foreign General Insurance	**1,388**	1,484	944	(6)	57
Total	**$ 6,132**	$ 5,696	$ 4,031	8%	41%
Net realized capital gains (losses)	**$ (106)**	$ 59	$ 334	—%	—%
Operating income (loss)[(a)(b)]:					
Domestic General Insurance					
DBG	**$ 7,305**	$ 5,845	$ (820)	25%	—%
Transatlantic	**661**	589	(39)	12	—
Personal Lines	**67**	432	195	(84)	122
Mortgage Guaranty	**(637)**	328	363	—	(10)
Foreign General Insurance	**3,137**	3,228	2,601	(3)	24
Reclassifications and eliminations	**(7)**	(10)	15	—	—
Total	**$10,526**	$ 10,412	$ 2,315	1%	350%

Management's Discussion and Analysis of Financial Condition and Results of Operations *Continued*

(in millions, except ratios)	**2007**	2006	2005	Percentage Increase/(Decrease) 2007 vs. 2006	2006 vs. 2005
Statutory underwriting profit (loss)[(b)(d)]:					
Domestic General Insurance					
DBG	**$ 3,404**	$ 2,322	$ (3,403)	47%	—%
Transatlantic	**165**	129	(434)	28	—
Personal Lines	**(191)**	204	(38)	—	—
Mortgage Guaranty	**(849)**	188	249	—	(24)
Foreign General Insurance	**1,544**	1,565	1,461	(1)	7
Total	**$ 4,073**	$ 4,408	$ (2,165)	(8)%	—%
Domestic General Insurance[(b)]:					
Loss ratio	**71.2**	69.6	90.1		
Expense ratio	**20.8**	21.4	21.0		
Combined ratio	**92.0**	91.0	111.1		
Foreign General Insurance[(b)]:					
Loss ratio	**50.6**	48.9	52.0		
Expense ratio[(c)]	**34.9**	33.6	31.8		
Combined ratio	**85.5**	82.5	83.8		
Consolidated[(b)]:					
Loss ratio	**65.6**	64.6	81.1		
Expense ratio	**24.7**	24.5	23.6		
Combined ratio	**90.3**	89.1	104.7		

(a) Includes the effect of out-of-period adjustments related to the accounting for UCITS in 2006. For DBG, the effect was an increase of $66 million, and for Foreign General Insurance, the effect was an increase of $424 million.

(b) Catastrophe-related losses increased the consolidated General Insurance combined ratio in 2007 and 2005 by 0.60 points and 7.06 points, respectively. There were no significant catastrophe-related losses in 2006. Catastrophe-related losses in 2007 and 2005 by reporting unit were as follows:

	2007		2005	
(in millions)	Insurance Related Losses	Net Reinstatement Premium Cost	Insurance Related Losses	Net Reinstatement Premium Cost
Reporting Unit:				
DBG	**$113**	**$(13)**	$1,811	$136
Transatlantic	**11**	**(1)**	463	45
Personal Lines	**61**	**14**	112	2
Mortgage Guaranty	**—**	**—**	10	—
Foreign General Insurance	**90**	**1**	229	80
Total	**$275**	**$ 1**	$2,625	$263

(c) Includes amortization of advertising costs.

(d) Statutory underwriting profit (loss) is a measure that U.S. domiciled insurance companies are required to report to their regulatory authorities. The following table reconciles statutory underwriting profit (loss) to operating income for General Insurance for the years ended December 31, 2007, 2006 and 2005:

(in millions)	Domestic Brokerage Group	Transatlantic	Personal Lines	Mortgage Guaranty	Foreign General Insurance	Reclassifications and Eliminations	Total
2007:							
Statutory underwriting profit (loss)	**$ 3,404**	**$ 165**	**$(191)**	**$(849)**	**$1,544**	**$ —**	**$ 4,073**
Increase in DAC	**97**	**17**	**29**	**57**	**227**	**—**	**427**
Net investment income	**3,879**	**470**	**231**	**158**	**1,388**	**6**	**6,132**
Net realized capital gains (losses)	**(75)**	**9**	**(2)**	**(3)**	**(22)**	**(13)**	**(106)**
Operating income (loss)	**$ 7,305**	**$ 661**	**$ 67**	**$(637)**	**$3,137**	**$ (7)**	**$10,526**
2006:							
Statutory underwriting profit (loss)	$ 2,322	$ 129	$ 204	$ 188	$1,565	$ —	$ 4,408
Increase in DAC	14	14	2	3	216	—	249
Net investment income	3,411	435	225	140	1,484	1	5,696
Net realized capital gains (losses)	98	11	1	(3)	(37)	(11)	59
Operating income (loss)	$ 5,845	$ 589	$ 432	$ 328	$3,228	$(10)	$10,412
2005:							
Statutory underwriting profit (loss)	$(3,403)	$(434)	$ (38)	$ 249	$1,461	$ —	$ (2,165)
Increase (decrease) in DAC	(21)	14	19	(8)	111	—	115
Net investment income	2,403	343	217	123	944	1	4,031
Net realized capital gains (losses)	201	38	(3)	(1)	85	14	334
Operating income (loss)	$ (820)	$ (39)	$ 195	$ 363	$2,601	$ 15	$ 2,315

AIG transacts business in most major foreign currencies. The following table summarizes the effect of changes in foreign currency exchange rates on the growth of General Insurance net premiums written for the years ended December 31, 2007 and 2006:

	2007	2006
Growth in original currency*	**3.5%**	7.4%
Foreign exchange effect	**1.4**	(0.2)
Growth as reported in U.S. dollars	**4.9%**	7.2%

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

2007 and 2006 Comparison

General Insurance operating income increased in 2007 compared to 2006 due to growth in net investment income, partially offset by a decline in underwriting profit and Net realized capital losses. The 2007 combined ratio increased to 90.3, an increase of 1.2 points compared to 2006, primarily due to an increase in the loss ratio of 1.0 points. The loss ratio for accident year 2007 recorded in 2007 was 2.3 points higher than the loss ratio recorded in 2006 for accident year 2006. Increases in Mortgage Guaranty losses accounted for a 2.1 point increase in the 2007 accident year loss ratio. The downward cycle in the U.S. housing market is not expected to improve until residential inventories return to a more normal level, and AIG expects that this downward cycle will continue to adversely affect Mortgage Guaranty's loss ratios for the foreseeable future. The higher accident year loss ratio was partially offset by favorable development on prior years, which reduced incurred losses by $606 million and $53 million in 2007 and 2006, respectively. Additional favorable loss development of $50 million (recognized in consolidation and related to certain asbestos settlements) reduced overall incurred losses.

General Insurance net premiums written increased in 2007 compared to 2006, reflecting growth in Foreign General Insurance from both established and new distribution channels, and the effect of changes in foreign currency exchange rates as well as growth in Mortgage Guaranty, primarily from international business.

General Insurance net investment income increased in 2007 by $436 million. Interest and dividend income increased $714 million in 2007 compared to 2006 as fixed maturities and equity securities increased by $11.6 billion and the average yield increased 10 basis points. Income from partnership investments increased $159 million in 2007 compared to 2006, primarily due to improved returns on underlying investments and higher levels of invested assets. Investment expenses in 2007 declined $60 million compared to 2006, primarily due to decreased interest expense on deposit liabilities. These increases to net investment income were partially offset by $490 million of income from an out of period UCITS adjustment recorded in 2006. Net realized capital losses in 2007 include other-than-temporary impairment charges of $276 million compared to $77 million in 2006. See also Capital Resources and Liquidity and Invested Assets herein.

In order to better align financial reporting with the manner in which AIG's chief operating decision makers manage their businesses, commencing in 2007, the foreign aviation business, which was historically reported in DBG, is now reported as part of Foreign General Insurance, and the oil rig and marine businesses, which were historically reported in Foreign General Insurance, are now reported as part of DBG. Prior period amounts have been revised to conform to the current presentation.

2006 and 2005 Comparison

General Insurance operating income increased in 2006 compared to 2005 due to growth in net premiums, a reduction in both

catastrophe losses and prior accident year development, and growth in Net investment income. The combined ratio improved to 89.1, a reduction of 15.6 points from 2005, including an improvement in the loss ratio of 16.5 points. The reduction in catastrophe losses represented 6.9 points and the reduction in prior year adverse development represented 11.5 points of the overall reduction. Net premiums written increased $3.0 billion or 7 percent in 2006 compared to 2005. Domestic General Insurance accounted for $1.6 billion of the increase as property rates improved and submission activity increased due to the strength of AIG's capacity, commitment to difficult markets and diverse product offerings. Foreign General Insurance contributed $1.4 billion to the increase in net premiums written. In 2005, Domestic General Insurance net premiums written increased by $300 million and Foreign General Insurance net premiums written decreased by the same amount as a result of the commutation of the Richmond reinsurance contract. The commutation partially offset the increase in Domestic General Insurance net premiums written in 2006 compared to 2005 and increased Foreign General Insurance net premiums written in 2006 compared to 2005.

In 2006, certain adjustments were made in conjunction with the remediation of the material weakness relating to balance sheet account reconciliations which increased earned premiums by $189 million and increased other expenses by $415 million. The combined effect of these adjustments increased the expense ratio by 0.9 points and decreased the loss ratio by 0.3 points.

General Insurance net investment income increased $1.67 billion in 2006 to $5.7 billion on higher levels of invested assets, strong cash flows, slightly higher yields and increased partnership income, and included increases from out of period adjustments of $490 million related to the accounting for certain interests in UCITS, $43 million related to partnership income and $85 million related to interest earned on a DBG deposit contract. See also Capital Resources and Liquidity — Liquidity and Invested Assets herein.

DBG Results

2007 and 2006 Comparison

DBG's operating income increased in 2007 compared to 2006 primarily due to growth in both net investment income and underwriting profit. The improvement is also reflected in the combined ratio, which declined 4.5 points in 2007 compared to 2006, primarily due to an improvement in the loss ratio of 3.3 points. Catastrophe-related losses increased the 2007 loss ratio by 0.4 points. The loss ratio for accident year 2007 recorded in 2007 was 0.9 points lower than the loss ratio recorded in 2006 for accident year 2006. The loss ratio for accident year 2006 has improved in each quarter since September 30, 2006. As a result, the 2007 accident year loss ratio is 2.8 points higher than the 2006 accident year loss ratio, reflecting reductions in 2006 accident year losses recorded through December 31, 2007. Prior year development reduced incurred losses by $390 million in 2007 and increased incurred losses by $175 million in 2006, accounting for 2.4 points of the improvement in the loss ratio.

DBG's net premiums written declined in 2007 compared to 2006 as ceded premiums as a percentage of gross written premiums increased to 24 percent in 2007 compared to 23 percent in 2006, primarily due to additional reinsurance for property risks to manage catastrophe exposures.

DBG's expense ratio decreased to 18.7 in 2007 compared to 19.8 in 2006, primarily due to the 2006 charge related to the remediation of the material weakness in internal control over certain balance sheet reconciliations that accounted for 2.1 points of the decline. The decline was partially offset by increases in operating expenses for marketing initiatives and operations.

DBG's net investment income increased in 2007 compared to 2006, as interest income increased $384 million in 2007, on growth in the bond portfolio resulting from investment of operating cash flows. Income from partnership investments increased $159 million in 2007 compared to 2006, primarily due to improved returns on the underlying investments. Other investment income declined $163 million in 2007 compared to 2006, primarily due to out of period adjustments of $194 million recorded in 2006. DBG recorded net realized capital losses in 2007 compared to net realized capital gains in 2006 primarily due to other-than-temporary impairment charges of $213 million in 2007 compared to $73 million in 2006.

2006 and 2005 Comparison

DBG's operating income was $5.85 billion in 2006 compared to a loss of $820 million in 2005, an improvement of $6.67 billion. The improvement is also reflected in the combined ratio, which declined to 89.9 in 2006 compared to 114.6 in 2005 primarily due to an improvement in the loss ratio of 24.9 points. The reduction in prior year adverse development and the reduction in catastrophe losses and related reinstatement premiums accounted for 20.7 points and 8.3 points, respectively, of the improvement.

DBG's net premiums written increased in 2006 compared to 2005 as property rates improved and submission activity increased due to the strength of AIG's capacity, commitment to difficult markets and diverse product offerings. Net premiums written in 2005 were reduced by $136 million due to reinstatement premiums related to catastrophes, offset by increases of $300 million for the Richmond commutation and $147 million related to an accrual for workers compensation premiums for payroll not yet reported by insured employers. The combined effect of these items reduced the growth rate for net premiums written by 1.3 percent.

The loss ratio in 2006 declined 24.9 points to 70.2. The 2005 loss ratio was negatively affected by catastrophe-related losses of $1.8 billion and related reinstatement premiums of $136 million. Adverse development on reserves for loss and loss adjustment expenses declined to $175 million in 2006 compared to $4.9 billion in 2005, accounting for 20.7 points of the decrease in the loss ratio.

DBG's expense ratio increased to 19.8 in 2006 compared to 19.5 in 2005, primarily due to an increase in other expenses that amounted to $498 million in 2006 (including out of period charges of $356 million) compared to $372 million in 2005. This increase added 0.4 points to the expense ratio.

DBG's net investment income increased by $1.0 billion in 2006 compared to 2005, as interest income increased $482 million on growth in the bond portfolio resulting from investment of operating cash flows and capital contributions. Partnership income increased from 2005 due to improved performance of the underlying investments, including initial public offering activity. Net investment income in 2006 included increases relating to out of period adjustments of $109 million for the accounting for UCITS and partnerships and $85 million related to interest earned on a deposit contract that did not exist in the prior year.

Transatlantic Results

2007 and 2006 Comparison

Transatlantic's net premiums written and net premiums earned increased in 2007 compared to 2006 due to increases in both domestic and international operations. The increase in statutory underwriting profit in 2007 compared to 2006 reflects improved underwriting results in Domestic operations. Operating income increased in 2007 compared to 2006 due principally to increased net investment income and improved underwriting results.

2006 and 2005 Comparison

Transatlantic's net premiums written and net premiums earned increased in 2006 compared to 2005 due primarily to increased writings in domestic operations. Operating income increased in 2006 compared to 2005 due largely to lower catastrophe losses and net ceded reinstatement premiums, and increased net investment income.

Personal Lines Results

2007 and 2006 Comparison

Personal Lines operating income in 2007 decreased by $365 million compared to 2006, largely due to an increase in incurred losses from a number of sources, leading to an overall increase in the loss ratio of 6.8 points. Prior year net adverse reserve development contributed 2.5 points of this increase in the loss ratio, as Personal Lines experienced $7 million in net adverse development (including $64 million in adverse development from businesses placed in runoff), compared to $111 million of favorable development in 2006. An additional 1.6 point increase in the loss ratio resulted from $61 million of losses and $14 million of reinstatement premiums due to the California wildfires. In addition, an increase in the loss ratio recorded in 2007 for accident year 2007 compared to the loss ratio recorded in 2006 for accident year 2006 of 2.7 points resulted, in part, from an increased frequency of large losses in the Private Client Group and average automobile premiums declining faster than loss trends.

Operating income also declined due to increased expenses. The expense ratio increased 1.1 points in 2007 compared to 2006, primarily due to $63 million of transaction and integration costs associated with the 2007 acquisition of the minority interest in 21st Century.

Net premiums written increased in 2007 compared to 2006 due to continued growth in the Private Client Group and increased new business production in the aigdirect.com business partially offset by a reduction in the Agency Auto business.

On September 27, 2007, AIG completed its previously announced acquisition of 21st Century, paying $759 million to acquire the remaining 39.2 percent of the shares of 21st Century that it did not previously own. As a result of the acquisition, the AIG Direct and 21st Century operations have been combined as aigdirect.com.

Under the purchase method of accounting, the assets and liabilities of 21st Century that were acquired were adjusted to their estimated fair values as of the date of the acquisition, and goodwill of $342 million was recorded. A customer relationship intangible asset, initially valued at $119 million, was also established.

2006 and 2005 Comparison

Personal Lines operating income increased $237 million in 2006 compared to 2005 reflecting a reduction in the loss ratio of 5.8 points. Favorable development on prior accident years reduced incurred losses by $111 million in 2006 compared to an increase of $14 million in 2005, accounting for 2.7 points of the decrease in the loss ratio. The 2005 catastrophe-related losses of $112 million added 2.4 points to the loss ratio. The loss ratio for the 2006 accident year improved 0.7 points primarily due to the termination of The Robert Plan relationship effective December 31, 2005 and growth in the Private Client Group. The improvement in the loss ratio was partially offset by an increase in the expense ratio of 0.6 points primarily due to investments in people and technology, national expansion efforts and lower response rates. Net premiums written were flat in 2006 compared to 2005, with growth in the Private Client Group and Agency Auto divisions offset by termination of The Robert Plan relationship. Growth in the Private Client Group spans multiple products, with a continued penetration of the high net worth market, strong brand promotion and innovative loss prevention programs.

Mortgage Guaranty Results

2007 and 2006 Comparison

Mortgage Guaranty's operating loss in 2007 was $637 million compared to operating income of $328 million in 2006 as the deteriorating U.S. residential housing market adversely affected losses incurred for both the domestic first- and second-lien businesses. Domestic first- and second-lien losses incurred increased 362 percent and 346 percent respectively, compared to 2006, resulting in loss ratios of 122.0 and 357.0, respectively, in 2007. Increases in domestic losses incurred resulted in an overall loss ratio of 168.6 in 2007 compared to 47.2 in 2006. Prior year development reduced incurred losses in 2007 by $25 million compared to a reduction of $115 million in 2006, which accounted for 12.7 points of the increase in the loss ratio.

Net premiums written increased in 2007 compared to 2006 primarily due to growth in the international markets, accounting for 19 percent of the increase in net premiums written. In addition

the increased use of mortgage insurance for credit enhancement as well as better persistency resulted in an increase in domestic first-lien premiums. UGC has taken steps to strengthen its underwriting guidelines and increase rates. It also discontinued new production for certain programs in the second-lien business beginning in the fourth quarter of 2006. However, UGC will continue to receive renewal premiums on that portfolio for the life of the loans, estimated to be three to five years, and will continue to be exposed to possible losses from future defaults.

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

UGC domestic mortgage risk in force totaled $29.8 billion as of December 31, 2007 and the 60-day delinquency ratio was 3.7 percent (based on number of policies, consistent with mortgage industry practice) compared to domestic mortgage risk in force of $24.9 billion and a delinquency ratio of 2.1 percent at December 31, 2006. Approximately 81 percent of the domestic mortgage risk is secured by first-lien, owner-occupied properties.

2006 and 2005 Comparison

Mortgage Guaranty operating income declined in 2006 from 2005 due primarily to unfavorable loss experience on third-party originated second-lien business with a credit quality lower than typical for UGC and a softening U.S. housing market. This increased Mortgage Guaranty's consolidated loss ratio in 2006 to 47.2 compared to 26.0 in 2005. The writing of this second-lien coverage, which began in 2005, was discontinued as of year end 2006. Losses in the second-lien business have been mitigated by a policy year aggregate limitation provision that is typically established for each lender.

Net premiums written increased due to growth in the domestic second-lien and international businesses as well as improved persistency in the domestic first-lien business. The expense ratio remained flat as premium growth covered increased expenses related to expansion internationally and continued investment in risk management resources.

Foreign General Insurance Results

2007 and 2006 Comparison

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

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

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

The 2007 expense ratio increased 1.3 points compared to 2006. This increase reflected the cost of realigning certain legal entities through which Foreign General Insurance operates and the increased significance of consumer lines of business, which have higher acquisition costs. These factors contributed 0.7 points to the 2007 expense ratio. AIG expects the expense ratio to increase in 2008 due to the continued cost of realigning certain legal entities through which Foreign General Insurance operates.

Net investment income decreased in 2007 compared to 2006 as the 2006 period included the out of period UCITS adjustments, which more than offset increases resulting from higher interest rates, increased cash flows and mutual fund income. Mutual fund income was $93 million higher than 2006 reflecting improved performance in the equity markets in 2007. Partnership income was essentially unchanged.

2006 and 2005 Comparison

Foreign General Insurance operating income increased in 2006 compared to 2005 due to out of period UCITS adjustments in 2006, the absence of significant catastrophe-related losses in 2006, rate increases and lower current accident year losses by Ascot on its U.S. book of business and lower asbestos and environmental reserve increases. These increases were partially offset by lower favorable loss development from prior accident years and adverse loss development on the 2005 hurricanes. Statutory underwriting profit increased $104 million in 2006 compared to 2005. Catastrophes in 2005 resulted in losses of $229 million and reinstatement premiums of $80 million.

Net premiums written increased 14 percent (15 percent in original currency) in 2006 compared to 2005, reflecting growth in both commercial and consumer lines driven by new business from both established and new distribution channels, including a wholly owned insurance company in Vietnam and Central Insurance Co., Ltd. in Taiwan. Ascot also contributed to the growth in net premiums written as a result of rate increases on its U.S. business. Consumer lines in Latin America and commercial lines in Europe, including the U.K., also contributed to the increase. Net premiums written in 2005 were reduced by reinstatement premiums related to catastrophes and a portfolio

transfer of unearned premium reserves to DBG related to the Richmond commutation, accounting for 4 percent of the increase in 2006 compared to 2005.

The loss ratio decreased 3.1 points in 2006 compared to 2005, as the absence of significant catastrophes in 2006 resulted in a decrease in the loss ratio of 2.8 points. The loss ratio also decreased due to rate increases and lower current year losses by Ascot on its U.S. book of business and lower asbestos and environmental reserve increases. These declines were partially offset by lower favorable loss development from prior accident years and adverse development on 2005 hurricanes.

The expense ratio increased 1.8 points in 2006 compared to 2005 due to a $59 million out of period adjustment for amortization of deferred advertising costs and a premium reduction of $61 million related to reconciliation remediation activities, in aggregate accounting for 0.7 points of the increase in the expense ratio. The expense ratio also increased due to growth in consumer business lines, which have higher acquisition expenses but historically lower loss ratios.

Net investment income increased $540 million in 2006 compared to 2005 primarily due to a $424 million out of period UCITS adjustment.

Reserve for Losses and Loss Expenses

The following table presents the components of the General Insurance gross reserve for losses and loss expenses (loss reserves) as of December 31, 2007 and 2006 by major lines of business on a statutory Annual Statement basis[a]:

(in millions)	**2007**	2006[b]
Other liability occurrence	**$20,580**	$19,327
Workers compensation	**15,568**	13,612
Other liability claims made	**13,878**	12,513
Auto liability	**6,068**	6,070
International	**7,036**	6,006
Property	**4,274**	5,499
Reinsurance	**3,127**	2,979
Medical malpractice	**2,361**	2,347
Products liability	**2,416**	2,239
Accident and health	**1,818**	1,693
Commercial multiple peril	**1,900**	1,651
Aircraft	**1,623**	1,629
Fidelity/surety	**1,222**	1,148
Mortgage Guaranty/Credit	**1,426**	567
Other	**2,203**	2,719
Total	**$85,500**	$79,999

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

(b) Allocations among various lines were revised based on the 2007 presentation.

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

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

At December 31, 2007, General Insurance net loss reserves increased $6.66 billion from 2006 to $69.29 billion. The net loss reserves represent loss reserves reduced by reinsurance recoverable, net of an allowance for unrecoverable reinsurance and applicable discount for future investment income.

The following table classifies the components of the General Insurance net loss reserve by business unit as of December 31, 2007 and 2006:

(in millions)	**2007**	2006
DBG[a]	**$47,392**	$44,119
Transatlantic	**6,900**	6,207
Personal Lines[b]	**2,417**	2,440
Mortgage Guaranty	**1,339**	460
Foreign General Insurance[c]	**11,240**	9,404
Total Net Loss Reserve	**$69,288**	$62,630

(a) At December 31, 2007 and 2006, respectively, DBG loss reserves include approximately $3.13 billion and $3.33 billion ($3.34 billion and $3.66 billion, respectively, before discount), related to business written by DBG but ceded to AIRCO and reported in AIRCO's statutory filings. DBG loss reserves also include approximately $590 million and $535 million related to business included in AIUO's statutory filings at December 31, 2007 and 2006, respectively.

(b) At December 31, 2007 and 2006, respectively, Personal Lines loss reserves include $894 million and $861 million related to business ceded to DBG and reported in DBG's statutory filings.

(c) At December 31, 2007 and 2006, respectively, Foreign General Insurance loss reserves include approximately $3.02 billion and $2.75 billion related to business reported in DBG's statutory filings.

The DBG net loss reserve of $47.4 billion is comprised principally of the business of AIG subsidiaries participating in the American Home Assurance Company (American Home)/National Union Fire Insurance Company of Pittsburgh, Pa. (National Union) pool (10 companies) and the surplus lines pool (Lexington, AIG Excess Liability Insurance Company and Landmark Insurance Company).

DBG cedes a quota share percentage of its other liability occurrence and products liability occurrence business to AIRCO. The quota share percentage ceded was 15 percent in 2007 and 20 percent in 2006 and covered all business written in these years for these lines by participants in the American Home/National Union pool. AIRCO's loss reserves relating to these quota share cessions from DBG are recorded on a discounted basis. As of December 31, 2007, AIRCO carried a discount of approximately $210 million applicable to the $3.34 billion in undiscounted reserves it assumed from the American Home/National Union pool via this quota share cession. AIRCO also carries approximately $540 million in net loss reserves relating to Foreign General Insurance business. These reserves are carried on an undiscounted basis.

The companies participating in the American Home/National Union pool have maintained a participation in the business written by AIU for decades. As of December 31, 2007, these AIU reserves carried by participants in the American Home/National Union pool totaled approximately $3.02 billion. The remaining Foreign General Insurance reserves are carried by AIUO, AIRCO, and other smaller AIG subsidiaries domiciled outside the United States. Statutory filings in the United States by AIG companies reflect all the business written by U.S. domiciled entities only, and therefore exclude business written by AIUO, AIRCO, and all other internationally domiciled subsidiaries. The total reserves carried at December 31, 2007 by AIUO and AIRCO were approximately $5.16 billion and $3.67 billion, respectively. AIRCO's $3.67 billion in total general insurance reserves consist of approximately $3.13 billion from business assumed from the American Home/National Union pool and an additional $540 million relating to Foreign General Insurance business.

Discounting of Reserves

At December 31, 2007, AIG's overall General Insurance net loss reserves reflect a loss reserve discount of $2.43 billion, including tabular and non-tabular calculations. The tabular workers compensation discount is calculated using a 3.5 percent interest rate and the 1979-81 Decennial Mortality Table. The non-tabular workers compensation discount is calculated separately for companies domiciled in New York and Pennsylvania, and follows the statutory regulations for each state. For New York companies, the discount is based on a five percent interest rate and the companies' own payout patterns. For Pennsylvania companies, the statute has specified discount factors for accident years 2001 and prior, which are based on a six percent interest rate and an industry payout pattern. For accident years 2002 and subsequent, the discount is based on the yield of U.S. Treasury securities ranging from one to twenty years and the company's own payout pattern, with the future expected payment for each year using the interest rate associated with the corresponding Treasury security yield for that time period. The discount is comprised of the following: $794 million — tabular discount for workers compensation in DBG; $1.42 billion — non-tabular discount for workers compensation in DBG; and, $210 million — non-tabular discount for other liability occurrence and products liability occurrence in AIRCO. The total undiscounted workers compensation loss reserve carried by DBG is approximately $13.3 billion as of December 31, 2007. The other liability occurrence and products liability occurrence business in AIRCO that is assumed from DBG is discounted based on the yield of U.S. Treasury securities ranging from one to twenty years and the DBG payout pattern for this business. The undiscounted reserves assumed by AIRCO from DBG totaled approximately $3.34 billion at December 31, 2007.

Results of the Reserving Process

Management believes that the General Insurance net loss reserves are adequate to cover General Insurance net losses and loss expenses as of December 31, 2007. While AIG regularly reviews the adequacy of established loss reserves, there can be no assurance that AIG's ultimate loss reserves will not develop adversely and materially exceed AIG's loss reserves as of December 31, 2007. In the opinion of management, such adverse development and resulting increase in reserves is not likely to have a material adverse effect on AIG's consolidated financial condition, although it could have a material adverse effect on AIG's consolidated results of operations for an individual reporting period. See also Item 1A. Risk Factors — Casualty Insurance and Underwriting Reserves.

The following table presents the reconciliation of net loss reserves for 2007, 2006 and 2005 as follows:

(in millions)	**2007**	2006	2005
Net reserve for losses and loss expenses at beginning of year	**$62,630**	$57,476	$47,254
Foreign exchange effect	**955**	741	(628)
Acquisitions[(a)]	**317**	55	—
Losses and loss expenses incurred:			
Current year	**30,261**	27,805	28,426
Prior years, other than accretion of discount	**(656)**	(53)	4,680[(b)]
Prior years, accretion of discount	**327**	300	(15)
Losses and loss expenses incurred	**29,932**	28,052	33,091
Losses and loss expenses paid:			
Current year	**9,684**	8,368	7,331
Prior years	**14,862**	15,326	14,910
Losses and loss expenses paid	**24,546**	23,694	22,241
Net reserve for losses and loss expenses at end of year	**$69,288**	$62,630	$57,476

(a) Reflects the opening balance with respect to the acquisitions of WüBa and the Central Insurance Co., Ltd. in 2007 and 2006, respectively.

(b) Includes fourth quarter charge of $1.8 billion.

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

(in millions)	**2007**	2006	2005
Prior Accident Year Development by Reporting Unit:			
DBG	**$ (390)**	$ 175	$4,878
Personal Lines	**7**	(111)	14
UGC	**(25)**	(115)	(103)
Foreign General Insurance	**(286)**	(183)	(378)
Sub total	**(694)**	(234)	4,411
Transatlantic	**88**	181	269
Asbestos settlements*	**(50)**	—	—
Prior years, other than accretion of discount	**$ (656)**	$ (53)	$4,680

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

(in millions)	**2007**	2006	2005
Prior Accident Year Development by Major Class of Business:			
Excess casualty (DBG)	**$ 73**	$ 102	$1,191
D&O and related management liability (DBG)	**(305)**	(20)	1,627
Excess workers compensation (DBG)	**(14)**	74	983
Reinsurance (Transatlantic)	**88**	181	269
Asbestos and environmental (primarily DBG)	**18**	208	930
All other, net	**(516)**	(598)	(320)
Prior years, other than accretion of discount	**$ (656)**	$ (53)	$4,680

Accident Year *(in millions)*	Calendar Year **2007**	2006	2005
Prior Accident Year Development by Accident Year:			
2006	**$ (1,248)**		
2005	**(446)**	$ (1,576)	
2004	**(428)**	(511)	$ (3,853)
2003	**37**	(212)	(63)
2002	**234**	373	1,360
2001	**263**	29	1,749
2000	**321**	338	1,323
1999	**47**	382	944
1998	**154**	41	605
1997 & Prior	**410**	1,083	2,615
Prior years, other than accretion of discount	**$ (656)**	$ (53)	$ 4,680

In determining the loss development from prior accident years, AIG conducts analyses to determine the change in estimated ultimate loss for each accident year for each profit center. For example, if loss emergence for a profit center is different than expected for certain accident years, the actuaries examine the indicated effect such emergence would have on the reserves of that profit center. In some cases, the higher or lower than expected emergence may result in no clear change in the ultimate loss estimate for the accident years in question, and no adjustment would be made to the profit center's reserves for prior accident years. In other cases, the higher or lower than expected emergence may result in a larger change, either favorable or unfavorable, than the difference between the actual and expected loss emergence. Such additional analyses were conducted for each profit center, as appropriate, in 2007 to determine the loss development from prior accident years for 2007. As part of its reserving process, AIG also considers notices of claims received with respect to emerging issues, such as those related to the U.S. mortgage and housing market.

The loss ratios recorded by AIG in 2006 took into account the results of the comprehensive reserve reviews that were completed in the fourth quarter of 2005. AIG's year-end 2005 reserve review reflected careful consideration of the reserve analyses prepared by AIG's internal actuarial staff with the assistance of third-party

actuaries. In determining the appropriate loss ratios for accident year 2006 for each class of business, AIG gave consideration to the loss ratios resulting from the 2005 reserve analyses as well as all other relevant information including rate changes, expected changes in loss costs, changes in coverage, reinsurance or mix of business, and other factors that may affect the loss ratios.

2007 Net Loss Development

In 2007, net loss development from prior accident years was favorable by approximately $656 million, including approximately $88 million of adverse development from Transatlantic; and excluding approximately $327 million from accretion of loss reserve discount. Excluding Transatlantic, as well as accretion of discount, net loss development in 2007 from prior accident years was favorable by approximately $744 million. The overall favorable development of $656 million consisted of approximately $2.12 billion of favorable development from accident years 2004 through 2006, partially offset by approximately $1.43 billion of adverse development from accident years 2002 and prior and $37 million of adverse development from accident year 2003. In 2007, most classes of AIG's business continued to experience favorable development for accident years 2004 through 2006. The majority of the adverse development from accident years 2002 and prior was related to development from excess casualty and primary workers compensation business within DBG and from Transatlantic. The development from accident year 2003 was primarily related to adverse development from excess casualty and primary workers compensation business within DBG offset by favorable development from most other classes of business. The overall favorable development of $656 million includes approximately $305 million pertaining to the D&O and related management liability classes of business within DBG, consisting of approximately $335 million of favorable development from accident years 2003 through 2006, partially offset by approximately $30 million of adverse development from accident years 2002 and prior. The overall favorable development of $656 million also includes approximately $300 million of adverse development from primary workers compensation business within DBG. See Volatility of Reserve Estimates and Sensitivity Analyses below.

2006 Net Loss Development

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

2005 Net Loss Development

In 2005, net loss development from prior accident years was adverse by approximately $4.68 billion, including approximately $269 million from Transatlantic. This $4.68 billion adverse development in 2005 was comprised of approximately $8.60 billion for the 2002 and prior accident years, partially offset by favorable development for accident years 2003 and 2004 for most classes of business, with the notable exception of D&O. The adverse loss development for 2002 and prior accident years was attributable to approximately $4.0 billion of development from the D&O and related management liability classes of business, excess casualty, and excess workers compensation, and to approximately $900 million of adverse development from asbestos and environmental claims. The remaining portion of the adverse development from 2002 and prior accident years included approximately $520 million related to Transatlantic with the balance spread across many other classes of business. Most classes of business produced favorable development for accident years 2003 and 2004, and adverse development for accident years 2001 and prior.

Net Loss Development by Class of Business

The following is a discussion of the primary reasons for the development in 2007, 2006 and 2005 for those classes of business that experienced significant prior accident year developments during the three-year period. See Asbestos and Environmental Reserves below for a further discussion of asbestos and environmental reserves and developments.

Excess Casualty: Excess Casualty reserves experienced significant adverse loss development in 2005, but there was only a relatively minor amount of adverse development in 2006 and 2007. The adverse development for all periods shown related principally to accident years 2002 and prior, and resulted from significant loss cost increases due to both frequency and severity of claims. The increase in loss costs resulted primarily from medical inflation, which increased the economic loss component of tort claims, advances in medical care, which extended the life span of severely injured claimants, and larger jury verdicts, which increased the value of severe tort claims. An additional factor affecting AIG's excess casualty experience in recent years has been the accelerated exhaustion of underlying primary policies for homebuilders. This has led to increased construction defect-related claims activity on AIG's excess policies. Many excess casualty policies were written on a multi-year basis in the late

1990s, which limited AIG's ability to respond to emerging market trends as rapidly as would otherwise be the case. In subsequent years, AIG responded to these emerging trends by increasing rates and implementing numerous policy form and coverage changes. This led to a significant improvement in experience beginning with accident year 2001. In 2007, a significant portion of the adverse development from accident years 2002 and prior also related to other latent exposures, including pharmaceutical and product aggregate-related exposures as well as the construction defect exposures noted above. AIG's exposure to these latent exposures was sharply reduced after 2002 due to significant changes in policy terms and conditions as well as underwriting guidelines.

For the year-end 2005 loss reserve review, AIG's actuaries responded to the continuing adverse development by further increasing the loss development factors applicable to accident years 1999 and subsequent by approximately 5 percent. In addition, to more accurately estimate losses for construction defect-related claims, a separate review was performed by AIG claims staff for accounts with significant exposure to these claims.

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

For the year-end 2007 loss reserve review, AIG claims staff updated its review of accounts with significant exposure to construction defect-related claims. AIG's actuaries determined that no significant changes in the assumptions were required. Prior accident year loss developments in 2007 were adverse by approximately $75 million, a minor amount for this class of business. However, AIG continued to experience adverse development in this class for accident years 2002 and prior, amounting to approximately $450 million in 2007. In addition, loss reserves developed adversely for accident year 2003 by approximately $100 million in 2007 for this class. The loss ratio for accident year 2003 remains very favorable for this class and has been relatively stable over the past several years. Favorable developments in 2007 for accident years 2004 through 2006 largely offset the adverse developments from accident years 2003 and prior. A significant portion of the adverse development from accident years 2002 and prior related to the latent exposures described above.

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

D&O and Related Management Liability Classes of Business: These classes of business experienced significant adverse development in 2005, but experienced slightly favorable development in 2006 and more significantly favorable development in 2007. The adverse development in 2005 related principally to accident years 2002 and prior. This adverse development resulted from significant loss cost escalation due to a variety of factors, including the following: the increase in frequency and severity of corporate bankruptcies; the increase in frequency of financial statement restatements; the sharp rise in market capitalization of publicly traded companies; and the increase in the number of initial public offerings, which led to an unprecedented number of IPO allocation/laddering suits in 2001. In addition, extensive utilization of multi-year policies during this period limited AIG's ability to respond to emerging trends as rapidly as would otherwise be the case. AIG experienced significant adverse loss development during the period 2002 through 2005 as a result of these issues. AIG responded to this development with rate increases and policy form and coverage changes to better contain future loss costs in this class of business.

For the year-end 2005 loss reserve review, AIG's actuaries responded to the continuing adverse development by further increasing the loss development factor assumptions. The loss development factors applicable to 1997 and subsequent accident years were increased by approximately 4 percent. In addition, AIG's actuaries began to give greater weight to loss development methods for accident years 2002 and 2003, in order to more fully respond to the recent loss experience. AIG's claims staff also conducted a series of ground-up claim projections covering all open claims for this business through accident year 2004. AIG's actuaries benchmarked the loss reserve indications for all accident years through 2004 to these claim projections.

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

For the year-end 2007 loss reserve review, AIG's actuaries determined that no significant changes in the assumptions were required. Prior accident year reserve development in 2007 was favorable by approximately $305 million, due primarily to favorable development from accident years 2004 and 2005, and to a lesser extent 2003 and 2006. AIG's actuaries continued to benchmark the loss reserve indications to the ground-up claim projections provided by AIG claims staff for this class of business. For the year-end 2007 loss reserve review, the ground-up claim projections included all accident years through 2006, and included stock options backdating-related exposures from accident year 2006. Accident year 2006 reserves developed favorably notwithstanding the effect of claims relating to stock options backdating, which totaled approximately $300 million. Further, AIG is closely monitoring claims activity in accident year 2007 relating to the U.S. residential mortgage market, consistent with the manner in which claims relating to stock options backdating were monitored

in 2006, and believes that its reserves as of December 31, 2007 are adequate for its D&O and related management liability classes of business.

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

Excess Workers Compensation: This class of business experienced significant adverse development in 2005, a relatively minor amount of adverse development in 2006, and a minor amount of favorable development in 2007. The adverse development in 2005 related to 2002 and prior accident years. This adverse development resulted primarily from significant loss cost increases, primarily attributable to rapidly increasing medical inflation and advances in medical care, which increased the cost of covered medical care and extended the life span of severely injured workers. The effect of these factors on excess workers compensation claims experience is leveraged, as frequency is increased by the rising number of claims that reach the excess layers.

In response to the significantly adverse loss development in 2005, an additional study was conducted for the 2005 year-end actuarial reserve analysis for DBG pertaining to the selection of loss development factors for this class of business. Claims for excess workers compensation exhibit an exceptionally long-tail of loss development, running for decades from the date the loss is incurred. Thus, the adequacy of loss reserves for this class is sensitive to the estimated loss development factors, as such factors may be applied to many years of loss experience. In order to better estimate the tail development for this class, AIG claims staff conducted a claim-by-claim projection of the expected ultimate paid loss for each open claim for 1998 and prior accident years as these are the primary years from which the tail factors are derived. The objective of the study was to provide a benchmark against which loss development factors in the tail could be evaluated. The resulting loss development factors utilized by the actuaries in the year-end 2005 study reflected an increase of approximately 18 percent from the factors used in the prior year study without the benefit of the claims benchmark. In addition, the loss cost trend assumption for excess workers compensation was increased from approximately 2.5 percent to 6 percent for the 2005 study.

For the year-end 2006 loss reserve review, AIG claims staff updated the claim-by-claim projection for each open claim for accident years 1999 and prior. These updated claims projections were utilized by the actuaries as a benchmark for loss development factors in the year-end 2006 study. AIG's actuaries determined that no significant changes in the assumptions were required. Prior accident year development in 2006 was adverse by approximately $70 million, a relatively minor amount for this class.

For the year-end 2007 loss reserve review, AIG claims staff again updated the claim-by-claim projection for each open claim for accident years 2000 and prior. These updated claims projections were utilized by the actuaries as a benchmark for loss development factors in the year-end 2007 study. AIG's actuaries determined that no significant changes in the assumptions were required. Prior accident year development in 2007 was favorable by approximately $15 million, an insignificant amount for this class.

Overview of Loss Reserving Process

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

Short-Tail Reserves

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

Long-Tail Reserves

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

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

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

- Loss trend factors which are used to establish expected loss ratios for subsequent accident years based on the projected loss ratio for prior accident years.
- Expected loss ratios for the latest accident year (i.e., accident year 2007 for the year-end 2007 loss reserve analysis) and, in some cases for accident years prior to the latest accident year. The expected loss ratio generally reflects the projected loss ratio from prior accident years, adjusted for the loss trend (see above) and the effect of rate changes and other quantifiable factors on the loss ratio. For low-frequency, high-severity classes such as excess casualty, expected loss ratios generally are used for at least the three most recent accident years.
- Loss development factors which are used to project the reported losses for each accident year to an ultimate basis. Generally, the actual loss development factors observed from prior accident years would be used as a basis to determine the loss development factors for the subsequent accident years.

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

Details of the Loss Reserving Process

The process of determining the current loss ratio for each class of business is based on a variety of factors. These include, but are not limited to, the following considerations: prior accident year and policy year loss ratios; rate changes; changes in coverage, reinsurance, or mix of business; and actual and anticipated changes in external factors affecting results, such as trends in loss costs or in the legal and claims environment. The current loss ratio for each class of business reflects input from actuarial, underwriting and claims staff and is intended to represent management's best estimate of the current loss ratio after reflecting all of the factors described above. At the close of each quarter, the assumptions underlying the loss ratios are reviewed to determine if the loss ratios based thereon remain appropriate. This process includes a review of the actual claims experience in the quarter, actual rate changes achieved, actual changes in coverage, reinsurance or mix of business, and changes in certain other factors that may affect the loss ratio. When this review suggests that the initially determined loss ratio is no longer appropriate, the loss ratio for current business is changed to reflect the revised assumptions.

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

Actuarial Methods for Major Classes of Business

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

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

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

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

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

frequency/severity methods to test loss reserves, due to the general nature of AIG's reserves being applicable to lower frequency, higher severity commercial classes of business where average claim severity is volatile.

Excess Casualty: AIG generally uses a combination of loss development methods and expected loss ratio methods for excess casualty classes. Expected loss ratio methods are generally utilized for at least the three latest accident years, due to the relatively low credibility of the reported losses. The loss experience is generally reviewed separately for lead umbrella classes and for other excess classes, due to the relatively shorter tail for lead umbrella business. Automobile-related claims are generally reviewed separately from non-auto claims, due to the shorter tail nature of the automobile related claims. The expected loss ratios utilized for recent accident years are based on the projected ultimate loss ratios of prior years, adjusted for rate changes, estimated loss cost trends and all other changes that can be quantified. The estimated loss cost trend utilized in the year-end 2007 reviews averaged approximately five percent for excess casualty classes. Frequency/severity methods are generally not utilized as the vast majority of reported claims do not result in a claim payment. In addition, the average severity varies significantly from accident year to accident year due to large losses which characterize this class of business, as well as changing proportions of claims which do not result in a claim payment.

D&O: AIG generally utilizes a combination of loss development methods and expected loss ratio methods for D&O and related management liability classes of business. Expected loss ratio methods are given more weight in the two most recent accident years, whereas loss development methods are given more weight in more mature accident years. Beginning with the year-end 2005 loss reserve review, AIG's actuaries began to utilize claim projections provided by AIG claims staff as a benchmark for determining the indicated ultimate losses for accident years 2004 and prior. For the year end 2007 loss reserve review, claims projections for accident years 2006 and prior were utilized. In prior years, AIG's actuaries had utilized these claims projections as a benchmark for profitability studies for major classes of D&O and related management liability business. The track record of these claims projections has indicated a very low margin of error, thus providing support for their usage as a benchmark in determining the estimated loss reserve. These classes of business reflect claims made coverage, and losses are characterized by low frequency and high severity. Thus, the claim projections can produce an accurate overall indicator of the ultimate loss exposure for these classes by identifying and estimating all large losses. Frequency/severity methods are generally not utilized for these classes as the overall losses are driven by large losses more than by claim frequency. Severity trends have varied significantly from accident year to accident year.

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

Excess Workers Compensation: AIG generally utilizes a combination of loss development methods and expected loss ratio methods. Loss development methods are given the greater weight for mature accident years such as 2001 and prior. Expected loss ratio methods are given the greater weight for the more recent accident years. Excess workers compensation is an extremely long-tail class of business, with loss emergence extending for decades. Therefore there is limited credibility in the reported losses for many of the more recent accident years. Beginning with the year-end 2005 loss reserve review, AIG's actuaries began to utilize claims projections provided by AIG claims staff to help determine the loss development factors for this class of business.

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

Commercial Automobile Liability: AIG generally utilizes loss development methods for all but the most recent accident year for commercial automobile classes of business. Expected loss ratio methods are generally given significant weight only in the most recent accident year. Frequency/severity methods are generally

not utilized due to significant changes and growth in this business over the years.

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

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

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

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

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

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

Mortgage Guaranty: AIG tests mortgage guaranty reserves using loss development methods, supplemented by an internal claim analysis by actuaries and staff who specialize in the mortgage guaranty business. The claim analysis projects ultimate losses for claims within each of several categories of delinquency based on actual historical experience and is essentially a frequency/severity analysis for each category of delinquency. Additional reserve tests using ''Bornhuetter Ferguson'' methods are also employed, as well as tests measuring losses as a percent of risk in force. Reserves are reviewed separately for each class of business to consider the loss development characteristics associated with the claims, the volume of claim data available for the applicable class and the applicability of various actuarial methods to the class.

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

International: Business written by AIG's Foreign General Insurance sub-segment includes both long-tail and short-tail classes of business. For long-tail classes of business, the actuarial methods utilized would be analogous to those described above. However, the majority of business written by Foreign General Insurance is short-tail, high frequency and low severity in nature. For this business, loss development methods are generally employed to

test the loss reserves. AIG maintains a data base of detailed historical premium and loss transactions in original currency for business written by Foreign General Insurance, thereby allowing AIG actuaries to determine the current reserves without any distortion from changes in exchange rates over time. In testing the Foreign General Insurance reserves, AIG's actuaries segment the data by region, country or class of business as appropriate to determine an optimal balance between homogeneity and credibility.

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

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

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

Volatility of Reserve Estimates and Sensitivity Analyses

As described above, AIG uses numerous assumptions in determining its best estimate of reserves for each class of business. The importance of any specific assumption can vary by both class of business and accident year. If actual experience differs from key assumptions used in establishing reserves, there is potential for significant variation in the development of loss reserves, particularly for long-tail casualty classes of business such as excess casualty, D&O or workers compensation. Set forth below is a sensitivity analysis that estimates the effect on the loss reserve position of using alternative loss trend or loss development factor assumptions rather than those actually used in determining AIG's best estimates in the year-end loss reserve analyses in 2007. The analysis addresses each major class of business for which a material deviation to AIG's overall reserve position is believed reasonably possible, and uses what AIG believes is a reasonably likely range of potential deviation for each class. There can be no assurance, however, that actual reserve development will be consistent with either the original or the adjusted loss trend or loss development factor assumptions, or that other assumptions made in the reserving process will not materially affect reserve development for a particular class of business.

Excess Casualty: For the excess casualty class of business, the assumed loss cost trend was approximately five percent. After evaluating the historical loss cost trends from prior accident years since the early 1990s, in AIG's judgment, it is reasonably likely that actual loss cost trends applicable to the year-end 2007 loss reserve review for excess casualty will range from negative five percent to positive 15 percent, or approximately ten percent lower or higher than the assumption actually utilized in the year-end 2007 reserve review. A ten percent change in the assumed loss cost trend for excess casualty would cause approximately a $2.4 billion increase or a $1.6 billion decrease in the net loss and loss expense reserve for this class of business. It should be emphasized that the ten percent deviations are not considered the highest possible deviations that might be expected, but rather what is considered by AIG to reflect a reasonably likely range of potential deviation. Actual loss cost trends in the early 1990s were negative for several years, including amounts below the negative five percent cited above, whereas actual loss cost trends in the late 1990s ran well into the double digits for several years, including amounts greater than the 15 percent cited above. Thus, there can be no assurance that loss trends will not deviate by more than ten percent. The loss cost trend assumption is critical for the excess casualty class of business due the long-tail nature of the claims and therefore is applied across many accident years.

For the excess casualty class of business, the assumed loss development factors are also a key assumption. After evaluating the historical loss development factors from prior accident years since the early 1990s, in AIG's judgment, it is reasonably likely that actual loss development factors will range from approximately 3.5 percent below those actually utilized in the year-end 2007 reserve review to approximately 6.5 percent above those factors actually utilized. If the loss development factor assumptions were changed by 3.5 percent and 6.5 percent, respectively, the net loss reserves for the excess casualty class would decrease by approximately $600 million under the lower assumptions or increase by approximately $1.0 billion under the higher assumptions. Generally, actual historical loss development factors are used to project future loss development. However there can be no assurance that future loss development patterns will be the same as in the past, or that they will not deviate by more than the amounts illustrated above. Moreover, as excess casualty is a long-tail class of business, any deviation in loss cost trends or in loss development factors might not be discernible for an extended

period of time subsequent to the recording of the initial loss reserve estimates for any accident year. Thus, there is the potential for the reserves with respect to a number of accident years to be significantly affected by changes in the loss cost trends or loss development factors that were initially relied upon in setting the reserves. These changes in loss trends or loss development factors could be attributable to changes in inflation or in the judicial environment, or in other social or economic conditions affecting claims. Thus, there is the potential for variations greater than the amounts cited above, either positively or negatively.

D&O and Related Management Liability Classes of Business: For D&O and related management liability classes of business, the assumed loss cost trend was approximately four percent. After evaluating the historical loss cost trends from prior accident years since the early 1990s, in AIG's judgment, it is reasonably likely that actual loss cost trends applicable to the year-end 2007 loss reserve review for these classes will range from negative 11 percent to positive 19 percent, or approximately 15 percent lower or higher than the assumption actually utilized in the year-end 2007 reserve review. A 15 percent change in the assumed loss cost trend for these classes would cause approximately a $550 million increase or a $500 million decrease in the net loss and loss expense reserves for these classes of business. It should be emphasized that the 15 percent deviations are not considered the highest possible deviations that might be expected, but rather what is considered by AIG to reflect a reasonably likely range of potential deviation. Actual loss cost trends for these classes in the early 1990s were negative for several years, including amounts below the negative 11 percent cited above, whereas actual loss cost trends in the late 1990s ran at nearly 50 percent per year for several years, vastly exceeding the 19 percent figure cited above. Because the D&O class of business has exhibited highly volatile loss trends from one accident year to the next, there is the possibility of an exceptionally high deviation.

For D&O and related management liability classes of business, the assumed loss development factors are also an important assumption but less critical than for excess casualty. Because these classes are written on a claims made basis, the loss reporting and development tail is much shorter than for excess casualty. However, the high severity nature of the claims does create the potential for significant deviations in loss development patterns from one year to the next. After evaluating the historical loss development factors for these classes of business for accident years since the early 1990s, in AIG's judgment, it is reasonably likely that actual loss development factors will range approximately 6 percent lower to 3.5 percent higher than those factors actually utilized in the year-end 2007 loss reserve review for these classes. If the loss development factor assumptions were changed by 6 percent and 3.5 percent, respectively, the net loss reserves for these classes would be estimated to decrease or increase by approximately $250 million and $125 million, respectively. As noted above for excess casualty, actual historical loss development factors are generally used to project future loss development. However, there can be no assurance that future loss development patterns will be the same as in the past, or that they will not deviate by more than the 6 percent or 3.5 percent amounts.

Excess Workers Compensation: For excess workers compensation business, loss costs were trended at six percent per annum. After reviewing actual industry loss trends for the past ten years, in AIG's judgment, it is reasonably likely that actual loss cost trends applicable to the year-end 2007 loss reserve review for excess workers compensation will range five percent lower or higher than this estimated loss trend. A five percent change in the assumed loss cost trend would cause approximately a $425 million increase or a $275 million decrease in the net loss reserves for this business. It should be emphasized that the actual loss cost trend could vary significantly from this assumption, and there can be no assurance that actual loss costs will not deviate, perhaps materially, by greater than five percent.

For excess workers compensation business, the assumed loss development factors are a critical assumption. Excess workers compensation is an extremely long-tail class of business, with a much greater than normal uncertainty as to the appropriate loss development factors for the tail of the loss development. After evaluating the historical loss development factors for prior accident years since the 1980s, in AIG's judgment, it is reasonably likely that actual loss development factors will range approximately 15 percent lower or higher than those factors actually utilized in the year-end 2007 loss reserve review for excess workers compensation. If the loss development factor assumptions were changed by 15 percent, the net loss reserves for excess workers compensation would increase or decrease by approximately $600 million. Given the exceptionally long-tail for this class of business, there is the potential for actual deviations in the loss development tail to exceed the deviations assumed, perhaps materially.

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

However, for primary workers compensation business the loss development factor assumptions are important. Generally, AIG's actual historical workers compensation loss development factors would be expected to provide a reasonably accurate predictor of future loss development. However, workers compensation is a long-tail class of business, and AIG's business reflects a very significant volume of losses particularly in recent accident years due to growth of the business. After evaluating the actual historical loss developments since the 1980s for this business, in AIG's judgment, it is reasonably likely that actual loss development factors will fall within the range of approximately 3.5 percent below to 8.25 percent above those actually utilized in the year-end 2007 loss reserve review. If the loss development factor assumptions were changed by 3.5 percent and 8.25 percent, respectively, the net loss reserves for workers compensation

would decrease or increase by approximately $800 million and $1.9 billion, respectively. It should be noted that loss emergence in 2006 and 2007 for this class was higher than historical averages, resulting in an increase in loss reserves for prior accident years. During 2007, reserves from prior accident years developed adversely by approximately $300 million for AIG's primary workers compensation business. AIG relies on longer term averages of historical loss development patterns in setting loss reserves; thus if loss emergence in subsequent years continues at the levels observed in 2006 and 2007 there could be additional adverse development for this class of business that could be more significant than the amount observed in 2007. However, AIG believes it is too soon to ascertain if this increased emergence represents a new trend in the pattern of loss development. For this class of business, there can be no assurance that actual deviations from the expected loss development factors will not exceed the deviations assumed, perhaps materially.

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

Asbestos and Environmental Reserves

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

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

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

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

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

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

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

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

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

With respect to asbestos claims handling, AIG's specialized claims staff operates to mitigate losses through proactive handling, supervision and resolution of asbestos cases. Thus, while AIG has resolved all claims with respect to miners and major manufacturers (Tier One), its claims staff continues to operate under the same proactive philosophy to resolve claims involving accounts with products containing asbestos (Tier Two), products

containing small amounts of asbestos, companies in the distribution process, and parties with remote, ill-defined involvement in asbestos (Tiers Three and Four). Through its commitment to appropriate staffing, training, and management oversight of asbestos cases, AIG seeks to mitigate its exposure to these claims.

To determine the appropriate loss reserve as of December 31, 2007 for its asbestos and environmental exposures, AIG performed a series of top-down and ground-up reserve analyses. In order to ensure it had the most comprehensive analysis possible, AIG engaged a third-party actuary to assist in a review of these exposures, including ground-up estimates for asbestos reserves consistent with the 2005 and 2006 reviews as well as a top-down report year projection for environmental reserves. Prior to 2005, AIG's reserve analyses for asbestos and environmental exposures was focused around a report year projection of aggregate losses for both asbestos and environmental reserves. Additional tests such as market share analyses were also performed. Ground-up analyses take into account policyholder-specific and claim-specific information that has been gathered over many years from a variety of sources. Ground-up studies can thus more accurately assess the exposure to AIG's layers of coverage for each policyholder, and hence for all policyholders in the aggregate, provided a sufficient sample of the policyholders can be modeled in this manner.

In order to ensure its ground-up analysis was comprehensive, AIG staff produced the information required at policy and claim level detail for nearly 1,000 asbestos defendants. This represented over 95 percent of all accounts for which AIG had received any claim notice of any amount pertaining to asbestos exposure. AIG did not set any minimum thresholds, such as amount of case reserve outstanding, or paid losses to date, that would have served to reduce the sample size and hence the comprehensiveness of the ground-up analysis. The results of the ground-up analysis for each significant account were examined by AIG's claims staff for reasonableness, for consistency with policy coverage terms, and any claim settlement terms applicable. Adjustments were incorporated accordingly. The results from the universe of modeled accounts, which as noted above reflects the vast majority of AIG's known exposures, were then utilized to estimate the ultimate losses from accounts or exposures that could not be modeled and to determine an appropriate provision for unreported claims.

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

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

For asbestos, these tests project the losses expected to be reported over the next nineteen years, i.e., from 2008 through 2026, based on the actual losses reported through 2007 and the expected future loss emergence for these claims. Three scenarios were tested, with a series of assumptions ranging from more optimistic to more conservative. In the first scenario, all carried asbestos case reserves are assumed to be within ten percent of their ultimate settlement value. The second scenario relies on an actuarial projection of report year development for asbestos claims reported from 1993 to the present to estimate case reserve adequacy as of year-end 2007. The third scenario relies on an actuarial projection of report year claims for asbestos but reflects claims reported from 1989 to the present to estimate case reserve adequacy as of year-end 2007. Based on the results of the prior report years for each of the three scenarios described above, the report year approach then projects forward to the year 2026 the expected future report year losses, based on AIG's estimate of reasonable loss trend assumptions. These calculations are performed on losses gross of reinsurance. The IBNR (including a provision for development of reported claims) on a net basis is based on applying a factor reflecting the expected ratio of net losses to gross losses for future loss emergence.

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

At year-end 2007, AIG considered a number of factors and recent experience in addition to the results of the respective top-down and ground-up analyses performed for asbestos and environmental reserves. AIG considered the significant uncertainty that remains as to AIG's ultimate liability relating to asbestos and environmental claims. This uncertainty is due to several factors including:

- The long latency period between asbestos exposure and disease manifestation and the resulting potential for involvement of multiple policy periods for individual claims;
- The increase in the volume of claims by currently unimpaired plaintiffs;
- Claims filed under the non-aggregate premises or operations section of general liability policies;
- The number of insureds seeking bankruptcy protection and the effect of prepackaged bankruptcies;
- Diverging legal interpretations; and
- With respect to environmental claims, the difficulty in estimating the allocation of remediation cost among various parties.

After carefully considering the results of the ground-up analysis, which AIG updates on an annual basis, as well as all of the above factors, including the recent report year experience, AIG increased its gross asbestos reserves by $75 million, all of which was reinsured, resulting in no increase to net reserves. Additionally, during 2007 a reduction in estimated reinsurance recoverable, partially offset by several large favorable asbestos settlements, resulted in a minor amount of adverse incurred loss development.

Based on the environmental top-down report year analysis performed in the fourth quarter of 2007, a minor increase in both gross and net reserves was recognized, resulting in the relatively minor amount of development shown in the table below.

A summary of reserve activity, including estimates for applicable IBNR, relating to asbestos and environmental claims separately and combined at December 31, 2007, 2006 and 2005 appears in the table below. The vast majority of such claims arise from policies written in 1984 and prior years. The current environmental policies that AIG underwrites on a claims-made basis have been excluded from the table below.

	2007		2006		2005	
(in millions)	Gross	Net	Gross[e]	Net	Gross[e]	Net
Asbestos:						
Reserve for losses and loss expenses at beginning of year	**$ 4,523**	**$1,889**	$4,501	$1,840	$2,622	$1,060
Losses and loss expenses incurred[a]	**96**	**5**	572	267	2,206[b]	903[b]
Losses and loss expenses paid[a]	**(755)**	**(440)**	(550)	(218)	(327)	(123)
Reserve for losses and loss expenses at end of year	**$ 3,864**	**$1,454**	$4,523	$1,889	$4,501	$1,840
Environmental:						
Reserve for losses and loss expenses at beginning of year	**$ 629**	**$ 290**	$ 969	$ 410	$1,018	$ 451
Losses and loss expenses incurred[a]	**10**	**13**	(231)	(59)	47[c]	27[c]
Losses and loss expenses paid[a]	**(124)**	**(66)**	(109)	(61)	(96)	(68)
Reserve for losses and loss expenses at end of year	**$ 515**	**$ 237**	$ 629	$ 290	$ 969	$ 410
Combined:						
Reserve for losses and loss expenses at beginning of year	**$ 5,152**	**$2,179**	$5,470	$2,250	$3,640	$1,511
Losses and loss expenses incurred[a]	**106**	**18**	341	208	2,253[d]	930[d]
Losses and loss expenses paid[a]	**(879)**	**(506)**	(659)	(279)	(423)	(191)
Reserve for losses and loss expenses at end of year	**$ 4,379**	**$1,691**	$5,152	$2,179	$5,470	$2,250

(a) All amounts pertain to policies underwritten in prior years, primarily to policies issued in 1984 and prior.

(b) Includes increases to gross losses and loss expense reserves of $2.0 billion and increases to net losses and loss expense reserves of $843 million for the fourth quarter of 2005.

(c) Includes increases to gross losses and loss expense reserves of $56 million and increases to net losses and loss expense reserves of $30 million for the fourth quarter of 2005.

(d) Includes increases to gross losses and loss expense reserves of $2.0 billion and increases to net losses and loss expense reserves of $873 million for the fourth quarter of 2005.

(e) Gross amounts were revised from the previous presentation to reflect the inclusion of certain reserves not previously identified as asbestos and environmental related. This revision had no effect on net reserves.

The gross and net IBNR included in the reserve for losses and loss expenses, relating to asbestos and environmental claims separately and combined, at December 31, 2007, 2006 and 2005 were estimated as follows:

	2007		2006		2005	
(in millions)	Gross	Net	Gross*	Net	Gross*	Net
Asbestos	**$2,701**	**$1,145**	$3,270	$1,469	$3,458	$1,465
Environmental	**325**	**131**	378	173	625	266
Combined	**$3,026**	**$1,276**	$3,648	$1,642	$4,083	$1,731

** Gross amounts were revised from the previous presentation to reflect the inclusion of certain reserves not previously identified as asbestos and environmental related. This revision had no effect on net reserves.*

A summary of asbestos and environmental claims count activity for the years ended December 31, 2007, 2006 and 2005 was as follows:

	2007			2006			2005		
	Asbestos	Environmental	Combined	Asbestos	Environmental	Combined	Asbestos	Environmental	Combined
Claims at beginning of year	**6,878**	**9,442**	**16,320**	7,293	9,873	17,166	7,575	8,216	15,791
Claims during year:									
Opened	**656**	**937**	**1,593**	643	1,383	2,026	854	5,253	6,107
Settled	**(150)**	**(179)**	**(329)**	(150)	(155)	(305)	(67)	(219)	(286)
Dismissed or otherwise resolved	**(821)**	**(2,548)**	**(3,369)**	(908)	(1,659)	(2,567)	(1,069)	(3,377)	(4,446)
Claims at end of year	**6,563**	**7,652**	**14,215**	6,878	9,442	16,320	7,293	9,873	17,166

Survival Ratios — Asbestos and Environmental

The table below presents AIG's survival ratios for asbestos and environmental claims at December 31, 2007, 2006 and 2005. The survival ratio is derived by dividing the current carried loss reserve by the average payments for the three most recent calendar years for these claims. Therefore, the survival ratio is a simplistic measure estimating the number of years it would be before the current ending loss reserves for these claims would be paid off using recent year average payments. The December 31, 2007 survival ratio is lower than the ratio at December 31, 2006 because the more recent periods included in the rolling average reflect higher claims payments. In addition, AIG's survival ratio for asbestos claims was negatively affected by the favorable settlements described above, which reduced gross and net asbestos survival ratios at December 31, 2007 by approximately 1.3 years and 2.6 years, respectively. Many factors, such as aggressive settlement procedures, mix of business and level of coverage provided, have a significant effect on the amount of asbestos and environmental reserves and payments and the resultant survival ratio. Moreover, as discussed above, the primary basis for AIG's determination of its reserves is not survival ratios, but instead the ground-up and top-down analysis. Thus, caution should be exercised in attempting to determine reserve adequacy for these claims based simply on this survival ratio.

AIG's survival ratios for asbestos and environmental claims, separately and combined were based upon a three-year average payment. These ratios for the years ended December 31, 2007, 2006 and 2005 were as follows:

	Gross*	Net
2007		
Survival ratios:		
Asbestos	**7.1**	**5.6**
Environmental	**4.7**	**3.7**
Combined	**6.7**	**5.2**
2006		
Survival ratios:		
Asbestos	11.8	12.9
Environmental	5.6	4.5
Combined	10.4	10.3
2005		
Survival ratios:		
Asbestos	16.0	19.8
Environmental	7.2	6.2
Combined	13.1	14.2

* *Gross amounts for 2006 and 2005 were revised from the previous presentation to reflect the inclusion of certain reserves not previously identified as asbestos and environmental related. This revision had no effect on net reserves.*

Life Insurance & Retirement Services Operations

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

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

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

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

In order to better align financial reporting with the manner in which AIG's chief operating decision makers manage their businesses, commencing in 2007, revenues and operating income related to foreign investment-type contracts, which were historically reported as a component of the Asset Management segment, are now reported as part of Foreign Life Insurance & Retirement Services. Prior period amounts have been revised to conform to the current presentation.

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

Foreign Life Insurance & Retirement Services

Japan and Other

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

Asia

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

Domestic Life Insurance

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

- American General Life and Accident Insurance Company (AGLA)

Domestic Retirement Services

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

Life Insurance & Retirement Services Results

Life Insurance & Retirement Services results for 2007, 2006 and 2005 were as follows:

(in millions)	Premiums and Other Considerations	Net Investment Income	Net Realized Capital Gains (Losses)	Total Revenues	Operating Income
2007					
Foreign Life Insurance & Retirement Services	**$26,601**	**$11,849**	**$ (187)**	**$38,263**	**$ 6,197**
Domestic Life Insurance	**5,836**	**3,995**	**(803)**	**9,028**	**642**
Domestic Retirement Services	**1,190**	**6,497**	**(1,408)**	**6,279**	**1,347**
Total	**$33,627**	**$22,341**	**$(2,398)**	**$53,570**	**$ 8,186**
2006					
Foreign Life Insurance & Retirement Services*	$24,166	$ 9,758	$ 707	$34,631	$ 6,881
Domestic Life Insurance	5,543	3,778	(215)	9,106	917
Domestic Retirement Services	1,057	6,488	(404)	7,141	2,323
Total	$30,766	$20,024	$ 88	$50,878	$10,121
2005					
Foreign Life Insurance & Retirement Services	$23,117	$ 8,718	$ 84	$31,919	$ 5,306
Domestic Life Insurance	5,447	3,733	35	9,215	1,495
Domestic Retirement Services	937	6,226	(277)	6,886	2,164
Total	$29,501	$18,677	$ (158)	$48,020	$ 8,965
Percentage Increase/(Decrease) 2007 vs. 2006:					
Foreign Life Insurance & Retirement Services	10%	21%	—%	10%	(10)%
Domestic Life Insurance	5	6	—	(1)	(30)
Domestic Retirement Services	13	—	—	(12)	(42)
Total	9%	12%	—%	5%	(19)%
Percentage Increase/(Decrease) 2006 vs. 2005:					
Foreign Life Insurance & Retirement Services	5%	12%	—%	8%	30%
Domestic Life Insurance	2	1	—	(1)	(39)
Domestic Retirement Services	13	4	—	4	7
Total	4%	7%	—%	6%	13%

** Included an out of period UCITS adjustment which increased net investment income by $240 million and operating income by $169 million.*

The following table presents the gross insurance in force for Life Insurance & Retirement Services at December 31, 2007, 2006 and 2005:

(in millions)	**2007**	2006	2005
Foreign*	**$1,327,251**	$1,162,699	$1,027,682
Domestic	**984,794**	907,901	825,151
Total	**$2,312,045**	$2,070,600	$1,852,833

** Includes increases (decreases) of $55.1 billion, $41.5 billion and $(76.5) billion related to changes in foreign exchange rates at December 31, 2007, 2006 and 2005, respectively.*

2007 and 2006 Comparison

The severe credit market disruption was a key driver of operating results in 2007 principally due to significant net realized capital losses resulting from other-than-temporary impairment charges of $2.8 billion and losses on derivative instruments not qualifying for hedge accounting treatment of $381 million compared to an other-than-temporary impairment charge of $641 million and gains on derivative instruments of $268 million in 2006. In addition, net investment income and certain products were negatively affected by the volatile markets. Life Insurance & Retirement Services continued its ongoing project to increase standardization of AIG's actuarial systems and processes throughout the world. Significant progress was made on these initiatives, with only a minimal effect on operating income in this segment. Premiums and other considerations increased in 2007 compared to 2006 despite a very competitive marketplace and a relatively flat yield curve for most of the year.

Life Insurance & Retirement Services total revenues in 2007 reflect growth in premiums and other considerations compared to 2006 due principally to strong life insurance production in the Foreign Life Insurance & Retirement Services operations, a growing block of U.K. single premium investment-oriented products and higher policyholder charges related to universal life and sales of payout annuities in the Domestic Life Insurance operations. Overall growth in premiums and other considerations was dampened by a continuing shift to interest sensitive products and the suspension of new sales on certain products in Japan resulting from an industry wide review by the tax authorities. Net investment income increased in 2007 compared to 2006 due to higher partnership and mutual fund income as well as higher policyholder investment income and trading gains and losses (together, policyholder trading gains). Policyholder trading gains are offset by a charge to incurred policy losses and benefits expense. Policyholder trading gains increased due to higher levels of assets and generally reflect the trend in equity markets. Policyholder trading gains were $2.9 billion in 2007 compared to $2.0 billion in 2006. Net investment income in 2006 included an increase of $240 million for an out of period adjustment related to the accounting for UCITS.

Operating income in 2007 was significantly adversely affected by net realized capital losses which totaled $2.4 billion, net of an out-of-period adjustment of $158 million related to foreign exchange remediation activities, compared to net realized capital gains of $88 million in 2006. Other factors affecting operating income include trading account losses of $150 million in the U.K. associated with certain investment-linked products, the adverse effect of $108 million related to SOP 05-1, which was adopted in 2007, additional claim expense of $67 million relating to an industry wide regulatory review of claims in Japan (compared to additional claim expense of $26 million in 2006) and a $118 million charge related to remediation activities in Asia. Incurred policyholder benefits increased $36 million in 2007 related to a closed block of Japanese business with guaranteed benefits. Partially offsetting these factors was a $52 million recovery in 2007 related to the Superior National arbitration. SOP 05-1 generally requires DAC related to group contracts to be amortized over a shorter duration than in prior periods and also requires that DAC be expensed at the time an individual policy is terminated or lapses, even if reinstated shortly thereafter. The effect of SOP 05-1 was most significant to the group products line in the Domestic Life Insurance operations.

Changes in actuarial estimates, including DAC unlockings and refinements to estimates resulting from actuarial valuation system enhancements and conversions, resulted in a net increase to operating income of $19 million during 2007. However, this net increase resulted from a number of items that had varying effects on the results of operations of certain operating units and lines of business. These adjustments resulted in an increase of $183 million in operating income for Foreign Life Insurance & Retirement Services and decreases in operating income of $52 million and $112 million for Domestic Life Insurance and Domestic Retirement Services, respectively. In addition, the related adjustments significantly affected both acquisition costs and incurred policy losses and benefits in the Consolidated Statement of Income.

Operating income in 2006 included an increase of $169 million for an out of period adjustment related to the accounting for UCITS and an increase of $163 million for an out-of-period adjustment related to corrections of par policyholder dividend reserves and allocations between participating and non-participating accounts, both of which were related to remediation efforts. In addition, operating income in 2006 included charges to Domestic Life Insurance operations of $125 million for the adverse Superior National arbitration ruling, $66 million related to the exit of the domestic financial institutions credit life business and $55 million related to other litigation.

2006 and 2005 Comparison

Life Insurance & Retirement Services revenues in 2006 increased compared to 2005. Growth in premiums and other considerations was dampened by the effect of foreign exchange, most notably by the weakening Japanese Yen. Net investment income was higher in 2006 compared to 2005 due to higher partnership and mutual fund income, which in 2006 included a positive out-of-period adjustment of $240 million related to the accounting for UCITS. Operating income grew by $1.2 billion from 2005, reflecting higher revenues, including net realized capital gains, and out-of-period reductions of policy benefits expense of $163 million in 2006 resulting from corrections of par policyholder dividend reserves and allocations between participating and non-participating accounts, both of which were related to remediation efforts. In addition, operating income in 2006 included charges for Domestic Life Insurance of $125 million for the adverse Superior National arbitration ruling, $66 million related to the exit of the domestic financial institutions credit life business and $55 million related to other litigation.

Foreign Life Insurance & Retirement Services Results

Foreign Life Insurance & Retirement Services results on a sub-product basis for 2007, 2006 and 2005 were as follows:

(in millions)	Premiums and Other Considerations	Net Investment Income	Net Realized Capital Gains (Losses)	Total Revenues	Operating Income
2007					
Life insurance	**$16,630**	**$ 7,473**	**$ 85**	**$24,188**	**$3,898**
Personal accident	**6,094**	**354**	**(3)**	**6,445**	**1,457**
Group products	**2,979**	**753**	**(76)**	**3,656**	**263**
Individual fixed annuities	**438**	**2,283**	**(171)**	**2,550**	**548**
Individual variable annuities	**460**	**986**	**(22)**	**1,424**	**31**
Total	**$26,601**	**$11,849**	**$(187)**	**$38,263**	**$6,197**
2006					
Life insurance[(a)]	$15,732	$ 5,937	$574	$22,243	$4,247
Personal accident	5,518	285	55	5,858	1,459
Group products	2,226	648	47	2,921	450
Individual fixed annuities	400	2,027	31	2,458	580
Individual variable annuities	290	861	—	1,151	145
Total	$24,166	$ 9,758	$707	$34,631	$6,881
2005					
Life insurance	$15,643	$ 4,884	$ 94	$20,621	$3,195
Personal accident	5,002	255	(30)	5,227	1,292
Group products	1,925	613	(9)	2,529	322
Individual fixed annuities	361	1,728	29	2,118	398
Individual variable annuities	186	1,238	—	1,424	99
Total	$23,117	$ 8,718	$ 84	$31,919	$5,306
Percentage Increase/(Decrease) 2007 vs. 2006:					
Life insurance	6%	26%	(85)%	9%	(8)%
Personal accident	10	24	—	10	—
Group products	34	16	—	25	(42)
Individual fixed annuities	10	13	—	4	(6)
Individual variable annuities	59	15	—	24	(79)
Total	10%	21%	—%	10%	(10)%
Percentage Increase/(Decrease) 2006 vs. 2005:					
Life insurance	1%	22%	—%	8%	33%
Personal accident	10	12	—	12	13
Group products	16	6	—	16	40
Individual fixed annuities	11	17	7	16	46
Individual variable annuities	56	(30)	—	(19)	46
Total	5%	12%	—%	8%	30%

(a) Includes the effect of an out of period UCITS adjustment in 2006, which increased net investment income by $237 million and operating income by $166 million.

AIG transacts business in most major foreign currencies and therefore premiums and other considerations reported in U.S. dollars vary by volume and from changes in foreign currency translation rates. The following table summarizes the effect of changes in foreign currency exchange rates on the growth of the Foreign Life Insurance & Retirement Services premiums and other considerations for the years ended December 31, 2007 and 2006:

	2007	2006
Growth in original currency*	**7.6%**	6.5%
Foreign exchange effect	**2.5**	(2.0)
Growth as reported in U.S. dollars	**10.1%**	4.5%

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

Management's Discussion and Analysis of Financial Condition and Results of Operations *Continued*

Japan and Other Results

Japan and Other results on a sub-product basis for 2007, 2006 and 2005 were as follows:

(in millions)	Premiums and Other Considerations	Net Investment Income	Net Realized Capital Gains (Losses)	Total Revenues	Operating Income
2007					
Life insurance	**$ 4,999**	**$2,113**	**$ (92)**	**$ 7,020**	**$1,193**
Personal accident	**4,225**	**204**	**(1)**	**4,428**	**1,071**
Group products	**2,318**	**626**	**1**	**2,945**	**250**
Individual fixed annuities	**386**	**2,160**	**(181)**	**2,365**	**500**
Individual variable annuities	**459**	**980**	**(21)**	**1,418**	**30**
Total	**$12,387**	**$6,083**	**$(294)**	**$18,176**	**$3,044**
2006					
Life insurance [(a)]	$ 4,783	$1,749	$ 316	$ 6,848	$1,731
Personal accident	3,957	162	49	4,168	1,122
Group products	1,740	541	13	2,294	272
Individual fixed annuities	337	1,930	28	2,295	553
Individual variable annuities	289	857	—	1,146	143
Total	$11,106	$5,239	$ 406	$16,751	$3,821
2005					
Life insurance	$ 4,864	$1,828	$ (52)	$ 6,640	$1,288
Personal accident	3,788	137	(15)	3,910	1,051
Group products	1,473	535	(34)	1,974	191
Individual fixed annuities	292	1,672	29	1,993	390
Individual variable annuities	186	1,234	—	1,420	100
Total	$10,603	$5,406	$ (72)	$15,937	$3,020
Percentage Increase/(Decrease) 2007 vs. 2006:					
Life insurance	5%	21%	—%	3%	(31)%
Personal accident	7	26	—	6	(5)
Group products	33	16	(92)	28	(8)
Individual fixed annuities	15	12	—	3	(10)
Individual variable annuities	59	14	—	24	(79)
Total	12%	16%	—%	9%	(20)%
Percentage Increase/(Decrease) 2006 vs. 2005:					
Life insurance	(2)%	(4)%	—%	3%	34%
Personal accident	4	18	—	7	7
Group products	18	1	—	16	42
Individual fixed annuities	15	15	(3)	15	42
Individual variable annuities	55	(31)	—	(19)	43
Total	5%	(3)%	—%	5%	27%

(a) Includes the effect of an out of period UCITS adjustment in 2006, which increased both net investment income and operating income by $29 million.

2007 and 2006 Comparison

Total revenues for Japan and Other in 2007 increased compared to 2006, primarily due to higher premiums and other considerations and net investment income partially offset by net realized capital losses. Net investment income increased in 2007 compared to 2006 due to higher levels of assets under management and higher policyholder trading gains partially offset by lower partnership and mutual fund income. Operating income decreased in 2007 compared to 2006 due principally to net realized capital losses, a $187 million charge related to changes in actuarial estimates, trading account losses of $150 million in the U.K. associated with certain investment-linked products, $67 million of additional claim expense related to the industry wide regulatory review of claims in Japan and increased incurred policyholder benefits of $36 million related to a closed block of Japanese business with guaranteed benefits. These decreases were partially offset by the positive effect of foreign exchange rates.

Life insurance premiums and other considerations increased moderately in 2007 compared to 2006. In Japan, single premium sales of U.S. dollar denominated interest sensitive whole life

products remained strong. First year premium sales declined, however, due to the suspension in April 2007 of increasing term products pending completion of an industry wide review by the National Tax Authority. Although the review was completed with the issue of a draft paper for comment in December 2007, the product remains suspended pending finalization of the report. In Europe, growth in premiums and other considerations was driven by the growing block of U.K. single premium investment-oriented products and the positive effect of foreign exchange rates. The growth in net investment income was due to growth in underlying invested assets and higher partnership income. Life insurance operating income declined in 2007 compared to 2006 due to net realized capital losses, compared to net realized capital gains in 2006. In addition, 2007 operating income was negatively affected by a $115 million charge related to changes in actuarial estimates, higher incurred policyholder benefits of $36 million related to a closed block of Japanese business with guaranteed benefits and $23 million of additional claim expense related to the claims review in Japan. Operating income in 2006 included the effect of an out of period UCITS adjustment, which increased both net investment income and operating income by $29 million.

Personal accident premiums and other considerations grew modestly as strong growth in Europe was offset by lower growth in Japan, particularly from the direct marketing distribution channel. Net investment income increased in 2007 compared to 2006 primarily due to growth in invested assets. Operating income declined in 2007 compared to 2006 due to a net realized capital loss, a $42 million charge related to changes in actuarial estimates, $42 million of additional claim expense related to the claims review in Japan and $20 million of additional expenses related to SOP 05-1.

Group products premiums and other considerations in 2007 increased significantly compared to 2006 primarily due to the growing credit business in Europe. Net investment income increased in 2007 compared to 2006, primarily due to higher assets under management related to the Brazil pension business. Operating income in 2007 declined compared to 2006 primarily due to $19 million of additional expenses related to SOP 05-1 and lower net realized capital gains.

Individual fixed annuity deposits improved in 2007 primarily due to sales in the U.K. and were partially offset by declining sales in Japan due to the effect of a weak Japanese Yen for most of the year as well as the market shift to variable annuity products. Assets under management, however, continued to grow. Individual fixed annuities premiums and other considerations growth reflects a shift to front-end load products and higher surrender charges from U.S. dollar products in Japan where a weak Japanese Yen makes it attractive for certain policyholders to lock-in foreign exchange gains in excess of surrender charges. Surrender charges were $151 million and $98 million in 2007 and 2006, respectively. Net investment income increased due to higher average investment yields and higher levels of assets under management. Operating income declined in 2007 compared to 2006 due to realized capital losses in 2007 versus realized capital gains in 2006.

Individual variable annuity deposits in 2007 declined compared to 2006 due to the effect of tax law changes in Europe that reduced tax benefits to policyholders, and lower sales in Japan due to increased competition and the introduction of a new law that increased sales compliance and customer suitability requirements. Variable annuity sales in Japan began to improve in the fourth quarter of 2007 as a new product, launched mid-year in 2007, gained acceptance and banks became more comfortable with the new law. The fees generated from the higher levels of assets under management increased premiums and other considerations in 2007 compared to 2006. Net investment income increased due to higher policyholder trading gains in 2007 compared to 2006. Operating income declined in 2007 compared to 2006 primarily due to $150 million of trading account losses on certain investment-linked products in the U.K. and net realized capital losses.

2006 and 2005 Comparison

Total revenues for Japan and Other increased in 2006 compared to 2005. Premiums and other considerations growth rates were dampened by the effect of foreign exchange, most notably by the weakening of the Japanese Yen. Net investment income in 2006 declined compared to 2005 due to lower policyholder trading gains in the individual variable annuity line. Total revenues in 2006 increased compared to 2005 due to realized capital gains relating primarily to derivative instruments for transactions that did not qualify for hedge accounting treatment under FAS 133. Operating income in 2006 increased compared to 2005 due to growth in the underlying retirement services businesses and realized capital gains of $406 million. Operating income in 2006 included the effect of an out of period UCITS adjustment which increased net investment income and operating income by $32 million. Operating income in 2006 was negatively affected by the weakening of the Japanese Yen against the U.S. dollar and the continued runoff of the older, higher margin in-force businesses of AIG Star Life and AIG Edison Life.

Management's Discussion and Analysis of Financial Condition and Results of Operations *Continued*

Asia Results

Asia results on a sub-product basis for 2007, 2006 and 2005 were as follows:

(in millions)	Premiums and Other Considerations	Net Investment Income	Net Realized Capital Gains (Losses)	Total Revenues	Operating Income (Loss)
2007					
Life insurance	**$11,631**	**$5,360**	**$177**	**$17,168**	**$2,705**
Personal accident	**1,869**	**150**	**(2)**	**2,017**	**386**
Group products	**661**	**127**	**(77)**	**711**	**13**
Individual fixed annuities	**52**	**123**	**10**	**185**	**48**
Individual variable annuities	**1**	**6**	**(1)**	**6**	**1**
Total	**$14,214**	**$5,766**	**$107**	**$20,087**	**$3,153**
2006					
Life insurance[(a)]	$10,949	$4,188	$258	$15,395	$2,516
Personal accident	1,561	123	6	1,690	337
Group products	486	107	34	627	178
Individual fixed annuities	63	97	3	163	27
Individual variable annuities	1	4	—	5	2
Total	$13,060	$4,519	$301	$17,880	$3,060
2005					
Life insurance	$10,779	$3,056	$146	$13,981	$1,907
Personal accident	1,214	118	(15)	1,317	241
Group products	452	78	25	555	131
Individual fixed annuities	69	56	—	125	8
Individual variable annuities	—	4	—	4	(1)
Total	$12,514	$3,312	$156	$15,982	$2,286
Percentage Increase/(Decrease) 2007 vs. 2006:					
Life insurance	6%	28%	(31)%	12%	8%
Personal accident	20	22	—	19	15
Group products	36	19	—	13	(93)
Individual fixed annuities	(17)	27	233	13	78
Individual variable annuities	—	50	—	20	(50)
Total	9%	28%	(64)%	12%	3%
Percentage Increase/(Decrease) 2006 vs. 2005:					
Life insurance	2%	37%	77%	10%	32%
Personal accident	29	4	—	28	40
Group products	8	37	36	13	36
Individual fixed annuities	(9)	73	—	30	238
Individual variable annuities	—	—	—	25	—
Total	4%	36%	93%	12%	34%

(a) Includes the effect of an out of period UCITS adjustment in 2006, which increased net investment income and operating income by $208 million and $137 million, respectively.

2007 and 2006 Comparison

Total revenues in Asia in 2007 increased compared to 2006 primarily due to higher premiums and other considerations and net investment income, partially offset by lower net realized capital gains. Premiums and other considerations increased in 2007 compared to 2006, notwithstanding a continued trend toward investment-oriented products where only a portion of policy charges are reported as premiums. Sales of investment-oriented life products have been particularly strong in Hong Kong, Korea and Singapore and more recently in Taiwan. Net investment income grew due to higher policyholder trading gains, higher partnership and unit investment trust income and growth in underlying invested assets. Net realized capital gains in 2007 were lower compared to 2006 due to an increase in other-than-temporary impairment charges and the change in fair value of derivatives that do not qualify for hedge accounting treatment under FAS 133, partially offset by a positive out-of-period adjustment of $158 million related to foreign exchange remediation activities. Operating income in 2007 increased compared to 2006. Operating income in 2007 included a $370 million positive effect of changes in actuarial estimates along with higher

partnership and UCITS income, partially offset by lower net realized capital gains and a $118 million charge related to remediation activity. Operating income in 2006 included an increase of $137 million from an out of period adjustment related to UCITS. In addition, operating income in 2006 included the positive effect of out of period reductions in participating policyholder dividend reserves of $163 million, primarily as a result of tax remediation adjustments and a correction to expense allocations between participating and non-participating accounts.

Life insurance premiums and other considerations in 2007 reflected a moderate increase compared to 2006, benefiting from improved sales in Thailand and the favorable effect of foreign exchange rates, partially offset by the shift in product mix from traditional life insurance products to investment-oriented products. Net investment income grew in 2007 compared to 2006 due primarily to higher policyholder trading gains, the growth in the underlying invested assets and higher partnership income. Operating income increased in 2007 compared to 2006 due to a $322 million positive effect of changes in actuarial estimates, partially offset by an $86 million charge related to remediation activity. Operating income in 2006 included the effect of the out of period UCITS adjustment and reduction in participating policyholder dividend reserves discussed above.

Personal accident revenues grew in 2007 compared to 2006 primarily due to higher premiums and other considerations, particularly in Korea and Taiwan. Operating income reflects the combined effect of premium growth and stable loss ratios and a $51 million positive effect related to changes in actuarial estimates in 2007.

Group products premiums and other considerations grew in 2007 compared to 2006 due to higher pension management fees and sales. However, operating income declined in 2007 compared to 2006, primarily due to net realized capital losses resulting from other-than-temporary impairment charges, a $29 million charge related to remediation activity and higher DAC amortization expense.

Individual fixed annuities total revenues grew in 2007 compared to 2006 due primarily to higher net investment income and increased net realized capital gains. Deposits in 2007 declined compared to 2006 due to increased competition and a market shift to variable life products, particularly in Korea.

2006 and 2005 Comparison

Revenues for Asia grew in 2006 compared to 2005. Premiums and other considerations in 2006 were negatively affected by the trend towards investment-oriented products as only a portion of the policy charges collected are reported as premiums. Net investment income in 2006 grew compared to 2005 due to higher policyholder trading gains. Net realized capital gains were significantly higher in 2006 compared to 2005 relating primarily to derivative instruments for transactions that do not qualify for hedge accounting treatment under FAS 133. Revenues and operating income in 2006 included increases of $208 million and $137 million, respectively, from out of period adjustments related to UCITS. In addition, operating income in 2006 increased due to a $163 million out of period adjustment related to participating policyholder dividend reserves primarily as a result of tax remediation adjustments and a correction to expense allocations between participating and non-participating accounts.

Domestic Life Insurance Results

Domestic Life Insurance results, presented on a sub-product basis for 2007, 2006 and 2005, were as follows:

(in millions)	Premiums and Other Considerations	Net Investment Income	Net Realized Capital Gains (Losses)	Total Revenues	Operating Income (Loss)
2007					
Life insurance	**$ 2,352**	**$ 1,528**	**$ (584)**	**$ 3,296**	**$ 226**
Home service	**767**	**640**	**(100)**	**1,307**	**216**
Group life/health	**842**	**200**	**(16)**	**1,026**	**67**
Payout annuities[(a)]	**1,820**	**1,153**	**(67)**	**2,906**	**74**
Individual fixed and runoff annuities	**55**	**474**	**(36)**	**493**	**59**
Total	**$ 5,836**	**$ 3,995**	**$ (803)**	**$ 9,028**	**$ 642**
2006					
Life insurance	$ 2,127	$ 1,377	$ (83)	$ 3,421	$ 654
Home service	790	630	(38)	1,382	282
Group life/health	995	213	(8)	1,200	(159)
Payout annuities[(a)]	1,582	1,004	(51)	2,535	76
Individual fixed and runoff annuities	49	554	(35)	568	64
Total	$ 5,543	$ 3,778	$ (215)	$ 9,106	$ 917

Management's Discussion and Analysis of Financial Condition and Results of Operations *Continued*

(in millions)	Premiums and Other Considerations	Net Investment Income	Net Realized Capital Gains (Losses)	Total Revenues	Operating Income (Loss)
2005					
Life insurance	$ 2,041	$ 1,352	$ 98	$ 3,491	$ 874
Home service	801	605	(2)	1,404	282
Group life/health	1,079	201	(1)	1,279	69
Payout annuities[(a)]	1,473	912	(34)	2,351	128
Individual fixed and runoff annuities	53	663	(26)	690	142
Total	$ 5,447	$ 3,733	$ 35	$ 9,215	$ 1,495
Percentage Increase/(Decrease) 2007 vs. 2006:					
Life insurance	11%	11%	—%	(4)%	(65)%
Home service	(3)	2	—	(5)	(23)
Group life/health	(15)	(6)	—	(15)	—
Payout annuities	15	15	—	15	(3)
Individual fixed and runoff annuities	12	(14)	—	(13)	(8)
Total	5%	6%	—%	(1)%	(30)%
Percentage Increase/(Decrease) 2006 vs. 2005:					
Life insurance	4%	2%	—%	(2)%	(25)%
Home service	(1)	4	—	(2)	—
Group life/health	(8)	6	—	(6)	—
Payout annuities	7	10	—	8	(41)
Individual fixed and runoff annuities	(8)	(16)	—	(18)	(55)
Total	2%	1%	—%	(1)%	(39)%

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

2007 and 2006 Comparison

Total Domestic Life Insurance revenues in 2007 decreased compared to 2006 primarily due to higher net realized capital losses, partially offset by higher premiums and other considerations and net investment income. Domestic Life Insurance premiums and other considerations increased in 2007 compared to 2006 primarily due to the growth in life insurance business in force and payout annuity premiums, which were partially offset by a decline in group life/health premiums due to exiting the financial institutions credit life business at the end of 2006. Domestic Life Insurance operating income decreased in 2007 compared to 2006, primarily due to higher net realized capital losses which consisted of losses related to sales of securities, other-than-temporary impairment writedowns of fixed income securities as well as derivative losses. The higher net realized capital losses in 2007 were partially offset by increases in premiums and other considerations and net investment income, and an improvement in group life/health results compared to 2006, which included a $125 million charge related to the Superior National workers compensation arbitration, a $66 million loss related to the exit from the financial institutions credit life business and a $55 million charge related to litigation reserves. Changes in actuarial estimates, including DAC unlockings and refinements in estimates resulting from actuarial valuation system enhancements, resulted in a net decrease in operating income of $52 million in 2007. Operating income in 2007 was also negatively affected by a $67 million increase in DAC amortization related to SOP 05-1, which was partially offset by a $52 million decrease in policy benefits due to additional reinsurance recoveries associated with Superior National.

Life insurance premiums and other considerations increased in 2007 compared to 2006 driven by growth in life insurance business in force and increased policyholder charges related to universal life and whole life products. Net investment income in 2007 compared to 2006 increased due to higher partnership income, higher call and tender income and positive changes from foreign denominated emerging market bonds. Life insurance operating income decreased in 2007 compared to 2006 primarily due to higher net realized capital losses and higher mortality in 2007, although mortality is still within expected ranges. In addition, operating income in 2007 included a $25 million increase in reserves related to changes in actuarial estimates and an $11 million increase in DAC amortization related to SOP 05-1.

Home service premiums and other considerations declined in 2007 compared to 2006 as the reduction in premiums in force from normal lapses and maturities exceeded sales growth. Net investment income in 2007 increased slightly compared to 2006 due to higher partnership income and positive changes from foreign denominated emerging market bonds. Home service operating income decreased largely due to higher net realized capital losses and an $11 million increase in DAC amortization related to SOP 05-1, partially offset by continued improvement in profit margins.

Group life/health premiums and other considerations in 2007 declined compared to 2006, primarily due to the exit from the financial institutions credit life business at the end of 2006 and tightened pricing and underwriting in the group employer product

lines. Group life/health operating income increased in 2007 compared to 2006. Operating income in 2007 included a $52 million decrease in policy benefits from additional reinsurance recoveries associated with Superior National, offset by an increase of $45 million in DAC amortization related to SOP 05-1. The operating loss in 2006 included a $125 million charge resulting from the loss of the Superior National arbitration, a $66 million loss related to exiting the financial institutions credit business and a $25 million charge for litigation reserves.

Payout annuities premiums and other considerations increased in 2007 compared to 2006 reflecting increased sales of structured settlements and terminal funding annuities. Net investment income increased in 2007 reflecting growth in insurance reserves and an increase in call and tender income on fixed income securities. Payout annuities operating income decreased slightly in 2007 as growth in the business was more than offset by higher net realized capital losses and by a $30 million out of period adjustment to increase group annuity reserves for payout annuities. Operating income in 2006 included a $24 million increase in reserves as various methodologies and assumptions were enhanced for payout annuity reserves.

Individual fixed and runoff annuities net investment income and operating income decreased in 2007 compared to 2006 reflecting declining insurance reserves. Operating income in 2006 included $30 million of increased amortization due to DAC unlocking to reflect lower in-force amounts.

2006 and 2005 Comparison

Premiums and other considerations for Domestic Life Insurance increased in 2006 compared to 2005 and were primarily driven by growth in the life insurance business in-force and payout annuity premiums, partially offset by declining in-force business in the home service and group life/health lines. Domestic Life Insurance operating income declined in 2006 compared to 2005 due to net realized capital losses and several significant transactions described below in 2006, partially offset by continued growth in life insurance and payout annuity business. Operating income in 2006 included a $125 million charge resulting from the loss of the Superior National arbitration and a $66 million loss related to exiting the financial institutions credit business both within the group life/health business. In addition, Domestic Life Insurance operating income was negatively affected by $55 million in litigation accruals, an increase in reserves of $24 million related to various methodologies and assumptions which were enhanced in the payout annuity business and a DAC unlocking charge of $30 million in the individual fixed and runoff annuities line to reflect lower in-force amounts.

The following table reflects Domestic Life Insurance periodic premium sales by product for 2007, 2006 and 2005:

				Percentage Increase/(Decrease)	
(in millions)	**2007**	2006	2005	2007 vs. 2006	2006 vs. 2005
Periodic Premium Sales By Product*:					
Universal life	**$230**	$334	$271	(31)%	23%
Variable universal life	**55**	56	44	(2)	27
Term life	**219**	240	229	(9)	5
Whole life/other	**9**	13	10	(31)	30
Total	**$513**	$643	$554	(20)%	16%

** Periodic premium represents premium from new business expected to be collected over a one-year period.*

2007 and 2006 Comparison

Domestic Life Insurance periodic premium sales declined in 2007 compared to 2006 primarily as a result of the repricing of certain universal life and term products and the tightening of underwriting standards during the second half of 2006. In the second half of 2007, AIG experienced positive sales growth in indexed universal life products and the sale of a large private placement variable universal life case.

2006 and 2005 Comparison

Domestic Life Insurance periodic premium sales increased in 2006 compared to 2005 primarily reflecting growth in the independent distribution platform. During the second half of 2006, certain universal life products were re-priced and underwriting standards were tightened.

Management's Discussion and Analysis of Financial Condition and Results of Operations *Continued*

Domestic Retirement Services Results

Domestic Retirement Services results, presented on a sub-product basis for 2007, 2006 and 2005 were as follows:

(in millions)	Premiums and Other Considerations	Net Investment Income	Net Realized Capital Gains (Losses)	Total Revenues	Operating Income
2007					
Group retirement products	**$ 446**	**$ 2,280**	**$ (451)**	**2,275**	**$ 696**
Individual fixed annuities	**96**	**3,664**	**(829)**	**2,931**	**530**
Individual variable annuities	**627**	**166**	**(45)**	**748**	**122**
Individual annuities — runoff*	**21**	**387**	**(83)**	**325**	**(1)**
Total	**$ 1,190**	**$ 6,497**	**$(1,408)**	**$ 6,279**	**$ 1,347**
2006					
Group retirement products	$ 386	$ 2,279	$ (144)	$ 2,521	$ 1,017
Individual fixed annuities	122	3,581	(257)	3,446	1,036
Individual variable annuities	531	202	5	738	193
Individual annuities — runoff*	18	426	(8)	436	77
Total	$ 1,057	$ 6,488	$ (404)	$ 7,141	$ 2,323
2005					
Group retirement products	$ 351	$ 2,233	$ (67)	$ 2,517	$ 1,055
Individual fixed annuities	97	3,346	(214)	3,229	858
Individual variable annuities	467	217	4	688	189
Individual annuities — runoff*	22	430	—	452	62
Total	$ 937	$ 6,226	$ (277)	$ 6,886	$ 2,164
Percentage Increase/(Decrease) 2007 vs. 2006:					
Group retirement products	16%	—%	—%	(10)%	(32)%
Individual fixed annuities	(21)	2	—	(15)	(49)
Individual variable annuities	18	(18)	—	1	(37)
Individual annuities — runoff	17	(9)	—	(25)	—
Total	13%	—%	—%	(12)%	(42)%
Percentage Increase/(Decrease) 2006 vs. 2005:					
Group retirement products	10%	2%	—%	—%	(4)%
Individual fixed annuities	26	7	—	7	21
Individual variable annuities	14	(7)	25	7	2
Individual annuities — runoff	(18)	(1)	—	(4)	24
Total	13%	4%	—%	4%	7%

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

2007 and 2006 Comparison

Total revenues and operating income for Domestic Retirement Services declined in 2007 compared to 2006 primarily due to increased net realized capital losses. Net realized capital losses for Domestic Retirement Services increased due to higher other-than-temporary impairment charges of $1.2 billion in 2007 compared to $368 million in 2006 and sales to reposition assets in certain investment portfolios for both group retirement products and individual fixed annuities, as well as from changes in the value of certain individual variable annuity product guarantees and related hedges associated with living benefit features. Changes in actuarial estimates, including DAC unlockings and refinements to estimates resulting from actuarial valuation system enhancements, resulted in a net decrease to operating income of $112 million in 2007.

Group retirement products operating income in 2007 decreased compared to 2006 primarily as a result of increased net realized capital losses due to higher other-than-temporary impairment charges and an increase in DAC amortization related to both an increase in surrenders and to policy changes adding guaranteed minimum withdrawal benefit riders to existing contracts. Operating income was also negatively affected in 2007 by an $18 million adjustment, primarily reflecting changes in actuarial estimates from the conversion to a new valuation system. These were partially offset by higher variable annuity fees which resulted from an increase in separate account assets compared to 2006.

Individual fixed annuities operating income in 2007 decreased compared to 2006 as a result of net realized capital losses due to higher other-than-temporary impairment charges partially offset by increases in partnership income. The decline in operating income also reflected higher DAC amortization and sales inducement costs related to increased surrenders and a $33 million charge reflecting changes in actuarial estimates from the conver-

sion to a new valuation system, as well as unlocking future assumptions and experience updates.

Individual variable annuities operating income decreased in 2007 compared to 2006 largely due to an increase in DAC amortization and sales inducement costs related to a $61 million adjustment reflecting changes in actuarial estimates. Net realized capital losses increased due to changes in the value of certain annuity product guarantees and related hedges associated with living benefit features and higher other-than-temporary impairment charges.

2006 and 2005 Comparison

Total Domestic Retirement Services operating income increased in 2006 compared to 2005 principally due to higher partnership and yield enhancement income in the individual fixed annuity product line. Group retirement products total revenues were flat in 2006 as improvements in partnership income and variable annuity fees were offset by increased net realized capital losses. The flat revenues, coupled with higher amortization of deferred acquisition costs related to internal replacements of existing contracts into new contracts, resulted in a decrease in group retirement operating income. Individual variable annuity total revenues increased in 2006, primarily driven by higher variable annuity fees resulting from an increase in assets under management. Partially offsetting these higher fees was an increase in DAC amortization resulting from increased surrender activity in the first half of 2006. In 2006, the individual annuities-runoff operating income increased, even though the underlying reserves decreased due to increased net spreads as a result of higher investment yields partially offset by increased realized capital losses.

The following table presents the account value roll forward for Domestic Retirement Services by product for 2007 and 2006:

(in millions)	**2007**	2006
Group retirement products		
Balance at beginning of year	**$ 64,357**	$ 59,312
Deposits — annuities	**5,898**	5,464
Deposits — mutual funds	**1,633**	1,361
Total Deposits	**7,531**	6,825
Surrenders and other withdrawals	**(6,551)**	(6,106)
Death benefits	**(262)**	(252)
Net inflows (outflows)	**718**	467
Change in fair value of underlying investments, interest credited, net of fees	**3,034**	4,578
Balance at end of year	**$ 68,109**	$ 64,357
Individual fixed annuities		
Balance at beginning of year	**$ 52,685**	$ 53,331
Deposits	**5,085**	5,331
Surrenders and other withdrawals	**(7,565)**	(6,379)
Death benefits	**(1,667)**	(1,649)
Net inflows (outflows)	**(4,147)**	(2,697)
Change in fair value of underlying investments, interest credited, net of fees	**1,970**	2,051
Balance at end of year	**$ 50,508**	$ 52,685
Individual variable annuities		
Balance at beginning of year	**$ 31,093**	$ 28,267
Deposits	**4,472**	4,266
Surrenders and other withdrawals	**(4,158)**	(3,894)
Death benefits	**(497)**	(486)
Net inflows (outflows)	**(183)**	(114)
Change in fair value of underlying investments, interest credited, net of fees	**2,198**	2,940
Balance at end of year	**$ 33,108**	$ 31,093
Total Domestic Retirement Services		
Balance at beginning of year	**$148,135**	$140,910
Deposits	**17,088**	16,422
Surrenders and other withdrawals	**(18,274)**	(16,379)
Death benefits	**(2,426)**	(2,387)
Net inflows (outflows)	**(3,612)**	(2,344)
Change in fair value of underlying investments, interest credited, net of fees	**7,202**	9,569
Balance at end of year, excluding runoff	**151,725**	148,135
Individual annuities runoff	**5,690**	6,326
Balance at end of year	**$157,415**	$154,461
General and separate account reserves and mutual funds		
General account reserve	**$ 88,801**	$ 92,070
Separate account reserve	**60,461**	55,988
Total general and separate account reserves	**149,262**	148,058
Group retirement mutual funds	**8,153**	6,403
Total reserves and mutual funds	**$157,415**	$154,461

2007 and 2006 Comparison

Domestic Retirement Services deposits increased in 2007 compared to 2006 primarily reflecting higher deposits in group retirement products and individual variable annuities, partially offset by a decrease in individual fixed annuities. Group retirement deposits increased 10 percent in 2007 compared to 2006 as a result of an increased focus on sales management and acquiring outside deposits. Mutual funds deposits increased 20 percent while group annuity deposits increased 8 percent. Over time,

growth in lower margin mutual fund products relative to annuity products will result in a gradual reduction in overall profit margins of this business. Individual fixed annuity sales continued to face increased competition from bank deposit products and money market funds offering very competitive short-term rates in the current yield curve environment, and as a result deposits decreased 5 percent in 2007 compared to 2006. Individual variable annuity deposits increased 5 percent in 2007 compared to 2006 despite the discontinuation of a major bank proprietary product.

Domestic Retirement Services surrenders and other withdrawals increased in 2007 compared to 2006. The increase primarily reflects higher surrenders in both group retirement products and individual fixed annuities. Group retirement surrenders increased as a result of both normal maturing of the business and higher large group surrenders in 2007 compared to 2006. Individual fixed annuity surrenders and withdrawals increased in 2007 due to both an increasing number of policies coming out of their surrender charge period and increased competition from bank deposit products. AIG expects this trend to continue into 2008 as a significant amount of business comes out of its surrender charge period.

The following table presents Domestic Retirement Services reserves by surrender charge category and surrender rates as of December 31, 2007 and 2006:

2007 *(in millions)*	Group Retirement Products*	Individual Fixed Annuities	Individual Variable Annuities
No surrender charge	**$49,770**	**$11,316**	**$13,014**
0% – 2%	**3,284**	**3,534**	**5,381**
Greater than 2% – 4%	**3,757**	**7,310**	**5,133**
Greater than 4%	**2,280**	**24,956**	**9,492**
Non-Surrenderable	**865**	**3,392**	**88**
Total Reserves	**$59,956**	**$50,508**	**$33,108**
Surrender rates	**9.8%**	**14.6%**	**12.8%**

2006 *(in millions)*	Group Retirement Products*	Individual Fixed Annuities	Individual Variable Annuities
No surrender charge	$42,741	$10,187	$11,467
0% – 2%	6,921	4,503	4,869
Greater than 2% – 4%	4,573	6,422	4,830
Greater than 4%	2,842	28,109	9,836
Non-Surrenderable	877	3,464	91
Total Reserves	$57,954	$52,685	$31,093
Surrender rates	9.9%	12.0%	13.3%

* *Excludes mutual funds of $8.2 billion and $6.4 billion in 2007 and 2006, respectively.*

Surrender rates increased for individual fixed annuities, while group retirement surrender rates decreased slightly in 2007 compared to 2006. Although group retirement surrenders increased compared to 2006, the surrender rate decreased slightly as a result of a 6 percent increase in reserves. The increase in the surrender rate for individual fixed annuities continues to be driven by a relatively flat yield curve and the general aging of the in-force block; however, less than 23 percent of the individual fixed annuity reserves as of December 31, 2007 were available for surrender without charge. Individual variable annuities surrender rates were slightly lower in 2007 compared to 2006.

An increase in the level of surrenders in any of these businesses or in the individual fixed annuities runoff block could accelerate the amortization of DAC and negatively affect fee income earned on assets under management.

Higher surrenders in the group retirement and individual fixed annuity blocks, offset somewhat by increased deposits in group retirement, resulted in negative net flows in 2007. The continuation of the current interest rate and competitive environment would prolong this trend.

Life Insurance & Retirement Services Net Investment Income and Net Realized Capital Gains (Losses)

The following table summarizes the components of net investment income for the years ended December 31, 2007, 2006 and 2005:

(in millions)	**2007**	2006	2005
Foreign Life Insurance & Retirement Services:			
Fixed maturities, including short-term investments	**$ 7,846**	$ 6,820	$ 6,059
Equity securities	**135**	80	51
Interest on mortgage and other loans	**466**	454	447
Partnership income	**128**	94	57
Unit investment trusts[(a)]	**439**	259	4
Other[(b)]	**275**	301	357
Total investment income before policyholder income and trading gains	**9,289**	8,008	6,975
Policyholder investment income and trading gains [(c)]	**2,899**	2,017	2,021
Total investment income	**12,188**	10,025	8,996
Investment expenses	**339**	267	278
Net investment income	**$11,849**	$ 9,758	$ 8,718
Domestic Life Insurance:			
Fixed maturities, including short-term investments	**$ 3,528**	$ 3,444	$ 3,481
Equity securities	**(4)**	(6)	(3)
Interest on mortgage and other loans	**418**	349	327
Partnership income — excluding Synfuels	**123**	80	135
Partnership loss — Synfuels	**(101)**	(107)	(143)
Unit investment trusts	**3**	5	—
Other[(b)]	**77**	67	(4)
Total investment income before policyholder income and trading gains	**4,044**	3,832	3,793
Policyholder investment income and trading gains[(c)]	**4**	—	—
Total investment income	**4,048**	3,832	3,793
Investment expenses	**53**	54	60
Net investment income	**$ 3,995**	$ 3,778	$ 3,733
Domestic Retirement Services:			
Fixed maturities, including short-term investments	**$ 5,376**	$ 5,645	$ 5,579
Equity securities	**30**	38	13
Interest on mortgage and other loans	**539**	449	401
Partnership income	**572**	425	224
Other[(b)]	**42**	(18)	60
Total investment income	**6,559**	6,539	6,277
Investment expenses	**62**	51	51
Net investment income	**$ 6,497**	$ 6,488	$ 6,226

(in millions)	**2007**	2006	2005
Total:			
Fixed maturities, including short-term investments	**$16,750**	$15,909	$15,119
Equity securities	**161**	112	61
Interest on mortgage and other loans	**1,423**	1,252	1,175
Partnership income — excluding Synfuels	**823**	599	416
Partnership loss — Synfuels	**(101)**	(107)	(143)
Unit investment trusts[(a)]	**442**	264	4
Other[(b)]	**394**	350	413
Total investment income before policyholder income and trading gains	**19,892**	18,379	17,045
Policyholder investment income and trading gains[(c)]	**2,903**	2,017	2,021
Total investment income	**22,795**	20,396	19,066
Investment expenses	**454**	372	389
Net investment income[(d)]	**$22,341**	$20,024	$18,677

(a) Includes the effect of an out of period UCITS adjustment in 2006, which increased net investment income by $240 million and operating income by $169 million.

(b) Includes real estate income, income on non-partnership invested assets, securities lending and Foreign Life Insurance & Retirement Services' equal share of the results of AIG Credit Card Company (Taiwan).

(c) Relates principally to assets held in various trading securities accounts that do not qualify for separate account treatment under SOP 03-1. These amounts are principally offset by an equal change included in incurred policy losses and benefits.

(d) Includes call and tender income.

2007 and 2006 Comparison

Net investment income increased $2.3 billion, or 12 percent in 2007 compared to 2006 as the invested asset base grew for fixed maturities, equity securities and mortgage and other loans. In addition, yield enhancement activity increased compared to 2006. Net investment income from UCITS in 2006 included a $240 million out of period increase. Policyholder trading gains increased in 2007 compared to 2006 principally due to an increase in assets under management, partially offset by trading account losses of $150 million on certain investment-linked products in the U.K. Net investment income for certain operations include investments in structured notes linked to emerging market sovereign debt that incorporates both interest rate risk and currency risk. These investments generated income of $45 million in 2007 compared to losses of $8 million in 2006. In addition, period to period comparisons of investment income for some investment activities, particularly partnership income, are affected by yield enhancement activity. See Invested Assets for further information.

AIG generates income tax credits as a result of investing in synthetic fuel production (synfuels) related to the partnership income (loss) shown in the above table and records those benefits separately from segment operating results in its consolidated provision for income taxes. The amounts of those income tax credits were $84 million, $127 million and $203 million for 2007, 2006 and 2005, respectively. These tax credits will no longer be generated after December 31, 2007. Synfuel production has ceased and the investments have been fully written off as of December 31, 2007.

2006 and 2005 Comparison

Net investment income increased 7 percent in 2006 compared to 2005 as income from fixed maturities, equity securities and mortgage and other loans income rose as the underlying invested asset base grew. Net investment income in 2006 also included the out of period increase relating to UCITS of $240 million.

The following table summarizes net realized capital gains (losses) for Life Insurance & Retirement Services by major category for the years ended December 31, 2007, 2006 and 2005:

(in millions)	**2007**	2006	2005
Foreign Life Insurance & Retirement Services:			
Sales of fixed maturities	**$ (187)**	$ (209)	$ 191
Sales of equity securities	**697**	459	281
Other:			
Other-than-temporary impairments[(a)]	**(1,026)**	(81)	(39)
Foreign exchange transactions[(b)]	**435**	106	40
Derivatives instruments	**(135)**	276	(599)
Other[(c)]	**29**	156	210
Total Foreign Life Insurance & Retirement Services	**$ (187)**	$ 707	$ 84
Domestic Life Insurance:			
Sales of fixed maturities	**$ (114)**	$ (33)	$ 65
Sales of equity securities	**5**	17	18
Other:			
Other-than-temporary impairments[(a)]	**(585)**	(192)	(119)
Foreign exchange transactions	**11**	(6)	11
Derivatives instruments	**(186)**	25	65
Other	**66**	(26)	(5)
Total Domestic Life Insurance	**$ (803)**	$ (215)	$ 35
Domestic Retirement Services:			
Sales of fixed maturities	**$ (192)**	$ 1	$ (106)
Sales of equity securities	**29**	31	115
Other:			
Other-than-temporary impairments[(a)]	**(1,187)**	(368)	(267)
Foreign exchange transactions	**27**	(13)	—
Derivatives instruments	**(60)**	(33)	(12)
Other	**(25)**	(22)	(7)
Total Domestic Retirement Services	**$ (1,408)**	$ (404)	$ (277)
Total:			
Sales of fixed maturities	**$ (493)**	$ (241)	$ 150
Sales of equity securities	**731**	507	414
Other:			
Other-than-temporary impairments[(a)]	**(2,798)**	(641)	(425)
Foreign exchange transactions[(b)]	**473**	87	51
Derivatives instruments	**(381)**	268	(546)
Other[(c)]	**70**	108	198
Total	**$ (2,398)**	$ 88	$ (158)

(a) See Invested Assets — Other-than-temporary impairments for additional information.

(b) Includes a positive out-of-period adjustment of $158 million in 2007 related to foreign exchange remediation activities.

(c) Includes gains (losses) of $(16) million, $88 million and $109 million in 2007, 2006 and 2005, respectively, allocated to participating policyholders.

2007 and 2006 Comparison

Net realized capital gains (losses) include normal portfolio transactions as well as derivative gains (losses) for transactions that did not qualify for hedge accounting treatment under FAS 133, foreign exchange gains and losses and other-than-temporary impairments. In 2007, Life Insurance & Retirement Services operations recorded $2.8 billion of other-than-temporary impairment charges compared to $641 million in 2006. For Foreign Life Insurance & Retirement Services operations, these losses were related to both the decline in value of U.S. dollar bonds held in Thailand and Singapore, which reflects the depreciation of the U.S. dollar against local currencies, and impairments due, in part, to the recent volatility in the securities markets. Net realized capital losses in the Foreign Life Insurance & Retirement Services operations in 2007 included losses of $135 million related to derivatives that did not qualify for hedge accounting treatment under FAS 133 compared to a gain of $276 million in 2006. Derivatives in the Foreign Life Insurance & Retirement Services operations are primarily used to economically hedge cash flows related to U.S. dollar bonds back to the respective currency of the country, principally in Taiwan, Thailand and Singapore. The corresponding foreign exchange gain or loss with respect to the economically hedged bond is deferred in accumulated other

comprehensive income until the bond is sold or deemed to be other-than-temporarily impaired.

For the Domestic Life Insurance and Domestic Retirement Services operations, the higher net realized capital losses resulted principally from other-than-temporary impairment charges of $1.8 billion in 2007 compared to $560 million in 2006 and from the sale of securities in 2007 to reposition assets in certain investment portfolios. Net realized capital losses in the Domestic Life Insurance operations in 2007 included losses of $186 million related to derivatives that did not qualify for hedge accounting treatment under FAS 133 compared to a gain of $25 million in 2006. Derivatives in the Domestic Life Insurance operations include affiliated interest rate swaps used to economically hedge cash flows on bonds and option contracts used to economically hedge cash flows on indexed annuity and universal life products. The corresponding gain or loss with respect to the economically hedged bond is deferred in accumulated other comprehensive income until the bond is sold, matures or deemed to be other-than-temporarily impaired. See Invested Assets — Valuation of Invested Assets — Portfolio Review herein.

2006 and 2005 Comparison

Net realized capital gains (losses) in 2006 improved $246 million compared to 2005 primarily due to gains on derivative instruments primarily used to economically hedge cash flows that did not qualify for hedge accounting treatment under FAS 133 and related primarily to the Foreign Life Insurance & Retirement Services operations.

Deferred Policy Acquisition Costs and Sales Inducement Assets

DAC for Life Insurance & Retirement Services products arises from the deferral of costs that vary with, and are directly related to, the acquisition of new or renewal business. Policy acquisition costs for life insurance products are generally deferred and amortized over the premium paying period in accordance with FAS 60. Policy acquisition costs that relate to universal life and investment-type products are deferred and amortized, with interest in relation to the incidence of estimated gross profits to be realized over the estimated lives of the contracts in accordance with FAS 97. Value of Business Acquired (VOBA) is determined at the time of acquisition and is reported on the consolidated balance sheet with DAC and amortized over the life of the business, similar to DAC. AIG offers sales inducements to contract holders (bonus interest) on certain annuity and investment contracts. Sales inducements are recognized as part of the liability for policyholders contract deposits on the consolidated balance sheet and are amortized over the life of the contract similar to DAC. Total deferred acquisition and sales inducement costs increased $549 million in 2007 compared to 2006 primarily due to higher production in the Foreign Life Insurance operations partially offset by lower Domestic Life Insurance & Retirement Services sales. Total amortization expense decreased $328 million compared to 2006. Annualized amortization expense levels in 2007 and 2006 were approximately 10 percent and 13 percent, respectively, of the opening DAC balance. The decline in amortization expense levels relates to changes in actuarial estimates, which is substantially offset by related adjustments to incurred policy losses and benefits.

The following table summarizes the major components of the changes in DAC/Value of Business Acquired (VOBA) and Sales Inducement Assets (SIA) for 2007 and 2006:

	2007			2006		
(in millions)	DAC/VOBA	SIA	Total	DAC/VOBA	SIA	Total
Foreign Life Insurance & Retirement Services						
Balance at beginning of year	**$21,153**	**$ 404**	**$21,557**	$17,638	$ 192	$17,830
Acquisition costs deferred	**5,640**	**241**	**5,881**	4,991	112	5,103
Amortization (charged) or credited to operating income:						
Related to net realized capital gains (losses)	**117**	**1**	**118**	5	(3)	2
Related to unlocking future assumptions	**(17)**	**(2)**	**(19)**	102	2	104
All other amortization[(a)]	**(1,979)**	**11**	**(1,968)**	(2,399)	(4)	(2,403)
Change in unrealized gains (losses) on securities	**301**	**16**	**317**	(132)	(6)	(138)
Increase due to foreign exchange	**831**	**10**	**841**	948	13	961
Other[(b)]	**129**	**—**	**129**	—	98	98
Balance at end of year[(a)]	**$26,175**	**$ 681**	**$26,856**	$21,153	$ 404	$21,557
Domestic Life Insurance						
Balance at beginning of year	**$ 6,006**	**$ 46**	**$ 6,052**	$ 5,184	$ 31	$ 5,215
Acquisition costs deferred	**895**	**15**	**910**	1,115	18	1,133
Amortization (charged) or credited to operating income:						
Related to net realized capital gains (losses)	**13**	**—**	**13**	23	—	23
Related to unlocking future assumptions	**6**	**(1)**	**5**	(42)	(1)	(43)
All other amortization[(a)]	**(671)**	**(7)**	**(678)**	(671)	(2)	(673)
Change in unrealized gains (losses) on securities	**162**	**—**	**162**	398	—	398
Increase (decrease) due to foreign exchange	**85**	**—**	**85**	(1)	—	(1)
Other[(b)]	**(64)**	**—**	**(64)**	—	—	—
Balance at end of year	**$ 6,432**	**$ 53**	**$ 6,485**	$ 6,006	$ 46	$ 6,052
Domestic Retirement Services						
Balance at beginning of year	**$ 5,651**	**$ 887**	**$ 6,538**	$ 5,284	$ 871	$ 6,155
Acquisition costs deferred	**741**	**201**	**942**	717	231	948
Amortization (charged) or credited to operating income:						
Related to net realized capital gains (losses)	**161**	**41**	**202**	62	19	81
Related to unlocking future assumptions	**(7)**	**(18)**	**(25)**	(3)	—	(3)
All other amortization[(a)]	**(990)**	**(174)**	**(1,164)**	(789)	(143)	(932)
Change in unrealized gains (losses) on securities	**282**	**54**	**336**	380	(91)	289
Balance at end of year	**$ 5,838**	**$ 991**	**$ 6,829**	$ 5,651	$ 887	$ 6,538
Total Life Insurance & Retirement Services						
Balance at beginning of year	**$32,810**	**$1,337**	**$34,147**	$28,106	$1,094	$29,200
Acquisition costs deferred	**7,276**	**457**	**7,733**	6,823	361	7,184
Amortization (charged) or credited to operating income:						
Related to net realized capital gains (losses)	**291**	**42**	**333**	90	16	106
Related to unlocking future assumptions	**(18)**	**(21)**	**(39)**	57	1	58
All other amortization[(a)]	**(3,640)**	**(170)**	**(3,810)**	(3,859)	(149)	(4,008)
Change in unrealized gains (losses) on securities	**745**	**70**	**815**	646	(97)	549
Increase due to foreign exchange	**916**	**10**	**926**	947	13	960
Other[(b)]	**65**	**—**	**65**	—	98	98
Balance at end of year	**$38,445**	**$1,725**	**$40,170**	$32,810	$1,337	$34,147

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

(b) In 2007, includes $(118) million for the cumulative effect of adoption of SOP 05-1 and $189 million related to balance sheet reclassifications. In 2006, primarily represents a balance sheet reclassification.

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

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

and AIG's results of operations could be significantly affected in such future periods.

Future Policy Benefit Reserves

Periodically, the net benefit reserves (policy benefit reserves less DAC) established for Life Insurance & Retirement Services companies are tested to ensure that, including consideration of future expected premium payments, they are adequate to provide for future policyholder benefit obligations. The assumptions used to perform the tests are current best-estimate assumptions as to policyholder mortality, morbidity, terminations, company maintenance expenses and invested asset returns. For long duration traditional business, a ''lock-in'' principle applies, whereby the assumptions used to calculate the benefit reserves and DAC are set when a policy is issued and do not change with changes in actual experience. These assumptions include margins for adverse deviation in the event that actual experience might deviate from these assumptions. For business in-force outside of North America, 45 percent of total policyholder benefit liabilities at December 31, 2007 resulted from traditional business where the lock-in principle applies. In most foreign locations, various guarantees are embedded in policies in force that may remain applicable for many decades into the future.

As experience changes over time, the best-estimate assumptions are updated to reflect the observed changes. Because of the long-term nature of many of AIG's liabilities subject to the lock-in principle, small changes in certain of the assumptions may cause large changes in the degree of reserve adequacy. In particular, changes in estimates of future invested asset return assumptions have a large effect on the degree of reserve adequacy.

During 2007, Life Insurance & Retirement Services continued its ongoing project to increase standardization of AIG's actuarial systems and processes throughout the world. In particular, there is an initiative within the Domestic Life Insurance & Retirement Services operations to consolidate the numerous actuarial valuation systems onto common platforms. This initiative began in 2006 and will continue into 2008. In the Foreign Life Insurance operations, actuarial reserves for certain blocks of business have been computed outside of the primary actuarial valuation systems and/or used methodologies that approximate amounts that would have been reported had these blocks of business been included in the primary actuarial valuation systems.

During 2007, Life Insurance & Retirement Services completed various system migrations, implemented more robust models for certain blocks of business and refined its method of approximation on any remaining blocks of business. The majority of these actions occurred in the fourth quarter of 2007 and any resulting changes in actuarial estimates were recorded in the fourth quarter of 2007 results of operations. The above changes in actuarial estimates, including unlockings, resulted in a net increase to operating income of $19 million during 2007. However, this net increase resulted from a number of items that had varying effects on the results of operations of certain operating units and lines of business. These adjustments resulted in an increase of $183 million in operating income for Foreign Life Insurance & Retirement Services and decreases in operating income of $52 million and $112 million for Domestic Life Insurance and Domestic Retirement Services, respectively. In addition, the related adjustments significantly affected both acquisition costs and incurred policy losses and benefits in the Consolidated Statement of Income due to reclassifications between DAC and future policy benefits reserves.

Taiwan

Beginning in 2000, the yield available on Taiwanese 10-year government bonds dropped from approximately 6 percent to 2.6 percent at December 31, 2007. Yields on most other invested assets have correspondingly dropped over the same period. Current sales are focused on products such as:

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

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

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

Future results of the reserve adequacy tests will involve significant management judgment as to mortality, morbidity, expense and termination rates and investment yields. Adverse changes in these assumptions could accelerate DAC amortization and necessitate reserve strengthening.

Financial Services Operations

AIG's Financial Services subsidiaries engage in diversified activities including aircraft and equipment leasing, capital markets, consumer finance and insurance premium finance.

Financial Services Results

Financial Services results were as follows:

(in millions)	**2007**	2006	2005	Percentage Increase/(Decrease) 2007 vs. 2006	2006 vs. 2005
Revenues:					
Aircraft Leasing[(a)]	**$ 4,694**	$4,082	$ 3,668	15%	11%
Capital Markets[(b)]	**(9,979)**	(186)	3,260	—	—
Consumer Finance[(c)]	**3,655**	3,587	3,563	2	1
Other, including intercompany adjustments	**321**	294	186	9	58
Total	**$ (1,309)**	$7,777	$10,677	—%	(27)%
Operating income (loss):					
Aircraft Leasing[(a)]	**$ 873**	$ 578	$ 769	51%	(25)%
Capital Markets[(b)]	**(10,557)**	(873)	2,661	—	—
Consumer Finance[(c)]	**171**	668	922	(74)	(28)
Other, including intercompany adjustments	**(2)**	10	72	—	(86)
Total	**$ (9,515)**	$ 383	$ 4,424	—%	(91)%

(a) Both revenues and operating income include gains (losses) from hedging activities that did not qualify for hedge accounting treatment under FAS 133, including the related foreign exchange gains and losses. In 2007, 2006 and 2005, the effect was $(37) million, $(73) million and $93 million, respectively. These amounts result primarily from interest rate and foreign currency derivatives that are effective economic hedges of borrowings. In the second quarter of 2007, ILFC began applying hedge accounting to most of its derivatives hedging interest rate and foreign exchange risks associated with its floating rate and foreign currency denominated borrowings.

(b) Revenues, shown net of interest expense of $4.6 billion, $3.2 billion and $3.0 billion in 2007, 2006 and 2005, respectively, were primarily from hedged financial positions entered into in connection with counterparty transactions. Both revenues and operating income include gains (losses) from hedging activities that did not qualify for hedge accounting treatment under FAS 133, including the related foreign exchange gains and losses. In 2007, 2006 and 2005, the effect was $211 million, $(1.8) billion and $2.0 billion, respectively. The year ended December 31, 2007 includes a $380 million out of period charge to reverse net gains recognized on transfers of available for sale securities among legal entities consolidated within AIGFP. The year ended December 31, 2006 includes an out of period charge of $223 million related to the remediation of the material weakness in internal control over the accounting for certain derivative transactions under FAS 133. In the first quarter of 2007, AIGFP began applying hedge accounting for certain of its interest rate swaps and foreign currency forward contracts hedging its investments and borrowings. In 2007, both revenues and operating income (loss) include an unrealized market valuation loss of $11.5 billion on AIGFP's super senior credit default swap portfolio and an other-than-temporary impairment charge of $643 million on AIGFP's available for sale investment securities recorded in other income.

(c) Both revenues and operating income include gains (losses) from hedging activities that did not qualify for hedge accounting treatment under FAS 133, including the related foreign exchange gains and losses. In 2007, 2006 and 2005, the effect was $(20) million, $(94) million and $75 million, respectively. These amounts result primarily from interest rate and foreign currency derivatives that are effective economic hedges of borrowings. In the second quarter of 2007, AGF began applying hedge accounting to most of its derivatives hedging interest rate and foreign exchange risks associated with its floating rate and foreign currency denominated borrowings. In 2007, includes a pre-tax charge of $178 million in connection with domestic consumer finance's mortgage banking activities.

2007 and 2006 Comparison

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

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

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

The year ended December 31, 2007 included an out of period charge of $380 million to reverse net gains recognized on transfers of available for sale securities among legal entities

consolidated within AIGFP. The year ended December 31, 2006 included out of period charges of $223 million related to the remediation of the material weakness in internal control over accounting for certain derivative transactions under FAS 133.

In order to better align financial reporting with the manner in which AIG's chief operating decision makers manage their businesses, beginning in 2007, net realized capital gains and losses, including derivative gains and losses and foreign exchange transaction gains and losses for Financial Services entities other than AIGFP, which were historically reported as a component of AIG's Other category, are now reported in Financial Services revenues and operating income. Prior period amounts have been revised to conform to the current presentation.

2006 and 2005 Comparison

Financial Services operating income decreased in 2006 compared to 2005, due primarily to the effect of hedging activities that did not qualify for hedge accounting treatment under FAS 133.

Aircraft Leasing

Aircraft Leasing operations represent the operations of ILFC, which generates its revenues primarily from leasing new and used commercial jet aircraft to foreign and domestic airlines. Revenues also result from the remarketing of commercial aircraft for ILFC's own account, and remarketing and fleet management services for airlines and financial institutions. ILFC finances its aircraft purchases primarily through the issuance of debt instruments. ILFC economically hedges part of its floating rate and substantially all of its foreign currency denominated debt using interest rate and foreign currency derivatives. Starting in the second quarter of 2007, ILFC began applying hedge accounting to most of its derivatives. All of ILFC's derivatives are effective economic hedges; however, since hedge accounting under FAS 133 was not applied prior to April 2, 2007, the benefits of using derivatives to hedge these exposures are not reflected in ILFC's 2006 corporate borrowing rate. The composite borrowing rates at December 31, 2007 and 2006 were 5.16 percent and 5.17 percent, respectively.

ILFC typically contracts to re-lease aircraft before the end of the existing lease term. For aircraft returned before the end of the lease term, ILFC has generally been able to re-lease such aircraft within two to six months of their return. As a lessor, ILFC considers an aircraft ''idle'' or ''off lease'' when the aircraft is not subject to a signed lease agreement or signed letter of intent. ILFC had no aircraft off lease at December 31, 2007, and all new aircraft scheduled for delivery through 2008 have been leased.

Aircraft Leasing Results

2007 and 2006 Comparison

ILFC's operating income increased in 2007 compared to 2006. Rental revenues increased by $596 million or 15 percent, driven by a larger aircraft fleet and higher lease rates. As of December 31, 2007, 900 aircraft in ILFC's fleet were subject to operating leases compared to 824 aircraft as of December 31, 2006. During 2007, ILFC realized income of $31 million from the sale of its rights against bankrupt airlines. The increase in revenues was partially offset by reduced flight equipment marketing revenues and increases in depreciation and interest expense. Flight equipment marketing revenues decreased by $40 million compared to 2006 due to fewer aircraft sales. Depreciation expense increased by $166 million, or 11 percent, in line with the increase in the size of the aircraft fleet. Interest expense increased by $176 million, or 12 percent, driven by additional borrowings to fund aircraft purchases and the rising cost of funds. In 2007 and 2006, the losses from hedging activities that did not qualify for hedge accounting treatment under FAS 133, including the related foreign exchange gains and losses, were $37 million and $73 million, respectively, in both revenues and operating income. During 2006, ILFC recorded charges to income related to a tax settlement in Australia, increased credit reserves and increased lease accruals, all of which totaled $37 million.

2006 and 2005 Comparison

ILFC's operating income decreased in 2006 compared to 2005. Rental revenues increased by $536 million or 16 percent, driven by a larger aircraft fleet, increased utilization and higher lease rates. During 2006, ILFC's fleet subject to operating leases increased by 78 airplanes to a total of 824. The increase in rental revenues was offset in part by increases in depreciation expense and interest expense, charges related to bankrupt airlines, as well as the settlement of a tax dispute in Australia related to the restructuring of ownership of aircraft. Depreciation expense increased by $200 million, or 14 percent, in line with the increase in the size of the aircraft fleet. Interest expense increased by $317 million, or 28 percent, driven by rising cost of funds, a weaker U.S. dollar against the Euro and the British Pound and additional borrowings funding aircraft purchases. As noted above, ILFC's interest expense did not reflect the benefit of hedging these exposures. In 2006 and 2005, the effect from hedging activities that did not qualify for hedge accounting treatment under FAS 133, including the related foreign exchange gains and losses, was a $73 million loss and a $93 million gain, respectively, in both revenues and operating income.

Capital Markets

Capital Markets represents the operations of AIGFP, which engages as principal in a wide variety of financial transactions, including standard and customized financial products involving commodities, credit, currencies, energy, equities and rates. The credit products include credit protection written through credit default swaps on super senior risk tranches of diversified pools of loans and debt securities. AIGFP also invests in a diversified portfolio of securities and principal investments and engages in borrowing activities involving the issuance of standard and structured notes and other securities, and entering into guaranteed investment agreements (GIAs).

As Capital Markets is a transaction-oriented operation, current and past revenues and operating results may not provide a basis for predicting future performance. AIG's Capital Markets opera-

tions derive a significant portion of their revenues from hedged financial positions entered into in connection with counterparty transactions. AIGFP also participates as a dealer in a wide variety of financial derivatives transactions. Revenues and operating income of the Capital Markets operations and the percentage change in these amounts for any given period are significantly affected by the number, size and profitability of transactions entered into during that period relative to those entered into during the prior period. Generally, the realization of transaction revenues as measured by the receipt of funds is not a significant reporting event as the gain or loss on AIGFP's trading transactions is currently reflected in operating income as the fair values change from period to period.

AIGFP's products generally require sophisticated models and significant management assumptions to determine fair values and, particularly during times of market disruption, the absence of observable market data can result in fair values at any given balance sheet date which are not indicative of the ultimate settlement values of the products.

Beginning in 2007, AIGFP applied hedge accounting under FAS 133 to certain of its interest rate swaps and foreign currency forward contracts hedging its investments and borrowings. As a result, AIGFP recognized in earnings the change in the fair value on the hedged items attributable to the hedged risks substantially offsetting the gains and losses on the derivatives designated as hedges. Prior to 2007, AIGFP did not apply hedge accounting under FAS 133 to any of its derivatives or related assets and liabilities. For further information on the effect of FAS 133 on AIGFP's business, see Risk Management — Segment Risk Management — Financial Services — Capital Markets Derivative Transactions and Note 8 to Consolidated Financial Statements.

Effective January 1, 2008, AIGFP elected to apply the fair value option to all eligible assets and liabilities, other than equity method investments. Electing the fair value option will allow AIGFP to more closely align its earnings with the economics of its transactions by recognizing the change in fair value on its derivatives and the offsetting change in fair value of the assets and liabilities being hedged concurrently through earnings. The adoption of FAS 159 with respect to elections made by AIGFP is currently being evaluated for the effect of recently issued draft guidance by the FASB, anticipated to be issued in final form in early 2008, and its potential effect on AIG's consolidated financial statements.

Capital Markets Results

2007 and 2006 Comparison

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

The unrealized market valuation losses related to AIGFP's super senior credit default swap portfolio, the preponderance of which relates to credit derivatives written on multi-sector CDO super senior tranches, were as follows:

(in millions)	Three months ended December 31, 2007	Year ended December 31, 2007
Multi-sector CDO	**$10,894**	$11,246
Corporate Debt/CLOs	**226**	226
Total	**$11,120**	$11,472

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

During the fourth quarter of 2007, certain of AIGFP's available for sale investments in super senior and AAA-rated bonds issued by multi-sector CDOs experienced severe declines in their fair value. As a result, AIGFP recorded an other-than-temporary impairment charge in other income of $643 million. Notwithstanding AIG's intent and ability to hold such securities until they recover in value, and despite structures which indicate that a substantial amount of the securities should continue to perform in accordance with their original terms, AIG concluded that it could not reasonably assert that the recovery period would be temporary. See also Invested Assets — Financial Services Invested Assets and Note 3 to Consolidated Financial Statements.

The change in fair value of AIGFP's credit default swaps that reference CDOs and the decline in fair value of its investments in CDOs were caused by the significant widening in spreads in the fourth quarter on asset-backed securities, principally those related to U.S. residential mortgages, the severe liquidity crisis affecting the structured finance markets and the effects of rating agency downgrades on those securities. AIG continues to believe that these unrealized market valuation losses are not indicative of the losses AIGFP may realize over time on this portfolio. Based upon its most current analyses, AIG believes that any credit impairment losses realized over time by AIGFP will not be material to AIG's consolidated financial condition, although it is possible that such realized losses could be material to AIG's consolidated results of operations for an individual reporting period.

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

The year ended December 31, 2007 included an out of period charge of $380 million to reverse net gains recognized in previous periods on transfers of available for sale securities among legal entities consolidated within AIGFP, and a $166 million reduction in fair value at March 31, 2007 of certain derivatives that were an integral part of, and economically hedge, the structured transac-

tions that were potentially affected by the proposed regulations issued by the U.S. Treasury Department discussed above in Overview of Operations and Business Results — Outlook. The net loss on AIGFP's derivatives recognized in 2006 included an out of period charge of $223 million related to the remediation of the material weakness in internal control over accounting for certain derivative transactions under FAS 133. The net loss also reflects the effect of increases in U.S. interest rates and a weakening of the U.S. dollar on derivatives hedging AIGFP's assets and liabilities.

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

The most significant component of Capital Markets operating expenses is compensation, which was approximately $423 million, $544 million and $481 million in 2007, 2006 and 2005, respectively. The amount of compensation was not affected by gains and losses arising from derivatives not qualifying for hedge accounting treatment under FAS 133. In light of the unrealized market valuation loss related to the AIGFP super senior credit default swap portfolio, to retain and motivate the affected AIGFP employees, a special incentive plan relating to 2007 was established. Under this plan, certain AIGFP employees were granted cash awards vesting over two years and payable in 2013. The expense related to these awards will be recognized ratably over the vesting period, beginning in 2008.

AIG elected to early adopt FAS 155, ''Accounting for Certain Hybrid Financial Instruments'' (FAS 155) in 2006. AIGFP elected to apply the fair value option permitted by FAS 155 to its structured notes and other financial liabilities containing embedded derivatives outstanding as of January 1, 2006. The cumulative effect of the adoption of FAS 155 on these instruments at January 1, 2006 was a pre-tax loss of $29 million. AIGFP recognized a loss of $351 million in 2007 and a loss of $287 million in 2006 on hybrid financial instruments for which it applied the fair value option under FAS 155. These amounts were largely offset by gains and losses on economic hedge positions also reflected in AIGFP's operating income or loss.

2006 and 2005 Comparison

Capital Markets reported an operating loss in 2006 compared to operating income in 2005. Improved results, primarily from increased transaction flow in AIGFP's credit, commodity index, energy and equity products, were more than offset by the loss resulting from the effect of derivatives not qualifying for hedge accounting treatment under FAS 133. This loss was $1.82 billion in 2006 compared to a gain of $2.01 billion in 2005, a decrease of $3.83 billion. A large part of the net loss on AIGFP's derivatives recognized in 2006 was due to the weakening of the U.S. dollar, primarily against the British Pound and Euro, resulting in a decrease in the fair value of the foreign currency derivatives hedging AIGFP's available for sale securities. The majority of the net gain on AIGFP's derivatives in 2005 was due to the strengthening of the U.S. dollar, primarily against the British Pound and Euro, which increased the fair value of the foreign currency derivatives hedging available for sale securities. To a lesser extent, the net gain in 2005 was due to the decrease in long-term U.S. interest rates, which increased the fair value of derivatives hedging AIGFP's assets and liabilities.

Financial market conditions in 2006 were characterized by a general flattening of interest rate yield curves across fixed income markets globally, tightening of credit spreads, higher equity valuations and a weaker U.S. dollar.

Consumer Finance

AIG's Consumer Finance operations in North America are principally conducted through AGF. AGF derives a substantial portion of its revenues from finance charges assessed on outstanding real estate loans, secured and unsecured non-real estate loans and retail sales finance receivables and credit-related insurance.

AGF's finance receivables are primarily sourced through its branches, although many of AGF's real estate loans are sourced through its centralized real estate operations, which include AGF's mortgage banking activities. The majority of the real estate loans originated by AGF's mortgage banking subsidiary are originated through broker relationships and are sold to investors on a servicing-released basis. Beginning in July 2003, AGF's mortgage banking subsidiaries originated and sold loans through a services arrangement with AIG Federal Savings Bank (AIG Bank), a federally chartered thrift and non-subsidiary of AGF. The services relationship was terminated in the first quarter of 2006. Since terminating the services relationship with AIG Bank, AGF's mortgage banking subsidiaries have originated these non-conforming real estate loans using their own state licenses.

On June 7, 2007, AIG's domestic consumer finance operations, consisting of AIG Bank, AGF's mortgage banking subsidiary Wilmington Finance, Inc. (WFI) and AGF, entered into a Supervisory Agreement with the OTS. The Supervisory Agreement pertains to certain mortgage loans originated in the name of AIG Bank from July 2003 through early May 2006 pursuant to the services agreement between WFI and AIG Bank, which was terminated in the first quarter of 2006. Pursuant to the terms of the Supervisory Agreement, AIG Bank, WFI and AGF have implemented a financial remediation program whereby certain borrowers may be provided loans on more affordable terms and/or reimbursed for certain fees. Pursuant to the requirements of the Supervisory Agreement, the services of an external consultant have been engaged to monitor, evaluate and periodically report to the OTS on compliance with the remediation program. The Supervisory Agreement will remain in effect until terminated, modified, or suspended in writing by the OTS. Failure to comply with the terms of the Agreement could result in the initiation of formal enforcement action by the OTS. Separately, the domestic consumer finance operations also committed to donate $15 million over a three-year period to certain not-for-profit organizations to support their efforts to promote financial literacy and credit counseling.

Management's best estimate of the cost of implementing the financial remediation plan contemplated by the Supervisory Agreement, including the $15 million donation, was $178 million which was recorded in 2007. The actual cost of implementing the financial remediation plan may differ from this estimate.

AIG's foreign consumer finance operations are principally conducted through AIG Consumer Finance Group, Inc. (AIGCFG). AIGCFG operates primarily in emerging and developing markets. AIGCFG has operations in Argentina, China, Hong Kong, Mexico, Philippines, Poland, Taiwan and Thailand and began operations in India in 2007 through the acquisition of a majority interest in a sales finance lending operation and the acquisition of a mortgage lending operation. In addition, in 2007, AIGCFG expanded its distribution channels in Thailand by acquiring an 80 percent interest in a company with a network of over 130 branches for secured consumer lending. AIGCFG is continuously exploring expansion opportunities in its existing operations as well as new geographic locations throughout the world.

Certain of the AIGCFG operations are partly or wholly owned by life insurance subsidiaries of AIG. Accordingly, the financial results of those companies are allocated between Financial Services and Life Insurance & Retirement Services according to their ownership percentages. While products vary by market, the businesses generally provide credit cards, unsecured and secured non-real estate loans, term deposits, savings accounts, retail sales finance and real estate loans. AIGCFG originates finance receivables through its branches and direct solicitation. AIGCFG also originates finance receivables indirectly through relationships with retailers, auto dealers, and independent agents.

Consumer Finance Results

2007 and 2006 Comparison

Consumer Finance operating income decreased in 2007 compared to 2006. Operating income from the domestic consumer finance operations, which include the operations of AGF and AIG Bank, decreased by $509 million, or 77 percent, in 2007 compared to 2006. In 2007, domestic results were adversely affected by the weakening housing market and tighter underwriting guidelines, which resulted in lower originations of real estate loans as well as the $178 million charge discussed above.

AGF's revenues decreased $95 million or 3 percent during 2007 compared to 2006. Revenues from AGF's mortgage banking activities decreased $389 million during 2007 compared to 2006, which includes the charges relating to the Supervisory Agreement. The decrease in revenues also reflects a significantly reduced origination volume, lower yields based on market conditions, tighter underwriting guidelines, reduced margins on loans sold and higher warranty reserves, which cover obligations to repurchase loans sold to third-party investors should there be a first payment default or breach of representations and warranties. AGF's revenues in 2007 also included a recovery of $65 million from a favorable out of court settlement.

AGF's operating income decreased in 2007 compared to 2006, due to reduced residential mortgage origination volumes, lower revenues from its mortgage banking activities and increases in the provision for finance receivable losses. AGF's interest expense increased by $81 million or seven percent as its borrowing rate increased in 2007 compared to 2006. During 2007, AGF recorded a net loss of $28 million on its derivatives that did not qualify for hedge accounting under FAS 133, including the related foreign exchange losses, compared to a net loss of $89 million in 2006. Commencing in the second quarter of 2007, AGF began applying hedge accounting.

AGF's net finance receivables totaled $25.5 billion at December 31, 2007, an increase of approximately $1.2 billion compared to December 31, 2006, including $19.5 billion of real estate secured loans, most of which were underwritten with full income verification. The increase in the net finance receivables resulted in a similar increase in revenues generated from these assets.

Although real estate loan originations declined in 2007, the softening of home price appreciation (reducing the equity customers may be able to extract from their homes by refinancing) contributed to an increase in non-real estate loans of 11 percent at December 31, 2007 compared to December 31, 2006. Retail sales finance receivables also increased 13 percent compared to December 31, 2006 due to increased marketing efforts and customer demand. AGF's centralized real estate operations finance receivables were essentially unchanged while branch business segment finance receivables increased by 8 percent during 2007.

AGF's allowance for finance receivable losses as a percentage of outstanding receivables was 2.36 percent at December 31, 2007 compared to 2.01 percent at December 31, 2006.

Revenues from the foreign consumer finance operations increased by 29 percent in 2007 compared to 2006. Loan growth, particularly in Poland, Thailand and Latin America, was the primary driver of the increased revenues. The increase in revenues was more than offset by higher expenses associated with branch expansions, acquisition activities and product promotion campaigns. Operating income in 2006 reflects AIGCFG's $47 million share of the allowance for losses related to industry-wide credit deterioration in the Taiwan credit card market.

2006 and 2005 Comparison

Consumer Finance operating income decreased in 2006 compared to 2005. Operating income from domestic consumer finance operations declined by $193 million, or 23 percent as a result of decreased originations and purchases of real estate loans and margin compression resulting from increased interest rates and flattened yield curves. The foreign operations operating income decreased primarily due to the credit deterioration in the Taiwan credit card market.

Domestically, the U.S. housing market deteriorated throughout 2006 and as a result, the real estate loan portfolio decreased slightly during 2006 due to lower refinancing activity. This lower refinancing activity also caused a significant decrease in originations and whole loan sales in AGF's mortgage banking operation, which resulted in a substantial reduction of revenue and operating income compared to the prior year. However, softening home prices (reducing the equity customers are able to extract from their homes when refinancing) and higher mortgage rates contributed to customers utilizing non-real estate loans, which increased 10 percent compared to 2005. Retail sales finance receivables also increased 23 percent due to increased marketing efforts and customer demand. Higher revenue resulting from portfolio growth was more than offset by higher interest expense. AGF's short-term borrowing rates were 5.14 percent in 2006 compared to

3.58 percent in 2005. AGF's long-term borrowing rates were 5.05 percent in 2006 compared to 4.41 percent in 2005. During 2006, AGF recorded a net loss of $89 million on its derivatives that did not qualify for hedge accounting under FAS 133, including the related foreign exchange losses, compared to a net gain of $69 million in 2005. AGF's net charge-off ratio improved to 0.95 percent in 2006 from 1.19 percent in 2005. The improvement in the net charge-off ratio in 2006 was primarily due to positive economic fundamentals. The U.S. economy continued to expand during the year, and the unemployment rate remained low, which improved the credit quality of AGF's portfolio. AGF's delinquency ratio remained relatively low, although it increased to 2.06 percent at December 31, 2006 from 1.93 percent at December 31, 2005. AGF reduced the hurricane Katrina portion of its allowance for finance receivable losses to $15 million at December 31, 2006 after the reevaluation of its remaining estimated losses. AGF's allowance ratio was 2.01 percent at December 31, 2006 compared to 2.20 percent at December 31, 2005.

Revenues from the foreign consumer finance operations increased by approximately 13 percent in 2006 compared to 2005. Loan growth, particularly in Poland and Argentina, was the primary driver behind the higher revenues. Higher revenues were more than offset, however, by AIGCFG's $47 million share of the allowance for losses related to industrywide credit deterioration in the Taiwan credit card market, increased cost of funds, and higher operating expenses in connection with expansion into new markets and distribution channels and new product promotions, resulting in lower operating income in 2006 compared to 2005.

Asset Management Operations

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

The revenues and operating income for this segment are affected by the general conditions in the equity and credit markets. In addition, net realized gains and performance fees are contingent upon various fund closings, maturity levels and market conditions.

Asset Management Results

Asset Management results were as follows:

(in millions)	**2007**	2006	2005	Percentage Increase/(Decrease) 2007 vs. 2006	2006 vs. 2005
Revenues:					
Spread-Based Investment business	**$2,023**	$2,713	$2,973	(25)%	(9)%
Institutional Asset Management*	**2,900**	1,240	1,026	134	21
Brokerage Services and Mutual Funds	**322**	293	257	10	14
Other Asset Management	**380**	297	326	28	(9)
Total	**$5,625**	$4,543	$4,582	24%	(1)%
Operating income:					
Spread-Based Investment business	**$ (89)**	$ 732	$1,194	—%	(39)%
Institutional Asset Management*	**784**	438	387	79	13
Brokerage Services and Mutual Funds	**100**	87	66	15	32
Other Asset Management	**369**	281	316	31	(11)
Total	**$1,164**	$1,538	$1,963	(24)%	(22)%

* *Includes the effect of consolidating the revenues and operating loss of warehoused investments totaling $778 million and $164 million, respectively, in 2007, a portion of which is offset in minority interest expense.*

2007 and 2006 Comparison

Asset Management revenues increased in 2007 compared to 2006 primarily due to increased partnership income, management fees, carried interest and the effect of consolidating several warehoused investments. AIG consolidates the operating results of warehoused investments until such time as they are sold or otherwise divested.

Asset Management operating income decreased in 2007 compared to 2006, due to foreign exchange, interest rate and credit-related mark to market losses and other-than-temporary impairment charges on fixed income investments. These other-than-temporary impairment charges were due primarily to changes in market liquidity and spreads. Partially offsetting these decreases were higher partnership income, increased gains on real estate investments and a gain on the sale of a portion of AIG's investment in Blackstone Group, L.P. in connection with its initial public offering.

In order to better align financial reporting with the manner in which AIG's chief operating decision makers manage their businesses, beginning in 2007, net realized capital gains and losses, and foreign exchange transaction gains and losses, which were previously reported as part of AIG's Other category, are now included in Asset Management revenues and operating income. In addition, revenues and operating income related to foreign

investment-type contracts, which were historically reported as a component of the Spread-Based Investment business, are now reported in the Life Insurance & Retirement Services segment. Also, commencing in 2007, the effect of consolidating managed partnerships and funds, which were historically reported as a component of the Institutional Asset Management business, are now reported in the Consolidation and eliminations category. Prior period amounts have been revised to conform to the current presentation.

2006 and 2005 Comparison

Asset Management operating income decreased in 2006 compared to 2005 as a decline in Spread-Based Investment operating income was partially offset by higher Institutional Asset Management operating income.

Spread-Based Investment Business Results

2007 and 2006 Comparison

The Spread-Based Investment business reported an operating loss in 2007 compared to operating income in 2006 due to foreign exchange, interest rate and credit-related mark to market losses and other-than-temporary impairment charges on fixed income investments, partially offset by increased partnership income. In 2007, the GIC program incurred foreign exchange losses of $526 million on foreign-denominated GIC reserves. Partially offsetting these losses were $269 million of net mark to market gains on derivative positions. These net gains included mark to market gains on foreign exchange derivatives used to economically hedge the effect of foreign exchange rate movements on foreign-denominated GIC reserves and mark to market losses on interest rate hedges that did not qualify for hedge accounting treatment.

The MIP experienced mark to market losses of $193 million due to interest rate and foreign exchange derivative positions that, while partially effective in hedging interest rate and foreign exchange risk, did not qualify for hedge accounting treatment and an additional $98 million due to credit default swap losses. The MIP credit default swaps are comprised of single-name high-grade corporate exposures. AIG enters into hedging arrangements to mitigate the effect of changes in currency and interest rates associated with the fixed and floating rate and foreign currency denominated obligations issued under these programs. Some of these hedging relationships qualify for hedge accounting treatment, while others do not. Commencing in the first quarter of 2007, AIG applied hedge accounting to certain derivative transactions related to the MIP. Income or loss from these hedges not qualifying for hedge accounting treatment are classified as net realized capital gains (losses) in AIG's Consolidated Statement of Income. The mark to market losses for 2007 were driven primarily by a decline in short-term interest rates, the decline in the value of the U.S. dollar and widening credit spreads.

Also contributing to the operating loss were other-than-temporary impairment charges on various fixed income investments held in the GIC and MIP portfolios of approximately $836 million as a result of movements in credit spreads and decreased market liquidity. See Invested Assets — Other-than-temporary impairments. These losses were partially offset by an increase in partnership income associated with the GIC. In addition to other-than-temporary impairments, unrealized losses on fixed income investments were driven by widening credit spreads, partially offset by gains due to falling interest rates. These unrealized losses are recorded in Accumulated other comprehensive income (loss).

During 2007, AIG has issued the equivalent of $8.1 billion of securities to fund the MIP in the Euromarkets and the U.S. public and private markets compared to $5.3 billion issued in 2006. At December 31, 2007, total issuances were $13.4 billion.

The following table illustrates the anticipated runoff of the domestic GIC portfolio at December 31, 2007:

(in billions)	Less Than One Year	1-3 Years	3+-5 Years	Over Five Years	Total
Domestic GICs	$9.4	$6.4	$2.7	$6.8	$25.3

2006 and 2005 Comparison

Operating income related to the Spread-Based Investment business declined in 2006 compared to 2005 due primarily to the continued runoff of GIC balances and spread compression related to increases in short-term interest rates. A significant portion of the remaining GIC portfolio consists of floating rate obligations. AIG has entered into hedges to manage against increases in short-term interest rates. AIG believes these hedges are economically effective, but they did not qualify for hedge accounting treatment. The decline in operating income was partially offset by improved partnership income, particularly during the fourth quarter of 2006.

Institutional Asset Management Results

2007 and 2006 Comparison

Operating income for Institutional Asset Management increased in 2007 compared to 2006 reflecting increased carried interest revenues driven by higher valuations of portfolio investments that are generally associated with improved performance in the equity markets. The increase also reflects a $398 million gain from the sale of a portion of AIG's investment in Blackstone Group, L.P. in connection with its initial public offering. Also contributing to this increase were higher base management fees driven by higher levels of third-party assets under management. Partially offsetting these increases were the operating losses from warehousing activities. The consolidated warehoused private equity investments are not wholly owned by AIG and thus, a significant portion of the effect of consolidating these operating losses is offset in minority interest, which is not a component of operating income.

AIG's unaffiliated client assets under management, including retail mutual funds and institutional accounts, increased 26 percent to $94.2 billion at December 31, 2007 compared to December 31, 2006. Additionally, AIG Investments successfully launched several new private equity and real estate funds in 2007, which provide both a base management fee and the opportunity for future incentive fees.

While unaffiliated client assets under management and the resulting management fees continue to increase, the growth in operating income has trailed the growth in revenues due to the additional costs associated with warehousing activities as well as the costs associated with sales and infrastructure enhancements. The sales and infrastructure enhancements are associated with AIG's planned expansion of marketing and distribution capabilities, combined with technology and operational infrastructure-related improvements.

2006 and 2005 Comparison

Operating income related to Institutional Asset Management increased in 2006 compared to 2005, primarily due to realized gains on real estate transactions as well as increased management fees. AIG's unaffiliated client assets under management, including both retail mutual funds and institutional accounts, increased 21 percent from year-end 2005 to $75 billion, resulting in higher management fee income. Partially offsetting this growth were lower carried interest on private equity investments, and higher expenses related to the planned expansion of marketing and distribution capabilities, combined with technology and operational infrastructure-related enhancements.

Other Operations

The operating loss of AIG's Other category for the years ended December 31, 2007, 2006 and 2005 was as follows:

(in millions)	**2007**	2006	2005
Other Operating Income (Loss):			
Equity earnings in partially owned companies	**$ 157**	$ 193	$ (124)
Interest expense	**(1,223)**	(859)	(541)
Unallocated corporate expenses*	**(560)**	(517)	(413)
Compensation expense — SICO Plans	**(39)**	(108)	(205)
Compensation expense — Starr tender offer	**—**	(54)	—
Net realized capital gains (losses)	**(409)**	(37)	269
Regulatory settlement costs	**—**	—	(1,644)
Other miscellaneous, net	**(66)**	(53)	(107)
Total Other	**$(2,140)**	$(1,435)	$(2,765)

* *Includes expenses of corporate staff not attributable to specific business segments, expenses related to efforts to improve internal controls, corporate initiatives and certain compensation plan expenses.*

2007 and 2006 Comparison

The operating loss of AIG's Other category increased in 2007 compared to 2006 reflecting higher interest expense that resulted from increased borrowings, higher unallocated corporate expenses and foreign exchange losses on foreign-denominated debt, a portion of which was economically hedged but did not qualify for hedge accounting treatment under FAS 133. In addition, Net realized capital gains (losses) in 2007 included an other-than-temporary impairment charge of $144 million related to an investment in a partially owned company and foreign exchange losses of $221 million on unhedged debt.

The operating loss in 2006 for AIG's Other category included an out of period charge of $61 million related to the SICO Plans and a one-time charge related to the Starr tender offer of $54 million. For a further discussion of these items, see Note 19 to Consolidated Financial Statements.

In 2007, no compensation cost was recognized, and compensation cost recognized in 2006 was reversed, with respect to awards under the Partners Plan because the performance threshold was not met. The amounts earned under the AIG Partners Plan will be determined by the Compensation Committee in the first quarter of 2008.

In order to better align financial reporting with the manner in which AIG's chief operating decision makers manage their businesses, beginning in 2007, derivative gains and losses and foreign exchange transaction gains and losses for Asset Management and Financial Services entities (other than AIGFP) are now included in Asset Management and Financial Services revenues and operating income. These amounts were previously reported as part of AIG's Other category. Prior period amounts have been revised to conform to the current presentation.

2006 and 2005 Comparison

Operating loss for AIG's Other category declined in 2006 compared to 2005, reflecting the regulatory settlement costs of $1.6 billion in 2005, as described under Item 3. Legal Proceedings, offset by increased interest expense in 2006 as a result of increased borrowings by the parent holding company and realized capital losses of $37 million. These declines were partially offset by increased equity earnings in certain partially owned companies.

Capital Resources and Liquidity

At December 31, 2007, AIG had total consolidated shareholders' equity of $95.8 billion and total consolidated borrowings of $176.0 billion. At that date, $67.9 billion of such borrowings were subsidiary borrowings not guaranteed by AIG.

In 2007, AIG issued an aggregate of $5.6 billion of junior subordinated debentures in five series of securities. Substantially all of the proceeds from these sales, net of expenses, are being used to purchase shares of AIG's common stock. A total of 76,361,209 shares were purchased during 2007.

Borrowings

Total borrowings at December 31, 2007 and 2006 were as follows:

(in millions)	**2007**	2006
Borrowings issued by AIG:		
Notes and bonds payable	**$ 14,588**	$ 8,915
Junior subordinated debt	**5,809**	—
Loans and mortgages payable	**729**	841
MIP matched notes and bonds payable	**14,267**	5,468
Series AIGFP matched notes and bonds payable	**874**	72
Total AIG borrowings	**36,267**	15,296
Borrowings guaranteed by AIG:		
AIGFP		
GIAs	**19,908**	20,664
Notes and bonds payable	**36,676**	37,528
Loans and mortgages payable	**1,384**	—
Hybrid financial instrument liabilities[(a)]	**7,479**	8,856
Total AIGFP borrowings	**65,447**	67,048
AIG Funding, Inc. commercial paper	**4,222**	4,821
AIGLH notes and bonds payable	**797**	797
Liabilities connected to trust preferred stock	**1,435**	1,440
Total borrowings issued or guaranteed by AIG	**108,168**	89,402
Borrowings not guaranteed by AIG:		
ILFC		
Commercial paper	**4,483**	2,747
Junior subordinated debt	**999**	999
Notes and bonds payable[(b)]	**25,737**	25,592
Total ILFC borrowings	**31,219**	29,338
AGF		
Commercial paper and extendible commercial notes	**3,801**	4,662
Junior subordinated debt	**349**	—
Notes and bonds payable	**22,369**	19,261
Total AGF borrowings	**26,519**	23,923
AIGCFG		
Commercial paper	**287**	227
Loans and mortgages payable	**1,839**	1,453
Total AIGCFG borrowings	**2,126**	1,680
AIG Finance Taiwan Limited commercial paper	**—**	26
Other subsidiaries	**775**	672
Borrowings of consolidated investments:		
A.I. Credit[(c)]	**321**	880
AIG Investments[(d)]	**1,636**	193
AIG Global Real Estate Investment[(d)]	**5,096**	2,307
AIG SunAmerica	**186**	203
ALICO	**3**	55
Total borrowings of consolidated investments	**7,242**	3,638
Total borrowings not guaranteed by AIG	**67,881**	59,277
Consolidated:		
Total commercial paper and extendible commercial notes	**$ 13,114**	$ 13,363
Total long-term borrowings	**162,935**	135,316
Total borrowings	**$176,049**	$148,679

(a) Represents structured notes issued by AIGFP that are accounted for using the fair value option.

(b) Includes borrowings under Export Credit Facility of $2.5 billion and $2.7 billion at December 31, 2007 and 2006, respectively.

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

(d) In 2007, increases in borrowings compared to 2006 were principally attributable to warehousing activities.

At December 31, 2007 and 2006, AIG's net borrowings amounted to $20.3 billion and $15.4 billion, respectively, as follows:

(in millions)	**2007**	2006
AIG's total borrowings	**$176,049**	$148,679
Less:		
Junior subordinated debt	**5,809**	—
Liabilities connected to trust preferred stock	**1,435**	1,440
MIP matched notes and bonds payable	**14,267**	5,468
Series AIGFP matched notes and bonds payable	**874**	72
AIGFP		
GIAs	**19,908**	20,664
Notes and bonds payable	**36,676**	37,528
Loans and mortgages payable	**1,384**	—
Hybrid financial instrument liabilities*	**7,479**	8,856
Borrowings not guaranteed by AIG	**67,881**	59,277
AIG's net borrowings	**$ 20,336**	$ 15,374

* *Represents structured notes issued by AIGFP that are accounted for at fair value.*

A roll forward of long-term borrowings, excluding borrowings of consolidated investments, for the year ended December 31, 2007 is as follows:

(in millions)	Balance at December 31, 2006	Issuances	Maturities and Repayments	Effect of Foreign Exchange	Other Changes	**Balance at December 31, 2007**
AIG						
Notes and bonds payable	$ 8,915	$ 5,591	$ (165)	$ 122	$ 125	**$ 14,588**
Junior subordinated debt	—	5,590	—	218	1	**5,809**
Loans and mortgages payable	841	600	(724)	12	—	**729**
MIP matched notes and bonds payable	5,468	8,092	—	(4)	711	**14,267**
Series AIGFP matched notes and bonds payable	72	810	(10)	—	2	**874**
AIGFP						
GIAs	20,664	8,830	(10,172)	43	543	**19,908**
Notes and bonds payable and hybrid financial instrument liabilities	46,384	50,854	(53,540)	321	136	**44,155**
Loans and mortgages payable	—	1,388	(9)	9	(4)	**1,384**
AIGLH notes and bonds payable	797	—	—	—	—	**797**
Liabilities connected to trust preferred stock	1,440	—	—	—	(5)	**1,435**
ILFC notes and bonds payable	25,592	3,783	(3,938)	295	5	**25,737**
ILFC junior subordinated debt	999	—	—	—	—	**999**
AGF notes and bonds payable	19,261	7,481	(4,824)	255	196	**22,369**
AGF junior subordinated debt	—	349	—	—	—	**349**
AIGCFG loans and mortgages payable	1,453	3,941	(3,647)	98	(6)	**1,839**
Other subsidiaries	672	189	(189)	3	100	**775**
Total	$ 132,558	$97,498	$ (77,218)	$ 1,372	$ 1,804	**$ 156,014**

AIG (Parent Company)

AIG intends to continue its customary practice of issuing debt securities from time to time to meet its financing needs and those of certain of its subsidiaries for general corporate purposes, as well as for the MIP. As of December 31, 2007, AIG had up to $17.5 billion of debt securities, preferred stock and other securities, and up to $12.0 billion of common stock, registered and available for issuance under its universal shelf registration statement.

AIG maintains a medium-term note program under its shelf registration statement. As of December 31, 2007, approximately $7.3 billion principal amount of senior notes were outstanding under the medium-term note program, of which $3.2 billion was used for AIG's general corporate purposes, $873 million was used by AIGFP (referred to as ''Series AIGFP'' in the preceding tables) and $3.2 billion was used to fund the MIP. The maturity dates of these notes range from 2008 to 2052. To the extent deemed appropriate, AIG may enter into swap transactions to manage its effective borrowing rates with respect to these notes.

AIG also maintains a Euro medium-term note program under which an aggregate nominal amount of up to $20.0 billion of senior notes may be outstanding at any one time. As of December 31, 2007, the equivalent of $12.7 billion of notes were outstanding under the program, of which $9.8 billion were used to fund the MIP and the remainder was used for AIG's general

corporate purposes. The aggregate amount outstanding includes $1.1 billion loss resulting from foreign exchange translation into U.S. dollars, of which $332 million loss relates to notes issued by AIG for general corporate purposes and $726 million loss relates to notes issued to fund the MIP. AIG has economically hedged the currency exposure arising from its foreign currency denominated notes.

During 2007, AIG issued in Rule 144A offerings an aggregate of $3.0 billion principal amount of senior notes, of which $650 million was used to fund the MIP and $2.3 billion was used for AIG's general corporate purposes.

AIG maintains a shelf registration statement in Japan, providing for the issuance of up to Japanese Yen 300 billion principal amount of senior notes, of which the equivalent of $450 million was outstanding as of December 31, 2007 and was used for AIG's general corporate purposes. AIG also maintains an Australian dollar debt program under which senior notes with an aggregate principal amount of up to 5 billion Australian dollars may be outstanding at any one time. Although as of December 31, 2007 there were no outstanding notes under the Australian program, AIG intends to use the program opportunistically to fund the MIP or for AIG's general corporate purposes.

During 2007, AIG issued an aggregate of $5.6 billion of junior subordinated debentures in five series of securities. Substantially all of the proceeds from these sales, net of expenses, are being used to repurchase shares of AIG's common stock. In connection with each series of junior subordinated debentures, AIG entered into a Replacement Capital Covenant (RCC) for the benefit of the holders of AIG's 6.25 percent senior notes due 2036. The RCCs provide that AIG will not repay, redeem, or purchase the applicable series of junior subordinated debentures on or before a specified date, unless AIG has received qualifying proceeds from the sale of replacement capital securities.

In October 2007, AIG borrowed a total of $500 million on an unsecured basis pursuant to a loan agreement with a third-party bank. The entire amount of the loan remained outstanding at December 31, 2007 and matures in October 2008.

AIG began applying hedge accounting for certain AIG parent transactions in the first quarter of 2007.

AIGFP

AIGFP uses the proceeds from the issuance of notes and bonds and GIA borrowings, as well as the issuance of Series AIGFP notes by AIG, to invest in a diversified portfolio of securities and derivative transactions. The borrowings may also be temporarily invested in securities purchased under agreements to resell. AIGFP's notes and bonds include structured debt instruments whose payment terms are linked to one or more financial or other indices (such as an equity index or commodity index or another measure that is not considered to be clearly and closely related to the debt instrument). These notes contain embedded derivatives that otherwise would be required to be accounted for separately under FAS 133. Upon AIG's early adoption of FAS 155, AIGFP elected the fair value option for these notes. The notes that are accounted for using the fair value option are reported separately under hybrid financial instrument liabilities. AIG guarantees the obligations of AIGFP under AIGFP's notes and bonds and GIA borrowings. See Liquidity herein and Note 8 to Consolidated Financial Statements.

AIGFP has a Euro medium-term note program under which an aggregate nominal amount of up to $20.0 billion of notes may be outstanding at any one time. As of December 31, 2007, $6.2 billion of notes were outstanding under the program. The notes issued under this program are guaranteed by AIG and are included in AIGFP's notes and bonds payable in the table of total borrowings.

AIG Funding

AIG Funding, Inc. (AIG Funding) issues commercial paper that is guaranteed by AIG in order to help fulfill the short-term cash requirements of AIG and its subsidiaries. The issuance of AIG Funding's commercial paper, including the guarantee by AIG, is subject to the approval of AIG's Board of Directors or the Finance Committee of the Board if it exceeds certain pre-approved limits.

As backup for the commercial paper program and for other general corporate purposes, AIG and AIG Funding maintain revolving credit facilities, which, as of December 31, 2007, had an aggregate of $9.3 billion available to be drawn and which are summarized below under Revolving Credit Facilities.

ILFC

ILFC fulfills its short-term cash requirements through operating cash flows and the issuance of commercial paper. The issuance of commercial paper is subject to the approval of ILFC's Board of Directors and is not guaranteed by AIG. ILFC maintains syndicated revolving credit facilities which, as of December 31, 2007, totaled $6.5 billion and which are summarized below under Revolving Credit Facilities. These facilities are used as back up for ILFC's maturing debt and other obligations.

As a well-known seasoned issuer, ILFC has filed an automatic shelf registration statement with the SEC allowing ILFC immediate access to the U.S. public debt markets. At December 31, 2007, $4.7 billion of debt securities had been issued under this registration statement and $5.9 billion had been issued under a prior registration statement. In addition, ILFC has a Euro medium-term note program for $7.0 billion, under which $3.8 billion in notes were outstanding at December 31, 2007. Notes issued under the Euro medium-term note program are included in ILFC notes and bonds payable in the preceding table of borrowings. The cumulative foreign exchange adjustment loss for the foreign currency denominated debt resulting from the effect of hedging activities that did not qualify for hedge accounting treatment under FAS 133 was $969 million at December 31, 2007 and $733 million at December 31, 2006. ILFC has substantially eliminated the currency exposure arising from foreign currency denominated notes by economically hedging the portion of the note exposure not already offset by Euro-denominated operating lease payments.

ILFC had a $4.3 billion Export Credit Facility for use in connection with the purchase of approximately 75 aircraft delivered through 2001. This facility was guaranteed by various European Export Credit Agencies. The interest rate varies from

5.75 percent to 5.90 percent on these amortizing ten-year borrowings depending on the delivery date of the aircraft. At December 31, 2007, ILFC had $664 million outstanding under this facility. The debt is collateralized by a pledge of the shares of a subsidiary of ILFC, which holds title to the aircraft financed under the facility.

In May 2004, ILFC entered into a similarly structured Export Credit Facility for up to a maximum of $2.6 billion for Airbus aircraft to be delivered through May 31, 2005. The facility was subsequently increased to $3.6 billion and extended to include aircraft to be delivered through May 31, 2008. The facility becomes available as the various European Export Credit Agencies provide their guarantees for aircraft based on a nine-month forward-looking calendar, and the interest rate is determined through a bid process. At December 31, 2007, ILFC had $1.9 billion outstanding under this facility. Borrowings with respect to these facilities are included in ILFC's notes and bonds payable in the preceding table of borrowings. The debt is collateralized by a pledge of shares of a subsidiary of ILFC, which holds title to the aircraft financed under the facility.

From time to time, ILFC enters into funded financing agreements. As of December 31, 2007, ILFC had a total of $1.1 billion outstanding, which has varying maturities through February 2012. The interest rates are LIBOR-based, with spreads ranging from 0.30 percent to 1.625 percent.

The proceeds of ILFC's debt financing are primarily used to purchase flight equipment, including progress payments during the construction phase. The primary sources for the repayment of this debt and the interest expense thereon are the cash flow from operations, proceeds from the sale of flight equipment and the rollover and refinancing of the prior debt. AIG does not guarantee the debt obligations of ILFC. See also Liquidity herein.

AGF

AGF fulfills most of its short-term cash borrowing requirements through the issuance of commercial paper. The issuance of commercial paper is subject to the approval of AGF's Board of Directors and is not guaranteed by AIG. AGF maintains committed syndicated revolving credit facilities which, as of December 31, 2007, totaled $4.8 billion and which are summarized below under Revolving Credit Facilities. The facilities can be used for general corporate purposes and to provide backup for AGF's commercial paper programs.

In January 2007, AGF issued junior subordinated debentures in an aggregate principal amount of $350 million that mature in January 2067. The debentures underlie a series of trust preferred securities sold by a trust sponsored by AGF in a Rule 144A/ Regulation S offering. AGF can redeem the debentures at par beginning in January 2017.

As of December 31, 2007, notes and bonds aggregating $22.4 billion were outstanding with maturity dates ranging from 2008 to 2031 at interest rates ranging from 1.94 percent to 8.45 percent. To the extent deemed appropriate, AGF may enter into swap transactions to manage its effective borrowing rates with respect to these notes and bonds. As a well-known seasoned issuer, AGF filed an automatic shelf registration statement with the SEC allowing AGF immediate access to the U.S. public debt markets. At December 31, 2007, AGF had remaining corporate authorization to issue up to $8.1 billion of debt securities under its shelf registration statements.

AGF's funding sources include a medium-term note program, private placement debt, retail note issuances, bank financing and securitizations of finance receivables that AGF accounts for as on-balance-sheet secured financings. In addition, AGF has become an established issuer of long-term debt in the international capital markets.

In addition to debt refinancing activities, proceeds from the collection of finance receivables are used to fund cash needs including the payment of principal and interest on AGF's debt. AIG does not guarantee any of the debt obligations of AGF. See also Liquidity.

AIGCFG

AIGCFG has a variety of funding mechanisms for its various markets, including retail and wholesale deposits, short and long-term bank loans, securitizations and intercompany subordinated debt. AIG Credit Card Company (Taiwan), a consumer finance business in Taiwan, and AIG Retail Bank PLC, a full service consumer bank in Thailand, have issued commercial paper for the funding of their respective operations. AIG does not guarantee any borrowings for AIGCFG businesses, including this commercial paper.

Revolving Credit Facilities

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

As of December 31, 2007 *(in millions)*

Facility	Size	Borrower(s)	Available Amount	Expiration	One-Year Term-Out Option
AIG:					
364-Day Syndicated Facility	$2,125	AIG/AIG Funding[a] AIG Capital Corporation[a]	$ 2,125	July 2008	Yes
5-Year Syndicated Facility	1,625	AIG/AIG Funding[a] AIG Capital Corporation[a]	1,625	July 2011	No
364-Day Bilateral Facility[b]	3,200	AIG/AIG Funding	210	December 2008	Yes
364-Day Intercompany Facility[c]	5,335	AIG	5,335	September 2008	Yes
Total AIG	$12,285		$ 9,295		
ILFC:					
5-Year Syndicated Facility	$2,500	ILFC	$ 2,500	October 2011	No
5-Year Syndicated Facility	2,000	ILFC	2,000	October 2010	No
5-Year Syndicated Facility	2,000	ILFC	2,000	October 2009	No
Total ILFC	$6,500		$ 6,500		
AGF:					
364-Day Syndicated Facility	$2,625	American General Finance Corporation American General Finance, Inc.[d]	$ 2,625	July 2008	Yes
5-Year Syndicated Facility	2,125	American General Finance Corporation	2,125	July 2010	No
Total AGF	$4,750		$ 4,750		

(a) Guaranteed by AIG.

(b) This facility can be drawn in the form of loans or letters of credit. All drawn amounts shown above are in the form of letters of credit.

(c) Subsidiaries of AIG are the lenders on this facility.

(d) American General Finance, Inc. is an eligible borrower for up to $400 million only.

Credit Ratings

The cost and availability of unsecured financing for AIG and its subsidiaries are generally dependent on their short- and long-term debt ratings. The following table presents the credit ratings of AIG and certain of its subsidiaries as of February 15, 2008. In parentheses, following the initial occurrence in the table of each rating, is an indication of that rating's relative rank within the agency's rating categories. That ranking refers only to the generic or major rating category and not to the modifiers appended to the rating by the rating agencies to denote relative position within such generic or major category.

	Short-term Debt			Senior Long-term Debt		
	Moody's	S&P	Fitch	Moody's[a]	S&P[b]	Fitch[c]
AIG	P-1 (1st of 3)	A-1+ (1st of 6)	F1+ (1st of 5)	Aa2[e](2nd of 9)	AA (2nd of 8)[f]	AA (2nd of 9)[h]
AIG Financial Products Corp.[d]	P-1	A-1+	—	Aa2[e]	AA[f]	—
AIG Funding, Inc.[d]	P-1	A-1+	F1+	—	—	—
ILFC	P-1	A-1+	F1 (1st of 5)	A1 (3rd of 9)	AA- (2nd of 8)[g]	A+ (3rd of 9)[h]
American General Finance Corporation	P-1	A-1 (1st of 6)	F1	A1	A+ (3rd of 8)	A+[h]
American General Finance, Inc.	P-1	A-1	F1	—	—	A+[h]

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

(b) Standard & Poor's, a division of the McGraw-Hill Companies (S&P) ratings may be modified by the addition of a plus or minus sign to show relative standing within the major rating categories.

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

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

(e) Negative rating outlook on Senior Unsecured Debt Ratings. A negative outlook by Moody's indicates that a rating may be lowered but is not necessarily a precursor of a ratings change.

(f) Negative rating outlook on Counterparty Credit Ratings. A negative outlook by S&P indicates that a rating may be lowered but is not necessarily a precursor of a ratings change.

(g) Negative rating outlook on Corporate Credit Rating. A negative outlook by S&P indicates that a rating may be lowered but is not necessarily a precursor of a ratings change.

(h) Issuer Default and Senior Unsecured Debt Ratings on Rating Watch Negative. Rating Watch Negative indicates that a rating has been placed on active rating watch status.

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

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

AIG believes that any of its own or its subsidiaries' contractual obligations that are subject to ''ratings triggers'' or financial covenants relating to ''ratings triggers'' would not have a material adverse effect on its financial condition or liquidity. Ratings downgrades could also trigger the application of termination provisions in certain of AIG's contracts, principally agreements entered into by AIGFP and assumed reinsurance contracts entered into by Transatlantic.

It is estimated that, as of the close of business on February 14, 2008, based on AIGFP's outstanding municipal GIAs and financial derivatives transactions as of such date, a downgrade of AIG's long-term senior debt ratings to 'Aa3' by Moody's or 'AA – ' by S&P would permit counterparties to call for approximately $1.39 billion of collateral. Further, additional downgrades could result in requirements for substantial additional collateral, which could have a material effect on how AIGFP manages its liquidity. The actual amount of additional collateral that AIGFP would be required to post to counterparties in the event of such downgrades depends on market conditions, the fair value of the outstanding affected transactions and other factors prevailing at the time of the downgrade. Additional obligations to post collateral would increase the demand on AIGFP's liquidity.

Contractual Obligations

Contractual obligations in total, and by remaining maturity at December 31, 2007 were as follows:

(in millions)	Total Payments	Payments due by Period: Less Than One Year	1-3 Years	3+-5 Years	Over Five Years
Borrowings[a]	$ 156,014	$ 43,891	$ 32,261	$ 26,032	$ 53,830
Interest payments on borrowings	83,551	5,326	8,899	7,073	62,253
Loss reserves[b]	85,500	23,513	26,078	12,397	23,512
Insurance and investment contract liabilities[c]	645,583	32,359	42,768	42,282	528,174
GIC liabilities[d]	29,797	9,266	8,052	3,458	9,021
Aircraft purchase commitments	20,104	4,174	3,852	2,095	9,983
Operating leases	4,426	747	1,041	693	1,945
Other purchase obligations[e]	1,091	1,056	35	—	—
Total[f]	$1,026,066	$120,332	$122,986	$ 94,030	$688,718

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

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

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

(d) Represents guaranteed maturities under GICs.

(e) Includes a $1.0 billion commitment to purchase shares under AIG's share repurchase program which was paid in January 2008 and options to acquire aircraft.

(f) Does not reflect unrecognized tax benefits of $1.3 billion, the timing of which is uncertain. However, it is reasonably possible that $50 million to $150 million may become payable during 2008. See Note 21 to Consolidated Financial Statements for a discussion on unrecognized tax benefits.

Off Balance Sheet Arrangements and Commercial Commitments

Off Balance Sheet Arrangements and Commercial Commitments in total, and by remaining maturity at December 31, 2007 were as follows:

(in millions)	Total Amounts Committed	Amount of Commitment Expiration: Less Than One Year	1-3 Years	3+-5 Years	Over Five Years
Guarantees:					
Liquidity facilities[a]	$ 2,495	$ 8	$ 8	$ 1,503	$ 976
Standby letters of credit	1,713	1,485	42	38	148
Construction guarantees[b]	687	—	—	—	687
Guarantees of indebtedness	1,124	106	83	500	435
All other guarantees	767	249	8	35	475
Commitments:					
Investment commitments[c]	9,071	3,527	3,604	1,684	256
Commitments to extend credit	1,325	496	591	238	—
Letters of credit	1,196	910	6	121	159
Investment protection agreements[d]	11,991	3,088	2,094	855	5,954
Maturity shortening puts[e]	2,333	1,234	1,099	—	—
Other commercial commitments	1,269	114	111	83	961
Total[f]	$ 33,971	$ 11,217	$ 7,646	$ 5,057	$ 10,051

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

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

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

(d) Written generally with respect to investments in hedge funds and funds of hedge funds.

(e) Represents obligations under 2a-7 Puts to purchase certain multi-sector CDOs at pre-determined contractual prices.

(f) Excludes commitments with respect to pension plans. The annual pension contribution for 2008 is expected to be approximately $118 million for U.S. and non-U.S. plans.

Arrangements with Variable Interest Entities

AIG enters into various off-balance-sheet (unconsolidated) arrangements with variable interest entities (VIEs) in the normal course of business. AIG's involvement with VIEs ranges from being a passive investor to designing and structuring, warehousing and managing the collateral of VIEs. AIG engages in transactions with VIEs as part of its investment activities to obtain funding and to facilitate client needs. AIG purchases debt securities (rated and unrated) and equity interests issued by VIEs, makes loans and provides other credit support to VIEs, enters into insurance, reinsurance and derivative transactions and leasing arrangements with VIEs, and acts as the warehouse agent and collateral manager for VIEs.

Under FIN 46(R), AIG consolidates a VIE when it is the primary beneficiary of the entity. The primary beneficiary is the party that either (i) absorbs a majority of the VIE's expected losses; (ii) receives a majority of the VIE's expected residual returns; or (iii) both. For a further discussion of AIG's involvement with VIEs, see Note 7 of Notes to Consolidated Financial Statements.

A significant portion of AIG's overall exposure to VIEs results from AIG Investment's real estate and investment funds.

In certain instances, AIG Investments acts as the collateral manager or general partner of an investment fund, private equity fund or hedge fund. Such entities are typically registered investment companies or qualify for the specialized investment company accounting in accordance with the AICPA Investment Company Audit and Accounting Guide. For investment partnerships, hedge funds and private equity funds, AIG acts as the general partner or manager of the fund and is responsible for carrying out the investment mandate of the VIE. Often, AIG's insurance operations participate in these AIG managed structures as a passive investor in the debt or equity issued by the VIE. Typically, AIG does not provide any guarantees to the investors in the VIE.

The following table summarizes, by investment activity, AIG's involvement with VIEs. Maximum exposure to loss, as detailed in the table below, is considered to be the notional amount of credit lines, guarantees and other credit support, and liquidity facilities, notional amounts of credit default swaps and certain total return swaps, and the amount invested in the debt or equity issued by the VIEs.

(As of December 31,)	Primary Beneficiary		Significant Variable Interest Holder*	
	Total Assets		Total Assets	Maximum Exposure to Loss
(in billions)	2007	2006	2007	2007
Description				
Real estate and investment funds	**$21.7**	$6.1	**$139.0**	**$18.5**
Tax planning VIEs	**0.5**	1.4	**12.1**	**6.3**
CLOs/CDOs/CBOs	**0.4**	—	**107.8**	**9.7**
Affordable housing partnerships	**2.7**	—	**0.9**	**0.9**
Other	**1.7**	1.6	**15.3**	**9.2**
Total	**$27.0**	$9.1	**$275.1**	**$44.6**

* *Includes $2.4 billion of assets held in an unconsolidated SIV sponsored by AIGFP in 2007. As of December 31, 2007, AIGFP's invested assets included $1.7 billion of securities purchased under agreements to resell, commercial paper and medium-term and capital notes issued by this entity.*

Following is additional information concerning AIG's involvement with collateralized debt obligations and its structured investment vehicle.

Collateralized Debt Obligations

In the normal course of its asset management operations, AIG manages or sponsors CDOs which issue debt and equity interests sold to third party investors. AIG's subsidiaries also invest in the debt and equity securities issued by these CDOs as part of their normal investment activities. AIG also invests in and manages CDOs sponsored by third parties, warehouses assets prior to the establishment of and sale of the warehoused assets to a CDO, enters into derivative contracts with CDOs, including credit default swaps, and acts as an asset manager to CDOs.

Categories of assets owned by these CDOs include residential and commercial mortgage and other asset-backed securities, corporate loans, high-yield and high-grade loans and bonds, and credit default contracts, among other assets, that have ratings ranging from AAA to unrated. AIGFP's portfolio of multi-sector CDOs and, to a lesser extent, certain AIG insurance subsidiaries' direct investments in CDOs, have experienced some downgrades within their asset portfolios. AIG does not expect that it will have to consolidate any of these structures.

These CDOs typically are funded with commercial paper, medium and long-term financing and equity with ratings that range from AAA to unrated. AIG has no obligation to purchase, and has not purchased, any commercial paper issued by these CDOs or provided any support to these CDOs in obtaining financing, and does not intend to do so. However, AIGFP has written the 2a-7 Puts which are included as part of its multi-sector credit default swap portfolio. Under the terms of these securities the holders are permitted or required, in certain circumstances, on a regular basis to tender their securities to the issuers at par. If an issuer's remarketing agent is unable to resell

the securities so tendered within the maximum interest rate spread range specified in the terms of the securities, AIGFP must purchase the securities at par as long as the securities have not experienced a default. During 2007, AIGFP purchased securities with a principal amount of approximately $754 million in connection with these obligations. In respect of certain of the 2a-7 Puts, AIGFP has contracted with third parties to provide liquidity for the securities if they are put to AIGFP for up to a three-year period. Such liquidity facilities totaled approximately $3 billion at December 31, 2007. As of February 26, 2008, AIGFP has not utilized these liquidity facilities. At December 31, 2007, AIGFP had approximately $6.5 billion of notional exposure on these 2a-7 Puts.

Structured Investment Vehicle

AIGFP sponsors one unconsolidated SIV that invests in variable rate, investment-grade debt securities with a weighted average remaining life of four years at December 31, 2007. Assets of the SIV totaled $2.4 billion at December 31, 2007. Approximately $31.9 million of these assets have been downgraded one notch from Aa3/AA– to A1/A+ by Moody's and S&P, respectively, since the purchase of these assets by the SIV. The SIV funds its assets by issuing secured financing, commercial paper, and medium-term notes that had a weighted-average remaining life of less than six months at December 31, 2007. The mismatch between the weighted average remaining life of the SIV's assets and liabilities has been removed through the funding support from AIGFP described in the next paragraph. The SIV also issued approximately $300 million of capital notes originally rated Baa2 and BBB by Moody's and S&P, respectively, and subsequently downgraded in 2007 to B3 and BB– (credit watch negative), respectively, of which AIGFP owns 12 percent.

At December 31, 2007, AIGFP had $1.7 billion of balance sheet exposure to this SIV representing investments in securities purchased under agreements to resell, commercial paper, and medium-term and capital notes. During the credit market disruptions during the last half of 2007, the SIV experienced difficulty attracting purchasers for its commercial paper and medium-term notes. In January 2008, AIGFP agreed to provide funding support to the SIV, as necessary, to allow the SIV to redeem its commercial paper and medium-term notes as they become due. Moody's affirmed the SIV's senior debt ratings of Aaa. S&P affirmed the SIV's long term issuer credit rating of AAA with a negative outlook and downgraded its capital notes from BB– to CCC– and this rating remains on credit watch negative. AIG does not believe its management of, and current or future investments in, the SIV could have any effect on AIG's debt ratings under any circumstances.

Shareholders' Equity

The changes in AIG's consolidated shareholders' equity during 2007 and 2006 follows:

(in millions)	**2007**	2006
Beginning of year	**$101,677**	$ 86,317
Net income	**6,200**	14,048
Unrealized appreciation (depreciation) of investments, net of tax	**(5,708)**	1,735
Cumulative translation adjustment, net of tax	**1,185**	936
Dividends to shareholders	**(1,964)**	(1,690)
Payments advanced to purchase shares, net	**(912)**	—
Share purchases	**(5,104)**	—
Other*	**427**	331
End of year	**$ 95,801**	$101,677

* *Reflects the effects of employee stock transactions and cumulative effect of accounting changes.*

As indicated in the table above, a significant portion of the 2007 decrease in AIG's consolidated equity during 2007 was the result of share purchases, substantially all of which were funded from the issuance of hybrid debt securities. The effect of these transactions was to replace high cost equity securities (common stock) with cost efficient hybrid securities, a substantial portion of which is treated as equity capital for the purpose of rating agency leverage calculations.

AIG has in the past reinvested most of its unrestricted earnings in its operations and believes such continued reinvestment in the future will be adequate to meet any foreseeable capital needs. However, AIG may choose from time to time to raise additional funds through the issuance of additional securities.

In February 2007, AIG's Board of Directors adopted a new dividend policy, which took effect with the dividend declared in the second quarter of 2007, providing that under ordinary circumstances, AIG's plan will be to increase its common stock dividend by approximately 20 percent annually. The payment of any dividend, however, is at the discretion of AIG's Board of Directors, and the future payment of dividends will depend on various factors, including the performance of AIG's businesses, AIG's consolidated financial position, results of operations and liquidity and the existence of investment opportunities.

Share Repurchases

From time to time, AIG may buy shares of its common stock for general corporate purposes, including to satisfy its obligations under various employee benefit plans. In February 2007, AIG's Board of Directors increased AIG's share repurchase program by authorizing the purchase of shares with an aggregate purchase price of $8 billion. In November 2007, AIG's Board of Directors authorized the purchase of an additional $8 billion in common stock. From March through December 31, 2007, AIG entered into structured share repurchase arrangements providing for the purchase of shares over time with an aggregate purchase price of

$7 billion, including a $1.0 billion commitment entered into in December 2007 but not funded until January 2008.

A total of 76,361,209 shares were purchased during 2007. The portion of the payments advanced by AIG under the structured share repurchase arrangements that had not yet been utilized to repurchase shares at December 31, 2007, amounting to $912 million, has been recorded as a component of shareholders' equity under the caption, Payments advanced to purchase shares. Purchases have continued subsequent to December 31, 2007, with an additional 12,196,187 shares purchased from January 1 through February 15, 2008. All shares purchased are recorded as treasury stock at cost.

At February 15, 2008, $10.25 billion was available for purchases under the aggregate authorization. AIG does not expect to purchase additional shares under its share repurchase program for the foreseeable future, other than to meet commitments that existed at December 31, 2007.

Dividends from Insurance Subsidiaries

Payments of dividends to AIG by its insurance subsidiaries are subject to certain restrictions imposed by regulatory authorities. With respect to AIG's domestic insurance subsidiaries, the payment of any dividend requires formal notice to the insurance department in which the particular insurance subsidiary is domiciled. Under the laws of many states, an insurer may pay a dividend without prior approval of the insurance regulator when the amount of the dividend is below certain regulatory thresholds. Other foreign jurisdictions, notably Bermuda, Japan, Hong Kong, Taiwan, the U.K., Thailand and Singapore, may restrict the ability of AIG's foreign insurance subsidiaries to pay dividends. Largely as a result of these restrictions, approximately 81 percent of the aggregate equity of AIG's consolidated subsidiaries was restricted from immediate transfer to AIG parent at December 31, 2007. See Regulation and Supervision herein. AIG cannot predict how recent regulatory investigations may affect the ability of its regulated subsidiaries to pay dividends. To AIG's knowledge, no AIG company is currently on any regulatory or similar ''watch list'' with regard to solvency. See also Liquidity herein, Note 12 to Consolidated Financial Statements and Item 1A. Risk Factors — Liquidity.

Regulation and Supervision

AIG's insurance subsidiaries, in common with other insurers, are subject to regulation and supervision by the states and jurisdictions in which they do business. In the United States, the NAIC has developed Risk-Based Capital (RBC) requirements. RBC relates an individual insurance company's statutory surplus to the risk inherent in its overall operations.

AIG's insurance subsidiaries file financial statements prepared in accordance with statutory accounting practices prescribed or permitted by domestic and foreign insurance regulatory authorities. The principal differences between statutory financial statements and financial statements prepared in accordance with U.S. GAAP for domestic companies are that statutory financial statements do not reflect DAC, some bond portfolios may be carried at amortized cost, assets and liabilities are presented net of reinsurance, policyholder liabilities are valued using more conservative assumptions and certain assets are non-admitted.

In connection with the filing of the 2005 statutory financial statements for AIG's Domestic General Insurance companies, AIG agreed with the relevant state insurance regulators on the statutory accounting treatment of various items. The regulatory authorities have also permitted certain of the domestic and foreign insurance subsidiaries to support the carrying value of their investments in certain non-insurance and foreign insurance subsidiaries by utilizing the AIG audited consolidated financial statements to satisfy the requirement that the U.S. GAAP-basis equity of such entities be audited. In addition, the regulatory authorities have permitted the Domestic General Insurance companies to utilize audited financial statements prepared on a basis of accounting other than U.S. GAAP to value investments in joint ventures, limited partnerships and hedge funds. AIG has received similar permitted practices authorizations from insurance regulatory authorities in connection with the 2007 and 2006 statutory financial statements. These permitted practices did not affect the Domestic General Insurance companies' compliance with minimum regulatory capital requirements.

Statutory capital of each company continued to exceed minimum company action level requirements following the adjustments, but AIG nonetheless contributed an additional $750 million of capital into American Home effective September 30, 2005 and contributed a further $2.25 billion of capital in February 2006 for a total of approximately $3 billion of capital into Domestic General Insurance subsidiaries effective December 31, 2005. To enhance their current capital positions, AIG suspended dividends from the DBG companies from the fourth quarter 2005 through 2006, dividend payments resumed in the first quarter of 2007. AIG believes it has the capital resources and liquidity to fund any necessary statutory capital contributions.

As discussed under Item 3. Legal Proceedings, various regulators have commenced investigations into certain insurance business practices. In addition, the OTS and other regulators routinely conduct examinations of AIG and its subsidiaries, including AIG's consumer finance operations. AIG cannot predict the ultimate effect that these investigations and examinations, or any additional regulation arising therefrom, might have on its business. Federal, state or local legislation may affect AIG's ability to operate and expand its various financial services businesses, and changes in the current laws, regulations or interpretations thereof may have a material adverse effect on these businesses.

AIG's U.S. operations are negatively affected under guarantee fund assessment laws which exist in most states. As a result of operating in a state which has guarantee fund assessment laws, a solvent insurance company may be assessed for certain obligations arising from the insolvencies of other insurance companies which operated in that state. AIG generally records these assessments upon notice. Additionally, certain states permit at least a portion of the assessed amount to be used as a credit against a company's future premium tax liabilities. Therefore, the ultimate net assessment cannot reasonably be estimated. The guarantee fund assessments net of credits recognized

in 2007, 2006 and 2005, respectively, were $87 million, $97 million and $124 million.

AIG is also required to participate in various involuntary pools (principally workers compensation business) which provide insurance coverage for those not able to obtain such coverage in the voluntary markets. This participation is also recorded upon notification, as these amounts cannot reasonably be estimated.

A substantial portion of AIG's General Insurance business and a majority of its Life Insurance & Retirement Services business are conducted in foreign countries. The degree of regulation and supervision in foreign jurisdictions varies. Generally, AIG, as well as the underwriting companies operating in such jurisdictions, must satisfy local regulatory requirements. Licenses issued by foreign authorities to AIG subsidiaries are subject to modification and revocation. Thus, AIG's insurance subsidiaries could be prevented from conducting future business in certain of the jurisdictions where they currently operate. AIG's international operations include operations in various developing nations. Both current and future foreign operations could be adversely affected by unfavorable political developments up to and including nationalization of AIG's operations without compensation. Adverse effects resulting from any one country may affect AIG's results of operations, liquidity and financial condition depending on the magnitude of the event and AIG's net financial exposure at that time in that country.

Foreign insurance operations are individually subject to local solvency margin requirements that require maintenance of adequate capitalization, which AIG complies with by country. In addition, certain foreign locations, notably Japan, have established regulations that can result in guarantee fund assessments. These have not had a material effect on AIG's financial condition or results of operations.

Liquidity

AIG manages liquidity at both the subsidiary and parent company levels. At December 31, 2007, AIG's consolidated invested assets included $65.6 billion in cash and short-term investments. Consolidated net cash provided from operating activities in 2007 amounted to $35.2 billion. At both the subsidiary and parent company level, liquidity management activities are intended to preserve and enhance funding stability, flexibility, and diversity through a wide range of potential operating environments and market conditions.

As a result of market disruption in the credit markets, AIG took steps to enhance the liquidity of its portfolios. Cash and short-term investments increased in all of AIG's major operating segments. In addition, AIG created an interdisciplinary Liquidity Risk Committee to measure, monitor, control and aggregate liquidity risks across AIG. While this Committee's responsibilities are broad, the Committee's initial focus is on portfolios with shorter-term contractual liabilities, such as securities lending in the United States and retail deposit-like products in the United Kingdom.

Management believes that AIG's liquid assets, cash provided by operations and access to the capital markets will enable it to meet its anticipated cash requirements, including the funding of increased dividends under AIG's current dividend policy. See also Item 1A. Risk Factors — Liquidity and Risk Management herein.

Insurance Operations

Insurance operating cash flow is derived from two sources, underwriting operations and investment operations. Cash flow from underwriting operations includes collections of periodic premiums and policyholders' contract deposits, and paid loss recoveries, less reinsurance premiums, losses, benefits, and acquisition and operating expenses. Generally, there is a time lag from when premiums are collected and losses and benefits are paid. Investment cash flow is primarily derived from interest and dividends received and includes realized capital gains net of realized capital losses.

Liquid assets include cash and short-term investments, fixed maturities that are not designated as held to maturity, and publicly traded equity securities. At December 31, 2007 and 2006, AIG's insurance operations had liquid assets of $476.1 billion and $428.4 billion, respectively. The portion of liquid assets comprised of cash and short-term investments was $45.5 billion and $19.9 billion at December 31, 2007 and 2006, respectively. At December 31, 2007, $380.9 billion, or 95 percent of the fixed maturity investments that were not designated as held to maturity in AIG's insurance company general account portfolios were rated investment grade. Given the size and liquidity profile of AIG's investment portfolios, AIG believes that deviations from its projected claim experience do not constitute a significant liquidity risk. AIG's asset/liability management process takes into account the expected maturity of investments and expected benefit payments and policy surrenders as well as the specific nature and risk profile of these liabilities. Historically, there has been no significant variation between the expected maturities of AIG's investments and the payment of claims.

See also Operating Review — General Insurance Operations — General Insurance Net Investment Income and Life Insurance & Retirement Services Operations — Life Insurance & Retirement Services Net Investment Income and Realized Capital Gains (Losses) herein.

General Insurance

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

Life Insurance & Retirement Services

Life Insurance & Retirement Services operating cash flow is derived from underwriting and investment activities. If a substantial portion of the Life Insurance & Retirement Services operations bond portfolio diminished significantly in value and/or defaulted, AIG might need to liquidate other portions of its Life Insurance & Retirement Services investment portfolio and/or arrange financing. Possible events causing such a liquidity strain could include economic collapse of a nation or region in which Life Insurance & Retirement Services operations exist, nationalization, catastrophic terrorist acts, or other economic or political upheaval. In addition, a significant rise in interest rates in a particular region or regions leading to a major increase in policyholder surrenders could also create a liquidity strain.

Financial Services

AIG's major Financial Services operating subsidiaries consist of AIGFP, ILFC, AGF and AIGCFG. Sources of funds considered in meeting the liquidity needs of AIGFP's operations include GIAs, issuance of long- and short-term debt, proceeds from maturities, sales of securities available for sale and securities and spot commodities leased or sold under repurchase agreements. ILFC, AGF and AIGCFG utilize the commercial paper markets, bank loans and bank credit facilities as sources of liquidity. ILFC and AGF also fund in the domestic and international capital markets without reliance on any guarantee from AIG. An additional source of liquidity for ILFC is the use of export credit facilities. AIGCFG also uses wholesale and retail bank deposits as sources of funds. On occasion, AIG has provided equity capital to ILFC, AGF and AIGCFG and provides intercompany loans to AIGCFG.

Financial Services liquidity could be impaired by an inability to access the capital markets or by collateral calls. The credit default swaps written by AIGFP on super senior tranches of multi-sector CDOs require, in most cases, physical settlement following an event constituting a failure to pay in respect of the underlying super senior CDO securities. The majority of the other credit default swaps are cash settled, whereby AIGFP would be required upon an event constituting a failure to pay in respect of the underlying super senior CDO securities to make cash payments to the counterparty equal to any actual losses that attach to the super senior risk layer, rather than to purchase the reference obligation. Additionally, certain of the credit default swaps are subject to collateral call provisions. In the case of such swaps written on CDOs, the amount of the collateral to be posted is determined based on the value of the CDO securities referenced in the documentation for the credit default swaps.

Asset Management

Asset Management's sources of funds include cash flows from investment management fees, carried interest and returns on various investments. These investments are financed through the issuance of AIG debt in the MIP, the issuance of GICs and funding from AIG. From time to time, AIG Investments utilizes temporary debt funding from AIG primarily to acquire warehoused investments. Subsequent to the initial investment, there are generally no liquidity demands with respect to these warehoused investments. To the extent adverse market conditions prevent AIG Investments from transferring or otherwise divesting these warehoused investments, repayment of the temporary equity funding provided by AIG would be delayed until the investment is transferred or otherwise divested.

AIG Investments incurs expenses associated with cash outflows from the operation of its business, including costs related to portfolio management and related back and middle office costs. In addition, cash is used in association with investment warehousing activities wherein AIG Investments funds and temporarily holds an investment until transferred, sold or otherwise divested.

Cash needs for the Spread-Based Investment business are principally the result of GIC maturities. Significant blocks of the GIC portfolio will mature over the next five years. AIG utilizes asset liability matching to control liquidity risks associated with this business. In addition, AIG believes that its products incorporate certain restrictions which encourage persistency, limiting the magnitude of unforeseen early surrenders in the GIC portfolio.

Liquidity for Asset Management operations can be affected by significant credit or geopolitical events that might cause a delay in fund closings, securitizations or an inability of AIG's clients to fund their capital commitments.

AIG (Parent Company)

The liquidity of the parent company is principally derived from its subsidiaries. The primary sources of cash flow are dividends and other payments from its regulated and unregulated subsidiaries, as well as issuance of debt securities. Primary uses of cash flow are for debt service, subsidiary funding, shareholder dividend payments and common stock repurchases. In 2007, AIG parent collected $4.9 billion in dividends and other payments from subsidiaries (primarily from insurance company subsidiaries), issued $11.7 billion of debt and retired $865 million of debt, excluding MIP and Series AIGFP debt. AIG parent also advanced $6 billion for structured share repurchase arrangements. Excluding MIP and Series AIGFP debt, AIG parent made interest payments totaling $550 million, made $5.90 billion in capital contributions to subsidiaries, and paid $1.93 billion in dividends to shareholders in 2007. In February 2008, AIG contributed approximately $445 million in the form of forgiveness of Federal income tax recoverables to certain domestic general insurance subsidiaries and $500 million to certain domestic life insurance subsidiaries, both effective December 31, 2007.

AIG parent funds its short-term working capital needs through commercial paper issued by AIG Funding. As of December 31, 2007, AIG Funding had $4.2 billion of commercial paper outstanding with an average maturity of 29 days. As additional liquidity, AIG parent and AIG Funding maintain committed revolving credit facilities that, as of December 31, 2007, had an aggregate of $9.3 billion available to be drawn, and which are summarized above under Revolving Credit Facilities.

At the parent company level, liquidity management activities are conducted in a manner intended to preserve and enhance funding stability, flexibility, and diversity through the full range of

potential operating environments and market conditions. Assessing liquidity risk involves forecasting of cash inflows and outflows on both a short- and long-term basis. Corporate Treasury is responsible for formulating the parent company's liquidity and contingency planning efforts, as well as for execution of AIG's specific funding activities. Through active liquidity management, AIG seeks to retain stable, reliable and cost-effective funding sources. In addition to current liquidity requirements, factors which affect funding decisions include market conditions, prevailing interest rates and the desired maturity profile of liabilities. The objectives of contingency planning are to ensure maintenance of appropriate liquidity during normal and stressed periods, to measure and project funding requirements during periods of stress, and to manage access to funding sources. Diversification of funding sources is an important element of AIG's liquidity risk management approach.

AIG's liquidity could be impaired by an inability to access the capital markets or by unforeseen significant outflows of cash. This situation may arise due to circumstances that AIG may be unable to control, such as a general market disruption or an operational problem that affects third parties or AIG. Regulatory and other legal restrictions may limit AIG's ability to transfer funds freely, either to or from its subsidiaries. In particular, many of AIG's subsidiaries, including its insurance subsidiaries, are subject to laws and regulations that authorize regulatory bodies to block or reduce the flow of funds to the parent holding company, or that prohibit such transfers altogether in certain circumstances. These laws and regulations may hinder AIG's ability to access funds that it may need to make payments on its obligations. Because of the wide geographic profile of AIG's regulated subsidiaries, management believes that these cash flows represent a diversified source of liquidity for AIG. For a further discussion of the regulatory environment in which AIG subsidiaries operate and other issues affecting AIG's liquidity, see Item 1A. Risk Factors.

Invested Assets

The following tables summarize the composition of AIG's invested assets by segment:

(in millions)	General Insurance	Life Insurance & Retirement Services	Financial Services	Asset Management	Other	Total
2007						
Fixed maturities:						
Bonds available for sale, at fair value	$ 74,057	$294,162	$ 1,400	$27,753	$ —	$397,372
Bonds held to maturity, at amortized cost	21,355	1	—	225	—	21,581
Bond trading securities, at fair value	—	9,948	—	34	—	9,982
Equity securities:						
Common stocks available for sale, at fair value	5,599	11,616	—	609	76	17,900
Common and preferred stocks trading, at fair value	321	21,026	—	29	—	21,376
Preferred stocks available for sale, at fair value	1,885	477	8	—	—	2,370
Mortgage and other loans receivable, net of allowance	13	24,851	1,365	7,442	56	33,727
Financial services assets:						
Flight equipment primarily under operating leases, net of accumulated depreciation	—	—	41,984	—	—	41,984
Securities available for sale, at fair value	—	—	40,305	—	—	40,305
Trading securities, at fair value	—	—	4,197	—	—	4,197
Spot commodities	—	—	238	—	—	238
Unrealized gain on swaps, options and forward transactions	—	—	17,134	—	(692)	16,442
Trade receivables	—	—	6,467	—	—	6,467
Securities purchased under agreements to resell, at contract value	—	—	20,950	—	—	20,950
Finance receivables, net of allowance	—	5	31,229	—	—	31,234
Securities lending invested collateral, at fair value	5,031	57,471	148	13,012	—	75,662
Other invested assets	11,895	19,015	3,663	17,261	6,989	58,823
Short-term investments, at cost	7,356	25,236	12,249	4,919	1,591	51,351
Total investments and financial services assets as shown on the balance sheet	127,512	463,808	181,337	71,284	8,020	851,961
Cash	497	1,000	389	269	129	2,284
Investment income due and accrued	1,431	4,728	29	401	(2)	6,587
Real estate, net of accumulated depreciation	349	976	17	89	231	1,662
Total invested assets*	$129,789	$470,512	$181,772	$72,043	$8,378	$862,494

** At December 31, 2007, approximately 65 percent and 35 percent of invested assets were held in domestic and foreign investments, respectively.*

(in millions)	General Insurance	Life Insurance & Retirement Services	Financial Services	Asset Management	Other	Total
2006						
Fixed maturities:						
Bonds available for sale, at fair value	$ 67,994	$288,018	$ 1,357	$29,500	$ —	$386,869
Bonds held to maturity, at amortized cost	21,437	—	—	—	—	21,437
Bond trading securities, at fair value	1	10,835	—	—	—	10,836
Equity securities:						
Common stocks available for sale, at fair value	4,245	8,705	—	226	80	13,256
Common stocks trading, at fair value	350	14,505	—	—	—	14,855
Preferred stocks available for sale, at fair value	1,884	650	5	—	—	2,539
Mortgage and other loans receivable, net of allowance	17	21,043	2,398	4,884	76	28,418
Financial services assets:						
Flight equipment primarily under operating leases, net of accumulated depreciation	—	—	39,875	—	—	39,875
Securities available for sale, at fair value	—	—	47,205	—	—	47,205
Trading securities, at fair value	—	—	5,031	—	—	5,031
Spot commodities	—	—	220	—	—	220
Unrealized gain on swaps, options and forward transactions	—	—	19,607	—	(355)	19,252
Trade receivables	—	—	4,317	—	—	4,317
Securities purchased under agreements to resell, at contract value	—	—	30,291	—	—	30,291
Finance receivables, net of allowance	—	—	29,573	—	—	29,573
Securities lending invested collateral, at fair value	5,376	50,099	76	13,755	—	69,306
Other invested assets	9,207	13,962	2,212	13,198	3,532	42,111
Short-term investments, at cost	3,281	15,192	2,807	6,198	5	27,483
Total investments and financial services assets as shown on the balance sheet	113,792	423,009	184,974	67,761	3,338	792,874
Cash	334	740	390	118	8	1,590
Investment income due and accrued	1,363	4,378	23	326	1	6,091
Real estate, net of accumulated depreciation	570	698	17	75	26	1,386
Total invested assets[(a)(b)]	$116,059	$428,825	$185,404	$68,280	$3,373	$801,941

(a) Certain reclassifications and format changes have been made to prior period amounts to conform to the current period presentation.
(b) At December 31, 2006, approximately 68 percent and 32 percent of invested assets were held in domestic and foreign investments, respectively.

Investment Strategy

AIG's investment strategies are tailored to the specific business needs of each operating unit. The investment objectives are driven by the business model for each of the businesses: General Insurance, Life Insurance, Retirement Services and Asset Management's Spread-Based Investment business. The primary objectives are in terms of preservation of capital, growth of surplus and generation of investment income to support the insurance products. At the local operating unit level, the strategies are based on considerations that include the local market, liability duration and cash flow characteristics, rating agency and regulatory capital considerations, legal investment limitations, tax optimization and diversification. In addition to local risk management considerations, AIG's corporate risk management guidelines impose limitations on concentrations to promote diversification by industry, asset class and geographic sector.

The amortized cost or cost and estimated fair value of AIG's available for sale and held to maturity securities at December 31, 2007 and 2006 were as follows:

	December 31, 2007*				December 31, 2006			
(in millions)	Amortized Cost or Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value	Amortized Cost or Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Available for sale:*								
U.S. government and government sponsored entities	**$ 7,956**	**$ 333**	**$ 37**	**$ 8,252**	$ 7,667	$ 221	$ 140	$ 7,748
Obligations of states, municipalities and political subdivisions	**46,087**	**927**	**160**	**46,854**	59,785	1,056	210	60,631
Non-U.S. governments	**67,023**	**3,920**	**743**	**70,200**	62,860	5,461	437	67,884
Corporate debt	**239,822**	**6,216**	**4,518**	**241,520**	257,383	7,443	2,536	262,290
Mortgage-backed, asset-backed and collateralized	**140,982**	**1,221**	**7,703**	**134,500**	104,687	502	362	104,827
Total bonds	**$501,870**	**$12,617**	**$13,161**	**$501,326**	$492,382	$14,683	$3,685	$ 503,380
Equity securities	**15,188**	**5,545**	**463**	**20,270**	13,147	2,807	159	15,795
Total	**$517,058**	**$18,162**	**$13,624**	**$521,596**	$505,529	$17,490	$3,844	$ 519,175
Held to maturity:*								
Bonds — Obligations of states, municipalities and political subdivisions	**$ 21,581**	**$ 609**	**$ 33**	**$ 22,157**	$ 21,437	$ 731	$ 14	$ 22,154

** At December 31, 2007 and 2006, fixed maturities held by AIG that were below investment grade or not rated totaled $27.0 billion and $26.6 billion, respectively.*

AIG's held to maturity and available for sale fixed maturity investments totaled $523.5 billion at December 31, 2007, compared to $525.5 billion at December 31, 2006. At December 31, 2007, approximately 63 percent of the fixed maturities investments were in domestic portfolios. Approximately 53 percent of such domestic securities were rated AAA by one or more of the principal rating agencies. Approximately five percent were below investment grade or not rated. AIG's investment decision process relies primarily on internally generated fundamental analysis and internal risk ratings. Third party rating services' ratings and opinions provide one source of independent perspectives for consideration in the internal analysis.

A significant portion of the foreign fixed income portfolio is rated by Moody's, S&P or similar foreign rating services. Rating services are not available in all overseas locations. The Credit Risk Committee (CRC) closely reviews the credit quality of the foreign portfolio's non-rated fixed income investments. At December 31, 2007, approximately 19 percent of the foreign fixed income investments were either rated AAA or, on the basis of AIG's internal analysis, were equivalent from a credit standpoint to securities so rated. Approximately five percent were below investment grade or not rated at that date. A large portion (approximately one third) of the foreign fixed income portfolio is sovereign fixed maturity securities supporting the policy liabilities in the country of issuance.

The credit ratings of AIG's fixed maturity investments, other than those of AIGFP, at December 31, 2007 and 2006 were as follows:

Rating	2007	2006
AAA	**38%**	37%
AA	**28**	26
A	**18**	20
BBB	**11**	12
Below investment grade	**4**	4
Non-rated	**1**	1
Total	**100%**	100%

The industry categories of AIG's available for sale corporate debt securities at December 31, 2007 were as follows:

Industry Category	Percentage
Industrials	**47%**
Financial Institutions	**42**
Utilities/Other	**11**
Total*	**100%**

** At December 31, 2007 approximately 95% of these investments were rated investment grade.*

The amortized cost, gross unrealized gains (losses) and fair value of AIG's investments in mortgage-backed, asset-backed and collateralized securities at December 31, 2007 were as follows:

	December 31, 2007			
(in millions)	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
AIG, excluding AIGFP:				
RMBS	$ 89,851	$ 433	$5,504	$ 84,780
CMBS	23,918	237	1,156	22,999
CDO/ABS	10,844	196	593	10,447
Subtotal, excluding AIGFP	124,613	866	7,253	118,226
Total AIGFP investments in mortgage-backed, asset-backed and collateralized securities	16,369	355	450	16,274
Total	$140,982	$1,221	$7,703	$134,500

Investments in Residential Mortgage-Backed Securities

As part of its strategy to diversify its investments, AIG invests in various types of securities, including residential mortgage-backed securities (RMBS).

The amortized cost, gross unrealized gains (losses) and estimated fair value of AIG's investments in RMBS securities, other than those of AIGFP, at December 31, 2007 were as follows:

	December 31, 2007				
(in millions)	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value	Percent of Total
Residential mortgage-backed securities:					
U.S. agencies	$14,575	$320	$ 70	$14,825	17%
Prime non-agency[(a)]	21,552	72	550	21,074	25
Alt-A	25,349	17	1,620	23,746	28
Other housing-related[(b)]	4,301	2	357	3,946	5
Subprime	24,074	22	2,907	21,189	25
Total	$89,851	$433	$ 5,504	$84,780	100%

(a) Includes foreign and jumbo RMBS-related securities.

(b) Primarily wrapped second-lien.

AIG's operations, other than AIGFP, held investments in RMBS with an estimated fair value of $84.8 billion at December 31, 2007, or approximately 10 percent of AIG's total invested assets. In addition, AIG's insurance operations held investments with a fair value totaling $4.0 billion in CDOs, of which $58 million included some level of subprime exposure. AIG's RMBS investments are predominantly in highly-rated tranches that contain substantial protection features through collateral subordination. At December 31, 2007, approximately 92 percent of these investments were rated AAA, and approximately 6 percent were rated AA by one or more of the principal rating agencies. AIG's investments rated BBB or below totaled $621 million, or less than 0.1 percent of AIG's total invested assets at December 31, 2007. As of February 25, 2008, $3.6 billion of AIG's RMBS backed primarily by subprime collateral had been downgraded as a result of rating agency actions since January 1, 2008, and $6 million of such investments had been upgraded. Subsequent to December 31, 2007, rating agencies have placed on watch for downgrade a majority of 2006 and 2007 vintage AAA-rated subprime RMBS in the market. For AIG, $9.7 billion was on watch for downgrade.

The fair value of AIG's RMBS investments, other than those of AIGFP, at December 31, 2007 by year of vintage and credit rating were as follows:

	Year of Vintage						
(in millions)	Prior	2003	2004	2005	2006	2007	Total
Rating:							
AAA	$4,053	$6,202	$7,070	$16,011	$25,392	$18,937	$77,665
AA	63	785	555	1,092	2,117	512	5,124
A	46	242	345	480	248	138	1,499
BBB and below	—	53	74	214	114	37	492
Total	$4,162	$7,282	$8,044	$17,797	$27,871	$19,624	$84,780

The fair value of AIG's Alt-A investments included in the RMBS investments above, other than those of AIGFP, at December 31, 2007 by year of vintage and credit rating were as follows:

	Year of Vintage						
(in millions)	Prior	2003	2004	2005	2006	2007	Total
Rating:							
AAA	$208	$623	$ 960	$4,899	$9,301	$6,512	$22,503
AA	23	199	150	391	117	11	891
A	1	37	51	137	48	6	280
BBB and below	—	11	19	36	6	—	72
Total	$232	$870	$1,180	$5,463	$9,472	$6,529	$23,746

The fair value of AIG's subprime RMBS investments, other than those of AIGFP, at December 31, 2007 by year of vintage and credit rating were as follows:

	Year of Vintage						
(in millions)	Prior	2003	2004	2005	2006	2007	Total
Rating:							
AAA	$127	$362	$557	$5,403	$7,926	$4,081	$18,456
AA	6	35	116	277	1,562	357	2,353
A	10	82	100	120	34	26	372
BBB and below	—	—	—	8	—	—	8
Total	$143	$479	$773	$5,808	$9,522	$4,464	$21,189

AIG's underwriting practices for investing in RMBS, other asset-backed securities and CDOs take into consideration the quality of the originator, the manager, the servicer, security credit ratings, underlying characteristics of the mortgages, borrower characteristics, and the level of credit enhancement in the transaction. AIG's strategy is typically to invest in securities rated AA or better and create diversification across multiple underlying asset classes.

General Insurance Invested Assets

In AIG's General Insurance business, the duration of liabilities for long-tail casualty lines is greater than other lines. As differentiated from the Life Insurance & Retirement Services companies, the focus is not on asset-liability matching, but on preservation of capital and growth of surplus.

Fixed income holdings of the Domestic General Insurance companies are comprised primarily of tax-exempt securities, which provide attractive risk-adjusted after-tax returns. These high quality municipal investments have an average rating of AA.

Fixed income assets held in Foreign General Insurance are of high quality and short to intermediate duration, averaging 3.6 years compared to 7.0 years for those in Domestic General Insurance.

While invested assets backing reserves are invested in conventional fixed income securities in Domestic General Insurance, a modest portion of surplus is allocated to large capitalization, high-dividend, public equity strategies and to alternative investments, including private equity and hedge funds. These investments have provided a combination of added diversification and attractive long-term returns.

General Insurance invested assets grew by $13.7 billion, or 12 percent, during 2007 as bond holdings grew by $6 billion. Listed equity holdings grew by $1.3 billion.

Life Insurance & Retirement Services Invested Assets

With respect to Life Insurance & Retirement Services, AIG uses asset-liability management as a tool worldwide in the life insurance business to influence the composition of the invested assets and appropriate marketing strategies. AIG's objective is to maintain a matched asset-liability structure. However, in certain markets, the absence of long-dated fixed income investment instruments may preclude a matched asset-liability position. In addition, AIG may occasionally determine that it is economically advantageous to be temporarily in an unmatched position. To the extent that AIG has maintained a matched asset-liability structure, the economic effect of interest rate fluctuations is partially mitigated.

AIG's investment strategy for the Life Insurance & Retirement Services segment is to produce cash flows greater than maturing insurance liabilities. AIG actively manages the asset-liability relationship in its foreign operations, even though certain territories lack qualified long-term investments or certain local regulatory authorities may impose investment restrictions. For example, in several Southeast Asian countries, the duration of investments is shorter than the effective maturity of the related policy liabilities. Therefore, there is risk that the reinvestment of the proceeds at the maturity of the initial investments may be at a yield below that of the interest required for the accretion of the policy liabilities. Additionally, there exists a future investment risk associated with certain policies currently in-force which will have premium receipts in the future. That is, the investment of these future premium receipts may be at a yield below that required to meet future policy liabilities.

AIG actively manages the interest rate assumptions and crediting rates used for its new and in force business. Business strategies continue to evolve to maintain profitability of the overall business. In some countries, new products are being introduced with minimal investment guarantees, resulting in a shift toward investment-linked savings products and away from traditional savings products with higher guarantees.

The investment of insurance cash flows and reinvestment of the proceeds of matured securities and coupons requires active management of investment yields while maintaining satisfactory investment quality and liquidity.

AIG may use alternative investments, including equities, real estate and foreign currency denominated fixed income instruments in certain foreign jurisdictions where interest rates remain low and there are limited long-dated bond markets to extend the duration or increase the yield of the investment portfolio to more closely match the requirements of the policyholder liabilities and DAC recoverability. This strategy has been effectively used in Japan and more recently by Nan Shan in Taiwan. In Japan, foreign assets, excluding those matched to foreign liabilities, were approximately 31 percent of statutory assets, which is below the maximum allowable percentage under current local regulation. Foreign assets comprised approximately 33 percent of Nan Shan's invested assets at December 31, 2007, slightly below the maximum allowable percentage under current local regulation. The majority of Nan Shan's in-force policy portfolio is traditional life and endowment insurance products with implicit interest rate guarantees. New business with lower interest rate guarantees are gradually reducing the overall interest requirements, but asset portfolio yields have declined faster due to the prolonged low interest rate environment. As a result, although the investment margins for a large block of in-force policies are negative, the block remains profitable overall because the mortality and expense margins presently exceed the negative investment spread. In response to the low interest rate environment and the volatile exchange rate of the Taiwanese dollar, Nan Shan is emphasizing new products with lower implied guarantees, including participating endowments and investment-linked products. Although the risks of a continued low interest rate environment coupled with a volatile Taiwanese dollar could increase net liabilities and require additional capital to maintain adequate local solvency margins, Nan Shan currently believes it has adequate resources to meet all future policy obligations.

AIG actively manages the asset-liability relationship in its domestic operations. This relationship is more easily managed through the availability of qualified long-term investments.

A number of guaranteed benefits, such as living benefits or guaranteed minimum death benefits, are offered on certain variable life and variable annuity products. AIG manages its exposure resulting from these long-term guarantees through reinsurance or capital market hedging instruments.

AIG invests in equities for various reasons, including diversifying its overall exposure to interest rate risk. Available for sale bonds and equity securities are subject to declines in fair value. Such declines in fair value are presented in unrealized appreciation or depreciation of investments, net of taxes, as a component of Accumulated other comprehensive income. Declines that are determined to be other-than-temporary are reflected in income in the period in which the intent to hold the securities to recovery no longer exists. See Valuation of Invested Assets herein. Generally, insurance regulations restrict the types of assets in which an insurance company may invest. When permitted by regulatory authorities and when deemed necessary to protect insurance assets, including invested assets, from adverse movements in foreign currency exchange rates, interest rates and equity prices, AIG and its insurance subsidiaries may enter into derivative transactions as end users to hedge their exposures. For a further discussion of AIG's use of derivatives, see Risk Management — Credit Risk Management — Derivatives herein.

In certain jurisdictions, significant regulatory and/or foreign governmental barriers exist which may not permit the immediate free flow of funds between insurance subsidiaries or from the insurance subsidiaries to AIG parent. For a discussion of these restrictions, see Item 1. Business — Regulation.

Life Insurance & Retirement Services invested assets grew by $41.7 billion, or 10 percent, during 2007 as bond holdings grew by $5.3 billion, and listed equity holdings grew by $9.3 billion, or 39 percent.

Financial Services Invested Assets

Financial Services Securities

Financial Services securities available for sale of $40.3 billion at December 31, 2007 is predominantly a diversified portfolio of high-grade fixed income securities where the individual securities have varying degrees of credit risk. At December 31, 2007, the average credit rating of this portfolio was in the AA+ category or the equivalent thereto as determined through rating agencies or internal review. AIGFP has also entered into credit derivative transactions to economically hedge its credit risk associated with $82 million of these securities. Securities deemed below investment grade at December 31, 2007 totalled $797 million in fair value, representing two percent of Financial Services securities available for sale. There have been no significant downgrades of these securities through February 15, 2008.

AIGFP's management objective is to minimize interest rate, currency, commodity and equity risks associated with its securities available for sale. When AIGFP purchases a security for its securities available for sale investment portfolio, it simultaneously enters into an offsetting hedge such that the payment terms of the hedging transaction offset the payment terms of the investment security. This achieves the economic result of converting the return on the underlying security to U.S. dollar LIBOR plus or minus a spread based on the underlying profit on each security on the initial trade date. The market risk associated with such hedges is managed on a portfolio basis.

Because hedge accounting treatment was not applied in 2006, the unrealized gains and losses on the derivative transactions with unaffiliated third parties were reflected in operating income. The unrealized gains and losses on the underlying securities available for sale resulting from changes in interest rates and currency rates and commodity and equity prices were included in accumulated other comprehensive income (loss), or in operating income, as appropriate. When a security is sold, the realized gain or loss with respect to this security is included in operating income.

Securities purchased under agreements to resell are treated as collateralized financing transactions. AIGFP takes possession of or obtains a security interest in securities purchased under agreements to resell.

Capital Markets

AIGFP uses the proceeds from the issuance of notes and bonds and GIAs to invest in a diversified portfolio of securities, including securities available for sale, and derivative transactions. The funds may also be invested in securities purchased under agreements to resell. The proceeds from the disposal of the aforementioned securities available for sale and securities purchased under agreements to resell are used to fund the maturing GIAs or other AIGFP financings, or to invest in new assets. For a further discussion of AIGFP's borrowings, see Capital Resources and Liquidity — Borrowings herein.

Capital Markets derivative transactions are carried at fair value. AIGFP reduces its economic risk exposure through similarly valued offsetting transactions including swaps, trading securities, options, forwards and futures. AIGFP's super senior credit default swaps include structural protection to help minimize risk. For a further discussion on the use of derivatives by Capital Markets, see Operating Review — Financial Services Operations — Capital Markets and Risk Management — Derivatives herein and Note 8 to Consolidated Financial Statements.

AIGFP owns inventories in certain commodities in which it trades, and may reduce the exposure to market risk through the use of swaps, forwards, futures, and option contracts. Physical commodities held in AIGFP's wholly owned broker-dealer subsidiary are recorded at fair value. All other commodities are recorded at the lower of cost or fair value.

Trading securities, at fair value, and securities and spot commodities sold but not yet purchased, at fair value, are marked to fair value daily with the unrealized gain or loss recognized in income. These trading securities are purchased and sold as necessary to meet the risk management and business objectives of Capital Markets operations.

The gross unrealized gains and gross unrealized losses of Capital Markets operations included in Financial Services assets and liabilities at December 31, 2007 were as follows:

(in millions)	Gross Unrealized Gains	Gross Unrealized Losses
Securities available for sale, at fair value	$ 939	$ 777
Unrealized gain/loss on swaps, options and forward transactions*	17,134	22,982

* *These amounts are also presented as the respective balance sheet amounts.*

ILFC

The cash used for the purchase of flight equipment is derived primarily from the proceeds of ILFC's debt financings. The primary sources for the repayment of this debt and the related interest expense are ILFC's cash flow from operations, proceeds from the sale of flight equipment and the rollover and refinancing of the prior debt. During 2007, ILFC acquired flight equipment costing $4.7 billion. For a further discussion of ILFC's borrowings, see Operating Review — Financial Services Operations — Aircraft Leasing and Capital Resources and Liquidity — Borrowings herein.

At December 31, 2007, ILFC had committed to purchase 234 new aircraft deliverable from 2008 through 2017 for an estimated aggregate purchase price of $20.1 billion. As of February 22, 2008, ILFC has entered into leases for all of the new aircraft to be delivered in 2008, and for 65 of 161 of the new aircraft to be delivered subsequent to 2008. ILFC will be required to find customers for any aircraft currently on order and any aircraft to be ordered, and it must arrange financing for portions of the purchase price of such equipment. ILFC has been successful to date both in placing its new aircraft on lease or under sales contract and obtaining adequate financing, but there can be no assurance that such success will continue in future environments.

Asset Management Invested Assets

Asset Management invested assets are primarily comprised of assets supporting AIG's Spread-Based Investment business, which includes AIG's MIP and domestic GIC programs.

The Spread-Based Investment business strategy is to generate spread income from investments yielding returns greater than AIG's cost of funds. The asset-liability relationship is actively managed. The goal of the MIP investment strategy is to capture a spread between income earned on investments and the funding costs of the program while mitigating interest rate and foreign currency exchange rate risk. The invested assets are predominantly fixed income securities and include U.S. residential mortgage-backed securities, asset-backed securities and commercial mortgage-backed securities. In addition, the MIP sold credit protection by issuing single-name high-grade corporate credit default swaps in 2007.

Asset Management invested assets grew by $3.8 billion during 2007. The growth in invested assets was primarily attributable to growth in other invested assets and mortgage and other loans receivable partially offset by a decrease in bond holdings, and short-term investments. These increases were primarily driven by continued growth of the MIP and the growth of AIG's Institutional Asset Management business. These increases were partially offset by the decrease in assets associated with the runoff of the domestic GIC program.

Securities Lending Activities

AIG's securities lending program is a centrally managed program facilitated by AIG Investments primarily for the benefit of certain of AIG's Insurance companies. Securities are loaned to various financial institutions, primarily major banks and brokerage firms. Cash collateral equal to 102 percent of the fair value of the loaned securities is received. The cash collateral is invested in highly-rated fixed income securities to earn a net spread.

AIG's liability to the borrower for collateral received was $82.0 billion and the fair value of the collateral reinvested was $75.7 billion as of December 31, 2007. In addition to the invested collateral, the securities on loan as well as all of the assets of the participating companies are generally available to satisfy the liability for collateral received.

The composition of the securities lending invested collateral by credit rating at December 31, 2007 was as follows:

(in millions)	AAA	AA	A	BBB/Not Rated	Short-Term	Total
Corporate debt	$ 1,191	$ 9,341	$3,448	$ 160	$ —	$ 14,140
Mortgage-backed, asset-backed and collateralized	47,180	2,226	22	82		49,510
Cash and short-term investments	—	—	—	—	12,012	12,012
Total	$ 48,371	$ 11,567	$3,470	$ 242	$ 12,012	$ 75,662

Participation in the securities lending program by reporting unit at December 31, 2007 was as follows:

	Percent Participation
Domestic Life Insurance and Retirement Services	79%
Foreign Life Insurance	10
Domestic General Insurance	3
Foreign General Insurance	4
Asset Management	4
Total	100.0%

On December 31, 2007, $11.4 billion (or 13.7 percent) of the liabilities were one-day tenor. These one-day tenor loans do not have a contractual end date but are terminable by either party on demand. The balance of the liabilities contractually mature within three months; however, the maturing loans are frequently renewed and rolled over to extended dates. Collateral held for this program at December 31, 2007 included interest bearing cash equivalents with overnight maturities of $12.0 billion.

Liquidity in the securities pool is managed based upon historical experience regarding volatility of daily, weekly and biweekly loan balances. Despite the current environment, the program has not experienced a significant decrease in loan balances.

In addition, the invested securities are carried at fair value with unrealized gains and losses recorded in accumulated other comprehensive income (loss) while net realized gains and losses are recorded in earnings. The net unrealized loss on the investments was $5.0 billion as of December 31, 2007. During 2007, AIG incurred net realized losses of $1.0 billion on this portfolio, predominantly related to other-than-temporary impairments.

Valuation of Invested Assets

Traded Securities

The valuation of AIG's investment portfolio involves obtaining a fair value for each security. The source for the fair value is generally from market exchanges or dealer quotations, with the exception of nontraded securities.

Nontraded Securities

AIG considers nontraded securities to mean certain fixed income investments, certain structured securities, direct private equities, limited partnerships, and hedge funds.

The aggregate carrying value of AIG's nontraded securities at December 31, 2007 was approximately $70 billion. The methodology used to estimate fair value of nontraded fixed income investments is by reference to traded securities with similar attributes and using a matrix pricing methodology. This methodology takes into account such factors as the issuer's industry, the security's rating and tenor, its coupon rate, its position in the capital structure of the issuer, and other relevant factors.

For certain structured securities, the carrying value is based on an estimate of the security's future cash flows pursuant to the requirements of Emerging Issues Task Force Issue No. 99-20,

''Recognition of Interest Income and Impairment on Purchased and Retained Beneficial Interests in Securitized Financial Assets.''

Hedge funds and limited partnerships in which AIG holds in the aggregate less than a five percent interest are carried at fair value.

With respect to hedge funds and limited partnerships in which AIG holds in the aggregate a five percent or greater interest, or less than a five percent interest but where AIG has more than a minor influence over the operations of the investee, AIG accounts for these investments using the equity method.

AIG obtains the fair value of its investments in limited partnerships and hedge funds from information provided by the general partner or manager of these investments, the accounts of which generally are audited on an annual basis.

Each of these investment categories is regularly tested to determine if impairment in value exists. Various valuation techniques are used with respect to each category in this determination.

For a discussion of accounting policies related to changes in fair value of invested assets, see Note 1 to Consolidated Financial Statements.

Portfolio Review

Other-Than-Temporary Impairments

AIG assesses its ability to hold any fixed maturity security in an unrealized loss position to its recovery, including fixed maturity securities classified as available for sale, at each balance sheet date. The decision to sell any such fixed maturity security classified as available for sale reflects the judgment of AIG's management that the security sold is unlikely to provide, on a relative value basis, as attractive a return in the future as alternative securities entailing comparable risks. With respect to distressed securities, the sale decision reflects management's judgment that the risk-discounted anticipated ultimate recovery is less than the value achievable on sale.

AIG evaluates its investments for impairments in valuation. The determination that a security has incurred an other-than-temporary impairment in value and the amount of any loss recognition requires the judgment of AIG's management and a regular review of its investments. See Note 1(c) to Consolidated Financial Statements for further information on AIG's policy.

Once a security has been identified as other-than-temporarily impaired, the amount of such impairment is determined by reference to that security's contemporaneous fair value and recorded as a charge to earnings.

In light of the recent significant disruption in the U.S. residential mortgage and credit markets, particularly in the fourth quarter, AIG has recognized an other-than-temporary impairment charge (severity loss) of $2.2 billion (including $643 million related to AIGFP's available for sale investment securities recorded in other income), primarily with respect to certain residential mortgage-backed securities and other structured securities. Even while retaining their investment grade ratings, such securities were priced at a significant discount to cost. Notwithstanding AIG's intent and ability to hold such securities indefinitely, and despite structures which indicate that a substantial amount of the securities should continue to perform in accordance with original terms, AIG concluded that it could not reasonably assert that the recovery period would be temporary.

As a result of AIG's periodic evaluation of its securities for other-than-temporary impairments in value, AIG recorded other-than-temporary impairment charges of $4.7 billion (including $643 million related to AIGFP recorded on other income), $944 million and $598 million in 2007, 2006 and 2005, respectively.

In addition to the above severity losses, AIG recorded other-than-temporary impairment charges in 2007, 2006 and 2005 related to:

- securities which AIG does not intend to hold until recovery;
- declines due to foreign exchange;
- issuer-specific credit events;
- certain structured securities impaired under EITF No. 99-20; and
- other impairments, including equity securities and partnership investments.

Net realized capital gains (losses) for the years ended December 31, 2007, 2006 and 2005 were as follows:

(in millions)	**2007**	2006	2005
Sales of fixed maturities	**$ (468)**	$(382)	$ 372
Sales of equity securities	**1,087**	813	643
Sales of real estate and other assets	**619**	303	88
Other-than-temporary impairments	**(4,072)**	(944)	(598)
Foreign exchange transactions	**(643)**	(382)	701
Derivative instruments	**(115)**	698	(865)
Total	**$(3,592)**	$ 106	$ 341
AIGFP other-than-temporary impairments*	**$ (643)**	$ —	$ —

** Reported as part of other income.*

Other-than-temporary impairment charges for the years ended December 31, 2007, 2006 and 2005 were as follows:

(in millions)	**2007**	2006	2005
Impairment type:			
Severity*	**$2,200**	$ —	$ —
Lack of intent to hold to recovery	**1,054**	619	335
Foreign currency declines	**500**	—	—
Issuer-specific credit events	**515**	279	257
Adverse projected cash flows on structured securities (EITF 99-20)	**446**	46	6
Total	**$4,715**	$944	$598

** Includes $643 million related to AIGFP reported in other income.*

Other-than-temporary impairment charges for the year ended December 31, 2007 by Reporting Segment were as follows:

(in millions)	General Insurance	Life Insurance & Retirement Services	Financial Services	Asset Management	Other	Total
Impairment Type:						
Severity	$ 71	$1,070	$643	$416	$ —	$2,200
Lack of intent to hold to recovery	91	885	7	71	—	1,054
Foreign currency declines	—	500	—	—	—	500
Issuer-specific credit events	113	177	—	69	156	515
Adverse projected cash flows on structured securities	1	166	—	279	—	446
Total	$276	$2,798	$650	$835	$156	$4,715

Other-than-temporary severity-related impairment charges for the year ended December 31, 2007 were as follows:

Rating:	RMBS	CDO	CMBS	Other Securities	Total
AAA	$ 168	$621	$ —	$ —	$ 789
AA	870	53	6	—	929
A	66	32	77	—	175
BBB and below	28	—	52	—	80
Nonrated	—	—	—	227	227
Total	$1,132	$706	$135	$227	$2,200

No other-than-temporary impairment charge with respect to any one single credit was significant to AIG's consolidated financial condition or results of operations, and no individual other-than-temporary impairment charge exceeded two percent of consolidated net income in 2007.

In periods subsequent to the recognition of an other-than-temporary impairment charge for fixed maturity securities, which is not credit or foreign exchange related, AIG generally accretes into income the discount or amortizes the reduced premium resulting from the reduction in cost basis over the remaining life of the security.

Commercial Mortgage Loan Exposure

At December 31, 2007, AIG had direct commercial mortgage loan exposure of $17.1 billion, with $16.3 billion representing U.S. loan exposure. At that date, none of the U.S. loans were in default or delinquent by 90 days or more. The remaining commercial mortgage loans are secured predominantly by properties in Japan. In addition, at December 31, 2007, AIG had approximately $2.0 billion in residential mortgage loans in jurisdictions outside the United States, primarily backed by properties in Taiwan and Thailand.

At December 31, 2007, AIG owned $23.9 billion in cost basis of CMBS. Approximately 78 percent of such holdings were rated ''AAA'', approximately 98 percent were rated ''A'' or higher, and less than 2 percent were rated ''BBB'' or below. At December 31, 2007, all such securities were current in the payment of principal and interest and none had default rates on underlying collateral at levels viewed by AIG as likely to result in the loss of principal or interest.

There have been disruptions in the commercial mortgage markets in general, and the CMBS market in particular, with credit default swaps indices and quoted prices of securities at levels consistent with a severe correction in lease rates, occupancy and fair value of properties. In addition, spreads in the primary mortgage market have widened significantly. While this capital market stress has not to date been reflected in the performance of commercial mortgage securitization in the form of increased defaults in underlying mortgage pools, pricing of CMBS has been adversely affected by market perceptions that underlying mortgage defaults will increase. As a result, AIG recognized $135 million of other-than-temporary impairment charges on CMBS trading at a severe discount to cost, despite the absence of any deterioration in performance of the underlying credits, because AIG concluded that it could not reasonably assert that the recovery period was temporary. At this time, AIG anticipates full recovery of principal and interest on the securities to which such other-than-temporary impairment charges were recorded.

An aging of the pre-tax unrealized losses of fixed maturity and equity securities, distributed as a percentage of cost relative to unrealized loss (the extent by which the fair value is less than amortized cost or cost), including the number of respective items, was as follows at December 31, 2007:

	Less than or equal to 20% of Cost[e]			Greater than 20% to 50% of Cost[e]			Greater than 50% of Cost[e]			Total		
Aging[d] *(dollars in millions)*	Cost[a]	Unrealized Loss	Items	Cost[a]	Unrealized Loss	Items	Cost[a]	Unrealized Loss	Items	Cost[a]	Unrealized Loss[b]	Items
Investment grade bonds												
0-6 months	$124,681	$ 5,099	16,539	$ 2,588	$ 681	633	$	$		$127,269	$ 5,780	17,172
7-12 months	53,515	3,078	7,174	3,219	859	1,110	—	—	—	56,734	3,937	8,284
>12 months	63,146	2,966	9,598	699	180	119				63,845	3,146	9,717
Total	$241,342	$11,143	33,311	$ 6,506	$1,720	1,862	$ —	$ —	—	$247,848	$12,863	35,173
Below investment grade bonds												
0-6 months	$ 5,909	$ 147	1,611	$ 68	$ 18	24	$ —	$ —	—	$ 5,977	$ 165	1,635
7-12 months	782	45	246	47	8	14	—	—	—	829	53	260
>12 months	1,222	61	204	70	19	9	—	—	—	1,292	80	213
Total	$ 7,913	$ 253	2,061	$ 185	$ 45	47	$ —	$ —	—	$ 8,098	$ 298	2,108
Total bonds												
0-6 months	$130,590	$ 5,246	18,150	$ 2,656	$ 699	657	$ —	$ —	—	$133,246	$ 5,945	18,807
7-12 months	54,297	3,123	7,420	3,266	867	1,124	—	—	—	57,563	3,990	8,544
>12 months	64,368	3,027	9,802	769	199	128	—	—	—	65,137	3,226	9,930
Total[c]	$249,255	$11,396	35,372	$ 6,691	$1,765	1,909	$ —	$ —	—	$255,946	$13,161	37,281
Equity securities												
0-6 months	$ 3,603	$ 297	2,051	$ 262	$ 69	39	$	$		$ 3,865	$ 366	2,090
7-12 months	283	33	181	285	64	36				568	97	217
>12 months	—	—	—	—	—	—	—	—	—	—	—	—
Total	$ 3,886	$ 330	2,232	$ 547	$ 133	75	$ —	$ —	—	$ 4,433	$ 463	2,307

(a) For bonds, represents amortized cost.

(b) The effect on net income of unrealized losses after taxes will be mitigated upon realization because certain realized losses will be charged to participating policyholder accounts, or realization will result in current decreases in the amortization of certain DAC.

(c) Includes securities lending invested collateral.

(d) Represents the number of continuous months that fair value has been less than cost by any amount.

(e) Represents the percentage by which fair value is less than cost at the balance sheet date.

Unrealized gains and losses

At December 31, 2007, the fair value of AIG's fixed maturity and equity securities aggregated $587.1 billion. At December 31, 2007, aggregate pre-tax unrealized gains for fixed maturity and equity securities were $18.1 billion ($11.8 billion after tax).

At December 31, 2007, the aggregate pre-tax gross unrealized losses on fixed maturity and equity securities were $13.6 billion

($8.9 billion after tax). Additional information about these securities is as follows:

- These securities were valued, in the aggregate, at approximately 95 percent of their current amortized cost.
- Less than three percent of these securities were valued at less than 20 percent of their current cost, or amortized cost.
- Less than four percent of the fixed income securities had issuer credit ratings which were below investment grade.

AIG did not consider these securities in an unrealized loss position to be other-than-temporarily impaired at December 31, 2007, as management has the intent and ability to hold these investments until they recover their cost basis. AIG believes the securities will generally continue to perform in accordance with the original terms, notwithstanding the present price declines.

At December 31, 2007, unrealized losses for fixed maturity securities and equity securities did not reflect any significant industry concentrations.

In 2007, unrealized losses related to investment grade bonds increased $9.3 billion ($6.1 billion after tax), reflecting the widening of credit spreads, partially offset by the effects of a decline in risk-free interest rates.

The amortized cost and fair value of fixed maturity securities available for sale in an unrealized loss position at December 31, 2007, by contractual maturity, is shown below:

(in millions)	Amortized Cost	Fair Value
Due in one year or less	$ 9,408	$ 9,300
Due after one year through five years	36,032	35,267
Due after five years through ten years	54,198	52,394
Due after ten years	56,557	53,578
Mortgage-backed, asset-backed and collateralized	99,751	92,246
Total	$255,946	$242,785

For the year ended December 31, 2007, the pre-tax realized losses incurred with respect to the sale of fixed maturities and equity securities were $1.3 billion. The aggregate fair value of securities sold was $38.0 billion, which was approximately 94 percent of amortized cost. The average period of time that securities sold at a loss during 2007 were trading continuously at a price below book value was approximately five months. See Risk Management — Investments herein for an additional discussion of investment risks associated with AIG's investment portfolio.

Risk Management

Overview

AIG believes that strong risk management practices and a sound internal control environment are fundamental to its continued success and profitable growth. Failure to manage risk properly exposes AIG to significant losses, regulatory issues and a damaged reputation.

The major risks to which AIG is exposed include the following:

- *Credit risk* — the potential loss arising from an obligor's inability or unwillingness to meet its obligations to AIG.
- *Market risk* — the potential loss arising from adverse fluctuations in interest rates, foreign currencies, equity and commodity prices, and their levels of volatility.
- *Operational risk* — the potential loss resulting from inadequate or failed internal processes, people, and systems, or from external events.
- *Liquidity risk* — the potential inability to meet all payment obligations when they become due.
- *General insurance risk* — the potential loss resulting from inadequate premiums, insufficient reserves and catastrophic exposures.
- *Life insurance risk* — the potential loss resulting from experience deviating from expectations for mortality, morbidity and termination rates in the insurance-oriented products and insufficient cash flows to cover contract liabilities in the retirement savings products.

AIG senior management establishes the framework, principles and guidelines for risk management. The primary focus of risk management is to assess the risk of AIG incurring economic losses from the risk categories outlined above. The business executives are responsible for establishing and implementing risk management processes and responding to the individual needs and issues within their business, including risk concentrations within their respective businesses with appropriate oversight by Enterprise Risk Management (ERM).

Corporate Risk Management

AIG's major risks are addressed at the corporate level through ERM, which is headed by AIG's Chief Risk Officer (CRO). ERM is responsible for assisting AIG's business leaders, executive management and the Board of Directors to identify, assess, quantify, manage and mitigate the risks incurred by AIG. Through the CRO, ERM reports to AIG's Chief Financial Officer, various senior management committees and the Board of Directors through the Finance and Audit Committees.

An important goal of ERM is to ensure that once appropriate governance, authorities, procedures and policies have been established, aggregated risks do not result in inappropriate concentrations. Senior management defines the policies, has established general operating parameters for its global businesses and has established various oversight committees to monitor the risks attendant to its businesses:

- The Financial Risk Committee (FRC) oversees AIG's market risk exposures to interest rates, foreign exchange and fair values of shares, partnership interests, real estate and other equity investments and provides strategic direction for AIG's asset-liability management. The FRC meets monthly and acts as a central mechanism for AIG senior management to review comprehensive information on AIG's financial exposures and to exercise broad control over these exposures. There are two subcommittees of the FRC.
  - The Foreign Exchange Committee monitors trends in foreign exchange rates, reviews AIG's foreign exchange exposures, and provides recommendations on foreign currency asset allocation and remittance hedging.

  - The Liquidity Risk Committee is responsible for liquidity policy and implementation at AIG Parent and exercises oversight and control of liquidity policies at each AIG entity. See Capital Resources and Liquidity herein.
- The CRC is responsible for the following:
  - approving credit risk policies and procedures for use throughout AIG;
  - delegating credit authority to business unit credit officers and select business unit managers;
  - approving transaction requests and limits for corporate, sovereign and cross-border credit exposures that exceed the delegated authorities;
  - establishing and maintaining AIG's risk rating process for corporate, financial and sovereign obligors; and
  - conducting regular reviews of credit risk exposures in the portfolios of all credit-incurring business units.
- The Derivatives Committee (DC) reviews any proposed derivative transaction or program not otherwise managed by AIGFP. The DC examines, among other things, the nature and purpose of the derivative transaction, its potential credit exposure, if any, and the estimated benefits.
- The CSFTC has the authority and responsibility to review and approve any proposed CSFT. A CSFT is any transaction or product that may involve a heightened legal, regulatory, accounting or reputational risk that is developed, marketed or proposed by AIG or a third party. The CSFTC provides guidance to and monitors the activities of transaction review committees (TRCs) which have been established in all major business units. TRCs have the responsibility to identify, review and refer CSFTs to the CSFTC.

Credit Risk Management

AIG devotes considerable resources, expertise and controls to managing its direct and indirect credit exposures, such as investments, deposits, loans, reinsurance recoverables and leases, as well as counterparty risk in derivatives activities, cessions of insurance risk to reinsurers and customers and credit risk assumed through credit derivatives written and financial guarantees. Credit risk is defined as the risk that AIG's customers or counterparties are unable or unwilling to repay their contractual obligations when they become due. Credit risk may also be manifested: (i) through the downgrading of credit ratings of counterparties whose credit instruments AIG may be holding, or, in some cases, insuring, causing the value of the assets to decline or insured risks to rise; and (ii) as cross-border risk where a country (sovereign government risk) or one or more non-sovereign obligors within a country are unable to repay an obligation or are unable to provide foreign exchange to service a credit or equity exposure incurred by another AIG business unit located outside that country.

AIG's credit risks are managed at the corporate level by the Credit Risk Management department (CRM) whose primary role is to support and supplement the work of the CRC. CRM is headed by AIG's Chief Credit Officer (CCO), who reports to AIG's CRO. AIG's CCO is primarily responsible for the development and maintenance of credit risk policies and procedures approved by the CRC. In discharging this function CRM has the following responsibilities:

- Manage the approval process for all requests for credit limits, program limits and transactions.
- Approve delegated credit authorities to CRM credit executives and business unit credit officers.
- Aggregate globally all credit exposure data by counterparty, country and industry and report risk concentrations regularly to the CRC and the Finance Committee of the Board of Directors.
- Administer regular in-depth portfolio credit reviews of all investment, derivative and credit-incurring business units and recommend any corrective actions where required.
- Develop methodologies for quantification and assessment of credit risks, including the establishment and maintenance of AIG's internal risk rating process.
- Approve appropriate credit reserves and methodologies at the business unit and enterprise levels.

AIG closely monitors and controls its company-wide credit risk concentrations and attempts to avoid unwanted or excessive risk accumulations, whether funded or unfunded. To minimize the level of credit risk in certain circumstances, AIG may require third-party guarantees, collateral, such as letters of credit or trust account deposits or reinsurance. These guarantees, letters of credit and reinsurance recoverables are also treated as credit exposure and are added to AIG's risk concentration exposure data.

AIG defines its aggregate credit exposures to a counterparty as the sum of its fixed maturities, loans, finance leases, derivatives (mark to market), deposits (in the case of financial institutions) and the specified credit equivalent exposure to certain insurance products which embody credit risk.

The following table presents AIG's largest credit exposures at December 31, 2007 as a percentage of total shareholders' equity:

Category	Risk Rating[(a)]	Credit Exposure as a Percentage of Total Shareholders' Equity
Investment Grade:		
10 largest combined	A+ (weighted average)[(b)]	84.8%
Single largest non-sovereign (financial institution)	AA–	8.4
Single largest corporate	AAA	5.4
Single largest sovereign	A	15.7
Non-Investment Grade:		
Single largest sovereign	BB–	1.8
Single largest non-sovereign	B+	0.5

(a) Risk rating is based on external ratings, or equivalent, based on AIG's internal risk rating process.

(b) Six of the ten largest credit exposures are to highly-rated financial institutions and three are to investment-grade rated sovereigns; none is rated lower than BBB+ or its equivalent.

AIG closely controls its aggregate cross-border exposures to avoid excessive concentrations in any one country or regional group of countries. AIG defines its cross-border exposure to include both cross-border credit exposures and its large cross-border investments in its own international subsidiaries. Ten countries had cross-border exposures in excess of 10 percent of total shareholders' equity; seven are AAA-rated and three are AA-rated.

In addition, AIG closely monitors its industry concentrations, the risks of which are often mitigated by the breadth and scope of AIG's international operations.

- AIG's single largest industry credit exposure is to the highly-rated global financial institutions sector, accounting for 87 percent of total shareholders' equity at December 31, 2007.
- Excluding the U.S. residential and commercial mortgage sectors, AIG's other industry credit concentrations in excess of 10 percent of total shareholders' equity at December 31, 2007 are to the following industries (in descending order by approximate size):
  - Electric and water utilities;
  - Oil and gas;
  - European regional financial institutions;
  - Global telecommunications companies;
  - Global life insurance carriers;
  - U.S.-based regional financial institutions;
  - Global securities firms and exchanges; and
  - Global reinsurance firms.

AIG participates in the U.S. residential and commercial mortgage markets through AGF, which originates principally first-lien mortgage loans and, to a lesser extent, second-lien mortgage loans to buyers and owners of residential housing; UGC which provides first loss mortgage guaranty insurance for high loan-to-value first- and second-lien residential mortgages; AIG Investments which invests in mortgage-backed securities and collateralized debt obligations, on behalf of AIG insurance and financial services subsidiaries, in which the underlying collateral comprises residential or commercial mortgage loans; and AIGFP which invests in highly rated tranches of RMBS, CMBS and CDOs and provides credit protection through credit default swaps on certain super senior tranches of CDOs. In addition, AIG Investments invests directly in commercial real estate properties and provides real estate commercial mortgage loans.

Some of AIG's exposures are insured (''wrapped'') by financial guarantor insurance companies, also known as ''monoline insurers'', which at December 31, 2007, provide AIG over $44 billion (carrying value) in financial support. The monoline insurers include MBIA, Ambac, FGIC, and others and provide support predominantly in the United States. AIG does not rely on the monoline insurance as its principal source of repayment when evaluating securities for purchase. All investment securities are evaluated primarily based on the underlying cash flow generation capacities of the issuer or cash flow characteristics of the security.

Approximately 96 percent of the monoline protection is provided on AIG Investments' fixed maturities exposures, of which municipal securities represent 74 percent of assets insured, substantially all of which had underlying credit ratings of ''A'' or higher. AIG considers that the monoline wrap for such securities is of limited support, as the default rate on single A and higher rated municipal bonds has historically been negligible. However, AIG anticipates that the failure of one or more monoline insurers may cause price volatility and other disruption in the municipal bond market, as market participants adjust to the absence of monoline credit support. AIG maintains a credit staff to evaluate its municipal bond holdings, and does not rely on monoline insurers in evaluating securities for its municipal bond portfolios.

Approximately four percent of AIG's monoline insurance supports AIGFP investment exposures.

For the non-municipal assets in the AIG Investments portfolio, at December 31, 2007, AIG owned $9.5 billion in cost basis or $8.8 billion in fair value of various types of asset-backed securities wrapped by one or more of the monoline insurers. Based on internal analysis, approximately $6.7 billion in cost basis represented holdings with underlying ratings estimated at BBB or higher. AIG has generally viewed the monoline credit support on these securities as significant only to ''tail'' risk, that is, the risk that as pools of underlying assets amortize, the remaining assets, or ''tail'', may suffer from adverse selection on prepayments or from a lack of adequate risk diversification. While

these securities initially had underlying investment grade ratings, poor pool performance has in some cases resulted in current ratings of below investment grade. The amount of ultimate loss exposure of these securities to the monoline insurers is a function of the ultimate performance of the collateral pools and cannot be reliably estimated. AIG believes that monoline insurers are currently providing payment support on approximately $380 million of such securities.

The CRC reviews quarterly concentration reports in all categories listed above as well as credit trends by risk ratings. The CRC may adjust limits to provide reasonable assurance that AIG does not incur excessive levels of credit risk and that AIG's credit risk profile is properly calibrated across business units.

Market Risk Management

AIG is exposed to market risks, primarily within its insurance and capital markets businesses. These asset-liability exposures are predominantly structural in nature, and not the result of speculative positioning to take advantage of short-term market opportunities. The Market Risk Management department (MRM), which reports to the CRO, is responsible for control and oversight of market risks in all aspects of AIG's financial services, insurance, and investment activities.

AIG's market exposures arise from the following:

- AIG is a globally diversified enterprise with capital deployed in a variety of currencies. Capital deployed in AIG's overseas businesses, when converted into U.S. dollars for financial reporting purposes, constitutes a ''long foreign currency/short U.S. dollar'' market exposure on AIG's balance sheet. Similarly, overseas earnings denominated in foreign currency also represent a ''long foreign currency/short U.S. dollar'' market exposure on AIG's income statement.
- Much of AIG's domestic capital is invested in U.S. fixed income or equity securities, leading to exposures to U.S. yields and equity markets.
- Several of AIG's Foreign Life Insurance subsidiaries operate in developing markets where maturities on longer-term life insurance liabilities exceed the maximum maturities of available local currency assets.

As a globally diversified enterprise, AIG is exposed to a variety of foreign currency risks. AIG earns a significant portion of its income from operations conducted in foreign currencies which must be translated into U.S. dollars for consolidated reporting purposes. Consequently, exchange rate fluctuations can cause volatility in AIG's reported earnings. When the U.S. dollar weakens against other currencies, AIG's earnings increase. When the U.S. dollar strengthens against other currencies, AIG's earnings decline.

The sensitivity of AIG's consolidated shareholders' equity to foreign exchange volatility is more complex. AIG has significant capital committed overseas, which rises in value on AIG's consolidated balance sheet when the U.S. dollar weakens. AIG also has significant U.S. dollar asset holdings overseas, which offset the foreign exchange exposure arising from AIG's overseas capital. Similar to the income statement, AIG's overall balance sheet is net long foreign currencies and net short U.S. dollars.

The table below provides an estimate of the sensitivity of shareholders' equity and net income to 10 percent changes in the value of the U.S. dollar relative to foreign currencies as of December 31, 2007, assuming a tax rate of 35 percent:

(in millions)	U.S. dollar up 10 percent	U.S. dollar down 10 percent
Shareholders' equity	$(466)	$466
Net income	$(220)	$220

AIG analyzes market risk using various statistical techniques including Value at Risk (VaR). VaR is a summary statistical measure that uses the estimated volatility and correlation of market factors to calculate the maximum loss that could occur over a defined period of time with a specified level of statistical confidence. VaR measures not only the size of individual exposures but also the interaction between different market exposures, thereby providing a portfolio approach to measuring market risk. Similar VaR methodologies are used to determine capital requirements for market risk within AIG's economic capital framework.

Insurance, Asset Management and Non-Trading Financial Services VaR

AIG performs one comprehensive VaR analysis across all of its non-trading businesses, and a separate VaR analysis for its trading business at AIGFP. The comprehensive VaR is categorized by AIG business segment (General Insurance, Life Insurance & Retirement Services, Financial Services and Asset Management) and also by market risk factor (interest rate, currency and equity). AIG's market risk VaR calculations include exposures to benchmark Treasury or swap interest rates, but do not include exposures to credit-based factors such as credit spreads. AIG's credit exposures within its invested assets and credit derivative portfolios are discussed in Credit Risk Management — Financial Services herein.

For the insurance segments, assets included are invested assets (excluding direct holdings of real estate) and liabilities included are reserve for losses and loss expenses, reserve for unearned premiums, future policy benefits for life and accident and health insurance contracts and other policyholders' funds. For financial services companies, loans and leases represent the majority of assets represented in the VaR calculation, while bonds and notes issued represent the majority of liabilities.

AIG calculated the VaR with respect to net fair values as of December 31, 2007 and 2006. The VaR number represents the maximum potential loss as of those dates that could be incurred with a 95 percent confidence (i.e., only five percent of historical scenarios show losses greater than the VaR figure) within a one-month holding period. AIG uses the historical simulation methodology that entails repricing all assets and liabilities under explicit changes in market rates within a specific historical time period. AIG uses the most recent three years of historical market information for interest rates, foreign exchange rates, and equity

index prices. For each scenario, each transaction was repriced. Segment and AIG-wide scenario values are then calculated by netting the values of all the underlying assets and liabilities.

The following table presents the period-end, average, high and low VaRs on a diversified basis and of each component of market risk for AIG's non-trading businesses. The diversified VaR is usually smaller than the sum of its components due to correlation effects.

	2007				2006			
		For the Year Ended December 31,				For the Year Ended December 31,		
(in millions)	As of December 31	Average	High	Low	As of December 31	Average	High	Low
Total AIG Non-Trading Market Risk:								
Diversified	**$ 5,593**	**$ 5,316**	**$ 5,619**	**$ 5,073**	$5,073	$5,209	$5,783	$4,852
Interest rate	**4,383**	**4,600**	**4,757**	**4,383**	4,577	4,962	5,765	4,498
Currency	**785**	**729**	**785**	**685**	686	641	707	509
Equity	**2,627**	**2,183**	**2,627**	**1,873**	1,873	1,754	1,873	1,650
General Insurance:								
Diversified	**$ 1,363**	**$ 1,637**	**$ 1,892**	**$ 1,363**	$1,717	$1,697	$1,776	$1,617
Interest rate	**1,117**	**1,492**	**1,792**	**1,117**	1,541	1,635	1,717	1,541
Currency	**255**	**222**	**255**	**205**	212	162	212	119
Equity	**835**	**659**	**835**	**573**	573	551	573	535
Life Insurance & Retirement Services:								
Diversified	**$ 5,180**	**$ 4,848**	**$ 5,180**	**$ 4,574**	$4,574	$4,672	$5,224	$4,307
Interest rate	**4,405**	**4,465**	**4,611**	**4,287**	4,471	4,563	5,060	4,229
Currency	**649**	**621**	**678**	**568**	568	538	592	459
Equity	**1,810**	**1,512**	**1,810**	**1,293**	1,293	1,228	1,299	1,133
Non-Trading Financial Services:								
Diversified	**$ 99**	**$ 117**	**$ 170**	**$ 85**	$ 125	$ 165	$ 252	$ 125
Interest rate	**95**	**116**	**168**	**76**	127	166	249	127
Currency	**13**	**12**	**13**	**11**	11	8	11	7
Equity	**1**	**1**	**1**	**1**	1	1	2	1
Asset Management:								
Diversified	**$ 38**	**$ 49**	**$ 74**	**$ 26**	$ 64	$ 144	$ 190	$ 64
Interest rate	**32**	**45**	**72**	**22**	63	145	192	63
Currency	**2**	**3**	**5**	**2**	3	4	7	3
Equity	**13**	**11**	**13**	**8**	8	9	13	8

AIG's total non-trading VaR increased from $5.1 billion at December 31, 2006 to $5.6 billion at December 31, 2007, primarily due to higher exposures to U.S. equity risk. The higher contribution of U.S. equity risk during 2007 was driven by a combination of three factors:

- increased U.S. equity investment allocation in the General Insurance and Life Insurance & Retirement Services segments,
- increased volatility in U.S. equity prices, and
- rising correlations between U.S. equities and AIG's structural duration exposures in Asia.

Interest rate and foreign exchange volatilities generally moderated during 2007.

Operational Risk Management

AIG's corporate-level Operational Risk Management department (ORM) oversees AIG's operational risk management practices. The Director of ORM reports to the CRO. ORM is responsible for establishing the framework, principles and guidelines for operational risk management. ORM also manages compliance with the requirements of the Sarbanes-Oxley Act of 2002.

Each business unit is responsible for implementing the components of AIG's operational risk management program to ensure that effective operational risk management practices are utilized throughout AIG.

Upon full implementation, the program will consist of a risk and control self assessment (RCSA) process, risk event data analysis, key risk indicators and governance. To date, AIG has developed the methodology for performing a combined operational risk and compliance RCSA in each of AIG's key business units.

Insurance Risk Management

Reinsurance

AIG uses reinsurance programs for its insurance risks as follows:

- facultative to cover large individual exposures;
- quota share treaties to cover specific books of business;
- excess of loss treaties to cover large losses;
- excess or surplus automatic treaties to cover individual life risks in excess of stated per-life retention limits; and
- catastrophe treaties to cover specific catastrophes including earthquake, windstorm and flood.

AIG's Reinsurance Security Department (RSD) conducts periodic detailed assessments of the financial status and condition of current and potential reinsurers, both foreign and domestic. The RSD monitors both the nature of the risks ceded to the reinsurers and the aggregation of total reinsurance recoverables ceded to reinsurers. Such assessments may include, but are not limited to, identifying if a reinsurer is appropriately licensed and has sufficient financial capacity, and evaluating the local economic environment in which a foreign reinsurer operates.

The RSD reviews the nature of the risks ceded to reinsurers and the need for credit risk mitigants. For example, in AIG's treaty reinsurance contracts, AIG frequently includes provisions that require a reinsurer to post collateral when a referenced event occurs. Furthermore, AIG limits its unsecured exposure to reinsurers through the use of credit triggers, which include, but are not limited to, insurer financial strength rating downgrades, declines in policyholders surplus below predetermined levels, decreases in the NAIC risk-based capital (RBC) ratio or reaching maximum limits of reinsurance recoverables. In addition, AIG's CRC reviews all reinsurer exposures and credit limits and approves most large reinsurer credit limits that represent actual or potential credit concentrations. AIG believes that no exposure to a single reinsurer represents an inappropriate concentration of risk to AIG, nor is AIG's business substantially dependent upon any single reinsurance contract.

AIG enters into intercompany reinsurance transactions for its General Insurance and Life Insurance & Retirement Services operations. AIG enters into these transactions as a sound and prudent business practice in order to maintain underwriting control and spread insurance risk among AIG's various legal entities and to leverage economies of scale with external reinsurers. When required for statutory recognition, AIG obtains letters of credit from third-party financial institutions to collateralize these intercompany transactions. At December 31, 2007, approximately $8.8 billion of letters of credit were outstanding to cover intercompany reinsurance transactions between subsidiaries.

Although reinsurance arrangements do not relieve AIG subsidiaries from their direct obligations to insureds, an efficient and effective reinsurance program substantially mitigates AIG's exposure to potentially significant losses. AIG continually evaluates the reinsurance markets and the relative attractiveness of various arrangements for coverage, including structures such as catastrophe bonds, insurance risk securitizations, ''sidecars'' and similar vehicles.

Based on this ongoing evaluation and other factors, effective December 31, 2007, Lexington and Concord Re Limited agreed to commute their quota share reinsurance agreement covering U.S. commercial property insurance business written by Lexington on a risk attaching basis. This agreement was effective in July 2006 and was due to expire on January 15, 2008.

For 2008, AIG purchased a U.S. catastrophe coverage of approximately $1.1 billion in excess of a per occurrence deductible of $1.5 billion. For Life Insurance & Retirement Services, AIG's 2008 catastrophe program covers losses of $250 million in excess of $200 million for Japan and Taiwan only.

Reinsurance Recoverable

General reinsurance recoverable assets are comprised of:

- balances due from reinsurers for indemnity losses and loss expenses billed to, but not yet collected from, reinsurers (Paid Losses Recoverable);
- ultimate ceded reserves for indemnity losses and expenses includes reserves for claims reported but not yet paid and estimates for IBNR (collectively, Ceded Loss Reserves); and
- Ceded Reserves for Unearned Premiums.

At December 31, 2007, general reinsurance assets of $21.5 billion include Paid Losses Recoverable of $1.8 billion and Ceded Loss Reserves of $16.2 billion, and $4.0 billion of Ceded Reserves for Unearned Premiums. The methods used to estimate IBNR and to establish the resulting ultimate losses involve projecting the frequency and severity of losses over multiple years and are continually reviewed and updated by management. Any adjustments are reflected in income currently. It is AIG's belief that the ceded reserves for losses and loss expenses at December 31, 2007 were representative of the ultimate losses recoverable. Actual losses may differ from the reserves currently ceded.

AIG manages the credit risk in its reinsurance relationships by transacting with reinsurers that it considers financially sound, and when necessary AIG requires reinsurers to post substantial collateral in the form of funds, securities and/or irrevocable letters of credit. This collateral can be drawn on for amounts that remain unpaid beyond specified time periods on an individual reinsurer basis. At December 31, 2007, approximately 55 percent of the general reinsurance assets were from unauthorized reinsurers. The terms authorized and unauthorized pertain to regulatory categories, not creditworthiness. More than 50 percent of these balances were collateralized, permitting statutory recognition. Additionally, with the approval of insurance regulators, AIG posted approximately $1.8 billion of letters of credit issued by commercial banks in favor of certain Domestic General Insurance companies to permit those companies statutory recognition of balances otherwise uncollateralized at December 31, 2007. The remaining 45 percent of the general reinsurance assets were from authorized reinsurers. At December 31, 2007, approximately 87 percent of the balances with respect to authorized reinsurers are from reinsurers rated A (excellent) or better, as rated by A.M. Best, or A (strong) or better, as rated by S&P. These ratings are measures of financial strength.

The following table provides information for each reinsurer representing in excess of five percent of AIG's reinsurance assets at December 31, 2007:

(in millions)	S&P Rating[(a)]	A.M. Best Rating[(a)]	Gross General Reinsurance Assets	Percent of General Reinsurance Assets, Net	Collateral Held[(b)]	Uncollateralized General Reinsurance Assets
Reinsurer:						
Swiss Reinsurance Group	AA-	A+	$1,818	8.5%	$372	$1,446
Berkshire Hathaway Insurance Group	AAA	A++	$1,618	7.5%	$212	$1,406
Munich Reinsurance Group	AA-	A+	$1,200	5.6%	$430	$ 770
Lloyd's Syndicates — Lloyd's of London[(c)]	A+	A	$1,089	5.1%	$113	$ 976

(a) Rating designations as of February 19, 2008.

(b) Excludes collateral held in excess of applicable treaty balances.

(c) Excludes Equitas gross reinsurance assets that are unrated, which are less than five percent of AIG's general reinsurance assets.

AIG maintains an allowance for estimated unrecoverable reinsurance of $520 million. At December 31, 2007, AIG had no significant reinsurance recoverables due from any individual reinsurer that was financially troubled (i.e., liquidated, insolvent, in receivership or otherwise subject to formal or informal regulatory restriction).

Segment Risk Management

Other than as described above, AIG manages its business risk oversight activities through its business segments.

Insurance Operations

AIG's multiple insurance businesses conducted on a global basis expose AIG to a wide variety of risks with different time horizons. These risks are managed throughout the organization, both centrally and locally, through a number of procedures, including: (i) pre-launch approval of product design, development and distribution; (ii) underwriting approval processes and authorities; (iii) exposure limits with ongoing monitoring; (iv) modeling and reporting of aggregations and limit concentrations at multiple levels (policy, line of business, product group, country, individual/group, correlation and catastrophic risk events); (v) compliance with financial reporting and capital and solvency targets; (vi) extensive use of reinsurance, both internal and third-party; and (vii) review and establishment of reserves.

AIG closely manages insurance risk by overseeing and controlling the nature and geographic location of the risks in each line of business underwritten, the terms and conditions of the underwriting and the premiums charged for taking on the risk. Concentrations of risk are analyzed using various modeling techniques and include, but are not limited to, wind, flood, earthquake, terrorism and accident.

AIG has two major categories of insurance risks as follows:

- *General Insurance* — risks covered include property, casualty, fidelity/surety, management liability and mortgage insurance. Risks in the general insurance segment are managed through aggregations and limitations of concentrations at multiple levels: policy, line of business, correlation and catastrophic risk events.
- *Life Insurance & Retirement Services* — risks include mortality and morbidity in the insurance-oriented products and insufficient cash flows to cover contract liabilities in the retirement savings-oriented products. Risks are managed through product design, sound medical underwriting, external traditional reinsurance programs and external catastrophe reinsurance programs.

AIG is a major purchaser of reinsurance for its insurance operations. The use of reinsurance facilitates insurance risk management (retention, volatility, concentrations) and capital planning locally (branch and subsidiary). AIG may purchase reinsurance on a pooling basis. Pooling of AIG's reinsurance risks enables AIG to purchase reinsurance more efficiently at a consolidated level, manage global counterparty risk and relationships and manage global catastrophe risks, both for the General Insurance and Life Insurance & Retirement Services businesses.

General Insurance

In General Insurance, underwriting risks are managed through the application approval process, exposure limitations as well as through exclusions, coverage limits and reinsurance. The risks covered by AIG are managed through limits on delegated underwriting authority, the use of sound underwriting practices, pricing procedures and the use of actuarial analysis as part of the determination of overall adequacy of provisions for insurance contract liabilities.

A primary goal of AIG in managing its General Insurance operations is to achieve an underwriting profit. To achieve this goal, AIG must be disciplined in its risk selection, and premiums must be adequate and terms and conditions appropriate to cover the risk accepted.

Catastrophe Exposures

The nature of AIG's business exposes it to various catastrophic events in which multiple losses across multiple lines of business can occur in any calendar year. In order to control this exposure, AIG uses a combination of techniques, including setting aggregate limits in key business units, monitoring and modeling accumulated exposures, and purchasing catastrophe reinsurance to supplement its other reinsurance protections.

Natural disasters such as hurricanes, earthquakes and other catastrophes have the potential to adversely affect AIG's operating results. Other risks, such as an outbreak of a pandemic disease, such as the Avian Influenza A Virus (H5N1), could

adversely affect AIG's business and operating results to an extent that may be only partially offset by reinsurance programs.

AIG evaluates catastrophic events and assesses the probability of occurrence and magnitude of catastrophic events through the use of industry recognized models, among other techniques. AIG updates these models by periodically monitoring the exposure to risks of AIG's worldwide General Insurance operations and adjusting such models accordingly. Following is an overview of modeled losses associated with the more significant natural perils, which includes exposures for DBG, Personal Lines, Foreign General (other than Ascot), and The Hartford Steam Boiler Inspection and Insurance Company. Transatlantic and Ascot utilize a different model, and their combined results are presented separately below. Significant life insurance and accident and health (A&H) exposures have been added to these results as well. The modeled results assume that all reinsurers fulfill their obligations to AIG in accordance with their terms.

It is important to recognize that there is no standard methodology to project the possible losses from total property and workers compensation exposures. Further, there are no industry standard assumptions to be utilized in projecting these losses. The use of different methodologies and assumptions could materially change the projected losses. Therefore, these modeled losses may not be comparable to estimates made by other companies.

These estimates are inherently uncertain and may not reflect AIG's maximum exposures to these events. It is highly likely that AIG's losses will vary, perhaps significantly, from these estimates.

AIG has revised the catastrophe exposure disclosures presented below from those included in the 2006 Annual Report on Form 10-K to reflect more recent data, as well as reinsurance programs in place as of January 31, 2008. The modeled results provided in the table below were based on the aggregate exceedence probability (AEP) losses which represent total property, workers compensation, life insurance, and A&H losses that may occur in any single year from one or more natural events. The life insurance and A&H data include exposures for United States, Japan, and Taiwan earthquakes. These represent the largest share of life insurance and A&H exposures to earthquake. A&H losses were modeled using December 2006 data, and life insurance losses were modeled using March 2006 data. Modeled life insurance results using more recent data will be available by May 2008. However, management does not believe that changes in the life insurance and A&H exposures will materially increase AIG's overall exposures. The updated property exposures were generally modeled with exposure data as of June 2007. Lexington commercial lines exposure, which represents the largest share of the modeled losses, was based on data as of October 2007. All reinsurance program structures, including both domestic and international structures, have also been updated. The values provided are based on 100-year return period losses, which have a one percent likelihood of being exceeded in any single year. Thus, the model projects that there is a one percent probability that AIG could incur in any year losses in excess of the modeled amounts for these perils. Losses include loss adjustment expenses and the net values include reinstatement premiums.

(in millions)	Gross	Net of 2008 Reinsurance	Net After Income Tax	% of Consolidated Shareholders' Equity at December 31, 2007
Natural Peril:				
Earthquake	$5,625	$3,397	$2,208	2.3%
Tropical Cyclone*	$5,802	$3,430	$2,230	2.3%

** Includes hurricanes, typhoons and other wind-related events.*

Gross earthquake and tropical cyclone modeled losses increased $1.9 billion and $1.0 billion, respectively, while net losses increased $923 million and $234 million, respectively. The earthquake probable maximum loss for 2007 now includes AIG's life insurance and A&H exposures that were previously not included. These changes also reflect overall increased exposure, changes in the Lexington quota share program, the inclusion of loss adjustment expenses, and changes in corporate catastrophe structure.

In addition to the return period loss, AIG evaluates potential single event earthquake and hurricane losses that may be incurred. The single events utilized are a subset of potential events identified and utilized by Lloyd's *(as described in Lloyd's Realistic Disaster Scenarios, Scenario Specifications, April 2006)* and referred to as Realistic Disaster Scenarios (RDSs). The purpose of this analysis is to utilize these RDSs to provide a reference frame and place into context the model results. However, it is important to note that the specific events used for this analysis do not necessarily represent the worst case loss that AIG could incur from this type of an event in these regions. The losses associated with the RDSs are included in the table below.

Single event modeled property and workers compensation losses to AIG's worldwide portfolio of risk for key geographic areas are set forth below. Gross values represent AIG's liability after the application of policy limits and deductibles, and net values represent losses after reinsurance is applied and include reinsurance reinstatement premiums. Both gross and net losses include loss adjustment expenses.

(in millions)	Gross	Net of 2008 Reinsurance
Natural Peril:		
San Francisco Earthquake	$6,236	$3,809
Miami Hurricane	$5,829	$3,280
Northeast Hurricane	$5,287	$3,739
Los Angeles Earthquake	$5,375	$3,297
Gulf Coast Hurricane	$3,730	$2,088
Japanese Earthquake	$1,109	$ 406
European Windstorm	$ 252	$ 89
Japanese Typhoon	$ 177	$ 103

AIG also monitors key international property risks utilizing modeled statistical return period losses. Based on these simulations, the 100-year return period loss for Japanese Earthquake is $510 million gross, and $170 million net, the 100-year return period loss for European Windstorm is $448 million gross, and $154 million net, and the 100-year return period loss for Japanese Typhoon is $340 million gross, and $212 million net.

The losses provided above do not include Transatlantic and Ascot. The combined earthquake and tropical cyclone 100-year return period modeled losses for Ascot and Transatlantic together are estimated to be $1.0 billion, on a gross basis, $749 million, net of reinsurance.

ACTUAL RESULTS IN ANY PERIOD ARE LIKELY TO VARY, PERHAPS MATERIALLY, FROM THE MODELED SCENARIOS, AND THE OCCURRENCE OF ONE OR MORE SEVERE EVENTS COULD HAVE A MATERIAL ADVERSE EFFECT ON AIG'S FINANCIAL CONDITION, RESULTS OF OPERATIONS AND LIQUIDITY.

Measures Implemented to Control Hurricane and Earthquake Catastrophic Risk

Catastrophic risk from the earthquake and hurricane perils is proactively managed through reinsurance programs, and aggregate accumulation monitoring. Catastrophe reinsurance is purchased by AIG from financially sound reinsurers. Recoveries under this program, along with other non-catastrophic reinsurance protections, are reflected in the net values provided in the tables above. In addition to catastrophic reinsurance programs, hurricane and earthquake exposures are controlled by periodically monitoring aggregate exposures. The aggregate exposures are calculated by compiling total liability within AIG defined hurricane and earthquake catastrophe risk zones and therefore represent the maximum that could be lost in any individual zone. These aggregate accumulations are tracked over time in order to monitor both long- and short-term trends. AIG's major property writers, Lexington and AIG Private Client Group, have also implemented catastrophe-related underwriting procedures and manage their books at an account level. Lexington individually models most accounts prior to binding in order to specifically quantify catastrophic risk for each account.

Terrorism

Exposure to loss from terrorist attack is controlled by limiting the aggregate accumulation of workers compensation and property insurance that is underwritten within defined target locations. Modeling is used to provide projections of probable maximum loss by target location based upon the actual exposures of AIG policyholders.

Terrorism risk is monitored to manage AIG's exposure. AIG shares its exposures to terrorism risks under the Terrorism Risk Insurance Act, which was recently extended through December 31, 2014 by the Terrorism Risk Insurance Program Reauthorization Act of 2007 (TRIA). During 2007, AIG's deductible under TRIA was approximately $4.0 billion, with a 15 percent share of certified terrorism losses in excess of the deductible. As of January 1, 2008, the deductible increased to $4.2 billion, with a 15 percent share of certified terrorism losses in excess of the deductible. AIG actively monitors and controls its aggregate accumulated exposure within the parameters of the protection provided by the TRIA.

Life Insurance & Retirement Services

In Life Insurance & Retirement Services, the primary risks are the following:

- underwriting, which represents the exposure to loss resulting from the actual policy experience emerging adversely in comparison to the assumptions made in the product pricing associated with mortality, morbidity, termination and expenses; and
- investment risk which represents the exposure to loss resulting from the cash flows from the invested assets being less than the cash flows required to meet the obligations of the expected policy and contract liabilities and the necessary return on investments.

AIG businesses manage these risks through exposure limitations and the active management of the asset-liability relationship in their operations. The emergence of significant adverse experience would require an adjustment to DAC and benefit reserves that could have a material adverse effect on AIG's consolidated results of operations for a particular period.

AIG's Foreign Life Insurance & Retirement Services companies generally limit their maximum underwriting exposure on life insurance of a single life to approximately $1.7 million of coverage. AIG's Domestic Life Insurance & Retirement Services companies limit their maximum underwriting exposure on life insurance of a single life to $15 million of coverage in certain circumstances by using yearly renewable term reinsurance. In Life Insurance & Retirement Services, the reinsurance programs provide risk mitigation per policy, per individual life for life and group covers and for catastrophic risk events.

Pandemic Influenza

The potential for a pandemic influenza outbreak has received much recent attention. While outbreaks of the Avian Flu continue to occur among poultry or wild birds in a number of countries in Asia, Europe, including the U.K., and Africa, transmission to humans has been rare to date. If the virus mutates to a form that can be transmitted from human to human, it has the potential to spread rapidly worldwide. If such an outbreak were to take place, early quarantine and vaccination could be critical to containment.

The contagion and mortality rates of any mutated H5N1 virus that can be transmitted from human to human are highly speculative. AIG continues to monitor the developing facts. A significant global outbreak could have a material adverse effect on Life Insurance & Retirement Services operating results and liquidity from increased mortality and morbidity rates. AIG continues to analyze its exposure to this serious threat and has engaged an external risk management firm to model loss scenarios associated with an outbreak of Avian Flu. For a ''mild'' scenario, AIG estimates its after-tax net losses under its life insurance policies due to Avian Flu at approximately 2 percent of consolidated shareholders' equity as of December 31, 2007. This estimate was calculated over a 3-year period, although the

majority of the losses would be incurred in the first year. The modeled losses calculated were based on 2006 policy data representing approximately 92 percent of AIG's individual life, group life and credit life books of business, net of reinsurance. This estimate does not include claims that could be made under other policies, such as business interruption or general liability policies, and does not reflect estimates for losses resulting from disruption of AIG's own business operations or asset losses that may arise out of such a pandemic. The model used to generate this estimate has only recently been developed. The reasonableness of the model and its underlying assumptions cannot readily be verified by reference to comparable historical events. As a result, AIG's actual losses from a pandemic influenza outbreak are likely to vary significantly from those predicted by the model.

Financial Services

AIG's Financial Services subsidiaries engage in diversified activities including aircraft and equipment leasing, capital markets, consumer finance and insurance premium finance.

Capital Markets

The Capital Markets operations of AIG are conducted primarily through AIGFP, which engages as principal in standard and customized interest rate, currency, equity, commodity, energy and credit products with top-tier corporations, financial institutions, governments, agencies, institutional investors and high-net-worth individuals throughout the world.

The senior management of AIG defines the policies and establishes general operating parameters for Capital Markets operations. AIG's senior management has established various oversight committees to monitor on an ongoing basis the various financial market, operational and credit risk attendant to the Capital Markets operations. The senior management of AIGFP reports the results of its operations to and reviews future strategies with AIG's senior management.

AIGFP actively manages its exposures to limit potential economic losses, while maximizing the rewards afforded by these business opportunities even though some products or derivatives may result in operating income volatility. In doing so, AIGFP must continually manage a variety of exposures including credit, market, liquidity, operational and legal risks.

Derivative Transactions

A counterparty may default on any obligation to AIG, including a derivative contract. Credit risk is a consequence of extending credit and/or carrying trading and investment positions. Credit risk exists for a derivative contract when that contract has a positive fair value to AIG. The maximum potential exposure will increase or decrease during the life of the derivative commitments as a function of maturity and market conditions. To help manage this risk, AIGFP's credit department operates within the guidelines set by the CRC. Transactions which fall outside these pre-established guidelines require the specific approval of the CRC. It is also AIG's policy to establish reserves for potential credit impairment when necessary.

In addition, AIGFP utilizes various credit enhancements, including letters of credit, guarantees, collateral, credit triggers, credit derivatives and margin agreements to reduce the credit risk relating to its outstanding financial derivative transactions. AIGFP requires credit enhancements in connection with specific transactions based on, among other things, the creditworthiness of the counterparties, and the transaction's size and maturity. Furthermore, AIGFP generally seeks to enter into agreements that have the benefit of set-off and close-out netting provisions. These provisions provide that, in the case of an early termination of a transaction, AIGFP can setoff its receivables from a counterparty against its payables to the same counterparty arising out of all covered transactions. As a result, where a legally enforceable netting agreement exists, the fair value of the transaction with the counterparty represents the net sum of estimated positive fair values. The fair value of AIGFP's interest rate, currency, commodity and equity swaps, options, swaptions, and forward commitments, futures, and forward contracts approximated $17.13 billion at December 31, 2007 and $19.61 billion at December 31, 2006. Where applicable, these amounts have been determined in accordance with the respective master netting agreements.

AIGFP evaluates the counterparty credit quality by reference to ratings from rating agencies or, where such ratings are not available, by internal analysis consistent with the risk rating policies of the CRC. In addition, AIGFP's credit approval process involves pre-set counterparty and country credit exposure limits and, for particularly credit-intensive transactions, requires approval from the CRC. AIG estimates that the average credit rating of Capital Markets derivatives counterparties, measured by reference to the fair value of its derivative portfolio as a whole, is equivalent to the AA rating category.

At December 31, 2007 and 2006, the fair value of Capital Markets derivatives portfolios by counterparty credit rating was as follows:

(in millions)	**2007**	2006
Rating:		
AAA	**$ 5,069**	$ 5,465
AA	**5,166**	8,321
A	**4,796**	3,690
BBB	**1,801**	2,032
Below investment grade	**302**	99
Total	**$17,134**	$19,607

Credit Derivatives

AIGFP enters into credit derivative transactions in the ordinary course of its business. The majority of AIGFP's credit derivatives require AIGFP to provide credit protection on a designated portfolio of loans or debt securities. AIGFP provides such credit protection on a ''second loss'' basis, under which AIGFP's payment obligations arise only after credit losses in the designated portfolio exceed a specified threshold amount or level of ''first losses.'' The threshold amount of credit losses that must be realized before AIGFP has any payment obligation is negotiated

by AIGFP for each transaction to provide that the likelihood of any payment obligation by AIGFP under each transaction is remote, even in severe recessionary market scenarios. The underwriting process for these derivatives included assumptions of severely stressed recessionary market scenarios to minimize the likelihood of realized losses under these obligations.

In certain cases, the credit risk associated with a designated portfolio is tranched into different layers of risk, which are then analyzed and rated by the credit rating agencies. Typically, there will be an equity layer covering the first credit losses in respect of the portfolio up to a specified percentage of the total portfolio, and then successive layers ranging from generally a BBB-rated layer to one or more AAA-rated layers. In transactions that are rated with respect to the risk layer or tranche that is immediately junior to the threshold level above which AIGFP's payment obligation would generally arise, a significant majority are rated AAA by the rating agencies. In transactions that are not rated, AIGFP applies the same risk criteria for setting the threshold level for its payment obligations. Therefore, the risk layer assumed by AIGFP with respect to the designated portfolio in these transactions is often called the ''super senior'' risk layer, defined as the layer of credit risk senior to a risk layer that has been rated AAA by the credit rating agencies, or if the transaction is not rated, equivalent thereto.

At December 31, 2007 the notional amounts and unrealized market valuation loss of the super senior credit default swap portfolio by asset classes were as follows:

	Notional Amount (in billions)	Unrealized Market Valuation Loss (in millions)
Corporate loans[(a)]	**$230**	$ —
Prime residential mortgages[(a)]	**149**	—
Corporate Debt/CLOs	**70**	226
Multi-sector CDO[(b)]	**78**	11,246
Total	**$527**	$11,472

(a) Predominantly represent transactions written to facilitate regulatory capital relief.

(b) Approximately $61.4 billion in notional amount of the multi-sector CDO pools include some exposure to U.S. subprime mortgages.

Approximately $379 billion (consisting of the corporate loans and prime residential mortgages) of the $527 billion in notional exposure of AIGFP's super senior credit default swap portfolio as of December 31, 2007 represents derivatives written for financial institutions, principally in Europe, for the purpose of providing them with regulatory capital relief rather than risk mitigation. In exchange for a minimum guaranteed fee, the counterparties receive credit protection in respect of diversified loan portfolios they own, thus improving their regulatory capital position. These derivatives are generally expected to terminate at no additional cost to the counterparty upon the counterparty's adoption of models compliant with the Basel II Accord. AIG expects that the majority of these transactions will be terminated within the next 12 to 18 months by AIGFP's counterparties as they implement models compliant with the new Basel II Accord. As of February 26, 2008, $54 billion in notional exposures have either been terminated or are in the process of being terminated. AIGFP was not required to make any payments as part of these terminations and in certain cases was paid a fee upon termination. In light of this experience to date and after other comprehensive analyses, AIG did not recognize an unrealized market valuation adjustment for this regulatory capital relief portfolio for the year ended December 31, 2007. AIG will continue to assess the valuation of this portfolio and monitor developments in the marketplace. There can be no assurance that AIG will not recognize unrealized market valuation losses from this portfolio in future periods. In addition to writing credit protection on the super senior risk layer on designated portfolios of loans or debt securities, AIGFP also wrote protection on tranches below the super senior risk layer. At December 31, 2007 the notional amount of the credit default swaps in the regulatory capital relief portfolio written on tranches below the super senior risk layer was $5.8 billion, with an estimated fair value of $(25) million.

AIGFP has also written credit protection on the super senior risk layer of diversified portfolios of investment grade corporate debt, collateralized loan obligations (CLOs) and multi-sector CDOs. AIGFP is at risk only on the super senior portion related to a diversified portfolio referenced to loans or debt securities. The super senior risk portion is the last tranche to suffer losses after significant subordination. Credit losses would have to erode all tranches junior to the super senior tranche before AIGFP would suffer any realized losses. The subordination level required for each transaction is determined based on internal modeling and analysis of the pool of underlying assets and is not dependent on ratings determined by the rating agencies. While the credit default swaps written on corporate debt obligations are cash settled, the majority of the credit default swaps written on CDOs and CLOs require physical settlement. Under a physical settlement arrangement, AIGFP would be required to purchase the referenced super senior security at par in the event of a non-payment on that security.

Certain of these credit derivatives are subject to collateral posting provisions. These provisions differ among counterparties and asset classes. In the case of most of the multi-sector CDO transactions, the amount of collateral required is determined based on the change in value of the underlying cash security that represents the super senior risk layer subject to credit protection, and not the change in value of the super senior credit derivative.

AIGFP is indirectly exposed to U.S. residential mortgage subprime collateral in the CDO portfolios, the majority of which is from 2004 and 2005 vintages. However, certain of the CDOs on which AIGFP provided credit protection permit the collateral manager to substitute collateral during the reinvestment period, subject to certain restrictions. As a result, in certain transactions, U.S. residential mortgage subprime collateral of 2006 and 2007 vintages has been added to the collateral pools. At December 31, 2007, U.S. residential mortgage subprime collateral of 2006 and 2007 vintages comprised approximately 4.9 percent of the total collateral pools underlying the entire portfolio of CDOs with credit protection.

AIGFP has written 2a-7 Puts in connection with certain multi-sector CDOs that allow the holders of the securities to treat the securities as eligible short-term 2a-7 investments under the

Investment Company Act of 1940. Holders of securities are permitted, in certain circumstances, to tender their securities to the issuers at par. If an issuer's remarketing agent is unable to resell the securities so tendered, AIGFP must purchase the securities at par as long as the security has not experienced a default. During 2007, AIGFP repurchased securities with a principal amount of approximately $754 million pursuant to these obligations. In certain transactions, AIGFP has contracted with third parties to provide liquidity for the securities if they are put to AIGFP for up to a three-year period. Such liquidity facilities totaled approximately $3 billion at December 31, 2007. As of February 26, 2008, AIGFP has not utilized these liquidity facilities. At December 31, 2007, AIGFP had approximately $6.5 billion of notional exposure on 2a-7 Puts, included as part of the multi-sector CDO portfolio discussed herein.

As of January 31, 2008, a significant majority of AIGFP's super senior exposures continued to have tranches below AIGFP's attachment point that have been explicitly rated AAA or, in AIGFP's judgment, would have been rated AAA had they been rated. AIGFP's portfolio of credit default swaps undergoes regular monitoring, modeling and analysis and contains protection through collateral subordination.

AIGFP accounts for its credit default swaps in accordance with FAS 133 ''Accounting For Derivative Instruments and Hedging Activities'' and Emerging Issues Task Force 02-3, ''Issues Involved in Accounting for Derivative Contracts Held for Trading Purposes and Contracts Involved in Energy Trading and Risk Management Activities'' (EITF 02-3). In accordance with EITF 02-3, AIGFP does not recognize income in earnings at the inception of each transaction because the inputs to value these instruments are not derivable from observable market data.

The valuation of the super senior credit derivatives has become increasingly challenging given the limitation on the availability of market observable information due to the lack of trading and price transparency in the structured finance market, particularly in the fourth quarter of 2007. These market conditions have increased the reliance on management estimates and judgments in arriving at an estimate of fair value for financial reporting purposes. Further, disparities in the valuation methodologies employed by market participants and the varying judgments reached by such participants when assessing volatile markets has increased the likelihood that the various parties to these instruments may arrive at significantly different estimates as to their fair values.

AIGFP's valuation methodologies for the super senior credit default swap portfolio have evolved in response to the deteriorating market conditions and the lack of sufficient market observable information. AIG has sought to calibrate the model to market information and to review the assumptions of the model on a regular basis.

AIGFP employs a modified version of the BET model to value its super senior credit default swap portfolio, including the 2a-7 Puts. The BET model utilizes default probabilities derived from credit spreads implied from market prices for the individual securities included in the underlying collateral pools securing the CDOs. AIGFP obtained prices on these securities from the CDO collateral managers.

The BET model also utilizes diversity scores, weighted average lives, recovery rates and discount rates. The determination of some of these inputs require the use of judgment and estimates, particularly in the absence of market observable data. AIGFP also employed a Monte Carlo simulation to assist in quantifying the effect on valuation of the CDO of the unique features of the CDO's structure such as triggers that divert cash flows to the most senior level of the capital structure.

The credit default swaps written by AIGFP cover only the failure of payment on the super senior CDO security. AIGFP does not own the securities in the CDO collateral pool. The credit spreads implied from the market prices of the securities in the CDO collateral pool incorporate the risk of default (credit risk), the market's price for liquidity risk and in distressed markets, the risk aversion costs. Spreads on credit derivatives tend to be narrower because, unlike in the case of investing in a bond, there is no need to fund the position (except when an actual credit event occurs). In times of illiquidity, the difference between spreads on cash securities and derivative instruments (the ''negative basis'') may be even wider for high quality assets. AIGFP was unable to reliably verify this negative basis due to the accelerating severe dislocation, illiquidity and lack of trading in the asset backed securities market during the fourth quarter of 2007 and early 2008. The valuations produced by the BET model therefore represent the valuations of the underlying super senior CDO cash securities with no recognition of the effect of the basis differential on that valuation.

AIGFP also considered the valuation of the super senior CDO securities provided by third parties, including counterparties to these transactions, and made adjustments as necessary.

As described above, AIGFP uses numerous assumptions in determining its best estimate of the fair value of the super senior credit default swap portfolio. The most significant assumption utilized in developing the estimate is the pricing of the securities within the CDO collateral pools. If the actual pricing of the securities within the collateral pools differs from the pricing used in estimating the fair value of the super senior credit default swap portfolio, there is potential for significant variation in the fair value estimate. A decrease by five points (for example, from 87 cents per dollar to 82 cents per dollar) in the aggregate price of the securities would cause an additional unrealized market valuation loss of approximately $3.7 billion, while an increase in the aggregate price of the securities by five points (for example, from 90 cents per dollar to 95 cents per dollar) would reduce the unrealized market valuation loss by approximately $3 billion. The effect on the unrealized market valuation loss is not proportional to the change in the aggregate price of the securities.

In the case of credit default swaps written on investment grade corporate debt and CLOs, AIGFP estimated the value of its obligations by reference to the relevant market indices or third party quotes on the underlying super senior tranches where available.

AIGFP monitors the underlying portfolios to determine whether the credit loss experience for any particular portfolio has caused

the likelihood of AIGFP having a payment obligation under the transaction to be greater than super senior risk.

As of February 26, 2008, AIGFP had received collateral calls from counterparties in respect of certain super senior credit default swaps (including those entered into by counterparties for regulatory capital relief purposes and those in respect of corporate debt/CLOs). AIG is aware that valuation estimates made by certain of the counterparties with respect to certain super senior credit default swaps or the underlying reference CDO securities, for purposes of determining the amount of collateral required to be posted by AIGFP in connection with such instruments, differ significantly from AIGFP's estimates. AIGFP has been able to successfully resolve some of the differences, including in certain cases entering into compromise collateral arrangements, some of which are for specified periods of time. AIGFP is also in discussions with other counterparties to resolve such valuation differences. As of February 26, 2008, AIGFP had posted collateral (or had received collateral, where offsetting exposures on other transactions resulted in the counterparty posting to AIGFP) based on exposures, calculated in respect of super senior default swaps, in an aggregate amount of approximately $5.3 billion. Valuation estimates made by counterparties for collateral purposes were considered in the determination of the fair value estimates of AIGFP's super senior credit default swap portfolio.

Both AIG's ERM department and AIGFP have conducted risk analyses of the super senior multi-sector CDO credit default swap portfolio of AIGFP. There is currently no probable and reasonably estimable realized loss in this portfolio at December 31, 2007. AIG's analyses have been conducted to assess the risk of incurring net realized losses over the remaining life of the portfolio. In addition to analyses of each individual risk in the portfolio, AIG conducted certain ratings-based stress tests, which centered around scenarios of further stress on the portfolio resulting from downgrades by the rating agencies from current levels on the underlying collateral in the CDO structures supported by AIGFP's credit default swaps. These rating actions would be prompted by factors such as the worsening beyond current estimates of delinquency and residential housing price deterioration in the underlying assets in the collateral securities of the CDO structures. The results of these stress tests indicated possible realized losses on a static basis, since the assumptions of losses in these stress tests assumed immediate realization of loss. Actual realized losses would only be experienced over time given the timing of losses incurred in the underlying portfolios and the timing of breaches of the subordination afforded to AIGFP through the structures of the CDO. No benefit was taken in these stress tests for cash flow diversion features, recoveries upon default or other risk mitigant benefits. Based on these analyses and stress tests, AIG believes that any losses realized over time by AIGFP as a result of meeting its obligations under these derivatives will not be material to AIG's consolidated financial condition, although it is possible that such realized losses could be material to AIG's consolidated results of operations for an individual reporting period.

Capital Markets Trading VaR

AIGFP attempts to minimize risk in benchmark interest rates, equities, commodities and foreign exchange. Market exposures in option implied volatilities, correlations and basis risks are also minimized over time but those are the main types of market risks that AIGFP manages.

AIGFP's minimal reliance on market risk driven revenue is reflected in its VaR. AIGFP's VaR calculation is based on the interest rate, equity, commodity and foreign exchange risk arising from its portfolio. Credit-related factors, such as credit spreads or credit default, are not included in AIGFP's VaR calculation. Because the market risk with respect to securities available for sale, at market, is substantially hedged, segregation of the financial instruments into trading and other than trading was not deemed necessary. AIGFP operates under established market risk limits based upon this VaR calculation. In addition, AIGFP backtests its VaR.

In the calculation of VaR for AIGFP, AIG uses the historical simulation methodology based on estimated changes to the value of all transactions under explicit changes in market rates and prices within a specific historical time period. AIGFP attempts to secure reliable and independent current market prices, such as published exchange prices, external subscription services such as Bloomberg or Reuters, or third-party or broker quotes. When such prices are not available, AIGFP uses an internal methodology which includes extrapolation from observable and verifiable prices nearest to the dates of the transactions. Historically, actual results have not deviated from these models in any material respect.

AIGFP reports its VaR level using a 95 percent confidence interval and a one-day holding period, facilitating risk comparison with AIGFP's trading peers and reflecting the fact that market risks can be actively assumed and offset in AIGFP's trading portfolio.

The following table presents the year-end, average, high, and low VaRs* on a diversified basis and of each component of market risk for Capital Markets operations for the years 2007 and 2006. The diversified VaR is usually smaller than the sum of its components due to correlation effects.

		For the Year Ended December 31, 2007				For the Year Ended December 31, 2006		
(in millions)	As of December 31	Average	High	Low	As of December 31	Average	High	Low
Total AIG trading market risk:								
Diversified	**$5**	**$5**	**$8**	**$4**	$4	$4	$7	$3
Interest rate	**3**	**2**	**3**	**2**	2	2	3	1
Currency	**1**	**1**	**2**	**1**	1	1	3	1
Equity	**3**	**3**	**5**	**2**	3	3	4	2
Commodity	**3**	**3**	**7**	**2**	5	3	5	2

** The VaR calculation has been changed from a 3-year time series to a 5-year time series. The December 31, 2006 VaR reflects this change.*

Aircraft Leasing

AIG's Aircraft Leasing operations represent the operations of ILFC, which generates its revenues primarily from leasing new and used commercial jet aircraft to foreign and domestic airlines and companies associated with the airline industry. Risks inherent in this business, and which are managed at the business unit level, include the following:

- the risk that there will be no market for the aircraft acquired;
- the risk that aircraft cannot be placed with lessees;
- the risk of nonperformance by lessees; and
- the risk that aircraft and related assets cannot be disposed of at the time and in a manner desired.

The airline industry is sensitive to changes in economic conditions and is cyclical and highly competitive. Airlines and related companies may be affected by political or economic instability, terrorist activities, changes in national policy, competitive pressures on certain air carriers, fuel prices and shortages, labor stoppages, insurance costs, recessions, world health issues and other political or economic events adversely affecting world or regional trading markets.

ILFC's revenues and operating income may be adversely affected by the volatile competitive environment in which its customers operate. ILFC is exposed to operating loss and liquidity strain through nonperformance of aircraft lessees, through owning aircraft which it is unable to sell or re-lease at acceptable rates at lease expiration and, in part, through committing to purchase aircraft which it is unable to lease.

ILFC manages the risk of nonperformance by its lessees with security deposit requirements, repossession rights, overhaul requirements and close monitoring of industry conditions through its marketing force. Approximately 90 percent of ILFC's fleet is leased to non-U.S. carriers, and the fleet, comprised of the most efficient aircraft in the airline industry, continues to be in high demand from such carriers.

Management formally reviews regularly, and no less frequently than quarterly, issues affecting ILFC's fleet, including events and circumstances that may cause impairment of aircraft values. Management evaluates aircraft in the fleet as necessary based on these events and circumstances in accordance with Statement of Financial Accounting Standards No. 144, ''Accounting for the Impairment or Disposal of Long-Lived Assets'' (FAS 144). ILFC has not recognized any impairment related to its fleet in 2007, 2006 or 2005. ILFC has been able to re-lease the aircraft without diminution in lease rates that would result in an impairment under FAS 144.

Consumer Finance

AIG's Consumer Finance operations provide a wide variety of consumer finance products, including real estate and other consumer loans, credit card loans, retail sales finance and credit-related insurance to customers both domestically and overseas, particularly in emerging markets. Consumer Finance operations include AGF as well as AIGCFG. AGF provides a wide variety of consumer finance products, including real estate loans, non-real estate loans, retail sales finance and credit-related insurance to customers in the United States, the U.K., Puerto Rico and the U.S. Virgin Islands. AIGCFG, through its subsidiaries, is engaged in developing a multi-product consumer finance business with an emphasis on emerging markets.

Many of AGF's borrowers are non-prime or subprime. The real estate loans are comprised principally of first-lien mortgages on residential real estate generally having a maximum term of 360 months, and are considered non-conforming. The real estate loans may be closed-end accounts or open-end home equity lines of credit and are principally fixed rate products. AGF does not offer mortgage products with borrower payment options that allow for negative amortization of the principal balance. The secured non-real estate loans are secured by consumer goods, automobiles or other personal property. Both secured and unsecured non-real estate loans and retail sales finance receivables generally have a maximum term of 60 months.

Current economic conditions, such as interest rate and employment levels, can have a direct effect on the borrowers' ability to repay these loans. AGF manages the credit risk inherent in its portfolio by using credit scoring models at the time of credit applications, established underwriting criteria, and, in certain cases, individual loan reviews. AGF monitors the quality of the finance receivables portfolio and determines the appropriate level of the allowance for losses through its Credit Strategy and Policy Committee. This Committee bases its conclusions on quantitative analyses, qualitative factors, current economic conditions and trends, and each Committee member's experience in the consumer finance industry.

Through 2007, the overall credit quality of AGF's finance receivables portfolio deteriorated modestly primarily due to negative economic fundamentals, a higher proportion of non-real estate loans and retail sales finance loans and the aging of the real estate loan portfolio. As of December 31, 2007, the 60-day delinquency rate for the entire portfolio increased by 78 basis points to 2.84 percent compared to 2006, while the 60-day delinquency rate for the real estate loans increased by 88 basis points to 2.64 percent. In 2007, AGF's net charge-off rate increased to 1.16 percent compared to 0.95 percent in 2006, which reflected $6 million of non-recurring recoveries. Further weakening in the U.S. housing market or the overall U.S. economy may adversely affect the credit quality of AGF's finance receivables.

AIGCFG monitors the quality of its finance receivable portfolio and determines the appropriate level of the allowance for losses through several internal committees. These committees base their conclusions on quantitative analysis, qualitative factors, current economic conditions and trends, political and regulatory implications, competition and the judgment of the committees' members.

AIG's Consumer Finance operations are exposed to credit risk and risk of loss resulting from adverse fluctuations in interest rates and payment defaults. Credit loss exposure is managed through a combination of underwriting controls, mix of finance receivables, collateral and collection efficiency. Large product programs are subject to CRC approval.

Over half of the finance receivables are real estate loans which are collateralized by the related properties. With respect to credit losses, the allowance for losses is maintained at a level considered adequate to absorb anticipated credit losses existing in that portfolio as of the balance sheet date.

Asset Management

AIG's Asset Management operations are exposed to various forms of credit, market and operational risks. Asset Management complies with AIG's corporate risk management guidelines and framework and is subject to periodic reviews by the CRC. In addition, transactions are referred to the Asset Management investment committees for approval of investment decisions.

The majority of the credit and market risk exposures within Asset Management results from the Spread-Based Investment business and the investment activities of AIG Global Real Estate.

In the Spread-Based Investment businesses, GIC and MIP, the primary risk is investment risk, which represents the exposure to loss resulting from the cash flows from the invested assets being less than the cash flows required to meet the obligations of the liabilities and the necessary return on investments. Credit risk is also a significant component of the investment strategy for these businesses. Market risk is taken in the form of duration and convexity risk. While AIG generally maintains a matched asset-liability relationship, it may occasionally determine that it is economically advantageous to be in an unmatched duration position. The risks in the spread-based businesses are managed through exposure limitations, active management of the investment portfolios and close oversight of the asset-liability relationship.

AIG Global Real Estate is exposed to the general conditions in global real estate markets and the credit markets. Such exposure can subject Asset Management to delays in real estate property development and sales, additional carrying costs and in turn affect operating results within the segment. These risks are mitigated through the underwriting process, transaction and contract terms and conditions and portfolio diversification by type of project, sponsor, real estate market and country. AIG's exposure to real estate investments is monitored on an ongoing basis by the Asset Management Real Estate Investment Committee.

Asset Management is also exposed to market risk with respect to the warehoused investing activities of AIG Investments. During the warehousing period, AIG bears the cost and risks associated with carrying these investments and consolidates them on its balance sheet and records the operating results until the investments are transferred, sold or otherwise divested. Changes in market conditions may negatively affect the fair value of these warehoused investments. Market conditions may impede AIG from launching new investment products for which these warehoused assets are being held, which could result in AIG not recovering its investment upon transfer or divestment. In the event that AIG is unable to transfer or otherwise divest its interest in the warehoused investment to third parties, AIG could be required to hold these investments indefinitely.

Economic Capital

Since mid-2005, AIG has been developing a firm-wide economic capital model to improve decision making and to enhance shareholder value. Economic Capital is the amount of capital the organization, its segments, profit centers, products or transactions require to cover potential, unexpected losses within a confidence level consistent with the risk appetite and risk tolerances specified by management. The Economic Capital requirement can then be compared with the Economic Capital resources available to AIG.

The Economic Capital requirement is driven by exposures to risks and interrelationships among various types of risks. As a global leader in insurance and financial services, AIG is exposed to various risks including underwriting, financial and operational risks. The Economic Capital initiative has modeled these risks into five major categories: property & casualty insurance risk, life insurance risk, market risk, credit risk and operational risk. Within each risk category, there are sub-risks that have been modeled in greater detail. The Economic Capital initiative also analyzes the interrelationships among various types of risk, aggregate exposure accumulation and concentration, and includes diversification benefits within and across risk categories and business segments.

A primary objective of the Economic Capital initiative is to develop a comprehensive framework to discuss capital and performance on a risk-adjusted basis internally with AIG management and externally with the investment community, credit providers, regulators and rating agencies. Economic Capital analysis provides a framework to validate AIG's capital adequacy, to measure more precisely capital efficiency at various levels throughout the organization, to allocate capital consistently among

AIG's businesses, to quantify the specific areas of diversification benefits and to assess relative economic value added by a business, product or transaction to AIG as a whole. The Economic Capital initiative will also provide necessary and relevant analyses and inputs in developing a more efficient capital structure. Other key areas of Economic Capital applications include strategic decision-making for mergers, acquisitions and divestitures, risk accumulation and concentration, risk retention, reinsurance and hedging strategies and product development and pricing.

During 2006, AIG developed a methodology framework that incorporates financial services industry best practices, maintains consistency with regulatory frameworks and reflects AIG's distinct global business and management strategies. By utilizing stochastic simulation techniques, where appropriate, AIG enhanced existing models or developed new ones through a collaborative effort among business executives, actuaries, finance specialists and risk professionals. The initial assessments provided useful insight into the overall capital strength of AIG and its segments.

Throughout 2007, AIG's focus has been on a wide range of business applications of the model together with the continued enhancement of the granularity of the model. Key methodology enhancements introduced during 2007 include capital fungibility and diversification among legal entities, business units and geographic regions, consistent economic scenarios in developed and developing markets, and extensive catastrophic scenario analysis and stress testing. Furthermore, AIG enhanced its comprehensive set of risk governance structures to support the model's inputs, assumptions and methodologies. Finally, AIG has engaged a panel of independent experts to provide further assurance to AIG's senior management, business segment executives and external constituents as to the validity of the model and its results for business segments and for AIG in the aggregate.

Besides model enhancements and firm-wide capital strength analysis, during 2007 AIG also incorporated its Economic Capital model and analysis into a number of specific business issues and in developing new business strategies. For example, economic capital analysis is being incorporated into the assessment phase for mergers, acquisitions and divestures, and in the development of capital markets solutions. In the reinsurance area, economic capital considerations are fundamental to the development of optimal risk retention and reinsurance strategies and management of credit exposures to reinsurance counterparties. In the Life Insurance & Retirement Services segment, the Economic Capital model has been used for product development, pricing and hedging strategies for living benefits in the variable annuity business. For life insurance products in Asian markets, enhanced asset-liability management strategies have been formulated for long duration liability structures and low interest rate environments in certain markets using the technology developed for AIG's Economic Capital model.

In 2008, AIG plans to extend the model's application by building on the work performed in 2007 for a wider range of businesses, segments, geographies and product lines. Commencing in 2008, the economic value added for each of AIG's business segments will be considered as an element, alongside other existing measures, in the evaluation of senior management performance. The capital planning and allocation process will continue to be enhanced by incorporating the regulatory, rating agency and economic capital requirements for business segments as well as the assessment of the mobility of excess economic capital.

Recent Accounting Standards

Accounting Changes

In September 2005, the American Institute of Certified Public Accountants (AICPA) issued Statement of Position 05-1, ''Accounting by Insurance Enterprises for Deferred Acquisition Costs in Connection with Modifications or Exchanges of Insurance Contracts.''

In February 2006, the Financial Accounting Standards Board (FASB) issued FAS 155, ''Accounting for Certain Hybrid Financial Instruments — an amendment of FAS 140 and FAS 133.''

In July 2006, the FASB issued FASB Interpretation No. 48, ''Accounting for Uncertainty in Income Taxes — an interpretation of FASB Statement No. 109.''

In July 2006, the FASB issued FASB Staff Position (FSP) No. 13-2, ''Accounting for a Change or Projected Change in the Timing of Cash Flows Relating to Income Taxes Generated by a Leveraged Lease Transaction.''

In September 2006, the FASB issued FAS No. 157, ''Fair Value Measurements.''

In September 2006, the FASB issued FAS 158, ''Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans — an amendment of FASB Statements No. 87, 88, 106 and 132R.''

In February 2007, the FASB issued FAS No. 159, ''The Fair Value Option for Financial Assets and Financial Liabilities.''

In June 2007, the AICPA issued Statement of Position No. 07-1, ''Clarification of the Scope of the Audit and Accounting Guide 'Audits of Investment Companies' and Accounting by Parent Companies and Equity Method Investors for Investments in Investment Companies.'' (Indefinitely deferred by the FASB)

In December 2007, the FASB issued FAS No. 141 (revised 2007), ''Business Combinations.''

In December 2007, the FASB issued FAS No. 160, ''Noncontrolling Interests in Consolidated Financial Statements, an amendment of ARB No. 51.''

For further discussion of these recent accounting standards and their application to AIG, see Note 1(hh) to Consolidated Financial Statements.

Item 7A.
Quantitative and Qualitative Disclosures About Market Risk

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

Item 8.
Financial Statements and Supplementary Data

American International Group, Inc. and Subsidiaries Index to Financial Statements and Schedules

Report of Independent Registered Public Accounting Firm

To the Board of Directors and Shareholders of American International Group, Inc.:

In our opinion, the consolidated financial statements listed in the accompanying index present fairly, in all material respects, the financial position of American International Group, Inc. and its subsidiaries (AIG) at December 31, 2007 and 2006, and the results of their operations and their cash flows for each of the three years in the period ended December 31, 2007 in conformity with accounting principles generally accepted in the United States of America. In addition, in our opinion, the financial statement schedules listed in the accompanying index present fairly, in all material respects, the information set forth therein when read in conjunction with the related consolidated financial statements. Also in our opinion, AIG did not maintain, in all material respects, effective internal control over financial reporting as of December 31, 2007, based on criteria established in *Internal Control — Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO) because a material weakness in internal control over financial reporting related to the AIGFP super senior credit default swap portfolio valuation process and oversight thereof existed as of that date. A material weakness is a deficiency, or a combination of deficiencies, in internal control over financial reporting, such that there is a reasonable possibility that a material misstatement of the annual or interim financial statements will not be prevented or detected on a timely basis. The material weakness referred to above is described in Management's Report on Internal Control Over Financial Reporting appearing under Item 9A. We considered this material weakness in determining the nature, timing, and extent of audit tests applied in our audit of the 2007 consolidated financial statements, and our opinion regarding the effectiveness of AIG's internal control over financial reporting does not affect our opinion on those consolidated financial statements. AIG's management is responsible for these financial statements and financial statement schedules, for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting, included in management's report referred to above. Our responsibility is to express opinions on these financial statements, on the financial statement schedules, and on AIG's internal control over financial reporting based on our integrated audits. We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement and whether effective internal control over financial reporting was maintained in all material respects. Our audits of the financial statements included examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. Our audit of internal control over financial reporting included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, and testing and evaluating the design and operating effectiveness of internal control based on the assessed risk. Our audits also included performing such other procedures as we considered necessary in the circumstances. We believe that our audits provide a reasonable basis for our opinions.

As described in Note 1 to the consolidated financial statements, as of January 1, 2007, AIG changed the manner in which it accounts for internal replacements of certain insurance and investment contracts, uncertainty in income taxes, and changes or projected changes in the timing of cash flows relating to income taxes generated by leveraged lease transactions.

As described in Notes 1 and 17 to the consolidated financial statements, AIG changed its accounting for certain hybrid financial instruments, life settlement contracts and share based compensation as of January 1, 2006, and certain employee benefit plans as of December 31, 2006.

A company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (i) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (ii) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (iii) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

PricewaterhouseCoopers LLP
New York, New York
February 28, 2008

Consolidated Balance Sheet

December 31, *(in millions)*	**2007**	2006
Assets:		
Investments and financial services assets:		
Fixed maturities:		
Bonds available for sale, at fair value (amortized cost: 2007 — $393,170; 2006 — $377,163)	**$ 397,372**	$386,869
Bonds held to maturity, at amortized cost (fair value: 2007 — $22,157; 2006 — $22,154)	**21,581**	21,437
Bond trading securities, at fair value (includes hybrid financial instruments: 2007 — $555; 2006 — $522)	**9,982**	10,836
Equity securities:		
Common stocks available for sale, at fair value (cost: 2007 — $12,588; 2006 — $10,662)	**17,900**	13,256
Common and preferred stocks trading, at fair value	**21,376**	14,855
Preferred stocks available for sale, at fair value (cost: 2007 — $2,600; 2006 — $2,485)	**2,370**	2,539
Mortgage and other loans receivable, net of allowance (2007 — $77; 2006 — $64) (includes loans held for sale: 2007 — $399)	**33,727**	28,418
Financial services assets:		
Flight equipment primarily under operating leases, net of accumulated depreciation (2007 — $10,499; 2006 — $8,835)	**41,984**	39,875
Securities available for sale, at fair value (cost: 2007 — $40,157; 2006 — $45,912)	**40,305**	47,205
Trading securities, at fair value	**4,197**	5,031
Spot commodities	**238**	220
Unrealized gain on swaps, options and forward transactions	**16,442**	19,252
Trade receivables	**6,467**	4,317
Securities purchased under agreements to resell, at contract value	**20,950**	30,291
Finance receivables, net of allowance (2007 — $878; 2006 — $737) (includes finance receivables held for sale: 2007 — $233; 2006 — $1,124)	**31,234**	29,573
Securities lending invested collateral, at fair value (cost: 2007 — $80,641; 2006 — $69,306)	**75,662**	69,306
Other invested assets	**58,823**	42,111
Short-term investments, at cost (approximates fair value)	**51,351**	27,483
Total investments and financial services assets	**851,961**	792,874
Cash	**2,284**	1,590
Investment income due and accrued	**6,587**	6,091
Premiums and insurance balances receivable, net of allowance (2007 — $662; 2006 — $756)	**18,395**	17,789
Reinsurance assets, net of allowance (2007 — $520; 2006 — $536)	**23,103**	23,355
Deferred policy acquisition costs	**43,150**	37,235
Investments in partially owned companies	**654**	1,101
Real estate and other fixed assets, net of accumulated depreciation (2007 — $5,446; 2006 — $4,940)	**5,518**	4,381
Separate and variable accounts	**78,684**	70,277
Goodwill	**9,414**	8,628
Other assets	**20,755**	16,089
Total assets	**$1,060,505**	$979,410

See Accompanying Notes to Consolidated Financial Statements.

Consolidated Balance Sheet *Continued*

December 31, *(in millions, except share data)*	**2007**	2006
Liabilities:		
Reserve for losses and loss expenses	**$ 85,500**	$ 79,999
Unearned premiums	**28,022**	26,271
Future policy benefits for life and accident and health insurance contracts	**136,068**	121,004
Policyholders' contract deposits	**258,459**	248,264
Other policyholders' funds	**12,599**	10,986
Commissions, expenses and taxes payable	**6,310**	5,305
Insurance balances payable	**4,878**	3,789
Funds held by companies under reinsurance treaties	**2,501**	2,602
Income taxes payable	**3,823**	9,546
Financial services liabilities:		
Securities sold under agreements to repurchase, at contract value	**8,331**	19,677
Trade payables	**10,568**	6,174
Securities and spot commodities sold but not yet purchased, at fair value	**4,709**	4,076
Unrealized loss on swaps, options and forward transactions	**20,613**	11,401
Trust deposits and deposits due to banks and other depositors	**4,903**	5,249
Commercial paper and extendible commercial notes	**13,114**	13,363
Long-term borrowings	**162,935**	135,316
Separate and variable accounts	**78,684**	70,277
Securities lending payable	**81,965**	70,198
Minority interest	**10,422**	7,778
Other liabilities (includes hybrid financial instruments at fair value: 2007 — $47; 2006 — $111)	**30,200**	26,267
Total liabilities	**964,604**	877,542
Preferred shareholders' equity in subsidiary companies	**100**	191
Commitments, Contingencies and Guarantees (See Note 12)		
Shareholders' equity:		
Common stock, $2.50 par value; 5,000,000,000 shares authorized; shares issued 2007 and 2006 — 2,751,327,476	**6,878**	6,878
Additional paid-in capital	**2,848**	2,590
Payments advanced to purchase shares	**(912)**	—
Retained earnings	**89,029**	84,996
Accumulated other comprehensive income (loss)	**4,643**	9,110
Treasury stock, at cost; 2007 — 221,743,421; 2006 — 150,131,273 shares of common stock (including 119,293,487 and 119,278,644 shares, respectively, held by subsidiaries)	**(6,685)**	(1,897)
Total shareholders' equity	**95,801**	101,677
Total liabilities, preferred shareholders' equity in subsidiary companies and shareholders' equity	**$1,060,505**	$ 979,410

See Accompanying Notes to Consolidated Financial Statements.

Consolidated Statement of Income

Years Ended December 31, *(in millions, except per share data)*	2007	2006	2005
Revenues:			
Premiums and other considerations	$ 79,302	$ 74,213	$ 70,310
Net investment income	28,619	26,070	22,584
Net realized capital gains (losses)	(3,592)	106	341
Unrealized market valuation losses on AIGFP super senior credit default swap portfolio	(11,472)	—	—
Other income	17,207	12,998	15,546
Total revenues	110,064	113,387	108,781
Benefits and expenses:			
Incurred policy losses and benefits	66,115	60,287	64,100
Insurance acquisition and other operating expenses	35,006	31,413	29,468
Total benefits and expenses	101,121	91,700	93,568
Income before income taxes, minority interest and cumulative effect of accounting changes	8,943	21,687	15,213
Income taxes (benefits):			
Current	3,219	5,489	2,587
Deferred	(1,764)	1,048	1,671
Total income taxes	1,455	6,537	4,258
Income before minority interest and cumulative effect of accounting changes	7,488	15,150	10,955
Minority interest	(1,288)	(1,136)	(478)
Income before cumulative effect of accounting changes	6,200	14,014	10,477
Cumulative effect of accounting changes, net of tax	—	34	—
Net income	$ 6,200	$ 14,048	$ 10,477
Earnings per common share:			
Basic			
Income before cumulative effect of accounting changes	$ 2.40	$ 5.38	$ 4.03
Cumulative effect of accounting changes, net of tax	—	0.01	—
Net income	$ 2.40	$ 5.39	$ 4.03
Diluted			
Income before cumulative effect of accounting changes	$ 2.39	$ 5.35	$ 3.99
Cumulative effect of accounting changes, net of tax	—	0.01	—
Net income	$ 2.39	$ 5.36	$ 3.99
Average shares outstanding:			
Basic	2,585	2,608	2,597
Diluted	2,598	2,623	2,627

See Accompanying Notes to Consolidated Financial Statements.

Consolidated Statement of Shareholders' Equity

Years Ended December 31, (in millions, except share and per share data)	Amounts 2007	Amounts 2006	Amounts 2005	Shares 2007	Shares 2006	Shares 2005
Common stock:						
Balance, beginning and end of year	**$ 6,878**	$ 6,878	$ 6,878	**2,751,327,476**	2,751,327,476	2,751,327,476
Additional paid-in capital:						
Balance, beginning of year	**2,590**	2,339	2,094			
Excess of cost over proceeds of common stock issued under stock plans	**(98)**	(128)	(91)			
Other	**356**	379	336			
Balance, end of year	**2,848**	2,590	2,339			
Payments advanced to purchase shares:						
Balance, beginning of year	**—**	—	—			
Payments advanced	**(6,000)**	—	—			
Shares purchased	**5,088**	—	—			
Balance, end of year	**(912)**	—	—			
Retained earnings:						
Balance, beginning of year	**84,996**	72,330	63,468			
Cumulative effect of accounting changes, net of tax	**(203)**	308	—			
Adjusted balance, beginning of year	**84,793**	72,638	63,468			
Net income	**6,200**	14,048	10,477			
Dividends to common shareholders ($0.77,$0.65 and $0.63 per share, respectively)	**(1,964)**	(1,690)	(1,615)			
Balance, end of year	**89,029**	84,996	72,330			
Accumulated other comprehensive income (loss):						
Unrealized appreciation (depreciation) of investments, net of tax:						
Balance, beginning of year	**10,083**	8,348	10,326			
Unrealized appreciation (depreciation) of investments, net of reclassification adjustments	**(8,046)**	2,574	(3,577)			
Income tax benefit (expense)	**2,338**	(839)	1,599			
Balance, end of year	**4,375**	10,083	8,348			
Foreign currency translation adjustments, net of tax:						
Balance, beginning of year	**(305)**	(1,241)	(701)			
Translation adjustment	**1,325**	1,283	(926)			
Income tax benefit (expense)	**(140)**	(347)	386			
Balance, end of year	**880**	(305)	(1,241)			
Net derivative gains (losses) arising from cash flow hedging activities:						
Balance, beginning of year	**(27)**	(25)	(53)			
Net deferred gains on cash flow hedges, net of reclassification adjustments	**(133)**	13	35			
Deferred income tax expense	**73**	(15)	(7)			
Balance, end of year	**(87)**	(27)	(25)			
Retirement plan liabilities adjustment, net of taxes:						
Balance, beginning of year	**(641)**	(115)	(128)			
Net actuarial loss	**197**	—	—			
Prior service credit	**(24)**	—	—			
Minimum pension liability adjustment	**—**	80	81			
Deferred income tax benefit (expense)	**(57)**	(74)	(68)			
Adjustment to initially apply FAS 158, net of tax	**—**	(532)	—			
Balance, end of year	**(525)**	(641)	(115)			
Accumulated other comprehensive income (loss), end of year	**4,643**	9,110	6,967			
Treasury stock, at cost:						
Balance, beginning of year	**(1,897)**	(2,197)	(2,211)	**(150,131,273)**	(154,680,704)	(154,904,286)
Cost of shares acquired	**(5,104)**	(20)	(176)	**(76,519,859)**	(288,365)	(2,654,272)
Issued under stock plans	**305**	291	173	**4,958,345**	4,579,913	2,625,227
Other	**11**	29	17	**(50,634)**	257,883	252,627
Balance, end of year	**(6,685)**	(1,897)	(2,197)	**(221,743,421)**	(150,131,273)	(154,680,704)
Total shareholders' equity, end of year	**$ 95,801**	$101,677	$86,317			

See Accompanying Notes to Consolidated Financial Statements.

Consolidated Statement of Cash Flows

Years Ended December 31, *(in millions)*	2007	2006	2005
Summary:			
Net cash provided by operating activities	**$ 35,171**	$ 6,287	$ 23,413
Net cash used in investing activities	**(68,007)**	(67,952)	(61,459)
Net cash provided by financing activities	**33,480**	61,244	38,097
Effect of exchange rate changes on cash	**50**	114	(163)
Change in cash	**694**	(307)	(112)
Cash at beginning of year	**1,590**	1,897	2,009
Cash at end of year	**$ 2,284**	$ 1,590	$ 1,897
Cash flows from operating activities:			
Net income	**$ 6,200**	$ 14,048	$ 10,477
Adjustments to reconcile net income to net cash provided by operating activities:			
Noncash revenues, expenses, gains and losses included in income:			
Unrealized market valuation losses on AIGFP super senior credit default swap portfolio	**11,472**	—	—
Net gains on sales of securities available for sale and other assets	**(1,349)**	(763)	(1,218)
Foreign exchange transaction (gains) losses	**(104)**	1,795	(3,330)
Net unrealized (gains) losses on non-AIGFP derivative assets and liabilities	**116**	(713)	878
Equity in income of partially owned companies and other invested assets	**(4,760)**	(3,990)	(1,421)
Amortization of deferred policy acquisition costs	**11,602**	11,578	10,693
Amortization of premium and discount on securities and long-term borrowings	**580**	699	207
Depreciation expenses, principally flight equipment	**2,790**	2,374	2,200
Provision for finance receivable losses	**646**	495	435
Other-than-temporary impairments	**4,715**	944	598
Changes in operating assets and liabilities:			
General and life insurance reserves	**16,242**	12,930	27,045
Premiums and insurance balances receivable and payable — net	**(207)**	(1,214)	192
Reinsurance assets	**923**	1,665	(5,365)
Capitalization of deferred policy acquisition costs	**(15,846)**	(15,363)	(14,454)
Investment income due and accrued	**(401)**	(249)	(171)
Funds held under reinsurance treaties	**(151)**	(1,612)	770
Other policyholders' funds	**1,374**	(498)	811
Income taxes payable	**(3,709)**	2,003	1,543
Commissions, expenses and taxes payable	**989**	408	140
Other assets and liabilities — net	**3,657**	(77)	2,863
Bonds, common and preferred stocks trading	**(3,667)**	(9,147)	(5,581)
Trade receivables and payables — net	**2,243**	(197)	2,272
Trading securities	**835**	1,339	(3,753)
Spot commodities	**(18)**	(128)	442
Net unrealized (gain) loss on swaps, options and forward transactions	**1,413**	(1,482)	934
Securities purchased under agreements to resell	**9,341**	(16,568)	9,953
Securities sold under agreements to repurchase	**(11,391)**	9,552	(12,534)
Securities and spot commodities sold but not yet purchased	**633**	(1,899)	571
Finance receivables and other loans held for sale — originations and purchases	**(5,145)**	(10,786)	(13,070)
Sales of finance receivables and other loans — held for sale	**5,671**	10,602	12,821
Other, net	**477**	541	(1,535)
Total adjustments	**28,971**	(7,761)	12,936
Net cash provided by operating activities	**$ 35,171**	$ 6,287	$ 23,413

See Accompanying Notes to Consolidated Financial Statements.

Consolidated Statement of Cash Flows *Continued*

Years Ended December 31, *(in millions)*	2007	2006	2005
Cash flows from investing activities:			
Proceeds from (payments for)			
Sales and maturities of fixed maturity securities available for sale and hybrid investments	**$132,320**	$ 112,894	$ 140,076
Sales of equity securities available for sale	**9,616**	12,475	11,661
Proceeds from fixed maturity securities held to maturity	**295**	205	46
Sales of flight equipment	**303**	697	573
Sales or distributions of other invested assets	**14,109**	14,084	14,899
Payments received on mortgage and other loans receivable	**9,062**	5,165	3,679
Principal payments received on finance receivables held for investment	**12,553**	12,586	12,461
Purchases of fixed maturity securities available for sale and hybrid investments	**(139,184)**	(146,465)	(175,657)
Purchases of equity securities available for sale	**(10,933)**	(14,482)	(13,273)
Purchases of fixed maturity securities held to maturity	**(266)**	(197)	(3,333)
Purchases of flight equipment	**(4,772)**	(6,009)	(6,193)
Purchases of other invested assets	**(25,327)**	(16,040)	(15,059)
Acquisitions, net of cash acquired	**(1,361)**	—	—
Mortgage and other loans receivable issued	**(12,439)**	(7,438)	(5,310)
Finance receivables held for investment — originations and purchases	**(15,271)**	(13,830)	(17,276)
Change in securities lending invested collateral	**(12,303)**	(9,835)	(10,301)
Net additions to real estate, fixed assets, and other assets	**(870)**	(1,097)	(941)
Net change in short-term investments	**(23,484)**	(10,620)	1,801
Net change in non-AIGFP derivative assets and liabilities	**(55)**	(45)	688
Net cash used in investing activities	**$ (68,007)**	(67,952)	(61,459)
Cash flows from financing activities:			
Proceeds from (payments for)			
Policyholders' contract deposits	**$ 64,829**	57,197	51,699
Policyholders' contract withdrawals	**(58,675)**	(43,413)	(36,339)
Change in other deposits	**(182)**	1,269	(957)
Change in commercial paper and extendible commercial notes	**(338)**	2,960	(702)
Long-term borrowings issued	**103,210**	71,028	67,061
Repayments on long-term borrowings	**(79,738)**	(36,489)	(51,402)
Change in securities lending payable	**11,757**	9,789	10,437
Redemption of subsidiary company preferred stock	**—**	—	(100)
Issuance of treasury stock	**206**	163	82
Payments advanced to purchase treasury stock	**(6,000)**	—	—
Cash dividends paid to shareholders	**(1,881)**	(1,638)	(1,421)
Acquisition of treasury stock	**(16)**	(20)	(176)
Other, net	**308**	398	(85)
Net cash provided by financing activities	**$ 33,480**	$ 61,244	$ 38,097
Supplementary disclosure of cash flow information:			
Cash paid during the period for:			
Interest	**$ 8,818**	$ 6,539	$ 4,883
Taxes	**$ 5,163**	$ 4,693	$ 2,593
Non-cash financing activities:			
Interest credited to policyholder accounts included in financing activities	**$ 11,628**	$ 10,746	$ 9,782
Treasury stock acquired using payments advanced to purchase shares	**$ 5,088**	$ —	$ —
Non-cash investing activities:			
Debt assumed on acquisitions and warehoused investments	**$ 791**	$ —	$ —

See accompanying Notes to Consolidated Financial Statements.

Consolidated Statement of Comprehensive Income

Years Ended December 31, *(in millions)*	**2007**	2006	2005
Net income	**$ 6,200**	$14,048	$10,477
Other comprehensive income (loss):			
Unrealized (depreciation) appreciation of investments — net of reclassification adjustments	**(8,046)**	2,574	(3,577)
Deferred income tax benefit (expense) on above changes	**2,338**	(839)	1,599
Foreign currency translation adjustments	**1,325**	1,283	(926)
Deferred income tax benefit (expense) on above changes	**(140)**	(347)	386
Net derivative gains arising from cash flow hedging activities — net of reclassification adjustments	**(133)**	13	35
Deferred income tax expense on above changes	**73**	(15)	(7)
Change in pension and postretirement unrecognized periodic benefit (cost)	**173**	80	81
Deferred income tax benefit (expense) on above changes	**(57)**	(74)	(68)
Other comprehensive income (loss)	**(4,467)**	2,675	(2,477)
Comprehensive income (loss)	**$ 1,733**	$16,723	$ 8,000

See Accompanying Notes to Consolidated Financial Statements.

Index of Notes to Consolidated Financial Statements

Notes to Consolidated Financial Statements

1. Summary of Significant Accounting Policies

Basis of Presentation

The consolidated financial statements include the accounts of AIG, its controlled subsidiaries, and variable interest entities in which AIG is the primary beneficiary. Entities that AIG does not consolidate but in which it holds 20 percent to 50 percent of the voting rights and/or has the ability to exercise significant influence are accounted for under the equity method.

Certain of AIG's foreign subsidiaries included in the consolidated financial statements report on a fiscal year ending November 30. The effect on AIG's consolidated financial condition and results of operations of all material events occurring between November 30 and December 31 for all periods presented has been recorded.

The accompanying consolidated financial statements have been prepared in accordance with U.S. generally accepted accounting principles (GAAP). All material intercompany accounts and transactions have been eliminated.

Description of Business

See Note 2 herein for a description of AIG's businesses.

Use of Estimates

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting periods. Actual results could differ, possibly materially, from those estimates.

AIG considers its most critical accounting estimates to be those with respect to reserves for losses and loss expenses, future policy benefits for life and accident and health contracts, estimated gross profits for investment-oriented products, recoverability of deferred policy acquisition costs (DAC), fair value measurements of certain assets and liabilities, including the super senior credit default swaps written by AIGFP, other-than-temporary impairments in the value of investments, the allowance for finance receivable losses and flight equipment recoverability.

During the second half of 2007, disruption in the global credit markets, coupled with the repricing of credit risk, and the U.S. housing market deterioration, particularly in the fourth quarter, created increasingly difficult conditions in the financial markets. These conditions have resulted in greater volatility, less liquidity, widening of credit spreads and a lack of price transparency in certain markets and have made it more difficult to value certain of AIG's invested assets and the obligations and collateral relating to certain financial instruments issued or held by AIG, such as AIGFP's super senior credit default swap portfolio.

Revisions and Reclassifications

In 2007, AIG determined that certain products that were historically reported as separate account assets under American Institute of Certified Public Accountants (AICPA) Statement of Position (SOP) 03-1, ''Accounting and Reporting by Insurance Enterprises for Certain Nontraditional Long-Duration Contracts and for Separate Accounts'' (SOP 03-1) should have been reported as general account assets. Accordingly, the December 31, 2006 consolidated balance sheet has been revised to reflect the transfer of $2.4 billion of assets from separate account assets to general account assets, and the same amount of liabilities from separate account liabilities to policyholders' contract deposits. This revision had no effect on consolidated income before income taxes, net income, or shareholders' equity for any period presented.

Certain reclassifications and format changes have been made to prior period amounts to conform to the current period presentation.

Out-of-Period Adjustments

During 2007 and 2006, AIG recorded the effects of certain out-of-period adjustments, which (decreased) increased net income by $(399) million and $65 million, respectively. During 2007, out-of-period adjustments collectively decreased pre-tax operating income by $372 million ($399 million after tax). The adjustments were comprised of a charge of $380 million ($247 million after tax) to reverse net gains on transfers of investment securities among legal entities consolidated within AIGFP and a corresponding increase to accumulated other comprehensive income (loss); $156 million of additional income tax expense related to the successful remediation of the material weakness in internal control over income tax accounting; $142 million ($92 million after tax) of additional expense related to insurance reserves and DAC in connection with improvements in its internal control over financial reporting and consolidation processes; $42 million ($29 million after tax) of additional expense, primarily related to other remediation activities; and $192 million ($125 million after tax) of net realized capital gains related to foreign exchange.

Accounting Policies

(a) Revenue Recognition and Expenses:

Premiums and Other Considerations: Premiums for short duration contracts and considerations received from retailers in connection with the sale of extended service contracts are earned primarily on a pro rata basis over the term of the related coverage. The reserve for unearned premiums includes the portion of premiums written and other considerations relating to the unexpired terms of coverage.

Premiums for long duration insurance products and life contingent annuities are recognized as revenues when due. Estimates for premiums due but not yet collected are accrued. Consideration for universal life and investment-type products consists of policy charges for the cost of insurance, administration, and surrenders during the period. Policy charges collected with respect to future services are deferred and recognized in a manner similar to DAC related to such products.

Net Investment Income: Net investment income represents income primarily from the following sources in AIG's insurance operations:

- Interest income and related expenses, including amortization of premiums and accretion of discounts on bonds with changes in

1. Summary of Significant Accounting Policies

Continued

the timing and the amount of expected principal and interest cash flows reflected in the yield, as applicable.

- Dividend income and distributions from common and preferred stock and other investments when receivable.
- Realized and unrealized gains and losses from investments in trading securities accounted for at fair value.
- Earnings from hedge funds and limited partnership investments accounted for under the equity method.
- The difference between the carrying amount of a life settlement contract and the life insurance proceeds of the underlying life insurance policy recorded in income upon the death of the insured.

Realized Capital Gains (Losses): Realized capital gains and losses are determined by specific identification. The realized capital gains and losses are generated primarily from the following sources:

- Sales of fixed maturity securities and equity securities (except trading securities accounted for at fair value), real estate, investments in joint ventures and limited partnerships and other types of investments.
- Reductions to the cost basis of fixed maturity securities and equity securities (except trading securities accounted for at fair value) and other invested assets for other-than-temporary impairments.
- Changes in fair value of derivatives that are not involved in qualifying hedging activities.
- Exchange gains and losses resulting from foreign currency transactions.

Other Income: Other income includes income from flight equipment, Asset Management operations, the operations of AIGFP and finance charges on consumer loans.

Income from flight equipment under operating leases is recognized over the life of the lease as rentals become receivable under the provisions of the lease or, in the case of leases with varying payments, under the straight-line method over the noncancelable term of the lease. In certain cases, leases provide for additional payments contingent on usage. Rental income is recognized at the time such usage occurs less a provision for future contractual aircraft maintenance. Gains and losses on flight equipment are recognized when flight equipment is sold and the risk of ownership of the equipment is passed to the new owner.

Income from Asset Management operations is generally recognized as revenues as services are performed. Certain costs incurred in the sale of mutual funds are deferred and subsequently amortized.

Income from the operations of AIGFP included in other income consists of the following:

- Interest income and related expenses, including amortization of premiums and accretion of discounts on bonds with changes in the timing and the amount of expected principal and interest cash flows reflected in the yield, as applicable.
- Dividend income and distributions from common and preferred stock and other investments when receivable.
- Changes in the fair value of derivatives (excluding the super senior credit default swap portfolio). In certain instances, no initial gain or loss is recognized in accordance with Emerging Issues Task Force Issue (EITF) 02-3, ''Issues Involved in Accounting for Derivative Contracts Held for Trading Purposes and Contracts Involved in Energy Trading and Risk Management Activities'' (EITF 02-3). The initial gain or loss is recognized in income over the life of the transaction or when observable market data becomes available.
- Realized and unrealized gains and losses from trading securities and spot commodities sold but not yet purchased, futures and hybrid financial instruments.
- Realized gains and losses from the sale of available for sale securities and investments in private equities, joint ventures, limited partnerships and other investments.
- Exchange gains and losses resulting from foreign currency transactions.
- Reductions to the cost basis of securities available for sale for other-than-temporary impairments.
- Earnings from hedge funds and limited partnership investments accounted for under the equity method.

Finance charges on consumer loans are recognized as revenue using the interest method. Revenue ceases to be accrued when contractual payments are not received for four consecutive months for loans and retail sales contracts, and for six months for revolving retail accounts and private label receivables. Extension fees, late charges, and prepayment penalties are recognized as revenue when received.

Incurred Policy Losses and Benefits: Incurred policy losses for short duration insurance contracts consist of the estimated ultimate cost of settling claims incurred within the reporting period, including incurred but not reported claims, plus the changes in estimates of current and prior period losses resulting from the continuous review process. Benefits for long duration insurance contracts consist of benefits paid and changes in future policy benefits liabilities. Benefits for universal life and investment-type products primarily consist of interest credited to policy account balances and benefit payments made in excess of policy account balances.

(b) Income Taxes: Deferred tax assets and liabilities are recorded for the effects of temporary differences between the tax basis of an asset or liability and its reported amount in the consolidated financial statements. AIG assesses its ability to realize deferred tax assets primarily based on the earnings history, the future earnings potential, the reversal of taxable temporary differences, and the tax planning strategies available to the legal entities when recognizing deferred tax assets in accordance with Statement of Financial Accounting Standards No. (FAS) 109, ''Accounting for Income Taxes'' (FAS 109). See Note 21 herein for a further discussion of income taxes.

(c) Investments in Fixed Maturities and Equity Securities: Bonds held to maturity are principally owned by insurance subsidiaries and are carried at amortized cost when AIG has the ability and positive intent to hold these securities until maturity.

1. Summary of Significant Accounting Policies

Continued

When AIG does not have the positive intent to hold bonds until maturity, these securities are classified as available for sale or as trading and are carried at fair value.

Premiums and discounts arising from the purchase of bonds classified as held to maturity or available for sale are treated as yield adjustments over their estimated lives, until maturity, or call date, if applicable.

Common and preferred stocks are carried at fair value.

AIG also enters into dollar roll agreements. These are agreements to sell mortgage-backed securities and to repurchase substantially similar securities at a specified price and date in the future. At December 31, 2007 and 2006, there were no dollar roll agreements outstanding.

For AIG's insurance subsidiaries, unrealized gains and losses on investments in trading securities are reported in Net investment income. Unrealized gains and losses from available for sale investments in equity and fixed maturity securities are reported as a separate component of Accumulated other comprehensive income (loss), net of deferred income taxes, in consolidated shareholders' equity. Investments in fixed maturities and equity securities are recorded on a trade-date basis.

AIG evaluates its investments for other-than-temporary impairment. The determination that a security has incurred an other-than-temporary impairment in value and the amount of any loss recognized requires the judgment of AIG's management and a continual review of its investments.

AIG evaluates its investments for other-than-temporary impairment such that a security is considered a candidate for other-than-temporary impairment if it meets any of the following criteria:

- Trading at a significant (25 percent or more) discount to par, amortized cost (if lower) or cost for an extended period of time (nine consecutive months or longer);
- The occurrence of a discrete credit event resulting in (i) the issuer defaulting on a material outstanding obligation; (ii) the issuer seeking protection from creditors under the bankruptcy laws or any similar laws intended for court supervised reorganization of insolvent enterprises; or (iii) the issuer proposing a voluntary reorganization pursuant to which creditors are asked to exchange their claims for cash or securities having a fair value substantially lower than par value of their claims; or
- AIG may not realize a full recovery on its investment regardless of the occurrence of one of the foregoing events.

The above criteria also consider circumstances of a rapid and severe market valuation decline, such as that experienced in current credit markets, in which AIG could not reasonably assert that the recovery period would be temporary.

At each balance sheet date, AIG evaluates its securities holdings with unrealized losses. When AIG does not intend to hold such securities until they have recovered their cost basis, based on the circumstances at the date of evaluation, AIG records the unrealized loss in income. If a loss is recognized from a sale subsequent to a balance sheet date pursuant to changes in circumstances, the loss is recognized in the period in which the intent to hold the securities to recovery no longer existed.

In periods subsequent to the recognition of an other-than-temporary impairment charge for fixed maturity securities, which is not credit or foreign exchange related, AIG generally accretes the discount or amortizes the reduced premium resulting from the reduction in cost basis over the remaining life of the security.

For certain investments in beneficial interests in securitized financial assets of less than high quality with contractual cash flows, including asset-backed securities, EITF 99-20, ''Recognition of Interest Income and Impairment on Purchased Beneficial Interests and Beneficial Interests that Continued to Be Held by a Transferor in Securitized Financial Assets'' requires periodic updates of AIG's best estimate of cash flows over the life of the security. If the fair value of an investment in beneficial interests in a securitized financial asset is less than its cost or amortized cost and there has been a decrease in the present value of the estimated cash flows since the last revised estimate, considering both their timing and amount, an other-than-temporary impairment charge is recognized. Interest income is recognized based on changes in the timing and the amount of expected principal and interest cash flows reflected in the yield.

AIG also considers its intent and ability to retain a temporarily depressed security until recovery. Estimating future cash flows is a quantitative and qualitative process that incorporates information received from third-party sources along with certain internal assumptions and judgments regarding the future performance of the underlying collateral. In addition, projections of expected future cash flows may change based upon new information regarding the performance of the underlying collateral.

(d) Mortgage and Other Loans Receivable — net: Mortgage and other loans receivable includes mortgage loans on real estate, policy loans and collateral, commercial and guaranteed loans. Mortgage loans on real estate and collateral, commercial and guaranteed loans are carried at unpaid principal balances less credit allowances and plus or minus adjustments for the accretion or amortization of discount or premium. Interest income on such loans is accrued as earned.

Impairment of mortgage loans on real estate and collateral and commercial loans is based on certain risk factors and when collection of all amounts due under the contractual terms is not probable. This impairment is generally measured based on the present value of expected future cash flows discounted at the loan's effective interest rate subject to the fair value of underlying collateral. Interest income on such impaired loans is recognized as cash is received.

Policy loans are carried at unpaid principal amount. There is no allowance for policy loans because these loans serve to reduce the death benefit paid when the death claim is made and the balances are effectively collateralized by the cash surrender value of the policy.

(e) Financial Services — Flight Equipment: Flight equipment is stated at cost, net of accumulated depreciation. Major additions, modifications and interest are capitalized. Normal maintenance and repairs, airframe and engine overhauls and

1. Summary of Significant Accounting Policies

Continued

compliance with return conditions of flight equipment on lease are provided by and paid for by the lessee. Under the provisions of most leases for certain airframe and engine overhauls, the lessee is reimbursed for certain costs incurred up to but not exceeding contingent rentals paid to AIG by the lessee. AIG provides a charge to income for such reimbursements based on the expected reimbursements during the life of the lease. For passenger aircraft, depreciation is generally computed on the straight-line basis to a residual value of approximately 15 percent of the cost of the asset over its estimated useful life of 25 years. For freighter aircraft, depreciation is computed on the straight-line basis to a zero residual value over its useful life of 35 years. At December 31, 2007, ILFC had twelve freighter aircraft in its fleet. Aircraft in the fleet are evaluated for impairment in accordance with FAS 144. FAS 144 requires long-lived assets to be evaluated for impairment whenever events or changes in circumstances indicate the carrying amount of an asset may not be recoverable. Recoverability of assets is measured by comparing the carrying amount of an asset to future undiscounted net cash flows expected to be generated by the asset. These evaluations for impairment are significantly affected by estimates of future net cash flows and other factors that involve uncertainty.

When assets are retired or disposed of, the cost and associated accumulated depreciation are removed from the related accounts and the difference, net of proceeds, is recorded as a gain or loss in Other income.

(f) Financial Services — Securities Available for Sale, at fair value: These securities are held to meet long-term investment objectives and are accounted for as available for sale, carried at fair values and recorded on a trade-date basis. This portfolio is hedged using interest rate, foreign exchange, commodity and equity derivatives. The market risk associated with such hedges is managed on a portfolio basis, with third-party hedging transactions executed as necessary. Because hedge accounting treatment is not achieved in accordance with FAS 133, ''Accounting for Derivative Instruments and Hedging Activities'' (FAS 133), the unrealized gains and losses on these securities resulting from changes in interest rates, currency rates and equity prices are recorded in Accumulated other comprehensive income (loss) in consolidated shareholders' equity while the unrealized gains and losses on the hedging instruments are reflected in Other income.

(g) Financial Services — Trading Securities, at fair value: Trading securities are held to meet short-term investment objectives and to economically hedge other securities. Trading securities are recorded on a trade-date basis and carried at fair value. Realized and unrealized gains and losses are reflected in Other income.

(h) Financial Services — Spot Commodities: Spot commodities held in AIGFP's wholly owned broker-dealer subsidiary are recorded at fair value. All other commodities are recorded at the lower of cost or fair value. Spot commodities are recorded on a trade-date basis. The exposure to market risk may be reduced through the use of forwards, futures and option contracts. Lower of cost or fair value reductions in commodity positions and unrealized gains and losses in related derivatives are reflected in Other income.

(i) Financial Services — Unrealized Gain and Unrealized Loss on Swaps, Options and Forward Transactions: Interest rate, currency, equity and commodity swaps (including AIGFP's super senior credit default swap portfolio), swaptions, options and forward transactions are accounted for as derivatives recorded on a trade-date basis, and carried at fair value. Unrealized gains and losses are reflected in income, when appropriate. In certain instances, when income is not recognized at inception of the contract under EITF 02-3, income is recognized over the life of the contract and as observable market data becomes available.

(j) Financial Services — Trade Receivables and Trade Payables: Trade receivables and Trade payables include option premiums paid and received and receivables from and payables to counterparties that relate to unrealized gains and losses on futures, forwards, and options and balances due from and due to clearing brokers and exchanges.

(k) Financial Services — Securities Purchased (Sold) Under Agreements to Resell (Repurchase), at contract value: Securities purchased under agreements to resell and Securities sold under agreements to repurchase are accounted for as collateralized borrowing or lending transactions and are recorded at their contracted resale or repurchase amounts, plus accrued interest. AIG's policy is to take possession of or obtain a security interest in securities purchased under agreements to resell.

AIG minimizes the credit risk that counterparties to transactions might be unable to fulfill their contractual obligations by monitoring customer credit exposure and collateral value and generally requiring additional collateral to be deposited with AIG when necessary.

(l) Financial Services — Finance Receivables: Finance receivables, which are reported net of unearned finance charges, are held for both investment purposes and for sale. Finance receivables held for investment purposes are carried at amortized cost, which includes accrued finance charges on interest bearing finance receivables, unamortized deferred origination costs, and unamortized net premiums and discounts on purchased finance receivables. The allowance for finance receivable losses is established through the provision for finance receivable losses charged to expense and is maintained at a level considered adequate to absorb estimated credit losses in the portfolio. The portfolio is periodically evaluated on a pooled basis and factors such as economic conditions, portfolio composition, and loss and delinquency experience are considered in the evaluation of the allowance.

Direct costs of originating finance receivables, net of nonrefundable points and fees, are deferred and included in the carrying amount of the related receivables. The amount deferred is amortized to income as an adjustment to finance charge revenues using the interest method.

1. Summary of Significant Accounting Policies

Continued

Finance receivables originated and intended for sale in the secondary market are carried at the lower of cost or fair value, as determined by aggregate outstanding commitments from investors or current investor yield requirements. American General Finance, Inc. (AGF) recognizes net unrealized losses through a valuation allowance by charges to income.

(m) Securities Lending Invested Collateral, at Fair Value and Securities Lending Payable: AIG's insurance and asset management operations lend their securities and primarily take cash as collateral with respect to the securities lent. Invested collateral consists of interest-bearing cash equivalents and floating rate bonds, whose changes in fair value are recorded as a separate component of Accumulated other comprehensive income (loss), net of deferred income taxes. The invested collateral is evaluated for other-than-temporary impairment by applying the same criteria used for investments in fixed maturities. Income earned on invested collateral, net of interest payable to the collateral provider, is recorded in Net investment income.

The fair value of securities pledged under securities lending arrangements was $76 billion and $69 billion at December 31, 2007 and 2006, respectively. These securities are included in bonds available for sale in AIG's consolidated balance sheet.

(n) Other Invested Assets: Other invested assets consist primarily of investments by AIG's insurance operations in hedge funds, private equity and limited partnerships.

Hedge funds and limited partnerships in which AIG's insurance operations hold in the aggregate less than a five percent interest are reported at fair value. The change in fair value is recognized as a component of Accumulated other comprehensive income (loss).

With respect to hedge funds and limited partnerships in which AIG holds in the aggregate a five percent or greater interest or less than a five percent interest but in which AIG has more than a minor influence over the operations of the investee, AIG's carrying value is its share of the net asset value of the funds or the partnerships. The changes in such net asset values, accounted for under the equity method, are recorded in Net investment income.

In applying the equity method of accounting, AIG consistently uses the most recently available financial information provided by the general partner or manager of each of these investments, which is one to three months prior to the end of AIG's reporting period. The financial statements of these investees are generally audited on an annual basis.

Also included in Other invested assets are real estate held for investment, aircraft asset investments held by non-financial services subsidiaries and investments in life settlement contracts. See Note 3(g) herein for further information.

(o) Short-term Investments: Short-term investments consist of interest-bearing cash equivalents, time deposits, and investments with original maturities within one year from the date of purchase, such as commercial paper.

(p) Cash: Cash represents cash on hand and non-interest bearing demand deposits.

(q) Reinsurance Assets: Reinsurance assets include the balances due from reinsurance and insurance companies under the terms of AIG's reinsurance agreements for paid and unpaid losses and loss expenses, ceded unearned premiums and ceded future policy benefits for life and accident and health insurance contracts and benefits paid and unpaid. Amounts related to paid and unpaid losses and benefits and loss expenses with respect to these reinsurance agreements are substantially collateralized.

(r) Deferred Policy Acquisition Costs:

Policy acquisition costs represent those costs, including commissions, premium taxes and other underwriting expenses that vary with and are primarily related to the acquisition of new business.

General Insurance: Policy acquisition costs are deferred and amortized over the period in which the related premiums written are earned. DAC is grouped consistent with the manner in which the insurance contracts are acquired, serviced and measured for profitability and is reviewed for recoverability based on the profitability of the underlying insurance contracts. Investment income is not anticipated in assessing the recoverability of DAC.

Life Insurance & Retirement Services: Policy acquisition costs for traditional life insurance products are generally deferred and amortized over the premium paying period in accordance with FAS 60, ''Accounting and Reporting by Insurance Enterprises'' (FAS 60). Policy acquisition costs and policy issuance costs related to universal life, participating life, and investment-type products (investment-oriented products) are deferred and amortized, with interest, in relation to the incidence of estimated gross profits to be realized over the estimated lives of the contracts in accordance with FAS 97, ''Accounting and Reporting by Insurance Enterprises for Certain Long-Duration Contracts and for Realized Gains and Losses from the Sale of Investments'' (FAS 97). Estimated gross profits are composed of net interest income, net realized investment gains and losses, fees, surrender charges, expenses, and mortality and morbidity gains and losses. If estimated gross profits change significantly, DAC is recalculated using the new assumptions. Any resulting adjustment is included in income as an adjustment to DAC. DAC is grouped consistent with the manner in which the insurance contracts are acquired, serviced and measured for profitability and is reviewed for recoverability based on the current and projected future profitability of the underlying insurance contracts.

The DAC for investment-oriented products is also adjusted with respect to estimated gross profits as a result of changes in the net unrealized gains or losses on fixed maturity and equity securities available for sale. Because fixed maturity and equity securities available for sale are carried at aggregate fair value, an adjustment is made to DAC equal to the change in amortization that would have been recorded if such securities had been sold at their stated aggregate fair value and the proceeds reinvested at current yields. The change in this adjustment, net of tax, is included with the change in net unrealized gains/losses on fixed

1. Summary of Significant Accounting Policies

Continued

maturity and equity securities available for sale that is credited or charged directly to Accumulated other comprehensive income (loss). Value of Business Acquired (VOBA) is determined at the time of acquisition and is reported in the consolidated balance sheet with DAC. This value is based on the present value of future pre-tax profits discounted at yields applicable at the time of purchase. For products accounted for under FAS 60, VOBA is amortized over the life of the business similar to that for DAC based on the assumptions at purchase. For products accounted for under FAS 97, VOBA is amortized in relation to the estimated gross profits to date for each period. As of December 31, 2007 and 2006, there had been no impairments of VOBA.

(s) Investments in Partially Owned Companies: Investments in partially owned companies represents investments entered into for strategic purposes and not solely for capital appreciation or for income generation. These investments are accounted for under the equity method. All other equity method investments are reported in Other invested assets. At December 31, 2007, AIG's significant investments in partially owned companies included its 26.0 percent interest in Tata AIG Life Insurance Company, Ltd., its 26.0 percent interest in Tata AIG General Insurance Company, Ltd. and its 25.4 percent interest in The Fuji Fire and Marine Insurance Co., Ltd. Dividends received from unconsolidated entities in which AIG's ownership interest is less than 50 percent were $30 million, $28 million and $146 million for the years ended December 31, 2007, 2006 and 2005, respectively. The undistributed earnings of unconsolidated entities in which AIG's ownership interest is less than 50 percent were $266 million, $300 million and $179 million at December 31, 2007, 2006 and 2005, respectively.

(t) Real Estate and Other Fixed Assets: The costs of buildings and furniture and equipment are depreciated principally on the straight-line basis over their estimated useful lives (maximum of 40 years for buildings and ten years for furniture and equipment). Expenditures for maintenance and repairs are charged to income as incurred; expenditures for betterments are capitalized and depreciated. AIG periodically assesses the carrying value of its real estate for purposes of determining any asset impairment.

Also included in Real Estate and Other Fixed Assets are capitalized software costs, which represent costs directly related to obtaining, developing or upgrading internal use software. Such costs are capitalized and amortized using the straight-line method over a period generally not exceeding five years.

(u) Separate and Variable Accounts: Separate and variable accounts represent funds for which investment income and investment gains and losses accrue directly to the policyholders who bear the investment risk. Each account has specific investment objectives, and the assets are carried at fair value. The assets of each account are legally segregated and are not subject to claims that arise out of any other business of AIG. The liabilities for these accounts are equal to the account assets.

(v) Goodwill: Goodwill is the excess of cost over the fair value of identifiable net assets acquired. Goodwill is reviewed for impairment on an annual basis, or more frequently if circumstances indicate that a possible impairment has occurred. The assessment of impairment involves a two-step process whereby an initial assessment for potential impairment is performed, followed by a measurement of the amount of impairment, if any. Impairment testing is performed using the fair value approach, which requires the use of estimates and judgment, at the ''reporting unit'' level. A reporting unit is the operating segment, or a business that is one level below the operating segment if discrete financial information is prepared and regularly reviewed by management at that level. The determination of a reporting unit's fair value is based on management's best estimate, which generally considers the market-based earning multiples of the unit's peer companies or expected future cash flows. If the carrying value of a reporting unit exceeds its fair value, an impairment is recognized as a charge against income equal to the excess of the carrying value of goodwill over its fair value. No impairments were recorded in 2007, 2006 or 2005. Changes in the carrying amount of goodwill result from business acquisitions, the payment of contingent consideration, foreign currency translation adjustments and purchase price adjustments.

(w) Other Assets: Other assets consist of prepaid expenses, including deferred advertising costs, sales inducement assets, non-AIGFP derivatives assets carried at fair value, deposits, other deferred charges and other intangible assets.

Certain direct response advertising costs are deferred and amortized over the expected future benefit period in accordance with SOP 93-7, ''Reporting on Advertising Costs.'' When AIG can demonstrate that its customers have responded specifically to direct-response advertising, the primary purpose of which is to elicit sales to customers, and when it can be shown such advertising results in probable future economic benefits, the advertising costs are capitalized. Deferred advertising costs are amortized on a cost-pool-by-cost-pool basis over the expected future economic benefit period and are reviewed regularly for recoverability. Deferred advertising costs totaled $1.35 billion and $1.05 billion at December 31, 2007 and 2006, respectively. The amount of expense amortized into income was $395 million, $359 million and $272 million, for the years ended 2007, 2006, and 2005, respectively.

AIG offers sales inducements, which include enhanced crediting rates or bonus payments to contract holders (bonus interest) on certain annuity and investment contract products. Sales inducements provided to the contractholder are recognized as part of the liability for policyholders' contract deposits in the consolidated balance sheet. Such amounts are deferred and amortized over the life of the contract using the same methodology and assumptions used to amortize DAC. To qualify for such accounting treatment, the bonus interest must be explicitly identified in the contract at inception, and AIG must demonstrate that such amounts are incremental to amounts AIG credits on similar contracts without bonus interest, and are higher than the contract's expected ongoing crediting rates for periods after the bonus period. The deferred bonus interest and other deferred

1. Summary of Significant Accounting Policies

Continued

sales inducement assets totaled $1.7 billion and $1.3 billion at December 31, 2007 and 2006, respectively. The amortization expense associated with these assets is reported within Incurred policy losses and benefits expense in the consolidated statement of income. Such amortization expense totaled $149 million, $132 million and $127 million for the years ended December 31, 2007, 2006 and 2005, respectively.

See Note 8 herein for a discussion of derivatives.

(x) Reserve for Losses and Loss Expenses: Losses and loss expenses are charged to income as incurred. The reserve for losses and loss expenses represents the accumulation of estimates for unpaid reported losses and includes provisions for losses incurred but not reported. The methods of determining such estimates and establishing resulting reserves, including amounts relating to allowances for estimated unrecoverable reinsurance, are reviewed and updated. If the estimate of reserves is determined to be inadequate or redundant, the increase or decrease is reflected in income. AIG discounts its loss reserves relating to workers compensation business written by its U.S. domiciled subsidiaries as permitted by the domiciliary statutory regulatory authorities.

(y) Future Policy Benefits for Life and Accident and Health Contracts and Policyholders' Contract Deposits: The liability for future policy benefits and policyholders' contract deposits are established using assumptions described in Note 9 herein. Future policy benefits for life and accident and health insurance contracts include provisions for future dividends to participating policyholders, accrued in accordance with all applicable regulatory or contractual provisions. Policyholders' contract deposits include AIG's liability for certain guarantee benefits accounted for as embedded derivatives at fair value in accordance with FAS 133.

(z) Other Policyholders' Funds: Other policyholders' funds are reported at cost and include any policyholders' funds on deposit that encompass premium deposits and similar items.

(aa) Financial Services — Securities and Spot Commodities Sold but not yet Purchased, at Fair Value: Securities and spot commodities sold but not yet purchased represent sales of securities and spot commodities not owned at the time of sale. The obligations arising from such transactions are recorded on a trade-date basis and carried at fair value. Also included are obligations under gold leases, which are accounted for as a debt host with an embedded gold derivative.

(bb) Commercial Paper and Extendible Commercial Notes and Long-Term Borrowings: AIG's funding is principally obtained from medium and long-term borrowings and commercial paper. Commercial paper, when issued at a discount, is recorded at the proceeds received and accreted to its par value. Extendible commercial notes are issued by AGF with initial maturities of up to 90 days, which AGF may extend to 390 days. Long-term borrowings are carried at the principal amount borrowed, net of unamortized discounts or premiums. See Note 11 herein for additional information.

Long-term borrowings also include liabilities connected to trust preferred stock principally related to outstanding securities issued by AIG Life Holdings (US), Inc. (AIGLH), a wholly owned subsidiary of AIG. Cash distributions on such preferred stock are accounted for as interest expense.

(cc) Other Liabilities: Other liabilities consist of other funds on deposit, non-AIGFP free-standing derivatives liabilities carried at fair value, and other payables. See Note 8 herein for a discussion of derivatives. AIG has entered into certain insurance and reinsurance contracts, primarily in its General Insurance segment, that do not contain sufficient insurance risk to be accounted for as insurance or reinsurance. Accordingly, the premiums received on such contracts, after deduction for certain related expenses, are recorded as deposits within Other liabilities in the consolidated balance sheet. Net proceeds of these deposits are invested and generate net investment income. As amounts are paid, consistent with the underlying contracts, the deposit liability is reduced.

(dd) Contingent Liabilities: Amounts are accrued for the resolution of claims that have either been asserted or are deemed probable of assertion if, in the opinion of management, it is both probable that a liability has been incurred and the amount of the liability can be reasonably estimated. In many cases, it is not possible to determine whether a liability has been incurred or to estimate the ultimate or minimum amount of that liability until years after the contingency arises, in which case, no accrual is made until that time.

(ee) Preferred Shareholders' Equity in Subsidiary Companies: Preferred shareholders' equity in subsidiary companies relates principally to outstanding preferred stock or interest of ILFC, a wholly owned subsidiary of AIG. Cash distributions on such preferred stock or interest are accounted for as interest expense.

(ff) Foreign Currency: Financial statement accounts expressed in foreign currencies are translated into U.S. dollars in accordance with FAS 52, ''Foreign Currency Translation'' (FAS 52). Under FAS 52, functional currency assets and liabilities are translated into U.S. dollars generally using rates of exchange prevailing at the balance sheet date of each respective subsidiary and the related translation adjustments are recorded as a separate component of Accumulated other comprehensive income (loss), net of any related taxes, in consolidated shareholders' equity. Functional currencies are generally the currencies of the local operating environment. Income statement accounts expressed in functional currencies are translated using average exchange rates during the period. The adjustments resulting from translation of financial statements of foreign entities operating in highly inflationary economies are recorded in income. Exchange gains and losses resulting from foreign currency transactions are recorded in income.

(gg) Earnings per Share: Basic earnings per share is based on the weighted average number of common shares outstanding, adjusted to reflect all stock dividends and stock splits. Diluted

1. Summary of Significant Accounting Policies

Continued

earnings per share is based on those shares used in basic earnings per share plus shares that would have been outstanding assuming issuance of common shares for all dilutive potential common shares outstanding, adjusted to reflect all stock dividends and stock splits.

(hh) Recent Accounting Standards:

Accounting Changes

SOP 05-1

In September 2005, the AICPA issued SOP 05-1, ''Accounting by Insurance Enterprises for Deferred Acquisition Costs in Connection with Modifications or Exchanges of Insurance Contracts'' (SOP 05-1). SOP 05-1 provides guidance on accounting for internal replacements of insurance and investment contracts other than those specifically described in FAS 97. SOP 05-1 defines an internal replacement as a modification in product benefits, features, rights, or coverage that occurs by the exchange of a contract for a new contract, or by amendment, endorsement, or rider to a contract, or by the election of a feature or coverage within a contract. Internal replacements that result in a substantially changed contract are accounted for as a termination and a replacement contract.

SOP 05-1 became effective on January 1, 2007 and generally affects the accounting for internal replacements occurring after that date. In the first quarter of 2007, AIG recorded a cumulative effect reduction of $82 million, net of tax, to the opening balance of retained earnings on the date of adoption. This adoption reflected changes in unamortized DAC, VOBA, deferred sales inducement assets, unearned revenue liabilities and future policy benefits for life and accident and health insurance contracts resulting from a shorter expected life related to certain group life and health insurance contracts and the effect on the gross profits of investment-oriented products related to previously anticipated future internal replacements. This cumulative effect adjustment affected only the Life Insurance & Retirement Services segment.

FAS 155

In February, 2006, the Financial Accounting Standards Board (FASB) issued FAS 155, ''Accounting for Certain Hybrid Financial Instruments — an amendment of FAS 140 and FAS 133'' (FAS 155). FAS 155 allows AIG to include changes in fair value in earnings on an instrument-by-instrument basis for any hybrid financial instrument that contains an embedded derivative that would otherwise be required to be bifurcated and accounted for separately under FAS 133. The election to measure the hybrid instrument at fair value is irrevocable at the acquisition or issuance date.

AIG elected to early adopt FAS 155 as of January 1, 2006, and apply FAS 155 fair value measurement to certain structured note liabilities and structured investments in AIG's available for sale portfolio that existed at December 31, 2005. The effect of this adoption resulted in an $11 million after-tax ($18 million pre-tax) decrease to opening retained earnings as of January 1, 2006, representing the difference between the fair value of these hybrid financial instruments and the prior carrying value as of December 31, 2005. The effect of adoption on after-tax gross gains and losses was $218 million ($336 million pre-tax) and $229 million ($354 million pre-tax), respectively.

In connection with AIG's early adoption of FAS 155, structured note liabilities of $8.9 billion, other structured liabilities in conjunction with equity derivative transactions of $111 million, and hybrid financial instruments of $522 million at December 31, 2006 are now carried at fair value. The effect on earnings for 2006, for changes in the fair value of hybrid financial instruments, was a pre-tax loss of $313 million, of which $287 million was reflected in Other income and was largely offset by gains on economic hedge positions which were also reflected in operating income, and $26 million was reflected in Net investment income.

FAS 158

In September 2006, the FASB issued FAS 158, ''Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans — an amendment of FASB Statements No. 87, 88, 106 and 132R'' (FAS 158). FAS 158 requires AIG to prospectively recognize the overfunded or underfunded status of defined benefit postretirement plans as an asset or liability in AIG's consolidated balance sheet and to recognize changes in that funded status in the year in which the changes occur through Other comprehensive income. FAS 158 also requires AIG to measure the funded status of plans as of the date of its year-end balance sheet, with limited exceptions. AIG adopted FAS 158 for the year ended December 31, 2006. The cumulative effect, net of deferred income taxes, on AIG's consolidated balance sheet at December 31, 2006 was a net reduction in shareholders' equity through a charge to Accumulated other comprehensive income (loss) of $532 million, with a corresponding net decrease of $538 million in total assets, and a net decrease of $6 million in total liabilities. See Note 18 herein for additional information on the adoption of FAS 158.

FIN 48

In July 2006, the FASB issued FASB Interpretation No. (FIN) 48, ''Accounting for Uncertainty in Income Taxes — an interpretation of FASB Statement No. 109'' (FIN 48), which clarifies the accounting for uncertainty in income tax positions. FIN 48 prescribes a recognition threshold and measurement attribute for the financial statement recognition and measurement of an income tax position taken or expected to be taken in a tax return. FIN 48 also provides guidance on derecognition, classification, interest and penalties, accounting in interim periods, and additional disclosures. AIG adopted FIN 48 on January 1, 2007. Upon adoption, AIG recognized a $71 million increase in the liability for unrecognized tax benefits, which was accounted for as a decrease to opening retained earnings as of January 1, 2007. See Note 21 for additional FIN 48 disclosures.

FSP 13-2

In July 2006, the FASB issued FASB Staff Position No. (FSP) FAS 13-2, ''Accounting for a Change or Projected

1. Summary of Significant Accounting Policies

Continued

Change in the Timing of Cash Flows Relating to Income Taxes Generated by a Leveraged Lease Transaction'' (FSP 13-2). FSP 13-2 addresses how a change or projected change in the timing of cash flows relating to income taxes generated by a leveraged lease transaction affects the accounting for the lease by the lessor, and directs that the tax assumptions be consistent with any FIN 48 uncertain tax position related to the lease. AIG adopted FSP 13-2 on January 1, 2007. Upon adoption, AIG recorded a $50 million decrease in the opening balance of retained earnings, net of tax, to reflect the cumulative effect of this change in accounting.

As a result of adopting SOP 05-1, FIN 48 and FSP 13-2, AIG recorded a total decrease to opening retained earnings of $203 million as of January 1, 2007.

Future Application of Accounting Standards

FAS 157

In September 2006, the FASB issued FAS 157, ''Fair Value Measurements'' (FAS 157). FAS 157 defines fair value, establishes a framework for measuring fair value and expands disclosure requirements regarding fair value measurements but does not change existing guidance about whether an instrument is carried at fair value. FAS 157 nullifies the guidance in EITF 02-3 that precluded the recognition of a trading profit at the inception of a derivative contract unless the fair value of such contract was obtained from a quoted market price or other valuation technique incorporating observable market data. FAS 157 also clarifies that an issuer's credit standing should be considered when measuring liabilities at fair value.

AIG adopted FAS 157 on January 1, 2008, its required effective date. FAS 157 must be applied prospectively, except that the difference between the carrying amount and fair value of a stand-alone derivative or hybrid instrument measured using the guidance in EITF 02-3 on recognition of a trading profit at the inception of a derivative, is to be applied as a cumulative-effect adjustment to opening retained earnings on January 1, 2008. The adoption of FAS 157 was not material to AIG's financial condition. However, the adoption of FAS 157 is expected to affect first quarter 2008 earnings, due to changes in the valuation methodology for hybrid financial instrument and derivative liabilities (both freestanding and embedded) currently carried at fair value. These methodology changes primarily include the incorporation of AIG's own credit risk and the inclusion of explicit risk margins, where appropriate.

FAS 159

In February 2007, the FASB issued FAS 159, ''The Fair Value Option for Financial Assets and Financial Liabilities'' (FAS 159). FAS 159 permits entities to choose to measure at fair value many financial instruments and certain other items that are not required to be measured at fair value. Subsequent changes in fair value for designated items are required to be reported in income. FAS 159 also establishes presentation and disclosure requirements for similar types of assets and liabilities measured at fair value. FAS 159 permits the fair value option election on an instrument-by-instrument basis for eligible items existing at the adoption date and at initial recognition of an asset or liability or upon an event that gives rise to a new basis of accounting for that instrument.

AIG adopted FAS 159 on January 1, 2008, its required effective date. The adoption of FAS 159 with respect to elections made in the Life Insurance & Retirement Services segment is expected to result in a decrease to opening 2008 retained earnings of approximately $600 million. The adoption of FAS 159 with respect to elections made by AIGFP is currently being evaluated for the effect of recently issued draft guidance by the FASB, anticipated to be issued in final form in early 2008, and its potential effect on AIG's consolidated financial statements.

SOP 07-1

In June 2007, the AICPA issued SOP No. 07-1 (SOP 07-1), ''Clarification of the Scope of the Audit and Accounting Guide 'Audits of Investment Companies' and Accounting by Parent Companies and Equity Method Investors for Investments in Investment Companies.'' SOP 07-1 amends the guidance for whether an entity may apply the Audit and Accounting Guide, ''Audits of Investment Companies'' (the Guide). In February 2008, the FASB issued an FSP indefinitely deferring the effective date of SOP 07-1.

FAS 141(R)

In December 2007, the FASB issued FAS 141 (revised 2007), ''Business Combinations'' (FAS 141(R)). FAS 141(R) changes the accounting for business combinations in a number of ways, including broadening the transactions or events that are considered business combinations, requiring an acquirer to recognize 100 percent of the fair values of assets acquired, liabilities assumed, and noncontrolling interests in acquisitions of less than a 100 percent controlling interest when the acquisition constitutes a change in control of the acquired entity, recognizing contingent consideration arrangements at their acquisition-date fair values with subsequent changes in fair value generally reflected in income, and recognizing preacquisition loss and gain contingencies at their acquisition-date fair values, among other changes.

FAS 141(R) is required to be adopted for business combinations for which the acquisition date is on or after the beginning of the first annual reporting period beginning on or after December 15, 2008 (January 1, 2009 for AIG). Early adoption is prohibited. AIG is evaluating the effect FAS 141(R) will have on its consolidated financial statements.

FAS 160

In December 2007, the FASB issued FAS 160, ''Noncontrolling Interests in Consolidated Financial Statements, an amendment of ARB No. 51'' (FAS 160). FAS 160 requires noncontrolling (i.e., minority) interests in partially owned consolidated subsidiaries to be classified in the consolidated balance sheet as a separate component of consolidated shareholders' equity. FAS 160 also

1. Summary of Significant Accounting Policies

Continued

establishes accounting rules for subsequent acquisitions and sales of noncontrolling interests and how noncontrolling interests should be presented in the consolidated statement of income. The noncontrolling interests' share of subsidiary income should be reported as a part of consolidated net income with disclosure of the attribution of consolidated net income to the controlling and noncontrolling interests on the face of the consolidated statement of income.

FAS 160 is required to be adopted in the first annual reporting period beginning on or after December 15, 2008 (January 1, 2009 for AIG) and earlier application is prohibited. FAS 160 must be adopted prospectively, except that noncontrolling interests should be reclassified from liabilities to a separate component of shareholders' equity and consolidated net income should be recast to include net income attributable to both the controlling and noncontrolling interests retrospectively. Had AIG adopted FAS 160 at December 31, 2007, AIG would have reclassified $10.4 billion of minority (i.e., noncontrolling) interests from liabilities to Shareholders' equity.

2. Segment Information

AIG identifies its reportable segments by product line consistent with its management structure. These segments and their respective operations are as follows:

General Insurance: AIG's General Insurance subsidiaries write substantially all lines of commercial property and casualty insurance and various personal lines both domestically and abroad. Revenues in the General Insurance segment represent General Insurance net Premiums and other considerations earned, Net investment income and Net realized capital gains (losses). AIG's principal General Insurance operations are as follows:

Domestic Brokerage Group (DBG) writes substantially all classes of business insurance in the U.S. and Canada, accepting such business mainly from insurance brokers.

Transatlantic Holdings, Inc. (Transatlantic) subsidiaries offer reinsurance on both a treaty and facultative basis to insurers in the U.S. and abroad. Transatlantic structures programs for a full range of property and casualty products with an emphasis on specialty risks.

AIG's Personal Lines operations provide automobile insurance through aigdirect.com, the newly formed operation resulting from the merger of AIG Direct and 21st Century Insurance Group (21st Century), and the Agency Auto Division, as well as a broad range of coverages for high net worth individuals through the AIG Private Client Group.

Mortgage Guaranty operations provide residential mortgage guaranty insurance that covers the first loss for credit defaults on high loan-to-value conventional first- and second-lien mortgages for the purchase or refinance of one to four family residences.

AIG's Foreign General Insurance group accepts risks primarily underwritten through American International Underwriters (AIU), a marketing unit consisting of wholly owned agencies and insurance companies. The Foreign General Insurance group also includes business written by AIG's foreign-based insurance subsidiaries. The Foreign General Insurance group uses various marketing methods to write both business and consumer lines insurance with certain refinements for local laws, customs and needs. AIU operates in Asia, the Pacific Rim, Europe, including the United Kingdom, Africa, the Middle East and Latin America.

Each of the General Insurance sub-segments is comprised of groupings of major products and services as follows: DBG is comprised of domestic commercial insurance products and services; Transatlantic is comprised of reinsurance products and services sold to other general insurance companies; Personal Lines is comprised of general insurance products and services sold to individuals; Mortgage Guaranty is comprised of products insuring against losses arising under certain loan agreements; and Foreign General is comprised of general insurance products sold overseas.

Life Insurance & Retirement Services: AIG's Life Insurance & Retirement Services subsidiaries offer a wide range of insurance and retirement savings products both domestically and abroad. Insurance-oriented products consist of individual and group life, payout annuities (including structured settlements), endowment and accident and health policies. Retirement savings products consist generally of fixed and variable annuities. Revenues in the Life Insurance & Retirement Services segment represent Life Insurance & Retirement Services Premiums and other considerations, Net investment income and Net realized capital gains (losses).

AIG's principal Foreign Life Insurance & Retirement Services operations are American Life Insurance Company (ALICO), American International Assurance Company, Limited, together with American International Assurance Company (Bermuda) Limited (AIA), Nan Shan Life Insurance Company, Ltd. (Nan Shan), The Philippine American Life and General Insurance Company (Philamlife), AIG Edison Life Insurance Company (AIG Edison Life) and AIG Star Life Insurance Co. Ltd. (AIG Star Life).

AIG's principal Domestic Life Insurance & Retirement Services operations are American General Life Insurance Company (AG Life), The United States Life Insurance Company in the City of New York (USLIFE), American General Life and Accident Insurance Company (AGLA and, collectively with AG Life and USLIFE, the Domestic Life Insurance internal reporting unit), AIG Annuity Insurance Company (AIG Annuity), The Variable Annuity Life Insurance Company (VALIC) and AIG Retirement Services, Inc (AIG SunAmerica and, collectively with AIG Annuity and VALIC, the Domestic Retirement Services internal reporting unit).

American International Reinsurance Company (AIRCO) acts primarily as an internal reinsurance company for AIG's insurance operations.

Life Insurance & Retirement Services is comprised of two major groupings of products and services: insurance-oriented products and services and retirement savings products and services.

Financial Services: AIG's Financial Services subsidiaries engage in diversified activities including aircraft and equipment leasing,

2. Segment Information

Continued

capital markets, consumer finance and insurance premium finance.

AIG's Aircraft Leasing operations represent the operations of International Lease Finance Corporation (ILFC), which generates its revenues primarily from leasing new and used commercial jet aircraft to domestic and foreign airlines. Revenues also result from the remarketing of commercial jets for its own account, and remarketing and fleet management services for airlines and for financial institutions.

Capital Markets represents the operations of AIGFP, which engages as principal in a wide variety of financial transactions, including standard and customized financial products involving commodities, credit, currencies, energy, equities and rates and provides credit protection through credit default swaps on certain super senior tranches of collateralized debt obligations (CDOs). AIGFP also invests in a diversified portfolio of securities and principal investments and engages in borrowing activities that include issuing standard and structured notes and other securities and entering into guaranteed investment agreements (GIAs).

Consumer Finance operations include American General Finance Inc. (AGF) as well as AIG Consumer Finance Group Inc. (AIGCFG). AGF and AIGCFG provide a wide variety of consumer finance products, including non-conforming real estate mortgages, consumer loans, retail sales finance and credit-related insurance to customers both domestically and overseas, particularly in emerging and developing markets.

Asset Management: AIG's Asset Management operations comprise a wide variety of investment-related services and investment products. Such services and products are offered to individuals, pension funds and institutions globally through AIG's Spread-Based Investment business, Institutional Asset Management, and Brokerage Services and Mutual Funds business. Revenues in the Asset Management segment represent investment income with respect to spread-based products and management, advisory and incentive fees.

2. Segment Information

Continued

The following table summarizes AIG's operations by reporting segment for the years ended December 31, 2007, 2006 and 2005:

	Operating Segments							
(in millions)	General Insurance	Life Insurance & Retirement Services[a]	Financial Services[a]	Asset Management[a]	Other[a][b]	Total	Consolidation and Eliminations[a]	Consolidated
2007								
Total revenues[c][d][e]	**$ 51,708**	**$ 53,570**	**$ (1,309)**	**$ 5,625**	**$ 457**	**$ 110,051**	**$ 13**	**$ 110,064**
Interest expense	**29**	**128**	**7,794**	**567**	**1,170**	**9,688**	**—**	**9,688**
Operating income (loss) before minority interest[d][e]	**10,526**	**8,186**	**(9,515)**	**1,164**	**(2,140)**	**8,221**	**722**	**8,943**
Income taxes (benefits)	**2,393**	**1,494**	**(3,260)**	**334**	**537**	**1,498**	**(43)**	**1,455**
Depreciation expense	**300**	**392**	**1,831**	**88**	**179**	**2,790**	**—**	**2,790**
Capital expenditures	**354**	**532**	**4,569**	**3,557**	**271**	**9,283**	**—**	**9,283**
Year-end identifiable assets	**181,708**	**615,386**	**203,894**	**77,274**	**126,874**	**1,205,136**	**(144,631)**	**1,060,505**
2006								
Total revenues[c][d]	$ 49,206	$ 50,878	$ 7,777	$ 4,543	$ 483	$ 112,887	$ 500	$ 113,387
Interest expense	23	74	6,005	105	744	6,951	—	6,951
Operating income (loss) before minority interest[d]	10,412	10,121	383	1,538	(1,435)	21,019	668	21,687
Income taxes (benefits)	2,351	2,892	(26)	575	719	6,511	26	6,537
Depreciation expense	274	268	1,655	13	164	2,374	—	2,374
Capital expenditures	375	711	6,278	835	244	8,443	—	8,443
Year-end identifiable assets	167,004	550,957	202,485	78,275	107,517	1,106,238	(126,828)	979,410
2005								
Total revenues[c][d]	$ 45,174	$ 48,020	$ 10,677	$ 4,582	$ 344	$ 108,797	$ (16)	$ 108,781
Interest expense	7	83	5,164	11	408	5,673	—	5,673
Operating income (loss) before minority interest[d]	2,315	8,965	4,424	1,963	(2,765)[f]	14,902	311	15,213
Income taxes (benefits)	169	2,407	1,418	723	(587)	4,130	128	4,258
Depreciation expense	273	268	1,447	43	169	2,200	—	2,200
Capital expenditures	417	590	6,300	25	194	7,526	—	7,526
Year-end identifiable assets	150,667	489,331	161,919	69,584	94,047	965,548	(112,500)	853,048

(a) *Beginning in 2007, revenues and operating income related to certain foreign investment contracts, which were historically reported as a component of the Asset Management segment, are now reported in the Life Insurance & Retirement Services segment, net realized capital gains and losses; including derivative gains and losses and foreign exchange transaction gains and losses for Financial Services entities other than AIGFP and Asset Management entities, which were previously reported as part of AIG's Other category, are now included in Asset Management and Financial Services revenues and operating income; and revenues and operating income related to consolidated managed partnerships and funds, which were historically reported in the Asset Management segment, are now being reported in Consolidation and eliminations. All prior periods have been revised to conform to the current presentation.*

(b) *Includes AIG Parent and other operations that are not required to be reported separately. The following table presents the operating loss for AIG's Other category for the years ended December 31, 2007, 2006 and 2005:*

For the Years Ended December 31, *(in millions)*	**2007**	2006	2005
Operating income (loss):			
Equity earnings in partially owned companies*	**$ 157**	$ 193	$ (124)
Interest expense	**(1,223)**	(859)	(541)
Unallocated corporate expenses	**(560)**	(517)	(413)
Compensation expense — SICO Plans	**(39)**	(108)	(205)
Compensation expense — Starr tender offer	**—**	(54)	—
Net realized capital gains (losses)	**(409)**	(37)	269
Regulatory settlement costs	**—**	—	(1,644)
Other miscellaneous, net	**(66)**	(53)	(107)
Total Other	**$ (2,140)**	$ (1,435)	$ (2,765)

* *Includes current year catastrophe-related losses from unconsolidated entities of $312 million in 2005. There were no significant catastrophe-related losses from unconsolidated entities in 2007 and 2006.*

2. Segment Information

Continued

(c) Represents the sum of General Insurance net premiums earned, Life Insurance & Retirement Services premiums and other considerations, net investment income, Financial Services interest, lease and finance charges, Asset Management investment income from spread-based products and management, advisory and incentive fees, and realized capital gains (losses).

(d) In 2007, 2006 and 2005, includes other-than-temporary impairment charges of $4.7 billion, $944 million and $598 million, respectively.

(e) Both revenues and operating income (loss) include an unrealized market valuation loss of $11.5 billion on AIGFP's super senior credit default swap portfolio and an other-than-temporary impairment charge of $643 million on AIGFP's available for sale investment securities reported in other income.

(f) Includes settlement costs of $1.64 billion as described in Note 12(a) Litigation and Investigations herein.

The following table summarizes AIG's General Insurance operations by major internal reporting unit for the years ended December 31, 2007, 2006 and 2005:

	General Insurance							
(in millions)	Domestic Brokerage Group	Transatlantic	Personal Lines	Mortgage Guaranty	Foreign General Insurance	Total Reportable Segment	Consolidation and Eliminations	Total General Insurance
2007								
Total revenues	**$ 27,653**	**$ 4,382**	**$4,924**	**$1,041**	**$13,715**	**$ 51,715**	**$ (7)**	**$ 51,708**
Losses & loss expenses incurred	**15,948**	**2,638**	**3,660**	**1,493**	**6,243**	**29,982**	**—**	**29,982**
Underwriting expenses	**4,400**	**1,083**	**1,197**	**185**	**4,335**	**11,200**	**—**	**11,200**
Operating income (loss)[(a)]	**7,305**	**661**	**67**	**(637)**	**3,137**	**10,533**	**(7)**	**10,526**
Depreciation expense	**97**	**2**	**70**	**6**	**125**	**300**	**—**	**300**
Capital expenditures	**93**	**4**	**81**	**21**	**155**	**354**	**—**	**354**
Year-end identifiable assets	**112,675**	**15,484**	**5,930**	**4,550**	**48,728**	**187,367**	**(5,659)**	**181,708**
2006								
Total revenues[(b)]	$ 27,419	$ 4,050	$4,871	$ 877	$11,999	$ 49,216	$ (10)	$ 49,206
Losses & loss expenses incurred	16,779	2,463	3,306	349	5,155	28,052	—	28,052
Underwriting expenses	4,795	998	1,133	200	3,616	10,742	—	10,742
Operating income[(a)(b)]	5,845	589	432	328	3,228	10,422	(10)	10,412
Depreciation expense	100	2	52	5	115	274	—	274
Capital expenditures	125	2	94	11	143	375	—	375
Year-end identifiable assets	104,866	14,268	5,391	3,604	43,879	172,008	(5,004)	167,004
2005								
Total revenues	$ 25,171	$ 3,766	$4,848	$ 655	$10,719	$ 45,159	$ 15	$ 45,174
Losses & loss expenses incurred	21,466	2,877	3,566	139	5,043	33,091	—	33,091
Underwriting expenses	4,525	928	1,087	153	3,075	9,768	—	9,768
Operating income (loss)[(a)(c)]	(820)[(d)]	(39)	195	363	2,601	2,300	15	2,315
Depreciation expense	114	2	48	4	105	273	—	273
Capital expenditures	119	2	94	6	196	417	—	417
Year-end identifiable assets	95,829	12,365	5,245	3,165	39,044	155,648	(4,981)	150,667

(a) Catastrophe-related losses in 2007 and 2005 by reporting unit were as follows. There were no significant catastrophe-related losses in 2006.

	2007		2005	
(in millions)	Insurance Related Losses	Net Reinstatement Premium Cost	Insurance Related Losses	Net Reinstatement Premium Cost
Reporting Unit:				
DBG	**$113**	**$(13)**	$1,811	$136
Transatlantic	**11**	**(1)**	463	45
Personal Lines	**61**	**14**	112	2
Mortgage Guaranty	**—**	**—**	10	—
Foreign General Insurance	**90**	**1**	229	80
Total	**$275**	**$ 1**	$2,625	$263

(b) Includes the effect of out of period adjustments related to the accounting for certain interests in unit investment trusts (UCITS). For DBG, the effect was an increase of $66 million in both revenues and operating income and for Foreign General Insurance, the effect was an increase of $424 million in both revenues and operating income.

(c) Includes the fourth quarter 2005 increase in net reserves of approximately $1.8 billion resulting from the annual review of General Insurance loss and loss adjustment reserves.

(d) Includes $291 million of expenses related to changes in estimates for uncollectible reinsurance and other premium balances, and $100 million of accrued expenses in connection with certain workers compensation insurance policies written between 1985 and 1996.

2. Segment Information

Continued

The following table summarizes AIG's Life Insurance & Retirement Services operations by major internal reporting unit for the years ended December 31, 2007, 2006 and 2005:

	Life Insurance & Retirement Services						
(in millions)	Japan and Other	Asia	Domestic Life Insurance	Domestic Retirement Services	Total Reportable Segment	Consolidation and Eliminations	Total Life Insurance & Retirement Services
2007							
Total revenues[(a)(b)]:							
Insurance-oriented products	**$ 14,393**	**$ 19,896**	**$ 8,535**	**$ —**	**$ 42,824**	**$ —**	**$ 42,824**
Retirement savings products	**3,783**	**191**	**493**	**6,279**	**10,746**	**—**	**10,746**
Total revenues	**18,176**	**20,087**	**9,028**	**6,279**	**53,570**	**—**	**53,570**
Operating income[(a)(b)]	**3,044**	**3,153**	**642**	**1,347**	**8,186**	**—**	**8,186**
Depreciation expense	**110**	**84**	**85**	**113**	**392**	**—**	**392**
Capital expenditures	**166**	**232**	**53**	**81**	**532**	**—**	**532**
Year-end identifiable assets	**177,413**	**132,521**	**108,908**	**203,441**	**622,283**	**(6,897)**	**615,386**
2006							
Total revenues[(a)(c)]:							
Insurance-oriented products	$ 13,310	$ 17,712	$ 8,538	$ —	$ 39,560	$ —	$ 39,560
Retirement savings products	3,441	168	568	7,141	11,318	—	11,318
Total revenues	16,751	17,880	9,106	7,141	50,878	—	50,878
Operating income[(a)(c)]	3,821	3,060	917	2,323	10,121	—	10,121
Depreciation expense	101	70	63	34	268	—	268
Capital expenditures	342	260	71	38	711	—	711
Year-end identifiable assets	152,409	108,850	103,624	192,885	557,768	(6,811)	550,957
2005							
Total revenues[(a)]:							
Insurance-oriented products	$ 12,524	$ 15,853	$ 8,525	$ —	$ 36,902	$ —	$ 36,902
Retirement savings products	3,413	129	690	6,886	11,118	—	11,118
Total revenues	15,937	15,982	9,215	6,886	48,020	—	48,020
Operating income[(a)]	3,020	2,286	1,495	2,164	8,965	—	8,965
Depreciation expense	91	81	65	31	268	—	268
Capital expenditures	153	340	71	26	590	—	590
Year-end identifiable assets	124,524	87,491	99,594	185,383	496,992	(7,661)	489,331

(a) In 2007, 2006 and 2005, includes other-than-temporary impairment charges of $2.8 billion, $641 million and $425 million, respectively.

(b) Includes a positive out-of-period adjustment of $158 million related to foreign exchange remediation activities.

(c) Includes the effect of out-of-period adjustments related to the accounting for UCITS in 2006, which increased revenues by $240 million and operating income by $169 million.

2. Segment Information

Continued

The following table summarizes AIG's Financial Services operations by major internal reporting unit for the years ended December 31, 2007, 2006 and 2005:

	Financial Services						
(in millions)	Aircraft Leasing[(a)]	Capital Markets[(b)]	Consumer Finance[(c)]	Other	Total Reportable Segment	Consolidation and Elimination	Total Financial Services
2007							
Total revenues[(d)(e)(f)(g)]	**$ 4,694**	**$ (9,979)**	**$ 3,655**	**$1,471**	**$ (159)**	**$(1,150)**	**$ (1,309)**
Interest expense[(e)]	**1,650**	**4,644**	**1,437**	**63**	**7,794**	**—**	**7,794**
Operating income (loss)[(e)(f)(g)]	**873**	**(10,557)**	**171**	**(2)**	**(9,515)**	**—**	**(9,515)**
Depreciation expense	**1,751**	**24**	**41**	**15**	**1,831**	**—**	**1,831**
Capital expenditures	**4,164**	**21**	**62**	**322**	**4,569**	**—**	**4,569**
Year-end identifiable assets	**44,970**	**115,487**	**36,822**	**17,357**	**214,636**	**(10,742)**	**203,894**
2006							
Total revenues[(d)(e)]	$ 4,082	$ (186)	$ 3,587	$ 320	$ 7,803	$ (26)	$ 7,777
Interest expense[(e)]	1,442	3,215	1,303	108	6,068	(63)	6,005
Operating income (loss)	578	(873)	668	10	383	—	383
Depreciation expense	1,584	19	41	11	1,655	—	1,655
Capital expenditures	6,012	15	52	199	6,278	—	6,278
Year-end identifiable assets	41,975	121,243	32,702	12,368	208,288	(5,803)	202,485
2005							
Total revenues[(d)(e)]	$ 3,668	$ 3,260	$ 3,563	$ 206	$ 10,697	$ (20)	$ 10,677
Interest expense[(e)]	1,125	3,033	1,005	201	5,364	(200)	5,164
Operating income	769	2,661	922	72	4,424	—	4,424
Depreciation expense	1,384	20	38	5	1,447	—	1,447
Capital expenditures	6,193	3	54	50	6,300	—	6,300
Year-end identifiable assets	37,515	90,090	30,704	7,984	166,293	(4,374)	161,919

(a) Both revenues and operating income include gains (losses) from hedging activities that did not qualify for hedge accounting treatment under FAS 133, including the related foreign exchange gains and losses. In 2007, 2006 and 2005, the effect was $(37) million, $(73) million and $93 million, respectively. These amounts result primarily from interest rate and foreign currency derivatives that are effective economic hedges of borrowings. In the second quarter of 2007, ILFC began applying hedge accounting to most of its derivatives hedging interest rate and foreign exchange risks associated with its floating rate and foreign currency denominated borrowings.

(b) Both revenues and operating income include gains (losses) from hedging activities that did not qualify for hedge accounting treatment under FAS 133, including the related foreign exchange gains and losses. In 2007, 2006 and 2005, the effect was $211 million, $(1.82) billion and $2.01 billion, respectively. The year ended December 31, 2007 includes a $380 million out of period charge to reverse net gains recognized on transfers of available for sale securities among legal entities consolidated within AIGFP. The year ended December 31, 2006 includes an out of period charge of $223 million related to the remediation of the material weakness in internal control over the accounting for certain derivative transactions under FAS 133. In the first quarter of 2007, AIGFP began applying hedge accounting for certain of its interest rate swaps and foreign currency forward contracts hedging its investments and borrowings.

(c) Both revenues and operating income include gains (losses) from hedging activities that did not qualify for hedge accounting treatment under FAS 133, including the related foreign exchange gains and losses. In 2007, 2006 and 2005, the effect was $(20) million, $(94) million and $75 million, respectively. These amounts result primarily from interest rate and foreign currency derivatives that are effective economic hedges of borrowings. In the second quarter of 2007, AGF began applying hedge accounting to most of its derivatives hedging interest rate and foreign exchange risks associated with its floating rate and foreign currency denominated borrowings.

(d) Represents primarily the sum of aircraft lease rentals from ILFC, AIGFP hedged financial positions entered into in connection with counterparty transactions, the effect of hedging activities that did not qualify for hedge accounting treatment under FAS 133, including the related foreign exchange gains and losses, and finance charges from consumer finance operations.

(e) Interest expense for the Capital Markets business is included in Revenues above and in Other income in the consolidated statement of income.

(f) Both revenues and operating income (loss) include an unrealized market valuation loss of $11.5 billion on AIGFP's super senior credit default swap portfolio and an other-than-temporary impairment charge of $643 million on AIGFP's available for sale investment securities reported in other income.

(g) Includes a pre-tax charge of $178 million in connection with domestic consumer finance's mortgage banking activities.

2. Segment Information

Continued

A substantial portion of AIG's operations is conducted in countries other than the United States and Canada. The following table summarizes AIG's operations by major geographic segment. Allocations have been made on the basis of the location of operations and assets.

	Geographic Segments			
(in millions)	Domestic[a]	Far East	Other Foreign	Consolidated
2007				
Total revenues	**$46,402**	**$36,512**	**$27,150**	**$110,064**
Real estate and other fixed assets, net of accumulated depreciation	**3,202**	**1,404**	**912**	**5,518**
Flight equipment primarily under operating leases, net of accumulated depreciation[b]	**41,984**	**—**	**—**	**41,984**
2006				
Total revenues	$57,984	$33,883	$21,520	$113,387
Real estate and other fixed assets, net of accumulated depreciation	2,432	1,082	867	4,381
Flight equipment primarily under operating leases, net of accumulated depreciation[b]	39,875	—	—	39,875
2005				
Total revenues	$59,858	$32,076	$16,847	$108,781
Real estate and other fixed assets, net of accumulated depreciation	1,905	929	807	3,641
Flight equipment primarily under operating leases, net of accumulated depreciation[b]	36,245	—	—	36,245

(a) Including revenues from insurance operations in Canada of $1.3 billion, $1.1 billion and $968 million in 2007, 2006 and 2005, respectively.

(b) Approximately 90 percent of ILFC's fleet is operated by foreign airlines.

3. Investments

(a) Statutory Deposits: Cash and securities with carrying values of $13.6 billion and $14.8 billion were deposited by AIG's insurance subsidiaries under requirements of regulatory authorities at December 31, 2007 and 2006, respectively.

(b) Net Investment Income: An analysis of net investment income follows:

Years Ended December 31, *(in millions)*	**2007**	2006	2005
Fixed maturities[a]	**$ 22,330**	$ 20,393	$ 18,690
Equities	**2,361**	1,733	1,716
Interest on mortgage and other loans	**1,423**	1,253	1,177
Partnerships	**1,986**	1,596	1,056
Mutual funds	**650**	845	4
Other invested assets[b]	**941**	1,293	820
Total investment income	**29,691**	27,113	23,463
Investment expenses	**1,072**	1,043	879
Net investment income	**$ 28,619**	$ 26,070	$ 22,584

(a) Includes short-term investments.

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

3. Investments

Continued

(c) Net Realized Gains and Losses:

The Net realized capital gains (losses) and increase (decrease) in unrealized appreciation of AIG's available for sale investments were as follows:

(in millions)	**2007**	2006	2005
Net realized capital gains (losses):			
Sales of fixed maturities	**$ (468)**	$ (382)	$ 372
Sales of equity securities	**1,087**	813	643
Sales of real estate and other assets	**619**	303	88
Other-than-temporary impairments	**(4,072)**	(944)	(598)
Foreign exchange transactions	**(643)**	(382)	701
Derivative instruments	**(115)**	698	(865)
Total	**$(3,592)**	$ 106	$ 341
Increase (decrease) in unrealized appreciation of investments:			
Fixed maturities	**$(5,504)**	$ (198)	$(4,656)
Equity securities	**2,440**	432	850
Other investments	**(3,842)**	986	2,138
AIGFP investments	**(1,140)**	1,354	(1,909)
Increase (decrease) in unrealized appreciation	**$(8,046)**	$ 2,574	$(3,577)

Net unrealized gains (losses) included in the consolidated statement of income from investment securities classified as trading securities in 2007, 2006 and 2005 were $1.1 billion, $938 million and $1.1 billion, respectively.

The gross realized gains and gross realized losses from sales of AIG's available for sale securities were as follows:

	2007		2006		2005	
(in millions)	Gross Realized Gains	Gross Realized Losses	Gross Realized Gains	Gross Realized Losses	Gross Realized Gains	Gross Realized Losses
Fixed maturities	**$ 680**	**$ 1,148**	$ 711	$1,093	$1,586	$1,214
Equity securities	**1,368**	**291**	1,111	320	930	354
Preferred stocks	**10**	**—**	22	—	101	34
Total	**$ 2,058**	**$ 1,439**	$1,844	$1,413	$2,617	$1,602

(d) Fair Value of Investment Securities:

The amortized cost or cost and estimated fair value of AIG's available for sale and held to maturity securities at December 31, 2007 and 2006 were as follows:

	December 31, 2007*				December 31, 2006			
(in millions)	Amortized Cost or Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value	Amortized Cost or Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Available for sale:*								
U.S. government and government sponsored entities	**$ 7,956**	**$ 333**	**$ 37**	**$ 8,252**	$ 7,667	$ 221	$ 140	$ 7,748
Obligations of states, municipalities and political subdivisions	**46,087**	**927**	**160**	**46,854**	59,785	1,056	210	60,631
Non-U.S. governments	**67,023**	**3,920**	**743**	**70,200**	62,860	5,461	437	67,884
Corporate debt	**239,822**	**6,216**	**4,518**	**241,520**	257,383	7,443	2,536	262,290
Mortgage-backed, asset-backed and collateralized	**140,982**	**1,221**	**7,703**	**134,500**	104,687	502	362	104,827
Total bonds	**$501,870**	**$12,617**	**$13,161**	**$501,326**	$492,382	$14,683	$3,685	$ 503,380
Equity securities	**15,188**	**5,545**	**463**	**20,270**	13,147	2,807	159	15,795
Total	**$517,058**	**$18,162**	**$13,624**	**$521,596**	$505,529	$17,490	$3,844	$ 519,175
Held to maturity:*								
Bonds — Obligations of states, municipalities and political subdivisions	**$ 21,581**	**$ 609**	**$ 33**	**$ 22,157**	$ 21,437	$ 731	$ 14	$ 22,154

** At December 31, 2007 and 2006, fixed maturities held by AIG that were below investment grade or not rated totaled $27.0 billion and $26.6 billion, respectively.*

3. Investments

Continued

The following table presents the amortized cost and estimated fair values of AIG's available for sale and held to maturity fixed maturity securities at December 31, 2007, by contractual maturity. Actual maturities may differ from contractual maturities because certain borrowers have the right to call or prepay certain obligations with or without call or prepayment penalties.

	Available for Sale		Held to Maturity	
(in millions)	Amortized Cost	Fair Value	Amortized Cost	Fair Value
Due in one year or less	$ 25,844	$ 25,994	$ 72	$ 69
Due after one year through five years	95,494	97,466	284	277
Due after five years through ten years	121,961	123,196	1,511	1,547
Due after ten years	117,589	120,170	19,714	20,264
Mortgage-backed, asset-backed and collateralized	140,982	134,500	—	—
Total available for sale	$501,870	$501,326	$ 21,581	$ 22,157

AIG's available for sale securities are recorded on the consolidated balance sheet at December 31, 2007 and 2006 as follows:

	Fair Value	
(in millions)	**2007**	2006
Bonds available for sale	**$397,372**	$386,869
Common stocks available for sale	**17,900**	13,256
Preferred stocks available for sale	**2,370**	2,539
Financial Services securities available for sale	**40,305**	47,205
Securities lending invested collateral	**63,649**	69,306
Total	**$521,596**	$519,175

(e) Non-Income Producing Invested Assets: At December 31, 2007, non-income producing invested assets were insignificant.

(f) Gross Unrealized Losses and Estimated Fair Values on Investments:

The following table summarizes the cost basis and gross unrealized losses on AIG's available for sale securities, aggregated by major investment category and length of time that individual securities have been in a continuous unrealized loss position, at December 31, 2007 and 2006:

	12 Months or less		More than 12 Months		Total	
(in millions)	Cost[a]	Unrealized Losses	Cost[a]	Unrealized Losses	Cost[a]	Unrealized Losses
2007						
Bonds[b]	**$190,809**	**$ 9,935**	**$65,137**	**$ 3,226**	**$255,946**	**$13,161**
Equity securities	**4,433**	**463**	**—**	**—**	**4,433**	**463**
Total	**$195,242**	**$10,398**	**$65,137**	**$ 3,226**	**$260,379**	**$13,624**
2006						
Bonds[b]	$ 69,656	$ 1,257	$84,040	$ 2,428	$153,696	$ 3,685
Equity securities	2,734	159	—	—	2,734	159
Total	$ 72,390	$ 1,416	$84,040	$ 2,428	$156,430	$ 3,844

(a) For bonds, represents amortized cost.

(b) Primarily relates to the corporate debt category.

At December 31, 2007, AIG held 37,281 and 2,307 of individual bond and stock investments, respectively, that were in an unrealized loss position, of which 9,930 individual investments were in an unrealized loss position for a continuous 12 months or longer.

AIG recorded other-than-temporary impairment charges of $4.7 billion (including $643 million related to AIGFP recorded in Other income), $944 million and $598 million in 2007, 2006 and 2005, respectively. See Note 1(c) herein for AIG's other-than-temporary impairment accounting policy.

3. Investments

Continued

(g) Other Invested Assets:

Other invested assets at December 31, 2007 and 2006 consisted of the following:

At December 31, (in millions)	2007	2006
Partnerships[(a)]	$ 28,938	$21,657
Mutual funds	4,891	4,892
Investment real estate[(b)]	9,877	5,694
Aircraft asset investments[(c)]	1,689	1,784
Life settlement contracts[(d)]	1,627	1,090
Consolidated managed partnerships and funds[(e)]	6,614	2,923
All other investments	5,187	4,071
Other invested assets	$ 58,823	$42,111

(a) Includes private equity partnerships and hedge funds.

(b) Net of accumulated depreciation of $548 million and $585 million in 2007 and 2006, respectively.

(c) Consist primarily of Life Insurance & Retirement Services investments in aircraft equipment.

(d) See paragraph (h) below for additional information.

(e) Represents AIG managed partnerships and funds that are consolidated.

At December 31, 2007 and 2006, $7.2 billion and $5.3 billion of Other invested assets related to available for sale investments carried at fair value, with unrealized gains and losses recorded in of Accumulated other comprehensive income (loss), net of deferred taxes, with almost all of the remaining investments being accounted for on the equity method of accounting. All of the investments are subject to impairment testing (see Note 1(c) herein). The gross unrealized loss on the investments accounted for as available for sale at December 31, 2007 was $621 million, the majority of which represents investments that have been in a continuous unrealized loss position for less than 12 months.

(h) Investments in Life Settlement Contracts: At December 31, 2007, the carrying value of AIG's life settlement contracts was $1.6 billion, and is included in Other invested assets in the consolidated balance sheet. These investments are monitored for impairment on a contract by contract basis quarterly. During 2007, income recognized on life settlement contracts previously held in non-consolidated trusts was $32 million, and is included in net investment income in the consolidated statement of income.

Further information regarding life settlement contracts at December 31, 2007 is as follows:

(dollars in millions)

Remaining Life Expectancy of Insureds	Number of Contracts	Carrying Value	Face Value (Death Benefits)
0 – 1 year	11	$ 7	$ 9
1 – 2 years	34	34	47
2 – 3 years	79	61	98
3 – 4 years	151	111	210
4 – 5 years	176	130	277
Thereafter	2,181	1,284	5,400
Total	2,632	$1,627	$6,041

At December 31, 2007, the anticipated life insurance premiums required to keep the life settlement contracts in force, payable in the ensuing twelve months ending December 31, 2008 and the four succeeding years ending December 31, 2012 are $132 million, $141 million, $149 million, $146 million, and $152 million, respectively.

In June 2006, AIG restructured its ownership of life settlement contracts with no effect on the economic substance of these investments. At the same time, AIG paid $610 million to its former co-investors to acquire all the remaining interests in life settlement contracts held in previously non-consolidated trusts. The life insurers for a small portion of AIG's consolidated life settlement contracts include AIG subsidiaries. As a result, amounts related to life insurance issued by AIG subsidiaries are eliminated in consolidation.

4. Lending activities

Mortgages and other loans receivable at December 31, 2007 and 2006 are comprised of the following:

Years Ended December 31, *(in millions)*	2007	2006
Mortgages – commercial	$17,105	$15,219
Mortgages – residential*	2,153	1,903
Life insurance policy loans	8,099	7,501
Collateral, guaranteed, and other commercial loans	6,447	3,859
Total mortgage and other loans receivable	33,804	28,482
Allowance for losses	(77)	(64)
Mortgage and other loans receivable, net	$33,727	$28,418

** Primarily consists of foreign mortgage loans.*

4. Lending activities

Continued

Finance receivables, net of unearned finance charges, were as follows:

Years Ended December 31, *(in millions)*	2007	2006
Real estate loans	**$20,023**	$20,321
Non-real estate loans	**5,447**	4,506
Retail sales finance	**3,659**	3,092
Credit card loans	**1,566**	1,413
Other loans	**1,417**	978
Total finance receivables	**32,112**	30,310
Allowance for losses	**(878)**	(737)
Finance receivables, net	**$31,234**	$29,573

5. Reinsurance

In the ordinary course of business, AIG's General Insurance and Life Insurance companies place reinsurance with other insurance companies in order to provide greater diversification of AIG's business and limit the potential for losses arising from large risks. In addition, AIG's General Insurance subsidiaries assume reinsurance from other insurance companies.

Supplemental information for gross loss and benefit reserves net of ceded reinsurance at December 31, 2007 and 2006 follows:

(in millions)	As Reported	Net of Reinsurance
2007		
Reserve for losses and loss expenses	**$ (85,500)**	**$ (69,288)**
Future policy benefits for life and accident and health insurance contracts	**(136,068)**	**(134,461)**
Reserve for unearned premiums	**(28,022)**	**(24,029)**
Reinsurance assets*	**21,811**	**—**
2006		
Reserve for losses and loss expenses	$ (79,999)	$ (62,630)
Future policy benefits for life and accident and health insurance contracts	(121,004)	(119,430)
Reserve for unearned premiums	(26,271)	(22,759)
Reinsurance assets*	22,456	—

** Represents gross reinsurance assets, excluding allowances and reinsurance recoverable on paid losses.*

AIRCO acts primarily as an internal reinsurance company for AIG's insurance operations. This facilitates insurance risk management (retention, volatility, concentrations) and capital planning locally (branch and subsidiary). It also allows AIG to pool its insurance risks and purchase reinsurance more efficiently at a consolidated level, manage global counterparty risk and relationships and manage global life catastrophe risks.

General Reinsurance

General reinsurance is effected under reinsurance treaties and by negotiation on individual risks. Certain of these reinsurance arrangements consist of excess of loss contracts which protect AIG against losses over stipulated amounts. Ceded premiums are considered prepaid reinsurance premiums and are recognized as a reduction of premiums earned over the contract period in proportion to the protection received. Amounts recoverable from general reinsurers are estimated in a manner consistent with the claims liabilities associated with the reinsurance and presented as a component of reinsurance assets. Assumed reinsurance premiums are earned primarily on a pro-rata basis over the terms of the reinsurance contracts. For both ceded and assumed reinsurance, risk transfer requirements must be met in order for reinsurance accounting to apply. If risk transfer requirements are not met, the contract is accounted for as a deposit, resulting in the recognition of cash flows under the contract through a deposit asset or liability and not as revenue or expense. To meet risk transfer requirements, a reinsurance contract must include both insurance risk, consisting of both underwriting and timing risk, and a reasonable possibility of a significant loss for the assuming entity. Similar risk transfer criteria are used to determine whether directly written insurance contracts should be accounted for as insurance or as a deposit.

5. Reinsurance

Continued

General Insurance premiums written and earned were comprised of the following:

Years Ended December 31, *(in millions)*	2007	2006	2005
Premiums written:			
Direct	**$ 52,055**	$ 49,609	$ 46,689
Assumed	**6,743**	6,671	6,036
Ceded	**(11,731)**	(11,414)	(10,853)
Total	**$ 47,067**	$ 44,866	$ 41,872
Premiums earned:			
Direct	**$ 50,403**	$ 47,973	$ 45,794
Assumed	**6,530**	6,449	5,921
Ceded	**(11,251)**	(10,971)	(10,906)
Total	**$ 45,682**	$ 43,451	$ 40,809

For the years ended December 31, 2007, 2006 and 2005, reinsurance recoveries, which reduced loss and loss expenses incurred, amounted to $9.0 billion, $8.3 billion and $20.7 billion, respectively.

Life Reinsurance

Life reinsurance is effected principally under yearly renewable term treaties. The premiums with respect to these treaties are considered prepaid reinsurance premiums and are recognized as a reduction of premiums earned over the contract period in proportion to the protection provided. Amounts recoverable from life reinsurers are estimated in a manner consistent with the assumptions used for the underlying policy benefits and are presented as a component of reinsurance assets.

Life Insurance & Retirement Services premiums were comprised of the following:

Years Ended December 31, *(in millions)*	2007	2006	2005
Gross premiums	**$34,585**	$32,247	$30,818
Ceded premiums	**(1,778)**	(1,481)	(1,317)
Premiums	**$32,807**	$30,766	$29,501

Life Insurance recoveries, which reduced death and other benefits, approximated $1.1 billion, $806 million and $770 million, respectively, for the years ended December 31, 2007, 2006 and 2005.

Life Insurance in-force ceded to other insurance companies was as follows:

At December 31, *(in millions)*	2007	2006	2005
Life Insurance in force ceded	**$402,654**	$408,970	$365,082

Life Insurance assumed represented less than 0.1 percent, 0.1 percent and 0.8 percent of gross Life Insurance in force at December 31, 2007, 2006 and 2005, respectively, and Life Insurance & Retirement Services premiums assumed represented 0.1 percent, 0.1 percent and 0.3 percent of gross premiums and other considerations for the years ended December 31, 2007, 2006 and 2005, respectively.

AIG's Domestic Life Insurance & Retirement Services operations utilize internal and third-party reinsurance relationships to manage insurance risks and to facilitate capital management strategies. Pools of highly-rated third-party reinsurers are utilized to manage net amounts at risk in excess of retention limits. AIG's Domestic Life Insurance companies also cede excess, non-economic reserves carried on a statutory-basis only on certain term and universal life insurance policies and certain fixed annuities to an offshore affiliate.

AIG generally obtains letters of credit in order to obtain statutory recognition of its intercompany reinsurance transactions. For this purpose, AIG has a $2.5 billion syndicated letter of credit facility outstanding at December 31, 2007, all of which relates to life intercompany reinsurance transactions.

AIG is also a party to a 364-day bilateral revolving credit facility for an aggregate amount of $3.2 billion. The facility can be drawn in the form of letters of credit with terms of up to eight years. At December 31, 2007, approximately $3.0 billion principal amount of letters of credit are outstanding under this facility, of which approximately $2.1 billion relates to life intercompany reinsurance transactions. AIG has also obtained approximately $377 million of letters of credit on a bilateral basis.

Reinsurance Security

AIG's third-party reinsurance arrangements do not relieve AIG from its direct obligation to its insureds. Thus, a credit exposure exists with respect to both general and life reinsurance ceded to the extent that any reinsurer fails to meet the obligations assumed under any reinsurance agreement. AIG holds substantial collateral as security under related reinsurance agreements in the form of funds, securities, and/or letters of credit. A provision has been recorded for estimated unrecoverable reinsurance. AIG has been largely successful in prior recovery efforts.

AIG evaluates the financial condition of its reinsurers and establishes limits per reinsurer through AIG's Credit Risk Committee. AIG believes that no exposure to a single reinsurer represents an inappropriate concentration of risk to AIG, nor is AIG's business substantially dependent upon any single reinsurer.

6. Deferred Policy Acquisition Costs

The following reflects the policy acquisition costs deferred for amortization against future income and the related amortization charged to income for General Insurance and Life Insurance & Retirement Services operations:

Years Ended December 31, *(in millions)*	**2007**	2006	2005
General Insurance operations:			
Balance at beginning of year	**$ 4,355**	$ 4,048	$ 3,998
Acquisition costs deferred	**8,661**	8,115	7,480
Amortization expense	**(8,235)**	(7,866)	(7,365)
Increase (decrease) due to foreign exchange and other	**(138)**	58	(65)
Balance at end of year	**$ 4,643**	$ 4,355	$ 4,048
Life Insurance & Retirement Services operations:			
Balance at beginning of year	**$32,810**	$28,106	$25,080
Acquisition costs deferred	**7,276**	6,823	6,513
Amortization expense[(a)]	**(3,367)**	(3,712)	(3,328)
Change in net unrealized gains (losses) on securities	**745**	646	977
Increase (decrease) due to foreign exchange	**916**	947	(1,136)
Other[(b)]	**65**	—	—
Subtotal	**$38,445**	$32,810	$28,106
Consolidation and eliminations	**62**	70	—
Balance at end of year[(c)]	**$38,507**	$32,880	$28,106
Total deferred policy acquisition costs	**$43,150**	$37,235	$32,154

(a) In 2007, amortization expense was reduced by $733 million related to changes in actuarial estimates, which was mostly offset in incurred policy losses and benefits.

(b) In 2007, includes the cumulative effect of the adoption of SOP 05-1 of $(118) million and a balance sheet reclassification of $189 million.

(c) Includes $5 million and $(720) million at December 31, 2007 and 2006, respectively, related to the effect of net unrealized gains and losses on available for sale securities.

Included in the above table is the VOBA, an intangible asset recorded during purchase accounting, which is amortized in a manner similar to DAC. Amortization of VOBA was $213 million, $239 million and $291 million in 2007, 2006 and 2005, respectively, while the unamortized balance was $1.86 billion, $1.98 billion and $2.14 billion at December 31, 2007, 2006 and 2005, respectively. The percentage of the unamortized balance of VOBA at 2007 expected to be amortized in 2008 through 2012 by year is: 11.7 percent, 10.2 percent, 8.4 percent, 6.6 percent and 5.9 percent, respectively, with 57.2 percent being amortized after five years. These projections are based on current estimates for investment, persistency, mortality and morbidity assumptions. The DAC amortization charged to income includes the increase or decrease of amortization for FAS 97-related realized capital gains (losses), primarily in the Domestic Retirement Services business. In 2007, 2006 and 2005, the rate of amortization expense decreased by $291 million, $90 million and $46 million, respectively.

There were no impairments of DAC or VOBA for the years ended December 31, 2007, 2006 and 2005.

7. Variable Interest Entities

FIN 46R, ''Consolidation of Variable Interest Entities'' clarifies the consolidation accounting for certain entities in which equity investors do not have the characteristics of a controlling financial interest or do not have sufficient equity that is at risk which would allow the entity to finance its activities without additional subordinated financial support. FIN 46R recognizes that consolidation based on majority voting interest should not apply to certain types of entities that are defined as VIEs. A VIE is consolidated by its primary beneficiary, which is the party that absorbs a majority of the expected losses or a majority of the expected residual returns of the VIE, or both.

AIG, in the normal course of business, is involved with various VIEs. In some cases, AIG has participated to varying degrees in the design of the entity. AIG's involvement in VIEs varies from being a passive investor to managing and structuring the activities of the VIE. AIG engages in transactions with VIEs to manage its investment needs, obtain funding as well as facilitate client needs through a global network of operating subsidiaries comprising AIG Global Asset Management Holdings Corp. and its subsidiaries and affiliated companies (collectively, AIG Investments) and AIGFP. AIG purchases debt securities (rated and unrated) and equity interests issued by VIEs, makes loans and provides other credit support to VIEs, enters into insurance and reinsurance transactions with VIEs, enters into leasing arrangements with VIEs, enters into derivative transactions with VIEs through AIGFP and acts as the collateral manager of VIEs through AIG Investments and AIGFP. Obligations to outside interest holders in VIEs consolidated by AIG are reported as liabilities in the consolidated financial statements. These interest holders generally have recourse only to the assets

7. Variable Interest Entities

Continued

and cash flows of the VIEs and do not have recourse to AIG, except when AIG has provided a guarantee to the VIE's interest holders.

AIG determines whether an entity is a VIE, who the variable interest holders are, and which party is the primary beneficiary of the VIE by performing an analysis of the design of the VIE that includes a review of, among other factors, its capital structure, contractual relationships and terms, nature of the entity's operations and purpose, nature of the entity's interests issued, AIG's interests in the entity which either create or absorb variability and related party relationships. AIG consolidates a VIE when all of AIG's interests in the VIE, when combined, absorb a majority of the expected losses or a majority of the expected residual returns of the VIE, or both. Assets held by VIEs which are currently consolidated because AIG is primary beneficiary (except for those VIEs where AIG also owns a majority voting interest), approximated $27.0 billion and $9.1 billion at December 31, 2007 and 2006, respectively. These consolidated assets are reflected in AIG's consolidated balance sheet as Investments and financial services assets.

In addition to the VIEs that are consolidated in accordance with FIN 46R, the Company has significant variable interests in certain other VIEs that are not consolidated because the Company is not the primary beneficiary. AIG applies quantitative and qualitative measures in identifying whether it is a primary beneficiary of a VIE and whether it holds a significant variable interest in a VIE.

For all VIEs in which it has a significant variable interest, including those in which it is the primary beneficiary, AIG reconsiders if it is the current primary beneficiary whenever a VIE's governing documents or contractual arrangements are changed in a manner that reallocates between the primary beneficiary and other unrelated parties, the obligation to absorb expected losses or right to receive expected residual returns. It also reconsiders its role as primary beneficiary when it sells or otherwise disposes of all or part of its variable interests in a VIE or when it acquires additional variable interests in a VIE. AIG does not reconsider whether it is a primary beneficiary solely as the result of operating losses incurred by an entity. Assets of VIEs where AIG has a significant variable interest and does not consolidate the VIE because AIG is not the primary beneficiary, approximated $275.1 billion at December 31, 2007. AIG's maximum exposure to loss from its involvement with these consolidated VIEs approximated $44.6 billion at December 31, 2007. For this purpose, maximum loss is considered to be the notional amount of credit lines, guarantees and other credit support, and liquidity facilities, the notional amounts of credit default swaps and certain total return swaps, and the amount invested in the debt or equity issued by the VIEs.

Entities for which AIG is the primary beneficiary and consolidates or in which AIG has a significant variable interest are described below.

Asset Management

In certain instances, AIG Investments acts as the collateral manager or general partner of an investment fund, collateralized debt obligation (CDO), collateralized loan obligation (CLO), private equity fund or hedge fund. Such entities are typically registered investment companies or qualify for the specialized investment company accounting in accordance with the AICPA Audit and Accounting Guide - Investment Companies. In CDO and CLO transactions, AIG establishes a trust or other special purpose entity that purchases a portfolio of assets such as bank loans, corporate debt, or non-performing credits and issues trust certificates or debt securities that represent interests in the portfolio of assets. These transactions can be cash-based or synthetic and are actively or passively managed. For investment partnerships, hedge funds and private equity funds, AIG acts as the general partner or manager of the fund and is responsible for carrying out the investment mandate of the VIE. Often, AIG's insurance operations participate in these AIG managed structures as a passive investor in the debt or equity issued by the VIE. Typically, AIG does not provide any guarantees to the investors in the VIE.

AIG Investments is an investor in various real estate investments. These investments are typically with unaffiliated third-party developers via a partnership or limited liability company structure. Some of these entities are VIEs. The activities of these VIEs principally consist of the development or redevelopment of all major types of commercial (retail, office, industrial, logistics parks, mixed use, etc.) and residential real estate. AIG's involvement varies from being a passive equity investor to actively managing the activities of the VIE.

In addition to changes in a VIE's governing documentation or capitalization structure, AIG reconsiders its decision with respect to whether it is the primary beneficiary for these VIEs, when AIG purchases, or when a VIE sells or otherwise disposes of, variable interests in the CDO, CLO, investment, partnership, hedge fund or private equity fund to other unrelated parties.

SunAmerica Affordable Housing Partnerships

SunAmerica Affordable Housing Partners, Inc. (SAAHP) organizes limited partnerships (investment partnerships) that are considered to be VIEs, and that are consolidated by AIG when AIG has determined that it is the primary beneficiary. The investment partnerships invest as limited partners in operating partnerships that develop and operate affordable housing qualifying for federal tax credits and a few market rate properties across the United States. The general partners in the operating partnerships are almost exclusively unaffiliated third-party developers. AIG does not normally consolidate an operating partnership if the general partner is an unaffiliated person. Through approximately 1,200 partnerships, SAAHP has invested in developments with approximately 157,000 apartment units nationwide, and has

7. Variable Interest Entities

Continued

syndicated over $7 billion in partnership equity since 1991 to other investors who will receive, among other benefits, tax credits under certain sections of the Internal Revenue Code. AIG Retirement Services, Inc. functions as the general partner in certain investment partnerships and acts both as a credit enhancer in certain transactions, through differing structures with respect to funding development costs for the operating partnerships, and as guarantor that investors will receive the tax benefits projected at the time of syndication. AIG Retirement Services, Inc. consolidates these investment partnerships as a result of the guarantee provided to the investors. As part of their incentive compensation, certain key SAAHP employees have been awarded residual cash flow interests in the partnerships, subject to certain vesting requirements. The operating income of SAAHP is reported, along with other SunAmerica partnership income, as a component of AIG's Asset Management segment.

Insurance Investments

As part of its investment activities, AIG's insurance operations invest in obligations which include debt and equity securities and interests issued by VIEs. These investments include investments in AIG sponsored and non-sponsored investment funds, hedge funds, private equity funds, and structured financing arrangements. The investments in these VIEs allow AIG's insurance entities to purchase assets permitted by insurance regulations while maximizing their return on these assets. AIG's insurance operations typically are not involved in the design or establishment of the VIE, nor do they actively participate in the management of the VIE.

In addition to changes in a VIE's governing documentation or capitalization structure, AIG reconsiders its position as to whether it is the primary beneficiary as the result of investments in these VIEs when AIG purchases or sells VIE issued debt and equity interests to other unrelated parties.

AIGFP

The variable interests that AIGFP may hold in VIEs include debt securities, equity interests, loans, derivative instruments and other credit support arrangements. Transactions associated with VIEs include an asset-backed commercial paper conduit, asset securitizations, collateralized debt obligations, investment vehicles and other structured financial transactions. AIGFP engages in these transactions to facilitate client needs for investment purposes and to obtain funding.

AIGFP invests in preferred securities issued by VIEs. Additionally, AIGFP establishes VIEs that issue preferred interests to third parties and uses the proceeds to provide financing to AIGFP subsidiaries. In certain instances, AIGFP consolidates these VIEs. Consistent with FIN 46R requirements, AIGFP reviews any changes in its holdings of a VIEs preferred stock investment as part of its reconsideration review to determine a VIE's primary beneficiary. In addition, AIG reviews all changes in such VIEs' governing documentation or capitalization structures as part of the determination of whether there is a change in the VIEs' primary beneficiaries.

AIGFP is the primary beneficiary of an asset-backed commercial paper conduit with which it entered into several total return swaps covering all the conduit's assets that absorb the majority of the expected losses of the entity. The assets of the conduit serve as collateral for the conduit's obligations. AIGFP is also the primary beneficiary of several structured financing transactions in which AIGFP holds the first loss position either by investing in the equity of the VIE or implicitly through a lending or derivative arrangement. These VIEs are subject to the reconsideration event reviews noted above.

In certain instances, AIGFP enters into liquidity facilities with various SPEs when AIGFP provides liquidity to the SPE in the form of a guarantee, derivative, or a letter of credit and does not consolidate the VIE. AIGFP also executes various swap and option transactions with VIEs. Such contractual arrangements are done in the ordinary course of business. Typically, interest rate derivatives such as interest rate swaps and options executed with VIEs are not deemed to be variable interests or significant variable interests because the underlying is an observable market interest rate and AIGFP as the derivative counterparty to the VIE is senior to the debt and equity holders.

In 2007, AIGFP sponsored its only structured investment vehicle (SIV) which invests in variable rate, investment-grade debt securities. The SIV is a VIE because is does not have sufficient equity to operate without subordinated capital notes which serve as equity though they are legally debt instruments. The capital notes absorb losses prior to the senior debt. Based on the sale of more than 88 percent of its capital notes to unrelated third-party investors and the continued holding by those investors of their capital notes, AIGFP is not the primary beneficiary of the SIV. AIGFP reviews its primary beneficiary position when the governing document or capital structure changes or the amount of senior or capital note holdings change. Based on a change in the governing documents under which AIGFP committed to provide short-term funding to the SIV, as necessary, a quantitative analysis performed under FIN 46R as of December 31, 2007 showed that AIGFP is not the primary beneficiary. This outcome is a result of the high credit quality of the assets and the fact that 85 percent of credit losses, if any, would be shared by other capital note holders. At December 31, 2007 assets of this unconsolidated SIV totaled $2.4 billion. AIGFP's invested assets at December 31, 2007 included $1.7 billion of securities purchased under agreements to resell and commercial paper and medium-term and capital notes issued by this entity.

AIGFP has entered into transactions with VIEs that are used, in part, to provide tax planning strategies to investors and/or AIGFP through an enhanced yield investment security. These structures typically provide financing to AIGFP and/or the investor at enhanced rates. AIGFP may be either the primary beneficiary of and consolidate the VIE, or may be a significant variable interest holder in the VIE.

8. Derivatives and Hedge Accounting

AIG uses derivatives and other financial instruments as part of its financial risk management programs and as part of its investment operations. AIGFP also transacts in derivatives as a dealer.

Derivatives, as defined in FAS 133, are financial arrangements among two or more parties with returns linked to or ''derived'' from some underlying equity, debt, commodity or other asset, liability, or foreign exchange rate or other index or the occurrence of a specified payment event. Derivative payments may be based on interest rates, exchange rates, prices of certain securities, commodities, or financial or commodity indices or other variables.

Unless subject to a scope exclusion, AIG carries all derivatives on the consolidated balance sheet at fair value. The changes in fair value of the derivative transactions of AIGFP are presented as a component of AIG's operating income.

AIGFP

AIGFP, in the ordinary course of operations and as principal, structures and enters into derivative transactions to meet the needs of counterparties who may be seeking to hedge certain aspects of such counterparties' operations or obtain a desired financial exposure. In most cases AIGFP does not hedge its exposures related to the credit default swaps it has written. AIGFP also enters into derivative transactions to mitigate risk in its exposures (interest rates, currencies, commodities, credit and equities) arising from such transactions. Such instruments are carried at market or fair value, whichever is appropriate, and are reflected on the balance sheet in ''Unrealized gain on swaps, options and forward transactions'' and ''Unrealized loss on swaps, options and forward contracts.''

Beginning in 2007, AIGFP designated certain interest rate swaps as fair value hedges of the benchmark interest rate risk on certain of its interest bearing financial assets and liabilities. In these hedging relationships, AIG is hedging its fixed rate available for sale securities and fixed rate borrowings. AIGFP also designated foreign currency forward contracts as fair value hedges for changes in spot foreign exchange rates of the non-U.S. dollar denominated available for sale debt securities. Under these strategies, all or portions of individual or multiple derivatives may be designated against a single hedged item.

At inception of each hedging relationship, AIGFP performs and documents its prospective assessments of hedge effectiveness to demonstrate that the hedge is expected to be highly effective. For hedges of interest rate risk, AIGFP uses regression to demonstrate the hedge is highly effective, while it uses the periodic dollar offset method for its foreign currency hedges. AIGFP uses the periodic dollar offset method to assess whether its hedging relationships were highly effective on a retrospective basis. The prospective and retrospective assessments are updated on a daily basis. The passage of time component of the hedging instruments and the forward points on foreign currency hedges are excluded from the assessment of hedge effectiveness and measurement of hedge ineffectiveness. AIGFP does not utilize the shortcut, matched terms or equivalent methods to assess hedge effectiveness.

The change in fair value of the derivative that qualifies under the requirements of FAS 133 as a fair value hedge is recorded in current period earnings along with the gain or loss on the hedged item for the hedged risk. For interest rate hedges, the adjustments to the carrying value of the hedged items are amortized into income using the effective yield method over the remaining life of the hedged item. Amounts excluded from the assessment of hedge effectiveness are recognized in current period earnings.

For the year ended December 31, 2007, AIGFP recognized net losses of $0.7 million in earnings, representing hedge ineffectiveness, and also recognized net losses of $456 million related to the portion of the hedging instruments excluded from the assessment of hedge effectiveness.

AIGFP's derivative transactions involving interest rate swap transactions generally involve the exchange of fixed and floating rate interest payment obligations without the exchange of the underlying notional amounts. AIGFP typically becomes a principal in the exchange of interest payments between the parties and, therefore, is exposed to counterparty credit risk and may be exposed to loss, if counterparties default. Currency, commodity, and equity swaps are similar to interest rate swaps, but involve the exchange of specific currencies or cashflows based on the underlying commodity, equity securities or indices. Also, they may involve the exchange of notional amounts at the beginning and end of the transaction. Swaptions are options where the holder has the right but not the obligation to enter into a swap transaction or cancel an existing swap transaction. At December 31, 2007, the aggregate notional amount of AIGFP's outstanding swap transactions approximated $2,133 billion, primarily related to interest rate swaps of approximately $1,167 billion.

AIGFP follows a policy of minimizing interest rate, currency, commodity, and equity risks associated with securities available for sale by entering into internal offsetting positions, on a security by security basis within its derivatives portfolio, thereby offsetting a significant portion of the unrealized appreciation and depreciation. In addition, to reduce its credit risk, AIGFP has entered into credit derivative transactions with respect to $82 million of securities available for sale to economically hedge its credit risk. As previously discussed, these economic offsets did not meet the hedge accounting requirements of FAS 133 and, therefore, are recorded in Other income in the Consolidated Statement of Income.

Notional amount represents a standard of measurement of the volume of swaps business of Capital Markets operations. Notional amount is not a quantification of market risk or credit risk and is not recorded on the consolidated balance sheet. Notional amounts generally represent those amounts used to calculate contractual cash flows to be exchanged and are not paid or received, except for certain contracts such as currency swaps.

The timing and the amount of cash flows relating to Capital Markets foreign exchange forwards and exchange traded futures and options contracts are determined by each of the respective contractual agreements.

8. Derivatives and Hedge Accounting

Continued

The following table presents the notional amounts by remaining maturity of Capital Markets' interest rate, credit default and currency swaps and swaptions derivatives portfolio at December 31, 2007 and 2006:

	Remaining Life of Notional Amount*					
(in millions)	One Year	Two Through Five Years	Six Through Ten Years	After Ten Years	**Total 2007**	Total 2006
Interest rate swaps	$441,801	$ 554,917	$156,634	$ 14,112	**$1,167,464**	$1,058,279
Credit default swaps	184,924	286,069	85,792	5,028	**561,813**	483,648
Currency swaps	38,384	135,187	41,675	9,029	**224,275**	218,091
Swaptions, equity and commodity swaps	57,709	62,849	35,270	23,139	**178,967**	180,040
Total	$722,818	$1,039,022	$319,371	$ 51,308	**$2,132,519**	$1,940,058

** Notional amount is not representative of either market risk or credit risk and is not recorded in the consolidated balance sheet.*

Futures and forward contracts are contracts that obligate the holder to sell or purchase foreign currencies, commodities or financial indices in which the seller/purchaser agrees to make/take delivery at a specified future date of a specified instrument, at a specified price or yield. Options are contracts that allow the holder of the option to purchase or sell the underlying commodity, currency or index at a specified price and within, or at, a specified period of time. As a writer of options, AIGFP generally receives an option premium and then manages the risk of any unfavorable change in the value of the underlying commodity, currency or index by entering into offsetting transactions with third-party market participants. Risks arise as a result of movements in current market prices from contracted prices, and the potential inability of the counterparties to meet their obligations under the contracts.

The following table presents Capital Markets futures, forward and option contracts portfolio by maturity and type of derivative at December 31, 2007 and 2006:

	Remaining Life					
(in millions)	One Year	Two Through Five Years	Six Through Ten Years	After Ten Years	**Total 2007**	Total 2006
Exchange traded futures and options contracts contractual amount	$ 27,588	$1,359	$ —	$ —	**$ 28,947**	$ 27,271
Over the counter forward contracts contractual amount	485,332	5,864	1,850	—	**493,046**	492,913
Total	$512,920	$7,223	$1,850	$ —	**$521,993**	$520,184

AIGFP Credit Default Swaps

AIGFP enters into credit derivative transactions in the ordinary course of its business. The majority of AIGFP's credit derivatives require AIGFP to provide credit protection on a designated portfolio of loans or debt securities. AIGFP provides such credit protection on a ''second loss'' basis, under which AIGFP's payment obligations arise only after credit losses in the designated portfolio exceed a specified threshold amount or level of ''first losses.'' The threshold amount of credit losses that must be realized before AIGFP has any payment obligation is negotiated by AIGFP for each transaction to provide that the likelihood of any payment obligation by AIGFP under each transaction is remote. The underwriting process for these derivatives included assumptions of severely stressed recessionary market scenarios to minimize the likelihood of realized losses under these obligations.

In certain cases, the credit risk associated with a designated portfolio is tranched into different layers of risk, which are then analyzed and rated by the credit rating agencies. Typically, there will be an equity layer covering the first credit losses in respect of the portfolio up to a specified percentage of the total portfolio, and then successive layers ranging from generally a BBB-rated layer to one or more AAA-rated layers. In transactions that are rated with respect to the risk layer or tranche that is immediately junior to the threshold level above which AIGFP's payment obligation would generally arise, a significant majority are rated AAA by the rating agencies. In transactions that are not rated, AIGFP applies the same risk criteria for setting the threshold level for its payment obligations. Therefore, the risk layer assumed by AIGFP with respect to the designated portfolio in these transactions is often called the ''super senior'' risk layer, defined as the layer of credit risk senior to a risk layer that has been rated AAA by the credit rating agencies, or if the transaction is not rated, equivalent thereto.

8. Derivatives and Hedge Accounting

Continued

At December 31, 2007 and 2006, the notional amounts and unrealized market valuation loss of the super senior credit default swap portfolio by asset classes were as follows:

	Notional Amount (in billions)	Unrealized Market Valuation Loss (in millions)
Corporate loans[(a)]	**$230**	$ —
Prime residential mortgages[(a)]	**149**	—
Corporate Debt/CLOs	**70**	226
Multi-sector CDO[(b)]	**78**	11,246
Total	**$527**	$11,472

(a) Predominantly represent transactions written to facilitate regulatory capital relief.
(b) Approximately $61.4 billion, in notional amount, of the multi-sector CDO pools includes some exposure to U.S. subprime mortgages.

Approximately $379 billion of the $527 billion in notional exposure of AIGFP's super senior credit default swap portfolio as of December 31, 2007 represents derivatives written for financial institutions, principally in Europe, for the purpose of providing them with regulatory capital relief rather than risk mitigation. In exchange for a minimum guaranteed fee, the counterparties receive credit protection in respect of portfolios of various debt securities or loans they own, thus improving their regulatory capital position. These derivatives are generally expected to terminate at no additional cost to the counterparty upon the counterparty's adoption of models compliant with the Basel II Accord. AIG expects that the majority of these transactions will terminate within the next 12 to 18 months. As of February 26, 2008, approximately $54 billion in notional exposures have either been terminated or are in the process of being terminated. AIGFP was not required to make any payments as part of these terminations and in certain cases was paid a fee upon termination. In light of this experience to date and after other comprehensive analyses, AIG did not recognize an unrealized market valuation adjustment for this regulatory capital relief portfolio for the year ended December 31, 2007. AIG will continue to assess the valuation of this portfolio and monitor developments in the marketplace. There can be no assurance that AIG will not recognize unrealized market valuation losses from this portfolio in future periods. In addition to writing credit protection on the super senior risk layer on designated portfolios of loans or debt securities, AIGFP also wrote protection on tranches below the super senior risk layer. At December 31, 2007 the notional amount of the credit default swaps in the regulatory capital relief portfolio written on tranches below the super senior risk layer was $5.8 billion, with an estimated fair value of $(25) million.

AIGFP has also written credit protection on the super senior risk layer of diversified portfolios of investment grade corporate debt, collateralized loan obligations (CLOs) and multi-sector CDOs. AIGFP is at risk only on the super senior portion related to a diversified portfolio of credits referenced to loans or debt securities. The super senior risk portion is the last tranche to suffer losses after significant subordination. Credit losses would have to erode all tranches junior to the super senior tranche before AIGFP would suffer any realized losses. The subordination level required for each transaction is determined based on internal modeling and analysis of the pool of underlying assets and is not dependent on ratings determined by the rating agencies. While the credit default swaps written on corporate debt obligations are cash settled, the majority of the credit default swaps written on CDOs and CLOs require physical settlement. Under a physical settlement arrangement, AIGFP would be required to purchase the referenced super senior note obligation at par in the event of a non-payment on that security.

Certain of these credit derivatives are subject to collateral posting provisions. These provisions differ among counterparties and asset classes. In the case of most of the multi-sector CDO transactions, the amount of collateral required is determined based on the change in value of the underlying cash security that represents the super senior risk layer subject to credit protection, and not the change in value of the super senior credit derivative.

AIGFP is indirectly exposed to U.S. residential mortgage subprime collateral in the CDO portfolios, the majority of which is from 2004 and 2005 vintages. However, certain of the CDOs on which AIGFP provided credit protection permit the collateral manager to substitute collateral during the reinvestment period, subject to certain restrictions. As a result, in certain transactions, U.S. residential mortgage subprime collateral of 2006 and 2007 vintages has been added to the collateral pools. At December 31, 2007, U.S. residential mortgage subprime collateral of 2006 and 2007 vintages comprised approximately 4.9 percent of the total collateral pools underlying the entire portfolio of CDOs with credit protection.

AIGFP has written maturity-shortening puts that allow the holders of the securities issued by certain multi-sector CDOs to treat the securities as eligible short-term 2a-7 investments under the Investment Company Act of 1940 (2a-7 Puts). Holders of securities are permitted, in certain circumstances, to tender their securities to the issuers at par. If an issuer's remarketing agent is unable to resell the securities so tendered, AIGFP must purchase the securities at par as long as the securities have not experienced a default. During 2007, AIGFP repurchased securities with a principal amount of approximately $754 million pursuant to these obligations. In certain transactions, AIGFP has contracted with third parties to provide liquidity for the notes if they are put to AIGFP for up to a three-year period. Such liquidity facilities totaled approximately $3 billion at December 31, 2007. As of February 26, 2008, AIGFP has not utilized these liquidity facilities. At December 31, 2007, AIGFP had approximately $6.5 billion of notional exposure on 2a-7 Puts, included as part of the multi-sector CDO portfolio discussed herein.

As of January 31, 2008, a significant majority of AIGFP's super senior exposures continued to have tranches below AIGFP's attachment point that have been explicitly rated AAA or, in AIGFP's judgment, would have been rated AAA had they been rated. AIGFP's portfolio of credit default swaps undergoes regular

8. Derivatives and Hedge Accounting

Continued

monitoring, modeling and analysis and contains protection through collateral subordination.

AIGFP accounts for its credit default swaps in accordance with FAS 133 ''Accounting For Derivative Instruments and Hedging Activities'' and Emerging Issues Task Force 02-3, ''Issues Involved in Accounting for Derivative Contracts Held for Trading Purposes and Contracts Involved in Energy Trading and Risk Management Activities'' (EITF 02-3). In accordance with EITF 02-3, AIGFP does not recognize income in earnings at the inception of each transaction because the inputs to value these instruments are not derivable from observable market data.

The valuation of the super senior credit derivatives has become increasingly challenging given the limitation on the availability of market observable information due to the lack of trading and price transparency in the structured finance market, particularly in the fourth quarter of 2007. These market conditions have increased the reliance on management estimates and judgments in arriving at an estimate of fair value for financial reporting purposes. Further, disparities in the valuation methodologies employed by market participants and the varying judgments reached by such participants when assessing volatile markets has increased the likelihood that the various parties to these instruments may arrive at significantly different estimates as to their fair values.

AIGFP's valuation methodologies for the super senior credit default swap portfolio have evolved in response to the deteriorating market conditions and the lack of sufficient market observable information. AIG has sought to calibrate the model to market information and to review the assumptions of the model on a regular basis.

AIGFP employs a modified version of the BET model to value its super senior credit default swap portfolio, including the 2a-7 Puts. The BET model utilizes default probabilities derived from credit spreads implied from market prices for the individual securities included in the underlying collateral pools securing the CDOs. AIGFP obtained prices on these securities from the CDO collateral managers.

The BET model also utilizes diversity scores, weighted average lives, recovery rates and discount rates. The determination of some of these inputs require the use of judgment and estimates, particularly in the absence of market observable data. AIGFP also employed a Monte Carlo simulation to assist in quantifying the effect on valuation of the CDO of the unique features of the CDO's structure such as triggers that divert cash flows to the most senior level of the capital structure.

The credit default swaps written by AIGFP cover only the failure of payment on the super senior CDO security. AIGFP does not own the securities in the CDO collateral pool. The credit spreads implied from the market prices of the securities in the CDO collateral pool incorporate the risk of default (credit risk), the market's price for liquidity risk and in distressed markets, the risk aversion costs. Spreads on credit derivatives tend to be narrower because, unlike in the case of investing in a bond, there is no need to fund the position (except when an actual credit event occurs). In times of illiquidity, the difference between spreads on cash securities and derivative instruments (the ''negative basis'') may be even wider for high quality assets. AIGFP was unable to reliably verify this negative basis due to the accelerating severe dislocation, illiquidity and lack of trading in the asset backed securities market during the fourth quarter of 2007 and early 2008. The valuations produced by the BET model therefore represent the valuations of the underlying super senior CDO cash securities with no recognition of the effect of the basis differential on that valuation.

AIGFP also considered the valuation of the super senior CDO securities provided by third parties, including counterparties to these transactions, and made adjustments as necessary.

As described above, AIGFP uses numerous assumptions in determining its best estimate of the fair value of the super senior credit default swap portfolio. The most significant assumption utilized in developing the estimate is the pricing of the securities within the CDO collateral pools. If the actual pricing of the securities within the collateral pools differs from the pricing used in estimating the fair value of the super senior credit default swap portfolio, there is potential for significant variation in the fair value estimate.

In the case of credit default swaps written on investment grade corporate debt and CLOs, AIGFP estimated the value of its obligations by reference to the relevant market indices or third party quotes on the underlying super senior tranches where available.

AIGFP monitors the underlying portfolios to determine whether the credit loss experience for any particular portfolio has caused the likelihood of AIGFP having a payment obligation under the transaction to be greater than super senior risk.

Other Derivative Users

AIG and its subsidiaries (other than AIGFP) also use derivatives and other instruments as part of their financial risk management programs. Interest rate derivatives (such as interest rate swaps) are used to manage interest rate risk associated with investments in fixed income securities, commercial paper issuances, medium- and long-term note offerings, and other interest rate sensitive assets and liabilities. In addition, foreign exchange derivatives (principally cross currency swaps, forwards and options) are used to economically mitigate risk associated with non-U.S. dollar denominated debt, net capital exposures and foreign exchange transactions. The derivatives are effective economic hedges of the exposures they are meant to offset.

In 2007, AIG and its subsidiaries other than AIGFP designated certain derivatives as either fair value or cash flow hedges of their debt. The fair value hedges included (i) interest rate swaps that were designated as hedges of the change in the fair value of fixed

8. Derivatives and Hedge Accounting

Continued

rate debt attributable to changes in the benchmark interest rate and (ii) foreign currency swaps designated as hedges of the change in fair value of foreign currency denominated debt attributable to changes in foreign exchange rates and/or the benchmark interest rate. With respect to the cash flow hedges, (i) interest rate swaps were designated as hedges of the changes in cash flows on floating rate debt attributable to changes in the benchmark interest rate, and (ii) foreign currency swaps were designated as hedges of changes in cash flows on foreign currency denominated debt attributable to changes in the benchmark interest rate and foreign exchange rates.

AIG assesses, both at the hedge's inception and on an ongoing basis, whether the derivatives used in hedging transactions are highly effective in offsetting changes in fair values or cash flows of hedged items. Regression analysis is employed to assess the effectiveness of these hedges both on a prospective and retrospective basis. AIG does not utilize the shortcut, matched terms or equivalent methods to assess hedge effectiveness.

The change in fair value of derivatives designated and effective as fair value hedges along with the gain or loss on the hedged item are recorded in current period earnings. Upon discontinuation of hedge accounting, the cumulative adjustment to the carrying value of the hedged item resulting from changes in the benchmark interest rate or exchange rate is amortized into income using the effective yield method over the remaining life of the hedged item. Amounts excluded from the assessment of hedge effectiveness are recognized in current period earnings. During the year ended December 31, 2007, AIG recognized a loss of $1 million in earnings related to the ineffective portion of the hedging instruments. During the year ended December 31, 2007, AIG also recognized gains of $3 million related to the change in the hedging instruments forward points excluded from the assessment of hedge effectiveness.

The effective portion of the change in fair value of a derivative qualifying as a cash flow hedge is recorded in Accumulated other comprehensive income (loss), until earnings are affected by the variability of cash flows in the hedged item. The ineffective portion of these hedges is recorded in net realized capital gains (losses). During the year ended December 31, 2007, AIG recognized gains of $1 million in earnings representing hedge ineffectiveness. At December 31, 2007, $36 million of the deferred net loss in Accumulated other comprehensive income is expected to be recognized in earnings during the next 12 months. All components of the derivatives' gains and losses were included in the assessment of hedge effectiveness. There were no instances of the discontinuation of hedge accounting in 2007.

In addition to hedging activities, AIG also uses derivative instruments with respect to investment operations, which include, among other things, credit default swaps, and purchasing investments with embedded derivatives, such as equity linked notes and convertible bonds. All changes in the fair value of these derivatives are recorded in earnings. AIG bifurcates an embedded derivative where: *(i)* the economic characteristics of the embedded instruments are not clearly and closely related to those of the remaining components of the financial instrument; *(ii)* the contract that embodies both the embedded derivative instrument and the host contract is not remeasured at fair value; and *(iii)* a separate instrument with the same terms as the embedded instrument meets the definition of a derivative under FAS 133.

9. Reserve for Losses and Loss Expenses and Future Life Policy Benefits and Policyholders' Contract Deposits

The following analysis provides a reconciliation of the activity in the reserve for losses and loss expenses:

Years Ended December 31, *(in millions)*	**2007**	2006	2005
At beginning of year:			
Reserve for losses and loss expenses	**$79,999**	$ 77,169	$ 61,878
Reinsurance recoverable	**(17,369)**	(19,693)	(14,624)
Total	**62,630**	57,476	47,254
Foreign exchange effect	**955**	741	(628)
Acquisitions[(a)]	**317**	55	—
Losses and loss expenses incurred:			
Current year	**30,261**	27,805	28,426
Prior years, other than accretion of discount	**(656)**	(53)	4,680[(b)]
Prior years, accretion of discount	**327**	300	(15)
Total	**29,932**	28,052	33,091
Losses and loss expenses paid:			
Current year	**9,684**	8,368	7,331
Prior years	**14,862**	15,326	14,910
Total	**24,546**	23,694	22,241
At end of year:			
Net reserve for losses and loss expenses	**69,288**	62,630	57,476
Reinsurance recoverable	**16,212**	17,369	19,693
Total	**$85,500**	$ 79,999	$ 77,169

(a) Reflects the opening balance with respect to the acquisition of WüBa and the Central Insurance Co., Ltd. in 2007 and 2006, respectively.

(b) Includes a fourth quarter charge of $1.8 billion resulting from the annual review of General Insurance loss and loss adjustment reserves.

9. Reserve for Losses and Loss Expenses and Future Life Policy Benefits and Policyholders' Contract Deposits

Continued

The analysis of the future policy benefits and policyholders' contract deposits liabilities follows:

At December 31, *(in millions)*	**2007**	2006
Future policy benefits:		
Long duration contracts	**$135,202**	$120,138
Short duration contracts	**866**	866
Total	**$136,068**	$121,004
Policyholders' contract deposits:		
Annuities	**$140,444**	$141,826
Guaranteed investment contracts	**25,321**	33,054
Universal life products	**27,114**	22,497
Variable products	**46,407**	34,821
Corporate life products	**2,124**	2,083
Other investment contracts	**17,049**	13,983
Total	**$258,459**	$248,264

Long duration contract liabilities included in future policy benefits, as presented in the preceding table, result primarily from life products. Short duration contract liabilities are primarily accident and health products. The liability for future life policy benefits has been established based upon the following assumptions:

- Interest rates (exclusive of immediate/terminal funding annuities), which vary by territory, year of issuance and products, range from 1.0 percent to 12.5 percent within the first 20 years. Interest rates on immediate/terminal funding annuities are at a maximum of 11.5 percent and grade to not greater than 6.0 percent.
- Mortality and surrender rates are based upon actual experience by geographical area modified to allow for variations in policy form. The weighted average lapse rate, including surrenders, for individual and group life approximated 5.7 percent.
- The portions of current and prior net income and of current unrealized appreciation of investments that can inure to the benefit of AIG are restricted in some cases by the insurance contracts and by the local insurance regulations of the jurisdictions in which the policies are in force.
- Participating life business represented approximately 12 percent of the gross insurance in force at December 31, 2007 and 25 percent of gross premiums and other considerations in 2007. The amount of annual dividends to be paid is determined locally by the boards of directors. Provisions for future dividend payments are computed by jurisdiction, reflecting local regulations.

The liability for policyholders' contract deposits has been established based on the following assumptions:

- Interest rates credited on deferred annuities, which vary by territory and year of issuance, range from 1.4 percent to, including bonuses, 13.0 percent. Less than 1.0 percent of the liabilities are credited at a rate greater than 9.0 percent. Current declared interest rates are generally guaranteed to remain in effect for a period of one year though some are guaranteed for longer periods. Withdrawal charges generally range from zero percent to 20.0 percent grading to zero over a period of zero to 19 years.
- Domestically, guaranteed investment contracts (GICs) have market value withdrawal provisions for any funds withdrawn other than benefit responsive payments. Interest rates credited generally range from 2.8 percent to 9.0 percent. The vast majority of these GICs mature within five years.
- Interest rates on corporate life insurance products are guaranteed at 4.0 percent and the weighted average rate credited in 2007 was 5.2 percent.
- The universal life funds have credited interest rates of 1.0 percent to 7.0 percent and guarantees ranging from 1.0 percent to 5.5 percent depending on the year of issue. Additionally, universal life funds are subject to surrender charges that amount to 12.0 percent of the aggregate fund balance grading to zero over a period not longer than 20 years.
- For variable products and investment contracts, policy values are expressed in terms of investment units. Each unit is linked to an asset portfolio. The value of a unit increases or decreases based on the value of the linked asset portfolio. The current liability at any time is the sum of the current unit value of all investment units plus any liability for guaranteed minimum death or withdrawal benefits.

Certain products are subject to experience adjustments. These include group life and group medical products, credit life contracts, accident and health insurance contracts/riders attached to life policies and, to a limited extent, reinsurance agreements with other direct insurers. Ultimate premiums from these contracts are estimated and recognized as revenue, and the unearned portions of the premiums recorded as liabilities. Experience adjustments vary according to the type of contract and the territory in which the policy is in force and are subject to local regulatory guidance.

10. Variable Life and Annuity Contracts

AIG follows American Institute of Certified Public Accountants Statement of Position 03-1 (SOP 03-1), which requires recognition of a liability for guaranteed minimum death benefits and other living benefits related to variable annuity and variable life contracts as well as certain disclosures for these products.

AIG reports variable contracts through separate and variable accounts when investment income and investment gains and losses accrue directly to, and investment risk is borne by, the contract holder (traditional variable annuities), and the separate account qualifies for separate account treatment under SOP 03-1. In some foreign jurisdictions, separate accounts are not legally insulated from general account creditors and therefore do not qualify for separate account treatment under SOP 03-1. In such cases, the variable contracts are reported as general account contracts even though the policyholder bears the risks associated with the performance of the assets. AIG also reports variable

10. Variable Life and Annuity Contracts

Continued

annuity and life contracts through separate and variable accounts, or general accounts when not qualified for separate account reporting, when AIG contractually guarantees to the contract holder (variable contracts with guarantees) either *(a)* total deposits made to the contract less any partial withdrawals plus a minimum return (and in minor instances, no minimum returns) (Net Deposits Plus a Minimum Return) or *(b)* the highest contract value attained, typically on any anniversary date minus any subsequent withdrawals following the contract anniversary (Highest Contract Value Attained). These guarantees include benefits that are payable in the event of death, annuitization, or, in other instances, at specified dates during the accumulation period. Such benefits are referred to as guaranteed minimum death benefits (GMDB), guaranteed minimum income benefits (GMIB), guaranteed minimum withdrawal benefits (GMWB) and guaranteed minimum account value benefits (GMAV). For AIG, GMDB is by far the most widely offered benefit.

The assets supporting the variable portion of both traditional variable annuities and variable contracts with guarantees are carried at fair value and reported as Separate and variable account assets with an equivalent summary total reported as Separate and variable account liabilities when the separate account qualifies for separate account treatment under SOP 03-1. Assets for separate accounts that do not qualify for separate account treatment are reported as trading account assets, and liabilities are included in the respective policyholder liability account of the general account. Amounts assessed against the contract holders for mortality, administrative, and other services are included in revenue and changes in liabilities for minimum guarantees are included in incurred policy losses and benefits in the consolidated statement of income. Separate and variable account net investment income, net investment gains and losses, and the related liability changes are offset within the same line item in the consolidated statement of income for those accounts that qualify for separate account treatment under SOP 03-1. Net investment income and gains and losses on trading accounts for contracts that do not qualify for separate account treatment under SOP 03-1 are reported in net investment income and are principally offset by amounts reported in incurred policy losses and benefits.

The vast majority of AIG's exposure on guarantees made to variable contract holders arises from GMDB. Details concerning AIG's GMDB exposures at December 31, 2007 and 2006 are as follows:

(dollars in billions)	Net Deposits Plus a Minimum Return	Highest Contract Value Attained
2007		
Account value[(a)]	**$66**	**$17**
Amount at risk[(b)]	**5**	**1**
Average attained age of contract holders by product	**38-69 years**	**55-72 years**
Range of guaranteed minimum return rates	**3-10%**	
2006		
Account value[(a)]	$64	$15
Amount at risk[(b)]	6	1
Average attained age of contract holders by product	38-70 years	56-71 years
Range of guaranteed minimum return rates	0-10%	

(a) Included in Policyholders' contract deposits in the consolidated balance sheet.

(b) Represents the amount of death benefit currently in excess of Account value.

The following summarizes GMDB liabilities for guarantees on variable contracts reflected in the general account.

(in millions)	**2007**	2006
Balance at January 1	**$406**	$442
Reserve increase	**111**	35
Benefits paid	**(54)**	(71)
Balance at December 31	**$463**	$406

The GMDB liability is determined each period end by estimating the expected value of death benefits in excess of the projected account balance and recognizing the excess ratably over the accumulation period based on total expected assessments. AIG regularly evaluates estimates used and adjusts the additional liability balance, with a related charge or credit to benefit expense, if actual experience or other evidence suggests that earlier assumptions should be revised.

The following assumptions and methodology were used to determine the GMDB liability at December 31, 2007:

- Data used was up to 1,000 stochastically generated investment performance scenarios.
- Mean investment performance assumptions ranged from three percent to approximately ten percent depending on the block of business.
- Volatility assumptions ranged from eight percent to 23 percent depending on the block of business.
- Mortality was assumed at between 50 percent and 102 percent of various life and annuity mortality tables.
- For domestic contracts, lapse rates vary by contract type and duration and ranged from zero percent to 40 percent. For

10. Variable Life and Annuity Contracts

Continued

Japan, lapse rates ranged from zero percent to 20 percent depending on the type of contract.

- For domestic contracts, the discount rate ranged from 3.25 percent to 11 percent. For Japan, the discount rate ranged from two percent to seven percent.

In addition to GMDB, AIG's contracts currently include to a lesser extent GMIB. The GMIB liability is determined each period end by estimating the expected value of the annuitization benefits in excess of the projected account balance at the date of annuitization and recognizing the excess ratably over the accumulation period based on total expected assessments. AIG periodically evaluates estimates used and adjusts the additional liability balance, with a related charge or credit to benefit expense, if actual experience or other evidence suggests that earlier assumptions should be revised.

AIG contracts currently include a minimal amount of GMAV and GMWB. GMAV and GMWB are considered to be embedded derivatives and are recognized at fair value through earnings. AIG enters into derivative contracts to economically hedge a portion of the exposure that arises from GMAV and GMWB.

11. Debt Outstanding

At December 31, 2007 and 2006, AIG's total borrowings were as follows:

(in millions)	**2007**	2006
Total long-term borrowings	**$162,935**	$135,316
Commercial paper and extendible commercial notes	**13,114**	13,363
Total borrowings	**$176,049**	$148,679

Maturities of Long-term borrowings at December 31, 2007, excluding borrowings of consolidated investments, are as follows:

(in millions)	Total	*2008*	*2009*	*2010*	*2011*	*2012*	*Thereafter*
AIG:							
Notes and bonds payable	$ 14,588	$ 1,591	$ 1,441	$ 1,349	$ 450	$ 27	$ 9,730
Junior subordinated debt	5,809	—	—	—	—	—	5,809
Loans and mortgages payable	729	627	—	—	—	—	102
MIP matched notes and bonds payable	14,267	200	1,218	2,309	3,188	2,039	5,313
Series AIGFP matched notes and bonds payable	874	65	77	32	25	56	619
Total AIG	36,267	2,483	2,736	3,690	3,663	2,122	21,573
AIGFP:							
GIAs	19,908	6,370	1,831	1,127	581	660	9,339
Notes and bonds payable	36,676	23,670	4,522	431	403	3,885	3,765
Loans and mortgages payable	1,384	—	—	—	—	160	1,224
Hybrid financial instrument liabilities[(a)]	7,479	1,581	425	1,739	693	332	2,709
Total AIGFP	65,447	31,621	6,778	3,297	1,677	5,037	17,037
AIGLH notes and bonds payable	797	—	—	499	—	—	298
Liabilities connected to trust preferred stock	1,435	—	—	—	—	—	1,435
ILFC[(b)]:							
Notes and bonds payable	22,111	4,065	2,978	3,808	4,021	3,531	3,708
Junior subordinated debt	999	—	—	—	—	—	999
Export credit facility[(c)]	2,542	522	470	356	266	237	691
Bank financings	1,084	25	471	103	160	325	—
Total ILFC	26,736	4,612	3,919	4,267	4,447	4,093	5,398
AGF[(b)]:							
Notes and bonds payable	22,369	4,085	4,108	2,200	2,902	2,073	7,001
Junior subordinated debt	349	—	—	—	—	—	349
Total AGF	22,718	4,085	4,108	2,200	2,902	2,073	7,350
AIGCFG Loans and mortgages payable[(b)]	1,839	1,000	542	225	11	7	54
Other subsidiaries[(b)]	775	90	—	—	—	—	685
Total	$156,014	$43,891	$18,083	$14,178	$12,700	$13,332	$53,830

(a) Represents structured notes issued by AIGFP that are accounted for at fair value.

(b) AIG does not guarantee these borrowings.

(c) Reflects future minimum payment for ILFC's borrowing under Export Credit Facilities.

11. Debt Outstanding

Continued

(a) Commercial Paper:

At December 31, 2007, the commercial paper issued and outstanding was as follows:

(dollars in millions)	Net Book Value	Unamortized Discount and Accrued Interest	Face Amount	Weighted Average Interest Rate	Weighted Average Maturity in Days
ILFC	$ 4,483	$16	$ 4,499	4.63%	28
AGF	3,607	10	3,617	4.85	25
AIG Funding	4,222	15	4,237	4.81	29
AIGCC — Taiwan[(a)]	151	—	151	2.81	42
AIGF — Thailand[(a)]	136	1	137	3.36	50
Total[(b)]	$12,599	$42	$12,641	—	—

(a) Issued in local currencies at prevailing local interest rates.

(b) Excludes $321 million of borrowings of consolidated investments and $194 million of extendible commercial notes.

At December 31, 2007, AIG did not guarantee the commercial paper of any of its subsidiaries other than AIG Funding.

(b) AIG Borrowings:

(i) Notes and bonds issued by AIG: AIG maintains a medium-term note program under its shelf registration statement. At December 31, 2007, approximately $7.3 billion principal amount of senior notes were outstanding under the medium-term note program, of which $3.2 billion was used for AIG's general corporate purposes, $873 million was used by AIGFP and $3.2 billion was used to fund the Matched Investment Program (MIP). The maturity dates of these notes range from 2008 to 2052. To the extent deemed appropriate, AIG may enter into swap transactions to manage its effective borrowing rates with respect to these notes.

AIG also maintains a Euro medium-term note program under which an aggregate nominal amount of up to $20.0 billion of senior notes may be outstanding at any one time. At December 31, 2007, the equivalent of $12.7 billion of notes were outstanding under the program, of which $9.8 billion were used to fund the MIP and the remainder was used for AIG's general corporate purposes. The aggregate amount outstanding includes a $1.1 billion loss resulting from foreign exchange translation into U.S. dollars, of which a $332 million loss relates to notes issued by AIG for general corporate purposes and a $726 million loss relates to notes issued to fund the MIP.

During 2007, AIG issued in Rule 144A offerings an aggregate of $3.0 billion principal amount of senior notes, of which $650 million was used to fund the MIP and $2.3 billion was used for AIG's general corporate purposes.

AIG maintains a shelf registration statement in Japan, providing for the issuance of up to Japanese Yen 300 billion principal amount of senior notes, of which the equivalent of $450 million was outstanding at December 31, 2007, and was used for AIG's general corporate purposes.

(ii) Junior subordinated debt: During 2007, AIG issued an aggregate of $5.6 billion of junior subordinated debentures in five series of securities. Substantially all of the proceeds from these sales, net of expenses, are being used to repurchase shares of AIG's common stock. In connection with each series of junior subordinated debentures, AIG entered into a Replacement Capital Covenant (RCC) for the benefit of the holders of AIG's 6.25 percent senior notes due 2036. The RCCs provide that AIG will not repay, redeem, or purchase the applicable series of junior subordinated debentures on or before a specified date, unless AIG has received qualifying proceeds from the sale of replacement capital securities.

(c) AIGFP Borrowings:

(i) Borrowings under Obligations of Guaranteed Investment Agreements: Borrowings under obligations of guaranteed investment agreements (GIAs), which are guaranteed by AIG, are recorded at the amount outstanding under each contract. Obligations may be called at various times prior to maturity at the option of the counterparty. Interest rates on these borrowings are primarily fixed, vary by maturity, and range up to 9.8 percent.

Funds received from GIA borrowings are invested in a diversified portfolio of securities and derivative transactions. At December 31, 2007, the fair value of securities pledged as collateral with respect to these obligations approximated $14.5 billion.

(ii) Notes and Bonds issued by AIGFP:

At December 31, 2007, AIGFP's notes and bonds outstanding, the proceeds of which are invested in a diversified portfolio of securities and derivative transactions, were as follows:

Range of Maturities *(dollars in millions)*	Currency	Range of Interest Rates	U.S. Dollar Carrying Value
2008 - 2054	U.S. dollar	0.26 - 9.00%	$ 29,490
2008 - 2049	Euro	1.25 - 6.53	8,819
2008 - 2012	United Kingdom pound	4.67 - 6.31	3,936
2008 - 2037	Japanese Yen	0.01 - 2.9	2,025
2008 - 2024	Swiss francs	0.25	512
2008	New Zealand dollar	8.35	386
2009 - 2017	Australian dollar	1.14 - 2.65	177
2008 - 2017	Other	4.39 - 4.95	194
Total			$ 45,539

AIGFP economically hedges its notes and bonds. AIG guarantees all of AIGFP's debt.

(iii) Hybrid financial instrument liabilities: AIGFP's notes and bonds include structured debt instruments whose payment terms are linked to one or more financial or other indices (such as an equity index or commodity index or another measure that is not considered to be clearly and closely related to the debt instrument). These notes contain embedded derivatives that otherwise

11. Debt Outstanding

Continued

would be required to be accounted for separately under FAS 133. Upon AIG's early adoption of FAS 155, AIGFP elected the fair value option for these notes. The notes that are accounted for using the fair value option are reported separately under hybrid financial instrument liabilities at fair value.

(d) AIGLH Borrowings: At December 31, 2007, AIGLH notes aggregating $797 million were outstanding with maturity dates ranging from 2010 to 2029 at interest rates from 6.625 percent to 7.50 percent. AIG guarantees the notes and bonds of AIGLH.

(e) Liabilities Connected to Trust Preferred Stock: AIGLH issued Junior Subordinated Debentures (liabilities) to certain trusts established by AIGLH, which represent the sole assets of the trusts. The trusts have no independent operations. The trusts issued mandatory redeemable preferred stock to investors. The interest terms and payment dates of the liabilities correspond to those of the preferred stock. AIGLH's obligations with respect to the liabilities and related agreements, when taken together, constitute a full and unconditional guarantee by AIGLH of payments due on the preferred securities. AIG guarantees the obligations of AIGLH with respect to these liabilities and related agreements. The liabilities are redeemable, under certain conditions, at the option of AIGLH on a proportionate basis.

At December 31, 2007, the preferred stock outstanding consisted of $300 million liquidation value of 8.5 percent preferred stock issued by American General Capital II in June 2000, $500 million liquidation value of 8.125 percent preferred stock issued by American General Institutional Capital B in March 1997, and $500 million liquidation value of 7.57 percent preferred stock issued by American General Institutional Capital A in December 1996.

(f) ILFC Borrowings:

(i) Notes and Bonds issued by ILFC: At December 31, 2007, notes aggregating $23.1 billion were outstanding, consisting of $10.8 billion of term notes, $11.3 billion of medium-term notes with maturities ranging from 2008 to 2014 and interest rates ranging from 2.75 percent to 5.75 percent and $1.0 billion of junior subordinated debt as discussed below. Notes aggregating $5.3 billion are at floating interest rates and the remainder are at fixed rates. To the extent deemed appropriate, ILFC may enter into swap transactions to manage its effective borrowing rates with respect to these notes.

As a well-known seasoned issuer, ILFC has filed an automatic shelf registration statement with the SEC allowing ILFC immediate access to the U.S. public debt markets. At December 31, 2007, $4.7 billion of debt securities had been issued under this registration statement and $5.9 billion had been issued under a prior registration statement. In addition, ILFC has a Euro medium term note program for $7.0 billion, under which $3.8 billion in notes were outstanding at December 31, 2007. Notes issued under the Euro medium-term note program are included in ILFC notes and bonds payable in the preceding table of borrowings. The cumulative foreign exchange adjustment loss for the foreign currency denominated debt was $969 million at December 31, 2007 and $733 million at December 31, 2006. ILFC has substantially eliminated the currency exposure arising from foreign currency denominated notes by economically hedging the portion of the note exposure not already offset by Euro-denominated operating lease payments.

(ii) Junior subordinated debt: In December 2005, ILFC issued two tranches of junior subordinated debt totaling $1.0 billion to underlie trust preferred securities issued by a trust sponsored by ILFC. Both tranches mature on December 21, 2065, but each tranche has a different call option. The $600 million tranche has a call date of December 21, 2010 and the $400 million tranche has a call date of December 21, 2015. The note with the 2010 call date has a fixed interest rate of 5.90 percent for the first five years. The note with the 2015 call date has a fixed interest rate of 6.25 percent for the first ten years. Both tranches have interest rate adjustments if the call option is not exercised. The new interest rate is a floating quarterly reset rate based on the initial credit spread plus the highest of (i) 3 month LIBOR, (ii) 10-year constant maturity treasury and (iii) 30-year constant maturity treasury.

(iii) Export credit facility: ILFC had a $4.3 billion Export Credit Facility (ECA) for use in connection with the purchase of approximately 75 aircraft delivered through 2001. This facility was guaranteed by various European Export Credit Agencies. The interest rate varies from 5.75 percent to 5.90 percent on these amortizing ten-year borrowings depending on the delivery date of the aircraft. At December 31, 2007, ILFC had $664 million outstanding under this facility. The debt is collateralized by a pledge of the shares of a subsidiary of ILFC, which holds title to the aircraft financed under the facility.

In May 2004, ILFC entered into a similarly structured ECA for up to a maximum of $2.6 billion for Airbus aircraft to be delivered through May 31, 2005. The facility was subsequently increased to $3.6 billion and extended to include aircraft to be delivered through May 31, 2008. The facility becomes available as the various European Export Credit Agencies provide their guarantees for aircraft based on a six-month forward-looking calendar, and the interest rate is determined through a bid process. At December 31, 2007, ILFC had $1.9 billion outstanding under this facility.

(iv) Bank Financings: From time to time, ILFC enters into various bank financings. At December 31, 2007, the total funded amount was $1.1 billion. The financings mature through 2012. AIG does not guarantee any of the debt obligations of ILFC.

(g) AGF Borrowings:

(i) Notes and bonds issued by AGF: At December 31, 2007, notes and bonds aggregating $22.4 billion were outstanding with maturity dates ranging from 2008 to 2031 at interest rates ranging from 1.94 percent to 8.45 percent. To the extent deemed appropriate, AGF may enter into swap transactions to manage its effective borrowing rates with respect to these notes.

As a well-known seasoned issuer, AGF has filed an automatic shelf registration statement with the SEC allowing AGF immediate access to the U.S. public debt markets.

AGF uses the proceeds from the issuance of notes and bonds for the funding of its finance receivables.

11. Debt Outstanding

Continued

(ii) Junior subordinated debt: In January 2007, AGF issued junior subordinated debentures in an aggregate principal amount of $350 million that mature in January 2067. The debentures underlie a series of trust preferred securities sold by a trust sponsored by AGF in a Rule 144A/Regulation S offering. AGF can redeem the debentures at par beginning in January 2017.

AIG does not guarantee any of the debt obligations of AGF.

(h) Other Notes, Bonds, Loans and Mortgages Payable at December 31, 2007, consisted of the following:

(in millions)	Uncollateralized Notes/Bonds/Loans Payable	Collateralized Loans and Mortgages Payable
AIGCFG	$1,839	$ —
AIG	729	—
Other subsidiaries	600	175
Total	$3,168	$175

(i) Interest Expense for All Indebtedness: Total interest expense for all indebtedness, net of capitalized interest, aggregated $9.69 billion in 2007, $6.95 billion in 2006 and $5.7 billion in 2005. Capitalized interest was $37 million in 2007, $59 million in 2006 and $64 million in 2005. Cash distributions on the preferred shareholders' equity in subsidiary companies of ILFC and liabilities connected to trust preferred stock of AIGLH subsidiaries are accounted for as interest expense in the consolidated statement of income. The cash distributions for ILFC were approximately $5 million for each of the years ended December 31, 2007, 2006 and 2005. The cash distributions for AIGLH subsidiaries were approximately $107 million, $107 million and $112 million for the years ended December 31, 2007, 2006 and 2005, respectively.

12. Commitments, Contingencies and Guarantees

In the normal course of business, various commitments and contingent liabilities are entered into by AIG and certain of its subsidiaries. In addition, AIG guarantees various obligations of certain subsidiaries.

(a) Litigation and Investigations

Litigation Arising from Operations. AIG and its subsidiaries, in common with the insurance and financial services industries in general, are subject to litigation, including claims for punitive damages, in the normal course of their business. In AIG's insurance operations, litigation arising from claims settlement activities is generally considered in the establishment of AIG's reserve for losses and loss expenses. However, the potential for increasing jury awards and settlements makes it difficult to assess the ultimate outcome of such litigation.

Litigation Arising from Insurance Operations — Caremark. AIG and certain of its subsidiaries have been named defendants in two putative class actions in state court in Alabama that arise out of the 1999 settlement of class and derivative litigation involving Caremark Rx, Inc. (Caremark). The plaintiffs in the second-filed action have intervened in the first-filed action, and the second-filed action has been dismissed. An excess policy issued by a subsidiary of AIG with respect to the 1999 litigation was expressly stated to be without limit of liability. In the current actions, plaintiffs allege that the judge approving the 1999 settlement was misled as to the extent of available insurance coverage and would not have approved the settlement had he known of the existence and/or unlimited nature of the excess policy. They further allege that AIG, its subsidiaries, and Caremark are liable for fraud and suppression for misrepresenting and/or concealing the nature and extent of coverage. In addition, the intervenor-plaintiffs allege that various lawyers and law firms who represented parties in the underlying class and derivative litigation (the ''Lawyer Defendants'') are also liable for fraud and suppression, misrepresentation, and breach of fiduciary duty. The complaints filed by the plaintiffs and the intervenor-plaintiffs request compensatory damages for the 1999 class in the amount of $3.2 billion, plus punitive damages. AIG and its subsidiaries deny the allegations of fraud and suppression and have asserted that information concerning the excess policy was publicly disclosed months prior to the approval of the settlement. AIG and its subsidiaries further assert that the current claims are barred by the statute of limitations and that plaintiffs' assertions that the statute was tolled cannot stand against the public disclosure of the excess coverage. The plaintiffs and intervenor-plaintiffs, in turn, have asserted that the disclosure was insufficient to inform them of the nature of the coverage and did not start the running of the statute of limitations. On November 26, 2007, the trial court issued an order that dismissed the intervenors' complaint against the Lawyer Defendants and entered a final judgment in favor of the Lawyer Defendants. The intervenors are appealing the dismissal of the Lawyer Defendants and have requested a stay of all trial court proceedings pending the appeal. If the motion to stay is granted, no further proceedings at the trial court level will occur until the appeal is resolved. If the motion to stay is denied, the next step will be to proceed with class discovery so that the trial court can determine, under standards mandated by the Alabama Supreme Court, whether the action should proceed as a class action. AIG cannot reasonably estimate either the likelihood of its prevailing in these actions or the potential damages in the event liability is determined.

Litigation Arising from Insurance Operations — Gunderson. A subsidiary of AIG has been named as a defendant in a putative class action lawsuit in the 14th Judicial District Court for the State of Louisiana. The *Gunderson* complaint alleges failure to comply with certain provisions of the Louisiana Any Willing Provider Act (the Act) relating to discounts taken by defendants on bills submitted by Louisiana medical providers and hospitals that provided treatment or services to workers compensation claimants and seeks monetary penalties and injunctive relief. On July 20, 2006, the court denied defendants' motion for summary judgment and granted plaintiffs' partial motion for summary judgment, holding that the AIG subsidiary was a ''group purchaser'' and, therefore, potentially subject to liability under the

12. Commitments, Contingencies and Guarantees

Continued

Act. On November 28, 2006, the court issued an order certifying a class of providers and hospitals. In an unrelated action also arising under the Act, a Louisiana appellate court ruled that the district court lacked jurisdiction to adjudicate the claims at issue. In response, defendants in *Gunderson* filed an exception for lack of subject matter jurisdiction. On January 19, 2007, the court denied the motion, holding that it has jurisdiction over the putative class claims. The AIG subsidiary has appealed the class certification and jurisdictional rulings. While the appeal was pending, the AIG subsidiary settled the lawsuit. On January 25, 2008, plaintiffs and the AIG subsidiary agreed to resolve the lawsuit on a class-wide basis for approximately $29 million. The court has preliminarily approved the settlement and will hold a final approval hearing on May 29, 2008. In the event that the settlement is not finally approved, AIG believes that it has meritorious defenses to plaintiffs' claims and expects that the ultimate resolution of this matter will not have a material adverse effect on AIG's consolidated financial condition or results of operations for any period.

2006 Regulatory Settlements. In February 2006, AIG reached a resolution of claims and matters under investigation with the United States Department of Justice (DOJ), the Securities and Exchange Commission (SEC), the Office of the New York Attorney General (NYAG) and the New York State Department of Insurance (DOI). AIG recorded an after-tax charge of $1.15 billion relating to these settlements in the fourth quarter of 2005.

The settlements resolved investigations conducted by the SEC, NYAG and DOI in connection with the accounting, financial reporting and insurance brokerage practices of AIG and its subsidiaries, as well as claims relating to the underpayment of certain workers compensation premium taxes and other assessments. These settlements did not, however, resolve investigations by regulators from other states into insurance brokerage practices related to contingent commissions and other broker-related conduct, such as alleged bid rigging. Nor did the settlements resolve any obligations that AIG may have to state guarantee funds in connection with any of these matters.

As a result of these settlements, AIG made payments or placed amounts in escrow in 2006 totaling approximately $1.64 billion, $225 million of which represented fines and penalties. Amounts held in escrow totaling $347 million, including interest thereon, are included in other assets at December 31, 2007. At that date, approximately $330 million of the funds were escrowed for settlement of claims resulting from the underpayment by AIG of its residual market assessments for workers compensation. On May 24, 2007, The National Workers Compensation Reinsurance Pool, on behalf of its participant members, filed a lawsuit against AIG with respect to the underpayment of such assessments. On August 6, 2007, the court denied AIG's motion seeking to dismiss or stay the complaint based on *Colorado River* abstention or *forum non conveniens*, or in the alternative, to transfer to the Southern District of New York. On December 26, 2007, the court denied AIG's motion to dismiss the complaint. AIG filed its answer on January 22, 2008. On February 5, 2008, following agreement of the parties, the court entered an order staying all proceedings through March 3, 2008. In addition, a similar lawsuit filed by the Minnesota Workers Compensation Reinsurance Association and the Minnesota Workers Compensation Insurers Association is pending. On August 6, 2007, AIG moved to dismiss the complaint and that motion is *sub judice*. A purported class action was filed in South Carolina Federal Court on January 25, 2008 against AIG and certain of its subsidiaries, on behalf of a class of employers that obtained workers compensation insurance from AIG companies and allegedly paid inflated premiums as a result of AIG's alleged underreporting of workers compensation premiums. AIG cannot currently estimate whether the amount ultimately required to settle these claims will exceed the funds escrowed or otherwise accrued for this purpose. AIG has settled litigation that was filed by the Minnesota Attorney General with respect to claims by the Minnesota Department of Revenue and the Minnesota Special Compensation Fund.

The National Association of Insurance Commissioners has formed a Market Analysis Working Group directed by the State of Indiana, which has commenced its own investigation into the underreporting of workers compensation premium. In early 2008, AIG was informed that the Market Analysis Working Group had been disbanded in favor of a multi-state targeted market conduct exam focusing on worker's compensation insurance.

The remaining escrowed funds, which amounted to $17 million at December 31, 2007, are set aside for settlements for certain specified AIG policyholders. As of February 20, 2008, eligible policyholders entitled to receive approximately $359 million (or 95 percent) of the excess casualty fund had opted to receive settlement payments in exchange for releasing AIG and its subsidiaries from liability relating to certain insurance brokerage practices. Amounts remaining in the excess casualty fund may be used by AIG to settle claims from other policyholders relating to such practices through February 29, 2008 (originally set for January 31, 2008 and later extended), after which they will be distributed pro rata to participating policyholders.

In addition to the escrowed funds, $800 million was deposited into a fund under the supervision of the SEC as part of the settlements to be available to resolve claims asserted against AIG by investors, including the shareholder lawsuits described herein.

Also, as part of the settlements, AIG agreed to retain, for a period of three years, an independent consultant to conduct a review that will include, among other things, the adequacy of AIG's internal control over financial reporting, the policies, procedures and effectiveness of AIG's regulatory, compliance and legal functions and the remediation plan that AIG has implemented as a result of its own internal review.

Other than as described above, at the current time, AIG cannot predict the outcome of the matters described above, or estimate any potential additional costs related to these matters.

Private Litigation

Securities Actions. Beginning in October 2004, a number of putative securities fraud class action suits were filed against AIG and consolidated as *In re American International Group, Inc.*

12. Commitments, Contingencies and Guarantees

Continued

Securities Litigation. Subsequently, a separate, though similar, securities fraud action was also brought against AIG by certain Florida pension funds. The lead plaintiff in the class action is a group of public retirement systems and pension funds benefiting Ohio state employees, suing on behalf of themselves and all purchasers of AIG's publicly traded securities between October 28, 1999 and April 1, 2005. The named defendants are AIG and a number of present and former AIG officers and directors, as well as Starr, SICO, General Reinsurance Corporation, and PricewaterhouseCoopers LLP (PwC), among others. The lead plaintiff alleges, among other things, that AIG: (1) concealed that it engaged in anti-competitive conduct through alleged payment of contingent commissions to brokers and participation in illegal bid-rigging; (2) concealed that it used ''income smoothing'' products and other techniques to inflate its earnings; (3) concealed that it marketed and sold ''income smoothing'' insurance products to other companies; and (4) misled investors about the scope of government investigations. In addition, the lead plaintiff alleges that AIG's former Chief Executive Officer manipulated AIG's stock price. The lead plaintiff asserts claims for violations of Sections 11 and 15 of the Securities Act of 1933, Section 10(b) of the Exchange Act, and Rule 10b-5 promulgated thereunder, Section 20(a) of the Exchange Act, and Section 20A of the Exchange Act. In April 2006, the court denied the defendants' motions to dismiss the second amended class action complaint and the Florida complaint. In December 2006, a third amended class action complaint was filed, which does not differ substantially from the prior complaint. Fact and class discovery is currently ongoing. On February 20, 2008, the lead plaintiff filed a motion for class certification.

ERISA Action. Between November 30, 2004 and July 1, 2005, several Employee Retirement Income Security Act of 1974 (ERISA) actions were filed on behalf of purported class of participants and beneficiaries of three pension plans sponsored by AIG or its subsidiaries. A consolidated complaint filed on September 26, 2005 alleges a class period between September 30, 2000 and May 31, 2005 and names as defendants AIG, the members of AIG's Retirement Board and the Administrative Boards of the plans at issue, and four present or former members of AIG's Board of Directors. The factual allegations in the complaint are essentially identical to those in the securities actions described above. The parties have reached an agreement in principle to settle this matter for an amount within AIG's insurance coverage limits.

Securities Action — Oregon State Court. On February 27, 2008, The State of Oregon, by and through the Oregon State Treasurer, and the Oregon Public Employee Retirement Board, on behalf of the Oregon Public Employee Retirement Fund, filed a lawsuit against American International Group, Inc. for damages arising out of plaintiffs' purchase of AIG common stock at prices that allegedly were inflated. Plaintiffs allege, among other things, that AIG: (1) made false and misleading statements concerning its accounting for a $500 million transaction with General Re; (2) concealed that it marketed and misrepresented its control over off-shore entities in order to improve financial results; (3) improperly accounted for underwriting losses as investment losses in connection with transactions involving CAPCO Reinsurance Company, Ltd. and Union Excess; (4) misled investors about the scope of government investigations; and (5) engaged in market manipulation through its then Chairman and CEO Maurice R. Greenburg. The complaint asserts claims for violations of Oregon Securities Law, and seeks compensatory damages in an amount in excess of $15 million, and prejudgment interest and costs and fees.

Derivative Actions — Southern District of New York. On November 20, 2007, two purported shareholder derivative actions were filed in the Southern District of New York naming as defendants the current directors of AIG and certain senior officers of AIG and its subsidiaries. Plaintiffs assert claims for breach of fiduciary duty, waste of corporate assets and unjust enrichment, as well as violations of Section 10(b) of the Exchange Act and Rule 10b-5 promulgated thereunder, and Section 20(a) of the Exchange Act, among other things, in connection with AIG's public disclosures regarding its exposure to what the lawsuits describe as the subprime market crisis. The actions were consolidated as *In re American International Group, Inc. 2007 Derivative Litigation*. On February 15, 2008, plaintiffs filed a consolidated amended complaint alleging the same causes of action. AIG may become subject to litigation with respect to these or similar issues.

Between October 25, 2004 and July 14, 2005, seven separate derivative actions were filed in the Southern District of New York, five of which were consolidated into a single action. The New York derivative complaint contains nearly the same types of allegations made in the securities fraud and ERISA actions described above. The named defendants include current and former officers and directors of AIG, as well as Marsh & McLennan Companies, Inc. (Marsh), SICO, Starr, ACE Limited and subsidiaries (ACE), General Reinsurance Corporation, PwC, and certain employees or officers of these entity defendants. Plaintiffs assert claims for breach of fiduciary duty, gross mismanagement, waste of corporate assets, unjust enrichment, insider selling, auditor breach of contract, auditor professional negligence and disgorgement from AIG's former Chief Executive Officer and Chief Financial Officer of incentive-based compensation and AIG share proceeds under Section 304 of the Sarbanes-Oxley Act, among others. Plaintiffs seek, among other things, compensatory damages, corporate governance reforms, and a voiding of the election of certain AIG directors. AIG's Board of Directors has appointed a special committee of independent directors (special committee) to review the matters asserted in the operative consolidated derivative complaint. The court has entered an order staying the derivative case in the Southern District of New York pending resolution of the consolidated derivative action in the Delaware Chancery Court (discussed below). The court also has entered an order that termination of certain named defendants from the Delaware derivative action applies to the New York derivative action without further order of the court. On October 17, 2007, plaintiffs and those AIG officer and director defendants against whom the shareholder plaintiffs in the Delaware action are no longer

12. Commitments, Contingencies and Guarantees

Continued

pursuing claims filed a stipulation providing for all claims in the New York action against such defendants to be dismissed with prejudice. Former directors and officers Maurice R. Greenberg and Howard I. Smith have asked the court to refrain from so ordering this stipulation.

Derivative Actions — Delaware Chancery Court. From October 2004 to April 2005, AIG shareholders filed five derivative complaints in the Delaware Chancery Court. All of these derivative lawsuits were consolidated into a single action as *In re American International Group, Inc. Consolidated Derivative Litigation*. The amended consolidated complaint named 43 defendants (not including nominal defendant AIG) who, like the New York consolidated derivative litigation, were current and former officers and directors of AIG, as well as other entities and certain of their current and former employees and directors. The factual allegations, legal claims and relief sought in the Delaware action are similar to those alleged in the New York derivative actions, except that shareholder plaintiffs in the Delaware derivative action assert claims only under state law. Earlier in 2007, the Court approved an agreement that AIG be realigned as plaintiff, and, on June 13, 2007, acting on the direction of the special committee, AIG filed an amended complaint against former directors and officers Maurice R. Greenberg and Howard I. Smith, alleging breach of fiduciary duty and indemnification. Also on June 13, 2007, the special committee filed a motion to terminate the litigation as to certain defendants, while taking no action as to others. Defendants Greenberg and Smith filed answers to AIG's complaint and brought third-party complaints against certain current and former AIG directors and officers, PwC and Regulatory Insurance Services, Inc. On September 28, 2007, AIG and the shareholder plaintiffs filed a combined amended complaint in which AIG continued to assert claims against defendants Greenberg and Smith and took no position as to the claims asserted by the shareholder plaintiffs in the remainder of the combined amended complaint. In that pleading, the shareholder plaintiffs are no longer pursuing claims against certain AIG officers and directors. In November 2007, the shareholder plaintiffs moved to sever their claims to a separate action. AIG joined the motion to the extent that, among other things, the claims against defendants Greenberg and Smith would remain in prosecution in the pending action. In addition, a number of parties, including AIG, filed motions to stay discovery. On February 12, 2008, the court granted AIG's motion to stay discovery pending the resolution of claims against AIG in the New York consolidated securities action. The court also denied plaintiff's motion to sever and directed the parties to coordinate a briefing schedule for the motions to dismiss.

A separate derivative lawsuit was filed in the Delaware Chancery Court against twenty directors and executives of AIG as well as against AIG as a nominal defendant that alleges, among other things, that the directors of AIG breached the fiduciary duties of loyalty and care by approving the payment of commissions to Starr and of rental and service fees to SICO and the executives breached their duty of loyalty by causing AIG to enter into contracts with Starr and SICO and their fiduciary duties by usurping AIG's corporate opportunity. The complaint further alleges that the Starr agencies did not provide any services that AIG was not capable of providing itself, and that the diversion of commissions to these entities was solely for the benefit of Starr's owners. The complaint also alleged that the service fees and rental payments made to SICO and its subsidiaries were improper. Under the terms of a stipulation approved by the Court on February 16, 2006, the claims against the outside independent directors were dismissed with prejudice, while the claims against the other directors were dismissed without prejudice. On October 31, 2005, Defendants Greenberg, Matthews and Smith, SICO and Starr filed motions to dismiss the amended complaint. In an opinion dated June 21, 2006, the Court denied defendants' motion to dismiss, except with respect to plaintiff's challenge to payments made to Starr before January 1, 2000. On July 21, 2006, plaintiff filed its second amended complaint, which alleges that, between January 1, 2000 and May 31, 2005, individual defendants breached their duty of loyalty by causing AIG to enter into contracts with Starr and SICO and breached their fiduciary duties by usurping AIG's corporate opportunity. Starr is charged with aiding and abetting breaches of fiduciary duty and unjust enrichment for its acceptance of the fees. SICO is no longer named as a defendant. On April 20, 2007, the individual defendants and Starr filed a motion seeking leave of the Court to assert a cross-claim against AIG and a third-party complaint against PwC and the directors previously dismissed from the action, as well as certain other AIG officers and employees. On June 13, 2007, the Court denied the individual defendants' motion to file a third-party complaint, but granted the proposed cross-claim against AIG. On June 27, 2007, Starr filed its cross-claim against AIG, alleging one count that includes contribution, unjust enrichment and setoff. AIG has filed an answer and moved to dismiss Starr's cross-claim to the extent it seeks affirmative relief, as opposed to a reduction in the judgment amount. On November 15, 2007, the court granted AIG's motion to dismiss the cross-claim by Starr to the extent that it sought affirmative relief from AIG. On November 21, 2007, shareholder plaintiff submitted a motion for leave to file its Third Amended Complaint in order to add Thomas Tizzio as a defendant. On February 14, 2008, the court granted this motion and allowed Mr. Tizzio until April 2008 to take additional discovery. Document discovery and depositions are otherwise complete.

Policyholder Actions. After the NYAG filed its complaint against insurance broker Marsh, policyholders brought multiple federal antitrust and Racketeer Influenced and Corrupt Organizations Act (RICO) class actions in jurisdictions across the nation against insurers and brokers, including AIG and a number of its subsidiaries, alleging that the insurers and brokers engaged in a broad conspiracy to allocate customers, steer business, and rig bids. These actions, including 24 complaints filed in different federal courts naming AIG or an AIG subsidiary as a defendant, were consolidated by the judicial panel on multi-district litigation and transferred to the United States District Court for the District of New Jersey for coordinated pretrial proceedings. The consolidated actions have proceeded in that court in two parallel actions, *In re*

12. Commitments, Contingencies and Guarantees

Continued

Insurance Brokerage Antitrust Litigation (the *First Commercial Complaint*) and *In re Employee Benefit Insurance Brokerage Antitrust Litigation* (the *First Employee Benefits Complaint,* and, together with the *First Commercial Complaint,* the multi-district litigation).

The plaintiffs in the *First Commercial Complaint* are nineteen corporations, individuals and public entities that contracted with the broker defendants for the provision of insurance brokerage services for a variety of insurance needs. The broker defendants are alleged to have placed insurance coverage on the plaintiffs' behalf with a number of insurance companies named as defendants, including AIG subsidiaries. The *First Commercial Complaint* also named ten brokers and fourteen other insurers as defendants (two of which have since settled). The *First Commercial Complaint* alleges that defendants engaged in a widespread conspiracy to allocate customers through ''bid-rigging'' and ''steering'' practices. The *First Commercial Complaint* also alleges that the insurer defendants permitted brokers to place business with AIG subsidiaries through wholesale intermediaries affiliated with or owned by those same brokers rather than placing the business with AIG subsidiaries directly. Finally, the *First Commercial Complaint* alleges that the insurer defendants entered into agreements with broker defendants that tied insurance placements to reinsurance placements in order to provide additional compensation to each broker. Plaintiffs assert that the defendants violated the Sherman Antitrust Act, RICO, the antitrust laws of 48 states and the District of Columbia, and are liable under common law breach of fiduciary duty and unjust enrichment theories. Plaintiffs seek treble damages plus interest and attorneys' fees as a result of the alleged RICO and Sherman Antitrust Act violations.

The plaintiffs in the *First Employee Benefits Complaint* are nine individual employees and corporate and municipal employers alleging claims on behalf of two separate nationwide purported classes: an employee class and an employer class that acquired insurance products from the defendants from August 26, 1994 to the date of any class certification. The *First Employee Benefits Complaint* names AIG, as well as eleven brokers and five other insurers, as defendants. The activities alleged in the *First Employee Benefits Complaint,* with certain exceptions, track the allegations of contingent commissions, bid-rigging and tying made in the *First Commercial Complaint.*

On October 3, 2006, Judge Hochberg of the District of New Jersey reserved in part and denied in part motions filed by the insurer defendants and broker defendants to dismiss the multi-district litigation. The Court also ordered the plaintiffs in both actions to file supplemental statements of particularity to elaborate on the allegations in their complaints. Plaintiffs filed their supplemental statements on October 25, 2006, and the AIG defendants, along with other insurer and broker defendants in the two consolidated actions, filed renewed motions to dismiss on November 30, 2006. On February 16, 2007, the case was transferred to Judge Garrett E. Brown, Chief Judge of the District of New Jersey. On April 5, 2007, Chief Judge Brown granted the defendants' renewed motions to dismiss the *First Commercial Complaint* and *First Employee Benefits Complaint* with respect to the antitrust and RICO claims. The claims were dismissed without prejudice and the plaintiffs were given 30 days, later extended to 45 days, to file amended complaints. On April 11, 2007, the Court stayed all proceedings, including all discovery, that are part of the multi-district litigation until any renewed motions to dismiss the amended complaints are resolved.

A number of complaints making allegations similar to those in the *First Commercial Complaint* have been filed against AIG and other defendants in state and federal courts around the country. The defendants have thus far been successful in having the federal actions transferred to the District of New Jersey and consolidated into the multi-district litigation. The AIG defendants have also sought to have state court actions making similar allegations stayed pending resolution of the multi-district litigation proceeding. In one state court action pending in Florida, the trial court recently decided not to grant an additional stay, but instead to allow the case to proceed. Defendants filed their motions to dismiss, and on September 24, 2007, the court denied the motions with respect to the state antitrust, RICO, and common law claims and granted the motions with respect to both the Florida insurance bad faith claim against AIG (with prejudice) and the punitive damages claim (without prejudice). Discovery in this action is ongoing.

Plaintiffs filed amended complaints in both *In re Insurance Brokerage Antitrust Litigation* (the *Second Commercial Complaint*) and *In re Employee Benefit Insurance Brokerage Antitrust Litigation* (the *Second Employee Benefits Complaint*) along with revised particularized statements in both actions on May 22, 2007. The allegations in the *Second Commercial Complaint* and the *Second Employee Benefits Complaint* are substantially similar to the allegations in the *First Commercial Complaint and First Employee Benefits Complaint,* respectively. The complaints also attempt to add several new parties and delete others; the *Second Commercial Complaint* adds two new plaintiffs and twenty seven new defendants (including three new AIG defendants), and the *Second Employee Benefits Complaint* adds eight new plaintiffs and nine new defendants (including two new AIG defendants). The defendants filed motions to dismiss the amended complaints and to strike the newly added parties. The Court granted (without leave to amend) defendants' motions to dismiss the federal antitrust and RICO claims on August 31, 2007 and September 28, 2007, respectively. The Court declined to exercise supplemental jurisdiction over the state law claims in the *Second Commercial Complaint* and therefore dismissed it in its entirety. On January 14, 2008, the court granted defendants' motion for summary judgment on the ERISA claims in the Second Employee Benefits Complaint and subsequently dismissed the remaining state law claims without prejudice, thereby dismissing the Second Employee Benefits Complaint in its entirety. On February 12, 2008, plaintiffs filed a notice of appeal to the United States Court of Appeals for the Third Circuit with respect to the dismissal of the Second Employee Benefits Complaint. Plaintiffs previously appealed the dismissal of the Second Commercial Complaint to the United

12. Commitments, Contingencies and Guarantees

Continued

States Court of Appeals for the Third Circuit on October 10, 2007. Several similar actions that were consolidated before Chief Judge Brown are still pending in the District Court. Those actions are currently stayed pending a decision by the court on whether they will proceed during the appeal of the dismissal of the Second Commercial Complaint and the Second Employee Benefits Complaint.

On August 24, 2007, the Ohio Attorney General filed a complaint in the Ohio Court of Common Pleas against AIG and a number of its subsidiaries, as well as several other broker and insurer defendants, asserting violation of Ohio's antitrust laws. The complaint, which is similar to the *Second Commercial Complaint,* alleges that AIG and the other broker and insurer defendants conspired to allocate customers, divide markets, and restrain competition in commercial lines of casualty insurance sold through the broker defendant. The complaint seeks treble damages on behalf of Ohio public purchasers of commercial casualty insurance, disgorgement on behalf of both public and private purchasers of commercial casualty insurance, as well as a $500 per day penalty for each day of conspiratorial conduct. AIG, along with other co-defendants, moved to dismiss the complaint on November 16, 2007. Discovery is stayed in the case pending a ruling on the motion to dismiss or until May 15, 2008, whichever occurs first.

SICO. In July, 2005, SICO filed a complaint against AIG in the Southern District of New York, claiming that AIG had refused to provide SICO access to certain artwork and asked the court to order AIG immediately to release the property to SICO. AIG filed an answer denying SICO's allegations and setting forth defenses to SICO's claims. In addition, AIG filed counterclaims asserting breach of contract, unjust enrichment, conversion, breach of fiduciary duty, a constructive trust and declaratory judgment, relating to SICO's breach of its commitment to use its AIG shares only for the benefit of AIG and AIG employees. Fact and expert discovery has been concluded and SICO's motion for summary judgment is pending.

Regulatory Investigations. Regulators from several states have commenced investigations into insurance brokerage practices related to contingent commissions and other industry wide practices as well as other broker-related conduct, such as alleged bid-rigging. In addition, various federal, state and foreign regulatory and governmental agencies are reviewing certain transactions and practices of AIG and its subsidiaries in connection with industry wide and other inquiries. AIG has cooperated, and will continue to cooperate, in producing documents and other information in response to subpoenas and other requests. On January 29, 2008, AIG reached settlement agreements with nine states and the District of Columbia. The settlement agreements call for AIG to pay a total of $12.5 million to be allocated among the ten jurisdictions and also require AIG to continue to maintain certain producer compensation disclosure and ongoing compliance initiatives. AIG will also continue to cooperate with these states in their ongoing investigations. AIG has not admitted liability under the settlement agreements and continues to deny the allegations. Nevertheless, AIG agreed to settle in order to avoid the expense and uncertainty of protracted litigation. The settlement agreements, which remain subject to court approvals, were reached with the Attorneys General of the States of Florida, Hawaii, Maryland, Michigan, Oregon, Texas and West Virginia, the Commonwealths of Massachusetts and Pennsylvania, and the District of Columbia, the Florida Department of Financial Services, and the Florida Office of Insurance Regulation. The agreement with the Texas Attorney General also settles allegations of anticompetitive conduct relating to AIG's relationship with Allied World Assurance Company and includes an additional settlement payment of $500,000 related thereto.

Wells Notices. AIG understands that some of its employees have received Wells notices in connection with previously disclosed SEC investigations of certain of AIG's transactions or accounting practices. Under SEC procedures, a Wells notice is an indication that the SEC staff has made a preliminary decision to recommend enforcement action that provides recipients with an opportunity to respond to the SEC staff before a formal recommendation is finalized. It is possible that additional current and former employees could receive similar notices in the future as the regulatory investigations proceed.

Effect on AIG

In the opinion of AIG management, AIG's ultimate liability for the unresolved litigation and investigation matters referred to above is not likely to have a material adverse effect on AIG's consolidated financial condition, although it is possible that the effect would be material to AIG's consolidated results of operations for an individual reporting period.

(b) Commitments

Flight Equipment

At December 31, 2007, ILFC had committed to purchase 234 new aircraft deliverable from 2008 through 2017 at an estimated aggregate purchase price of $20.1 billion. ILFC will be required to find customers for any aircraft acquired, and it must arrange financing for portions of the purchase price of such equipment.

Minimum future rental income on noncancelable operating leases of flight equipment which have been delivered at December 31, 2007 was as follows:

(in millions)	
2008	$ 4,142
2009	3,783
2010	3,274
2011	2,726
2012	2,075
Remaining years after 2012	4,921
Total	$20,921

Flight equipment is leased, under operating leases, with remaining terms ranging from 1 to 12 years.

12. Commitments, Contingencies and Guarantees

Continued

Lease Commitments

AIG and its subsidiaries occupy leased space in many locations under various long-term leases and have entered into various leases covering the long-term use of data processing equipment.

At December 31, 2007, the future minimum lease payments under operating leases were as follows:

(in millions)	
2008	$ 747
2009	581
2010	460
2011	371
2012	322
Remaining years after 2012	1,945
Total	$4,426

Rent expense approximated $771 million, $657 million, and $597 million for the years ended December 31, 2007, 2006, and 2005, respectively.

Other Commitments

In the normal course of business, AIG enters into commitments to invest in limited partnerships, private equities, hedge funds and mutual funds and to purchase and develop real estate in the U.S. and abroad. These commitments totaled $9.1 billion at December 31, 2007.

On June 27, 2005, AIG entered into an agreement pursuant to which AIG agrees, subject to certain conditions, to make any payment that is not promptly paid with respect to the benefits accrued by certain employees of AIG and its subsidiaries under the SICO Plans (as discussed in Note 19 herein).

(c) Contingencies

Loss Reserves

Although AIG regularly reviews the adequacy of the established reserve for losses and loss expenses, there can be no assurance that AIG's ultimate loss reserves will not develop adversely and materially exceed AIG's current loss reserves. Estimation of ultimate net losses, loss expenses and loss reserves is a complex process for long-tail casualty lines of business, which include excess and umbrella liability, directors and officers liability (D&O), professional liability, medical malpractice, workers compensation, general liability, products liability and related classes, as well as for asbestos and environmental exposures. Generally, actual historical loss development factors are used to project future loss development. However, there can be no assurance that future loss development patterns will be the same as in the past. Moreover, any deviation in loss cost trends or in loss development factors might not be discernible for an extended period of time subsequent to the recording of the initial loss reserve estimates for any accident year. Thus, there is the potential for reserves with respect to a number of years to be significantly affected by changes in loss cost trends or loss development factors that were relied upon in setting the reserves. These changes in loss cost trends or loss development factors could be attributable to changes in inflation, in labor and material costs or in the judicial environment, or in other social or economic phenomena affecting claims.

Synthetic Fuel Tax Credits. AIG generated income tax credits as a result of investing in synthetic fuel production. Tax credits generated from the production and sale of synthetic fuel under the Internal Revenue Code were subject to an annual phase-out provision based on the average wellhead price of domestic crude oil. The price range within which the tax credits are phased-out was originally established in 1980 and is adjusted annually for inflation. Depending on the price of domestic crude oil for a particular year, all or a portion of the tax credits generated in that year might be eliminated. AIG evaluated the production levels of its synthetic fuel production facilities in light of the risk of phase-out of the associated tax credits. As a result of fluctuating domestic crude oil prices, AIG evaluated and adjusted production levels when appropriate in light of this risk. Under current legislation, the opportunity to generate additional tax credits from the production and sale of synthetic fuel expired on December 31, 2007.

Lease Transactions. In June and August, 2007, field agents at the Internal Revenue Service (IRS) issued Notices of Proposed Adjustment (NOPAs) relating to a series of lease transactions by an AIG subsidiary. In the NOPAs, the field agents asserted that the leasing transactions were ''lease-in lease-out'' transactions described in Revenue Ruling 2002-69 and proposed adjustments to taxable income of approximately $203 million in the aggregate for the years 1998, 1999, 2001 and 2002.

(d) Guarantees

AIG and certain of its subsidiaries become parties to derivative financial instruments with market risk resulting from both dealer and end-user activities and to reduce currency, interest rate, equity and commodity exposures. These instruments are carried at their estimated fair values in the consolidated balance sheet. The vast majority of AIG's derivative activity is transacted by AIGFP. See also Note 8 herein.

AIG has issued unconditional guarantees with respect to the prompt payment, when due, of all present and future payment obligations and liabilities of AIGFP arising from transactions entered into by AIGFP.

SAI Deferred Compensation Holdings, Inc., a wholly owned subsidiary of AIG, has established a deferred compensation plan for registered representatives of certain AIG subsidiaries, pursuant to which participants have the opportunity to invest deferred commissions and fees on a notional basis. The value of the deferred compensation fluctuates with the value of the deferred investment alternatives chosen. AIG has provided a full and unconditional guarantee of the obligations of SAI Deferred Compensation Holdings, Inc. to pay the deferred compensation under the plan.

13. Preferred Shareholders' Equity in Subsidiary Companies

At December 31, 2007, preferred shareholders' equity in subsidiary companies represents preferred stocks issued by ILFC, a wholly owned subsidiary of AIG.

At December 31, 2007, the preferred stock consists of 1,000 shares of market auction preferred stock (MAPS) in two series (Series A and B) of 500 shares each. Each of the MAPS shares has a liquidation value of $100,000 per share and is not convertible. The dividend rate, other than the initial rate, for each dividend period for each series is reset approximately every seven weeks (49 days) on the basis of orders placed in an auction. During 2006, ILFC extended each of the MAPS dividend periods for three years. At December 31, 2007, the dividend rate for Series A MAPS was 4.70 percent and the dividend rate for Series B MAPS was 5.59 percent.

14. Shareholders' Equity and Earnings Per Share

Shareholders' Equity

AIG parent depends on its subsidiaries for cash flow in the form of loans, advances, reimbursement for shared expenses, and dividends. AIG's insurance subsidiaries are subject to regulatory restrictions on the amount of dividends that can be remitted to AIG parent. These restrictions vary by jurisdiction. For example, unless permitted by the New York Superintendent of Insurance, general insurance companies domiciled in New York may not pay dividends to shareholders that, in any twelve-month period, exceed the lesser of ten percent of such company's statutory policyholders' surplus or 100 percent of its ''adjusted net investment income,'' as defined. Generally, less severe restrictions applicable to both general and life insurance companies exist in most of the other states in which AIG's insurance subsidiaries are domiciled. Certain foreign jurisdictions have restrictions that could delay or limit the remittance of dividends. There are also various local restrictions limiting cash loans and advances to AIG by its subsidiaries. Largely as a result of these restrictions, approximately 81 percent of the aggregate equity of AIG's consolidated subsidiaries was restricted from immediate transfer to AIG parent at December 31, 2007.

Dividends declared per common share were $0.77, $0.65, and $0.63 in 2007, 2006, and 2005, respectively.

During 2007 and 2005, AIG repurchased 76 million and 2 million shares of its common stock, respectively, at a total cost of $5.1 billion and $165 million, respectively. The average price paid per share for repurchased shares was $66.84 and $66.46 in 2007 and 2005, respectively. During 2006, AIG did not purchase any shares of its common stock under its existing share repurchase authorization.

At December 31, 2007, there were 6,000,000 shares of AIG's $5 par value serial preferred stock authorized, issuable in series, none of which were outstanding.

14. Shareholders' Equity and Earnings Per Share

Continued

Earnings Per Share

Basic earnings per share is based on the weighted average number of common shares outstanding, adjusted to reflect all stock dividends and stock splits. Diluted earnings per share is based on those shares used in basic earnings per share plus shares that would have been outstanding assuming issuance of common shares for all dilutive potential common shares outstanding, adjusted to reflect all stock dividends and stock splits.

The computation of earnings per share for the years ended December 31, 2007, 2006 and 2005 was as follows:

Years Ended December 31, *(in millions, except per share data)*	**2007**	2006	2005
Numerator for earnings per share:			
Income before cumulative effect of an accounting change	**$ 6,200**	$14,014	$10,477
Cumulative effect of an accounting change, net of tax	**—**	34	—
Net income applicable to common stock for basic EPS	**6,200**	14,048	10,477
Interest on contingently convertible bonds, net of tax	**—**	10	11
Net income applicable to common stock for diluted EPS	**6,200**	14,058	10,488
Cumulative effect of an accounting change, net of tax	**—**	(34)	—
Income before cumulative effect of an accounting change applicable to common stock for diluted EPS	**$ 6,200**	$14,024	$10,488
Denominator for earnings per share:			
Weighted average shares outstanding used in the computation of EPS:			
Common stock issued	**2,751**	2,751	2,751
Common stock in treasury	**(179)**	(153)	(155)
Deferred shares	**13**	10	1
Weighted average shares outstanding — basic	**2,585**	2,608	2,597
Incremental shares from potential common stock:			
Weighted average number of shares arising from outstanding employee stock plans (treasury stock method)*	**13**	7	21
Contingently convertible bonds	**—**	8	9
Weighted average shares outstanding — diluted*	**2,598**	2,623	2,627
Earnings per share:			
Basic:			
Income before cumulative effect of an accounting change	**$ 2.40**	$ 5.38	$ 4.03
Cumulative effect of an accounting change, net of tax	**—**	0.01	—
Net income	**$ 2.40**	$ 5.39	$ 4.03
Diluted:			
Income before cumulative effect of an accounting change	**$ 2.39**	$ 5.35	$ 3.99
Cumulative effect of an accounting change, net of tax	**—**	0.01	—
Net income	**$ 2.39**	$ 5.36	$ 3.99

* *Certain shares arising from employee stock plans were not included in the computation of diluted earnings per share if the exercise price of the options exceeded the average market price and were antidilutive. The number of shares excluded were 8 million, 13 million and 19 million for the years ended December 31, 2007, 2006 and 2005, respectively.*

15. Statutory Financial Data

Statutory surplus and net income for General Insurance and Life Insurance & Retirement Services operations in accordance with statutory accounting practices were as follows:

Years Ended December 31, *(in millions)*	2007	2006	2005
Statutory surplus[(a)]:			
General Insurance	**$37,705**	$32,665	$24,508
Life Insurance & Retirement Services	**33,212**	35,058	30,739
Statutory net income[(a)(b)]:			
General Insurance[(c)]	**8,018**	8,010	1,713
Life Insurance & Retirement Services[(a)]	**4,465**	5,088	4,762

(a) Statutory surplus and net income with respect to foreign operations are estimated at November 30. The basis of presentation for branches of AIA is the Hong Kong statutory filing basis. The basis of presentation for branches of ALICO is the U.S. statutory filing basis. AIG Star Life, AIG Edison Life, Nan Shan and Philamlife are estimated based on their respective local country filing basis.

(b) Includes realized capital gains and losses and taxes.

(c) Includes catastrophe losses, net of tax, of $177 million and $1.9 billion in 2007 and 2005, respectively.

AIG's insurance subsidiaries file financial statements prepared in accordance with statutory accounting practices prescribed or permitted by domestic and foreign insurance regulatory authorities. The differences between statutory financial statements and financial statements prepared in accordance with U.S. GAAP vary between domestic and foreign by jurisdiction. The principal differences are that statutory financial statements do not reflect DAC, some bond portfolios may be carried at amortized cost, assets and liabilities are presented net of reinsurance, policyholder liabilities are generally valued using more conservative assumptions and certain assets are non-admitted.

At December 31, 2007, 2006 and 2005, statutory capital of AIG's insurance subsidiaries exceeded minimum company action level requirements. In 2005, AIG nonetheless contributed an additional $750 million of capital into American Home Assurance Company (American Home) effective September 30, 2005 and contributed a further $2.25 billion of capital in February 2006 for a total of approximately $3 billion of capital into Domestic General Insurance subsidiaries effective December 31, 2005.

16. Fair Value of Financial Instruments

FAS 107, ''Disclosures about Fair Value of Financial Instruments'' (FAS 107), requires disclosure of fair value information about financial instruments for which it is practicable to estimate such fair value. FAS 107 excludes certain financial instruments, including those related to insurance contracts and lease contracts.

The fair value of a financial instrument is the amount that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. The degree of judgment used in measuring the fair value of financial instruments generally correlates with the level of pricing observability. Financial instruments with quoted prices in active markets generally have more pricing observability and less judgment is used in measuring fair value. Conversely, financial instruments traded in other than active markets or that do not have quoted prices have less observability and are measured at fair value using valuation models or other pricing techniques that require more judgment. Pricing observability is affected by a number of factors, including the type of financial instrument, whether the financial instrument is new to the market and not yet established, the characteristics specific to the transaction and general market conditions.

Fixed maturities, equity securities, securities available for sale, trading securities and securities sold under agreements to repurchase: AIG maximizes the use of observable inputs and minimizes the use of unobservable inputs when measuring fair value. AIG obtains market price data to value financial instruments whenever such information is available. Market price data generally is obtained from market exchanges or dealer quotations. The types of instruments valued based on market price data include G-7 government and agency securities, equities listed in active markets, and investments in publicly traded mutual funds with quoted market prices.

AIG estimates the fair value of fixed income instruments not traded in active markets by referring to traded securities with similar attributes and using a matrix pricing methodology. This methodology considers such factors as the issuer's industry, the security's rating and tenor, its coupon rate, its position in the capital structure of the issuer, and other relevant factors. The types of fixed income instruments not traded in active markets include non-G-7 government securities, municipal bonds, certain hybrid financial instruments, most investment-grade and high-yield corporate bonds, and most mortgage- and asset-backed products.

AIG initially estimates the fair value of equity instruments not traded in active markets by reference to the transaction price. This valuation is adjusted only when changes to inputs and assumptions are corroborated by evidence such as transactions in similar instruments, completed or pending third-party transactions in the underlying investment or comparable entities, subsequent rounds of financing, recapitalizations and other transactions across the capital structure, offerings in the equity capital markets, and changes in financial ratios or cash flows.

For equity and fixed income instruments that are not traded in active markets or that are subject to transfer restrictions, valuations are adjusted to reflect illiquidity and/or non-transferability, and such adjustments generally are based on available market evidence. In the absence of such evidence, management's best estimate is used.

Unrealized gain (loss) on swaps, options and forward transactions: Unrealized gain (loss) on swaps, options and forward transactions (derivative assets and liabilities) can be exchange-traded or traded over the counter (OTC). AIG generally values exchange-traded derivatives within portfolios using models that calibrate to market clearing levels and that eliminate timing

16. Fair Value of Financial Instruments

Continued

differences between the closing price of the exchange-traded derivatives and their underlying instruments.

OTC derivatives are valued using market transactions and other market evidence whenever possible, including market-based inputs to models, model calibration to market clearing transactions, broker or dealer quotations or alternative pricing sources with reasonable levels of price transparency. When models are used, the selection of a particular model to value an OTC derivative depends on the contractual terms of, and specific risks inherent in, the instrument as well as the availability of pricing information in the market. AIG generally uses similar models to value similar instruments. Valuation models require a variety of inputs, including contractual terms, market prices and rates, yield curves, credit curves, measures of volatility, prepayment rates and correlations of such inputs. For OTC derivatives that trade in liquid markets, such as generic forwards, swaps and options, model inputs can generally be verified and model selection does not involve significant management judgment.

Certain OTC derivatives trade in less liquid markets with limited pricing information, and the determination of fair value for these derivatives is inherently more difficult. When AIG does not have corroborating market evidence to support significant model inputs and cannot verify the model to market transactions, transaction price is initially used as the best estimate of fair value. Accordingly, when a pricing model is used to value such an instrument, the model is adjusted so that the model value at inception equals the transaction price. Subsequent to initial recognition, AIG updates valuation inputs when corroborated by evidence such as similar market transactions, third-party pricing services and/or broker or dealer quotations, or other empirical market data. When appropriate, valuations are adjusted for various factors such as liquidity, bid/offer spreads and credit considerations. Such adjustments are generally based on available market evidence. In the absence of such evidence, management's best estimate is used.

Mortgage and other loans receivable: When practical, the fair values of loans on real estate and collateral loans were estimated using discounted cash flow calculations based upon AIG's current incremental lending rates for similar type loans. The fair values of the policy loans were not calculated as AIG believes it would have to expend excessive costs for the benefits derived.

Finance receivables: Fair values were estimated using discounted cash flow calculations based upon the weighted average rates currently being offered for similar finance receivables.

Securities lending invested collateral and securities lending payable: Securities lending collateral are floating rate fixed maturity securities recorded at fair value. Fair values were based upon quoted market prices or internally developed models consistent with the methodology for other fixed maturity securities. The contract values of securities lending payable approximate fair value as these obligations are short-term in nature.

Spot commodities: Fair values were based on current market prices of reference spot futures contracts traded on exchanges.

Cash, short-term investments, trade receivables, trade payables, securities purchased (sold) under agreements to resell (repurchase), commercial paper and extendible commercial notes: The carrying values of these assets and liabilities approximate fair values because of the relatively short period of time between origination and expected realization.

Other invested assets: Consisting principally of hedge funds and limited partnerships. Fair values are determined based on the net asset values provided by the general partner or manager of each investment. AIG obtains the fair value of its investments in limited partnerships and hedge funds from information provided by the general partner or manager of these investments, the accounts of which generally are audited on an annual basis. The transaction price is used as the best estimate of fair value at inception.

Policyholders' contract deposits: Fair values were estimated using discounted cash flow calculations based upon interest rates currently being offered for similar contracts with maturities consistent with those remaining for the contracts being valued.

Securities and spot commodities sold but not yet purchased: The carrying amounts for the securities and spot commodities sold but not yet purchased approximate fair values. Fair values for securities and spot commodities sold short were based on current market prices.

Trust deposits and deposits due to banks and other depositors: To the extent certain amounts are not demand deposits or certificates of deposit which mature in more than one year, fair values were not calculated as AIG believes it would have to expend excessive costs for the benefits derived.

Commercial paper and extendible commercial notes: The carrying amount approximates fair value.

Long-term borrowings: When practical, the fair values of these obligations were estimated using discounted cash flow calculations based upon AIG's current incremental borrowing rates for similar types of borrowings with maturities consistent with those remaining for the debt being valued.

16. Fair Value of Financial Instruments

Continued

The carrying values and fair values of AIG's financial instruments at December 31, 2007 and 2006 were as follows:

	2007		2006	
(in millions)	Carrying Value[a]	Fair Value	Carrying Value[a]	Fair Value
Assets:				
Fixed maturities	**$428,935**	**$429,511**	$419,142	$419,859
Equity securities	**41,646**	**41,646**	30,650	30,650
Mortgage and other loans receivable	**33,727**	**34,123**	28,418	28,655
Securities available for sale	**40,305**	**40,305**	47,205	47,205
Trading securities	**4,197**	**4,197**	5,031	5,031
Spot commodities	**238**	**238**	220	220
Unrealized gain on swaps, options and forward transactions	**16,442**	**16,442**	19,252	19,252
Trade receivables	**6,467**	**6,467**	4,317	4,317
Securities purchased under agreements to resell	**20,950**	**20,950**	30,291	30,291
Finance receivables, net of allowance	**31,234**	**28,693**	29,573	26,712
Securities lending invested collateral	**75,662**	**75,662**	69,306	69,306
Other invested assets[b]	**57,134**	**57,979**	42,111	42,418
Short-term investments	**51,351**	**51,351**	27,483	27,483
Cash	**2,284**	**2,284**	1,590	1,590
Liabilities:				
Policyholders' contract deposits	**258,459**	**259,045**	248,264	243,570
Securities sold under agreements to repurchase	**8,331**	**9,048**	19,677	19,677
Trade payables	**10,568**	**10,568**	6,174	6,174
Securities and spot commodities sold but not yet purchased	**4,709**	**4,709**	4,076	4,076
Unrealized loss on swaps, options and forward transactions	**20,613**	**20,613**	11,401	11,401
Trust deposits and deposits due to banks and other depositors	**4,903**	**4,986**	5,249	5,261
Commercial paper and extendible commercial notes	**13,114**	**13,114**	13,363	13,363
Long-term borrowings	**162,935**	**165,064**	135,316	135,605
Securities lending payable	**81,965**	**81,965**	70,198	70,198

(a) The carrying value of all other financial instruments approximates fair value.
(b) Excludes aircraft asset investments held by non-Financial Services subsidiaries.

17. Share-based Employee Compensation Plans

During the year ended December 31, 2007, AIG employees had received compensation pursuant to awards under seven different share-based employee compensation plans: *(i)* AIG 1999 Stock Option Plan, as amended (1999 Plan); *(ii)* AIG 1996 Employee Stock Purchase Plan, as amended (1996 Plan); *(iii)* AIG 2002 Stock Incentive Plan, as amended (2002 Plan) under which AIG has issued time-vested restricted stock units (RSUs) and performance restricted stock units (performance RSUs); *(iv)* AIG 2007 Stock Incentive Plan, as amended (2007 Plan); *(v)* SICO's Deferred Compensation Profit Participation Plans (SICO Plans); *(vi)* AIG's 2005-2006 Deferred Compensation Profit Participation Plan (AIG DCPPP) and *(vii)* the AIG Partners Plan. The AIG DCPPP was adopted as a replacement for the SICO Plans for the 2005-2006 period, and the AIG Partners Plan replaced the AIG DCPPP. Share-based employee compensation earned under the AIG DCPPP was granted as time-vested RSUs under the 2002 Plan. Share-based employee compensation awarded under the AIG Partners Plan was granted as performance-based RSUs under the 2002 Plan, except for the December 2007 grant which was made under the 2007 Plan. All future grants will be made under the 2007 Plan. Although awards granted under all the plans described above remained outstanding at December 31, 2007, future grants of options, RSUs and performance RSUs can be made only under the 2007 Plan. AIG currently settles share option exercises and other share awards to participants by issuing shares it previously acquired and holds in its treasury account, except for share awards made by SICO, which are settled by SICO.

In 2006 and for prior years, AIG's non-employee directors received share-based compensation in the form of options granted pursuant to the 1999 Plan and grants of AIG common stock with delivery deferred until retirement from the Board, pursuant to the AIG Director Stock Plan, which was approved by the shareholders at the 2004 Annual Meeting of Shareholders and which is now a subplan under the 2007 Plan. From and after May 16, 2007, non-employee directors receive deferred stock units (DSUs) under the 2007 Plan with delivery deferred until retirement from the Board.

From January 1, 2003 through December 31, 2005, AIG accounted for share-based payment transactions with employees under FAS 123, ''Accounting for Stock-Based Compensation.'' Share-based employee compensation expense from option awards was not recognized in the consolidated statement of income in prior periods. Effective January 1, 2006, AIG adopted the fair

17. Share-based Employee Compensation Plans

Continued

value recognition provisions of FAS 123R. FAS 123R requires that companies use a fair value method to value share-based payments and recognize the related compensation expense in net earnings. AIG adopted FAS 123R using the modified prospective application method, and accordingly, financial statement amounts for the prior periods presented have not been restated to reflect the fair value method of expensing share-based compensation under FAS 123R. The modified prospective application method requires recognition of the fair value of share-based compensation for shares subscribed for or granted on or after January 1, 2006 and all previously granted but unvested awards at January 1, 2006.

The adoption of FAS 123R resulted in share-based compensation expense of approximately $17 million during 2006, related to awards that were accounted for under Accounting Principles Board Opinion 25, ''Accounting for Stock Issued to Employees.'' FAS 123R also requires AIG to estimate forfeitures in calculating the expense relating to share-based compensation, rather than recognizing these forfeitures and corresponding reductions in expense as they occur. The cumulative effect of adoption of $46 million was recorded as a cumulative effect of an accounting change, net of tax. FAS 123R requires AIG to reflect the cash savings resulting from excess tax benefits in its financial statements as cash flow from financing activities, rather than as cash flow from operating activities as in prior periods. The amount of this excess tax benefit in 2007 and 2006 was $26.1 million and $27.9 million, respectively.

Included in AIG's consolidated statement of income for the years ended December 31, 2007 and 2006 was pre-tax share-based compensation expense of $275 million ($216 million after tax), and $353 million ($326 million after tax), respectively. Share-based compensation expense in 2006 included a one-time compensation cost of approximately $54 million related to the Starr tender offer and various out of period adjustments totaling $61 million, primarily relating to stock splits and other miscellaneous items for the SICO Plans. See Note 19 herein for a discussion of the Starr tender offer.

1999 Stock Option Plan

The 1999 Plan was approved by the shareholders at the 2000 Annual Meeting of Shareholders, with certain amendments approved at the 2003 Annual Meeting of Shareholders. The 1999 Plan superseded the 1991 Employee Stock Option Plan (the 1991 Plan), although outstanding options granted under the 1991 Plan continue until exercise or expiration. Options granted under the 1999 Plan generally vest over four years (25 percent vesting per year) and expire 10 years from the date of grant. The 2007 Plan supersedes the 1999 Plan.

At December 31, 2007, there were no shares reserved for future grants under the 1999 Plan and 36,363,769 shares reserved for issuance under the 1999 and 1991 Plans.

Deferrals

At December 31, 2007, AIG was obligated to issue 12,521,342 shares in connection with previous exercises of options with delivery deferred.

Valuation

AIG uses a binomial lattice model to calculate the fair value of stock option grants. A more detailed description of the valuation methodology is provided below.

The following weighted-average assumptions were used for stock options granted in 2007, 2006 and 2005:

	2007	2006	2005
Expected annual dividend yield[(a)]	**1.39%**	0.92%	0.71%
Expected volatility[(b)]	**32.82%**	23.50%	27.30%
Risk-free interest rate[(c)]	**4.08%**	4.61%	4.17%
Expected term[(d)]	**7 years**	7 years	7 years

(a) The dividend yield is determined at the grant date.

(b) In 2007, expected volatility is the average of historical volatility (based on seven years of daily stock price changes) and the implied volatility of actively traded options on AIG shares.

(c) The interest rate curves used in the valuation model were the U.S. Treasury STRIP rates with terms from 3 months to 10 years.

(d) The contractual term of the option is generally 10 years with an expected term of 7 years calculated based on an analysis of historical employee exercise behavior and employee turnover (post-vesting terminations). The early exercise rate is a function of time elapsed since the grant. Fifteen years of historical data were used to estimate the early exercise rate.

17. Share-based Employee Compensation Plans

Continued

Additional information with respect to AIG's stock option plans at December 31, 2007, and changes for the year then ended, were as follows:

Options:	Shares	Weighted Average Exercise Price	Weighted Average Remaining Contractual Life	Aggregate Intrinsic Values (in millions)
Outstanding at beginning of year	47,655,720	$ 57.99		
Granted	1,738,530	$ 57.43		
Exercised*	(12,308,493)	$ 40.00		
Forfeited or expired	(721,988)	$ 69.00		
Outstanding at end of year	36,363,769	$ 63.83	4.81	$59
Options exercisable at end of year	30,703,527	$ 63.98	4.10	$57
Weighted average fair value per share of options granted		$ 20.97		

* *Includes options with respect to 8,489,584 shares exercised with delivery deferred, resulting in obligations to issue 4,138,713 shares.*

Vested and expected-to-vest options at December 31, 2007, included in the table above, totaled 34,349,762, with a weighted average exercise price of $64.14, a weighted average contractual life of 4.46 years and an aggregate intrinsic value of $57 million.

At December 31, 2007, total unrecognized compensation cost (net of expected forfeitures) was $100 million and $3 million related to non-vested share-based compensation awards granted under the 1999 Plan and the 1996 Plan, respectively, with blended weighted average periods of 1.38 years and 0.41 years, respectively. The cost of awards outstanding under these plans at December 31, 2007 is expected to be recognized over approximately four years and one year, respectively, for the 1999 Plan and the 1996 Plan.

The intrinsic value of options exercised during 2007 was approximately $360 million. The fair value of options vesting during 2007 was approximately $63 million. AIG received $482 million and $104 million in cash during 2007 and 2006, respectively, from the exercise of stock options. The tax benefits realized as a result of stock option exercises were $16 million and $35 million in 2007 and 2006, respectively.

2002 Stock Incentive Plan

The 2002 Plan was adopted at the 2002 Annual Meeting of shareholders and amended and restated by AIG's Board of Directors on September 18, 2002. During 2007 and 2006, 179,106 and 6,836,785 RSUs, respectively, including performance RSUs, were granted under the 2002 Plan. Because the 2002 Plan has been superseded by the 2007 Plan, there were no shares reserved for issuance in connection with future awards at December 31, 2007. Substantially all time-vested RSUs granted under the 2002 Plan vest on the fourth anniversary of the date of grant.

2007 Stock Incentive Plan

The 2007 Plan was adopted at the 2007 Annual Meeting of shareholders and amended and restated by AIG's Board of Directors on November 14, 2007. The 2007 Plan supersedes the 1999 Plan and the 2002 Plan. During 2007, 7,121,252 RSUs, including performance RSUs were granted under the 2007 Plan. Each RSU, performance RSU and DSU awarded reduces the number of shares available for future grants by 2.9 shares. At December 31, 2007, there were 157,562,672 shares reserved for issuance under the 2007 Plan. A significant majority of the time-vested RSUs granted in 2007 under the 2007 Plan vest on the fourth anniversary of the date of grant.

Non-Employee Director Stock Awards

The methodology used for valuing employee stock options is also used to value director stock options. Director stock options vest one year after the grant date, but are otherwise the same as employee stock options. Commencing in 2007, directors no longer receive awards of options. Options with respect to 40,000 shares and 32,500 shares were granted during 2006 and 2005, respectively.

In 2007, AIG granted to directors 22,542 DSUs, including DSUs representing dividend-equivalent amounts. AIG also granted to directors 6,375 shares, 14,000 shares and 6,250 shares, with delivery deferred, during 2007, 2006 and 2005, respectively, under the Director Stock Plan.

17. Share-based Employee Compensation Plans

Continued

Employee Stock Purchase Plan

AIG's 1996 Plan provides that eligible employees (those employed at least one year) may receive privileges to purchase up to an aggregate of 10,000,000 shares of AIG common stock, at a price equal to 85 percent of the fair market value on the date of the grant of the purchase privilege. Purchase privileges are granted quarterly and are limited to the number of whole shares that can be purchased on an annual basis by an amount equal to the lesser of 10 percent of an employee's annual salary or $10,000.

SICO Plans

The SICO Plans provide that shares of AIG common stock currently held by SICO are set aside for the benefit of the participant and distributed upon retirement. The SICO Board of Directors currently may permit an early payout of shares under certain circumstances. Prior to payout, the participant is not entitled to vote, dispose of or receive dividends with respect to such shares, and shares are subject to forfeiture under certain conditions, including but not limited to the participant's termination of employment with AIG prior to normal retirement age.

Historically, SICO's Board of Directors could elect to pay a participant cash in lieu of shares of AIG common stock. On December 9, 2005, SICO notified participants that essentially all subsequent distributions would be made only in shares, and not cash. At that date, AIG modified its accounting for the SICO Plans from variable to fixed measurement accounting. Variable measurement accounting is used for those few awards for which cash elections had been made prior to March 2005. At December 9, 2005, there were 12,650,292 non-vested AIG shares under the SICO Plans with a weighted average fair value per share of $61.92. The SICO Plans are also described in Note 19 herein.

Although none of the costs of the various benefits provided under the SICO Plans have been paid by AIG, AIG has recorded compensation expense for the deferred compensation amounts payable to AIG employees by SICO, with an offsetting amount credited to additional paid-in capital reflecting amounts deemed contributed by SICO.

A significant portion of the awards under the SICO Plans vest the year after the participant reaches age 65, provided that the participant remains employed by AIG through age 65. The portion of the awards for which early payout is available vest on the applicable payout date.

AIG DCPPP

In September 2005, AIG adopted the AIG DCPPP to provide share-based compensation to key AIG employees, including senior executive officers. The AIG DCPPP was modeled on the SICO Plans.

The AIG DCPPP contingently allocated a fixed number of time-vested RSUs to each participant if AIG's cumulative adjusted earnings per share in 2005 and 2006 exceeded that in 2003 and 2004 as determined by AIG's Compensation Committee. This goal was met, and pursuant to the terms of the DCPPP Plan, 3,696,836 time-vested RSUs were awarded in 2007. These RSUs vest in three pre-retirement installments and a final retirement installment at age 65.

At December 31, 2007, RSU awards with respect to 3,272,268 shares remained outstanding.

AIG Partners Plan

On June 26, 2006, AIG's Compensation Committee approved two grants under the AIG Partners Plan. The first grant had a performance period that ran from January 1, 2006 through December 31, 2007. The second grant has a performance period that runs from January 1, 2007 through December 31, 2008. In December 2007, the Compensation Committee approved a grant with a performance period from January 1, 2008 through December 31, 2009. The Compensation Committee will approve the performance metrics for this grant in the first quarter of 2008. All grants vest 50 percent on the fourth and sixth anniversaries of the first day of the related performance period. The Compensation Committee approved the performance metrics for the first two grants prior to the date of grant. The measurement of the first two grants is deemed to have occurred on June 26, 2006 when there was mutual understanding of the key terms and conditions of the first two grants. In 2007, no compensation cost was recognized, and compensation cost recognized in 2006 was reversed, for the first grant under the Partners Plan because the performance threshold for these awards was not met.

Valuation

The fair value of each award granted under the plans described above is based on the closing price of AIG stock on the date of grant.

17. Share-based Employee Compensation Plans

Continued

The following table presents a summary of shares relating to outstanding awards unvested under the foregoing plans at December 31, 2007, and changes for the year then ended*:

	Number of Shares					Weighted Average Grant-Date Fair Value				
	Time-vested RSUs	AIG DCPPP	Partners Plan	Total AIG Plan	Total SICO Plans	Time-vested RSUs	AIG DCPPP	Partners Plan	Total AIG Plans	Total SICO Plans
Unvested at January 1, 2007	7,181,595	4,590,622	3,607,040	15,379,257	11,443,772	$66.56	$52.09	$56.50	$59.88	$61.72
Granted	4,752,738	—	2,547,620	7,300,358	—	57.90	—	53.93	56.51	—
Vested	(168,214)	(196,690)	(550)	(365,454)	(1,691,306)	63.82	61.44	66.97	62.55	64.18
Forfeited	(422,431)	(173,472)	(1,212,585)	(1,808,488)	(282,657)	65.34	53.25	56.83	58.47	59.93
Unvested at December 31, 2007	11,343,688	4,220,460	4,941,525	20,505,673	9,469,809	$63.01	$54.53	$55.08	$59.36	$61.27

** Options and DSUs awarded under the 2007 Plan are not included. For the AIG DCPPP, includes all incremental shares granted or to be granted.*

The total unrecognized compensation cost (net of expected forfeitures) related to non-vested share-based compensation awards granted under the 2002 Plan, the 2007 Plan, the AIG DCPPP, and the SICO Plans at December 31, 2007 and the blended weighted-average periods over which those costs are expected to be recognized at December 31, 2007 are as follows:

(in millions)	Unrecognized Compensation Cost	Blended Weighted-Average Period
Time-vested RSUs - 2002 Plan	$218	1.35 years
Time-vested RSUs - 2007 Plan	$209	2.05 years
AIG DCPPP	$146	5.47 years
Total AIG Plans	$573	2.65 years
Total SICO Plans	$249	5.93 years

The total cost for awards outstanding at December 31, 2007 under the 2002 Plan, the 2007 Plan, the AIG DCPPP and the SICO Plans is expected to be recognized over approximately 4 years, 4 years, 32 years and 32 years, respectively.

18. Employee Benefits

Pension Plans

AIG, its subsidiaries and certain affiliated companies, offer various defined benefit plans to eligible employees based on either completion of a specified period of continuous service or date of hire, subject to age limitations.

AIG's U.S. retirement plan is a qualified, noncontributory defined benefit plan which is subject to the provisions of ERISA. U.S. employees who are employed by a participating company, have attained age 21 and completed twelve months of continuous service are eligible to participate in this plan. Employees generally vest after 5 years of service. Unreduced benefits are paid to retirees at normal retirement (age 65) and are based upon a percentage of final average compensation multiplied by years of credited service, up to 44 years. Non-U.S. defined benefit plans are generally either based on the employee's years of credited service and compensation in the years preceding retirement, or on points accumulated based on the employee's job grade and other factors during each year of service.

In 2007, AIG acquired the outstanding minority interest of 21st Century. Assets, obligations and costs with respect to 21st Century's plans are included herein. The assumptions used by 21st Century in its plans were not significantly different from those used by AIG in AIG's U.S. plans.

AIG also sponsors several unfunded defined benefit plans for certain employees, including key executives, designed to supplement pension benefits provided by AIG's other retirement plans. These include the AIG Excess Retirement Income Plan, which provides a benefit equal to the reduction in benefits payable to certain employees under the AIG U.S. retirement plan as a result of federal tax limitations on compensation and benefits payable, and the Supplemental Executive Retirement Plan (Supplemental Plan), which provides additional retirement benefits to designated executives. Under the Supplemental Plan, an annual benefit accrues at a percentage of final average pay multiplied by each year of credited service, not greater than 60 percent of final average pay, reduced by any benefits from the current and any predecessor retirement plans (including the AIG Excess Retirement Income Plan and any comparable plans), Social Security, if any, and from any qualified pension plan of prior employers.

Postretirement Plans

AIG and its subsidiaries also provide postretirement medical care and life insurance benefits in the U.S. and in certain non-U.S. countries. Eligibility in the various plans is generally based upon completion of a specified period of eligible service and attaining a specified age. Overseas, benefits vary by geographic location.

U.S. postretirement medical and life insurance benefits are based upon the employee electing immediate retirement and having a minimum of ten years of service. Medical benefits are contributory, while the life insurance benefits are non-contributory. Retiree medical contributions vary with age and length of service and range from requiring no cost for pre-1989 retirees to requiring actual premium payments reduced by certain credits for post-1993 retirees. These contributions are subject to adjustment annually. Other cost sharing features of the medical plan include deductibles, coinsurance and Medicare coordination and a lifetime maximum benefit of $2 million.

18. Employee Benefits

Continued

The following table presents the funded status of the plans, reconciled to the amount reported in the consolidated balance sheet at December 31, 2007 and 2006. The measurement date for some of the non-U.S. defined benefit pension and postretirement plans is November 30, consistent with the fiscal year end of the sponsoring companies. For all other plans, measurement occurs as of December 31, 2007.

	Pension				Postretirement[a]			
	Non-U.S. Plans[b]		U.S. Plans[c]		Non-U.S. Plans		U.S. Plans	
(in millions)	**2007**	2006	**2007**	2006	**2007**	2006	**2007**	2006
Change in projected benefit obligation:								
Benefit obligation, beginning of year	**$ 1,578**	$1,351	**$ 3,079**	$3,131	**$ 53**	$ 43	**$ 252**	$ 205
Service cost	**90**	78	**135**	130	**5**	4	**11**	6
Interest cost	**50**	36	**186**	169	**3**	2	**15**	11
Participant contributions	**4**	1	**—**	—	**—**	—	**—**	—
Actuarial (gain) loss	**(12)**	(40)	**(159)**	(245)	**(2)**	5	**(3)**	(1)
Plan amendments and mergers	**(2)**	—	**17**	—	**—**	—	**—**	47
Benefits paid:								
AIG assets	**(36)**	(28)	**(11)**	(10)	**(1)**	(1)	**(18)**	(16)
Plan assets	**(43)**	(27)	**(91)**	(84)	**—**	—	**—**	—
Effect of foreign currency fluctuation	**78**	71	**—**	—	**4**	—	**—**	—
Other	**38**	136	**—**	(12)	**17**	—	**—**	—
Projected benefit obligation, end of year	**$ 1,745**	$1,578	**$ 3,156**	$3,079	**$ 79**	$ 53	**$ 257**	$ 252
Change in plan assets:								
Fair value of plan assets, at beginning of year	**$ 850**	$ 699	**$ 2,760**	$2,561	**$ —**	$ —	**$ —**	$ —
Actual return on plan assets, net of expenses	**36**	33	**162**	282	**—**	—	**—**	—
AIG contributions	**87**	69	**309**	11	**1**	1	**18**	16
Participant contributions	**4**	1	**—**	—	**—**	—	**—**	—
Benefits paid:								
AIG assets	**(36)**	(28)	**(11)**	(10)	**(1)**	(1)	**(18)**	(16)
Plan assets	**(43)**	(27)	**(91)**	(84)	**—**	—	**—**	—
Effect of foreign currency fluctuation	**51**	41	**—**	—	**—**	—	**—**	—
Other	**3**	62	**—**	—	**—**	—	**—**	—
Fair value of plan assets, end of year	**$ 952**	$ 850	**$ 3,129**	$2,760	**$ —**	$ —	**$ —**	$ —
Funded status, end of year	**$ (793)**	$ (728)	**$ (27)**	$ (319)	**$ (79)**	$(53)	**$ (257)**	$(252)
Amounts recognized in the consolidated balance sheet:								
Assets	**$ 28**	$ 18	**$ 228**	$ —	**$ —**	$ —	**$ —**	$ —
Liabilities	**(821)**	(746)	**(255)**	(319)	**(79)**	(53)	**(257)**	(252)
Total amounts recognized	**$ (793)**	$ (728)	**$ (27)**	$ (319)	**$ (79)**	$(53)	**$ (257)**	$(252)
Amounts recognized in Accumulated other comprehensive income (loss):								
Net loss	**$ 242**	$ 256	**$ 513**	$ 687	**$ 6**	$ 7	**$ (5)**	$ 3
Prior service cost (credit)	**(67)**	(72)	**(2)**	(20)	**—**	—	**23**	22
Total amounts recognized	**$ 175**	$ 184	**$ 511**	$ 667	**$ 6**	$ 7	**$ 18**	$ 25

(a) AIG does not currently fund postretirement benefits.

(b) Includes unfunded plans for which the aggregate pension benefit obligation was $559 million and $494 million at December 2007, and 2006, respectively. For 2007 and 2006, approximately 83% pertain to Japanese plans, which are not required by local regulation to be funded. The projected benefit obligation for these plans total $464 million and $414 million, respectively.

(c) Includes non-qualified unfunded plans, for which the aggregate projected benefit obligation was $240 million and $228 million at December 2007 and 2006, respectively.

18. Employee Benefits

Continued

The accumulated benefit obligations for both non-U.S. and U.S. pension benefit plans at December 31, 2007 and 2006 were as follows:

(in millions)	**2007**	2006
Non-U.S. pension benefit plans	**$1,504**	$1,384
U.S. pension benefit plans	**$2,752**	$2,689

Defined benefit pension plan obligations in which the projected benefit obligation was in excess of the related plan assets and in which the accumulated benefit obligation was in excess of the related plan assets at December 31, 2007 and 2006 were as follows:

	PBO exceeds fair value of plan assets				ABO exceeds fair value of plan assets			
	Non-U.S. Plans		U.S. Plans		Non-U.S. Plans		U.S. Plans	
(in millions)	**2007**	2006	**2007**	2006	**2007**	2006	**2007**	2006
Projected benefit obligation	**$ 1,676**	$1,486	**$ 368**	$3,079	**$ 1,415**	$1,465	**$ 240**	$240
Accumulated benefit obligation	**1,462**	1,323	**317**	2,689	**1,277**	1,311	**206**	204
Fair value of plan assets	**855**	740	**113**	2,760	**652**	723	**—**	11

The following table presents the components of net periodic benefit cost recognized in income and other amounts recognized in Accumulated other comprehensive income (loss) with respect to the defined benefit pension plans and other postretirement benefit plans for the year ended December 31, 2007 and 2006 (no amounts related to the adoption of FAS 158 were recognized in Accumulated other comprehensive income (loss) for the year ended 2005):

	Pension						Postretirement					
	Non-U.S. Plans			U.S. Plans			Non-U.S. Plans			U.S. Plans		
(in millions)	**2007**	2006	2005	**2007**	2006	2005	**2007**	2006	2005	**2007**	2006	2005
Components of net periodic benefit cost:												
Service cost	**$ 90**	$ 78	$ 71	**$ 135**	$ 130	$ 111	**$ 5**	$ 4	$ 4	**$ 11**	$ 6	$ 5
Interest cost	**50**	36	32	**186**	169	153	**3**	2	2	**15**	11	11
Expected return on assets	**(36)**	(28)	(21)	**(216)**	(201)	(180)	**—**	—	—	**—**	—	—
Amortization of prior service cost	**(10)**	(9)	(10)	**(3)**	(3)	(3)	**—**	—	—	**(2)**	(6)	(6)
Amortization of transitional obligation	**1**	1	1	**—**	—	—	**—**	—	—	**—**	—	—
Recognition of net actuarial (gains)/losses	**9**	16	21	**43**	75	55	**—**	—	—	**—**	—	—
Other	**1**	1	7	**14**	6	1	**—**	—	—	**—**	—	—
Net periodic benefit cost	**$105**	$ 95	$101	**$ 159**	$ 176	$ 137	**$ 8**	$ 6	$ 6	**$ 24**	$ 11	$ 10
Total recognized in Accumulated other comprehensive income (loss)	**$ (10)**	$ 38	—	**$(155)**	$ 24	—	**$ (2)**	$ —	—	**$ (7)**	$ —	$ —
Total recognized in net periodic benefit cost and other comprehensive income	**$ 95**	$133	$101	**$ 4**	$ 200	$ 137	**$ 6**	$ 6	$ 6	**$ 17**	$ 11	$ 10

The estimated net loss and prior service credit that will be amortized from Accumulated other comprehensive income into net periodic benefit cost over the next fiscal year are $31 million and $11 million, respectively, for AIG's combined defined benefit pension plans. For the defined benefit postretirement plans, the estimated amortization from Accumulated other comprehensive income for net loss, prior service credit and transition obligation that will be amortized into net periodic benefit cost over the next fiscal year will be less than $5 million in the aggregate.

18. Employee Benefits

Continued

Assumptions

The weighted average assumptions used to determine the benefit obligations at December 31, 2007 and 2006 are as follows:

	Pension		Postretirement	
	Non-U.S. Plans	U.S. Plans	Non-U.S. Plans	U.S. Plans
2007				
Discount rate	**2.00 - 11.00%**	**6.50%**	**2.75 - 6.50%**	**6.50%**
Rate of compensation increase	**1.50 - 9.00%**	**4.25%**	**3.00 - 3.50%**	**4.25%**
2006				
Discount rate	2.25 - 10.75%	6.00%	4.00 - 5.75%	6.00%
Rate of compensation increase	1.50 - 10.00%	4.25%	3.00%	4.25%

The benefit obligations for non-U.S. plans reflect those assumptions that were most appropriate for the local economic environments of each of the subsidiaries providing such benefits.

Assumed health care cost trend rates for the U.S. plans were as follows:

	2007	2006
Following year:		
Medical (before age 65)	**9.00%**	8.00%
Medical (age 65 and older)	**7.00%**	6.70%
Ultimate rate to which cost increase is assumed to decline	**5.00%**	5.00%
Year in which the ultimate trend rate is reached:		
Medical (before age 65)	**2015**	2013
Medical (age 65 and older)	**2015**	2013

A one percent point change in the assumed healthcare cost trend rate would have the following effect on AIG's postretirement benefit obligations at December 31, 2007 and 2006:

	One Percent Increase		One Percent Decrease	
(in millions)	**2007**	2006	**2007**	2006
Non-U.S. plans	**$12**	$10	**$(8)**	$(7)
U.S. plans	**$ 6**	$ 3	**$(5)**	$(3)

AIG's postretirement plans provide benefits primarily in the form of defined employer contributions rather than defined employer benefits. Changes in the assumed healthcare cost trend rate are subject to caps for U.S. plans. AIG's non-U.S. postretirement plans are not subject to caps.

18. Employee Benefits

Continued

The weighted average assumptions used to determine the net periodic benefit costs for the years ended December 31, 2007, 2006 and 2005 were as follows:

	Pension		Postretirement	
	Non-U.S. Plans*	U.S. Plans	Non-U.S. Plans*	U.S. Plans
2007				
Discount rate	**2.25 - 10.75%**	**6.00%**	**4.00 - 5.75%**	**6.00%**
Rate of compensation increase	**1.50 - 10.00%**	**4.25%**	**3.00%**	**4.25%**
Expected return on assets	**2.50 - 10.50%**	**8.00%**	**N/A**	**N/A**
2006				
Discount rate	1.75 - 12.00%	5.50%	4.50 - 5.50%	5.50%
Rate of compensation increase	1.50 - 10.00%	4.25%	2.50 - 3.00%	4.25%
Expected return on assets	2.50 - 13.50%	8.00%	N/A	N/A
2005				
Discount rate	1.75 - 12.00%	5.75%	4.50 - 6.00%	5.75%
Rate of compensation increase	1.50 - 10.00%	4.25%	3.00%	4.25%
Expected return on assets	2.15 - 13.50%	8.00%	N/A	N/A

* *The benefit obligations for non-U.S. plans reflect those assumptions that were most appropriate for the local economic environments of the subsidiaries providing such benefits.*

Discount Rate Methodology

The projected benefit cash flows under the AIG U.S. Retirement Plan were discounted using the spot rates derived from the Citigroup Pension Discount Curve at December 31, 2007 and 2006 and an equivalent single discount rate was derived resulting in the same liability. This single discount rate was rounded to the nearest 25 basis points, namely 6.5 percent and 6.0 percent at December 31, 2007 and 2006, respectively. The rates applied to other U.S. plans were not significantly different from those discussed above.

Both funded and unfunded plans for Japan represent over 62 percent of the liabilities of the non-U.S. pension plans at December 31, 2007 and 2006, respectively. The discount rate for Japan was selected by reference to the published Moody's/S&P AA Corporate Bond Universe at the measurement date having regard to the duration of the plans' liabilities.

Plan assets

The asset allocation percentage by major asset class for AIG's plans at December 31, 2007 and 2006, and the target allocation for 2008 follow:

	Non-U.S. Plans-Allocation			U.S. Plans-Allocation		
	Target 2008	**Actual 2007**	Actual 2006	Target 2008	**Actual 2007**	Actual 2006
Asset class:						
Equity securities	50%	**50%**	47%	42%	**56%**	64%
Debt securities	28	**28**	32	32	**30**	26
Other	22	**22**	21	26	**14**	10
Total	100%	**100%**	100%	100%	**100%**	100%

Other includes cash, insurance contracts, real estate, private equity and hedge funds asset classes.

No shares of AIG common stock were included in the U.S. plans at December 31, 2007 and 55,680 shares of AIG common stock with a value of $4 million were included in the U.S. plans at December 31, 2006.

The investment strategy with respect to AIG's pension plan assets is designed to achieve investment returns that will fully fund the pension plan over the long term, while limiting the risk of under funding over shorter time periods.

The expected rate of return with respect to AIG's domestic pension plan was 8.0 percent for years ended December 31, 2007 and 2006. This rate of return is an aggregation of expected returns within each asset category that, when combined with AIG's contribution to the plan, will maintain the plan's ability to meet all required benefit obligations. The return with respect to each asset class considers both historical returns and the future expectations for such returns.

18. Employee Benefits

Continued

Expected Cash Flows

Funding for the U.S. pension plan ranges from the minimum amount required by ERISA to the maximum amount that would be deductible for U.S. tax purposes. This range is generally not determined until the fourth quarter. Contributed amounts in excess of the minimum amounts are deemed voluntary. Amounts in excess of the maximum amount would be subject to an excise tax and may not be deductible under the Internal Revenue Code. Supplemental and excess plans' payments and postretirement plan payments are deductible when paid.

During 2007 AIG contributed $396 million to its U.S. and non-U.S. pension plans. The annual pension contribution in 2008 is expected to be approximately $118 million for U.S. and non-U.S. plans.

The expected future benefit payments, net of participants' contributions, with respect to the defined benefit pension plans and other postretirement benefit plans, are as follows:

	Pension		Postretirement	
(in millions)	Non-U.S. Plans	U.S. Plans	Non-U.S. Plans	U.S. Plans
2008	$ 74	$ 135	$ 1	$ 17
2009	79	130	1	17
2010	79	139	1	18
2011	85	150	1	18
2012	85	163	2	19
2013-2017	474	1,022	10	102

Defined Contribution Plans

In addition to several small defined contribution plans, AIG sponsors a voluntary savings plan for domestic employees (the AIG Incentive Savings plan), which provides for salary reduction contributions by employees and matching contributions by AIG of up to seven percent of annual salary depending on the employees' years of service. Pre-tax expense associated with this plan was $114 million, $104 million and $96 million in 2007, 2006 and 2005, respectively.

19. Benefits Provided by Starr International Company, Inc. and C.V. Starr & Co., Inc.

SICO has provided a series of two-year Deferred Compensation Profit Participation Plans (SICO Plans) to certain AIG employees. The SICO Plans came into being in 1975 when the voting shareholders and Board of Directors of SICO, a private holding company whose principal asset is AIG common stock, decided that a portion of the capital value of SICO should be used to provide an incentive plan for the current and succeeding managements of all American International companies, including AIG.

None of the costs of the various benefits provided under the SICO Plans has been paid by AIG, although AIG has recorded a charge to reported earnings for the deferred compensation amounts paid to AIG employees by SICO, with an offsetting amount credited to additional paid-in capital reflecting amounts deemed contributed by SICO. The SICO Plans provide that shares currently owned by SICO are set aside by SICO for the benefit of the participant and distributed upon retirement. The SICO Board of Directors currently may permit an early payout of units under certain circumstances. Prior to payout, the participant is not entitled to vote, dispose of or receive dividends with respect to such shares, and shares are subject to forfeiture under certain conditions, including but not limited to the participant's voluntary termination of employment with AIG prior to normal retirement age. Under the SICO Plans, SICO's Board of Directors may elect to pay a participant cash in lieu of shares of AIG common stock. Following notification from SICO to participants in the SICO Plans that it will settle specific future awards under the SICO Plans with shares rather than cash, AIG modified its accounting for the SICO Plans from variable to fixed measurement accounting. AIG gave effect to this change in settlement method beginning on December 9, 2005, the date of SICO's notice to participants in the SICO Plans. See also Note 12(a) Commitments herein.

Compensation expense in 2006 included various out of period adjustments totaling $61 million, primarily relating to stock-splits and other miscellaneous items for the SICO plans. See also Note 17 herein.

In January 2006, C.V. Starr & Co., Inc. (Starr) completed its tender offer to purchase Starr interests from AIG employees. In conjunction with AIG's adoption of FAS 123R, Starr is considered to be an ''economic interest holder'' in AIG. As a result, compensation expense of $54 million was recorded in 2006 results with respect to the Starr tender offer.

As a result of its changing relationship with Starr and SICO, AIG has established new executive compensation plans to replace the SICO plans and investment opportunities previously provided by Starr. See Note 17 for a description of these plans.

Compensation expense with respect to the SICO Plans aggregated $39 million, $108 million and $205 million in 2007, 2006 and 2005, respectively.

20. Ownership and Transactions With Related Parties

(a) Ownership: According to the Schedule 13D filed on March 20, 2007 by Starr, SICO, Edward E. Matthews, Maurice R. Greenberg, the Maurice R. and Corinne P. Greenberg Family Foundation, Inc., the Universal Foundation, Inc., the Maurice R. and Corinne P. Greenberg Joint Tenancy Company, LLC and the C.V. Starr & Co., Inc. Trust, these reporting persons could be deemed to beneficially own 354,987,261 shares of AIG's common stock at that date. Based on the shares of AIG's common stock outstanding at January 31, 2008, this ownership would represent approximately 14.1 percent of the voting stock of AIG. Although these reporting persons have made filings under Section 16 of the Exchange Act, reporting sales of shares of common stock, no amendment to the Schedule 13D has been filed to report a change in ownership subsequent to March 20, 2007.

(b) Transactions with Related Parties: Prior to the termination of their agency relationships with Starr during 2006, AIG and

20. Ownership and Transactions With Related Parties

Continued

its subsidiaries paid commissions to Starr and its subsidiaries for the production and management of insurance business in the ordinary course of business. Payment for the production of insurance business to Starr aggregated approximately $12 million in 2007, $47 million in 2006, and $214 million in 2005. AIG also received no rental fees in 2007, approximately $4 million in 2006, and $23 million in 2005 from Starr, and paid no rental fees in 2007 or 2006 and approximately $20,000 in 2005 to Starr. AIG also received none in 2007 and 2006 and approximately $2 million in 2005, respectively, from SICO, and paid none in 2007 and 2006 and approximately $1 million in 2005 to SICO, as reimbursement for services rendered at cost. AIG also paid to SICO $2 million in 2007, $2 million in 2006, and $3 million in 2005 in rental fees. There are no significant receivables from/payables to related parties at December 31, 2007.

21. Federal Income Taxes

Tax Filings

AIG and its eligible U.S. subsidiaries file a consolidated U.S. federal income tax return. Prior to 2007, Life Insurance subsidiaries of AIG Life Holdings (US), Inc. (AIGLH), formerly known as American General Corporation, also filed a consolidated U.S. federal income tax return and were not eligible to be included in AIG's consolidated federal income tax return. AIGLH will be included in the 2007 AIG consolidated federal income tax return. Other U.S. subsidiaries included in the consolidated financial statements also file separate U.S. federal income tax returns. Subsidiaries operating outside the U.S. are taxed, and income tax expense is recorded, based on applicable U.S. and foreign statutes.

Undistributed Earnings and Distributions from Life Surplus

U.S. federal income taxes have not been provided on $1.5 billion of undistributed earnings of certain U.S. subsidiaries that are not included in the consolidated AIG U.S. federal income tax return. Tax planning strategies are available, and would be utilized, to eliminate the tax liability related to these earnings. U.S. federal income taxes have not been provided on the undistributed earnings of certain non-U.S. subsidiaries to the extent that such earnings have been reinvested abroad indefinitely. At December 31, 2007, the cumulative amount of undistributed earnings in these subsidiaries approximated $21.2 billion. Determining the deferred tax liability that would arise if these earnings were not permanently reinvested abroad is not practicable.

A component of life insurance surplus accumulated prior to 1984 is not taxable unless it exceeds certain statutory limitations or is distributed to shareholders. The American Jobs Creation Act of 2004 amended the federal income tax law to permit life insurance companies to distribute amounts from their policyholders' surplus accounts in 2005 and 2006 without incurring federal income tax on the distributions. In 2005 and 2006, AIG made distributions and eliminated the aggregate balance of $945 million from its policyholders' surplus accounts.

Tax Examinations

In December 2007, AIG reached a settlement with the IRS in the United States Tax Court for SunAmerica, Inc. and Subsidiaries (''SunAmerica'') for tax years ended September 30, 1993 and September 30, 1994, which are years prior to AIG's 1999 acquisition of SunAmerica. The terms of this settlement will be incorporated into the IRS examinations for tax years of SunAmerica from September 30, 1995 through December 31, 1998, and for SunAmerica Life Insurance Company and Subsidiaries for tax year December 31, 1999, to resolve these years. As a result of this settlement, a net refund is due AIG for the periods from 1993 to 1999, the amount of which is immaterial to AIG's consolidated financial condition. The IRS's examination of the separate life consolidated federal return for SunAmerica Life and its subsidiaries for years 2000-2002 was closed in January 2008 with a signed settlement agreement. An immaterial amount is payable to the IRS for these years. AIG is in a net refund position for all years 1993-2002 for aggregated SunAmerica audits.

AIGLH's tax years prior to 2000 are closed. Although a Revenue Agent's Report has not yet been issued to AIGLH for years ended December 31, 2000, August 29, 2001, December 31, 2001, and December 31, 2002, AIGLH has received from the IRS a notice of proposed adjustment for certain items during that period.

The statute of limitations for all tax years prior to 1997 has now expired for AIG's consolidated federal income tax return. In June, 2007, AIG filed a refund claim for years 1991-1996. The refund claim relates to the tax effects of the restatements of AIG's 2004 and prior financial statements. A refund claim for the tax years ending December 31, 1997-2004 will be filed before September 30, 2008.

AIG has executed a partial settlement with the IRS for tax years 1997 through 1999. Two issues remain open, neither one of which, separately or in total, is material to AIG's consolidated financial condition. The statute of limitations for these years expires on March 31, 2008. AIG is currently under examination for the tax years 2000 through 2002.

AIG believes there are substantial arguments in support of the tax positions taken in its tax returns. Although the final outcome of any issue still outstanding is uncertain, AIG believes that any tax obligation, including interest thereon, would not be material to AIG's consolidated financial condition, results of operations, or liquidity.

21. Federal Income Taxes

Continued

The pretax components of U.S. and foreign income reflect the locations in which such pretax income was generated. The pretax U.S. and foreign income was as follows for the years ended December 31, 2007, 2006 and 2005:

(in millions)	**2007**	2006	2005
U.S.	**$ (3,957)**	$ 9,862	$ 6,103
Foreign	**12,900**	11,825	9,110
Total	**$ 8,943**	$21,687	$15,213

The provision for income taxes for the years ended December 31, 2007, 2006 and 2005 consists of the following:

Years Ended December 31, (in millions)	**2007**	2006	2005
Foreign and U.S. components of actual income tax expense:			
Foreign:			
Current	**$ 3,157**	$ 2,725	$ 974
Deferred	**461**	933	426
U.S.:			
Current	**62**	2,764	1,613
Deferred	**(2,225)**	115	1,245
Total	**$ 1,455**	$ 6,537	$ 4,258

The U.S. federal income tax rate was 35 percent for 2007, 2006 and 2005. Actual tax expense on income differs from the ''expected'' amount computed by applying the federal income tax rate because of the following:

	2007		2006		2005	
Years Ended December 31, *(dollars in millions)*	Amount	Percent of Pretax Income	Amount	Percent of Pretax Income	Amount	Percent of Pretax Income
U.S. federal income tax at statutory rate	**$3,130**	**35.0%**	$7,591	35.0%	$5,325	35.0%
Adjustments:						
Tax exempt interest	**(823)**	**(9.2)**	(718)	(3.3)	(566)	(3.7)
Partnerships and joint ventures	**(312)**	**(3.5)**	(265)	(1.2)	(85)	(0.5)
Synthetic fuel and other tax credits	**(127)**	**(1.4)**	(196)	(0.9)	(296)	(1.9)
Effect of foreign operations	**(294)**	**(3.3)**	(132)	(0.6)	(253)	(1.7)
Dividends received deduction	**(129)**	**(1.4)**	(102)	(0.5)	(117)	(0.8)
State income taxes	**45**	**0.5**	59	0.3	86	0.6
Nondeductible compensation	**41**	**0.5**	61	0.3	83	0.5
SICO benefit	**(194)**	**(2.2)**	—	—	—	—
Other	**118**	**1.3**	239	1.0	81	0.5
Actual income tax expense	**$1,455**	**16.3%**	$6,537	30.1%	$4,258	28.0%

21. Federal Income Taxes

Continued

The components of the net deferred tax liability at December 31, 2007 and 2006 were as follows:

(in millions)	**2007**	2006
Deferred tax assets:		
Loss reserve discount	**$ 2,249**	$ 1,969
Unearned premium reserve reduction	**1,743**	1,352
Unrealized depreciation of investments	**104**	—
Loan loss and other reserves	**1,408**	1,054
Investments in foreign subsidiaries and joint ventures	**1,121**	420
Adjustment to life policy reserves	**3,213**	3,584
NOL's and tax attributes	**1,814**	222
Accruals not currently deductible, and other	**1,305**	1,209
Deferred tax assets*	**12,957**	9,810
Valuation allowance	**(223)**	(11)
Net deferred tax assets	**12,734**	9,799
Deferred tax liabilities:		
Deferred policy acquisition costs	**11,716**	10,396
Flight equipment, fixed assets and intangible assets	**5,239**	4,377
Unrealized appreciation of investments	**—**	3,370
Other	**1,041**	508
Total deferred tax liabilities	**17,996**	18,651
Net deferred tax liability	**$ 5,262**	$ 8,852

* *AIG has recorded deferred tax assets for alternative minimum tax credit carry forwards of $101 million and $222 million at December 31, 2007 and 2006, respectively. In 2007, AIG generated net operating loss carryforwards, unused foreign tax credits and general business tax credits in the amount of $4.2 billion, $130 million and $125 million, respectively. Net operating loss carryforwards and general business tax credits may be carried forward for twenty years while foreign tax credits may be carried forward for ten years. Unused minimum tax credits are available for future use without expiration.*

A reconciliation of the beginning and ending balances of the total amounts of gross unrecognized tax benefits is as follows:

(in millions)	**2007**
Gross unrecognized tax benefits at January 1, 2007	**$ 1,138**
Agreed audit adjustments with taxing authorities included in the beginning balance	**(188)**
Increases in tax positions for prior years	**646**
Decreases in tax positions for prior years	**(189)**
Increases in tax positions for current year	**82**
Lapse in statute of limitations	**(1)**
Settlements	**(178)**
Gross unrecognized tax benefits at December 31, 2007	**$ 1,310**

At December 31, 2007, AIG's unrecognized tax benefits, excluding interest and penalties, were $1.3 billion, which includes $299 million related to tax positions the disallowance of which would not affect the annual effective income tax rate. Accordingly, the amount of unrecognized tax benefits that, if recognized, would favorably affect the effective tax rate were $1.0 billion.

Interest and penalties related to unrecognized tax benefits are recognized in income tax expense. At January 1, 2007 and December 31, 2007, AIG had accrued $175 million and $281 million, respectively, for the payment of interest (net of the federal benefit) and penalties. For the year ended December 31, 2007, AIG recognized $170 million of interest (net of the federal benefit) and penalties in the Consolidated Statement of Income.

AIG continually evaluates adjustments proposed by taxing authorities. At December 31, 2007, such proposed adjustments would not result in a material change to AIG's consolidated financial condition. However, AIG believes that it is reasonably possible that the balance of the unrecognized tax benefits could decrease by $50 to $150 million within the next twelve months due to settlements or the expiration of statutes.

Listed below are the tax years that remain subject to examination by major tax jurisdictions:

Major Tax Jurisdictions	Open Tax Years
United States	1997-2006
United Kingdom	2003-2006
Hong Kong	1997-2006
Malaysia	1999-2006
Singapore	1993-2006
Thailand	2001-2006
Taiwan	2000-2006
Japan	2000-2006
Korea	2001-2006
France	2003-2006

The reserve for uncertain tax positions increased in the fourth quarter 2007 by $210 million for items attributable to prior restatements, including certain tax positions associated with compensation deductions. In addition, income tax expense has been reduced by $162 million for interest receivable from the IRS attributable to refund claims for prior restatements.

22. Quarterly Financial Information (Unaudited)

The following quarterly financial information for each of the three months ended March 31, June 30, September 30 and December 31, 2007 and 2006 is unaudited. However, in the opinion of management, all adjustments (consisting only of normal recurring adjustments) necessary for a fair statement of the results of operations for such periods, have been made.

Consolidated Statements of Operations

	Three Months Ended							
	March 31,		June 30,		September 30,		December 31,	
(in millions, except per share data)	**2007**	2006	**2007**	2006	**2007***	2006	**2007***	2006
Total revenues	**$30,645**	$27,278	**$31,150**	$26,854	**$29,836**	$29,247	**$18,433**	$30,008
Income (loss) before income taxes, minority interest and cumulative effect of an accounting change	**6,172**	4,793	**6,328**	5,241	**4,879**	6,301	**(8,436)**	5,352
Income (loss) before cumulative effect of an accounting change	**4,130**	3,161	**4,277**	3,190	**3,085**	4,224	**(5,292)**	3,439
Net income (loss)	**$ 4,130**	$ 3,195	**$ 4,277**	$ 3,190	**$ 3,085**	$ 4,224	**$ (5,292)**	$ 3,439
Earnings per common share:								
Basic								
Income (loss) before cumulative effect of an accounting change	**$ 1.58**	$ 1.21	**$ 1.64**	$ 1.23	**$ 1.20**	$ 1.62	**$ (2.08)**	$ 1.32
Cumulative effect of an accounting change, net of tax	**—**	0.01	**—**	—	**—**	—	**—**	—
Net income (loss)	**$ 1.58**	$ 1.22	**$ 1.64**	$ 1.23	**$ 1.20**	$ 1.62	**$ (2.08)**	$ 1.32
Diluted								
Income (loss) before cumulative effect of an accounting change	**$ 1.58**	$ 1.21	**$ 1.64**	$ 1.21	**$ 1.19**	$ 1.61	**$ (2.08)**	$ 1.31
Cumulative effect of an accounting change, net of tax	**—**	0.01	**—**	—	**—**	—	**—**	—
Net income (loss)	**$ 1.58**	$ 1.22	**$ 1.64**	$ 1.21	**$ 1.19**	$ 1.61	**$ (2.08)**	$ 1.31
Average shares outstanding:								
Basic	**2,612**	2,605	**2,602**	2,606	**2,576**	2,607	**2,550**	2,610
Diluted	**2,621**	2,624	**2,613**	2,625	**2,589**	2,626	**2,550**	2,622

* *Both revenues and operating income include (i) an unrealized market valuation loss of $352 million and $11.1 billion in the third quarter and fourth quarter of 2007, respectively, on AIGFP's super senior credit default swap portfolio and (ii) other-than-temporary impairment charges of $3.3 billion in the fourth quarter of 2007.*

23. Information Provided in Connection With Outstanding Debt

The following condensed consolidating financial statements reflect the following:

- AIGLH, formerly known as American General Corporation, is a holding company and a wholly owned subsidiary of AIG. AIG provides a full and unconditional guarantee of all outstanding debt of AIGLH.
- AIG Liquidity Corp. is a wholly owned subsidiary of AIG. AIG provides a full and unconditional guarantee of all obligations of AIG Liquidity Corp.
- AIG Program Funding, Inc. is a wholly owned subsidiary of AIG. AIG provides a full and unconditional guarantee of all obligations of AIG Program Funding, Inc., which was established in 2007.

Condensed Consolidating Balance Sheet

(in millions)	American International Group, Inc. (As Guarantor)	AIGLH	AIG Liquidity Corp.	AIG Program Funding, Inc.	Other Subsidiaries	Eliminations	Consolidated AIG
December 31, 2007							
Assets:							
Investments and financial services assets	**$ 14,648**	**$ 40**	**$ —**	**$ —**	**$ 859,063**	**$ (21,790)**	**$ 851,961**
Cash	**84**	**1**	**—**	**—**	**2,199**	**—**	**2,284**
Carrying value of subsidiaries and partially owned companies, at equity	**111,714**	**24,396**	**—**	**—**	**18,542**	**(153,998)**	**654**
Other assets	**9,414**	**2,592**	**—**	**—**	**193,445**	**155**	**205,606**
Total assets	**$135,860**	**$27,029**	**$ —**	**$ —**	**$1,073,249**	**$(175,633)**	**$1,060,505**
Liabilities:							
Insurance liabilities	**$ 43**	**$ —**	**$ —**	**$ —**	**$ 534,369**	**$ (75)**	**$ 534,337**
Debt	**36,045**	**2,136**	**—**	**—**	**156,003**	**(18,135)**	**176,049**
Other liabilities	**3,971**	**2,826**	**—**	**—**	**250,506**	**(3,085)**	**254,218**
Total liabilities	**40,059**	**4,962**	**—**	**—**	**940,878**	**(21,295)**	**964,604**
Preferred shareholders' equity in subsidiary companies	**—**	**—**	**—**	**—**	**100**	**—**	**100**
Total shareholders' equity	**95,801**	**22,067**	**—**	**—**	**132,271**	**(154,338)**	**95,801**
Total liabilities, preferred shareholders' equity in subsidiary companies and shareholders' equity	**$135,860**	**$27,029**	**$ —**	**$ —**	**$1,073,249**	**$(175,633)**	**$1,060,505**
December 31, 2006							
Assets:							
Investments and financial services assets	$ 7,346	$ —	$ *	$ —	$ 800,350	$ (14,822)	$ 792,874
Cash	76	—	*	—	1,514	—	1,590
Carrying value of subsidiaries and partially owned companies, at equity	109,125	27,967	—	—	8,436	(144,427)	1,101
Other assets	3,989	2,622	*	—	179,183	(1,949)	183,845
Total assets	$120,536	$30,589	$ *	$ —	$ 989,483	$(161,198)	$ 979,410
Liabilities:							
Insurance liabilities	$ 21	$ —	$ —	$ —	$ 498,263	$ (64)	$ 498,220
Debt	15,157	2,136	*	—	146,206	(14,820)	148,679
Other liabilities	3,681	3,508	*	—	224,936	(1,482)	230,643
Total liabilities	18,859	5,644	*	$ —	869,405	(16,366)	877,542
Preferred shareholders' equity in subsidiary companies	—	—	—	—	191	—	191
Total shareholders' equity	101,677	24,945	*	—	119,887	(144,832)	101,677
Total liabilities, preferred shareholders' equity in subsidiary companies and shareholders' equity	$120,536	$30,589	$ *	$ —	$ 989,483	$(161,198)	$ 979,410

* *Less than $1 million.*

23. Information Provided in Connection With Outstanding Debt

Continued

Condensed Consolidating Statement of Income

(in millions)	American International Group, Inc. Guarantor	AIGLH	AIG Liquidity Corp.	AIG Program Funding, Inc.	Other Subsidiaries	Eliminations	Consolidated AIG
Year Ended December 31, 2007							
Operating income (loss)	**$ (2,379)**	**$ (152)**	**$ ***	**$ —**	**$11,474**	**$ —**	**$ 8,943**
Equity in undistributed net income of consolidated subsidiaries	**3,121**	**(27)**	**—**	**—**	**—**	**(3,094)**	**—**
Dividend income from consolidated subsidiaries	**4,685**	**1,358**	**—**	**—**	**—**	**(6,043)**	**—**
Income taxes (benefits)	**(773)**	**248**	*****	**—**	**1,980**	**—**	**1,455**
Minority interest	**—**	**—**	**—**	**—**	**(1,288)**	**—**	**(1,288)**
Net income (loss)	**$ 6,200**	**$ 931**	**$ ***	**$ —**	**$ 8,206**	**$ (9,137)**	**$ 6,200**
Year Ended December 31, 2006							
Operating income (loss)	$ (786)	$ 122	$ *	$ —	$22,351	$ —	$21,687
Equity in undistributed net income of consolidated subsidiaries	13,308	1,263	—	—	—	(14,571)	—
Dividend income from consolidated subsidiaries	1,689	602	—	—	—	(2,291)	—
Income taxes (benefits)	197	(131)	*	—	6,471	—	6,537
Minority interest	—	—	—	—	(1,136)	—	(1,136)
Cumulative effect of an accounting change	34	—	—	—	—	—	34
Net income (loss)	$14,048	$2,118	$ *	$ —	$14,744	$(16,862)	$14,048
Year Ended December 31, 2005							
Operating income (loss)	$ (1,569)	$ (200)	$ *	$ —	$16,982	$ —	$15,213
Equity in undistributed net income of consolidated subsidiaries	10,156	2,530	—	—	—	(12,686)	—
Dividend income from consolidated subsidiaries	1,958	—	—	—	—	(1,958)	—
Income taxes (benefits)	68	(92)	*	—	4,282	—	4,258
Minority interest	—	—	—	—	(478)	—	(478)
Net income (loss)	$10,477	$2,422	$ *	$ —	$12,222	$(14,644)	$10,477

** Less than $1 million.*

23. Information Provided in Connection With Outstanding Debt

Continued

Condensed Consolidating Statements of Cash Flow

(in millions)	American International Group, Inc. Guarantor	AIGLH	AIG Liquidity Corp.	AIG Program Funding, Inc.	Other Subsidiaries	Consolidated AIG
Year Ended December 31, 2007						
Net cash provided by (used in) operating activities	**$ (770)**	**$ 214**	**$ ***	**$ —**	**$ 35,727**	**$ 35,171**
Cash flows from investing:						
Invested assets disposed	**3,057**	**—**	**—**	**—**	**175,201**	**178,258**
Invested assets acquired	**(9,666)**	**—**	**—**	**—**	**(235,729)**	**(245,395)**
Other	**(4,128)**	**—**	*****	**—**	**3,258**	**(870)**
Net cash used in investing activities	**(10,737)**	**—**	*****	**—**	**(57,270)**	**(68,007)**
Cash flows from financing activities:						
Issuance of debt	**20,582**	**—**	**—**	**—**	**82,628**	**103,210**
Repayments of debt	**(1,253)**	**—**	**—**	**—**	**(78,823)**	**(80,076)**
Payments advanced to purchase shares	**(6,000)**	**—**	**—**	**—**	**—**	**(6,000)**
Cash dividends paid to shareholders	**(1,881)**	**—**	**—**	**—**	**—**	**(1,881)**
Other	**67**	**(213)**	*****	**—**	**18,373**	**18,227**
Net cash provided by (used in) financing activities	**11,515**	**(213)**	*****	**—**	**22,178**	**33,480**
Effect of exchange rate changes on cash	**—**	**—**	**—**	**—**	**50**	**50**
Change in cash	**8**	**1**	*****	**—**	**685**	**694**
Cash at beginning of year	**76**	**—**	**—**	**—**	**1,514**	**1,590**
Cash at end of year	**$ 84**	**$ 1**	**$ ***	**$ —**	**$ 2,199**	**$ 2,284**
Year Ended December 31, 2006						
Net cash provided by (used in) operating activities	$ (590)	$ 258	$ *	$ —	$ 6,619	$ 6,287
Cash flows from investing:						
Invested assets disposed	3,402	—	—	—	154,704	158,106
Invested assets acquired	(8,298)	—	—	—	(216,663)	(224,961)
Other	(2,747)	(67)	*	—	1,717	(1,097)
Net cash used in investing activities	(7,643)	(67)	*	—	(60,242)	(67,952)
Cash flows from financing activities:						
Issuance of debt	12,038	—	—	—	61,950	73,988
Repayments of debt	(2,417)	—	—	—	(34,072)	(36,489)
Cash dividends paid to shareholders	(1,638)	—	—	—	—	(1,638)
Other	136	(191)	*	—	25,438	25,383
Net cash provided by (used in) financing activities	8,119	(191)	*	—	53,316	61,244
Effect of exchange rate changes on cash	—	—	—	—	114	114
Change in cash	(114)	—	*	—	(193)	(307)
Cash at beginning of year	190	—	—	—	1,707	1,897
Cash at end of year	$ 76	$ —	$ *	$ —	$ 1,514	$ 1,590
Year Ended December 31, 2005						
Net cash provided by operating activities	$ 1,854	$ 805	$ *	$ —	$ 20,754	$ 23,413
Cash flows from investing:						
Invested assets disposed	—	—	—	—	185,884	185,884
Invested assets acquired	(598)	—	—	—	(245,804)	(246,402)
Other	(1,083)	(247)	*	—	389	(941)
Net cash used in investing activities	(1,681)	(247)	*	—	(59,531)	(61,459)
Cash flows from financing activities:						
Issuance of debt	2,101	—	—	—	64,960	67,061
Repayments of debt	(607)	(398)	—	—	(51,099)	(52,104)
Cash dividends paid to shareholders	(1,421)	—	—	—	—	(1,421)
Other	(73)	(160)	*	—	24,794	24,561
Net cash provided by (used in) financing activities	—	(558)	*	—	38,655	38,097
Effect of exchange rate changes on cash	—		—	—	(163)	(163)
Change in cash	173	—	*	—	(285)	(112)
Cash at beginning of year	17	—	—	—	1,992	2,009
Cash at end of year	$ 190	$ —	$ *	$ —	$ 1,707	$ 1,897

* *Less than $1 million.*

24. Cash Flows

As part of its ongoing remediation activities, AIG has made certain revisions to the Consolidated Statement of Cash Flows, primarily relating to the effect of reclassifying certain policyholders' account balances, the elimination of certain intercompany balances and revisions related to separate account assets. Accordingly, AIG revised the previous periods presented to conform to the revised presentation.

The revisions and their effect in the consolidated statement of cash flows for the years ended 2006 and 2005 are presented below:

	For the Years Ended December 31,	
(in millions)	2006	2005
Cash flows from operating activities — As previously reported	$ 6,829	$ 25,382
Revisions	(542)	(1,969)
Cash flows from operating activities — As revised	$ 6,287	$ 23,413
Cash flows from investing activities — As previously reported	$(67,040)	$(62,500)
Revisions	(912)	1,041
Cash flows from investing activities — As revised	$(67,952)	$(61,459)
Cash flows from financing activities — As previously reported	$ 59,790	$ 37,169
Revisions	1,454	928
Cash flows from financing activities — As revised	$ 61,244	$ 38,097

There was no effect on ending cash balances.

Part II – Other Information

Item 9.
Changes in and Disagreements With Accountants on Accounting and Financial Disclosure

None.

Item 9A.
Controls and Procedures

Evaluation of Disclosure Controls and Procedures

In connection with the preparation of this Annual Report on Form 10-K, an evaluation was carried out by AIG's management, with the participation of AIG's Chief Executive Officer and Chief Financial Officer, of the effectiveness of AIG's disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934 (Exchange Act)) as of December 31, 2007. Disclosure controls and procedures are designed to ensure that information required to be disclosed in reports filed or submitted under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in SEC rules and forms and that such information is accumulated and communicated to management, including the Chief Executive Officer and Chief Financial Officer, to allow timely decisions regarding required disclosures.

During the evaluation of disclosure controls and procedures as of December 31, 2007 conducted during the preparation of AIG's financial statements to be included in this Annual Report on Form 10-K, a material weakness in internal control over financial reporting relating to the fair value valuation of the AIGFP super senior credit default swap portfolio was identified. As a result of this material weakness, described more fully below, AIG's Chief Executive Officer and Chief Financial Officer concluded that, as of December 31, 2007, AIG's disclosure controls and procedures were ineffective.

As of December 31, 2007 and as described under Remediation of Prior Material Weaknesses in Internal Control Over Financial Reporting below, the material weakness relating to the controls over income tax accounting no longer existed.

Notwithstanding the existence of this material weakness in internal control over financial reporting relating to the fair value valuation of the AIGFP super senior credit default swap portfolio, AIG believes that the consolidated financial statements in this Annual Report on Form 10-K fairly present, in all material respects, AIG's consolidated financial condition as of December 31, 2007 and 2006, and consolidated results of its operations and cash flows for the years ended December 31, 2007, 2006 and 2005, in conformity with U.S. generally accepted accounting principles (GAAP).

Management's Report on Internal Control Over Financial Reporting

Management of AIG is responsible for establishing and maintaining adequate internal control over financial reporting. AIG's internal control over financial reporting is a process, under the supervision of AIG's Chief Executive Officer and Chief Financial Officer, designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of AIG's financial statements for external purposes in accordance with GAAP.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

AIG management conducted an assessment of the effectiveness of AIG's internal control over financial reporting as of December 31, 2007 based on the criteria established in *Internal Control — Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO).

A material weakness is a deficiency, or a combination of deficiencies, in internal control over financial reporting, such that there is a reasonable possibility that a material misstatement of AIG's annual or interim financial statements will not be prevented or detected on a timely basis. AIG management has concluded that, as of December 31, 2007, the following material weakness existed relating to the fair value valuation of the AIGFP super senior credit default swap portfolio.

As of December 31, 2007, controls over the AIGFP super senior credit default swap portfolio valuation process and oversight thereof were not effective. AIG had insufficient resources to design and carry out effective controls to prevent or detect errors and to determine appropriate disclosures on a timely basis with respect to the processes and models introduced in the fourth quarter of 2007. As a result, AIG had not fully developed its controls to assess, on a timely basis, the relevance to its valuation of all third party information. Also, controls to permit the appropriate oversight and monitoring of the AIGFP super senior credit default swap portfolio valuation process, including timely sharing of information at the appropriate levels of the organization, did not operate effectively. As a result, controls over the AIGFP super senior credit default swap portfolio valuation process and oversight thereof were not adequate to prevent or detect misstatements in the accuracy of management's fair value estimates and disclosures on a timely basis, resulting in adjustments for purposes of AIG's December 31, 2007 consolidated financial statements. In addition, this deficiency could result in a misstatement in management's fair value estimates or disclosures that could be material to AIG's annual or interim consolidated financial statements that would not be prevented or detected on a timely basis.

Solely as a result of the material weakness in internal control over the fair value valuation of the AIGFP super senior credit default swap portfolio described above, AIG management has concluded that, as of December 31, 2007, AIG's internal control over financial reporting was not effective based on the criteria in *Internal Control — Integrated Framework* issued by the COSO.

The effectiveness of AIG's internal control over financial reporting as of December 31, 2007 has been audited by PricewaterhouseCoopers LLP, an independent registered public

accounting firm, as stated in their report, which is included in this Annual Report on Form 10-K.

Remediation of Prior Material Weakness in Internal Control Over Financial Reporting

AIG has been actively engaged in the implementation of remediation efforts to address the material weakness in controls over income tax accounting that was in existence at December 31, 2006. These remediation efforts, outlined below, are specifically designed to address the material weakness identified by AIG management. As a result of its assessment of the effectiveness of internal control over financial reporting, AIG management determined that as of December 31, 2007, the material weakness relating to the controls over income tax accounting no longer existed.

AIG's remediation efforts were governed by a Steering Committee, under the direction of AIG's Chief Risk Officer and included AIG's Chief Executive Officer, Chief Financial Officer and Comptroller. The status of remediation was reviewed with the Audit Committee who was advised of issues encountered and key decisions reached by AIG management.

As of December 31, 2006, AIG did not maintain effective controls over the determination and reporting of certain components of the provision for income taxes and related income tax balances. Specifically, AIG did not maintain effective controls to review and monitor the accuracy of the components of the income tax provision calculations and related income tax balances and to monitor the differences between the income tax basis and the financial reporting basis of assets and liabilities to effectively reconcile the differences to the deferred income tax balances.

During 2007, AIG management took the following actions to remediate this material weakness:

- Implemented standard key controls to review and monitor the income tax provision and related income tax balances at applicable AIG business units globally and parent company, and conducted testing of these controls to verify their effectiveness,
- Completed the evaluation and reconciliation of certain historical balance sheet income tax accounts at applicable AIG business units globally and parent company, as well as a more detailed financial statement exposure analysis of income tax balances,
- Hired additional qualified staff, including Tax Directors and Tax Accountants, at designated business units globally and parent company, and
- Continued the development and dissemination of income tax accounting training and education programs at parent company and business unit levels through site visits and training conferences.

AIG continues to develop further enhancements to its controls over income tax accounting at certain business units. Based upon the significant actions taken and the testing and evaluation of the effectiveness of the controls, AIG management has concluded the material weakness in AIG's controls over income tax accounting no longer existed as of December 31, 2007.

Continuing Remediation

AIG is actively engaged in the development and implementation of a remediation plan to address the material weakness in controls over the fair value valuation of the AIGFP super senior credit default swap portfolio and oversight thereof as of December 31, 2007. The components of this remediation plan, once implemented, are intended to ensure that the key controls over the valuation process are operating effectively and are sustainable. These components include assigning dedicated and experienced resources at AIGFP with the responsibility for valuation, enhancing the technical resources at AIG over the valuation of the super senior credit default swap portfolio and strengthening corporate oversight over the valuation methodologies and processes. AIG management continues to assign the highest priority to AIG's remediation efforts in this area, with the goal of remediating this material weakness by year-end 2008.

AIG'S remediation efforts will be governed by a Steering Committee under the direction of AIG's Chief Risk Officer and also including AIG's Chief Executive Officer, Chief Financial Officer and Comptroller. The status of remediation of the material weakness will be reviewed with the Audit Committee and this Committee will be advised of issues encountered and key decisions reached by AIG management relating to the remediation efforts.

Notwithstanding the existence of this material weakness in internal control over financial reporting relating to the fair value valuation of the AIGFP super senior credit default swap portfolio, due to the substantive alternative procedures performed and compensating controls introduced after December 31, 2007, AIG believes that the consolidated financial statements fairly present, in all material respects, AIG's consolidated financial condition as of December 31, 2007 and 2006, and consolidated results of its operations and cash flows for the years ended December 31, 2007, 2006 and 2005, in conformity with GAAP.

AIG recognizes that continued improvement in its internal controls over financial reporting and consolidation processes, investment accounting, reinsurance accounting and income tax accounting, is necessary. Over time, AIG intends to reduce its reliance on certain manual controls that have been established. AIG is currently developing new systems and processes which will allow it to rely on front-end preventive and detective controls which will be more sustainable over the long term. To accomplish its goals, AIG recognizes its need to continue strengthening and investing in financial personnel, systems and processes. AIG is committed to continuing the significant investments over the next several years necessary to make these improvements.

Changes in Internal Control over Financial Reporting

Changes in AIG's internal control over financial reporting during the quarter ended December 31, 2007 that have materially affected, or are reasonably likely to materially affect, AIG's internal control over financial reporting have been described above.

Item 9B.
Other Information

None.

Part III

Item 10.
Directors, Executive Officers and Corporate Governance

Except for the information provided in Part I under the heading ''Directors and Executive Officers of AIG'', this item, including information regarding AIG's audit committee and audit committee financial expert, any material changes to the procedures by which security holders may recommend nominees to AIG's board of directors, if any, and information relating to AIG's code of ethics that applies to its directors, executive officers and senior financial officers, is omitted because a definitive proxy statement which involves the election of directors will be filed with the SEC not later than 120 days after the close of the fiscal year pursuant to Regulation 14A.

Item 11.
Executive Compensation

This item is omitted because a definitive proxy statement which involves the election of directors will be filed with the SEC not later than 120 days after the close of the fiscal year pursuant to Regulation 14A.

Item 12.
Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters

This item is omitted because a definitive proxy statement which involves the election of directors will be filed with the SEC not later than 120 days after the close of the fiscal year pursuant to Regulation 14A.

Item 13.
Certain Relationships and Related Transactions, and Director Independence

This item is omitted because a definitive proxy statement which involves the election of directors will be filed with the SEC not later than 120 days after the close of the fiscal year pursuant to Regulation 14A.

Item 14.
Principal Accountant Fees and Services

This item is omitted because a definitive proxy statement which involves the election of directors will be filed with the SEC not later than 120 days after the close of the fiscal year pursuant to Regulation 14A.

Part IV

Item 15.
Exhibits and Financial Statement Schedules

(a) Financial Statements and Schedules. See accompanying Index to Financial Statements.

(b) Exhibits. See accompanying Exhibit Index.

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, as amended, the Registrant has duly caused this Annual Report on Form 10-K to be signed on its behalf by the undersigned, thereunto duly authorized, in the City of New York and State of New York, on the 28th of February, 2008.

AMERICAN INTERNATIONAL GROUP, INC.

By /s/ MARTIN J. SULLIVAN
(Martin J. Sullivan, President and Chief Executive Officer)

KNOW ALL PERSONS BY THESE PRESENTS, that each person whose signature appears below constitutes and appoints Martin J. Sullivan and Steven J. Bensinger, and each of them severally, his or her true and lawful attorney-in-fact, with full power of substitution and resubstitution, to sign in his or her name, place and stead, in any and all capacities, to do any and all things and execute any and all instruments that such attorney may deem necessary or advisable under the Securities Exchange Act of 1934, as amended, and any rules, regulations and requirements of the U.S. Securities and Exchange Commission in connection with this Annual Report on Form 10-K and any and all amendments hereto, as fully for all intents and purposes as he or she might or could do in person, and hereby ratifies and confirms all said attorneys-in-fact and agents, each acting alone, and his or her substitute or substitutes, may lawfully do or cause to be done by virtue hereof.

Pursuant to the requirements of the Securities Exchange Act of 1934, as amended, this Annual Report on Form 10-K has been signed below by the following persons in the capacities indicated on the 28th of February, 2008.

Signature	Title
/s/ MARTIN J. SULLIVAN (Martin J. Sullivan)	President, Chief Executive Officer and Director (Principal Executive Officer)
/s/ STEVEN J. BENSINGER (Steven J. Bensinger)	Executive Vice President and Chief Financial Officer (Principal Financial Officer)
/s/ DAVID L. HERZOG (David L. Herzog)	Senior Vice President and Comptroller (Principal Accounting Officer)
/s/ STEPHEN F. BOLLENBACH (Stephen F. Bollenbach)	Director
/s/ MARSHALL A. COHEN (Marshall A. Cohen)	Director
/s/ MARTIN S. FELDSTEIN (Martin S. Feldstein)	Director
/s/ ELLEN V. FUTTER (Ellen V. Futter)	Director
/s/ STEPHEN L. HAMMERMAN (Stephen L. Hammerman)	Director
/s/ RICHARD C. HOLBROOKE (Richard C. Holbrooke)	Director

Signature	Title
/s/ Fred H. Langhammer (Fred H. Langhammer)	Director
/s/ George L. Miles, Jr. (George L. Miles, Jr.)	Director
/s/ Morris W. Offit (Morris W. Offit)	Director
/s/ James F. Orr III (James F. Orr III)	Director
/s/ Virginia M. Rometty (Virginia M. Rometty)	Director
/s/ Michael H. Sutton (Michael H. Sutton)	Director
/s/ Edmund S.W. Tse (Edmund S.W. Tse)	Director
/s/ Robert B. Willumstad (Robert B. Willumstad)	Director
/s/ Frank G. Zarb (Frank G. Zarb)	Director

EXHIBIT INDEX

Exhibit Number	Description	Location
2	Plan of acquisition, reorganization, arrangement, liquidation or succession	
	Agreement and Plan of Merger, dated as of May 11, 2001, among American International Group, Inc., Washington Acquisition Corporation and American General Corporation	Incorporated by reference to Exhibit 2.1(i)(a) to AIG's Registration Statement on Form S-4 (File No. 333-62688).
3(i)(a)	Restated Certificate of Incorporation of AIG	Incorporated by reference to Exhibit 3(i) to AIG's Annual Report on Form 10-K for the year ended December 31, 1996 (File No. 1-8787).
3(i)(b)	Certificate of Amendment of Certificate of Incorporation of AIG, filed June 3, 1998	Incorporated by reference to Exhibit 3(i) to AIG's Quarterly Report on Form 10-Q for the quarter ended June 30, 1998 (File No. 1-8787).
3(i)(c)	Certificate of Merger of SunAmerica Inc. with and into AIG, filed December 30, 1998 and effective January 1, 1999	Incorporated by reference to Exhibit 3(i) to AIG's Annual Report on Form 10-K for the year ended December 31, 1998 (File No. 1-8787).
3(i)(d)	Certificate of Amendment of Certificate of Incorporation of AIG, filed June 5, 2000	Incorporated by reference to Exhibit 3(i)(c) to AIG's Registration Statement on Form S-4 (File No. 333-45828).
3(ii)	Amended and Restated By-laws of AIG	Incorporated by reference to Exhibit 3(i) to AIG's Current Report on Form 8-K filed with the SEC on January 17, 2008 (File No. 1-8787).
4	Instruments defining the rights of security holders, including indentures	Certain instruments defining the rights of holders of long-term debt securities of AIG and its subsidiaries are omitted pursuant to Item 601(b)(4)(iii) of Regulation S-K. AIG hereby undertakes to furnish to the Commission, upon request, copies of any such instruments.
9	Voting Trust Agreement	None.
10	Material contracts*	
	(1) AIG 1969 Employee Stock Option Plan and Agreement Form	Filed as exhibit to AIG's Registration Statement (File No. 2-44043) and incorporated herein by reference.
	(2) AIG 1972 Employee Stock Option Plan	Filed as exhibit to AIG's Registration Statement (File No. 2-44702) and incorporated herein by reference.
	(3) AIG 1972 Employee Stock Purchase Plan	Filed as exhibit to AIG's Registration Statement (File No. 2-44043) and incorporated herein by reference.
	(4) AIG 1984 Employee Stock Purchase Plan	Filed as exhibit to AIG's Registration Statement (File No. 2-91945) and incorporated herein by reference.
	(5) AIG Amended and Restated 1996 Employee Stock Purchase Plan	Filed as exhibit to AIG's Definitive Proxy Statement dated April 4, 2003 (File No. 1-8787) and incorporated herein by reference.
	(6) AIG 2003 Japan Employee Stock Purchase Plan	Incorporated by reference to Exhibit 4 to AIG's Registration Statement on Form S-8 (File No. 333-111737).
	(7) AIG 1977 Stock Option and Stock Appreciation Rights Plan	Filed as exhibit to AIG's Registration Statement (File No. 2-59317) and incorporated herein by reference.
	(8) AIG 1982 Employee Stock Option Plan	Filed as exhibit to AIG's Registration Statement (File No. 2-78291) and incorporated herein by reference.
	(9) AIG 1987 Employee Stock Option Plan	Filed as exhibit to AIG's Definitive Proxy Statement dated April 6, 1987 (File No. 0-4652) and incorporated herein by reference.
	(10) AIG 1991 Employee Stock Option Plan	Filed as exhibit to AIG's Definitive Proxy Statement dated April 4, 1997 (File No. 1-8787) and incorporated herein by reference.

** All material contracts are management contracts or compensatory plans or arrangements, except items (66), (67), (68) and (69).*

Exhibit Number		Description	Location
	(11)	AIG Amended and Restated 1999 Stock Option Plan	Filed as exhibit to AIG's Definitive Proxy Statement dated April 4, 2003 (File No. 1-8787) and incorporated herein by reference.
	(12)	Form of Stock Option Grant Agreement under the AIG Amended and Restated 1999 Stock Option Plan	Incorporated by reference to Exhibit 10(a) to AIG's Quarterly Report on Form 10-Q for the quarter ended September 30, 2004 (File No. 1-8787).
	(13)	AIG Amended and Restated 2002 Stock Incentive Plan	Incorporated by reference to Exhibit 4(a) to AIG's Registration Statement on Form S-8 (File No. 333-101967).
	(14)	Form of Restricted Stock Unit Award Agreement under the AIG Amended and Restated 2002 Stock Incentive Plan	Incorporated by reference to Exhibit 10(b) to AIG's Quarterly Report on Form 10-Q for the quarter ended September 30, 2004 (File No. 1-8787).
	(15)	AIG Executive Deferred Compensation Plan	Incorporated by reference to Exhibit 4(a) to AIG's Registration Statement on Form S-8 (File No. 333-101640).
	(16)	AIG Supplemental Incentive Savings Plan	Incorporated by reference to Exhibit 4(b) to AIG's Registration Statement on Form S-8 (File No. 333-101640).
	(17)	AIG Director Stock Plan	Filed as an exhibit to AIG's Definitive Proxy Statement dated April 5, 2004 (File No. 1-8787) and incorporated herein by reference.
	(18)	AIG Chief Executive Officer Annual Compensation Plan	Filed as an exhibit to AIG's Definitive Proxy Statement dated April 5, 2004 (File No. 1-8787) and incorporated herein by reference.
	(19)	AIRCO 1972 Employee Stock Option Plan	Incorporated by reference to AIG's Joint Proxy Statement and Prospectus (File No. 2-61994).
	(20)	AIRCO 1977 Stock Option and Stock Appreciation Rights Plan	Incorporated by reference to AIG's Joint Proxy Statement and Prospectus (File No. 2-61994).
	(21)	Purchase Agreement between AIA and Mr. E.S.W. Tse	Incorporated by reference to Exhibit 10(l) to AIG's Annual Report on Form 10-K for the year ended December 31, 1997 (File No. 1-8787).
	(22)	Retention and Employment Agreement between AIG and Jay S. Wintrob	Incorporated by reference to Exhibit 10(m) to AIG's Annual Report on Form 10-K for the year ended December 31, 1998 (File No. 1-8787).
	(23)	SunAmerica Inc. 1988 Employee Stock Plan	Incorporated by reference to Exhibit 4(a) to AIG's Registration Statement on Form S-8 (File No. 333-70069).
	(24)	SunAmerica 1997 Employee Incentive Stock Plan	Incorporated by reference to Exhibit 4(b) to AIG's Registration Statement on Form S-8 (File No. 333-70069).
	(25)	SunAmerica Nonemployee Directors' Stock Option Plan	Incorporated by reference to Exhibit 4(c) to AIG's Registration Statement on Form S-8 (File No. 333-70069).
	(26)	SunAmerica 1995 Performance Stock Plan	Incorporated by reference to Exhibit 4(d) to AIG's Registration Statement on Form S-8 (File No. 333-70069).
	(27)	SunAmerica Inc. 1998 Long-Term Performance-Based Incentive Plan For the Chief Executive Officer	Incorporated by reference to Exhibit 4(e) to AIG's Registration Statement on Form S-8 (File No. 333-70069).
	(28)	SunAmerica Inc. Long-Term Performance-Based Incentive Plan Amended and Restated 1997	Incorporated by reference to Exhibit 4(f) to AIG's Registration Statement on Form S-8 (File No. 333-70069).
	(29)	SunAmerica Five Year Deferred Cash Plan	Incorporated by reference to Exhibit 4(a) to AIG's Registration Statement on Form S-8 (File No. 333-31346).
	(30)	SunAmerica Executive Savings Plan	Incorporated by reference to Exhibit 4(b) to AIG's Registration Statement on Form S-8 (File No. 333-31346).

Exhibit Number		Description	Location
	(31)	HSB Group, Inc. 1995 Stock Option Plan	Incorporated by reference to Exhibit 10(iii)(f) to HSB's Annual Report on Form 10-K for the year ended December 31, 1999 (File No. 1-13135).
	(32)	HSB Group, Inc. 1985 Stock Option Plan	Incorporated by reference to Exhibit 10(iii)(a) HSB's Quarterly Report on Form 10-Q for the quarter ended September 30, 1998 (File No. 1-13135).
	(33)	HSB Group, Inc. Employee's Thrift Incentive Plan	Incorporated by reference to Exhibit 4(i)(c) to The Hartford Steam Boiler Inspection and Insurance Company's Registration Statement on Form S-8 (File No. 33-36519).
	(34)	American General Corporation 1984 Stock and Incentive Plan	Incorporated by reference to Exhibit 10.1 to American General Corporation's Quarterly Report on Form 10-Q for the quarter ended June 30, 1998 (File No. 1-7981).
	(35)	Amendment to American General Corporation 1984 Stock and Incentive Plan (January 2000)	Incorporated by reference to Exhibit 10.2 to American General Corporation's Annual Report on Form 10-K for the year ended December 31, 1999 (File No. 1-7981).
	(36)	American General Corporation 1994 Stock and Incentive Plan (January 2000)	Incorporated by reference to Exhibit 10.2 to American General Corporation's Quarterly Report on Form 10-Q for the quarter ended June 30, 1998 (File No. 1-7981).
	(37)	Amendment to American General Corporation 1994 Stock and Incentive Plan (January 1999)	Incorporated by reference to Exhibit 10.4 to American General Corporation's Annual Report on Form 10-K for the year ended December 31, 1999 (File No. 1-7981).
	(38)	Amendment to American General Corporation 1994 Stock and Incentive Plan (January 2000)	Incorporated by reference to Exhibit 10.5 to American General Corporation's Annual Report on Form 10-K for the year ended December 31, 1999 (File No. 1-7981).
	(39)	Amendment to American General Corporation 1994 Stock and Incentive Plan (November 2000)	Incorporated by reference to Exhibit 10.1 to American General Corporation's Quarterly Report on Form 10-Q for the quarter ended September 30, 2000 (File No. 1-7981).
	(40)	American General Corporation 1997 Stock and Incentive Plan	Incorporated by reference to Exhibit 10.3 to American General Corporation's Quarterly Report on Form 10-Q for the quarter ended June 30, 1998 (File No. 1-7981).
	(41)	Amendment to American General Corporation 1997 Stock and Incentive Plan (January 1999)	Incorporated by reference to Exhibit 10.7 to American General Corporation's Annual Report on Form 10-K for the year ended December 31, 1999 (File No. 1-7981).
	(42)	Amendment to American General Corporation 1997 Stock and Incentive Plan (November 2000)	Incorporated by reference to Exhibit 10.2 to American General Corporation's Quarterly Report on Form 10-Q for the quarter ended September 30, 2000 (File No. 1-7981).
	(43)	American General Corporation 1999 Stock and Incentive Plan	Incorporated by reference to Exhibit 10.4 to American General Corporation's Annual Report on Form 10-K for the year ended December 31, 1998 (File No. 1-7981).
	(44)	Amendment to American General Corporation 1999 Stock and Incentive Plan (January 1999)	Incorporated by reference to Exhibit 10.9 to American General Corporation's Annual Report on Form 10-K for the year ended December 31, 1999 (File No. 1-7981).
	(45)	Amendment to American General Corporation 1999 Stock and Incentive Plan (November 2000)	Incorporated by reference to Exhibit 10.3 to American General Corporation's Quarterly Report on Form 10-Q for the quarter ended September 30, 2000 (File No. 1-7981).
	(46)	Amended and Restated American General Corporation Deferred Compensation Plan (12/11/00)	Incorporated by reference to Exhibit 10.13 to American General Corporation's Annual Report on Form 10-K for the year ended December 31, 2000 (File No. 1-7981).

Exhibit Number	Description	Location
(47)	Amended and Restated Restoration of Retirement Income Plan for Certain Employees Participating in the Restated American General Retirement Plan (Restoration of Retirement Income Plan) (12/31/98)	Incorporated by reference to Exhibit 10.14 to American General Corporation's Annual Report on Form 10-K for the year ended December 31, 2000 (File No. 1-7981).
(48)	Amended and Restated American General Supplemental Thrift Plan (12/31/98)	Incorporated by reference to Exhibit 10.15 to American General Corporation's Annual Report on Form 10-K for the year ended December 31, 2000 (File No. 1-7981).
(49)	American General Employees' Thrift and Incentive Plan (restated July 1, 2001)	Incorporated by reference to Exhibit 4(a) to AIG's Registration Statement on Form S-8 (File No. 333-68640).
(50)	American General Agents' and Managers' Thrift and Incentive Plan (restated July 1, 2001)	Incorporated by reference to Exhibit 4(b) to AIG's Registration Statement on Form S-8 (File No. 333-68640).
(51)	CommLoCo Thrift Plan (restated July 1, 2001)	Incorporated by reference to Exhibit 4(c) to AIG's Registration Statement on Form S-8 (File No. 333-68640).
(52)	Western National Corporation 1993 Stock and Incentive Plan, as amended	Incorporated by reference to Exhibit 10.18 to Western National Corporation's Annual Report on Form 10-K for the year ended December 31, 1995 (File No. 1-12540).
(53)	USLIFE Corporation 1991 Stock Option Plan, as amended	Incorporated by reference to USLIFE Corporation's Quarterly Report on Form 10-Q for the quarter ended September 30, 1995 (File No. 1-5683).
(54)	Employment Agreement, Amendment to Employment Agreement, and Split-Dollar Agreement, including Assignment of Life Insurance Policy as Collateral, with Rodney O. Martin, Jr.	Incorporated by reference to Exhibit 10(xx) to AIG's Annual Report on Form 10-K for the year ended December 31, 2002 (File No. 1-8787).
(55)	Employment Arrangements with Richard W. Scott	
	(a) Employment Agreement	Incorporated by reference to Exhibit 10.3 to American General Corporation's Quarterly Report on Form 10-Q for the quarter ended March 31, 2000 (File No. 1-7981).
	(b) Change in Control Severance Agreement	Incorporated by reference to Exhibit 10.32 to American General Corporation's Annual Report on Form 10-K for the year ended December 31, 1999 (File No. 1-7981).
	(c) Amendment to Employment Arrangements	Incorporated by reference to Exhibit 10(zz)(iii) to AIG's Annual Report on Form 10-K for the year ended December 31, 2003 (File No. 1-8787).
(56)	Letter from AIG to Martin J. Sullivan, dated March 16, 2005	Incorporated by reference to Exhibit 10.1 to AIG's Current Report on Form 8-K filed with the SEC on March 17, 2005 (File No. 1-8787).
(57)	Letter from AIG to Steven J. Bensinger, dated March 16, 2005	Incorporated by reference to Exhibit 10.3 to AIG's Current Report on Form 8-K filed with the SEC on March 17, 2005 (File No. 1-8787).
(58)	Employment Agreement between AIG and Martin J. Sullivan, dated as of June 27, 2005	Incorporated by reference to Exhibit 10(1) to AIG's Quarterly Report on Form 10-Q for the quarter ended March 31, 2005 (File No. 1-8787).
(59)	Employment Agreement between AIG and Steven J. Bensinger, dated as of June 27, 2005	Incorporated by reference to Exhibit 10(3) to AIG's Quarterly Report on Form 10-Q for the quarter ended March 31, 2005 (File No. 1-8787).
(60)	Executive Severance Plan, effective as of June 27, 2005	Incorporated by reference to Exhibit 10(4) to AIG's Quarterly Report on Form 10-Q for the quarter ended March 31, 2005 (File No. 1-8787).

Exhibit Number		Description	Location
	(61)	Assurance Agreement, by AIG in favor of eligible employees, dated as of June 27, 2005, relating to certain obligations of Starr International Company, Inc.	Incorporated by reference to Exhibit 10(6) to AIG's Quarterly Report on Form 10-Q for the quarter ended March 31, 2005 (File No. 1-8787).
	(62)	2005/2006 Deferred Compensation Profit Participation Plan	Incorporated by reference to Exhibit 10.1 to AIG's Current Report on Form 8-K filed with the SEC on September 26, 2005 (File No. 1-8787).
	(63)	Summary of Director Compensation	Incorporated by reference to Exhibit 10.1 to AIG's Quarterly Report on Form 10-Q filed with the SEC on August 8, 2007 (File No. 1-8787).
	(64)	AIG 2005 Senior Partners Plan	Incorporated by reference to Exhibit 10.1 to AIG's Current Report on Form 8-K filed with the SEC on December 20, 2005 (File No. 1-8787).
	(65)	AIG Special Restricted Stock Unit Award Agreement with Steven J. Bensinger, dated January 6, 2006	Incorporated by reference to Exhibit 10.1 to AIG's Current Report on Form 8-K filed with the SEC on January 9, 2006 (File No. 1-8787).
	(66)	Agreement with the United States Department of Justice, dated February 7, 2006	Incorporated by reference to Exhibit 10.1 to AIG's Current Report on Form 8-K filed with the SEC on February 9, 2006 (File No. 1-8787).
	(67)	Final Judgment and Consent with the Securities and Exchange Commission, including the related complaint, dated February 9, 2006	Incorporated by reference to Exhibit 10.2 to AIG's Current Report on Form 8-K filed with the SEC on February 9, 2006 (File No. 1-8787).
	(68)	Agreement between the Attorney General of the State of New York and AIG and its Subsidiaries, dated January 18, 2006	Incorporated by reference to Exhibit 10.3 to AIG's Current Report on Form 8-K filed with the SEC on February 9, 2006 (File No. 1-8787).
	(69)	Stipulation with the State of New York Insurance Department, dated January 18, 2006	Incorporated by reference to Exhibit 10.4 to AIG's Current Report on Form 8-K filed with the SEC on February 9, 2006 (File No. 1-8787).
	(70)	AIG Senior Partners Plan (amended and restated)	Incorporated by reference to Exhibit 10.1 to AIG's Current Report on Form 8-K filed with the SEC on July 21, 2006 (File No. 1-8787).
	(71)	AIG Partners Plan	Incorporated by reference to Exhibit 10.2 to AIG's Current Report on Form 8-K filed with the SEC on May 22, 2006 (File No. 1-8787).
	(72)	AIG Executive Incentive Plan	Incorporated by reference to Exhibit 10.1 to AIG's Current Report on Form 8-K filed with the SEC on May 22, 2006 (File No. 1-8787).
	(73)	AIG Amended and Restated 2007 Stock Incentive Plan	Incorporated by reference to Exhibit 4 to AIG's Registration Statement on Form S-8 (File No. 333-148148).
	(74)	AIG Form of Stock Option Award Agreement	Incorporated by reference to Exhibit 10.A to AIG's Registration Statement on Form S-8 (File No. 333-148148).
	(75)	AIG Form of Performance RSU Award Agreement	Incorporated by reference to Exhibit 10.B to AIG's Registration Statement on Form S-8 (File No. 333-148148).
	(76)	AIG Form of Time-Vested RSU Award Agreement	Incorporated by reference to Exhibit 10.C to AIG's Registration Statement on Form S-8 (File No. 333-148148).
	(77)	AIG Form of Time-Vested RSU Award Agreement with Four-Year Pro Rata Vesting	Incorporated by reference to Exhibit 10.D to AIG's Registration Statement on Form S-8 (File No. 333-148148).
	(78)	AIG Form of Time-Vested RSU Award Agreement with Three-Year Pro Rata Vesting	Incorporated by reference to Exhibit 10.E to AIG's Registration Statement on Form S-8 (File No. 333-148148).
	(79)	AIG Form of Non-Employee Director Deferred Stock Units Award Agreement	Incorporated by reference to Exhibit 10.F to AIG's Registration Statement on Form S-8 (File No. 333-148148).
11		Statement re computation of per share earnings	Included in Note 14 to Consolidated Financial Statements.

Exhibit Number	Description	Location
12	Computation of Ratios of Earnings to Fixed Charges	Filed herewith.
13	Annual report to security holders	Not required to be filed.
18	Letter re change in accounting principles	None.
21	Subsidiaries of Registrant	Filed herewith.
23	Consent of PricewaterhouseCoopers LLP	Filed herewith.
24	Power of attorney	Included on the signature page hereof.
31	Rule 13a-14(a)/15d-14(a) Certifications	Filed herewith.
32	Section 1350 Certifications	Filed herewith.
99	Additional exhibits	None.

Summary of Investments — Other than Investments in Related Parties

Schedule I

At December 31, 2007 *(in millions)*	Cost*	Fair Value	Amount at which shown in the Balance Sheet
Fixed maturities:			
U.S. government and government-sponsored entities	$ 4,291	$ 4,492	$ 4,492
Obligations of states, municipalities and political subdivisions	67,414	68,770	68,182
Non U.S. governments	67,373	70,510	70,514
Public utilities	8,581	8,743	8,743
All other corporate	277,162	276,996	277,004
Total fixed maturities	424,821	429,511	428,935
Equity securities and mutual funds:			
Common stocks:			
Public utilities	443	562	562
Banks, trust and insurance companies	1,920	3,725	3,725
Industrial, miscellaneous and all other	8,909	12,045	12,045
Total common stocks	11,272	16,332	16,332
Preferred stocks	2,599	2,370	2,370
Mutual Funds	21,012	22,944	22,944
Total equity securities and mutual funds	34,883	41,646	41,646
Mortgage and other loans receivable	33,727	34,123	33,727
Financial services assets:			
Securities available for sale, at fair value	40,157	40,305	40,305
Trading securities, at fair value	—	4,197	4,197
Spot commodities	—	238	238
Unrealized gain on swaps, options and forward transactions	—	16,442	16,442
Trade receivables	6,467	6,467	6,467
Securities purchased under agreements to resell, at contract value	20,950	20,950	20,950
Finance receivables, net of allowance	31,234	28,693	31,234
Securities lending invested collateral, at fair value	80,641	75,662	75,662
Other invested assets	57,000	59,668	58,823
Short-term investments, at cost (approximates fair value)	51,351	51,351	51,351
Total investments	—	—	$809,977

* *Original cost of equity securities and fixed maturities are reduced by other-than-temporary impairment charges, and, as to fixed maturities, reduced by repayments and adjusted for amortization of premiums or accrual of discounts.*

Condensed Financial Information of Registrant
Balance Sheet — Parent Company Only

Schedule II

December 31, *(in millions)*	**2007**	2006
Assets:		
Cash	**$ 84**	$ 76
Invested assets	**14,648**	7,346
Carrying value of subsidiaries and partially owned companies, at equity	**111,714**	109,125
Premiums and insurance balances receivable — net	**311**	222
Other assets	**9,103**	3,767
Total assets	**135,860**	120,536
Liabilities:		
Insurance balances payable	**43**	21
Due to affiliates — net	**3,916**	1,841
Notes and bonds payable	**20,397**	8,917
Loans payable	**500**	700
AIG MIP matched notes and bonds payable	**14,274**	5,468
Series AIGFP matched notes and bonds payable	**874**	72
Other liabilities	**55**	1,840
Total liabilities	**40,059**	18,859
Shareholders' equity:		
Common stock	**6,878**	6,878
Additional paid-in capital	**1,936**	2,590
Retained earnings	**89,029**	84,996
Accumulated other comprehensive income	**4,643**	9,110
Treasury stock	**(6,685)**	(1,897)
Total shareholders' equity	**95,801**	101,677
Total liabilities and shareholders' equity	**$135,860**	$120,536

See Accompanying Notes to Financial Statements — Parent Company Only.

Statement of Income — Parent Company Only

Years Ended December 31, *(in millions)*	**2007**	2006	2005
Agency income (loss)	**$ 10**	$ 9	$ 3
Financial services income	**69**	531	507
Asset management income (loss)	**99**	34	(3)
Cash dividend income from consolidated subsidiaries	**4,685**	1,689	1,958
Dividend income from partially-owned companies	**9**	11	127
Equity in undistributed net income of consolidated subsidiaries and partially owned companies	**3,121**	13,308	10,156
Other expenses, net	**(2,566)**	(1,371)	(2,203)
Cumulative effect of an accounting change	**—**	34	—
Income before income taxes	**5,427**	14,245	10,545
Income taxes (benefits)	**(773)**	197	68
Net income	**$ 6,200**	$14,048	$10,477

See Accompanying Notes to Financial Statements — Parent Company Only.

Condensed Financial Information of Registrant *Continued*
Statement of Cash Flows — Parent Company Only

Schedule II

Years Ended December 31, *(in millions)*	**2007**	2006	2005
Cash flows from operating activities:			
Net income	**$ 6,200**	$ 14,048	$ 10,477
Adjustments to reconcile net income to net cash provided by operating activities:			
Noncash revenues, expenses, gains and losses included in income:			
Equity in undistributed net income of consolidated subsidiaries and partially owned companies	**(9,941)**	(13,308)	(10,156)
Foreign exchange transaction (gains) losses	**333**	232	—
Changes in operating assets and liabilities:			
Change in premiums and insurance balances receivable and payable	**(44)**	(423)	15
Loan receivables held for sale — purchases	**(404)**	—	—
Sales of loan receivables — held for sale	**40**	—	—
Other, net	**3,046**	(1,139)	1,518
Total adjustments	**(6,970)**	(14,638)	(8,623)
Net cash provided by (used in) operating activities	**(770)**	(590)	1,854
Cash flows from investing activities:			
Purchase of investments	**(7,640)**	(7,875)	—
Sale of investments	**3,057**	3,402	—
Change in short-term investments	**(3,631)**	414	(598)
Contributions to subsidiaries and investments in partially owned companies	**(755)**	(3,017)	(966)
Mortgage and other loan receivables — originations and purchases	**(2,026)**	(423)	—
Payments received on mortgages and other loan receivables	**498**	15	—
Other, net	**(240)**	(159)	(117)
Net cash used in investing activities	**(10,737)**	(7,643)	(1,681)
Cash flows from financing activities:			
Notes, bonds and loans issued	**20,582**	12,038	2,101
Repayments of notes, bonds and loans	**(1,253)**	(2,417)	(607)
Issuance of treasury stock	**217**	163	82
Cash dividends paid to shareholders	**(1,881)**	(1,638)	(1,421)
Payments advanced to purchase shares	**(6,000)**	—	—
Acquisition of treasury stock	**(16)**	(20)	(176)
Other, net	**(134)**	(7)	21
Net cash (used in) provided by financing activities	**11,515**	8,119	—
Change in cash	**8**	(114)	173
Cash at beginning of year	**76**	190	17
Cash at end of year	**$ 84**	$ 76	$ 190

NOTES TO FINANCIAL STATEMENTS — PARENT COMPANY ONLY

(1) Agency operations conducted in New York through the North American Division of AIU are included in the financial statements of the parent company.

(2) Certain prior period amounts have been reclassified to conform to the current period presentation.

(3) ''Equity in undistributed net income of consolidated subsidiaries and partially owned companies'' in the accompanying Statement of Income — Parent Company Only — includes equity in income of the minority-owned insurance operations.

Supplementary Insurance Information

Schedule III

At December 31, 2007, 2006 and 2005 and for the years then ended

Segment *(in millions)*	Deferred Policy Acquisition Costs	Reserves for Losses and Loss Expenses, Future Policy Benefits[(a)]	Reserve for Unearned Premiums	Policy and Contract Claims[(b)]	Premiums and Other Considerations Revenue	Net Investment Income	Losses and Loss Expenses Incurred, Benefits	Amortization of Deferred Policy Acquisition Costs	Other Operating Expenses	Net Premiums Written
2007										
General Insurance	**$ 4,643**	**$ 85,500**	**$28,022**	**$ —**	**$45,682**	**$ 6,132**	**$29,982**	**$ 8,235**	**$2,965**	**$47,067**
Life Insurance & Retirement Services	**38,445**	**136,068**	**—**	**3,123**	**33,627**	**22,341**	**36,188**	**3,367**	**5,829**	**—**
Other	**62**	**—**	**—**	**—**	**(4)**	**(11)**	**(55)**	**—**	**—**	**—**
	$43,150	**$221,568**	**$28,022**	**$3,123**	**$79,305**	**$28,462**	**$66,115**	**$11,602**	**$8,794**	**$47,067**
2006										
General Insurance	$ 4,355	$ 79,999	$26,271	$ —	$43,451	$ 5,696	$28,052	$ 7,866	$2,876	$44,866
Life Insurance & Retirement Services	32,810	121,004	—	2,788	30,766	20,024	32,086	3,712	4,959	—
Other	70	—	—	—	(4)	350	149	—	—	—
	$37,235	$201,003	$26,271	$2,788	$74,213	$26,070	$60,287	$11,578	$7,835	$44,866
2005										
General Insurance	$ 4,048	$ 77,169	$24,243	$ —	$40,809	$ 4,031	$33,091	$ 7,365	$2,403	$41,872
Life Insurance & Retirement Services	28,106	107,825	—	2,473	29,501	18,677	31,009	3,328	4,718	—
Other	—	—	—	—	—	(124)	—	—	—	—
	$32,154	$184,994	$24,243	$2,473	$70,310	$22,584	$64,100	$10,693	$7,121	$41,872

(a) Reserves for losses and loss expenses with respect to the General Insurance operations are net of discounts of $2.43 billion, $2.26 billion and $2.11 billion at December 31, 2007, 2006 and 2005, respectively.

(b) Reflected in insurance balances payable on the accompanying consolidated balance sheet.

Reinsurance

Schedule IV

At December 31, 2007, 2006 and 2005 and for the years then ended

(dollars in millions)	Gross Amount	Ceded to Other Companies	Assumed from Other Companies	Net Amount	Percent of Amount Assumed to Net
2007					
Life Insurance in-force	**$2,311,022**	**$402,654**	**$ 1,023**	**$1,909,391**	**0.1%**
Premiums:					
General Insurance	**$ 52,055**	**$ 11,731**	**$ 6,743**	**$ 47,067**	**14.3%**
Life Insurance & Retirement Services	**34,555**	**1,778**	**30**	**32,807***	**0.1**
Total premiums	**$ 86,610**	**$ 13,509**	**$ 6,773**	**$ 79,874**	**8.5%**
2006					
Life Insurance in-force	$2,069,617	$408,970	$ 983	$1,661,630	0.1%
Premiums:					
General Insurance	$ 49,609	$ 11,414	$ 6,671	$ 44,866	14.9%
Life Insurance & Retirement Services	32,227	1,481	20	30,766*	0.1
Total premiums	$ 81,836	$ 12,895	$ 6,691	$ 75,632	8.8%
2005					
Life Insurance in-force	$1,838,337	$365,082	$14,496	$1,487,751	1.0%
Premiums:					
General Insurance	$ 46,689	$ 10,853	$ 6,036	$ 41,872	14.4%
Life Insurance & Retirement Services	30,738	1,317	80	29,501*	0.3
Total premiums	$ 77,427	$ 12,170	$ 6,116	$ 71,373	8.6%

** Includes accident and health premiums of $6.76 billion, $7.11 billion and $6.51 billion in 2007, 2006 and 2005, respectively.*

Valuation and Qualifying Accounts

Schedule V

For the years ended December 31, 2007, 2006 and 2005

(in millions)	Balance, Beginning of Year	Additions: Charged to Costs and Expenses	Additions: Charge offs	Other Changes[(a)]	Balance, End of Year
2007					
Allowance for mortgage and other loans receivable	**$ 64**	**$ 22**	**$ (7)**	**$ (2)**	**$ 77**
Allowance for finance receivables	**737**	**646**	**(632)**	**127**	**878**
Allowance for premiums and insurances balances receivable	**756**	**114**	**(216)**	**8**	**662**
Allowance for reinsurance assets	**536**	**131**	**(62)**	**(85)**	**520**
Overhaul reserve[(b)]	**245**	**290**	**—**	**(163)**	**372**
2006					
Allowance for mortgage and other loans receivable	$ 64	$ 17	$ (11)	$ (6)	$ 64
Allowance for finance receivables	670	495	(534)	106	737
Allowance for premiums and insurances balances receivable	871	240	(481)	126	756
Allowance for reinsurance assets	999	147	(381)	(229)	536
Overhaul reserve[(b)]	127	264	—	(146)	245
2005					
Allowance for mortgage and other loans receivable	$ 83	$ 1	$ (26)	$ 6	$ 64
Allowance for finance receivables	571	435	(414)	78	670
Allowance for premiums and insurances balances receivable	561	418	(104)	(4)	871
Allowance for reinsurance assets	846	185	(49)	17	999
Overhaul reserve[(b)]	68	245	—	(186)	127

(a) Includes recoveries of amounts previously charged off and reclassifications to/from other accounts.

(b) Amounts for Overhaul reserve represent reimbursements to lessees for overhauls performed and amounts transferred to buyers for aircraft sold and is included in Other liabilities in the consolidated balance sheet.

Computation of Ratios of Earnings to Fixed Charges

Exhibit 12

Years Ended December 31, *(in millions, except ratios)*	**2007**	2006	2005	2004	2003
Income before income taxes, minority interest and cumulative effect of accounting changes	**$ 8,943**	$21,687	$15,213	$14,845	$11,907
Less — Equity income of less than 50% owned companies	**160**	188	(129)	164	146
Add — Dividends from less than 50% owned companies	**30**	28	146	22	13
	8,813	21,527	15,488	14,703	11,774
Add — Fixed charges	**11,470**	9,062	7,663	6,049	5,762
Less — Capitalized interest	**37**	59	64	59	52
Income before income taxes, minority interest, cumulative effect of accounting changes and fixed charges	**$20,246**	$30,530	$23,087	$20,693	$17,484
Fixed charges:					
Interest costs	**$11,213**	$ 8,843	$ 7,464	$ 5,860	$ 5,588
Rental expense*	**257**	219	199	189	174
Total fixed charges	**$11,470**	$ 9,062	$ 7,663	$ 6,049	$ 5,762
Ratio of earnings to fixed charges	**1.77**	3.37	3.01	3.42	3.03
Secondary Ratio					
Interest credited to GIC and GIA policy and contract holders	**$ (6,660)**	$ (5,128)	$ (4,760)	$ (3,674)	$ (3,578)
Total fixed charges excluding interest credited to GIC and GIA policy and contract holders	**$ 4,810**	$ 3,934	$ 2,903	$ 2,375	$ 2,184
Secondary ratio of earnings to fixed charges	**2.82**	6.46	6.31	7.17	6.37

** The proportion deemed representative of the interest factor.*

The secondary ratio is disclosed for the convenience of fixed income investors and the rating agencies that serve them and is more comparable to the ratios disclosed by all issuers of fixed income securities. The secondary ratio removes interest credited to guaranteed investment contract (GIC) policyholders and guaranteed investment agreement (GIA) contractholders. Such interest expenses are also removed from earnings used in this calculation. GICs and GIAs are entered into by AIG's insurance subsidiaries, principally SunAmerica Life Insurance Company and AIG Financial Products Corp. and its subsidiaries, respectively. The proceeds from GICs and GIAs are invested in a diversified portfolio of securities, primarily investment grade bonds. The assets acquired yield rates greater than the rates on the related policyholders obligation or contract, with the intent of earning a profit from the spread.

Subsidiaries of Registrant

Exhibit 21

As of December 31, 2007	Jurisdiction of Incorporation or Organization	Percentage of Voting Securities held by Immediate Parent[1]
American International Group, Inc.[(2)]	Delaware	[(3)]
AIG Capital Corporation	Delaware	100
AIG Capital India Private Limited	India	99.99[(4)]
AIG Global Asset Management Company (India) Private Limited	India	99[(5)]
AIG Consumer Finance Group, Inc.	Delaware	100
AIG Bank Polska S.A.	Poland	99.92
AIG Credit SA	Poland	100
Compania Financiera Argentina S.A.	Argentina	100
AIG Credit Corp.	Delaware	100
A.I. Credit Consumer Discount Company	Pennsylvania	100
A.I. Credit Corp.	New Hampshire	100
AICCO, Inc.	Delaware	100
AICCO, Inc.	California	100
AIG Credit Corp. of Canada	Canada	100
Imperial Premium Funding, Inc.	Delaware	100
AIG Equipment Finance Holdings, Inc.	Delaware	100
AIG Commercial Equipment Finance, Inc.	Delaware	100
AIG Commercial Equipment Finance Company, Canada	Canada	100
AIG Rail Services, Inc.	Delaware	100
AIG Finance Holdings, Inc.	New York	100
AIG Finance (Hong Kong) Limited	Hong Kong	100
American General Finance, Inc.	Indiana	100
American General Auto Finance, Inc.	Delaware	100
American General Finance Corporation	Indiana	100
Merit Life Insurance Co.	Indiana	100
MorEquity, Inc.	Nevada	100
Wilmington Finance, Inc.	Delaware	100
Ocean Finance and Mortgages Limited	England	100
Yosemite Insurance Company	Indiana	100
CommoLoCo, Inc.	Puerto Rico	100
American General Financial Services of Alabama, Inc.	Delaware	100
AIG Global Asset Management Holdings Corp.	Delaware	100
AIG Asset Management Services, Inc.	Delaware	100
AIG Capital Partners, Inc.	Delaware	100
AIG Equity Sales Corp.	New York	100
AIG Global Investment Corp.	New Jersey	100
AIG Global Real Estate Investment Corp.	Delaware	100
AIG Securities Lending Corp.	Delaware	100
Brazos Capital Management, L.P.	Delaware	100
International Lease Finance Corporation	California	67.23[(6)]
AIG Egypt Insurance Company S.A.E.	Egypt	90.05[(7)]
AIG Federal Savings Bank	USA	100
AIG Financial Advisor Services, Inc.	Delaware	100
AIG Global Investment (Luxembourg) S.A.	Luxembourg	100
AIG Financial Products Corp.	Delaware	100
AIG Matched Funding Corp.	Delaware	100
Banque AIG	France	90[(8)]
AIG Funding, Inc.	Delaware	100
AIG Global Trade & Political Risk Insurance Company	New Jersey	100
AIG Israel Insurance Company Ltd.	Israel	50.01
AIG Kazakhstan Insurance Company	Kazakhstan	60

Subsidiaries of Registrant *Continued*

As of December 31, 2007	Jurisdiction of Incorporation or Organization	Percentage of Voting Securities held by Immediate Parent[1]
AIG Life Holdings (International) LLC	Delaware	100
AIG Star Life Insurance Co., Ltd.	Japan	100
American International Reinsurance Company, Ltd.	Bermuda	100
AIG Edison Life Insurance Company	Japan	90[(9)]
American International Assurance Company, Limited	Hong Kong	100
American International Assurance Company (Australia) Limited	Australia	100
American International Assurance Company (Bermuda) Limited	Bermuda	100
American International Assurance Co. (Vietnam) Limited	Vietnam	100
Tata AIG Life Insurance Company Limited	India	26
Nan Shan Life Insurance Company, Ltd.	Taiwan	95.27
AIG Life Holdings (US), Inc.	Texas	100
AGC Life Insurance Company	Missouri	100
AIG Annuity Insurance Company	Texas	100
AIG Life Holdings (Canada), ULC	Canada	100
AIG Assurance Canada	Canada	100
AIG Life Insurance Company of Canada	Canada	100
AIG Life of Bermuda, Ltd.	Bermuda	100
AIG Life Insurance Company	Delaware	100
American General Life and Accident Insurance Company	Tennessee	100
Volunteer Vermont Holdings, LLC	Vermont	100
Volunteer Vermont Reinsurance Company	Vermont	100
American General Life Insurance Company	Texas	100
AIG Enterprise Services, LLC	Delaware	100
American General Annuity Service Corporation	Texas	100
American General Life Companies, LLC	Delaware	100
The Variable Annuity Life Insurance Company	Texas	100
AIG Retirement Services Company	Texas	100
American International Life Assurance Company of New York	New York	100
American General Bancassurance Services, Inc.	Illinois	100
American General Property Insurance Company	Tennessee	51.85[(10)]
American General Property Insurance Company of Florida	Florida	100
The United States Life Insurance Company in the City of New York	New York	100
American General Assurance Company	Illinois	100
American General Indemnity Company	Illinois	100
American General Investment Management Corporation	Delaware	100
American General Realty Investment Corporation	Texas	100
Knickerbocker Corporation	Texas	100
AIG Life Insurance Company of Puerto Rico	Puerto Rico	100
AIG Life Insurance Company (Switzerland) Ltd.	Switzerland	100
AIG Liquidity Corp.	Delaware	100
AIG Privat Bank AG	Switzerland	100
AIG Property Casualty Group, Inc.	Delaware	100
AIG Commercial Insurance Group, Inc.	Delaware	100
AIG Aviation, Inc.	Georgia	100
AIG Casualty Company	Pennsylvania	100
AIG Risk Management, Inc.	New York	100
AIU Insurance Company	New York	52[(11)]
AIG General Insurance Company China Limited	China	100
AIG General Insurance (Taiwan) Co., Ltd.	Taiwan	100

Subsidiaries of Registrant *Continued*

As of December 31, 2007	Jurisdiction of Incorporation or Organization	Percentage of Voting Securities held by Immediate Parent[1]
American Home Assurance Company	New York	100
AIG General Insurance (Malaysia) Berhad	Malaysia	100
AIG Hawaii Insurance Company, Inc.	Hawaii	100
American Pacific Insurance Company, Inc.	Hawaii	100
American International Realty Corp.	Delaware	31.5[(12)]
Pine Street Real Estate Holdings Corp.	New Hampshire	31.47[(13)]
Transatlantic Holdings, Inc.	Delaware	33.24[(14)]
Transatlantic Reinsurance Company	New York	100
Putnam Reinsurance Company	New York	100
Trans Re Zurich	Switzerland	100
American International Surplus Lines Agency, Inc.	New Jersey	100
Audubon Insurance Company	Louisiana	100
Agency Management Corporation	Louisiana	100
The Gulf Agency, Inc.	Alabama	100
Audubon Indemnity Company	Mississippi	100
Commerce and Industry Insurance Company	New York	100
American International Insurance Company	New York	50[(15)]
AIG Advantage Insurance Company	Minnesota	100
American International Insurance Company of California, Inc.	California	100
American International Insurance Company of New Jersey	New Jersey	100
Commerce and Industry Insurance Company of Canada	Canada	100
The Insurance Company of the State of Pennsylvania	Pennsylvania	100
Landmark Insurance Company	California	100
National Union Fire Insurance Company of Pittsburgh, Pa	Pennsylvania	100
AIG Domestic Claims, Inc.	Delaware	100
American International Specialty Lines Insurance Company	Illinois	70[(16)]
Lexington Insurance Company	Delaware	70[(17)]
AIG Centennial Insurance Company	Pennsylvania	100
AIG Auto Insurance Company of New Jersey	New Jersey	100
AIG Preferred Insurance Company	Pennsylvania	100
AIG Premier Insurance Company	Pennsylvania	100
AIG Indemnity Insurance Company	Pennsylvania	100
JI Accident & Fire Insurance Company, Ltd.	Japan	50
National Union Fire Insurance Company of Louisiana	Louisiana	100
National Union Fire Insurance Company of Vermont	Vermont	100
21st Century Insurance Group	Delaware	32[(18)]
21st Century Casualty Company	California	100
21st Century Insurance Company	California	100
21st Century Insurance Company of the Southwest	Texas	100
AIG Excess Liability Insurance Company Ltd.	Delaware	100
AIG Excess Liability Insurance International Limited	Ireland	100
New Hampshire Insurance Company	Pennsylvania	100
AI Network Corporation	Delaware	100
AIG Europe, S.A.	France	70.48[(19)]
American International Pacific Insurance Company	Colorado	100
American International South Insurance Company	Pennsylvania	100
Granite State Insurance Company	Pennsylvania	100
Illinois National Insurance Co.	Illinois	100
New Hampshire Indemnity Company, Inc.	Pennsylvania	100
AIG National Insurance Company, Inc.	New York	100
New Hampshire Insurance Services, Inc.	New Hampshire	100
Risk Specialists Companies, Inc.	Delaware	100
HSB Group, Inc.	Delaware	100
The Hartford Steam Boiler Inspection and Insurance Company	Connecticut	100

Subsidiaries of Registrant *Continued*

As of December 31, 2007	Jurisdiction of Incorporation or Organization	Percentage of Voting Securities held by Immediate Parent[1]
The Hartford Steam Boiler Inspection and Insurance Company of Connecticut	Connecticut	100
HSB Engineering Insurance Limited	England	100
The Boiler Inspection and Insurance Company of Canada	Canada	100
United Guaranty Corporation	North Carolina	36.31[20]
A.I.G. Mortgage Holdings Israel, Ltd.	Israel	87.32
E.M.I. - Ezer Mortgage Insurance Company, Ltd.	Israel	100
AIG United Guaranty Agenzia Di Assirazione S.R.L	Italy	100
AIG United Guaranty Insurance (Asia) Limited	Hong Kong	100
AIG United Guaranty Mexico, S.A.	Mexico	100
AIG United Guaranty Mortgage Insurance Company Canada	Canada	100
AIG United Guaranty Re, Ltd.	Ireland	100
United Guaranty Insurance Company	North Carolina	100
United Guaranty Mortgage Insurance Company	North Carolina	100
United Guaranty Mortgage Insurance Company of North Carolina	North Carolina	100
United Guaranty Partners Insurance Company	Vermont	100
United Guaranty Residential Insurance Company	North Carolina	75.03[21]
United Guaranty Credit Insurance Company	North Carolina	100
United Guaranty Commercial Insurance Company of North Carolina	North Carolina	100
United Guaranty Mortgage Indemnity Company	North Carolina	100
United Guaranty Residential Insurance Company of North Carolina	North Carolina	100
United Guaranty Services, Inc.	North Carolina	100
AIG Marketing, Inc.	Delaware	100
American International Insurance Company of Delaware	Delaware	100
Hawaii Insurance Consultants, Ltd.	Hawaii	100
AIG Retirement Services, Inc.	Delaware	100
SunAmerica Life Insurance Company	Arizona	100
SunAmerica Investments, Inc.	Georgia	70[22]
AIG Advisor Group, Inc.	Maryland	100
AIG Financial Advisors, Inc.	Delaware	100
Advantage Capital Corporation	New York	100
American General Securities Incorporated	Texas	100
FSC Securities Corporation	Delaware	100
Royal Alliance Associates, Inc.	Delaware	100
AIG SunAmerica Life Assurance Company	Arizona	100
AIG SunAmerica Asset Management Corp.	Delaware	100
AIG SunAmerica Capital Services, Inc.	Delaware	100
First SunAmerica Life Insurance Company	New York	100
AIG Global Services, Inc.	New Hampshire	100
AIG Trading Group Inc.	Delaware	100
AIG International Inc.	Delaware	100
AIU Holdings LLC	Delaware	100
AIG Central Europe & CIS Insurance Holdings Corporation	Delaware	100
AIG Bulgaria Insurance and Reinsurance Company EAD	Bulgaria	100
AIG Czech Republic pojistovna, a.s.	Czech Republic	100
AIG Memsa Holdings, Inc.	Delaware	100
AIG Hayleys Investment Holdings (Private) Ltd.	Sri Lanka	80
Hayleys AIG Insurance Company Limited	Sri Lanka	100
AIG Iraq, Inc.	Delaware	100
AIG Lebanon S.A.L.	Lebanon	100
AIG Libya, Inc.	Delaware	100
AIG Sigorta A.S.	Turkey	100
Tata AIG General Insurance Company Limited	India	26

Subsidiaries of Registrant *Continued*

As of December 31, 2007	Jurisdiction of Incorporation or Organization	Percentage of Voting Securities held by Immediate Parent[1]
AIU Africa Holdings, Inc.	Delaware	100
AIG Kenya Insurance Company Limited	Kenya	66.67
AIU North America, Inc.	New York	100
American International Underwriters Corporation	New York	100
American International Underwriters Overseas, Ltd.	Bermuda	100
A.I.G. Colombia Seguros Generales S.A.	Colombia	94[23]
AIG Brasil Companhia de Seguros S.A.	Brazil	50
AIG Europe (Ireland) Limited	Ireland	100
AIG General Insurance (Thailand) Ltd.	Thailand	100
AIG General Insurance (Vietnam) Company Limited	Vietnam	100
AIG MEMSA Insurance Company Limited	United Arab Emirates	100
AIG UK Holdings Limited	England	82.8[24]
AIG Germany Holding GmbH	Germany	100
Wurttembergische und Badische Versicherungs-AG	Germany	100
DARAG Deutsche Versicherungs-und Ruckversicherungs-Aktiengesellschaft	Germany	100
AIG UK Financing Limited	England	100
AIG UK Sub Holdings Limited	England	100
AIG UK Limited	England	100
AIG UK Services Limited	England	100
AIG Takaful - Enaya B.S.C.	Bahrain	100
American International Insurance Company of Puerto Rico	Puerto Rico	100
Arabian American Insurance Company (Bahrain) E.C.	Bahrain	100
La Meridional Compania Argentina de Seguros S.A.	Argentina	100
La Seguridad de Centroamerica Compania de Seguros S.A.	Guatemala	100
Richmond Insurance Company Limited	Bermuda	100
Underwriters Adjustment Company, Inc.	Panama	100
American Life Insurance Company	Delaware	100
AIG Life Bulgaria Zhivotozastrahovatelna Druzhestvo .A.D.	Bulgaria	100
ALICO, S.A.	France	100
First American Polish Life Insurance and Reinsurance Company, S.A.	Poland	100
Inversiones Interamericana S.A.	Chile	99.99
Pharaonic American Life Insurance Company	Egypt	74.87[25]
Unibanco AIG Seguros S.A.	Brazil	46.06[26]
American Security Life Insurance Company, Ltd.	Lichtenstein	100
Delaware American Life Insurance Company	Delaware	100
Mt. Mansfield Company, Inc.	Vermont	100
The Philippine American Life and General Insurance Company	Philippines	99.78
Pacific Union Assurance Company	California	100
Philam Equitable Life Assurance Company, Inc.	Philippines	95
Philam Insurance Company, Inc.	Philippines	100

(1) Percentages include directors' qualifying shares.

(2) All subsidiaries listed are consolidated in the accompanying financial statements. Certain subsidiaries have been omitted from the tabulation. The omitted subsidiaries, when considered in the aggregate as a single subsidiary, do not constitute a significant subsidiary.

(3) The common stock is owned approximately 14.1 percent by C.V. Starr & Co., Inc., Edward E. Matthews, Maurice R. and Corinne P. Greenberg Joint Tenancy Company, LLC, Starr International Company, Inc., The Maurice R. Greenberg and Corinne P. Greenberg Family Foundation, Inc. and the Universal Foundation, Inc.

(4) Also owned 0.01 percent by AIG Global Investment Corp.

(5) Also owned 1 percent by AIG Capital Corporation.

(6) Also owned 32.77 percent by National Union Fire Insurance Company of Pittsburgh, Pa.

(7) Also owned 4.69 percent by AIG Memsa Holdings, Inc.

(8) Also owned 10 percent by AIG Matched Funding Corp.

(9) Also owned 10 percent by a subsidiary of American Life Insurance Company.

(10) Also owned 48.15 percent by American General Life and Accident Insurance Company.

Subsidiaries of Registrant *Continued*

(11) Also owned 8 percent by The Insurance Company of the State of Pennsylvania, 32 percent by National Union Fire Insurance Company of the Pittsburgh, Pa., and 8 percent by AIG Casualty Company.

(12) Also owned by 11 other AIG subsidiaries.

(13) Also owned by 11 other AIG subsidiaries.

(14) Also owned 25.78 percent by AIG.

(15) Also owned 25 percent by American Home Assurance Company and 25 percent by AIU Insurance Company.

(16) Also owned 20 percent by the Insurance Company of the State of Pennsylvania and 10 percent by AIG Casualty Company.

(17) Also owned 20 percent by the Insurance Company of the State of Pennsylvania and 10 percent by AIG Casualty Company.

(18) Also owned 16.3 percent by American Home Assurance Company, 31.1 percent by Commerce and Industry Insurance Company and 20.6 percent by New Hampshire Insurance Company.

(19) 100 percent held together with AIG companies.

(20) Also owned 45.88 percent by National Union Fire Insurance Company of Pittsburgh, Pa., 16.95 percent by New Hampshire Insurance Company and 0.86 percent by The Insurance Company of the State of Pennsylvania.

(21) Also owned 24.97 percent by United Guaranty Residential Insurance Company of North Carolina.

(22) Also owned 30 percent by AIG Retirement Services, Inc.

(23) Also owned 3.24 percent by American International Underwriters de Colombia Ltd.

(24) Also owned 5.6 percent by American International Company, Limited, 2.5 percent by AIG Europe (Ireland) Ltd., 8.5 percent by American International Underwriters Overseas Association and 0.6 percent by New Hampshire Insurance Company.

(25) Also owned 7.5 percent by AIG Egypt Insurance Company.

(26) Also owned 0.92 percent by American International Underwriters Overseas, Ltd.

Consent of Independent Registered Public Accounting Firm

Exhibit 23

We hereby consent to the incorporation by reference in the Registration Statements on Form S-8 and Form S-3 (No. 2-45346, No. 2-75875, No. 2-78291, No. 2-91945, No. 33-18073, No. 33-57250, No. 333-48639, No. 333-58095, No. 333-70069, No. 333-83813, No. 333-31346, No. 333-39976, No. 333-45828, No. 333-50198, No. 333-52938, No. 333-68640, No. 333-74187, No. 333-101640, No. 333-101967, No. 333-108466, No. 333-111737, No. 333-115911, No. 333-106040, No. 333-132561, No. 333-143992 and No. 333-148148) of American International Group, Inc. of our report dated February 28, 2008, relating to the financial statements, financial statement schedules, and the effectiveness of internal control over financial reporting, which appears in this Annual Report on Form 10-K.

PricewaterhouseCoopers LLP

New York, New York
February 28, 2008

Exhibit 31

CERTIFICATIONS

I, Martin J. Sullivan, certify that:

1. I have reviewed this Annual Report on Form 10-K of American International Group, Inc.;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:

(a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

(b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

(c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

(d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):

(a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

(b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: February 28, 2008

/s/ Martin J. Sullivan

Martin J. Sullivan
President and Chief Executive Officer

CERTIFICATIONS

I, Steven J. Bensinger, certify that:

1. I have reviewed this Annual Report on Form 10-K of American International Group, Inc.;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:

(a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

(b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

(c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

(d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):

(a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

(b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: February 28, 2008

/s/ Steven J. Bensinger

Steven J. Bensinger
Executive Vice President and Chief Financial Officer

Exhibit 32

CERTIFICATION

In connection with this Annual Report on Form 10-K of American International Group, Inc. (the ''Company'') for the year ended December 31, 2007, as filed with the Securities and Exchange Commission on the date hereof (the ''Report''), I, Martin J. Sullivan, President and Chief Executive Officer of the Company, certify, pursuant to 18 U.S.C. Section 1350, that to my knowledge:

(1) The Report fully complies with the requirements of Section 13(a) or 15(d), as applicable, of the Securities Exchange Act of 1934; and

(2) The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Date: February 28, 2008

/s/ MARTIN J. SULLIVAN

Martin J. Sullivan
President and Chief Executive Officer

The foregoing certification is being furnished solely pursuant to 18 U.S.C. Section 1350 and is not being filed as part of the Report or as a separate disclosure document.

CERTIFICATION

In connection with this Annual Report on Form 10-K of American International Group, Inc. (the ''Company'') for the year ended December 31, 2007, as filed with the Securities and Exchange Commission on the date hereof (the ''Report''), I, Steven J. Bensinger, Executive Vice President and Chief Financial Officer of the Company, certify, pursuant to 18 U.S.C. Section 1350, that to my knowledge:

(1) The Report fully complies with the requirements of Section 13(a) or 15(d), as applicable, of the Securities Exchange Act of 1934; and

(2) The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Date: February 28, 2008

/s/ Steven J. Bensinger

Steven J. Bensinger
Executive Vice President and Chief Financial Officer

The foregoing certification is being furnished solely pursuant to 18 U.S.C. Section 1350 and is not being filed as part of the Report or as a separate disclosure document.

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

Form 10-Q

(Mark One)

☑ QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended March 31, 2008

or

☐ TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the transition period from to

Commission File Number 1-8787

American International Group, Inc.

(Exact name of registrant as specified in its charter)

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

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

Former name, former address and former fiscal year, if changed since last report: None

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

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

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

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes ☐ No ☑

As of April 30, 2008, there were 2,492,061,043 shares outstanding of the registrant's common stock.

TABLE OF CONTENTS

Explanatory Note

Throughout this report, AIG's operations formerly referred to as the Domestic Brokerage Group (DBG) are referred to as AIG Commercial Insurance (Commercial Insurance). See page 48 for additional information.

Part I – FINANCIAL INFORMATION

ITEM 1. Financial Statements (unaudited)

CONSOLIDATED BALANCE SHEET

(in millions) (unaudited)

	March 31, 2008	December 31, 2007
Assets:		
Investments and Financial Services assets:		
Fixed maturities:		
Bonds available for sale, at fair value (amortized cost: 2008 – $396,168; 2007 – $393,170)	**$ 395,487**	$ 397,372
Bonds held to maturity, at amortized cost (fair value: 2008 – $21,839; 2007 – $22,157)	**21,566**	21,581
Bond trading securities, at fair value	**9,375**	9,982
Equity securities:		
Common stocks available for sale, at fair value (cost: 2008 – $12,387; 2007 – $12,588)	**16,122**	17,900
Common and preferred stocks trading, at fair value	**21,671**	21,376
Preferred stocks available for sale, at fair value (cost: 2008 – $2,609; 2007 – $2,600)	**2,451**	2,370
Mortgage and other loans receivable, net of allowance (2008 – $87; 2007 – $77) (held for sale: 2008 – $6; 2007 – $377 (amount measured at fair value: 2008 – $810)	**34,373**	33,727
Financial Services assets:		
Flight equipment primarily under operating leases, net of accumulated depreciation (2008 – $10,932; 2007 – $10,499)	**42,832**	41,984
Securities available for sale, at fair value (cost: 2008 – $1,143; 2007 – $40,157)	**1,096**	40,305
Trading securities, at fair value	**35,998**	4,197
Spot commodities, at fair value in 2008	**728**	238
Unrealized gain on swaps, options and forward transactions, at fair value	**20,598**	16,442
Trade receivables	**8,896**	6,467
Securities purchased under agreements to resell, at fair value in 2008	**19,708**	20,950
Finance receivables, net of allowance (2008 – $985; 2007 – $878) (receivables held for sale: 2008 – $80; 2007 – $233)	**32,601**	31,234
Securities lending invested collateral, at fair value (cost: 2008 – $73,610; 2007 – $80,641)	**64,261**	75,662
Other invested assets (amount measured at fair value: 2008 – $21,688; 2007 – $20,827)	**61,191**	58,823
Short-term investments (amount measured at fair value: 2008 – $2,801)	**52,298**	51,351
Total Investments and Financial Services assets	**841,252**	851,961
Cash	**2,489**	2,284
Investment income due and accrued	**6,696**	6,587
Premiums and insurance balances receivable, net of allowance (2008 – $638; 2007 – $662)	**20,437**	18,395
Reinsurance assets, net of allowance (2008 – $526; 2007 – $520)	**22,895**	23,103
Deferred policy acquisition costs	**44,066**	43,150
Investments in partially owned companies	**710**	654
Real estate and other fixed assets, net of accumulated depreciation (2008 – $5,630; 2007 – $5,446)	**5,635**	5,518
Separate and variable accounts, at fair value	**72,973**	78,684
Goodwill	**10,182**	9,414
Income taxes receivable	**2,762**	—
Other assets (amount measured at fair value: 2008 – $5,123; 2007 – $4,152)	**20,989**	20,755
Total assets	**$1,051,086**	$1,060,505

See Accompanying Notes to Consolidated Financial Statements.

CONSOLIDATED BALANCE SHEET *(continued)*

(in millions, except share data) (unaudited)

	March 31, 2008	December 31, 2007
Liabilities:		
Reserve for losses and loss expenses	**$ 86,860**	$ 85,500
Unearned premiums	**28,889**	28,022
Future policy benefits for life and accident and health insurance contracts	**143,425**	136,068
Policyholders' contract deposits (amount measured at fair value: 2008 – $4,118; 2007 – $295)	**261,264**	258,459
Other policyholders' funds	**13,191**	12,599
Commissions, expenses and taxes payable	**5,523**	6,310
Insurance balances payable	**5,504**	4,878
Funds held by companies under reinsurance treaties	**2,505**	2,501
Income taxes payable	**—**	3,823
Financial Services liabilities:		
Securities sold under agreements to repurchase (amount measured at fair value: 2008 – $8,271)	**9,674**	8,331
Trade payables	**9,494**	10,568
Securities and spot commodities sold but not yet purchased, at fair value	**3,806**	4,709
Unrealized loss on swaps, options and forward transactions, at fair value	**30,376**	20,613
Trust deposits and deposits due to banks and other depositors (amount measured at fair value: 2008 – $262)	**5,662**	4,903
Commercial paper and extendible commercial notes	**13,261**	13,114
Long-term borrowings (amount measured at fair value: 2008 – $59,254)	**158,909**	162,935
Separate and variable accounts	**72,973**	78,684
Securities lending payable	**77,775**	81,965
Minority interest	**10,834**	10,422
Other liabilities (amount measured at fair value: 2008 – $6,295; 2007 – $3,262)	**31,358**	30,200
Total liabilities	**971,283**	964,604
Preferred shareholders' equity in subsidiary companies	**100**	100
Commitments, Contingencies and Guarantees (See Note 6)		
Shareholders' equity:		
Common stock, $2.50 par value; 5,000,000,000 shares authorized; shares issued 2008 and 2007 – 2,751,327,476	**6,878**	6,878
Additional paid-in capital	**2,938**	2,848
Payments advanced to purchase shares	**(179)**	(912)
Retained earnings	**79,732**	89,029
Accumulated other comprehensive income (loss)	**(1,271)**	4,643
Treasury stock, at cost; 2008 – 255,499,218; 2007 – 221,743,421 shares of common stock	**(8,395)**	(6,685)
Total shareholders' equity	**79,703**	95,801
Total liabilities, preferred shareholders' equity in subsidiary companies and shareholders' equity	**$1,051,086**	$1,060,505

See Accompanying Notes to Consolidated Financial Statements.

CONSOLIDATED STATEMENT OF INCOME (LOSS)

(in millions, except per share data) (unaudited)

	Three Months Ended March 31,	
	2008	2007
Revenues:		
Premiums and other considerations	**$ 20,672**	$19,642
Net investment income	**4,954**	7,124
Net realized capital gains (losses)	**(6,089)**	(70)
Unrealized market valuation losses on AIGFP super senior credit default swap portfolio	**(9,107)**	—
Other income	**3,601**	3,949
Total revenues	**14,031**	30,645
Benefits and expenses:		
Incurred policy losses and benefits	**15,882**	16,146
Insurance acquisition and other operating expenses	**9,413**	8,327
Total benefits and expenses	**25,295**	24,473
Income (loss) before income taxes (benefits) and minority interest	**(11,264)**	6,172
Income taxes (benefits)	**(3,537)**	1,726
Income (loss) before minority interest	**(7,727)**	4,446
Minority interest	**(78)**	(316)
Net income (loss)	**$ (7,805)**	$ 4,130
Earnings (loss) per common share:		
Basic	**$ (3.09)**	$ 1.58
Diluted	**$ (3.09)**	$ 1.58
Dividends declared per common share	**$ 0.200**	$ 0.165
Average shares outstanding:		
Basic	**2,528**	2,612
Diluted	**2,528**	2,621

See Accompanying Notes to Consolidated Financial Statements.

CONSOLIDATED STATEMENT OF CASH FLOWS

(in millions) (unaudited)

	Three Months Ended March 31,	
	2008	2007
Summary:		
Net cash provided by operating activities	**$ 8,293**	$ 9,930
Net cash provided by (used in) investing activities	**3,529**	(18,024)
Net cash provided by (used in) financing activities	**(11,675)**	8,216
Effect of exchange rate changes on cash	**58**	(10)
Change in cash	**205**	112
Cash at beginning of year period	**2,284**	1,590
Cash at end of year period	**$ 2,489**	$ 1,702
Cash flows from operating activities:		
Net income (loss)	**$ (7,805)**	$ 4,130
Adjustments to reconcile net income (loss) to net cash provided by operating activities:		
Noncash revenues, expenses, gains and losses included in income (loss):		
Unrealized market valuation losses on AIGFP super senior credit default swap portfolio	**9,107**	—
Net gains on sales of securities available for sale and other assets	**(245)**	(250)
Foreign exchange transaction (gains) losses	**996**	305
Net unrealized (gains) losses on non-AIGFP derivatives and other assets and liabilities	**2,124**	61
Equity in income of partially owned companies and other invested assets	**(79)**	(1,329)
Amortization of deferred policy acquisition costs	**3,156**	2,868
Depreciation and other amortization	**885**	824
Provision for mortgage, other loans and finance receivables	**251**	87
Other-than-temporary impairments	**5,642**	467
Changes in operating assets and liabilities:		
General and life insurance reserves	**4,855**	4,380
Premiums and insurance balances receivable and payable – net	**(1,588)**	(1,192)
Reinsurance assets	**241**	223
Capitalization of deferred policy acquisition costs	**(4,183)**	(3,697)
Investment income due and accrued	**(37)**	(109)
Funds held under reinsurance treaties	**(12)**	(158)
Other policyholders' funds	**289**	412
Income taxes receivable and payable – net	**(2,635)**	1,076
Commissions, expenses and taxes payable	**(27)**	661
Other assets and liabilities – net	**814**	636
Trade receivables and payables – net	**(3,503)**	1,805
Trading securities	**1,079**	(1,453)
Spot commodities	**(490)**	147
Net unrealized (gain) loss on swaps, options and forward transactions	**(2,646)**	962
Securities purchased under agreements to resell	**1,241**	889
Securities sold under agreements to repurchase	**1,283**	(2,100)
Securities and spot commodities sold but not yet purchased	**(914)**	(20)
Finance receivables and other loans held for sale – originations and purchases	**(166)**	(2,473)
Sales of finance receivables and other loans – held for sale	**363**	2,574
Other, net	**297**	204
Total adjustments	**16,098**	5,800
Net cash provided by operating activities	**$ 8,293**	$ 9,930

See Accompanying Notes to Consolidated Financial Statements.

CONSOLIDATED STATEMENT OF CASH FLOWS

(in millions) (unaudited)

	Three Months Ended March 31,	
	2008	2007
Cash flows from investing activities:		
Proceeds from (payments for)		
Sales and maturities of fixed maturity securities available for sale and hybrid investments	**$ 21,208**	$ 30,073
Sales of equity securities available for sale	**2,772**	2,137
Proceeds from fixed maturity securities held to maturity	**46**	18
Sales of trading securities	**14,196**	—
Sales of flight equipment	**128**	27
Sales or distributions of other invested assets	**4,895**	2,701
Payments received on mortgage and other loans receivable	**1,843**	733
Principal payments received on finance receivables held for investment	**3,510**	3,349
Purchases of fixed maturity securities available for sale and hybrid investments	**(21,054)**	(34,016)
Purchases of equity securities available for sale	**(2,512)**	(2,436)
Purchases of fixed maturity securities held to maturity	**(16)**	(9)
Purchases of trading securities	**(9,126)**	—
Purchases of flight equipment (including progress payments)	**(1,388)**	(1,917)
Purchases of other invested assets	**(6,363)**	(5,740)
Mortgage and other loans receivable issued	**(1,711)**	(2,543)
Finance receivables held for investment — originations and purchases	**(4,978)**	(3,409)
Change in securities lending invested collateral	**4,153**	(5,521)
Net additions to real estate, fixed assets, and other assets	**(237)**	(259)
Net change in short-term investments	**(1,682)**	(1,250)
Net change in non-AIGFP derivative assets and liabilities	**(155)**	38
Net cash provided by (used in) investing activities	**$ 3,529**	$(18,024)
Cash flows from financing activities:		
Proceeds from (payments for)		
Policyholders' contract deposits	**$ 16,439**	$ 14,001
Policyholders' contract withdrawals	**(15,600)**	(15,309)
Change in other deposits	**629**	(1,340)
Change in commercial paper and extendible commercial notes	**112**	396
Long-term borrowings issued	**12,559**	24,358
Repayments on long-term borrowings	**(19,908)**	(16,324)
Change in securities lending payable	**(4,200)**	5,716
Issuance of treasury stock	**14**	52
Payments advanced to purchase treasury stock	**(1,000)**	(3,000)
Cash dividends paid to shareholders	**(498)**	(430)
Acquisition of treasury stock	**—**	(16)
Other, net	**(222)**	112
Net cash provided by (used in) financing activities	**$(11,675)**	$ 8,216
Supplementary disclosure of cash flow information:		
Cash paid (received) during the period for:		
Interest	**$ 1,615**	$ 1,901
Taxes	**$ (901)**	$ 640
Non-cash financing activities:		
Interest credited to policyholder accounts included in financing activities	**$ 1,241**	$ 2,879
Treasury stock acquired using payments advanced to purchase shares	**$ 1,733**	$ 149
Non-cash investing activities:		
Debt assumed on acquisitions and warehoused investments	**$ —**	$ 638

See Accompanying Notes to Consolidated Financial Statements.

CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME (LOSS)

(in millions) (unaudited)

	Three Months Ended March 31,	
	2008	2007
Net income (loss)	**$ (7,805)**	$ 4,130
Other comprehensive income (loss):		
Cumulative effect of accounting changes	**(162)**	—
Deferred income tax benefit on above changes	**57**	—
Unrealized (depreciation) appreciation of investments – net of reclassification adjustments	**(10,572)**	1,309
Deferred income tax benefit (expense) on above changes	**3,748**	(458)
Foreign currency translation adjustments	**1,346**	(165)
Deferred income tax benefit (expense) on above changes	**(251)**	28
Net derivative gains (losses) arising from cash flow hedging activities – net of reclassification adjustments	**(133)**	1
Deferred income tax benefit on above changes	**45**	27
Change in pension and postretirement unrecognized periodic benefit	**6**	3
Deferred income tax benefit (expense) on above changes	**2**	(1)
Other comprehensive income (loss)	**(5,914)**	744
Comprehensive income (loss)	**$(13,719)**	$ 4,874

See Accompanying Notes to Consolidated Financial Statements.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited)*

1. Summary of Significant Accounting Policies

Basis of Presentation

These unaudited condensed consolidated financial statements do not include all disclosures required by accounting principles generally accepted in the United States (GAAP) for complete financial statements and should be read in conjunction with the audited consolidated financial statements and the related notes included in the Annual Report on Form 10-K of American International Group, Inc. (AIG) for the year ended December 31, 2007 (2007 Annual Report on Form 10-K).

In the opinion of management, these consolidated financial statements contain the normal recurring adjustments necessary for a fair statement of the results presented herein. All material intercompany accounts and transactions have been eliminated.

Certain reclassifications and format changes have been made to prior period amounts to conform to the current period presentation.

Recent Accounting Standards

Accounting Changes

FAS 157

In September 2006, the Financial Accounting Standards Board (FASB) issued Statement of Financial Accounting Standards (FAS) No. 157, "Fair Value Measurements" (FAS 157). FAS 157 defines fair value, establishes a framework for measuring fair value and expands disclosure requirements regarding fair value measurements but does not change existing guidance about whether an asset or liability is carried at fair value. FAS 157 nullifies the guidance in Emerging Issues Task Force (EITF) Issue No. 02-3, "Issues Involved in Accounting for Derivative Contracts Held for Trading Purposes and Contracts Involved in Energy Trading and Risk Management Activities," (EITF 02-3) that precluded the recognition of a trading profit at the inception of a derivative contract unless the fair value of such contract was obtained from a quoted market price or other valuation technique incorporating observable market data. FAS 157 also clarifies that an issuer's credit standing should be considered when measuring liabilities at fair value. The fair value measurement and related disclosure guidance in FAS 157 do not apply to fair value measurements associated with AIG's share-based employee compensation awards accounted for in accordance with FAS 123(R), "Share-Based Payment."

AIG adopted FAS 157 on January 1, 2008, its required effective date. FAS 157 must be applied prospectively, except for certain stand-alone derivatives and hybrid instruments initially measured using the guidance in EITF 02-3, which must be applied as a cumulative effect accounting change to retained earnings at January 1, 2008. The cumulative effect, net of taxes, of adopting FAS 157 on AIG's consolidated balance sheet was an increase in retained earnings of $4 million.

The most significant effect of adopting FAS 157 on AIG's first quarter 2008 results related to changes in fair value methodologies with respect to both liabilities already carried at fair value, primarily hybrid notes and derivatives, and newly elected liabilities measured at fair value (see FAS 159 discussion below). Specifically, the incorporation of AIG's own credit spreads and the incorporation of explicit risk margins (embedded policy derivatives only) resulted in an increase of $2.8 billion to pre-tax income ($1.8 billion after tax) for the first three months of 2008. The total increase in pre-tax income attributable to changes in AIG's own credit spreads of $2,648 million for AIG Financial Products Corp. and AIG Trading Group Inc. and their respective subsidiaries (collectively, AIGFP) was substantially offset by the effect of changes in counterparty credit spreads for assets measured at fair value at AIGFP of $2,620 million.

See Note 3 to the Consolidated Financial Statements for additional FAS 157 disclosures.

FAS 159

In February 2007, the FASB issued FAS 159, "The Fair Value Option for Financial Assets and Financial Liabilities" (FAS 159). FAS 159 permits entities to choose to measure at fair value many financial instruments and certain other items that are not required to be measured at fair value. Subsequent changes in fair value for designated items are required to be reported in income. FAS 159 also establishes presentation and disclosure requirements for similar types of assets and liabilities measured at fair value. FAS 159 permits the fair value option election on an instrument-by-instrument basis for eligible items existing at the adoption date and at initial recognition of an asset or liability or upon an event that gives rise to a new basis of accounting for that instrument.

AIG adopted FAS 159 on January 1, 2008, its required effective date. The adoption of FAS 159 with respect to elections made in the Life Insurance & Retirement Services segment resulted in an after-tax decrease to 2008 opening retained earnings of $559 million. The adoption of FAS 159 with respect to elections made by AIGFP resulted in an after-tax decrease to 2008 opening retained earnings of $448 million. Included in this amount are net unrealized gains of $105 million that were reclassified to retained earnings from accumulated other comprehensive income (loss) related to available for sale securities recorded on the consolidated balance sheet at January 1, 2008 for which the fair value option was elected.

See Note 3 to the Consolidated Financial Statements for additional FAS 159 disclosures.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

1. Summary of Significant Accounting Policies *(continued)*

FAS 157 and FAS 159

The following table summarizes the after-tax increase (decrease) from adopting FAS 157 and FAS 159 on the opening shareholders' equity accounts at January 1, 2008:

	At January 1, 2008		
(in millions)	Accumulated Other Comprehensive Income/(Loss)	Retained Earnings	Cumulative Effect of Accounting Changes
FAS 157	$ —	$ 4	$ 4
FAS 159	(105)	(1,007)	(1,112)
Cumulative effect of accounting changes	$(105)	$(1,003)	$(1,108)

FIN 39-1

In April 2007, the FASB directed the FASB Staff to issue FSP No. FIN 39-1, "Amendment of FASB Interpretation No. 39" (FSP FIN 39-1). FSP FIN 39-1 modifies FIN No. 39, "Offsetting of Amounts Related to Certain Contracts," and permits companies to offset cash collateral receivables or payables against derivative instruments under certain circumstances. FSP FIN 39-1 became effective on January 1, 2008 for AIG. Consistent with prior practice, AIG elected not to offset cash collateral receivables or payables against derivative instruments. At March 31, 2008, the amounts of cash collateral received and paid were $8.7 billion and $7.2 billion, respectively.

Future Application of Accounting Standards

FAS 141(R)

In December 2007, the FASB issued FAS 141 (revised 2007), "Business Combinations" (FAS 141(R)). FAS 141(R) changes the accounting for business combinations in a number of ways, including broadening the transactions or events that are considered business combinations; requiring an acquirer to recognize 100 percent of the fair value of assets acquired, liabilities assumed, and noncontrolling (i.e., minority) interests; recognizing contingent consideration arrangements at their acquisition-date fair values with subsequent changes in fair value generally reflected in income; and recognizing preacquisition loss and gain contingencies at their acquisition-date fair values, among other changes.

AIG is required to adopt FAS 141(R) for business combinations for which the acquisition date is on or after January 1, 2009. Early adoption is prohibited.

FAS 160

In December 2007, the FASB issued FAS 160, "Noncontrolling Interests in Consolidated Financial Statements, an amendment of ARB No. 51" (FAS 160). FAS 160 requires noncontrolling (i.e., minority) interests in partially owned consolidated subsidiaries to be classified in the consolidated balance sheet as a separate component of consolidated shareholders' equity. FAS 160 also establishes accounting rules for subsequent acquisitions and sales of noncontrolling interests and how noncontrolling interests should be presented in the consolidated statement of income. The noncontrolling interests' share of subsidiary income should be reported as a part of consolidated net income with disclosure of the attribution of consolidated net income to the controlling and noncontrolling interests on the face of the consolidated statement of income.

FAS 160 is required to be adopted by AIG on January 1, 2009 and early adoption is prohibited. FAS 160 must be adopted prospectively, except that noncontrolling interests should be reclassified from liabilities to a separate component of shareholders' equity and consolidated net income should be recast to include net income attributable to both the controlling and noncontrolling interests retrospectively. Had AIG adopted FAS 160 at March 31, 2008, AIG would have reclassified $10.8 billion of noncontrolling (i.e., minority) interests from liabilities to shareholders' equity. Additionally, both consolidated net income (loss) and consolidated comprehensive income (loss) for the three-month periods ended March 31, 2008 and 2007 would have increased by $78 million and $316 million, respectively, to include the net income (loss) attributed to the noncontrolling interests.

FAS 161

In March 2008, the FASB issued FAS 161, "Disclosures about Derivative Instruments and Hedging Activities – an amendment of FASB Statement No. 133" (FAS 161). FAS 161 requires enhanced disclosures about (a) how and why AIG uses derivative instruments, (b) how derivative instruments and related hedged items are accounted for under FAS No. 133, "Accounting for Derivative Instruments and Hedging Activities" (FAS 133), and its related interpretations, and (c) how derivative instruments and related hedged items affect AIG's consolidated financial condition, results of operations, and cash flows. FAS 161 is effective for AIG beginning with financial statements issued in the first quarter of 2009. Because FAS 161 only requires additional disclosures about derivatives, it will have no effect on AIG's consolidated financial condition, results of operations or cash flows.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

2. Segment Information

AIG identifies its reportable segments by product line consistent with its management structure. These segments are General Insurance, Life Insurance & Retirement Services, Financial Services and Asset Management.

AIG's operations by major operating segment were as follows:

Operating Segments *(in millions)*	Three Months Ended March 31, **2008**	2007
Total revenues[(a)]:		
General Insurance	**$ 12,289**	$12,903
Life Insurance & Retirement Services[(b)]	**8,752**	13,682
Financial Services[(c)(d)]	**(6,560)**	2,201
Asset Management[(e)]	**(149)**	1,669
Other	**(128)**	131
Consolidation and eliminations	**(173)**	59
Total	**$ 14,031**	$30,645
Operating income (loss)[(a)]:		
General Insurance	**$ 1,337**	$ 3,096
Life Insurance & Retirement Services[(b)]	**(1,831)**	2,281
Financial Services[(c)(d)]	**(8,772)**	292
Asset Management[(e)]	**(1,251)**	758
Other[(f)]	**(768)**	(470)
Consolidation and eliminations	**21**	215
Total	**$ (11,264)**	$ 6,172

(a) For the three-month periods ended March 31, 2008 and 2007, includes other-than-temporary impairment charges of $5.6 billion and $467 million, respectively. Also includes gains (losses) from hedging activities that did not qualify for hedge accounting treatment under FAS 133, including the related foreign exchange gains and losses. For the three-month periods ended March 31, 2008 and 2007, the effect was $(748) million and $(452) million, respectively, in both revenues and operating income (loss). These amounts result primarily from interest rate and foreign currency derivatives that are effective economic hedges of investments and borrowings.

(b) For the three-month periods ended March 31, 2008 and 2007, includes other-than-temporary impairment charges of $4.4 billion and $392 million, respectively.

(c) Includes gains (losses) from hedging activities that did not qualify for hedge accounting treatment under FAS 133, including the related foreign exchange gains and losses. For the three-month periods ended March 31, 2008 and 2007, the effect was $(204) million and $(160) million, respectively, in both revenues and operating income (loss). These amounts result primarily from interest rate and foreign currency derivatives that are effective economic hedges of investments and borrowings.

(d) For the three-month period ended March 31, 2008, both revenues and operating income (loss) include an unrealized market valuation loss of $9.1 billion on AIGFP's super senior credit default swap portfolio.

(e) Includes net realized capital losses of $1.4 billion for the three-month period ended March 31, 2008, including other-than-temporary impairment charges of $1.0 billion.

(f) Includes AIG parent and other operations that are not required to be reported separately. The following table presents the operating loss for AIG's Other category:

Other *(in millions)*	Three Months Ended March 31, **2008**	2007
Operating income (loss):		
Equity earnings in partially owned companies	**$ 8**	$ 41
Interest expense	**(368)**	(252)
Unallocated corporate expenses[(a)]	**(93)**	(172)
Net realized capital gains (losses)[(b)]	**(265)**	(49)
Other miscellaneous, net	**(50)**	(38)
Total Other	**$(768)**	$(470)

(a) Includes expenses of corporate staff not attributable to specific operating segments, expenses related to efforts to improve internal controls, corporate initiatives and certain compensation plan expenses.

(b) The increase in net realized capital losses reflected higher foreign exchange losses on foreign-denominated debt, a portion of which was economically hedged but did not qualify for hedge accounting treatment under FAS 133, and losses on non-hedged derivatives in the first three months of 2008.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

2. Segment Information *(continued)*

AIG's General Insurance operations by major internal reporting unit were as follows:

General Insurance *(in millions)*	Three Months Ended March 31, **2008**	2007
Total revenues:		
Commercial Insurance	**$ 5,987**	$ 7,091
Transatlantic	**1,119**	1,096
Personal Lines	**1,252**	1,213
Mortgage Guaranty	**298**	248
Foreign General Insurance	**3,628**	3,262
Reclassifications and eliminations	**5**	(7)
Total	**$12,289**	$12,903
Operating income (loss):		
Commercial Insurance	**$ 785**	$ 1,929
Transatlantic	**162**	151
Personal Lines	**3**	106
Mortgage Guaranty	**(354)**	8
Foreign General Insurance	**736**	909
Reclassifications and eliminations	**5**	(7)
Total	**$ 1,337**	$ 3,096

AIG's Life Insurance & Retirement Services operations by major internal reporting unit were as follows:

Life Insurance & Retirement Services *(in millions)*	Three Months Ended March 31, **2008**	2007
Total revenues:		
Foreign:		
Japan and Other	**$ 3,896**	$ 4,770
Asia	**4,277**	4,491
Domestic:		
Domestic Life Insurance	**1,283**	2,521
Domestic Retirement Services	**(704)**	1,900
Total	**$ 8,752**	$13,682
Operating income (loss):		
Foreign:		
Japan and Other	**$ 483**	$ 913
Asia	**252**	371
Domestic:		
Domestic Life Insurance	**(870)**	345
Domestic Retirement Services	**(1,696)**	652
Total	**$(1,831)**	$ 2,281

AIG's Financial Services operations by major internal reporting unit were as follows:

Financial Services *(in millions)*	Three Months Ended March 31, **2008**	2007
Total revenues:		
Aircraft Leasing	**$ 1,165**	$1,058
Capital Markets[(a)]	**(8,743)**	228
Consumer Finance[(b)]	**931**	845
Other, including intercompany adjustments	**87**	70
Total	**$(6,560)**	$2,201
Operating income (loss):		
Aircraft Leasing	**$ 221**	$ 164
Capital Markets[(a)]	**(8,927)**	68
Consumer Finance[(b)]	**(52)**	36
Other, including intercompany adjustments	**(14)**	24
Total	**$(8,772)**	$ 292

(a) Revenues, shown net of interest expense of $511 million and $1.1 billion in the three-month periods ended March 31, 2008 and 2007, respectively, were primarily from hedged financial positions entered into in connection with counterparty transactions. In the three-month period ended March 31, 2008, both revenues and operating income (loss) include an unrealized market valuation loss of $9.1 billion on AIGFP's super senior credit default swap portfolio.

(b) For the three-month period ended March 31, 2007 includes a pre-tax charge of $128 million in connection with domestic Consumer Finance's mortgage banking activities.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

3. Fair Value Measurements

Effective January 1, 2008 AIG adopted FAS 157 and FAS 159, which specify measurement and disclosure standards related to assets and liabilities measured at fair value. See Note 1 to the Consolidated Financial Statements for additional information.

The most significant effect of adopting FAS 157 on AIG's first quarter 2008 results related to changes in fair value methodologies with respect to both liabilities already carried at fair value, primarily hybrid notes and derivatives, and newly elected liabilities measured at fair value (see FAS 159 discussion below). Specifically, the incorporation of AIG's own credit spreads and the incorporation of explicit risk margins (embedded policy derivatives only) resulted in an increase of $2.8 billion to pre-tax income ($1.8 billion after tax) for the first three months of 2008 as follows:

(in millions)	Net Pre-tax Increase (Decrease)	Liabilities Carried at Fair Value	Business Segment Affected
Income statement caption:			
Net realized capital gains (losses)	$ 288	Freestanding derivatives	All segments - excluding AIGFP
	(155)	Embedded policy derivatives	Life Insurance & Retirement Services
Unrealized market valuation losses on AIGFP super senior credit default swap portfolio	65*	Super senior credit default swap portfolio	AIGFP
Other income	2,583*	Notes, GICs, derivatives, other liabilities	AIGFP
Net pre-tax increase	$2,781		
Liabilities already carried at fair value	$1,334		
Newly elected liabilities measured at fair value (FAS 159 elected)	1,447		
Net pre-tax increase	$2,781		

* *The total increase to pre-tax income attributable to changes in AIG's own credit spreads of $2,648 million for AIGFP was substantially offset by the effect of changes in counterparty credit spreads for assets measured at fair value at AIGFP of $2,620 million.*

Fair Value Measurements on a Recurring Basis

AIG measures at fair value on a recurring basis financial instruments in its trading and available for sale securities portfolios, certain mortgage and other loans receivable, certain spot commodities, derivative assets and liabilities, securities purchased (sold) under agreements to resell (repurchase), securities lending invested collateral, non-traded equity investments included in other invested assets, certain short-term investments, separate and variable account assets, certain policyholders' contract deposits, securities and spot commodities sold but not yet purchased, certain trust deposits and deposits due to banks and other depositors, certain long-term borrowings, and certain hybrid financial instruments included in other liabilities. The fair value of a financial instrument is the amount that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date.

The degree of judgment used in measuring the fair value of financial instruments generally correlates with the level of pricing observability. Financial instruments with quoted prices in active markets generally have more pricing observability and less judgment is used in measuring fair value. Conversely, financial instruments traded in other-than-active markets or that do not have quoted prices have less observability and are measured at fair value using valuation models or other pricing techniques that require more judgment. Pricing observability is affected by a number of factors, including the type of financial instrument, whether the financial instrument is new to the market and not yet established, the characteristics specific to the transaction and general market conditions.

Fixed Maturities — Trading and Available for Sale

AIG maximizes the use of observable inputs and minimizes the use of unobservable inputs when measuring fair value. Whenever available, AIG obtains quoted prices in active markets for identical assets at the balance sheet date to measure at fair value fixed maturity instruments in its trading and available for sale portfolios. Market price data generally is obtained from exchange or dealer markets.

AIG estimates the fair value of fixed maturity instruments not traded in active markets, including securities purchased (sold) under agreements to resell (repurchase), and mortgage and other loans receivable for which AIG elected the fair value option, by referring to traded securities with similar attributes, using dealer quotations and a matrix pricing methodology, or discounted cash flow analyses. This methodology considers such factors as the issuer's industry, the security's rating and tenor, its coupon rate, its position in the capital structure of the issuer, yield curves, credit curves, prepayment rates and other relevant factors. For fixed maturity instruments that are not traded in active markets or that are subject to transfer restrictions, valuations are adjusted to reflect illiquidity and/or non-transferability, and such adjustments generally are based on available market evidence. In the absence of such evidence, management's best estimate is used.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

3. Fair Value Measurements *(continued)*

Equity Securities Traded in Active Markets — Trading and Available for Sale

AIG maximizes the use of observable inputs and minimizes the use of unobservable inputs when measuring fair value. Whenever available, AIG obtains quoted prices in active markets for identical assets at the balance sheet date to measure at fair value marketable equity securities in its trading and available for sale portfolios. Market price data generally is obtained from exchange or dealer markets.

Direct Private Equity Securities Not Traded in Active Markets — Other Invested Assets

AIG initially estimates the fair value of equity instruments not traded in active markets by reference to the transaction price. This valuation is adjusted only when changes to inputs and assumptions are corroborated by evidence such as transactions in similar instruments, completed or pending third-party transactions in the underlying investment or comparable entities, subsequent rounds of financing, recapitalizations and other transactions across the capital structure, offerings in the equity capital markets, and changes in financial ratios or cash flows. For equity securities that are not traded in active markets or that are subject to transfer restrictions, valuations are adjusted to reflect illiquidity and/or non-transferability and such adjustments generally are based on available market evidence. In the absence of such evidence, management's best estimate is used. AIG initially estimates the fair value of investments in private limited partnerships and hedge funds by reference to the transaction price. Subsequently, AIG obtains the fair value of these investments generally from net asset value information provided by the general partner or manager of the investments, the financial statements of which generally are audited annually.

Separate and Variable Account Assets

Separate and variable account assets are composed primarily of registered and unregistered open-end mutual funds that generally trade daily and are measured at fair value in the manner discussed above for equity securities traded in active markets.

Freestanding Derivatives

Derivative assets and liabilities can be exchange-traded or traded over the counter (OTC). AIG generally values exchange-traded derivatives within portfolios using models that calibrate to market clearing levels and eliminate timing differences between the closing price of the exchange-traded derivatives and their underlying instruments.

OTC derivatives are valued using market transactions and other market evidence whenever possible, including market-based inputs to models, model calibration to market clearing transactions, broker or dealer quotations or alternative pricing sources with reasonable levels of price transparency. When models are used, the selection of a particular model to value an OTC derivative depends on the contractual terms of, and specific risks inherent in, the instrument as well as the availability of pricing information in the market. AIG generally uses similar models to value similar instruments. Valuation models require a variety of inputs, including contractual terms, market prices and rates, yield curves, credit curves, measures of volatility, prepayment rates and correlations of such inputs. For OTC derivatives that trade in liquid markets, such as generic forwards, swaps and options, model inputs can generally be corroborated by observable market data by correlation or other means, and model selection does not involve significant management judgment.

Certain OTC derivatives trade in less liquid markets with limited pricing information, and the determination of fair value for these derivatives is inherently more difficult. When AIG does not have corroborating market evidence to support significant model inputs and cannot verify the model to market transactions, the transaction price is initially used as the best estimate of fair value. Accordingly, when a pricing model is used to value such an instrument, the model is adjusted so the model value at inception equals the transaction price. Subsequent to initial recognition, AIG updates valuation inputs when corroborated by evidence such as similar market transactions, third-party pricing services and/or broker or dealer quotations, or other empirical market data. When appropriate, valuations are adjusted for various factors such as liquidity, bid/offer spreads and credit considerations. Such adjustments are generally based on available market evidence. In the absence of such evidence, management's best estimate is used.

With the adoption of FAS 157 on January 1, 2008, AIG's own credit risk has been considered and is incorporated into the fair value measurement of all freestanding derivative liabilities.

Embedded Policy Derivatives

The fair value of embedded policy derivatives contained in certain variable annuity and equity-indexed annuity and life contracts is measured based on actuarial and capital market assumptions related to projected cash flows over the expected lives of the contracts. These cash flow estimates primarily include benefits and related fees assessed, when applicable, and incorporate expectations about policyholder behavior. Estimates of future policyholder behavior are subjective and based primarily on AIG's historical experience. With respect to embedded policy derivatives in AIG's variable annuity contracts, because of the dynamic and complex nature of the expected

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

3. Fair Value Measurements *(continued)*

cash flows, risk neutral valuations are used. Estimating the underlying cash flows for these products involves many estimates and judgments, including those regarding expected market rates of return, market volatility, correlations of market index returns to funds, fund performance, discount rates and policyholder behavior. With respect to embedded policy derivatives in AIG's equity-indexed annuity and life contracts, option pricing models are used to estimate fair value, taking into account assumptions for future equity indexed growth rates, volatility of the equity index, future interest rates, and determination on adjusting the participation rate and the cap on equity indexed credited rates in light of market conditions and policyholder behavior assumptions. With the adoption of FAS 157, these methodologies were not changed, with the exception of incorporating an explicit risk margin to take into consideration market participant estimates of projected cash flows and policyholder behavior.

AIGFP's Super Senior Credit Default Swap Portfolio

AIGFP values its credit default swaps written on the most senior risk layers (super senior) of designated pools of debt securities or loans using internal valuation models, third-party prices and market indices. The specific valuation methodologies vary based on the nature of the referenced obligations and availability of market prices. AIGFP uses a modified version of the Binomial Expansion Technique (BET) model to value its credit default swap portfolio written on super senior tranches of collateralized debt obligations (CDOs), including maturity-shortening puts that allow the holders of the securities issued by certain CDOs to treat the securities as short-term eligible 2a-7 investments under the Investment Company Act of 1940 (2a-7 Puts). The BET model uses default probabilities derived from credit spreads implied from market prices for the individual securities included in the underlying collateral pools securing the CDOs, as well as diversity scores, weighted average lives, recovery rates and discount rates. The determination of some of these inputs requires the use of judgment and estimates, particularly in the absence of market observable data. AIGFP also employs a Monte Carlo simulation to assist in quantifying the effect on the valuation of the CDOs of the unique aspects of the CDOs' structures such as triggers that divert cash flows to the most senior part of the capital structure. In the determination of fair value, AIGFP also considers collateral calls and the price estimates for the super senior CDO securities provided by third parties, including counterparties to these transactions.

In the case of credit default swaps written on investment-grade corporate debt and collateralized loan obligations (CLOs), AIGFP estimates the value of its obligations by reference to the relevant market indices or third-party quotes on the underlying super senior tranches where available.

In the case of credit default swaps written to facilitate regulatory capital relief for AIGFP's European financial institution counterparties, AIGFP estimates the fair value of these derivatives by considering observable market transactions, including the early termination of these transactions by counterparties, and other market data, to the extent relevant.

Policyholders' Contract Deposits

Policyholders' contract deposits accounted for at fair value beginning January 1, 2008 are measured using an income approach by taking into consideration the following factors:

- Current policyholder account values and related surrender charges,
- The present value of estimated future cash inflows (policy fees) and outflows (benefits and maintenance expenses) associated with the product using risk neutral valuations, incorporating expectations about policyholder behavior, market returns and other factors, and
- A risk margin that market participants would require for a market return and the uncertainty inherent in the model inputs.

The change in fair value of these policyholders' contract deposits is recorded as incurred policy losses and benefits in the consolidated statement of income (loss).

Fair Value Measurements on a Non-Recurring Basis

AIG also measures the fair value of certain assets on a non-recurring basis, generally quarterly, annually, or when events or changes in circumstances indicate that the carrying amount of the asset may not be recoverable. These assets include held to maturity securities, cost and equity-method investments, life settlement contracts, aircraft, collateral securing foreclosed loans and real estate and other fixed assets, goodwill, and other intangible assets. AIG uses a variety of techniques to measure the fair value of these assets when appropriate, as described below:

- *Held to Maturity Securities, Cost and Equity-Method Investments:* When AIG determines the carrying value of these assets may not be recoverable, AIG records the assets at fair value with the loss recognized in income. In such cases, AIG measures the fair value of these assets using the techniques discussed above for fixed maturities and equity securities.
- *Life Settlement Contracts:* AIG measures the fair value of individual life settlement contracts (which are included in other invested assets) whenever the carrying value plus the undiscounted future costs that are expected to be incurred to keep the life settlement contract in force exceed the expected proceeds from the contract. In those situations, the fair value is determined on a discounted cash flows basis, incorporating current life expectancy assumptions.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

3. Fair Value Measurements *(continued)*

The discount rate incorporates current information about market interest rates, the credit exposure to the insurance company that issued the life settlement contract and AIG's estimate of the risk margin an investor in the contracts would require.

- *Flight Equipment Primarily Under Operating Leases:* When AIG determines the carrying value of its commercial aircraft may not be recoverable, AIG records the aircraft at fair value with the loss recognized in income. AIG measures the fair value of its commercial aircraft using an income approach based on the present value of all cash flows from existing and projected lease payments (based on historical experience and current expectations of market participants) including net contingent rentals for the period extending to the end of the aircraft's economic life in its highest and best use configuration, plus its disposition value.
- *Collateral Securing Foreclosed Loans and Real Estate and Other Fixed Assets:* When AIG takes collateral in connection with foreclosed loans, AIG generally bases its estimate of fair value on the price that would be received in a current transaction to sell the asset by itself.
- *Goodwill:* AIG tests goodwill for impairment whenever events or changes in circumstances indicate the carrying amount of goodwill may not be recoverable, but at least annually. When AIG determines goodwill may be impaired, AIG uses techniques that consider market-based earnings multiples of the unit's peer companies or discounted cash flow techniques based on the price that could be received in a current transaction to sell the asset assuming the asset would be used with other assets as a group (in-use premise).
- *Intangible Assets:* AIG tests its intangible assets for impairment whenever events or changes in circumstances indicate the carrying amount of an intangible asset may not be recoverable. AIG measures the fair value of intangible assets based on an in-use premise that considers the same factors used to estimate the fair value of its real estate and other fixed assets under an in-use premise discussed above.

See Notes 1(c), (d), (e), (t), and (v) to Consolidated Financial Statements included in the 2007 Annual Report on Form 10-K for additional information about how AIG tests various asset classes for impairment.

Fair Value Hierarchy

Beginning January 1, 2008, assets and liabilities recorded at fair value in the consolidated balance sheet are measured and classified in a hierarchy for disclosure purposes consisting of three "levels" based on the observability of inputs available in the marketplace used to measure the fair values as discussed below:

- *Level 1:* Fair value measurements that are quoted prices (unadjusted) in active markets that AIG has the ability to access for identical assets or liabilities. Market price data generally is obtained from exchange or dealer markets. AIG does not adjust the quoted price for such instruments. Assets and liabilities measured at fair value on a recurring basis and classified as Level 1 include certain government and agency securities, actively traded listed common stocks and derivative contracts, most separate account assets and most mutual funds.
- *Level 2:* Fair value measurements based on inputs other than quoted prices included in Level 1 that are observable for the asset or liability, either directly or indirectly. Level 2 inputs include quoted prices for similar assets and liabilities in active markets, and inputs other than quoted prices that are observable for the asset or liability, such as interest rates and yield curves that are observable at commonly quoted intervals. Assets and liabilities measured at fair value on a recurring basis and classified as Level 2 generally include certain government securities, most investment-grade and high-yield corporate bonds, certain asset-backed securities, certain listed equities, state, municipal and provincial obligations, hybrid securities, mutual fund and hedge fund investments, derivative contracts, guaranteed investment agreements at AIGFP and physical commodities.
- *Level 3:* Fair value measurements based on valuation techniques that use significant inputs that are unobservable. These measurements include circumstances in which there is little, if any, market activity for the asset or liability. In certain cases, the inputs used to measure fair value may fall into different levels of the fair value hierarchy. In such cases, the level in the fair value hierarchy within which the fair value measurement in its entirety falls is determined based on the lowest level input that is significant to the fair value measurement in its entirety. AIG's assessment of the significance of a particular input to the fair value measurement in its entirety requires judgment. In making the assessment, AIG considers factors specific to the asset or liability. Assets and liabilities measured at fair value on a recurring basis and classified as Level 3 include certain distressed asset-backed securities, structured credit products, certain derivative contracts (including AIGFP's super senior credit default swap portfolio), policyholders' contract deposits carried at fair value, private equity and real estate fund investments, and direct private equity investments. AIG's non-financial-instrument assets that are measured at fair value on a non-recurring basis generally are classified as Level 3.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

3. Fair Value Measurements *(continued)*

Assets and Liabilities Measured at Fair Value on a Recurring Basis

The following table presents information about assets and liabilities measured at fair value on a recurring basis at March 31, 2008, and indicates the level of the fair value measurement based on the levels of the inputs used:

(in millions)	Level 1	Level 2	Level 3	Counterparty Netting	Total March 31, 2008
Assets:					
Bonds available for sale	$ 731	$377,558	$ 17,198	$ —	$395,487
Bond trading securities	2	9,257	116	—	9,375
Common stocks available for sale	15,473	398	251	—	16,122
Common and preferred stocks trading	19,814	1,832	25	—	21,671
Preferred stocks available for sale	—	2,318	133	—	2,451
Mortgage and other loans receivable	—	810	—	—	810
Financial Services assets:					
Securities available for sale	2	800	294	—	1,096
Trading securities	1,130	31,449	3,419	—	35,998
Spot commodities	—	728	—	—	728
Unrealized gain on swaps, options and forward transactions	—	72,071	3,582	(55,055)	20,598
Securities purchased under agreements to resell	—	19,708	—	—	19,708
Securities lending invested collateral[(a)]	—	45,904	10,611	—	56,515
Other invested assets[(b)]	2,739	7,550	11,399	—	21,688
Short-term investments[(a)]	—	21,280	—	—	21,280
Separate and variable accounts	68,820	3,088	1,065	—	72,973
Other assets	83	4,937	371	(268)	5,123
Total	$108,794	$599,688	$ 48,464	$ (55,323)	$701,623
Liabilities:					
Policyholders' contract deposits	$ —	$ —	$ 4,118	$ —	$ 4,118
Financial Services liabilities:					
Securities sold under agreements to repurchase	—	8,051	220	—	8,271
Securities and spot commodities sold but not yet purchased	399	3,407	—	—	3,806
Unrealized loss on swaps, options and forward transactions[(c)]	—	60,989	24,442	(55,055)	30,376
Trust deposits and deposits due to banks and other depositors	—	262	—	—	262
Long-term borrowings	—	56,416	2,838	—	59,254
Other liabilities	2	6,453	108	(268)	6,295
Total	$ 401	$135,578	$ 31,726	$ (55,323)	$112,382

(a) Included in Level 2 securities lending invested collateral and short-term investments are securities that are carried at cost, which approximates fair value, of $1.1 billion and $18.5 billion, respectively.

(b) Approximately 13 percent of the fair value of the assets recorded as Level 3 are a result of the consolidation of various private equity, hedge fund and fund-of-funds investments. AIG's ownership in these funds represented 23 percent, or $1.5 billion of the Level 3 amount.

(c) Included in Level 3 are unrealized market valuation losses of $20.6 billion on AIGFP super senior credit default swap portfolio.

At March 31, 2008, Level 3 assets totaled $48.5 billion, representing 5 percent of total assets, and Level 3 liabilities totaled $31.7 billion, representing 3 percent of total liabilities.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

3. Fair Value Measurements *(continued)*

The following table presents changes during the three-month period ended March 31, 2008 in Level 3 assets and liabilities measured at fair value on a recurring basis, together with the balances of such assets and liabilities at January 1, 2008 and March 31, 2008, and the realized and unrealized gains (losses) recorded in income during the three-month period ended March 31, 2008 related to the Level 3 assets and liabilities that remained on the consolidated balance sheet at March 31, 2008:

(in millions)	Balance January 1, 2008	Net Realized and Unrealized Gains (Losses) Included in Income*	Accumulated Other Comprehensive Income (Loss)	Purchases, Sales, Issuances and Settlements-net	Transfers In (out)	Balance March 31, 2008	Unrealized Gains (Losses) on Instruments Held at March 31, 2008
Assets:							
Bonds available for sale	$ 19,024	$ (1,049)	$(464)	$ (177)	$ (136)	$ 17,198	$ —
Bond trading securities	141	(25)	—	—	—	116	(12)
Common stocks available for sale	224	(1)	3	25	—	251	—
Common and preferred stocks trading	30	—	1	(6)	—	25	—
Preferred stocks available for sale	135	1	(2)	(8)	7	133	—
Financial Services assets:							
Securities available for sale	285	—	6	5	(2)	294	—
Trading securities	4,422	(962)	—	(10)	(31)	3,419	(963)
Securities lending invested collateral	12,890	(2,333)	167	(217)	104	10,611	—
Other invested assets	10,411	345	67	625	(49)	11,399	111
Separate and variable accounts	1,003	30	—	32	—	1,065	31
Other assets	158	24	1	188	—	371	25
Total	$ 48,723	$ (3,970)	$(221)	$ 457	$ (107)	$ 44,882	$ (808)
Liabilities:							
Policyholders' contract deposits	$ (3,674)	$ (186)	$ (64)	$ (194)	$ —	$ (4,118)	$ (199)
Financial Services liabilities:							
Securities sold under agreements to repurchase	(208)	(17)	—	5	—	(220)	(17)
Unrealized loss on swaps, options and forward transactions, net	(11,718)	(8,884)	—	(189)	(69)	(20,860)	(9,111)
Long-term borrowings	(3,578)	116	—	456	168	(2,838)	223
Other liabilities	(520)	(105)	—	517	—	(108)	82
Total	$ (19,698)	$ (9,076)	$ (64)	$ 595	$ 99	$ (28,144)	$ (9,022)

** Net realized and unrealized gains and losses shown above are reported on the consolidated statement of income (loss) primarily as follows:*

Major category of Assets/Liabilities	Consolidated Statement of Income (Loss) Line Items
Financial Services Assets and Liabilities	• Other income • Unrealized market valuation losses on AIGFP super senior credit default swap portfolio
Invested assets	• Net realized capital gains (losses)
Policyholders' contract deposits	• Incurred policy losses and benefits • Net realized capital gains (losses)

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

3. Fair Value Measurements *(continued)*

Both observable and unobservable inputs may be used to determine the fair values of positions classified in Level 3 in the tables above. As a result, the unrealized gains (losses) on instruments held at March 31, 2008 may include changes in fair value that were attributable to both observable (e.g., changes in market interest rates) and unobservable inputs (e.g., changes in unobservable long-dated volatilities).

AIG uses various hedging techniques to manage risks associated with certain positions, including those classified within Level 3. Such techniques may include the purchase or sale of financial instruments that are classified within Level 1 and/or Level 2. As a result, the realized and unrealized gains (losses) for assets and liabilities classified within Level 3 presented in the table above do not reflect the related realized or unrealized gains (losses) on hedging instruments that are classified within Level 1 and/or Level 2.

Changes in the fair value of separate and variable account assets are completely offset in the consolidated statement of income (loss) by changes in separate and variable account liabilities, which are not carried at fair value and therefore not included in the foregoing tables.

Fair Value Measured on a Non-Recurring Basis

At March 31, 2008, AIG had assets measured at fair value on a non-recurring basis on which it recorded an impairment charge totaling $45 million during the three-month period ended March 31, 2008. This charge resulted from the write-off of goodwill related to Mortgage Guaranty.

Fair Value Option

FAS 159 permits a company to choose to measure at fair value many financial instruments and certain other assets and liabilities that are not required to be measured at fair value. Subsequent changes in fair value for designated items are required to be reported in income. Unrealized gains and losses on financial instruments in AIG's insurance businesses and in AIGFP for which the fair value option was elected under FAS 159 are classified in incurred policy losses and benefits and in other income, respectively, in the consolidated statement of income (loss).

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

3. Fair Value Measurements *(continued)*

The following table presents the gains or losses recorded during the three-month period ended March 31, 2008 related to the eligible instruments for which AIG elected the fair value option and the related transition adjustment recorded as a decrease to opening shareholders' equity at January 1, 2008[(a)]:

(in millions)	January 1, 2008 prior to Adoption	Transition Adjustment upon Adoption	January 1, 2008 after Adoption	Gain (Loss) Three Months Ended March 31, 2008
Mortgage and other loans receivable	$ 1,109	$ —	$ 1,109	$ 68
Financial Services assets[(b)]:				
Trading securities (formerly available for sale)	39,278	5	39,283	(433)
Securities purchased under agreements to resell	20,950	1	20,951	268
Other invested assets	321	(1)	320	10
Short-term investments	6,969	—	6,969	24
Deferred policy acquisition costs	1,147	(1,147)	—	—
Other assets	435	(435)	—	—
Future policy benefits for life, accident and health insurance contracts	299	299	—	—
Policyholders' contract deposits[(c)]	3,739	360	3,379	115
Financial Services liabilities[(b)]:				
Securities sold under agreements to repurchase	6,750	(10)	6,760	(296)
Securities and spot commodities sold but not yet purchased	3,797	(10)	3,807	21
Trust deposits and deposits due to banks and other depositors	216	(25)	241	(15)
Long-term borrowings	57,968	(675)	58,643	(973)
Other liabilities	1,792	—	1,792	(33)
Total gain or loss for the three-month period ended March 31, 2008				$(1,244)
Pre-tax cumulative effect of adopting the fair value option		(1,638)		
Decrease in deferred tax liabilities		526		
Cumulative effect of adopting the fair value option		$(1,112)		

(a) Certain of AIG's financial instruments are required to be accounted for at fair value, with changes in fair value included in earnings, under FAS 115, "Accounting for Certain Investments in Debt and Equity Securities," or FAS 133 and are not included in the table above.

(b) AIGFP elected to apply the fair value option to all eligible assets and liabilities (other than equity method investments, trade receivables and trade payables) because electing the fair value option will allow AIGFP to more closely align its earnings with the economics of its transactions by recognizing concurrently through earnings the change in fair value of its derivatives and the offsetting change in fair value of the assets and liabilities being hedged as well as the manner in which the business is evaluated by management. Substantially all of the gain (loss) amounts shown above are reported in other income on the consolidated statement of income (loss).

(c) AIG elected to apply the fair value option to certain single premium variable life products in Japan and an investment-linked life insurance product sold principally in Asia, both classified within policyholders' contract deposits in the consolidated balance sheet. AIG elected the fair value option for these liabilities to more closely align its accounting with the economics of its transactions. For the investment-linked product sold principally in Asia, the election will more effectively align changes in the fair value of assets with a commensurate change in the fair value of policyholders' liabilities. For the single premium life products in Japan, the fair value option election will allow AIG to economically hedge the inherent market risks associated with this business in an efficient and effective manner through the use of derivative instruments. The hedging program, once finalized and implemented, will result in the accounting presentation for this business more closely mirroring the underlying economics and the way the business is managed, with the change in the fair value of derivatives and underlying assets largely offsetting the change in fair value of the policy liabilities. AIG did not elect the fair value option for other liabilities classified in policyholders' contract deposits because other contracts do not share the same contract features that created the disparity between the accounting presentation and the economic performance.

Interest income and expense and dividend income on assets and liabilities elected under the fair value option are recognized and classified in the consolidated statement of income (loss) depending on the nature of the instrument and related market conventions. At AIGFP, interest and dividends and interest expense are included in other income. Otherwise, interest and dividends are included in interest and dividend income or interest expense. See Note 1(a) to the Consolidated Financial Statements included in the 2007 Annual Report on Form 10-K for additional information about AIG's policies for recognition, measurement, and disclosure of interest and dividend income and interest expense.

During the three-month period ended March 31, 2008, AIG recognized gains of $1.4 billion attributable to the observable effect of the widening of credit spreads on AIG's own liabilities for which the fair value option was elected. AIG calculates the effect of these credit spread changes using discounted cash flow techniques that incorporate current

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

3. Fair Value Measurements *(continued)*

market interest rates, AIG's observable credit spreads on these liabilities and other factors that mitigate the risk of nonperformance such as collateral posted.

The following table presents the difference between fair values and the aggregate contractual principal amounts of mortgage and other loans receivable and long-term borrowings, for which the fair value option was elected.

(in millions)	Fair Value at March 31, 2008	Principal Amount Due Upon Maturity	Difference
Assets:			
Mortgage and other loans receivable	$ 810	$ 774	$ 36
Liabilities:			
Long-term borrowings	$ 53,057	$ 51,769	$ 1,288

At March 31, 2008, there were no mortgage and other loans receivable for which the fair value option was elected, that were 90 days or more past due and in non-accrual status.

4. Shareholders' Equity and Earnings (Loss) Per Share

Shareholders' Equity

The changes in AIG's consolidated shareholders' equity were as follows:

	Three Months Ended March 31,	
(in millions)	**2008**	2007
Beginning of year	**$95,801**	$101,677
Net income (loss)	**(7,805)**	4,130
Unrealized (depreciation) appreciation of investments, net of tax	**(6,824)**	851
Cumulative translation adjustment, net of tax	**1,095**	(137)
Dividends to shareholders	**(488)**	(430)
Payments advanced to purchase shares, net	**733**	(2,851)
Share purchases	**(1,733)**	—
Cumulative effect of accounting changes, net of tax	**(1,108)**	(203)
Other*	**32**	18
End of period	**$79,703**	$103,055

** Reflects the effects of employee stock transactions.*

From time to time, AIG may buy shares of its common stock for general corporate purposes, including to satisfy its obligations under various share-based employee compensation plans. In February 2007, AIG's Board of Directors increased AIG's share repurchase program by authorizing the purchase of shares with an aggregate purchase price of $8 billion. In November 2007, AIG's Board of Directors authorized the purchase of an additional $8 billion in common stock. In 2007, AIG entered into structured share repurchase arrangements providing for the purchase of shares over time with an aggregate purchase price of $7 billion.

A total of 34,093,783 shares were purchased during the first quarter of 2008 to meet commitments that existed at December 31, 2007. The portion of the payments advanced by AIG under the structured share purchase arrangements that had not yet been utilized to purchase shares at March 31, 2008, amounting to $179 million, has been recorded as a component of shareholders' equity under the caption, Payments advanced to purchase shares. Subsequent to March 31, 2008, an additional 3,832,276 shares were purchased, satisfying the balance of the commitments existing at December 31, 2007 that had not been satisfied at March 31, 2008. All shares purchased are recorded as treasury stock at cost.

At May 7, 2008, $9 billion was available for purchases under the aggregate authorization. AIG does not expect to purchase additional shares under its share repurchase program for the foreseeable future.

The quarterly dividend of $0.20 per common share declared in November 2007 was paid on March 21, 2008.

Share-based Employee Compensation Plans

During the first quarter of 2008, AIG reviewed the vesting schedules of its share-based employee compensation plans, and on March 11, 2008, AIG's management and the Compensation Committee of AIG's Board of Directors determined that, to fulfill the objective of attracting and retaining high quality personnel, the vesting schedules of certain awards outstanding under these plans and all awards made in the future under these plans should be shortened. As a result, the unamortized share-based employee compensation cost related to the affected awards will be amortized over shorter periods. AIG estimates the modifications will accelerate the amortization of this cost by $116 million and $90 million in 2008 and 2009, respectively, with a corresponding reduction in amortization expense related to these awards of $206 million in 2010 through 2013.

Earnings (Loss) Per Share (EPS)

Basic EPS is based on the weighted average number of common shares outstanding, adjusted to reflect all stock dividends and stock splits. Diluted EPS is based on those shares used in basic EPS plus shares that would have been outstanding assuming issuance of common shares for all dilutive potential common shares outstanding, adjusted to reflect all stock dividends and stock splits.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

4. Shareholders' Equity and Earnings (Loss) Per Share *(continued)*

The computation of basic and diluted EPS was as follows:

(in millions, except per share data)	Three Months Ended March 31, **2008**	2007
Numerator for EPS:		
Net income (loss)	**$ (7,805)**	$4,130
Denominator for EPS:		
Weighted average shares outstanding used in the computation of EPS:		
Common stock issued	**2,751**	2,751
Common stock in treasury	**(237)**	(150)
Deferred shares	**14**	11
Weighted average shares outstanding – basic	**2,528**	2,612
Incremental shares arising from awards outstanding under share-based employee compensation plans *	**–**	9
Weighted average shares outstanding – diluted*	**2,528**	2,621
EPS:		
Basic	**$ (3.09)**	$ 1.58
Diluted	**$ (3.09)**	$ 1.58

* *Calculated using the treasury stock method. Certain potential common shares arising from share-based employee compensation plans were not included in the computation of diluted EPS because the effect would have been antidilutive. The number of potential shares excluded was 7 million for the three-month period ended March 31, 2007.*

5. Ownership

According to the Schedule 13D filed on March 20, 2007 by Starr, SICO, Edward E. Matthews, Maurice R. Greenberg, the Maurice R. and Corinne P. Greenberg Family Foundation, Inc., the Universal Foundation, Inc., the Maurice R. and Corinne P. Greenberg Joint Tenancy Company, LLC and the C.V. Starr & Co., Inc. Trust, these reporting persons could be considered to beneficially own 354,987,261 shares of AIG's common stock at that date. Based on the shares of AIG's common stock outstanding at April 30, 2008, this ownership would represent approximately 14 percent of the voting stock of AIG. Although these reporting persons have made filings under Section 16 of the Exchange Act, reporting sales of shares of common stock, no amendment to the Schedule 13D has been filed to report a change in ownership subsequent to March 20, 2007.

6. Commitments, Contingencies and Guarantees

AIG and its subsidiaries, in common with the insurance and financial services industries in general, are subject to litigation, including claims for punitive damages, in the normal course of their business. At the current time, AIG cannot predict the outcome of the matters described below, or estimate any potential additional costs related to these matters, unless otherwise indicated. In AIG's insurance operations, litigation arising from claims settlement activities is generally considered in the establishment of AIG's reserve for losses and loss expenses. However, the potential for increasing jury awards and settlements makes it difficult to assess the ultimate outcome of such litigation. In addition, in the normal course of business, various commitments and contingent liabilities are entered into by AIG and certain of its subsidiaries. AIG also guarantees various obligations of certain subsidiaries.

(a) Litigation and Investigations

Litigation Arising from Insurance Operations – Caremark. AIG and certain of its subsidiaries have been named defendants in two putative class actions in state court in Alabama that arise out of the 1999 settlement of class and derivative litigation involving Caremark Rx, Inc. (Caremark). The plaintiffs in the second-filed action have intervened in the first-filed action, and the second-filed action has been dismissed. An excess policy issued by a subsidiary of AIG with respect to the 1999 litigation was expressly stated to be without limit of liability. In the current actions, plaintiffs allege that the judge approving the 1999 settlement was misled as to the extent of available insurance coverage and would not have approved the settlement had he known of the existence and/or unlimited nature of the excess policy. They further allege that AIG, its subsidiaries, and Caremark are liable for fraud and suppression for misrepresenting and/or concealing the nature and extent of coverage. In addition, the intervenor-plaintiffs allege that various lawyers and law firms who represented parties in the underlying class and derivative litigation (the Lawyer Defendants) are also liable for fraud and suppression, misrepresentation, and breach of fiduciary duty. The complaints filed by the plaintiffs and the intervenor-plaintiffs request compensatory damages for the 1999 class in the amount of $3.2 billion, plus punitive damages. AIG and its subsidiaries deny the allegations of fraud and suppression

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

6. Commitments, Contingencies and Guarantees *(continued)*

and have asserted that information concerning the excess policy was publicly disclosed months prior to the approval of the settlement. AIG and its subsidiaries further assert that the current claims are barred by the statute of limitations and that plaintiffs' assertions that the statute was tolled cannot stand against the public disclosure of the excess coverage. The plaintiffs and intervenor-plaintiffs, in turn, have asserted that the disclosure was insufficient to inform them of the nature of the coverage and did not start the running of the statute of limitations. On November 26, 2007, the trial court issued an order that dismissed the intervenors' complaint against the Lawyer Defendants and entered a final judgment in favor of the Lawyer Defendants. The intervenors are appealing the dismissal of the Lawyer Defendants and on January 2, 2008, requested a stay of all trial court proceedings pending the appeal. On March 4, 2008, the trial court granted the motion for a stay. No further proceedings at the trial court level will occur until the appeal of the dismissal of the Lawyer Defendants is resolved. AIG cannot reasonably estimate either the likelihood of its prevailing in these actions or the potential damages in the event liability is determined.

Litigation Arising from Insurance Operations – Gunderson. A subsidiary of AIG has been named as a defendant in a putative class action lawsuit in the 14th Judicial District Court for the State of Louisiana. The *Gunderson* complaint alleges failure to comply with certain provisions of the Louisiana Any Willing Provider Act (the Act) relating to discounts taken by defendants on bills submitted by Louisiana medical providers and hospitals that provided treatment or services to workers compensation claimants and seeks monetary penalties and injunctive relief. On July 20, 2006, the court denied defendants' motion for summary judgment and granted plaintiffs' partial motion for summary judgment, holding that the AIG subsidiary was a "group purchaser" and, therefore, potentially subject to liability under the Act. On November 28, 2006, the court issued an order certifying a class of providers and hospitals. In an unrelated action also arising under the Act, a Louisiana appellate court ruled that the district court lacked jurisdiction to adjudicate the claims at issue. In response, defendants in *Gunderson* filed an exception for lack of subject matter jurisdiction. On January 19, 2007, the court denied the motion, holding that it has jurisdiction over the putative class claims. The AIG subsidiary appealed the class certification and jurisdictional rulings. While the appeal was pending, the AIG subsidiary settled the lawsuit. On January 25, 2008, plaintiffs and the AIG subsidiary agreed to resolve the lawsuit on a class-wide basis for approximately $29 million. The court has preliminarily approved the settlement and will hold a final approval hearing on May 29, 2008. In the event that the settlement is not finally approved, AIG believes that it has meritorious defenses to plaintiffs' claims and expects that the ultimate resolution of this matter will not have a material adverse effect on AIG's consolidated financial condition or results of operations for any period.

2006 Regulatory Settlements. In February 2006, AIG reached a resolution of claims and matters under investigation with the United States Department of Justice (DOJ), the Securities and Exchange Commission (SEC), the Office of the New York Attorney General (NYAG) and the New York State Department of Insurance (DOI). AIG recorded an after-tax charge of $1.15 billion relating to these settlements in the fourth quarter of 2005.

The settlements resolved investigations conducted by the SEC, NYAG and DOI in connection with the accounting, financial reporting and insurance brokerage practices of AIG and its subsidiaries, as well as claims relating to the underpayment of certain workers compensation premium taxes and other assessments. These settlements did not, however, resolve investigations by regulators from other states into insurance brokerage practices related to contingent commissions and other broker-related conduct, such as alleged bid rigging. Nor did the settlements resolve any obligations that AIG may have to state guarantee funds in connection with any of these matters.

As a result of these settlements, AIG made payments or placed amounts in escrow in 2006 totaling approximately $1.64 billion, $225 million of which represented fines and penalties. Amounts held in escrow totaling $346 million, including interest thereon, are included in other assets at March 31, 2008. At that date, approximately $332 million of the funds were escrowed for settlement of claims resulting from the underpayment by AIG of its residual market assessments for workers compensation.

The remaining escrowed funds, which amounted to $14 million, were set aside to pay certain AIG insurance company subsidiary policyholders who purchased excess casualty policies through Marsh & McLennan Companies, Inc. (Marsh) and Marsh Inc. (the Excess Casualty Fund). As of February 29, 2008, eligible policyholders entitled to receive approximately $359 million (or 95 percent) of the Excess Casualty Fund had opted to receive settlement payments in exchange for releasing AIG and its subsidiaries from liability relating to certain insurance brokerage practices. In accordance with the settlement agreements, all amounts remaining in the Excess Casualty Fund were used by AIG to settle claims asserted by other policyholders relating to such practices.

In addition to the escrowed funds, $800 million was deposited into a fund under the supervision of the SEC as part of the settlements to be available to resolve claims asserted

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

6. Commitments, Contingencies and Guarantees *(continued)*

against AIG by investors, including the shareholder lawsuits described herein.

Also, as part of the settlements, AIG agreed to retain, for a period of three years, an independent consultant to conduct a review that will include, among other things, the adequacy of AIG's internal control over financial reporting, the policies, procedures and effectiveness of AIG's regulatory, compliance and legal functions and the remediation plan that AIG has implemented as a result of its own internal review.

Other Regulatory Settlements. As noted above, AIG's 2006 regulatory settlements with the SEC, DOJ and NYAG did not resolve investigations by regulators from other states into insurance brokerage practices. AIG entered into agreements effective January 29, 2008 with the Attorneys General of the States of Florida, Hawaii, Maryland, Michigan, Oregon, Texas and West Virginia; the Commonwealths of Massachusetts and Pennsylvania; and the District of Columbia; as well as the Florida Department of Financial Services and the Florida Office of Insurance Regulation, relating to their respective industry wide investigations into producer compensation and insurance placement practices. The settlements call for total payments of $12.5 million to be allocated among the ten jurisdictions representing restitution to state agencies and reimbursement of the costs of the investigation. During the term of the settlement agreements, AIG will continue to maintain certain producer compensation disclosure and ongoing compliance initiatives. AIG will also continue to cooperate with the industry wide investigations. The agreement with the Texas Attorney General also settles allegations of anticompetitive conduct relating to AIG's relationship with Allied World Assurance Company and includes an additional settlement payment of $500,000 related thereto.

AIG also entered into an agreement effective March 13, 2008 with the Pennsylvania Insurance Department relating to the Department's investigation into the affairs of AIG and certain of its Pennsylvania-domiciled insurance company subsidiaries. The settlement calls for total payments of approximately $13.5 million, of which approximately $4.4 million was paid under previous settlement agreements. During the term of the settlement agreement, AIG will provide annual reinsurance reports, as well as maintain certain producer compensation disclosure and ongoing compliance initiatives.

In addition, AIG has settled litigation that was filed by the Minnesota Attorney General with respect to claims by the Minnesota Department of Revenue and the Minnesota Special Compensation Fund that AIG underreported its workers' compensation premium.

Private Litigation

Securities Actions – Southern District of New York. Beginning in October 2004, a number of putative securities fraud class action suits were filed in the Southern District of New York against AIG and consolidated as *In re American International Group, Inc. Securities Litigation*. Subsequently, a separate, though similar, securities fraud action was also brought against AIG by certain Florida pension funds. The lead plaintiff in the class action is a group of public retirement systems and pension funds benefiting Ohio state employees, suing on behalf of themselves and all purchasers of AIG's publicly traded securities between October 28, 1999 and April 1, 2005. The named defendants are AIG and a number of present and former AIG officers and directors, as well as Starr, SICO, General Reinsurance Corporation, and PricewaterhouseCoopers LLP (PwC), among others. The lead plaintiff alleges, among other things, that AIG: (1) concealed that it engaged in anti-competitive conduct through alleged payment of contingent commissions to brokers and participation in illegal bid-rigging; (2) concealed that it used "income smoothing" products and other techniques to inflate its earnings; (3) concealed that it marketed and sold "income smoothing" insurance products to other companies; and (4) misled investors about the scope of government investigations. In addition, the lead plaintiff alleges that AIG's former Chief Executive Officer manipulated AIG's stock price. The lead plaintiff asserts claims for violations of Sections 11 and 15 of the Securities Act of 1933, Section 10(b) of the Exchange Act and Rule 10b-5 promulgated thereunder, Section 20(a) of the Exchange Act, and Section 20A of the Exchange Act. In April 2006, the court denied the defendants' motions to dismiss the second amended class action complaint and the Florida complaint. In December 2006, a third amended class action complaint was filed, which does not differ substantially from the prior complaint. Fact and class discovery is currently ongoing. On February 20, 2008, the lead plaintiff filed a motion for class certification.

ERISA Actions – Southern District of New York. Between November 30, 2004 and July 1, 2005, several Employee Retirement Income Security Act of 1974 (ERISA) actions were filed in the Southern District of New York on behalf of purported class participants and beneficiaries of three pension plans sponsored by AIG or its subsidiaries. A consolidated complaint filed on September 26, 2005 alleges a class period between September 30, 2000 and May 31, 2005 and names as defendants AIG, the members of AIG's Retirement Board and the Administrative Boards of the plans at issue, and present or former members of AIG's Board of Directors. The factual allegations in the complaint are essentially identical to those in the securities actions described above. The parties have reached an agreement in principle to settle this matter for an amount within AIG's insurance cov-

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

6. Commitments, Contingencies and Guarantees *(continued)*

erage limits. The court has scheduled a hearing for May 29, 2008 to consider preliminary approval of the settlement, prior to which a formal settlement agreement is to be submitted by the parties.

Securities Action – Oregon State Court. On February 27, 2008, the State of Oregon, by and through the Oregon State Treasurer, and the Oregon Public Employee Retirement Board, on behalf of the Oregon Public Employee Retirement Fund, filed a lawsuit in Oregon state court against AIG for damages arising out of plaintiffs' purchase of AIG common stock at prices that allegedly were inflated. Plaintiffs allege, among other things, that AIG: (1) made false and misleading statements concerning its accounting for a $500 million transaction with General Re; (2) concealed that it marketed and misrepresented its control over off-shore entities in order to improve financial results; (3) improperly accounted for underwriting losses as investment losses in connection with transactions involving CAPCO Reinsurance Company, Ltd. and Union Excess; (4) misled investors about the scope of government investigations; and (5) engaged in market manipulation through its then Chairman and CEO Maurice R. Greenberg. The complaint asserts claims for violations of Oregon securities law, and seeks compensatory damages in an amount in excess of $15 million, and prejudgment interest and costs and fees. On April 9, 2008, AIG removed the case to federal court and filed a motion to have the case transferred to the Southern District of New York.

Derivative Actions – Southern District of New York. On November 20, 2007, two purported shareholder derivative actions were filed in the Southern District of New York naming as defendants the current directors of AIG and certain senior officers of AIG and its subsidiaries. Plaintiffs assert claims for breach of fiduciary duty, waste of corporate assets and unjust enrichment, as well as violations of Section 10(b) of the Exchange Act and Rule 10b-5 promulgated thereunder, and Section 20(a) of the Exchange Act, among other things, in connection with AIG's public disclosures regarding its exposure to what the lawsuits describe as the subprime market crisis. The actions were consolidated as *In re American International Group, Inc. 2007 Derivative Litigation*. On February 15, 2008, plaintiffs filed a consolidated amended complaint alleging the same causes of action. On April 15, 2008, motions to dismiss the action were filed on behalf of all defendants. AIG may become subject to litigation with respect to these or similar issues.

Between October 25, 2004 and July 14, 2005, seven separate derivative actions were filed in the Southern District of New York, five of which were consolidated into a single action. The New York derivative complaint contains nearly the same types of allegations made in the securities fraud action. The named defendants include current and former officers and directors of AIG, as well as Marsh, SICO, Starr, ACE Limited and subsidiaries (ACE), General Reinsurance Corporation, PwC, and certain employees or officers of these entity defendants. Plaintiffs assert claims for breach of fiduciary duty, gross mismanagement, waste of corporate assets, unjust enrichment, insider selling, auditor breach of contract, auditor professional negligence and disgorgement from AIG's former Chief Executive Officer and Chief Financial Officer of incentive-based compensation and AIG share proceeds under Section 304 of the Sarbanes-Oxley Act, among others. Plaintiffs seek, among other things, compensatory damages, corporate governance reforms, and a voiding of the election of certain AIG directors. AIG's Board of Directors has appointed a special committee of independent directors (special committee) to review the matters asserted in the operative consolidated derivative complaint. The court has entered an order staying the derivative case in the Southern District of New York pending resolution of the consolidated derivative action in the Delaware Chancery Court (discussed below). The court also has entered an order that termination of certain named defendants from the Delaware derivative action applies to the New York derivative action without further order of the court. On October 17, 2007, plaintiffs and those AIG officer and director defendants against whom the shareholder plaintiffs in the Delaware action are no longer pursuing claims filed a stipulation providing for all claims in the New York action against such defendants to be dismissed with prejudice. Former directors and officers Maurice R. Greenberg and Howard I. Smith have asked the court to refrain from so ordering this stipulation.

Derivative Actions – Delaware Chancery Court. From October 2004 to April 2005, AIG shareholders filed five derivative complaints in the Delaware Chancery Court. All of these derivative lawsuits were consolidated into a single action as *In re American International Group, Inc. Consolidated Derivative Litigation*. The amended consolidated complaint named 43 defendants (not including nominal defendant AIG) who, like the New York consolidated derivative litigation, were current and former officers and directors of AIG, as well as other entities and certain of their current and former employees and directors. The factual allegations, legal claims and relief sought in the Delaware action are similar to those alleged in the New York derivative actions, except that shareholder plaintiffs in the Delaware derivative action assert claims only under state law. Earlier in 2007, the court approved an agreement that AIG be realigned as plaintiff, and, on June 13, 2007, acting on the direction of the special committee, AIG filed an amended complaint against former directors and officers Maurice R. Greenberg and Howard I. Smith, alleging breach of fiduciary duty and indemnification. Also on June 13, 2007, the special committee filed a motion to

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

6. Commitments, Contingencies and Guarantees *(continued)*

terminate the litigation as to certain defendants, while taking no action as to others. Defendants Greenberg and Smith filed answers to AIG's complaint and brought third-party complaints against certain current and former AIG directors and officers, PwC and Regulatory Insurance Services, Inc. On September 28, 2007, AIG and the shareholder plaintiffs filed a combined amended complaint in which AIG continued to assert claims against defendants Greenberg and Smith and took no position as to the claims asserted by the shareholder plaintiffs in the remainder of the combined amended complaint. In that pleading, the shareholder plaintiffs are no longer pursuing claims against certain AIG officers and directors. In November 2007, the shareholder plaintiffs moved to sever their claims to a separate action. AIG joined the motion to the extent that, among other things, the claims against defendants Greenberg and Smith would remain in prosecution in the pending action. In addition, a number of parties, including AIG, filed motions to stay discovery. On February 12, 2008, the court granted AIG's motion to stay discovery pending the resolution of claims against AIG in the New York consolidated securities action. The court also denied plaintiff's motion to sever and directed the parties to coordinate a briefing schedule for the motions to dismiss. On April 11, 2008, the shareholder plaintiffs filed the First Amended Combined Complaint, which adds claims against Maurice Greenberg, Edward Matthews, and Thomas Tizzio for breach of fiduciary duty based on alleged bid-rigging in the municipal derivatives market. On April 15, 2008, shareholder plaintiffs submitted a stipulation dismissing Evan Greenberg without prejudice.

A separate derivative lawsuit was filed in the Delaware Chancery Court against twenty directors and executives of AIG as well as against AIG as a nominal defendant that alleges, among other things, that the directors of AIG breached the fiduciary duties of loyalty and care by approving the payment of commissions to Starr and of rental and service fees to SICO and the executives breached their duty of loyalty by causing AIG to enter into contracts with Starr and SICO and their fiduciary duties by usurping AIG's corporate opportunity. The complaint further alleges that the Starr agencies did not provide any services that AIG was not capable of providing itself, and that the diversion of commissions to these entities was solely for the benefit of Starr's owners. The complaint also alleges that the service fees and rental payments made to SICO and its subsidiaries were improper. Under the terms of a stipulation approved by the court on February 16, 2006, the claims against the outside independent directors were dismissed with prejudice, while the claims against the other directors were dismissed without prejudice. On October 31, 2005, Defendants Greenberg, Matthews and Smith, SICO and Starr filed motions to dismiss the amended complaint. In an opinion dated June 21, 2006, the Court denied defendants' motion to dismiss, except with respect to plaintiff's challenge to payments made to Starr before January 1, 2000. On July 21, 2006, plaintiff filed its second amended complaint, which alleges that, between January 1, 2000 and May 31, 2005, individual defendants breached their duty of loyalty by causing AIG to enter into contracts with Starr and SICO and breached their fiduciary duties by usurping AIG's corporate opportunity. Starr is charged with aiding and abetting breaches of fiduciary duty and unjust enrichment for its acceptance of the fees. SICO is no longer named as a defendant. On April 20, 2007, the individual defendants and Starr filed a motion seeking leave of the Court to assert a cross-claim against AIG and a third-party complaint against PwC and the directors previously dismissed from the action, as well as certain other AIG officers and employees. On June 13, 2007, the court denied the individual defendants' motion to file a third-party complaint, but granted the proposed cross-claim against AIG. On June 27, 2007, Starr filed its cross-claim against AIG, alleging one count that includes contribution, unjust enrichment and set-off. AIG has filed an answer and moved to dismiss Starr's cross-claim to the extent it seeks affirmative relief, as opposed to a reduction in the judgment amount. On November 15, 2007, the court granted AIG's motion to dismiss the cross-claim by Starr to the extent that it sought affirmative relief from AIG. On November 21, 2007, shareholder plaintiff submitted a motion for leave to file its third amended complaint in order to add Thomas Tizzio as a defendant. On February 14, 2008, the court granted this motion and allowed Mr. Tizzio until April 2008 to take additional discovery. Document discovery and depositions are otherwise complete. Plaintiff has informed the court that the parties do not intend to file motions for summary judgment. Trial is currently scheduled to begin in September 2008.

Derivative Action – Supreme Court of New York, Nassau County. On February 29, 2008, a purported shareholder derivative complaint was filed in the Supreme Court of Nassau County, asserting the same state law claims against the same defendants as in the consolidated amended complaint filed on February 15, 2008 in the Southern District of New York, *In re American International Group, Inc. 2007 Derivative Litigation,* which is discussed above.

Policyholder Actions. After the NYAG filed its complaint against insurance broker Marsh, policyholders brought multiple federal antitrust and Racketeer Influenced and Corrupt Organizations Act (RICO) class actions in jurisdictions across the nation against insurers and brokers, including AIG and a number of its subsidiaries, alleging that the insurers and brokers engaged in a broad conspiracy to allocate customers, steer business, and rig bids. These actions,

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

6. Commitments, Contingencies and Guarantees *(continued)*

including 24 complaints filed in different federal courts naming AIG or an AIG subsidiary as a defendant, were consolidated by the judicial panel on multi-district litigation and transferred to the United States District Court for the District of New Jersey for coordinated pretrial proceedings. The consolidated actions have proceeded in that court in two parallel actions, *In re Insurance Brokerage Antitrust Litigation* (the *Commercial Complaint*) and *In re Employee Benefit Insurance Brokerage Antitrust Litigation* (the *Employee Benefits Complaint,* and, together with the *Commercial Complaint,* the multi-district litigation).

The plaintiffs in the *Commercial Complaint* are a group of corporations, individuals and public entities that contracted with the broker defendants for the provision of insurance brokerage services for a variety of insurance needs. The broker defendants are alleged to have placed insurance coverage on the plaintiffs' behalf with a number of insurance companies named as defendants, including AIG subsidiaries. The *Commercial Complaint* also named various brokers and other insurers as defendants (two of which have since settled). The *Commercial Complaint* alleges, among other things, that defendants engaged in a widespread conspiracy to allocate customers through "bid-rigging" and "steering" practices. Plaintiffs assert that the defendants violated the Sherman Antitrust Act, RICO, and the antitrust laws of 48 states and the District of Columbia, and are liable under common law breach of fiduciary duty and unjust enrichment theories. Plaintiffs seek treble damages plus interest and attorneys' fees as a result of the alleged RICO and Sherman Antitrust Act violations.

The plaintiffs in the *Employee Benefits Complaint* are a group of individual employees and corporate and municipal employers alleging claims on behalf of two separate nationwide purported classes: an employee class and an employer class that acquired insurance products from the defendants from August 26, 1994 to the date of any class certification. The *Employee Benefits Complaint* names AIG, as well as various other brokers and insurers, as defendants. The activities alleged in the *Employee Benefits Complaint,* with certain exceptions, track the allegations made in the *Commercial Complaint*.

The Court in connection with the Commercial Complaint granted (without leave to amend) defendants' motions to dismiss the federal antitrust and RICO claims on August 31, 2007 and September 28, 2007, respectively. The court declined to exercise supplemental jurisdiction over the state law claims in the *Commercial Complaint* and therefore dismissed it in its entirety. On January 14, 2008, the court granted defendants' motion for summary judgment on the ERISA claims in the *Employee Benefits Complaint* and subsequently dismissed the remaining state law claims without prejudice, thereby dismissing the *Employee Benefits Complaint* in its entirety. On February 12, 2008, plaintiffs filed a notice of appeal to the United States Court of Appeals for the Third Circuit with respect to the dismissal of the *Employee Benefits Complaint*. Plaintiffs previously appealed the dismissal of the *Commercial Complaint* to the United States Court of Appeals for the Third Circuit on October 10, 2007. On February 19, 2008, appellants filed their appeal brief with the Third Circuit with respect to the *Commercial Complaint*, and appellees filed their brief on April 7, 2008. Oral argument has not yet been scheduled in that appeal.

A number of complaints making allegations similar to those in the multi-district litigation have been filed against AIG and other defendants in state and federal courts around the country. The defendants have thus far been successful in having the federal actions transferred to the District of New Jersey and consolidated into the multi-district litigation. These additional consolidated actions are still pending in the District Court, but are currently stayed pending a decision by the court on whether they will proceed during the appeal of the dismissal of the multi-district litigation. The AIG defendants have also sought to have state court actions making similar allegations stayed pending resolution of the multi-district litigation proceeding. These efforts have generally been successful, although plaintiffs in one case pending in Texas state court have moved to re-open discovery; a hearing on that motion was held on April 9, 2008 at which the court deferred ruling on the motion until defendants file their Special Exceptions. Using amounts from the Excess Casualty Fund described above, AIG has recently settled several of the various federal and state actions alleging claims similar to those in the multi-district litigation, including a state court action pending in Florida in which discovery had been allowed to proceed.

Ohio Attorney General Action. On August 24, 2007, the Ohio Attorney General filed a complaint in the Ohio Court of Common Pleas against AIG and a number of its subsidiaries, as well as several other broker and insurer defendants, asserting violation of Ohio's antitrust laws. The complaint, which is similar to the *Commercial Complaint*, alleges that AIG and the other broker and insurer defendants conspired to allocate customers, divide markets, and restrain competition in commercial lines of casualty insurance sold through the broker defendant. The complaint seeks treble damages on behalf of Ohio public purchasers of commercial casualty insurance, disgorgement on behalf of both public and private purchasers of commercial casualty insurance, as well as a $500 per day penalty for each day of conspiratorial conduct. AIG, along with other co-defendants, moved to dismiss the complaint on November 16, 2007. Discovery is

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

6. Commitments, Contingencies and Guarantees *(continued)*

stayed in the case pending a ruling on the motion to dismiss or until May 15, 2008, whichever occurs first.

Workers' Compensation Litigation. On May 24, 2007, the National Workers Compensation Reinsurance Pool (the NWCRP), on behalf of its participant members, filed a lawsuit in the United States District Court for the Northern District of Illinois against AIG with respect to the underpayment by AIG of its residual market assessments for workers compensation. The complaint alleges claims for violations of RICO, breach of contract, fraud and related state law claims arising out of AIG's alleged underpayment of these assessments between 1970 and the present and seeks damages purportedly in excess of $1 billion. On August 6, 2007, the court denied AIG's motion seeking to dismiss or stay the complaint or, in the alternative, to transfer to the Southern District of New York. On December 26, 2007, the court denied AIG's motion to dismiss the complaint. AIG filed its answer on January 22, 2008. On March 17, 2008, AIG filed an amended answer, counterclaims and third-party claims against NCCI (in its capacity as attorney-in-fact for the NWCRP), the NWCRP, its board members, and certain of the other insurance companies that are members of the NWCRP. The counterclaims and third-party claims allege violations of RICO, as well as claims for conspiracy, fraud, and other state law claims. On April 3, 2008, the court entered an order staying discovery through June 17, 2008.

In addition, a similar lawsuit was filed by the Minnesota Workers Compensation Reinsurance Association and the Minnesota Workers Compensation Insurers Association in the United States District Court for the District of Minnesota. On August 6, 2007, AIG moved to dismiss the complaint. On March 28, 2008, the court granted that motion and dismissed the case in its entirety. On April 25, 2008, plaintiffs filed a notice of appeal of the dismissal with the United States Court of Appeals for the Eighth Circuit. On the same day, plaintiffs filed a new complaint making similar allegations in Minnesota state court. A purported class action was also filed in the United States District Court for the District of South Carolina on January 25, 2008 against AIG and certain of its subsidiaries, on behalf of a class of employers that obtained workers' compensation insurance from AIG companies and allegedly paid inflated premiums as a result of AIG's alleged underreporting of workers' compensation premiums. An amended complaint in the South Carolina action was filed on March 24, 2008, and AIG filed a motion to dismiss the amended complaint on April 21, 2008.

SICO. In July, 2005, SICO filed a complaint against AIG in the Southern District of New York, claiming that AIG had refused to provide SICO access to certain artwork and asked the court to order AIG immediately to release the property to SICO. AIG filed an answer denying SICO's allegations and setting forth defenses to SICO's claims. In addition, AIG filed counterclaims asserting breach of contract, unjust enrichment, conversion, breach of fiduciary duty, a constructive trust and declaratory judgment, relating to SICO's breach of its commitment to use its AIG shares only for the benefit of AIG and AIG employees. Fact and expert discovery has been concluded and SICO's motion for summary judgment is pending.

Starr Foundation. On May 7, 2008, the Starr Foundation filed a complaint in New York State Supreme Court against AIG, Martin Sullivan and Steven Bensinger, asserting a claim for common law fraud. The Starr Foundation is a not-for-profit corporation that holds approximately 15.4 million shares of AIG stock, and was created by AIG's founder, Cornelius Vander Starr. The complaint alleges that the defendants made materially misleading statements and omissions concerning alleged multi-billion dollar losses in AIG's portfolio of credit default swaps. The complaint asserts that if the Starr Foundation had known the truth about the alleged losses, it would have sold its remaining shares of AIG stock. The complaint alleges that the Starr Foundation has suffered damages of at least $300 million.

Regulatory Investigations. Various federal, state and foreign regulatory and governmental agencies are reviewing certain public disclosures, transactions and practices of AIG and its subsidiaries in connection with industry wide and other inquiries. AIG has cooperated, and will continue to cooperate, in producing documents and other information in response to subpoenas and other requests. During 2006, the Settlement Review Working Group of the National Association of Insurance Commissioners (NAIC), under the direction of Indiana, Minnesota and Rhode Island, began an investigation into the underreporting of workers' compensation premiums. In late 2007, the Settlement Review Working Group recommended that a multi-state targeted market conduct examination focusing on workers' compensation insurance be commenced under the direction of the NAIC's Market Analysis Working Group. AIG was informed of the multi-state targeted market conduct examination in January of 2008. AIG has been advised that the lead states in the multi-state examination are Delaware, Florida, Indiana, Massachusetts, Minnesota, Pennsylvania and Rhode Island and that all other states (and the District of Columbia) have agreed to participate with the exception of New York, Ohio and Nevada. AIG has also been advised that the examination will focus on both legacy issues and AIG's current compliance with legal requirements applicable to AIG's writing and reporting of workers' compensation insurance. Although AIG has been advised by counsel engaged by the lead states to assist in their investigation, to date no determinations have been made with

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

6. Commitments, Contingencies and Guarantees *(continued)*

respect to these issues. AIG cannot predict the outcome of the investigation and there can be no assurance that any regulatory action resulting from the investigation will not have a material adverse effect on AIG's consolidated results of operations for an individual reporting period as well as on the ongoing operations of certain of AIG's businesses.

Wells Notices. AIG understands that some of its employees have received Wells notices in connection with previously disclosed SEC investigations of certain of AIG's transactions or accounting practices. Under SEC procedures, a Wells notice is an indication that the SEC staff has made a preliminary decision to recommend enforcement action that provides recipients with an opportunity to respond to the SEC staff before a formal recommendation is finalized. It is possible that additional current and former employees could receive similar notices in the future as the regulatory investigations proceed.

Effect on AIG

In the opinion of AIG management, AIG's ultimate liability for the unresolved litigation and investigation matters referred to above is not likely to have a material adverse effect on AIG's consolidated financial condition, although it is possible that the effect would be material to AIG's consolidated results of operations for an individual reporting period.

(b) Commitments

Flight Equipment

At March 31, 2008, ILFC had committed to purchase 211 new aircraft deliverable from 2008 through 2017 at an estimated aggregate purchase price of $18.8 billion. ILFC will be required to find customers for any aircraft acquired, and it must arrange financing for portions of the purchase price of such equipment.

ILFC ordered 74 Boeing 787 aircraft with the first ten originally scheduled to be delivered in 2010. Boeing has made several announcements concerning the delays in the deliveries of the 787s. Boeing has informed ILFC that its 787 deliveries will be delayed by an average in excess of 27 months per aircraft and span across ILFC's entire order, with the original contracted deliveries running from 2010 through 2017.

Other Commitments

In the normal course of business, AIG enters into commitments to invest in limited partnerships, private equities, hedge funds and mutual funds and to purchase and develop real estate in the U.S. and abroad. These commitments totaled $8.5 billion at March 31, 2008.

On June 27, 2005, AIG entered into an agreement pursuant to which AIG agreed, subject to certain conditions, to make any payment that is not promptly paid with respect to the benefits accrued by certain employees of AIG and its subsidiaries under the SICO Plans (as discussed in the 2007 Annual Report on Form 10-K).

(c) Contingencies

Loss Reserves. Although AIG regularly reviews the adequacy of the established reserve for losses and loss expenses, there can be no assurance that AIG's ultimate loss reserves will not develop adversely and materially exceed AIG's current loss reserves. Estimation of ultimate net losses, loss expenses and loss reserves is a complex process for long-tail casualty lines of business, which include excess and umbrella liability, directors and officers liability (D&O), professional liability, medical malpractice, workers' compensation, general liability, products liability and related classes, as well as for asbestos and environmental exposures. Generally, actual historical loss development factors are used to project future loss development. However, there can be no assurance that future loss development patterns will be the same as in the past. Moreover, any deviation in loss cost trends or in loss development factors might not be discernible for an extended period of time subsequent to the recording of the initial loss reserve estimates for any accident year. Thus, there is the potential for reserves with respect to a number of years to be significantly affected by changes in loss cost trends or loss development factors that were relied upon in setting the reserves. These changes in loss cost trends or loss development factors could be attributable to changes in inflation, in labor and material costs or in the judicial environment, or in other social or economic phenomena affecting claims.

Benefits Provided by Starr International Company, Inc. and C.V. Starr & Co., Inc. SICO has provided a series of two-year Deferred Compensation Profit Participation Plans (SICO Plans) to certain AIG employees. The SICO Plans were created in 1975 when the voting shareholders and Board of Directors of SICO, a private holding company whose principal asset is AIG common stock, decided that a portion of the capital value of SICO should be used to provide an incentive plan for the current and succeeding managements of all American International companies, including AIG.

None of the costs of the various benefits provided under the SICO Plans has been paid by AIG, although AIG has recorded a charge to reported earnings for the deferred compensation amounts paid to AIG employees by SICO, with an offsetting amount credited to additional paid-in capital reflecting amounts considered to be contributed by SICO. The SICO Plans provide that shares currently owned by SICO are

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

6. Commitments, Contingencies and Guarantees *(continued)*

set aside by SICO for the benefit of the participant and distributed upon retirement. The SICO Board of Directors currently may permit an early payout of units under certain circumstances. Prior to payout, the participant is not entitled to vote, dispose of or receive dividends with respect to such shares, and shares are subject to forfeiture under certain conditions, including but not limited to the participant's voluntary termination of employment with AIG prior to normal retirement age. Under the SICO Plans, SICO's Board of Directors may elect to pay a participant cash in lieu of shares of AIG common stock. Following notification from SICO to participants in the SICO Plans that it will settle specific future awards under the SICO Plans with shares rather than cash, AIG modified its accounting for the SICO Plans from variable to fixed measurement accounting. AIG gave effect to this change in settlement method beginning on December 9, 2005, the date of SICO's notice to participants in the SICO Plans.

(d) Guarantees

AIG and certain of its subsidiaries become parties to derivative financial instruments with market risk resulting from both dealer and end-user activities and to reduce currency, interest rate, equity and commodity exposures. These instruments are carried at their estimated fair values in the consolidated balance sheet. The majority of AIG's derivative activity is transacted by AIGFP. See Note 8 to the 2007 Annual Report on Form 10-K.

AIG has issued unconditional guarantees with respect to the prompt payment, when due, of all present and future payment obligations and liabilities of AIGFP arising from transactions entered into by AIGFP.

SAI Deferred Compensation Holdings, Inc., a wholly owned subsidiary of AIG, has established a deferred compensation plan for registered representatives of certain AIG subsidiaries, pursuant to which participants have the opportunity to invest deferred commissions and fees on a notional basis. The value of the deferred compensation fluctuates with the value of the deferred investment alternatives chosen. AIG has provided a full and unconditional guarantee of the obligations of SAI Deferred Compensation Holdings, Inc. to pay the deferred compensation under the plan.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

7. Employee Benefits

The components of the net periodic benefit costs with respect to pensions and other postretirement benefits were as follows:

	Pensions			Postretirement		
(in millions)	Non-U.S. Plans	U.S. Plans	Total	Non-U.S. Plans	U.S. Plans	Total
Three Months Ended March 31, 2008						
Components of net periodic benefit cost:						
Service cost	**$ 24**	**$ 32**	**$ 56**	**$ 2**	**$ 2**	**$ 4**
Interest cost	**14**	**50**	**64**	**1**	**4**	**5**
Expected return on assets	**(11)**	**(60)**	**(71)**	**–**	**–**	**–**
Amortization of prior service cost	**(3)**	**–**	**(3)**	**–**	**–**	**–**
Amortization of net loss	**4**	**4**	**8**	**–**	**–**	**–**
Net periodic benefit cost	**$ 28**	**$ 26**	**$ 54**	**$ 3**	**$ 6**	**$ 9**
Three Months Ended March 31, 2007						
Components of net periodic benefit cost:						
Service cost	$ 23	$ 30	$ 53	$ 1	$ 2	$ 3
Interest cost	12	45	57	1	4	5
Expected return on assets	(9)	(53)	(62)	–	–	–
Amortization of prior service cost	(2)	(1)	(3)	–	–	–
Amortization of net loss	2	9	11	–	–	–
Net periodic benefit cost	$ 26	$ 30	$ 56	$ 2	$ 6	$ 8

8. Federal Income Taxes

Interim Period Tax Assumptions and Effective Tax Rates

AIG's interim period tax expense or benefit is measured using an estimated annual effective tax rate. To the extent that a portion of AIG's annual pretax income or loss cannot be reliably estimated, the actual tax expense or benefit applicable to that income or loss is reported in the interim period in which the related income or loss is reported. AIG is unable to reliably estimate other-than-temporary impairments and the operating results of AIGFP. Therefore, the related tax effects calculated at the statutory tax rate of 35 percent are reported as discrete adjustments to the estimated annual effective tax rate that AIG applies to all other pretax income.

The effective tax rate on pre-tax income for the year ended December 31, 2007 was 16.3 percent. The effective rate was low due to the unrealized market valuation losses on AIGFP's super senior credit default swap portfolio and other-than-temporary impairment charges. The effective tax rate on the pre-tax loss for the first three months of 2008 was 31.4 percent. The effective rate was lower than the statutory rate of 35 percent due primarily to $703 million of tax charges for the first three months of 2008, comprised of increases in the reserves for uncertain tax positions and other discrete period items.

Tax Filings and Examinations

On April 3, 2008, AIG filed a refund claim for tax years 1997 through 2004. The refund claim relates to the tax effect of the restatement of AIG's 2004 and prior financial statements.

On March 20, 2008, AIG received a Statutory Notice of Deficiency (the Notice) from the United States Internal Revenue Service (IRS) asserting liability for additional taxes for the 1997 through 1999 tax years. The Notice asserted that AIG owes additional taxes of $329 million, including penalties, and focuses principally on two issues: the timing of deductions and the disallowance of foreign tax credits associated with cross border financing transactions. The transactions that are the subject of the Notice (the Affected Transactions) extend beyond the period covered by the Notice, and it is likely that the IRS will seek to challenge those later periods. It is also possible that the IRS will consider other transactions to be similar to the Affected Transactions. AIG disagrees with the Notice and plans to contest the IRS' assertions. AIG believes that it is adequately reserved for any liability that could result from the IRS actions.

In April 2008, two separate court decisions were rendered relating to certain "lease-in, lease-out" transactions, which were adverse to the taxpayers. In accordance with FIN 48, AIG will evaluate in the second quarter of 2008 the effect of these decisions on lease transactions of AIG subsidi-

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

8. Federal Income Taxes *(continued)*

aries. Any resulting adjustment is not expected to be material to AIG's consolidated results of operations or its consolidated financial condition.

FIN 48

As of March 31, 2008 and December 31, 2007, AIG's unrecognized tax benefits, excluding interest and penalties, were $2.5 billion and $1.3 billion, respectively. The increase during the period is attributable to foreign tax credits associated with cross border financing transactions and to income and expense allocations across jurisdictions. As of March 31, 2008 and December 31, 2007, AIG's unrecognized tax benefits included $923 million and $299 million, respectively, related to tax positions the disallowance of which would not affect the effective tax rate. The increase during the period is attributable to U.S. deferred taxes associated with income and expense allocations across jurisdictions. Accordingly, as of March 31, 2008 and December 31, 2007, the amount of unrecognized tax benefits that, if recognized, would favorably affect the effective tax rate were $1.5 billion and $1.0 billion, respectively.

Interest and penalties related to unrecognized tax benefits are recognized in income tax expense. At March 31, 2008, AIG had accrued $351 million, for the payment of interest (net of the federal benefit) and penalties.

AIG continually evaluates proposed adjustments by taxing authorities. At March 31, 2008, such proposed adjustments would not result in a material change to AIG's consolidated financial condition, although it is possible that the effect could be material to AIG's consolidated results of operations for an individual reporting period. Although it is reasonably possible that a significant change in the balance of unrecognized tax benefits may occur within the next twelve months, at this time it is not possible to estimate the range of the change due to the uncertainty of the potential outcomes.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

9. Information Provided in Connection with Outstanding Debt

The following condensed consolidating financial statements reflect the following:

- **AIG Life Holdings (US), Inc. (AIGLH), formerly known as American General Corporation, is a holding company and a wholly owned subsidiary of AIG. AIG provides a full and unconditional guarantee of all outstanding debt of AIGLH.**
- **AIG Liquidity Corp. is a wholly owned subsidiary of AIG. AIG provides a full and unconditional guarantee of all obligations of AIG Liquidity Corp.**
- **AIG Program Funding, Inc. is a wholly owned subsidiary of AIG. AIG provides a full and unconditional guarantee of all obligations of AIG Program Funding, Inc., which was established in 2007.**

Condensed Consolidating Balance Sheet

(in millions)	American International Group, Inc. (As Guarantor)	AIGLH	AIG Liquidity Corp.	AIG Program Funding, Inc.	Other Subsidiaries	Eliminations	Consolidated AIG
March 31, 2008							
Assets:							
Investments and Financial Services assets	**$ 12,895**	**$ 40**	**$ –**	**$ –**	**$ 850,273**	**$ (21,956)**	**$ 841,252**
Cash	**273**		**–**	**–**	**2,216**		**2,489**
Carrying value of subsidiaries and partially owned companies, at equity	**98,742**	**20,900**	**–**	**–**	**24,545**	**(143,477)**	**710**
Other assets	**8,339**	**2,621**	**–**	**–**	**195,436**	**239**	**206,635**
Total assets	**$120,249**	**$23,561**	**$ –**	**$ –**	**$1,072,470**	**$ (165,194)**	**$1,051,086**
Liabilities:							
Insurance liabilities	**$ –**	**$ –**	**$ –**	**$ –**	**$ 547,260**	**$ (99)**	**$ 547,161**
Debt	**37,363**	**2,136**	**–**	**–**	**151,859**	**(19,188)**	**172,170**
Other liabilities	**3,183**	**2,929**	**–**	**–**	**247,923**	**(2,083)**	**251,952**
Total liabilities	**40,546**	**5,065**	**–**	**–**	**947,042**	**(21,370)**	**971,283**
Preferred shareholders' equity in subsidiary companies	**–**	**–**	**–**	**–**	**100**		**100**
Total shareholders' equity	**79,703**	**18,496**	**–**	**–**	**125,328**	**(143,824)**	**79,703**
Total liabilities, preferred shareholders' equity in subsidiary companies and shareholders' equity	**$120,249**	**$23,561**	**$ –**	**$ –**	**$1,072,470**	**$ (165,194)**	**$1,051,086**
December 31, 2007							
Assets:							
Investments and Financial Services assets	$ 14,648	$ 40	$ –	$ –	$ 859,063	$ (21,790)	$ 851,961
Cash	84	1	–	–	2,199	–	2,284
Carrying value of subsidiaries and partially owned companies, at equity	111,714	24,396	–	–	18,542	(153,998)	654
Other assets	9,414	2,592	–	–	193,445	155	205,606
Total assets	$135,860	$27,029	$ –	$ –	$1,073,249	$ (175,633)	$1,060,505
Liabilities:							
Insurance liabilities	$ 43	$ –	$ –	$ –	$ 534,369	$ (75)	$ 534,337
Debt	36,045	2,136	–	–	156,003	(18,135)	176,049
Other liabilities	3,971	2,826	–	–	250,506	(3,085)	254,218
Total liabilities	40,059	4,962	–	–	940,878	(21,295)	964,604
Preferred shareholders' equity in subsidiary companies	–	–	–	–	100	–	100
Total shareholders' equity	95,801	22,067	–	–	132,271	(154,338)	95,801
Total liabilities, preferred shareholders' equity in subsidiary companies and shareholders' equity	$135,860	$27,029	$ –	$ –	$1,073,249	$ (175,633)	$1,060,505

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

9. Information Provided in Connection with Outstanding Debt *(continued)*

Condensed Consolidating Statement of Income (Loss)

(in millions)	American International Group, Inc. (As Guarantor)	AIGLH	AIG Liquidity Corp.	AIG Program Funding, Inc.	Other Subsidiaries	Eliminations	Consolidated AIG
Three Months Ended March 31, 2008							
Operating income (loss)	**$ (833)**	**$ (21)**	**$ ***	**$ –**	**$ (10,410)**	**$ –**	**$(11,264)**
Equity in undistributed net income of consolidated subsidiaries	**(7,754)**	**(1,246)**	**–**	**–**	**–**	**9,000**	**–**
Dividend income from consolidated subsidiaries	**749**	**–**	**–**	**–**	**–**	**(749)**	**–**
Income taxes (benefits)	**(33)**	**(3)**	*****	**–**	**(3,501)**		**(3,537)**
Minority interest	**–**	**–**	**–**	**–**	**(78)**		**(78)**
Net income (loss)	**$ (7,805)**	**$ (1,264)**	**$ ***	**$ –**	**$ (6,987)**	**$ 8,251**	**$ (7,805)**
Three Months Ended March 31, 2007							
Operating income (loss)	$ (261)	$ (73)	$ *	$ –	$ 6,506	$ –	$ 6,172
Equity in undistributed net income of consolidated subsidiaries	3,244	151	–	–	–	(3,395)	–
Dividend income from consolidated subsidiaries	1,286	440	–	–	–	(1,726)	–
Income taxes (benefits)	139	8	*	–	1,579	–	1,726
Minority interest	–	–	–	–	(316)	–	(316)
Net income (loss)	$ 4,130	$ 510	$ *	$ –	$ 4,611	$ (5,121)	$ 4,130

**Less than $1 million.*

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

9. Information Provided in Connection with Outstanding Debt *(continued)*

Condensed Consolidating Statement of Cash Flows

(in millions)	American International Group, Inc. (As Guarantor)	AIGLH	AIG Liquidity Corp.	AIG Program Funding, Inc.	Other Subsidiaries	Consolidated AIG
Three Months Ended March 31, 2008						
Net cash provided by operating activities	**$ 504**	**$ 557**	**$ ***	**$ –**	**$ 7,232**	**$ 8,293**
Cash flows from investing:						
Invested assets disposed	**214**	**–**	**–**	**–**	**52,537**	**52,751**
Invested assets acquired	**(329)**	**–**	**–**	**–**	**(48,656)**	**(48,985)**
Other	**2,723**	**(58)**	*****	**–**	**(2,902)**	**(237)**
Net cash provided by (used) in investing activities	**2,608**	**(58)**	*****	**–**	**979**	**3,529**
Cash flows from financing activities:						
Issuance of debt	**214**	**–**	**–**	**–**	**12,457**	**12,671**
Repayments of debt	**(28)**	**–**	**–**	**–**	**(19,880)**	**(19,908)**
Payments advanced to purchase shares	**(1,000)**	**–**	**–**	**–**	**–**	**(1,000)**
Cash dividends paid to shareholders	**(498)**	**–**	**–**	**–**	**–**	**(498)**
Other	**(1,610)**	**(500)**	*****	**–**	**(830)**	**(2,940)**
Net cash used in financing activities	**(2,922)**	**(500)**	*****	**–**	**(8,253)**	**(11,675)**
Effect of exchange rate changes on cash	**–**	**–**	**–**	**–**	**58**	**58**
Change in cash	**190**	**(1)**	*****	**–**	**16**	**205**
Cash at beginning of period	**84**	**1**	**–**	**–**	**2,199**	**2,284**
Cash at end of period	**$ 274**	**$ –**	**$ ***	**$ –**	**$ 2,215**	**$ 2,489**
Three Months Ended March 31, 2007						
Net cash provided by operating activities	$ 261	$ 48	$ *	$ –	$ 9,621	$ 9,930
Cash flows from investing:						
Invested assets disposed	170	–	–	–	38,906	39,076
Invested assets acquired	(3,520)	–	–	–	(53,321)	(56,841)
Other	349	(48)	*	–	(560)	(259)
Net cash used in investing activities	(3,001)	(48)	*	–	(14,975)	(18,024)
Cash flows from financing activities:						
Issuance of debt	6,831	–	–	–	17,923	24,754
Repayments of debt	(728)	–	–	–	(15,596)	(16,324)
Payments advanced to purchase shares	(3,000)	–	–	–	–	(3,000)
Cash dividends paid to shareholders	(430)	–	–	–	–	(430)
Other	38	–	*	–	3,178	3,216
Net cash provided by financing activities	2,711	–	*	–	5,505	8,216
Effect of exchange rate changes on cash	–	–	–	–	(10)	(10)
Change in cash	(29)	–	*	–	141	112
Cash at beginning of period	76	–	–	–	1,514	1,590
Cash at end of period	$ 47	$ –	$ *	$ –	$ 1,655	$ 1,702

**Less than $1 million.*

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

10. Cash Flows

AIG has made certain revisions to the Consolidated Statement of Cash Flows, primarily relating to the effect of reclassifying certain policyholders' account balances, the elimination of certain intercompany balances and revisions related to separate account assets. Accordingly, AIG revised the previous periods presented to conform to the revised presentation. There was no effect on ending cash balances.

The revisions and their effect on the Consolidated Statement of Cash Flows for the three months ended March 31, 2007 were as follows:

(in millions)	Originally Reported March 31, 2007	Revisions	As Revised
Cash flows from operating activities	$ 8,633	$ 1,297	$ 9,930
Cash flows from investing activities	(16,863)	(1,161)	(18,024)
Cash flows from financing activities	8,352	(136)	8,216

ITEM 2. Management's Discussion and Analysis of Financial Condition and Results of Operations

Management's Discussion and Analysis of Financial Condition and Results of Operations is designed to provide the reader a narrative with respect to AIG's operations, financial condition and liquidity and certain other significant matters.

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Cautionary Statement Regarding Projections and Other Information About Future Events

This Quarterly Report on Form 10-Q and other publicly available documents may include, and AIG's officers and representatives may from time to time make, projections concerning financial information and statements concerning future economic performance and events, plans and objectives relating to management, operations, products and services, and assumptions underlying these projections and statements. These projections and statements are not historical facts but instead represent only AIG's belief regarding future events, many of which, by their nature, are inherently uncertain and outside AIG's control. These projections and statements may address, among other things, the status and potential future outcome of the current regulatory and civil proceedings against AIG and their potential effect on AIG's businesses, financial condition, results of operations, cash flows and liquidity, AIG's exposures to subprime mortgages, monoline insurers and the residential real estate market and AIG's strategy for growth, product development, market position, financial results and reserves. It is possible that AIG's actual results and financial condition may differ, possibly materially, from the anticipated results and financial condition indicated in these projections and statements. Factors that could cause AIG's actual results to differ, possibly materially, from those in the specific projections and statements are discussed in Outlook and throughout this Management's Discussion and Analysis of Financial Condition and Results of Operations and in Item 1A. Risk Factors of AIG's Annual Report on Form 10-K for the year ended December 31, 2007 (2007 Annual Report on Form 10-K). AIG is not under any obligation (and expressly disclaims any such obligations) to update or alter any projection or other statement, whether written or oral, that may be made from time to time, whether as a result of new information, future events or otherwise.

In addition to reviewing AIG's results for the first three months of 2008, this Management's Discussion and Analysis of Financial Condition and Results of Operations supplements and updates the information and discussion included in the 2007 Annual Report on Form 10-K. Throughout this Management's Discussion and Analysis of Financial Condition and Results of Operations, AIG presents its operations in the way it believes will be most meaningful. Statutory loss ratios and combined ratios are presented in accordance with accounting principles prescribed by insurance regulatory authorities because these are standard measures of performance filed with insurance regulatory authorities and used for analysis in the insurance industry and thus allow more meaningful comparisons with AIG's insurance competitors. AIG also uses cross-references to additional information included in this Quarterly Report on Form 10-Q and in the 2007 Annual Report on Form 10-K to assist readers seeking related information on a particular subject.

Overview of Operations and Business Results

AIG identifies its reportable segments by product line, consistent with its management structure. These segments are General Insurance, Life Insurance & Retirement Services, Financial Services and Asset Management. Through these operating segments, AIG provides insurance, financial and investment products and services to both businesses and individuals in more than 130 countries and jurisdictions. This geographic, product and service diversification is one of AIG's major strengths and sets it apart from its competitors. AIG's Other category consists of items not allocated to AIG's operating segments.

AIG's subsidiaries serve commercial, institutional and individual customers through an extensive property-casualty and life insurance and retirement services network. In the United States, AIG companies are the largest underwriters of commercial and industrial insurance and are among the largest life insurance and retirement services operations as well. AIG's Financial Services businesses include commercial aircraft and equipment leasing, capital markets operations and consumer finance, both in the United States and abroad. AIG also provides asset management services to institutions and individuals. As part of its Spread-Based Investment activities, and to finance its operations, AIG issues various debt instruments in the public and private markets.

Outlook

The following paragraphs supplement and update the information and discussion included in Management's Discussion and Analysis of Financial Condition and Results of Operations — Outlook in the 2007 Annual Report on Form 10-K to reflect developments in or affecting AIG's business to date during 2008. These paragraphs also supplement and update Item 1A. Risk Factors in the 2007 Annual Report on Form 10-K.

General Trends

In mid-2007, the U.S. residential mortgage market began to experience serious disruption due to credit quality deterioration in a significant portion of loans originated, particularly to non-prime and subprime borrowers; evolving changes in the regulatory environment; a slower residential housing market; increased cost of borrowings for mortgage participants; and illiquid credit markets. The conditions continued and worsened throughout 2007 and the first quarter of 2008, expanding into the broader U.S. credit markets and resulting in greater volatility, less liquidity, widening of credit spreads, a lack of price transparency and increased credit losses in certain markets.

AIG participates in the U.S. residential mortgage market in several ways: American General Finance, Inc. (AGF) originates principally first-lien mortgage loans and to a lesser extent second-lien mortgage loans to buyers and owners of residential housing; United Guaranty Corporation (UGC) provides first loss mortgage guaranty insurance for high loan-to-value first- and second-lien residential mortgages; AIG insurance and financial services subsidiaries invest in mortgage-backed securities and collateralized debt obligations (CDOs), in which the underlying collateral is composed in whole or in part of residential mortgage loans; and AIG Financial Products Corp. and AIG Trading Group Inc. and their respective subsidiaries (collectively, AIGFP) provides credit protection through credit default swaps on certain super senior tranches of CDOs, a significant majority of which have AAA underlying or subordinate layers.

Continuing disruption in the U.S. residential mortgage and other credit markets may also increase claim activity in the financial institution segment of AIG's directors and officers liability (D&O) and professional liability classes of business. However, based on its review of information currently available, AIG believes overall loss activity for the broader D&O and professional liability classes is likely to remain within or near the levels observed during the last several years, which include losses related to stock options backdating as well as to the U.S. residential mortgage market.

The operating results of AIG's consumer finance and mortgage guaranty operations in the United States have been and are likely to continue to be adversely affected by the factors referred to above. The downward cycle in the U.S. housing market is not expected to improve until residential inventories return to a more normal level and the mortgage credit market stabilizes. The duration and severity of the downward cycle could be further negatively affected in the event of an economic recession. AIG expects that this downward cycle will continue to adversely affect UGC's operating results for the foreseeable future and will result in a

significant operating loss for UGC in 2008 and possibly beyond. AIG also incurred substantial unrealized market valuation losses on AIGFP's super senior credit default swap portfolio and substantial other-than-temporary impairment charges on AIG's available for sale securities in the first quarter of 2008 and fourth quarter of 2007. The results from AIG's operations with exposure to the U.S. residential mortgage market will be highly dependent on future market conditions. Continuing market deterioration will cause AIG to report additional unrealized market valuation losses and impairment charges.

The ongoing effect of the downward cycle in the U.S. housing market on AIG's consolidated financial condition could be material if the market disruption continues to expand beyond the residential mortgage markets, although AIG seeks to mitigate the risks to its business by disciplined underwriting and active risk management.

Credit ratings are important to AIG's business, results of operations and liquidity. Downgrades in AIG's credit ratings could increase AIG's borrowing costs and could adversely affect its competitive position and liquidity. With respect to AIG's liquidity, it is estimated that, as of the close of business on April 30, 2008, based on AIGFP's outstanding municipal guaranteed investment agreements (GIAs) and financial derivative transactions at that date, a downgrade of AIG's longer-term senior debt ratings to 'Aa3' by Moody's Investors Service (Moody's) or 'AA–' by Standard & Poor's, a division of the McGraw-Hill Companies (S&P) would permit counterparties to call for approximately $1.8 billion of collateral, while a downgrade to 'A1' by Moody's or A+ by S&P would permit counterparties to call for approximately $9.8 billion of additional collateral. Further downgrades could result in requirements for substantial additional collateral, which could have a material adverse effect on how AIGFP manages its liquidity. The actual amount of collateral that AIGFP would be required to post to counterparties in the event of such downgrades depends on market conditions, the fair value of outstanding affected transactions and other factors prevailing at the time of the downgrade. Additional obligations to post collateral would increase the demands on AIGFP's liquidity.

Globally, heightened regulatory scrutiny of financial services companies in many jurisdictions has the potential to affect future financial results through higher compliance costs. This is particularly true in the United States, where federal and state authorities have commenced various investigations of the financial services industry, and in Japan and Southeast Asia, where financial institutions have received remediation orders affecting consumer and policyholder rights.

Capital Resources

In light of the ongoing significant effects the disruption in the U.S. housing and credit markets is having on AIG's results, AIG is planning to raise additional capital to fortify its balance sheet and increase financial flexibility.

General Insurance

The commercial property and casualty insurance industry has historically experienced cycles of price erosion followed by rate strengthening as a result of catastrophes or other significant losses that affect the overall capacity of the industry to provide coverage. As premium rates decline, AIG will generally experience higher current accident year loss ratios, as the written premiums are earned, and higher expense ratios if written premiums decline more quickly than expenses. Despite industry price erosion in commercial lines, AIG expects to continue to identify profitable opportunities and build attractive new general insurance businesses as a result of AIG's broad product line and extensive distribution networks in the United States and abroad.

Workers' compensation remains under considerable pricing pressure, as statutory rates continue to decline. Rates for most casualty lines of insurance continue to decline due to competitive pressures, particularly for aviation, excess casualty and D&O exposures. Rates for commercial property lines are also declining following another year of relatively low catastrophe losses. Further price erosion is expected during the remainder of 2008 for the commercial lines; AIG seeks to mitigate the decline by constantly seeking out profitable opportunities across its diverse product lines and distribution networks while maintaining a commitment to underwriting discipline. There can be no assurance that price erosion will not become more widespread or that AIG's profitability will not deteriorate from current levels in major commercial lines.

The personal lines market has softened considerably and further deterioration in underwriting results is expected to continue through 2009. A generally weakening economy and increasing loss trends are contributing factors. AIG is filing for rate increases and tightening underwriting guidelines where necessary in response to the changing market conditions.

Life Insurance & Retirement Services

Disruption in the U.S. residential mortgage and credit markets had a significant adverse effect on Life Insurance & Retirement Services operating results, specifically its net investment income and net realized capital losses in 2007 and the first three months of 2008, and AIG expects that this disruption will continue to be a key factor in the remainder of 2008 and beyond, especially in its U.S.-based operations. The volatility in operating results will be further magnified by the

continuing market shift to variable products with living benefits.

In response to the market disruption, AIG, including Domestic Life and Domestic Retirement Services, has been increasing its liquidity position and investing in shorter duration investments. While prudent in the current environment, such actions will reduce overall investment yields.

Recent capital markets volatility has put pressure on credit lenders resulting in increased costs for premium financing, which could affect future sales of products where such financing is used, primarily in large universal life policies in Domestic Life Insurance.

The U.S. dollar has significantly weakened against many currencies, resulting in a favorable effect on operating results due to the translation of foreign currencies to the U.S. dollar. However, the weakened dollar has an unfavorable effect on other-than-temporary impairments in Foreign Life Insurance & Retirement Services and will continue to affect operating results throughout 2008.

An additional capital contribution to operations in Taiwan is planned for the second quarter of 2008 in order to meet the needs of this growing business and increased risk-based capital requirements. The amount of the additional capital contribution is expected to be approximately $400 million.

Financial Services

AIG exercises significant judgment in the valuation of its various credit default swap portfolios. AIG uses pricing models and other methodologies to value these portfolios that take into account, where applicable, and to the extent possible, third-party prices, pricing matrices, the movement of indices (such as the CDX and iTraxx), collateral calls and other observable market data. There is no uniform methodology used by market participants in valuing these types of portfolios. AIG believes that the assumptions and judgments it makes are reasonable and lead to an overall methodology that is reasonable, but other market participants may use other methodologies, including, among other things, models, indices and selection of third-party pricing sources, that are based upon different assumptions and judgments, and these methodologies may generate materially different values. AIG regularly updates and analyzes the appropriateness of its valuation methodologies. Updates to or changes in AIG's methodologies or assumptions may materially change AIG's estimates of the value of its credit default swap portfolios.

For additional information regarding AIG's methodology, models and assumptions with respect to the valuation and credit-based analyses of the AIGFP super senior credit default swap portfolio see Critical Accounting Estimates — Fair Value Measurements of Certain Financial Assets and Liabilities — AIGFP's Super Senior Credit Default Swap Portfolio, and — Valuation of Level 3 Assets and Liabilities — Super senior credit default swap portfolio. Also refer to Risk Management — Credit Derivatives.

The ongoing disruption in the U.S. residential mortgage and credit markets and the downgrades of residential mortgage-backed securities and CDO securities by rating agencies continue to adversely affect the fair value of the super senior credit default swap portfolio written by AIGFP. AIG expects that continuing limitations on the availability of market observable data will affect AIG's determinations of the fair value of these derivatives, including by preventing AIG, for the foreseeable future, from recognizing the beneficial effect of the differential between credit spreads used to price a credit default swap and spreads implied from prices of the CDO bonds referenced by such swap. The fair value of these derivatives is expected to continue to fluctuate, perhaps materially, in response to changing market conditions, and AIG's estimates of the value of AIGFP's super senior credit derivative portfolio at future dates could therefore be materially different from current estimates. Further declines in the fair values of these derivatives may require AIGFP to post additional collateral which may be material to AIGFP's financial condition.

Under the terms of most of these credit derivatives, losses to AIG would generally result from the credit impairment of the referenced CDO bonds that AIG would acquire in satisfying its swap obligations. Based upon its most current analyses, AIG believes that any credit impairment losses which may emerge over time at AIGFP will not be material to AIG's consolidated financial condition, but could be material to the manner in which AIG manages its liquidity. In making this assessment, AIG uses a credit-based analysis to estimate potential realized credit impairment losses from AIGFP's super senior credit default swap portfolio. This analysis makes various assumptions as to estimates of future stresses on the portfolio resulting from further downgrades by the rating agencies of the CDO collateral. In addition, during the first quarter of 2008, AIG introduced another methodology called a roll rate analysis. This methodology rolls forward current and estimated future delinquencies and defaults in underlying mortgages in the CDO collateral pools to estimate potential losses in the CDOs. Due to the dislocation in the market for CDO collateral, AIG does not use the market values of the underlying CDO collateral in estimating its potential realized credit impairment losses. The use of factors derived from market-observable prices in models used to determine the estimates for future realized credit impairment losses would result in materially higher estimates of realized credit impairment losses. AIG's credit-based analyses estimate potential realized credit impairment pre-tax losses at

approximately $1.2 billion to approximately $2.4 billion. Other types of analyses or models could result in materially different estimates. AIG is aware that other market participants have used different assumptions and methodologies to estimate the potential realized credit impairment losses on AIGFP's super senior credit default swap portfolio, resulting in a significantly higher estimate than that resulting from AIG's credit-based analysis. For example, a third-party analysis provided to AIG, that AIG understands uses credit and market value inputs, estimates the potential realized pre-tax losses on AIGFP's super senior credit default swap portfolio at between approximately $9 billion and approximately $11 billion. (AIG expresses no view as to the reasonableness of this third-party estimate and does not intend to seek an update of this estimate.) There can be no assurance that AIG's estimate will not change or that the ultimate realized losses on AIGFP's super senior credit default swap portfolio will not exceed any current estimates.

Approximately $335 billion of the $469 billion in notional exposure on AIGFP's super senior credit default swap portfolio as of March 31, 2008 was written to facilitate regulatory capital relief for financial institutions primarily in Europe. AIG expects that the majority of these transactions will be terminated within the next 12 to 24 months by AIGFP's counterparties as they implement models compliant with the new Basel II Accord. As of April 30, 2008, $55 billion in notional exposures have either been terminated or are in the process of being terminated at the request of counterparties. In its 2007 Annual Report on Form 10-K, AIG had previously reported that as of February 26, 2008, $54 billion in notional exposures have either been terminated or are in the process of being terminated. AIG has recently refined its approach to estimating its net notional exposures on certain of these transactions that have unique features. The notional exposures on transactions terminated or that were in the process of being terminated as of February 26, 2008 is $46 billion under the refined method. AIGFP was not required to make any payments as part of these terminations and in certain cases was paid a fee upon termination.

In light of this experience to date and after other comprehensive analyses, AIG determined that there was no unrealized market valuation adjustment to be recognized for this regulatory capital relief portfolio for the three months ended March 31, 2008. AIG will continue to assess the valuation of this portfolio and monitor developments in the marketplace. Given the significant deterioration in the global credit markets and the risk that AIGFP's expectations with respect to the termination of these transactions by its counterparties may not materialize, there can be no assurance that AIG will not recognize unrealized market valuation losses from this portfolio in future periods, and recognition of even a small percentage decline in the fair value of this portfolio could be material to an individual reporting period. These transactions contributed approximately $89 million to AIGFP's revenues in the three-months ended March 31, 2008. If AIGFP is not successful in replacing the revenues generated by these transactions, AIGFP's operating results could be materially adversely affected.

Approximately $57 billion of the $469 billion in notional exposure on AIGFP's super senior credit default swaps as of March 31, 2008 was written on investment grade corporate debt and CLOs. There is no uniform methodology to estimate the fair value of corporate super senior credit default swaps. AIG estimates the fair value of its corporate credit default swap portfolio by reference to benchmark indices, including the CDX and iTraxx, and third-party prices and collateral calls. AIG believes that its methodology to value the corporate credit default swap portfolio is reasonable, but other market participants use other methodologies and these methodologies may generate materially different fair value estimates. No assurance can be given that the fair value of AIG's corporate credit default swap portfolio would not change materially if other market indices or pricing sources were used to estimate the fair value of the portfolio.

For a description of important factors that may affect the operations and initiatives described above, see Item 1A. Risk Factors in the 2007 Annual Report on Form 10-K.

Consolidated Results

AIG's consolidated revenues, income (loss) before income taxes, minority interest and net income (loss) were as follows:

(in millions)	Three Months Ended March 31, **2008**	2007	Percentage Increase/ (Decrease)
Total revenues	**$ 14,031**	$30,645	(54)%
Income (loss) before income taxes and minority interest	**(11,264)**	6,172	—
Net income (loss)	**$ (7,805)**	$ 4,130	—%

AIG's consolidated revenues decreased in the three months ended March 31, 2008 compared to the same period in 2007 due to an unrealized market valuation loss of $9.1 billion on AIGFP's super senior credit default swap portfolio recorded in other income, higher net realized capital losses and a decline in net investment income, which more than offset growth in premiums and other considerations in the Life Insurance & Retirement Services segment. Net realized capital losses of $6.1 billion in the three months ended March 31, 2008 included other-than-temporary impairment charges of $5.6 billion, primarily related to the significant disruption in the residential mortgage and credit markets and investment-

related losses of $779 million where AIG lacks the intent to hold the investments to recovery. Total other-than-temporary impairment charges in the three months ended March 31, 2007 were $467 million. See Invested Assets — Portfolio Review — Other-than-temporary impairments herein. The decline in net investment income reflects lower returns from partnerships, hedge funds and mutual funds as well as lower policyholder trading gains in Life Insurance & Retirement Services. Policyholder trading gains are offset by a charge to incurred policy losses and benefits expense.

Income (loss) before income taxes and minority interest declined in the three months ended March 31, 2008 due primarily to the losses described above.

Income Taxes

The effective tax rate on pre-tax income for the year ended December 31, 2007 was 16.3 percent. The effective rate was low due to the unrealized market valuation losses on AIGFP's super senior credit default swap portfolio and other-than-temporary impairment charges. The effective tax rate on the pre-tax loss for the first three months of 2008 was 31.4 percent. The effective rate was lower than the statutory rate of 35 percent due primarily to $703 million of tax charges for the first three months of 2008, comprised of increases in the reserves for uncertain tax positions and other discrete period items. See also Note 8 to Consolidated Financial Statements.

Segment Results

The following table summarizes the operations of each principal segment. (See also Note 2 to Consolidated Financial Statements.)

Operating Segments *(in millions)*	Three Months Ended March 31, **2008**	2007	Percentage Increase/ (Decrease)
Total revenues[(a)]:			
General Insurance	**$ 12,289**	$12,903	(5)%
Life Insurance & Retirement Services[(b)]	**8,752**	13,682	(36)
Financial Services[(c)(d)]	**(6,560)**	2,201	—
Asset Management[(e)]	**(149)**	1,669	—
Other	**(128)**	131	—
Consolidation and eliminations	**(173)**	59	—
Total	**$ 14,031**	$30,645	(54)%
Operating income (loss)[(a)]:			
General Insurance	**$ 1,337**	$ 3,096	(57)%
Life Insurance & Retirement Services[(b)]	**(1,831)**	2,281	—
Financial Services[(c)(d)]	**(8,772)**	292	—
Asset Management[(e)]	**(1,251)**	758	—
Other	**(768)**	(470)	—
Consolidation and eliminations	**21**	215	(90)
Total	**$(11,264)**	$ 6,172	—%

(a) For the three-month periods ended March 31, 2008 and 2007, includes other-than-temporary impairment charges of $5.6 billion and $467 million, respectively. Also includes gains (losses) from hedging activities that did not qualify for hedge accounting treatment under Statement of Financial Accounting Standards (FAS) No. 133, "Accounting for Derivative Instruments and Hedging Activities" (FAS 133), including the related foreign exchange gains and losses. For the three-month periods ended March 31, 2008 and 2007, the effect was $(748) million and $(452) million, respectively, in both revenues and operating income (loss). These amounts result primarily from interest rate and foreign currency derivatives that are effective economic hedges of investments and borrowings.

(b) For the three-month periods ended March 31, 2008 and 2007, includes other-than-temporary impairment charges of $4.4 billion and $392 million, respectively.

(c) Includes gains (losses) from hedging activities that did not qualify for hedge accounting treatment under FAS 133, including the related foreign exchange gains and losses. For the three-month periods ended March 31, 2008 and 2007, the effect was $(204) million and $(160) million, respectively, in both revenues and operating income (loss). These amounts result primarily from interest rate and foreign currency derivatives that are effective economic hedges of investments and borrowings.

(d) For the three-month period ended March 31, 2008, both revenues and operating income (loss) include an unrealized market valuation loss of $9.1 billion on AIGFP's super senior credit default swap portfolio.

(e) Includes net realized capital losses of $1.4 billion for the three-month period ended March 31, 2008, including other-than-temporary impairment charges of $1.0 billion.

General Insurance

AIG's General Insurance operations provide property and casualty products and services throughout the world. Revenues in the General Insurance segment represent net premiums earned, net investment income and net realized capital gains (losses). The decrease in General Insurance revenues in the first three months of 2008 compared to the same period in 2007 was due to net realized capital losses for the first three months of 2008 compared to net realized capital gains in the same period of 2007 and lower net investment income as returns on partnership investments declined. The decrease in General Insurance operating income in the first three months of 2008 compared to the same period in 2007 was driven by AIG Commercial Insurance (Commercial Insurance), reflecting lower underwriting profit and net investment income, as well as net realized capital losses incurred by Commercial Insurance in 2008. Operating losses from the Mortgage Guaranty business and a decline in Foreign General Insurance net investment income in the first three months of 2008 also contributed to the decrease in General Insurance operating income.

Life Insurance & Retirement Services

AIG's Life Insurance & Retirement Services operations provide insurance, financial and investment-oriented products throughout the world. Revenues in the Life Insurance & Retirement Services operations represent premiums and other considerations, net investment income and net realized capital gains (losses). Foreign operations contributed approximately 80 percent and 78 percent of AIG's Life Insurance & Retirement Services premiums and other considerations for the first three months of 2008 and 2007, respectively.

Life Insurance & Retirement Services operating income (loss) declined in the first three months of 2008 compared to the same period in 2007 primarily due to higher net realized capital losses in 2008. In addition, the operating loss in the first three months of 2008 was negatively affected by trading account losses in the U.K. associated with certain investment-linked products and an increase in incurred policyholder benefits related to a closed block of Japan business with guaranteed benefits. These declines were partially offset by reductions in deferred policy acquisition costs (DAC) and sales inducement asset (SIA) amortization related to realized capital losses and growth in the underlying reserves which reflects increased assets under management.

Financial Services

AIG's Financial Services subsidiaries engage in diversified activities including aircraft and equipment leasing, capital markets, consumer finance and insurance premium finance. Revenues in the Financial Services segment include interest, realized and unrealized gains and losses, including the unrealized market valuation losses on AIGFP's super senior credit default swap portfolio, and lease and finance charges.

Financial Services reported an operating loss in the first three months of 2008 compared to operating income in the same period in 2007, primarily due to an unrealized market valuation loss of $9.1 billion on AIGFP's super senior credit default swap portfolio and a decline in operating income for AGF. Capital Markets net operating loss for the first three months of 2008 was $8.9 billion, reflecting the pre-tax unrealized market valuation loss on the super senior credit default swap portfolio. The net loss also includes an increase to pre-tax earnings of $2,648 million attributable to changes in AIG's credit spreads which were substantially offset by the effect of changes in counterparty credit spreads on assets measured at fair value of $2,620 million. On January 1, 2008, AIGFP elected the fair value option for almost all of its eligible financial assets and liabilities. Included in the first quarter 2008 net operating loss is the transition amount of $291 million related to the adoption of FAS 157 and FAS 159.

In the first three months of 2007, AGF's mortgage banking operations recorded a pre-tax charge of $128 million, representing the estimated cost of implementing the Supervisory Agreement entered into with the Office of Thrift Supervision (OTS).

Operating income for ILFC increased in the first three months of 2008 compared to the same period in 2007 driven to a large extent by a larger aircraft fleet, higher lease rates and higher utilization.

Asset Management

AIG's Asset Management operations include institutional and retail asset management, broker-dealer services and Spread-Based Investment businesses. Revenues in the Asset Management segment represent investment income with respect to spread-based products and management, advisory and incentive fees.

Asset Management operating income decreased in the first three months of 2008 compared to the same period in 2007, due to other-than-temporary impairment charges on fixed income investments, lower partnership income and mark to market losses on interest rate and foreign currency hedge positions not qualifying for hedge accounting related to the Spread-Based Investment business.

Capital Resources

At March 31, 2008, AIG had total consolidated shareholders' equity of $79.7 billion and total consolidated borrowings of $172.2 billion. At that date, $68.3 billion of such borrowings were subsidiary borrowings not guaranteed by AIG.

In February 2007, AIG's Board of Directors increased AIG's share repurchase program by authorizing the purchase of shares with an aggregate purchase price of $8 billion. In November 2007, AIG's Board of Directors authorized the purchase of an additional $8 billion in common stock. At May 7, 2008, $9 billion was available for purchase under the aggregate authorization. A total of 34,093,783 shares were purchased during the first three months of 2008. Subsequent to March 31, 2008, an additional 3,832,276 shares were purchased, satisfying the balance of the commitments existing at December 31, 2007 that had not been satisfied at March 31, 2008. AIG does not expect to purchase additional shares under its share repurchase program for the foreseeable future.

Liquidity

AIG manages liquidity at both the subsidiary and parent company levels. At March 31, 2008, AIG's consolidated invested assets, primarily held by its subsidiaries, included $63.6 billion in cash and short-term investments. Consolidated net cash provided from operating activities in the first three months of 2008 amounted to $8.3 billion. At both the subsidiary and parent company level, liquidity management activities are intended to preserve and enhance

funding stability, flexibility, and diversity through a wide range of potential operating environments and market conditions. AIG's primary sources of cash flow are dividends and other payments from its regulated and unregulated subsidiaries, as well as issuances of debt securities. Primary uses of cash flow are for debt service, subsidiary funding, shareholder dividend payments and common stock repurchases. Management believes that AIG's liquid assets, cash provided by operations and access to the capital markets will enable it to meet its anticipated cash requirements, including the funding of dividends under AIG's dividend policy.

Critical Accounting Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America (GAAP) requires the application of accounting policies that often involve a significant degree of judgment. AIG considers that its accounting policies that are most dependent on the application of estimates and assumptions, and therefore viewed as critical accounting estimates, to be those relating to reserves for losses and loss expenses, future policy benefits for life and accident and health contracts, recoverability of DAC, estimated gross profits for investment-oriented products, fair value measurements of certain financial assets and liabilities, other-than-temporary impairments, the allowance for finance receivable losses and flight equipment recoverability. These accounting estimates require the use of assumptions about matters, some of which are highly uncertain at the time of estimation. To the extent actual experience differs from the assumptions used, AIG's results of operations would be directly affected.

Throughout this Management's Discussion and Analysis of Financial Condition and Results of Operations, AIG's critical accounting estimates are discussed in detail. The major categories for which assumptions are developed and used to establish each critical accounting estimate are highlighted below.

Reserves for Losses and Loss Expenses (General Insurance):

- *Loss trend factors:* used to establish expected loss ratios for subsequent accident years based on premium rate adequacy and the projected loss ratio with respect to prior accident years.
- *Expected loss ratios for the latest accident year:* in this case, accident year 2007 for the year-end 2007 loss reserve analysis. For low-frequency, high-severity classes such as excess casualty, expected loss ratios generally are utilized for at least the three most recent accident years.
- *Loss development factors:* used to project the reported losses for each accident year to an ultimate amount.
- *Reinsurance recoverable on unpaid losses:* the expected recoveries from reinsurers on losses that have not yet been reported and/or settled.

Future Policy Benefits for Life and Accident and Health Contracts (Life Insurance & Retirement Services):

- *Interest rates:* which vary by geographical region, year of issuance and products.
- *Mortality, morbidity and surrender rates:* based upon actual experience by geographical region modified to allow for variation in policy form, risk classification and distribution channel.

Deferred Policy Acquisition Costs (Life Insurance & Retirement Services):

- *Recoverability:* based on current and future expected profitability, which is affected by interest rates, foreign exchange rates, mortality experience and policy persistency.

Deferred Policy Acquisition Costs (General Insurance):

- *Recoverability:* based upon the current terms and profitability of the underlying insurance contracts.

Estimated Gross Profits for Investment-Oriented Products (Life Insurance & Retirement Services):

- *Estimated gross profits:* to be realized over the estimated duration of the contracts (investment-oriented products) affect the carrying value of DAC, unearned revenue liability, SIAs and associated amortization patterns. Estimated gross profits include investment income and gains and losses on investments less required interest, actual mortality and other expenses.

Allowance for Finance Receivable Losses (Financial Services):

- *Historical defaults and delinquency experience:* utilizing factors, such as delinquency ratio, allowance ratio, charge-off ratio and charge-off coverage.
- *Portfolio characteristics:* portfolio composition and consideration of the recent changes to underwriting criteria and portfolio seasoning.
- *External factors:* consideration of current economic conditions, including levels of unemployment and personal bankruptcies.
- *Migration analysis:* empirical technique measuring historical movement of similar finance receivables through various levels of repayment, delinquency, and loss categories to existing finance receivable pools.

Flight Equipment Recoverability (Financial Services):

- *Expected undiscounted future net cash flows:* based upon current lease rates, projected future lease rates and estimated terminal values of each aircraft based on expectations of market participants.

Other-Than-Temporary Impairments:
AIG evaluates its investments for impairment such that a security is considered a candidate for other-than-temporary impairment if it meets any of the following criteria:

- Trading at a significant (25 percent or more) discount to par, amortized cost (if lower) or cost for an extended period of time (nine consecutive months or longer);
- The occurrence of a discrete credit event resulting in (i) the issuer defaulting on a material outstanding obligation; (ii) the issuer seeking protection from creditors under the bankruptcy laws or any similar laws intended for court supervised reorganization of insolvent enterprises; or (iii) the issuer proposing a voluntary reorganization pursuant to which creditors are asked to exchange their claims for cash or securities having a fair value substantially lower than par value of their claims; or
- AIG may not realize a full recovery on its investment, regardless of the occurrence of one of the foregoing events.

The determination that a security has incurred an other-than-temporary decline in value requires the judgment of management and consideration of the fundamental condition of the issuer, its near-term prospects and all the relevant facts and circumstances. The above criteria also consider circumstances of a rapid and severe market valuation decline, such as that experienced in current credit markets, in which AIG could not reasonably assert that the recovery period would be temporary (severity losses). For further discussion, see Portfolio Review — Other-Than-Temporary Impairments.

At each balance sheet date, AIG evaluates its securities holdings with unrealized losses. When AIG does not intend to hold such securities until they have recovered their cost basis, AIG records the unrealized loss in income. If a loss is recognized from a sale subsequent to a balance sheet date pursuant to changes in circumstances, the loss is recognized in the period in which the intent to hold the securities to recovery no longer existed.

In periods subsequent to the recognition of an other-than-temporary impairment charge for fixed maturity securities, which is not credit or foreign exchange related, AIG generally accretes into income the discount or amortizes the reduced premium resulting from the reduction in cost basis over the remaining life of the security.

Fair Value Measurements of Certain Financial Assets and Liabilities:

AIG measures at fair value on a recurring basis financial instruments in its trading and available for sale securities portfolios, certain mortgage and other loans receivable, certain spot commodities, derivative assets and liabilities, securities purchased (sold) under agreements to resell (repurchase), securities lending invested collateral, non-marketable equity investments, included in other invested assets, certain policyholders' contract deposits, securities and spot commodities sold but not yet purchased, certain trust deposits and deposits due to banks and other depositors, certain long-term borrowings, and certain hybrid financial instruments included in other liabilities. The fair value of a financial instrument is the amount that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date.

The degree of judgment used in measuring the fair value of financial instruments generally correlates with the level of pricing observability. Financial instruments with quoted prices in active markets generally have more pricing observability and less judgment is used in measuring fair value. Conversely, financial instruments traded in other-than-active markets or that do not have quoted prices have less observability and are measured at fair value using valuation models or other pricing techniques that require more judgment. Pricing observability is affected by a number of factors, including the type of financial instrument, whether the financial instrument is new to the market and not yet established, the characteristics specific to the transaction and general market conditions.

Fixed Maturities — Trading and Available for Sale

AIG maximizes the use of observable inputs and minimizes the use of unobservable inputs when measuring fair value. Whenever available, AIG obtains quoted prices in active markets for identical assets at the balance sheet date to measure at fair value fixed maturity instruments in its trading and available for sale portfolios. Market price data generally is obtained from exchange or dealer markets.

AIG estimates the fair value of fixed maturity instruments not traded in active markets, including securities purchased (sold) under agreements to resell (repurchase) and mortgage and other loans receivable, for which AIG elected the fair value option by referring to traded securities with similar attributes, using dealer quotations and matrix pricing methodologies, or discounted cash flow analyses. This methodology considers such factors as the issuer's industry, the security's rating and tenor, its coupon rate, its position in the capital structure of the issuer, yield curves, credit curves, prepayment rates and other relevant factors. For fixed maturity instruments that are not traded in active markets or that are subject to transfer restrictions, valuations are adjusted to reflect illiquidity and/or non-transferability, and such adjustments generally are based on available market evidence. In the absence of such evidence, management's best estimate is used.

Equity Securities Traded in Active Markets — Trading and Available for Sale

AIG maximizes the use of observable inputs and minimizes the use of unobservable inputs when measuring fair value. Whenever available, AIG obtains quoted prices in active markets for identical assets at the balance sheet date to measure at fair value marketable equity securities in its trading and available for sale portfolios. Market price data generally is obtained from exchange or dealer markets.

Direct Private Equity Securities Not Traded in Active Markets — Other Invested Assets

AIG initially estimates the fair value of equity securities not traded in active markets by reference to the transaction price. This valuation is adjusted only when changes to inputs and assumptions are corroborated by evidence such as transactions in similar instruments, completed or pending third-party transactions in the underlying investment or comparable entities, subsequent rounds of financing, recapitalizations and other transactions across the capital structure, offerings in the equity capital markets, and changes in financial ratios or cash flows. For equity securities that are not traded in active markets or that are subject to transfer restrictions, valuations are adjusted to reflect illiquidity and/or non-transferability and such adjustments generally are based on available market evidence. In the absence of such evidence, management's best estimate is used. AIG initially estimates the fair value of investments in private limited partnerships and hedge funds by reference to the transaction price. Subsequently, AIG obtains the fair value of these investments generally from net asset value information provided by the general partner or manager of the investments, the financial statements of which generally are audited annually.

Separate and Variable Account Assets

Separate and variable account assets are composed primarily of registered and unregistered open-end mutual funds that generally trade daily and are measured at fair value in the manner discussed above for equity securities traded in active markets.

Freestanding Derivatives

Derivative assets and liabilities can be exchange-traded or traded over the counter (OTC). AIG generally values exchange-traded derivatives within portfolios using models that calibrate to market clearing levels and eliminate timing differences between the closing price of the exchange-traded derivatives and their underlying instruments.

OTC derivatives are valued using market transactions and other market evidence whenever possible, including market-based inputs to models, model calibration to market clearing transactions, broker or dealer quotations or alternative pricing sources with reasonable levels of price transparency. When models are used, the selection of a particular model to value an OTC derivative depends on the contractual terms of, and specific risks inherent in, the instrument as well as the availability of pricing information in the market. AIG generally uses similar models to value similar instruments. Valuation models require a variety of inputs, including contractual terms, market prices and rates, yield curves, credit curves, measures of volatility, prepayment rates and correlations of such inputs. For OTC derivatives that trade in liquid markets, such as generic forwards, swaps and options, model inputs can generally be corroborated by observable market data by correlation or other means and model selection does not involve significant management judgment.

Certain OTC derivatives trade in less liquid markets with limited pricing information and the determination of fair value for these derivatives is inherently more difficult. When AIG does not have corroborating market evidence to support significant model inputs and cannot verify the model to market transactions, the transaction price is initially used as the best estimate of fair value. Accordingly, when a pricing model is used to value such an instrument, the model is adjusted so the model value at inception equals the transaction price. Subsequent to initial recognition, AIG updates valuation inputs when corroborated by evidence such as similar market transactions, third-party pricing services and/or broker or dealer quotations, or other empirical market data. When appropriate, valuations are adjusted for various factors such as liquidity, bid/offer spreads and credit considerations. Such adjustments are generally based on available market evidence. In the absence of such evidence, management's best estimate is used.

With the adoption of FAS 157 on January 1, 2008, AIG's own credit risk has been considered and is incorporated into the fair value measurement of all freestanding derivative liabilities.

Embedded Policy Derivatives

The fair value of embedded policy derivatives contained in certain variable annuity and equity-indexed annuity and life contracts is measured based on actuarial and capital market assumptions related to projected cash flows over the expected lives of the contracts. These cash flow estimates primarily include benefits and related fees assessed, when applicable, and incorporate expectations about policyholder behavior. Estimates of future policyholder behavior are subjective and based primarily on AIG's historical experience. With respect to embedded policy derivatives in AIG's variable annuity contracts, because of the dynamic and complex nature of the expected cash flows, risk neutral valuations are used. Estimating the underlying cash flows for these products involves many estimates and judgments, including those regarding expected market rates of return, market volatility,

correlations of market index returns to funds, fund performance, discount rates and policyholder behavior. With respect to embedded policy derivatives in AIG's equity-indexed annuity and life contracts, option pricing models are used to estimate fair value, taking into account assumptions for future equity indexed growth rates, volatility of the equity index, future interest rates, and determination on adjusting the participation rate and the cap on equity indexed credited rates in light of market conditions and policyholder behavior assumptions. With the adoption of FAS 157, these methodologies were not changed, with the exception of incorporating an explicit risk margin to take into consideration market participant estimates of projected cash flows and policyholder behavior.

AIGFP's Super Senior Credit Default Swap Portfolio

AIGFP values its credit default swaps written on the most senior risk layers (super senior) of designated pools of debt securities or loans using internal valuation models, third-party prices and market indices. The specific valuation methodologies vary based on the nature of the referenced obligations and availability of market prices. AIGFP uses a modified version of the Binomial Expansion Technique (BET) model to value its credit default swap portfolio written on super senior tranches of CDOs, including maturity-shortening puts that allow the holders of the securities issued by certain CDOs to treat the securities as short-term eligible 2a-7 investments under the Investment Company Act of 1940 (2a-7 Puts). The BET model uses default probabilities derived from credit spreads implied from market prices for the individual securities included in the underlying collateral pools securing the CDOs, as well as diversity scores, weighted average lives, recovery rates and discount rates. The determination of some of these inputs requires the use of judgment and estimates, particularly in the absence of market observable data. AIGFP also employs a Monte Carlo simulation to assist in quantifying the effect on the valuation of the CDOs of the unique aspects of the CDOs' structure such as triggers that divert cash flows to the most senior part of the capital structure. In the determination of fair value, AIGFP also considers collateral calls and the price estimates for the super senior CDO securities provided by third parties, including counterparties to these transactions. See Note 3 to Consolidated Financial Statements for additional information about fair value measurements.

In the case of credit default swaps written on investment-grade corporate debt and CLOs, AIGFP estimates the value of its obligations by reference to the relevant market indices or third-party quotes on the underlying super senior tranches where available.

In the case of credit default swaps written to facilitate regulatory capital relief for AIGFP's European financial institution counterparties, AIGFP estimates the fair value of these derivatives by considering observable market transactions, including the early termination of these transactions by counterparties, and other market data, to the extent relevant.

Policyholders' Contract Deposits

Policyholders' contract deposits accounted for at fair value beginning January 1, 2008 are measured using an income approach by taking into consideration the following factors:

- Current policyholder account values and related surrender charges,
- The present value of estimated future cash inflows (policy fees) and outflows (benefits and maintenance expenses) associated with the product using risk neutral valuations, incorporating expectations about policyholder behavior, market returns and other factors, and
- A risk margin that market participants would require for a market return and the uncertainty inherent in the model inputs.

The change in fair value of these policyholders' contract deposits is recorded as incurred policy losses and benefits in the consolidated statement of income (loss).

Level 3 Assets and Liabilities

Under FAS 157, assets and liabilities recorded at fair value in the consolidated balance sheet are classified in a hierarchy for disclosure purposes consisting of three "levels" based on the observability of inputs available in the marketplace used to measure the fair value. See Note 3 to the Consolidated Financial Statements for additional information about fair value measurements.

At March 31, 2008, AIG classified $48.5 billion and $31.7 billion of assets and liabilities, respectively, measured at fair value on a recurring basis as Level 3. This represented 5 percent and 3 percent of the total assets and liabilities, respectively, measured at fair value on a recurring basis. Level 3 fair value measurements are based on valuation techniques that use at least one significant input that is unobservable. These measurements are made under circumstances in which there is little, if any, market activity for the asset or liability. AIG's assessment of the significance of a particular input to the fair value measurement in its entirety requires judgment.

In making the assessment, AIG considers factors specific to the asset or liability. In certain cases, the inputs used to measure fair value of an asset or a liability may fall into different levels of the fair value hierarchy. In such cases, the level in the fair value hierarchy within which the fair value measurement in its entirety is classified is determined based on the lowest level input that is significant to the fair value measurement in its entirety.

Valuation of Level 3 Assets and Liabilities

AIG values its assets and liabilities classified as Level 3 using judgment and valuation models or other pricing techniques that require a variety of inputs including contractual terms, market prices and rates, yield curves, credit curves, measures of volatility, prepayment rates and correlations of such inputs, some of which may be unobservable. The following paragraphs describe the methods AIG uses to measure on a recurring basis the fair value of the major classes of assets and liabilities classified in Level 3.

Private equity and real estate fund investments: These assets initially are valued at the transaction price, i.e., the price paid to acquire the asset. Subsequently, they are measured based on net asset value using information provided by the general partner or manager of these investments, the accounts of which generally are audited on an annual basis.

Corporate bonds and private placement debt: These assets initially are valued at the transaction price. Subsequently, they are valued using market data for similar instruments (e.g., recent transactions, bond spreads or credit default swap spreads), comparisons to benchmark derivative indices or movements in underlying credit spreads. When observable price quotations are not available, fair value is determined based on cash flow models with yield curves, bond or single-name credit default swap spreads and recovery rates based on collateral values as key inputs.

Certain Residential Mortgage-Backed Securities (RMBS): These assets initially are valued at the transaction price. Subsequently, they may be valued by comparison to transactions in instruments with similar collateral and risk profiles, remittances received and updated cumulative loss data on underlying obligations, discounted cash flow techniques, and/or option adjusted spread analyses.

Certain Asset-Backed Securities (ABS) — non-mortgage: These assets initially are valued at the transaction price. Subsequently, they may be valued based on external price/spread data. When position-specific external price data are not observable, the valuation is based on prices of comparable securities.

CDOs: These assets initially are valued at the transaction price. Subsequently, they are valued based on external price/spread data from independent third parties, matrix pricing, or using the BET model.

Super senior credit default swap portfolio: AIGFP writes credit protection on the super senior risk layer of diversified portfolios of investment-grade corporate debt, collateralized loan obligations (CLOs) and multi-sector CDOs. AIGFP is at risk only on the super senior portion related to a diversified portfolio referenced to loans or debt securities, which is the last tranche to suffer losses after significant subordination.

At March 31, 2008 the notional amounts and unrealized market valuation loss of the super senior credit default swap portfolio, including certain regulatory capital relief driven trades, by asset class were as follows:

		Unrealized Market Valuation Loss	
	Notional Amount *(in billions)*	Three Months Ended March 31, 2008 *(in millions)*	Cumulative At March 31, 2008 *(in millions)*
Corporate loans[(a)]	$192	$ –	$ –
Prime residential mortgages[(a)]	143	–	–
Corporate debt/CLOs	57	896	1,123
Multi-sector CDOs[(b)]	77	8,037	19,281
Mezzanine tranches[(c)]	6	174	174
Total	$475	$9,107	$20,578

(a) Predominantly represent transactions written to facilitate regulatory capital relief.

(b) Approximately $60.6 billion in notional amount of the multi-sector CDO pools include some exposure to U.S. sub-prime mortgages.

(c) Represents credit default swaps written by AIGFP on tranches below super senior on certain regulatory capital relief trades.

The valuation of the super senior credit derivatives has become increasingly challenging given the limitation on the availability of market observable information due to the lack of trading and price transparency in the structured finance market, particularly during and since the fourth quarter of 2007. These market conditions have increased the reliance on management estimates and judgments in arriving at an estimate of fair value for financial reporting purposes. Further, disparities in the valuation methodologies employed by market participants and the varying judgments reached by such participants when assessing volatile markets has increased the likelihood that the various parties to these instruments may arrive at significantly different estimates as to their fair values.

AIGFP's valuation methodologies for the super senior credit default swap portfolio have evolved in response to the deteriorating market conditions and the lack of sufficient market observable information. AIG has sought to calibrate the model to market information and to review the assumptions of the model on a regular basis.

AIGFP employs a modified version of the BET model to value its credit default swap portfolio written on the super senior securities issued by CDOs, including the embedded 2a-7 Puts. The BET model uses default probabilities derived from credit spreads implied from market prices for the individual securities included in the underlying collateral pools securing the CDOs. AIGFP obtained prices on these securities from the CDO collateral managers.

The BET model also uses diversity scores, weighted average lives, recovery rates and discount rates. The

determination of some of these inputs requires the use of judgment and estimates, particularly in the absence of market observable data. AIGFP also employs a Monte Carlo simulation to assist in quantifying the effect on valuation of the CDO of the unique features of the CDOs' structure such as triggers that divert cash flows to the most senior level of the capital structure.

AIG selected the BET model for the following reasons:

- it is known and utilized by other institutions;
- it has been studied extensively, documented and enhanced over many years;
- it is transparent and relatively simple to apply;
- the parameters required to run the BET model are generally observable; and
- it can easily be modified to use probabilities of default and expected losses derived from the underlying collateral securities market prices instead of using rating-based historical probabilities of default.

AIG's implementation of the BET model uses a Monte Carlo simulation of the cash flows of each underlying CDO for various scenarios of defaults by the underlying collateral securities. The Monte Carlo simulation allows the model to take into account the cash flow waterfall and to capture the benefits due to cash flow diversion within each CDO.

The BET model has certain limitations. A well known limitation of the BET model is that it can understate the expected losses for super senior tranches when default correlations are high. The model uses correlations implied from diversity scores which do not capture the tendency for correlations to increase as defaults increase. Recognizing this concern, AIG tested the sensitivity of the valuations to the diversity scores. The results of the testing demonstrated that the valuations are not very sensitive to the diversity scores because the expected losses generated from the prices of the collateral pool securities are currently high, breaching the attachment point in most transactions. Once the attachment point is breached by a sufficient amount, the diversity scores, and their implied correlations, are no longer a significant driver of the valuation of a super senior tranche.

The credit default swaps written by AIGFP generally cover the failure of payment on the super senior CDO security. AIGFP does not own the securities in the CDO collateral pool. The credit spreads implied from the market prices of the securities in the CDO collateral pool incorporate the risk of default (credit risk), the market's price for liquidity risk and in distressed markets, the risk aversion costs. Spreads on credit derivatives tend to be narrower than the credit spreads implied from the market prices of the securities in the CDO collateral pool because, unlike investing in a bond, there is no need to fund the position (except when an actual credit event occurs). In times of illiquidity, the difference between spreads on cash securities and derivative instruments (the negative basis) may be even wider for high quality assets. AIGFP was unable to reliably verify this negative basis with market observable inputs due to the accelerating severe dislocation, illiquidity and lack of trading in the asset-backed securities market during the fourth quarter of 2007 and the first quarter of 2008. The valuations produced by the BET model therefore represent the valuations of the underlying super senior CDO cash securities based on AIG's assumptions about those securities, albeit with no recognition of any potential favorable effect of the basis differential on that valuation. AIGFP also considered the valuation of the super senior CDO securities provided by third parties, including counterparties to these transactions, and made adjustments as necessary.

The most significant assumption used in developing the estimate is the pricing of the securities within the CDO collateral pools. These prices are used to derive default probabilities that are used in the BET model. If the actual pricing of the securities within the collateral pools differs from the pricing used in estimating the fair value of the super senior credit default swap portfolio, there is potential for material variation in the fair value estimate. A decrease by five points (for example, from 87 cents per dollar to 82 cents per dollar) in the aggregate price of the securities would cause an additional unrealized market valuation loss of approximately $3.9 billion, while an increase in the aggregate price of the securities by five points (for example, from 90 cents per dollar to 95 cents per dollar) would reduce the unrealized market valuation loss by approximately $3.7 billion. The effect on the unrealized market valuation loss is not directly proportional to the change in the aggregate price of the securities.

The following table presents other key inputs used in the valuation of the credit derivative portfolio written on the super senior securities issued by multi-sector CDOs, and the potential increase (decrease) to the unrealized market valuation loss at March 31, 2008 calculated using the BET model for changes in these key inputs. The adjustments to the key inputs incorporated in the sensitivity analysis below are based on management's judgment of reasonably possible ranges for these inputs:

(in millions)	Increase (Decrease) To Unrealized Market Valuation Loss
Weighted average lives	
Effect of an increase of 1 year	$ 375
Effect of a decrease of 1 year	(620)
Recovery rates	
Effect of an increase of 10%	(103)
Effect of a decrease of 10%	194
Diversity scores	
Effect of an increase of 5	(40)
Effect of a decrease of 5	15
Discount curve	
Effect of an increase of 100 basis points	70

These results are calculated by stressing a particular assumption independently of changes in any other assumption. No assurance can be given that the actual levels of the key inputs will not exceed, perhaps significantly, the ranges assumed by AIG for purposes of the above analysis. No assumption should be made that results calculated from the use of other changes in these key inputs can be interpolated or extrapolated from the results set forth above.

In the case of credit default swaps written on investment grade corporate debt and CLOs, AIGFP estimates the value of its obligations by reference to the relevant market indices or third-party quotes on the underlying super senior tranches where available.

The following table represents the relevant market credit indices and index CDS maturity used in the valuation of the credit default swap portfolio written on investment-grade corporate debt and the increase (decrease) to the unrealized market valuation loss at March 31, 2008 corresponding to changes in these market credit indices and maturity:

(in millions)	Increase (Decrease) To Unrealized Market Valuation Loss		
CDS maturity (in years)	5	7	10
CDX Index			
Effect of an increase of 10 basis points	$26	$51	$ 5
Effect of a decrease of 10 basis points	(26)	(51)	(5)
iTraxx Index			
Effect of an increase of 10 basis points	11	37	13
Effect of a decrease of 10 basis points	(11)	(37)	(13)

These results are calculated by stressing a particular assumption independently of changes in any other assumption. No assurance can be given that the actual levels of the indices and maturity will not exceed, perhaps significantly, the ranges assumed by AIG for purposes of the above analysis. No assumption should be made that results calculated from the use of other changes in these indices and maturity can be interpolated or extrapolated from the results set forth above.

For additional information about AIG's super senior credit default swap portfolio, see Operating Review — Capital Markets Results and Risk Management — Credit Derivatives.

Other derivatives. Valuation models that incorporate unobservable inputs initially are calibrated to the transaction price. Subsequent valuations are based on observable inputs to the valuation model (e.g., interest rates, credit spreads, volatilities, etc.). Model inputs are changed only when corroborated by market data.

Valuation Controls

AIG is actively developing and implementing a remediation plan to address the material weakness in internal control relating to the fair value valuation of the AIGFP super senior credit default swap portfolio, and oversight thereof as described in Item 9A. of the 2007 Annual Report on Form 10-K. AIG is developing new systems and processes to reduce reliance on certain manual controls that have been established as compensating controls over valuation of this portfolio and in other areas, and is strengthening the resources required to remediate this weakness. Notwithstanding this need to continue strengthening these controls, AIG has an oversight structure that includes appropriate segregation of duties with respect to the valuation of its financial instruments. Senior management, independent of the trading and investing functions, is responsible for the oversight of control and valuation policies and for reporting the results of these controls and policies to AIG's Audit Committee. AIG employs procedures for the approval of new transaction types and markets, price verification, periodic review of profit and loss, and review of valuation models by personnel with appropriate technical knowledge of relevant products and markets. These procedures are performed by personnel independent of the trading and investing functions. For valuations that require inputs with little or no market observability, AIG compares the results of its valuation models to actual subsequent transactions.

Operating Review

General Insurance Operations

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

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

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

Transatlantic Holdings, Inc. (Transatlantic) subsidiaries offer reinsurance capacity on both a treaty and facultative basis both in the U.S. and abroad. Transatlantic structures

programs for a full range of property and casualty products with an emphasis on specialty risk.

AIG's Personal Lines operations provide automobile insurance through aigdirect.com, the newly formed operation resulting from the 2007 combination of AIG Direct and 21st Century Insurance Group (21st Century) operations, and the Agency Auto Division, as well as a broad range of coverages for high net worth individuals through the AIG Private Client Group.

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

AIG's Foreign General Insurance Group writes both commercial and consumer lines of insurance which is primarily underwritten through American International Underwriters (AIU), a marketing unit consisting of wholly owned agencies and insurance companies. The Foreign General Insurance Group also includes business written by AIG's foreign-based insurance subsidiaries.

General Insurance Results

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

(in millions, except ratios)	Three Months Ended March 31, 2008	Three Months Ended March 31, 2007	Percentage Increase/ (Decrease)
Net premiums written:			
AIG Property Casualty Group			
Commercial Insurance	**$ 5,113**	$ 6,009	(15)%
Transatlantic	**1,036**	984	5
Personal Lines	**1,288**	1,229	5
Mortgage Guaranty	**304**	266	14
Foreign General Insurance	**4,339**	3,618	20
Total	**$ 12,080**	$ 12,106	–%
Net premiums earned:			
AIG Property Casualty Group			
Commercial Insurance	**$ 5,417**	$ 5,981	(9)%
Transatlantic	**1,017**	965	5
Personal Lines	**1,199**	1,155	4
Mortgage Guaranty	**256**	210	22
Foreign General Insurance	**3,468**	2,908	19
Total	**$ 11,357**	$ 11,219	1%
Net investment income:			
AIG Property Casualty Group			
Commercial Insurance	**$ 743**	$ 1,033	(28)%
Transatlantic	**117**	116	1
Personal Lines	**57**	57	–
Mortgage Guaranty	**44**	37	19
Foreign General Insurance	**242**	319	(24)
Reclassifications and eliminations	**2**	1	100
Total	**$ 1,205**	$ 1,563	(23)%
Net realized capital gains (losses)	**$ (273)**	$ 121	–%
Operating income (loss):			
AIG Property Casualty Group			
Commercial Insurance	**$ 785**	$ 1,929	(59)%
Transatlantic	**162**	151	7
Personal Lines	**3**	106	(97)
Mortgage Guaranty	**(354)**	8	–
Foreign General Insurance	**736**	909	(19)
Reclassifications and eliminations	**5**	(7)	–
Total	**$ 1,337**	$ 3,096	(57)%
Statutory underwriting profit (loss)[(b)]:			
AIG Property Casualty Group			
Commercial Insurance	**$ 218**	$ 784	(72)%
Transatlantic	**54**	16	238
Personal Lines	**(63)**	33	–
Mortgage Guaranty	**(407)**	(42)	–
Foreign General Insurance	**364**	402	(9)
Total	**$ 166**	$ 1,193	(86)%
AIG Property Casualty Group:			
Loss Ratio	**78.6**	68.9	
Expense Ratio	**24.3**	21.1	
Combined Ratio	**102.9**	90.0	
Foreign General Insurance:			
Loss Ratio	**51.8**	50.6	
Expense Ratio[(a)]	**30.2**	28.6	
Combined ratio	**82.0**	79.2	
Consolidated:			
Loss Ratio	**70.4**	64.2	
Expense Ratio	**26.4**	23.3	
Combined Ratio	**96.8**	87.5	

(a) Includes amortization of advertising costs.

(b) Statutory underwriting profit (loss) is a measure that U.S. domiciled insurance companies are required to report to their regulatory authorities. The following table reconciles statutory underwriting profit (loss) to operating income for General Insurance:

(in millions)	Commercial Insurance	Transatlantic	Personal Lines	Mortgage Guaranty	Foreign General Insurance	Reclassifications and Eliminations	Total
Three Months Ended March 31, 2008:							
Statutory underwriting profit (loss)	**$ 218**	**$ 54**	**$ (63)**	**$(407)**	**$364**	**$ –**	**$ 166**
Increase (decrease) in DAC	**(3)**	**6**	**13**	**11**	**212**	**–**	**239**
Net investment income	**743**	**117**	**57**	**44**	**242**	**2**	**1,205**
Net realized capital gains (losses)	**(173)**	**(15)**	**(4)**	**(2)**	**(82)**	**3**	**(273)**
Operating income (loss)	**$ 785**	**$162**	**$ 3**	**$(354)**	**$736**	**$ 5**	**$1,337**
Three Months Ended March 31, 2007:							
Statutory underwriting profit (loss)	$ 784	$ 16	$ 33	$ (42)	$402	$ –	$1,193
Increase in DAC	35	4	15	12	153	–	219
Net investment income	1,033	116	57	37	319	1	1,563
Net realized capital gains (losses)	77	15	1	1	35	(8)	121
Operating income (loss)	$1,929	$151	$106	$ 8	$909	$(7)	$3,096

AIG transacts business in most major foreign currencies. The effects of changes in foreign currency exchange rates on the growth of General Insurance net premiums written were as follows:

	Three Months Ended March 31,	
	2008	2007
Growth in original currency*	**(3.3)%**	6.2%
Foreign exchange effect	**3.1**	1.4
Growth as reported in U.S. dollars	**(0.2)%**	7.6%

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

General Insurance operating income decreased in the first three months of 2008 compared to the same period in 2007 due to declines in both net investment income and underwriting profit as well as net realized capital losses in the first three months of 2008. The combined ratio for the three months ended March 31, 2008 increased to 96.8, an increase of 9.3 points compared to the same period in 2007, primarily due to an increase in the loss ratio of 6.2 points. The loss ratio for accident year 2008 recorded in the first three months of 2008 was 4.1 points higher than the loss ratio recorded in the first three months of 2007 for accident year 2007. The increase in the accident year loss ratio was due to an increase in Mortgage Guaranty losses as well as declining premium rates in most casualty lines of insurance due to competitive pressures. Increases in Mortgage Guaranty losses accounted for a 2.9 point increase in the 2008 accident year loss ratio. The downward cycle in the U.S. housing market is not expected to improve until residential inventories return to a more normal level, and AIG expects that this downward cycle will continue to adversely affect Mortgage Guaranty's loss ratios for the foreseeable future. Favorable development from prior years reduced incurred losses by $127 million and $131 million in the first three months of 2008 and 2007, respectively. The favorable development in 2008 includes $339 million of favorable development related to policies whose premiums vary with the level of losses incurred (loss sensitive policies). Loss sensitive policies did not have a significant effect in 2007. The favorable development on loss sensitive policies had no effect on underwriting profit as it was entirely offset by a reduction in earned premiums. However, this reduction in earned premiums reduced the loss ratio by 0.9 points compared to the same period in 2007. Other loss development for the first three months of 2008 increased incurred losses by $212 million, accounting for 3.0 points of the increase in the loss ratio compared to the same period of 2007. Additional favorable loss development in the first three months of 2008 and 2007, of $37 million and $17 million, respectively (recognized in consolidation and related to certain asbestos settlements), reduced overall incurred losses.

General Insurance net premiums written decreased in the first three months of 2008 compared to the same period in 2007, primarily due to a reduction of $339 million in Commercial Insurance loss sensitive policies and declines in Commercial Insurance workers' compensation premiums due to reductions in statutory rates and increased competition. The decline in Commercial Insurance was partially offset by growth in Foreign General Insurance from both established and new distribution channels, and the effect of changes in foreign currency exchange rates as well as growth in Mortgage Guaranty, primarily the domestic first-lien business.

General Insurance net investment income declined in the first three months of 2008 by $358 million compared to the same period in 2007. Interest and dividend income increased $109 million in the first three months of 2008 compared to the same period in 2007 as fixed maturities and equity securities increased by $8.8 billion and the average yield was substantially unchanged for both periods. Income from partnership and mutual fund investments declined $524 million in the first three months of 2008 compared to the same period in 2007, primarily due to poor performance in the equity markets in 2008. Investment expenses in the first three months of 2008 declined $50 million compared to the same period in 2007, primarily due to decreased interest expense on deposit liabilities. Net realized capital losses in the first three months of 2008 include other-than-temporary impairment charges of $155 million compared to $46 million in the same period of 2007. See also Capital Resources and Liquidity and Invested Assets herein.

Commercial Insurance Results

Commercial Insurance's operating income decreased in the first three months of 2008 compared to the same period in 2007 primarily due to declines in both net investment income and underwriting profit. The decline is also reflected in the combined ratio, which increased 10.5 points in the first three months of 2008 compared to the same period in 2007. The loss ratio for accident year 2008, including 1.4 points related to Atlanta catastrophe tornado losses, recorded in the first three months of 2008 was 3.8 points higher than the loss ratio recorded in the first three months of 2007 for accident year 2007. Prior year development reduced incurred losses by $217 million in the first three months of 2008 compared to $87 million in the first three months of 2007. The favorable development for 2008 includes $339 million of favorable development related to loss sensitive polices. The favorable development on loss sensitive policies had no effect on underwriting profit as it was entirely offset by a reduction in earned premiums. However, given the reduction in earned premiums, there was a reduction in the loss ratio of 1.6 points compared to the same period of 2007 related to loss sensitive policies. Other loss development for the first three months of 2008 increased incurred losses by $122 million, accounting for 3.6 points of the increase in the loss ratio compared to the same period of 2007.

Commercial Insurance's net premiums written declined in the first three months of 2008 compared to the same period in 2007 primarily due to declines in workers' compensation premiums and the effect of the loss sensitive policies described above.

Commercial Insurance's expense ratio increased to 23.9 in the first three months of 2008 compared to 19.2 in the same period of 2007. Return premiums on loss sensitive policies reduced net premiums written, without a corresponding reduction in expenses, increasing the expense ratio by 1.4 points for the first three months of 2008 compared to the same period in 2007. The ratio of general expenses to current period net premiums written increased 1.9 points in the first three months of 2008 compared to the same period in 2007 as Commercial Insurance continued to invest in systems and process improvements to enhance operating efficiency over the long term. The ratio of net acquisition expenses to current period net premiums written increased 1.0 points in the first three months of 2008 compared to the same period in 2007 due to higher commissions to brokers and a reduction in ceding commissions resulting from increased retention of business.

Commercial Insurance's net investment income declined in the first three months of 2008 compared to the same period in 2007, as income from partnership and mutual fund investments decreased $409 million in the first three months of 2008 compared to the same period in 2007, primarily due to poor performance in the equity markets in 2008. This decrease was partially offset by an increase in interest income of $40 million in the first three months of 2008, due to growth in the bond portfolio resulting from investment of operating cash flows. Commercial Insurance recorded net realized capital losses in the first three months of 2008 compared to net realized capital gains in the same period of 2007 primarily due to other-than-temporary impairment charges of $144 million in the first three months of 2008, primarily related to equity securities, compared to $36 million in the first three months of 2007.

Transatlantic Results

Transatlantic's net premiums written increased in the first three months of 2008 compared to the same period in 2007 due to growth in domestic operations and changes in foreign exchange rates. The increase in statutory underwriting profit in the first three months of 2008 compared to the same period in 2007 reflects improved underwriting results in international operations. The 2007 international underwriting results were adversely affected by European windstorm losses. Operating income increased in the first three months of 2008 compared to the same period in 2007 primarily due to improved underwriting results, partially offset by net realized capital losses in 2008 compared to net realized capital gains in 2007.

Personal Lines Results

Personal Lines operating income decreased $103 million in the first three months of 2008 compared to the same period in 2007 due to a deterioration in underwriting performance as reflected by the combined ratio, which increased to 103.4 in the first three months of 2008 compared to 95.5 in the same period in 2007. The loss ratio increased 8.5 points, including an increase in the 2008 accident year loss ratio of 3.0 points, due primarily to increased frequency of homeowner claims in the Private Client Group and declining rates for automobile policies. Prior year development increased incurred losses by $36 million in the first three months of 2008 compared to a reduction of $29 million in the same period in 2007, accounting for 5.5 points of the increase in the loss ratio.

The expense ratio decreased 0.6 points in the first three months of 2008 compared to the same period in 2007, primarily due to expense savings following the integration of the 21st Century operations.

Net premiums written increased in the first three months of 2008 compared to the same period in 2007 primarily due to continued growth in the Private Client Group, and an increase in aigdirect.com, partially offset by a reduction from the Agency Auto business.

Mortgage Guaranty Results

Mortgage Guaranty's operating loss in the first three months of 2008 was $354 million compared to operating income of $8 million in the first three months of 2007 as the deteriorating U.S. residential housing market adversely affected losses incurred for both the domestic first- and second-lien businesses. Domestic first- and second-lien losses incurred increased 363 percent and 123 percent respectively, compared to the first three months of 2007, resulting in loss ratios of 203.6 and 442.4, respectively, in the first three months of 2008. Increases in domestic losses incurred resulted in an overall loss ratio of 235.6 in the first three months of 2008 compared to 92.2 in the first three months of 2007. Prior year development increased incurred losses by $68 million and $31 million for the first three months of 2008 and 2007, respectively, accounting for 12.0 points of the increase in the 2008 loss ratio.

Net premiums written increased in the first three months of 2008 compared to the same period in 2007 primarily due to growth in domestic first-lien premiums due to the increased use of mortgage insurance for credit enhancement as well as better persistency. UGC has taken steps to strengthen its underwriting guidelines and increase rates. It also discontinued new production for certain programs in the second-lien business beginning in the fourth quarter of 2006. However, UGC will continue to receive renewal premiums on that portfolio for the life of the loans, estimated to be three to five years, and will continue to be exposed to losses from future defaults.

The expense ratio in the first three months of 2008 was 19.8, down from 21.7 in the same period of 2007 as premium growth offset the effect of increased expenses related to UGC's international expansion and the employment of additional operational resources in the second-lien business.

UGC domestic mortgage risk in force totaled $31.5 billion as of March 31, 2008 and the 60-day delinquency ratio was 4.0 percent (based on number of policies, consistent with mortgage industry practice) compared to domestic mortgage risk in force of $25.4 billion and a delinquency ratio of 2.1 percent at March 31, 2007. Approximately 82 percent of the domestic mortgage risk is secured by first-lien, owner-occupied properties.

Foreign General Insurance Results

Foreign General Insurance operating income decreased in the first three months of 2008 compared to the same period in 2007, due primarily to decreases in net investment income and net realized capital losses in the first three months of 2008.

Net premiums written increased 20 percent (11 percent in original currency) in the first three months of 2008 compared to the same period in 2007, reflecting strong growth in commercial and consumer lines driven by new business from both established and new distribution channels, including the late 2007 acquisition of Württembergische und Badische Versicherungs – AG (WüBa) in Germany. Net premiums written for commercial lines increased due to new business in the U.K. and Europe and decreases in the use of reinsurance, partially offset by declines in premium rates. Growth in personal accident business in Latin America, Asia and Europe also contributed to the increase. Net premiums written for the Lloyd's syndicate Ascot and aviation continued to decline due to rate decreases and increased market competition. Auto production declined due to increased price competition and underwriting actions taken to improve profitability.

The loss ratio in the first three months 2008 increased 1.2 points compared to the same period in 2007. The increase is due to favorable loss development on prior accident years of $17 million in the first three months of 2008 compared to $64 million in the first three months of 2007, higher severe but non-catastrophic losses and higher losses in aviation. Partially offsetting these increases was an improvement in the personal accident loss ratio, particularly in Asia.

The expense ratio in the first three months of 2008 increased 1.6 points compared to the same period in 2007. This increase reflects the cost of realigning certain legal entities through which Foreign General Insurance operates, the acquisition of WüBa and the increased significance of consumer lines of business, which have higher acquisition costs. These factors contributed 0.8 points to the expense ratio in the first three months of 2008. AIG expects the expense ratio to continue to increase in 2008 due to the cost of realigning certain legal entities through which Foreign General Insurance operates.

Net investment income decreased in the first three months of 2008 compared to the same period in 2007. Mutual fund income was $105 million lower than the first three months of 2007 reflecting weak performance in the equity markets in 2008, partially offset by higher interest income of $34 million.

Reserve for Losses and Loss Expenses

The following table presents the components of the General Insurance gross reserve for losses and loss expenses (loss reserves) by major lines of business on a statutory Annual Statement basis*:

(in millions)	**March 31, 2008**	December 31, 2007
Other liability occurrence	**$ 20,635**	$ 20,580
Workers compensation	**15,080**	15,568
Other liability claims made	**13,709**	13,878
International	**8,348**	7,036
Auto liability	**6,157**	6,068
Property	**4,431**	4,274
Reinsurance	**3,234**	3,127
Products liability	**2,417**	2,416
Medical malpractice	**2,301**	2,361
Mortgage guaranty/credit	**1,832**	1,426
Accident and health	**1,815**	1,818
Commercial multiple peril	**1,796**	1,900
Aircraft	**1,731**	1,623
Fidelity/surety	**1,201**	1,222
Other	**2,173**	2,203
Total	**$ 86,860**	$ 85,500

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

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

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

At March 31, 2008, General Insurance net loss reserves increased $1.22 billion from the prior year-end to $70.51 billion. The net loss reserves represent loss reserves reduced by reinsurance recoverable, net of an allowance for unrecoverable reinsurance and applicable discount for future investment income.

The following table classifies the components of the General Insurance net loss reserve by business unit:

(in millions)	**March 31, 2008**	December 31, 2007
Commercial Insurance[(a)]	**$47,751**	$47,392
Transatlantic	**7,136**	6,900
Personal Lines[(b)]	**2,409**	2,417
Mortgage Guaranty	**1,598**	1,339
Foreign General Insurance[(c)]	**11,613**	11,240
Total Net Loss Reserve	**$70,507**	$69,288

(a) At March 31, 2008 and December 31, 2007, respectively, Commercial Insurance loss reserves include approximately $2.99 billion and $3.13 billion ($3.19 billion and $3.34 billion, respectively, before discount), related to business written by Commercial Insurance but ceded to American International Reinsurance Company Limited (AIRCO) and reported in AIRCO's statutory filings. Commercial Insurance loss reserves also include approximately $624 million and $590 million related to business included in AIUO's statutory filings at March 31, 2008 and December 31, 2007, respectively.

(b) At March 31, 2008 and December 31, 2007, respectively, Personal Lines loss reserves include $971 million and $894 million related to business ceded to Commercial Insurance and reported in Commercial Insurance's statutory filings.

(c) At March 31, 2008 and December 31, 2007, respectively, Foreign General Insurance loss reserves include approximately $1.97 billion and $3.02 billion related to business reported in Commercial Insurance's statutory filings.

The Commercial Insurance net loss reserve of $47.8 billion is comprised principally of the business of AIG subsidiaries participating in the American Home Assurance Company (American Home)/National Union Fire Insurance Company of Pittsburgh, Pa. (National Union) pool (10 companies) and the surplus lines pool (Lexington Insurance Company, AIG Excess Liability Insurance Company and Landmark Insurance Company).

Commercial Insurance cedes a quota share percentage of its other liability occurrence and products liability occurrence business to AIRCO. The quota share percentage ceded was 10 percent in the first three months of 2008 and 15 percent in 2007 and covered all business written in these years for these lines by participants in the American Home/National Union pool. AIRCO's loss reserves relating to these quota share cessions from Commercial Insurance are recorded on a discounted basis. As of March 31, 2008, AIRCO carried a discount of approximately $200 million applicable to the $3.19 billion in undiscounted reserves it assumed from the

American Home/National Union pool via this quota share cession. AIRCO also carries approximately $537 million in net loss reserves relating to Foreign General Insurance business. These reserves are carried on an undiscounted basis.

The companies participating in the American Home/National Union pool have maintained a participation in the business written by AIU for decades. As of March 31, 2008, these AIU reserves carried by participants in the American Home/National Union pool totaled approximately $1.97 billion. The remaining Foreign General Insurance reserves are carried by American International Underwriter Overseas, Ltd. (AIUO), AIRCO, AIG U.K., and other smaller AIG subsidiaries domiciled outside the United States. Statutory filings in the United States by AIG companies reflect all the business written by U.S. domiciled entities only, and therefore exclude business written by AIUO, AIRCO, and all other internationally domiciled subsidiaries. The total reserves carried at March 31, 2008 by AIUO and AIRCO were approximately $3.41 billion and $3.53 billion, respectively. AIRCO's $3.53 billion in total general insurance reserves consist of approximately $2.99 billion from business assumed from the American Home/National Union pool and an additional $537 million relating to Foreign General Insurance business.

Discounting of Reserves

At March 31, 2008, AIG's overall General Insurance net loss reserves reflect a loss reserve discount of $2.43 billion, including tabular and non-tabular calculations. The tabular workers compensation discount is calculated using a 3.5 percent interest rate and the 1979-81 Decennial Mortality Table. The non-tabular workers' compensation discount is calculated separately for companies domiciled in New York and Pennsylvania, and follows the statutory regulations for each state. For New York companies, the discount is based on a five percent interest rate and the companies' own payout patterns. For Pennsylvania companies, the statute has specified discount factors for accident years 2001 and prior, which are based on a six percent interest rate and an industry payout pattern. For accident years 2002 and subsequent, the discount is based on the yield of U.S. Treasury securities ranging from one to twenty years and the company's own payout pattern, with the future expected payment for each year using the interest rate associated with the corresponding Treasury security yield for that time period. The discount is comprised of the following: $794 million — tabular discount for workers' compensation in Commercial Insurance; $1.44 billion — non-tabular discount for workers' compensation in Commercial Insurance; and $200 million — non-tabular discount for other liability occurrence and products liability occurrence in AIRCO. The total undiscounted workers' compensation loss reserve carried by Commercial Insurance is approximately $13.3 billion as of March 31, 2008. The other liability occurrence and products liability occurrence business in AIRCO that is assumed from Commercial Insurance is discounted based on the yield of U.S. Treasury securities ranging from one to twenty years and the Commercial Insurance payout pattern for this business. The undiscounted reserves assumed by AIRCO from Commercial Insurance totaled approximately $3.19 billion at March 31, 2008.

Quarterly Reserving Process

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

The reconciliation of net loss reserves was as follows:

	Three Months Ended March 31,	
(in millions)	**2008**	2007
Net reserve for losses and loss expenses at beginning of year	**$69,288**	$62,630
Foreign exchange effect	**70**	(38)
Losses and loss expenses incurred:		
Current year	**8,021**	7,215
Prior years, other than accretion of discount	**(164)**	(148)
Prior years, accretion of discount	**104**	116
Losses and loss expenses incurred	**7,961**	7,183
Losses and loss expenses paid	**6,812**	5,741
Net reserve for losses and loss expenses at end of period	**$70,507**	$64,034

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

(in millions)	Three Months Ended March 31, 2008	2007
Prior Accident Year Development by Reporting Unit:		
Commercial Insurance	**$ (217)**	$ (87)
Personal Lines	**36**	(29)
Mortgage Guaranty	**68**	31
Foreign General Insurance	**(17)**	(64)
Subtotal	**(130)**	(149)
Transatlantic	**3**	18
Asbestos settlements*	**(37)**	(17)
Prior years, other than accretion of discount	**$ (164)**	$ (148)

* *Amounts for 2007 have been conformed to the 2008 presentation.*

(in millions)	Calendar Year 2008	2007
Prior Accident Year Development by Accident Year:		
2007	**$ (35)**	
2006	**(178)**	$ (178)
2005	**(204)**	(31)
2004	**(131)**	(47)
2003	**(24)**	(9)
2002	**6**	18
2001 & prior	**402**	99
Prior years, other than accretion of discount	**$ (164)**	$ (148)

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

2008 Net Loss Development

In the first three months of 2008, net loss development from prior accident years was favorable by approximately $164 million, including approximately $339 million of favorable development relating to loss sensitive business (which was offset by an equal amount of negative earned premium development), and excluding approximately $104 million from accretion of loss reserve discount. Excluding both the favorable development relating to loss sensitive business and accretion of loss reserve discount, net loss development from prior accident years in the first three months of 2008 was adverse by approximately $175 million. The overall favorable development of $164 million consisted of approximately $572 million of favorable development from accident years 2003 through 2007 partially offset by approximately $408 million of adverse loss development from accident years 2002 and prior. Excluding the favorable development from loss sensitive business, the overall adverse development of $175 million consisted of approximately $269 million of favorable development from accident years 2003 through 2007 offset by approximately $444 million of adverse development from accident years 2002 and prior. The adverse development from accident years 2002 and prior was primarily related to excess casualty business within Commercial Insurance for the 2000 and prior accident years. The favorable development from accident years 2003 through 2007 included approximately $300 million in favorable development from loss sensitive business written by AIG Risk Management, and approximately $160 million in favorable development from business written by Lexington Insurance Company, including Healthcare, AIG CAT Excess, Casualty and Program business. AIG Executive Liability business contributed approximately $50 million to the favorable development from accident years 2004 and 2005, relating primarily to D&O. Accident year 2007 produced overall favorable development of approximately $35 million, which included approximately $76 million of adverse development from Mortgage Guaranty and $18 million of adverse development from Personal Lines, offset by favorable development from most classes of business in Commercial Insurance and from Transatlantic.

2007 Net Loss Development

In the first three months of 2007, net loss development from prior accident years was favorable by approximately $148 million, including approximately $36 million of adverse development pertaining to the major hurricanes in 2004 and 2005; and $18 million of adverse development from the general reinsurance operations of Transatlantic; and excluding approximately $116 million from accretion of loss reserve discount. Excluding catastrophes and Transatlantic, as well as accretion of discount, net loss development in the first three months of 2007 from prior accident years was favorable by approximately $202 million. The overall favorable development of $148 million consisted of approximately $265 million of favorable development from accident years 2003 through 2006, partially offset by approximately $117 million of adverse development from accident years 2002 and prior. For the first three months of 2007, most classes of AIG's business continued to experience

favorable development for accident years 2003 through 2006. The adverse development from accident years 2002 and prior reflected development from excess casualty within Commercial Insurance and from Transatlantic.

Asbestos and Environmental Reserves

The estimation of loss reserves relating to asbestos and environmental claims on insurance policies written many years ago is subject to greater uncertainty than other types of claims due to inconsistent court decisions as well as judicial interpretations and legislative actions that in some cases have tended to broaden coverage beyond the original intent of such policies and in others have expanded theories of liability.

As described more fully in the 2007 Annual Report on Form 10-K, AIG's reserves relating to asbestos and environmental claims reflect a comprehensive ground-up analysis. In the first three months of 2008, AIG maintained the ultimate loss estimates for asbestos and environmental claims resulting from the recently completed reserve analyses. A relatively minor amount of favorable incurred loss development pertaining to asbestos was reflected in the first three months of 2008, as presented in the table that follows. This development was primarily attributable to one large settlement.

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

	Three Months Ended March 31,			
	2008		2007	
(in millions)	Gross	Net	Gross[a]	Net
Asbestos:				
Reserve for losses and loss expenses at beginning of year	**$3,864**	**$1,454**	$4,523	$1,889
Losses and loss expenses incurred[b]	**(29)**	**(33)**	(10)	(17)
Losses and loss expenses paid[b]	**(237)**	**(121)**	(200)	(128)
Reserve for losses and loss expenses at end of period	**$3,598**	**$1,300**	$4,313	$1,744
Environmental:				
Reserve for losses and loss expenses at beginning of year	**$ 515**	**$ 237**	$ 629	$ 290
Losses and loss expenses incurred[b]	**(5)**	**—**	—	—
Losses and loss expenses paid[b]	**(14)**	**(10)**	(15)	(9)
Reserve for losses and loss expenses at end of period	**$ 496**	**$ 227**	$ 614	$ 281
Combined:				
Reserve for losses and loss expenses at beginning of year	**$4,379**	**$1,691**	$5,152	$2,179
Losses and loss expenses incurred[b]	**(34)**	**(33)**	(10)	(17)
Losses and loss expenses paid[b]	**(251)**	**(131)**	(215)	(137)
Reserve for losses and loss expenses at end of period	**$4,094**	**$1,527**	$4,927	$2,025

(a) Gross amounts were revised from the presentation in prior periods to reflect the inclusion of certain reserves not previously identified as asbestos and environmental related. This revision had no effect on net reserves.

(b) All amounts pertain to policies underwritten in prior years, primarily to policies issued in 1984 and prior.

The gross and net IBNR included in the reserve for losses and loss expenses, relating to asbestos and environmental claims separately and combined, were estimated as follows:

	Three Months Ended March 31,			
	2008		2007	
(in millions)	Gross	Net	Gross*	Net
Asbestos	**$2,409**	**$1,052**	$3,249	$1,436
Environmental	**344**	**132**	368	161
Combined	**$2,753**	**$1,184**	$3,617	$1,597

** Gross amounts were revised from the presentation in prior periods to reflect the inclusion of certain reserves not previously identified as asbestos and environmental related. This revision had no effect on net reserves.*

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

	Three Months Ended March 31,					
	2008			2007		
	Asbestos	Environmental	Combined	Asbestos	Environmental	Combined
Claims at beginning of year	**6,563**	**7,652**	**14,215**	6,878	9,442	16,320
Claims during year:						
Opened	**198**	**321**	**519**	200	411	611
Settled	**(30)**	**(39)**	**(69)**	(32)	(13)	(45)
Dismissed or otherwise resolved	**(344)**	**(669)**	**(1,013)**	(246)	(389)	(635)
Claims at end of period	**6,387**	**7,265**	**13,652**	6,800	9,451	16,251

Survival Ratios — Asbestos and Environmental

The following table presents AIG's survival ratios for asbestos and environmental claims at March 31, 2008 and 2007. The survival ratio is derived by dividing the current carried loss reserve by the average payments for the three most recent calendar years for these claims. Therefore, the survival ratio is a simplistic measure estimating the number of years it would be before the current ending loss reserves for these claims would be paid off using recent year average payments. The March 31, 2008 survival ratio is lower than the ratio at March 31, 2007 because the more recent periods included in the rolling average reflect higher claims payments. In addition, AIG's survival ratio for asbestos claims was negatively affected by the favorable settlement described above, as well as several similar settlements during 2007. These settlements reduced gross and net asbestos survival ratios at March 31, 2008 by approximately 1.6 years and 3.2 years, respectively, and reduced gross and net asbestos survival ratios at March 31, 2007 by approximately 1.0 year and 2.4 years, respectively. Many factors, such as aggressive settlement procedures, mix of business and level of coverage provided, have a significant effect on the amount of asbestos and environmental reserves and payments and the resultant survival ratio. Moreover, as discussed above, the primary basis for AIG's determination of its reserves is not survival ratios, but instead the ground-up and top-down analysis. Thus, caution should be exercised in attempting to determine reserve adequacy for these claims based simply on this survival ratio.

AIG's survival ratios for asbestos and environmental claims, separately and combined were based upon a three-year average payment. These ratios at March 31, 2008 and 2007 were as follows:

	Gross*	Net
2008		
Survival ratios:		
Asbestos	6.1	4.5
Environmental	4.8	3.6
Combined	5.9	4.3
2007		
Survival ratios:		
Asbestos	10.4	9.9
Environmental	5.8	4.4
Combined	9.5	8.4

** Gross amounts for 2007 were revised from the presentation in prior periods to reflect the inclusion of certain reserves not previously identified as asbestos and environmental related. This revision had no effect on net reserves.*

Life Insurance & Retirement Services Operations

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

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

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

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

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

Foreign Life Insurance & Retirement Services

Japan and Other

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

Asia

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

Domestic Life Insurance

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

Domestic Retirement Services

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

Life Insurance & Retirement Services Results

Life Insurance & Retirement Services results were as follows:

(in millions)	Premiums and Other Considerations	Net Investment Income	Net Realized Capital Gains (Losses)	Total Revenues	Operating Income (Loss)
Three Months Ended March 31, 2008					
Foreign Life Insurance & Retirement Services	**$7,447**	**$1,448**	**$ (722)**	**$ 8,173**	**$ 735**
Domestic Life Insurance	**1,587**	**984**	**(1,288)**	**1,283**	**(870)**
Domestic Retirement Services	**284**	**1,371**	**(2,359)**	**(704)**	**(1,696)**
Total	**$9,318**	**$3,803**	**$(4,369)**	**$ 8,752**	**$(1,831)**
Three Months Ended March 31, 2007					
Foreign Life Insurance & Retirement Services	$6,613	$2,883	$ (235)	$ 9,261	$ 1,284
Domestic Life Insurance	1,528	1,005	(12)	2,521	345
Domestic Retirement Services	284	1,625	(9)	1,900	652
Total	$8,425	$5,513	$ (256)	$13,682	$ 2,281
Percentage Increase/(Decrease) from Prior Year:					
Foreign Life Insurance & Retirement Services	13%	(50)%	–%	(12)%	(43)%
Domestic Life Insurance	4	(2)	–	(49)	–
Domestic Retirement Services	–	(16)	–	–	–
Total	11%	(31)%	–%	(36)%	–%

The gross insurance in force for Life Insurance & Retirement Services was as follows:

(in millions)	**March 31, 2008**	December 31, 2007
Foreign*	**$1,411,374**	$ 1,327,251
Domestic	**998,771**	984,794
Total	**$2,410,145**	$ 2,312,045

** Includes an increase of $46.6 billion related to changes in foreign exchange rates at March 31, 2008.*

Disruption in the U.S. residential mortgage and credit markets was the key driver of operating results for the first three months of 2008 primarily due to significant net realized capital losses resulting from other-than-temporary impairment charges of $4.4 billion compared to other-than-temporary impairment charges of $392 million in the same period of 2007. In addition, net investment income and certain products continued to be negatively affected by the volatile markets.

Life Insurance & Retirement Services total revenues in the first three months of 2008 reflect growth in premiums and other considerations compared to the same period in 2007, primarily due to strong life insurance production in the Foreign Life Insurance & Retirement Services operations, growth in a block of U.K. investment-oriented products and higher sales of payout annuities in the Domestic Life Insurance operations. Overall growth in premiums and other considerations was dampened by a continuing shift to investment-oriented products and the suspension in the second quarter of 2007 of new sales on certain products in Japan pending completion of an industry wide review by the tax authorities. This review was finalized in March 2008 and resulted in lower tax deductibility of these products. Although sales of these products have restarted in Japan, it is expected that sales will be at lower than historical levels.

Net investment income decreased in the first three months of 2008 compared to the same period in 2007 due to lower partnership and mutual fund income as well as lower policyholder investment income and trading gains and losses (together, policyholder trading gains (losses)) reflecting equity market declines. Policyholder trading gains and losses are offset by a charge to incurred policy losses and benefits expense. Policyholder trading gains and losses generally reflect the trends in equity markets, principally in Japan and Asia. Policyholder trading losses were $785 million in the first three months of 2008 compared to gains of $797 million in the same period of 2007.

The operating loss in the first three months of 2008 was significantly affected by net realized capital losses which totaled $4.4 billion compared to net realized capital losses of $256 million in the same period in 2007. The higher net realized capital losses were primarily related to severity impairments and foreign exchange losses due to the credit market disruption and weakening of the dollar against Asian currencies. The higher net realized capital losses and lower yield enhancement investment income more than offset the positive effect of growth in underlying reserves which reflects increased assets under management. Other factors that negatively affected operating income in the first three months of 2008 were trading account losses of $88 million in the U.K. associated with certain investment-linked products and an increase in incurred policyholder benefits of $80 million related to a closed block of Japan business with guaranteed benefits, partially offset by the favorable effect of foreign exchange rates. Operating income in the first three months of 2008 included a DAC and SIA benefit of $267 million related to net realized capital losses in the first three months of 2008 compared to $11 million in the same period in 2007.

Operating income in the first three months of 2007 included additional claim expense of $37 million related to the industry wide regulatory review of claims in Japan and a $50 million charge related to balance sheet reconciliation remediation activities in Asia.

The most significant effect on the Life Insurance & Retirement Services results from AIG's adoption of FAS 157 was the change in measurement of fair value for embedded policy derivatives. The pre-tax effect of adoption related to embedded policy derivatives was an increase in net realized capital losses of $155 million as of January 1, 2008, partially offset by a $47 million DAC benefit related to these losses. The effect of initial adoption was primarily due to an increase in the embedded policy derivative liability valuations resulting from the inclusion of explicit risk margins.

AIG adopted FAS 159 on January 1, 2008 and elected to apply the fair value option to a closed block of single premium variable life business in Japan and for an investment-linked product sold principally in Asia. The adoption of FAS 159 with respect to these fair value elections resulted in a decrease to 2008 opening retained earnings of $559 million, net of tax. The fair value of the liabilities for these policies totaled $3.5 billion at March 31, 2008 and is reported in policyholders' contract deposits.

Foreign Life Insurance & Retirement Services Results

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

(in millions)	Premiums and Other Considerations	Net Investment Income	Net Realized Capital Gains (Losses)	Total Revenues	Operating Income (Loss)
Three Months Ended March 31, 2008					
Life insurance	**$4,512**	**$ 919**	**$(567)**	**$4,864**	**$ 231**
Personal accident	**1,691**	**92**	**(40)**	**1,743**	**377**
Group products	**996**	**153**	**(30)**	**1,119**	**89**
Individual fixed annuities	**129**	**569**	**(113)**	**585**	**58**
Individual variable annuities	**119**	**(285)**	**28**	**(138)**	**(20)**
Total	**$7,447**	**$1,448**	**$(722)**	**$8,173**	**$ 735**
Three Months Ended March 31, 2007					
Life insurance	$4,167	$1,557	$(168)	$5,556	$ 652
Personal accident	1,473	83	(8)	1,548	368
Group products	753	174	(21)	906	63
Individual fixed annuities	128	574	(37)	665	149
Individual variable annuities	92	495	(1)	586	52
Total	$6,613	$2,883	$(235)	$9,261	$1,284
Percentage Increase/(Decrease) from Prior Year:					
Life insurance	8%	(41)%	–%	(12)%	(65)%
Personal accident	15	11	–	13	2
Group products	32	(12)	–	24	41
Individual fixed annuities	1	(1)	–	(12)	(61)
Individual variable annuities	29	–	–	–	–
Total	13%	(50)%	–%	(12)%	(43)%

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

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

	Three Months Ended March 31,	
	2008	2007
Growth in original currency*	**6.8%**	5.2%
Foreign exchange effect	**5.8**	2.9
Growth as reported in U.S. dollars	**12.6%**	8.1%

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

Japan and Other Results

Japan and Other results on a sub-product basis were as follows:

(in millions)	Premiums and Other Considerations	Net Investment Income	Net Realized Capital Gains (Losses)	Total Revenues	Operating Income (Loss)
Three Months Ended March 31, 2008					
Life insurance	**$1,328**	**$ 337**	**$(247)**	**$1,418**	**$ 57**
Personal accident	**1,177**	**52**	**(28)**	**1,201**	**301**
Group products	**750**	**111**	**(7)**	**854**	**71**
Individual fixed annuities	**117**	**536**	**(89)**	**564**	**68**
Individual variable annuities	**117**	**(286)**	**28**	**(141)**	**(14)**
Total	**$3,489**	**$ 750**	**$(343)**	**$3,896**	**$483**
Three Months Ended March 31, 2007					
Life insurance	$1,216	$ 550	$ (18)	$1,748	$352
Personal accident	1,028	50	2	1,080	289
Group products	575	150	5	730	73
Individual fixed annuities	116	546	(35)	627	147
Individual variable annuities	91	494	–	585	52
Total	$3,026	$1,790	$ (46)	$4,770	$913
Percentage Increase/(Decrease) from Prior Year:					
Life insurance	9%	(39)%	–%	(19)%	(84)%
Personal accident	14	4	–	11	4
Group products	30	(26)	–	17	(3)
Individual fixed annuities	1	(2)	–	(10)	(54)
Individual variable annuities	29	–	–	–	–
Total	15%	(58)%	–%	(18)%	(47)%

Total revenues for Japan and Other in the first three months of 2008 decreased compared to the same period in 2007 primarily due to higher net realized capital losses and lower net investment income from partnerships and mutual funds, which more than offset growth in premiums and other considerations and net investment income from fixed maturity securities. Operating income decreased in the first three months of 2008 compared to the same period in 2007 primarily due to the effect of market volatility which resulted in higher net realized capital losses, trading account losses of $88 million in the U.K. associated with certain investment-linked products, and increased incurred policyholder benefits of $80 million related to a closed block of Japan single premium variable life business with guaranteed benefits. A hedging strategy is being implemented for the Japan block of business which is expected to help mitigate the effect of equity market volatility on these liabilities beginning in the second half of 2008. Growth of in force reserves and the positive effect of foreign exchange rates partially offset the losses caused by market volatility.

Life insurance premiums and other considerations increased in the first three months of 2008 compared to the same period in 2007 reflecting growth in new business as further described below. Net investment income declined due to policyholder trading losses of $224 million compared to policyholder trading gains of $95 million in 2007 along with lower partnership income. Life insurance operating income declined in the first three months of 2008 compared to the same period in 2007 due to increased net realized capital losses and increased policyholder benefits related to a closed block of Japan business, which were partially offset by claims expense in the first three months of 2007 of $12 million related to the industry wide regulatory review of claims in Japan.

Personal accident premiums and other considerations reflected growth due to the launch of a new single premium product in Japan and a favorable foreign exchange effect. Net investment income increased modestly in the first three months of 2008 compared to the same period in 2007 primarily due to growth in invested assets. Operating income increased in the first three months of 2008 compared to the same period in 2007 due to growth in in force reserves and lower claim expense of $28 million associated with the claims review in Japan, partially offset by net realized capital losses. Loss ratios for this product continue to be stable.

Group products premiums and other considerations in the first three months of 2008 increased compared to the same period in 2007 primarily due to the growing credit business in Europe and the employee benefits group life and medical business in Europe, Brazil and the Middle East. Net investment income declined in the first three months of 2008 compared to the same period in 2007 primarily due to lower policyholder trading gains. Operating income in the first three months of 2008 declined slightly compared to the same period in 2007 primarily due to net realized capital losses.

Individual fixed annuities premiums and other considerations in the first three months of 2008 were essentially unchanged compared to the same period in 2007 as surrender charges on non-Yen annuity products declined in Japan. Net investment income declined due to policyholder trading losses in Europe compared to gains in the first quarter of 2007, which more than offset the effect of higher assets under management and increased net investment spreads in

Japan. Although fixed annuity reserves were higher in the first three months of 2008 compared to the same period in 2007, operating income declined due to higher net realized capital losses and the lower surrender charge income in Japan.

Individual variable annuities premiums and other considerations increased in the first three months of 2008 compared to the same period in 2007 due to the fees generated from the higher levels of assets under management. Net investment income decreased reflecting the effect of equity market volatility which resulted in policyholder trading losses of $195 million for the first three months of 2008 compared to gains of $494 million for the same period in 2007. Variable annuity reserves at the end of the first quarter of 2008 were higher than at the same period in 2007 due to deposit growth in Japan and the U.K. However, operating income declined in the first three months of 2008 compared to the same period in 2007 due to $88 million of trading account losses in the U.K.

First year premium, single premium and annuity deposits for Japan and Other were as follows:

	Three Months Ended March 31,		Percentage Increase/ (Decrease)	
(in millions)	**2008**	2007	U.S.$	Original Currency
First year premium	**$ 642**	$ 620	4%	(6)%
Single premium	**2,956**	1,997	48%	44%
Annuity deposits	**5,507**	4,071	35%	33%

First year premium sales in the first three months of 2008 grew modestly in U.S. dollar terms, but declined on an original currency basis compared to the same period in 2007. First year premium life insurance sales in Japan continue to reflect the effect of the suspension of the increasing term product in April 2007, but sales in Europe remained robust. Personal accident first year premium sales declined due to lower direct marketing sales in Japan. Sales in Europe were strong, particularly in the credit and group life and medical lines, and in Brazil as pension sales increased.

Single premium interest sensitive life insurance sales remained strong in Japan while guaranteed income bond sales continued to perform well in Europe. A new single premium personal accident and health product was launched in Japan during the first quarter of 2008 with the majority of sales coming through banks which were recently deregulated and are now able to sell accident and health products.

Annuity deposits increased in the first three months of 2008 compared to the same period in 2007 as both fixed and variable products performed well. In Japan, fixed annuity products improved as the Japanese Yen strengthened making non-Yen products more attractive to Japanese consumers. In the U.K., variable annuity deposits continued to reflect strong growth.

Asia Results

Asia results, presented on a sub-product basis were as follows:

(in millions)	Premiums and Other Considerations	Net Investment Income	Net Realized Capital Gains (Losses)	Total Revenues	Operating Income (Loss)
Three Months Ended March 31, 2008					
Life insurance	**$3,184**	**$ 582**	**$(320)**	**$3,446**	**$ 174**
Personal accident	**514**	**40**	**(12)**	**542**	**76**
Group products	**246**	**42**	**(23)**	**265**	**18**
Individual fixed annuities	**12**	**33**	**(24)**	**21**	**(10)**
Individual variable annuities	**2**	**1**	**—**	**3**	**(6)**
Total	**$3,958**	**$ 698**	**$(379)**	**$4,277**	**$ 252**
Three Months Ended March 31, 2007					
Life insurance	$2,951	$1,007	$(150)	$3,808	$ 300
Personal accident	445	33	(10)	468	79
Group products	178	24	(26)	176	(10)
Individual fixed annuities	12	28	(2)	38	2
Individual variable annuities	1	1	(1)	1	—
Total	$3,587	$1,093	$(189)	$4,491	$ 371
Percentage Increase/(Decrease) from Prior Year:					
Life insurance	8%	(42)%	—%	(10)%	(42)%
Personal accident	16	21	—	16	(4)
Group products	38	75	—	51	—
Individual fixed annuities	—	18	—	(45)	—
Individual variable annuities	100	—	—	—	—
Total	10%	(36)%	—%	(5)%	(32)%

Total revenues in Asia in the first three months of 2008 decreased compared to the same period in 2007 primarily due to the negative effect of policyholder trading losses on net investment income and higher net realized capital losses, which more than offset the growth in premiums and other considerations. Premiums and other considerations increased in the first three months of 2008 compared to the same period in 2007, notwithstanding a continued trend toward investment-oriented products where only a portion of policy charges are reported as premiums. Net investment income declined due to policyholder trading losses in 2008 compared to gains in the same period in 2007 and lower partnership and unit investment trust income. Net realized capital losses in the first three months of 2008 included higher other-than-temporary impairment charges partially offset by a positive change in the fair value of derivatives that do not qualify for hedge accounting treatment under FAS 133 compared to the same period last year. Operating income in the first three months of 2008 decreased compared to the same period in 2007 due to higher net realized capital losses and lower net investment income. Operating income in the first three months of 2007 included a $50 million charge related to balance sheet reconciliation remediation activity.

Life insurance premiums and other considerations in the first three months of 2008 increased compared to the same period in 2007, benefiting from improved sales in Singapore, Malaysia and Thailand and the favorable effect of foreign exchange rates, partially offset by a shift in product mix from traditional life insurance products to investment-oriented products. Net investment income decreased in the first three months of 2008 due to $336 million of policyholder trading losses compared to gains of $76 million for the same period in 2007. Operating income decreased in the first three months of 2008 compared to the same period in 2007 primarily due to market volatility, which resulted in higher net realized capital losses and lower net investment income which more than offset the benefit of strong growth in reserves and the favorable effect of foreign exchange. Operating income in the first three months of 2007 included a $50 million charge related to balance sheet reconciliation remediation activity.

Personal accident revenues grew in the first three months of 2008 compared to the same period in 2007 primarily due to higher premiums and other considerations, particularly in Korea, and an increase in net investment income resulting from growth in invested assets. Operating income declined slightly due to higher claims in Taiwan.

Group products premiums and other considerations grew in the first three months of 2008 compared to the same period in 2007 due to new group contracts in Singapore, Korea and Australia. Operating income increased in the first three months of 2008 compared to the same period in 2007 primarily due to improved production results. In addition, operating income in the first three months of 2007 included a $13 million reserve charge.

The operating loss in 2008 for individual variable annuities resulted from start-up costs for new variable annuity products launched in Taiwan during the quarter.

First year premium, single premium and annuity deposits for Asia were as follows:

(in millions)	Three Months Ended March 31, 2008	2007	Percentage Increase/ (Decrease) U.S.$	Original Currency
First year premium	**$718**	$674	7%	4%
Single premium	**957**	648	48%	42%
Annuity deposits	**332**	131	153%	150%

First year premium sales in the first three months of 2008 grew moderately compared to the same period in 2007 as the sales focus shifted more to single premium products. In China and Taiwan, life insurance first year premium sales declined as China sales continued to focus on single premium investment-oriented products, and in Taiwan sales shifted to a newly launched single premium variable annuity product. The group products business performed well in Singapore, Korea and Australia.

Single premium sales in the first three months of 2008 grew significantly compared to the same period in 2007 primarily due to investment-oriented life insurance sales, particularly in Singapore, Hong Kong, China and Malaysia, as well as strong group pension sales in Thailand.

Annuity deposits in the first three months of 2008 more than doubled the level reported for the same period in 2007 due to the launch of the new variable annuity product in Taiwan and higher deposits in Korea as a result of an improved interest rate environment.

Domestic Life Insurance Results

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

(in millions)	Premiums and Other Considerations	Net Investment Income	Net Realized Capital Gains (Losses)	Total Revenues	Operating Income (Loss)
Three Months Ended March 31, 2008					
Life insurance	**$ 589**	**$ 373**	**$(1,055)**	**$ (93)**	**$(839)**
Home service	**188**	**153**	**(140)**	**201**	**(62)**
Group life/health	**204**	**47**	**(14)**	**237**	**2**
Payout annuities *	**594**	**303**	**(22)**	**875**	**38**
Individual fixed and runoff annuities	**12**	**108**	**(57)**	**63**	**(9)**
Total	**$1,587**	**$ 984**	**$(1,288)**	**$1,283**	**$(870)**
Three Months Ended March 31, 2007					
Life insurance	$ 578	$ 372	$ (3)	$ 947	$ 187
Home service	195	161	(2)	354	82
Group life/health	229	53	(1)	281	3
Payout annuities *	512	289	(6)	795	51
Individual fixed and runoff annuities	14	130	—	144	22
Total	$1,528	$1,005	$ (12)	$2,521	$ 345
Percentage Increase/(Decrease) from Prior Year:					
Life insurance	2%	—%	—%	—%	—%
Home service	(4)	(5)	—	(43)	—
Group life/health	(11)	(11)	—	(16)	(33)
Payout annuities	16	5	—	10	(25)
Individual fixed and runoff annuities	(14)	(17)	—	(56)	—
Total	4%	(2)%	—%	(49)%	—%

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

Total Domestic Life Insurance revenues decreased in the first three months of 2008 compared to the same period in 2007 primarily due to significantly higher net realized capital losses, partially offset by slightly higher premiums and other considerations. Domestic Life Insurance premiums and other considerations increased in the first three months of 2008 compared to the same period in 2007 primarily due to strong payout annuity sales and growth in life insurance business in force. Net investment income decreased in the first three months of 2008 compared to the same period in 2007 primarily from lower call and tender income and higher policyholder trading losses which result in a direct offset in incurred policy losses and benefits. Net investment income in the first three months of 2008 benefited from lower losses of $29 million from investments in synthetic fuel production (Synfuel) compared to the same period in 2007. Domestic Life Insurance operating income decreased in the first three months of 2008 compared to the same period in 2007 primarily due to higher net realized capital losses including other-than-temporary impairment charges and derivative losses. The operating results for the first three months of 2008 benefited from increased premiums and other considerations, underwriting gains in certain product lines and $20 million of lower DAC amortization related to net realized capital losses associated with both investment losses and embedded policy derivatives related to the adoption of FAS 157.

Life insurance premiums and other considerations increased in the first three months of 2008 compared to the

same period in 2007 driven by growth in life insurance business in force and increased policyholder charges related to universal life and whole life products. Net investment income in the first three months of 2008 increased slightly compared to the same period in 2007 due to lower Synfuel losses, offset by lower call and tender income and higher policyholder trading losses. The policyholder trading losses result in a direct offset in incurred policy losses and benefits. Life insurance operating results were lower in the first three months of 2008 compared to the same period in 2007 primarily due to higher net realized capital losses which were partially offset by continued growth in the in force business.

Home service premiums and other considerations declined in the first three months of 2008 compared to the same period in 2007 as the reduction of premiums in force from normal lapses and maturities exceeded sales growth. Net investment income in the first three months of 2008 decreased compared to the same period in 2007 due to lower call and tender income which was partially offset by lower Synfuel losses. The home service operating results were also affected by higher net realized capital losses which were partially offset by continued improvement in profit margins on both the in force and new business.

Group life/health premiums and other considerations declined in the first three months of 2008 compared to the same period in 2007 primarily due to continued tightened underwriting in the group employer product lines. Group life/health operating income decreased in the first three months of 2008 compared to the same period in 2007 primarily due to higher net realized capital losses, partially offset by a lower effect of AICPA SOP 05-1, "Accounting by Insurance Enterprises for Deferred Acquisition Costs in Connection with Modifications or Exchanges of Insurance Contracts" (SOP 05-1) compared to the same period in 2007. Group life and health operating results also benefited from underwriting gains across several product lines.

Payout annuities premiums and other considerations increased in the first three months of 2008 compared to the same period in 2007 reflecting strong sales of structured settlements and terminal funding annuities in the U.S. and Canada. Net investment income increased in the first three months of 2008 reflecting growth in insurance reserves, partially offset by a $20 million decrease in call and tender income. Payout annuities operating results in the first three months of 2008 benefited from growth of the in force business and favorable mortality experience which were partially offset by higher net realized capital losses.

Individual fixed and runoff annuities premiums and other considerations along with net investment income decreased in the first three months of 2008 compared to the same period in 2007 reflecting declining insurance reserves. Operating results for the first three months of 2008 are lower compared to the same period in 2007. Higher net realized capital losses were partially offset by lower amortization of DAC of $15 million, primarily related to net realized capital losses associated with both investment losses and embedded policy derivatives related to the adoption of FAS 157.

Domestic Life Insurance periodic premium sales by product were as follows:

(in millions)	Three Months Ended March 31, **2008**	2007	Percentage Increase/ (Decrease)
Periodic Premium Sales By Product*:			
Universal life	**$ 47**	$ 51	(8)%
Variable universal life	**27**	13	108
Term life	**52**	55	(5)
Whole life/other	**3**	2	50
Total	**$129**	$121	7%

** Periodic premium represents premium from new business expected to be collected over a one-year period.*

Domestic Life Insurance periodic premium sales increased in the first three months of 2008 compared to the same period in 2007 primarily as a result of strong private placement variable universal life sales. The U.S. life insurance market remains highly competitive and Domestic Life's emphasis on maintaining new business margins continues to affect production activity, particularly within the term life product category.

Domestic Retirement Services Results

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

(in millions)	Premiums and Other Considerations	Net Investment Income	Net Realized Capital Gains (Losses)	Total Revenues	Operating Income (Loss)
Three Months Ended March 31, 2008					
Group retirement products	**$107**	**$ 494**	**$ (740)**	**$ (139)**	**$ (493)**
Individual fixed annuities	**23**	**759**	**(1,246)**	**(464)**	**(956)**
Individual variable annuities	**152**	**35**	**(252)**	**(65)**	**(137)**
Individual annuities – runoff*	**2**	**83**	**(121)**	**(36)**	**(110)**
Total	**$284**	**$1,371**	**$(2,359)**	**$ (704)**	**$(1,696)**
Three Months Ended March 31, 2007					
Group retirement products	$105	$ 570	$ (10)	$ 665	$ 276
Individual fixed annuities	25	914	(11)	928	303
Individual variable annuities	146	42	10	198	52
Individual annuities – runoff*	8	99	2	109	21
Total	$284	$1,625	$ (9)	$1,900	$ 652
Percentage Increase/(Decrease) from Prior Year:					
Group retirement products	2%	(13)%	–%	–%	–%
Individual fixed annuities	(8)	(17)	–	–	–
Individual variable annuities	4	(17)	–	–	–
Individual annuities – runoff	(75)	(16)	–	–	–
Total	—%	(16)%	–%	–%	–%

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

Total revenues and operating income for Domestic Retirement Services declined in the first three months of 2008 compared to the same period in 2007 primarily due to significantly increased net realized capital losses and lower partnership and yield enhancement income. Net realized capital losses for Domestic Retirement Services increased primarily due to higher other-than-temporary impairment charges of $2.2 billion in the first three months of 2008 compared to $42 million in the same period in 2007.

Both group retirement products and individual fixed annuities operating income in the first three months of 2008 decreased compared to the same period in 2007 primarily as a result of increased net realized capital losses due to higher other-than-temporary impairment charges, and lower net investment income due to lower partnership and yield enhancement income. In addition, increased levels of short-term investments further reduced the overall investment yield. These decreases were partially offset by decreases in DAC amortization and sales inducement costs of $168 million related to the net realized capital losses.

Individual variable annuities operating income decreased in the first three months of 2008 compared to the same period in 2007 primarily as a result of increased net realized capital losses largely due to increased embedded policy derivative liability valuations primarily as a result of the adoption of FAS 157, as well as higher other-than-temporary impairment charges. The increase in net realized capital losses was partially offset by decreases in DAC amortization and sales inducement costs of $77 million related to the net realized capital losses.

The account value rollforward for Domestic Retirement Services by product was as follows:

(in millions)	Three Months Ended March 31, 2008	2007
Group retirement products		
Balance at beginning of year	**$ 68,109**	$ 64,357
Deposits – annuities	**1,453**	1,418
Deposits – mutual funds	**424**	465
Total deposits	**1,877**	1,883
Surrenders and other withdrawals	**(1,490)**	(1,925)
Death benefits	**(59)**	(60)
Net inflows (outflows)	**328**	(102)
Change in fair value of underlying investments, interest credited, net of fees	**(2,797)**	961
Balance at end of period	**$ 65,640**	$ 65,216
Individual fixed annuities		
Balance at beginning of year	**$ 50,508**	$ 52,685
Deposits	**2,531**	1,231
Surrenders and other withdrawals	**(1,579)**	(1,660)
Death benefits	**(382)**	(408)
Net inflows (outflows)	**570**	(837)
Change in fair value of underlying investments, interest credited, net of fees	**462**	491
Balance at end of period	**$ 51,540**	$ 52,339
Individual variable annuities		
Balance at beginning of year	**$ 33,108**	$ 31,093
Deposits	**1,017**	1,008
Surrenders and other withdrawals	**(909)**	(990)
Death benefits	**(127)**	(121)
Net inflows (outflows)	**(19)**	(103)
Change in fair value of underlying investments, interest credited, net of fees	**(2,259)**	442
Balance at end of period	**$ 30,830**	$ 31,432
Total Domestic Retirement Services		
Balance at beginning of year	**$151,725**	$148,135
Deposits	**5,425**	4,122
Surrenders and other withdrawals	**(3,978)**	(4,575)
Death benefits	**(568)**	(589)
Net inflows (outflows)	**879**	(1,042)
Change in fair value of underlying investments, interest credited, net of fees	**(4,594)**	1,894
Balance at end of year, excluding runoff	**148,010**	148,987
Individual annuities runoff	**5,580**	6,135
Balance at end of period	**$153,590**	$155,122
General and separate account reserves and mutual funds		
General account reserve	**$ 90,576**	$ 91,145
Separate account reserve	**54,952**	57,106
Total general and separate account reserves	**145,528**	148,251
Group retirement mutual funds	**8,062**	6,871
Total reserves and mutual funds	**$153,590**	$155,122

Higher deposits in the individual fixed annuity blocks in combination with lower surrenders in all product lines resulted in positive net flows in the first three months of 2008.

Domestic Retirement Services deposits increased in the first three months of 2008 compared to the same period in 2007 primarily reflecting higher deposits in individual fixed annuities. Group retirement and individual variable annuity deposits were essentially unchanged in the first three months of 2008 compared to the same period in 2007. The significant improvement in individual fixed annuity sales was due to continued steepening of the yield curve and mutual fund money market products offering less competitive crediting rates than those currently available on fixed annuities.

Domestic Retirement Services surrenders and other withdrawals decreased in all product lines in the first three months of 2008 compared to the same period in 2007. Group retirement surrenders decreased in the first three months of 2008 compared to the same period in 2007 as a result of a few large group mutual fund surrenders in the first three months of 2007. Individual fixed annuity surrenders decreased in the first three months of 2008 due to decreasing competition from bank deposit and mutual fund money market products.

Domestic Retirement Services reserves by surrender charge category and surrender rates were as follows:

(in millions)	Group Retirement Products*	Individual Fixed Annuities	Individual Variable Annuities
March 31, 2008			
No surrender charge	**$48,890**	**$11,410**	**$12,072**
0% - 2%	**2,520**	**3,359**	**4,627**
Greater than 2% - 4%	**2,901**	**7,490**	**4,156**
Greater than 4%	**2,363**	**25,932**	**9,568**
Non-Surrenderable	**904**	**3,349**	**407**
Total reserves	**$57,578**	**$51,540**	**$30,830**
Surrender rates	**9.1%**	**12.5%**	**11.7%**
March 31, 2007			
No surrender charge	$43,889	$10,513	$11,721
0% - 2%	6,323	4,406	5,022
Greater than 2% - 4%	3,732	6,395	4,960
Greater than 4%	3,523	27,579	9,640
Non-Surrenderable	879	3,446	89
Total reserves	$58,346	$52,339	$31,432
Surrender rates	11.9%	12.7%	12.6%

** Excludes mutual funds of $8.1 billion and $6.9 billion at March 31, 2008 and 2007, respectively.*

Surrender rates decreased for all three product lines in the first three months of 2008 compared to the same period in 2007. The surrender rate for individual fixed annuities continues to be driven by the yield curve and the general aging of the in force block. However, less than 23 percent of the individual fixed annuity reserves as of March 31, 2008 were available for surrender without charge.

An increase in the level of surrenders in any of these businesses or in the individual fixed annuities runoff block could accelerate the amortization of DAC and negatively affect fee income earned on assets under management.

Life Insurance & Retirement Services Net Investment Income and Net Realized Capital Gains (Losses)

The components of net investment income for Life Insurance & Retirement Services were as follows:

(in millions)	Three Months Ended March 31, 2008	2007
Foreign Life Insurance & Retirement Services:		
Fixed maturities, including short-term investments	**$2,125**	$1,899
Equity securities	**51**	(3)
Interest on mortgage and other loans	**132**	113
Partnership income	**2**	48
Unit investment trusts	**(99)**	35
Other[(a)]	**112**	68
Total investment income before policyholder income and trading gains (losses)	**2,323**	2,160
Policyholder investment income and trading gains (losses)[(b)]	**(762)**	797
Total investment income	**1,561**	2,957
Investment expenses	**113**	74
Net investment income	**$1,448**	$2,883
Domestic Life Insurance:		
Fixed maturities, including short-term investments	**$ 864**	$ 911
Equity securities	**17**	(1)
Interest on mortgage and other loans	**97**	100
Partnership income — excluding Synfuels	**31**	27
Partnership loss — Synfuels	**(4)**	(33)
Unit investment trusts	**(2)**	2
Other[(a)]	**21**	14
Total investment income before policyholder income and trading gains (losses)	**1,024**	1,020
Policyholder investment income and trading gains (losses)[(b)]	**(23)**	—
Total investment income	**1,001**	1,020
Investment expenses	**17**	15
Net investment income	**$ 984**	$1,005
Domestic Retirement Services:		
Fixed maturities, including short-term investments	**$1,211**	$1,400
Equity securities	**3**	3
Interest on mortgage and other loans	**148**	121
Partnership income	**11**	130
Other[(a)]	**13**	(12)
Total investment income	**1,386**	1,642
Investment expenses	**15**	17
Net investment income	**$1,371**	$1,625
Total:		
Fixed maturities, including short-term investments	**$4,200**	$4,210
Equity securities	**71**	(1)
Interest on mortgage and other loans	**377**	334
Partnership income — excluding Synfuels	**44**	205
Partnership loss — Synfuels	**(4)**	(33)
Unit investment trusts	**(101)**	37
Other[(a)]	**146**	70
Total investment income before policyholder income and trading gains (losses)	**4,733**	4,822
Policyholder investment income and trading gains (losses)[(b)]	**(785)**	797
Total investment income	**3,948**	5,619
Investment expenses	**145**	106
Net investment income	**$3,803**	$5,513

(a) Includes real estate income, income on non-partnership invested assets, securities lending and Foreign Life Insurance & Retirement Services' equal share of the results of AIG Credit Card Company (Taiwan).

(b) Relates principally to assets held in various trading securities accounts that do not qualify for separate account treatment under AICPA SOP 03-1, "Accounting and Reporting by Insurance Enterprises for Certain Nontraditional Long-Duration Contracts and for Separate Accounts" (SOP 03-1). These amounts are principally offset by an equal change included in incurred policy losses and benefits.

Net investment income decreased $1.7 billion, or 31 percent in the first three months of 2008 compared to the same period in 2007, reflective of the recent market volatility. For the first three months of 2008, policyholder trading losses were $785 million compared to gains of $797 million in the same period of 2007 reflecting equity market declines in Japan and Asia. In addition, lower yield enhancement income from equity investments was negatively affected.

Historically, AIG generated income tax credits as a result of investing in Synfuels related to the partnership income (loss) shown in the table above. Synfuel production ceased effective December 31, 2007.

The components of net realized capital gains (losses) for Life Insurance & Retirement Services were as follows:

(in millions)	Three Months Ended March 31, 2008	2007
Foreign Life Insurance & Retirement Services:		
Sales of fixed maturities	**$ (3)**	$ (20)
Sales of equity securities	**79**	32
Other:		
Other-than-temporary impairments[(a)]	**(1,016)**	(331)
Foreign exchange transactions	**(23)**	115
Derivatives instruments	**115**	(117)
Other[(b)]	**126**	86
Total Foreign Life Insurance & Retirement Services	**$ (722)**	$(235)
Domestic Life Insurance:		
Sales of fixed maturities	**$ 8**	$ 19
Sales of equity securities	**1**	1
Other:		
Other-than-temporary impairments[(a)]	**(1,219)**	(19)
Foreign exchange transactions	**(2)**	2
Derivatives instruments	**(125)**	(11)
Other[(c)]	**49**	(4)
Total Domestic Life Insurance	**$ (1,288)**	$ (12)
Domestic Retirement Services:		
Sales of fixed maturities	**$ (8)**	$ 19
Sales of equity securities	**20**	11
Other:		
Other-than-temporary impairments[(a)]	**(2,157)**	(42)
Foreign exchange transactions	**(15)**	6
Derivatives instruments	**100**	5
Other[(c)]	**(299)**	(8)
Total Domestic Retirement Services	**$ (2,359)**	$ (9)
Total:		
Sales of fixed maturities	**$ (3)**	$ 18
Sales of equity securities	**100**	44
Other:		
Other-than-temporary impairments[(a)]	**(4,392)**	(392)
Foreign exchange transactions	**(40)**	123
Derivatives instruments	**90**	(123)
Other[(b)(c)]	**(124)**	74
Total	**$ (4,369)**	$(256)

(a) See Invested Assets — Other-than-temporary impairments for additional information.

(b) Includes losses of $11 million and $71 million in the first three months of 2008 and 2007, respectively, allocated to participating policyholders.

(c) Includes losses of $12 million and $143 million for Domestic Life Insurance and Domestic Retirement Services, respectively, related to the adoption of FAS 157 related to embedded policy derivatives.

Included in net realized capital gains (losses) are gains (losses) on sales of investments, derivative gains (losses) for transactions that did not qualify for hedge accounting treatment under FAS 133, foreign exchange gains and losses, other-than-temporary impairments and the effects of the adoption of FAS 157 further described below. In the first three months of 2008, Life Insurance & Retirement Services operations recorded $4.4 billion of other-than-temporary impairment charges compared to $392 million in the same period in 2007. The increased other-than-temporary Foreign Life Insurance & Retirement Services losses were primarily driven by severity losses and foreign currency declines. See Invested Assets — Valuation of Invested Assets — Portfolio Review herein for further information. Foreign currency losses of $401 million related primarily to the decline in value of U.S. dollar bonds held in Taiwan, Singapore and Thailand against those respective currencies. Derivatives in the Foreign Life Insurance & Retirement Services operations are primarily used to economically hedge cash flows related to U.S. dollar bonds back to the respective currency of the country, principally in Taiwan, Thailand and Singapore. These derivatives do not qualify for hedge accounting treatment under FAS 133 and are recorded in net realized capital gains (losses). The corresponding foreign exchange gain or loss with respect to the economically hedged bond is deferred in accumulated other comprehensive income (loss) until the bond is sold or deemed to be other-than-temporarily impaired.

In the first three months of 2008, the Domestic Life Insurance and Domestic Retirement Services operations incurred higher net realized capital losses primarily due to other-than-temporary impairment charges related to severity. Derivatives in the Domestic Life Insurance operations include

affiliated interest rate swaps used to economically hedge cash flows on bonds and option contracts used to economically hedge cash flows on indexed annuity and universal life products. These derivatives do not qualify for hedge accounting treatment under FAS 133 and are recorded in net realized capital gains (losses). The corresponding gain or loss with respect to the economically hedged bond is deferred in accumulated other comprehensive income (loss) until the bond is sold, matures or deemed to be other-than-temporarily impaired.

The most significant effect of AIG's adoption of FAS 157 was the change in measurement of fair value for embedded policy derivatives. The pre-tax effect of adoption related to embedded policy derivatives was an increase in net realized capital losses of $155 million as of January 1, 2008. The effect of initial adoption was primarily due to an increase in the embedded policy derivative liability valuations resulting from the inclusion of explicit risk margins.

Deferred Policy Acquisition Costs and Sales Inducement Assets

DAC for Life Insurance & Retirement Services products arises from the deferral of costs that vary with, and are directly related to, the acquisition of new or renewal business. Policy acquisition costs for life insurance products are generally deferred and amortized over the premium paying period in accordance with FAS 60, "Accounting and Reporting by Insurance Enterprises" (FAS 60). Policy acquisition costs that relate to universal life and investment-type products are generally deferred and amortized, with interest in relation to the incidence of estimated gross profits to be realized over the estimated lives of the contracts in accordance with FAS 97. Value of Business Acquired (VOBA) is determined at the time of acquisition and is reported on the consolidated balance sheet with DAC and amortized over the life of the business, similar to DAC. AIG offers sales inducements to contract holders (bonus interest) on certain annuity and investment contracts. Sales inducements are recognized as part of the liability for policyholders' contract deposits on the consolidated balance sheet and are amortized over the life of the contract similar to DAC. Total deferred acquisition and sales inducement costs increased $186 million in the first three months of 2008 compared to the same period in 2007 primarily due to higher production in the Foreign Life Insurance operations partially offset by lower Domestic Life Insurance and Domestic Retirement Services sales. Total amortization expense decreased slightly in the first three months of 2008 compared to the same period in 2007. The amortization in 2008 was reduced by the adoption of FAS 159 and $267 million credited to operating income related to net realized capital losses in the first three months of 2008 compared to $11 million in the same period of 2007 reflecting significantly higher other-than-temporary impairment charges. As a result, annualized amortization expense levels in the first three months of 2008 and 2007 were approximately 11 percent and 13 percent, respectively, of the opening DAC balance.

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

The major components of the changes in DAC/VOBA and SIA were as follows:

(in millions)	Three Months Ended March 31,					
	2008			2007		
	DAC/VOBA	SIA	Total	DAC/VOBA	SIA	Total
Foreign Life Insurance & Retirement Services						
Balance at beginning of year	**$26,175**	**$ 681**	**$26,856**	$21,153	$ 404	$21,557
Acquisition costs deferred	**1,344**	**33**	**1,377**	1,227	22	1,249
Amortization (charged) or credited to operating income:						
Related to net realized capital gains (losses)	**15**	**(2)**	**13**	19	1	20
Related to unlocking future assumptions	**(4)**	**(2)**	**(6)**	11	—	11
All other amortization	**(909)**	**(24)**	**(933)**	(650)	(7)	(657)
Change in unrealized gains (losses) on securities	**(86)**	**(1)**	**(87)**	(10)	(2)	(12)
Increase (decrease) due to foreign exchange	**980**	**—**	**980**	(185)	—	(185)
Other*	**(1,145)**	**(299)**	**(1,444)**	(60)	—	(60)
Balance at end of period	**$26,370**	**$ 386**	**$26,756**	$21,505	$ 418	$21,923
Domestic Life Insurance						
Balance at beginning of year	**$ 6,432**	**$ 53**	**$ 6,485**	$ 6,006	$ 46	$ 6,052
Acquisition costs deferred	**219**	**5**	**224**	234	4	238
Amortization (charged) or credited to operating income:						
Related to net realized capital gains (losses)	**20**	**—**	**20**	—	—	—
Related to unlocking future assumptions	**—**	**—**	**—**	1	—	1
All other amortization	**(153)**	**(1)**	**(154)**	(177)	(2)	(179)
Change in unrealized gains (losses) on securities	**94**	**—**	**94**	21	—	21
Increase (decrease) due to foreign exchange	**(23)**	**—**	**(23)**	5	—	5
Other*	**—**	**—**	**—**	(64)	—	(64)
Balance at end of period	**$ 6,589**	**$ 57**	**$ 6,646**	$ 6,026	$ 48	$ 6,074
Domestic Retirement Services						
Balance at beginning of year	**$ 5,838**	**$ 991**	**$ 6,829**	$ 5,651	$ 887	$ 6,538
Acquisition costs deferred	**239**	**53**	**292**	169	51	220
Amortization (charged) or credited to operating income:						
Related to net realized capital gains (losses)	**190**	**44**	**234**	(8)	(1)	(9)
Related to unlocking future assumptions	**—**	**—**	**—**	2	—	2
All other amortization	**(190)**	**(44)**	**(234)**	(221)	(39)	(260)
Change in unrealized gains (losses) on securities	**69**	**29**	**98**	(74)	(22)	(96)
Increase (decrease) due to foreign exchange	**1**	**—**	**1**	—	—	—
Balance at end of period	**$ 6,147**	**$1,073**	**$ 7,220**	$ 5,519	$ 876	$ 6,395
Total Life Insurance & Retirement Services						
Balance at beginning of year	**$38,445**	**$1,725**	**$40,170**	$32,810	$1,337	$34,147
Acquisition costs deferred	**1,802**	**91**	**1,893**	1,630	77	1,707
Amortization (charged) or credited to operating income:						
Related to net realized capital gains (losses)	**225**	**42**	**267**	11	—	11
Related to unlocking future assumptions	**(4)**	**(2)**	**(6)**	14	—	14
All other amortization	**(1,252)**	**(69)**	**(1,321)**	(1,048)	(48)	(1,096)
Change in unrealized gains (losses) on securities	**77**	**28**	**105**	(63)	(24)	(87)
Increase (decrease) due to foreign exchange	**958**	**—**	**958**	(180)	—	(180)
Other*	**(1,145)**	**(299)**	**(1,444)**	(124)	—	(124)
Balance at end of period	**$39,106**	**$1,516**	**$40,622**	$33,050	$1,342	$34,392

** In 2008, primarily represents the cumulative effect of adoption of FAS 159. In 2007, primarily represents the cumulative effect of adoption of SOP 05-1.*

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

DAC, VOBA and SIA for insurance-oriented, investment-oriented and retirement services products are reviewed for recoverability, which involves estimating the

future profitability of current business. This review involves significant management judgment. If actual future profitability is substantially lower than estimated, AIG's DAC, VOBA and SIA may be subject to an impairment charge and AIG's results of operations could be significantly affected in future periods.

Future Policy Benefit Reserves

Periodically, the net benefit reserves (policy benefit reserves less DAC) established for Life Insurance & Retirement Services companies are tested to ensure that, including consideration of future expected premium payments, they are adequate to provide for future policyholder benefit obligations. The assumptions used to perform the tests are current best-estimate assumptions as to policyholder mortality, morbidity, terminations, company maintenance expenses and invested asset returns. For long duration traditional business, a "lock-in" principle applies, whereby the assumptions used to calculate the benefit reserves and DAC are set when a policy is issued and do not change with changes in actual experience. These assumptions include margins for adverse deviation in the event that actual experience might deviate from these assumptions. For business in force outside of North America, 46 percent of total policyholder benefit liabilities at March 31, 2008 represent traditional business where the lock-in principle applies. In most foreign locations, various guarantees are embedded in policies in force that may remain applicable for many decades into the future.

As experience changes over time, the best-estimate assumptions are updated to reflect observed changes. Because of the long-term nature of many of AIG's liabilities subject to the lock-in principle, small changes in certain of the assumptions may cause large changes in the degree of reserve adequacy. In particular, changes in estimates of future invested asset return assumptions have a large effect on the degree of reserve adequacy.

Taiwan

Beginning in 2000, the yield available on Taiwanese 10-year government bonds dropped from approximately 6 percent to 2.4 percent at March 31, 2008. Yields on most other invested assets have correspondingly dropped over the same period. Current sales are focused on products such as:

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

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

- Observed historical mortality improvement trends have been projected to 2014;
- Morbidity, expense and termination rates have been updated to reflect recent experience;
- Taiwan government bond rates are expected to remain at current levels for 10 years and gradually increase to best-estimate assumptions of a market consensus view of long-term interest rate expectations;
- Foreign assets are assumed to comprise 35 percent of invested assets, resulting in a composite long-term investment assumption of approximately 4.8 percent; and
- The currently permitted practice of offsetting positive mortality experience with negative interest margins, thus eliminating the need for mortality dividends, will continue.

Future results of the reserve adequacy tests will involve significant management judgment as to mortality, morbidity, expense and termination rates and investment yields. Adverse changes in these assumptions could accelerate DAC amortization and necessitate reserve strengthening.

Financial Services Operations

AIG's Financial Services subsidiaries engage in diversified activities including aircraft and equipment leasing, capital markets, consumer finance and insurance premium finance.

Financial Services Results

Financial Services results were as follows:

(in millions)	Three Months Ended March 31, 2008	Three Months Ended March 31, 2007	Percentage Increase/ (Decrease)
Total revenues:			
Aircraft Leasing	**$ 1,165**	$ 1,058	10%
Capital Markets[(a)]	**(8,743)**	228	—
Consumer Finance[(b)]	**931**	845	10
Other, including intercompany adjustments	**87**	70	24
Total	**$ (6,560)**	$ 2,201	—%
Operating income (loss):			
Aircraft Leasing	**$ 221**	$ 164	35%
Capital Markets[(a)]	**(8,927)**	68	—
Consumer Finance[(b)]	**(52)**	36	—
Other, including intercompany adjustments	**(14)**	24	—
Total	**$ (8,772)**	$ 292	—%

(a) Revenues, shown net of interest expense of $511 million and $1.1 billion in the three-month periods ended March 31, 2008 and 2007, respectively, were primarily from hedged financial positions entered into in connection with counterparty transactions. In the three-month period ended March 31, 2008, both revenues and operating income (loss) include an unrealized market valuation loss of $9.1 billion on AIGFP's super senior credit default swap portfolio.

(b) For the three-month period ended March 31, 2007, includes a pre-tax charge of $128 million in connection with domestic consumer finance's mortgage banking activities.

Financial Services reported an operating loss in the first three months of 2008 compared to operating income in the same period of 2007 primarily due to an unrealized market valuation loss of $9.1 billion on AIGFP's super senior credit default swap portfolio and a decline in operating income for AGF. AGF's operating income declined in the first three months of 2008 compared to the same period in 2007 primarily due to increases in the provision for finance receivable losses and unfavorable variances related to derivatives.

ILFC generated strong operating income growth in the first three months of 2008 compared to the same period in 2007, driven to a large extent by a larger aircraft fleet, higher lease rates and higher utilization.

Aircraft Leasing

Aircraft Leasing operations represent the operations of ILFC, which generates its revenues primarily from leasing new and used commercial jet aircraft to foreign and domestic airlines. Revenues also result from the remarketing of commercial aircraft for ILFC's own account, and remarketing and fleet management services for airlines and financial institutions. ILFC finances its aircraft purchases primarily through the issuance of debt instruments. ILFC economically hedges part of its floating rate and substantially all of its foreign currency denominated debt using interest rate and foreign currency derivatives. Starting in the second quarter of 2007, ILFC began applying hedge accounting to most of its derivatives. The composite borrowing rates at March 31, 2008 and 2007 were 4.79 percent and 5.19 percent, respectively.

ILFC typically contracts to re-lease aircraft before the end of the existing lease term. For aircraft returned before the end of the lease term, ILFC has generally been able to re-lease such aircraft within two to six months of their return. As a lessor, ILFC considers an aircraft "idle" or "off lease" when the aircraft is not subject to a signed lease agreement or signed letter of intent. Subsequent to March 31, 2008, thirteen planes were returned to ILFC by bankrupt lessees. ILFC expects to re-lease these planes to other lessees and may incur related costs. As of April 30, 2008, ILFC had leased 10 of the thirteen aircraft.

Aircraft Leasing Results

ILFC's operating income increased in the first three months of 2008 compared to the same period in 2007. Rental revenues increased by $121 million or 11 percent, driven by a larger aircraft fleet and higher lease rates. As of March 31, 2008, 921 aircraft in ILFC's fleet were subject to operating leases compared to 856 aircraft as of March 31, 2007. ILFC had one aircraft off lease at March 31, 2008 and 2007, and all new aircraft scheduled for delivery through 2008 have been leased. Flight equipment marketing revenues increased by $8 million in the first three months of 2008 compared to the same period in 2007 due to an increase in aircraft sales. The increase in revenues was partially offset by an increase in depreciation and a credit value adjustment on derivatives as a result of the adoption of FAS 157. Depreciation expense increased by $44 million, or 11 percent, in line with the increase in the size of the aircraft fleet. In the first three months of 2008 and 2007, the losses from hedging activities that did not qualify for hedge accounting treatment under

FAS 133, including the related foreign exchange gains and losses, were $48 million and $37 million, respectively, in both revenues and operating income. The net derivative loss for the three-month period ended March 31, 2008 includes the effect of changes in AIG's credit spreads of $39 million, of which $12 million represents the transition amount from the adoption of FAS 157.

Capital Markets

Capital Markets represents the operations of AIGFP, which engages as principal in a wide variety of financial transactions, including standard and customized financial products involving commodities, credit, currencies, energy, equities and rates. The credit products include credit protection written through credit default swaps on super senior risk tranches of diversified pools of loans and debt securities. AIGFP also invests in a diversified portfolio of securities and principal investments and engages in borrowing activities involving the issuance of standard and structured notes and other securities, and entering into GIAs.

As Capital Markets is a transaction-oriented operation, current and past revenues and operating results may not provide a basis for predicting future performance. AIG's Capital Markets operations derive a significant portion of their revenues from hedged financial positions entered into in connection with counterparty transactions. AIGFP also participates as a dealer in a wide variety of financial derivatives transactions. Revenues and operating income of the Capital Markets operations and the percentage change in these amounts for any given period are significantly affected by changes in the fair value of AIGFP's assets and liabilities and by the number, size and profitability of transactions entered into during that period relative to those entered into during the prior period. Generally, the realization of transaction revenues as measured by the receipt of funds is not a significant reporting event as the gain or loss on AIGFP's trading transactions is currently reflected in operating income as the fair values change from period to period.

AIGFP's products generally require sophisticated models and significant management assumptions to determine fair values and, particularly during times of market disruption, the absence of observable market data can result in fair values at any given balance sheet date that are not indicative of the ultimate settlement values of the products.

Capital Markets Results

Capital Markets reported an operating loss in the first three months of 2008 compared to operating income in the same period of 2007, primarily due to unrealized market valuation losses related to AIGFP's super senior credit default swap portfolio principally written on multi-sector CDOs. These losses were partially offset by net unrealized market gains related to certain credit default swaps purchased against the AAA to BBB-rated risk layers on portfolios of reference obligations. Financial market conditions in the first three months of 2008 were characterized by widening credit spreads and declining interest rates.

In addition to writing credit protection on the super senior risk layer on designated portfolios of loans or debt securities, AIGFP also wrote protection on tranches below the super senior risk layer. At March 31, 2008, the net notional amount of the credit default swaps in the regulatory capital relief portfolio written on tranches below the super senior risk layer was $5.7 billion, with an estimated fair value loss of $174 million.

At March 31, 2008 the notional amounts and unrealized market valuation loss of the super senior credit default swap portfolio, including certain regulatory capital relief driven trades, by asset class were as follows:

		Unrealized Market Valuation Loss	
	Notional Amount *(in billions)*	Three Months Ended March 31, 2008 *(in millions)*	Cumulative At March 31, 2008 *(in millions)*
Corporate loans[(a)]	$192	$ –	$ –
Prime residential mortgages[(a)]	143	–	–
Corporate debt/CLOs	57	896	1,123
Multi-sector CDOs[(b)]	77	8,037	19,281
Mezzanine tranches[(c)]	6	174	174
Total	$475	$9,107	$20,578

(a) Predominantly represent transactions written to facilitate regulatory capital relief.

(b) Approximately $60.6 billion in notional amount of the multi-sector CDO pools include some exposure to U.S. sub-prime mortgages.

(c) Represents credit default swaps written by AIGFP on tranches below super senior on certain regulatory capital relief trades.

AIGFP purchased protection at the AAA- to BBB-rated risk layers on portfolios of reference obligations that include multi-sector CDO obligations. During the first three months of 2008, unrealized market valuation gains of $130 million on the related credit default swaps and embedded credit derivatives in credit-linked notes were fully offset by the fair value adjustment on the underlying assets.

The change in fair value of AIGFP's credit default swaps was caused by the significant widening in spreads in the first quarter of 2008 driven by the credit concerns resulting from U.S. residential mortgages, the severe liquidity crisis affecting the markets and the effects of rating agency downgrades on structured securities. Based upon its most current analyses, AIG believes that any credit impairment losses which may emerge over time at AIGFP will not be material to AIG's consolidated financial condition, but could be material to the manner in which AIG manages its liquidity.

The net loss recognized for the first three months of 2007 included a $166 million reduction in fair value of

certain derivatives that are an integral part of, and economically hedge, the structured transactions potentially affected by the proposed guidance by the U.S. Treasury Department affecting the ability to claim foreign tax credits.

The most significant component of Capital Markets operating expenses is compensation, which was approximately $143 million and $123 million in the first three months of 2008 and 2007, respectively. The amount of compensation was not affected by gains and losses arising from derivatives not qualifying for hedge accounting treatment under FAS 133. In the first quarter of 2008, AIGFP established an employee retention plan, which guarantees a broad group of AIGFP's employees and consultants a minimum level of compensation for each of the 2008 and 2009 compensation years, subject to mandatory partial deferral which, in certain circumstances, will be indexed to the price of AIG stock. The deferred amounts may be reduced in the event of losses prior to payment. The expense related to the plan is being recognized over the vesting period, beginning in the first quarter of 2008.

Effective January 1, 2008, AIGFP adopted FAS 157. The most significant effect of adopting FAS 157 was a change in the valuation methodologies for hybrid financial instruments and derivative liabilities (both freestanding and embedded) historically carried at fair value. The changes were primarily to incorporate AIGFP's own credit risk, when appropriate, in the fair value measurements.

Effective January 1, 2008, AIGFP also elected to apply the fair value option to all eligible assets and liabilities, other than equity method investments and trade receivables and trade payables. Electing the fair value option allows AIGFP to more closely align its earnings with the economics of its transactions by recognizing the change in fair value of its derivatives and the offsetting change in fair value of the assets and liabilities being hedged concurrently through earnings.

Capital Markets net operating loss for the first three months of 2008 includes an increase to pre-tax earnings of $2,648 million attributable to changes in AIG's credit spreads which were substantially offset by the effect of changes in counterparty credit spreads on assets measured at fair value of $2,620 million. Included in the first quarter 2008 net operating loss is the transition amount of $291 million related to the adoption of FAS 157 and FAS 159, as well as a credit valuation adjustment gain of $217 million for derivatives AIGFP entered into with other AIG entities, which is eliminated in consolidation.

The following table presents AIGFP's credit spread gains (losses) for the three-month period ended March 31, 2008 (excluding intercompany transactions):

(in millions)

Counterparty Credit Spread Sensitivity on Assets		AIG Inc.'s Own Credit Spread Sensitivity on Liabilities	
Available for sale bonds	$(2,148)	Term notes	$ 261
Loans and other assets	(24)	Hybrid term notes	662
Derivative assets	(448)	GIC's	1,156
		Other liabilities	30
		Derivative liabilities*	539
Decrease in assets	$(2,620)	Decrease in liabilities	$2,648
Net pre-tax increase to other income	$ 28		

**Includes super senior CDS portfolio*

AIGFP recognized a loss of $166 million in the first three months of 2007 on hybrid financial instruments for which it applied the fair value option under FAS 155, "Accounting for Certain Hybrid Financial Instruments — an amendment of FASB Statements No. 133 and 140" (FAS 155). These amounts were largely offset by gains and losses on economic hedge positions also reflected in AIGFP's operating income or loss.

Consumer Finance

AIG's Consumer Finance operations in North America are principally conducted through AGF. AGF derives a substantial portion of its revenues from finance charges assessed on outstanding real estate loans, secured and unsecured non-real estate loans and retail sales finance receivables and credit-related insurance.

Effective February 29, 2008, AGF purchased a portion of Equity One, Inc.'s consumer finance receivable portfolio consisting of $1.0 billion of real estate loans, $290 million of non-real estate loans, and $156 million of retail sales finance receivables.

AIG's foreign consumer finance operations are principally conducted through AIG Consumer Finance Group, Inc. (AIGCFG). AIGCFG operates primarily in emerging and developing markets. AIGCFG has operations in Argentina, China, Hong Kong, Mexico, Philippines, Poland, Taiwan, Thailand and India. In April 2008, AIGCFG decided to sell or liquidate its existing operations in Taiwan.

Certain of the AIGCFG operations are partly or wholly owned by life insurance subsidiaries of AIG. Accordingly, the financial results of those companies are allocated between Financial Services and Life Insurance & Retirement Services according to their ownership percentages. While products vary by market, the businesses generally provide credit cards, unsecured and secured non-real estate loans, term deposits, savings accounts, retail sales finance and real estate loans. AIGCFG originates finance receivables through its branches

and direct solicitation. AIGCFG also originates finance receivables indirectly through relationships with retailers, auto dealers, and independent agents.

Consumer Finance Results

Consumer Finance operating income decreased in the first three months of 2008 compared to the same period in 2007. Operating income from the domestic consumer finance operations, which include the operations of AGF and AIG Federal Savings Bank, decreased by $75 million in the first three months of 2008 compared to the same period in 2007. In the first three months of 2007, domestic results were adversely affected by the weakening housing market and tighter underwriting guidelines, which resulted in lower originations of real estate loans as well as the $128 million charge relating to the estimated cost of implementing the Supervisory Agreement entered into with the OTS.

AGF's revenues increased $23 million or 3 percent during the first three months of 2008 compared to the same period in 2007. Revenues from AGF's finance receivables benefited from the $1.5 billion finance receivable purchase in first quarter 2008, but were partially offset by reduced residential mortgage originations reflecting the slower U.S. housing market. Revenues from AGF's mortgage banking activities increased $111 million during the first three months of 2008 compared to the same period in 2007 (which included the first quarter 2007 charge of $128 million related to the Supervisory Agreement). The first three months of 2007 included a recovery of $65 million from a favorable out of court settlement.

AGF's operating income declined in the first three months of 2008 compared to the same period in 2007 primarily due to increases in the provision for finance receivable losses and unfavorable variances related to derivatives. During the first three months of 2008, AGF recorded a net loss of $43 million on its derivatives that did not qualify for hedge accounting under FAS 133, including the related foreign exchange losses, compared to a net loss of $36 million in the same period in 2007. The net derivative loss for the three-month period ended March 31, 2008 includes the effect of changes in AIG's credit spreads amounting to $39 million, of which $13 million represents the transition amount from the adoption of FAS 157. Commencing in the second quarter of 2007, AGF began applying hedge accounting.

AGF's net finance receivables totaled $26.7 billion at March 31, 2008, an increase of approximately $2.2 billion compared to the prior year period, including the purchase of $1.5 billion of finance receivables from Equity One, Inc. on February 29, 2008. The increase in the net finance receivables resulted in a similar increase in revenues generated from these assets.

Revenues from the foreign consumer finance operations increased by 40 percent in the first three months of 2008 compared to the same period in 2007. Loan growth, particularly in Poland, Mexico and Latin America, was the primary driver of the increased revenues. In addition, revenues from recently acquired businesses in India and Thailand contributed to the increase. The increase in revenues was more than offset by higher expenses associated with branch expansions, acquisition activities and product promotion campaigns.

Credit Quality of Finance Receivables

The overall credit quality of AGF's finance receivables portfolio deteriorated due to negative economic fundamentals, a higher proportion of non-real estate loans and retail sales finance receivables and the aging of the real estate loan portfolio.

At March 31, 2008, the 60-day delinquency rate for the entire portfolio increased by 106 basis points to 3.11 percent compared to the same period in 2007, while the 60-day delinquency rate for the real estate loans increased by 116 basis points to 2.99 percent. For the three months ended March 31, 2008, AGF's net charge-off rate increased to 1.53 percent compared to 0.97 percent for the same period in 2007.

AGF's allowance for finance receivable losses as a percentage of outstanding receivables was 2.55 percent at March 31, 2008 compared to 1.99 percent at March 31, 2007.

Asset Management Operations

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

The revenues and operating income (loss) for this segment are affected by the general conditions in the equity and credit markets. In addition, net realized gains and performance fees are contingent upon various fund closings, maturity levels and market conditions.

Spread-Based Investment Business

AIG's Spread-Based Investment business includes the results of AIG's proprietary Spread-Based Investment operations, the Matched Investment Program (MIP), which was launched in September of 2005 to replace the Guaranteed Investment Contract (GIC) program, which is in runoff. The MIP is an investment strategy that involves investing in various asset classes with financing provided through third parties. This business uses various risk mitigating strategies designed to hedge interest rate and currency risk associated with underlying investments and related liabilities.

Institutional Asset Management

AIG's Institutional Asset Management business, conducted through AIG Investments, provides an array of investment products and services globally to institutional investors, pension funds, AIG subsidiaries and high net worth investors. These products include traditional equity and fixed income investments, and a wide range of alternative asset classes. These services include investment advisory and subadvisory services, investment monitoring and investment transaction structuring. Within the fixed income and equity asset classes, AIG Investments offers various forms of structured investments aimed at achieving superior returns or capital preservation. Within the alternative asset class, AIG Investments offers hedge and private equity fund-of-funds, direct investments and distressed debt investments.

AIG Global Real Estate provides a wide range of real estate investment and management services for AIG subsidiaries, as well as for third-party institutional investors, high net worth investors and pension funds. Through a strategic network of local real estate ventures, AIG Global Real Estate actively invests in and develops office, industrial, multi-family residential, retail, hotel and resort properties globally.

AIG Private Bank offers banking, trading and investment management services to private clients and institutions globally.

From time to time, AIG Investments acquires alternative investments, primarily consisting of direct controlling equity interests in private enterprises, with the intention of "warehousing" such investments until the investment or economic benefit thereof is transferred to a fund or other AIG-managed investment product. During the warehousing period, AIG bears the cost and risks associated with carrying these investments and consolidates them on its balance sheet and records the operating results until the investments are transferred, sold or otherwise divested. Changes in market conditions may negatively affect the fair value of these warehoused investments. Market conditions may impede AIG from launching new investment products for which these warehoused assets are being held, which could result in AIG not recovering its investment upon transfer or divestment. In the event that AIG is unable to transfer or otherwise divest its interest in the warehoused investment to third parties, AIG could be required to hold these investments indefinitely. In certain instances, the consolidated warehoused investments are not wholly owned by AIG. In such cases, AIG shares the risk associated with warehousing the asset with the minority interest investors.

Brokerage Services and Mutual Funds

AIG's Brokerage Services and Mutual Funds business, conducted through AIG Advisor Group, Inc. and AIG SunAmerica Asset Management Corp., provides broker-dealer related services and mutual funds to retail investors, group trusts and corporate accounts through an independent network of financial advisors. AIG Advisor Group, Inc., a subsidiary of AIG Retirement Services, Inc., is comprised of several broker-dealer entities that provide these services to clients primarily in the U.S. marketplace. AIG SunAmerica Asset Management Corp. manages, advises and/or administers retail mutual funds, as well as the underlying assets of variable annuities sold by AIG SunAmerica and VALIC to individuals and groups throughout the United States.

Other Asset Management

Included in Other Asset Management is income or loss from certain AIG SunAmerica sponsored partnerships and partnership investments. Partnership assets consist of investments in a diversified portfolio of private equity funds, affordable housing partnerships and hedge fund investments.

Asset Management Results

Asset Management results were as follows:

(in millions)	Three Months Ended March 31, **2008**	2007	Percentage Increase/ (Decrease)
Total revenues:			
Spread-Based Investment business	**$ (809)**	$ 1,015	—%
Institutional Asset Management*	**524**	429	22
Brokerage Services and Mutual Funds	**74**	78	(5)
Other Asset Management	**62**	147	(58)
Total	**$ (149)**	$ 1,669	—%
Operating income (loss):			
Spread-Based Investment business	**$ (1,251)**	$ 491	—%
Institutional Asset Management*	**(78)**	97	—
Brokerage Services and Mutual Funds	**19**	26	(27)
Other Asset Management	**59**	144	(59)
Total	**$ (1,251)**	$ 758	—%

** Includes the effect of consolidating the revenues and operating losses of warehoused investments totaling $233 million and $92 million, respectively, in the first three months of 2008 and $30 million and $12 million, respectively, in the first three months of 2007, a portion of which is offset in minority interest expense.*

Asset Management recognized an operating loss in the first three months of 2008 compared to operating income in the same period in 2007 primarily due to other-than-temporary impairment charges on fixed income investments, significantly lower partnership income, increased foreign exchange, interest rate and credit-related net mark to market losses, lower carried interest revenues and the effect of consolidating several warehoused investments. AIG consolidates the operating results of warehoused investments until such time as they are sold or otherwise divested. The other-than-temporary impairment charges were due primarily to changes in market liquidity and spreads.

Spread-Based Investment Business Results

The Spread-Based Investment business reported an operating loss in the first three months of 2008 compared to operating income in the same period in 2007 due to significantly higher net realized capital losses and lower partnership income. Included in the operating loss were net realized capital losses of $1.3 billion for the first three months of 2008, compared to $20 million in the 2007 period. Net realized capital losses for the first three months of 2008 primarily consist of $1.0 billion in other-than-temporary impairment charges on fixed income securities for both the GIC and MIP, $366 million in foreign exchange related losses on foreign denominated GIC reserves and mark to market losses of $131 million on credit default swap investments held by the MIP. Partially offsetting these losses were net mark to market gains of $160 million on interest rate and foreign exchange hedges not qualifying for hedge accounting treatment for both the GIC and MIP. Net realized capital losses of $20 million for the first three months of 2007 primarily reflect $29 million of other-than-temporary impairment charges, $69 million of foreign exchange related losses on foreign denominated GIC reserves, partially offset by realized gains of $54 million on the sale of fixed income and equity securities and $23 million in net mark to market gains on interest rate and foreign exchange hedges.

The other-than-temporary impairment charges on fixed income investments held in the GIC and MIP portfolios were $539 million for the GIC and $494 million for the MIP for the first three months of 2008 and resulted from widening credit spreads and decreased market liquidity. See Invested Assets — Portfolio Review — Other-than-temporary impairments. In addition to the other-than-temporary impairments, unrealized losses on fixed maturity investments were recorded in accumulated other comprehensive income (loss) and were driven by widening credit spreads and decreased market liquidity, partially offset by gains resulting from falling interest rates.

In the GIC program, income from partnership investments was $45 million for the first three months of 2008, a decline of $417 million from the same period of 2007 due to significantly higher performance in the first three months of 2007. Also contributing to the decline was the one-time distribution from a single partnership of $164 million in the first three months of 2007. Foreign exchange losses on foreign-denominated GIC reserves increased by $297 million in the first three months of 2008 as a result of the continued weakening of the U.S. dollar. As noted below, a significant portion of these GIC reserves will mature in 2008. Partially offsetting the decline in partnership income and increased foreign exchange losses was an increase in mark to market gains on derivative positions of $479 million. These gains included mark to market gains on interest rate and foreign exchange derivatives used to economically hedge the effect of interest rate and foreign exchange rate movements on GIC reserves. Although these economic hedges are partially effective in hedging the interest rate and foreign exchange risk, they did not qualify for hedge accounting treatment.

The MIP experienced mark to market losses of $324 million due primarily to interest rate and foreign exchange derivative positions that, while partially effective in hedging interest rate and foreign exchange risk, did not qualify for hedge accounting treatment and an additional $131 million in mark to market losses were recognized due to credit default swap investments. The MIP credit default swaps are comprised predominantly of single-name high-grade corporate exposures. The mark to market losses for the first three months of 2008 were driven primarily by a decline in short-term interest rates, the decline in value of the U.S. dollar and widening credit spreads. AIG enters into hedging arrangements to mitigate the effect of changes in currency and interest rates associated with the fixed and floating rate and foreign currency denominated obligations issued under these programs. Some of these hedging relationships qualify for hedge accounting treatment, while others do not. Income or loss from these hedges not qualifying for hedge accounting treatment are classified as net realized capital gains (losses) in AIG's Consolidated Statement of Income (Loss).

AIG did not issue any additional debt to fund the MIP in the first three months of 2008. Through March 31, 2008, the MIP had cumulative debt issuances of $13.4 billion.

The anticipated runoff of the domestic GIC portfolio at March 31, 2008 was as follows:

(in billions)	Less Than One Year	1-3 Years	3+-5 Years	Over Five Years	Total
Domestic GICs	$10.2	$4.8	$2.9	$5.7	$23.6

Institutional Asset Management Results

Institutional Asset Management recognized an operating loss in the first three months of 2008 compared to operating income in the same period in 2007 reflecting lower carried interest revenues and increased depreciation and amortization expense due to additional real estate investments acquired in late 2007. AIG recognizes carried

interest revenues on an unrealized basis by reflecting the amount owed to AIG as of the balance sheet date based on the related funds' performance. Also contributing to this decrease were the operating losses of certain consolidated warehoused private equity investments. The reduction in these revenues is due to significantly higher fund performance in the first three months of 2007. The consolidated warehoused private equity investments are not wholly owned by AIG and thus, a significant portion of the effect of consolidating these operating losses is offset in minority interest, which is not a component of operating income. Slightly offsetting these decreases were higher base management fees driven by an increase of approximately $15 billion in unaffiliated client assets under management.

AIG's unaffiliated client assets under management, including retail mutual funds and institutional accounts, were $91.4 billion at March 31, 2008, a decline of 3 percent compared to December 31, 2007 and an increase of 19 percent compared to $76.5 billion at March 31, 2007. The decline from December 31, 2007 primarily reflected market valuation declines in the equity and fixed income markets. The increase from March 31, 2007 was driven by new business.

Other Asset Management Results

Revenues and operating income related to the Other Asset Management activities decreased in the first three months of 2008 compared to the same period in 2007 due to lower income from partnership investments. Similar to the investments held in the Spread-Based Investment business, these investments experienced significantly higher performance in the first three months of 2007.

Other Operations

The operating loss of AIG's Other category was as follows:

	Three Months Ended March 31,	
(in millions)	**2008**	2007
Operating income (loss):		
Equity earnings in partially owned companies	**$ 8**	$ 41
Interest expense	**(368)**	(252)
Unallocated corporate expenses*	**(93)**	(172)
Net realized capital gains (losses)	**(265)**	(49)
Other miscellaneous, net	**(50)**	(38)
Total Other	**$(768)**	$(470)

** Includes expenses of corporate staff not attributable to specific operating segments, expenses related to efforts to improve internal controls, corporate initiatives and certain compensation plan expenses.*

The operating loss of AIG's Other category increased in the first three months of 2008 compared to the same period in 2007 reflecting higher interest expense that resulted from increased borrowings, and higher net realized capital losses, partially offset by lower unallocated corporate expenses. The increase in net realized capital losses reflected higher foreign exchange losses on foreign-denominated debt, a portion of which was economically hedged but did not qualify for hedge accounting treatment under FAS 133, and losses on non-hedged derivatives in the first three months of 2008. Other miscellaneous, net included a $45 million write-off of goodwill related to Mortgage Guaranty in the first three months of 2008.

Capital Resources and Liquidity

At March 31, 2008, AIG had total consolidated shareholders' equity of $79.7 billion and total consolidated borrowings of $172.2 billion. At that date, $68.3 billion of such borrowings were subsidiary borrowings not guaranteed by AIG.

A total of 34,093,783 shares were purchased during the first three months of 2008. Subsequent to March 31, 2008, an additional 3,832,276 shares were repurchased, satisfying the balance of the commitments existing at December 31, 2007 that had not been satisfied at March 31, 2008. AIG does not expect to purchase additional shares under its share repurchase program for the foreseeable future.

Borrowings

AIG's total borrowings were as follows:

(in millions)	**March 31, 2008**	December 31, 2007
Borrowings issued by AIG:		
Notes and bonds payable	**$ 14,800**	$ 14,588
Junior subordinated debt	**5,898**	5,809
Loans and mortgages payable	**584**	729
MIP matched notes and bonds payable	**15,080**	14,267
Series AIGFP matched notes and bonds payable	**1,071**	874
Total AIG borrowings	**37,433**	36,267
Borrowings guaranteed by AIG:		
AIGFP[(a)]		
GIAs	**20,142**	19,908
Notes and bonds payable	**31,485**	36,676
Loans and mortgages payable	**1,429**	1,384
Hybrid financial instrument liabilities[(b)]	**6,198**	7,479
Total AIGFP borrowings	**59,254**	65,447
AIG Funding, Inc. commercial paper	**5,008**	4,222
AIGLH notes and bonds payable	**797**	797
Liabilities connected to trust preferred stock	**1,424**	1,435
Total borrowings issued or guaranteed by AIG	**103,916**	108,168
Borrowings not guaranteed by AIG:		
ILFC		
Commercial paper	**4,392**	4,483
Junior subordinated debt	**999**	999
Notes and bonds payable[(c)]	**26,645**	25,737
Total ILFC borrowings	**32,036**	31,219
AGF		
Commercial paper and extendible commercial notes	**3,418**	3,801
Junior subordinated debt	**349**	349
Notes and bonds payable	**21,905**	22,369
Total AGF borrowings	**25,672**	26,519
AIGCFG		
Commercial paper	**223**	287
Loans and mortgages payable	**1,991**	1,839
Total AIGCFG borrowings	**2,214**	2,126
Other subsidiaries	**783**	775
Borrowings of consolidated investments:		
A.I. Credit[(d)]	**220**	321
AIG Investments	**1,636**	1,636
AIG Global Real Estate Investment	**5,534**	5,096
AIG SunAmerica	**156**	186
ALICO	**3**	3
Total borrowings of consolidated investments	**7,549**	7,242
Total borrowings not guaranteed by AIG	**68,254**	67,881
Consolidated:		
Total commercial paper and extendible commercial notes	**$ 13,261**	$ 13,114
Total long-term borrowings	**158,909**	162,935
Total borrowings	**$172,170**	$176,049

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

(b) Represents structured notes issued by AIGFP that are accounted for using the fair value option at 2008 and 2007.

(c) Includes borrowings under Export Credit Facility of $2.5 billion at March 31, 2008 and December 31, 2007.

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

AIG's net borrowings were as follows:

(in millions)	**March 31, 2008**	December 31, 2007
AIG's total borrowings	**$172,170**	$176,049
Less:		
Junior subordinated debt	**5,898**	5,809
Liabilities connected to trust preferred stock	**1,424**	1,435
MIP matched notes and bonds payable	**15,080**	14,267
Series AIGFP matched notes and bonds payable	**1,071**	874
AIGFP[(a)]		
GIAs	**20,142**	19,908
Notes and bonds payable	**31,485**	36,676
Loans and mortgages payable	**1,429**	1,384
Hybrid financial instrument liabilities[(b)]	**6,198**	7,479
Borrowings not guaranteed by AIG	**68,254**	67,881
AIG's net borrowings	**$ 21,189**	$ 20,336

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

(b) Represents structured notes issued by AIGFP that are accounted for using the fair value option at 2008 and 2007.

The roll forward of long-term borrowings, excluding borrowings of consolidated investments, for the three months ended March 31, 2008 was as follows:

(in millions)

	Balance at December 31, 2007	Issuances	Maturities and Repayments	Effect of Foreign Exchange	Other Changes[(b)]	**Balance at March 31, 2008**
AIG						
Notes and bonds payable	$ 14,588	$ —	$ —	$ 73	$ 139	**$ 14,800**
Junior subordinated debt	5,809	—	—	89	—	**5,898**
Loans and mortgages payable	729	4	(131)	(2)	(16)	**584**
MIP matched notes and bonds payable	14,267	—	—	17	796	**15,080**
Series AIGFP matched notes and bonds payable	874	214	(28)	—	11	**1,071**
AIGFP[(a)]						
GIAs	19,908	1,299	(2,014)	—	949	**20,142**
Notes and bonds payable and hybrid financial instrument liabilities	44,155	7,755	(15,302)	—	1,075	**37,683**
Loans and mortgages payable	1,384	—	(66)	—	111	**1,429**
AIGLH notes and bonds payable	797	—	—	—	—	**797**
Liabilities connected to trust preferred stock	1,435	—	(10)	—	(1)	**1,424**
ILFC notes and bonds payable	25,737	1,448	(839)	299	—	**26,645**
ILFC junior subordinated debt	999	—	—	—	—	**999**
AGF notes and bonds payable	22,369	293	(965)	153	55	**21,905**
AGF junior subordinated debt	349	—	—	—	—	**349**
AIGCFG loans and mortgages payable	1,839	855	(800)	97	—	**1,991**
Other subsidiaries	775	11	(17)	12	2	**783**
Total	$156,014	$11,879	$(20,172)	$ 738	$ 3,121	**$ 151,580**

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

(b) Includes the cumulative effect of the adoption of FAS 159.

AIG (Parent Company)

AIG intends to continue its customary practice of issuing debt securities from time to time to meet its financing needs and those of certain of its subsidiaries for general corporate purposes, as well as for the MIP. As of March 31, 2008, AIG had up to $17.3 billion of debt securities, preferred stock and other securities, and up to $16.5 billion of common stock, registered and available for issuance under its universal shelf registration statement.

AIG maintains a medium-term note program under its shelf registration statement. As of March 31, 2008, approximately $7.6 billion principal amount of senior notes were outstanding under the medium-term note program, of which $3.2 billion was used for AIG's general corporate purposes, $1.1 billion was used by AIGFP (referred to as "Series AIGFP" in the preceding tables) and $3.3 billion was used to fund the MIP. The maturity dates of these notes range from 2008 to 2052. To the extent considered appropriate, AIG may enter into swap transactions to manage its effective borrowing rates with respect to these notes.

AIG also maintains a Euro medium-term note program under which an aggregate nominal amount of up to $20.0 billion of senior notes may be outstanding at any one

time. As of March 31, 2008, the equivalent of $13.5 billion of notes were outstanding under the program, of which $10.4 billion were used to fund the MIP and the remainder was used for AIG's general corporate purposes. The aggregate amount outstanding includes $1.9 billion loss resulting from foreign exchange translation into U.S. dollars, of which $472 million loss relates to notes issued by AIG for general corporate purposes and $1.4 billion loss relates to notes issued to fund the MIP. AIG has economically hedged the currency exposure arising from its foreign currency denominated notes.

AIG maintains a shelf registration statement in Japan, providing for the issuance of up to Japanese Yen 300 billion principal amount of senior notes, of which the equivalent of $506 million was outstanding as of March 31, 2008 and was used for AIG's general corporate purposes. AIG also maintains an Australian dollar debt program under which senior notes with an aggregate principal amount of up to 5 billion Australian dollars may be outstanding at any one time. Although as of March 31, 2008 there were no outstanding notes under the Australian program, AIG intends to use the program opportunistically to fund the MIP or for AIG's general corporate purposes.

In October 2007, AIG borrowed a total of $500 million on an unsecured basis pursuant to a loan agreement with a third-party bank. The entire amount of the loan remained outstanding at March 31, 2008 and matures in October 2008.

AIGFP

AIGFP uses the proceeds from the issuance of notes and bonds and GIA borrowings, as well as the issuance of Series AIGFP notes by AIG, to invest in a diversified portfolio of securities and derivative transactions. The borrowings may also be temporarily invested in securities purchased under agreements to resell. AIGFP's notes and bonds include structured debt instruments whose payment terms are linked to one or more financial or other indices (such as an equity index or commodity index or another measure that is not considered to be clearly and closely related to the debt instrument). These notes contain embedded derivatives that otherwise would be required to be accounted for separately under FAS 133. Upon AIG's adoption of FAS 155 in 2006, AIGFP elected the fair value option for these notes. The notes that are accounted for using the fair value option are reported separately under hybrid financial instrument liabilities. AIG guarantees the obligations of AIGFP under AIGFP's notes and bonds and GIA borrowings. See Liquidity herein.

AIGFP has a Euro medium-term note program under which an aggregate nominal amount of up to $20.0 billion of notes may be outstanding at any one time. As of March 31, 2008, $5.1 billion of notes were outstanding under the program. The notes issued under this program are guaranteed by AIG and are included in AIGFP's notes and bonds payable in the table of total borrowings.

AIG Funding

AIG Funding, Inc. (AIG Funding) issues commercial paper that is guaranteed by AIG in order to help fulfill the short-term cash requirements of AIG and its subsidiaries. The level of issuances of AIG Funding's commercial paper, including the guarantee by AIG, is subject to the approval of AIG's Board of Directors or the Finance Committee of the Board if it exceeds certain pre-approved limits.

As backup for the commercial paper program and for other general corporate purposes, AIG and AIG Funding maintain revolving credit facilities, which, as of March 31, 2008, had an aggregate of $9.5 billion available to be drawn and which are summarized below under Revolving Credit Facilities.

ILFC

ILFC fulfills its short-term cash requirements through operating cash flows and the issuance of commercial paper. The issuance of commercial paper is subject to the approval of ILFC's Board of Directors and is not guaranteed by AIG. ILFC maintains syndicated revolving credit facilities which, as of March 31, 2008, totaled $6.5 billion and which are summarized below under Revolving Credit Facilities. These facilities are used as back up for ILFC's maturing debt and other obligations.

As a well-known seasoned issuer, ILFC has filed an automatic shelf registration statement with the Securities and Exchange Commission (SEC) allowing ILFC immediate access to the U.S. public debt markets. At March 31, 2008, $6.0 billion of debt securities had been issued under this registration statement and $6.0 billion had been issued under a prior registration statement. In addition, ILFC has a Euro medium-term note program for $7.0 billion, under which $3.8 billion in notes were outstanding at March 31, 2008. Notes issued under the Euro medium-term note program are included in ILFC notes and bonds payable in the preceding table of borrowings. The cumulative foreign exchange adjustment loss for the foreign currency denominated debt was $1.3 billion at March 31, 2008 and $969 million at December 31, 2007. ILFC has substantially eliminated the currency exposure arising from foreign currency denominated notes by economically hedging the note exposure.

ILFC had a $4.3 billion Export Credit Facility for use in connection with the purchase of approximately 75 aircraft delivered through 2001. This facility was guaranteed by various European Export Credit Agencies. The interest rate varies from 5.75 percent to 5.90 percent on these amortizing ten-year borrowings depending on the delivery date of the aircraft. At March 31, 2008, ILFC had $603 million

outstanding under this facility. The debt is collateralized by a pledge of the shares of a subsidiary of ILFC, which holds title to the aircraft financed under the facility.

In May 2004, ILFC entered into a similarly structured Export Credit Facility for up to a maximum of $2.6 billion for Airbus aircraft to be delivered through May 31, 2005. The facility was subsequently increased to $3.6 billion and extended to include aircraft to be delivered through May 31, 2008. The facility becomes available as the various European Export Credit Agencies provide their guarantees for aircraft based on a six-month forward-looking calendar, and the interest rate is determined through a bid process. At March 31, 2008, ILFC had $1.9 billion outstanding under this facility. The debt is collateralized by a pledge of shares of a subsidiary of ILFC, which holds title to the aircraft financed under the facility. Borrowings with respect to these facilities are included in ILFC's notes and bonds payable in the preceding table of borrowings.

From time to time, ILFC enters into funded financing agreements. As of March 31, 2008, ILFC had a total of $1.1 billion outstanding, which has varying maturities through February 2012. The interest rates are LIBOR-based, with spreads ranging from 0.30 percent to 1.625 percent.

The proceeds of ILFC's debt financing are primarily used to purchase flight equipment, including progress payments during the construction phase. The primary sources for the repayment of this debt and the interest expense thereon are the cash flow from operations, proceeds from the sale of flight equipment and the rollover and refinancing of the prior debt. AIG does not guarantee the debt obligations of ILFC. See also Liquidity herein.

AGF

AGF fulfills most of its short-term cash borrowing requirements through the issuance of commercial paper. The issuance of commercial paper is subject to the approval of AGF's Board of Directors and is not guaranteed by AIG. AGF maintains committed syndicated revolving credit facilities which, as of March 31, 2008, totaled $4.8 billion and which are summarized below under Revolving Credit Facilities. The facilities can be used for general corporate purposes and to provide backup for AGF's commercial paper programs.

As of March 31, 2008, notes and bonds aggregating $21.9 billion were outstanding with maturity dates ranging from 2008 to 2031 at interest rates ranging from 1.94 percent to 8.45 percent. To the extent considered appropriate, AGF may enter into swap transactions to manage its effective borrowing rates with respect to these notes and bonds. As a well-known seasoned issuer, AGF filed an automatic shelf registration statement with the SEC allowing AGF immediate access to the U.S. public debt markets. At March 31, 2008, AGF had remaining corporate authorization to issue up to $8.0 billion of debt securities under its shelf registration statement.

AGF's funding sources include an SEC-registered medium-term note program, private placement debt, retail note issuances, bank financing and securitizations of finance receivables that AGF accounts for as on-balance-sheet secured financings. In addition, AGF has become a recognized issuer of long-term debt in the international capital markets and has recently established a Euro medium-term note program.

In addition to debt refinancing activities, proceeds from the collection of finance receivables are used to fund cash needs including the payment of principal and interest on AGF's debt. AIG does not guarantee any of the debt obligations of AGF. See also Liquidity herein.

AIGCFG

AIGCFG has a variety of funding mechanisms for its various markets, including retail and wholesale deposits, short- and long-term bank loans, securitizations and intercompany subordinated debt. AIG Credit Card Company (Taiwan), a consumer finance business in Taiwan, and AIG Retail Bank PLC, a full service consumer bank in Thailand, have issued commercial paper for the funding of their respective operations. AIG does not guarantee any borrowings for AIGCFG businesses, including this commercial paper.

Revolving Credit Facilities

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

As of March 31, 2008 (in millions)

Facility	Size	Borrower(s)	Available Amount	Expiration	One-Year Term-Out Option
AIG:					
364-Day Syndicated Facility	$ 2,125	AIG/AIG Funding[(a)] AIG Capital Corporation[(a)]	$2,125	July 2008	Yes
5-Year Syndicated Facility	1,625	AIG/AIG Funding[(a)] AIG Capital Corporation[(a)]	1,625	July 2011	No
364-Day Bilateral Facility[(b)]	3,200	AIG/AIG Funding	378	December 2008	Yes
364-Day Intercompany Facility[(c)]	5,335	AIG	5,335	September 2008	Yes
Total AIG	$12,285		$9,463		
ILFC:					
5-Year Syndicated Facility	$ 2,500	ILFC	$2,500	October 2011	No
5-Year Syndicated Facility	2,000	ILFC	2,000	October 2010	No
5-Year Syndicated Facility	2,000	ILFC	2,000	October 2009	No
Total ILFC	$ 6,500		$6,500		
AGF:					
364-Day Syndicated Facility	$ 2,625	American General Finance Corporation American General Finance, Inc.[(d)]	$2,625	July 2008	Yes
5-Year Syndicated Facility	2,125	American General Finance Corporation	2,125	July 2010	No
Total AGF	$ 4,750		$4,750		

(a) Guaranteed by AIG.
(b) This facility can be drawn in the form of loans or letters of credit. All drawn amounts shown above are in the form of letters of credit.
(c) Subsidiaries of AIG are the lenders on this facility.
(d) American General Finance, Inc. is an eligible borrower for up to $400 million only.

Credit Ratings

The cost and availability of unsecured financing for AIG and its subsidiaries are generally dependent on their short- and long-term debt ratings. The following table presents the credit ratings of AIG and certain of its subsidiaries as of April 30, 2008. In parentheses, following the initial occurrence in the table of each rating, is an indication of that rating's relative rank within the agency's rating categories. That ranking refers only to the generic or major rating category and not to the modifiers appended to the rating by the rating agencies to denote relative position within such generic or major category.

	Short-term Debt			Senior Long-term Debt		
	Moody's	S&P	Fitch	Moody's[(a)]	S&P[(b)]	Fitch[(c)]
AIG	P-1 (1st of 3)	A-1+ (1st of 6)	F1+ (1st of 5)	Aa2[(e)] (2nd of 9)	AA (2nd of 8)[(f)]	AA (2nd of 9)[(h)]
AIG Financial Products Corp.[(d)]	P-1	A-1+	–	Aa2[(e)]	AA[(f)]	–
AIG Funding, Inc.[(d)]	P-1	A-1+	F1+	–	–	–
ILFC	P-1	A-1+	F1 (1st of 5)	A1 (3rd of 9)	AA- (2nd of 8)[(g)]	A+ (3rd of 9)[(h)]
American General Finance Corporation	P-1	A-1 (1st of 6)	F1	A1	A+ (3rd of 8)	A+[(h)]
American General Finance, Inc.	P-1	A-1	F1	–	–	A+[(h)]

(a) Moody's appends numerical modifiers 1, 2 and 3 to the generic rating categories to show relative position within rating categories.
(b) S&P ratings may be modified by the addition of a plus or minus sign to show relative standing within the major rating categories.
(c) Fitch Ratings (Fitch) ratings may be modified by the addition of a plus or minus sign to show relative standing within the major rating categories.
(d) AIG guarantees all obligations of AIG Financial Products Corp. and AIG Funding, Inc.
(e) Negative rating outlook on Senior Unsecured Debt Ratings. A negative outlook by Moody's indicates that a rating may be lowered but is not necessarily a precursor of a ratings change.
(f) Negative rating outlook on Counterparty Credit Ratings. A negative outlook by S&P indicates that a rating may be lowered but is not necessarily a precursor of a ratings change.
(g) Negative rating outlook on Corporate Credit Rating. A negative outlook by S&P indicates that a rating may be lowered but is not necessarily a precursor of a ratings change.
(h) Issuer Default and Senior Unsecured Debt Ratings on Rating Watch Negative. Rating Watch Negative indicates that a rating has been placed on active rating watch status.

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

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

AIG believes that any of its own or its subsidiaries' contractual obligations that are subject to "ratings triggers" or financial covenants relating to "ratings triggers" would not have a material adverse effect on its financial condition or liquidity. Ratings downgrades could also trigger the application of termination provisions in certain of AIG's contracts, principally agreements entered into by AIGFP and assumed reinsurance contracts entered into by Transatlantic.

It is estimated that, as of the close of business on April 30, 2008, based on AIGFP's outstanding municipal GIAs and financial derivatives transactions at that date, a downgrade of AIG's long-term senior debt ratings to 'Aa3' by Moody's or 'AA–' by S&P would permit counterparties to call for approximately $1.8 billion of collateral, while a downgrade to 'A1' by Moody's or A+ by S&P would permit counterparties to call for approximately $9.8 billion of additional collateral. Further downgrades could result in requirements for substantial additional collateral, which could have a material effect on how AIGFP manages its liquidity. The actual amount of additional collateral that AIGFP would be required to post to counterparties in the event of such downgrades depends on market conditions, the fair value of the outstanding affected transactions and other factors prevailing at the time of the downgrade. Additional obligations to post collateral would increase the demands on AIGFP's liquidity.

Contractual Obligations

Contractual obligations in total, and by remaining maturity at March 31, 2008 were as follows:

		Payments due by Period			
(in millions)	Total Payments	Less Than One Year	1-3 Years	3+-5 Years	Over Five Years
Borrowings[(a)]	$ 151,580	$ 41,629	$ 34,248	$ 25,133	$ 50,570
Interest payments on borrowings	56,344	5,463	9,436	7,725	33,720
Loss reserves[(b)]	86,860	23,886	26,492	12,595	23,887
Insurance and investment contract liabilities[(c)]	689,494	32,232	43,761	41,932	571,569
GIC liabilities[(d)]	27,285	10,437	5,374	3,600	7,874
Aircraft purchase commitments	18,794	2,779	3,901	2,112	10,002
Other long-term obligations	144	53	80	11	—
Total[(e)(f)]	$1,030,501	$116,479	$123,292	$ 93,108	$697,622

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

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

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

(d) Represents guaranteed maturities under GICs.

(e) Does not reflect unrecognized tax benefits of $2.5 billion, the timing of which is uncertain.

(f) The majority of AIG's credit default swaps require AIG to provide credit protection on a designated portfolio of loans or debt securities. AIG provides such credit protection on a "second loss" basis, under which AIG's payment obligations arise only after credit losses in the designated portfolio exceed a specified threshold amount or level of "first losses." Through May 7, 2008, AIG has made no payments under these contracts and because of the high degree of uncertainty regarding the amount and the long-term timing of any potential future cash flows under these contracts, AIG is unable to make reasonable estimates of any cash settlements at this time.

Off Balance Sheet Arrangements and Commercial Commitments

Off balance sheet arrangements and commercial commitments in total, and by remaining maturity at March 31, 2008 were as follows:

		Amount of Commitment Expiration			
(in millions)	Total Amounts Committed	Less Than One Year	1-3 Years	3+-5 Years	Over Five Years
Guarantees:					
Liquidity facilities[(a)]	$ 2,540	$ 8	$ 8	$2,204	$ 320
Standby letters of credit	1,708	1,483	44	34	147
Construction guarantees[(b)]	681	—	—	—	681
Guarantees of indebtedness	1,243	147	144	500	452
All other guarantees	662	97	25	41	499
Commitments:					
Investment commitments[(c)]	8,452	2,956	3,796	1,490	210
Commitments to extend credit	777	135	502	124	16
Letters of credit	1,174	895	—	119	160
Investment protection agreements[(d)]	7,870	2,463	1,413	677	3,317
Maturity shortening puts[(e)]	2,602	1,186	1,114	238	64
Other commercial commitments[(f)]	1,183	92	57	79	955
Total[(f)]	$28,892	$9,462	$7,103	$5,506	$6,821

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

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

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

(d) Written generally with respect to investments in hedge funds and funds of hedge funds.

(e) Represents obligations under 2a-7 Puts to purchase certain multi-sector CDOs at pre-determined contractual prices.

(f) Includes options to acquire aircraft. Excludes commitments with respect to pension plans. The annual pension contribution for 2008 is expected to be approximately $118 million for U.S. and non-U.S. plans.

Arrangements with Variable Interest Entities and Structured Investment Vehicles

As of March 31, 2008 there have been no significant changes in arrangements with variable interest entities or structured investment vehicles from those reported in the 2007 Annual Report on Form 10-K.

Shareholders' Equity

The changes in AIG's consolidated shareholders' equity were as follows:

(in millions)	Three Months Ended March 31, 2008
Beginning of year	$ 95,801
Net loss	(7,805)
Unrealized depreciation of investments, net of tax	(6,824)
Cumulative translation adjustment, net of tax	1,095
Dividends to shareholders	(488)
Payments advanced to purchase shares, net	733
Share purchases	(1,733)
Cumulative effect of accounting changes, net of tax	(1,108)
Other*	32
End of period	$ 79,703

** Reflects the effects of employee stock transactions.*

AIG has in the past reinvested most of its unrestricted earnings in its operations and believes such continued reinvestment in the future will be adequate to meet any foreseeable capital needs. However, AIG may choose from time to time to raise additional funds through the issuance of additional securities.

In February 2007, AIG's Board of Directors adopted a new dividend policy, which took effect with the dividend declared in the second quarter of 2007, providing that under ordinary circumstances, AIG's plan will be to increase its common stock dividend by approximately 20 percent annually. The payment of any dividend, however, is at the discretion of AIG's Board of Directors, and the future payment of dividends will depend on various factors, including the performance of AIG's businesses, AIG's consolidated financial condition, results of operations and liquidity and the existence of investment opportunities. With due consideration of the foregoing policy, in light of current market conditions, on May 7, 2008, AIG's Board of Directors declared a quarterly cash dividend on the common stock of $0.22 per share, payable on September 19, 2008 to shareholders of record on September 5, 2008, representing a 10 percent increase.

Share Repurchases

From time to time, AIG may buy shares of its common stock for general corporate purposes, including to satisfy its obligations under various employee benefit plans. In February 2007, AIG's Board of Directors increased AIG's share repurchase program by authorizing the purchase of shares with an aggregate purchase price of $8 billion. In November 2007, AIG's Board of Directors authorized the purchase of an additional $8 billion in common stock. In 2007, AIG entered into structured share repurchase arrangements providing for the purchase of shares over time with an aggregate purchase price of $7 billion.

A total of 34,093,783 shares were purchased during the first three months of 2008 to meet commitments that existed at December 31, 2007. The portion of the payments advanced by AIG under the structured share purchase arrangements that had not yet been utilized to purchase shares at March 31, 2008, amounting to $179 million, has been recorded as a component of shareholders' equity under the caption, Payments advanced to purchase shares. Subsequent to March 31, 2008, an additional 3,832,276 shares were purchased, satisfying the balance of the commitments existing at December 31, 2007 that had not been satisfied at March 31, 2008. All shares purchased are recorded as treasury stock at cost.

At May 7, 2008, $9 billion was available for purchases under the aggregate authorization. AIG does not expect to purchase additional shares under its share repurchase program for the foreseeable future.

Share-based Employee Compensation Plans

During the first quarter of 2008, AIG reviewed the vesting schedules of its share-based employee compensation plans, and on March 11, 2008, AIG's management and the Compensation Committee of AIG's Board of Directors determined that, to fulfill the objective of attracting and retaining high quality personnel, the vesting schedules of certain awards outstanding under these plans and all awards made in the future under these plans should be shortened. As a result, the unamortized share-based employee compensation cost related to the affected awards will be amortized over shorter periods. AIG estimates the modifications will accelerate the amortization of this cost by $116 million and $90 million in 2008 and 2009, respectively, with a corresponding reduction in amortization expense related to these awards of $206 million in 2010 through 2013.

Liquidity

AIG manages liquidity at both the subsidiary and parent company levels. At March 31, 2008, AIG's consolidated invested assets included $63.6 billion in cash and short-term investments. Consolidated net cash provided from operating activities in the first three months of 2008 amounted to $8.3 billion. At both the subsidiary and parent company level, liquidity management activities are intended to preserve and enhance funding stability, flexibility, and diversity through a wide range of potential operating environments and market conditions. AIG's primary sources of cash flow are dividends and other payments from its regulated and unregulated subsidiaries, as well as issuances of debt securities. Primary uses of cash flow are for debt service, subsidiary funding, shareholder dividend payments and common stock repurchases. Management believes that AIG's liquid assets, cash provided by operations and access to the capital markets will enable it to meet its anticipated cash requirements, including the funding of increased dividends under AIG's current dividend policy.

AIG (Parent Company)

The liquidity of the parent company is principally derived from its subsidiaries. The primary sources of cash flow are dividends and other payments from its regulated and unregulated subsidiaries, as well as issuance of debt securities. Primary uses of cash flow are for debt service, subsidiary funding, shareholder dividend payments and common stock repurchases. In the first three months of 2008, AIG parent collected $769 million in dividends and other payments from subsidiaries (primarily from insurance company subsidiaries). Excluding MIP and Series AIGFP debt, AIG parent made interest payments totaling $194 million, made $536 million in capital contributions to subsidiaries, and paid $512 million in dividends to shareholders in the first three months of 2008.

AIG parent funds its short-term working capital needs through commercial paper issued by AIG Funding. As of March 31, 2008, AIG Funding had $5.0 billion of commercial paper outstanding with an average maturity of 21 days. As additional liquidity, AIG parent and AIG Funding maintain committed revolving credit facilities that, as of March 31, 2008, had an aggregate of $9.5 billion available to be drawn, and which are summarized above under Revolving Credit Facilities.

Invested Assets

The following tables summarize the composition of AIG's invested assets by segment:

(in millions)	General Insurance	Life Insurance & Retirement Services	Financial Services	Asset Management	Other	Total
March 31, 2008						
Fixed maturities:						
Bonds available for sale, at fair value	$ 73,110	$296,442	$ 1,386	$24,549	$ —	$395,487
Bonds held to maturity, at amortized cost	21,344	1	—	221	—	21,566
Bond trading securities, at fair value	—	9,340	—	35	—	9,375
Equity securities:						
Common stocks available for sale, at fair value	4,669	10,896	—	483	74	16,122
Common and preferred stocks trading, at fair value	301	21,341	—	29	—	21,671
Preferred stocks available for sale, at fair value	1,952	491	8	—	—	2,451
Mortgage and other loans receivable, net of allowance	16	25,870	1,110	7,332	45	34,373
Financial Services assets:						
Flight equipment primarily under operating leases, net of accumulated depreciation	—	—	42,832	—	—	42,832
Securities available for sale, at fair value	—	—	1,096	—	—	1,096
Trading securities, at fair value	—	—	35,998	—	—	35,998
Spot commodities, at fair value	—	—	728	—	—	728
Unrealized gain on swaps, options and forward transactions, at fair value	—	—	21,376	—	(778)	20,598
Trade receivables	—	—	8,896	—	—	8,896
Securities purchased under agreements to resell, at fair value	—	—	19,708	—	—	19,708
Finance receivables, net of allowance	—	5	32,596	—	—	32,601
Securities lending invested collateral, at fair value	5,381	50,201	146	8,533	—	64,261
Other invested assets	12,196	19,599	3,843	18,028	7,525	61,191
Short-term investments	8,552	30,902	5,878	5,435	1,531	52,298
Total Investments and Financial Services assets as shown on the balance sheet	127,521	465,088	175,601	64,645	8,397	841,252
Cash	478	1,062	378	293	278	2,489
Investment income due and accrued	1,337	5,036	27	298	(2)	6,696
Real estate, net of accumulated depreciation	348	1,013	20	94	226	1,701
Total invested assets*	$129,684	$472,199	$176,026	$65,330	$8,899	$852,138

** At March 31, 2008, approximately 64 percent and 36 percent of invested assets were held in domestic and foreign investments, respectively.*

(in millions)	General Insurance	Life Insurance & Retirement Services	Financial Services	Asset Management	Other	Total
December 31, 2007						
Fixed maturities:						
Bonds available for sale, at fair value	$ 74,057	$294,162	$ 1,400	$27,753	$ –	$397,372
Bonds held to maturity, at amortized cost	21,355	1	–	225	–	21,581
Bond trading securities, at fair value	–	9,948	–	34	–	9,982
Equity securities:						
Common stocks available for sale, at fair value	5,599	11,616	–	609	76	17,900
Common and preferred stocks trading, at fair value	321	21,026	–	29	–	21,376
Preferred stocks available for sale, at fair value	1,885	477	8	–	–	2,370
Mortgage and other loans receivable, net of allowance	13	24,851	1,365	7,442	56	33,727
Financial Services assets:						
Flight equipment primarily under operating leases, net of accumulated depreciation	–	–	41,984	–	–	41,984
Securities available for sale, at fair value	–	–	40,305	–	–	40,305
Trading securities, at fair value	–	–	4,197	–	–	4,197
Spot commodities	–	–	238	–	–	238
Unrealized gain on swaps, options and forward transactions, at fair value	–	–	17,134	–	(692)	16,442
Trade receivables	–	–	6,467	–	–	6,467
Securities purchased under agreements to resell, at contract value	–	–	20,950	–	–	20,950
Finance receivables, net of allowance	–	5	31,229	–	–	31,234
Securities lending invested collateral, at fair value	5,031	57,471	148	13,012	–	75,662
Other invested assets	11,895	19,015	3,663	17,261	6,989	58,823
Short-term investments	7,356	25,236	12,249	4,919	1,591	51,351
Total Investments and Financial Services assets as shown on the balance sheet	127,512	463,808	181,337	71,284	8,020	851,961
Cash	497	1,000	389	269	129	2,284
Investment income due and accrued	1,431	4,728	29	401	(2)	6,587
Real estate, net of accumulated depreciation	349	976	17	89	231	1,662
Total invested assets*	$129,789	$470,512	$181,772	$72,043	$8,378	$862,494

** At December 31, 2007, approximately 65 percent and 35 percent of invested assets were held in domestic and foreign investments, respectively.*

Investment Strategy

AIG's investment strategies are tailored to the specific business needs of each operating unit. The investment objectives are driven by the business model for each of the businesses: General Insurance, Life Insurance, Retirement Services and Asset Management's Spread-Based Investment business. The primary objectives are in terms of preservation of capital, growth of surplus and generation of investment income to support the insurance products. At the local operating unit level, the strategies are based on considerations that include the local market, liability duration and cash flow characteristics, rating agency and regulatory capital considerations, legal investment limitations, tax optimization and diversification. In addition to local risk management considerations, AIG's corporate risk management guidelines impose limitations on concentrations to promote diversification by industry, asset class and geographic sector.

The amortized cost or cost and fair value of AIG's available for sale and held to maturity securities were as follows:

	March 31, 2008				December 31, 2007			
(in millions)	Amortized Cost or Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value	Amortized Cost or Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Bonds – available for sale:[(a)]								
U.S. government and government sponsored entities	**$ 4,388**	**$ 266**	**$ 29**	**$ 4,625**	$ 7,956	$ 333	$ 37	$ 8,252
Obligations of states, municipalities and political subdivisions	**44,953**	**757**	**753**	**44,957**	46,087	927	160	46,854
Non-U.S. governments	**71,730**	**4,899**	**697**	**75,932**	67,023	3,920	743	70,200
Corporate debt	**224,101**	**5,977**	**5,994**	**224,084**	239,822	6,216	4,518	241,520
Mortgage-backed, asset-backed and collateralized	**116,900**	**826**	**15,329**	**102,397**	140,982	1,221	7,703	134,500
Total bonds	**$462,072**	**$ 12,725**	**$ 22,802**	**$451,995**	$501,870	$12,617	$13,161	$501,326
Equity securities	**14,996**	**4,202**	**625**	**18,573**	15,188	5,545	463	20,270
Total	**$477,068**	**$ 16,927**	**$ 23,427**	**$470,568**	$517,058	$18,162	$13,624	$521,596
Held to maturity:[(b)]	**$ 21,566**	**$ 428**	**$ 155**	**$ 21,839**	$ 21,581	$ 609	$ 33	$ 22,157

(a) At December 31, 2007, included AIGFP available for sale securities with a fair value of $39.3 billion, for which AIGFP elected the fair value option effective January 1, 2008, consisting primarily of corporate debt, mortgage-backed, asset-backed and collateralized securities. At March 31, 2008 and December 31, 2007, fixed maturities held by AIG that were below investment grade or not rated totaled $20.7 billion and $27.0 billion, respectively.

(b) Represents obligations of states, municipalities and political subdivisions.

AIG's held to maturity and available for sale fixed maturity investments totaled $473.8 billion at March 31, 2008, compared to $523.5 billion at December 31, 2007. At March 31, 2008, approximately 57 percent of the fixed maturities investments were in domestic portfolios. Approximately 45 percent of such domestic securities were rated AAA by one or more of the principal rating agencies. Approximately four percent were below investment grade or not rated. AIG's investment decision process relies primarily on internally generated fundamental analysis and internal risk ratings. Third-party rating services' ratings and opinions provide one source of independent perspectives for consideration in the internal analysis.

A significant portion of the foreign fixed income portfolio is rated by Moody's, S&P or similar foreign rating services. Rating services are not available in all overseas locations. AIG's Credit Risk Committee (CRC) closely reviews the credit quality of the foreign portfolio's non-rated fixed income investments. At March 31, 2008, approximately 21 percent of the foreign fixed income investments were either rated AAA or, on the basis of AIG's internal analysis, were equivalent from a credit standpoint to securities so rated. Approximately four percent were below investment grade or not rated at that date. A large portion (approximately one third) of the foreign fixed income portfolio is sovereign fixed maturity securities supporting the policy liabilities in the country of issuance.

The credit ratings of AIG's fixed maturity investments, other than those of AIGFP, were as follows:

Rating	**March 31, 2008**	December 31, 2007
AAA	**35%**	38%
AA	**31**	28
A	**18**	18
BBB	**11**	11
Below investment grade	**4**	4
Non-rated	**1**	1
Total	**100%**	100%

The industry categories of AIG's available for sale corporate debt securities were as follows:

Industry Category	**March 31, 2008**	December 31, 2007
Financial institutions	**45%**	42%
Utilities	**11**	11
Communications	**8**	8
Consumer noncyclical	**7**	7
Capital goods	**6**	6
Consumer cyclical	**5**	5
Energy	**5**	4
Other	**13**	17
Total*	**100%**	100%

** At both March 31, 2008 and December 31, 2007, approximately 95 percent of these investments were rated investment grade.*

Investments in RMBS, CMBS, CDOs and ABS

As part of its strategy to diversify its investments, AIG invests in various types of securities, including RMBS, commercial mortgage-backed securities (CMBS), CDOs and ABS.

The amortized cost, gross unrealized gains (losses) and fair value of AIG's investments in RMBS, CMBS, CDOs and ABS were as follows:

	March 31, 2008				December 31, 2007			
(in millions)	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Bonds — available for sale:								
AIG, excluding AIGFP:								
RMBS	**$ 82,325**	**$499**	**$11,183**	**$ 71,641**	$ 89,851	$ 433	$5,504	$ 84,780
CMBS	**23,034**	**185**	**2,686**	**20,533**	23,918	237	1,156	22,999
CDO/ABS	**11,541**	**142**	**1,460**	**10,223**	10,844	196	593	10,447
Subtotal, excluding AIGFP	**116,900**	**826**	**15,329**	**102,397**	124,613	866	7,253	118,226
AIGFP*	—	—	—	—	16,369	355	450	16,274
Total	**$116,900**	**$826**	**$15,329**	**$102,397**	$140,982	$1,221	$7,703	$134,500

* *Represents total AIGFP investments in mortgage-backed, asset-backed and collateralized securities for which AIGFP has elected the fair value option effective January 1, 2008. At March 31, 2008, the fair value of these securities were $16.8 billion. An additional $2.1 billion related to insurance company investments is included in Bonds — trading.*

Investments in RMBS

The amortized cost, gross unrealized gains (losses) and fair value of AIG's investments in RMBS securities, other than those of AIGFP, were as follows:

	March 31, 2008					December 31, 2007				
(in millions)	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value	Percent of Total	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value	Percent of Total
RMBS:										
U.S. agencies	**$14,541**	**$409**	**$ 87**	**$14,863**	**21%**	$14,575	$320	$ 70	$14,825	17%
Prime non-agency[(a)]	**18,671**	**47**	**1,733**	**16,985**	**24**	21,552	72	550	21,074	25
Alt-A	**23,701**	**8**	**5,416**	**18,293**	**25**	25,349	17	1,620	23,746	28
Other housing-related[(b)]	**3,769**	**3**	**651**	**3,121**	**4**	4,301	2	357	3,946	5
Subprime	**21,643**	**32**	**3,296**	**18,379**	**26**	24,074	22	2,907	21,189	25
Total	**$82,325**	**$499**	**$11,183**	**$71,641**	**100%**	$89,851	$433	$5,504	$84,780	100%

(a) Includes foreign and jumbo RMBS-related securities.
(b) Primarily wrapped second-lien.

AIG's operations, other than AIGFP, held investments in RMBS with an estimated fair value of $71.6 billion at March 31, 2008, or approximately 8 percent of AIG's total invested assets. In addition, AIG's insurance operations held investments with a fair value totaling $3.2 billion in CDOs, of which $45 million included some level of subprime exposure. AIG's RMBS investments are predominantly in highly-rated tranches that contain substantial protection features through collateral subordination. At March 31, 2008, approximately 90 percent of these investments were rated AAA, and approximately 6 percent were rated AA by one or more of the principal rating agencies. AIG's investments rated BBB or below totaled $1.7 billion, or less than 0.2 percent of AIG's total invested assets at March 31, 2008. As of April 30, 2008, $7.5 billion of AIG's RMBS backed primarily by subprime collateral had been downgraded as a result of rating agency actions since January 1, 2008, and $12 million of such investments had been upgraded. Of the downgrades, $6.6 billion were AAA rated securities. In addition to the downgrades, as of April 30, 2008, the rating agencies had $9.6 billion of RMBS on watch for downgrade.

The amortized cost of AIG's RMBS investments, other than those of AIGFP, at March 31, 2008 by year of vintage and credit rating were as follows:

	Year of Vintage						
(in billions)	Prior	2004	2005	2006	2007	2008	Total
Rating:							
Total RMBS							
AAA	$ 9,775	$6,276	$14,920	$24,173	$18,475	$733	$74,352
AA	894	537	1,148	1,441	707	—	4,727
A	259	255	395	485	107	11	1,512
BBB and below	164	337	303	759	171	—	1,734
Total RMBS	$11,092	$7,405	$16,766	$26,858	$19,460	$744	$82,325
Alt-A RMBS							
AAA	$ 810	$ 890	$ 4,635	$ 9,610	$ 6,433	$ —	$22,378
AA	237	152	423	99	10	—	921
A	38	55	128	34	6	—	261
BBB and below	13	46	74	8	—	—	141
Total Alt-A	$ 1,098	$1,143	$ 5,260	$ 9,751	$ 6,449	$ —	$23,701
Subprime RMBS							
AAA	$ 511	$ 463	$ 5,242	$ 8,129	$ 4,555	$ —	$18,900
AA	41	101	280	899	334	—	1,655
A	86	98	92	165	19	—	460
BBB and below	3	80	28	512	5	—	628
Total Subprime	$ 641	$ 742	$ 5,642	$ 9,705	$ 4,913	$ —	$21,643

AIG's underwriting practices for investing in RMBS, other ABS and CDOs take into consideration the quality of the originator, the manager, the servicer, security credit ratings, underlying characteristics of the mortgages, borrower characteristics, and the level of credit enhancement in the transaction. AIG's strategy is typically to invest in securities rated AA or better and create diversification across multiple underlying asset classes.

Investments in CMBS

The amortized cost of AIG's CMBS investments, other than those of AIGFP, at March 31, 2008 was as follows:

(in millions)	Amortized Cost	Percent of Total
CMBS (traditional)	$20,358	89%
ReRemic/CRE CDO	1,940	8
Agency	256	1
Other	480	2
Total	$23,034	100%

The percentage of AIG's CMBS investments, other than those of AIGFP, at March 31, 2008 by credit rating was as follows:

	Percentage
Rating:	
AAA	78%
AA	13
A	8
BBB and below	1
Total	100%

The percentage of AIG's CMBS investments, other than those of AIGFP, by year of vintage at March 31, 2008 was as follows:

	Percentage
Year:	
2007	23%
2006	14
2005	19
2004	16
2003 and prior	28
Total	100%

The percentage of AIG's CMBS investments, other than those of AIGFP, by geographic region at March 31, 2008 was as follows:

	Percentage
Geographic region:	
New York	17%
California	15
Texas	7
Florida	6
Virginia	4
Illinois	4
New Jersey	3
Pennsylvania	3
Georgia	3
Massachusetts	3
All Other	35
Total	100%

At March 31, 2008, AIG held $23.0 billion in cost basis of CMBS. Approximately 78 percent of such holdings were rated AAA, approximately 21 percent were rated AA or A, and approximately 1 percent were rated BBB or below. At March 31, 2008, all such securities were current in the payment of principal and interest and none had default rates on underlying collateral at levels viewed by AIG as likely to result in the loss of principal or interest.

There have been disruptions in the commercial mortgage markets in general, and the CMBS market in particular, with credit default swaps indices and quoted prices of securities at levels consistent with a severe correction in lease rates, occupancy and fair value of properties. In addition, spreads in the primary mortgage market have widened significantly.

While this capital market stress has not to date been reflected in the performance of commercial mortgage securitization in the form of increased defaults in underlying mortgage pools, pricing of CMBS has been adversely affected by market perceptions that underlying mortgage defaults will increase. As a result, AIG recognized $556 million of other-than-temporary impairment charges in the first three months of 2008 on CMBS trading at a severe discount to cost, despite the absence of any deterioration in performance of the underlying credits, because AIG concluded that it could not reasonably assert that the recovery period was temporary. At this time, AIG anticipates substantial recovery of principal and interest on the securities to which such other-than-temporary impairment charges were recorded.

Investments in CDOs

The amortized cost of AIG's CDO investments, other than those of AIGFP, by collateral type at March 31, 2008 was as follows:

(in millions)	Amortized Cost	Percent of Total
Collateral Type:		
Bank loans (CLO)	$2,080	49%
Synthetic investment grade	1,340	32
Other	744	18
Subprime ABS	47	1
Total	$4,211	100%

The amortized cost of the AIG's CDO investments, other than those of AIGFP, by credit rating at March 31, 2008 was as follows:

(in millions)	Amortized Cost	Percent of Total
Rating:		
AAA	$ 763	18%
AA	902	21
A	2,127	51
BBB	316	8
Below investment grade and equity	103	2
Total	$4,211	100%

Securities Lending Activities

AIG's securities lending program is a centrally managed program facilitated by AIG Investments primarily for the benefit of certain of AIG's insurance companies. Securities are loaned to various financial institutions, primarily major banks and brokerage firms. Cash collateral generally equal to 102 percent of the fair value of the loaned securities is received. The cash collateral is invested in highly-rated fixed income securities to earn a net spread.

AIG's liability to the borrower for collateral received was $77.8 billion and the fair value of the collateral reinvested was $64.3 billion as of March 31, 2008. In addition to the invested collateral, the securities on loan as well as all of the assets of the participating companies are generally available to satisfy the liability for collateral received.

The composition of the securities lending invested collateral by credit rating at March 31, 2008 was as follows:

(in millions)	AAA	AA	A	BBB/Not Rated	Short-Term	Total
Corporate debt	$ 3,569	$4,179	$4,199	$2,534	$ —	$14,481
Mortgage-backed, asset-backed and collateralized	37,052	1,605	936	1,339	—	40,932
Cash and short-term investments	—	—	—	—	8,848	8,848
Total	$40,621	$5,784	$5,135	$3,873	$8,848	$64,261

Participation in the securities lending program by reporting unit at March 31, 2008 was as follows:

	Percent Participation
Domestic Life Insurance and Domestic Retirement Services	68%
Foreign Life Insurance	10
AIG Property Casualty Group	4
Foreign General Insurance	5
Asset Management	13
Total	100%

On March 31, 2008, $9.8 billion (or 14 percent) of the liabilities were one-day tenor. These one-day tenor loans do not have a contractual end date but are terminable by either party on demand. The balance of the liabilities contractually mature over the next sixty days; however, the maturing loans are frequently renewed and rolled over to extended dates. Collateral held for this program at March 31, 2008 included interest bearing cash equivalents with overnight maturities of $8.8 billion and other short-term investments of $1.8 billion.

Liquidity in the securities pool is managed based upon historical experience regarding volatility of daily, weekly and biweekly loan balances. Despite the current environment, the program has not experienced a significant decrease in loan balances.

In addition, the invested securities are carried at fair value with unrealized gains and losses recorded in accumulated other comprehensive income (loss) while net realized gains and losses are recorded in earnings. The net unrealized loss on the investments was $9.4 billion as of March 31, 2008. During the first three months of 2008, AIG recorded net realized losses of $2.9 billion on this portfolio, predominantly related to other-than-temporary impairments.

Portfolio Review

Other-Than-Temporary Impairments

AIG assesses its ability to hold any fixed maturity security in an unrealized loss position to its recovery, including fixed maturity securities classified as available for sale, at each balance sheet date. The decision to sell any such fixed maturity security classified as available for sale reflects the judgment of AIG's management that the security sold is unlikely to provide, on a relative value basis, as attractive a return in the future as alternative securities entailing comparable risks. With respect to distressed securities, the sale decision reflects management's judgment that the risk-discounted anticipated ultimate recovery is less than the value achievable on sale.

AIG evaluates its investments for impairments in valuation. The determination that a security has incurred an other-than-temporary decline in value requires the judgment of management and consideration of the fundamental condition of the issuer, its near-term prospects and all the relevant facts and circumstances. See Critical Accounting Estimates – Other-than-temporary impairments herein for further information on AIG's policy.

Once a security has been identified as other-than-temporarily impaired, the amount of such impairment is determined by reference to that security's contemporaneous fair value and recorded as a charge to earnings.

In light of the recent significant disruption in the U.S. residential mortgage and credit markets, AIG has recognized an other-than-temporary impairment charge (severity loss) of $4.1 billion in the first three months of 2008, primarily with respect to certain RMBS and other structured securities. Even while retaining their investment grade ratings, such securities were priced at a significant discount to cost. Notwithstanding AIG's intent and ability to hold such securities indefinitely, and despite structures that indicate that a substantial amount of the securities should continue to perform in accordance with original terms, AIG concluded that it could not reasonably assert that the recovery period would be temporary.

As a result of AIG's periodic evaluation of its securities for other-than-temporary impairments in value, AIG recorded other-than-temporary impairment charges of $5.6 billion and $467 million in the first three months of 2008 and 2007, respectively.

In addition to the above severity losses, AIG recorded other-than-temporary impairment charges in the first three months of 2008 and 2007 related to:

- securities that AIG does not intend to hold until recovery;
- declines due to foreign exchange;
- issuer-specific credit events;

- certain structured securities impaired under Emerging Issues Task Force Issue No. 99-20, "Recognition of Interest Income and Impairment on Purchased Beneficial Interests and Beneficial Interests that Continue to be Held by a Transferor in Securitized Financial Assets"; and
- other impairments, including equity securities and partnership investments.

Net realized capital gains (losses) were as follows:

(in millions)	Three Months Ended March 31, **2008**	2007
Sales of fixed maturities	**$ 19**	$ 41
Sales of equity securities	**80**	158
Sales of real estate and other assets	**(147)**	135
Other-than-temporary impairments	**(5,593)**	(467)
Foreign exchange transactions	**(664)**	136
Derivative instruments	**216**	(73)
Total	**$ (6,089)**	$ (70)

Other-than-temporary impairment charges by reporting segment were as follows:

(in millions)	General Insurance	Life Insurance & Retirement Services	Financial Services	Asset Management	Other	Total
Three months ended March 31, 2008						
Impairment Type:						
Severity	**$ 112**	**$ 3,156**	**$ 11**	**$ 825**	**$ 1**	**$ 4,105**
Lack of intent to hold to recovery	**21**	**691**	**1**	**66**	**—**	**779**
Foreign currency declines	**—**	**401**	**—**	**—**	**—**	**401**
Issuer-specific credit events	**22**	**112**	**—**	**37**	**—**	**171**
Adverse projected cash flows on structured securities	**—**	**32**	**—**	**105**	**—**	**137**
Total	**$ 155**	**$ 4,392**	**$ 12**	**$ 1,033**	**$ 1**	**$ 5,593**
Three months ended March 31, 2007						
Impairment Type:						
Severity	$ —	$ —	$ —	$ —	$ —	$ —
Lack of intent to hold to recovery	8	87	—	2	—	97
Foreign currency declines	—	212	—	—	—	212
Issuer-specific credit events	38	92	—	27	—	157
Adverse projected cash flows on structured securities	—	1	—	—	—	1
Total	$ 46	$ 392	$ —	$ 29	$ —	$ 467

Other-than-temporary severity-related impairment charges for the three-month period ended March 31, 2008 by type of security and credit rating were as follows:

Rating: *(millions)*	RMBS	CDO	CMBS	Other Securities	Total
Fixed Maturities:					
AAA	$1,496	$ 21	$117	$ 12	$1,646
AA	853	40	39	1	933
A	306	49	298	4	657
BBB and below	493	–	63	20	576
Nonrated	–	–	–	17	17
Equities	–	–	–	276	276
Total	$3,148	$110	$517	$330	$4,105

No other-than-temporary impairment charge with respect to any one single counterparty was significant to AIG's consolidated financial condition or results of operations, and no individual other-than-temporary impairment charge exceeded two percent of the consolidated net loss in the first three months of 2008.

In periods subsequent to the recognition of an other-than-temporary impairment charge for fixed maturity securities that is not credit or foreign exchange related, AIG generally accretes into income the discount or amortizes the reduced premium resulting from the reduction in cost basis over the remaining life of the security. The amount of

accretion recognized in earnings for the three months ended March 31, 2008 was $12 million.

Commercial Mortgage Loan Exposure

At March 31, 2008, AIG had direct commercial mortgage loan exposure of $19.5 billion, with $16.3 billion representing U.S. loan exposure. At that date, none of the U.S. loans were in default or delinquent by 90 days or more. The remaining commercial mortgage loans are secured predominantly by properties in Japan. In addition, at March 31, 2008, AIG had approximately $2.1 billion in residential mortgage loans in jurisdictions outside the United States, primarily backed by properties in Taiwan and Thailand.

An aging of the pre-tax unrealized losses of fixed maturity and equity securities, distributed as a percentage of cost relative to unrealized loss (the extent by which the fair value is less than amortized cost or cost), including the number of respective items, at March 31, 2008 was as follows:

	Less than or equal to 20% of Cost[b]			Greater than 20% to 50% of Cost[b]			Greater than 50% of Cost[b]			Total		
Aging[a] *(dollars in millions)*	Cost[c]	Unrealized Loss	Items	Cost[c]	Unrealized Loss	Items	Cost[c]	Unrealized Loss	Items	Cost[c]	Unrealized Loss[d]	Items
Investment grade bonds												
0-6 months	$ 80,455	$ 3,382	10,558	$ 3,255	$ 874	361	$ —	$ —	—	$ 83,710	$ 4,256	10,919
7-12 months	66,645	4,748	4,922	29,120	8,975	1,208	—	—	—	95,765	13,723	6,130
>12 months	43,498	3,129	8,549	5,029	1,296	619	—	—	—	48,527	4,425	9,168
Total	$190,598	$11,259	24,029	$37,404	$11,145	2,188	$ —	$ —	—	$228,002	$22,404	26,217
Below investment grade bonds												
0-6 months	$ 5,077	$ 157	1,647	$ 80	$ 24	24	$ —	$ —	—	$ 5,157	$ 181	1,671
7-12 months	1,052	77	251	101	28	21	—	—	—	1,153	105	272
>12 months	985	73	27,578	152	39	14	—	—	—	1,137	112	27,592
Total	$ 7,114	$ 307	29,476	$ 333	$ 91	59	$ —	$ —	—	$ 7,447	$ 398	29,535
Total bonds												
0-6 months	$ 85,532	$ 3,539	12,205	$ 3,335	$ 898	385	$ —	$ —	—	$ 88,867	$ 4,437	12,590
7-12 months	67,697	4,825	5,173	29,221	9,003	1,229	—	—	—	96,918	13,828	6,402
>12 months	44,483	3,202	36,127	5,181	1,335	633	—	—	—	49,664	4,537	36,760
Total[e]	$197,712	$11,566	53,505	$37,737	$11,236	2,247	$ —	$ —	—	$235,449	$22,802	55,752
Equity securities												
0-6 months	$ 4,030	$ 233	2,994	$ 691	$ 183	890	$ —	$ —	—	$ 4,721	$ 416	3,884
7-12 months	1,033	104	336	350	105	252	—	—	—	1,383	209	588
>12 months	—	—	—	—	—	—	—	—	—	—	—	—
Total	$ 5,063	$ 337	3,330	$ 1,041	$ 288	1,142	$ —	$ —	—	$ 6,104	$ 625	4,472

(a) Represents the number of consecutive months that fair value has been less than cost by any amount.

(b) Represents the percentage by which fair value is less than cost at the balance sheet date.

(c) For bonds, represents amortized cost.

(d) The effect on net income of unrealized losses after taxes will be mitigated upon realization because certain realized losses will be charged to participating policyholder accounts, or realization will result in current decreases in the amortization of certain DAC.

(e) Includes securities lending invested collateral.

Unrealized gains and losses

At March 31, 2008, the carrying value of AIG's fixed maturity and equity securities aggregated $523.2 billion. At March 31, 2008, aggregate pre-tax unrealized gains for fixed maturity and equity securities were $16.9 billion ($11.0 billion after tax).

At March 31, 2008, the aggregate pre-tax gross unrealized losses on fixed maturity and equity securities were $23.4 billion ($15.2 billion after tax). Additional information about these securities is as follows:

- These securities were valued, in the aggregate, at approximately 90 percent of their current amortized cost.
- Approximately 16 percent of these securities were valued at less than 20 percent of their current cost, or amortized cost.
- Less than four percent of the fixed income securities had issuer credit ratings that were below investment grade.

AIG did not consider these securities in an unrealized loss position to be other-than-temporarily impaired at March 31, 2008, because management has the intent and ability to hold these investments until they recover their cost basis. AIG believes the securities will generally continue to perform in accordance with the original terms, notwithstanding the present price declines.

For the three months ended March 31, 2008, unrealized losses related to investment grade bonds increased $9.5 billion ($6.2 billion after tax), reflecting the widening of credit spreads, partially offset by the effects of a decline in risk-free interest rates.

The amortized cost and fair value of fixed maturity securities available for sale in an unrealized loss position at March 31, 2008, by contractual maturity, were as follows:

(in millions)	Amortized Cost	Fair Value
Due in one year or less	$ 4,833	$ 4,749
Due after one year through five years	31,486	30,367
Due after five years through ten years	41,225	39,037
Due after ten years	61,830	57,819
Mortgage-backed, asset-backed and collateralized	96,075	80,675
Total	$235,449	$212,647

For the three months ended March 31, 2008, the pre-tax realized losses incurred with respect to the sale of fixed maturities and equity securities were $0.4 billion. The aggregate fair value of securities sold was $5.0 billion, which was approximately 92 percent of amortized cost. The average period of time that securities sold at a loss during the three months ended March 31, 2008 were trading continuously at a price below book value was approximately five months. See Risk Management — Credit Risk Management in the 2007 Annual Report on Form 10-K for an additional discussion of investment risks associated with AIG's investment portfolio.

Risk Management

For a complete discussion of AIG's risk management program, see Management's Discussion and Analysis of Financial Condition and Results of Operations in the 2007 Annual Report on Form 10-K.

AIG has continued to invest in human resources, systems and processes in the enterprise risk management functions, both at the corporate and business unit levels. These efforts include implementing systems and processes to ensure the aggregation of the various categories of risk across business units and as a whole, and incorporating forward-looking analyses and stress tests. These initiatives are ongoing and will take time to implement, including the hiring of additional qualified personnel.

Credit Risk Management

AIG defines its aggregate credit exposures to a counterparty as the sum of its fixed maturities, loans, finance leases, derivatives (mark to market), deposits (in the case of financial institutions) and the specified credit equivalent exposure to certain insurance products which embody credit risk.

The following table presents AIG's largest credit exposures at March 31, 2008 as a percentage of total consolidated shareholders' equity:

Category	Risk Rating[(a)]	Credit Exposure as a Percentage of Total Consolidated Shareholders' Equity
Investment Grade:		
10 largest combined	A+ (weighted average)[(b)]	108.0%
Single largest non-sovereign (financial institution)	AA-	10.4
Single largest corporate	AAA	7.2
Single largest sovereign	AA-	21.5
Non-Investment Grade:		
Single largest sovereign	BB-	2.4
Single largest non-sovereign	BB	0.5

(a) Risk rating is based on external ratings, or equivalent, based on AIG's internal risk rating process.

(b) Five of the ten largest credit exposures are to highly-rated financial institutions and four are to investment-grade rated sovereigns; none is rated lower than BBB+ or its equivalent.

AIG closely controls its aggregate cross-border exposures to avoid excessive concentrations in any one country or regional group of countries. AIG defines its cross-border exposure to include both cross-border credit exposures and its large cross-border investments in its own international subsidiaries. Thirteen countries had cross-border exposures in excess of 10 percent of total consolidated shareholders' equity at March 31, 2008. At that date eight were AAA-rated, four were AA-rated and one was A-rated.

In addition, AIG closely monitors its industry concentrations, the risks of which are often mitigated by the breadth and scope of AIG's international operations. Excluding the U.S. residential and commercial mortgage sectors, AIG's single largest industry credit exposure is to the highly-rated global financial institutions sector, accounting for 109 percent of total consolidated shareholders' equity at March 31, 2008. AIG's other industry credit concentrations in excess of 10 percent of total consolidated shareholders' equity are in the following industries (in descending order by approximate size):

- Oil and gas;
- Electric and water utilities;
- Global life insurance carriers;
- European regional financial institutions;
- Global telecommunications companies;

- U.S.-based regional financial institutions;
- Global securities firms and exchanges;
- Global reinsurance firms;
- Healthcare companies; and
- Retail companies.

Other than as described above, there were no significant changes to AIG's credit exposures as set forth in Risk Management – Corporate Risk Management – Credit Risk Management in the 2007 Annual Report on Form 10-K.

Market Risk Management

Insurance, Asset Management and Non-Trading Financial Services Value at Risk (VaR)

AIG performs one comprehensive VaR analysis across all of its non-trading businesses, and a separate VaR analysis for its trading business at AIGFP. The comprehensive VaR is categorized by AIG business segment (General Insurance, Life Insurance & Retirement Services, Financial Services and Asset Management) and also by market risk factor (interest rate, currency and equity). AIG's market risk VaR calculations include exposures to benchmark Treasury or swap interest rates, but do not include exposures to credit-based factors such as credit spreads. AIG's credit exposures within its invested assets and credit derivative portfolios are discussed in Segment Risk Management — Financial Services in the 2007 Annual Report on Form 10-K.

For the insurance segments, assets included are invested assets (excluding direct holdings of real estate) and liabilities included are reserve for losses and loss expenses, reserve for unearned premiums, future policy benefits for life and accident and health insurance contracts and other policyholders' funds. For financial services companies, loans and leases represent the majority of assets represented in the VaR calculation, while bonds and notes issued represent the majority of liabilities.

AIG calculated the VaR with respect to net fair values as of March 31, 2008 and December 31, 2007. The VaR number represents the maximum potential loss as of those dates that could be incurred with a 95 percent confidence (i.e., only five percent of historical scenarios show losses greater than the VaR figure) within a one-month holding period. AIG uses the historical simulation methodology that entails repricing all assets and liabilities under explicit changes in market rates within a specific historical time period. AIG uses the most recent three years of historical market information for interest rates, foreign exchange rates, and equity index prices. For each scenario, each transaction was repriced. Segment and AIG-wide scenario values are then calculated by netting the values of all the underlying assets and liabilities.

The following table presents the period-end, average, high and low VaRs on a diversified basis and of each component of market risk for AIG's non-trading businesses. The diversified VaR is usually smaller than the sum of its components due to correlation effects.

	2008				2007			
	As of	Three Months Ended March 31,			As of	Year Ended December 31,		
(in millions)	March 31	Average	High	Low	December 31	Average	High	Low
Total AIG non-trading market risk:								
Diversified	**$6,851**	**$6,222**	**$6,851**	**$5,593**	$5,593	$5,316	$5,619	$5,073
Interest rate	**5,190**	**4,787**	**5,190**	**4,383**	4,383	4,600	4,757	4,383
Currency	**844**	**814**	**844**	**785**	785	729	785	685
Equity	**3,268**	**2,948**	**3,268**	**2,627**	2,627	2,183	2,627	1,873
General Insurance:								
Diversified	**$1,356**	**$1,360**	**$1,363**	**$1,356**	$1,363	$1,637	$1,892	$1,363
Interest rate	**1,078**	**1,098**	**1,117**	**1,078**	1,117	1,492	1,792	1,117
Currency	**306**	**281**	**306**	**255**	255	222	255	205
Equity	**1,008**	**922**	**1,008**	**835**	835	659	835	573
Life Insurance & Retirement Services:								
Diversified	**$6,284**	**$5,732**	**$6,284**	**$5,180**	$5,180	$4,848	$5,180	$4,574
Interest rate	**4,987**	**4,696**	**4,987**	**4,405**	4,405	4,465	4,611	4,287
Currency	**621**	**635**	**649**	**621**	649	621	678	568
Equity	**2,210**	**2,010**	**2,210**	**1,810**	1,810	1,512	1,810	1,293
Non-Trading Financial Services:								
Diversified	**$ 167**	**$ 133**	**$ 167**	**$ 99**	$ 99	$ 117	$ 170	$ 85
Interest rate	**164**	**129**	**164**	**95**	95	116	168	76
Currency	**15**	**14**	**15**	**13**	13	12	13	11
Equity	**1**	**1**	**1**	**1**	1	1	1	1
Asset Management:								
Diversified	**$ 50**	**$ 44**	**$ 50**	**$ 38**	$ 38	$ 49	$ 74	$ 26
Interest rate	**41**	**37**	**41**	**32**	32	45	72	22
Currency	**2**	**2**	**2**	**2**	2	3	5	2
Equity	**12**	**13**	**13**	**12**	13	11	13	8

AIG's total non-trading market risk VaR increased from $5.6 billion at the end of 2007 to $6.9 billion as of March 31, 2008. The biggest drivers were market valuation effects (lower interest rates), increased volatilities in equity markets and "tail" effects (increased riskiness of the worst 5 percent of simulated portfolio outcomes that determine VaR). These factors more than offset the effect of reduced correlations (i.e., increased diversification) between U.S. equities and Asian interest rates.

Capital Markets Trading VaR

AIGFP attempts to minimize risk in benchmark interest rates, equities, commodities and foreign exchange. Market exposures in option implied volatilities, correlations and basis risks are also minimized over time.

AIGFP's minimal reliance on market risk driven revenue is reflected in its VaR. AIGFP's VaR calculation is based on the interest rate, equity, commodity and foreign exchange risk arising from its portfolio. Credit-related factors, such as credit spreads or credit default, are not included in AIGFP's VaR calculation. Because the market risk with respect to securities available for sale, at market, is substantially hedged, segregation of the financial instruments into trading and other than trading was not considered necessary. AIGFP operates under established market risk limits based upon this VaR calculation. In addition, AIGFP backtests its VaR.

In the calculation of VaR for AIGFP, AIG uses the historical simulation methodology based on estimated changes to the value of all transactions under explicit changes in market rates and prices within a specific historical time period. AIGFP attempts to secure reliable and independent current market prices, such as published exchange prices, external subscription services such as Bloomberg or Reuters, or third-party or broker quotes. When such prices are not available, AIGFP uses an internal methodology that includes extrapolation from observable and verifiable prices nearest to the dates of the transactions. Historically, actual results have not deviated from these models in any material respect.

AIGFP reports its VaR level using a 95 percent confidence level and a one-day holding period, facilitating risk comparison with AIGFP's trading peers and reflecting the fact that market risks can be actively assumed and offset in AIGFP's trading portfolio.

The following table presents the year-end, average, high, and low VaRs on a diversified basis and of each component of market risk for Capital Markets operations. The diversified VaR is usually smaller than the sum of its components due to correlation effects.

(in millions)	As of March 31	Three Months Ended March 31, 2008 Average	High	Low	As of December 31	Year Ended December 31, 2007 Average	High	Low
Capital Markets trading market risk:								
Diversified	**$ 6**	**$ 6**	**$8**	**$5**	$ 5	$5	$8	$4
Interest rate	**3**	**3**	**3**	**2**	3	2	3	2
Currency	**2**	**1**	**2**	**–**	1	1	2	1
Equity	**2**	**3**	**4**	**2**	3	3	5	2
Commodity	**5**	**4**	**6**	**3**	3	3	7	2

Credit Derivatives

AIGFP enters into credit derivative transactions in the ordinary course of its business. The majority of AIGFP's credit derivatives require AIGFP to provide credit protection on a designated portfolio of loans or debt securities. AIGFP provides such credit protection on a "second loss" basis, under which AIGFP's payment obligations arise only after credit losses in the designated portfolio exceed a specified threshold amount or level of "first losses." The threshold amount of credit losses that must be realized before AIGFP has any payment obligation is negotiated by AIGFP for each transaction to provide that the likelihood of any payment obligation by AIGFP under each transaction is remote, even in severe recessionary market scenarios. The underwriting process for these derivatives included assumptions of severely stressed recessionary market scenarios to minimize the likelihood of realized losses under these obligations.

In certain cases, the credit risk associated with a designated portfolio is tranched into different layers of risk, which are then analyzed and rated by the credit rating agencies. Typically, there will be an equity layer covering the first credit losses in respect of the portfolio up to a specified percentage of the total portfolio, and then successive layers ranging from generally a BBB-rated layer to one or more AAA-rated layers. In transactions that are rated with respect to the risk layer or tranche that is immediately junior to the threshold level above which AIGFP's payment obligation would generally arise, a significant majority are rated AAA by the rating agencies. In transactions that are not rated, AIGFP applies the same risk criteria for setting the threshold level for its payment obligations. Therefore, the risk layer assumed by AIGFP with respect to the designated portfolio in these transactions is often called the "super senior" risk layer, defined as the layer of credit risk senior to a risk layer that has been rated AAA by the credit rating agencies, or if the transaction is not rated, equivalent thereto.

Approximately $335 billion (consisting of corporate loans and prime residential mortgages) of the $469 billion in notional exposure of AIGFP's super senior credit default swap portfolio as of March 31, 2008 represented derivatives written for financial institutions, principally in Europe, for the purpose of providing regulatory capital relief rather than risk mitigation. In exchange for a minimum guaranteed fee, the counterparties receive credit protection with respect to diversified loan portfolios they own, thus improving their regulatory capital position. These derivatives are generally expected to terminate at no additional cost to the counterparty upon the counterparty's adoption of models compliant with the Basel II Accord. AIG expects that the majority of these transactions will be terminated within the next 12 to 24 months by AIGFP's counterparties as they implement those models. As of April 30, 2008, $55 billion in notional exposures have either been terminated or are in the process of being terminated. In its 2007 Annual Report on Form 10-K, AIG had previously reported that as of February 26, 2008, $54 billion in notional exposures have either been terminated or are in the process of being terminated. AIG has recently refined its approach to estimating its net notional exposures on certain of these transactions that have unique features. The notional exposures on transactions terminated or that were in the process of being terminated as of February 26, 2008 is $46 billion under the refined method. AIGFP was not required to make any payments as part of these terminations and in certain cases was paid a fee upon termination.

In light of this experience to date and after other comprehensive analyses, AIG determined that there was no unrealized market valuation adjustment for this regulatory capital relief portfolio for the three months ended March 31, 2008. AIG will continue to assess the valuation of this portfolio and monitor developments in the marketplace. Given the significant deterioration in the credit markets and the risk that AIGFP's expectations with respect to the termination of these transactions by its counterparties may not materialize, there can be no assurance that AIG will not recognize unrealized market valuation losses from this portfolio in future periods, and recognition of even a small percentage decline in the fair value of this portfolio could be material to an individual reporting period.

Approximately $57 billion of the $469 billion in notional exposure on AIGFP's super senior credit default swaps as of March 31, 2008 was written on investment grade corporate debt and CLOs. There is no uniform methodology to estimate the fair value of corporate super senior credit default swaps. AIG estimates the fair value of its corporate credit default swap portfolio by reference to benchmark indices, including the CDX and iTraxx, and third-party prices and collateral calls. AIG believes that its methodology to value the corporate credit default swap portfolio is reasonable, but other market participants use other methodologies and these methodologies may generate materially different fair value estimates. No assurance can be given that the fair value of AIG's corporate credit default swap portfolio would not change materially if other market indices or pricing sources were used to estimate the fair value of the portfolio.

In addition to writing credit protection on the super senior risk layer on designated portfolios of loans or debt securities, AIGFP also wrote protection on tranches below the super senior risk layer. At March 31, 2008 the notional amount of the credit default swaps in the regulatory capital relief portfolio written on tranches below the super senior risk layer was $5.7 billion, with an estimated fair value loss of $174 million.

AIGFP has also written credit protection on the super senior risk layer of diversified portfolios of investment grade corporate debt, CLOs and multi-sector CDOs. AIGFP is at risk only on the super senior portion related to a diversified portfolio referenced to loans or debt securities. The super senior risk portion is the last tranche to suffer losses after significant subordination. Credit losses would have to erode all tranches junior to the super senior tranche before AIGFP would suffer any realized losses. The subordination level required for each transaction is determined based on internal modeling and analysis of the pool of underlying assets and is not dependent on ratings determined by the rating agencies. While the credit default swaps written on corporate debt obligations are cash settled, the majority of the credit default swaps written on CDOs and CLOs require physical settlement. Under a physical settlement arrangement, AIGFP would be required to purchase the referenced super senior security at par in the event of a non-payment on that security. Certain of the AIGFP credit default swaps with an aggregate notional amount totaling $8.7 billion protect CDOs that include over-collateralization provisions that adjust the value of the collateral based, in part, on the ratings of the collateral for the CDOs. If the over collateralization provisions are not satisfied, an event of default would occur creating a right to accelerate. In certain of these circumstances, AIGFP may be required to purchase the referenced super senior security at par upon the acceleration of the security. AIGFP cannot currently quantify its obligations which might occur in the future under these provisions, or determine the timing of any purchases that might be required. Therefore, there can be no assurance that satisfaction of these obligations by AIGFP will not have a material effect on the manner in which AIG manages its liquidity.

AIGFP has written 2a-7 Puts in connection with certain multi-sector CDOs that allow the holders of the securities to treat the securities as eligible short-term 2a-7 investments under the Investment Company Act of 1940. Holders of securities are permitted, in certain circumstances, to tender their securities to the issuers at par. If an issuer's remarketing agent is unable to resell the securities so tendered, AIGFP must purchase the securities at par as long as the security has not experienced a default. During the first three months of 2008, AIGFP repurchased securities with a principal amount of approximately $235 million in connection with these obligations. In certain transactions, AIGFP has contracted with third parties to provide liquidity for the securities if they are put to AIGFP for up to a three-year period. Such liquidity facilities totaled $2.6 billion at March 31, 2008. As of April 30, 2008, AIGFP has utilized less than $200 million of these liquidity facilities. At April 30, 2008, AIGFP had $5.7 billion of notional exposure on 2a-7 Puts, included as part of the multi-sector CDO portfolio discussed herein.

As of April 30, 2008, a significant majority of AIGFP's super senior exposures continued to have tranches below AIGFP's attachment point that have been explicitly rated AAA or, in AIGFP's judgment, would have been rated AAA had they been rated. AIGFP's portfolio of credit default swaps undergoes regular monitoring, modeling and analysis and contains protection through collateral subordination.

Certain of these credit derivatives are subject to collateral posting provisions. These provisions differ among counterparties and asset classes. In the case of most of the multi-sector CDO transactions, the amount of collateral required is determined based on the change in value of the underlying cash security that represents the super senior risk layer subject to credit protection, and not the change in value of the super senior credit derivative.

As of April 30, 2008, AIGFP had received collateral calls from counterparties in respect of certain super senior credit default swaps (including those entered into by counterparties for regulatory capital relief purposes and those in respect of corporate debt/CLOs). At times, valuation estimates made by certain of the counterparties with respect to certain super senior credit default swaps or the underlying reference CDO securities, for purposes of determining the amount of collateral required to be posted by AIGFP in connection with such instruments, have differed significantly from AIGFP's estimates. In almost all cases, AIGFP has been able to successfully resolve the differences or otherwise reach an accommodation such that collateral posting levels are not currently the subject of ongoing negotiations, including in certain cases entering into compromise collateral arrange-

ments, some of which are for specified periods of time. AIGFP is currently in active discussions with a small number of other counterparties to resolve such valuation differences. As of April 30, 2008, AIGFP had posted collateral (or had received collateral, where offsetting exposures on other transactions resulted in the counterparty posting to AIGFP) based on exposures, calculated in respect of super senior credit default swaps, in an aggregate net amount of $9.7 billion. Valuation estimates made by counterparties for collateral purposes were considered in the determination of the fair value estimates of AIGFP's super senior credit default swap portfolio.

AIG has conducted risk analyses of the super senior multi-sector CDO credit default swap portfolio of AIGFP. AIG's analyses have been conducted to assess the risk of incurring net realized losses over the remaining life of the portfolio. In addition to analyses of each individual risk in the portfolio, AIG conducted certain ratings-based stress tests, which centered around scenarios of further stress on the portfolio resulting from downgrades by the rating agencies from current levels on the underlying collateral in the CDO structures supported by AIGFP's credit default swaps. These rating actions would be prompted by factors such as the worsening beyond current estimates of delinquency and residential housing price deterioration in the underlying assets in the collateral securities of the CDO structures. The results of these stress tests indicated possible realized losses on a static basis, because the assumptions of losses in these stress tests assumed immediate realization of loss. Actual realized losses would only be experienced over time given the timing of losses incurred in the underlying portfolios and the timing of breaches of the subordination afforded to AIGFP through the structures of the CDO. No benefit was taken in these stress tests for cash flow diversion features, recoveries upon default or other risk mitigant benefits.

During the first quarter of 2008, AIG developed an additional methodology to estimate its potential realized credit impairment losses from AIGFP's super senior multi-sector CDO credit default swap portfolio. The methodology combines a roll rate estimate of the losses emanating from the subprime and Alt-A RMBS collateral securities in the multi-sector CDOs, plus an estimate of losses arising from the CDOs inside the collateral pools (inner CDOs).

In the roll rate analysis, default rates on mortgages in various stages of delinquency (30 days past due, 60 days past due, 90 days past due, bankruptcy or foreclosure, real estate owned) are projected out at various rates (called roll rates) to estimate total potential defaults. Loss severities are then applied to the defaults to estimate realized credit impairment losses. In addition, loss timing curves to the performing mortgages are also applied to estimate how much of the non-delinquent portfolio is likely to default given mortgage seasoning ("age" of the mortgage). Finally, AIG applies loss estimates to the inner CDOs, using inner CDO loss estimates that depend on the vintage, type (high grade and mezzanine) and rating of the CDO.

ITEM 3. Quantitative and Qualitative Disclosures About Market Risk

Included in Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations.

ITEM 4. Controls and Procedures

In connection with the preparation of this Quarterly Report on Form 10-Q, an evaluation was carried out by AIG's management, with the participation of AIG's Chief Executive Officer and Chief Financial Officer, of the effectiveness of AIG's disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934 (Exchange Act)). Disclosure controls and procedures are designed to ensure that information required to be disclosed in reports filed or submitted under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in SEC rules and forms and that such information is accumulated and communicated to management, including the Chief Executive Officer and Chief Financial Officer, to allow timely decisions regarding required disclosures. Solely as a result of the previously identified material weakness in internal control over the fair value valuation of the AIGFP super senior credit default swap portfolio and oversight thereof as described in the 2007 Annual Report on Form 10-K, AIG's Chief Executive Officer and Chief Financial Officer have concluded that, as of March 31, 2008, AIG's disclosure controls and procedures were ineffective. Notwithstanding the existence of this material weakness, AIG believes that the consolidated financial statements in this Quarterly Report on Form 10-Q fairly present, in all material respects, AIG's consolidated financial condition as of March 31, 2008 and December 31, 2007 and consolidated results of operations and cash flows for the three-month periods ended March 31, 2008 and 2007, in conformity with GAAP. In addition, there has been no change in AIG's internal control over financial reporting (as defined in Rule 13a-15(f) under the Exchange Act) that occurred during the quarter ended March 31, 2008 that has materially affected, or is reasonably likely to materially affect, AIG's internal control over financial reporting.

Throughout 2008 and 2007, AIG recorded out of period adjustments, many of which were detected as part of continuing remediation efforts. It is AIG's policy to record all error

corrections, without regard to materiality, and AIG has an established, formal process for the identification, evaluation and recording of all out of period adjustments. This process includes a heightened sensitivity for potential errors related to the internal control matters discussed in Item 9A. of the 2007 Annual Report on Form 10-K. AIG distinguishes error corrections from changes in estimates by evaluating the facts and circumstances of such items, including considering whether information was capable of being known at the time of original recording. AIG has evaluated the adjustments recorded in 2008 and 2007 from a qualitative and quantitative perspective and concluded that such adjustments are immaterial individually and in the aggregate to the current and prior periods.

Part II – OTHER INFORMATION

ITEM 2. Unregistered Sales of Equity Securities and Use of Proceeds

Information with respect to purchases of AIG Common stock during the three months ended March 31, 2008 was as follows:

Period	Total Number of Shares Purchased[(a)]	Average Price Paid per Share	Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs	Maximum Number of Shares that May Yet Be Purchased Under the Plans or Programs at End of Month[(b)]
January 1 - 31	7,367,032	$54.55	7,367,032	
February 1 - 29	12,639,601	50.98	12,639,601	
March 1 - 31	14,087,150	48.73	14,087,150	
Total	34,093,783	$50.82	34,093,783	

(a) Reflects date of delivery. Does not include 1,066 shares delivered or attested to in satisfaction of the exercise price by holders of AIG employee stock options exercised during the three months ended March 31, 2008.

(b) In February 2007, AIG's Board of Directors increased AIG's share repurchase program by authorizing the repurchase of shares with an aggregate purchase price of $8 billion. In November 2007, AIG's Board of Directors authorized the repurchase of an additional $8 billion in common stock. A balance of $9.18 billion remained for purchases under the program as of March 31, 2008, although $179 million of that amount has been advanced by AIG to purchase shares under the program.

Subsequent to March 31, 2008, an additional 3,832,276 shares were purchased, satisfying the balance of the commitments existing at December 31, 2007 that had not been satisfied at March 31, 2008. AIG does not expect to purchase additional shares under its share repurchase program for the foreseeable future.

ITEM 6. Exhibits

See accompanying Exhibit Index.

SIGNATURE

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

AMERICAN INTERNATIONAL GROUP, INC.
(Registrant)

/s/ STEVEN J. BENSINGER

Steven J. Bensinger
Executive Vice President and Chief Financial Officer

/s/ DAVID L. HERZOG

David L. Herzog
Senior Vice President and Comptroller
(Principal Accounting Officer)

Dated: May 8, 2008

EXHIBIT INDEX

Exhibit Number	Description	Location
10.1	Partners Plan (Amended and Restated as of March 11, 2008)	Filed herewith.
10.2	Senior Partners Plan (Amended and Restated as of March 11, 2008)	Filed herewith.
11	Statement re computation of per share earnings	Included in Note 4 of Notes to Consolidated Financial Statements.
12	Statement re computation of ratios	Filed herewith.
31	Rule 13a-14(a)/15d-14(a) Certifications	Filed herewith.
32	Section 1350 Certifications	Filed herewith.

Exhibit 12

American International Group, Inc.
Computation of Ratios of Earnings to Fixed Charges

(in millions, except ratios)	Three Months Ended March 31, **2008**	2007
Income (loss) before income taxes and minority interest	**$(11,264)**	$ 6,172
Less – Equity income of less than 50% owned persons	**9**	42
Add – Dividends from less than 50% owned persons	**—**	—
	(11,273)	6,130
Add – Fixed charges	**2,192**	2,672
Less – Capitalized interest	**9**	11
Income (loss) before income taxes, minority interest and fixed charges	**$ (9,090)**	$ 8,791
Fixed charges:		
Interest costs	**$ 2,117**	$ 2,612
Rental expense[a]	**75**	60
Total fixed charges	**$ 2,192**	$ 2,672
Ratio of earnings to fixed charges	**[b]**	3.29
Secondary Ratio		
Interest credited to GIC and GIA policy and contract holders	**$ (926)**	$(1,579)
Total fixed charges excluding interest credited to GIC and GIA policy and contract holders	**$ 1,266**	$ 1,093
Secondary ratio of earnings to fixed charges	**[b]**	6.60

(a) The proportion considered representative of the interest factor.

(b) Earnings were inadequate to cover total fixed charges by $11,282 million for the three-month period ended March 31, 2008. The coverage deficiency for total fixed charges excluding interest credited to GIC and GIA policy and contract holders was $10,356 million for the three-month period ended March 31, 2008.

The secondary ratio is disclosed for the convenience of fixed income investors and the rating agencies that serve them and is more comparable to the ratios disclosed by all issuers of fixed income securities. The secondary ratio removes interest credited to guaranteed investment contract (GIC) policyholders and guaranteed investment agreement (GIA) contract holders. Such interest expenses are also removed from income (loss) before income taxes and minority interest used in this calculation. GICs and GIAs are entered into by AIG's insurance subsidiaries, principally Sun America Life Insurance Company and AIG Financial Products Corp. and its subsidiaries, respectively. The proceeds from GICs and GIAs are invested in a diversified portfolio of securities, primarily investment grade bonds. The assets acquired yield rates greater than the rates on the related policyholders obligation or agreement, with the intent of earning operating income from the spread.

Exhibit 31

CERTIFICATIONS

I, Martin J. Sullivan, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q of American International Group, Inc.;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:

(a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

(b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

(c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

(d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):

(a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

(b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

/s/ MARTIN J. SULLIVAN

Martin J. Sullivan
President and Chief Executive Officer

Date: May 8, 2008

CERTIFICATIONS

I, Steven J. Bensinger, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q of American International Group, Inc.;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:

(a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

(b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

(c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

(d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):

(a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

(b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

/s/ STEVEN J. BENSINGER

Steven J. Bensinger
Executive Vice President and Chief Financial Officer

Date: May 8, 2008

Exhibit 32

CERTIFICATION

In connection with the Quarterly Report on Form 10-Q of American International Group, Inc. (the "Company") for the quarter ended March 31, 2008, as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, Martin J. Sullivan, President and Chief Executive Officer of the Company, certify, pursuant to 18 U.S.C. Section 1350, that to my knowledge:

1. The Report fully complies with the requirements of Section 13(a) or 15(d), as applicable, of the Securities Exchange Act of 1934; and

2. The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

/s/ MARTIN J. SULLIVAN

Martin J. Sullivan
President and Chief Executive Officer

Date: May 8, 2008

The foregoing certification is being furnished solely pursuant to 18 U.S.C. Section 1350 and is not being filed as part of the Report or as a separate disclosure document.

CERTIFICATION

In connection with the Quarterly Report on Form 10-Q of American International Group, Inc. (the "Company") for the quarter ended March 31, 2008, as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, Steven J. Bensinger, Executive Vice President and Chief Financial Officer of the Company, certify, pursuant to 18 U.S.C. Section 1350, that to my knowledge:

1. The Report fully complies with the requirements of Section 13(a) or 15(d), as applicable, of the Securities Exchange Act of 1934; and

2. The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

/s/ STEVEN J. BENSINGER

Steven J. Bensinger
Executive Vice President and Chief Financial Officer

Date: May 8, 2008

The foregoing certification is being furnished solely pursuant to 18 U.S.C. Section 1350 and is not being filed as part of the Report or as a separate disclosure document.

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

Form 10-Q

(Mark One)

☑ QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended June 30, 2008

or

☐ TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the transition period from to

Commission File Number 1-8787

American International Group, Inc.

(Exact name of registrant as specified in its charter)

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

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

Former name, former address and former fiscal year, if changed since last report: None

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

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

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

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes ☐ No ☑

As of July 31, 2008, there were 2,688,833,724 shares outstanding of the registrant's common stock.

TABLE OF CONTENTS

Part I – FINANCIAL INFORMATION

ITEM 1. Financial Statements (unaudited)

CONSOLIDATED BALANCE SHEET

(in millions) (unaudited)

	June 30, 2008	December 31, 2007
Assets:		
Investments and Financial Services assets:		
Fixed maturity securities:		
Bonds available for sale, at fair value (amortized cost: 2008 – $400,052; 2007 – $393,170)	**$ 393,316**	$ 397,372
Bonds held to maturity, at amortized cost (fair value: 2008 – $21,809; 2007 – $22,157)	**21,632**	21,581
Bond trading securities, at fair value	**8,801**	9,982
Equity securities:		
Common stocks available for sale, at fair value (cost: 2008 – $13,490; 2007 – $12,588)	**17,306**	17,900
Common and preferred stocks trading, at fair value	**22,514**	21,376
Preferred stocks available for sale, at fair value (cost: 2008 – $2,596; 2007 – $2,600)	**2,496**	2,370
Mortgage and other loans receivable, net of allowance (2008 – $99; 2007 – $77) (held for sale: 2008 – $30; 2007 – $377 (amount measured at fair value: 2008 – $745)	**34,384**	33,727
Financial Services assets:		
Flight equipment primarily under operating leases, net of accumulated depreciation (2008 – $11,359; 2007 – $10,499)	**43,887**	41,984
Securities available for sale, at fair value (cost: 2008 – $1,246; 2007 – $40,157)	**1,205**	40,305
Trading securities, at fair value	**35,170**	4,197
Spot commodities, at fair value	**90**	238
Unrealized gain on swaps, options and forward transactions, at fair value	**11,548**	12,318
Trade receivables	**2,294**	672
Securities purchased under agreements to resell, at fair value in 2008	**16,597**	20,950
Finance receivables, net of allowance (2008 – $1,133; 2007 – $878) (held for sale: 2008 – $36; 2007 – $233)	**33,311**	31,234
Securities lending invested collateral, at fair value (cost: 2008 – $67,758; 2007 – $80,641)	**59,530**	75,662
Other invested assets (amount measured at fair value: 2008 – $22,099; 2007 – $20,827)	**62,029**	58,823
Short-term investments (amount measured at fair value: 2008 – $24,167)	**69,492**	51,351
Total Investments and Financial Services assets	**835,602**	842,042
Cash	**2,229**	2,284
Investment income due and accrued	**6,614**	6,587
Premiums and insurance balances receivable, net of allowance (2008 – $596; 2007 – $662)	**20,050**	18,395
Reinsurance assets, net of allowance (2008 – $502; 2007 – $520)	**22,940**	23,103
Current and deferred income taxes	**8,211**	—
Deferred policy acquisition costs	**46,733**	43,914
Investments in partially owned companies	**628**	654
Real estate and other fixed assets, net of accumulated depreciation (2008 – $5,710; 2007 – $5,446)	**5,692**	5,518
Separate and variable accounts, at fair value	**73,401**	78,684
Goodwill	**10,661**	9,414
Other assets (amount measured at fair value: 2008 – $2,452; 2007 – $4,152)	**17,115**	17,766
Total assets	**$1,049,876**	$1,048,361

See Accompanying Notes to Consolidated Financial Statements.

CONSOLIDATED BALANCE SHEET *(continued)*

(in millions, except share data) (unaudited)

	June 30, 2008	December 31, 2007
Liabilities:		
Reserve for losses and loss expenses	**$ 88,747**	$ 85,500
Unearned premiums	**28,738**	27,703
Future policy benefits for life and accident and health insurance contracts	**147,232**	136,387
Policyholders' contract deposits (amount measured at fair value: 2008 – $4,179; 2007 – $295)	**265,411**	258,459
Other policyholders' funds	**13,773**	12,599
Commissions, expenses and taxes payable	**5,597**	6,310
Insurance balances payable	**5,569**	4,878
Funds held by companies under reinsurance treaties	**2,498**	2,501
Current income taxes payable	**—**	3,823
Financial Services liabilities:		
Securities sold under agreements to repurchase (amount measured at fair value: 2008 – $8,338)	**9,659**	8,331
Trade payables	**1,622**	6,445
Securities and spot commodities sold but not yet purchased, at fair value	**3,189**	4,709
Unrealized loss on swaps, options and forward transactions, at fair value	**24,232**	14,817
Trust deposits and deposits due to banks and other depositors (amount measured at fair value: 2008 – $240)	**6,165**	4,903
Commercial paper and extendible commercial notes	**15,061**	13,114
Long-term borrowings (amount measured at fair value: 2008 – $53,839)	**163,577**	162,935
Separate and variable accounts	**73,401**	78,684
Securities lending payable	**75,056**	81,965
Minority interest	**11,149**	10,422
Other liabilities (amount measured at fair value: 2008 – $6,861; 2007 – $3,262)	**31,012**	27,975
Total liabilities	**971,688**	952,460
Preferred shareholders' equity in subsidiary companies	**100**	100
Commitments, Contingencies and Guarantees (See Note 6)		
Shareholders' equity:		
Common stock, $2.50 par value; 5,000,000,000 shares authorized; shares issued 2008 – 2,948,038,001; 2007 – 2,751,327,476	**7,370**	6,878
Additional paid-in capital	**9,446**	2,848
Payments advanced to purchase shares	**—**	(912)
Retained earnings	**73,743**	89,029
Accumulated other comprehensive income (loss)	**(3,903)**	4,643
Treasury stock, at cost; 2008 – 259,225,244; 2007 – 221,743,421 shares of common stock	**(8,568)**	(6,685)
Total shareholders' equity	**78,088**	95,801
Total liabilities, preferred shareholders' equity in subsidiary companies and shareholders' equity	**$1,049,876**	$1,048,361

See Accompanying Notes to Consolidated Financial Statements.

CONSOLIDATED STATEMENT OF INCOME (LOSS)

(in millions, except per share data) (unaudited)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2008	2007	**2008**	2007
Revenues:				
Premiums and other considerations	**$21,735**	$19,533	**$ 42,407**	$39,175
Net investment income	**6,728**	7,853	**11,682**	14,977
Net realized capital losses	**(6,081)**	(28)	**(12,170)**	(98)
Unrealized market valuation losses on AIGFP super senior credit default swap portfolio	**(5,565)**	—	**(14,672)**	—
Other income	**3,116**	3,792	**6,717**	7,741
Total revenues	**19,933**	31,150	**33,964**	61,795
Benefits and expenses:				
Incurred policy losses and benefits	**18,450**	16,221	**34,332**	32,367
Insurance acquisition and other operating expenses	**10,239**	8,601	**19,652**	16,928
Total benefits and expenses	**28,689**	24,822	**53,984**	49,295
Income (loss) before income taxes (benefits) and minority interest	**(8,756)**	6,328	**(20,020)**	12,500
Income taxes (benefits)	**(3,357)**	1,679	**(6,894)**	3,405
Income (loss) before minority interest	**(5,399)**	4,649	**(13,126)**	9,095
Minority interest	**42**	(372)	**(36)**	(688)
Net income (loss)	**$ (5,357)**	$ 4,277	**$(13,162)**	$ 8,407
Earnings (loss) per common share:				
Basic	**$ (2.06)**	$ 1.64	**$ (5.11)**	$ 3.22
Diluted	**$ (2.06)**	$ 1.64	**$ (5.11)**	$ 3.21
Dividends declared per common share	**$ 0.220**	$ 0.200	**$ 0.420**	$ 0.365
Average shares outstanding:				
Basic	**2,605**	2,602	**2,575**	2,607
Diluted	**2,605**	2,613	**2,575**	2,621

See Accompanying Notes to Consolidated Financial Statements.

CONSOLIDATED STATEMENT OF SHAREHOLDERS' EQUITY

	Six Months Ended June 30, 2008	
(in millions, except share and per share data) (unaudited)	Amounts	Shares
Common stock:		
Balance, beginning of period	$ 6,878	2,751,327,476
Issuances	492	196,710,525
Balance, end of period	7,370	2,948,038,001
Additional paid-in capital:		
Balance, beginning of period	2,848	
Excess of proceeds over par value of common stock issued	6,851	
Present value of future contract adjustment payments related to issuance of equity units	(431)	
Excess of cost over proceeds of common stock issued under stock plans	(13)	
Other	191	
Balance, end of period	9,446	
Payments advanced to purchase shares:		
Balance, beginning of period	(912)	
Payments advanced	(1,000)	
Shares purchased	1,912	
Balance, end of period	—	
Retained earnings:		
Balance, beginning of period	89,029	
Cumulative effect of accounting changes, net of tax	(1,003)	
Adjusted balance, beginning of period	88,026	
Net loss	(13,162)	
Dividends to common shareholders ($0.42 per share)	(1,121)	
Balance, end of period	73,743	
Accumulated other comprehensive income (loss):		
Unrealized appreciation (depreciation) of investments, net of tax:		
Balance, beginning of period	4,375	
Cumulative effect of accounting changes, net of tax	(105)	
Adjusted balance, beginning of period	4,270	
Unrealized depreciation of investments, net of reclassification adjustments	(14,254)	
Income tax benefit	4,813	
Balance, end of period	(5,171)	
Foreign currency translation adjustments, net of tax:		
Balance, beginning of period	880	
Translation adjustment	1,108	
Income tax expense	(124)	
Balance, end of period	1,864	
Net derivative gains (losses) arising from cash flow hedging activities:		
Balance, beginning of period	(87)	
Net deferred gains on cash flow hedges, net of reclassification adjustments	11	
Deferred income tax expense	(5)	
Balance, end of period	(81)	
Retirement plan liabilities adjustment, net of taxes:		
Balance, beginning of period	(525)	
Net actuarial loss	18	
Prior service credit	(5)	
Deferred income tax expense	(3)	
Balance, end of period	(515)	
Accumulated other comprehensive income (loss), end of period	(3,903)	
Treasury stock, at cost:		
Balance, beginning of period	(6,685)	(221,743,421)
Shares acquired	(1,912)	(37,927,125)
Issued under stock plans	24	443,767
Other	5	1,535
Balance, end of period	(8,568)	(259,225,244)
Total shareholders' equity, end of period	$78,088	

See Accompanying Notes to Consolidated Financial Statements.

CONSOLIDATED STATEMENT OF CASH FLOWS

(in millions) (unaudited)

	Six Months Ended June 30,	
	2008	2007
Summary:		
Net cash provided by (used in) operating activities	**$ 16,589**	$ 17,431
Net cash provided by (used in) investing activities	**(21,963)**	(40,314)
Net cash provided by (used in) financing activities	**5,274**	22,947
Effect of exchange rate changes on cash	**45**	(19)
Change in cash	**(55)**	45
Cash at beginning of year period	**2,284**	1,590
Cash at end of year period	**$ 2,229**	$ 1,635
Cash flows from operating activities:		
Net income (loss)	**$(13,162)**	$ 8,407
Adjustments to reconcile net income (loss) to net cash provided by operating activities:		
Noncash revenues, expenses, gains and losses included in income (loss):		
Unrealized market valuation losses on AIGFP super senior credit default swap portfolio	**14,672**	—
Net gains on sales of securities available for sale and other assets	**(494)**	(732)
Foreign exchange transaction (gains) losses	**857**	639
Net unrealized (gains) losses on non-AIGFP derivatives and other assets and liabilities	**2,086**	(123)
Equity in income of partially owned companies and other invested assets	**(151)**	(2,747)
Amortization of deferred policy acquisition costs	**7,343**	5,911
Depreciation and other amortization	**1,799**	1,608
Provision for mortgage, other loans and finance receivables	**578**	229
Other-than-temporary impairments	**12,416**	884
Changes in operating assets and liabilities:		
General and life insurance reserves	**9,748**	8,238
Premiums and insurance balances receivable and payable – net	**(1,104)**	(941)
Reinsurance assets	**196**	434
Capitalization of deferred policy acquisition costs	**(9,160)**	(7,567)
Investment income due and accrued	**118**	(44)
Funds held under reinsurance treaties	**(25)**	(210)
Other policyholders' funds	**851**	879
Income taxes receivable and payable – net	**(6,960)**	(225)
Commissions, expenses and taxes payable	**52**	724
Other assets and liabilities – net	**1,809**	553
Trade receivables and payables – net	**(6,446)**	(925)
Trading securities	**930**	(2,258)
Spot commodities	**148**	127
Net unrealized (gain) loss on swaps, options and forward transactions	**(3,993)**	1,317
Securities purchased under agreements to resell	**4,353**	2,116
Securities sold under agreements to repurchase	**1,237**	(226)
Securities and spot commodities sold but not yet purchased	**(1,531)**	221
Finance receivables and other loans held for sale – originations and purchases	**(279)**	(3,957)
Sales of finance receivables and other loans – held for sale	**492**	4,177
Other, net	**209**	922
Total adjustments	**29,751**	9,024
Net cash provided by operating activities	**$ 16,589**	$ 17,431

See Accompanying Notes to Consolidated Financial Statements.

CONSOLIDATED STATEMENT OF CASH FLOWS *(continued)*

(in millions) (unaudited)

	Six Months Ended June 30,	
	2008	2007
Cash flows from investing activities:		
Proceeds from (payments for)		
Sales and maturities of fixed maturity securities available for sale and hybrid investments	**$ 42,026**	$ 64,563
Sales of equity securities available for sale	**4,861**	4,275
Proceeds from fixed maturity securities held to maturity	**33**	133
Sales of trading securities	**14,120**	—
Sales of flight equipment	**372**	28
Sales or distributions of other invested assets	**8,715**	6,208
Payments received on mortgage and other loans receivable	**3,457**	2,270
Principal payments received on finance receivables held for investment	**6,757**	6,430
Purchases of fixed maturity securities available for sale and hybrid investments	**(47,114)**	(72,348)
Purchases of equity securities available for sale	**(5,808)**	(5,852)
Purchases of fixed maturity securities held to maturity	**(88)**	(129)
Purchases of trading securities	**(9,244)**	—
Purchases of flight equipment (including progress payments)	**(2,950)**	(3,883)
Purchases of other invested assets	**(11,988)**	(12,171)
Mortgage and other loans receivable issued	**(3,340)**	(5,029)
Finance receivables held for investment – originations and purchases	**(8,778)**	(7,387)
Change in securities lending invested collateral	**6,315**	(11,772)
Net additions to real estate, fixed assets, and other assets	**(663)**	(466)
Net change in short-term investments	**(18,832)**	(4,636)
Net change in non-AIGFP derivative assets and liabilities	**186**	(548)
Net cash provided by (used in) investing activities	**$(21,963)**	$(40,314)
Cash flows from financing activities:		
Proceeds from (payments for)		
Policyholders' contract deposits	**$ 33,322**	$ 28,769
Policyholders' contract withdrawals	**(27,926)**	(29,379)
Change in other deposits	**682**	(823)
Change in commercial paper and extendible commercial notes	**1,930**	1,768
Long-term borrowings issued	**55,685**	50,091
Repayments on long-term borrowings	**(56,645)**	(34,937)
Change in securities lending payable	**(6,919)**	12,021
Proceeds from common stock issued	**7,343**	—
Issuance of treasury stock	**11**	180
Payments advanced to purchase treasury stock	**(1,000)**	(4,000)
Cash dividends paid to shareholders	**(1,036)**	(859)
Acquisition of treasury stock	**—**	(16)
Other, net	**(173)**	132
Net cash provided by (used in) financing activities	**$ 5,274**	$ 22,947
Supplementary disclosure of cash flow information:		
Cash paid (received) during the period for:		
Interest	**$ 3,493**	$ 3,744
Taxes	**$ 66**	$ 3,524
Non-cash financing activities:		
Interest credited to policyholder accounts included in financing activities	**$ 3,815**	$ 5,932
Treasury stock acquired using payments advanced to purchase shares	**$ 1,912**	$ 1,664
Present value of future contract adjustment payments related to issuance of equity units	**$ 431**	$ —
Non-cash investing activities:		
Debt assumed on acquisitions and warehoused investments	**$ 153**	$ 354

See Accompanying Notes to Consolidated Financial Statements.

CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME (LOSS)

(in millions) (unaudited)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2008	2007	**2008**	2007
Net income (loss)	**$ (5,357)**	$ 4,277	**$(13,162)**	$ 8,407
Other comprehensive income (loss):				
Cumulative effect of accounting changes	**—**	—	**(162)**	—
Deferred income tax benefit on above changes	**—**	—	**57**	—
Unrealized (depreciation) appreciation of investments – net of reclassification adjustments	**(3,682)**	(2,161)	**(14,254)**	(852)
Deferred income tax benefit on above changes	**1,065**	598	**4,813**	140
Foreign currency translation adjustments	**(238)**	(164)	**1,108**	(329)
Deferred income tax benefit (expense) on above changes	**127**	7	**(124)**	35
Net derivative gains (losses) arising from cash flow hedging activities – net of reclassification adjustments	**144**	61	**11**	62
Deferred income tax benefit on above changes	**(50)**	(22)	**(5)**	5
Change in pension and postretirement unrecognized periodic benefit	**7**	15	**13**	18
Deferred income tax benefit (expense) on above changes	**(5)**	(1)	**(3)**	(2)
Other comprehensive income (loss)	**(2,632)**	(1,667)	**(8,546)**	(923)
Comprehensive income (loss)	**$ (7,989)**	$ 2,610	**$(21,708)**	$ 7,484

See Accompanying Notes to Consolidated Financial Statements.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited)*

1. Summary of Significant Accounting Policies

Basis of Presentation

These unaudited condensed consolidated financial statements do not include all disclosures required by accounting principles generally accepted in the United States (GAAP) for complete financial statements and should be read in conjunction with the audited consolidated financial statements and the related notes included in the Annual Report on Form 10-K of American International Group, Inc. (AIG) for the year ended December 31, 2007 (2007 Annual Report on Form 10-K).

In the opinion of management, these consolidated financial statements contain the normal recurring adjustments necessary for a fair statement of the results presented herein. All material intercompany accounts and transactions have been eliminated.

Changes in Presentation

In the second quarter of 2008, AIG determined that certain accident and health contracts in its Foreign General Insurance reporting unit, which were previously accounted for as short duration contracts, should be treated as long duration insurance products. Accordingly, the December 31, 2007 consolidated balance sheet has been revised to reflect the reclassification of $763 million of deferred direct response advertising costs, previously reported in other assets, to deferred policy acquisition costs. Additionally, $320 million has been reclassified on the consolidated balance sheet as of December 31, 2007 from unearned premiums to future policy benefits for life and accident and health insurance contracts. These revisions did not have a material effect on AIG's consolidated income before income taxes, net income, or shareholders' equity for any period presented.

In addition, see Recent Accounting Standards — Accounting Changes, below for a discussion of AIG's adoption of FASB Staff Position (FSP) No. FIN 39-1, "Amendment of FASB Interpretation No. 39" (FSP FIN 39-1).

Additionally, certain other reclassifications and format changes have been made to prior period amounts to conform to the current period presentation.

Recent Accounting Standards

Accounting Changes

FAS 157

In September 2006, the Financial Accounting Standards Board (FASB) issued Statement of Financial Accounting Standards (FAS) No. 157, "Fair Value Measurements" (FAS 157). FAS 157 defines fair value, establishes a framework for measuring fair value and expands disclosure requirements regarding fair value measurements but does not change existing guidance about whether an asset or liability is carried at fair value. FAS 157 nullifies the guidance in Emerging Issues Task Force (EITF) Issue No. 02-3, "Issues Involved in Accounting for Derivative Contracts Held for Trading Purposes and Contracts Involved in Energy Trading and Risk Management Activities," (EITF 02-3) that precluded the recognition of a trading profit at the inception of a derivative contract unless the fair value of such contract was obtained from a quoted market price or other valuation technique incorporating observable market data. FAS 157 also clarifies that an issuer's credit standing should be considered when measuring liabilities at fair value. The fair value measurement and related disclosure guidance in FAS 157 do not apply to fair value measurements associated with AIG's share-based employee compensation awards accounted for in accordance with FAS 123(R), "Share-Based Payment."

AIG adopted FAS 157 on January 1, 2008, its required effective date. FAS 157 must be applied prospectively, except for certain stand-alone derivatives and hybrid instruments initially measured using the guidance in EITF 02-3, which must be applied as a cumulative effect accounting change to retained earnings at January 1, 2008. The cumulative effect, net of taxes, of adopting FAS 157 on AIG's consolidated balance sheet was an increase in retained earnings of $4 million.

The most significant effect of adopting FAS 157 on AIG's consolidated results of operations for the three- and six-month periods ended June 30, 2008 related to changes in fair value methodologies with respect to both liabilities already carried at fair value, primarily hybrid notes and derivatives, and newly elected liabilities measured at fair value (see FAS 159 discussion below). Specifically, the incorporation of AIG's own credit spreads and the incorporation of explicit risk margins (embedded policy derivatives at transition only) resulted in a decrease in pre-tax income of $149 million ($97 million after tax) and an increase in pre-tax income of $2.6 billion ($1.7 billion after tax) for the three- and six-month periods ended June 30, 2008, respectively. The effect of the changes in AIG's own credit spreads was a decrease in pre-tax income of $112 million and an increase of $2.5 billion for the three- and six-month periods ended June 30, 2008, respectively. The effect of the changes in counterparty credit spreads for assets measured at fair value at AIG Financial Products Corp. and AIG Trading Group Inc. and their respective subsidiaries (AIGFP) was decreases of $362 million and $3.0 billion for the three- and six-month periods ended June 30, 2008, respectively.

See Note 3 to the Consolidated Financial Statements for additional FAS 157 disclosures.

FAS 159

In February 2007, the FASB issued FAS 159, "The Fair Value Option for Financial Assets and Financial Liabilities" (FAS 159). FAS 159 permits entities to choose to measure at

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

1. Summary of Significant Accounting Policies *(continued)*

fair value many financial instruments and certain other items that are not required to be measured at fair value. Subsequent changes in fair value for designated items are required to be reported in income. FAS 159 also establishes presentation and disclosure requirements for similar types of assets and liabilities measured at fair value. FAS 159 permits the fair value option election on an instrument-by-instrument basis for eligible items existing at the adoption date and at initial recognition of an asset or liability, or upon most events that give rise to a new basis of accounting for that instrument.

AIG adopted FAS 159 on January 1, 2008, its required effective date. The adoption of FAS 159 with respect to elections made in the Life Insurance & Retirement Services segment resulted in an after-tax decrease to 2008 opening retained earnings of $559 million. The adoption of FAS 159 with respect to elections made by AIGFP resulted in an after-tax decrease to 2008 opening retained earnings of $448 million. Included in this amount are net unrealized gains of $105 million that were reclassified to retained earnings from accumulated other comprehensive income (loss) related to available for sale securities recorded on the consolidated balance sheet at January 1, 2008 for which the fair value option was elected.

See Note 3 to the Consolidated Financial Statements for additional FAS 159 disclosures.

FAS 157 and FAS 159

The following table summarizes the after-tax increase (decrease) from adopting FAS 157 and FAS 159 on the opening shareholders' equity accounts at January 1, 2008:

	At January 1, 2008		
(in millions)	Accumulated Other Comprehensive Income/(Loss)	Retained Earnings	Cumulative Effect of Accounting Changes
FAS 157	$ —	$ 4	$ 4
FAS 159	(105)	(1,007)	(1,112)
Cumulative effect of accounting changes	$(105)	$(1,003)	$(1,108)

FSP FIN 39-1

In April 2007, the FASB directed the FASB Staff to issue FSP FIN 39-1. FSP FIN 39-1 modifies FIN No. 39, "Offsetting of Amounts Related to Certain Contracts," and permits companies to offset cash collateral receivables or payables against derivative instruments under certain circumstances. AIG adopted the provisions of FSP FIN 39-1 effective January 1, 2008, which requires retrospective application to all prior periods presented. At June 30, 2008, the amounts of cash collateral received and paid that were offset against net derivative positions totaled $7.3 billion and $12.3 billion, respectively. The cash collateral received and paid related to AIGFP derivative instruments were previously recorded in trade payables and trade receivables. Cash collateral received related to non-AIGFP derivative instruments was previously recorded in other liabilities. Accordingly, the derivative assets and liabilities at December 31, 2007 have been reduced by $6.3 billion and $5.8 billion, respectively, related to the netting of cash collateral.

Future Application of Accounting Standards

FAS 141(R)

In December 2007, the FASB issued FAS 141 (revised 2007), "Business Combinations" (FAS 141(R)). FAS 141(R) changes the accounting for business combinations in a number of ways, including broadening the transactions or events that are considered business combinations; requiring an acquirer to recognize 100 percent of the fair value of assets acquired, liabilities assumed, and noncontrolling (i.e., minority) interests; recognizing contingent consideration arrangements at their acquisition-date fair values with subsequent changes in fair value generally reflected in income; and recognizing preacquisition loss and gain contingencies at their acquisition-date fair values, among other changes.

AIG is required to adopt FAS 141(R) for business combinations for which the acquisition date is on or after January 1, 2009. Early adoption is prohibited.

FAS 160

In December 2007, the FASB issued FAS 160, "Noncontrolling Interests in Consolidated Financial Statements, an amendment of ARB No. 51" (FAS 160). FAS 160 requires noncontrolling (i.e., minority) interests in partially owned consolidated subsidiaries to be classified in the consolidated balance sheet as a separate component of consolidated shareholders' equity. FAS 160 also establishes accounting rules for subsequent acquisitions and sales of noncontrolling interests and provides for how noncontrolling interests should be presented in the consolidated statement of income. The noncontrolling interests' share of subsidiary income should be reported as a part of consolidated net income with disclosure of the attribution of consolidated net income to the controlling and noncontrolling interests on the face of the consolidated statement of income.

AIG is required to adopt FAS 160 on January 1, 2009 and early application is prohibited. FAS 160 must be adopted prospectively, except that noncontrolling interests should be reclassified from liabilities to a separate component of shareholders' equity and consolidated net income should be recast to include net income attributable to both the controlling and noncontrolling interests retrospectively. AIG is currently assessing the effect that adopting FAS 160 will have on its consolidated financial statements.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

1. Summary of Significant Accounting Policies *(continued)*

FAS 161

In March 2008, the FASB issued FAS 161, "Disclosures about Derivative Instruments and Hedging Activities – an amendment of FASB Statement No. 133" (FAS 161). FAS 161 requires enhanced disclosures about (a) how and why AIG uses derivative instruments, (b) how derivative instruments and related hedged items are accounted for under FAS No. 133, "Accounting for Derivative Instruments and Hedging Activities" (FAS 133), and its related interpretations, and (c) how derivative instruments and related hedged items affect AIG's consolidated financial condition, results of operations, and cash flows. FAS 161 is effective for AIG beginning with financial statements issued in the first quarter of 2009. Because FAS 161 only requires additional disclosures about derivatives, it will have no effect on AIG's consolidated financial condition, results of operations or cash flows.

FAS 162

In May 2008, the FASB issued FAS 162, "The Hierarchy of Generally Accepted Accounting Principles" (FAS 162). FAS 162 identifies the sources of accounting principles and the framework for selecting the principles to be used in the preparation of financial statements presented in conformity with GAAP but does not change current practices. FAS 162 will become effective on the 60th day following Securities and Exchange Commission (SEC) approval of the Public Company Accounting Oversight Board amendments to remove GAAP hierarchy from the auditing standards. FAS 162 will have no effect on AIG's consolidated financial condition, results of operations or cash flows.

FSP FAS 140-3

In February 2008, the FASB issued FSP FAS No. 140-3, "Accounting for Transfers of Financial Assets and Repurchase Financing Transactions" (FSP FAS 140-3). FSP FAS 140-3 requires an initial transfer of a financial asset and a repurchase financing that was entered into contemporaneously with or in contemplation of the initial transfer to be evaluated as a linked transaction unless certain criteria are met. FSP FAS 140-3 is effective for AIG beginning January 1, 2009 and will be applied to new transactions entered into from that date forward. Early adoption is prohibited. AIG is currently assessing the effect that adopting FSP FAS 140-3 will have on its consolidated financial statements but does not believe the effect will be material.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

2. Segment Information

AIG identifies its reportable segments by product line consistent with its management structure. These segments are General Insurance, Life Insurance & Retirement Services, Financial Services and Asset Management.

AIG's operations by major operating segment were as follows:

Operating Segments *(in millions)*	Three Months Ended June 30, **2008**	2007	Six Months Ended June 30, **2008**	2007
Total revenues[(a)]:				
General Insurance	**$ 12,757**	$12,928	**$ 25,046**	$25,831
Life Insurance & Retirement Services[(b)]	**10,161**	14,023	**18,913**	27,705
Financial Services[(c)(d)]	**(3,605)**	2,123	**(10,165)**	4,324
Asset Management[(e)]	**797**	1,781	**648**	3,450
Other	**208**	263	**80**	394
Consolidation and eliminations	**(385)**	32	**(558)**	91
Total	**$ 19,933**	$31,150	**$ 33,964**	$61,795
Operating income (loss)[(a)]:				
General Insurance	**$ 827**	$ 2,976	**$ 2,164**	$ 6,072
Life Insurance & Retirement Services[(b)]	**(2,401)**	2,620	**(4,232)**	4,901
Financial Services[(c)(d)]	**(5,905)**	47	**(14,677)**	339
Asset Management[(e)]	**(314)**	927	**(1,565)**	1,685
Other[(f)]	**(715)**	(460)	**(1,483)**	(930)
Consolidation and eliminations	**(248)**	218	**(227)**	433
Total	**$ (8,756)**	$ 6,328	**$ (20,020)**	$12,500

(a) Includes other-than-temporary impairment charges of $6.8 billion and $417 million for the three-month periods ended June 30, 2008 and 2007, respectively, and $12.4 billion and $884 million for the six-month periods ended June 30, 2008 and 2007, respectively. Also includes gains (losses) from hedging activities that did not qualify for hedge accounting treatment under FAS 133, including the related foreign exchange gains and losses. For the three-month periods ended June 30, 2008 and 2007, the effect was $272 million and $(430) million, respectively. For the six-month periods ended June 30, 2008 and 2007, the effect was $(476) million and $(882) million, respectively. These amounts result primarily from interest rate and foreign currency derivatives that are effective economic hedges of investments and borrowings.

(b) Includes other-than-temporary impairment charges of $5.2 billion and $324 million for the three-month periods ended June 30, 2008 and 2007, respectively, and $9.6 billion and $716 million for the six-month periods ended June 30, 2008 and 2007, respectively.

(c) Includes gains (losses) from hedging activities that did not qualify for hedge accounting treatment under FAS 133, including the related foreign exchange gains and losses. For the three-month periods ended June 30, 2008 and 2007, the effect was $5 million and $(443) million, respectively. For the six-month periods ended June 30, 2008 and 2007, the effect was $(199) million and $(603) million, respectively. These amounts result primarily from interest rate and foreign currency derivatives that are effective economic hedges of investments and borrowings.

(d) For the three- and six-month periods ended June 30, 2008, includes unrealized market valuation losses of $5.6 billion and $14.7 billion, respectively, on AIGFP's super senior credit default swap portfolio.

(e) Includes net realized capital losses of $464 million and $1.9 billion for the three- and six-month periods ended June 30, 2008, respectively, including other-than-temporary impairment charges of $882 million and $1.9 billion, respectively.

(f) Includes AIG parent and other operations that are not required to be reported separately. The following table presents the operating loss for AIG's Other category:

Other *(in millions)*	Three Months Ended June 30, **2008**	2007	Six Months Ended June 30, **2008**	2007
Operating income (loss):				
Equity earnings in partially owned companies	**$ 8**	$ 50	**$ 16**	$ 91
Interest expense	**(452)**	(302)	**(820)**	(554)
Unallocated corporate expenses[(a)]	**(282)**	(210)	**(375)**	(382)
Net realized capital gains (losses)[(b)]	**30**	22	**(235)**	(27)
Other miscellaneous, net	**(19)**	(20)	**(69)**	(58)
Total Other	**$ (715)**	$(460)	**$ (1,483)**	$(930)

(a) Includes expenses of corporate staff not attributable to specific operating segments, expenses related to efforts to improve internal controls, corporate initiatives and certain compensation plan expenses. For the three- and six-month periods ended June 30, 2008, includes a charge of $101 million as a result of the settlement of a dispute in connection with the July 2008 purchase of the balance of Ascot Underwriting Holdings Ltd., partially offset by a decrease in certain compensation plan expenses.

(b) The increase in net realized capital losses in the six-month period ended June 30, 2008 reflected higher foreign exchange losses on foreign-denominated debt, a portion of which was economically hedged but did not qualify for hedge accounting treatment under FAS 133, and losses on non-hedged derivatives.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

2. Segment Information *(continued)*

AIG's General Insurance operations by major internal reporting unit were as follows:

General Insurance *(in millions)*	Three Months Ended June 30, 2008	Three Months Ended June 30, 2007	Six Months Ended June 30, 2008	Six Months Ended June 30, 2007
Total revenues:				
Commercial Insurance	**$ 5,937**	$ 6,904	**$ 11,924**	$13,995
Transatlantic	**1,103**	1,069	**2,222**	2,165
Personal Lines	**1,259**	1,223	**2,511**	2,436
Mortgage Guaranty	**313**	257	**611**	505
Foreign General Insurance	**4,139**	3,475	**7,767**	6,737
Reclassifications and eliminations	**6**	—	**11**	(7)
Total	**$ 12,757**	$12,928	**$ 25,046**	$25,831
Operating income (loss):				
Commercial Insurance	**$ 381**	$ 1,904	**$ 1,166**	$ 3,833
Transatlantic	**141**	168	**303**	319
Personal Lines	**21**	118	**24**	224
Mortgage Guaranty	**(518)**	(81)	**(872)**	(73)
Foreign General Insurance	**796**	867	**1,532**	1,776
Reclassifications and eliminations	**6**	—	**11**	(7)
Total	**$ 827**	$ 2,976	**$ 2,164**	$ 6,072

AIG's Life Insurance & Retirement Services operations by major internal reporting unit were as follows:

Life Insurance & Retirement Services *(in millions)*	Three Months Ended June 30, 2008	Three Months Ended June 30, 2007	Six Months Ended June 30, 2008	Six Months Ended June 30, 2007
Total revenues:				
Foreign:				
Japan and Other	**$ 5,369**	$ 4,863	**$ 9,265**	$ 9,633
Asia	**4,575**	5,019	**8,852**	9,510
Domestic:				
Domestic Life Insurance	**1,234**	2,359	**2,517**	4,880
Domestic Retirement Services	**(1,017)**	1,782	**(1,721)**	3,682
Total	**$ 10,161**	$14,023	**$ 18,913**	$27,705
Operating income (loss):				
Foreign:				
Japan and Other	**$ 577**	$ 810	**$ 1,060**	$ 1,723
Asia	**196**	844	**448**	1,215
Domestic:				
Domestic Life Insurance	**(1,005)**	368	**(1,875)**	713
Domestic Retirement Services	**(2,169)**	598	**(3,865)**	1,250
Total	**$ (2,401)**	$ 2,620	**$ (4,232)**	$ 4,901

AIG's Financial Services operations by major internal reporting unit were as follows:

Financial Services *(in millions)*	Three Months Ended June 30, 2008	Three Months Ended June 30, 2007	Six Months Ended June 30, 2008	Six Months Ended June 30, 2007
Total revenues:				
Aircraft Leasing	**$ 1,298**	$1,173	**$ 2,463**	$2,231
Capital Markets[(a)]	**(6,088)**	(67)	**(14,831)**	161
Consumer Finance[(b)]	**1,028**	911	**1,959**	1,756
Other, including intercompany adjustments	**157**	106	**244**	176
Total	**$ (3,605)**	$2,123	**$ (10,165)**	$4,324
Operating income (loss):				
Aircraft Leasing	**$ 334**	$ 207	**$ 555**	$ 371
Capital Markets[(a)]	**(6,284)**	(255)	**(15,211)**	(187)
Consumer Finance[(b)]	**(33)**	75	**(85)**	111
Other, including intercompany adjustments	**78**	20	**64**	44
Total	**$ (5,905)**	$ 47	**$ (14,677)**	$ 339

(a) Revenues are shown net of interest expense of $1.2 billion and $805 million in the three-month periods ended June 30, 2008 and 2007, respectively, and $1.7 billion and $1.9 billion for the six-month periods ended June 30, 2008 and 2007, respectively. In the three- and six-month periods ended June 30, 2008, both revenues and operating income (loss) includes unrealized market valuation losses of $5.6 billion and $14.7 billion, respectively, on AIGFP's super senior credit default swap portfolio.

(b) The three- and six-month periods ended June 30, 2007 included pre-tax charges of $50 million and $178 million, respectively, in connection with domestic Consumer Finance's mortgage banking activities. Based on a current evaluation of the estimated cost of implementing the Supervisory Agreement entered into with the Office of Thrift Supervision (OTS), partial reversals of these prior year charges of $25 million and $43 million, respectively, are included in the three- and six-month periods ended June 30, 2008.

AIG's Asset Management operations consist of a single internal reporting unit.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

3. Fair Value Measurements

Effective January 1, 2008 AIG adopted FAS 157 and FAS 159, which specify measurement and disclosure standards related to assets and liabilities measured at fair value. See Note 1 to the Consolidated Financial Statements for additional information.

The most significant effect of adopting FAS 157 on AIG's results of operations for the three- and six-month periods ended June 30, 2008 related to changes in fair value methodologies with respect to both liabilities already carried at fair value, primarily hybrid notes and derivatives, and newly elected liabilities measured at fair value (see FAS 159 discussion below). Specifically, the incorporation of AIG's own credit spreads and the incorporation of explicit risk margins (embedded policy derivatives at transition only) resulted in a decrease of $149 million to pre-tax income ($97 million after tax) and an increase of $2.6 billion to pre-tax income ($1.7 billion after tax) for the three- and six-month periods ended June 30, 2008, respectively, as follows:

	Net Pre-Tax Increase (Decrease)			
(in millions)	Three Months Ended June 30, 2008	Six Months Ended June 30, 2008	Liabilities Carried at Fair Value	Business Segment Affected
Income statement caption:				
Net realized capital gains (losses)	**$ (37)**	**$ 251**	Freestanding derivatives	All segments - excluding AIGFP
	—	**(155)**	Embedded policy derivatives	Life Insurance & Retirement Services
Unrealized market valuation losses on AIGFP super senior credit default swap portfolio	**44***	**109***	Super senior credit default swap portfolio	AIGFP
Other income	**(156)***	**2,427***	Notes, GIAs, derivatives, other liabilities	AIGFP
Net pre-tax increase	**$ (149)**	**$2,632**		
Liabilities already carried at fair value	**$ 20**	**$1,354**		
Newly elected liabilities measured at fair value (FAS 159 elected)	**(169)**	**1,278**		
Net pre-tax increase	**$ (149)**	**$2,632**		

* *The effect of changes in AIG's own credit spreads on pre-tax income for AIGFP was a decrease of $112 million and an increase of $2.5 billion for the three- and six-month periods ended June 30, 2008, respectively. The effect of the changes in counterparty credit spreads for assets measured at fair value at AIGFP was decreases in pre-tax income of $362 million and $3.0 billion for the three- and six-month periods ended June 30, 2008, respectively.*

Fair Value Measurements on a Recurring Basis

AIG measures at fair value on a recurring basis financial instruments in its trading and available for sale securities portfolios, certain mortgage and other loans receivable, certain spot commodities, derivative assets and liabilities, securities purchased (sold) under agreements to resell (repurchase), securities lending invested collateral, non-traded equity investments and certain private limited partnership and certain hedge funds included in other invested assets, certain short-term investments, separate and variable account assets, certain policyholders' contract deposits, securities and spot commodities sold but not yet purchased, certain trust deposits and deposits due to banks and other depositors, certain long-term borrowings, and certain hybrid financial instruments included in other liabilities. The fair value of a financial instrument is the amount that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date.

The degree of judgment used in measuring the fair value of financial instruments generally correlates with the level of pricing observability. Financial instruments with quoted prices in active markets generally have more pricing observability and less judgment is used in measuring fair value. Conversely, financial instruments traded in other-than-active markets or that do not have quoted prices have less observability and are measured at fair value using valuation models or other pricing techniques that require more judgment. Pricing observability is affected by a number of factors, including the type of financial instrument, whether the financial instrument is new to the market and not yet established, the characteristics specific to the transaction and general market conditions.

Fixed Maturity Securities — Trading and Available for Sale

AIG maximizes the use of observable inputs and minimizes the use of unobservable inputs when measuring fair value. Whenever available, AIG obtains quoted prices in active markets for identical assets at the balance sheet date to measure at fair value fixed maturity securities in its trading and available for sale portfolios. Market price data generally is obtained from exchange or dealer markets.

AIG estimates the fair value of fixed maturity securities not traded in active markets, including securities purchased (sold) under agreements to resell (repurchase), and mortgage and other loans receivable for which AIG elected the fair value option, by referring to traded securities with similar attributes, using dealer quotations, a matrix pricing methodology, discounted cash flow analyses or internal valuation models. This methodology considers such factors as the issuer's industry, the security's rating and tenor, its coupon rate, its position in the capital structure of the issuer, yield curves, credit curves, prepayment rates and other relevant factors. For fixed maturity instruments that are not traded in active markets or that are subject to transfer restrictions, valuations are adjusted to reflect illiquidity and/or non-transferability, and such adjustments generally are based on avail-

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

3. Fair Value Measurements *(continued)*

able market evidence. In the absence of such evidence, management's best estimate is used.

Equity Securities Traded in Active Markets — Trading and Available for Sale

AIG maximizes the use of observable inputs and minimizes the use of unobservable inputs when measuring fair value. Whenever available, AIG obtains quoted prices in active markets for identical assets at the balance sheet date to measure at fair value marketable equity securities in its trading and available for sale portfolios. Market price data generally is obtained from exchange or dealer markets.

Non-Traded Equity Investments — Other Invested Assets

AIG initially estimates the fair value of equity instruments not traded in active markets by reference to the transaction price. This valuation is adjusted only when changes to inputs and assumptions are corroborated by evidence such as transactions in similar instruments, completed or pending third-party transactions in the underlying investment or comparable entities, subsequent rounds of financing, recapitalizations and other transactions across the capital structure, offerings in the equity capital markets, and changes in financial ratios or cash flows. For equity securities that are not traded in active markets or that are subject to transfer restrictions, valuations are adjusted to reflect illiquidity and/or non-transferability and such adjustments generally are based on available market evidence. In the absence of such evidence, management's best estimate is used.

Private Limited Partnership and Hedge Fund Investments — Other Invested Assets

AIG initially estimates the fair value of investments in certain private limited partnerships and certain hedge funds by reference to the transaction price. Subsequently, AIG obtains the fair value of these investments generally from net asset value information provided by the general partner or manager of the investments, the financial statements of which generally are audited annually.

Separate and Variable Account Assets

Separate and variable account assets are composed primarily of registered and unregistered open-end mutual funds that generally trade daily and are measured at fair value in the manner discussed above for equity securities traded in active markets.

Freestanding Derivatives

Derivative assets and liabilities can be exchange-traded or traded over the counter (OTC). AIG generally values exchange-traded derivatives using quoted prices in active markets for identical derivatives at the balance sheet date.

OTC derivatives are valued using market transactions and other market evidence whenever possible, including market-based inputs to models, model calibration to market clearing transactions, broker or dealer quotations or alternative pricing sources with reasonable levels of price transparency. When models are used, the selection of a particular model to value an OTC derivative depends on the contractual terms of, and specific risks inherent in, the instrument as well as the availability of pricing information in the market. AIG generally uses similar models to value similar instruments. Valuation models require a variety of inputs, including contractual terms, market prices and rates, yield curves, credit curves, measures of volatility, prepayment rates and correlations of such inputs. For OTC derivatives that trade in liquid markets, such as generic forwards, swaps and options, model inputs can generally be corroborated by observable market data by correlation or other means, and model selection does not involve significant management judgment.

Certain OTC derivatives trade in less liquid markets with limited pricing information, and the determination of fair value for these derivatives is inherently more difficult. When AIG does not have corroborating market evidence to support significant model inputs and cannot verify the model to market transactions, the transaction price is initially used as the best estimate of fair value. Accordingly, when a pricing model is used to value such an instrument, the model is adjusted so the model value at inception equals the transaction price. Subsequent to initial recognition, AIG updates valuation inputs when corroborated by evidence such as similar market transactions, third-party pricing services and/or broker or dealer quotations, or other empirical market data. When appropriate, valuations are adjusted for various factors such as liquidity, bid/offer spreads and credit considerations. Such adjustments are generally based on available market evidence. In the absence of such evidence, management's best estimate is used.

With the adoption of FAS 157 on January 1, 2008, AIG's own credit risk has been considered and is incorporated into the fair value measurement of all freestanding derivative liabilities.

Embedded Policy Derivatives

The fair value of embedded policy derivatives contained in certain variable annuity and equity-indexed annuity and life contracts is measured based on actuarial and capital market assumptions related to projected cash flows over the expected lives of the contracts. These cash flow estimates primarily include benefits and related fees assessed, when applicable, and incorporate expectations about policyholder behavior. Estimates of future policyholder behavior are subjective and based primarily on AIG's historical experience. With respect to embedded policy derivatives in AIG's variable annuity contracts, because of the dynamic and complex nature of the

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

3. Fair Value Measurements *(continued)*

expected cash flows, risk neutral valuations are used. Estimating the underlying cash flows for these products involves many estimates and judgments, including those regarding expected market rates of return, market volatility, correlations of market index returns to funds, fund performance, discount rates and policyholder behavior. With respect to embedded policy derivatives in AIG's equity-indexed annuity and life contracts, option pricing models are used to estimate fair value, taking into account assumptions for future equity index growth rates, volatility of the equity index, future interest rates, and determinations on adjusting the participation rate and the cap on equity indexed credited rates in light of market conditions and policyholder behavior assumptions. With the adoption of FAS 157, these methodologies were not changed, with the exception of incorporating an explicit risk margin to take into consideration market participant estimates of projected cash flows and policyholder behavior.

AIGFP's Super Senior Credit Default Swap Portfolio

AIGFP values its credit default swaps written on the most senior risk layers (super senior) of designated pools of debt securities or loans using internal valuation models, third-party prices and market indices. The specific valuation methodologies vary based on the nature of the referenced obligations and availability of market prices. AIGFP uses a modified version of the Binomial Expansion Technique (BET) model to value its credit default swap portfolio written on super senior tranches of collateralized debt obligations (CDOs) of asset-backed securities (ABS), including maturity-shortening puts that allow the holders of the securities issued by certain CDOs to treat the securities as short-term eligible 2a-7 investments under the Investment Company Act of 1940 (2a-7 Puts). The BET model uses default probabilities derived from credit spreads implied from prices for the individual securities included in the underlying collateral pools securing the CDOs, as well as diversity scores, weighted average lives, recovery rates and discount rates. Prices for the individual securities held by a CDO are obtained in most cases from the CDO collateral managers, to the extent available. The CDO collateral managers obtain these prices from various sources, which include dealer quotations, third party pricing services and in-house valuation models. To the extent there is a lag in the prices provided by the collateral managers, AIGFP rolls forward these prices to the end of the quarter using data provided by a third-party pricing service. Where a price for an individual security is not provided by the CDO collateral manager, AIGFP derives the price from a matrix that averages the prices of the various securities at the level of ABS category, vintage and the rating of the reference security. The determination of some of these inputs requires the use of judgment and estimates, particularly in the absence of market observable data. AIGFP also employs a Monte Carlo simulation to assist in quantifying the effect on the valuation of the CDOs of the unique aspects of the CDOs' structures such as triggers that divert cash flows to the most senior part of the capital structure. In the determination of fair value, AIGFP also considers prices from collateral calls by counterparties to these transactions and the price estimates for the super senior CDO securities provided by third parties.

In the case of credit default swaps written on investment-grade corporate debt and collateralized loan obligations (CLOs), AIGFP estimates the value of its obligations by reference to the relevant market indices or third-party quotes on the underlying super senior tranches when available.

In the case of credit default swaps written to facilitate regulatory capital relief for AIGFP's European financial institution counterparties, AIGFP estimates the fair value of these derivatives by considering observable market transactions, including the early termination of these transactions by counterparties, and other market data, to the extent relevant.

Policyholders' Contract Deposits

Policyholders' contract deposits accounted for at fair value beginning January 1, 2008 are measured using an income approach by taking into consideration the following factors:

- Current policyholder account values and related surrender charges,
- The present value of estimated future cash inflows (policy fees) and outflows (benefits and maintenance expenses) associated with the product using risk neutral valuations, incorporating expectations about policyholder behavior, market returns and other factors, and
- A risk margin that market participants would require for a market return and the uncertainty inherent in the model inputs.

The change in fair value of these policyholders' contract deposits is recorded as incurred policy losses and benefits in the consolidated statement of income (loss).

Fair Value Measurements on a Non-Recurring Basis

AIG also measures the fair value of certain assets on a non-recurring basis, generally quarterly, annually, or when events or changes in circumstances indicate that the carrying amount of the asset may not be recoverable. These assets include held to maturity securities, cost and equity-method investments, life settlement contracts, flight equipment, collateral securing foreclosed loans and real estate and other fixed assets, goodwill, and other intangible assets. AIG uses a variety of techniques to measure the fair value of these assets when appropriate, as described below:

- *Held to Maturity Securities, Cost and Equity-Method Investments:* When AIG determines the carrying value of these assets may not be recoverable, AIG records the assets

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

3. Fair Value Measurements *(continued)*

at fair value with the loss recognized in income. In such cases, AIG measures the fair value of these assets using the techniques discussed above for fixed maturities and equity securities.

- *Life Settlement Contracts:* AIG measures the fair value of individual life settlement contracts (which are included in other invested assets) whenever the carrying value plus the undiscounted future costs that are expected to be incurred to keep the life settlement contract in force exceed the expected proceeds from the contract. In those situations, the fair value is determined on a discounted cash flows basis, incorporating current life expectancy assumptions. The discount rate incorporates current information about market interest rates, the credit exposure to the insurance company that issued the life settlement contract and AIG's estimate of the risk margin an investor in the contracts would require.
- *Flight Equipment Primarily Under Operating Leases:* When AIG determines the carrying value of its commercial aircraft may not be recoverable, AIG records the aircraft at fair value with the loss recognized in income. AIG measures the fair value of its commercial aircraft using an income approach based on the present value of all cash flows from existing and projected lease payments (based on historical experience and current expectations of market participants) including net contingent rentals for the period extending to the end of the aircraft's economic life in its highest and best use configuration, plus its disposition value.
- *Collateral Securing Foreclosed Loans and Real Estate and Other Fixed Assets:* When AIG takes collateral in connection with foreclosed loans, AIG generally bases its estimate of fair value on the price that would be received in a current transaction to sell the asset by itself.
- *Goodwill:* AIG tests goodwill for impairment whenever events or changes in circumstances indicate the carrying amount of goodwill may not be recoverable, but at least annually. When AIG determines goodwill may be impaired, AIG uses techniques that consider market-based earnings multiples of the unit's peer companies or discounted cash flow techniques based on the price that could be received in a current transaction to sell the asset assuming the asset would be used with other assets as a group (in-use premise).
- *Intangible Assets:* AIG tests its intangible assets for impairment whenever events or changes in circumstances indicate the carrying amount of an intangible asset may not be recoverable. AIG measures the fair value of intangible assets based on an in-use premise that considers the same factors used to estimate the fair value of its real estate and other fixed assets under an in-use premise discussed above.

See Notes 1(c), (d), (e), (t), and (v) to Consolidated Financial Statements included in the 2007 Annual Report on Form 10-K for additional information about how AIG tests various asset classes for impairment.

Fair Value Hierarchy

Beginning January 1, 2008, assets and liabilities recorded at fair value in the consolidated balance sheet are measured and classified in a hierarchy for disclosure purposes consisting of three "levels" based on the observability of inputs available in the marketplace used to measure the fair values as discussed below:

- *Level 1:* Fair value measurements that are quoted prices (unadjusted) in active markets that AIG has the ability to access for identical assets or liabilities. Market price data generally is obtained from exchange or dealer markets. AIG does not adjust the quoted price for such instruments. Assets and liabilities measured at fair value on a recurring basis and classified as Level 1 include certain government and agency securities, actively traded listed common stocks and derivative contracts, most separate account assets and most mutual funds.
- *Level 2:* Fair value measurements based on inputs other than quoted prices included in Level 1 that are observable for the asset or liability, either directly or indirectly. Level 2 inputs include quoted prices for similar assets and liabilities in active markets, and inputs other than quoted prices that are observable for the asset or liability, such as interest rates and yield curves that are observable at commonly quoted intervals. Assets and liabilities measured at fair value on a recurring basis and classified as Level 2 generally include certain government securities, most investment-grade and high-yield corporate bonds, certain asset-backed securities, certain listed equities, state, municipal and provincial obligations, hybrid securities, mutual fund and hedge fund investments, derivative contracts, guaranteed investment agreements at AIGFP and physical commodities.
- *Level 3:* Fair value measurements based on valuation techniques that use significant inputs that are unobservable. These measurements include circumstances in which there is little, if any, market activity for the asset or liability. In certain cases, the inputs used to measure fair value may fall into different levels of the fair value hierarchy. In such cases, the level in the fair value hierarchy within which the fair value measurement in its entirety falls is determined based on the lowest level input that is significant to the fair value measurement in its entirety. AIG's assessment of the significance of a particular input to the fair value measurement in its entirety requires judgment. In

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

3. Fair Value Measurements *(continued)*

making the assessment, AIG considers factors specific to the asset or liability. Assets and liabilities measured at fair value on a recurring basis and classified as Level 3 include certain distressed ABS, structured credit products, certain derivative contracts (including AIGFP's super senior credit default swap portfolio), policyholders' contract deposits carried at fair value, private equity and real estate fund investments, and direct private equity investments. AIG's non-financial-instrument assets that are measured at fair value on a non-recurring basis generally are classified as Level 3.

Assets and Liabilities Measured at Fair Value on a Recurring Basis

The following table presents information about assets and liabilities measured at fair value on a recurring basis at June 30, 2008, and indicates the level of the fair value measurement based on the levels of the inputs used:

(in millions)	Level 1	Level 2	Level 3	Counterparty Netting	Total June 30, 2008
Assets:					
Bonds available for sale	$ 3,986	$370,850	$18,480	$ –	$393,316
Bond trading securities	1	8,605	195	–	8,801
Common stocks available for sale	16,812	267	227	–	17,306
Common and preferred stocks trading	21,510	999	5	–	22,514
Preferred stocks available for sale	–	2,238	258	–	2,496
Mortgage and other loans receivable	–	741	4	–	745
Financial Services assets:					
Securities available for sale	2	831	372	–	1,205
Trading securities	1,276	30,214	3,680	–	35,170
Spot commodities	–	90	–	–	90
Unrealized gain on swaps, options and forward transactions	–	59,493	3,625	(51,570)	11,548
Securities purchased under agreements to resell	–	16,597	–	–	16,597
Securities lending invested collateral[(a)]	–	40,595	8,489	–	49,084
Other invested assets[(b)]	2,643	7,588	11,868	–	22,099
Short-term investments[(c)]	39	24,128	–	–	24,167
Separate and variable accounts	69,162	3,061	1,178	–	73,401
Other assets	94	4,611	353	(2,606)	2,452
Total	$115,525	$570,908	$48,734	$(54,176)	$680,991
Liabilities:					
Policyholders' contract deposits	$ –	$ –	$ 4,179	$ –	$ 4,179
Other policyholders' funds	2	–	–	–	2
Financial Services liabilities:					
Securities sold under agreements to repurchase	–	8,298	40	–	8,338
Securities and spot commodities sold but not yet purchased	94	3,095	–	–	3,189
Unrealized loss on swaps, options and forward transactions[(d)]	–	52,897	30,299	(58,964)	24,232
Trust deposits and deposits due to banks and other depositors	–	240	–	–	240
Long-term borrowings	–	51,150	2,689	–	53,839
Other liabilities	6	7,005	44	(194)	6,861
Total	$ 102	$122,685	$37,251	$(59,158)	$100,880

(a) Amounts exclude short-term investments that are carried at cost, which approximates fair value of $10.4 billion.

(b) Approximately 13 percent of the fair value of the assets recorded as Level 3 relates to various private equity, real estate, hedge fund and fund-of-funds investments. AIG's ownership in these funds represented 22 percent, or $1.4 billion of the Level 3 amount.

(c) Level 2 includes short-term investments that are carried at cost, which approximates fair value of $23.1 billion.

(d) Included in Level 3 are unrealized market valuation losses of $26.1 billion on AIGFP super senior credit default swap portfolio.

At June 30, 2008, Level 3 assets totaled $48.7 billion, representing 4.7 percent of total assets, and Level 3 liabilities totaled $37.3 billion, representing 3.8 percent of total liabilities.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

3. Fair Value Measurements *(continued)*

The following tables present changes during the three- and six-month periods ended June 30, 2008 in Level 3 assets and liabilities measured at fair value on a recurring basis, and the realized and unrealized gains (losses) recorded in income during the three- and six-month periods ended June 30, 2008 related to the Level 3 assets and liabilities that remained on the consolidated balance sheet at June 30, 2008:

(in millions)	Balance Beginning of Period[(a)]	Net Realized and Unrealized Gains (Losses) Included in Income[(b)]	Accumulated Other Comprehensive Income (Loss)	Purchases, Sales, Issuances and Settlements-net	Transfers In (Out)	Balance at June 30, 2008	Changes in Unrealized Gains (Losses) on Instruments Held at June 30, 2008
Three Months Ended June 30, 2008:							
Assets:							
Bonds available for sale	$ 17,198	$ (679)	$ (58)	$ (34)	$2,053	$ 18,480	$ –
Bond trading securities	116	5	2	15	57	195	7
Common stocks available for sale	251	(3)	(3)	(15)	(3)	227	–
Common and preferred stocks trading	25	(1)	1	(13)	(7)	5	–
Preferred stocks available for sale	133	(3)	8	(59)	179	258	–
Mortgage and other loans receivable	–	–	–	–	4	4	–
Financial Services assets:							
Securities available for sale	294	(3)	2	77	2	372	–
Trading securities	3,419	(472)	–	713	20	3,680	(361)
Securities lending invested collateral	9,622	(1,346)	908	(590)	(105)	8,489	–
Other invested assets	11,348	(153)	70	533	70	11,868	166
Separate and variable accounts	1,065	(3)	–	116	–	1,178	(4)
Other assets	337	(6)	–	3	–	334	(6)
Total	$ 43,808	$ (2,664)	$ 930	$ 746	$2,270	$ 45,090	$ (198)
Liabilities:							
Policyholders' contract deposits	$ (4,118)	$ 129	$ 13	$ (203)	$ –	$ (4,179)	$ 62
Financial Services liabilities:							
Securities sold under agreements to repurchase	(220)	(3)	–	(39)	222	(40)	1
Unrealized loss on swaps, options and forward transactions, net	(20,860)	(5,679)	–	(240)	105	(26,674)	(5,496)
Long-term borrowings	(2,838)	(25)	–	182	(8)	(2,689)	(12)
Other liabilities	(74)	32	(1)	17	1	(25)	52
Total	$(28,110)	$ (5,546)	$ 12	$ (283)	$ 320	$(33,607)	$ (5,393)
Six Months Ended June 30, 2008:							
Assets:							
Bonds available for sale	$ 18,786	$ (1,444)	$ (550)	$ (224)	$1,912	$ 18,480	$ –
Bond trading securities	141	(20)	2	15	57	195	(10)
Common stocks available for sale	224	(5)	–	11	(3)	227	
Common and preferred stocks trading	30	(1)	2	(19)	(7)	5	–
Preferred stocks available for sale	135	(2)	6	(67)	186	258	–
Mortgage and other loans receivable	–	–	–	–	4	4	–
Financial Services assets:							
Securities available for sale	285	(3)	8	82	–	372	–
Trading securities	4,422	(1,433)	–	702	(11)	3,680	(1,233)
Securities lending invested collateral	11,353	(3,138)	1,087	(818)	5	8,489	–
Other invested assets	10,373	192	137	1,148	18	11,868	818
Separate and variable accounts	1,003	27	–	148	–	1,178	27
Other assets	141	–	–	193	–	334	–
Total	$ 46,893	$ (5,827)	$ 692	$ 1,171	$2,161	$ 45,090	$ (398)
Liabilities:							
Policyholders' contract deposits	$ (3,674)	$ (57)	$ (51)	$ (397)	$ –	$ (4,179)	$ (221)
Financial Services liabilities:							
Securities sold under agreements to repurchase	(208)	(20)	–	(34)	222	(40)	1
Unrealized loss on swaps, options and forward transactions, net	(11,718)	(14,562)	–	(429)	35	(26,674)	(14,693)
Long-term borrowings	(3,578)	90	–	638	161	(2,689)	–
Other liabilities	(503)	(55)	–	532	1	(25)	28
Total	$(19,681)	$(14,604)	$ (51)	$ 310	$ 419	$(33,607)	$ (14,885)

(a) Certain recharacterizations of amounts previously reported in Level 3 were identified in the second quarter of 2008, and have been adjusted. The effect of these reclassifications and recharacterizations on Level 3 net assets were net decreases of $1.8 billion and $1.0 billion at January 1, 2008 and March 31, 2008, respectively. The Consolidated Statement of Income, the Consolidated Balance Sheet, and the Consolidated Statement of Cash Flows presented in the 2008

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

3. Fair Value Measurements *(continued)*

first quarter Form 10-Q were not affected by these changes. Total Level 3 derivative exposures have been netted on these tables for presentation purposes only.

(b) Net realized and unrealized gains and losses shown above are reported on the consolidated statement of income (loss) primarily as follows:

Major category of Assets /Liabilities	Consolidated Statement of Income (Loss) Line Items
Financial Services assets and liabilities	• Other income • Unrealized market valuation losses on AIGFP super senior credit default swap portfolio
Other invested assets	• Net realized capital gains (losses)
Policyholders' contract deposits	• Incurred policy losses and benefits • Net realized capital gains (losses)

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

3. Fair Value Measurements *(continued)*

Both observable and unobservable inputs may be used to determine the fair values of positions classified in Level 3 in the tables above. As a result, the unrealized gains (losses) on instruments held at June 30, 2008 may include changes in fair value that were attributable to both observable (e.g., changes in market interest rates) and unobservable inputs (e.g., changes in unobservable long-dated volatilities).

AIG uses various hedging techniques to manage risks associated with certain positions, including those classified within Level 3. Such techniques may include the purchase or sale of financial instruments that are classified within Level 1 and/or Level 2. As a result, the realized and unrealized gains (losses) for assets and liabilities classified within Level 3 presented in the table above do not reflect the related realized or unrealized gains (losses) on hedging instruments that are classified within Level 1 and/or Level 2.

Changes in the fair value of separate and variable account assets are completely offset in the consolidated statement of income (loss) by changes in separate and variable account liabilities, which are not carried at fair value and therefore not included in the foregoing tables.

Fair Value Measured on a Non-Recurring Basis

At June 30, 2008, AIG had assets measured at fair value on a non-recurring basis on which it recorded impairment charges totaling $107 million during the six-month period ended June 30, 2008. These charges included a $45 million write-off of goodwill related to the Mortgage Guaranty reporting unit; a $49 million impairment charge on real estate owned, real estate loans held for sale and other intangible assets for American General Finance, Inc.; and impairment charges on other assets of $13 million.

Fair Value Option

FAS 159 permits a company to choose to measure at fair value many financial instruments and certain other assets and liabilities that are not required to be measured at fair value. Subsequent changes in fair value for designated items are required to be reported in income. Unrealized gains and losses on financial instruments in AIG's insurance businesses and in AIGFP for which the fair value option was elected under FAS 159 are classified in incurred policy losses and benefits and in other income, respectively, in the consolidated statement of income (loss).

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

3. Fair Value Measurements *(continued)*

The following table presents the gains or losses recorded during the three- and six-month periods ended June 30, 2008 related to the eligible instruments for which AIG elected the fair value option and the related transition adjustment recorded as a decrease to opening shareholders' equity at January 1, 2008[(a)]:

(in millions)	January 1, 2008 prior to Adoption	Transition Adjustment upon Adoption	January 1, 2008 after Adoption	Gain (Loss) Three Months Ended June 30, 2008	Gain (Loss) Six Months Ended June 30, 2008
Mortgage and other loans receivable	$ 1,109	$ —	$ 1,109	$ 11	$ 79
Financial Services assets[(b)]:					
Trading securities (formerly available for sale)	39,278	5	39,283	(718)	(1,151)
Securities purchased under agreements to resell	20,950	1	20,951	307	575
Other invested assets	321	(1)	320	2	12
Short-term investments	6,969	—	6,969	43	67
Deferred policy acquisition costs	1,147	(1,147)	—	—	—
Other assets	435	(435)	—	—	—
Future policy benefits for life, accident and health insurance contracts	299	299	—	—	—
Policyholders' contract deposits[(c)]	3,739	360	3,379	3	118
Financial Services liabilities[(b)]:					
Securities sold under agreements to repurchase	6,750	(10)	6,760	(120)	(416)
Securities and spot commodities sold but not yet purchased	3,797	(10)	3,807	(34)	(13)
Trust deposits and deposits due to banks and other depositors	216	(25)	241	4	(11)
Long-term borrowings	57,968	(675)	58,643	582	(391)
Other liabilities	1,792	—	1,792	(286)	(319)
Total gain (loss) for the three- and six-month periods ended June 30, 2008				$(206)	$(1,450)
Pre-tax cumulative effect of adopting the fair value option		(1,638)			
Decrease in deferred tax liabilities		526			
Cumulative effect of adopting the fair value option		$(1,112)			

(a) Certain of AIG's financial instruments are required to be accounted for at fair value, with changes in fair value included in earnings, under FAS 115, "Accounting for Certain Investments in Debt and Equity Securities," or FAS 133 and are not included in the table above.

(b) AIGFP elected to apply the fair value option to all eligible assets and liabilities (other than equity method investments, trade receivables and trade payables) because electing the fair value option will allow AIGFP to more closely align its earnings with the economics of its transactions by recognizing concurrently through earnings the change in fair value of its derivatives and the offsetting change in fair value of the assets and liabilities being hedged as well as the manner in which the business is evaluated by management. Substantially all of the gain (loss) amounts shown above are reported in other income on the consolidated statement of income (loss).

(c) AIG elected to apply the fair value option to certain single premium variable life products in Japan and an investment-linked life insurance product sold principally in Asia, both classified within policyholders' contract deposits in the consolidated balance sheet. AIG elected the fair value option for these liabilities to more closely align its accounting with the economics of its transactions. For the investment-linked product sold principally in Asia, the election will more effectively align changes in the fair value of assets with a commensurate change in the fair value of policyholders' liabilities. For the single premium life products in Japan, the fair value option election will allow AIG to economically hedge the inherent market risks associated with this business in an efficient and effective manner through the use of derivative instruments. The hedging program, which was initiated in the second quarter of 2008, results in an accounting presentation for this business that more closely reflects the underlying economics and the way the business is managed, with the change in the fair value of derivatives and underlying assets largely offsetting the change in fair value of the policy liabilities. AIG did not elect the fair value option for other liabilities classified in policyholders' contract deposits because other contracts do not share the same contract features that created the disparity between the accounting presentation and the economic performance.

Interest income and expense and dividend income on assets and liabilities elected under the fair value option are recognized and classified in the consolidated statement of income (loss) depending on the nature of the instrument and related market conventions. At AIGFP, interest and dividends and interest expense are included in other income. Otherwise, interest and dividends are included in net investment income in the consolidated statement of income (loss). See Note 1(a) to the Consolidated Financial Statements included in the 2007 Annual Report on Form 10-K for additional information about AIG's policies for recognition, measurement, and disclosure of interest and dividend income and interest expense.

During the three- and six-month periods ended June 30, 2008, AIG recognized a loss of $169 million and a gain of $1.3 billion, respectively, attributable to the observable effect of changes in credit spreads on AIG's own liabilities for which the fair value option was elected. AIG calculates the effect of these credit spread changes using discounted cash flow techniques that incorporate current market interest rates, AIG's ob-

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

3. Fair Value Measurements *(continued)*

servable credit spreads on these liabilities and other factors that mitigate the risk of nonperformance such as collateral posted.

The following table presents the difference between fair values and the aggregate contractual principal amounts of mortgage and other loans receivable and long-term borrowings, for which the fair value option was elected:

(in millions)	Fair Value at June 30, 2008	Principal Amount Due Upon Maturity	Difference
Assets:			
Mortgage and other loans receivable	$ 745	$ 716	$ 29
Liabilities:			
Long-term borrowings	$48,176	$47,168	$1,008

At June 30, 2008, there were no mortgage and other loans receivable for which the fair value option was elected, that were 90 days or more past due and in non-accrual status.

4. Shareholders' Equity and Earnings (Loss) Per Share

Shareholders' Equity

From time to time, AIG may buy shares of its common stock for general corporate purposes, including to satisfy its obligations under various share-based employee compensation plans. In February 2007, AIG's Board of Directors increased AIG's share repurchase program by authorizing the purchase of shares with an aggregate purchase price of $8 billion. In November 2007, AIG's Board of Directors authorized the purchase of an additional $8 billion in common stock. In 2007, AIG entered into structured share repurchase arrangements providing for the purchase of shares over time with an aggregate purchase price of $7 billion.

A total of 37,926,059 shares were purchased during the first six months of 2008 to meet commitments that existed at December 31, 2007. At August 5, 2008, $9 billion was available for purchases under the aggregate authorization. AIG does not expect to purchase additional shares under its share repurchase program for the foreseeable future.

The quarterly dividend per common share declared in May 2008 and payable on September 19, 2008 is $0.22.

In May 2008, AIG sold 196,710,525 shares of common stock at a price per share of $38 for gross proceeds of $7.47 billion and 78,400,000 equity units at a price per unit of $75 for gross proceeds of $5.88 billion. The equity units, the key terms of which are summarized below, are recorded as long-term borrowings on the consolidated balance sheet.

Equity Units

Each equity unit has an initial stated amount of $75 and consists of a stock purchase contract issued by AIG and, initially, a 1/40th or 2.5 percent undivided beneficial ownership interest in three series of junior subordinated debentures (Series B-1, B-2 and B-3), each with a principal amount of $1,000.

Each stock purchase contract requires its holder to purchase, and requires AIG to sell, a variable number of shares of AIG common stock for $25 in cash on each of the following dates: February 15, 2011, May 1, 2011 and August 1, 2011. The number of shares that AIG is obligated to deliver on each stock purchase date is set forth in the chart below (where the "applicable market value" is an average of the trading prices of AIG's common stock over the 20-trading-day period ending on the third business day prior to the relevant stock purchase date).

If the applicable market value is:	then AIG is obligated to issue:
• Greater than or equal to $45.60	• 0.54823 shares per stock purchase contract
• Between $45.60 and $38.00	• Shares equal to $25 divided by the applicable market value
• Less than or equal to $38.00	• 0.6579 shares per stock purchase contract

Basic earnings (loss) per share (EPS) will not be affected by outstanding stock purchase contracts. Diluted EPS will be determined considering the potential dilution from outstanding stock purchase contracts using the treasury stock method, and therefore diluted EPS will not be affected by outstanding stock purchase contracts until the applicable market value exceeds $45.60.

AIG is obligated to pay quarterly contract adjustment payments to the holders of the stock purchase contracts, at an initial annual rate of 2.7067 percent applied to the stated amount. The present value of the contract adjustment payments, $431 million, was recognized at inception as a liability (a component of other liabilities), and was recorded as a reduction to additional paid-in capital.

In addition to the stock purchase contracts, as part of the equity units, AIG issued $1.96 billion of each of the Series B-1, B-2 and B-3 junior subordinated debentures, which initially pay interest at rates of 5.67 percent, 5.82 percent and 5.89 percent, respectively. For accounting purposes, AIG allocated the proceeds of the equity units between the stock purchase contracts and the junior subordinated debentures on a relative fair value basis. AIG determined that the fair value of the stock purchase contract at issuance was zero, and therefore all of the proceeds were allocated to the junior subordinated debentures.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

4. Shareholders' Equity and Earnings (Loss) Per Share *(continued)*

Share-based Employee Compensation Plans

During the first quarter of 2008, AIG reviewed the vesting schedules of its share-based employee compensation plans, and on March 11, 2008, AIG's management and the Compensation and Management Resources Committee of AIG's Board of Directors determined that, to fulfill the objective of attracting and retaining high quality personnel, the vesting schedules of certain awards outstanding under these plans and all awards made in the future under these plans should be shortened.

For accounting purposes, a modification of the terms or conditions of an equity award is treated as an exchange of the original award for a new award. As a result of this modification, the incremental compensation cost related to the affected awards totaled $24 million and will, together with the unamortized originally-measured compensation cost, be amortized over shorter periods. AIG estimates the modifications will increase the amortization of this cost by $106 million and $46 million in 2008 and 2009, respectively, with a related reduction in amortization expense of $128 million in 2010 through 2013.

In the second quarter of 2008, reversals of previously accrued costs related to certain performance-based compensation plans were made, as performance to date is below the performance thresholds set forth in those plans.

Earnings (Loss) Per Share (EPS)

Basic EPS is based on the weighted average number of common shares outstanding, adjusted to reflect all stock dividends and stock splits. Diluted EPS is based on those shares used in basic EPS plus shares that would have been outstanding assuming issuance of common shares for all dilutive potential common shares outstanding, adjusted to reflect all stock dividends and stock splits.

The computation of basic and diluted EPS was as follows:

	Three Months Ended June 30,		Six Months Ended June 30,	
(in millions, except per share data)	**2008**	2007	**2008**	2007
Numerator for EPS:				
Net income (loss)	**$(5,357)**	$4,277	**$(13,162)**	$8,407
Denominator for EPS:				
Weighted average shares outstanding used in the computation of EPS:				
Common stock issued	**2,850**	2,751	**2,808**	2,751
Common stock in treasury	**(258)**	(161)	**(247)**	(156)
Deferred shares	**13**	12	**14**	12
Weighted average shares outstanding – basic	**2,605**	2,602	**2,575**	2,607
Incremental shares arising from awards outstanding under share-based employee compensation plans*	**—**	11	**—**	14
Weighted average shares outstanding – diluted*	**2,605**	2,613	**2,575**	2,621
EPS:				
Basic	**$ (2.06)**	$ 1.64	**$ (5.11)**	$ 3.22
Diluted	**$ (2.06)**	$ 1.64	**$ (5.11)**	$ 3.21

* *Calculated using the treasury stock method. Certain potential common shares arising from share-based employee compensation plans were not included in the computation of diluted EPS because the effect would have been antidilutive. The number of potential shares excluded was 7 million for the six-month period ended 2007.*

5. Ownership

According to the Schedule 13D filed on March 20, 2007 by C.V. Starr & Co., Inc. (Starr), Starr International Company, Inc. (SICO), Edward E. Matthews, Maurice R. Greenberg, the Maurice R. and Corinne P. Greenberg Family Foundation, Inc., the Universal Foundation, Inc., the Maurice R. and Corinne P. Greenberg Joint Tenancy Company, LLC and the C.V. Starr & Co., Inc. Trust, these reporting persons could be considered to beneficially own 354,987,261 shares of AIG's common stock at that date. Based on the shares of AIG's common stock outstanding at July 31, 2008, this ownership would represent approximately 13 percent of the voting stock of AIG. Although these reporting persons have made filings under Section 16 of the Exchange Act, reporting sales of shares of common stock, no amendment to the Schedule 13D has been filed to report a change in ownership subsequent to March 20, 2007.

6. Commitments, Contingencies and Guarantees

(a) Litigation and Investigations

AIG and its subsidiaries, in common with the insurance and financial services industries in general, are subject to litigation, including claims for punitive damages, in the normal course of their business. At the current time, AIG cannot predict the outcome of the matters described below, or estimate any potential additional costs related to these matters, unless otherwise indicated. In AIG's insurance operations, litigation arising from claims settlement activities is generally considered in the establishment of AIG's reserve for losses

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

6. Commitments, Contingencies and Guarantees *(continued)*

and loss expenses. However, the potential for increasing jury awards and settlements makes it difficult to assess the ultimate outcome of such litigation.

Various federal, state and foreign regulatory and governmental agencies are reviewing certain public disclosures, transactions and practices of AIG and its subsidiaries in connection with industry wide and other inquiries. These reviews include the inquiries by the SEC and U.S. Department of Justice (DOJ), previously confirmed by AIG, with respect to AIG's valuation of and disclosures relating to the AIGFP super senior credit default swap portfolio. AIG has cooperated, and will continue to cooperate, in producing documents and other information in response to subpoenas and other requests. In connection with some of the SEC investigations, AIG understands that some of its employees have received Wells notices and it is possible that additional current and former employees could receive similar notices in the future. Under SEC procedures, a Wells notice is an indication that the SEC staff has made a preliminary decision to recommend enforcement action that provides recipients with an opportunity to respond to the SEC staff before a formal recommendation is finalized.

In the opinion of AIG management, AIG's ultimate liability for the unresolved litigation and investigation matters referred to below is not likely to have a material adverse effect on AIG's consolidated financial condition, although it is possible that the effect would be material to AIG's consolidated results of operations for an individual reporting period.

Litigation Relating to AIGFP's Super Senior Credit Default Swap Portfolio

Securities Actions – Southern District of New York. On May 21, 2008, a purported securities fraud class action complaint was filed against AIG and certain of its current and former officers and directors in the United States District Court for the Southern District of New York (the Southern District of New York). The complaint alleges that defendants made statements during the period May 11, 2007 through May 9, 2008 in press releases, the Company's quarterly and year-end filings and during conference calls with analysts which were materially false and misleading and which artificially inflated the price of the Company's stock. The alleged false and misleading statements relate to, among other things, unrealized market valuation losses on AIGFP's super senior credit default swap portfolio as a result of severe credit market disruption. The complaint alleges claims under Sections 10(b) and 20(a) of the Exchange Act. Three additional purported securities class action complaints were subsequently filed in the Southern District of New York, all containing similar allegations. One of the additional complaints filed on June 19, 2008, alleges a purported class period of November 10, 2006 through June 6, 2008. The Court has not yet appointed a lead plaintiff in these actions.

ERISA Actions – Southern District of New York. On June 25, 2008, the Company, certain of its executive officers and directors, and unnamed members of the Company's Retirement Board and Investment Committee were named as defendants in two nearly identical separate actions filed in the Southern District of New York. The actions purport to be brought as class actions on behalf of all participants in or beneficiaries of certain pension plans sponsored by AIG or its subsidiaries (the Plans) during the period May 11, 2007 to June 25, 2008 and whose participant accounts included investments in the Company's common stock. Plaintiffs allege, among other things, that the defendants breached their fiduciary responsibilities to Plan participants and their beneficiaries under the Employee Retirement Income Security Act of 1974, as amended (ERISA), by: (i) failing to prudently and loyally manage the Plans and the Plans' assets; (ii) failing to provide complete and accurate information to participants and beneficiaries about the Company and the value of the Company's stock; (iii) failing to monitor appointed Plan fiduciaries and to provide them with complete and accurate information; and (iv) breach of the duty to avoid conflicts of interest. The alleged ERISA violations relate to, among other things, the defendants' purported failure to monitor and/or disclose unrealized market valuation losses on AIGFP's super senior credit default swap portfolio as a result of severe credit market disruption. Three additional purported ERISA class action complaints were subsequently filed in the Southern District of New York, both containing similar allegations. It is anticipated that these actions will all be consolidated and that the Court will then appoint a lead plaintiff in the consolidated action.

Derivative Actions – Southern District of New York. On November 20, 2007, two purported shareholder derivative actions were filed in the Southern District of New York naming as defendants the then current directors of AIG and certain senior officers of AIG and its subsidiaries. Plaintiffs assert claims for breach of fiduciary duty, waste of corporate assets and unjust enrichment, as well as violations of Section 10(b) of the Exchange Act and Rule 10b-5 promulgated thereunder, and Section 20(a) of the Exchange Act, among other things, in connection with AIG's public disclosures regarding its exposure to what the lawsuits describe as the subprime market crisis. The actions were consolidated as In re American International Group, Inc. 2007 Derivative Litigation (the 2007 Derivative Litigation). On February 15, 2008, plaintiffs filed a consolidated amended complaint alleging the same causes of action. On April 15, 2008, motions to dismiss the action were filed on behalf of all defendants.

On June 9, 2008, a purported shareholder derivative action was filed in the Southern District of New York assert-

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

6. Commitments, Contingencies and Guarantees *(continued)*

ing claims on behalf of AIG based generally on the same allegations as in the consolidated amended complaint in the 2007 Derivative Litigation. On June 10, 2008, the clerk of the court was informed that the action should be consolidated with the 2007 Derivative Litigation.

Derivative Action – Supreme Court of New York. On February 29, 2008, a purported shareholder derivative complaint was filed in the Supreme Court of Nassau County, asserting the same state law claims against the same defendants as in the consolidated amended complaint in the 2007 Derivative Litigation. On May 19, 2008, defendants filed a motion to dismiss or to stay the proceedings in light of the pending 2007 Derivative Litigation.

Action by the Starr Foundation – Supreme Court of New York. On May 7, 2008, the Starr Foundation filed a complaint in New York State Supreme Court against AIG, AIG's former Chief Executive Officer, Martin Sullivan, and AIG's Chief Financial Officer, Steven Bensinger, asserting a claim for common law fraud. The complaint alleges that the defendants made materially misleading statements and omissions concerning alleged multi-billion dollar losses in AIG's portfolio of credit default swaps. The complaint asserts that if the Starr Foundation had known the truth about the alleged losses, it would have sold its remaining shares of AIG stock. The complaint alleges that the Starr Foundation has suffered damages of at least $300 million. On May 30, 2008, a motion to dismiss the complaint was filed on behalf of defendants.

2006 Regulatory Settlements and Related Matters

2006 Regulatory Settlements. In February 2006, AIG reached a resolution of claims and matters under investigation with the United States Department of Justice (DOJ), the SEC, the Office of the New York Attorney General (NYAG) and the New York State Department of Insurance (DOI). AIG recorded an after-tax charge of $1.15 billion relating to these settlements in the fourth quarter of 2005. The settlements resolved investigations conducted by the SEC, NYAG and DOI in connection with the accounting, financial reporting and insurance brokerage practices of AIG and its subsidiaries, as well as claims relating to the underpayment of certain workers compensation premium taxes and other assessments. These settlements did not, however, resolve investigations by regulators from other states into insurance brokerage practices related to contingent commissions and other broker-related conduct, such as alleged bid rigging. Nor did the settlements resolve any obligations that AIG may have to state guarantee funds in connection with any of these matters.

As a result of these settlements, AIG made payments or placed amounts in escrow in 2006 totaling approximately $1.64 billion, $225 million of which represented fines and penalties. Amounts held in escrow totaling $334 million, including interest thereon, are included in other assets at June 30, 2008. At that date, all of the funds were escrowed for settlement of claims resulting from the underpayment by AIG of its residual market assessments for workers compensation.

In addition to the escrowed funds, $800 million was deposited into a fund under the supervision of the SEC as part of the settlements to be available to resolve claims asserted against AIG by investors, including the securities class action shareholder lawsuits described below.

Also, as part of the settlements, AIG agreed to retain, for a period of three years, an independent consultant to conduct a review that will include, among other things, the adequacy of AIG's internal control over financial reporting, the policies, procedures and effectiveness of AIG's regulatory, compliance and legal functions and the remediation plan that AIG has implemented as a result of its own internal review.

Other Regulatory Settlements. AIG's 2006 regulatory settlements with the SEC, DOJ, NYAG and DOI did not resolve investigations by regulators from other states into insurance brokerage practices. AIG entered into agreements effective January 29, 2008 with the Attorneys General of the States of Florida, Hawaii, Maryland, Michigan, Oregon, Texas and West Virginia; the Commonwealths of Massachusetts and Pennsylvania; and the District of Columbia; as well as the Florida Department of Financial Services and the Florida Office of Insurance Regulation, relating to their respective industry wide investigations into producer compensation and insurance placement practices. The settlements call for total payments of $12.5 million to be allocated among the ten jurisdictions representing restitution to state agencies and reimbursement of the costs of the investigation. During the term of the settlement agreements, AIG will continue to maintain certain producer compensation disclosure and ongoing compliance initiatives. AIG will also continue to cooperate with the industry wide investigations. The agreement with the Texas Attorney General also settles allegations of anticompetitive conduct relating to AIG's relationship with Allied World Assurance Company and includes an additional settlement payment of $500,000 related thereto.

AIG entered into an agreement effective March 13, 2008 with the Pennsylvania Insurance Department relating to the Department's investigation into the affairs of AIG and certain of its Pennsylvania-domiciled insurance company subsidiaries. The settlement calls for total payments of approximately $13.5 million, of which approximately $4.4 million was paid under previous settlement agreements. During the term of the settlement agreement, AIG will provide annual reinsurance

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

6. Commitments, Contingencies and Guarantees *(continued)*

reports, as well as maintain certain producer compensation disclosure and ongoing compliance initiatives.

NAIC Examination of Workers Compensation Premium Reporting. During 2006, the Settlement Review Working Group of the National Association of Insurance Commissioners (NAIC), under the direction of the states of Indiana, Minnesota and Rhode Island, began an investigation into the underreporting of workers' compensation premiums. In late 2007, the Settlement Review Working Group recommended that a multi-state targeted market conduct examination focusing on workers' compensation insurance be commenced under the direction of the NAIC's Market Analysis Working Group. AIG was informed of the multi-state targeted market conduct examination in January 2008. AIG has been advised that the lead states in the multi-state examination are Delaware, Florida, Indiana, Massachusetts, Minnesota, New York, Pennsylvania, and Rhode Island and that all other states (and the District of Columbia) have agreed to participate. AIG has also been advised that the examination will focus on both legacy issues and AIG's current compliance with legal requirements applicable to AIG's writing and reporting of workers' compensation insurance, but as of July 31, 2008 no determinations had been made with respect to these issues.

Securities Action – Southern District of New York. Beginning in October 2004, a number of putative securities fraud class action suits were filed in the Southern District of New York against AIG and consolidated as In re American International Group, Inc. Securities Litigation. Subsequently, a separate, though similar, securities fraud action was also brought against AIG by certain Florida pension funds. The lead plaintiff in the class action is a group of public retirement systems and pension funds benefiting Ohio state employees, suing on behalf of themselves and all purchasers of AIG's publicly traded securities between October 28, 1999 and April 1, 2005. The named defendants are AIG and a number of present and former AIG officers and directors, as well as Starr, SICO, General Reinsurance Corporation (General Re), and PricewaterhouseCoopers LLP (PwC), among others. The lead plaintiff alleges, among other things, that AIG: (1) concealed that it engaged in anti-competitive conduct through alleged payment of contingent commissions to brokers and participation in illegal bid-rigging; (2) concealed that it used "income smoothing" products and other techniques to inflate its earnings; (3) concealed that it marketed and sold "income smoothing" insurance products to other companies; and (4) misled investors about the scope of government investigations. In addition, the lead plaintiff alleges that AIG's former Chief Executive Officer, Maurice R. Greenberg, manipulated AIG's stock price. The lead plaintiff asserts claims for violations of Sections 11 and 15 of the Securities Act of 1933, Section 10(b) of the Exchange Act and Rule 10b-5 promulgated thereunder, Section 20(a) of the Exchange Act, and Section 20A of the Exchange Act. In April 2006, the court denied the defendants' motions to dismiss the second amended class action complaint and the Florida complaint. In December 2006, a third amended class action complaint was filed, which does not differ substantially from the prior complaint. Fact and class discovery is currently ongoing. On February 20, 2008, the lead plaintiff filed a motion for class certification. On June 9, 2008, the lead plaintiff filed a motion for leave to amend its complaint to include allegations related to unrealized market valuation losses on AIGFP's super senior credit default swap portfolio. On July 17, 2008, the Court denied lead plaintiffs' motion for leave to amend.

ERISA Action – Southern District of New York. Between November 30, 2004 and July 1, 2005, several ERISA actions were filed in the Southern District of New York on behalf of purported class participants and beneficiaries of three pension plans sponsored by AIG or its subsidiaries. A consolidated complaint filed on September 26, 2005 alleges a class period between September 30, 2000 and May 31, 2005 and names as defendants AIG, the members of AIG's Retirement Board and the Administrative Boards of the plans at issue, and present or former members of AIG's Board of Directors. The factual allegations in the complaint are essentially identical to those in the securities actions described above. The parties have reached an agreement to settle this matter for an amount within AIG's insurance coverage limits. On July 3, 2008, the Court granted preliminary approval of the settlement. The Court has scheduled a hearing on final settlement approval for October 7, 2008.

Derivative Action – Southern District of New York. Between October 25, 2004 and July 14, 2005, seven separate derivative actions were filed in the Southern District of New York, five of which were consolidated into a single action (the New York 2004/2005 Derivative Litigation). The complaint in this action contains nearly the same types of allegations made in the securities fraud action described above. The named defendants include current and former officers and directors of AIG, as well as Marsh & McLennan Companies, Inc. (Marsh), SICO, Starr, ACE Limited and subsidiaries (ACE), General Re, PwC, and certain employees or officers of these entity defendants. Plaintiffs assert claims for breach of fiduciary duty, gross mismanagement, waste of corporate assets, unjust enrichment, insider selling, auditor breach of contract, auditor professional negligence and disgorgement from AIG's former Chief Executive Officer, Maurice R. Greenberg, and former Chief Financial Officer, Howard I. Smith, of incentive-based compensation and AIG share proceeds under Section 304 of the Sarbanes-Oxley Act, among others. Plaintiffs seek, among other things, compensatory damages, corporate governance reforms, and a voiding of the election of

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

6. Commitments, Contingencies and Guarantees *(continued)*

certain AIG directors. AIG's Board of Directors has appointed a special committee of independent directors (special committee) to review the matters asserted in the operative consolidated derivative complaint. The court has entered an order staying this action pending resolution of the Delaware 2004/2005 Derivative Litigation discussed below. The court also has entered an order that termination of certain named defendants from the Delaware action applies to this action without further order of the court. On October 17, 2007, plaintiffs and those AIG officer and director defendants against whom the shareholder plaintiffs in the Delaware action are no longer pursuing claims filed a stipulation providing for all claims in this action against such defendants to be dismissed with prejudice. Former directors and officers Maurice R. Greenberg and Howard I. Smith have asked the court to refrain from so ordering this stipulation.

Derivative Actions – Delaware Chancery Court. From October 2004 to April 2005, AIG shareholders filed five derivative complaints in the Delaware Chancery Court. All of these derivative lawsuits were consolidated into a single action as In re American International Group, Inc. Consolidated Derivative Litigation (the Delaware 2004/2005 Derivative Litigation). The amended consolidated complaint named 43 defendants (not including nominal defendant AIG) who, as in the New York 2004/2005 Derivative Litigation, were current and former officers and directors of AIG, as well as other entities and certain of their current and former employees and directors. The factual allegations, legal claims and relief sought in this action are similar to those alleged in the New York 2004/2005 Derivative Litigation, except that the claims are only under state law. Earlier in 2007, the court approved an agreement that AIG be realigned as plaintiff, and, on June 13, 2007, acting on the direction of the special committee, AIG filed an amended complaint against former directors and officers Maurice R. Greenberg and Howard I. Smith, alleging breach of fiduciary duty and indemnification. Also on June 13, 2007, the special committee filed a motion to terminate the litigation as to certain defendants, while taking no action as to others. Defendants Greenberg and Smith filed answers to AIG's complaint and brought third-party complaints against certain current and former AIG directors and officers, PwC and Regulatory Insurance Services, Inc. On September 28, 2007, AIG and the shareholder plaintiffs filed a combined amended complaint in which AIG continued to assert claims against defendants Greenberg and Smith and took no position as to the claims asserted by the shareholder plaintiffs in the remainder of the combined amended complaint. In that pleading, the shareholder plaintiffs are no longer pursuing claims against certain AIG officers and directors. On February 12, 2008, the court granted AIG's motion to stay discovery pending the resolution of claims against AIG in the New York consolidated securities action. The court also directed the parties to coordinate a briefing schedule for the motions to dismiss. On April 11, 2008, the shareholder plaintiffs filed the First Amended Combined Complaint, which added claims against former AIG directors and officers Maurice Greenberg, Edward Matthews, and Thomas Tizzio for breach of fiduciary duty based on alleged bid-rigging in the municipal derivatives market. On April 15, 2008, shareholder plaintiffs submitted a stipulation dismissing former AIG director and officer, Evan Greenberg, without prejudice. On June 13, 2008, certain defendants filed motions to dismiss the shareholder plaintiffs' portions of the complaint.

AIG is also named as a defendant in a derivative action in the Delaware Chancery Court brought by shareholders of Marsh. On July 10, 2008, shareholder plaintiffs filed a second consolidated amended complaint, which contains claims against AIG for aiding and abetting a breach of fiduciary duty and contribution and indemnification in connection with alleged bid-rigging and steering practices in the commercial insurance market.

Policyholder Antitrust and RICO Actions. Commencing in 2004, policyholders brought multiple federal antitrust and Racketeer Influenced and Corrupt Organizations Act (RICO) class actions in jurisdictions across the nation against insurers and brokers, including AIG and a number of its subsidiaries, alleging that the insurers and brokers engaged in a broad conspiracy to allocate customers, steer business, and rig bids. These actions, including 24 complaints filed in different federal courts naming AIG or an AIG subsidiary as a defendant, were consolidated by the judicial panel on multi-district litigation and transferred to the United States District Court for the District of New Jersey for coordinated pretrial proceedings. The consolidated actions have proceeded in that court in two parallel actions, In re Insurance Brokerage Antitrust Litigation (the Commercial Complaint) and In re Employee Benefit Insurance Brokerage Antitrust Litigation (the Employee Benefits Complaint, and, together with the Commercial Complaint, the multi-district litigation).

The plaintiffs in the Commercial Complaint are a group of corporations, individuals and public entities that contracted with the broker defendants for the provision of insurance brokerage services for a variety of insurance needs. The broker defendants are alleged to have placed insurance coverage on the plaintiffs' behalf with a number of insurance companies named as defendants, including AIG subsidiaries. The Commercial Complaint also named various brokers and other insurers as defendants (three of which have since settled). The Commercial Complaint alleges, among other things, that defendants engaged in a widespread conspiracy to allocate customers through bid-rigging and steering prac-

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

6. Commitments, Contingencies and Guarantees *(continued)*

tices. Plaintiffs assert that the defendants violated the Sherman Antitrust Act, RICO, and the antitrust laws of 48 states and the District of Columbia, and are liable under common law breach of fiduciary duty and unjust enrichment theories. Plaintiffs seek treble damages plus interest and attorneys' fees as a result of the alleged RICO and Sherman Antitrust Act violations.

The plaintiffs in the Employee Benefits Complaint are a group of individual employees and corporate and municipal employers alleging claims on behalf of two separate nationwide purported classes: an employee class and an employer class that acquired insurance products from the defendants from August 26, 1994 to the date of any class certification. The Employee Benefits Complaint names AIG, as well as various other brokers and insurers, as defendants. The activities alleged in the Employee Benefits Complaint, with certain exceptions, track the allegations made in the Commercial Complaint.

The Court in connection with the Commercial Complaint granted (without leave to amend) defendants' motions to dismiss the federal antitrust and RICO claims on August 31, 2007 and September 28, 2007, respectively. The court declined to exercise supplemental jurisdiction over the state law claims in the Commercial Complaint and therefore dismissed it in its entirety. On January 14, 2008, the court granted defendants' motion for summary judgment on the ERISA claims in the Employee Benefits Complaint and subsequently dismissed the remaining state law claims without prejudice, thereby dismissing the Employee Benefits Complaint in its entirety. On February 12, 2008, plaintiffs filed a notice of appeal to the United States Court of Appeals for the Third Circuit with respect to the dismissal of the Employee Benefits Complaint. Plaintiffs previously appealed the dismissal of the Commercial Complaint to the United States Court of Appeals for the Third Circuit on October 10, 2007. On July 2, 2008, the Third Circuit stayed all proceedings in both appeals pending resolution in the district court of joint motions for approval of class plaintiffs' settlement with the Marsh defendants. On July 10, 2008, appellants filed a motion to vacate the stay, which was granted on July 30, 2008. On July 31, 2008, the Third Circuit informed the parties that oral argument in both appeals had been tentatively scheduled for April 20, 2009.

A number of complaints making allegations similar to those in the multi-district litigation have been filed against AIG and other defendants in state and federal courts around the country. The defendants have thus far been successful in having the federal actions transferred to the District of New Jersey and consolidated into the multi-district litigation. These additional consolidated actions are still pending in the District Court, but are currently stayed pending a decision by the court on whether they will proceed during the appeal of the dismissal of the multi-district litigation. The AIG defendants have also sought to have state court actions making similar allegations stayed pending resolution of the multi-district litigation proceeding. These efforts have generally been successful, although plaintiffs in one case pending in Texas state court have moved to re-open discovery; a hearing on that motion was held on April 9, 2008 at which the court deferred ruling on the motion until defendants file their Special Exceptions. AIG has recently settled several of the various federal and state actions alleging claims similar to those in the multi-district litigation, including a state court action pending in Florida in which discovery had been allowed to proceed.

Ohio Attorney General Action – Ohio Court of Common Pleas. On August 24, 2007, the Ohio Attorney General filed a complaint in the Ohio Court of Common Pleas against AIG and a number of its subsidiaries, as well as several other broker and insurer defendants, asserting violation of Ohio's antitrust laws. The complaint, which is similar to the Commercial Complaint, alleges that AIG and the other broker and insurer defendants conspired to allocate customers, divide markets, and restrain competition in commercial lines of casualty insurance sold through the broker defendant. The complaint seeks treble damages on behalf of Ohio public purchasers of commercial casualty insurance, disgorgement on behalf of both public and private purchasers of commercial casualty insurance, as well as a $500 per day penalty for each day of conspiratorial conduct. AIG, along with other co-defendants, moved to dismiss the complaint on November 16, 2007. On June 30, 2008, the Court denied defendants' motion to dismiss.

Action Relating to Workers Compensation Premium Reporting – Northern District of Illinois. On May 24, 2007, the National Workers Compensation Reinsurance Pool (the NWCRP), on behalf of its participant members, filed a lawsuit in the United States District Court for the Northern District of Illinois against AIG with respect to the underpayment by AIG of its residual market assessments for workers compensation. The complaint alleges claims for violations of RICO, breach of contract, fraud and related state law claims arising out of AIG's alleged underpayment of these assessments between 1970 and the present and seeks damages purportedly in excess of $1 billion. On August 6, 2007, the court denied AIG's motion seeking to dismiss or stay the complaint or, in the alternative, to transfer to the Southern District of New York. On December 26, 2007, the court denied AIG's motion to dismiss the complaint. On March 17, 2008, AIG filed an amended answer, counterclaims and third-party claims against NCCI (in its capacity as attorney-in-fact for the NWCRP), the NWCRP, its board members, and certain of the other insurance companies that are members of the

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

6. Commitments, Contingencies and Guarantees *(continued)*

NWCRP alleging violations of RICO, as well as claims for conspiracy, fraud, and other state law claims. The counterclaim- and third-party defendants filed motions to dismiss on June 9, 2008. The motions are scheduled for decision on November 20, 2008. Discovery is currently ongoing while the motions are pending.

Action Relating to Workers Compensation Premium Reporting – Minnesota. On February 16, 2006, the Attorney General of the State of Minnesota filed a complaint against AIG with respect to claims by the Minnesota Department of Revenue and the Minnesota Special Compensation Fund, alleging that AIG made false statements and reports to Minnesota agencies and regulators, unlawfully reducing AIG's contributions and payments to Minnesota and certain state funds relating to its workers' compensation premiums. While AIG settled that litigation in December 2007, a similar lawsuit was filed by the Minnesota Workers Compensation Reinsurance Association and the Minnesota Workers Compensation Insurers Association in the United States District Court for the District of Minnesota. On March 28, 2008, the court granted AIG's motion to dismiss the case in its entirety. On April 25, 2008, plaintiffs appealed to the United States Court of Appeals for the Eighth Circuit and also filed a new complaint making similar allegations in Minnesota state court. On April 30, 2008, substantially identical claims were also filed in Minnesota state court by the Minnesota Insurance Guaranty Association and Minnesota Assigned Risk Plan.

Action Relating to Workers Compensation Premium Reporting – District of South Carolina. A purported class action was also filed in the United States District Court for the District of South Carolina on January 25, 2008 against AIG and certain of its subsidiaries, on behalf of a class of employers that obtained workers' compensation insurance from AIG companies and allegedly paid inflated premiums as a result of AIG's alleged underreporting of workers' compensation premiums. An amended complaint in the South Carolina action was filed on March 24, 2008, and AIG filed a motion to dismiss the amended complaint on April 21, 2008. On July 8, 2008, the South Carolina court granted AIG's motion to dismiss all claims without prejudice and granted plaintiff leave to refile subject to certain conditions.

Litigation Relating to SICO and Starr

SICO Action. In July, 2005 SICO filed a complaint against AIG in the Southern District of New York, claiming that AIG had refused to provide SICO access to certain artwork, and asking the court to order AIG immediately to release the property to SICO. AIG filed an answer denying SICO's allegations and setting forth defenses to SICO's claims. In addition, AIG filed counterclaims asserting breach of contract, unjust enrichment, conversion, breach of fiduciary duty, a constructive trust and declaratory judgment, relating to SICO's breach of its commitment to use its AIG shares only for the benefit of AIG and AIG employees. On June 23, 2008, the Court denied in part and granted in part SICO's motion for summary judgment, and on July 31, 2008 the parties submitted a joint pre-trial order.

Derivative Action Relating to Starr and SICO. On December 31, 2002, a derivative lawsuit was filed in the Delaware Chancery Court against twenty directors and executives of AIG as well as against AIG as a nominal defendant that alleges, among other things, that the directors of AIG breached the fiduciary duties of loyalty and care by approving the payment of commissions to insurance managing general agencies owned by Starr and of rental and service fees to SICO and the executives breached their duty of loyalty by causing AIG to enter into contracts with Starr and SICO and their fiduciary duties by usurping AIG's corporate opportunities. The complaint further alleges that the Starr agencies did not provide any services that AIG was not capable of providing itself, and that the diversion of commissions to these entities was solely for the benefit of Starr's owners. The complaint also alleges that the service fees and rental payments made to SICO and its subsidiaries were improper. Under the terms of a stipulation approved by the court on February 16, 2006, the claims against the outside independent directors were dismissed with prejudice, while the claims against the other directors were dismissed without prejudice. In an opinion dated June 21, 2006, the Court denied defendants' motion to dismiss, except with respect to plaintiff's challenge to payments made to Starr before January 1, 2000. On July 21, 2006, plaintiff filed its second amended complaint, which alleges that, between January 1, 2000 and May 31, 2005, individual defendants breached their duty of loyalty by causing AIG to enter into contracts with Starr and SICO and breached their fiduciary duties by usurping AIG's corporate opportunity. Starr is charged with aiding and abetting breaches of fiduciary duty and unjust enrichment for its acceptance of the fees. SICO is no longer named as a defendant. On June 27, 2007, Starr filed a cross-claim against AIG, alleging one count that includes contribution, unjust enrichment and setoff. On November 15, 2007, the court granted AIG's motion to dismiss the cross-claim by Starr to the extent that it sought affirmative relief from AIG. On February 14, 2008, the court granted a motion to add former AIG officer Thomas Tizzio as a defendant. As a result, the remaining defendants in the case are AIG (the nominal defendant), Starr and former directors and officers Maurice Greenberg, Howard Smith, Edward Matthews and Thomas Tizzio. Trial is currently scheduled to begin in September 2008.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

6. Commitments, Contingencies and Guarantees *(continued)*

Litigation Matters Relating to AIG's General Insurance Operations

Caremark. AIG and certain of its subsidiaries have been named defendants in two putative class actions in state court in Alabama that arise out of the 1999 settlement of class and derivative litigation involving Caremark Rx, Inc. (Caremark). The plaintiffs in the second-filed action have intervened in the first-filed action, and the second-filed action has been dismissed. An excess policy issued by a subsidiary of AIG with respect to the 1999 litigation was expressly stated to be without limit of liability. In the current actions, plaintiffs allege that the judge approving the 1999 settlement was misled as to the extent of available insurance coverage and would not have approved the settlement had he known of the existence and/or unlimited nature of the excess policy. They further allege that AIG, its subsidiaries, and Caremark are liable for fraud and suppression for misrepresenting and/or concealing the nature and extent of coverage. In addition, the intervenor-plaintiffs allege that various lawyers and law firms who represented parties in the underlying class and derivative litigation (the Lawyer Defendants) are also liable for fraud and suppression, misrepresentation, and breach of fiduciary duty. The complaints filed by the plaintiffs and the intervenor-plaintiffs request compensatory damages for the 1999 class in the amount of $3.2 billion, plus punitive damages. AIG and its subsidiaries deny the allegations of fraud and suppression and have asserted that information concerning the excess policy was publicly disclosed months prior to the approval of the settlement. AIG and its subsidiaries further assert that the current claims are barred by the statute of limitations and that plaintiffs' assertions that the statute was tolled cannot stand against the public disclosure of the excess coverage. The plaintiffs and intervenor-plaintiffs, in turn, have asserted that the disclosure was insufficient to inform them of the nature of the coverage and did not start the running of the statute of limitations. On November 26, 2007, the trial court issued an order that dismissed the intervenors' complaint against the Lawyer Defendants and entered a final judgment in favor of the Lawyer Defendants. The intervenors are appealing the dismissal of the Lawyer Defendants and on January 2, 2008, requested a stay of all trial court proceedings pending the appeal. On March 4, 2008, the trial court granted the motion for a stay. No further proceedings at the trial court level will occur until the appeal of the dismissal of the Lawyer Defendants is resolved. AIG cannot reasonably estimate either the likelihood of its prevailing in these actions or the potential damages in the event liability is determined.

Gunderson. A subsidiary of AIG has been named as a defendant in a putative class action lawsuit in the 14th Judicial District Court for the State of Louisiana. The complaint alleges failure to comply with certain provisions of the Louisiana Any Willing Provider Act relating to discounts taken by defendants on bills submitted by Louisiana medical providers and hospitals that provided treatment or services to workers compensation claimants and seeks monetary penalties and injunctive relief. On January 25, 2008, plaintiffs and the AIG subsidiary agreed to resolve the lawsuit on a class-wide basis for approximately $29 million. On May 29, 2008, the court entered a Final Order and Judgment, approving the settlement and fully and finally resolving the litigation.

(b) Commitments

Flight Equipment

At June 30, 2008, International Lease Finance Corporation (ILFC) had committed to purchase 179 new aircraft deliverable from 2008 through 2019 at an estimated aggregate purchase price of $17.6 billion. ILFC will be required to find customers for any aircraft acquired, and it must arrange financing for portions of the purchase price of such equipment.

ILFC ordered 74 Boeing 787 aircraft with the first aircraft now scheduled to be delivered in late 2011. Boeing has made several announcements concerning the delays in the deliveries of the 787s. Boeing has informed ILFC that its 787 deliveries will be delayed 19-30 months with an average delay in excess of 27 months per aircraft and span across ILFC's entire order, with the original contracted deliveries running from 2010 through 2017.

Other Commitments

In the normal course of business, AIG enters into commitments to invest in limited partnerships, private equities, hedge funds and mutual funds and to purchase and develop real estate in the U.S. and abroad. These commitments totaled $8.7 billion at June 30, 2008.

On June 27, 2005, AIG entered into an agreement pursuant to which AIG agreed, subject to certain conditions, to make any payment that is not promptly paid with respect to the benefits accrued by certain employees of AIG and its subsidiaries under the SICO Plans (as discussed below under "Benefits Provided by Starr International Company, Inc. and C.V. Starr & Co., Inc.").

(c) Contingencies

Loss Reserves. Although AIG regularly reviews the adequacy of the established reserve for losses and loss expenses, there can be no assurance that AIG's ultimate loss reserves will not develop adversely and materially exceed AIG's current loss reserves. Estimation of ultimate net losses, loss expenses and loss reserves is a complex process for long-tail casualty lines of business, which include excess and umbrella liability, directors and officers liability (D&O), professional liability, medical malpractice, workers' compensation, general liability, products liability and related classes, as well as for asbes-

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

6. Commitments, Contingencies and Guarantees *(continued)*

tos and environmental exposures. Generally, actual historical loss development factors are used to project future loss development. However, there can be no assurance that future loss development patterns will be the same as in the past. Moreover, any deviation in loss cost trends or in loss development factors might not be discernible for an extended period of time subsequent to the recording of the initial loss reserve estimates for any accident year. Thus, there is the potential for reserves with respect to a number of years to be significantly affected by changes in loss cost trends or loss development factors that were relied upon in setting the reserves. These changes in loss cost trends or loss development factors could be attributable to changes in inflation, in labor and material costs or in the judicial environment, or in other social or economic phenomena affecting claims.

Benefits Provided by Starr International Company, Inc. and C.V. Starr & Co., Inc. SICO has provided a series of two-year Deferred Compensation Profit Participation Plans (SICO Plans) to certain AIG employees. The SICO Plans were created in 1975 when the voting shareholders and Board of Directors of SICO, a private holding company whose principal asset is AIG common stock, decided that a portion of the capital value of SICO should be used to provide an incentive plan for the current and succeeding managements of all American International companies, including AIG.

None of the costs of the various benefits provided under the SICO Plans has been paid by AIG, although AIG has recorded a charge to reported earnings for the deferred compensation amounts paid to AIG employees by SICO, with an offsetting amount credited to additional paid-in capital reflecting amounts considered to be contributed by SICO. The SICO Plans provide that shares currently owned by SICO are set aside by SICO for the benefit of the participant and distributed upon retirement. The SICO Board of Directors currently may permit an early payout of units under certain circumstances. Prior to payout, the participant is not entitled to vote, dispose of or receive dividends with respect to such shares, and shares are subject to forfeiture under certain conditions, including but not limited to the participant's voluntary termination of employment with AIG prior to normal retirement age. Under the SICO Plans, SICO's Board of Directors may elect to pay a participant cash in lieu of shares of AIG common stock. Following notification from SICO to participants in the SICO Plans that it will settle specific future awards under the SICO Plans with shares rather than cash, AIG modified its accounting for the SICO Plans from variable to fixed measurement accounting. AIG gave effect to this change in settlement method beginning on December 9, 2005, the date of SICO's notice to participants in the SICO Plans.

(d) Guarantees

AIG and certain of its subsidiaries become parties to derivative financial instruments with market risk resulting from both dealer and end-user activities to reduce currency, interest rate, equity and commodity exposures. These instruments are carried at their fair value in the consolidated balance sheet. The majority of AIG's derivative activity is transacted by AIGFP. See Note 8 to the 2007 Annual Report on Form 10-K.

AIG has issued unconditional guarantees with respect to the prompt payment, when due, of all present and future payment obligations and liabilities of AIGFP arising from transactions entered into by AIGFP.

SAI Deferred Compensation Holdings, Inc., a wholly owned subsidiary of AIG, has established a deferred compensation plan for registered representatives of certain AIG subsidiaries, pursuant to which participants have the opportunity to invest deferred commissions and fees on a notional basis. The value of the deferred compensation fluctuates with the value of the deferred investment alternatives chosen. AIG has provided a full and unconditional guarantee of the obligations of SAI Deferred Compensation Holdings, Inc. to pay the deferred compensation under the plan.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

7. Employee Benefits

The components of the net periodic benefit cost with respect to pensions and other postretirement benefits were as follows:

	Pensions			Postretirement		
(in millions)	Non-U.S. Plans	U.S. Plans	Total	Non-U.S. Plans	U.S. Plans	Total
Three Months Ended June 30, 2008						
Components of net periodic benefit cost:						
Service cost	**$ 26**	**$ 32**	**$ 58**	**$ 2**	**$ 2**	**$ 4**
Interest cost	**14**	**50**	**64**	**1**	**4**	**5**
Expected return on assets	**(12)**	**(59)**	**(71)**	**–**	**–**	**–**
Amortization of prior service cost	**(2)**	**(1)**	**(3)**	**–**	**–**	**–**
Amortization of net loss	**3**	**5**	**8**	**–**	**–**	**–**
Settlement loss	**2**	**–**	**2**	**–**	**–**	**–**
Net periodic benefit cost	**$ 31**	**$ 27**	**$ 58**	**$ 3**	**$ 6**	**$ 9**
Three Months Ended June 30, 2007						
Components of net periodic benefit cost:						
Service cost	$ 21	$ 30	$ 51	$ 2	$ 3	$ 5
Interest cost	12	44	56	–	4	4
Expected return on assets	(9)	(54)	(63)	–	–	–
Amortization of prior service cost	(3)	–	(3)	–	(1)	(1)
Amortization of net loss	3	9	12	–	–	–
Settlement loss	1	–	1	–	–	–
Net periodic benefit cost	$ 25	$ 29	$ 54	$ 2	$ 6	$ 8
Six Months Ended June 30, 2008						
Components of net periodic benefit cost:						
Service cost	**$ 50**	**$ 64**	**$ 114**	**$ 4**	**$ 4**	**$ 8**
Interest cost	**28**	**100**	**128**	**2**	**8**	**10**
Expected return on assets	**(23)**	**(119)**	**(142)**	**–**	**–**	**–**
Amortization of prior service cost	**(5)**	**(1)**	**(6)**	**–**	**–**	**–**
Amortization of net loss	**7**	**9**	**16**	**–**	**–**	**–**
Settlement loss	**2**	**–**	**2**	**–**	**–**	**–**
Net periodic benefit cost	**$ 59**	**$ 53**	**$ 112**	**$ 6**	**$ 12**	**$ 18**
Six Months Ended June 30, 2007						
Components of net periodic benefit cost:						
Service cost	$ 44	$ 60	$ 104	$ 3	$ 5	$ 8
Interest cost	24	89	113	1	8	9
Expected return on assets	(18)	(107)	(125)	–	–	–
Amortization of prior service cost	(5)	(1)	(6)	–	(1)	(1)
Amortization of net loss	5	18	23	–	–	–
Settlement loss	1	–	1	–	–	–
Net periodic benefit cost	$ 51	$ 59	$ 110	$ 4	$ 12	$ 16

8. Federal Income Taxes

Interim Period Tax Assumptions and Effective Tax Rates

AIG's interim period tax expense or benefit is measured using an estimated annual effective tax rate. To the extent that a portion of AIG's annual pretax income or loss cannot be reliably estimated, the actual tax expense or benefit applicable to that income or loss is reported in the interim period in which the related income or loss is reported. AIG is unable to reliably estimate other-than-temporary impairments and the operating results of AIGFP. Therefore, the related tax effect of other-than-temporary impairments, which is calculated at the applicable local statutory rate (predominantly 35 percent), and the operating results of AIGFP, which are tax effected at the U.S. statutory tax rate of 35 percent, are reported as discrete adjustments to the estimated annual effective tax rate that AIG applies to all other pretax income.

The effective tax rate on the pre-tax loss for the three-month period ended June 30, 2008 was 38.4 percent. The effective tax rate was higher than the statutory rate of 35

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

8. Federal Income Taxes *(continued)*

percent due primarily to tax benefits from foreign operations and tax exempt interest. The effective tax rate on the pre-tax loss for the six-month period ended June 30, 2008 was 34.4 percent. The effective tax rate was adversely affected by $703 million of tax charges from the first three months of 2008, comprised of increases in the reserves for uncertain tax positions and other discrete period items. The effective tax rate on the pre-tax income for the three- and six-month periods ended June 30, 2007 was 26.5 percent and 27.2 percent, respectively. The effective tax rates were low, due primarily to benefits from remediation adjustments and the recognition of tax benefits associated with the SICO Plan for which the compensation expense was recognized in prior years.

Tax Filings and Examinations

On April 3, 2008, AIG filed a refund claim for tax years 1997 through 2004. The refund claim relates to the tax effect of the restatement of AIG's 2004 and prior financial statements.

There has been no material change to the status of the assertion of additional tax made by the Internal Revenue Service (IRS) in their Statutory Notice of Deficiency as described in AIG's Quarterly Report on Form 10-Q for the quarter ended March 31, 2008. AIG continues to believe that it has adequate reserves for any liability that could result from the IRS actions.

In the second quarter of 2008, three separate court decisions were rendered relating to certain leasing transactions, which were adverse to the affected taxpayers. In accordance with FIN 48 and FSP 13-2, AIG evaluated the effect of these decisions on leasing transactions of AIG subsidiaries and adjusted the timing of cash flows relating to income taxes generated by the transactions. AIG recorded a $100 million after-tax charge in the quarter ended June 30, 2008 as a result of this evaluation.

FIN 48

As of June 30, 2008 and December 31, 2007, AIG's unrecognized tax benefits, excluding interest and penalties, were $2.5 billion and $1.3 billion, respectively. As of June 30, 2008 and December 31, 2007, AIG's unrecognized tax benefits included $965 million and $299 million, respectively, related to tax positions the disallowance of which would not affect the effective tax rate. Accordingly, as of June 30, 2008 and December 31, 2007, the amount of unrecognized tax benefits that, if recognized, would favorably affect the effective tax rate was $1.5 billion and $1.0 billion, respectively. Substantially all of the increase as of June 30, 2008 was attributable to the quarter ended March 31, 2008.

At June 30, 2008, AIG had accrued $429 million for the payment of interest (net of the federal benefit) and penalties.

AIG continually evaluates proposed adjustments by taxing authorities. At June 30, 2008, such proposed adjustments would not result in a material change to AIG's consolidated financial condition, although it is possible that the effect could be material to AIG's consolidated results of operations for an individual reporting period. Although it is reasonably possible that a significant change in the balance of unrecognized tax benefits may occur within the next twelve months, at this time it is not possible to estimate the range of the change due to the uncertainty of the potential outcomes.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

9. Information Provided in Connection with Outstanding Debt

The following condensed consolidating financial statements reflect the following:

- **AIG Life Holdings (US), Inc. (AIGLH), formerly known as American General Corporation, is a holding company and a wholly owned subsidiary of AIG. AIG provides a full and unconditional guarantee of all outstanding debt of AIGLH.**
- **AIG Liquidity Corp. is a wholly owned subsidiary of AIG. AIG provides a full and unconditional guarantee of all obligations of AIG Liquidity Corp.**
- **AIG Program Funding, Inc. is a wholly owned subsidiary of AIG. AIG provides a full and unconditional guarantee of all obligations of AIG Program Funding, Inc.**

Condensed Consolidating Balance Sheet

(in millions)	American International Group, Inc. (As Guarantor)	AIGLH	AIG Liquidity Corp.	AIG Program Funding, Inc.	Other Subsidiaries	Eliminations	Consolidated AIG
June 30, 2008							
Assets:							
Investments and Financial Services assets	**$ 28,453**	**$ 40**	**$ –**	**$ –**	**$ 829,778**	**$ (22,669)**	**$ 835,602**
Cash	**3**	**–**	**–**	**–**	**2,226**	**–**	**2,229**
Carrying value of subsidiaries and partially owned companies, at equity	**91,567**	**19,869**	**–**	**–**	**19,151**	**(129,959)**	**628**
Other assets	**19,511**	**2,608**	**–**	**–**	**189,172**	**126**	**211,417**
Total assets	**$139,534**	**$22,517**	**$ –**	**$ –**	**$1,040,327**	**$ (152,502)**	**$1,049,876**
Liabilities:							
Insurance liabilities	**$ –**	**$ –**	**$ –**	**$ –**	**$ 557,673**	**$ (108)**	**$ 557,565**
Debt	**47,827**	**2,136**	**–**	**–**	**149,034**	**(20,359)**	**178,638**
Other liabilities	**13,619**	**2,991**	**–**	**–**	**220,587**	**(1,712)**	**235,485**
Total liabilities	**61,446**	**5,127**	**–**	**–**	**927,294**	**(22,179)**	**971,688**
Preferred shareholders' equity in subsidiary companies	**–**	**–**	**–**	**–**	**100**	**–**	**100**
Total shareholders' equity	**78,088**	**17,390**	**–**	**–**	**112,933**	**(130,323)**	**78,088**
Total liabilities, preferred shareholders' equity in subsidiary companies and shareholders' equity	**$139,534**	**$22,517**	**$ –**	**$ –**	**$1,040,327**	**$ (152,502)**	**$1,049,876**
December 31, 2007							
Assets:							
Investments and Financial Services assets	$ 14,648	$ 40	$ –	$ –	$ 849,144	$ (21,790)	$ 842,042
Cash	84	1	–	–	2,199	–	2,284
Carrying value of subsidiaries and partially owned companies, at equity	111,714	24,396	–	–	18,542	(153,998)	654
Other assets	9,414	2,592	–	–	191,220	155	203,381
Total assets	$135,860	$27,029	$ –	$ –	$1,061,105	$ (175,633)	$1,048,361
Liabilities:							
Insurance liabilities	$ 43	$ –	$ –	$ –	$ 534,369	$ (75)	$ 534,337
Debt	36,045	2,136	–	–	156,003	(18,135)	176,049
Other liabilities	3,971	2,826	–	–	238,362	(3,085)	242,074
Total liabilities	40,059	4,962	–	–	928,734	(21,295)	952,460
Preferred shareholders' equity in subsidiary companies	–	–	–	–	100	–	100
Total shareholders' equity	95,801	22,067	–	–	132,271	(154,338)	95,801
Total liabilities, preferred shareholders' equity in subsidiary companies and shareholders' equity	$135,860	$27,029	$ –	$ –	$1,061,105	$ (175,633)	$1,048,361

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

9. Information Provided in Connection with Outstanding Debt *(continued)*

Condensed Consolidating Statement of Income (Loss)

(in millions)	American International Group, Inc. (As Guarantor)	AIGLH	AIG Liquidity Corp.	AIG Program Funding, Inc.	Other Subsidiaries	Eliminations	Consolidated AIG
Three Months Ended June 30, 2008							
Operating income (loss)	**$ (52)**	**$ (20)**	**$***	**$–**	**$ (8,684)**	**$ –**	**$ (8,756)**
Equity in undistributed net income of consolidated subsidiaries	**(6,164)**	**(1,729)**	**–**	**–**	**–**	**7,893**	**–**
Dividend income from consolidated subsidiaries	**724**	**–**	**–**	**–**	**–**	**(724)**	**–**
Income taxes (benefits)	**(135)**	**(4)**	*****	**–**	**(3,218)**	**–**	**(3,357)**
Minority interest	**–**	**–**	**–**	**–**	**42**	**–**	**42**
Net income (loss)	**$ (5,357)**	**$(1,745)**	**$***	**$–**	**$ (5,424)**	**$ 7,169**	**$ (5,357)**
Three Months Ended June 30, 2007							
Operating income (loss)	$ (282)	$ (13)	$*	$–	$ 6,623	$ –	$ 6,328
Equity in undistributed net income of consolidated subsidiaries	3,605	340	–	–	–	(3,945)	–
Dividend income from consolidated subsidiaries	879	218	–	–	–	(1,097)	–
Income taxes (benefits)	(75)	(15)	*	–	1,769	–	1,679
Minority interest	–	–	–	–	(372)	–	(372)
Net income (loss)	$ 4,277	$ 560	$*	$–	$ 4,482	$ (5,042)	$ 4,277
Six Months Ended June 30, 2008							
Operating income (loss)	**$ (885)**	**$ (41)**	**$***	**$–**	**$(19,094)**	**$ –**	**$(20,020)**
Equity in undistributed net income of consolidated subsidiaries	**(13,918)**	**(2,975)**	**–**	**–**	**–**	**16,893**	**–**
Dividend income from consolidated subsidiaries	**1,473**	**–**	**–**	**–**	**–**	**(1,473)**	**–**
Income taxes (benefits)	**(168)**	**(7)**	*****	**–**	**(6,719)**	**–**	**(6,894)**
Minority interest	**–**	**–**	**–**	**–**	**(36)**	**–**	**(36)**
Net income (loss)	**$(13,162)**	**$(3,009)**	**$***	**$–**	**$(12,411)**	**$ 15,420**	**$(13,162)**
Six Months Ended June 30, 2007							
Operating income (loss)	$ (543)	$ (86)	$*	$–	$ 13,129	$ –	$ 12,500
Equity in undistributed net income of consolidated subsidiaries	6,849	491	–	–	–	(7,340)	–
Dividend income from consolidated subsidiaries	2,165	658	–	–	–	(2,823)	–
Income taxes (benefits)	64	(7)	*	–	3,348	–	3,405
Minority interest	–	–	–	–	(688)	–	(688)
Net income (loss)	$ 8,407	$ 1,070	$*	$–	$ 9,093	$(10,163)	$ 8,407

**Less than $1 million.*

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

9. Information Provided in Connection with Outstanding Debt *(continued)*

Condensed Consolidating Statement of Cash Flows

(in millions)	American International Group, Inc. (As Guarantor)	AIGLH	AIG Liquidity Corp.	AIG Program Funding, Inc.	Other Subsidiaries	Consolidated AIG
Six Months Ended June 30, 2008						
Net cash provided by (used in) operating activities	**$ (594)**	**$ 115**	**$ ***	**$ –**	**$ 17,068**	**$ 16,589**
Cash flows from investing:						
Invested assets disposed	**603**	**–**	**–**	**–**	**79,738**	**80,341**
Invested assets acquired	**(2,096)**	**–**	**–**	**–**	**(87,214)**	**(89,310)**
Other	**(11,466)**	**(116)**	*****	**–**	**(1,412)**	**(12,994)**
Net cash provided by (used in) investing activities	**(12,959)**	**(116)**	*****	**–**	**(8,888)**	**(21,963)**
Cash flows from financing activities:						
Issuance of debt	**13,080**	**–**	**–**	**–**	**42,605**	**55,685**
Repayments of debt	**(1,912)**	**–**	**–**	**–**	**(54,733)**	**(56,645)**
Proceeds from common stock issued	**7,343**				**–**	**7,343**
Payments advanced to purchase shares	**(1,000)**	**–**	**–**	**–**	**–**	**(1,000)**
Cash dividends paid to shareholders	**(1,036)**	**–**	**–**	**–**	**–**	**(1,036)**
Other	**(3,003)**	**–**	*****	**–**	**3,930**	**927**
Net cash provided by (used in) financing activities	**13,472**	**–**	*****	**–**	**(8,198)**	**5,274**
Effect of exchange rate changes on cash	**–**	**–**	**–**	**–**	**45**	**45**
Change in cash	**(81)**	**(1)**	*****	**–**	**27**	**(55)**
Cash at beginning of period	**84**	**1**	**–**	**–**	**2,199**	**2,284**
Cash at end of period	**$ 3**	**$ –**	**$ ***	**$ –**	**$ 2,226**	**$ 2,229**
Six Months Ended June 30, 2007						
Net cash provided by (used in) operating activities	$ (1,076)	$ 172	$ *	$ –	$ 18,335	$ 17,431
Cash flows from investing:						
Invested assets disposed	1,768	–	–	–	82,139	83,907
Invested assets acquired	(6,857)	–	–	–	(99,942)	(106,799)
Other	(2,012)	(76)	*	–	(15,334)	(17,422)
Net cash provided by (used in) investing activities	(7,101)	(76)	*	–	(33,137)	(40,314)
Cash flows from financing activities:						
Issuance of debt	11,958	–	–	–	38,133	50,091
Repayments of debt	(790)	–	–	–	(34,147)	(34,937)
Proceeds from common stock issued	–	–	–	–	–	–
Payments advanced to purchase shares	(4,000)	–	–	–	–	(4,000)
Cash dividends paid to shareholders	(859)	–	–	–	–	(859)
Other	1,828	(96)	*	–	10,920	12,652
Net cash provided by (used in) financing activities	8,137	(96)	*	–	14,906	22,947
Effect of exchange rate changes on cash	–	–	–	–	(19)	(19)
Change in cash	(40)	–	*	–	85	45
Cash at beginning of period	76	–	–	–	1,514	1,590
Cash at end of period	$ 36	$ –	$ *	$ –	$ 1,599	$ 1,635

**Less than $1 million.*

During the second quarter of 2008, AIG made certain revisions to the American International Group, Inc. (as Guarantor) Condensed Statement of Cash Flows, primarily relating to the effect of reclassifying certain intercompany and securities lending balances. Accordingly, AIG revised the previous period presented to conform to the revised presentation. There was no effect on the Consolidated Statement of Cash Flows or ending cash balances.

The revisions and their effect on the American International Group, Inc. (as Guarantor) Condensed Statement of Cash Flows for the six months ended June 30, 2007 were as follows:

(in millions)	Originally Reported June 30, 2007	Revisions	As Revised
Cash flows provided by (used in) operating activities	$ 743	$(1,819)	$ (1,076)
Cash flows provided by (used in) investing activities	(7,215)	114	(7,101)
Cash flows provided by (used in) financing activities	6,432	1,705	8,137

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

10. Cash Flows

During 2007, AIG made certain revisions to the Consolidated Statement of Cash Flows, primarily relating to the effect of reclassifying certain policyholders' account balances, the elimination of certain intercompany balances and revisions related to separate account assets. Accordingly, AIG revised the previous periods presented to conform to the revised presentation. There was no effect on ending cash balances.

In addition, the table below reflects the effects of the adoption of FSP FIN 39-1 as discussed in Note 1, Summary of Significant Accounting Policies.

The revisions and their effect on the Consolidated Statement of Cash Flows for the six months ended June 30, 2007 were as follows:

(in millions)	Originally Reported June 30, 2007	Revisions	As Revised
Cash flows provided by (used in) from operating activities	$ 15,071	$ 2,360	$ 17,431
Cash flows provided by (used in) from investing activities	(37,873)	(2,441)	(40,314)
Cash flows provided by (used in) financing activities	22,866	81	22,947

ITEM 2. Management's Discussion and Analysis of Financial Condition and Results of Operations

Management's Discussion and Analysis of Financial Condition and Results of Operations is designed to provide the reader a narrative with respect to AIG's operations, financial condition and liquidity and certain other significant matters.

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Cautionary Statement Regarding Projections and Other Information About Future Events

This Quarterly Report on Form 10-Q and other publicly available documents may include, and AIG's officers and representatives may from time to time make, projections concerning financial information and statements concerning future economic performance and events, plans and objectives relating to management, operations, products and services, and assumptions underlying these projections and statements. These projections and statements are not historical facts but instead represent only AIG's belief regarding future events, many of which, by their nature, are inherently uncertain and outside AIG's control. These projections and statements may address, among other things, the status and potential future outcome of the current regulatory and civil proceedings against AIG and their potential effect on AIG's businesses, financial condition, results of operations, cash flows and liquidity, AIG's exposures to subprime mortgages, monoline insurers and the residential and commercial real estate markets and AIG's strategy for growth, product development, market position, financial results and reserves. It is possible that AIG's actual results and financial condition may differ, possibly materially, from the anticipated results and financial condition indicated in these projections and statements. Factors that could cause AIG's actual results to differ, possibly materially, from those in the specific projections and statements are discussed in Outlook and throughout this Management's Discussion and Analysis of Financial Condition and Results of Operations and in Item 1A. Risk Factors of AIG's Annual Report on Form 10-K for the year ended December 31, 2007 (2007 Annual Report on Form 10-K). AIG is not under any obligation (and expressly disclaims any such obligations) to update or alter any projection or other statement, whether written or oral, that may be made from time to time, whether as a result of new information, future events or otherwise.

In addition to reviewing AIG's results for the three and six months ended June 30, 2008, this Management's Discussion and Analysis of Financial Condition and Results of Operations supplements and updates the information and discussion included in the 2007 Annual Report on Form 10-K. Throughout this Management's Discussion and Analysis of Financial Condition and Results of Operations, AIG presents its operations in the way it believes will be most meaningful. Statutory loss ratios and combined ratios are presented in accordance with accounting principles prescribed by insurance regulatory authorities because these are standard measures of performance filed with insurance regulatory authorities and used for analysis in the insurance industry and thus allow more meaningful comparisons with AIG's insurance competitors. AIG also uses cross-references to additional information included in this Quarterly Report on Form 10-Q and in the 2007 Annual Report on Form 10-K to assist readers seeking related information on a particular subject.

Overview of Operations and Business Results

AIG identifies its reportable segments by product line, consistent with its management structure. These segments are General Insurance, Life Insurance & Retirement Services, Financial Services and Asset Management. Through these operating segments, AIG provides insurance, financial and investment products and services to both businesses and individuals in more than 130 countries and jurisdictions. This geographic, product and service diversification is one of AIG's major strengths and sets it apart from its competitors. AIG's Other category consists of items not allocated to AIG's operating segments.

AIG's subsidiaries serve commercial, institutional and individual customers through an extensive property-casualty and life insurance and retirement services network. In the United States, AIG companies are the largest underwriters of commercial and industrial insurance and are among the largest life insurance and retirement services operations as well. AIG's Financial Services businesses include commercial aircraft and equipment leasing, capital markets operations and consumer finance, both in the United States and abroad. AIG also provides asset management services to institutions and individuals. As part of its Spread-Based Investment activities, and to finance its operations, AIG issues various debt instruments in the public and private markets.

Outlook

The following paragraphs supplement and update the information and discussion included in Management's Discussion and Analysis of Financial Condition and Results of Operations — Outlook in the 2007 Annual Report on Form 10-K to reflect developments in or affecting AIG's business to date during 2008. These paragraphs also supplement and update Item 1A. Risk Factors in the 2007 Annual Report on Form 10-K.

General Trends

In mid-2007, the U.S. residential mortgage market began to experience serious disruption due to credit quality deterioration in a significant portion of loans originated, particularly to non-prime and subprime borrowers; evolving changes in the regulatory environment; a residential housing market characterized by a slowing pace of transactions and declining prices; increased cost and reduced availability of borrowings for mortgage participants; a rising unemployment rate; increased delinquencies in non-mortgage consumer credit; and illiquid credit markets. The conditions continued and worsened throughout 2007 and to date in 2008, expanding into the broader U.S. credit markets and resulting in greater volatility, less liquidity, widening of credit spreads, a lack of price transparency and increased credit losses in certain markets.

AIG participates in the U.S. residential mortgage market in several ways: American General Finance, Inc. (AGF) originates principally first-lien mortgage loans and to a lesser extent second-lien mortgage loans to buyers and owners of residential housing; United Guaranty Corporation (UGC) provides first loss mortgage guaranty insurance for high loan-to-value first- and second-lien residential mortgages; AIG insurance and financial services subsidiaries invest in mortgage-backed securities and collateralized debt obligations (CDOs), in which the underlying collateral is composed in whole or in part of residential mortgage loans; and AIG Financial Products Corp. and AIG Trading Group Inc. and their respective subsidiaries (collectively, AIGFP) provides credit protection through credit default swaps on certain super senior tranches of CDOs.

Continuing disruption in the U.S. residential mortgage and other credit markets may also increase claim activity in the financial institution segment of AIG's directors and officers liability (D&O) and professional liability classes of business. However, based on its review of information currently available, AIG believes overall loss activity for the broader D&O and professional liability classes is likely to remain within or near the levels observed during the last several years, which include losses related to stock options backdating as well as to the U.S. residential mortgage market.

The operating results of AIG's consumer finance and mortgage guaranty operations in the United States have been and are likely to continue to be adversely affected by the factors referred to above. The downward cycle in the U.S. housing market is not expected to improve until residential inventories return to a more normal level and the mortgage credit market stabilizes. The duration and severity of the downward cycle could be further negatively affected in the event of an economic recession. AIG expects that this

downward cycle will continue to adversely affect UGC's operating results for the foreseeable future and will result in a significant operating loss for UGC through at least the first half of 2009. AIG also incurred substantial unrealized market valuation losses on AIGFP's super senior credit default swap portfolio and substantial other-than-temporary impairment charges on AIG's available for sale securities in the first six months of 2008 and fourth quarter of 2007. The results from AIG's operations with exposure to the U.S. residential mortgage market will be highly dependent on future market conditions. Continuing market deterioration will cause AIG to report additional unrealized market valuation losses and impairment charges. Given the current difficult market conditions, AIG is not able to predict the extent of any future market valuation losses or impairment charges. Moreover, AIG is unable to assess the effect, if any, that recent transactions involving sales of large portfolios of CDOs will have on the pricing of its credit default swaps, referenced CDOs or available for sale securities or on collateral posting requirements. There can be no assurance that increased claims activity, operating losses, unrealized market valuation losses and impairment charges will not be material to AIG's consolidated financial condition or AIG's consolidated results of operations for an individual reporting period.

The ongoing effect of the downward cycle in the U.S. housing market on AIG's consolidated financial condition could be material if the market disruption continues to expand beyond the residential mortgage markets, notwithstanding AIG's efforts to mitigate the risks to its business by disciplined underwriting and active risk management. AIG is also exploring measures to further protect its capital, reduce risks where appropriate and enhance its overall liquidity.

A significant portion of AIGFP's guaranteed investment agreements (GIAs) and financial derivative transactions include provisions that require AIGFP, upon a downgrade of AIG's long-term debt ratings, to post collateral or, with the consent of the counterparties, assign or repay its positions or arrange a substitute guarantee of its obligations by an obligor with higher debt ratings.

It is estimated that, as of the close of business on July 31, 2008, based on AIGFP's outstanding municipal GIAs and financial derivative transactions at that date, a downgrade of AIG's long-term senior debt ratings to 'A1' by Moody's Investors Service (Moody's) and 'A+' by Standard & Poor's, a division of The McGraw-Hill Companies, Inc. (S&P), would permit counterparties to make additional calls for up to approximately $13.3 billion of collateral, while a downgrade to 'A2' by Moody's and 'A' by S&P would permit counterparties to call for approximately $1.2 billion of additional collateral. If either of Moody's or S&P downgraded AIG's ratings to 'A1' or 'A+', respectively, the estimated collateral call would be for up to approximately $10.5 billion, while a downgrade to 'A2' or 'A', respectively, by either of the two rating agencies would permit counterparties to call for up to approximately $1.1 billion of additional collateral.

Furthermore, a downgrade of AIG's long-term senior debt ratings to 'A1' by Moody's or to the same levels by both rating agencies would permit either AIG or the counterparties to elect early termination of contracts resulting in payments of up to approximately $4.6 billion, while a downgrade to 'A2' by Moody's and 'A' by S&P would permit either AIG or the counterparties to elect early termination of additional contracts resulting in additional payments of up to approximately $800 million. AIGFP believes that it is unlikely that certain of these counterparties would exercise their rights to elect termination of their contracts given the substantial economic benefit that such counterparties would forfeit upon termination.

The actual amount of collateral that AIGFP would be required to post to counterparties in the event of such downgrades, or the aggregate amount of payments that AIG could be required to make, depends on market conditions, the fair value of outstanding affected transactions and other factors prevailing at the time of the downgrade. Additional obligations to post collateral or the costs of assignment, repayment or alternative credit support would increase the demands on AIG's liquidity. Further downgrades could result in requirements for substantial additional collateral, which could have a material adverse effect on AIG's liquidity. For a further discussion of AIG's credit ratings and the potential effect of posting collateral on AIG's liquidity, see — Capital Resources and Liquidity — Credit Ratings and — Liquidity herein.

Globally, heightened regulatory scrutiny of financial services companies in many jurisdictions has the potential to affect future financial results through higher compliance costs. This is particularly true in the United States, where federal and state authorities have commenced various investigations of the financial services industry, and in Japan and Southeast Asia, where financial institutions have received remediation orders affecting consumer and policyholder rights.

As a result of the disruption of the U.S. residential housing market, AIG recognized other-than-temporary impairment charges over the last three quarters. Accordingly, any accretion to the expected recovery amount will be recognized in earnings in future periods over the expected recovery periods.

AIG tested goodwill for impairment as of June 30, 2008 and no impairment was identified. However, as a result of structural trends in the consumer finance market and the current competitive environment in the personal lines market,

the excess of the fair value over the carrying value of AIG's Consumer Finance and Personal Lines reporting units has narrowed. As of June 30, 2008, goodwill related to each of these reporting units amounted to approximately $700 million. A continuation of these trends could result in impairment in goodwill for these reporting units in the future.

General Insurance

The commercial property and casualty insurance industry has historically experienced cycles of price erosion followed by rate strengthening as a result of catastrophes or other significant losses that affect the overall capacity of the industry to provide coverage. As premium rates decline, AIG will generally experience higher current accident year loss ratios, as the written premiums are earned, and higher expense ratios if written premiums decline more quickly than expenses. Despite industry price erosion in commercial lines, AIG expects to continue to identify profitable opportunities and build attractive new general insurance businesses as a result of AIG's broad product line and extensive distribution networks in the United States and abroad.

Workers compensation remains under considerable pricing pressure, as statutory rates continue to decline. Rates for most casualty lines of insurance continue to decline due to competitive pressures, particularly for aviation, excess casualty and D&O exposures. Rates for commercial property lines are also declining following another year of relatively low catastrophe losses in 2007, a decline that is continuing despite increased natural catastrophe losses in 2008. Further price erosion is expected during the remainder of 2008 for the commercial lines. AIG seeks to mitigate the decline by constantly seeking out profitable opportunities across its diverse product lines and distribution networks while maintaining a commitment to underwriting discipline. There can be no assurance that price erosion will not become more widespread or that AIG's profitability will not deteriorate from current levels in major commercial lines.

The personal lines automobile insurance industry is currently experiencing a soft market. Industry underwriting results are expected to deteriorate due to a generally weakening economy and increasing loss trends. AIG's personal auto business has been affected by these trends, but AIG has filed rate increases, tightened underwriting guidelines and made pricing enhancements to seek to improve the underwriting results.

AIG has capital maintenance agreements with the companies included in the Commercial Insurance and Mortgage Guaranty reporting units that set forth procedures through which AIG will provide ongoing capital support. AIG expects that additional capital contributions may be required during the remainder of 2008 pursuant to these agreements.

Life Insurance & Retirement Services

Disruption in the U.S. residential mortgage and credit markets had a significant adverse effect on Life Insurance & Retirement Services operating results, specifically its net investment income and net realized capital losses in 2007 and the first six months of 2008, and AIG expects that this disruption will continue to be a key factor in the remainder of 2008 and beyond, especially in its U.S.-based operations. The volatility in operating results will be further magnified by the continuing market shift to variable products with living benefits.

In response to the market disruption, AIG, including Domestic Life and Domestic Retirement Services, has been increasing its liquidity position and investing in shorter duration investments. While prudent in the current environment, such actions will reduce overall investment yields for the foreseeable future.

Recent capital markets volatility has put pressure on credit lenders resulting in increased costs for premium financing, which could affect future sales of products where such financing is used, primarily in large universal life policies in Domestic Life Insurance.

The U.S. dollar has significantly weakened against many currencies, resulting in a favorable effect on operating results due to the translation of foreign currencies to the U.S. dollar. However, the weakened dollar has an unfavorable effect on other-than-temporary impairments in Foreign Life Insurance & Retirement Services and will continue to affect operating results throughout 2008.

During the second quarter of 2008, AIG made capital contributions aggregating $1.1 billion to the surplus of certain of its Domestic Life Insurance and Domestic Retirement Services subsidiaries to replace a portion of the capital lost as a result of net realized capital losses, including other-than temporary impairments. In Taiwan, $361 million was contributed to meet the needs of this growing business and increased risk-based capital requirements. AIG expects that it will make additional capital contributions to these operations during the remainder of 2008, in large measure due to the continued effect of net realized capital losses resulting from severity-related other-than-temporary impairment charges.

Financial Services

During 2008, AIGFP's revenues from certain products have declined, in part, as a consequence of the continued disruption in the credit markets, the general decline in liquidity in the marketplace, and AIGFP's efforts to manage its liquidity. Furthermore, AIGFP has not been able to replace revenues previously generated from certain structured tax and credit derivative transactions that were terminated or matured at the end of 2007 and early 2008. AIG expects that

AIGFP's operating results will continue to be adversely affected for the foreseeable future.

AIG exercises significant judgment in the valuation of its various credit default swap portfolios. AIG uses pricing models and other methodologies to value these portfolios that take into account, where applicable, and to the extent possible, third-party prices, pricing matrices, the movement of indices (such as the CDX and iTraxx), collateral calls and other observable market data. AIG believes that the assumptions and judgments it makes are reasonable and lead to an overall methodology that is reasonable, but other market participants may use other methodologies, including, among other things, models, indices and selection of third-party pricing sources, that are based upon different assumptions and judgments, and these methodologies may generate materially different values.

For additional information regarding AIG's methodology, models and assumptions with respect to the valuation and credit-based analyses of the AIGFP super senior credit default swap portfolio, see Critical Accounting Estimates — Fair Value Measurements of Certain Financial Assets and Liabilities — AIGFP's Super Senior Credit Default Swap Portfolio, and — Valuation of Level 3 Assets and Liabilities — Super senior credit default swap portfolio. See Risk Management — Credit Derivatives.

The ongoing disruption in the U.S. residential mortgage and credit markets and the downgrades of residential mortgage-backed securities and CDO securities by rating agencies continue to adversely affect the fair value of the super senior credit default swap portfolio written by AIGFP. AIG expects that continuing limitations on the availability of market observable data will affect AIG's determinations of the fair value of these derivatives. The fair value of these derivatives is expected to continue to fluctuate, perhaps materially, in response to changing market conditions, and AIG's estimates of the value of AIGFP's super senior credit default swap portfolio at future dates could therefore be materially different from current estimates. Further declines in the fair values of these derivatives may also require AIGFP to post additional collateral which may be material to AIGFP's financial condition.

At June 30, 2008, the fair value of AIGFP's super senior credit default swap portfolio, a net loss of $26.1 billion, represents AIG's best estimate of the amount it would need to pay a willing, able and knowledgeable third party to assume the obligations under AIGFP's super senior credit default swap portfolio at that date.

At June 30, 2008, AIG used a roll rate analysis to stress the AIGFP super senior multi-sector CDO credit default swap portfolio for potential pre-tax realized credit losses. Two scenarios illustrated in this process resulted in potential realized credit losses of approximately $5.0 billion (Scenario A) and approximately $8.5 billion (Scenario B). Actual ultimate realized credit losses are likely to vary, perhaps materially, from these scenarios, and there can be no assurance that the ultimate realized credit losses related to the AIGFP super senior multi-sector CDO credit default swap portfolio will be consistent with either scenario or that such realized credit losses will not exceed the potential realized credit losses illustrated by Scenario B. For a further discussion of AIG's stress testing using the roll rate analyses, see Risk Management — Stress Testing/Sensitivity Analysis.

Approximately $307 billion of the $441 billion in notional exposure on AIGFP's super senior credit default swap portfolio as of June 30, 2008 was written to facilitate regulatory capital relief for financial institutions primarily in Europe. AIG expects that the majority of these transactions will be terminated within the next 9 to 21 months by AIGFP's counterparties when they no longer provide the regulatory capital benefit.

In light of early termination experience to date and after other comprehensive analyses, AIG determined that there was no unrealized market valuation adjustment to be recognized for this regulatory capital relief portfolio for the six months ended June 30, 2008 other than for transactions where AIGFP believes the counterparties are no longer using the transactions to obtain regulatory capital relief. AIG will continue to assess the valuation of this portfolio and monitor developments in the marketplace. Given the significant deterioration in the global credit markets and the risk that AIGFP's expectations with respect to the termination of these transactions by its counterparties may not materialize, there can be no assurance that AIG will not recognize unrealized market valuation losses from this portfolio in future periods, and recognition of even a small percentage decline in the fair value of this portfolio could be material to an individual reporting period. These transactions contributed approximately $156 million to AIGFP's revenues in the six-month period ended June 30, 2008. If AIGFP is not successful in replacing the revenues generated by these transactions, AIGFP's operating results could be materially adversely affected.

The airline industry is experiencing financial stress primarily due to record-high fuel costs, tightening of the credit markets and generally worsening economic conditions. This financial stress is causing a slow-down in the airline industry, and will likely have a negative effect on future lease rates and could begin to influence ILFC's results of operations as some airlines may approach ILFC to renegotiate transactions.

Asset Management

In the Institutional Asset Management business, management fees are earned based on the value of assets under management or committed capital. Declines in the equity and credit markets negatively affect the value of these investments

which may result in lower base management fees. Additionally, real estate investments are made through AIG Global Real Estate Investment Corp. (AIG Global Real Estate), typically for the purpose of development or repositioning and subsequent sale. Softening of the real estate and/or credit markets may delay the timing of development, repositioning and subsequent sale of these investments.

From time to time, AIG Global Asset Management Holdings Corp. and its subsidiaries and affiliated companies (collectively, AIG Investments) acquires alternative investments, primarily consisting of direct controlling equity interests in private enterprises, with the intention of transferring such investments to a to-be-established AIG sponsored fund or acquiring such investments to be held temporarily until distribution to a third party or AIG affiliate is completed (warehoused assets). Market conditions may impede AIG from launching new investment products for which these warehoused assets are being held. Market conditions may also prevent AIG from recovering its investment upon transfer or divestment.

For a description of important factors that may affect the operations and initiatives described above, see Item 1A. Risk Factors in the 2007 Annual Report on Form 10-K.

Consolidated Results

AIG's consolidated revenues, income (loss) before income taxes, minority interest and net income (loss) were as follows:

(in millions)	Three Months Ended June 30, **2008**	2007	Percentage Increase/ (Decrease)	Six Months Ended June 30, **2008**	2007	Percentage Increase/ (Decrease)
Total revenues	**$ 19,933**	$31,150	(36)%	**$ 33,964**	$61,795	(45)%
Income (loss) before income taxes and minority interest	**(8,756)**	6,328	—	**(20,020)**	12,500	—
Net income (loss)	**$ (5,357)**	$ 4,277	—%	**$(13,162)**	$ 8,407	—%

AIG's consolidated revenues decreased in the three and six-month periods ended June 30, 2008 compared to the same periods in 2007 due to unrealized market valuation losses of $5.6 billion and $14.7 billion, respectively, on AIGFP's super senior credit default swap portfolio recorded in other income, higher net realized capital losses and a decline in net investment income, which more than offset growth in premiums and other considerations in the Life Insurance & Retirement Services segment. Net realized capital losses of $6.1 billion and $12.2 billion in the three and six-month periods ended June 30, 2008, respectively, included other-than-temporary impairment charges of $6.8 billion and $12.4 billion, primarily related to the significant disruption in the residential mortgage and credit markets and investment-related losses of $241 million and $1.0 billion where AIG lacks the intent to hold the investments to recovery. Total other-than-temporary impairment charges in the three- and six-month periods ended June 30, 2007 were $417 million and $884 million, respectively. See Invested Assets — Portfolio Review — Other-Than-Temporary Impairments herein. The decline in net investment income reflects higher trading account losses in the U.K., lower returns from yield enhancement income, partnerships, hedge funds and mutual funds as well as lower policyholder trading gains in Life Insurance & Retirement Services. Policyholder trading gains are offset by a charge to incurred policy losses and benefits expense.

Income (loss) before income taxes and minority interest declined in the three- and six-month periods ended June 30, 2008 due primarily to the losses described above.

Income Taxes

The effective tax rate on the pre-tax loss for the three-month period ended June 30, 2008 was 38.4 percent. The effective tax rate was higher than the statutory rate of 35 percent due primarily to tax benefits from foreign operations and tax exempt interest. The effective tax rate on the pre-tax loss for the six-month period ended June 30, 2008 was 34.4 percent. The effective tax rate was adversely affected by $703 million of tax charges from the first three months of 2008, comprised of increases in the reserves for uncertain tax positions and other discrete period items. The effective tax rate on the pre-tax income for the three- and six-month periods ended June 30, 2007 was 26.5 percent and 27.2 percent, respectively. The effective tax rates were low due primarily to benefits from remediation adjustments and the recognition of tax benefits associated with the SICO Plan for which the compensation expense was recognized in prior years. See also Note 8 to Consolidated Financial Statements.

Segment Results

The following table summarizes the operations of each principal segment: (See also Note 2 to Consolidated Financial Statements.)

Operating Segments *(in millions)*	Three Months Ended June 30, **2008**	2007	Percentage Increase/ (Decrease)	Six Months Ended June 30, **2008**	2007	Percentage Increase/ (Decrease)
Total revenues[(a)]:						
General Insurance	**$ 12,757**	$12,928	(1)%	**$ 25,046**	$25,831	(3)%
Life Insurance & Retirement Services[(b)]	**10,161**	14,023	(28)	**18,913**	27,705	(32)
Financial Services[(c)(d)]	**(3,605)**	2,123	—	**(10,165)**	4,324	—
Asset Management[(e)]	**797**	1,781	(55)	**648**	3,450	(81)
Other	**208**	263	(21)	**80**	394	(80)
Consolidation and eliminations	**(385)**	32	—	**(558)**	91	—
Total	**$ 19,933**	$31,150	(36)%	**$ 33,964**	$61,795	(45)%
Operating income (loss)[(a)]:						
General Insurance	**$ 827**	$ 2,976	(72)%	**$ 2,164**	$ 6,072	(64)%
Life Insurance & Retirement Services[(b)]	**(2,401)**	2,620	—	**(4,232)**	4,901	—
Financial Services[(c)(d)]	**(5,905)**	47	—	**(14,677)**	339	—
Asset Management[(e)]	**(314)**	927	—	**(1,565)**	1,685	—
Other	**(715)**	(460)	—	**(1,483)**	(930)	—
Consolidation and eliminations	**(248)**	218	—	**(227)**	433	—
Total	**$ (8,756)**	$ 6,328	—	**$(20,020)**	$12,500	—%

(a) Includes other-than-temporary impairment charges of $6.8 billion and $417 million for the three-month periods ended June 30, 2008 and 2007, respectively, and $12.4 billion and $884 million for the six-month periods ended June 30, 2008 and 2007, respectively. Also includes gains (losses) from hedging activities that did not qualify for hedge accounting treatment under FAS No. 133, "Accounting for Derivative Instruments and Hedging Activities" (FAS 133), including the related foreign exchange gains and losses. For the three-month periods ended June 30, 2008 and 2007, the effect was $272 million and $(430) million, respectively, in both revenues and operating income (loss). For the six-month periods ended June 30, 2008 and 2007, the effect was $(476) million and $(882) million, respectively, in both revenues and operating income (loss). These amounts result primarily from interest rate and foreign currency derivatives that are effective economic hedges of investments and borrowings.

(b) Includes other-than-temporary impairment charges of $5.2 billion and $324 million for the three-month periods ended June 30, 2008 and 2007, respectively, and $9.6 billion and $716 million for the six-month periods ended June 30, 2008 and 2007, respectively.

(c) Includes gains (losses) from hedging activities that did not qualify for hedge accounting treatment under FAS 133, including the related foreign exchange gains and losses. For the three-month periods ended June 30, 2008 and 2007, the effect was $5 million and $(443) million, respectively, in both revenues and operating income (loss). For the six-month periods ended June 30, 2008 and 2007, the effect was $(199) million and $(603) million, respectively, in both revenues and operating income (loss). These amounts result primarily from interest rate and foreign currency derivatives that are effective economic hedges of investments and borrowings.

(d) For the three- and six-month periods ended June 30, 2008, both revenues and operating income (loss) include unrealized market valuation losses of $5.6 billion and $14.7 billion, respectively, on AIGFP's super senior credit default swap portfolio.

(e) Includes net realized capital losses of $464 million and $1.9 billion for the three- and six-month periods ended June 30, 2008, respectively, including other-than-temporary impairment charges of $882 million and $1.9 billion, respectively.

General Insurance

AIG's General Insurance operations provide property and casualty products and services throughout the world. Revenues in the General Insurance segment represent net premiums earned, net investment income and net realized capital gains (losses). The decrease in General Insurance revenues in the three-month period ended June 30, 2008 compared to the same period in 2007 was due to higher net realized capital losses in the three-month period ended June 30, 2008 compared to the same period in 2007 and lower net investment income as returns on partnership investments declined. The decrease in General Insurance revenues in the six-month period ended June 30, 2008 compared to the same period in 2007 was due to net realized capital losses in the six-month period ended June 30, 2008 compared to net realized capital gains in the same period of 2007 and lower net investment income as returns on partnership investments declined. The decrease in General Insurance operating income in the three- and six-month periods ended June 30, 2008 compared to the same period in 2007 was principally due to lower underwriting profit and net investment income from AIG Commercial Insurance (Commercial Insurance) as well as net realized capital losses incurred by Commercial Insurance in 2008. Operating losses from the Mortgage Guaranty business and a decline in Foreign General Insurance net investment income in 2008 also contributed to the decrease in General Insurance operating income.

Life Insurance & Retirement Services

AIG's Life Insurance & Retirement Services operations provide insurance, financial and investment-oriented products throughout the world. Revenues in the Life Insurance & Retirement Services operations represent premiums and other considerations, net investment income and net realized capital gains (losses). Foreign operations contributed approximately 80 percent of AIG's Life Insurance & Retirement Services premiums and other considerations for both the three- and six-month periods ended June 30, 2008 and 2007.

Life Insurance & Retirement Services reported operating losses in the three- and six-month periods of 2008 compared to operating income in the same period in 2007, primarily due to lower net investment income and higher net realized capital losses in 2008, which were partially offset by the favorable effect of foreign exchange rates, lower deferred

policy acquisition costs (DAC) and sales inducement asset (SIA) amortization related to realized capital losses, growth in the underlying reserves which reflects increased assets under management and increased business in force.

Financial Services

AIG's Financial Services subsidiaries engage in diversified activities including aircraft and equipment leasing, capital markets, consumer finance and insurance premium finance. Revenues in the Financial Services segment include interest, realized and unrealized gains and losses, including the unrealized market valuation losses on AIGFP's super senior credit default swap portfolio, and lease and finance charges.

Financial Services reported operating losses in the three- and six-month periods ended June 30, 2008 compared to operating income in the same periods in 2007, primarily due to unrealized market valuation losses of $5.6 billion and $14.7 billion in the three- and six-month periods ended June 30, 2008, respectively, on AIGFP's super senior credit default swap portfolio, the remaining operating loss resulting from the change in credit spreads on AIGFP's other assets and liabilities and a decline in operating income for AGF. Capital Markets net operating loss for the three- and six-month periods ended June 30, 2008 was $6.3 billion and $15.2 billion, respectively, reflecting the pre-tax unrealized market valuation loss on the super senior credit default swap portfolio. Included in the unrealized market valuation loss were gains of $44 million and $109 million as a result of the effects of AIG's own credit spreads on the valuation of these derivatives for the three- and six-month periods ended June 30, 2008, respectively. The effect of the changes in AIG's own credit spreads, including the aforementioned amounts reflected in the unrealized market valuation loss, was a decrease in pre-tax income of $112 million and an increase of $2.5 billion for the three- and six-month periods ended June 30, 2008, respectively. The effect of the changes in counterparty credit spreads for assets measured at fair value at AIGFP was a decrease of $362 million and $3.0 billion for the three- and six-month periods ended June 30, 2008, respectively. On January 1, 2008, AIGFP elected the fair value option for almost all of its eligible financial assets and liabilities. Included in the first quarter 2008 net operating loss was the transition amount of $291 million related to the adoption of FAS 157 and FAS 159.

AGF's operating income declined in the three- and six-month periods ended June 30, 2008 compared to the same periods in 2007, primarily due to increases in the provision for finance receivable losses and unfavorable variances related to derivatives which economically hedge AGF debt. AGF's operating income for the three- and six- month periods ended June 30, 2008 also reflected a pre-tax charge of $27 million resulting from AGF's decision to cease its wholesale originations (originations through mortgage brokers).

In the second quarter and first six months of 2007, the domestic consumer finance operations recorded pre-tax charges of $50 million and $178 million, respectively, representing the estimated cost of implementing the Supervisory Agreement entered into with the Office of Thrift Supervision (OTS), which are discussed in the Consumer Finance results of operations section. Based on the current estimated cost of implementing the Supervisory Agreement, partial reversals of these prior year charges of $25 million and $43 million were recorded for the three- and six-month periods ended June 30, 2008, respectively.

Operating income for ILFC increased in the three and six-month periods ended June 30, 2008 compared to the same periods in 2007 driven to a large extent by a larger aircraft fleet, higher lease rates and higher utilization and lower composite borrowing rates.

Asset Management

AIG's Asset Management operations include institutional asset management, broker-dealer related services and mutual funds and the Spread-Based Investment business. Revenues in the Asset Management segment represent investment income with respect to spread-based products, and management and advisory fees, carried interest revenues on the performance of the underlying funds, and realized gains on real estate investments in institutional products.

Asset Management reported operating losses in the three- and six-month periods ended June 30, 2008 compared to operating income in the same periods in 2007, due to other-than-temporary impairment charges on fixed maturity securities, lower partnership income and a decline in carried interest revenues. 2007 results included a gain of $398 million related to the sale of a portion of AIG's investment in The Blackstone Group L.P. in connection with its initial public offering.

Capital Resources

At June 30, 2008, AIG had total consolidated shareholders' equity of $78.1 billion and total consolidated borrowings of $178.6 billion. At that date, $68.6 billion of such borrowings were subsidiary borrowings not guaranteed by AIG.

In May 2008, AIG raised a total of approximately $20 billion through the sale of: (i) 196,710,525 shares of AIG common stock at a price per share of $38, for an aggregate amount of $7.47 billion; (ii) 78.4 million equity units at a price per unit of $75, for an aggregate amount of $5.88 billion; and (iii) $6.9 billion of junior subordinated debentures in three series. The equity units and junior subordinated debentures receive hybrid equity treatment from the major rating agencies under their current policies.

Liquidity

AIG manages liquidity at both the subsidiary and parent company levels. At June 30, 2008, AIG's consolidated invested assets, primarily held by its subsidiaries, included $82.2 billion in cash and short-term investments. Consolidated net cash provided from operating activities in the first six months of 2008 amounted to $16.6 billion. At both the subsidiary and parent company level, liquidity management activities are intended to preserve and enhance funding stability, flexibility, and diversity through a wide range of potential operating environments and market conditions. AIG's primary sources of cash flow are dividends and other payments from its regulated and unregulated subsidiaries, as well as issuances of debt and equity securities. Primary uses of cash flow are for debt service, subsidiary funding, shareholder dividend payments and common stock repurchases. Management believes that AIG's liquid assets, cash provided by operations and access to the capital markets will enable it to meet its anticipated cash requirements.

For additional information, see Capital Resources and Liquidity.

Critical Accounting Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America (GAAP) requires the application of accounting policies that often involve a significant degree of judgment. AIG considers that its accounting policies that are most dependent on the application of estimates and assumptions, and therefore viewed as critical accounting estimates, to be those relating to reserves for losses and loss expenses, future policy benefits for life and accident and health contracts, recoverability of DAC, estimated gross profits for investment-oriented products, fair value measurements of certain financial assets and liabilities, other-than-temporary impairments, the allowance for finance receivable losses and flight equipment recoverability. These accounting estimates require the use of assumptions about matters, some of which are highly uncertain at the time of estimation. To the extent actual experience differs from the assumptions used, AIG's results of operations would be directly affected.

Throughout this Management's Discussion and Analysis of Financial Condition and Results of Operations, AIG's critical accounting estimates are discussed in detail. The major categories for which assumptions are developed and used to establish each critical accounting estimate are highlighted below.

Reserves for Losses and Loss Expenses (General Insurance):

- *Loss trend factors:* used to establish expected loss ratios for subsequent accident years based on premium rate adequacy and the projected loss ratio with respect to prior accident years.
- *Expected loss ratios for the latest accident year:* in this case, accident year 2008 for the year-end 2008 loss reserve analysis. For low-frequency, high-severity classes such as excess casualty, expected loss ratios generally are utilized for at least the three most recent accident years.
- *Loss development factors:* used to project the reported losses for each accident year to an ultimate amount.
- *Reinsurance recoverable on unpaid losses:* the expected recoveries from reinsurers on losses that have not yet been reported and/or settled.

Future Policy Benefits for Life and Accident and Health Contracts (Life Insurance & Retirement Services):

- *Interest rates:* which vary by geographical region, year of issuance and products.
- *Mortality, morbidity and surrender rates:* based upon actual experience by geographical region modified to allow for variation in policy form, risk classification and distribution channel.

Deferred Policy Acquisition Costs (Life Insurance & Retirement Services):

- *Recoverability:* based on current and future expected profitability, which is affected by interest rates, foreign exchange rates, mortality/morbidity experience, expenses, investment returns and policy persistency.

Deferred Policy Acquisition Costs (General Insurance):

- *Recoverability:* based upon the current terms and profitability of the underlying insurance contracts.

Estimated Gross Profits for Investment-Oriented Products (Life Insurance & Retirement Services):

- *Estimated gross profits:* to be realized over the estimated duration of the contracts (investment-oriented products) affect the carrying value of DAC, unearned revenue liability, SIAs and associated amortization patterns. Estimated gross profits include investment income and gains and losses on investments less required interest, actual mortality and other expenses.

Allowance for Finance Receivable Losses (Financial Services):

- *Historical defaults and delinquency experience:* utilizing factors, such as delinquency ratio, allowance ratio, charge-off ratio and charge-off coverage.
- *Portfolio characteristics:* portfolio composition and consideration of the recent changes to underwriting criteria and portfolio seasoning.
- *External factors:* consideration of current economic conditions, including levels of unemployment and personal bankruptcies.

- *Migration analysis:* empirical technique measuring historical movement of similar finance receivables through various levels of repayment, delinquency, and loss categories to existing finance receivable pools.

Flight Equipment Recoverability (Financial Services):

- *Expected undiscounted future net cash flows:* based upon current lease rates, projected future lease rates and estimated terminal values of each aircraft based on expectations of market participants.

Other-Than-Temporary Impairments:

AIG evaluates its investments for impairment such that a security is considered a candidate for other-than-temporary impairment if it meets any of the following criteria:

- Trading at a significant (25 percent or more) discount to par, amortized cost (if lower) or cost for an extended period of time (nine consecutive months or longer);
- The occurrence of a discrete credit event resulting in (i) the issuer defaulting on a material outstanding obligation; (ii) the issuer seeking protection from creditors under the bankruptcy laws or any similar laws intended for court supervised reorganization of insolvent enterprises; or (iii) the issuer proposing a voluntary reorganization pursuant to which creditors are asked to exchange their claims for cash or securities having a fair value substantially lower than par value of their claims; or
- AIG may not realize a full recovery on its investment, regardless of the occurrence of one of the foregoing events.

The determination that a security has incurred an other-than-temporary decline in value requires the judgment of management and consideration of the fundamental condition of the issuer, its near-term prospects and all the relevant facts and circumstances. The above criteria also consider circumstances of a rapid and severe market valuation decline, such as that experienced in current credit markets, in which AIG could not reasonably assert that the recovery period would be temporary (severity losses). For further discussion, see Invested Assets — Portfolio Review — Other-Than-Temporary Impairments.

At each balance sheet date, AIG evaluates its securities holdings with unrealized losses. When AIG does not intend to hold such securities until they have recovered their cost basis, AIG records the unrealized loss in income. If a loss is recognized from a sale subsequent to a balance sheet date pursuant to changes in circumstances, the loss is recognized in the period in which the intent to hold the securities to recovery no longer existed.

In periods subsequent to the recognition of an other-than-temporary impairment charge for fixed maturity securities, which is not credit or foreign exchange related, AIG generally accretes into income the discount or amortizes the reduced premium resulting from the reduction in cost basis over the remaining life of the security.

Fair Value Measurements of Certain Financial Assets and Liabilities:

AIG measures at fair value on a recurring basis financial instruments in its trading and available for sale securities portfolios, certain mortgage and other loans receivable, certain spot commodities, derivative assets and liabilities, securities purchased (sold) under agreements to resell (repurchase), securities lending invested collateral, non-marketable equity investments, included in other invested assets, certain policyholders' contract deposits, securities and spot commodities sold but not yet purchased, certain trust deposits and deposits due to banks and other depositors, certain long-term borrowings, and certain hybrid financial instruments included in other liabilities. The fair value of a financial instrument is the amount that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date.

The degree of judgment used in measuring the fair value of financial instruments generally correlates with the level of pricing observability. Financial instruments with quoted prices in active markets generally have more pricing observability and less judgment is used in measuring fair value. Conversely, financial instruments traded in other-than-active markets or that do not have quoted prices have less observability and are measured at fair value using valuation models or other pricing techniques that require more judgment. Pricing observability is affected by a number of factors, including the type of financial instrument, whether the financial instrument is new to the market and not yet established, the characteristics specific to the transaction and general market conditions.

Fixed Maturity Securities — Trading and Available for Sale

AIG maximizes the use of observable inputs and minimizes the use of unobservable inputs when measuring fair value. Whenever available, AIG obtains quoted prices in active markets for identical assets at the balance sheet date to measure at fair value fixed maturity securities in its trading and available for sale portfolios. Market price data generally is obtained from exchange or dealer markets.

AIG estimates the fair value of fixed maturity securities not traded in active markets, including securities purchased (sold) under agreements to resell (repurchase) and mortgage and other loans receivable, for which AIG elected the fair value option by referring to traded securities with similar attributes, using dealer quotations and matrix pricing methodologies, or discounted cash flow analyses. This

methodology considers such factors as the issuer's industry, the security's rating and tenor, its coupon rate, its position in the capital structure of the issuer, yield curves, credit curves, prepayment rates and other relevant factors. For fixed maturity securities that are not traded in active markets or that are subject to transfer restrictions, valuations are adjusted to reflect illiquidity and/or non-transferability, and such adjustments generally are based on available market evidence. In the absence of such evidence, management's best estimate is used.

Equity Securities Traded in Active Markets — Trading and Available for Sale

AIG maximizes the use of observable inputs and minimizes the use of unobservable inputs when measuring fair value. Whenever available, AIG obtains quoted prices in active markets for identical assets at the balance sheet date to measure at fair value marketable equity securities in its trading and available for sale portfolios. Market price data generally is obtained from exchange or dealer markets.

Direct Private Equity Securities Not Traded in Active Markets — Other Invested Assets

AIG initially estimates the fair value of equity securities not traded in active markets by reference to the transaction price. This valuation is adjusted only when changes to inputs and assumptions are corroborated by evidence such as transactions in similar instruments, completed or pending third-party transactions in the underlying investment or comparable entities, subsequent rounds of financing, recapitalizations and other transactions across the capital structure, offerings in the equity capital markets, and changes in financial ratios or cash flows. For equity securities that are not traded in active markets or that are subject to transfer restrictions, valuations are adjusted to reflect illiquidity and/or non-transferability and such adjustments generally are based on available market evidence. In the absence of such evidence, management's best estimate is used. AIG initially estimates the fair value of investments in private limited partnerships and hedge funds by reference to the transaction price. Subsequently, AIG obtains the fair value of these investments generally from net asset value information provided by the general partner or manager of the investments, the financial statements of which generally are audited annually.

Separate and Variable Account Assets

Separate and variable account assets are composed primarily of registered and unregistered open-end mutual funds that generally trade daily and are measured at fair value in the manner discussed above for equity securities traded in active markets.

Freestanding Derivatives

Derivative assets and liabilities can be exchange-traded or traded over the counter (OTC). AIG generally values exchange-traded derivatives within portfolios using models that calibrate to market clearing levels and eliminate timing differences between the closing price of the exchange-traded derivatives and their underlying instruments.

OTC derivatives are valued using market transactions and other market evidence whenever possible, including market-based inputs to models, model calibration to market clearing transactions, broker or dealer quotations or alternative pricing sources with reasonable levels of price transparency. When models are used, the selection of a particular model to value an OTC derivative depends on the contractual terms of, and specific risks inherent in, the instrument as well as the availability of pricing information in the market. AIG generally uses similar models to value similar instruments. Valuation models require a variety of inputs, including contractual terms, market prices and rates, yield curves, credit curves, measures of volatility, prepayment rates and correlations of such inputs. For OTC derivatives that trade in liquid markets, such as generic forwards, swaps and options, model inputs can generally be corroborated by observable market data by correlation or other means and model selection does not involve significant management judgment.

Certain OTC derivatives trade in less liquid markets with limited pricing information and the determination of fair value for these derivatives is inherently more difficult. When AIG does not have corroborating market evidence to support significant model inputs and cannot verify the model to market transactions, the transaction price is initially used as the best estimate of fair value. Accordingly, when a pricing model is used to value such an instrument, the model is adjusted so the model value at inception equals the transaction price. Subsequent to initial recognition, AIG updates valuation inputs when corroborated by evidence such as similar market transactions, third-party pricing services and/or broker or dealer quotations, or other empirical market data. When appropriate, valuations are adjusted for various factors such as liquidity, bid/offer spreads and credit considerations. Such adjustments are generally based on available market evidence. In the absence of such evidence, management's best estimate is used.

With the adoption of FAS 157 on January 1, 2008, AIG's own credit risk has been considered and is incorporated into the fair value measurement of all freestanding derivative liabilities.

Embedded Policy Derivatives

The fair value of embedded policy derivatives contained in certain variable annuity and equity-indexed annuity and life contracts is measured based on actuarial and capital market

assumptions related to projected cash flows over the expected lives of the contracts. These cash flow estimates primarily include benefits and related fees assessed, when applicable, and incorporate expectations about policyholder behavior. Estimates of future policyholder behavior are subjective and based primarily on AIG's historical experience. With respect to embedded policy derivatives in AIG's variable annuity contracts, because of the dynamic and complex nature of the expected cash flows, risk neutral valuations are used. Estimating the underlying cash flows for these products involves many estimates and judgments, including those regarding expected market rates of return, market volatility, correlations of market index returns to funds, fund performance, discount rates and policyholder behavior. With respect to embedded policy derivatives in AIG's equity-indexed annuity and life contracts, option pricing models are used to estimate fair value, taking into account assumptions for future equity indexed growth rates, volatility of the equity index, future interest rates, and determination on adjusting the participation rate and the cap on equity indexed credited rates in light of market conditions and policyholder behavior assumptions. With the adoption of FAS 157, these methodologies were not changed, with the exception of incorporating an explicit risk margin to take into consideration market participant estimates of projected cash flows and policyholder behavior.

AIGFP's Super Senior Credit Default Swap Portfolio

AIGFP values its credit default swaps written on the most senior risk layers (super senior) of designated pools of debt securities or loans using internal valuation models, third-party prices and market indices. The specific valuation methodologies vary based on the nature of the referenced obligations and availability of market prices. AIGFP uses a modified version of the Binomial Expansion Technique (BET) model to value its credit default swap portfolio written on super senior tranches of CDOs of asset-backed securities (ABS), including maturity-shortening puts that allow the holders of the securities issued by certain CDOs to treat the securities as short-term eligible 2a-7 investments under the Investment Company Act of 1940 (2a-7 Puts). The BET model uses default probabilities derived from credit spreads implied from market prices for the individual securities included in the underlying collateral pools securing the CDOs, as well as diversity scores, weighted average lives, recovery rates and discount rates. Prices for the individual securities held by a CDO are obtained in most cases from the CDO collateral managers, to the extent available. The CDO collateral managers obtain these prices from various sources, which include dealer quotations, third-party pricing services and in-house valuation models. To the extent there is a lag in the prices provided by the collateral managers, AIGFP rolls forward these prices to the end of the quarter using data provided by a third-party pricing service. Where a price for an individual security is not provided by the CDO collateral manager, AIGFP derives the price from a matrix that averages the prices of the various securities at the level of ABS category, vintage and the rating of the referenced security. The determination of some of these inputs requires the use of judgment and estimates, particularly in the absence of market observable data. AIGFP also employs a Monte Carlo simulation to assist in quantifying the effect on the valuation of the CDOs of the unique aspects of the CDOs' structure such as triggers that divert cash flows to the most senior part of the capital structure. In the determination of fair value, AIGFP also considers collateral calls and the price estimates for the super senior CDO securities provided by third parties, including counterparties to these transactions. See Note 3 to Consolidated Financial Statements for additional information about fair value measurements.

In the case of credit default swaps written on investment-grade corporate debt and CLOs, AIGFP estimates the value of its obligations by reference to the relevant market indices or third-party quotes on the underlying super senior tranches where available.

In the case of credit default swaps written to facilitate regulatory capital relief for AIGFP's European financial institution counterparties, AIGFP estimates the fair value of these derivatives by considering observable market transactions, including the early termination of these transactions by counterparties, and other market data, to the extent relevant.

Policyholders' Contract Deposits

Policyholders' contract deposits accounted for at fair value beginning January 1, 2008 are measured using an income approach by taking into consideration the following factors:

- Current policyholder account values and related surrender charges,
- The present value of estimated future cash inflows (policy fees) and outflows (benefits and maintenance expenses) associated with the product using risk neutral valuations, incorporating expectations about policyholder behavior, market returns and other factors, and
- A risk margin that market participants would require for a market return and the uncertainty inherent in the model inputs.

The change in fair value of these policyholders' contract deposits is recorded as incurred policy losses and benefits in the consolidated statement of income (loss).

Level 3 Assets and Liabilities

Under FAS 157, assets and liabilities recorded at fair value in the consolidated balance sheet are classified in a hierarchy for disclosure purposes consisting of three "levels" based on the

observability of inputs available in the marketplace used to measure the fair value. See Note 3 to the Consolidated Financial Statements for additional information about fair value measurements.

At June 30, 2008, AIG classified $48.7 billion and $37.3 billion of assets and liabilities, respectively, measured at fair value on a recurring basis as Level 3. This represented 4.7 percent and 3.8 percent of the total assets and liabilities, respectively, measured at fair value on a recurring basis. Level 3 fair value measurements are based on valuation techniques that use at least one significant input that is unobservable. These measurements are made under circumstances in which there is little, if any, market activity for the asset or liability. AIG's assessment of the significance of a particular input to the fair value measurement in its entirety requires judgment.

In making the assessment, AIG considers factors specific to the asset or liability. In certain cases, the inputs used to measure fair value of an asset or a liability may fall into different levels of the fair value hierarchy. In such cases, the level in the fair value hierarchy within which the fair value measurement in its entirety is classified is determined based on the lowest level input that is significant to the fair value measurement in its entirety.

Valuation of Level 3 Assets and Liabilities

AIG values its assets and liabilities classified as Level 3 using judgment and valuation models or other pricing techniques that require a variety of inputs including contractual terms, market prices and rates, yield curves, credit curves, measures of volatility, prepayment rates and correlations of such inputs, some of which may be unobservable. The following paragraphs describe the methods AIG uses to measure on a recurring basis the fair value of the major classes of assets and liabilities classified in Level 3.

Private equity and real estate fund investments: These assets initially are valued at the transaction price, i.e., the price paid to acquire the asset. Subsequently, they are measured based on net asset value using information provided by the general partner or manager of these investments, the accounts of which generally are audited on an annual basis.

Corporate bonds and private placement debt: These assets initially are valued at the transaction price. Subsequently, they are valued using market data for similar instruments (e.g., recent transactions, bond spreads or credit default swap spreads), comparisons to benchmark derivative indices or movements in underlying credit spreads. When observable price quotations are not available, fair value is determined based on cash flow models with yield curves, bond or single-name credit default swap spreads and estimated recovery rates.

Certain Residential Mortgage-Backed Securities (RMBS): These assets initially are valued at the transaction price. Subsequently, they may be valued by comparison to transactions in instruments with similar collateral and risk profiles, remittances received and updated cumulative loss data on underlying obligations, discounted cash flow techniques, and/or option adjusted spread analyses.

Certain Asset-Backed Securities — non-mortgage: These assets initially are valued at the transaction price. Subsequently, they may be valued based on external price/spread data. When position-specific external price data are not observable, the valuation is based on prices of comparable securities.

CDOs: These assets initially are valued at the transaction price. Subsequently, they are valued based on external price/spread data from independent third parties, dealer quotations, matrix pricing, or using the BET model.

Super senior credit default swap portfolio: AIGFP wrote credit protection on the super senior risk layer of diversified portfolios of investment-grade corporate debt, CLOs and multi-sector CDOs. In these transactions, AIGFP is at risk only on the super senior portion related to a diversified portfolio referenced to loans or debt securities, which is the last tranche to suffer losses after significant subordination. AIGFP also wrote protection on tranches below the super senior layer.

At June 30, 2008, the notional amount, fair value and unrealized market valuation loss of the AIGFP super senior credit default swap portfolio, including certain regulatory capital relief transactions, by asset class were as follows:

			Unrealized Market Valuation Loss (Gain)	
(in millions)	Notional Amount	Fair Value Loss at June 30, 2008	Three Months Ended June 30, 2008[a]	Six Months Ended June 30, 2008[a]
Regulatory Capital:[b]				
Corporate loans	$172,717	$ —	$ —	$ —
Prime residential mortgages	132,612	—	—	—
Other[c][d]	1,619	125	125	125
Total	306,948	125	125	125
Arbitrage:				
Multi-sector CDOs[e]	80,301	24,785	5,569	13,606
Corporate debt/CLOs	53,767	996	(126)	770
Total	134,068	25,781	5,443	14,376
Mezzanine tranches[f]	5,824	171	(3)	171
Total	$446,840	$26,077[g]	$5,565	$14,672

(a) Includes credit valuation adjustment gains of $44 million and $109 million, respectively, for the three- and six-month periods ended June 30, 2008.

(b) Represents predominantly transactions written to facilitate regulatory capital relief.

(c) Represents transactions where AIGFP believes the counterparties are no longer using the transactions to obtain regulatory capital relief.

(d) During the second quarter of 2008, a European RMBS regulatory capital relief transaction with a notional amount of $1.6 billion was not

terminated as expected when it no longer provided regulatory capital relief to the counterparty.

(e) Approximately $57.8 billion in net notional amount includes some exposure to U.S. sub-prime mortgages and approximately $9.6 billion in net notional amount includes CDOs of CMBS.

(f) Represents credit default swaps written by AIGFP on tranches below super senior on certain regulatory capital relief trades.

(g) Fair value amounts are shown before the effects of counterparty netting adjustments.

The valuation of the super senior credit derivatives continues to be challenging given the limitation on the availability of market observable information due to the lack of trading and price transparency in the structured finance market, particularly during and since the fourth quarter of 2007. These market conditions have increased the reliance on management estimates and judgments in arriving at an estimate of fair value for financial reporting purposes. Further, disparities in the valuation methodologies employed by market participants and the varying judgments reached by such participants when assessing volatile markets has increased the likelihood that the various parties to these instruments may arrive at significantly different estimates as to their fair values.

AIGFP's valuation methodologies for the super senior credit default swap portfolio have evolved in response to the deteriorating market conditions and the lack of sufficient market observable information. AIG has sought to calibrate the model to market information and to review the assumptions of the model on a regular basis.

During the second quarter of 2008, AIGFP implemented further refinements to the cash flow waterfall used by the BET model and the assumptions used therein. These refinements reflected the ability of a CDO to use principal proceeds to cover interest payment obligations on lower-rated tranches, the ability of a CDO to use principal proceeds to cure a breach of an overcollateralization test, the ability of a CDO to amortize certain senior CDO tranches on a pro-rata or sequential basis and the preferential payment of management fees. To the extent there is a lag in the prices provided by the collateral managers, AIG refines those prices by rolling them forward to the end of the quarter using prices provided by a third-party pricing service. The net effect of these refinements was an increase in the unrealized market valuation loss of $342 million. Refinements made during the first quarter of 2008 had only a de minimus effect on the unrealized market valuation loss.

AIGFP employs a modified version of the BET model to value its credit default swap portfolio written on the super senior securities issued by CDOs, including the embedded 2a-7 Puts. The BET model uses default probabilities derived from credit spreads implied from market prices for the individual securities included in the underlying collateral pools securing the CDOs. AIGFP obtained prices on these securities primarily from the CDO collateral managers.

The BET model also uses diversity scores, weighted average lives, recovery rates and discount rates. The determination of some of these inputs requires the use of judgment and estimates, particularly in the absence of market observable data. AIGFP also employs a Monte Carlo simulation to assist in quantifying the effect on valuation of the CDO of the unique features of the CDOs' structure such as triggers that divert cash flows to the most senior level of the capital structure.

AIG selected the BET model for the following reasons:

- it is known and utilized by other institutions;
- it has been studied extensively, documented and enhanced over many years;
- it is transparent and relatively simple to apply;
- the parameters required to run the BET model are generally observable; and
- it can easily be modified to use probabilities of default and expected losses derived from the underlying collateral securities market prices instead of using rating-based historical probabilities of default.

AIG's implementation of the BET model uses a Monte Carlo simulation of the cash flows of each underlying CDO for various scenarios of defaults by the underlying collateral securities. The Monte Carlo simulation allows the model to take into account the cash flow waterfall and to capture the benefits due to cash flow diversion within each CDO.

The BET model has certain limitations. A well known limitation of the BET model is that it can understate the expected losses for super senior tranches when default correlations are high. The model uses correlations implied from diversity scores which do not capture the tendency for correlations to increase as defaults increase. Recognizing this concern, AIG tested the sensitivity of the valuations to the diversity scores. The results of the testing demonstrated that the valuations are not very sensitive to the diversity scores because the expected losses generated from the prices of the collateral pool securities are currently high, breaching the attachment point in most transactions. Once the attachment point is breached by a sufficient amount, the diversity scores, and their implied correlations, are no longer a significant driver of the valuation of a super senior tranche.

The credit default swaps written by AIGFP generally cover the failure of payment on the super senior CDO security, which in certain cases may also cover the acceleration of the super senior CDO security upon an event of default of the CDO. AIGFP does not own the securities in the CDO collateral pool. The credit spreads implied from the market prices of the securities in the CDO collateral pool incorporate the risk of default (credit risk), the market's price for liquidity risk and in distressed markets, the risk aversion

costs. Spreads on credit derivatives tend to be narrower than the credit spreads implied from the market prices of the securities in the CDO collateral pool because, unlike investing in a bond, there is no need to fund the position (except when an actual credit event occurs). In times of illiquidity, the difference between spreads on cash securities and derivative instruments (the negative basis) may be even wider for high quality assets. AIGFP was unable to reliably verify this negative basis with market observable inputs due to the accelerating severe dislocation, illiquidity and lack of trading in the ABS market during the fourth quarter of 2007 and the first six months of 2008. The valuations produced by the BET model therefore represent the valuations of the underlying super senior CDO cash securities based on AIG's assumptions about those securities, albeit with no recognition of any potential effect of the basis differential on that valuation. AIGFP also considered the valuation of the super senior CDO securities provided by third parties, including counterparties to these transactions, and made adjustments as necessary.

Valuation Sensitivity

Set forth in the paragraphs below are sensitivity analyses that estimate the effects of using alternative pricing and other key inputs on AIG's calculation of the unrealized market valuation loss related to the AIGFP super senior credit default swap portfolio. While AIG believes that the ranges used in these analyses are reasonable, given the current difficult market conditions, AIG is unable to predict which of the scenarios is most likely to occur. AIG is also unable to assess the effect, if any, that recent transactions involving sales of large portfolios of CDOs will have on the pricing of the AIGFP super senior credit default swap portfolio. Actual results in any period are likely to vary, perhaps materially, from the modeled scenarios, and there can be no assurance that the unrealized market valuation loss related to the AIGFP super senior credit default swap portfolio will be consistent with any of the sensitivity analyses.

The most significant assumption used in developing the estimate is the pricing of the securities within the CDO collateral pools. These prices are used to derive default probabilities and expected losses that are used in the BET model. If the actual pricing of the securities within the collateral pools differs from the pricing used in estimating the fair value of the super senior credit default swap portfolio, there is potential for material variation in the fair value estimate. A decrease by five points (for example, from 87 cents per dollar to 82 cents per dollar) in the aggregate price of the underlying collateral securities would cause an additional unrealized market valuation loss of approximately $4.0 billion, while an increase in the aggregate price of the underlying collateral securities by five points (for example, from 90 cents per dollar to 95 cents per dollar) would reduce the unrealized market valuation loss by approximately $3.9 billion. Any further declines in the value of the underlying collateral securities held by a CDO will similarly affect the value of the super senior CDO securities given their significantly depressed valuations. Given the current difficult market conditions, AIG cannot predict reasonably likely changes in the prices of the underlying collateral securities held within a CDO at this time.

The following table presents other key inputs used in the valuation of the credit default swap portfolio written on the super senior securities issued by multi-sector CDOs, and the potential increase (decrease) to the unrealized market valuation loss at June 30, 2008 calculated using the BET model for changes in these key inputs:

(in millions)	Increase (Decrease) To Unrealized Market Valuation Loss
Weighted average lives	
Effect of an increase of 1 year	$ 519
Effect of a decrease of 1 year	(905)
Recovery rates	
Effect of an increase of 10%	(18)
Effect of a decrease of 10%	254
Diversity scores	
Effect of an increase of 5	(84)
Effect of a decrease of 5	261
Discount curve	
Effect of an increase of 100 basis points	181

These results are calculated by stressing a particular assumption independently of changes in any other assumption. No assurance can be given that the actual levels of the key inputs will not exceed, perhaps significantly, the ranges assumed by AIG for purposes of the above analysis. No assumption should be made that results calculated from the use of other changes in these key inputs can be interpolated or extrapolated from the results set forth above.

In the case of credit default swaps written on investment grade corporate debt and CLOs, AIGFP estimates the value of its obligations by reference to the relevant market indices or third-party quotes on the underlying super senior tranches where available.

The following table represents the relevant market credit indices and index CDS maturity used in the valuation of the credit default swap portfolio written on investment-grade corporate debt and the increase (decrease) to the unrealized market valuation loss at June 30, 2008 corresponding to changes in these market credit indices and maturity:

(in millions)			Increase (Decrease) To Unrealized Market Valuation Loss
CDS maturity (in years)	5	7	10
CDX Index			
Effect of an increase of 10 basis points	$(23)	$ (48)	$(10)
Effect of a decrease of 10 basis points	23	49	10
iTraxx Index			
Effect of an increase of 10 basis points	(11)	(37)	(8)
Effect of a decrease of 10 basis points	11	37	8

These results are calculated by stressing a particular assumption independently of changes in any other assumption. No assurance can be given that the actual levels of the indices and maturity will not exceed, perhaps significantly, the ranges assumed by AIG for purposes of the above analysis. No assumption should be made that results calculated from the use of other changes in these indices and maturity can be interpolated or extrapolated from the results set forth above.

For additional information about AIGFP's super senior credit default swap portfolio, see Risk Management — Credit Derivatives.

Other derivatives. Valuation models that incorporate unobservable inputs initially are calibrated to the transaction price. Subsequent valuations are based on observable inputs to the valuation model (e.g., interest rates, credit spreads, volatilities, etc.). Model inputs are changed only when corroborated by market data.

Transfers into Level 3

During the three-months ended June 30, 2008, AIG transferred from Level 2 to Level 3 approximately $2.3 billion of assets, primarily representing fixed maturity securities for which the significant inputs used to measure the fair value of the securities became unobservable primarily as a result of the significant disruption in the credit markets. See Note 3 to the Consolidated Financial Statements for additional information about transfers into Level 3.

Valuation Controls

AIG is actively developing and implementing a remediation plan to address the material weakness in internal control relating to the fair value valuation of the AIGFP super senior credit default swap portfolio, and oversight thereof as described in Item 9A. of the 2007 Annual Report on Form 10-K. AIG is developing new systems and processes to reduce reliance on certain manual controls that have been established as compensating controls over valuation of this portfolio and in other areas, and is strengthening the resources required to remediate this weakness. Notwithstanding this need to continue strengthening these controls, AIG has an oversight structure that includes appropriate segregation of duties with respect to the valuation of its financial instruments. Senior management, independent of the trading and investing functions, is responsible for the oversight of control and valuation policies and for reporting the results of these controls and policies to AIG's Audit Committee. AIG employs procedures for the approval of new transaction types and markets, price verification, periodic review of profit and loss, and review of valuation models by personnel with appropriate technical knowledge of relevant products and markets. These procedures are performed by personnel independent of the trading and investing functions. For valuations that require inputs with little or no market observability, AIG compares the results of its valuation models to actual subsequent transactions.

Operating Review

General Insurance Operations

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

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

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

Transatlantic Holdings, Inc. (Transatlantic) subsidiaries offer reinsurance capacity on both a treaty and facultative basis both in the U.S. and abroad. Transatlantic structures programs for a full range of property and casualty products with an emphasis on specialty risk.

AIG's Personal Lines operations provide automobile insurance through aigdirect.com, its direct marketing distribution channel, and the Agency Auto Division, its independent agent/broker distribution channel. It also

provides a broad range of coverages for high net worth individuals through the AIG Private Client Group (Private Client Group). Coverages for the Personal Lines operations are written predominantly in the United States.

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

AIG's Foreign General Insurance Group writes both commercial and consumer lines of insurance which is primarily underwritten through American International Underwriters (AIU), a marketing unit consisting of wholly owned agencies and insurance companies. The Foreign General Insurance Group also includes business written by AIG's foreign-based insurance subsidiaries.

General Insurance Results

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

(in millions, except ratios)	Three Months Ended June 30, 2008	Three Months Ended June 30, 2007	Percentage Increase/ (Decrease)	Six Months Ended June 30, 2008	Six Months Ended June 30, 2007	Percentage Increase/ (Decrease)
Net premiums written:						
AIG Property Casualty Group						
Commercial Insurance	**$ 5,988**	$ 6,439	(7)%	**$11,101**	$12,448	(11)%
Transatlantic	**988**	983	1	**2,024**	1,967	3
Personal Lines	**1,230**	1,203	2	**2,518**	2,432	4
Mortgage Guaranty	**288**	272	6	**592**	538	10
Foreign General Insurance	**3,726**	3,242	15	**8,065**	6,860	18
Total	**$12,220**	$12,139	1%	**$24,300**	$24,245	—%
Net premiums earned:						
AIG Property Casualty Group						
Commercial Insurance	**$ 5,912**	$ 5,996	(1)%	**$11,329**	$11,977	(5)%
Transatlantic	**1,023**	948	8	**2,040**	1,913	7
Personal Lines	**1,209**	1,168	4	**2,408**	2,323	4
Mortgage Guaranty	**269**	221	22	**525**	431	22
Foreign General Insurance	**3,740**	3,030	23	**7,208**	5,938	21
Total	**$12,153**	$11,363	7%	**$23,510**	$22,582	4%
Net investment income:						
AIG Property Casualty Group						
Commercial Insurance	**$ 587**	$ 984	(40)%	**$ 1,330**	$ 2,017	(34)%
Transatlantic	**120**	119	1	**237**	235	1
Personal Lines	**56**	57	(2)	**113**	114	(1)
Mortgage Guaranty	**44**	39	13	**88**	76	16
Foreign General Insurance	**357**	427	(16)	**599**	746	(20)
Reclassifications and eliminations	**3**	2	50	**5**	3	67
Total	**$ 1,167**	$ 1,628	(28)%	**$ 2,372**	$ 3,191	(26)%
Net realized capital gains (losses)	**$ (563)**	$ (63)	—%	**$ (836)**	$ 58	—%
Operating income (loss):						
AIG Property Casualty Group						
Commercial Insurance	**$ 381**	$ 1,904	(80)%	**$ 1,166**	$ 3,833	(70)%
Transatlantic	**141**	168	(16)	**303**	319	(5)
Personal Lines	**21**	118	(82)	**24**	224	(89)
Mortgage Guaranty	**(518)**	(81)	—	**(872)**	(73)	—
Foreign General Insurance	**796**	867	(8)	**1,532**	1,776	(14)
Reclassifications and eliminations	**6**	—	—	**11**	(7)	—
Total	**$ 827**	$ 2,976	(72)%	**$ 2,164**	$ 6,072	(64)%
Statutory underwriting profit (loss)[(b)]:						
AIG Property Casualty Group						
Commercial Insurance	**$ 357**	$ 946	(62)%	**$ 575**	$ 1,730	(67)%
Transatlantic	**66**	37	78	**120**	53	126
Personal Lines	**(42)**	56	—	**(105)**	89	—
Mortgage Guaranty	**(564)**	(126)	—	**(971)**	(168)	—
Foreign General Insurance	**443**	371	19	**807**	773	4
Total	**$ 260**	$ 1,284	(80)%	**$ 426**	$ 2,477	(83)%
AIG Property Casualty Group:						
Loss Ratio	**80.6**	68.2		**79.6**	68.5	
Expense Ratio	**21.4**	19.6		**22.8**	20.3	
Combined Ratio	**102.0**	87.8		**102.4**	88.8	
Foreign General Insurance:						
Loss Ratio	**53.7**	52.1		**52.8**	51.4	
Expense Ratio[(a)]	**34.6**	33.3		**32.2**	30.8	
Combined ratio	**88.3**	85.4		**85.0**	82.2	
Consolidated:						
Loss Ratio	**72.3**	63.9		**71.4**	64.0	
Expense Ratio	**25.4**	23.2		**25.9**	23.3	
Combined Ratio	**97.7**	87.1		**97.3**	87.3	

(a) Includes amortization of advertising costs.

(b) Statutory underwriting profit (loss) is a measure that U.S. domiciled insurance companies are required to report to their regulatory authorities. The following table reconciles statutory underwriting profit (loss) to operating income for General Insurance:

(in millions)	Commercial Insurance	Transatlantic	Personal Lines	Mortgage Guaranty	Foreign General Insurance	Reclassifications and Eliminations	Total
Three Months Ended June 30, 2008:							
Statutory underwriting profit (loss)	**$ 357**	**$ 66**	**$ (42)**	**$ (564)**	**$ 443**	**$ –**	**$ 260**
Increase (decrease) in DAC	**(1)**	**(5)**	**13**	**2**	**(46)**	**–**	**(37)**
Net investment income	**587**	**120**	**56**	**44**	**357**	**3**	**1,167**
Net realized capital gains (losses)	**(562)**	**(40)**	**(6)**	**–**	**42**	**3**	**(563)**
Operating income (loss)	**$ 381**	**$ 141**	**$ 21**	**$ (518)**	**$ 796**	**$ 6**	**$ 827**
Three Months Ended June 30, 2007:							
Statutory underwriting profit (loss)	$ 946	$ 37	$ 56	$ (126)	$ 371	$ –	$1,284
Increase (decrease) in DAC	50	10	7	9	51	–	127
Net investment income	984	119	57	39	427	2	1,628
Net realized capital gains (losses)	(76)	2	(2)	(3)	18	(2)	(63)
Operating income (loss)	$1,904	$ 168	$ 118	$ (81)	$ 867	$ –	$2,976
Six Months Ended June 30, 2008:							
Statutory underwriting profit (loss)	**$ 575**	**$ 120**	**$ (105)**	**$ (971)**	**$ 807**	**$ –**	**$ 426**
Increase (decrease) in DAC	**(4)**	**1**	**26**	**13**	**166**	**–**	**202**
Net investment income	**1,330**	**237**	**113**	**88**	**599**	**5**	**2,372**
Net realized capital gains (losses)	**(735)**	**(55)**	**(10)**	**(2)**	**(40)**	**6**	**(836)**
Operating income (loss)	**$1,166**	**$ 303**	**$ 24**	**$ (872)**	**$1,532**	**$ 11**	**$2,164**
Six Months Ended June 30, 2007:							
Statutory underwriting profit (loss)	$1,730	$ 53	$ 89	$ (168)	$ 773	$ –	$2,477
Increase (decrease) in DAC	85	14	22	21	204	–	346
Net investment income	2,017	235	114	76	746	3	3,191
Net realized capital gains (losses)	1	17	(1)	(2)	53	(10)	58
Operating income (loss)	$3,833	$ 319	$ 224	$ (73)	$1,776	$ (7)	$6,072

AIG transacts business in most major foreign currencies. The effects of changes in foreign currency exchange rates on the growth of General Insurance net premiums written were as follows:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2008	2007	**2008**	2007
Growth in original currency*	**(2.2)%**	3.3%	**(2.8)%**	4.7%
Foreign exchange effect	**2.9**	1.0	**3.0**	1.2
Growth as reported in U.S. dollars	**0.7%**	4.3%	**0.2%**	5.9%

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

Quarterly General Insurance Results

General Insurance operating income decreased in the three-month period ended June 30, 2008 compared to the same period in 2007 due to declines in both underwriting profit and net investment income as well as increased net realized capital losses in the three month-period ended June 30, 2008. The combined ratio for the three-month period ended June 30, 2008 increased to 97.7, an increase of 10.6 points compared to the same period in 2007, primarily due to an increase in the loss ratio of 8.4 points. The loss ratio for accident year 2008 recorded in the three-month period ended June 30, 2008 was 6.2 points higher than the loss ratio recorded in the three-month period ended June 30, 2007 for accident year 2007. Increases in Mortgage Guaranty losses accounted for 3.6 points of the increase in the 2008 accident year loss ratio. The downward cycle in the U.S. housing market is not expected to improve until residential inventories return to a more normal level, and AIG expects that this downward cycle will continue to adversely affect Mortgage Guaranty's loss ratios for the foreseeable future. The loss ratio also increased for other property and casualty lines due to premium rate decreases and changes in loss trends. Unfavorable prior year development increased incurred losses by $93 million in the three-month period ended June 30, 2008 while favorable prior year development decreased incurred losses by $87 million in the three-month period ended June 30, 2007, accounting for 1.5 points of the increase in the loss ratio.

General Insurance net premiums written increased in the three-month period ended June 30, 2008 compared to the same period in 2007, as a decline in Commercial Insurance resulting from declining rates was offset by growth in Foreign General Insurance from both established and new distribution channels, and the positive effect of changes in foreign currency exchange rates.

General Insurance net investment income declined in the three-month period ended June 30, 2008 by $461 million compared to the same period in 2007. Interest and dividend income increased $60 million in the three-month period ended June 30, 2008 compared to the same period in 2007 as investments in fixed maturities and equity securities increased by $9.0 billion and the average yield was substantially unchanged for both periods. Income from partnership and mutual fund investments declined $413 million in the three-month period ended June 30, 2008 compared to the same period in 2007, primarily due to weaker equity market performance in 2008.

Net realized capital losses in the three-month period ended June 30, 2008 include other-than-temporary

impairment charges of $685 million principally on fixed maturity securities, compared to $84 million in the same period of 2007. See also Capital Resources and Liquidity and Invested Assets herein.

Year-to-Date General Insurance Results

General Insurance operating income decreased in the six-month period ended June 30, 2008 compared to the same period in 2007 due to declines in both underwriting profit and net investment income as well as net realized capital losses in the six month-period ended June 30, 2008 compared to net realized capital gains in the same period in 2007. The combined ratio for the six-month period ended June 30, 2008 increased to 97.3, an increase of 10.0 points compared to the same period in 2007, primarily due to an increase in the loss ratio of 7.4 points. The loss ratio for accident year 2008 recorded in the six-month period ended June 30, 2008 was 5.2 points higher than the loss ratio recorded in the six-month period ended June 30, 2007 for accident year 2007. Increases in Mortgage Guaranty losses accounted for 3.3 points of the increase in the 2008 accident year loss ratio. The loss ratio also increased for other property and casualty lines due to premium rate decreases and changes in loss trends. Favorable development from prior years and increases in the loss reserve discount reduced incurred losses by $84 million and $342 million in the six-month periods ended June 30, 2008 and 2007, respectively. The favorable development in the six-month period ended June 30, 2008 includes $339 million of favorable development recognized in the first three months of 2008, related to policies whose premiums vary with the level of losses incurred (loss sensitive policies). Loss sensitive policies did not have a significant effect in 2007. The favorable development on loss sensitive policies had no effect on underwriting profit as it was entirely offset by a reduction in earned premiums. The reduction in incurred losses and earned premiums resulting from loss sensitive policies reduced the loss ratio by 0.4 points compared to the same period in 2007. Other unfavorable loss development, partially offset by increases in the loss reserve discount for the six-month period ended June 30, 2008, increased incurred losses by $255 million, accounting for 2.6 points of the increase in the loss ratio compared to the same period of 2007. Favorable loss development in the six-month periods ended June 30, 2008 and 2007, of $37 million and $50 million, respectively (recognized in consolidation and related to certain asbestos settlements), reduced overall incurred losses.

General Insurance net premiums written were essentially unchanged in the six-month period ended June 30, 2008 compared to the same period in 2007, as a decline in Commercial Insurance rates was offset by growth in Foreign General Insurance from both established and new distribution channels; the positive effect of changes in foreign currency exchange rates; and, to a lesser extent, growth in the Private Client Group of Personal Lines and in Mortgage Guaranty.

General Insurance net investment income declined in the six-month period ended June 30, 2008 by $819 million compared to the same period in 2007. Interest and dividend income increased $169 million in the six-month period ended June 30, 2008 compared to the same period in 2007 as investment in fixed maturities and equity securities increased by $9.0 billion and the average yield was substantially unchanged for both periods. Income from partnership and mutual fund investments declined $937 million in the six-month period ended June 30, 2008 compared to the same period in 2007, primarily due to poor performance in the equity markets in 2008. Investment expenses declined $55 million the six-month period ended June 30, 2008 compared to the same period in 2007, primarily due to decreased interest expense on deposit liabilities.

Net realized capital losses in the six-month period ended June 30, 2008 include other-than-temporary impairment charges of $840 million compared to $130 million in the same period of 2007. See also Capital Resources and Liquidity and Invested Assets herein.

Quarterly Commercial Insurance Results

Commercial Insurance's operating income decreased in the three-month period ended June 30, 2008 compared to the same period in 2007 primarily due to declines in both underwriting profit and net investment income as well as increased net realized capital losses in the three-month period ended June 30, 2008. The decline is also reflected in the combined ratio, which increased 10.8 points in the three-month period ended June 30, 2008 compared to the same period in 2007. The loss ratio for accident year 2008, recorded in the three-month period ended June 30, 2008 was 5.1 points higher than the loss ratio recorded in the three-month period ended June 30, 2007 for accident year 2007. The increase in the 2008 accident year loss ratio includes 1.4 points for losses related to the Midwest floods with the remaining increase due to higher casualty losses and the effect of premium rate declines and several large fire losses. Unfavorable prior year development increased incurred losses by $75 million in the three-month period ended June 30, 2008 while favorable prior year development decreased incurred losses by $65 million in the three-month period ended June 30, 2007, accounting for 2.3 points of the increase in the loss ratio. Increases in the loss reserve discount reduced incurred losses by $50 million and $125 million in the three-month periods ended June 30, 2008 and 2007, respectively, accounting for 1.2 points of the increase in the loss ratio. Commercial Insurance's net premiums written declined in the three-month period ended June 30, 2008 compared to the same period in 2007 primarily due to declines in workers' compensation premiums and other casualty lines of business.

Commercial Insurance's expense ratio increased to 19.6 in the three-month period ended June 30, 2008 compared to 17.5 in the same period of 2007. The increase in the expense ratio was due to changes in property reinsurance programs, increases in the provision for uncollectible premiums and changes in the mix of business. The 2008 property reinsurance programs include more excess of loss treaties, which have little or no ceding commissions, and less pro rata treaties, which have ceding commissions, compared to the 2007 property reinsurance programs. Provision for uncollectible premiums increased by $39 million in the three-month period ended June 30, 2008 compared to the same period in 2007, primarily due to increased provisions for uncollectible workers' compensation premium receivables. In general, net premiums written increased in lines of business with higher expense ratios and lower loss ratios compared to other Commercial Insurance lines of business, contributing to the increase in the expense ratio for the three-month period ended June 30, 2008 compared to the same period in 2007. In addition, Commercial Insurance continued to invest in systems and process improvements to enhance operating efficiency and controls over the long term.

Commercial Insurance's net investment income declined in the three-month period ended June 30, 2008 compared to the same period in 2007, primarily due to a decline in income from partnership and mutual fund investments which decreased $290 million in the three-month period ended June 30, 2008 compared to the same period in 2007.

Commercial Insurance recorded net realized capital losses in the three-month period ended June 30, 2008 compared to net realized capital gains in the same period of 2007, primarily due to other-than-temporary impairment charges of $632 million in the three-month period ended June 30, 2008, principally related to fixed maturity securities, compared to $77 million in the same period in 2007.

Year-to-Date Commercial Insurance Results

Commercial Insurance's operating income decreased in the six-month period ended June 30, 2008 compared to the same period in 2007, primarily due to declines in both underwriting profit and net investment income, as well as net realized capital losses in the six-month period ended June 30, 2008. The decline is also reflected in the combined ratio, which increased 10.6 points in the six-month period ended June 30, 2008 compared to the same period in 2007. The loss ratio for accident year 2008 recorded in the six-month period ended June 30, 2008 included a 1.4 point effect related to the Atlanta tornado and Midwest flood catastrophe losses, and was 4.4 points higher than the loss ratio recorded in the six-month period ended June 30, 2007 for accident year 2007. Prior year development and increases in the loss reserve discount reduced incurred losses by $192 million and $276 million in the six-month periods ended June 30, 2008 and 2007, respectively. The favorable development for 2008 includes $339 million of favorable development related to loss sensitive polices. The favorable development on loss sensitive policies had no effect on underwriting profit as the reduction in incurred losses was entirely offset by a reduction in earned premiums. However, the reductions in both earned premiums and incurred losses accounted for a reduction in the loss ratio of 0.8 points compared to the same period of 2007 related to loss sensitive policies. Other unfavorable loss development less the increase in the loss reserve discount resulted in a net increase in incurred losses of $147 million, accounting for 3.6 points of the increase in the loss ratio compared to the same period in 2007.

Commercial Insurance's net premiums written declined in the six-month period ended June 30, 2008 compared to the same period in 2007 primarily due to declines in workers' compensation premiums and the effect of the loss sensitive policies described above and other casualty lines of business.

Commercial Insurance's expense ratio increased to 21.6 in the six-month period ended June 30, 2008 compared to 18.3 in the same period of 2007. Return premiums on loss sensitive policies reduced net premiums written, without a corresponding reduction in expenses, increasing the expense ratio by 0.6 points for the six-month period ended June 30, 2008 compared to the same period in 2007. The remaining increase in the expense ratio primarily resulted from changes in property reinsurance programs, increases in the provision for uncollectible premiums and changes in the mix of business as discussed above.

Commercial Insurance's net investment income declined in the six-month period ended June 30, 2008 compared to the same period in 2007, primarily due to a decline in income from partnership and mutual fund investments which decreased $699 million in the six-month period ended June 30, 2008 compared to the same period in 2007.

Commercial Insurance recorded net realized capital losses in the six-month period ended June 30, 2008 compared to net realized capital gains in the same period in 2007, primarily due to other-than-temporary impairment charges of $776 million in the six-month period ended June 30, 2008, related to both fixed maturity and equity securities, compared to $113 million in the same period in 2007.

Quarterly Transatlantic Results

Transatlantic's operating income decreased in the three-month period ended June 30, 2008 compared to the same period in 2007, primarily due to an increase in net realized capital losses, partially offset by an increase in statutory underwriting profit. The increase in net realized capital losses is due principally to other-than-temporary impairment charges primarily related to domestic residential asset-backed fixed maturity securities and, to a much lesser extent, equity securities. The increase in statutory underwriting profit in the three-month period ended June 30, 2008 compared to the

same period in 2007 reflects improved underwriting results in domestic operations.

Year-to-Date Transatlantic Results

Transatlantic's operating income decreased in the six-month period ended June 30, 2008 compared to the same period in 2007 primarily due to an increase in net realized capital losses, partially offset by an increase in statutory underwriting profit. The increase in net realized capital losses is due principally to other-than-temporary impairment charges primarily related to domestic residential asset-backed fixed maturity securities and, to a much lesser extent, equity securities. The increase in statutory underwriting profit in the six-month period ended June 30, 2008 compared to the same period in 2007 reflects improved underwriting results in domestic and international operations. The 2007 international underwriting results were adversely affected by European windstorm related losses.

Quarterly Personal Lines Results

Personal Lines operating income decreased in the three-month period ended June 30, 2008 compared to the same period in 2007 due to a deterioration in underwriting performance as reflected by the combined ratio, which increased to 103.0 in the three-month period ended June 30, 2008 compared to 94.5 in the same period in 2007. The loss ratio increased 6.5 points, including an increase in the 2008 accident year loss ratio of 1.4 points, due primarily to an increase in the accident year loss ratio for automobile policies, partially offset by a decline in the accident year loss ratio for the Private Client Group. The 2008 accident year loss ratio for automobile polices increased 3.6 points compared to the loss ratio recorded in the three-month period ended June 30, 2007 for the 2007 accident year, due to declining premium rates and increased frequency and severity of losses. Prior year loss development increased incurred losses by $29 million in the three-month period ended June 30, 2008 compared to a reduction of $32 million in the same period in 2007, accounting for 5.1 points of the increase in the loss ratio. The current period adverse loss development on prior years is primarily related to greater than expected bodily injury severity and property damage frequency.

The expense ratio increased 2.0 points in the three-month period ended June 30, 2008 compared to the same period in 2007, primarily due to a change in business mix as the Private Client Group, which carries a higher expense ratio, represented an increased percentage of the Personal Lines division's net premiums written. Additionally, a decrease to ceding commissions as a result of a restructured reinsurance program, integration costs relating to 21st Century Insurance Group (21st Century) and a litigation charge contributed to the overall increase in the expense ratio.

Net premiums written increased in the three-month period ended June 30, 2008 compared to the same period in 2007, primarily due to continued growth in the Private Client Group, partially offset by reductions in both the aigdirect.com and Agency Auto businesses. The growth in the Private Client Group reflects the execution of a plan to expand its distribution network. Since June 2007, the Private Client Group has expanded its agency network by 23 percent. Additionally, the Private Client Group's net premiums written increased as a result of a restructured reinsurance program which decreased premiums ceded to reinsurers. The decrease in the aigdirect.com and Agency Auto business reflects the effects of planned reductions in these lines as the underlying loss experience has deteriorated.

Year-to-Date Personal Lines Results

Personal Lines operating income decreased in the six-month period ended June 30, 2008 compared to the same period in 2007 due to a deterioration in underwriting performance as reflected by the combined ratio, which increased to 103.2 in the six-month period ended June 30, 2008 compared to 95.0 in the same period in 2007. The loss ratio increased 7.5 points, including an increase in the 2008 accident year loss ratio of 2.2 points due to an increase in the accident year loss ratio for automobile policies. The 2008 accident year loss ratio for automobile polices increased 3.7 points compared to the loss ratio recorded in the six-month period ended June 30, 2007 for the 2007 accident year, due to declining premium rates and increased frequency and severity of losses. Prior year development increased incurred losses by $65 million in the six-month period ended June 30, 2008 compared to a reduction of $61 million in the same period in 2007, accounting for 5.3 points of the increase in the loss ratio. The current period adverse loss development on prior years is primarily related to greater than expected bodily injury severity and property damage frequency.

The expense ratio increased 0.7 points in the six-month period ended June 30, 2008 compared to the same period in 2007, primarily due to a change in business mix as the Private Client Group, which carries a higher expense ratio, represented an increased percentage of the Personal Lines division's net premiums written. Also, a decrease to ceding commissions as a result of a restructured reinsurance program, integration costs relating to 21st Century and a litigation charge contributed to the increase in the expense ratio.

Net premiums written increased in the six-month period ended June 30, 2008 compared to the same period in 2007, primarily due to continued growth in the Private Client Group, partially offset by reductions in both the aigdirect.com and Agency Auto businesses. The growth in the Private Client Group reflects the execution of a plan to expand the distribution network. Additionally, the Private Client Group's net premiums written increased as a result of a

restructured reinsurance program which decreased premiums ceded to reinsurers. The decrease in the aigdirect.com and Agency Auto business reflect the effects of planned reductions in these lines as the underlying loss experience has deteriorated.

Quarterly Mortgage Guaranty Results

Mortgage Guaranty's operating loss in the three-month period ended June 30, 2008 increased compared to the same period in 2007 as the deteriorating U.S. residential housing market adversely affected losses incurred for both the domestic first- and second-lien businesses. Historically, a large percentage of reported defaults were "cured" resulting in no loss to UGC. A cure can occur when a borrower brings the mortgage current, refinances the existing mortgage, sells the home and pays off the current balance or enters into a payment plan with the lender to bring the mortgage current. In the current market, loans are less likely to cure, increasing the probability that a defaulted loan will result in a claim payment. UGC has reflected that lower cure probability in its current estimate of unpaid losses resulting in higher loss reserves and an increase in incurred losses. Domestic first- and second-lien losses incurred increased 264 percent and 107 percent respectively, compared to the same period in 2007, resulting in loss ratios of 253.9 and 556.0, respectively, in the three-month period ended June 30, 2008. Increases in domestic losses incurred resulted in an overall loss ratio of 292.0 in the three-month period ended June 30, 2008 compared to 129.9 in the same period in 2007.

Net premiums written increased in the three-month period ended June 30, 2008 compared to the same period in 2007, primarily due to growth in domestic first-lien premiums as a result of the increased use of mortgage insurance for credit enhancement as well as a higher persistency rate. UGC has taken steps to strengthen its underwriting guidelines and increase rates. It also discontinued new production for certain programs in the second-lien business beginning in the fourth quarter of 2006. However, UGC will continue to receive renewal premiums on that portfolio for the life of the loans, estimated to be three to five years, and will continue to be exposed to losses from future defaults.

The expense ratio in the three-month period ended June 30, 2008 was 16.5, down from 22.4 in the same period of 2007 as expenses declined 22 percent. UGC has tightened its monitoring and control over expenses in response to the adverse conditions in the U.S. residential housing market, resulting in the decline in operating expenses and the related expense ratio.

UGC domestic mortgage risk in force totaled $31.8 billion as of June 30, 2008 and the 60-day delinquency ratio was 4.9 percent (based on number of policies, consistent with mortgage industry practice) compared to domestic mortgage risk in force of $26.5 billion and a delinquency ratio of 2.5 percent at June 30, 2007. Approximately 83 percent of the domestic mortgage risk is secured by first-lien, owner-occupied properties.

Year-to-Date Mortgage Guaranty Results

Mortgage Guaranty's operating loss in the six-month period ended June 30, 2008 increased compared to the same period in 2007 as the deteriorating U.S. residential housing market adversely affected losses incurred for both the domestic first- and second-lien businesses. Domestic first- and second-lien losses incurred increased 302 percent and 113 percent respectively, compared to the six-month period ended June 30, 2007, resulting in loss ratios of 229.0 and 500.7, respectively, in the six-month period ended June 30, 2008. Increases in domestic losses incurred resulted in an overall loss ratio of 264.5 in the six-month period ended June 30, 2008 compared to 111.5 in the six-month period ended June 30, 2007.

Net premiums written increased in the six-month period ended June 30, 2008 compared to the same period in 2007, primarily due to growth in domestic first-lien premiums due to the increased use of mortgage insurance for credit enhancement as well as a higher persistency rate.

The expense ratio in the six-month period ended June 30, 2008 was 18.2 percent, down from 22.1 percent in the same period in 2007 as premium growth combined with a 9 percent reduction in expenses resulted in the decline in the expense ratio.

Quarterly Foreign General Insurance Results

Foreign General Insurance operating income decreased in the three-month period ended June 30, 2008 compared to the same period in 2007, primarily due to a decrease in both underwriting profit and net investment income.

Net premiums written increased 15 percent (5 percent in original currency) in the three-month period ended June 30, 2008 compared to the same period in 2007, reflecting growth in commercial and consumer lines driven by new business from both established and new distribution channels, including the late 2007 acquisition of Württembergische und Badische Versicherungs — AG (WüBa) in Germany. Net premiums written for commercial lines increased due to new business, mainly in European markets, and decreases in the use of reinsurance, partially offset by declines in premium rates. Aviation production increased due to improved account retention and increased production in the space aviation business. Net premiums written for the Lloyd's syndicate continued to decline due to rate decreases and increased market competition.

The loss ratio in the three-month period ended June 30, 2008 increased 1.5 points compared to the same period in

2007, primarily due to an increase in severe but non-catastrophe losses and higher loss frequency in the current accident year. Partially offsetting these increases was a 2.1 point loss ratio improvement due to $67 million of catastrophe losses in the prior year period with no significant catastrophe losses in the current period.

The expense ratio in the three-month period ended June 30, 2008 increased 1.3 points compared to the same period in 2007. This increase reflects the cost of realigning certain legal entities through which Foreign General Insurance operates, and the increased significance of consumer lines of business, which have higher acquisition costs. AIG expects the expense ratio to continue to increase in 2008 due to the cost of realigning certain legal entities through which Foreign General Insurance operates.

Net investment income decreased in the three-month period ended June 30, 2008 compared to the same period in 2007. Mutual fund income was $67 million lower than the three-month period ended June 30, 2007 reflecting weaker performance in the equity markets in 2008, partially offset by higher interest and dividend income of $41 million.

Year-to-Date Foreign General Insurance Results

Foreign General Insurance operating income decreased in the six-month period ended June 30, 2008 compared to the same period in 2007, primarily due to decreases in net investment income and net realized capital losses.

Net premiums written increased 18 percent (8 percent in original currency) in the six-month period ended June 30, 2008 compared to the same period in 2007, reflecting strong growth in commercial and consumer lines driven by new business from both established and new distribution channels, including the WüBa acquisition. Net premiums written for commercial lines increased due to new business in the U.K. and Europe and decreases in the use of reinsurance, partially offset by declines in premium rates. Growth in personal accident business in Latin America, Asia and Europe also contributed to the increase. Net premiums written for the Lloyd's syndicate Ascot continued to decline due to rate decreases and increased market competition.

The loss ratio in the six-month period ended June 30, 2008 increased 1.4 points compared to the same period in 2007. Prior accident year development reduced incurred losses by $16 million and $68 million in the first six months of 2008 and 2007, respectively, accounting for 0.9 points of the increase. The current accident year loss ratio excluding catastrophe losses increased by 1.6 points primarily due to higher severe but non-catastrophe losses and higher loss frequency. Partially offsetting this increase in loss ratio is $67 million of catastrophe losses in the prior year period with no significant catastrophe losses in the current period, resulting in a loss ratio decrease of 1.1 points.

The expense ratio in the six-month period ended June 30, 2008 increased 1.4 points compared to the same period in 2007 reflecting the continued cost of realigning certain legal entities through which Foreign General Insurance operates, and the increased significance of consumer lines of business, which have higher acquisition costs.

Net investment income decreased in the six-month period ended June 30, 2008 compared to the same period in 2007. Mutual fund income was $172 million lower than the six-month period ended June 30, 2007, reflecting weaker performance in the equity markets in 2008, partially offset by higher interest and dividend income of $70 million.

Reserve for Losses and Loss Expenses

The following table presents the components of the General Insurance gross reserve for losses and loss expenses (loss reserves) by major lines of business on a statutory Annual Statement basis*:

(in millions)	**June 30, 2008**	December 31, 2007
Other liability occurrence	**$ 21,233**	$ 20,580
Workers compensation	**15,234**	15,568
Other liability claims made	**13,896**	13,878
International	**8,372**	7,036
Auto liability	**6,240**	6,068
Property	**4,554**	4,274
Reinsurance	**3,395**	3,127
Products liability	**2,430**	2,416
Medical malpractice	**2,307**	2,361
Mortgage guaranty/credit	**2,291**	1,426
Accident and health	**1,831**	1,818
Commercial multiple peril	**1,796**	1,900
Aircraft	**1,725**	1,623
Fidelity/surety	**1,221**	1,222
Other	**2,222**	2,203
Total	**$ 88,747**	$ 85,500

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

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

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

At June 30, 2008, General Insurance net loss reserves increased $3.04 billion from the prior year-end to $72.33 billion. The net loss reserves represent loss reserves reduced by reinsurance recoverable, net of an allowance for unrecoverable reinsurance and applicable discount for future investment income.

The following table classifies the components of the General Insurance net loss reserve by business unit:

(in millions)	**June 30, 2008**	December 31, 2007
Commercial Insurance[(a)]	**$48,443**	$47,392
Transatlantic	**7,317**	6,900
Personal Lines[(b)]	**2,448**	2,417
Mortgage Guaranty	**2,057**	1,339
Foreign General Insurance[(c)]	**12,066**	11,240
Total Net Loss Reserve	**$72,331**	$69,288

(a) At June 30, 2008 and December 31, 2007, Commercial Insurance loss reserves include approximately $2.89 billion and $3.13 billion, respectively, ($3.08 billion and $3.34 billion, respectively, before discount), related to business written by Commercial Insurance but ceded to American International Reinsurance Company Limited (AIRCO) and reported in AIRCO's statutory filings. Commercial Insurance loss reserves also include approximately $648 million and $590 million related to business included in AIUO's statutory filings at June 30, 2008 and December 31, 2007, respectively.

(b) At June 30, 2008 and December 31, 2007, Personal Lines loss reserves include $1.03 billion and $894 million, respectively, related to business ceded to Commercial Insurance and reported in Commercial Insurance's statutory filings.

(c) At June 30, 2008 and December 31, 2007, Foreign General Insurance loss reserves include approximately $2.04 billion and $3.02 billion, respectively, related to business reported in Commercial Insurance's statutory filings.

The Commercial Insurance net loss reserve is comprised principally of the business of AIG subsidiaries participating in the American Home Assurance Company (American Home)/ National Union Fire Insurance Company of Pittsburgh, Pa. (National Union) pool (10 companies) and the surplus lines pool (Lexington Insurance Company, AIG Excess Liability Insurance Company and Landmark Insurance Company).

Commercial Insurance cedes a quota share percentage of its other liability occurrence and products liability occurrence business to AIRCO. The quota share percentage ceded was 10 percent in the six-month period ended 2008 and 15 percent in 2007 and covered all business written in these years for these lines by participants in the American Home/ National Union pool. AIRCO's loss reserves relating to these quota share cessions from Commercial Insurance are recorded on a discounted basis. As of June 30, 2008, AIRCO carried a discount of approximately $190 million applicable to the $3.08 billion in undiscounted reserves it assumed from the American Home/National Union pool via this quota share cession. AIRCO also carries approximately $532 million in net loss reserves relating to Foreign General Insurance business. These reserves are carried on an undiscounted basis.

The companies participating in the American Home/ National Union pool have maintained a participation in the business written by AIU for decades. As of June 30, 2008, these AIU reserves carried by participants in the American Home/National Union pool totaled approximately $2.04 billion. The remaining Foreign General Insurance reserves are carried by American International Underwriter Overseas, Ltd. (AIUO), AIRCO, AIG U.K., and other smaller AIG subsidiaries domiciled outside the United States. Statutory filings in the United States by AIG companies reflect all the business written by U.S. domiciled entities only, and therefore exclude business written by AIUO, AIRCO, and all other internationally domiciled subsidiaries. The total reserves carried at June 30, 2008 by AIUO and AIRCO were approximately $3.63 billion and $3.42 billion, respectively. AIRCO's $3.42 billion in total general insurance reserves consist of approximately $2.89 billion from business assumed from the American Home/National Union pool and an additional $532 million relating to Foreign General Insurance business.

Discounting of Reserves

At June 30, 2008, AIG's overall General Insurance net loss reserves reflect a loss reserve discount of $2.48 billion, including tabular and non-tabular calculations. The tabular workers compensation discount is calculated using a 3.5 percent interest rate and the 1979-81 Decennial Mortality Table. The non-tabular workers compensation discount is calculated separately for companies domiciled in New York and Pennsylvania, and follows the statutory regulations for each state. For New York companies, the discount is based on a five percent interest rate and the companies' own payout patterns. For Pennsylvania companies, the statute has specified discount factors for accident years 2001 and prior, which are based on a six percent interest rate and an industry payout pattern. For accident years 2002 and subsequent, the

discount is based on the yield of U.S. Treasury securities ranging from one to twenty years and the companies' own payout patterns, with the future expected payment for each year using the interest rate associated with the corresponding Treasury security yield for that time period. The discount is comprised of the following: $794 million — tabular discount for workers' compensation in Commercial Insurance; $1.49 billion — non-tabular discount for workers' compensation in Commercial Insurance; and $190 million — non-tabular discount for other liability occurrence and products liability occurrence in AIRCO. The total undiscounted workers' compensation loss reserve carried by Commercial Insurance is approximately $13.5 billion as of June 30, 2008. The other liability occurrence and products liability occurrence business in AIRCO that is assumed from Commercial Insurance is discounted based on the yield of U.S. Treasury securities ranging from one to twenty years and the Commercial Insurance payout pattern for this business. The undiscounted reserves assumed by AIRCO from Commercial Insurance totaled approximately $3.08 billion at June 30, 2008.

Quarterly Reserving Process

AIG believes that the General Insurance net loss reserves are adequate to cover General Insurance net losses and loss expenses as of June 30, 2008. While AIG regularly reviews the adequacy of established loss reserves, there can be no assurance that AIG's ultimate loss reserves will not develop adversely and materially exceed AIG's loss reserves as of June 30, 2008. In the opinion of management, such adverse development and resulting increase in reserves is not likely to have a material adverse effect on AIG's consolidated financial condition, although it could have a material adverse effect on AIG's consolidated results of operations for an individual reporting period.

The reconciliation of net loss reserves was as follows:

	Three Months Ended June 30,		Six Months Ended June 30,	
(in millions)	**2008**	2007	**2008**	2007
Net reserve for losses and loss expenses at beginning of period	**$70,507**	$64,034	**$69,288**	$62,630
Foreign exchange effect	**193**	252	**263**	214
Losses and loss expenses incurred:				
Current year	**8,620**	7,334	**16,641**	14,549
Prior years, other than accretion of discount	**93**	(120)	**(71)**	(268)
Prior years, accretion of discount	**72**	12	**176**	128
Losses and loss expenses incurred	**8,785**	7,226	**16,746**	14,409
Losses and loss expenses paid	**7,154**	6,315	**13,966**	12,056
Net reserve for losses and loss expenses at end of period	**$72,331**	$65,197	**$72,331**	$65,197

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

	Three Months Ended June 30,		Six Months Ended June 30,	
(in millions)	**2008**	2007	**2008**	2007
Prior Accident Year Development by Reporting Unit:				
Commercial Insurance	**$ 75**	$ (65)	**$ (142)**	$ (152)
Personal Lines	**29**	(32)	**65**	(61)
Mortgage Guaranty	**(10)**	(4)	**58**	27
Foreign General Insurance	**1**	(4)	**(16)**	(68)
Subtotal	**95**	(105)	**(35)**	(254)
Transatlantic	**(2)**	18	**1**	36
Asbestos settlements	**—**	(33)	**(37)**	(50)
Prior years, other than accretion of discount	**$ 93**	$ (120)	**$ (71)**	$ (268)

	Calendar Year	
(in millions)	**2008**	2007
Prior Accident Year Development by Accident Year:		
2007	**$ (135)**	
2006	**(256)**	$ (454)
2005	**(260)**	(165)
2004	**(190)**	(136)
2003	**16**	15
2002	**18**	112
2001 and prior	**736**	360
Prior years, other than accretion of discount	**$ (71)**	$ (268)

In determining the quarterly loss development from prior accident years, AIG conducts analyses to determine the change in estimated ultimate loss for each accident year for each profit center. For example, if loss emergence for a profit center is different than expected for certain accident years, the actuaries examine the indicated effect such emergence would have on the reserves of that profit center. In some cases, the higher or lower than expected emergence may result in no clear change in the ultimate loss estimate for the accident years in question, and no adjustment would be made to the profit center's reserves for prior accident years. In other cases, the higher or lower than expected emergence may result in a larger change, either favorable or unfavorable, than the difference between the actual and expected loss emergence. Such additional analyses were conducted for each profit center, as appropriate, in the three-month period ended June 30, 2008 to determine the loss development from prior accident years for the three-month period ended June 30, 2008. As part of its quarterly reserving process, AIG also considers notices of claims received with respect to emerging issues, such as those related to the U.S. mortgage and housing market.

2008 Net Loss Development

In the three-month period ended June 30, 2008, net loss development from prior accident years was adverse by approximately $93 million, excluding approximately $72 million from accretion of loss reserve discount. The overall adverse development of $93 million consisted of approximately $292 million of favorable development from accident years 2004 through 2007 offset by approximately $385 million of adverse loss development from accident years 2003 and prior. The adverse development from accident years 2003 and prior was primarily related to excess casualty business within Commercial Insurance. The favorable development from accident years 2004 through 2007 included approximately $80 million of favorable development from business written by Lexington Insurance Company, including Healthcare and Casualty and Program businesses. AIG Executive Liability business contributed approximately $65 million to the favorable development from accident years 2004 and 2005, relating primarily to D&O. Within Commercial Insurance, the overall adverse development of $75 million consisted of approximately $160 million of adverse development relating to excess casualty business and $50 million of adverse development relating to property business, partially offset by favorable development from D&O, healthcare and other classes. A significant portion of the adverse development relating to excess casualty was related to a variety of latent exposures, including construction defect exposures, product aggregate exposure and pharmaceutical related exposures, as well as a significant number of other large losses primarily from accident years 1998 through 2002. In addition, the loss development assumptions applicable to excess casualty reserves were modified in the second quarter of 2008 to reflect the adverse experience being observed, and this caused approximately $90 million of the overall adverse development from accident years 2003 and prior. Excess casualty results for the more recent accident years, i.e. 2004 and subsequent years, has continued to be favorable. AIG's exposure to these latent exposures was reduced after 2002 due to significant changes in policy terms and conditions as well as underwriting guidelines.

In the six-month period ended June 30, 2008, net loss development from prior accident years was favorable by approximately $71 million, including approximately $339 million of favorable development relating to loss sensitive business in the first three months of 2008 (which was offset by an equal amount of negative earned premium development), and excluding approximately $176 million from accretion of loss reserve discount. Excluding both the favorable development relating to loss sensitive business and accretion of loss reserve discount, net loss development from prior accident years in the six-month period ended June 30, 2008, was adverse by approximately $268 million. The overall favorable development of $71 million consisted of approximately $841 million of favorable development from accident years 2004 through 2007 partially offset by approximately $770 million of adverse loss development from accident years 2003 and prior. Excluding the favorable development from loss sensitive business, the overall adverse development of $268 million consisted of approximately $561 million of favorable development from accident years 2004 through 2007 offset by approximately $829 million of adverse development from accident years 2003 and prior. The adverse development from accident years 2003 and prior was primarily related to excess casualty business within Commercial Insurance. The favorable development from accident years 2004 through 2007 included approximately $280 million in favorable development from loss sensitive business written by AIG Risk Management, and approximately $220 million in favorable development from business written by Lexington Insurance Company, including Healthcare, AIG CAT Excess, Casualty and Program businesses. AIG Executive Liability business contributed approximately $110 million to the favorable development from accident years 2004 and 2005, relating primarily to D&O. The adverse development from accident years 2003 and prior included approximately $200 million related to claims involving MTBE, a gasoline additive, primarily on excess casualty business within Commercial Insurance from accident years 2000 and prior. In addition, as described above for the three months ended June 30, 2008, the excess casualty adverse developments reflect a variety of other latent claims and large losses, as well as a $90 million increase resulting from the modification of loss development factors to reflect adverse experience in excess casualty.

2007 Net Loss Development

In the three-month period ended June 30, 2007, net loss development from prior accident years was favorable by approximately $120 million, including approximately $18 million of adverse development from the general reinsurance operations of Transatlantic; and excluding approximately $12 million from accretion of loss reserve discount. Excluding Transatlantic, as well as accretion of discount, net loss development in the three-month period ended June 30, 2007 from prior accident years was favorable by approximately $138 million. The overall favorable development of $120 million consisted of approximately $475 million of favorable development from accident years 2003 through 2006, partially offset by approximately $355 million of adverse development from accident years 2002 and prior. For the three-month period ended June 30, 2007, most classes of AIG's business continued to experience favorable development for accident years 2003 through 2006. The majority of the adverse development from accident years 2002 and prior was related to developments from excess casualty business within Commercial Insurance and from Transatlantic.

In the six-month period ended June 30, 2007, net loss development from prior accident years was favorable by approximately $268 million, including approximately $36 million of adverse development from the general reinsurance operations of Transatlantic; and excluding approximately $128 million from accretion of loss reserve discount. Excluding Transatlantic, as well as accretion of discount, net loss development in the six-month period ended June 30, 2007 from prior accident years was favorable by approximately $304 million. The overall favorable development of $268 million consisted of approximately $740 million of favorable development from accident years 2003 through 2006, partially offset by approximately $472 million of adverse development from accident years 2002 and prior. For the six-month period ended June 30, 2007, most classes of AIG's business continued to experience favorable development for accident years 2003 through 2006. The majority of the adverse development from accident years 2002 and prior was related to development from excess casualty business within Commercial Insurance and from Transatlantic.

Asbestos and Environmental Reserves

The estimation of loss reserves relating to asbestos and environmental claims on insurance policies written many years ago is subject to greater uncertainty than other types of claims due to inconsistent court decisions as well as judicial interpretations and legislative actions that in some cases have tended to broaden coverage beyond the original intent of such policies and in others have expanded theories of liability.

As described more fully in the 2007 Annual Report on Form 10-K, AIG's reserves relating to asbestos and environmental claims reflect a comprehensive ground-up analysis. In the six-month period ended June 30, 2008, AIG maintained the ultimate loss estimates for asbestos and environmental claims resulting from the recently completed reserve analyses. A minor amount of adverse incurred loss development pertaining to asbestos was reflected in the six-month period ended June 30, 2008, as presented in the table that follows. This development was primarily attributable to several large defendants, the effect of which was largely offset by one large favorable settlement. A moderate amount of favorable gross incurred loss development pertaining to environmental was reflected in the six-month period ended June 30, 2008, as presented in the table that follows. This development was primarily attributable to recent favorable experience which was fully reinsured, resulting in no favorable net development on environmental net reserves.

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

	Six Months Ended June 30,			
	2008		2007	
(in millions)	Gross	Net	Gross[a]	Net
Asbestos:				
Reserve for losses and loss expenses at beginning of year	**$3,864**	**$1,454**	$4,523	$1,889
Losses and loss expenses incurred[b]	**60**	**4**	10	(25)
Losses and loss expenses paid[b]	**(383)**	**(170)**	(454)	(268)
Reserve for losses and loss expenses at end of period	**$3,541**	**$1,288**	$4,079	$1,596
Environmental:				
Reserve for losses and loss expenses at beginning of year	**$ 515**	**$ 237**	$ 629	$ 290
Losses and loss expenses incurred[b]	**(40)**	**1**	—	(1)
Losses and loss expenses paid[b]	**(25)**	**(17)**	(54)	(31)
Reserve for losses and loss expenses at end of period	**$ 450**	**$ 221**	$ 575	$ 258
Combined:				
Reserve for losses and loss expenses at beginning of year	**$4,379**	**$1,691**	$5,152	$2,179
Losses and loss expenses incurred[b]	**20**	**5**	10	(26)
Losses and loss expenses paid[b]	**(408)**	**(187)**	(508)	(299)
Reserve for losses and loss expenses at end of period	**$3,991**	**$1,509**	$4,654	$1,854

(a) Gross amounts were revised from the presentation in prior periods to reflect the inclusion of certain reserves not previously identified as asbestos and environmental related. This revision had no effect on net reserves.

(b) All amounts pertain to policies underwritten in prior years, primarily to policies issued in 1984 and prior.

The gross and net IBNR included in the reserve for losses and loss expenses, relating to asbestos and environmental claims separately and combined, were estimated as follows:

	Six Months Ended June 30,			
	2008		2007	
(in millions)	Gross	Net	Gross*	Net
Asbestos	**$2,256**	**$ 997**	$3,068	$1,279
Environmental	**264**	**117**	355	148
Combined	**$2,520**	**$1,114**	$3,423	$1,427

* *Gross amounts were revised from the presentation in prior periods to reflect the inclusion of certain reserves not previously identified as asbestos and environmental related. This revision had no effect on net reserves.*

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

	Six Months Ended June 30,					
	2008			2007		
	Asbestos	Environmental	Combined	Asbestos	Environmental	Combined
Claims at beginning of year	**6,563**	**7,652**	**14,215**	6,878	9,442	16,320
Claims during year:						
Opened	**392**	**674**	**1,066**	300	695	995
Settled	**(97)**	**(65)**	**(162)**	(66)	(59)	(125)
Dismissed or otherwise resolved	**(551)**	**(1,172)**	**(1,723)**	(544)	(899)	(1,443)
Claims at end of period	**6,307**	**7,089**	**13,396**	6,568	9,179	15,747

Survival Ratios — Asbestos and Environmental

The following table presents AIG's survival ratios for asbestos and environmental claims at June 30, 2008 and 2007. The survival ratio is derived by dividing the current carried loss reserve by the average payments for the three most recent calendar years for these claims. Therefore, the survival ratio is a simplistic measure estimating the number of years it would be before the current ending loss reserves for these claims would be paid off using recent year average payments. The June 30, 2008 survival ratio is lower than the ratio at June 30, 2007 because the more recent periods included in the rolling average reflect higher claims payments. In addition, AIG's survival ratio for asbestos claims was negatively affected by the favorable settlement described above, as well as several similar settlements during 2007. These settlements reduced gross and net asbestos survival ratios at June 30, 2008 by approximately 1.4 years and 3.0 years, respectively, and reduced gross and net asbestos survival ratios at June 30, 2007 by approximately 1.7 years and 4.1 years, respectively. Many factors, such as aggressive settlement procedures, mix of business and level of coverage

provided, have a significant effect on the amount of asbestos and environmental reserves and payments and the resultant survival ratio. Moreover, as discussed above, the primary basis for AIG's determination of its reserves is not survival ratios, but instead the ground-up and top-down analysis. Thus, caution should be exercised in attempting to determine reserve adequacy for these claims based simply on this survival ratio.

AIG's survival ratios for asbestos and environmental claims, separately and combined were based upon a three-year average payment. These ratios at June 30, 2008 and 2007 were as follows:

	Gross*	Net
2008		
Survival ratios:		
Asbestos	5.7	4.3
Environmental	4.5	3.7
Combined	5.5	4.2
2007		
Survival ratios:		
Asbestos	8.6	7.4
Environmental	5.2	4.0
Combined	8.0	6.6

** Gross amounts for 2007 were revised from the presentation in prior periods to reflect the inclusion of certain reserves not previously identified as asbestos and environmental related. This revision had no effect on net reserves.*

Operating Review

Life Insurance & Retirement Services Operations

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

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

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

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

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

Foreign Life Insurance & Retirement Services

Japan and Other

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

Asia

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

Domestic Life Insurance

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

Domestic Retirement Services

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

Life Insurance & Retirement Services Results

Life Insurance & Retirement Services results were as follows:

(in millions)	Premiums and Other Considerations	Net Investment Income	Net Realized Capital Gains (Losses)	Total Revenues	Operating Income (Loss)
Three Months Ended June 30, 2008					
Foreign Life Insurance & Retirement Services	**$ 7,691**	**$ 3,162**	**$ (909)**	**$ 9,944**	**$ 773**
Domestic Life Insurance	**1,604**	**1,006**	**(1,376)**	**1,234**	**(1,005)**
Domestic Retirement Services	**290**	**1,418**	**(2,725)**	**(1,017)**	**(2,169)**
Total	**$ 9,585**	**$ 5,586**	**$(5,010)**	**$10,161**	**$(2,401)**
Three months ended June 30, 2007					
Foreign Life Insurance & Retirement Services	$ 6,503	$ 3,361	$ 18	$ 9,882	$ 1,654
Domestic Life Insurance	1,369	1,006	(16)	2,359	368
Domestic Retirement Services	298	1,765	(281)	1,782	598
Total	$ 8,170	$ 6,132	$ (279)	$14,023	$ 2,620
Percentage Increase/(Decrease) from Prior Year:					
Foreign Life Insurance & Retirement Services	18%	(6)%	—%	1%	(53)%
Domestic Life Insurance	17	—	—	(48)	—
Domestic Retirement Services	(3)	(20)	—	—	—
Total	17%	(9)%	—%	(28)%	—%
Six Months Ended June 30, 2008					
Foreign Life Insurance & Retirement Services	**$15,138**	**$ 4,610**	**$(1,631)**	**$18,117**	**$ 1,508**
Domestic Life Insurance	**3,191**	**1,990**	**(2,664)**	**2,517**	**(1,875)**
Domestic Retirement Services	**574**	**2,789**	**(5,084)**	**(1,721)**	**(3,865)**
Total	**$18,903**	**$ 9,389**	**$(9,379)**	**$18,913**	**$(4,232)**
Six months ended June 30, 2007					
Foreign Life Insurance & Retirement Services	$13,116	$ 6,244	$ (217)	$19,143	$ 2,938
Domestic Life Insurance	2,897	2,011	(28)	4,880	713
Domestic Retirement Services	582	3,390	(290)	3,682	1,250
Total	$16,595	$11,645	$ (535)	$27,705	$ 4,901
Percentage Increase/(Decrease) from Prior Year:					
Foreign Life Insurance & Retirement Services	15%	(26)%	—%	(5)%	(49)%
Domestic Life Insurance	10	(1)	—	(48)	—
Domestic Retirement Services	(1)	(18)	—	—	—
Total	14%	(19)%	—%	(32)%	—%

The gross insurance in force for Life Insurance & Retirement Services was as follows:

(in millions)	**June 30, 2008**	December 31, 2007
Foreign*	**$1,438,309**	$ 1,327,251
Domestic	**1,014,785**	984,794
Total	**$2,453,094**	$ 2,312,045

** Includes an increase of $45.2 billion related to changes in foreign exchange rates at June 30, 2008.*

Disruption in the U.S. residential mortgage and credit markets was the key driver of operating results in the three- and six-month periods ended June 30, 2008 primarily due to significant net realized capital losses resulting from other-than-temporary impairment charges of $5.2 billion and $9.6 billion in the three- and six-month periods ended June 30, 2008, respectively, compared to $324 million and $716 million in the same periods of 2007. In addition, net investment income and certain products continued to be affected by the volatile markets.

Life Insurance & Retirement Services total revenues in the three- and six-month periods ended June 30, 2008 reflect growth in premiums and other considerations compared to the same periods in 2007, primarily due to strong production in the Foreign Life Insurance & Retirement Services operations and sales of payout annuities in Domestic Life Insurance. Overall growth in premiums and other considerations was dampened by a continuing shift to investment-oriented products and the suspension in the second quarter of 2007 of new sales on certain products in Japan pending completion of an industry wide review by the tax authorities. This review was finalized in March 2008 and resulted in lower tax deductibility of these products for the policyholder. Although sales of these products have restarted in Japan, it is expected that sales will be at lower than historical levels.

Net investment income decreased in the three- and six-month periods ended June 30, 2008 compared to the same period in 2007 due to significantly lower partnership, yield enhancement and mutual fund income, trading account losses of $133 million and $221 million, respectively, in the U.K. associated with certain investment-linked products and increased levels of short-term investments. Policyholder investment income and trading gains and losses (together, policyholder trading gains (losses)) were $617 million and $(168) million in the three- and six-month periods ended June 30, 2008, respectively, compared to gains of $1.1 billion and $1.9 billion in the same periods in 2007, reflecting equity

market declines. Policyholder trading gains (losses) are offset by a charge to incurred policy losses and benefits expense. Policyholder trading gains (losses) generally reflect the trends in equity markets, principally in Japan and Asia.

The higher net realized capital losses in the three- and six-month periods ended June 30, 2008 compared to the same periods in 2007 were primarily related to severity impairments due to the credit market disruption and foreign exchange losses as a result of the weakening of the dollar against foreign currencies.

In addition to the higher net realized capital losses and lower net investment income noted above, the operating loss for the three- and six-month periods ended June 30, 2008 was unfavorably affected by an increased negative investment spread in Taiwan and changes in actuarial estimates totaling $31 million in connection with Domestic Retirement Services' variable annuity products. These decreases were partially offset by the favorable effect of foreign exchange rates. Operating loss in the three-month period ended June 30, 2008 included a DAC and SIA benefit of $212 million related to net realized capital losses compared to a benefit of $103 million in the same period in 2007. Operating loss in the six-month period ended June 30, 2008 included a DAC and SIA benefit of $479 million related to net realized capital losses compared to $114 million in the same period in 2007.

In 2007, operating income included charges of $25 million and $62 million for the three- and six–month periods ended June 30, 2007, respectively, related to a regulatory claims review in Japan.

AIG adopted FAS 157 on January 1, 2008 and the most significant effect on the Life Insurance & Retirement Services results was the change in measurement of fair value for embedded policy derivatives. The pre – tax effect of adoption related to embedded policy derivatives was an increase in net realized capital losses of $155 million as of January 1, 2008, partially offset by a $47 million DAC benefit related to these losses. The effect of initial adoption was primarily due to an increase in the embedded policy derivative liability valuations resulting from the inclusion of explicit risk margins.

AIG adopted FAS 159 on January 1, 2008 and elected to apply the fair value option to a closed block of single premium variable life business in Japan and for an investment – linked product sold principally in Asia. The adoption of FAS 159 with respect to these fair value elections resulted in a decrease to 2008 opening retained earnings of $559 million, net of tax. The fair value of the liabilities for these policies totaled $3.6 billion at June 30, 2008 and is reported in policyholders' contract deposits.

Foreign Life Insurance & Retirement Services Results

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

(in millions)	Premiums and Other Considerations	Net Investment Income	Net Realized Capital Gains (Losses)	Total Revenues	Operating Income (Loss)
Three Months Ended June 30, 2008					
Life insurance	**$ 4,634**	**$1,813**	**$ (750)**	**$ 5,697**	**$ 252**
Personal accident	**1,855**	**109**	**(26)**	**1,938**	**386**
Group products	**1,002**	**244**	**(11)**	**1,235**	**116**
Individual fixed annuities	**79**	**660**	**(115)**	**624**	**44**
Individual variable annuities	**121**	**336**	**(7)**	**450**	**(25)**
Total	**$ 7,691**	**$3,162**	**$ (909)**	**$ 9,944**	**$ 773**
Three Months Ended June 30, 2007					
Life insurance	$ 4,105	$2,092	$ 141	$ 6,338	$1,155
Personal accident	1,487	87	2	1,576	325
Group products	690	222	(6)	906	89
Individual fixed annuities	118	574	(120)	572	52
Individual variable annuities	103	386	1	490	33
Total	$ 6,503	$3,361	$ 18	$ 9,882	$1,654
Percentage Increase/(Decrease) from Prior Year:					
Life insurance	13%	(13)%	—%	(10)%	(78)%
Personal accident	25	25	—	23	19
Group products	45	10	—	36	30
Individual fixed annuities	(33)	15	—	9	(15)
Individual variable annuities	17	(13)	—	(8)	—
Total	18%	(6)%	—%	1%	(53)%
Six Months Ended June 30, 2008					
Life insurance	**$ 9,146**	**$2,732**	**$(1,317)**	**$10,561**	**$ 483**
Personal accident	**3,546**	**201**	**(66)**	**3,681**	**763**
Group products	**1,998**	**397**	**(41)**	**2,354**	**206**
Individual fixed annuities	**208**	**1,229**	**(228)**	**1,209**	**102**
Individual variable annuities	**240**	**51**	**21**	**312**	**(46)**
Total	**$15,138**	**$4,610**	**$(1,631)**	**$18,117**	**$1,508**
Six Months Ended June 30, 2007					
Life insurance	$ 8,272	$3,649	$ (27)	$11,894	$1,807
Personal accident	2,960	170	(6)	3,124	693
Group products	1,443	396	(27)	1,812	152
Individual fixed annuities	246	1,148	(157)	1,237	201
Individual variable annuities	195	881	—	1,076	85
Total	$13,116	$6,244	$ (217)	$19,143	$2,938
Percentage Increase/(Decrease) from Prior Year:					
Life insurance	11%	(25)%	—%	(11)%	(73)%
Personal accident	20	18	—	18	10
Group products	38	—	—	30	36
Individual fixed annuities	(15)	7	—	(2)	(49)
Individual variable annuities	23	(94)	—	(71)	—
Total	15%	(26)%	—%	(5)%	(49)%

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

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

	Three Months Ended June 30,		Six Months Ended June 30,	
	2008	2007	**2008**	2007
Growth in original currency*	**7.5%**	7.8%	**7.1%**	6.5%
Foreign exchange effect	**10.8**	0.9	**8.3**	1.9
Growth as reported in U.S. dollars	**18.3%**	8.7%	**15.4%**	8.4%

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

Quarterly Japan and Other Results

First year premium, single premium and annuity deposits for Japan and Other were as follows:

(in millions)	Three Months Ended June 30, 2008	Three Months Ended June 30, 2007	Percentage Increase/(Decrease) U.S.$	Percentage Increase/(Decrease) Original Currency
First year premium	**$ 734**	$ 673	9%	(4)%
Single premium	**2,178**	2,121	3%	(1)%
Annuity deposits	**6,018**	4,141	45%	43%

First year premium sales in the three-month period ended June 30, 2008 grew moderately in U.S. dollar terms, but declined on an original currency basis compared to the same period in 2007. First year premium life insurance sales in Japan declined reflecting the continued effect of the suspension of the increasing term products in April 2007 which more than offset strong growth of the more profitable U.S. dollar products in Japan. Personal accident first year premium sales were flat compared to the same period in 2007. Group products sales increased primarily due to pension sales in Brazil and credit life business in the Middle East.

Single premium interest sensitive life insurance sales remained strong in Japan in the three-month period ended June 30, 2008, while guaranteed income bond sales in the U.K. decreased in that period due to sales efforts being focused on the launch of a new variable annuity product. In Japan, a new single premium personal accident and health product was successfully launched during the first quarter of 2008 with the majority of sales coming through banks which were recently deregulated and are now able to sell accident and health products. Group products single premium sales increased substantially with higher production in Brazil, the U.K. and Poland due to the launch of new products and the addition of large group accounts.

Annuity deposits increased in the three-month period ended June 30, 2008 compared to the same period in 2007 as both fixed and variable products performed well. In Japan, fixed annuity deposits increased significantly due to an improved exchange rate environment and volatile equity markets. Net flows for Japan fixed annuities increased from $165 million in the three-month period ended June 30, 2007 to $1.2 billion in the three-month period ended June 30, 2008. In the U.K., variable annuity deposits continued to reflect strong growth due to the launch of a new product.

Japan and Other results on a sub–product basis were as follows:

(in millions)	Premiums and Other Considerations	Net Investment Income	Net Realized Capital Gains (Losses)	Total Revenues	Operating Income (Loss)
Three Months Ended June 30, 2008					
Life insurance	**$ 1,568**	**$ 643**	**$(298)**	**$ 1,913**	**$ 144**
Personal accident	**1,336**	**69**	**(7)**	**1,398**	**338**
Group products	**802**	**229**	**(10)**	**1,021**	**84**
Individual fixed annuities	**70**	**626**	**(107)**	**589**	**43**
Individual variable annuities	**120**	**335**	**(7)**	**448**	**(32)**
Total	**$ 3,896**	**$1,902**	**$(429)**	**$ 5,369**	**$ 577**
Three Months Ended June 30, 2007					
Life insurance	$ 1,350	$ 641	$ 33	$ 2,024	$ 438
Personal accident	1,041	52	—	1,093	243
Group products	539	201	1	741	63
Individual fixed annuities	101	546	(129)	518	34
Individual variable annuities	102	385	—	487	32
Total	$ 3,133	$1,825	$ (95)	$ 4,863	$ 810
Percentage Increase/(Decrease) from Prior Year:					
Life insurance	16%	—%	—%	(5)%	(67)%
Personal accident	28	33	—	28	39
Group products	49	14	—	38	33
Individual fixed annuities	(31)	15	—	14	26
Individual variable annuities	18	(13)	—	(8)	—
Total	24%	4%	—%	10%	(29)%

Total revenues for Japan and Other in the three-month period ended June 30, 2008 increased compared to the same period in 2007 primarily due to growth in premiums and other considerations, partially offset by higher net realized capital losses. Realized capital losses increased primarily due to higher other-than-temporary impairments of ABS and Japan real estate investment trusts. Net investment income grew modestly in the period as higher interest and dividends more than offset lower partnership and mutual fund income of $13 million and higher mark to market trading losses of $119 million related to certain investment-linked products in the U.K. compared to the same period in 2007.

Operating income declined in the three-month period ended June 30, 2008 compared to the same period in 2007 due to significantly increased realized capital losses and the higher trading losses, partially offset by $25 million of lower benefit costs in Japan related to the regulatory claims review which negatively affected prior year results, lower benefit costs of $37 million, net of hedge gains and losses, resulting from an increase in the Japanese equity market and interest rates which

had the effect of reducing policy liabilities carried at fair value under FAS 159 and the positive effect of foreign exchange. During the latter part of the second quarter of 2008, management implemented a previously announced hedging program that is expected to reduce future volatility of the policy liabilities carried at fair value under FAS 159.

Year-to-Date Japan and Other Results

First year premium, single premium and annuity deposits for Japan and Other were as follows:

(in millions)	Six Months Ended June 30, 2008	Six Months Ended June 30, 2007	Percentage Increase/ (Decrease) U.S.$	Percentage Increase/ (Decrease) Original Currency
First year premium	**$1,376**	$1,293	6%	(4)%
Single premium	**5,134**	4,118	25%	21%
Annuity deposits	**11,525**	8,212	40%	38%

First year premium sales in the six-month period ended June 30, 2008 grew modestly in U.S. dollar terms, but declined on an original currency basis compared to the same period in 2007. The lower first year premium sales primarily reflect the effect of suspending sales of increasing term products in Japan during the second quarter of last year. Due to the large premium size for the increasing term products, the sales suspension masks the positive underlying growth of more profitable U.S. dollar products in Japan and other life insurance products in Europe and the Middle East. Personal accident first year premium sales were flat compared to the same period in 2007.

Single premium interest sensitive life insurance sales remained strong in Japan and guaranteed income bond sales in the U.K. were higher than the same period last year, although sales are shifting to a new variable annuity product and that trend is expected to continue for the remainder of the year. A new single premium personal accident and health product launched in Japan during the first quarter of 2008 continues to perform well and sales which started through banks are being expanded to the agency channels.

Annuity deposits increased in the six-month period ended June 30, 2008 compared to the same period in 2007 as both fixed and variable products performed well. In Japan, fixed annuity products improved due to the launch of new products and a favorable exchange rate environment for non-yen denominated products. Net flows for Japan individual fixed annuities increased from $56 million in the six-month period ended June 30, 2007 to $1.8 billion in the six-month period ended June 30, 2008. Variable annuity deposit growth in the U.K. was favorably affected by the launch of a new product.

Japan and Other results on a sub-product basis were as follows:

(in millions)	Premiums and Other Considerations	Net Investment Income	Net Realized Capital Gains (Losses)	Total Revenues	Operating Income (Loss)
Six Months Ended June 30, 2008					
Life insurance	**$ 2,896**	**$ 980**	**$ (545)**	**$ 3,331**	**$ 201**
Personal accident	**2,513**	**121**	**(35)**	**2,599**	**639**
Group products	**1,552**	**340**	**(17)**	**1,875**	**156**
Individual fixed annuities	**187**	**1,162**	**(196)**	**1,153**	**111**
Individual variable annuities	**237**	**49**	**21**	**307**	**(47)**
Total	**$ 7,385**	**$ 2,652**	**$ (772)**	**$ 9,265**	**$ 1,060**
Six Months Ended June 30, 2007					
Life insurance	$ 2,566	$ 1,191	$ 15	$ 3,772	$ 790
Personal accident	2,069	102	2	2,173	532
Group products	1,114	351	6	1,471	136
Individual fixed annuities	217	1,092	(164)	1,145	181
Individual variable annuities	193	879	—	1,072	84
Total	$ 6,159	$ 3,615	$ (141)	$ 9,633	$ 1,723
Percentage Increase/(Decrease) from Prior Year:					
Life insurance	13%	(18)%	—%	(12)%	(75)%
Personal accident	21	19	—	20	20
Group products	39	(3)	—	27	15
Individual fixed annuities	(14)	6	—	1	(39)
Individual variable annuities	23	(94)%	—	(71)%	—
Total	20%	(27)%	—%	(4)%	(38)%

Total revenues for Japan and Other in the six-month period ended June 30, 2008 decreased compared to the same period in 2007 primarily due to higher net realized capital losses and lower net investment income. Net investment income declined due to lower policyholder trading gains, partnership and mutual fund income as well as mark to market trading losses related to investment-linked products in the U.K. Policyholder trading gains declined to $176 million for the six-month period ended June 30, 2008 from $1.4 billion for the same period in 2007. Policyholder trading gains (losses) are offset by a charge to incurred policy losses and benefits expense. Partnership and mutual fund income for the six-month period ended June 30, 2008 was $59 million lower than the same period in 2007. Trading account losses in the U.K. on certain investment-linked products were $221 million for the six-month period ended June 30, 2008

compared to a loss of $14 million in the same period in 2007. Net realized capital losses grew significantly in the period primarily due to other-than-temporary impairments.

Despite the continued strong growth in the underlying business and the positive effect of foreign exchange, the decline in total revenues resulted in lower operating income for the six-month period ended June 30, 2008 compared to the same period in 2007. Operating income for the six-month period ended June 30, 2008 was favorably affected by lower benefit costs of $62 million related to the regulatory claims review in Japan, which negatively affected last year's results. Operating income was negatively affected by higher benefit costs of $43 million, net of hedge gains and losses, resulting from volatility in the Japanese equity market and interest rates which impact variable life fair value liabilities under FAS 159 and lower DAC benefit related to realized capital losses of $57 million compared to a benefit of $41 million in the same period in 2007.

Quarterly Asia Results

First year premium, single premium and annuity deposits for Asia were as follows:

(in millions)	Three Months Ended June 30, 2008	Three Months Ended June 30, 2007	Percentage Increase/(Decrease) U.S.$	Percentage Increase/(Decrease) Original Currency
First year premium	**$ 762**	$ 740	3%	—%
Single premium	**893**	922	(3)%	(9)%
Annuity deposits	**334**	240	39%	34%

First year premium sales in the three-month period ended June 30, 2008 grew modestly on a U.S. dollar basis but were flat on an original currency basis compared to the same period in 2007 as the sales focus shifted more to single premium products. In Hong Kong and Singapore, life insurance first year premium sales increased due to promotional campaigns and increased bancassurance sales. However, Taiwan first year life insurance sales declined as the focus has shifted to a newly launched variable annuity product. First year personal accident premiums declined due to increased competition in the direct marketing channel in Korea, which offset positive growth in other parts of Asia. The group products business performed well, particularly in Australia.

Single premium sales in the three-month period ended June 30, 2008 decreased as sales in Taiwan shifted to the new variable annuity product. This decrease was partially offset by strong investment-oriented life insurance sales, particularly in Singapore and Korea and single premium credit life sales in Thailand and Taiwan.

Annuity deposits in the three-month period ended June 30, 2008 rose significantly compared to the same period in 2007 due to the launch of the new variable annuity product in Taiwan.

Asia results, presented on a sub-product basis were as follows:

(in millions)	Premiums and Other Considerations	Net Investment Income	Net Realized Capital Gains (Losses)	Total Revenues	Operating Income
Three Months Ended June 30, 2008					
Life insurance	**$3,066**	**$1,170**	**$ (452)**	**$3,784**	**$ 108**
Personal accident	**519**	**40**	**(19)**	**540**	**48**
Group products	**200**	**15**	**(1)**	**214**	**32**
Individual fixed annuities	**9**	**34**	**(8)**	**35**	**1**
Individual variable annuities	**1**	**1**	**—**	**2**	**7**
Total	**$3,795**	**$1,260**	**$ (480)**	**$4,575**	**$ 196**
Three Months Ended June 30, 2007					
Life insurance	$2,755	$1,451	$ 108	$4,314	$ 717
Personal accident	446	35	2	483	82
Group products	151	21	(7)	165	26
Individual fixed annuities	17	28	9	54	18
Individual variable annuities	1	1	1	3	1
Total	$3,370	$1,536	$ 113	$5,019	$ 844
Percentage Increase/(Decrease) from Prior Year:					
Life insurance	11%	(19)%	—%	(12)%	(85)%
Personal accident	16	14	—	12	(41)
Group products	32	(29)	—	30	23
Individual fixed annuities	(47)	21	—	(35)	(94)
Individual variable annuities	—	—	—	(33)	—
Total	13%	(18)%	—%	(9)%	(77)%

Total revenues for Asia in the three-month period ended June 30, 2008 decreased compared to the same period in 2007, primarily due to the negative effect of policyholder trading gains (losses) on net investment income and higher net realized capital losses, which more than offset the growth in premiums and other considerations. Premiums and other considerations increased in the three-month period ended June 30, 2008 compared to the same period in 2007, despite a continued

trend toward investment-oriented products where only a portion of policy charges are reported as premiums. Personal accident premiums grew despite flat first year premium growth due to a successful retention initiative. Group products premiums grew, reflecting increased first year premiums. Net investment income declined due to policyholder trading losses of $7 million in 2008 compared to gains of $415 million in the same period in 2007 and a reduction in partnership and mutual fund income, which was $44 million lower than the same period in 2007. Net realized capital losses in the three-month period ended June 30, 2008 included higher other-than-temporary impairment charges and higher losses on the fair value of derivatives that do not qualify for hedge accounting treatment under FAS 133 compared to the same period in 2007.

Operating income in the three-month period ended June 30, 2008 decreased compared to the same period in 2007 principally due to higher net realized capital losses and lower net investment income relative to growth in the business. Operating income was also affected by the favorable effect of foreign exchange rates and the unfavorable effect of the increased negative investment spread in Taiwan resulting from lower investment returns.

Year-to-Date Asia Results

First year premium, single premium and annuity deposits for Asia were as follows:

	Six Months Ended June 30,		Percentage Increase/ (Decrease)	
(in millions)	**2008**	2007	U.S.$	Original Currency
First year premium	**$1,480**	$1,414	5%	2%
Single premium	**1,850**	1,570	18%	12%
Annuity deposits	**666**	371	80%	76%

First year premium sales in the six-month period ended June 30, 2008 grew moderately compared to the same period in 2007 as the sales focus shifted more to single premium and annuity products. In Taiwan, life insurance first year premium sales declined as sales shifted to a newly launched variable annuity product. The group products business performed well in Australia, Singapore and Hong Kong.

Single premium sales in the six-month period ended June 30, 2008 grew significantly compared to the same period in 2007 primarily due to investment-oriented life insurance sales, particularly in Singapore, Hong Kong, and Korea, as well as strong credit life sales in Thailand.

Annuity deposits in the six-month period ended June 30, 2008 more than doubled the level reported for the same period in 2007 due to the launch of the new variable annuity product in Taiwan. Deposits in Korea were down in the six-month period ended June 30, 2008 compared to the same period last year due to a recent market shift toward variable products.

Asia results, presented on a sub-product basis were as follows:

(in millions)	Premiums and Other Considerations	Net Investment Income	Net Realized Capital Gains (Losses)	Total Revenues	Operating Income (Loss)
Six Months Ended June 30, 2008					
Life insurance	**$6,250**	**$1,752**	**$(772)**	**$7,230**	**$ 282**
Personal accident	**1,033**	**80**	**(31)**	**1,082**	**124**
Group products	**446**	**57**	**(24)**	**479**	**50**
Individual fixed annuities	**21**	**67**	**(32)**	**56**	**(9)**
Individual variable annuities	**3**	**2**	**—**	**5**	**1**
Total	**$7,753**	**$1,958**	**$(859)**	**$8,852**	**$ 448**
Six Months Ended June 30, 2007					
Life insurance	$5,706	$2,458	$ (42)	$8,122	$1,017
Personal accident	891	68	(8)	951	161
Group products	329	45	(33)	341	16
Individual fixed annuities	29	56	7	92	20
Individual variable annuities	2	2	—	4	1
Total	$6,957	$2,629	$ (76)	$9,510	$1,215
Percentage Increase/(Decrease) from Prior Year:					
Life insurance	10%	(29)%	—%	(11)%	(72)%
Personal accident	16	18	—	14	(23)
Group products	36	27	—	40	—
Individual fixed annuities	(28)	20	—	(39)	—
Individual variable annuities	50	—	—	25	—
Total	11%	(26)%	—%	(7)%	(63)%

Total revenues in Asia in the six-month period ended June 30, 2008 decreased compared to the same period in 2007 primarily due to lower net investment income and higher net realized capital losses, which more than offset the growth in premiums and other considerations. Net investment income declined due to policyholder trading losses of $332 million in 2008 compared to gains of $494 million in 2007 and lower partnership and mutual fund income. Partnership and mutual fund income for the six-month period ended June 30, 2008 was $184 million lower than the same period in 2007. The higher realized capital losses were primarily due to other-than-temporary impairment of dollar denominated securities

held in Singapore and Taiwan which declined in value due to a weakening U.S. dollar.

Operating income for the six-month period ended June 30, 2008 declined compared to the same period in 2007 primarily as a result of lower revenues. Results for the year were also affected by lower operating income in Taiwan due to the increased negative investment spread resulting from lower investment returns.

Quarterly Domestic Life Insurance Results

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

(in millions)	Premiums and Other Considerations	Net Investment Income	Net Realized Capital Gains (Losses)	Total Revenues	Operating Income (Loss)
Three Months Ended June 30, 2008					
Life insurance	**$ 621**	**$ 365**	**$(1,110)**	**$ (124)**	**$ (918)**
Home service	**186**	**163**	**(198)**	**151**	**(112)**
Group life/health	**218**	**48**	**(13)**	**253**	**4**
Payout annuities*	**564**	**320**	**(33)**	**851**	**17**
Individual fixed and runoff annuities	**15**	**110**	**(22)**	**103**	**4**
Total	**$1,604**	**$1,006**	**$(1,376)**	**$1,234**	**$(1,005)**
Three Months Ended June 30, 2007					
Life insurance	$ 603	$ 402	$ 43	$1,048	$ 262
Home service	192	158	(11)	339	66
Group life/health	197	51	(4)	244	1
Payout annuities*	364	276	(35)	605	17
Individual fixed and runoff annuities	13	119	(9)	123	22
Total	$1,369	$1,006	$ (16)	$2,359	$ 368
Percentage Increase/(Decrease) from Prior Year:					
Life insurance	3%	(9)%	—%	—%	—%
Home service	(3)	3	—	(55)	—
Group life/health	11	(6)	—	4	—
Payout annuities	55	16	—	41	—
Individual fixed and runoff annuities	15	(8)	—	(16)	(82)
Total	17%	—%	—%	(48)%	—%

* *Includes structured settlements, single premium immediate annuities and terminal funding annuities.*

Total Domestic Life Insurance revenues decreased in the three-month period ended June 30, 2008 compared to the same period in 2007 due to significantly higher net realized capital losses, partially offset by higher premiums and other considerations. The increase in net realized capital losses was primarily driven by other-than-temporary impairments of ABS related to AIG's securities lending program. See Invested Assets – Securities Lending Activities for further information. Domestic Life Insurance premiums and other considerations increased in the three-month period ended June 30, 2008 compared to the same period in 2007 primarily due to strong payout annuity deposits and growth in life insurance business in force. The growth in payout annuity deposits was driven by structured settlements and terminal funding annuities in both the U.S. and Canada. Net investment income for the three-month period ended June 30, 2008 was consistent with the same period in 2007 despite growth in the underlying business. Net investment income for the three-month period ended June 30, 2008 was affected by lower partnership and other yield enhancement income of $66 million and reduced overall investment yield from increased levels of short-term investments. Offsetting these items was higher net investment income due to the phase out of losses related to synthetic fuel production investments (Synfuel) of $38 million.

Operating income for the three-month period ended June 30, 2008 compared to the same period in 2007 decreased due principally to higher net realized capital losses as described above, partially offset by the growth in the in force block of life insurance and payout annuities and favorable mortality experience in the life insurance business during the quarter. Home service operating income decreased due to higher net realized capital losses partially offset by improved margins on the in-force business. Group life/health operating income increased due to favorable development on the financial institutions credit life run-off block, improved underwriting results on certain product lines and lower DAC amortization costs compared to the same period in 2007. In addition, 2007 operating income was positively affected by a $15 million litigation accrual release. Operating income during the three-month period ended June 30, 2008 includes a DAC benefit related to realized capital losses of $17 million compared to a benefit of $4 million in the same period in 2007.

Year-to-Date Domestic Life Insurance Results

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

(in millions)	Premiums and Other Considerations	Net Investment Income	Net Realized Capital Gains (Losses)	Total Revenues	Operating Income (Loss)
Six Months Ended June 30, 2008					
Life insurance	**$1,210**	**$ 738**	**$(2,165)**	**$ (217)**	**$(1,757)**
Home service	**374**	**316**	**(338)**	**352**	**(174)**
Group life/health	**422**	**95**	**(27)**	**490**	**6**
Payout annuities*	**1,158**	**623**	**(55)**	**1,726**	**55**
Individual fixed and runoff annuities	**27**	**218**	**(79)**	**166**	**(5)**
Total	**$3,191**	**$1,990**	**$(2,664)**	**$2,517**	**$(1,875)**
Six Months Ended June 30, 2007					
Life insurance	$1,181	$ 774	$ 40	$1,995	$ 449
Home service	387	319	(13)	693	148
Group life/health	426	104	(5)	525	4
Payout annuities*	876	565	(41)	1,400	68
Individual fixed and runoff annuities	27	249	(9)	267	44
Total	$2,897	$2,011	$ (28)	$4,880	$ 713
Percentage Increase/(Decrease) from Prior Year:					
Life insurance	2%	(5)%	—%	—%	—%
Home service	(3)	(1)	—	(49)	—
Group life/health	(1)	(9)	—	(7)	50
Payout annuities	32	10	—	23	(19)
Individual fixed and runoff annuities	—	(12)	—	(38)	—
Total	10%	(1)%	—%	(48)%	—%

** Includes structured settlements, single premium immediate annuities and terminal funding annuities.*

Total Domestic Life Insurance revenues decreased in the six-month period ended June 30, 2008 compared to the same period in 2007 due to higher net realized capital losses and lower net investment income partially offset by higher premiums and other considerations. The increase in net realized capital losses was primarily driven by other-than-temporary impairments of ABS related to AIG's securities lending program. See Invested Assets – Investments in RMBS, CMBS, CDOs and ABS – Investments in ABS and – Securities Lending Activities for further information. Domestic Life Insurance premiums and other considerations increased in the six-month period ended June 30, 2008 compared to the same period in 2007 primarily due to strong payout annuity deposits and growth in life insurance business in force. The growth in payout annuity deposits was driven by sales of structured settlements and terminal funding annuities in both the U.S. and Canada. Net investment income declined in the six-month period ended June 30, 2008 compared to the same period in 2007 despite growth in the underlying business. Net investment income for the six-month period ended June 30, 2008 was affected by lower partnership and other yield enhancement income of $102 million and reduced overall investment yield from increased levels of short-term investments. Offsetting these items was higher net investment income due to the phase out of losses related to Synfuel investments of $67 million.

Operating income for the six-month period ended June 30, 2008 compared to the same period in 2007 decreased due principally to higher net realized capital losses and the lower net investment income as described above. Partially offsetting these items was the growth in the in force block of life insurance and payout annuities and favorable mortality experience in the life insurance and payout annuities businesses. Home service operating income decreased due to higher net realized capital losses partially offset by improved margins on the in-force business. Group life/health operating income increased due to favorable development on the financial institutions credit life run-off block, improved underwriting results on certain product lines and lower DAC amortization costs compared to the same period in 2007. In addition, 2007 operating income was positively affected by a $16 million litigation accrual release. Operating income during the six-month period ended June 30, 2008 includes a DAC benefit related to realized capital losses of $37 million compared to a benefit of $4 million in the same period in 2007.

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

(in millions)	Three Months Ended June 30, 2008	Three Months Ended June 30, 2007	Percentage Increase/ (Decrease)	Six Months Ended June 30, 2008	Six Months Ended June 30, 2007	Percentage Increase/ (Decrease)
Life insurance						
Periodic premium by product:						
Universal life	$ 46	$ 47	(2)%	$ 93	$ 98	(5)%
Variable universal life	15	12	25	42	25	68
Term life	61	57	7	113	112	1
Whole life/other	3	3	—	6	5	20
Total periodic premiums by product	125	119	5%	254	240	6%
Unscheduled and single deposits	113	115	(2)	173	181	(4)
Total life insurance	238	234	2%	427	421	1%
Home service						
Life insurance and accident and health	24	25	(4)%	44	49	(10)%
Fixed annuities	40	25	60	69	45	53
Unscheduled and single deposits	5	5	—	10	8	25
Total home service	69	55	25%	123	102	21%
Group life/health	31	22	41%	72	60	20%
Payout annuities	751	600	25%	1,550	1,285	21%
Individual fixed and runoff annuities	256	101	—%	340	188	81%
Total sales and deposits	**$1,345**	**$1,012**	**33%**	**$2,512**	**$2,056**	**22%**

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

Domestic Life Insurance periodic premium sales increased 5 percent and 6 percent in the three- and six-month periods ended June 30, 2008, respectively, compared to the same period in 2007 primarily as a result of strong private placement variable universal life sales. The U.S. life insurance market remains highly competitive and Domestic Life's emphasis on maintaining new business margins has negatively affected sales of term and universal life products, although recent enhancements to term products have resulted in an increase in term sales. Group life/health growth was driven by increased sales of supplemental health and voluntary products. Payout annuities have experienced strong growth from terminal funding and structured settlement sales in both the U.S. and Canada. Home service growth was primarily from increased fixed annuity deposits. Individual fixed and runoff annuities sales and deposits have increased as a result of the current interest rate environment as credited rates offered during the quarter were more competitive with the rates offered by banks on certificates of deposit.

Quarterly Domestic Retirement Services Results

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

(in millions)	Premiums and Other Considerations	Net Investment Income	Net Realized Capital Gains (Losses)	Total Revenues	Operating Income (Loss)
Three Months Ended June 30, 2008					
Group retirement products	**$111**	**$ 488**	**$ (940)**	**$ (341)**	**$ (699)**
Individual fixed annuities	**17**	**817**	**(1,591)**	**(757)**	**(1,274)**
Individual variable annuities	**157**	**34**	**(43)**	**148**	**(50)**
Individual annuities — runoff*	**5**	**79**	**(151)**	**(67)**	**(146)**
Total	**$290**	**$1,418**	**$(2,725)**	**$(1,017)**	**$(2,169)**
Three Months Ended June 30, 2007					
Group retirement products	$112	$ 641	$ (103)	$ 650	$ 265
Individual fixed annuities	26	981	(158)	849	261
Individual variable annuities	155	43	(17)	181	53
Individual annuities — runoff*	5	100	(3)	102	19
Total	$298	$1,765	$ (281)	$ 1,782	$ 598
Percentage Increase/(Decrease) from Prior Year:					
Group retirement products	(1)%	(24)%	—%	—%	—%
Individual fixed annuities	(35)	(17)	—	—	—
Individual variable annuities	1	(21)	—	(18)	—
Individual annuities — runoff	—	(21)	—	—	—
Total	(3)%	(20)%	—%	—%	—%

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

Total revenues and operating income for Domestic Retirement Services declined in the three-month period ended June 30, 2008 compared to the same period in 2007, primarily due to significantly increased net realized capital

losses, lower partnership income of $170 million and lower yield enhancement income of $78 million. Net realized capital losses for Domestic Retirement Services increased primarily due to higher other-than-temporary impairment charges of $2.7 billion in the three-month period ended June 30, 2008 compared to $144 million in the same period in 2007, primarily driven by severity losses on ABS related to AIG's securities lending program.

Operating income for group retirement products and individual fixed annuities decreased in the three-month period ended June 30, 2008 compared to the same period in 2007, primarily as a result of increased net realized capital losses due to higher other-than-temporary impairment charges, lower partnership income, lower yield enhancement income and reduced overall investment yield from increased levels of short-term investments. These decreases were partially offset by decreases in DAC amortization and sales inducement costs of $164 million related to the net realized capital losses compared to $58 million in the same period in 2007.

Individual variable annuities operating income decreased in the three-month period ended June 30, 2008 compared to the same period in 2007, primarily due to a $31 million increase in benefit reserves and related DAC amortization adjustment reflecting changes in actuarial estimates and to increased net realized capital losses largely due to higher other-than-temporary impairment charges.

Year-to-Date Domestic Retirement Services Results

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

(in millions)	Premiums and Other Considerations	Net Investment Income	Net Realized Capital Gains (Losses)	Total Revenues	Operating Income (Loss)
Six Months Ended June 30, 2008					
Group retirement products	**$218**	**$ 982**	**$(1,680)**	**$ (480)**	**$(1,192)**
Individual fixed annuities	**40**	**1,576**	**(2,837)**	**(1,221)**	**(2,230)**
Individual variable annuities	**309**	**69**	**(295)**	**83**	**(187)**
Individual annuities – runoff*	**7**	**162**	**(272)**	**(103)**	**(256)**
Total	**$574**	**$2,789**	**$(5,084)**	**$(1,721)**	**$(3,865)**
Six Months Ended June 30, 2007					
Group retirement products	$217	$1,211	$ (113)	$ 1,315	$ 541
Individual fixed annuities	51	1,895	(169)	1,777	564
Individual variable annuities	301	85	(7)	379	105
Individual annuities – runoff*	13	199	(1)	211	40
Total	$582	$3,390	$ (290)	$ 3,682	$ 1,250
Percentage Increase/(Decrease) from Prior Year:					
Group retirement products	—%	(19)%	—%	—%	—%
Individual fixed annuities	(22)	(17)	—	—	—
Individual variable annuities	3	(19)	—	(78)	—
Individual annuities – runoff	(46)	(19)	—	—	—
Total	(1)%	(18)%	—%	—%	—%

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

Total revenues and operating income for Domestic Retirement Services declined significantly in the six-month period ended June 30, 2008 compared to the same period in 2007 primarily due to significantly increased net realized capital losses and lower partnership and yield enhancement income. Net realized capital losses for Domestic Retirement Services increased primarily due to higher other-than-temporary impairment charges of $4.8 billion in the six-month period ended June 30, 2008 compared to $186 million in the same period in 2007.

Both group retirement products and individual fixed annuities operating income in the six-month period ended June 30, 2008 decreased compared to the same period in 2007 primarily as a result of increased net realized capital losses due to higher other-than-temporary impairment charges, lower net investment income due to lower partnership income of $289 million, lower yield enhancement income of $152 million and reduced overall investment yield from increased levels of short term investments. These decreases were partially offset by decreases in DAC amortization and sales inducement costs of $329 million related to the net realized capital losses compared to $55 million in the same period in 2007.

Individual variable annuities operating income decreased in the six-month period ended June 30, 2008 compared to the same period in 2007 primarily as a result of increased net realized capital losses principally due to other-than-temporary impairment charges. In addition, benefit reserves and DAC amortization and sales inducement costs increased by a combined $31 million due to changes in actuarial estimates, offset by decreases in DAC amortization and sales inducement costs of $56 million related to the net realized capital losses compared to $6 million in the same period in 2007.

The account value roll forward for Domestic Retirement Services by product was as follows:

(in millions)	Three Months Ended June 30, 2008	Three Months Ended June 30, 2007	Six Months Ended June 30, 2008	Six Months Ended June 30, 2007
Group retirement products				
Balance at beginning of period	**$ 65,640**	$ 65,216	**$ 68,109**	$ 64,357
Deposits – annuities	**1,472**	1,463	**2,925**	2,881
Deposits – mutual funds	**371**	330	**795**	795
Total deposits	**1,843**	1,793	**3,720**	3,676
Surrenders and other withdrawals	**(1,282)**	(1,487)	**(2,772)**	(3,412)
Death benefits	**(64)**	(70)	**(123)**	(130)
Net inflows (outflows)	**497**	236	**825**	134
Change in fair value of underlying investments, interest credited, net of fees	**52**	2,234	**(2,745)**	3,195
Other	**—**	1	**—**	1
Balance at end of period	**$ 66,189**	$ 67,687	**$ 66,189**	$ 67,687
Individual fixed annuities				
Balance at beginning of period	**$ 51,540**	$ 52,339	**$ 50,508**	$ 52,685
Deposits	**1,944**	1,633	**4,475**	2,864
Surrenders and other withdrawals	**(1,461)**	(1,859)	**(3,040)**	(3,519)
Death benefits	**(442)**	(449)	**(824)**	(857)
Net inflows (outflows)	**41**	(675)	**611**	(1,512)
Change in fair value of underlying investments, interest credited, net of fees	**496**	506	**958**	997
Balance at end of period	**$ 52,077**	$ 52,170	**$ 52,077**	$ 52,170
Individual variable annuities				
Balance at beginning of period	**$ 30,830**	$ 31,432	**$ 33,108**	$ 31,093
Deposits	**1,122**	1,204	**2,139**	2,212
Surrenders and other withdrawals	**(964)**	(1,057)	**(1,873)**	(2,047)
Death benefits	**(123)**	(129)	**(250)**	(250)
Net inflows (outflows)	**35**	18	**16**	(85)
Change in fair value of underlying investments, interest credited, net of fees	**(198)**	1,601	**(2,457)**	2,043
Balance at end of period	**$ 30,667**	$ 33,051	**$ 30,667**	$ 33,051
Total Domestic Retirement Services				
Balance at beginning of period	**$148,010**	$148,987	**$151,725**	$148,135
Deposits	**4,909**	4,630	**10,334**	8,752
Surrenders and other withdrawals	**(3,707)**	(4,403)	**(7,685)**	(8,978)
Death benefits	**(629)**	(648)	**(1,197)**	(1,237)
Net inflows (outflows)	**573**	(421)	**1,452**	(1,463)
Change in fair value of underlying investments, interest credited, net of fees	**350**	4,341	**(4,244)**	6,235
Other	**—**	1	**—**	1
Balance at end of period, excluding runoff	**148,933**	152,908	**148,933**	152,908
Individual annuities runoff	**5,476**	5,977	**5,476**	5,977
Balance at end of period	**$154,409**	$158,885	**$154,409**	$158,885
General and separate account reserves and mutual funds				
General account reserve			**$ 91,467**	$ 90,729
Separate account reserve			**54,629**	60,554
Total general and separate account reserves			**146,096**	151,283
Group retirement mutual funds			**8,313**	7,602
Total reserves and mutual funds			**$154,409**	$158,885

The improvement in individual fixed annuity deposits was due to a steepened yield curve, providing the opportunity to offer higher interest crediting rates than certificates of deposits (CDs) and mutual fund money market rates available at the time. However, beginning in the three-month period ended June 30, 2008, CDs offering more competitive crediting rates than those currently available on fixed annuities have started to slow fixed annuity sales.

Domestic Retirement Services surrenders and other withdrawals decreased in all product lines in the three and six-month periods ended June 30, 2008 compared to the same periods in 2007. In general, surrenders and other withdrawals decreased as a result of the relative lack of attractive alternative investment products. Group retirement surrenders and withdrawals decreased as a result of a few large group mutual fund surrenders in the first quarter of 2007 and a general reduction in second quarter 2008 surrenders.

Domestic Retirement Services reserves by surrender charge category and surrender rates were as follows:

(in millions)	Group Retirement Products*	Individual Fixed Annuities	Individual Variable Annuities
June 30, 2008			
No surrender charge	**$48,399**	**$11,465**	**$12,288**
0% - 2%	**2,659**	**3,519**	**4,545**
Greater than 2% – 4%	**3,309**	**7,325**	**4,002**
Greater than 4%	**2,621**	**26,441**	**9,524**
Non-surrenderable	**888**	**3,327**	**308**
Total reserves	**$57,876**	**$52,077**	**$30,667**
Surrender rates	**8.4%**	**11.8%**	**12.0%**
June 30, 2007			
No surrender charge	$45,361	$10,813	$12,591
0% - 2%	6,734	4,068	5,424
Greater than 2% – 4%	3,872	6,665	5,589
Greater than 4%	3,241	27,182	9,355
Non-surrenderable	877	3,442	92
Total reserves	$60,085	$52,170	$33,051
Surrender rates	10.4%	13.4%	12.8%

** Excludes mutual funds of $8.3 billion and $7.6 billion at June 30, 2008 and 2007, respectively.*

Surrender rates decreased for all three product lines in the three- and six-month periods ended June 30, 2008 compared to the same periods in 2007. The surrender rate for individual fixed annuities continues to be driven by the yield curve and the general aging of the in-force block. However, less than 23 percent of the individual fixed annuity reserves as of June 30, 2008 were available for surrender without charge.

An increase in the level of surrenders in any of these businesses could accelerate the amortization of DAC and negatively affect fee income earned on assets under management.

Life Insurance & Retirement Services Net Investment Income and Net Realized Capital Gains (Losses)

The components of net investment income for Life Insurance & Retirement Services were as follows:

	Three Months Ended June 30,		Six Months Ended June 30,	
(in millions)	**2008**	2007	**2008**	2007
Foreign Life Insurance & Retirement Services:				
Fixed maturities, including short-term investments	**$2,334**	$1,940	**$4,547**	$ 3,839
Equity securities	**79**	126	**111**	98
Interest on mortgage and other loans	**143**	114	**275**	227
Partnership income	**9**	38	**11**	86
Mutual funds	**76**	103	**(4)**	163
Trading account losses	**(133)**	(14)	**(221)**	(14)
Other[(a)]	**134**	60	**246**	128
Total investment income before policyholder income and trading gains (losses)	**2,642**	2,367	**4,965**	4,527
Policyholder investment income and trading gains (losses)[(b)]	**606**	1,079	**(156)**	1,876
Total investment income	**3,248**	3,446	**4,809**	6,403
Investment expenses	**86**	85	**199**	159
Net investment income	**$3,162**	$3,361	**$4,610**	$ 6,244
Domestic Life Insurance:				
Fixed maturities, including short-term investments	**$ 847**	$ 870	**$1,711**	$ 1,781
Equity securities	**24**	(2)	**41**	(3)
Interest on mortgage and other loans	**105**	102	**202**	202
Partnership income — excluding Synfuels	**(6)**	60	**25**	87
Partnership loss — Synfuels	**(4)**	(42)	**(8)**	(75)
Mutual funds	**3**	3	**1**	5
Other[(a)]	**41**	26	**62**	40
Total investment income before policyholder income and trading gains (losses)	**1,010**	1,017	**2,034**	2,037
Policyholder investment income and trading gains (losses)[(b)]	**11**	—	**(12)**	—
Total investment income	**1,021**	1,017	**2,022**	2,037
Investment expenses	**15**	11	**32**	26
Net investment income	**$1,006**	$1,006	**$1,990**	$ 2,011
Domestic Retirement Services:				
Fixed maturities, including short-term investments	**$1,137**	$1,364	**$2,348**	$ 2,764
Equity securities	**6**	21	**9**	24
Interest on mortgage and other loans	**149**	135	**297**	256
Partnership income	**83**	253	**94**	383
Other[(a)]	**59**	4	**72**	(8)
Total investment income	**1,434**	1,777	**2,820**	3,419
Investment expenses	**16**	12	**31**	29
Net investment income	**$1,418**	$1,765	**$2,789**	$ 3,390
Total:				
Fixed maturities, including short-term investments	**$4,318**	$4,174	**$8,606**	$ 8,384
Equity securities	**109**	145	**161**	119
Interest on mortgage and other loans	**397**	351	**774**	685
Partnership income — excluding Synfuels	**86**	351	**130**	556
Partnership loss — Synfuels	**(4)**	(42)	**(8)**	(75)
Mutual funds	**79**	106	**(3)**	168
Trading account losses	**(133)**	(14)	**(221)**	(14)
Other[(a)]	**234**	90	**380**	160
Total investment income before policyholder income and trading gains (losses)	**5,086**	5,161	**9,819**	9,983
Policyholder investment income and trading gains (losses)[(b)]	**617**	1,079	**(168)**	1,876
Total investment income	**5,703**	6,240	**9,651**	11,859
Investment expenses	**117**	108	**262**	214
Net investment income	**$5,586**	$6,132	**$9,389**	$11,645

(a) Includes real estate income, income on non-partnership invested assets, securities lending and Foreign Life Insurance & Retirement Services' equal share of the results of AIG Credit Card Company (Taiwan).

(b) Relates principally to assets held in various trading securities accounts that do not qualify for separate account treatment under AICPA SOP 03-1, "Accounting and Reporting by Insurance Enterprises for Certain Nontraditional Long-Duration Contracts and for Separate Accounts" (SOP 03-1). These amounts are principally offset by an equal change included in incurred policy losses and benefits.

Net investment income decreased $546 million and $2.3 billion in the three- and six-month periods ended June 30, 2008 compared to the same periods in 2007, respectively, reflective of the recent market volatility. For the three- and six-month periods ended June 30, 2008, policyholder trading gains (losses) were $617 million and $(168) million, respectively, compared to gains of $1.1 billion and $1.9 billion in the same period of 2007 reflecting equity market declines in Japan and Asia. In addition, net investment income was negatively affected by

lower yield enhancement income from equity investments, and higher trading account losses of $119 million and $207 million for the three- and six-month periods ended June 30, 2008 compared to the same periods in 2007. Domestic Retirement Services held higher balances in cash and short-term investments which negatively affected investment income on fixed maturity securities. Historically, AIG generated income tax credits as a result of investing in Synfuels related to the partnership income (loss) shown in the table above. Synfuel production ceased effective December 31, 2007.

The components of net realized capital gains (losses) for Life Insurance & Retirement Services were as follows:

	Three Months Ended June 30,		Six Months Ended June 30,	
(in millions)	**2008**	2007	**2008**	2007
Foreign Life Insurance & Retirement Services:				
Sales of fixed maturities	**$ 19**	$ (25)	**$ 16**	$ (45)
Sales of equity securities	**192**	180	**271**	212
Other:				
Other-than-temporary impairments[(a)]	**(1,071)**	(131)	**(2,087)**	(462)
Foreign exchange transactions	**(170)**	(25)	**(193)**	90
Derivatives instruments	**(32)**	52	**83**	(65)
Other[(b)]	**153**	(33)	**279**	53
Total Foreign Life Insurance & Retirement Services	**$ (909)**	$ 18	**$ (1,631)**	$(217)
Domestic Life Insurance:				
Sales of fixed maturities	**$ (18)**	$ (58)	**$ (10)**	$ (39)
Sales of equity securities	**2**	4	**3**	5
Other:				
Other-than-temporary impairments[(a)]	**(1,440)**	(49)	**(2,659)**	(68)
Foreign exchange transactions	**6**	–	**4**	2
Derivatives instruments	**58**	41	**(67)**	30
Other[(c)]	**16**	46	**65**	42
Total Domestic Life Insurance	**$ (1,376)**	$ (16)	**$ (2,664)**	$ (28)
Domestic Retirement Services:				
Sales of fixed maturities	**$ (55)**	$ (79)	**$ (63)**	$ (60)
Sales of equity securities	**3**	5	**23**	16
Other:				
Other-than-temporary impairments[(a)]	**(2,682)**	(144)	**(4,839)**	(186)
Foreign exchange transactions	**14**	1	**(1)**	7
Derivatives instruments	**15**	(52)	**(185)**	(47)
Other[(c)]	**(20)**	(12)	**(19)**	(20)
Total Domestic Retirement Services	**$ (2,725)**	$(281)	**$ (5,084)**	$(290)
Total:				
Sales of fixed maturities	**$ (54)**	$(162)	**$ (57)**	$(144)
Sales of equity securities	**197**	189	**297**	233
Other:				
Other-than-temporary impairments[(a)]	**(5,193)**	(324)	**(9,585)**	(716)
Foreign exchange transactions	**(150)**	(24)	**(190)**	99
Derivatives instruments	**41**	41	**(169)**	(82)
Other[(b)(c)]	**149**	1	**325**	75
Total	**$ (5,010)**	$(279)	**$ (9,379)**	$(535)

(a) See Invested Assets — Portfolio Review — Other-Than-Temporary Impairments for additional information.

(b) Includes losses of $167 million and gains of $66 million allocated to participating policyholders for the three-month periods ended June 30, 2008 and 2007, respectively, and losses of $178 million and $5 million for the six-month periods ended June 30, 2008 and 2007, respectively.

(c) Includes losses of $12 million and $143 million for the six-month period ended June 30, 2008 for Domestic Life Insurance and Domestic Retirement Services, respectively, related to the adoption of FAS 157 related to embedded policy derivatives.

Included in net realized capital gains (losses) are gains (losses) on sales of investments, derivative gains (losses) for transactions that did not qualify for hedge accounting treatment under FAS 133, foreign exchange gains and losses, other-than-temporary impairments and the effects of the adoption of FAS 157 further described below.

Foreign Life Insurance & Retirement Services net realized capital losses were significantly higher in the first six months of 2008 compared to the same period in 2007. The increased Foreign Life Insurance & Retirement Services other-than-temporary impairments were primarily driven by severity losses and foreign currency declines. See Invested Assets — Portfolio Review herein for further information. Foreign currency losses of $170 million and $193 million in the three and six-month periods ended June 30, 2008, respectively, related primarily to the decline in value of U.S. dollar bonds supporting liabilities denominated in Taiwan dollars, Singapore dollars, Japanese yen and British pounds sterling. Derivatives in the Foreign Life Insurance & Retirement Services operations are primarily used to economically hedge cash flows related to U.S. dollar bonds back to the respective currency of the country, principally in Taiwan, Thailand and Singapore. These derivatives do not

qualify for hedge accounting treatment under FAS 133 and are recorded in net realized capital gains (losses). The corresponding foreign exchange gain or loss with respect to the economically hedged bond is deferred in accumulated other comprehensive income (loss) until the bond is sold, matures or deemed to be other-than-temporarily impaired.

In the three- and six-month periods ended June 30, 2008, the Domestic Life Insurance and Domestic Retirement Services operations incurred higher net realized capital losses primarily due to other-than-temporary impairment charges related to severity. Derivatives in the Domestic Life Insurance operations include affiliated interest rate swaps used to economically hedge cash flows on bonds and option contracts used to economically hedge cash flows on indexed annuity and universal life products. These derivatives do not qualify for hedge accounting treatment under FAS 133 and are recorded in net realized capital gains (losses). The corresponding gain or loss with respect to the economically hedged bond is deferred in accumulated other comprehensive income (loss) until the bond is sold, matures or is deemed to be other-than-temporarily impaired.

The most significant effect of AIG's adoption of FAS 157 was the change in measurement of fair value for embedded policy derivatives. The pre-tax effect of adoption related to embedded policy derivatives was an increase in net realized capital losses of $155 million as of January 1, 2008. The effect of initial adoption was primarily due to an increase in the embedded policy derivative liability valuations resulting from the inclusion of explicit risk margins.

Deferred Policy Acquisition Costs and Sales Inducement Assets

DAC for Life Insurance & Retirement Services products arises from the deferral of costs that vary with, and are directly related to, the acquisition of new or renewal business. Policy acquisition costs for life insurance products are generally deferred and amortized over the premium paying period in accordance with FAS 60, "Accounting and Reporting by Insurance Enterprises" (FAS 60). Policy acquisition costs that relate to universal life and investment-type products are generally deferred and amortized, with interest in relation to the incidence of estimated gross profits to be realized over the estimated lives of the contracts in accordance with FAS 97. Value of Business Acquired (VOBA) is determined at the time of acquisition and is reported on the consolidated balance sheet with DAC and amortized over the life of the business, similar to DAC. AIG offers sales inducements to contract holders (bonus interest) on certain annuity and investment contracts. Sales inducements are recognized as part of the liability for policyholders' contract deposits on the consolidated balance sheet and are amortized over the life of the contract similar to DAC. The deferral of acquisition and sales inducement costs increased $280 million in the six-month period ended June 30, 2008 compared to the same period in 2007 primarily due to higher production in the Foreign Life Insurance operations and Domestic Retirement Services. Total amortization expense increased by $81 million in the six-month period ended June 30, 2008 compared to the same period in 2007. The current year amortization includes a $479 million increase to operating income related to net realized capital losses in the first six months of 2008 compared to $114 million in the same period of 2007 reflecting significantly higher other-than-temporary impairment charges. Annualized amortization expense levels in the first six months of 2008 and 2007 were approximately 11 percent and 12 percent, respectively, of the opening DAC balance.

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

The major components of the changes in DAC/VOBA and SIA were as follows:

(in millions)	Six Months Ended June 30, 2008 DAC/VOBA	2008 SIA	2008 Total	2007 DAC/VOBA	2007 SIA	2007 Total
Foreign Life Insurance & Retirement Services						
Balance at beginning of year	**$26,175**	**$ 681**	**$26,856**	$21,153	$ 404	$21,557
Acquisition costs deferred	**2,711**	**49**	**2,760**	2,510	60	2,570
Amortization (charged) or credited to operating income:						
Related to net realized capital gains (losses)	**60**	**(3)**	**57**	45	1	46
Related to unlocking future assumptions	**(4)**	**(2)**	**(6)**	30	2	32
All other amortization	**(1,783)**	**(28)**	**(1,811)**	(1,344)	2	(1,342)
Change in unrealized gains (losses) on securities	**692**	**5**	**697**	531	7	538
Increase (decrease) due to foreign exchange	**781**	**2**	**783**	(230)	1	(229)
Other*	**(1,090)**	**(299)**	**(1,389)**	(78)	—	(78)
Balance at end of period	**$27,542**	**$ 405**	**$27,947**	$22,617	$ 477	$23,094
Domestic Life Insurance						
Balance at beginning of year	**$ 6,432**	**$ 53**	**$ 6,485**	$ 6,006	$ 46	$ 6,052
Acquisition costs deferred	**439**	**10**	**449**	442	10	452
Amortization (charged) or credited to operating income:						
Related to net realized capital gains (losses)	**37**	**—**	**37**	4	—	4
All other amortization	**(302)**	**(5)**	**(307)**	(344)	(3)	(347)
Change in unrealized gains (losses) on securities	**210**	**—**	**210**	230	—	230
Increase (decrease) due to foreign exchange	**(17)**	**—**	**(17)**	45	—	45
Other*	**—**	**—**	**—**	(64)		(64)
Balance at end of period	**$ 6,799**	**$ 58**	**$ 6,857**	$ 6,319	$ 53	$ 6,372
Domestic Retirement Services						
Balance at beginning of year	**$ 5,838**	**$ 991**	**$ 6,829**	$ 5,651	$ 887	$ 6,538
Acquisition costs deferred	**462**	**108**	**570**	376	101	477
Amortization (charged) or credited to operating income:						
Related to net realized capital gains (losses)	**309**	**76**	**385**	52	12	64
Related to unlocking future assumptions	**—**	**—**	**—**	2	—	2
All other amortization	**(409)**	**(92)**	**(501)**	(445)	(79)	(524)
Change in unrealized gains (losses) on securities	**439**	**96**	**535**	318	64	382
Increase (decrease) due to foreign exchange	**1**	**—**	**1**	—	—	—
Balance at end of period	**$ 6,640**	**$1,179**	**$ 7,819**	$ 5,954	$ 985	$ 6,939
Total Life Insurance & Retirement Services						
Balance at beginning of year	**$38,445**	**$1,725**	**$40,170**	$32,810	$1,337	$34,147
Acquisition costs deferred	**3,612**	**167**	**3,779**	3,328	171	3,499
Amortization (charged) or credited to operating income:						
Related to net realized capital gains (losses)	**406**	**73**	**479**	101	13	114
Related to unlocking future assumptions	**(4)**	**(2)**	**(6)**	32	2	34
All other amortization	**(2,494)**	**(125)**	**(2,619)**	(2,133)	(80)	(2,213)
Change in unrealized gains (losses) on securities	**1,341**	**101**	**1,442**	1,079	71	1,150
Increase (decrease) due to foreign exchange	**765**	**2**	**767**	(185)	1	(184)
Other*	**(1,090)**	**(299)**	**(1,389)**	(142)	—	(142)
Balance at end of period	**$40,981**	**$1,642**	**$42,623**	$34,890	$1,515	$36,405

** In 2008, primarily represents the cumulative effect of adoption of FAS 159. In 2007, primarily represents the cumulative effect of adoption of SOP 05-1.*

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

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

charge and AIG's results of operations could be significantly affected in future periods.

Future Policy Benefit Reserves

Periodically, the net benefit reserves (policy benefit reserves less DAC) established for Life Insurance & Retirement Services companies are tested to ensure that, including consideration of future expected premium payments, they are adequate to provide for future policyholder benefit obligations. The assumptions used to perform the tests are current best-estimate assumptions as to policyholder mortality, morbidity, terminations, company maintenance expenses and invested asset returns. For long duration traditional business, a "lock-in" principle applies, whereby the assumptions used to calculate the benefit reserves and DAC are set when a policy is issued and do not change with changes in actual experience. These assumptions include margins for adverse deviation in the event that actual experience might deviate from these assumptions. For business in force outside of North America, 46 percent of total policyholder benefit liabilities at June 30, 2008 represent traditional business where the lock-in principle applies. In most foreign locations, various guarantees are embedded in policies in force that may remain applicable for many decades into the future.

As experience changes over time, the best-estimate assumptions are updated to reflect observed changes. Because of the long-term nature of many of AIG's liabilities subject to the lock-in principle, small changes in certain of the assumptions may cause large changes in the degree of reserve adequacy. In particular, changes in estimates of future invested asset return assumptions have a large effect on the degree of reserve adequacy.

Taiwan

Beginning in 2000, the yield available on Taiwanese 10-year government bonds dropped from approximately 6 percent to 2.7 percent at June 30, 2008. Yields on most other invested assets have correspondingly dropped over the same period. Current sales are focused on products such as:

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

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

- Observed historical mortality improvement trends have been projected to 2014;
- Morbidity, expense and termination rates have been updated to reflect recent experience;
- Taiwan government bond rates are expected to remain at current levels for 10 years and gradually increase to best-estimate assumptions of a market consensus view of long-term interest rate expectations;
- Foreign assets are assumed to comprise 35 percent of invested assets, resulting in a composite long-term investment assumption of approximately 4.8 percent; and
- The current practice permitted in Taiwan of offsetting positive mortality experience with negative interest margins, thus eliminating the need for mortality dividends, will continue.

Future results of the reserve adequacy tests will involve significant management judgment as to mortality, morbidity, expense and termination rates and investment yields. Adverse changes in these assumptions could accelerate DAC amortization and necessitate reserve strengthening.

Financial Services Operations

AIG's Financial Services subsidiaries engage in diversified activities including aircraft and equipment leasing, capital markets, consumer finance and insurance premium finance.

Financial Services Results

Financial Services results were as follows:

(in millions)	Three Months Ended June 30, 2008	Three Months Ended June 30, 2007	Percentage Increase/ (Decrease)	Six Months Ended June 30, 2008	Six Months Ended June 30, 2007	Percentage Increase/ (Decrease)
Total revenues:						
Aircraft Leasing	**$ 1,298**	$ 1,173	11%	**$ 2,463**	$ 2,231	10%
Capital Markets[(a)]	**(6,088)**	(67)	—	**(14,831)**	161	—
Consumer Finance[(b)]	**1,028**	911	13	**1,959**	1,756	12
Other, including intercompany adjustments	**157**	106	48	**244**	176	39
Total	**$ (3,605)**	$ 2,123	—%	**$ (10,165)**	$ 4,324	—%
Operating income (loss):						
Aircraft Leasing	**$ 334**	$ 207	61%	**$ 555**	$ 371	50%
Capital Markets[(a)]	**(6,284)**	(255)	—	**(15,211)**	(187)	—
Consumer Finance[(b)]	**(33)**	75	—	**(85)**	111	—
Other, including intercompany adjustments	**78**	20	290	**64**	44	45
Total	**$ (5,905)**	$ 47	—%	**$ (14,677)**	$ 339	—%

(a) Revenues are shown net of interest expense of $1.2 billion and $805 million in the three-month periods ended June 30, 2008 and 2007, respectively, and $1.7 billion and $1.9 billion for the six-month periods ended June 30, 2008 and 2007, respectively. In the three- and six-month periods ended June 30, 2008, both revenues and operating income (loss) include unrealized market valuation losses of $5.6 billion and $14.7 billion, respectively, on AIGFP's super senior credit default swap portfolio.

(b) The three-month and six-month periods ended June 30, 2007 included pre-tax charges of $50 million and $178 million, respectively, in connection with domestic Consumer Finance's mortgage banking activities. Based on a current evaluation of the estimated cost of implementing the Supervisory Agreement entered into with the OTS, partial reversals of these prior year charges included in the three- and six-month periods ended June 30, 2008 were $25 million and $43 million, respectively.

Financial Services reported operating losses in the three- and six-month periods ended June 30, 2008 compared to operating income in the same periods in 2007, primarily due to unrealized market valuation losses of $5.6 billion and $14.7 billion in the three- and six-month periods ended June 30, 2008, respectively, on AIGFP's super senior credit default swap portfolio, the remaining operating loss resulting from the change in credit spreads on AIGFP's other assets and liabilities and a decline in operating income for AGF. AGF's operating income declined in the three- and six-month periods ended June 30, 2008 compared to the same periods in 2007 primarily due to increases in the provision for finance receivable losses and unfavorable variances related to derivatives that economically hedge AGF debt. In addition, in the three months ended June 30, 2008, AGF recorded a pre-tax charge of $27 million resulting from AGF's decision to cease its wholesale originations.

ILFC generated strong operating income growth in the three- and six-month periods ended June 30, 2008 compared to the same periods in 2007, driven to a large extent by a larger aircraft fleet, higher lease rates and higher utilization and lower composite borrowing rates.

Aircraft Leasing

Aircraft Leasing operations represent the operations of ILFC, which generates its revenues primarily from leasing new and used commercial jet aircraft to foreign and domestic airlines. Revenues also result from the remarketing of commercial aircraft for ILFC's own account, and remarketing and fleet management services for airlines and financial institutions. ILFC finances its aircraft purchases primarily through the issuance of debt instruments. ILFC economically hedges part of its floating rate and substantially all of its foreign currency denominated debt using interest rate and foreign currency derivatives. Starting in the second quarter of 2007, ILFC began applying hedge accounting to most of its derivatives. The composite borrowing rates, which include the effect of derivatives, at June 30, 2008 and 2007 were 4.74 percent and 5.25 percent, respectively.

ILFC typically contracts to re-lease aircraft before the end of the existing lease term. For aircraft returned before the end of the lease term, ILFC has generally been able to re-lease such aircraft within two to six months of their return. As a lessor, ILFC considers an aircraft "idle" or "off lease" when the aircraft is not subject to a signed lease agreement or signed letter of intent. During the three-month period ended June 30, 2008, 16 planes were returned to ILFC by bankrupt lessees. As of July 31, 2008, ILFC has leased all of the 16 aircraft.

Quarterly Aircraft Leasing Results

ILFC's operating income increased in the three-month period ended June 30, 2008 compared to the same period in 2007. Rental revenues increased by $130 million or 11 percent,

driven by a larger aircraft fleet, higher lease rates and higher utilization. As of June 30, 2008, 947 aircraft in ILFC's fleet were subject to operating leases compared to 894 aircraft as of June 30, 2007. ILFC had no aircraft off lease at July 31, 2008. Flight equipment marketing revenues increased by $26 million in the three-month period ended June 30, 2008 compared to the same period in 2007 due to an increase in aircraft sales. Interest expense decreased by $41 million in the three-month period ended June 30, 2008 compared to the same period in 2007 as a result of lower short-term interest rates. The increases in revenues were partially offset by an increase in depreciation and a credit value adjustment on derivatives. Depreciation expense increased by $30 million, or 7 percent, in line with the increase in the size of the aircraft fleet. In the three-month period ended June 30, 2008 and 2007, the gains (losses) from hedging activities that did not qualify for hedge accounting treatment under FAS 133, including the related foreign exchange gains and losses, were $(15) million and $24 million, respectively, in both revenues and operating income. The net derivative loss for the three-month period ended June 30, 2008 includes the effect of changes in AIG's credit spreads of $11 million.

Year-to-Date Aircraft Leasing Results

ILFC's operating income increased in the six-month period ended June 30, 2008 compared to the same period in 2007. Rental revenues increased by $251 million or 11 percent, driven by a larger aircraft fleet, higher lease rates and higher utilization. As of June 30, 2008, 947 aircraft in ILFC's fleet were subject to operating leases compared to 894 aircraft as of June 30, 2007. ILFC had no aircraft off lease at July 31, 2008, and all of the new aircraft scheduled for delivery through 2009 have been leased. Flight equipment marketing revenues increased by $34 million in the six-month period ended June 30, 2008 compared to the same period in 2007 due to an increase in aircraft sales. Interest expense decreased by $30 million in the six-month period ended June 30, 2008, compared to the same period in 2007, as a result of lower short-term interest rates. The increases in revenues were partially offset by an increase in depreciation and a credit value adjustment on derivatives as a result of the adoption of FAS 157. Depreciation expense increased by $75 million, or 9 percent, in line with the increase in the size of the aircraft fleet. In the six-month period ended June 30, 2008 and 2007, the gains (losses) from hedging activities that did not qualify for hedge accounting treatment under FAS 133, including the related foreign exchange gains and losses, were $(63) million and $(13) million, respectively, in both revenues and operating income. The net derivative loss for the six-month period ended June 30, 2008 includes the effect of changes in AIG's credit spreads of $51 million, of which $12 million represents the transition amount from the adoption of FAS 157.

Capital Markets

Capital Markets represents the operations of AIGFP, which engages as principal in a wide variety of financial transactions, including standard and customized financial products involving commodities, credit, currencies, energy, equities and rates. The credit products include credit protection written through credit default swaps on super senior risk tranches of diversified pools of loans and debt securities. AIGFP also invests in a diversified portfolio of securities and principal investments and engages in borrowing activities involving the issuance of standard and structured notes and other securities, and entering into GIAs.

As Capital Markets is a transaction-oriented operation, current and past revenues and operating results may not provide a basis for predicting future performance. Through 2007, AIG's Capital Markets operations derived a significant portion of their revenues from hedged financial positions entered into in connection with counterparty transactions. AIGFP also participates as a dealer in a wide variety of financial derivatives transactions. Revenues and operating income of the Capital Markets operations and the percentage change in these amounts for any given period are significantly affected by changes in the fair value of AIGFP's assets and liabilities and by the number, size and profitability of transactions entered into during that period relative to those entered into during the prior period. Generally, the realization of transaction revenues as measured by the receipt of funds is not a significant reporting event as the gain or loss on AIGFP's trading transactions is currently reflected in operating income as the fair values change from period to period.

AIGFP's products generally require sophisticated models and significant management assumptions to determine fair values and, particularly during times of market disruption, the absence of observable market data can result in fair values at any given balance sheet date that are not indicative of the ultimate settlement values of the products.

Quarterly Capital Markets Results

Capital Markets reported an operating loss in the three-month period ended June 30, 2008 compared to operating income in the same period of 2007, primarily due to unrealized market valuation losses related to AIGFP's super senior credit default swap portfolio principally written on multi-sector CDOs. Financial market conditions during the second quarter of 2008 were characterized by widening credit spreads.

In addition to writing credit protection on the super senior risk layer on designated portfolios of loans or debt securities, AIGFP also wrote protection on tranches below the super senior risk layer. At June 30, 2008, the net notional amount of the credit default swaps in the regulatory capital relief portfolio written on tranches below the super senior

risk layer was $5.8 billion, with an estimated fair value loss of $171 million.

At June 30, 2008, the notional amount, fair value and unrealized market valuation loss of the AIGFP super senior credit default swap portfolio, including certain regulatory capital relief transactions, by asset class were as follows:

(in millions)	Notional Amount	Fair Value Loss at June 30, 2008	Unrealized Market Valuation Loss (Gain) Three Months Ended June 30, 2008[a]	Unrealized Market Valuation Loss (Gain) Six Months Ended June 30, 2008[a]
Regulatory Capital:[b]				
Corporate loans	$172,717	$ —	$ —	$ —
Prime residential mortgages	132,612	—	—	—
Other[c][d]	1,619	125	125	125
Total	306,948	125	125	125
Arbitrage:				
Multi-sector CDOs[e]	80,301	24,785	5,569	13,606
Corporate debt/CLOs	53,767	996	(126)	770
Total	134,068	25,781	5,443	14,376
Mezzanine tranches[f]	5,824	171	(3)	171
Total	$446,840	$ 26,077[g]	$5,565	$14,672

(a) Includes credit valuation adjustment gains of $44 million and $109 million, respectively, for the three- and six-month periods ended June 30, 2008.

(b) Represents predominantly transactions written to facilitate regulatory capital relief.

(c) Represents transactions where AIGFP believes the counterparties are no longer using the transactions to obtain regulatory capital relief.

(d) During the second quarter of 2008, a European RMBS regulatory capital relief transaction with a notional amount of $1.6 billion was not terminated as expected when it no longer provided regulatory capital relief to the counterparty.

(e) Approximately $57.8 billion in net notional amount includes some exposure to U.S. sub-prime mortgages and approximately $9.6 billion in net notional amount includes CDOs of CMBS.

(f) Represents credit default swaps written by AIGFP on tranches below super senior on certain regulatory capital relief trades.

(g) Fair value amounts are shown before the effects of counterparty netting adjustments.

During the second quarter of 2008, AIGFP implemented further refinements to the cash flow waterfall used by the BET model and the assumptions used therein. These refinements reflected the ability of a CDO to use principal proceeds to cover interest payment obligations on lower-rated tranches, the ability of a CDO to use principal proceeds to cure a breach of an overcollateralization test, the ability of a CDO to amortize certain senior CDO tranches on a pro-rata or sequential basis and the preferential payment of management fees. To the extent there is a lag in the prices provided by the collateral managers, AIG refines those prices by rolling them forward to the end of the quarter using prices provided by a third party pricing service. The net effect of these refinements was an incremental unrealized market valuation loss of $342 million. Refinements made during the first quarter of 2008 had only a de minimus effect on the unrealized market valuation loss.

During the three months ended June 30, 2008, AIGFP issued new 2a-7 Puts on the super senior security issued by a CDO of AAA-rated commercial mortgage-backed securities (CMBS) pursuant to a facility that was entered into in 2005. The terms of the facility required AIGFP to issue such options up to a notional amount of $7.5 billion. Approximately $2.1 billion were issued in November 2007 with the remainder issued in June 2008. Under the terms of the put options, AIGFP is required to purchase the referenced super senior obligations in the event of a failed remarketing of those securities. Upon the exercise of the put options, the counterparty will provide funding to AIGFP to purchase and hold the referenced super senior obligations for a period ranging from three to six years. At this time, AIGFP is not party to any commitments to enter into any new 2a-7 Puts. Included in the unrealized market valuation loss of the super senior credit default swap portfolio for the second quarter of 2008 was a loss of $810 million resulting from the change in fair value of these newly issued 2a-7 Puts.

In May 2008, AIGFP extinguished its obligations with respect to a credit default swap by purchasing the protected CDO security for $103 million, its principal amount outstanding related to this obligation. Additionally, AIGFP purchased $682 million of other super senior CDO securities in connection with 2a-7 Puts. Upon purchase, these securities were included in AIGFP's trading portfolio at their fair value. Approximately $67 million of the cumulative unrealized market valuation loss previously recognized on these derivatives as of March 31, 2008 was realized as a result of these purchases.

The change in fair value of AIGFP's credit default swaps was caused by the significant widening in spreads and the downgrades of RMBS and CDO securities by rating agencies in the six-month period ended June 30, 2008 driven by the credit concerns resulting from U.S. residential mortgages, the severe liquidity crisis affecting the markets and the effects of rating agency downgrades on structured securities.

Capital markets net operating loss for the three-month period ended June 30, 2008 includes a net loss of $474 million representing the effect of changes in credit spreads on the valuation of AIGFP's assets and liabilities, including $44 million of gains reflected in the unrealized market valuation loss on super senior credit default swaps. Losses of $362 million on the assets were primarily due to continued significant widening of credit spreads on CDOs and ABS products, which represent a significant portion of AIGFP's investment portfolio. While historically AIG's credit spreads and those on its assets moved in a similar fashion, that relationship did not exist in the second quarter of 2008. Credit spreads on the ABS and CDO investments widened significantly more than the widening in AIG's credit spreads. Furthermore, while AIG's credit spreads increased during the second quarter of 2008, the credit valuation adjustment on its

liabilities decreased due to a decline in AIGFP's outstanding debt obligations and the shortened maturity of its liabilities.

The following table presents AIGFP's credit spread gains (losses) for the three-month period ended June 30, 2008 (excluding intercompany transactions):

(in millions)

Counterparty Credit Spread Sensitivity on Assets		AIG Inc.'s Own Credit Spread Sensitivity on Liabilities	
Trading securities	$ (503)	Term notes	$ (79)
Loans and other assets	(4)	Hybrid term notes	(47)
Derivative assets	145	GIA's	(84)
		Other liabilities	(2)
		Derivative liabilities*	100
Decrease in assets	$ (362)	Increase in liabilities	$ (112)
Net pre-tax decrease to other income	$ (474)		

* *Includes super senior CDS portfolio*

During 2008, AIGFP's revenues from certain products have declined, in part, as a consequence of the continued disruption in the credit markets, the general decline in liquidity in the marketplace, and AIGFP's efforts to manage its liquidity. Furthermore, AIGFP has not been able to replace revenues previously generated from certain structured tax transactions that were terminated or matured at the end of 2007 and early 2008.

The most significant component of Capital Markets operating expenses is compensation, which was $155 million and $153 million in the three-month periods ended June 30, 2008 and 2007, respectively. The amount of compensation was not affected by gains and losses arising from derivatives not qualifying for hedge accounting treatment under FAS 133. In the first quarter of 2008, AIGFP established an employee retention plan, which guarantees a broad group of AIGFP's employees and consultants a minimum level of compensation for each of the 2008 and 2009 compensation years, subject to mandatory partial deferral which, in certain circumstances, will be indexed to the price of AIG stock. The deferred amounts may be reduced in the event of losses prior to payment. The expense related to the plan is being recognized over the vesting period, beginning in the first quarter of 2008.

AIGFP recognized a gain of $196 million in the three-month period ended June 30, 2007 on hybrid financial instruments for which it applied the fair value option under FAS 155, "Accounting for Certain Hybrid Financial Instruments — an amendment of FASB Statements No. 133 and 140" (FAS 155). These amounts were largely offset by gains and losses on economic hedge positions also reflected in AIGFP's operating income or loss.

Year-to-Date Capital Markets Results

Capital Markets reported an increased operating loss in the six-month period ended June 30, 2008 compared to the operating loss in the same period of 2007, primarily due to unrealized market valuation losses related to AIGFP's super senior credit default swap portfolio principally written on multi-sector CDOs. Financial market conditions in the six-month period ended June 30, 2008 were characterized by widening credit spreads and declining interest rates.

The net loss recognized for the six-month period ended June 30, 2007 included a $166 million reduction in fair value of certain derivatives that are an integral part of, and economically hedge, the structured transactions potentially affected by the proposed guidance by the U.S. Treasury Department affecting the ability to claim foreign tax credits.

Effective January 1, 2008, AIGFP adopted FAS 157. The most significant effect of adopting FAS 157 was a change in the valuation methodologies for hybrid financial instruments and derivative liabilities (both freestanding and embedded) historically carried at fair value. The changes were primarily to incorporate AIGFP's own credit risk, when appropriate, in the fair value measurements.

Effective January 1, 2008, AIGFP also elected to apply the fair value option under FAS 159 to all eligible assets and liabilities, other than equity method investments and trade receivables and trade payables. Electing the fair value option allows AIGFP to more closely align its earnings with the economics of its transactions by recognizing the change in fair value of its derivatives and the offsetting change in fair value of the assets and liabilities being hedged concurrently through earnings.

Capital Markets net operating loss for the six-month period ended June 30, 2008 includes an increase to pre-tax earnings of $2.5 billion attributable to changes in AIG's credit spreads, including $109 million of gains reflected in the unrealized market valuation loss on super senior credit default swaps, which were offset by the effect of changes in counterparty credit spreads on assets measured at fair value of $3.0 billion. Included in the six-month period ended June 30, 2008 net operating loss is the transition amount of $291 million related to the adoption of FAS 157 and FAS 159, as well as a credit valuation adjustment gain of $193 million for derivatives AIGFP entered into with other AIG entities, which is eliminated in consolidation.

The following table presents AIGFP's credit spread gains (losses) for the six-month period ended June 30, 2008 (excluding intercompany transactions):

(in millions)

Counterparty Credit Spread Sensitivity on Assets		AIG Inc.'s Own Credit Spread Sensitivity on Liabilities	
Trading securities	$(2,651)	Term notes	$ 182
Loans and other assets	(28)	Hybrid term notes	615
Derivative assets	(303)	GIA's	1,072
		Other liabilities	28
		Derivative liabilities*	639
Decrease in assets	$(2,982)	Decrease in liabilities	$2,536
Net pre-tax decrease to other income	$ (446)		

* *Includes super senior CDS portfolio*

AIGFP recognized a gain of $30 million in the six-month period ended June 30, 2007 on hybrid financial instruments for which it applied the fair value option under FAS 155. These amounts were largely offset by gains and losses on economic hedge positions also reflected in AIGFP's operating income or loss.

Capital Markets compensation expense was $298 million and $276 million in the six-month periods ended June 30, 2008 and 2007, respectively. The amount of compensation was not affected by gains and losses arising from derivatives not qualifying for hedge accounting treatment under FAS 133.

Consumer Finance

AIG's Consumer Finance operations in North America are principally conducted through AGF. AGF derives most of its revenues from finance charges assessed on outstanding real estate loans, secured and unsecured non-real estate loans and retail sales finance receivables and credit-related insurance.

Effective February 29, 2008, AGF purchased a portion of Equity One, Inc.'s consumer branch finance receivable portfolio consisting of $1.0 billion of real estate loans, $290 million of non-real estate loans, and $156 million of retail sales finance receivables.

AIG's foreign consumer finance operations are principally conducted through AIG Consumer Finance Group, Inc. (AIGCFG). AIGCFG operates primarily in emerging and developing markets. AIGCFG has operations in Argentina, China, Hong Kong, Mexico, Philippines, Poland, Taiwan, Thailand, India and Colombia. In April 2008, AIGCFG decided to sell or liquidate its existing operations in Taiwan.

Certain of the AIGCFG operations are partly or wholly owned by life insurance subsidiaries of AIG. Accordingly, the financial results of those companies are allocated between Financial Services and Life Insurance & Retirement Services according to their ownership percentages. While products vary by market, the businesses generally provide credit cards, unsecured and secured non-real estate loans, term deposits, savings accounts, retail sales finance and real estate loans. AIGCFG originates finance receivables through its branches and direct solicitation. AIGCFG also originates finance receivables indirectly through relationships with retailers, auto dealers, and independent agents.

Quarterly Consumer Finance Results

Consumer Finance operating income decreased in the three-month period ended June 30, 2008 compared to the same period in 2007. Operating income from the domestic consumer finance operations, which include the operations of AGF and AIG Federal Savings Bank, decreased by $115 million in the three-month period ended June 30, 2008 compared to the same period in 2007. In the three-month period ended June 30, 2007, domestic results were adversely affected by the weakening housing market, which resulted in lower originations of real estate loans as well as the additional $50 million charge relating to the estimated cost of implementing the Supervisory Agreement entered into with the OTS.

AGF's revenues increased $29 million or 4 percent during the three-month period ended June 30, 2008 compared to the same period in 2007. Revenues from AGF's finance receivables benefited from the $1.5 billion finance receivable purchase in first quarter 2008, but were partially offset by reduced residential mortgage originations reflecting the slower U.S. housing market. Revenues from AGF's mortgage banking activities increased $55 million during the three-month period ended June 30, 2008 compared to the same period in 2007 (which included the second quarter 2007 charge of $50 million related to the Supervisory Agreement). Based on a current evaluation of the estimated cost of implementing the Supervisory Agreement entered into with the OTS, a partial reversal of $25 million of these prior year charges was recorded in the second quarter of 2008.

During 2007 and the six months ended June 30, 2008, the U.S. residential real estate and credit markets experienced significant turmoil as housing prices softened, unemployment increased, consumer delinquencies increased, and credit availability contracted and became more expensive for consumers and financial institutions. These market developments are reflected in AGF's decline in operating income in 2007 and 2008. AGF's operating income declined in the three-month period ended June 30, 2008 compared to the same period in 2007 primarily due to increases in the provision for finance receivable loss of $153 million and unfavorable variances related to derivatives that economically hedge AGF debt. During the three-month period ended June 30, 2008, AGF recorded a net gain of $5 million on its derivatives that did not qualify for hedge accounting under FAS 133, compared to a net gain of $17 million in the same period in 2007. The net derivative

gain for the three-month period ended June 30, 2008 reflected the effect of changes in AIG's credit spreads. AGF's operating income also reflected a pre-tax charge of $27 million resulting from AGF's decision to cease its wholesale originations.

AGF's net finance receivables totaled $26.5 billion at June 30, 2008, an increase of approximately $1.6 billion compared to the prior year period, including the purchase of $1.5 billion of finance receivables from Equity One, Inc. on February 29, 2008. The increase in the net finance receivables resulted in a similar increase in revenues generated from these assets.

Revenues from the foreign consumer finance operations increased by 50 percent in the three-month period ended June 30, 2008 compared to the same period in 2007. Loan growth, particularly in Poland, Mexico and Latin America, was the primary driver of the increased revenues. In addition, revenues from recently acquired businesses in India and Thailand contributed to the increase. The increase in revenues was more than offset by higher expenses associated with branch expansions, acquisition activities and product promotion campaigns.

Year-to-Date Consumer Finance Results

Consumer Finance operating income decreased in the six-month period ended June 30, 2008 compared to the same period in 2007. Operating income from the domestic consumer finance operations, which include the operations of AGF and AIG Federal Savings Bank, decreased by $190 million in the six-month period ended June 30, 2008 compared to the same period in 2007. In the six-month period ended June 30, 2007, domestic results were adversely affected by the weakening housing market, which resulted in lower originations of real estate loans as well as the $178 million charge relating to the estimated cost of implementing the Supervisory Agreement entered into with the OTS.

AGF's revenues increased $52 million or 4 percent during the six-month period ended June 30, 2008 compared to the same period in 2007. Revenues from AGF's finance receivables benefited from the $1.5 billion finance receivable purchase in first quarter 2008, but were partially offset by reduced residential mortgage originations reflecting the slower U.S. housing market. Revenues from AGF's mortgage banking activities increased $165 million during the six-month period ended June 30, 2008 compared to the same period in 2007 (which included a charge of $178 million related to the Supervisory Agreement in the six-month period ended June 30, 2007). Prior year charges of $43 million were reversed in the six months ended June 30, 2008, related to the Supervisory Agreement. The six-month period ended June 30, 2007 included a recovery of $65 million from a favorable out of court settlement.

AGF's operating income declined in the six-month period ended June 30, 2008 compared to the same period in 2007 primarily due to increases in the provision for finance receivable loss of $273 million and unfavorable variances related to derivatives that economically hedge AGF debt. During the six-month period ended June 30, 2008, AGF recorded a net loss of $38 million on its derivatives that did not qualify for hedge accounting under FAS 133, including the related foreign exchange losses, compared to a net loss of $19 million in the same period in 2007. The net derivative loss for the six-month period ended June 30, 2008 includes the effect of changes in AIG's credit spreads amounting to $34 million, of which $13 million represents the transition amount from the adoption of FAS 157. AGF's operating income also reflected a pre-tax charge of $27 million resulting from AGF's decision to cease its wholesale originations.

Revenues from the foreign consumer finance operations increased by 45 percent in the six-month period ended June 30, 2008 compared to the same period in 2007. Loan growth, particularly in Poland, Mexico and Latin America, was the primary driver of the increased revenues. In addition, revenues from recently acquired businesses in India and Thailand contributed to the increase. The increase in revenues was more than offset by higher expenses associated with branch expansions, acquisition activities and product promotion campaigns.

Credit Quality of Finance Receivables

The overall credit quality of AGF's finance receivables portfolio deteriorated during the six-month period ended June 30, 2008 due to negative economic fundamentals, the aging of the real estate loan portfolio and a higher proportion of non-real estate loans and retail sales finance receivables.

At June 30, 2008, the 60-day delinquency rate for the entire portfolio increased by 138 basis points to 3.56 percent compared to the same period in 2007, while the 60-day delinquency rate for the real estate loans increased by 155 basis points to 3.50 percent. For the three-month period ended June 30, 2008, AGF's net charge-off rate increased to 1.73 percent compared to 1.02 percent for the same period in 2007 and for the six-month period ended June 30, 2008 increased to 1.64 percent compared to 1.00 percent for the same period in 2007.

AGF's allowance for finance receivable losses as a percentage of outstanding receivables was 3.02 percent at June 30, 2008 compared to 2.04 percent at June 30, 2007.

Asset Management Operations

AIG's Asset Management operations comprise a wide variety of investment-related services and investment products. These services and products are offered to individuals, pension funds and institutions (including AIG subsidiaries)

globally through AIG's Spread-Based Investment business, Institutional Asset Management, and Brokerage Services and Mutual Funds business. Also included in Asset Management operations are the results of certain SunAmerica sponsored partnership investments.

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

Spread-Based Investment Business

AIG's Spread-Based Investment business includes the results of AIG's proprietary Spread-Based Investment operations, the Matched Investment Program (MIP), which was launched in September of 2005 to replace the Guaranteed Investment Contract (GIC) program, which is in runoff whereby no new GIC contracts are being written. The MIP is an investment strategy that involves investing in various asset classes with financing provided through third parties. This business uses various risk mitigating strategies designed to hedge interest rate and currency risk associated with underlying investments and related liabilities.

Institutional Asset Management

AIG's Institutional Asset Management business, conducted through AIG Investments, provides an array of investment products and services globally to institutional investors, pension funds, AIG subsidiaries and high net worth investors. These products include traditional equity and fixed maturity securities, and a wide range of alternative asset classes. These services include investment advisory and subadvisory services, investment monitoring, securities lending and transaction structuring. Within the fixed maturity and equity asset classes, AIG Investments offers various forms of structured investments aimed at achieving superior returns or capital preservation. Within the alternative asset class, AIG Investments offers hedge and private equity funds and fund-of-funds, direct investments and distressed debt investments.

AIG Global Real Estate provides a wide range of real estate investment and management services for AIG subsidiaries, as well as for third-party institutional investors, high net worth investors and pension funds. Through a strategic network of local real estate ventures, AIG Global Real Estate actively invests in and develops office, industrial, multi-family residential, retail, mixed-use hotel and resort properties located around the world.

AIG Private Bank offers banking, trading and investment management services to private clients and institutions globally. To further focus on its wealth management expansion efforts, AIG Private Bank Ltd. entered into a joint venture agreement with Bank Sarasin & Co. Ltd. Under this agreement, a new Swiss bank was established, into which both AIG Private Bank Ltd. and Bank Sarasin & Co. Ltd. contributed their retail banking businesses. The new bank commenced operations on July 1, 2008 with assets under management of approximately $8 billion.

From time to time, AIG Investments acquires warehoused assets. During the warehousing period, AIG bears the cost and risks associated with carrying these investments and consolidates them on its balance sheet and records the operating results until the investments are transferred, sold or otherwise divested. Changes in market conditions may negatively affect the fair value of these warehoused investments. Market conditions may impede AIG from launching new investment products for which these warehoused assets are being held. Market conditions may also prevent AIG from recovering its investment upon transfer or divestment. In the event that AIG is unable to transfer or otherwise divest its interest in the warehoused investment to third parties, AIG could be required to hold these investments indefinitely. In certain instances, the consolidated warehoused investments are not wholly owned by AIG. In such cases, AIG shares the risk associated with warehousing the asset with the minority interest investors.

Brokerage Services and Mutual Funds

AIG's Brokerage Services and Mutual Funds business, conducted through AIG Advisor Group, Inc. and AIG SunAmerica Asset Management Corp., provides broker-dealer related services and mutual funds to retail investors, group trusts and corporate accounts through an independent network of financial advisors. AIG Advisor Group, Inc., a subsidiary of AIG Retirement Services, Inc., is comprised of several broker-dealer entities that provide these services to clients primarily in the U.S. marketplace. AIG SunAmerica Asset Management Corp. manages, advises and/or administers retail mutual funds, as well as the underlying assets of variable annuities sold by AIG SunAmerica and VALIC to individuals and groups throughout the United States.

Other Asset Management

Included in Other Asset Management is income or loss from certain AIG SunAmerica sponsored partnerships and partnership investments. Partnership assets consist of investments in a diversified portfolio of private equity funds, affordable housing partnerships and hedge fund investments.

Asset Management Results

Asset Management results were as follows:

(in millions)	Three Months Ended June 30, 2008	Three Months Ended June 30, 2007	Percentage Increase/ (Decrease)	Six Months Ended June 30, 2008	Six Months Ended June 30, 2007	Percentage Increase/ (Decrease)
Total revenues:						
Spread-Based Investment business	**$ 2**	$ 734	—%	**$ (807)**	$ 1,749	—%
Institutional Asset Management	**687**	869	(21)	**1,211**	1,298	(7)
Brokerage Services and Mutual Funds	**74**	82	(10)	**148**	160	(8)
Other Asset Management	**34**	96	(65)	**96**	243	(60)
Total	**$ 797**	$ 1,781	(55)%	**$ 648**	$ 3,450	(81)%
Operating income (loss):						
Spread-Based Investment business	**$ (420)**	$ 244	—%	**$ (1,671)**	$ 735	—%
Institutional Asset Management	**58**	569	(90)	**(20)**	666	—
Brokerage Services and Mutual Funds	**17**	21	(19)	**36**	47	(23)
Other Asset Management	**31**	93	(67)	**90**	237	(62)
Total	**$ (314)**	$ 927	—%	**$ (1,565)**	$ 1,685	—%

Asset Management recognized operating losses in the three- and six-month periods ended June 30, 2008 compared to operating income in the same periods in 2007, primarily due to other-than-temporary impairment charges on fixed income investments, significantly lower partnership income, and lower carried interest revenues. Included in the second quarter 2007 operating income was a gain on the sale of a portion of AIG's investment in The Blackstone Group L.P. in connection with its initial public offering.

Quarterly Spread-Based Investment Business Results

The Spread-Based Investment business reported an operating loss in the three-month period ended June 30, 2008 compared to operating income in the same period in 2007 due to significantly higher net realized capital losses and lower partnership income. Included in the operating loss were net realized capital losses of $549 million for the three-month period ended June 30, 2008, compared to $67 million in the 2007 period. Net realized capital losses for the three-month period ended June 30, 2008 primarily consist of $880 million in other-than-temporary impairment charges on fixed maturity securities for both the GIC and MIP portfolios, partially offset by net mark to market gains of $255 million on interest rate and foreign exchange hedges not qualifying for hedge accounting treatment for both the GIC and MIP and net foreign exchange gains on foreign currency denominated GIC and MIP liabilities. Net realized capital losses of $67 million for the three-month period ended June 30, 2007 primarily reflect $86 million of net mark to market losses on interest rate and foreign exchange hedges, partially offset by net foreign exchange related gains on the MIP and GIC.

The other-than-temporary impairment charges on fixed maturity securities held in the GIC and MIP portfolios were $522 million for the GIC and $358 million for the MIP for the three-month period ended June 30, 2008. These impairments primarily resulted from severity losses. See Invested Assets — Portfolio Review — Other-Than-Temporary Impairments. In addition to the other-than-temporary impairments, unrealized losses on fixed maturity securities were recorded in accumulated other comprehensive income (loss) and were primarily driven by price declines resulting from decreased market liquidity, partially offset by unrealized gains resulting from falling interest rates.

In the GIC program, income from partnership investments declined $237 million for the three-month period ended June 30, 2008, compared to the same period of 2007, reflecting significantly higher returns in the 2007 period and weaker market conditions in 2008. Partially offsetting this decline were foreign exchange gains on foreign currency denominated GIC reserves, which increased by $76 million in the three-month period ended June 30, 2008 compared to the same period in 2007 as a result of the weakening of the U.S. dollar. As noted below, a significant portion of these GIC reserves mature in 2008.

The MIP experienced net mark to market gains of $253 million in the second quarter of 2008 due primarily to interest rate and foreign exchange derivative positions that, while partially effective in hedging interest rate and foreign exchange risk, did not qualify for hedge accounting treatment and an additional $22 million in mark to market gains due to credit default swap investments. The MIP invests in credit default swaps comprised predominantly of single-name high-grade corporate exposures. The mark to market gains for the three-month period ended June 30, 2008 were driven primarily by an increase in interest rates and the tightening of corporate credit spreads. AIG enters into hedging arrangements to mitigate the effect of changes in currency and interest rates associated with the fixed and floating rate and foreign currency denominated obligations issued under these programs. Some of these hedging relationships qualify for hedge accounting treatment, while others do not. Income or loss from these hedges not qualifying for hedge accounting

treatment are classified as net realized capital gains (losses) in AIG's Consolidated Statement of Income (Loss).

Year-to-Date Spread-Based Investment Business Results

The Spread-Based Investment business reported an operating loss in the six-month period ended June 30, 2008 compared to operating income in the same period in 2007 due to significantly higher net realized capital losses and lower partnership income. Included in the operating loss were net realized capital losses of $1.9 billion for the six-month period ended June 30, 2008, compared to $87 million in the same period in 2007. Net realized capital losses for the six-month period ended June 30, 2008 primarily consist of $1.9 billion in other-than-temporary impairment charges on fixed maturity securities for both the GIC and MIP, $325 million in foreign exchange related losses on foreign denominated GIC reserves and mark to market losses of $109 million on credit default swap investments held by the MIP. Partially offsetting these losses were net mark to market gains of $414 million on interest rate and foreign exchange hedges not qualifying for hedge accounting treatment for both the GIC and MIP. Net realized capital losses of $87 million for the six-month period ended June 30, 2007 primarily reflect $30 million of other-than-temporary impairment charges, $89 million of net foreign exchange related losses on foreign denominated, liabilities in both the GIC and MIP and $29 million in net mark to market losses on interest rate and foreign exchange hedges, partially offset by realized gains of $43 million on the sale of fixed maturity and equity securities in the GIC.

The other-than-temporary impairment charges on fixed maturity securities held in the GIC and MIP portfolios were $1.1 billion for the GIC and $852 million for the MIP for the six-month period ended June 30, 2008, primarily resulting from severity losses. See Invested Assets — Portfolio Review — Other-Than-Temporary Impairments. In addition to the other-than-temporary impairments, unrealized losses on fixed maturity securities were recorded in accumulated other comprehensive income (loss) and were primarily driven by price declines resulting from decreased market liquidity, partially offset by unrealized gains resulting from falling interest rates.

In the GIC program, income from partnership investments was $44 million for the six-month period ended June 30, 2008, a decline of $654 million from the same period of 2007 due to significantly higher returns in the 2007 period and weaker market conditions in 2008. Also contributing to the decline was the one-time distribution from a single partnership of $164 million in the six-month period ended June 30, 2007. Foreign exchange losses on foreign-denominated GIC reserves increased by $221 million in the six-month period ended June 30, 2008 as a result of the weakening of the U.S. dollar. As noted below, a significant portion of these GIC reserves mature in the next twelve months. Partially offsetting the decline in partnership income and increased foreign exchange losses was an increase in net mark to market gains on derivative positions of $464 million. These gains included net mark to market gains on interest rate and foreign exchange derivatives used to economically hedge the effect of interest rate and foreign exchange rate movements on GIC reserves. Although these economic hedges are partially effective in hedging the interest rate and foreign exchange risk, they did not qualify for hedge accounting treatment.

The MIP experienced net mark to market losses of $79 million for the six-month period ended June 30, 2008, due primarily to interest rate and foreign exchange derivative positions that, while partially effective in hedging interest rate and foreign exchange risk, did not qualify for hedge accounting treatment and an additional $109 million in net mark to market losses were recognized due to credit default swap investments. These net mark to market losses were driven primarily by a decline in interest rates, a decline in value of the U.S. dollar and the widening of corporate credit spreads.

AIG did not issue any additional debt to fund the MIP in the six-month period ended June 30, 2008. Through June 30, 2008, the MIP had cumulative debt issuances of $13.4 billion.

The GIC is in runoff with no new GICs issued subsequent to 2006. The anticipated runoff of the domestic GIC portfolio at June 30, 2008 was as follows:

(in billions)	Less Than One Year	1-3 Years	3(+)-5 Years	Over Five Years	Total
Domestic GICs	$11.2	$4.2	$2.0	$5.6	$23.0

It is expected that available cash, cash flows from investments and sales of investments on an opportunistic basis in anticipation of cash needs throughout the year will be sufficient to repay GIC liabilities as they mature.

Quarterly Institutional Asset Management Results

Institutional Asset Management operating income decreased in the three-month period ended June 30, 2008 compared to the same period in 2007. Included in the second quarter of 2007, operating income was a gain of $398 million related to the sale of a portion of AIG's investment in The Blackstone Group L.P. (Blackstone) in connection with its initial public offering. The decline also reflects lower partnership income in the second quarter of 2008, along with lower carried interest revenues and lower real estate related gains. AIG recognizes carried interest revenues on an unrealized basis by reflecting the amount owed to AIG as of the balance sheet date based on the related funds' performance. The reduction in carried interest revenues was driven by lower unrealized carry due to significantly higher fund performance in the three-month period ended June 30, 2007. The decline in real estate related gains was a function of market conditions and the timing of

proprietary real estate investment sales. Offsetting these decreases were higher base management fees, driven by a net increase of approximately $4.3 billion in unaffiliated client assets under management.

Total operating income (loss) from various consolidated warehoused investments for the three-month periods ended June 30, 2008 and 2007 was $14 million and $(27) million, respectively. A portion of these amounts is offset in minority interest expense, which is not a component of operating income (loss).

Year-to-Date Institutional Asset Management Results

Institutional Asset Management recognized an operating loss in the six-month period ended June 30, 2008 compared to operating income in the same period in 2007 reflecting lower carried interest revenues and lower partnership income in the 2008 period, along with the effect from the sale in 2007 of a portion of AIG's investment in Blackstone. Also contributing to the decline in operating income were lower real estate related gains and increased depreciation and amortization expense due to additional real estate investments acquired in late 2007. The reduction in carried interest revenues was driven by lower unrealized carry due to significantly higher fund performance in the six-month period ended June 20, 2007. Slightly offsetting these decreases were higher base management fees driven by a net increase of approximately $2.6 billion in unaffiliated client assets under management.

Total operating losses from various consolidated warehoused investments for the six-month periods ended June 30, 2008 and 2007 were $77 million and $39 million, respectively. A portion of these amounts is offset in minority interest expense, which is not a component of operating income (loss).

AIG's unaffiliated client assets under management, including retail mutual funds and institutional accounts, were $96.4 billion at June 30, 2008, a decline of 5 percent compared to December 31, 2007 and an increase of 5 percent compared to $92.1 billion at June 30, 2007. The decline from December 31, 2007 primarily reflected market valuation declines in the equity and fixed income markets. The increase from June 30, 2007 was driven by new business.

Brokerage Services and Mutual Funds

Revenues and operating income related to Brokerage Services and Mutual Fund activities decreased due to lower fee income as a result of a lower asset base.

Other Asset Management Results

Revenues and operating income related to the Other Asset Management activities decreased in the three- and six-month periods ended June 30, 2008 compared to the same periods in 2007 due to lower income from partnership investments. Similar to the investments held in the Spread-Based Investment business, these investments experienced significantly higher returns in the three- and six-month periods ended June 30, 2007 and weaker market conditions in 2008.

Other Operations

The operating loss of AIG's Other category was as follows:

	Three Months Ended June 30,		Six Months Ended June 30,	
(in millions)	**2008**	2007	**2008**	2007
Operating income (loss):				
Equity earnings in partially owned companies	**$ 8**	$ 50	**$ 16**	$ 91
Interest expense	**(452)**	(302)	**(820)**	(554)
Unallocated corporate expenses*	**(282)**	(210)	**(375)**	(382)
Net realized capital gains (losses)	**30**	22	**(235)**	(27)
Other miscellaneous, net	**(19)**	(20)	**(69)**	(58)
Total Other	**$(715)**	$(460)	**$ (1,483)**	$(930)

** Includes a charge for settlement of a dispute, expenses of corporate staff not attributable to specific operating segments, expenses related to efforts to improve internal controls, corporate initiatives and certain compensation plan expenses.*

The operating loss of AIG's Other category increased in the three-month period ended June 30, 2008 compared to the same period in 2007 reflecting higher interest expense that resulted from increased borrowings, including interest on the debt and equity units from the dates of issuance in May 2008, higher unallocated corporate expenses primarily from a charge of $101 million as a result of settlement of a dispute in connection with the July 2008 purchase of the balance of Ascot Underwriting Holdings, Ltd., additional charitable contribution commitments and severance compensation for Martin Sullivan, AIG's former Chief Executive Officer, partially offset by reversals of previously accrued costs related to certain long-term performance-based compensation plans, as performance to date is below the performance thresholds set forth in those plans.

The operating loss in the six-month period ended June 30, 2008 increased compared to the same period in 2007 reflecting higher interest expense that resulted from increased borrowings, including interest on the debt and equity units from the dates of issuance in May 2008, and higher net realized capital losses and lower equity earnings in partially owned companies. The increase in net realized capital losses in the six-month period ended June 30, 2008 reflected higher foreign exchange losses on foreign-denominated debt, a portion of which was economically hedged but did not qualify for hedge accounting treatment under FAS 133, and losses on non-hedged derivatives. Other miscellaneous, net included a $45 million write-off of goodwill related to Mortgage Guaranty in the six-month period ended June 30, 2008.

Capital Resources and Liquidity

At June 30, 2008, AIG had total consolidated shareholders' equity of $78.1 billion and total consolidated borrowings of $178.6 billion. At that date, $68.6 billion of such borrowings were subsidiary borrowings not guaranteed by AIG.

In May 2008, AIG raised a total of approximately $20 billion through the sale of:

- 196,710,525 shares of AIG common stock in a public offering at a price per share of $38, for an aggregate amount of $7.47 billion;
- 78.4 million equity units in a public offering at a price per unit of $75, for an aggregate amount of $5.88 billion. The equity units consist of an ownership interest in AIG junior subordinated debentures and a stock purchase contract obligating the holder of an equity unit to purchase, and obligating AIG to sell, a variable number of shares of AIG common stock on three dates in 2011 (a minimum of 128,944,480 shares and a maximum of 154,738,080 shares, subject to anti-dilution adjustments); and
- $6.9 billion in unregistered offerings of junior subordinated debentures in three series: $4.0 billion 8.175 percent Series A-6 junior subordinated debentures, EUR 750 million 8.0 percent Series A-7 junior subordinated debentures, and GBP 900 million 8.625 percent Series A-8 junior subordinated debentures.

The equity units and junior subordinated debentures receive hybrid equity treatment from the major rating agencies under their current policies but are recorded as long-term borrowings on the consolidated balance sheet.

Borrowings

AIG's total borrowings were as follows:

(in millions)	**June 30, 2008**	December 31, 2007
Borrowings issued by AIG:		
Notes and bonds payable	**$ 12,960**	$ 14,588
Junior subordinated debt	**12,866**	5,809
Junior subordinated debt attributable to equity units	**5,880**	—
Loans and mortgages payable	**893**	729
MIP matched notes and bonds payable	**14,621**	14,267
Series AIGFP matched notes and bonds payable	**998**	874
Total AIG borrowings	**48,218**	36,267
Borrowings guaranteed by AIG:		
AIGFP[(a)]		
GIAs	**18,296**	19,908
Notes and bonds payable	**28,304**	36,676
Loans and mortgages payable	**1,577**	1,384
Hybrid financial instrument liabilities[(b)]	**5,662**	7,479
Total AIGFP borrowings	**53,839**	65,447
AIG Funding, Inc. commercial paper	**5,765**	4,222
AIGLH notes and bonds payable	**797**	797
Liabilities connected to trust preferred stock	**1,415**	1,435
Total borrowings issued or guaranteed by AIG	**110,034**	108,168
Borrowings not guaranteed by AIG:		
ILFC		
Commercial paper	**4,608**	4,483
Junior subordinated debt	**999**	999
Notes and bonds payable[(c)]	**26,818**	25,737
Total ILFC borrowings	**32,425**	31,219
AGF		
Commercial paper and extendible commercial notes	**3,912**	3,801
Junior subordinated debt	**349**	349
Notes and bonds payable	**21,204**	22,369
Total AGF borrowings	**25,465**	26,519
AIGCFG		
Commercial paper	**273**	287
Loans and mortgages payable	**2,257**	1,839
Total AIGCFG borrowings	**2,530**	2,126
AIG Finance Taiwan Limited commercial paper	**3**	—
Other subsidiaries	**709**	775
Borrowings of consolidated investments:		
A.I. Credit[(d)]	**500**	321
AIG Investments	**1,502**	1,636
AIG Global Real Estate Investment	**5,294**	5,096
AIG SunAmerica	**176**	186
ALICO	**—**	3
Total borrowings of consolidated investments	**7,472**	7,242
Total borrowings not guaranteed by AIG	**68,604**	67,881
Consolidated:		
Total commercial paper and extendible commercial notes	**15,061**	13,114
Total long-term borrowings	**163,577**	162,935
Total borrowings	**$178,638**	$176,049

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

(b) Represents structured notes issued by AIGFP that are accounted for using the fair value option at 2008 and 2007.

(c) Includes borrowings under Export Credit Facility of $2.6 billion and $2.5 billion at June 30, 2008 and December 31, 2007, respectively.

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

The roll forward of long-term borrowings, excluding borrowings of consolidated investments, for the six months ended June 30, 2008 was as follows:

(in millions)

	Balance at December 31, 2007	Issuances	Maturities and Repayments	Effect of Foreign Exchange	Other Changes[b]	**Balance at June 30, 2008**
AIG						
Notes and bonds payable	$ 14,588	$ —	$ (1,792)	$ 70	$ 94	**$ 12,960**
Junior subordinated debt	5,809	6,953	—	104	—	**12,866**
Junior subordinated debt attributable to equity units	—	5,880	—	—	—	**5,880**
Loans and mortgages payable	729	306	(140)	14	(16)	**893**
MIP matched notes and bonds payable	14,267	—	—	20	334	**14,621**
Series AIGFP matched notes and bonds payable	874	214	(95)	—	5	**998**
AIGFP[a]						
GIAs	19,908	2,944	(5,039)	—	483	**18,296**
Notes and bonds payable and hybrid financial instrument liabilities	44,155	33,553	(44,951)	—	1,209	**33,966**
Loans and mortgages payable	1,384	235	(165)	—	123	**1,577**
AIGLH notes and bonds payable	797	—	—	—	—	**797**
Liabilities connected to trust preferred stock	1,435	—	(19)	—	(1)	**1,415**
ILFC notes and bonds payable	25,737	2,680	(1,884)	286	(1)	**26,818**
ILFC junior subordinated debt	999	—	—	—	—	**999**
AGF notes and bonds payable	22,369	736	(2,098)	147	50	**21,204**
AGF junior subordinated debt	349	—	—	—	—	**349**
AIGCFG loans and mortgages payable	1,839	1,234	(1,089)	123	150	**2,257**
Other subsidiaries	775	23	(102)	10	3	**709**
Total	$156,014	$54,758	$(57,374)	$ 774	$ 2,433	**$156,605**

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

(b) Includes the cumulative effect of the adoption of FAS 159.

AIG (Parent Company)

AIG intends to continue its customary practice of issuing debt securities from time to time to meet its financing needs and those of certain of its subsidiaries for general corporate purposes, as well as to opportunistically fund the MIP. As of June 30, 2008, approximately $7.4 billion principal amount of senior notes were outstanding under AIG's medium-term note program, of which $3.2 billion was used for AIG's general corporate purposes, $1.0 billion was used by AIGFP (referred to as "Series AIGFP" in the preceding tables) and $3.2 billion was used to fund the MIP. The maturity dates of these notes range from 2008 to 2052. To the extent considered appropriate, AIG may enter into swap transactions to manage its effective borrowing rates with respect to these notes.

AIG also maintains a Euro medium-term note program under which an aggregate nominal amount of up to $20.0 billion of senior notes may be outstanding at any one time. As of June 30, 2008, the equivalent of $13.1 billion of notes were outstanding under the program, of which $10.0 billion were used to fund the MIP and the remainder was used for AIG's general corporate purposes. The aggregate amount outstanding includes a $1.7 billion loss resulting from foreign exchange translation into U.S. dollars, of which $451 million loss relates to notes issued by AIG for general corporate purposes and $1.2 billion loss relates to notes issued to fund the MIP. AIG has economically hedged the currency exposure arising from its foreign currency denominated notes.

AIG maintains a shelf registration statement in Japan, providing for the issuance of up to Japanese yen 300 billion principal amount of senior notes, of which the equivalent of $470 million was outstanding as of June 30, 2008 and was used for AIG's general corporate purposes. AIG also maintains an Australian dollar debt program under which senior notes with an aggregate principal amount of up to 5 billion Australian dollars may be outstanding at any one time. Although as of June 30, 2008 there were no outstanding notes under the Australian program, AIG intends to use the program opportunistically to fund the MIP or for AIG's general corporate purposes.

In May 2008, AIG issued $5.88 billion of junior subordinated debentures which form part of the equity units sold by AIG in a public offering. In addition, AIG sold a total of $6.9 billion of junior subordinated debentures in Rule 144A/Regulation S offerings in three series: $4.0 billion 8.175 percent Series A-6 junior subordinated debentures; EUR 750 million 8.0 percent Series A-7 junior subordinated debentures; and GBP 900 million 8.625 percent Series A-8 junior subordinated debentures. AIG may redeem the A-6 debentures without penalty on or after May 15, 2038 and may redeem the A-7 and A-8 debentures on or after May 22,

2018 without penalty. After these dates, the debentures will bear interest at floating rates. AIG agreed pursuant to a replacement capital covenant that it will not repay, redeem, or purchase the Series A-6, A-7 or A-8 junior subordinated debentures on or before a specified date, unless AIG has received qualifying proceeds from the sale of replacement capital securities. The equity units and the Series A-6, A-7 and A-8 junior subordinated debentures receive hybrid equity treatment from the major rating agencies under their current policies but are recorded as long-term borrowings on the consolidated balance sheet.

In October 2007, AIG borrowed a total of $500 million on an unsecured basis pursuant to a loan agreement with a third-party bank. The entire amount of the loan remained outstanding at June 30, 2008 and will mature in October 2008.

AIGFP

AIGFP uses the proceeds from the issuance of notes and bonds and GIA borrowings, as well as the issuance of Series AIGFP notes by AIG, to invest in a diversified portfolio of securities and derivative transactions. The borrowings may also be temporarily invested in securities purchased under agreements to resell. AIGFP's notes and bonds include structured debt instruments whose payment terms are linked to one or more financial or other indices (such as an equity index or commodity index or another measure that is not considered to be clearly and closely related to the debt instrument). These notes contain embedded derivatives that otherwise would be required to be accounted for separately under FAS 133. Upon AIG's adoption of FAS 155 in 2006, AIGFP elected the fair value option for these notes. The notes that are accounted for using the fair value option are reported separately under hybrid financial instrument liabilities. AIG guarantees the obligations of AIGFP under AIGFP's notes and bonds and GIA borrowings. See Liquidity herein.

AIGFP has a Euro medium-term note program under which an aggregate nominal amount of up to $20.0 billion of notes may be outstanding at any one time. As of June 30, 2008, $4.3 billion of notes were outstanding under the program. The notes issued under this program are guaranteed by AIG and are included in AIGFP's notes and bonds payable in the table of total borrowings.

AIG Funding

AIG Funding, Inc. (AIG Funding) issues commercial paper that is guaranteed by AIG to help fulfill the short-term cash requirements of AIG and its subsidiaries. The level of issuances of AIG Funding's commercial paper, including the guarantee by AIG, is subject to the approval of AIG's Board of Directors or the Finance Committee of the Board if it exceeds certain pre-approved limits.

As backup for the commercial paper program and for other general corporate purposes, AIG and AIG Funding maintain revolving credit facilities, which, as of June 30, 2008, had an aggregate of $9.2 billion available to be drawn and which are summarized below under Revolving Credit Facilities. In July 2008, AIG and AIG Funding renewed their 364-day syndicated revolving credit facility.

ILFC

ILFC fulfills its short-term cash requirements through operating cash flows and the issuance of commercial paper. The issuance of commercial paper is subject to the approval of ILFC's Board of Directors and is not guaranteed by AIG. ILFC maintains syndicated revolving credit facilities which, as of June 30, 2008, totaled $6.5 billion and which are summarized below under Revolving Credit Facilities. These facilities are used as back up for ILFC's maturing debt and other obligations.

As a well-known seasoned issuer, ILFC has filed an automatic shelf registration statement with the SEC allowing ILFC immediate access to the U.S. public debt markets. At June 30, 2008, $6.8 billion of debt securities had been issued under this registration statement and $6.1 billion had been issued under a prior registration statement. In addition, ILFC has a Euro medium-term note program for $7.0 billion, under which $3.8 billion in notes were outstanding at June 30, 2008. Notes issued under the Euro medium-term note program are included in ILFC notes and bonds payable in the preceding table of borrowings. The cumulative foreign exchange adjustment loss for the foreign currency denominated debt was $1.3 billion at June 30, 2008 and $969 million at December 31, 2007. ILFC has substantially eliminated the currency exposure arising from foreign currency denominated notes by economically hedging the note exposure.

ILFC had a $4.3 billion Export Credit Facility for use in connection with the purchase of approximately 75 aircraft delivered through 2001. This facility was guaranteed by various European Export Credit Agencies. The interest rate varies from 5.75 percent to 5.90 percent on these amortizing ten-year borrowings depending on the delivery date of the aircraft. At June 30, 2008, ILFC had $504 million outstanding under this facility. The debt is collateralized by a pledge of the shares of a subsidiary of ILFC, which holds title to the aircraft financed under the facility.

In May 2004, ILFC entered into a similarly structured Export Credit Facility for up to a maximum of $2.6 billion for Airbus aircraft to be delivered through May 31, 2005. The facility was subsequently increased to $3.6 billion and extended to include aircraft to be delivered through May 31, 2009. The facility becomes available as the various European Export Credit Agencies provide their guarantees for aircraft based on a six-month forward-looking calendar, and the interest rate is determined through a bid process. The interest rates are either LIBOR based with spreads ranging from

0.01 percent to 0.28 percent or at fixed rates ranging from 4.2 percent to 4.7 percent. At June 30, 2008, ILFC had $2.1 billion outstanding under this facility. The debt is collateralized by a pledge of shares of a subsidiary of ILFC, which holds title to the aircraft financed under the facility. Borrowings with respect to these facilities are included in ILFC's notes and bonds payable in the preceding table of borrowings.

From time to time, ILFC enters into funded financing agreements. As of June 30, 2008, ILFC had a total of $1.1 billion outstanding, which has varying maturities through February 2012. The interest rates are LIBOR-based, with spreads ranging from 0.30 percent to 1.625 percent.

The proceeds of ILFC's debt financing are primarily used to purchase flight equipment, including progress payments during the construction phase. The primary sources for the repayment of this debt and the interest expense thereon are the cash flow from operations, proceeds from the sale of flight equipment and the rollover and refinancing of the prior debt. AIG does not guarantee the debt obligations of ILFC. See also Liquidity herein.

AGF

AGF fulfills most of its short-term cash borrowing requirements through the issuance of commercial paper. The issuance of commercial paper is subject to the approval of AGF's Board of Directors and is not guaranteed by AIG. AGF maintains committed syndicated revolving credit facilities which, as of June 30, 2008, totaled $4.8 billion and which are summarized below under Revolving Credit Facilities. The facilities can be used for general corporate purposes and to provide backup for AGF's commercial paper programs. In July 2008, AGF renewed its expiring $2.625 billion 364-day revolving credit facility and decreased the amount to $2.45 billion.

As of June 30, 2008, notes and bonds aggregating $21.2 billion were outstanding with maturity dates ranging from 2008 to 2031 at interest rates ranging from 2.13 percent to 8.45 percent. To the extent considered appropriate, AGF may enter into swap transactions to manage its effective borrowing rates with respect to these notes and bonds. As a well-known seasoned issuer, AGF has an automatic shelf registration statement on file with the SEC that permits AGF immediate access to the U.S. public debt markets.

AGF's funding sources include an SEC-registered medium-term note program, private placement debt, retail note issuances, bank financing and securitizations of finance receivables that AGF accounts for as on-balance-sheet secured financings. In addition, AGF has become a recognized issuer of long-term debt in the international capital markets and has established a $5.0 billion Euro medium-term note program. There are currently no outstanding notes under AGF's Euro program.

In addition to debt refinancing activities, proceeds from the collection of finance receivables are used to fund cash needs including the payment of principal and interest on AGF's debt. AIG does not guarantee any of the debt obligations of AGF. See also Liquidity herein.

AIGCFG

AIGCFG has a variety of funding mechanisms for its various markets, including retail and wholesale deposits, short- and long-term bank loans, securitizations and intercompany subordinated debt. AIG Credit Card Company (Taiwan), a consumer finance business in Taiwan, and AIG Retail Bank PLC, a full service consumer bank in Thailand, have issued commercial paper for the funding of their respective operations. AIG does not guarantee any borrowings for AIGCFG businesses, including this commercial paper.

Revolving Credit Facilities

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

As of June 30, 2008 (in millions)

Facility	Size	Borrower(s)	Available Amount	Expiration	One-Year Term-Out Option
AIG:					
364-Day Syndicated Facility	$ 2,125	AIG/AIG Funding[(a)] AIG Capital Corporation[(a)]	$2,125	July 2008[(b)]	Yes
5-Year Syndicated Facility	1,625	AIG/AIG Funding[(a)] AIG Capital Corporation[(a)]	1,625	July 2011	No
364-Day Bilateral Facility[(c)]	3,200	AIG/AIG Funding	102	December 2008	Yes
364-Day Intercompany Facility[(d)]	5,335	AIG	5,335	September 2008	Yes
Total AIG	$12,285		$9,187		
ILFC:					
5-Year Syndicated Facility	$ 2,500	ILFC	$2,500	October 2011	No
5-Year Syndicated Facility	2,000	ILFC	2,000	October 2010	No
5-Year Syndicated Facility	2,000	ILFC	2,000	October 2009	No
Total ILFC	$ 6,500		$6,500		
AGF:					
364-Day Syndicated Facility	$ 2,625	American General Finance Corporation American General Finance, Inc.[(e)]	$2,625	July 2008[(f)]	Yes
5-Year Syndicated Facility	2,125	American General Finance Corporation	2,125	July 2010	No
Total AGF	$ 4,750		$4,750		

(a) Guaranteed by AIG.
(b) In July 2008, this facility was resyndicated at the same aggregate amount and the expiration was extended to July 2009.
(c) This facility can be drawn in the form of loans or letters of credit. All drawn amounts shown above are in the form of letters of credit.
(d) Subsidiaries of AIG are the lenders on this facility.
(e) American General Finance, Inc. is an eligible borrower for up to $400 million only.
(f) In July 2008, this facility was resyndicated at an aggregate amount of $2.45 billion and the expiration was extended to July 2009.

Credit Ratings

The cost and availability of unsecured financing for AIG and its subsidiaries are generally dependent on their short- and long-term debt ratings. The following table presents the credit ratings of AIG and certain of its subsidiaries as of July 31, 2008. In parentheses, following the initial occurrence in the table of each rating, is an indication of that rating's relative rank within the agency's rating categories. That ranking refers only to the generic or major rating category and not to the modifiers appended to the rating by the rating agencies to denote relative position within such generic or major category.

	Short-term Debt			Senior Long-term Debt		
	Moody's	S&P	Fitch	Moody's[(a)]	S&P[(b)]	Fitch[(c)]
AIG	P-1 (1st of 3)	A-1+ (1st of 6)	F1+ (1st of 5)	Aa3 (2nd of 9)[(e)]	AA- (2nd of 8)[(f)]	AA- (2nd of 9)[(g)]
AIG Financial Products Corp.[(d)]	P-1	A-1+	–	Aa3[(e)]	AA-[(f)]	–
AIG Funding, Inc.[(d)]	P-1	A-1+	F1+	–	–	–
ILFC	P-1	A-1 (1st of 6)	F1 (1st of 5)	A1 (3rd of 9)[(e)]	A+ (3rd of 8)[(f)]	A (3rd of 9)
American General Finance Corporation	P-1	A-1	F1	A1[(e)]	A+[(f)]	A
American General Finance, Inc.	P-1	A-1	F1	–	–	A

(a) Moody's appends numerical modifiers 1, 2 and 3 to the generic rating categories to show relative position within rating categories.
(b) S&P ratings may be modified by the addition of a plus or minus sign to show relative standing within the major rating categories.
(c) Fitch Ratings (Fitch) ratings may be modified by the addition of a plus or minus sign to show relative standing within the major rating categories.
(d) AIG guarantees all obligations of AIG Financial Products Corp. and AIG Funding, Inc.
(e) Negative outlook. A negative outlook by Moody's indicates that a rating may be lowered but is not necessarily a precursor of a ratings change.
(f) Negative outlook on Counterparty Credit Ratings or Corporate Credit Ratings. A negative outlook by S&P indicates that a rating may be lowered but is not necessarily a precursor of a ratings change.
(g) Negative outlook on Issuer Default and Senior Unsecured Debt Ratings. A negative outlook by Fitch indicates that a rating may be lowered but is not necessarily a precursor of a ratings change.

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

"Ratings triggers" have been defined by one independent rating agency to include clauses or agreements the outcome of which depends upon the level of ratings maintained by one or

more rating agencies. "Ratings triggers" generally relate to events that (i) could result in the termination or limitation of credit availability, or require accelerated repayment, (ii) could result in the termination of business contracts or (iii) could require a company to post collateral for the benefit of counterparties.

A significant portion of AIGFP's GIAs and financial derivative transactions include provisions that require AIGFP, upon a downgrade of AIG's long-term debt ratings, to post collateral or, with the consent of the counterparties, assign or repay its positions or arrange a substitute guarantee of its obligations by an obligor with higher debt ratings.

It is estimated that, as of the close of business on July 31, 2008, based on AIGFP's outstanding municipal GIAs and financial derivative transactions at that date, a downgrade of AIG's long-term senior debt ratings to 'A1' by Moody's and 'A+' by S&P would permit counterparties to make additional calls for up to approximately $13.3 billion of collateral, while a downgrade to 'A2' by Moody's and 'A' by S&P would permit counterparties to call for approximately $1.2 billion of additional collateral. If either of Moody's or S&P downgraded AIG's ratings to 'A1' or 'A+', respectively, the estimated collateral call would be for up to approximately $10.5 billion, while a downgrade to 'A2' or 'A', respectively, by either of the two rating agencies would permit counterparties to call for up to approximately $1.1 billion of additional collateral.

Furthermore, a downgrade of AIG's long-term senior debt ratings to 'A1' by Moody's or to the same levels by both rating agencies would permit either AIG or the counterparties to elect early termination of contracts resulting in payments of up to approximately $4.6 billion, while a downgrade to 'A2' by Moody's and 'A' by S&P would permit either AIG or the counterparties to elect early termination of additional contracts resulting in additional payments of up to approximately $800 million. AIGFP believes that it is unlikely that certain of these counterparties would exercise their rights to elect termination of their contracts given the substantial economic benefit that such counterparties would forfeit upon termination.

The actual amount of collateral that AIGFP would be required to post to counterparties in the event of such downgrades, or the aggregate amount of payments that AIG could be required to make, depends on market conditions, the fair value of outstanding affected transactions and other factors prevailing at the time of the downgrade. Additional obligations to post collateral or the costs of assignment, repayment or alternative credit support would increase the demands on AIG's liquidity. Further downgrades could result in requirements for substantial additional collateral, which could have a material adverse effect on AIG's liquidity.

Contractual Obligations

Contractual obligations in total, and by remaining maturity at June 30, 2008 were as follows:

		Payments due by Period			
(in millions)	Total Payments	Less Than One Year	1-3 Years	3+-5 Years	Over Five Years
Borrowings[(a)]	$ 156,605	$ 34,019	$ 33,408	$25,983	$ 63,195
Interest payments on borrowings	78,502	5,930	11,136	9,477	51,959
Loss reserves[(b)]	88,747	24,405	27,068	12,869	24,405
Insurance and investment contract liabilities[(c)]	706,108	31,947	43,609	41,707	588,845
GIC liabilities[(d)]	25,458	11,011	4,766	2,421	7,260
Aircraft purchase commitments	17,566	1,018	3,206	3,295	10,047
Other long-term obligations	609	221	361	27	—
Total[(e)(f)]	$1,073,595	$108,551	$123,554	$95,779	$745,711

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

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

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

(d) Represents guaranteed maturities under GICs.

(e) Does not reflect unrecognized tax benefits of $2.5 billion, the timing of which is uncertain.

(f) The majority of AIGFP's credit default swaps require AIGFP to provide credit protection on a designated portfolio of loans or debt securities. At June 30, 2008, AIG had recorded $26.1 billion of cumulative unrealized market valuation losses in its financial statements relating to AIGFP's super senior credit default swap portfolio, net of amounts realized in extinguishing derivative obligations. However, AIG's credit-based stress testing scenarios illustrate potential pre-tax realized credit losses from these contracts at approximately $5.0 billion and approximately $8.5 billion at that date. Due to the long-term maturities of these credit default swaps, AIG is unable to make reasonable estimates of the periods during which any payments would be made.

Off Balance Sheet Arrangements and Commercial Commitments

Off balance sheet arrangements and commercial commitments in total, and by remaining maturity at June 30, 2008 were as follows:

		Amount of Commitment Expiration			
(in millions)	Total Amounts Committed	Less Than One Year	1-3 Years	3+-5 Years	Over Five Years
Guarantees:					
Liquidity facilities[(a)]	$ 2,552	$ 72	$ 884	$ 1,325	$ 271
Standby letters of credit	1,702	1,481	45	32	144
Construction guarantees[(b)]	490	—	—	—	490
Guarantees of indebtedness	1,284	147	144	500	493
All other guarantees	1,104	159	165	27	753
Commitments:					
Investment commitments[(c)]	8,711	3,304	3,619	1,605	183
Commitments to extend credit	1,828	1,352	366	110	—
Letters of credit	1,115	835	120	—	160
Maturity shortening puts[(d)]	7,995	2,071	2,595	1,648	1,681
Other commercial commitments[(e)]	1,193	83	23	79	1,008
Total[(f)]	$ 27,974	$ 9,504	$ 7,961	$ 5,326	$ 5,183

(a) Primarily liquidity facilities provided in connection with certain municipal swap transactions and collateralized bond obligations.
(b) Primarily AIG SunAmerica construction guarantees connected to affordable housing investments.
(c) Includes commitments to invest in limited partnerships, private equity, hedge funds and mutual funds and commitments to purchase and develop real estate in the United States and abroad.
(d) Represents obligations under 2a-7 Puts to purchase certain multi-sector CDOs at pre-determined contractual prices.
(e) Includes options to acquire aircraft. Excludes commitments with respect to pension plans. The annual pension contribution for 2008 is expected to be approximately $118 million for U.S. and non-U.S. plans.

Arrangements with Variable Interest Entities and Structured Investment Vehicles

AIG enters into various off-balance-sheet (unconsolidated) arrangements with variable interest entities (VIEs) in the normal course of business. AIG's involvement with VIEs ranges from being a passive investor to designing and structuring, warehousing and managing the collateral of VIEs. AIG engages in transactions with VIEs as part of its investment activities to obtain funding and to facilitate client needs. AIG purchases debt securities (rated and unrated) and equity interests issued by VIEs, makes loans and provides other credit support to VIEs, enters into insurance, reinsurance and derivative transactions and leasing arrangements with VIEs, and acts as the warehouse agent and collateral manager for VIEs. Interest holders in the VIEs generally have recourse only to the assets and cash flows of the VIEs and do not have recourse to AIG, except when AIG has provided a guarantee to the VIE's interest holders.

Under FIN 46(R), AIG consolidates a VIE when it is the primary beneficiary of the entity. The primary beneficiary is the party that either (i) absorbs a majority of the VIE's expected losses; (ii) receives a majority of the VIE's expected residual returns; or (iii) both. For a further discussion of AIG's involvement with VIEs, see Note 7 of Notes to Consolidated Financial Statements in the 2007 Annual Report on Form 10-K.

A significant portion of AIG's overall exposure to VIEs results from AIG Investment's real estate and investment funds.

In certain instances, AIG Investments acts as the collateral manager or general partner of an investment fund, private equity fund or hedge fund. Such entities are typically registered investment companies or qualify for the specialized investment company accounting in accordance with the AICPA Investment Company Audit and Accounting Guide. For investment partnerships, hedge funds and private equity funds, AIG acts as the general partner or manager of the fund and is responsible for carrying out the investment mandate of the VIE. Often, AIG's insurance operations participate in these AIG managed structures as a passive investor in the

debt or equity issued by the VIE. Typically, AIG does not provide any guarantees to the investors in the VIE.

During 2008, AIG reduced its maximum exposure to loss from its involvement with unconsolidated VIEs by approximately $6.6 billion, primarily as a result of the termination of certain of AIGFP's transactions. Substantially all of AIG's exposure to these unconsolidated VIEs is represented by its equity investment in them, and such investment is reflected on the consolidated balance sheet.

Shareholders' Equity

The changes in AIG's consolidated shareholders' equity were as follows:

(in millions)	Six Months Ended June 30, 2008
Beginning of year	**$95,801**
Net income (loss)	**(13,162)**
Unrealized (depreciation) appreciation of investments, net of tax	**(9,441)**
Cumulative translation adjustment, net of tax	**984**
Dividends to shareholders	**(1,121)**
Payments advanced to purchase shares, net	**912**
New share issuance	**7,343**
Share purchases	**(1,912)**
Cumulative effect of accounting changes, net of tax	**(1,108)**
Other*	**(208)**
End of period	**$78,088**

** Reflects the effects of employee stock transactions and the present value of future contract adjustment payments related to the issuance of equity units.*

New Share Issuance

In May 2008, AIG sold in a public offering 196,710,525 shares of its common stock at a price per share of $38. Concurrent with the common stock offering, AIG sold 78.4 million equity units at a price per unit of $75. The equity units consist of an ownership interest in AIG junior subordinated debentures and a stock purchase contract obligating the holder of an equity unit to purchase, and obligating AIG to sell, on each of February 15, 2011, May 1, 2011 and August 1, 2011, for a price of $25, a variable number of shares of AIG common stock, that is not less than 0.54823 shares and not more than 0.6579 shares, subject to anti-dilution adjustments. Accordingly, a maximum number of 154,738,080 shares and a minimum number of 128,944,480 shares of AIG common stock will be issued in the year 2011 under the stock purchase contracts, subject to anti-dilution adjustments.

In February 2007, AIG's Board of Directors adopted a new dividend policy, which took effect with the dividend declared in the second quarter of 2007, providing that under ordinary circumstances, AIG's plan will be to increase its common stock dividend by approximately 20 percent annually. The payment of any dividend, however, is at the discretion of AIG's Board of Directors, and the future payment of dividends will depend on various factors, including the performance of AIG's businesses, AIG's consolidated financial condition, results of operations and liquidity and the existence of investment opportunities. With due consideration of the foregoing policy, in light of then current market conditions, on May 7, 2008, AIG's Board of Directors declared a quarterly cash dividend on the common stock of $0.22 per share, payable on September 19, 2008 to shareholders of record on September 5, 2008, representing a 10 percent increase. No assurance can be given under current market conditions that the Board of Directors will further increase AIG's dividend or maintain the dividend at current levels.

Share Repurchases

From time to time, AIG may buy shares of its common stock for general corporate purposes, including to satisfy its obligations under various employee benefit plans. In February 2007, AIG's Board of Directors increased AIG's share repurchase program by authorizing the purchase of shares with an aggregate purchase price of $8 billion. In November 2007, AIG's Board of Directors authorized the purchase of an additional $8 billion in common stock. In 2007, AIG entered into structured share repurchase arrangements providing for the purchase of shares over time with an aggregate purchase price of $7 billion.

A total of 37,926,059 shares were purchased during the six-month period ended June 30, 2008 to meet commitments that existed at December 31, 2007. All shares purchased are recorded as treasury stock at cost.

At August 5, 2008, $9 billion was available for purchases under the aggregate authorization. AIG does not expect to purchase additional shares under its share repurchase program for the foreseeable future.

Liquidity

AIG manages liquidity at both the subsidiary and parent company levels. At June 30, 2008, AIG's consolidated invested assets included $82.2 billion in cash and short-term investments (including $10.4 billion of securities lending cash and short-term investments). Consolidated net cash provided from operating activities in the six-month period ended June 30, 2008 amounted to $16.6 billion. At both the subsidiary and parent company level, liquidity management activities are intended to preserve and enhance funding stability, flexibility, and diversity through a wide range of potential operating environments and market conditions. AIG's primary sources of cash flow are dividends and other payments from its regulated and unregulated subsidiaries, as well as issuances of debt and equity securities. Primary uses of cash flow are for debt service, subsidiary funding,

shareholder dividend payments and common stock repurchases. Management believes that AIG's liquid assets, cash provided by operations and access to the capital markets will enable it to meet its anticipated cash requirements.

AIG (Parent Company)

The liquidity of the parent company is principally derived from its subsidiaries. The primary sources of cash flow are dividends and other payments from its regulated and unregulated subsidiaries, as well as issuance of debt securities. Primary uses of cash flow are for debt service, subsidiary funding, shareholder dividend payments and common stock repurchases. In the six-month period ended June 30, 2008, AIG parent collected $1.4 billion in dividends and other payments from subsidiaries (primarily from insurance company subsidiaries). Excluding MIP and Series AIGFP debt, AIG parent made interest payments totaling $522 million, made $2.4 billion in net capital contributions to subsidiaries, and paid $1.1 billion in dividends to shareholders in the six-month period ended June 30, 2008.

AIG parent funds its short-term working capital needs through commercial paper issued by AIG Funding. As of June 30, 2008, AIG Funding had $5.8 billion of commercial paper outstanding with an average maturity of 33 days. As additional liquidity, AIG parent and AIG Funding maintain committed revolving credit facilities that, as of June 30, 2008, had an aggregate of $9.2 billion available to be drawn, and which are summarized above under Revolving Credit Facilities.

Invested Assets

The following tables summarize the composition of AIG's invested assets by segment:

(in millions)	General Insurance	Life Insurance & Retirement Services	Financial Services	Asset Management	Other	Total
June 30, 2008						
Fixed maturity securities:						
Bonds available for sale, at fair value	$ 72,981	$297,095	$ 1,370	$21,870	$ —	$393,316
Bonds held to maturity, at amortized cost	21,346	1	—	285	—	21,632
Bond trading securities, at fair value	—	8,764	—	37	—	8,801
Equity securities:						
Common stocks available for sale, at fair value	4,522	12,018	—	787	(21)	17,306
Common and preferred stocks trading, at fair value	285	22,200	—	29	—	22,514
Preferred stocks available for sale, at fair value	1,943	543	10	—	—	2,496
Mortgage and other loans receivable, net of allowance	16	26,010	1,038	7,275	45	34,384
Financial Services assets:						
Flight equipment primarily under operating leases, net of accumulated depreciation	—	—	43,887	—	—	43,887
Securities available for sale, at fair value	—	—	1,205	—	—	1,205
Trading securities, at fair value	—	—	35,170	—	—	35,170
Spot commodities, at fair value	—	—	90	—	—	90
Unrealized gain on swaps, options and forward transactions, at fair value	—	—	12,720	—	(1,172)	11,548
Trade receivables	—	—	2,294	—	—	2,294
Securities purchased under agreements to resell, at fair value	—	—	16,597	—	—	16,597
Finance receivables, net of allowance	—	5	33,306	—	—	33,311
Securities lending invested collateral, at fair value	4,951	48,312	141	6,126	—	59,530
Other invested assets	12,616	20,810	3,670	17,840	7,093	62,029
Short-term investments	9,967	32,724	3,974	7,125	15,702	69,492
Total Investments and Financial Services assets as shown on the balance sheet	128,627	468,482	155,472	61,374	21,647	835,602
Cash	499	979	476	269	6	2,229
Investment income due and accrued	1,380	4,952	29	255	(2)	6,614
Real estate, net of accumulated depreciation	342	965	28	95	224	1,654
Total invested assets*	$130,848	$475,378	$156,005	$61,993	$21,875	$846,099

** At June 30, 2008, approximately 63 percent and 37 percent of invested assets were held in domestic and foreign investments, respectively.*

(in millions)	General Insurance	Life Insurance & Retirement Services	Financial Services	Asset Management	Other	Total
December 31, 2007						
Fixed maturity securities:						
Bonds available for sale, at fair value	$ 74,057	$294,162	$ 1,400	$27,753	$ —	$397,372
Bonds held to maturity, at amortized cost	21,355	1	—	225	—	21,581
Bond trading securities, at fair value	—	9,948	—	34	—	9,982
Equity securities:						
Common stocks available for sale, at fair value	5,599	11,616	—	609	76	17,900
Common and preferred stocks trading, at fair value	321	21,026	—	29	—	21,376
Preferred stocks available for sale, at fair value	1,885	477	8	—	—	2,370
Mortgage and other loans receivable, net of allowance	13	24,851	1,365	7,442	56	33,727
Financial Services assets:						
Flight equipment primarily under operating leases, net of accumulated depreciation	—	—	41,984	—	—	41,984
Securities available for sale, at fair value	—	—	40,305	—	—	40,305
Trading securities, at fair value	—	—	4,197	—	—	4,197
Spot commodities	—	—	238	—	—	238
Unrealized gain on swaps, options and forward transactions, at fair value	—	—	13,010	—	(692)	12,318
Trade receivables	—	—	672	—	—	672
Securities purchased under agreements to resell, at contract value	—	—	20,950	—	—	20,950
Finance receivables, net of allowance	—	5	31,229	—	—	31,234
Securities lending invested collateral, at fair value	5,031	57,471	148	13,012	—	75,662
Other invested assets	11,895	19,015	3,663	17,261	6,989	58,823
Short-term investments	7,356	25,236	12,249	4,919	1,591	51,351
Total Investments and Financial Services assets as shown on the balance sheet	127,512	463,808	171,418	71,284	8,020	842,042
Cash	497	1,000	389	269	129	2,284
Investment income due and accrued	1,431	4,728	29	401	(2)	6,587
Real estate, net of accumulated depreciation	349	976	17	89	231	1,662
Total invested assets*	$129,789	$470,512	$171,853	$72,043	$8,378	$852,575

** At December 31, 2007, approximately 65 percent and 35 percent of invested assets were held in domestic and foreign investments, respectively.*

Investment Strategy

AIG's investment strategies are tailored to the specific business needs of each operating unit. The investment objectives are driven by the business model for each of the businesses: General Insurance, Life Insurance, Retirement Services and Asset Management's Spread-Based Investment business. The primary objectives are liquidity, preservation of capital, growth of surplus and generation of investment income to support the insurance products. At the local operating unit level, the strategies are based on considerations that include the local market, liability duration and cash flow characteristics, rating agency and regulatory capital considerations, legal investment limitations, tax optimization and diversification. In addition to local risk management considerations, AIG's corporate risk management guidelines impose limitations on concentrations to promote diversification by industry, asset class and geographic sector.

The majority of assets backing insurance liabilities at AIG consist of intermediate and long duration fixed maturity securities. In the case of Life Insurance & Retirement Services companies, as well as in the GIC and MIP portfolios of the Asset Management segment, the fundamental investment strategy is, as near as is practicable, to match the duration characteristics of the liabilities with comparable duration assets. Fixed maturity securities held by the insurance companies included in the AIG Property Casualty Group consist primarily of laddered holdings of tax-exempt municipal bonds, which provide attractive after-tax return, limited credit risk and generally good liquidity. Fixed maturity securities held by Foreign General Insurance companies consist primarily of intermediate duration high grade securities.

The market price of fixed maturity securities reflects numerous components, including interest rate environment, credit spread, embedded optionality (such as call features), liquidity, structural complexity, foreign exchange risk, and other credit and non-credit factors. However, in most circumstances, pricing is most sensitive to interest rates, such that the market price declines as interest rates rise, and

increases as interest rates fall. This effect is more pronounced for longer duration securities.

AIG marks to market the vast majority of the invested assets held by its insurance companies pursuant to FAS 115, "Accounting for Certain Investments in Debt and Equity Securities," and related accounting pronouncements. However, with limited exceptions (primarily with respect to separate account products consolidated on AIG's balance sheet pursuant to SOP 03-01), AIG does not mark to market its insurance liabilities for changes in interest rates, even though rising interest rates have the effect of reducing the fair value of such liabilities, and falling interest rates have the opposite effect. This results in the recording of changes in unrealized gains (losses) on securities in Accumulated other comprehensive income resulting from changes in interest rates without any correlative, inverse changes in gains (losses) on AIG's liabilities. Because AIG's asset duration in certain low-yield currencies, particularly Japan and Taiwan, is shorter than its liability duration, AIG views increasing interest rates in these countries as economically advantageous, notwithstanding the effect that higher rates have on the market value of its fixed maturity portfolio.

The majority of AIG's non-floating rate fixed maturity portfolio is held to support intermediate and long duration liabilities. Assuming no other changes in factors affecting the valuation of fixed maturity securities, each 10 basis point (1/10 of 1 percent) increase in interest rates results in a decline of approximately $2.4 billion in the pre-tax fair value of the fixed maturity portfolio. In most jurisdictions in which AIG operates, including the United States, such interest rate related changes in portfolio value are ignored for purposes of measuring regulatory capital adequacy.

The amortized cost or cost and fair value of AIG's available for sale and held to maturity securities were as follows:

	June 30, 2008				December 31, 2007			
(in millions)	Amortized Cost or Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value	Amortized Cost or Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Bonds – available for sale:[(a)]								
U.S. government and government sponsored entities	**$ 4,588**	**$ 158**	**$ 34**	**$ 4,712**	$ 7,956	$ 333	$ 37	$ 8,252
Obligations of states, municipalities and political subdivisions	**45,847**	**465**	**660**	**45,652**	46,087	927	160	46,854
Non-U.S. governments	**72,596**	**3,606**	**1,285**	**74,917**	67,023	3,920	743	70,200
Corporate debt	**223,902**	**3,693**	**8,247**	**219,348**	239,822	6,216	4,518	241,520
Mortgage-backed, asset-backed and collateralized	**111,678**	**840**	**13,541**	**98,977**	140,982	1,221	7,703	134,500
Total bonds	**$458,611**	**$ 8,762**	**$ 23,767**	**$443,606**	$501,870	$12,617	$13,161	$501,326
Equity securities	**16,086**	**4,332**	**616**	**19,802**	15,188	5,545	463	20,270
Total	**$474,697**	**$ 13,094**	**$ 24,383**	**$463,408**	$517,058	$18,162	$13,624	$521,596
Held to maturity:[(b)]	**$ 21,632**	**$ 322**	**$ 145**	**$ 21,809**	$ 21,581	$ 609	$ 33	$ 22,157

(a) At December 31, 2007, included AIGFP available for sale securities with a fair value of $39.3 billion, for which AIGFP elected the fair value option effective January 1, 2008, consisting primarily of corporate debt, mortgage-backed, asset-backed and collateralized securities. At June 30, 2008 and December 31, 2007, fixed maturities held by AIG that were below investment grade or not rated totaled $23.0 billion and $27.0 billion, respectively.

(b) Represents obligations of states, municipalities and political subdivisions.

AIG's held to maturity and available for sale fixed maturity investments totaled $465.4 billion at June 30, 2008, compared to $523.5 billion at December 31, 2007. At June 30, 2008, approximately 56 percent of the fixed maturity securities were held by domestic entities. Approximately 38 percent of such domestic securities were rated AAA by one or more of the principal rating agencies. Approximately five percent were below investment grade or not rated. AIG's investment decision process relies primarily on internally generated fundamental analysis and internal risk ratings. Third-party rating services' ratings and opinions provide one source of independent perspectives for consideration in the internal analysis.

A significant portion of the foreign fixed maturity portfolio is rated by Moody's, S&P or similar foreign rating services. Rating services are not available in all overseas locations. AIG's Credit Risk Committee (CRC) closely reviews the credit quality of the foreign portfolio's non-rated fixed maturity securities. At June 30, 2008, approximately 20 percent of the foreign fixed maturity securities were either rated AAA or, on the basis of AIG's internal analysis, were equivalent from a credit standpoint to securities so rated. Approximately four percent were below investment grade or not rated at that date. Approximately one third of the foreign fixed maturity portfolio is sovereign fixed maturity securities supporting the policy liabilities in the country of issuance.

The credit ratings of AIG's fixed maturity securities, other than those of AIGFP, were as follows:

Rating	**June 30, 2008**	December 31, 2007
AAA	**30%**	38%
AA	**30**	28
A	**22**	18
BBB	**13**	11
Below investment grade	**4**	4
Non-rated	**1**	1
Total	**100%**	100%

The industry categories of AIG's available for sale corporate debt securities, other than those of AIGFP, were as follows:

Industry Category	**June 30, 2008**	December 31, 2007
Financial institutions	**43%**	42%
Utilities	**12**	11
Communications	**8**	8
Consumer noncyclical	**7**	7
Capital goods	**6**	6
Consumer cyclical	**5**	5
Energy	**5**	4
Other	**14**	17
Total*	**100%**	100%

** At both June 30, 2008 and December 31, 2007, approximately 95 percent of these investments were rated investment grade.*

Investments in RMBS, CMBS, CDOs and ABS

As part of its strategy to diversify its investments, AIG invests in various types of securities, including RMBS, CMBS, CDOs and ABS.

The amortized cost, gross unrealized gains (losses) and fair value of AIG's investments in RMBS, CMBS, CDOs and ABS were as follows:

	June 30, 2008				December 31, 2007			
(in millions)	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Bonds — available for sale:								
AIG, excluding AIGFP:								
RMBS	**$ 77,531**	**$506**	**$10,139**	**$67,898**	$ 89,851	$ 433	$5,504	$ 84,780
CMBS	**22,935**	**210**	**1,942**	**21,203**	23,918	237	1,156	22,999
CDO/ABS	**11,212**	**124**	**1,460**	**9,876**	10,844	196	593	10,447
Subtotal, excluding AIGFP	**111,678**	**840**	**13,541**	**98,977**	124,613	866	7,253	118,226
AIGFP*	—	—	—	—	16,369	355	450	16,274
Total	**$111,678**	**$840**	**$13,541**	**$98,977**	$140,982	$1,221	$7,703	$134,500

* *Represents total AIGFP investments in mortgage-backed, asset-backed and collateralized securities for which AIGFP has elected the fair value option effective January 1, 2008. At June 30, 2008, the fair value of these securities were $20.3 billion. An additional $1.8 billion related to insurance company investments is included in Bonds — trading.*

Investments in RMBS

The amortized cost, gross unrealized gains (losses) and fair value of AIG's investments in RMBS securities, other than those of AIGFP, were as follows:

	June 30, 2008					December 31, 2007				
(in millions)	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value	Percent of Total	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value	Percent of Total
RMBS:										
U.S. agencies	**$16,642**	**$243**	**$ 181**	**$16,704**	**25%**	$14,575	$320	$ 70	$14,825	17%
Prime non-agency[(a)]	**17,575**	**36**	**1,646**	**15,965**	**23**	21,552	72	550	21,074	25
Alt-A	**20,236**	**69**	**3,896**	**16,409**	**24**	25,349	17	1,620	23,746	28
Other housing-related[(b)]	**3,090**	**2**	**532**	**2,560**	**4**	4,301	2	357	3,946	5
Subprime	**19,988**	**156**	**3,884**	**16,260**	**24**	24,074	22	2,907	21,189	25
Total	**$77,531**	**$506**	**$10,139**	**$67,898**	**100%**	$89,851	$433	$5,504	$84,780	100%

(a) Includes foreign and jumbo RMBS-related securities.
(b) Primarily wrapped second-lien.

AIG's operations, other than AIGFP, held investments in RMBS with an estimated fair value of $67.9 billion at June 30, 2008, or approximately 8 percent of AIG's total invested assets. In addition, AIG's insurance operations held investments with a fair value totaling $3.1 billion in CDOs, of which $39 million included some level of subprime exposure. AIG's RMBS investments are predominantly in highly-rated tranches that contain substantial protection features through collateral subordination. At June 30, 2008, approximately 87 percent of these investments were rated AAA, and approximately 8 percent were rated AA by one or more of the principal rating agencies. AIG's investments rated BBB or below totaled $2.7 billion, or less than 0.3 percent of AIG's total invested assets at June 30, 2008. As of July 30, 2008, $10.9 billion of AIG's RMBS backed primarily by subprime collateral had been downgraded as a result of rating agency actions since January 1, 2008, and $212 million of such investments had been upgraded. Of the downgrades, $10.0 billion were AAA rated securities. In addition to the downgrades, as of July 30, 2008, the rating agencies had $6.1 billion of RMBS on watch for downgrade.

The amortized cost of AIG's RMBS investments, other than those of AIGFP, at June 30, 2008 by year of vintage and credit rating were as follows:

	Year of Vintage						
(in billions)	Prior	2004	2005	2006	2007	2008	Total
Rating:							
Total RMBS							
AAA	$ 8,968	$6,057	$13,149	$20,561	$15,485	$3,011	$67,231
AA	1,030	648	1,539	1,940	1,250	—	6,407
A	221	193	265	273	193	9	1,154
BBB and below	168	306	378	870	964	53	2,739
Total RMBS	$10,387	$7,204	$15,331	$23,644	$17,892	$3,073	$77,531
Alt-A RMBS							
AAA	$ 753	$ 850	$ 4,312	$ 7,606	$ 5,290	$ —	$18,811
AA	241	164	301	99	280	—	1,085
A	27	41	89	18	42	—	217
BBB and below	15	27	68	13	—	—	123
Total Alt-A	$ 1,036	$1,082	$ 4,770	$ 7,736	$ 5,612	$ —	$20,236
Subprime RMBS							
AAA	$ 398	$ 423	$ 4,403	$ 7,760	$ 3,884	$ —	$16,868
AA	129	102	398	785	276	—	1,690
A	77	62	68	126	103	—	436
BBB and below	1	66	65	475	387	—	994
Total Subprime	$ 605	$ 653	$ 4,934	$ 9,146	$ 4,650	$ —	$19,988

AIG's underwriting practices for investing in RMBS, other ABS and CDOs take into consideration the quality of the originator, the manager, the servicer, security credit ratings, underlying characteristics of the mortgages, borrower characteristics, and the level of credit enhancement in the transaction. AIG's strategy is typically to invest in securities rated AA or better and create diversification across multiple underlying asset classes.

Investments in CMBS

The amortized cost of AIG's CMBS investments, other than those of AIGFP, at June 30, 2008 was as follows:

(in millions)	Amortized Cost	Percent of Total
CMBS (traditional)	$20,819	91%
ReRemic/CRE CDO	1,465	6
Agency	246	1
Other	405	2
Total	$22,935	100%

The percentage of AIG's CMBS investments, other than those of AIGFP, at June 30, 2008 by credit rating was as follows:

	Percentage
Rating:	
AAA	79%
AA	12
A	7
BBB and below	2
Total	100%

The percentage of AIG's CMBS investments, other than those of AIGFP, by year of vintage at June 30, 2008 was as follows:

	Percentage
Year:	
2008	1%
2007	24
2006	14
2005	18
2004	15
2003 and prior	28
Total	100%

The percentage of AIG's CMBS investments, other than those of AIGFP, by geographic region at June 30, 2008 was as follows:

	Percentage
Geographic region:	
New York	17%
California	15
Texas	7
Florida	6
Virginia	4
Illinois	4
New Jersey	3
Pennsylvania	3
Georgia	3
Massachusetts	3
All Other	35
Total	100%

At June 30, 2008, AIG held $23 billion in cost basis of CMBS. Approximately 79 percent of such holdings were rated AAA, approximately 19 percent were rated AA or A, and approximately 2 percent were rated BBB or below. At June 30, 2008, all such securities were current in the payment of principal and interest.

There have been disruptions in the commercial mortgage markets in general, and the CMBS market in particular, with credit default swaps indices and quoted prices of securities at levels consistent with a severe correction in lease rates, occupancy and fair value of properties. In addition, spreads in the primary mortgage market have widened significantly.

While this capital market stress has not to date been reflected in the performance of commercial mortgage securitization in the form of increased defaults in underlying mortgage pools, pricing of CMBS has been adversely affected by market perceptions that underlying mortgage defaults will increase. As a result, AIG recognized $387 million of other-than-temporary impairment charges in the three-month period ended June 30, 2008 on CMBS trading at a severe discount to cost, despite the absence of any deterioration in performance of the underlying credits, because AIG concluded that it could not reasonably assert that the recovery period was temporary. At this time, AIG anticipates substantial recovery of principal and interest on the securities to which such other-than-temporary impairment charges were recorded.

Investments in CDOs

The amortized cost of AIG's CDO investments, other than those of AIGFP, by collateral type at June 30, 2008 was as follows:

(in millions)	Amortized Cost	Percent of Total
Collateral Type:		
Bank loans (CLO)	$2,108	51%
Synthetic investment grade	1,233	30
Other	733	18
Subprime ABS	46	1
Total	$4,120	100%

The amortized cost of the AIG's CDO investments, other than those of AIGFP, by credit rating at June 30, 2008 was as follows:

(in millions)	Amortized Cost	Percent of Total
Rating:		
AAA	$ 872	21%
AA	766	19
A	2,085	51
BBB	313	8
Below investment grade and equity	84	1
Total	$4,120	100%

Securities Lending Activities

AIG's securities lending program is a centrally managed program by AIG Investments for the benefit of certain of AIG's insurance companies and the Asset Management segment. Securities are loaned to various financial institutions, primarily major banks and brokerage firms. Cash collateral generally ranging from 100 to 102 percent of the fair value of the loaned securities is received and is invested in fixed maturity securities to earn a net spread. To the extent that the collateral received is less than 102 percent, AIG has agreed with its insurance companies to deposit funds to the collateral pool for the benefit of the insurance company participants.

AIG's liability to the borrower for collateral received was $75.1 billion and the fair value of the collateral reinvested was $59.5 billion as of June 30, 2008. In addition to the invested collateral, the securities on loan as well as all of the assets of the lending companies are generally available to satisfy the liability for collateral received.

The composition of the securities lending invested collateral by credit rating at June 30, 2008 was as follows:

(in millions)	AAA	AA	A	BBB/Not Rated	Short-Term	Total
Corporate debt	$ 696	$ 7,407	$3,557	$1,245	$ —	$12,905
Mortgage-backed, asset-backed and collateralized	30,933	3,170	437	1,640	—	36,180
Cash and short-term investments	—	—	—	—	10,445	10,445
Total	$31,629	$10,577	$3,994	$2,885	$10,445	$59,530

Participation in the securities lending program by reporting unit at June 30, 2008 was as follows:

	Percent Participation
Domestic Life Insurance and Domestic Retirement Services	71%
Foreign Life Insurance	11
AIG Property Casualty Group	4
Foreign General Insurance	5
Asset Management	9
Total	100%

On June 30, 2008, $7.3 billion (or 10 percent) of the liabilities were one-day tenor. These one-day tenor loans do not have a contractual end date but are terminable by either party on demand. Substantially all of the balance of the liabilities contractually mature over the next thirty days. However, the maturing loans are frequently renewed and rolled over to extended dates. Collateral held for this program at June 30, 2008 included interest bearing cash equivalents with overnight maturities of $10.4 billion and other short-term investments of $1.4 billion.

Liquidity in the securities pool is managed based upon historical experience regarding volatility of daily, weekly and biweekly loan balances. The decline in the level of securities lent, and thus the liability for collateral due back to the borrowers, is the result of AIG's overall strategy to reduce the size of this program over time.

In addition, the invested securities are carried at fair value with unrealized gains and losses recorded in accumulated other comprehensive income (loss) while net realized gains and losses are recorded in earnings. The net unrealized loss on the investments was $8.2 billion as of June 30, 2008. During the three- and six-month periods ended June 30, 2008, AIG recorded net realized losses of $3.8 billion and $6.7 billion, respectively, on this portfolio, predominantly related to other-than-temporary impairments.

AIG has agreed to deposit into the securities pool an amount equal to the investment losses realized by the pool in connection with sales of impaired securities, up to $5 billion.

Portfolio Review

Other-Than-Temporary Impairments

AIG assesses its ability to hold any fixed maturity security in an unrealized loss position to its recovery, including fixed maturity securities classified as available for sale, at each balance sheet date. The decision to sell any such fixed maturity security classified as available for sale reflects the judgment of AIG's management that the security sold is unlikely to provide, on a relative value basis, as attractive a return in the future as alternative securities entailing comparable risks. With respect to distressed securities, the sale decision reflects management's judgment that the risk-discounted anticipated ultimate recovery is less than the value achievable on sale.

AIG evaluates its investments for impairments in valuation as well as credit. The determination that a security has incurred an other-than-temporary decline in value requires the judgment of management and consideration of the fundamental condition of the issuer, its near-term prospects and all the relevant facts and circumstances. See Critical Accounting Estimates — Other-Than-Temporary Impairments herein for further information on AIG's policy.

Once a security has been identified as other-than-temporarily impaired, the amount of such impairment is determined by reference to that security's contemporaneous fair value and recorded as a charge to earnings.

In light of the recent significant disruption in the U.S. residential mortgage and credit markets, AIG has recognized an other-than-temporary impairment charge (severity loss) of $4.8 billion and $8.9 billion in the three- and six-month periods ended June 30, 2008, primarily related to certain RMBS and other structured securities. Even while retaining their investment grade ratings and timely continuation of interest and principal payments, such securities were priced at a significant discount to cost (generally below 60 cents on the dollar). Notwithstanding AIG's intent and ability to hold such securities indefinitely, and despite structures that indicate that a substantial amount of the securities should continue to perform in accordance with original terms, AIG concluded that it could not reasonably assert that the recovery period would be temporary.

As a result of AIG's periodic evaluation of its securities for other-than-temporary impairments in value, AIG recorded other-than-temporary impairment charges of $6.8 billion and $417 million in the three-month periods ended June 30, 2008 and 2007, respectively, and $12.4 billion and $884 million in the six-month periods ended June 30, 2008 and 2007, respectively.

In addition to the above severity losses, AIG recorded other-than-temporary impairment charges in the three- and six-month periods ended June 30, 2008 and 2007 related to:

- securities that AIG does not intend to hold until recovery;
- declines due to foreign exchange rates;
- issuer-specific credit events;
- certain structured securities impaired under Emerging Issues Task Force Issue No. 99-20, "Recognition of Interest Income and Impairment on Purchased Beneficial Interests and Beneficial Interests that Continue to be Held by a Transferor in Securitized Financial Assets"; and
- other impairments, including equity securities and partnership investments.

The composition of net realized capital gains (losses), which include other-than-temporary impairments, were as follows:

(in millions)	Three Months Ended June 30, **2008**	2007	Six Months Ended June 30, **2008**	2007
Sales of fixed maturities	**$ (29)**	$ (210)	**$ (10)**	$ (169)
Sales of equity securities	**240**	285	**320**	443
Sales of real estate and other assets	**172**	364	**325**	499
Other-than-temporary impairments	**(6,777)**	(417)	**(12,370)**	(884)
Foreign exchange transactions	**(74)**	(244)	**(738)**	(108)
Derivative instruments	**387**	194	**303**	121
Total	**$ (6,081)**	$ (28)	**$ (12,170)**	$ (98)

Other-than-temporary impairment charges by reporting segment were as follows:

(in millions)	General Insurance	Life Insurance & Retirement Services	Financial Services	Asset Management	Other	Total
Three months ended June 30, 2008						
Impairment Type:						
Severity	**$ (633)**	**$ (3,374)**	**$ (16)**	**$ (820)**	**$ —**	**$ (4,843)**
Trading at 25 percent or more discount for nine consecutive months	**—**	**—**	**—**	**—**	**—**	**—**
Lack of intent to hold to recovery	**—**	**(237)**	**(1)**	**(3)**	**—**	**(241)**
Foreign currency declines	**—**	**(633)**	**—**	**—**	**—**	**(633)**
Issuer-specific credit events	**(46)**	**(276)**	**—**	**—**	**—**	**(322)**
Adverse projected cash flows on structured securities	**(6)**	**(673)**	**—**	**(59)**	**—**	**(738)**
Total	**$ (685)**	**$ (5,193)**	**$ (17)**	**$ (882)**	**$ —**	**$ (6,777)**
Three months ended June 30, 2007						
Impairment Type:						
Severity	$ —	$ —	$ —	$ —	$ —	$ —
Trading at 25 percent or more discount for nine consecutive months	—	(6)	—	—	—	(6)
Lack of intent to hold to recovery	(64)	(211)	(2)	—	—	(277)
Foreign currency declines	—	(92)	—	—	—	(92)
Issuer-specific credit events	(20)	(9)	—	—	(6)	(35)
Adverse projected cash flows on structured securities	—	(6)	—	(1)	—	(7)
Total	$ (84)	$ (324)	$ (2)	$ (1)	$ (6)	$ (417)
Six months ended June 30, 2008						
Impairment Type:						
Severity	**$ (745)**	**$ (6,530)**	**$ (27)**	**$ (1,645)**	**$ (1)**	**$ (8,948)**
Trading at 25 percent or more discount for nine consecutive months	**—**	**—**	**—**	**—**	**—**	**—**
Lack of intent to hold to recovery	**(21)**	**(928)**	**(2)**	**(70)**	**—**	**(1,021)**
Foreign currency declines	**—**	**(1,034)**	**—**	**—**	**—**	**(1,034)**
Issuer-specific credit events	**(67)**	**(388)**	**—**	**(38)**	**—**	**(493)**
Adverse projected cash flows on structured securities	**(7)**	**(705)**	**—**	**(162)**	**—**	**(874)**
Total	**$ (840)**	**$ (9,585)**	**$ (29)**	**$ (1,915)**	**$ (1)**	**$(12,370)**
Six months ended June 30, 2007						
Impairment Type:						
Severity	$ —	$ —	$ —	$ —	$ —	$ —
Trading at 25 percent or more discount for nine consecutive months	—	(6)	—	—	—	(6)
Lack of intent to hold to recovery	(72)	(298)	(2)	(2)	—	(374)
Foreign currency declines	—	(304)	—	—	—	(304)
Issuer-specific credit events	(58)	(101)	—	(27)	(6)	(192)
Adverse projected cash flows on structured securities	—	(7)	—	(1)	—	(8)
Total	$ (130)	$ (716)	$ (2)	$ (30)	$ (6)	$ (884)

Other-than-temporary severity-related impairment charges for the three- and six-month periods ended June 30, 2008 by type of security and credit rating were as follows:

Rating: *(in millions)*	RMBS	CDO	CMBS	Other Securities	Total
Three months ended June 30, 2008					
Fixed Maturities:					
AAA	**$2,964**	**$ 1**	**$106**	**$ —**	**$ 3,071**
AA	**704**	**1**	**32**	**—**	**737**
A	**178**	**6**	**187**	**—**	**371**
BBB and below	**254**	**39**	**62**	**—**	**355**
Nonrated	**—**	**—**	**—**	**—**	**—**
Equities	**—**	**—**	**—**	**309**	**309**
Total	**$4,100**	**$ 47**	**$387**	**$309**	**$ 4,843**
Six months ended June 30, 2008*					
Fixed Maturities:					
AAA	**$4,460**	**$ 22**	**$223**	**$ 12**	**$ 4,717**
AA	**1,556**	**41**	**71**	**1**	**1,669**
A	**482**	**55**	**485**	**4**	**1,026**
BBB and below	**750**	**39**	**125**	**20**	**934**
Nonrated	**—**	**—**	**—**	**17**	**17**
Equities	**—**	**—**	**—**	**585**	**585**
Total	**$7,248**	**$157**	**$904**	**$639**	**$ 8,948**

**Ratings are as of the date of the impairment charge.*

No other-than-temporary impairment charge with respect to any one single counterparty was significant to AIG's consolidated financial condition or results of operations, and no individual other-than-temporary impairment charge exceeded two percent of the consolidated net loss in the six-month period ended June 30, 2008.

In periods subsequent to the recognition of an other-than-temporary impairment charge for fixed maturity securities that is not credit or foreign exchange related, AIG generally accretes into income the discount or amortizes the reduced premium resulting from the reduction in cost basis over the remaining life of the security. The amount of accretion recognized in earnings for the three- and six-month periods ended June 30, 2008 was $75 million and $87 million, respectively.

Commercial Mortgage Loan Exposure

At June 30, 2008, AIG had direct commercial mortgage loan exposure of $17.1 billion, with $15.8 billion representing U.S. loan exposure. At that date, substantially all of the U.S. loans were current. The remaining commercial mortgage loans are secured predominantly by properties in Japan. In addition, at June 30, 2008, AIG had approximately $2.3 billion in residential mortgage loans in jurisdictions outside the United States, primarily backed by properties in Taiwan and Thailand.

An aging of the pre-tax unrealized losses of fixed maturity and equity securities, distributed as a percentage of cost relative to unrealized loss (the extent by which the fair value is less than amortized cost or cost), including the number of respective items, at June 30, 2008 was as follows:

Aging[a] (dollars in millions)	Less than or equal to 20% of Cost[b]			Greater than 20% to 50% of Cost[b]			Greater than 50% of Cost[b]			Total		
	Cost[c]	Unrealized Loss	Items	Cost[c]	Unrealized Loss	Items	Cost[c]	Unrealized Loss	Items	Cost[c]	Unrealized Loss[d]	Items
Investment grade bonds												
0-6 months	$133,610	$ 4,302	19,544	$ 1,910	$ 467	334	$ —	$ —	—	$135,520	$ 4,769	19,878
7-12 months	56,297	4,597	4,337	23,676	7,118	740	—	—	—	79,973	11,715	5,077
>12 months	58,277	4,773	8,523	7,541	2,074	827	—	—	—	65,818	6,847	9,350
Total	$248,184	$13,672	32,404	$33,127	$9,659	1,901	$ —	$ —	—	$281,311	$23,331	34,305
Below investment grade bonds												
0-6 months	$ 6,215	$ 173	1,384	$ 154	$ 54	24	$ —	$ —	—	$ 6,369	$ 227	1,408
7-12 months	1,294	94	349	74	21	21	—	—	—	1,368	115	370
>12 months	1,163	79	540	59	15	14	—	—	—	1,222	94	554
Total	$ 8,672	$ 346	2,273	$ 287	$ 90	59	$ —	$ —	—	$ 8,959	$ 436	2,332
Total bonds												
0-6 months	$139,826	$ 4,475	20,928	$ 2,064	$ 521	358	$ —	$ —	—	$141,890	$ 4,996	21,286
7-12 months	57,590	4,691	4,686	23,750	7,139	761	—	—	—	81,340	11,830	5,447
>12 months	59,440	4,852	9,063	7,600	2,089	841	—	—	—	67,040	6,941	9,904
Total[e]	$256,856	$14,018	34,677	$33,414	$9,749[f]	1,960	$ —	$ —	—	$290,270	$23,767	36,637
Equity securities												
0-6 months	$ 4,590	$ 336	3,900	$ 316	$ 86	667	$ —	$ —	—	$ 4,906	$ 422	4,567
7-12 months	747	86	325	381	108	272	—	—	—	1,128	194	597
>12 months	—	—	—	—	—	—	—	—	—	—	—	—
Total	$ 5,337	$ 422	4,225	$ 697	$ 194	939	$ —	$ —	—	$ 6,034	$ 616	5,164

(a) Represents the number of consecutive months that fair value has been less than cost by any amount.

(b) Represents the percentage by which fair value is less than cost at the balance sheet date.

(c) For bonds, represents amortized cost.

(d) The effect on net income of unrealized losses after taxes will be mitigated upon realization because certain realized losses will be charged to participating policyholder accounts, or realization will result in current decreases in the amortization of certain DAC.

(e) Includes securities lending invested collateral.

(f) Of this $9.7 billion, $6.7 billion relates to RMBS, CMBS, CDOs and ABS with unrealized losses between 25 percent and 50 percent; and $1.9 billion relates to RMBS, CMBS, CDOs and ABS with unrealized losses between 20 percent and 25 percent. The balance represents all other classes of fixed maturity securities.

The aging of the unrealized losses of RMBS, CMBS, CDOs and ABS with fair values between 20 percent and 50 percent less than their cost at June 30, 2008 (in footnote (f) to the table above) is shown in the table below, which provides the period in which those securities in unrealized loss positions would become candidates for impairment solely because they have been trading at a discount for nine consecutive months (AIG's other-than-temporary aging guideline) without regard to the level of discount (AIG's other-than-temporary trading level guideline), assuming prices remained unchanged.

(in millions) Unrealized loss percent	Third Quarter 2008	Fourth Quarter 2008	First Quarter 2009	Total
25 to 50 percent	$69	$3,574	$3,104	$6,747
20 to less than 25 percent	$ 6	$ 35	$1,856	$1,897

Given the current difficult market conditions, AIG is not able to predict reasonably likely changes in the prices of these securities. Moreover, AIG is unable to assess the effect, if any, that recent transactions involving sales of large portfolios of CDOs will have on the pricing of its available for sale securities.

Unrealized gains and losses

At June 30, 2008, the carrying value of AIG's fixed maturity and equity securities aggregated $516.4 billion. At June 30, 2008, aggregate pre-tax unrealized gains for fixed maturity and equity securities were $13.1 billion ($8.5 billion after tax).

At June 30, 2008, the aggregate pre-tax gross unrealized losses on fixed maturity and equity securities were

$24.4 billion ($15.9 billion after tax). Additional information about these securities is as follows:

- These securities were valued, in the aggregate, at approximately 92 percent of their current amortized cost.
- Approximately 12 percent of these securities were valued at less than 20 percent of their current cost, or amortized cost.
- Approximately three percent of the fixed maturity securities had issuer credit ratings that were below investment grade.

AIG did not consider these securities in an unrealized loss position to be other-than-temporarily impaired at June 30, 2008, because management has the intent and ability to hold these investments until they recover their cost basis. AIG believes the securities will generally continue to perform in accordance with the original terms, notwithstanding the present price declines.

For the three- and six-month periods ended June 30, 2008, unrealized losses related to investment grade bonds increased $1.0 billion ($0.7 billion after tax) and $10.5 billion ($6.8 billion after tax), respectively, reflecting the widening of credit spreads, partially offset by the effects of a decline in risk-free interest rates.

The amortized cost and fair value of fixed maturity securities available for sale in an unrealized loss position at June 30, 2008, by contractual maturity, were as follows:

(in millions)	Amortized Cost	Fair Value
Due in one year or less	$ 8,067	$ 7,945
Due after one year through five years	43,226	41,595
Due after five years through ten years	68,941	65,592
Due after ten years	77,824	72,700
Mortgage-backed, asset-backed and collateralized	92,212	78,671
Total	$290,270	$266,503

For the six-month period ended June 30, 2008, the pre-tax realized losses incurred with respect to the sale of fixed maturities and equity securities were $0.8 billion. The aggregate fair value of securities sold was $8.9 billion, which was approximately 92 percent of amortized cost. The average period of time that securities sold at a loss during the six-month period ended June 30, 2008 were trading continuously at a price below book value was approximately five months. See Risk Management — Corporate Risk Management — Credit Risk Management in the 2007 Annual Report on Form 10-K for an additional discussion of investment risks associated with AIG's investment portfolio.

Risk Management

For a complete discussion of AIG's risk management program, see Risk Management in the 2007 Annual Report on Form 10-K.

AIG has continued to invest in human resources, systems and processes in the enterprise risk management functions, both at the corporate and business unit levels. These efforts include implementing systems and processes to ensure the aggregation of the various categories of risk across business units and as a whole, and incorporating forward-looking analyses and stress tests. These initiatives are ongoing and will take time to implement, including the hiring of additional qualified personnel.

Credit Risk Management

AIG defines its aggregate credit exposures to a counterparty as the sum of its fixed maturities, loans, finance leases, derivatives (mark to market), deposits (in the case of financial institutions) and the specified credit equivalent exposure to certain insurance products which embody credit risk.

The following table presents AIG's largest credit exposures at June 30, 2008 as a percentage of total consolidated shareholders' equity:

Category	Risk Rating[(a)]	Credit Exposure as a Percentage of Total Consolidated Shareholders' Equity
Investment Grade:		
10 largest combined	A+ (weighted) average[(b)]	113.9%
Single largest non- sovereign (financial institution)	A+	13.3
Single largest corporate	AAA	9.0
Single largest sovereign	A	22.2
Non-Investment Grade:		
Single largest sovereign	BB+	1.0
Single largest non- sovereign	BB+	0.6

(a) Risk rating is based on external ratings, or equivalent based on AIG's internal risk rating process.

(b) Five of the ten largest credit exposures are to highly-rated financial institutions and four are to investment-grade rated sovereigns; none is rated lower than BBB+ or its equivalent.

AIG closely controls its aggregate cross-border exposures to avoid excessive concentrations in any one country or regional group of countries. AIG defines its cross-border exposure to include both cross-border credit exposures and its large cross-border investments in its own international subsidiaries. Thirteen countries had cross-border exposures in excess of 10 percent of total consolidated shareholders' equity at June 30, 2008. At that date eight were AAA-rated, four were AA-rated and one was A-rated.

In addition, AIG closely monitors its industry concentrations, the risks of which are often mitigated by the breadth and scope of AIG's international operations. Excluding the U.S. residential and commercial mortgage sectors, AIG's single largest industry credit exposure is to the highly-rated global financial institutions sector, accounting for 128 percent of total consolidated shareholders' equity at June 30, 2008 (compared to 87 percent at December 31, 2007, as a portion of the proceeds of the May 2008 capital raising was deposited with banks). AIG's other industry credit

concentrations in excess of 10 percent of total consolidated shareholders' equity are in the following industries (in descending order by approximate size):

- Oil and gas;
- Electric and water utilities;
- European regional financial institutions;
- Global life insurance carriers;
- Global telecommunications companies;
- U.S.-based regional financial institutions;
- Global securities firms and exchanges;
- Global reinsurance firms;
- Government sponsored entities;
- Healthcare companies; and
- Retail companies.

Other than as described above, there were no significant changes to AIG's credit exposures as set forth in Risk Management — Corporate Risk Management — Credit Risk Management in the 2007 Annual Report on Form 10-K.

Market Risk Management

Insurance, Asset Management and Non-Trading Financial Services Value at Risk (VaR)

AIG performs one comprehensive VaR analysis across all of its non-trading businesses, and a separate VaR analysis for its trading business at AIGFP. The comprehensive VaR is categorized by AIG business segment (General Insurance, Life Insurance & Retirement Services, Financial Services and Asset Management) and also by market risk factor (interest rate, currency and equity). AIG's market risk VaR calculations include exposures to benchmark Treasury or swap interest rates, but do not include exposures to credit-based factors such as credit spreads. AIG's credit exposures within its invested assets and credit derivative portfolios are discussed in Risk Management — Segment Risk Management — Financial Services in the 2007 Annual Report on Form 10-K.

For the insurance segments, assets included are invested assets (excluding direct holdings of real estate) and liabilities included are reserve for losses and loss expenses, reserve for unearned premiums, future policy benefits for life and accident and health insurance contracts and other policyholders' funds. For financial services companies, loans and leases represent the majority of assets represented in the VaR calculation, while bonds and notes issued represent the majority of liabilities.

AIG calculated the VaR with respect to net fair values as of June 30, 2008 and December 31, 2007. The VaR number represents the maximum potential loss as of those dates that could be incurred with a 95 percent confidence (i.e., only five percent of historical scenarios show losses greater than the VaR figure) within a one-month holding period. AIG uses the historical simulation methodology that entails repricing all assets and liabilities under explicit changes in market rates within a specific historical time period. AIG uses the most recent three years of historical market information for interest rates, foreign exchange rates, and equity index prices. For each scenario, each transaction was repriced. Segment and AIG-wide scenario values are then calculated by netting the values of all the underlying assets and liabilities.

The following table presents the period-end, average, high and low VaRs on a diversified basis and of each component of market risk for AIG's non-trading businesses. The diversified VaR is usually smaller than the sum of its components due to correlation effects.

	2008				2007			
	As of	Six Months Ended June 30,			As of	Year Ended December 31,		
(in millions)	June 30	Average	High	Low	December 31	Average	High	Low
Total AIG non-trading market risk:								
Diversified	**$6,645**	**$6,363**	**$6,851**	**$5,593**	$5,593	$5,316	$5,619	$5,073
Interest rate	**4,822**	**4,798**	**5,190**	**4,383**	4,383	4,600	4,757	4,383
Currency	**1,022**	**884**	**1,022**	**785**	785	729	785	685
Equity	**3,138**	**3,011**	**3,268**	**2,627**	2,627	2,183	2,627	1,873
General Insurance:								
Diversified	**$1,377**	**$1,365**	**$1,377**	**$1,356**	$1,363	$1,637	$1,892	$1,363
Interest rate	**1,218**	**1,138**	**1,218**	**1,078**	1,117	1,492	1,792	1,117
Currency	**328**	**296**	**328**	**255**	255	222	255	205
Equity	**1,030**	**958**	**1,030**	**835**	835	659	835	573
Life Insurance & Retirement Services:								
Diversified	**$6,096**	**$5,853**	**$6,284**	**$5,180**	$5,180	$4,848	$5,180	$4,574
Interest rate	**4,658**	**4,683**	**4,987**	**4,405**	4,405	4,465	4,611	4,287
Currency	**807**	**693**	**807**	**621**	649	621	678	568
Equity	**2,196**	**2,072**	**2,210**	**1,810**	1,810	1,512	1,810	1,293
Non-Trading Financial Services:								
Diversified	**$ 131**	**$ 132**	**$ 167**	**$ 99**	$ 99	$ 117	$ 170	$ 85
Interest rate	**125**	**128**	**164**	**95**	95	116	168	76
Currency	**17**	**15**	**17**	**13**	13	12	13	11
Equity	**2**	**1**	**2**	**1**	1	1	1	1
Asset Management:								
Diversified	**$ 61**	**$ 50**	**$ 61**	**$ 38**	$ 38	$ 49	$ 74	$ 26
Interest rate	**56**	**43**	**56**	**32**	32	45	72	22
Currency	**2**	**2**	**2**	**2**	2	3	5	2
Equity	**11**	**12**	**13**	**11**	13	11	13	8

AIG's total non-trading market risk VaR increased from $5.6 billion at year-end 2007 to $6.6 billion at June 30, 2008. The biggest drivers of this increase were updated liability cash flow projections, increased volatilities in equity markets and "tail" effects (increased riskiness of the worst 5 percent of simulated portfolio outcomes that determine VaR).

Capital Markets Trading VaR

AIGFP attempts to minimize risk in benchmark interest rates, equities, commodities and foreign exchange. Market exposures in option implied volatilities, correlations and basis risks are also minimized over time.

AIGFP's minimal reliance on market risk driven revenue is reflected in its VaR. AIGFP's VaR calculation is based on the interest rate, equity, commodity and foreign exchange risk arising from its portfolio. Credit-related factors, such as credit spreads or credit default, are not included in AIGFP's VaR calculation. Because the market risk with respect to securities available for sale, at market, is substantially hedged, segregation of the financial instruments into trading and other than trading was not considered necessary. AIGFP operates under established market risk limits based upon this VaR calculation. In addition, AIGFP backtests its VaR.

In the calculation of VaR for AIGFP, AIG uses the historical simulation methodology based on estimated changes to the value of all transactions under explicit changes in market rates and prices within a specific historical time period. AIGFP attempts to secure reliable and independent current market prices, such as published exchange prices, external subscription services such as Bloomberg or Reuters, or third-party or broker quotes. When such prices are not available, AIGFP uses an internal methodology that includes extrapolation from observable and verifiable prices nearest to the dates of the transactions. Historically, actual results have not deviated from these models in any material respect.

AIGFP reports its VaR level using a 95 percent confidence level and a one-day holding period, facilitating risk comparison with AIGFP's trading peers and reflecting the fact that market risks can be actively assumed and offset in AIGFP's trading portfolio.

The following table presents the year-end, average, high, and low VaRs on a diversified basis and of each component of market risk for Capital Markets operations. The diversified VaR is usually smaller than the sum of its components due to correlation effects.

	As of	Six Months Ended June 30, 2008			As of	Year Ended December 31, 2007		
(in millions)	June 30	Average	High	Low	December 31	Average	High	Low
Capital Markets trading market risk:								
Diversified	**$6**	**$6**	**$9**	**$ 5**	$5	$5	$8	$4
Interest rate	**2**	**2**	**3**	**1**	3	2	3	2
Currency	**1**	**1**	**2**	**—**	1	1	2	1
Equity	**2**	**2**	**4**	**2**	3	3	5	2
Commodity	**5**	**5**	**7**	**3**	3	3	7	2

Credit Derivatives

AIGFP enters into credit derivative transactions in the ordinary course of its business. The majority of AIGFP's credit derivatives require AIGFP to provide credit protection on a designated portfolio of loans or debt securities. AIGFP provides such credit protection on a "second loss" basis, under which AIGFP's payment obligations arise only after credit losses in the designated portfolio exceed a specified threshold amount or level of "first losses."

In certain cases, the credit risk associated with a designated portfolio is tranched into different layers of risk, which are then analyzed and rated by the credit rating agencies. Typically, there will be an equity layer covering the first credit losses in respect of the portfolio up to a specified percentage of the total portfolio, and then successive layers ranging from generally a BBB-rated layer to one or more AAA-rated layers. In transactions that are rated with respect to the risk layer or tranche that is immediately junior to the threshold level above which AIGFP's payment obligation would generally arise, a significant majority were rated AAA at origination by the rating agencies. In transactions that are not rated, AIGFP applies the same risk criteria for setting the threshold level for its payment obligations. Therefore, the risk layer assumed by AIGFP with respect to the designated portfolio in these transactions is often called the "super senior" risk layer, defined as the layer of credit risk senior to a risk layer that has been rated AAA by the credit rating agencies, or if the transaction is not rated, equivalent thereto.

Approximately $307 billion (consisting of corporate loans and prime residential mortgages) of the $441 billion in notional exposure of AIGFP's super senior credit default swap portfolio as of June 30, 2008 represented derivatives written for financial institutions, principally in Europe, for the purpose of providing regulatory capital relief rather than risk mitigation. In exchange for a minimum guaranteed fee, the counterparties receive credit protection with respect to diversified loan portfolios they own, thus improving their regulatory capital position. These derivatives are generally expected to terminate at no additional cost to the counterparty when they no longer provide the regulatory capital benefit. AIG expects that the majority of these transactions will be terminated within the next 9 to 21 months by AIGFP's counterparties. As of July 31, 2008, $80.7 billion in notional exposures have either been terminated or are in the process of being terminated. AIGFP was not required to make any payments as part of these terminations and in certain cases was paid a fee upon termination.

In light of early termination experience to date and after other comprehensive analyses, AIG determined that there was no unrealized market valuation adjustment for this regulatory capital relief portfolio for the six-month period ended June 30, 2008 other than for transactions where AIGFP believes the counterparties are no longer using the transactions to obtain regulatory capital relief. AIG will continue to assess the valuation of this portfolio and monitor developments in the marketplace. Given the significant deterioration in the credit markets and the risk that AIGFP's expectations with respect to the termination of these transactions by its counterparties may not materialize, there can be no assurance that AIG will not recognize unrealized market valuation losses from this portfolio in future periods, and recognition of even a small percentage decline in the fair value of this portfolio could be material to an individual reporting period.

During the second quarter of 2008, a regulatory capital relief transaction with a notional amount of $1.6 billion and a fair value loss of $125 million was not terminated as expected when it no longer provided regulatory capital benefit to the counterparty. This transaction provided protection on an RMBS unlike the other regulatory transactions which provide protection on loan portfolios held by the counterparties. The documentation for this transaction contains provisions not included in AIGFP's other regulatory capital relief transactions, which enable the counterparty to arbitrage a specific credit exposure.

Approximately $54 billion of the $441 billion in notional exposure on AIGFP's super senior credit default swaps as of June 30, 2008 was written on designated pools of investment grade corporate debt and CLOs. AIG estimates

the fair value of this corporate credit default swap portfolio by reference to benchmark indices, including the CDX and iTraxx, and third-party prices and collateral calls. No assurance can be given that the fair value of AIG's corporate credit default swap portfolio would not change materially if other market indices or pricing sources were used to estimate the fair value of the portfolio.

In addition to writing credit protection on the super senior risk layer on designated portfolios of loans or debt securities, AIGFP also wrote protection on tranches below the super senior risk layer. At June 30, 2008 the notional amount of the credit default swaps in the regulatory capital relief portfolio written on tranches below the super senior risk layer was $5.8 billion, with an estimated fair value loss of $171 million.

While the credit default swaps written on corporate debt obligations are cash settled, the majority of the credit default swaps written on CDOs and CLOs require physical settlement. Under a physical settlement arrangement, AIGFP would be required to purchase the referenced super senior security at par in the event of a non-payment on that security. Certain of the AIGFP credit default swaps with an aggregate notional amount totaling $8.2 billion protect CDOs that include over-collateralization provisions that adjust the value of the collateral based, in part, on the ratings of the collateral underlying the CDOs. If the over-collateralization provisions are not satisfied, an event of default would occur creating a right to accelerate. In certain of these circumstances, AIGFP may be required to purchase the referenced super senior security at par upon the acceleration of the security. As of July 31, 2008, six CDOs for which AIGFP had written credit protection on the super senior CDO securities had experienced events of default. One of these CDOs has been accelerated and AIGFP extinguished a portion of its swap obligations by purchasing the protected CDO security for $103 million, principal amount outstanding related to this obligation. AIGFP's remaining notional exposure with respect to these CDOs was $1.5 billion at July 31, 2008. AIGFP cannot currently quantify its obligations which might occur in the future under the foregoing provisions, or determine the timing of any additional purchases that might be required. Therefore, there can be no assurance that the extinguishment of these obligations by AIGFP will not have a material effect on AIG's liquidity.

AIGFP has written 2a-7 Puts in connection with certain multi-sector CDOs that allow the holders of the securities to treat the securities as eligible short-term 2a-7 investments under the Investment Company Act of 1940. Holders of securities are permitted, in certain circumstances, to tender their securities to the issuers at par. If an issuer's remarketing agent is unable to resell the securities so tendered, AIGFP must purchase the securities at par as long as the security has not experienced a default. During the six-month period ended June 30, 2008, AIGFP repurchased securities with a principal amount of approximately $917 million in connection with these obligations. In certain transactions, AIGFP has contracted with third parties to provide liquidity for the securities if they are put to AIGFP for up to a three-year period. Such liquidity facilities totaled $8.5 billion at June 30, 2008. As of August 5, 2008, AIGFP has utilized $3.2 billion of these liquidity facilities. At June 30, 2008, AIGFP had $11.3 billion of notional exposure on 2a-7 Puts, included as part of the multi-sector CDO portfolio discussed herein.

Certain of these credit derivatives are subject to collateral posting provisions. These provisions differ among counterparties and asset classes. In the case of most of the multi-sector CDO transactions, the amount of collateral required is determined based on the change in value of the underlying cash security that represents the super senior risk layer subject to credit protection, and not on the change in value of the super senior credit derivative.

As of July 31, 2008, AIGFP had received collateral calls from counterparties in respect of certain super senior credit default swaps (including those entered into by counterparties for regulatory capital relief purposes and those in respect of corporate debt/CLOs). At times, valuation estimates made by certain of the counterparties with respect to certain super senior credit default swaps or the underlying reference CDO securities, for purposes of determining the amount of collateral required to be posted by AIGFP in connection with such instruments, have differed significantly from AIGFP's estimates. AIG is unable to assess the effect, if any, that recent transactions involving sales of large portfolios of CDOs will have on collateral posting requirements. In almost all cases, AIGFP has been able to successfully resolve the differences or otherwise reach an accommodation with respect to collateral posting levels, including in certain cases by entering into compromise collateral arrangements, some of which are for specified periods of time. Due to the ongoing nature of these collateral calls, AIGFP may engage in discussions with one or more counterparties in respect of these differences at any time. As of July 31, 2008, AIGFP had posted collateral (or had received collateral, where offsetting exposures on other transactions resulted in the counterparty posting to AIGFP) based on exposures, calculated in respect of super senior credit default swaps, in an aggregate net amount of $16.5 billion. Valuation estimates made by counterparties for collateral purposes were considered in the determination of the fair value estimates of AIGFP's super senior credit default swap portfolio.

The unrealized market valuation losses of $26.1 billion recorded on AIGFP's super senior multi-sector CDO credit default swap portfolio represents the cumulative change in fair value of these derivatives, which represents AIG's best estimate of the amount it would need to pay to a willing, able and knowledgeable third party to assume the obligations under

AIGFP's super senior multi-sector credit default swap portfolio as of June 30, 2008.

Stress Testing/Sensitivity Analysis

At June 30, 2008, AIG used a roll rate analysis to stress the AIGFP super senior multi-sector CDO credit default swap portfolio for potential pre-tax realized credit losses that it may incur if the multi-sector CDO super senior credit default swap portfolio and the referenced obligations acquired by AIGFP in extinguishing its obligations under the swaps are held to maturity. Credit losses represent an estimate of the potential shortfall of principal and/or interest cash flows on the referenced obligations and credits underlying the portfolio that will not be recovered assuming the portfolio and referenced obligations are held to maturity. Two scenarios illustrated in this process resulted in potential pre-tax realized credit losses of approximately $5.0 billion (Scenario A) and approximately $8.5 billion (Scenario B). Actual ultimate realized credit losses are likely to vary, perhaps materially, from these scenarios, and there can be no assurance that the ultimate realized credit losses related to the AIGFP super senior multi-sector CDO credit default swap portfolio will be consistent with either scenario or that such realized credit losses will not exceed the potential realized credit losses illustrated by Scenario B.

In prior quarters, AIG conducted risk analyses of the AIGFP super senior multi-sector CDO credit default swap portfolio using certain ratings-based static stress tests, which centered around scenarios of further stress on the portfolio resulting from downgrades by the rating agencies from current levels on the underlying collateral in the CDO structures supported by AIGFP's credit default swaps. During the first quarter of 2008, AIG developed an additional methodology to conduct stress tests for potential realized credit losses from AIGFP's super senior multi-sector CDO credit default swap portfolio that combined a roll rate estimate of the losses emanating from the subprime and Alt-A RMBS collateral securities in the multi-sector CDOs, plus an estimate of losses arising from CDO securities (inner CDOs) and other ABS, such as CMBS, credit card and auto loan ABS, held by the CDOs. In conducting its risk analyses as of June 30, 2008, AIG discontinued use of the rating-based static stress test and used only the roll rate stress test because it believes that the roll rate stress test provides a more reasonable analysis methodology to illustrate potential realized credit losses than the rating-based static stress test used previously.

In the second quarter of 2008, AIG stressed the AIGFP super senior multi-sector CDO credit default swap portfolio using a roll rate analysis as applied to all RMBS collateral including subprime, Alt-A and prime residential mortgages that comprise the subprime, Alt-A and prime RMBS. This analysis assumed that certain percentages of actual delinquent mortgages will roll into default and foreclosure. It also assumed that certain percentages of non-delinquent mortgages will become delinquent and default over time, with those delinquency percentages depending on the age of the mortgage pool. To those assumed defaults AIG applied loss severities (one minus recovery) to derive estimated ultimate losses for each mortgage pool comprising a subprime, Alt-A and prime RMBS. Because subprime, Alt-A and prime RMBS have differing characteristics, the roll rates and loss severities differed. AIG then estimated tranche losses from these roll rate losses by applying the pool losses up through the capital structure of the RMBS. In this estimate of tranche losses, AIG introduced in the quarter an enhancement to the roll rate analysis to take into account the cash flow waterfall and to capture the potential effects, both positive and negative, of cash flow diversion within each CDO. To these estimated subprime, Alt-A and prime RMBS losses AIG added estimated credit losses on the inner CDOs and other ABS, such as CMBS, credit card and auto loan ABS, calculated by using rating-based static percentages, in the case of inner CDOs varying by vintage and type of CDO, and, in the case of other ABS, by rating. In addition to the foregoing, the analysis incorporates the effects of certain other factors such as mortgage prepayment rates, excess spread and delinquency triggers. The total of the roll rate losses and the losses on the inner CDOs and other ABS using two different scenarios of assumptions yielded estimated potential pre-tax realized credit losses of approximately $5.0 billion and approximately $8.5 billion.

At March 31, 2008, AIG's credit-based analyses estimated potential pre-tax realized credit losses at approximately $1.2 billion to $2.4 billion. The estimate of $2.4 billion was derived using the roll rate stress test described above. The increase in the estimated potential realized credit loss illustrated by Scenarios A and B was the result of both enhancements to the model and changes in the assumptions used. The model was enhanced by inclusion of prime RMBS into the portfolio of securities subjected to the roll rate analysis and the introduction of analytics to capture the potential effects of the cash flow waterfall. Changes in assumptions included revisions to the roll rate percentages and loss severities on subprime and Alt-A mortgages in view of deteriorating real estate market conditions, as well as a higher stress to other ABS collateral and the use of current inner CDO ratings in the rating-based static percentage. The potential realized credit loss illustrated by Scenario B is the result of applying different, more highly stressed assumptions to the roll rate analysis model than those used in Scenario A.

Due to the dislocation in the market for CDO and RMBS collateral, AIG does not use the market values of the underlying CDO collateral in estimating its potential realized credit losses. The use of factors derived from market-observable prices in models used to determine the estimates for future realized credit losses could result in materially higher estimates of potential realized credit losses.

Under the terms of most of these credit derivatives, credit losses to AIG would generally result from the credit

impairment of the referenced obligations that AIG would acquire in extinguishing its swap obligations. Based upon its most current analyses, AIG believes that any credit losses which may emerge over time at AIGFP will not be material to AIG's consolidated financial condition, but could be material to AIG's liquidity. Other types of analyses or models could result in materially different estimates. AIG is aware that other market participants have used different assumptions and methodologies to estimate the potential realized credit losses on AIGFP's super senior multi-sector CDO credit default swap portfolio, resulting in significantly higher estimates than those resulting from AIG's roll rate stress testing scenarios. Actual ultimate realized credit losses are likely to vary, perhaps materially, from AIG's roll rate stress testing scenarios, and there can be no assurance that the ultimate realized credit losses related to the AIGFP super senior multi-sector CDO credit default swap portfolio will be consistent with either scenario or that such realized credit losses will not exceed the potential realized credit losses illustrated by Scenario B.

The potential realized credit losses illustrated in Scenarios A and B are lower than the fair value of AIGFP's super senior multi-sector CDO credit default swap portfolio, a net loss of $26.1 billion at June 30, 2008. The net loss represents AIG's best estimate of the amount it would need to pay to a willing third party to assume the obligations under AIGFP's super senior multi-sector CDO credit default swap portfolio. The fair value of AIGFP's super senior multi-sector CDO credit default swap portfolio is based upon fair value accounting principles, which rely on third-party prices for both the underlying collateral securities and the CDOs that AIGFP's super senior credit default swaps wrap. These prices currently incorporate liquidity premiums, risk aversion elements and credit risk modeling, which in some instances may use more conservative assumptions than those used by AIG in its roll rate stress testing. Due to the ongoing disruption in the U.S. residential mortgage market and credit markets and the downgrades of RMBS and CDOs by the rating agencies, the market continues to lack transparency around the pricing of these securities. These prices are not necessarily reflective of the ultimate potential realized credit losses AIGFP could incur in the future related to the AIGFP super senior multi-sector CDO credit default swap portfolio, and AIG believes they incorporate a significant amount of market-driven risk aversion.

ITEM 3. Quantitative and Qualitative Disclosures About Market Risk

Included in Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations.

ITEM 4. Controls and Procedures

In connection with the preparation of this Quarterly Report on Form 10-Q, an evaluation was carried out by AIG's management, with the participation of AIG's Chief Executive Officer and Chief Financial Officer, of the effectiveness of AIG's disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934 (Exchange Act)). Disclosure controls and procedures are designed to ensure that information required to be disclosed in reports filed or submitted under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in SEC rules and forms and that such information is accumulated and communicated to management, including the Chief Executive Officer and Chief Financial Officer, to allow timely decisions regarding required disclosures. Solely as a result of the previously identified material weakness in internal control over the fair value valuation of the AIGFP super senior credit default swap portfolio and oversight thereof as described in the 2007 Annual Report on Form 10-K, AIG's Chief Executive Officer and Chief Financial Officer have concluded that, as of June 30, 2008, AIG's disclosure controls and procedures were ineffective. Notwithstanding the existence of this material weakness, AIG believes that the consolidated financial statements in this Quarterly Report on Form 10-Q fairly present, in all material respects, AIG's consolidated financial condition as of June 30, 2008 and December 31, 2007 and consolidated results of operations for the three- and six-month periods ended June 30, 2008 and 2007 and consolidated cash flows for the six-month periods ended June 30, 2008 and 2007, in conformity with GAAP. In addition, there has been no change in AIG's internal control over financial reporting (as defined in Rule 13a-15(f) under the Exchange Act) that occurred during the quarter ended June 30, 2008 that has materially affected, or is reasonably likely to materially affect, AIG's internal control over financial reporting.

Throughout 2008 and 2007, AIG recorded out of period adjustments, many of which were detected as part of continuing remediation efforts. It is AIG's policy to record all error corrections, without regard to materiality, and AIG has an established, formal process for the identification, evaluation and recording of all out of period adjustments. This process includes a heightened sensitivity for potential errors related to the internal control matters discussed in Item 9A. of the 2007 Annual Report on Form 10-K. AIG distinguishes error corrections from changes in estimates by evaluating the facts and circumstances of such items, including considering whether information was capable of being known at the time of original recording. AIG has evaluated the adjustments recorded in 2008 and 2007 from a qualitative and quantitative perspective and concluded that such adjustments are immaterial individually and in the aggregate to the current and prior periods.

Part II – OTHER INFORMATION

ITEM 2. Unregistered Sales of Equity Securities and Use of Proceeds

Information with respect to purchases of AIG Common stock during the three months ended June 30, 2008 was as follows:

Period	Total Number of Shares Purchased[(a)]	Average Price Paid per Share	Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs	Maximum Number of Shares that May Yet Be Purchased Under the Plans or Programs at End of Month[(b)]
April 1 - 30	3,832,276	$46.78	3,832,276	
May 1 - 31	—		—	
June 1 - 30	—		—	
Total	3,832,276	$46.78	3,832,276	

(a) Reflects date of delivery. Does not include 4,245 shares delivered or attested to in satisfaction of the exercise price by holders of AIG employee stock options exercised during the three months ended June 30, 2008.

(b) In February 2007, AIG's Board of Directors increased AIG's share repurchase program by authorizing the repurchase of shares with an aggregate purchase price of $8 billion. In November 2007, AIG's Board of Directors authorized the repurchase of an additional $8 billion in common stock. A balance of $9 billion remained for purchases under the program as of June 30, 2008. AIG does not expect to purchase additional shares under its share repurchase program for the foreseeable future.

ITEM 4. Submission of Matters to a Vote of Security Holders

At the Annual Meeting of Shareholders held on May 14, 2008, the Shareholders:

(a) Elected thirteen directors as follows:

Nominee	Shares For	Shares Withheld	Abstained
Stephen F. Bollenbach	1,685,779,934	501,561,929	63,124,235
Martin S. Feldstein	1,691,691,682	506,469,958	52,304,458
Ellen V. Futter	1,652,157,470	542,842,042	55,466,586
Richard C. Holbrooke	1,518,501,128	675,477,016	56,487,954
Fred H. Langhammer	1,675,419,092	541,328,771	33,718,235
George L. Miles, Jr.	1,496,407,272	717,640,163	36,418,663
Morris W. Offit	1,532,712,325	682,550,113	35,203,660
James F. Orr III	1,603,644,400	609,750,276	37,071,422
Virginia M. Rometty	1,653,815,644	542,266,335	54,384,119
Martin J. Sullivan	1,691,337,900	520,729,226	38,398,972
Michael H. Sutton	1,499,773,544	715,209,935	35,482,619
Edmund S.W. Tse	1,690,069,518	521,903,489	38,493,091
Robert B. Willumstad	1,658,750,176	556,048,522	35,667,400

There were no broker non-votes with respect to this item.

(b) Approved by a vote of 1,599,775,289 shares for and 616,864,546 shares against, with 33,826,263 shares abstaining, a proposal to ratify the selection of PricewaterhouseCoopers LLP as the independent registered public accounting firm for 2008. There were no broker non-votes with respect to this item.

(c) Rejected by a vote of 313,891,912 shares for and 1,363,468,866 shares against, with 391,665,309 shares abstaining and 181,440,011 broker non-votes, a shareholder proposal relating to the human right to water.

(d) Rejected by a vote of 347,720,077 shares for and 1,357,015,652 shares against, with 364,290,358 shares abstaining and 181,440,011 broker non-votes, a shareholder proposal relating to the reporting of political contributions.

ITEM 6. Exhibits

See accompanying Exhibit Index.

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

AMERICAN INTERNATIONAL GROUP, INC.
(Registrant)

/s/ STEVEN J. BENSINGER

Steven J. Bensinger
Vice Chairman — Financial Services and
Chief Financial Officer

/s/ DAVID L. HERZOG

David L. Herzog
Senior Vice President and Comptroller
Principal Accounting Officer

Dated: August 6, 2008

EXHIBIT INDEX

Exhibit Number	Description	Location
11	Statement re computation of per share earnings	Included in Note 4 of Notes to Consolidated Financial Statements.
12	Computation of ratios of earnings to fixed charges	Filed herewith.
31	Rule 13a-14(a)/15d-14(a) Certifications	Filed herewith.
32	Section 1350 Certifications	Filed herewith.

Exhibit 12

American International Group, Inc.
Computation of Ratios of Earnings to Fixed Charges

(in millions, except ratios)	Three Months Ended June 30, **2008**	2007	Six Months Ended June 30, **2008**	2007
Income (loss) before income taxes and minority interest	**$ (8,756)**	$ 6,328	**$(20,020)**	$12,500
Less – Equity income of less than 50% owned persons	**8**	49	**17**	91
Add – Dividends from less than 50% owned persons	**21**	25	**21**	25
	(8,743)	6,304	**(20,016)**	12,434
Add – Fixed charges	**2,901**	2,442	**5,093**	5,114
Less – Capitalized interest	**6**	9	**15**	20
Income (loss) before income taxes, minority interest and fixed charges	**$ (5,848)**	$ 8,737	**$(14,938)**	$17,528
Fixed charges:				
Interest costs	**$ 2,826**	$ 2,381	**$ 4,943**	$ 4,993
Rental expense[(a)]	**75**	61	**150**	121
Total fixed charges	**$ 2,901**	$ 2,442	**$ 5,093**	$ 5,114
Ratio of earnings to fixed charges	[(b)]	3.58	[(b)]	3.43
Secondary Ratio				
Interest credited to GIC and GIA policy and contract holders	**$ (1,594)**	$(1,268)	**$ (2,520)**	$ (2,847)
Total fixed charges excluding interest credited to GIC and GIA policy and contract holders	**$ 1,307**	$ 1,174	**$ 2,573**	$ 2,267
Secondary ratio of earnings to fixed charges	[(b)]	6.36	[(b)]	6.48

(a) The proportion considered representative of the interest factor.

(b) Earnings were inadequate to cover total fixed charges by $8,749 million and $20,031 million for the three- and six-month periods ended June 30, 2008. The coverage deficiency for total fixed charges excluding interest credited to GIC and GIA policy and contract holders was $7,155 million and $17,511 million for the three- and six-month periods ended June 30, 2008.

The secondary ratio is disclosed for the convenience of fixed income investors and the rating agencies that serve them and is more comparable to the ratios disclosed by all issuers of fixed maturity securities. The secondary ratio removes interest credited to guaranteed investment contract (GIC) policyholders and guaranteed investment agreement (GIA) contract holders. Such interest expenses are also removed from income (loss) before income taxes and minority interest used in this calculation. GICs and GIAs are entered into by AIG's insurance subsidiaries, principally SunAmerica Life Insurance Company and AIG Financial Products Corp. and its subsidiaries, respectively. The proceeds from GICs and GIAs are invested in a diversified portfolio of securities, primarily investment grade bonds. The assets acquired yield rates greater than the rates on the related policyholders obligation or agreement, with the intent of earning operating income from the spread.

Exhibit 31

CERTIFICATIONS

I, Robert B. Willumstad, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q of American International Group, Inc.;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:

(a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

(b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

(c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

(d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):

(a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

(b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

/s/ ROBERT B. WILLUMSTAD

Robert B. Willumstad
Chairman and Chief Executive Officer

Date: August 6, 2008

CERTIFICATIONS

I, Steven J. Bensinger, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q of American International Group, Inc.;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:

(a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

(b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

(c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

(d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):

(a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

(b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

/s/ STEVEN J. BENSINGER

Steven J. Bensinger
Vice Chairman — Financial Services and
Chief Financial Officer

Date: August 6, 2008

Exhibit 32

CERTIFICATION

In connection with the Quarterly Report on Form 10-Q of American International Group, Inc. (the "Company") for the quarter ended June 30, 2008, as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, Robert B. Willumstad, Chairman and Chief Executive Officer of the Company, certify, pursuant to 18 U.S.C. Section 1350, that to my knowledge:

1. The Report fully complies with the requirements of Section 13(a) or 15(d), as applicable, of the Securities Exchange Act of 1934; and

2. The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

/s/ ROBERT B. WILLUMSTAD

Robert B. Willumstad
Chairman and Chief Executive Officer

Date: August 6, 2008

The foregoing certification is being furnished solely pursuant to 18 U.S.C. Section 1350 and is not being filed as part of the Report or as a separate disclosure document.

CERTIFICATION

In connection with the Quarterly Report on Form 10-Q of American International Group, Inc. (the "Company") for the quarter ended June 30, 2008, as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, Steven J. Bensinger, Vice Chairman — Financial Services and Chief Financial Officer of the Company, certify, pursuant to 18 U.S.C. Section 1350, that to my knowledge:

1. The Report fully complies with the requirements of Section 13(a) or 15(d), as applicable, of the Securities Exchange Act of 1934; and

2. The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

/s/ STEVEN J. BENSINGER

Steven J. Bensinger
Vice Chairman — Financial Services and
Chief Financial Officer

Date: August 6, 2008

The foregoing certification is being furnished solely pursuant to 18 U.S.C. Section 1350 and is not being filed as part of the Report or as a separate disclosure document.

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

Form 10-Q

(Mark One)

☑ QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended September 30, 2008

or

☐ TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the transition period from to

Commission File Number 1-8787

American International Group, Inc.

(Exact name of registrant as specified in its charter)

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

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

Former name, former address and former fiscal year, if changed since last report: None

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

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

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

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes ☐ No ☑

As of October 31, 2008, there were 2,689,938,313 shares outstanding of the registrant's common stock.

TABLE OF CONTENTS

Part I – FINANCIAL INFORMATION

ITEM 1. Financial Statements (unaudited)

CONSOLIDATED BALANCE SHEET

(in millions) (unaudited)

	September 30, 2008	December 31, 2007
Assets:		
Investments and Financial Services assets:		
Fixed maturity securities:		
Bonds available for sale, at fair value (amortized cost: 2008 – $412,877; 2007 – $393,170)	**$ 394,494**	$ 397,372
Bonds held to maturity, at amortized cost (fair value: 2008 – $0; 2007 – $22,157)	**–**	21,581
Bond trading securities, at fair value	**7,552**	9,982
Equity securities:		
Common stocks available for sale, at fair value (cost: 2008 – $11,317; 2007 – $12,588)	**11,459**	17,900
Common and preferred stocks trading, at fair value	**20,674**	21,376
Preferred stocks available for sale, at fair value (cost: 2008 – $1,590; 2007 – $2,600)	**1,464**	2,370
Mortgage and other loans receivable, net of allowance (2008 – $90; 2007 – $77) (held for sale: 2008 – $26; 2007 – $377) (amount measured at fair value: 2008 – $328)	**33,724**	33,727
Financial Services assets:		
Flight equipment primarily under operating leases, net of accumulated depreciation (2008 – $11,812; 2007 – $10,499)	**43,561**	41,984
Securities available for sale, at fair value (cost: 2008 – $2,568; 2007 – $40,157)	**2,326**	40,305
Trading securities, at fair value	**36,136**	4,197
Spot commodities, at fair value	**34**	238
Unrealized gain on swaps, options and forward transactions, at fair value	**10,034**	12,318
Trade receivables	**4,617**	672
Securities purchased under agreements to resell, at fair value in 2008	**12,100**	20,950
Finance receivables, net of allowance (2008 – $1,290; 2007 – $878) (held for sale: 2008 – $26; 2007 – $233)	**32,590**	31,234
Securities lending invested collateral, at fair value (cost: 2008 – $41,336; 2007 – $80,641)	**41,511**	75,662
Other invested assets (amount measured at fair value: 2008 – $21,528; 2007 – $20,827)	**58,723**	58,823
Short-term investments (amount measured at fair value: 2008 – $22,590)	**52,484**	51,351
Total Investments and Financial Services assets	**763,483**	842,042
Cash	**18,570**	2,284
Investment income due and accrued	**7,008**	6,587
Premiums and insurance balances receivable, net of allowance (2008 – $582; 2007 – $662)	**19,106**	18,395
Reinsurance assets, net of allowance (2008 – $471; 2007 – $520)	**23,943**	23,103
Current and deferred income taxes	**14,833**	–
Deferred policy acquisition costs	**48,182**	43,914
Investments in partially owned companies	**591**	654
Real estate and other fixed assets, net of accumulated depreciation (2008 – $5,814; 2007 – $5,446)	**5,730**	5,518
Separate and variable accounts, at fair value	**65,472**	78,684
Goodwill	**10,334**	9,414
Other assets, including prepaid commitment asset of $24,204 in 2008 (amount measured at fair value: 2008 – $1,623; 2007 – $4,152)	**44,985**	17,766
Total assets	**$1,022,237**	$1,048,361

See Accompanying Notes to Consolidated Financial Statements.

CONSOLIDATED BALANCE SHEET *(continued)*

(in millions, except share data) (unaudited)

	September 30, 2008	December 31, 2007
Liabilities:		
Reserve for losses and loss expenses	**$ 90,877**	$ 85,500
Unearned premiums	**28,448**	27,703
Future policy benefits for life and accident and health insurance contracts	**146,802**	136,387
Policyholders' contract deposits (amount measured at fair value: 2008 – $4,282; 2007 – $295)	**259,792**	258,459
Other policyholders' funds	**13,940**	12,599
Commissions, expenses and taxes payable	**5,577**	6,310
Insurance balances payable	**5,428**	4,878
Funds held by companies under reinsurance treaties	**2,462**	2,501
Current and deferred income taxes	**–**	3,823
Financial Services liabilities:		
Securities sold under agreements to repurchase (amount measured at fair value: 2008 – $7,193)	**8,407**	8,331
Trade payables	**3,094**	6,445
Securities and spot commodities sold but not yet purchased, at fair value	**2,566**	4,709
Unrealized loss on swaps, options and forward transactions, at fair value	**6,325**	14,817
Trust deposits and deposits due to banks and other depositors (amount measured at fair value: 2008 – $215)	**5,946**	4,903
Commercial paper and extendible commercial notes	**5,600**	13,114
Federal Reserve Bank of New York credit facility	**62,960**	–
Other long-term borrowings (amount measured at fair value: 2008 – $39,149)	**155,990**	162,935
Separate and variable accounts	**65,472**	78,684
Securities lending payable	**42,800**	81,965
Minority interest	**11,713**	10,422
Other liabilities (amount measured at fair value: 2008 – $3,389; 2007 – $3,262)	**26,756**	27,975
Total liabilities	**950,955**	952,460
Preferred shareholders' equity in subsidiary companies	**100**	100
Commitments, contingencies and guarantees (See Note 7)		
Shareholders' equity:		
Common stock, $2.50 par value; 5,000,000,000 shares authorized; shares issued 2008 – 2,948,038,001; 2007 – 2,751,327,476	**7,370**	6,878
Additional paid-in capital	**32,501**	2,848
Payments advanced to purchase shares	**–**	(912)
Retained earnings	**49,291**	89,029
Accumulated other comprehensive income (loss)	**(9,480)**	4,643
Treasury stock, at cost; 2008 – 258,123,304; 2007 – 221,743,421 shares of common stock	**(8,500)**	(6,685)
Total shareholders' equity	**71,182**	95,801
Total liabilities, preferred shareholders' equity in subsidiary companies and shareholders' equity	**$1,022,237**	$1,048,361

See Accompanying Notes to Consolidated Financial Statements.

CONSOLIDATED STATEMENT OF INCOME (LOSS)

(in millions, except per share data) (unaudited)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2008	2007	**2008**	2007
Revenues:				
Premiums and other considerations	**$ 21,082**	$19,733	**$ 63,489**	$58,908
Net investment income	**2,946**	6,172	**14,628**	21,149
Net realized capital losses	**(18,312)**	(864)	**(30,482)**	(962)
Unrealized market valuation losses on AIGFP super senior credit default swap portfolio	**(7,054)**	(352)	**(21,726)**	(352)
Other income	**2,236**	5,147	**8,953**	12,888
Total revenues	**898**	29,836	**34,862**	91,631
Benefits and expenses:				
Incurred policy losses and benefits	**17,189**	15,595	**51,521**	47,962
Policy acquisition and other insurance expenses	**6,919**	5,357	**18,560**	15,508
Interest expense	**2,297**	1,232	**4,902**	3,425
Other expenses	**2,678**	2,773	**8,084**	7,357
Total benefits and expenses	**29,083**	24,957	**83,067**	74,252
Income (loss) before income taxes (benefits) and minority interest	**(28,185)**	4,879	**(48,205)**	17,379
Income taxes (benefits)	**(3,480)**	1,463	**(10,374)**	4,868
Income (loss) before minority interest	**(24,705)**	3,416	**(37,831)**	12,511
Minority interest	**237**	(331)	**201**	(1,019)
Net income (loss)	**$(24,468)**	$ 3,085	**$(37,630)**	$11,492
Earnings (loss) per common share:				
Basic	**$ (9.05)**	$ 1.20	**$ (14.40)**	$ 4.43
Diluted	**$ (9.05)**	$ 1.19	**$ (14.40)**	$ 4.40
Dividends declared per common share	**$ –**	$ 0.200	**$ 0.420**	$ 0.565
Weighted average shares outstanding:				
Basic	**2,703**	2,576	**2,613**	2,596
Diluted	**2,703**	2,589	**2,613**	2,609

See Accompanying Notes to Consolidated Financial Statements.

CONSOLIDATED STATEMENT OF SHAREHOLDERS' EQUITY

(in millions, except share and per share data) (unaudited)	Nine Months Ended September 30, 2008 Amounts	Shares
Common stock:		
Balance, beginning of period	$ 6,878	2,751,327,476
Issuances	492	196,710,525
Balance, end of period	7,370	2,948,038,001
Additional paid-in capital:		
Balance, beginning of period	2,848	
Excess of proceeds over par value of common stock issued	6,851	
Present value of future contract adjustment payments related to issuance of equity units	(431)	
Consideration received for preferred stock not yet issued	23,000	
Excess of cost over proceeds of common stock issued under stock plans	(80)	
Other	313	
Balance, end of period	32,501	
Payments advanced to purchase shares:		
Balance, beginning of period	(912)	
Payments advanced	(1,000)	
Shares purchased	1,912	
Balance, end of period	–	
Retained earnings:		
Balance, beginning of period	89,029	
Cumulative effect of accounting changes, net of tax	(1,003)	
Adjusted balance, beginning of period	88,026	
Net loss	(37,630)	
Dividends to common shareholders ($0.42 per share)	(1,105)	
Balance, end of period	49,291	
Accumulated other comprehensive income (loss):		
Unrealized appreciation (depreciation) of investments, net of tax:		
Balance, beginning of period	4,375	
Cumulative effect of accounting changes, net of tax	(105)	
Adjusted balance, beginning of period	4,270	
Unrealized appreciation (depreciation) on investments, net of reclassification adjustments	(20,874)	
Deferred income tax benefit	7,491	
Balance, end of period	(9,113)	
Foreign currency translation adjustments, net of tax:		
Balance, beginning of period	880	
Translation adjustment	(275)	
Deferred income tax expense	(304)	
Balance, end of period	301	
Net derivative gains (losses) arising from cash flow hedging activities, net of tax:		
Balance, beginning of period	(87)	
Net deferred gains on cash flow hedges, net of reclassification adjustments	2	
Deferred income tax expense	(1)	
Balance, end of period	(86)	
Retirement plan liabilities adjustment, net of tax:		
Balance, beginning of period	(525)	
Net actuarial loss	(47)	
Prior service credit	(9)	
Deferred income tax expense	(1)	
Balance, end of period	(582)	
Accumulated other comprehensive income (loss), end of period	(9,480)	
Treasury stock, at cost:		
Balance, beginning of period	(6,685)	(221,743,421)
Shares acquired	(1,912)	(37,927,125)
Issued under stock plans	24	1,545,316
Other	73	1,926
Balance, end of period	(8,500)	(258,123,304)
Total shareholders' equity, end of period	$ 71,182	

See Accompanying Notes to Consolidated Financial Statements.

CONSOLIDATED STATEMENT OF CASH FLOWS

(in millions) (unaudited)

	Nine Months Ended September 30, 2008	2007
Summary:		
Net cash provided by (used in) operating activities	**$ 2,182**	$ 27,549
Net cash provided by (used in) investing activities	**(7,460)**	(65,862)
Net cash provided by (used in) financing activities	**21,559**	38,964
Effect of exchange rate changes on cash	**5**	8
Change in cash	**16,286**	659
Cash at beginning of period	**2,284**	1,590
Cash at end of period	**$ 18,570**	$ 2,249
Cash flows from operating activities:		
Net income (loss)	**$(37,630)**	$ 11,492
Adjustments to reconcile net income (loss) to net cash provided by operating activities:		
Noncash revenues, expenses, gains and losses included in income (loss):		
Unrealized market valuation losses on AIGFP super senior credit default swap portfolio	**$ 21,726**	$ 352
Net (gains) losses on sales of securities available for sale and other assets	**2**	(1,110)
Foreign exchange transaction (gains) losses	**(1,409)**	1,214
Net unrealized (gains) losses on non-AIGFP derivatives and other assets and liabilities	**5,779**	(103)
Equity in (income) loss of partially owned companies and other invested assets	**2,000**	(3,336)
Amortization of deferred policy acquisition costs	**10,645**	9,115
Depreciation and other amortization	**2,727**	2,984
Provision for mortgage, other loans and finance receivables	**955**	391
Other-than-temporary impairments	**32,246**	1,413
Impairments of goodwill and other assets	**632**	–
Amortization of costs related to Federal Reserve Bank of New York credit facility	**802**	–
Changes in operating assets and liabilities:		
General and life insurance reserves	**14,834**	12,127
Premiums and insurance balances receivable and payable – net	**(396)**	515
Reinsurance assets	**(863)**	561
Capitalization of deferred policy acquisition costs	**(12,710)**	(11,684)
Investment income due and accrued	**(398)**	(538)
Funds held under reinsurance treaties	**(49)**	(166)
Other policyholders' funds	**1,206**	746
Income taxes receivable and payable – net	**(10,935)**	707
Commissions, expenses and taxes payable	**155**	1,110
Other assets and liabilities – net	**(1,084)**	1,674
Trade receivables and payables – net	**(7,297)**	(2,546)
Trading securities	**1,729**	2,002
Spot commodities	**204**	105
Net unrealized (gain) loss on swaps, options and forward transactions (net of collateral)	**(28,191)**	1,707
Securities purchased under agreements to resell	**8,831**	(6,898)
Securities sold under agreements to repurchase	**41**	3,686
Securities and spot commodities sold but not yet purchased	**(2,154)**	660
Finance receivables and other loans held for sale – originations and purchases	**(346)**	(4,735)
Sales of finance receivables and other loans – held for sale	**545**	5,119
Other, net	**585**	985
Total adjustments	**39,812**	16,057
Net cash provided by operating activities	**$ 2,182**	$ 27,549

See Accompanying Notes to Consolidated Financial Statements.

CONSOLIDATED STATEMENT OF CASH FLOWS *(continued)*

(in millions) (unaudited)

	Nine Months Ended September 30, 2008	2007
Cash flows from investing activities:		
Proceeds from (payments for)		
Sales and maturities of fixed maturity securities available for sale and hybrid investments	**$ 65,584**	$ 96,737
Sales of equity securities available for sale	**8,117**	6,700
Proceeds from fixed maturity securities held to maturity	**126**	175
Sales of trading securities	**19,348**	–
Sales of flight equipment	**430**	95
Sales or distributions of other invested assets	**11,840**	9,298
Payments received on mortgage and other loans receivable	**4,809**	4,170
Principal payments received on finance receivables held for investment	**9,731**	9,554
Purchases of fixed maturity securities available for sale and hybrid investments	**(75,938)**	(108,879)
Purchases of equity securities available for sale	**(7,701)**	(8,438)
Purchases of fixed maturity securities held to maturity	**(88)**	(154)
Purchases of trading securities	**(20,488)**	–
Purchases of flight equipment (including progress payments)	**(3,200)**	(3,925)
Purchases of other invested assets	**(16,030)**	(20,677)
Mortgage and other loans receivable issued	**(4,939)**	(7,354)
Finance receivables held for investment – originations and purchases	**(11,697)**	(11,394)
Change in securities lending invested collateral	**20,245**	(18,723)
Net additions to real estate, fixed assets, and other assets	**(1,034)**	(1,004)
Net change in short-term investments	**(6,116)**	(11,764)
Net change in non-AIGFP derivative assets and liabilities	**(459)**	(279)
Net cash used in investing activities	**$ (7,460)**	$ (65,862)
Cash flows from financing activities:		
Proceeds from (payments for)		
Policyholders' contract deposits	**$ 46,446**	$ 45,766
Policyholders' contract withdrawals	**(42,381)**	(43,574)
Change in other deposits	**747**	(446)
Change in commercial paper and extendible commercial notes	**(7,540)**	2,526
Other long-term borrowings issued	**111,558**	72,039
Federal Reserve Bank of New York credit facility borrowings	**61,000**	–
Repayments on other long-term borrowings	**(114,051)**	(49,643)
Change in securities lending payable	**(39,127)**	18,156
Proceeds from common stock issued	**7,343**	–
Issuance of treasury stock	**9**	204
Payments advanced to purchase shares	**(1,000)**	(5,000)
Cash dividends paid to shareholders	**(1,629)**	(1,372)
Acquisition of treasury stock	**–**	(16)
Other, net	**184**	324
Net cash provided by financing activities	**$ 21,559**	$ 38,964
Supplementary disclosure of cash flow information:		
Cash paid (received) during the period for:		
Interest	**$ 4,953**	$ 6,190
Taxes	**$ 562**	$ 4,044
Non-cash financing activities:		
Consideration received for preferred stock not yet issued	**$ 23,000**	–
Interest credited to policyholder accounts included in financing activities	**$ 5,737**	$ 7,553
Treasury stock acquired using payments advanced to purchase shares	**$ 1,912**	$ 3,725
Present value of future contract adjustment payments related to issuance of equity units	**$ 431**	$ –
Non-cash investing activities:		
Debt assumed on acquisitions and warehoused investments	**$ 153**	$ 358
Liability related to purchase of additional interest in 21st Century	**$ –**	$ 759

See Accompanying Notes to Consolidated Financial Statements.

CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME (LOSS)

(in millions) (unaudited)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2008	2007	**2008**	2007
Net income (loss)	**$(24,468)**	$ 3,085	**$(37,630)**	$11,492
Other comprehensive income (loss):				
Cumulative effect of accounting changes	**–**	–	**(162)**	–
Deferred income tax benefit on above changes	**–**	–	**57**	–
Unrealized (depreciation) appreciation of investments – net of reclassification adjustments	**(6,620)**	(3,394)	**(20,874)**	(4,246)
Deferred income tax benefit on above changes	**2,678**	941	**7,491**	1,081
Foreign currency translation adjustments	**(1,383)**	619	**(275)**	290
Deferred income tax benefit (expense) on above changes	**(180)**	(109)	**(304)**	(74)
Net derivative gains (losses) arising from cash flow hedging activities – net of reclassification adjustments	**(9)**	(93)	**2**	(31)
Deferred income tax benefit on above changes	**4**	34	**(1)**	39
Change in pension and postretirement unrecognized periodic benefit	**(69)**	17	**(56)**	35
Deferred income tax benefit (expense) on above changes	**2**	(8)	**(1)**	(10)
Other comprehensive income (loss)	**(5,577)**	(1,993)	**(14,123)**	(2,916)
Comprehensive income (loss)	**$(30,045)**	$ 1,092	**$(51,753)**	$ 8,576

See Accompanying Notes to Consolidated Financial Statements.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited)*

1. Summary of Significant Accounting Policies

Basis of Presentation

These unaudited condensed consolidated financial statements do not include all disclosures required by accounting principles generally accepted in the United States (GAAP) for complete financial statements and should be read in conjunction with the audited consolidated financial statements and the related notes included in the Annual Report on Form 10-K of American International Group, Inc. (AIG) for the year ended December 31, 2007 (2007 Annual Report on Form 10-K).

In the opinion of management, these consolidated financial statements contain the normal recurring adjustments necessary for a fair statement of the results presented herein. All material intercompany accounts and transactions have been eliminated.

Going Concern Considerations

During the third quarter of 2008, requirements to post collateral in connection with AIGFP's credit default swap (CDS) portfolio and other AIGFP transactions and to fund returns of securities lending collateral placed stress on AIG's liquidity. AIG's stock price declined from $22.76 on September 8, 2008 to $4.76 on September 15, 2008. On that date, AIG's long-term debt ratings were downgraded by Standard & Poor's, a division of The McGraw-Hill Companies, Inc. (S&P), Moody's Investors Service (Moody's) and Fitch Ratings (Fitch), which triggered additional requirements for liquidity. These and other events severely limited AIG's access to debt and equity markets.

On September 22, 2008, AIG entered into an $85 billion revolving credit agreement (the Fed Credit Agreement) with the Federal Reserve Bank of New York (the NY Fed) and, pursuant to the Fed Credit Agreement, AIG agreed to issue 100,000 shares of Series C Perpetual, Convertible, Participating Preferred Stock (the Series C Preferred Stock) to a trust for the benefit of the United States Treasury (the Trust) (see Notes 4 and 5 to the Consolidated Financial Statements). At September 30, 2008, amounts owed under the facility created pursuant to the Fed Credit Agreement (the Fed Facility) totaled $63 billion, including accrued fees and interest.

Since September 30, 2008, AIG has borrowed additional amounts under the Fed Facility and has announced plans to sell assets and businesses to repay amounts owed in connection with the Fed Credit Agreement. In addition, subsequent to September 30, 2008, certain of AIG's domestic life insurance subsidiaries entered into an agreement with the NY Fed pursuant to which the NY Fed has borrowed, in return for cash collateral, investment grade fixed maturity securities from the insurance subsidiaries. As described in Note 11 to the Consolidated Financial Statements, AIG announced on November 10, 2008 that it had entered into an agreement in principle as part of the Troubled Asset Relief Program (TARP) pursuant to which the United States Treasury will purchase from AIG $40 billion liquidation preference of newly issued perpetual preferred stock and a 10-year warrant exercisable for shares of AIG common stock equal to 2% of the outstanding shares of common stock, and that the NY Fed and AIG had agreed to amend the Fed Credit Agreement to reduce the interest rate on outstanding borrowings and undrawn amounts, extend the term from two years to five years, reduce the number of shares of common stock of AIG to be issued upon conversion of the Series C Preferred Stock held by the Trust so that the government's overall interest will not exceed 79.9 percent and revise the total amount available under the Fed Facility. In addition, four AIG affiliates are participating in the NY Fed's Commercial Paper Funding Facility (CPFF). AIG also has announced its intention to enter into other agreements with the NY Fed to limit AIG's future liquidity exposures to the multi-sector credit default swap portfolio and securities lending programs.

In assessing AIG's current financial position and developing operating plans for the future, management has made significant judgments and estimates with respect to the potential financial and liquidity effects of AIG's risks and uncertainties, including but not limited to:

- the potential adverse effects on AIG's businesses that could result if there are further downgrades by rating agencies, including in particular, the uncertainty in estimating, for the super senior credit default swaps, both the number of counterparties who may elect to terminate under contractual termination provisions and the amount that would be required to be paid in the event of a downgrade;
- the potential for continued declines in bond and equity markets; and
- the potential effect on AIG if the capital levels of its regulated and unregulated subsidiaries prove inadequate to support current business plans; and
- the effect on AIG's businesses of continued compliance with the covenants of the Fed Credit Agreement.

Based on the agreement in principle, management's plans to stabilize AIG's businesses and dispose of its non-core assets, and after consideration of the risks and uncertainties to such plans, management believes that it will have adequate liquidity to finance and operate AIG's businesses, execute its disposition plan and repay its obligations for at least the next twelve months.

It is possible that the actual outcome of one or more of management's plans could be materially different, or that one

1. Summary of Significant Accounting Policies *(continued)*

or more of management's significant judgments or estimates about the potential effects of the risks and uncertainties could prove to be materially incorrect or that the agreements in principle disclosed in Note 11 to the Consolidated Financial Statements (and as discussed below) do not result in completed transactions. If one or more of these possible outcomes were realized, AIG may not have sufficient cash to meet its obligations. If AIG needs funds in excess of amounts available from the sources described below, AIG would need to find additional financing and, if such additional financing were to be unavailable, there could exist substantial doubt about AIG's ability to continue as a going concern.

AIG's consolidated financial statements have been prepared on a going concern basis, which contemplates the realization of assets and the satisfaction of liabilities in the normal course of business. These consolidated financial statements do not include any adjustments relating to the recoverability and classification of recorded assets nor relating to the amounts and classification of liabilities that may be necessary should we be unable to continue as a going concern.

Investment Pricing

Certain of AIG's foreign subsidiaries included in the consolidated financial statements report on a fiscal period ended August 31. The effect on AIG's consolidated financial condition and results of operations of all material events occurring between August 31 and September 30 for all periods presented has been recorded. AIG determined the significant and rapid world-wide market decline in September 2008 to be an intervening event that had a material effect on its consolidated financial position and results of operations. AIG reflected this recent market decline throughout its investment portfolio. Accordingly, AIG recorded $1.3 billion ($845 million after tax) of hedge and mutual fund investment losses in net investment income, $1.1 billion ($910 million after tax) of other than temporary impairment charges, and $5.4 billion ($3.2 billion after tax) of unrealized depreciation on investments.

Revisions and Reclassifications

During the third quarter of 2008, AIG began reporting interest expense and other expenses separately on the consolidated statement of income (loss). Interest expense represents interest expense on short-term and long-term borrowings. Other expenses represent all other expenses not separately disclosed on the consolidated statement of income (loss). Prior period amounts were revised to conform to the current period presentation.

In the second quarter of 2008, AIG determined that certain accident and health contracts in its Foreign General Insurance reporting unit, which were previously accounted for as short duration contracts, should be treated as long duration insurance products. Accordingly, the December 31, 2007 consolidated balance sheet has been revised to reflect the reclassification of $763 million of deferred direct response advertising costs, previously reported in other assets, to deferred policy acquisition costs (DAC). Additionally, $320 million has been reclassified in the consolidated balance sheet as of December 31, 2007 from unearned premiums to future policy benefits for life and accident and health insurance contracts. These revisions did not have a material effect on AIG's consolidated income before income taxes, net income, or shareholders' equity for any period presented.

See Recent Accounting Standards — Accounting Changes below for a discussion of AIG's adoption of the Financial Accounting Standards Board (FASB) Staff Position (FSP) FASB Interpretation No. (FIN) 39-1, "Amendment of FASB Interpretation No. 39" (FSP FIN 39-1).

Certain other reclassifications and format changes have been made to prior period amounts to conform to the current period presentation.

Fixed Maturity Securities, Held to Maturity — Change in Intent

During the third quarter of 2008, AIG transferred all securities previously classified as held to maturity to available for sale. As a result of the continuing disruption in the credit markets during the third quarter of 2008, AIG changed its intent to hold to maturity certain tax-exempt municipal securities held by its insurance subsidiaries, which comprised substantially all of AIG's held to maturity securities. This change in intent resulted from a change in certain subsidiaries' investment strategies to increase their allocations to taxable securities, reflecting AIG's net operating loss position. As of September 30, 2008, the securities had a carrying value of $20.8 billion and a net unrealized loss of $752 million. No securities previously classified as held to maturity were sold during the third quarter.

Recent Accounting Standards

Accounting Changes

FAS 157

In September 2006, the FASB issued Statement of Financial Accounting Standards (FAS) No. 157, "Fair Value Measurements" (FAS 157). FAS 157 defines fair value, establishes a framework for measuring fair value and expands disclosure requirements regarding fair value measurements but does not change existing guidance about whether an asset or liability is

1. Summary of Significant Accounting Policies *(continued)*

carried at fair value. FAS 157 nullifies the guidance in Emerging Issues Task Force (EITF) Issue No. 02-3, "Issues Involved in Accounting for Derivative Contracts Held for Trading Purposes and Contracts Involved in Energy Trading and Risk Management Activities," (EITF 02-3) that precluded the recognition of a trading profit at the inception of a derivative contract unless the fair value of such contract was obtained from a quoted market price or other valuation technique incorporating observable market data. FAS 157 also clarifies that an issuer's credit standing should be considered when measuring liabilities at fair value. The fair value measurement and related disclosure guidance in FAS 157 do not apply to fair value measurements associated with AIG's share-based employee compensation awards accounted for in accordance with FAS 123(R), "Share-Based Payment."

AIG adopted FAS 157 on January 1, 2008, its required effective date. FAS 157 must be applied prospectively, except for certain stand-alone derivatives and hybrid instruments initially measured using the guidance in EITF 02-3, which must be applied as a cumulative effect accounting change to retained earnings at January 1, 2008. The cumulative effect, net of taxes, of adopting FAS 157 on AIG's consolidated balance sheet was an increase in retained earnings of $4 million.

The most significant effect of adopting FAS 157 on AIG's consolidated results of operations for the three- and nine-month periods ended September 30, 2008 related to changes in fair value methodologies with respect to both liabilities already carried at fair value, primarily hybrid notes and derivatives, and newly elected liabilities measured at fair value (see FAS 159 discussion below). Specifically, the incorporation of AIG's own credit spreads and the incorporation of explicit risk margins (embedded policy derivatives at transition only) resulted in a increase in pre-tax income of $2.4 billion ($1.5 billion after tax) and an increase in pre-tax income of $5.0 billion ($3.2 billion after tax) for the three- and nine-month periods ended September 30, 2008, respectively. The effects of the changes in AIG's own credit spreads on pre-tax income for AIG Financial Products Corp. and AIG Trading Group Inc. and their respective subsidiaries (AIGFP) were increases of $1.3 billion and $3.8 billion for the three- and nine-month periods ended September 30, 2008, respectively. The effect of the changes in counterparty credit spreads for assets measured at fair value at AIGFP were decreases in pre-tax income of $2.3 billion and $5.3 billion for the three- and nine-month periods ended September 30, 2008, respectively.

See Note 3 to the Consolidated Financial Statements for additional FAS 157 disclosures.

FAS 159

In February 2007, the FASB issued FAS 159, "The Fair Value Option for Financial Assets and Financial Liabilities" (FAS 159). FAS 159 permits entities to choose to measure at fair value many financial instruments and certain other items that are not required to be measured at fair value. Subsequent changes in fair value for designated items are required to be reported in income. FAS 159 also establishes presentation and disclosure requirements for similar types of assets and liabilities measured at fair value. FAS 159 permits the fair value option election on an instrument-by-instrument basis for eligible items existing at the adoption date and at initial recognition of an asset or liability, or upon most events that give rise to a new basis of accounting for that instrument.

AIG adopted FAS 159 on January 1, 2008, its required effective date. The adoption of FAS 159 with respect to elections made in the Life Insurance & Retirement Services segment resulted in an after-tax decrease to 2008 opening retained earnings of $559 million. The adoption of FAS 159 with respect to elections made by AIGFP resulted in an after-tax decrease to 2008 opening retained earnings of $448 million. Included in this amount are net unrealized gains of $105 million that were reclassified to retained earnings from accumulated other comprehensive income (loss) related to available for sale securities recorded in the consolidated balance sheet at January 1, 2008 for which the fair value option was elected.

See Note 3 to the Consolidated Financial Statements for additional FAS 159 disclosures.

FAS 157 and FAS 159

The following table summarizes the after-tax increase (decrease) from adopting FAS 157 and FAS 159 on the opening shareholders' equity accounts at January 1, 2008:

	At January 1, 2008		
(in millions)	Accumulated Other Comprehensive Income/(Loss)	Retained Earnings	Cumulative Effect of Accounting Changes
FAS 157	$ –	$ 4	$ 4
FAS 159	(105)	(1,007)	(1,112)
Cumulative effect of accounting changes	$(105)	$(1,003)	$(1,108)

FSP FIN 39-1

In April 2007, the FASB issued FSP FIN 39-1, which modifies FASB Interpretation (FIN) No. 39, "Offsetting of Amounts Related to Certain Contracts," and permits companies to offset cash collateral receivables or payables against derivative instruments under certain circumstances. AIG adopted the provisions of FSP FIN 39-1 effective January 1, 2008, which

1. Summary of Significant Accounting Policies *(continued)*

requires retrospective application to all prior periods presented. At September 30, 2008, the amounts of cash collateral received and posted that were offset against net derivative positions totaled $6.5 billion and $33.1 billion, respectively. The cash collateral received and paid related to AIGFP derivative instruments was previously recorded in both trade payables and trade receivables. Cash collateral received related to non-AIGFP derivative instruments was previously recorded in other liabilities. Accordingly, the derivative assets and liabilities at December 31, 2007 have been reduced by $6.3 billion and $5.8 billion, respectively, related to the netting of cash collateral.

FSP FAS 157-3

In October 2008, the FASB issued FSP FAS 157-3, "Determining the Fair Value of a Financial Asset When the Market for That Asset Is Not Active" (FSP FAS 157-3). FSP FAS 157-3 provides guidance clarifying certain aspects of FAS 157 with respect to the fair value measurements of a security when the market for that security is inactive. AIG adopted this guidance in the third quarter of 2008. The effects of adopting FSP FAS 157-3 on AIG's consolidated financial condition and results of operations were not material.

Future Application of Accounting Standards

FAS 141(R)

In December 2007, the FASB issued FAS 141 (revised 2007), "Business Combinations" (FAS 141(R)). FAS 141(R) changes the accounting for business combinations in a number of ways, including broadening the transactions or events that are considered business combinations; requiring an acquirer to recognize 100 percent of the fair value of assets acquired, liabilities assumed, and noncontrolling (i.e., minority) interests; recognizing contingent consideration arrangements at their acquisition-date fair values with subsequent changes in fair value generally reflected in income; and recognizing preacquisition loss and gain contingencies at their acquisition-date fair values, among other changes.

AIG is required to adopt FAS 141(R) for business combinations for which the acquisition date is on or after January 1, 2009. Early adoption is prohibited.

FAS 160

In December 2007, the FASB issued FAS 160, "Noncontrolling Interests in Consolidated Financial Statements, an amendment of ARB No. 51" (FAS 160). FAS 160 requires noncontrolling (i.e., minority) interests in partially owned consolidated subsidiaries to be classified in the consolidated balance sheet as a separate component of consolidated shareholders' equity. FAS 160 also establishes accounting rules for subsequent acquisitions and sales of noncontrolling interests and provides for how noncontrolling interests should be presented in the consolidated statement of income. The noncontrolling interests' share of subsidiary income should be reported as a part of consolidated net income with disclosure of the attribution of consolidated net income to the controlling and noncontrolling interests on the face of the consolidated statement of income.

AIG is required to adopt FAS 160 on January 1, 2009 and early application is prohibited. FAS 160 must be adopted prospectively, except that noncontrolling interests should be reclassified from liabilities to a separate component of shareholders' equity and consolidated net income should be recast to include net income attributable to both the controlling and noncontrolling interests retrospectively. AIG is currently assessing the effect that adopting FAS 160 will have on its consolidated financial statements.

FAS 161

In March 2008, the FASB issued FAS 161, "Disclosures about Derivative Instruments and Hedging Activities — an amendment of FASB Statement No. 133" (FAS 161). FAS 161 requires enhanced disclosures about (a) how and why AIG uses derivative instruments, (b) how derivative instruments and related hedged items are accounted for under FAS No. 133, "Accounting for Derivative Instruments and Hedging Activities" (FAS 133), and its related interpretations, and (c) how derivative instruments and related hedged items affect AIG's consolidated financial condition, results of operations, and cash flows. FAS 161 is effective for AIG beginning with financial statements issued in the first quarter of 2009. Because FAS 161 only requires additional disclosures about derivatives, it will have no effect on AIG's consolidated financial condition, results of operations or cash flows.

FAS 162

In May 2008, the FASB issued FAS 162, "The Hierarchy of Generally Accepted Accounting Principles" (FAS 162). FAS 162 identifies the sources of accounting principles and the framework for selecting the principles to be used in the preparation of financial statements presented in conformity with GAAP but does not change current practices. FAS 162 will become effective on the 60th day following Securities and Exchange Commission (SEC) approval of the Public Company Accounting Oversight Board amendments to remove GAAP hierarchy from the auditing standards. FAS 162 will have no effect on AIG's consolidated financial condition, results of operations or cash flows.

FSP FAS 140-3

In February 2008, the FASB issued FSP No. FAS 140-3, "Accounting for Transfers of Financial Assets and Repurchase

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

1. Summary of Significant Accounting Policies *(continued)*

Financing Transactions" (FSP FAS 140-3). FSP FAS 140-3 requires an initial transfer of a financial asset and a repurchase financing that was entered into contemporaneously with or in contemplation of the initial transfer to be evaluated as a linked transaction unless certain criteria are met. FSP FAS 140-3 is effective for AIG beginning January 1, 2009 and will be applied to new transactions entered into from that date forward. Early adoption is prohibited. AIG is currently assessing the effect that adopting FSP FAS 140-3 will have on its consolidated financial statements but does not believe the effect will be material.

FSP FAS 133-1 and FIN 45-4

In September 2008, the FASB issued FASB Staff Position No. FAS 133-1 and FIN 45-4, "Disclosures about Credit Derivatives and Certain Guarantees: An amendment of FASB Statement No. 133 and FASB Interpretation No. 45" (FSP). The FSP amends FAS 133 to require additional disclosures by sellers of credit derivatives, including derivatives embedded in a hybrid instrument. The FSP also amends FIN No. 45, "Guarantor's Accounting and Disclosure Requirement for Guarantees, Including Indirect Guarantees of Indebtedness of Others", to require an additional disclosure about the current status of the payment/performance risk of a guarantee. The FSP is effective for AIG beginning with the year-end 2008 financial statements. Because the FSP only requires additional disclosures about credit derivatives and guarantees, it will have no effect on AIG's consolidated financial condition, results of operations or cash flows.

2. Segment Information

AIG identifies its operating segments by product line consistent with its management structure. These segments are General Insurance, Life Insurance & Retirement Services, Financial Services, and Asset Management.

AIG's operations by operating segment were as follows:

Operating Segments *(in millions)*	Three Months Ended September 30, **2008**	2007	Nine Months Ended September 30, **2008**	2007
Total revenues[(a)]:				
General Insurance	**$ 10,808**	$12,758	**$ 35,854**	$38,589
Life Insurance & Retirement Services	**(4,642)**	12,632	**14,271**	40,337
Financial Services	**(5,851)**	2,785	**(16,016)**	7,109
Asset Management	**10**	1,519	**658**	4,969
Other	**451**	13	**531**	407
Consolidation and eliminations	**122**	129	**(436)**	220
Total	**$ 898**	$29,836	**$ 34,862**	$91,631
Operating income (loss)[(a)]:				
General Insurance	**$ (2,557)**	$ 2,439	**$ (393)**	$ 8,511
Life Insurance & Retirement Services	**(15,329)**	1,999	**(19,561)**	6,900
Financial Services	**(8,203)**	669	**(22,880)**	1,008
Asset Management	**(1,144)**	121	**(2,709)**	1,806
Other[(b)]	**(1,416)**	(627)	**(2,899)**	(1,557)
Consolidation and eliminations	**464**	278	**237**	711
Total	**$(28,185)**	$ 4,879	**$(48,205)**	$17,379

(a) To better align financial reporting with the manner in which AIG's chief operating decision maker manages the business, beginning in the third quarter of 2008, AIG's own credit risk valuation adjustments on intercompany transactions are excluded from segment revenues and operating income.

(b) Includes AIG parent and other operations that are not required to be reported separately. The following table presents the operating loss for AIG's Other category:

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

2. Segment Information *(continued)*

Other *(in millions)*	Three Months Ended September 30, **2008**	2007	Nine Months Ended September 30, **2008**	2007
Operating income (loss):				
Equity earnings in partially owned companies	**$ (13)**	$ 37	**$ 3**	$ 128
Interest expense on Fed Facility	**(802)**	–	**(802)**	–
Other interest expense	**(571)**	(315)	**(1,391)**	(869)
Unallocated corporate expenses	**(154)**	(166)	**(529)**	(548)
Net realized capital gains (losses)	**139**	(199)	**(96)**	(226)
Other miscellaneous, net	**(15)**	16	**(84)**	(42)
Total Other	**$(1,416)**	$(627)	**$(2,899)**	$(1,557)

AIG's General Insurance operations by major internal reporting unit were as follows:

General Insurance *(in millions)*	Three Months Ended September 30, **2008**	2007	Nine Months Ended September 30, **2008**	2007
Total revenues:				
Commercial Insurance	**$ 5,105**	$ 6,736	**$17,029**	$20,731
Transatlantic	**961**	1,088	**3,183**	3,253
Personal Lines	**1,207**	1,252	**3,718**	3,688
Mortgage Guaranty	**300**	267	**911**	772
Foreign General Insurance	**3,224**	3,413	**10,991**	10,150
Reclassifications and eliminations	**11**	2	**22**	(5)
Total	**$10,808**	$12,758	**$35,854**	$38,589
Operating income (loss):				
Commercial Insurance	**$ (1,109)**	$ 1,829	**$ 57**	$ 5,662
Transatlantic	**(155)**	189	**148**	508
Personal Lines	**23**	28	**47**	252
Mortgage Guaranty	**(1,118)**	(216)	**(1,990)**	(289)
Foreign General Insurance	**(209)**	607	**1,323**	2,383
Reclassifications and eliminations	**11**	2	**22**	(5)
Total	**$ (2,557)**	$ 2,439	**$ (393)**	$ 8,511

AIG's Life Insurance & Retirement Services operations by major internal reporting unit were as follows:

Life Insurance & Retirement Services *(in millions)*	Three Months Ended September 30, **2008**	2007	Nine Months Ended September 30, **2008**	2007
Total revenues:				
Foreign:				
Japan and Other	**$ 2,566**	$ 4,315	**$ 11,831**	$13,948
Asia	**1,812**	4,695	**10,664**	14,205
Domestic:				
Domestic Life Insurance	**(1,704)**	2,185	**813**	7,065
Domestic Retirement Services	**(7,316)**	1,437	**(9,037)**	5,119
Total	**$ (4,642)**	$12,632	**$ 14,271**	$40,337
Operating income (loss):				
Foreign:				
Japan and Other	**$ (1,074)**	$ 1,030	**$ (14)**	$ 2,753
Asia	**(1,419)**	706	**(971)**	1,921
Domestic:				
Domestic Life Insurance	**(3,911)**	61	**(5,786)**	774
Domestic Retirement Services	**(8,925)**	202	**(12,790)**	1,452
Total	**$(15,329)**	$ 1,999	**$(19,561)**	$ 6,900

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

2. Segment Information *(continued)*

AIG's Financial Services operations by major internal reporting unit were as follows:

Financial Services *(in millions)*	Three Months Ended September 30, **2008**	2007	Nine Months Ended September 30, **2008**	2007
Total revenues:				
Aircraft Leasing	**$ 1,367**	$1,237	**$ 3,830**	$3,468
Capital Markets	**(8,337)**	540	**(23,168)**	701
Consumer Finance	**1,029**	940	**2,988**	2,696
Other, including intercompany adjustments	**90**	68	**334**	244
Total	**$(5,851)**	$2,785	**$(16,016)**	$7,109
Operating income (loss):				
Aircraft Leasing	**$ 366**	$ 254	**$ 921**	$ 625
Capital Markets	**(8,073)**	370	**(23,284)**	183
Consumer Finance	**(474)**	69	**(559)**	180
Other, including intercompany adjustments	**(22)**	(24)	**42**	20
Total	**$(8,203)**	$ 669	**$(22,880)**	$1,008

AIG's Asset Management operations consist of a single internal reporting unit.

3. Fair Value Measurements

Effective January 1, 2008 AIG adopted FAS 157 and FAS 159, which specify measurement and disclosure standards related to assets and liabilities measured at fair value. See Note 1 to the Consolidated Financial Statements for additional information.

The most significant effect of adopting FAS 157 on AIG's results of operations for the three- and nine-month periods ended September 30, 2008 related to changes in fair value methodologies with respect to both liabilities already carried at fair value, primarily hybrid notes and derivatives, and newly elected liabilities measured at fair value (see FAS 159 discussion below). Specifically, the incorporation of AIG's own credit spreads and the incorporation of explicit risk margins (embedded policy derivatives at transition only) resulted in a increase of $2.4 billion to pre-tax income ($1.5 billion after tax) and an increase of $5.0 billion to pre-tax income ($3.2 billion after tax) for the three- and nine-month periods ended September 30, 2008, respectively, as follows:

(in millions)	Net Pre-Tax Increase (Decrease) Three Months Ended September 30, 2008	Nine Months Ended September 30, 2008	Liabilities Carried at Fair Value	Business Segment Affected
Income statement caption:				
Net realized capital losses	**$1,074**	**$1,325**	Freestanding derivatives	All segments - excluding AIGFP
	–	**(155)**	Embedded policy derivatives	Life Insurance & Retirement Services
Unrealized market valuation losses on AIGFP super senior credit default swap portfolio	**98**	**207**	Super senior credit default swap portfolio	AIGFP
Other income	**$1,194***	**$3,621***	Notes, GIAs, derivatives, other liabilities	AIGFP
Net pre-tax increase	**$2,366**	**$4,998**		
Liabilities already carried at fair value	**$2,550**	**$3,904**		
Newly elected liabilities measured at fair value (FAS 159 elected)	**(184)**	**1,094**		
Net pre-tax increase	**$2,366**	**$4,998**		

**The effect of changes in AIG's own credit spreads on pre-tax income for AIGFP was an increase of $1.3 billion and $3.8 billion for the three- and nine-month periods ended September 30, 2008, respectively. The effect of the changes in counterparty credit spreads for assets measured at fair value at AIGFP was a decrease in pre-tax income of $2.3 billion and $5.3 billion for the three- and nine-month periods ended September 30, 2008, respectively.*

Fair Value Measurements on a Recurring Basis

AIG measures at fair value on a recurring basis financial instruments in its trading and available for sale securities portfolios, certain mortgage and other loans receivable, certain spot commodities, derivative assets and liabilities, securities purchased (sold) under agreements to resell (repurchase), securities lending invested collateral, non-traded equity investments and certain private limited partnerships and certain hedge funds included in other invested assets, certain short-term investments, separate and variable account assets, certain policyholders' contract deposits, securities and spot commodities sold but not yet purchased, certain trust deposits and deposits due to banks and other depositors, certain long-term borrowings, and certain hybrid financial instruments included in other liabilities. The fair value of a financial instrument is the amount that would be received on sale of an asset or paid to transfer a liability in an orderly

3. Fair Value Measurements *(continued)*

transaction between market participants at the measurement date.

The degree of judgment used in measuring the fair value of financial instruments generally correlates with the level of pricing observability. Financial instruments with quoted prices in active markets generally have more pricing observability and less judgment is used in measuring fair value. Conversely, financial instruments traded in other-than-active markets or that do not have quoted prices have less observability and are measured at fair value using valuation models or other pricing techniques that require more judgment. An active market is one in which transactions for the asset or liability being valued occur with sufficient frequency and volume to provide pricing information on an ongoing basis. An other-than-active market is one in which there are few transactions, the prices are not current, price quotations vary substantially either over time or among market makers, or in which little information is released publicly for the asset or liability being valued. Pricing observability is affected by a number of factors, including the type of financial instrument, whether the financial instrument is new to the market and not yet established, the characteristics specific to the transaction and general market conditions.

Incorporation of Credit Risk in Fair Value Measurements

- *AIG's Own Credit Risk*. Fair value measurements for AIGFP's debt, guaranteed investment agreements (GIAs), and structured note liabilities incorporate AIG's own credit risk by discounting cash flows at rates that incorporate AIG's currently observable credit default swap spreads and take into consideration collateral posted by AIG with counterparties at the balance sheet date.

  Fair value measurements for freestanding derivatives incorporate AIG's own credit risk by determining the explicit cost for each counterparty to protect against its net credit exposure to AIG at the balance sheet date by reference to observable AIG credit default swap spreads. A counterparty's net credit exposure to AIG is determined based on master netting agreements, which take into consideration all derivative positions with AIG, as well as collateral posted by AIG with the counterparty at the balance sheet date.

  Fair value measurements for embedded policy derivatives and policyholders' contract deposits take into consideration that policyholder liabilities are senior in priority to general creditors of AIG and therefore are much less sensitive to changes in AIG credit default swap or cash issuance spreads.

- *Counterparty Credit Risk*. Fair value measurements for freestanding derivatives incorporate counterparty credit by determining the explicit cost for AIG to protect against its net credit exposure to each counterparty at the balance sheet date by reference to observable counterparty credit default swap spreads. AIG's net credit exposure to a counterparty is determined based on master netting agreements, which take into consideration all derivative positions with the counterparty, as well as collateral posted by the counterparty at the balance sheet date.

Fair values for fixed maturity securities based on observable market prices for identical or similar instruments implicitly include the incorporation of counterparty credit risk. Fair values for fixed maturity securities based on internal models incorporate counterparty credit risk by using discount rates that take into consideration cash issuance spreads for similar instruments or other observable information.

Fixed Maturity Securities — Trading and Available for Sale

AIG maximizes the use of observable inputs and minimizes the use of unobservable inputs when measuring fair value. Whenever available, AIG obtains quoted prices in active markets for identical assets at the balance sheet date to measure at fair value fixed maturity securities in its trading and available for sale portfolios. Market price data generally is obtained from exchange or dealer markets.

AIG estimates the fair value of fixed maturity securities not traded in active markets, including securities purchased (sold) under agreements to resell (repurchase), and mortgage and other loans receivable for which AIG elected the fair value option, by referring to traded securities with similar attributes, using dealer quotations, a matrix pricing methodology, discounted cash flow analyses or internal valuation models. This methodology considers such factors as the issuer's industry, the security's rating and tenor, its coupon rate, its position in the capital structure of the issuer, yield curves, credit curves, prepayment rates and other relevant factors. For fixed maturity instruments that are not traded in active markets or that are subject to transfer restrictions, valuations are adjusted to reflect illiquidity and/or non-transferability, and such adjustments generally are based on available market evidence. In the absence of such evidence, management's best estimate is used.

Equity Securities Traded in Active Markets — Trading and Available for Sale

AIG maximizes the use of observable inputs and minimizes the use of unobservable inputs when measuring fair value. Whenever available, AIG obtains quoted prices in active markets for identical assets at the balance sheet date to measure at fair value marketable equity securities in its trading and available for sale portfolios. Market price data generally is obtained from exchange or dealer markets.

3. Fair Value Measurements *(continued)*

Non-Traded Equity Investments — Other Invested Assets

AIG initially estimates the fair value of equity instruments not traded in active markets by reference to the transaction price. This valuation is adjusted only when changes to inputs and assumptions are corroborated by evidence such as transactions in similar instruments, completed or pending third-party transactions in the underlying investment or comparable entities, subsequent rounds of financing, recapitalizations and other transactions across the capital structure, offerings in the equity capital markets, and changes in financial ratios or cash flows. For equity securities that are not traded in active markets or that are subject to transfer restrictions, valuations are adjusted to reflect illiquidity and/or non-transferability and such adjustments generally are based on available market evidence. In the absence of such evidence, management's best estimate is used.

Private Limited Partnership and Hedge Fund Investments — Other Invested Assets

AIG initially estimates the fair value of investments in certain private limited partnerships and certain hedge funds by reference to the transaction price. Subsequently, AIG obtains the fair value of these investments generally from net asset value information provided by the general partner or manager of the investments, the financial statements of which generally are audited annually.

Separate and Variable Account Assets

Separate and variable account assets are composed primarily of registered and unregistered open-end mutual funds that generally trade daily and are measured at fair value in the manner discussed above for equity securities traded in active markets.

Freestanding Derivatives

Derivative assets and liabilities can be exchange-traded or traded over the counter (OTC). AIG generally values exchange-traded derivatives using quoted prices in active markets for identical derivatives at the balance sheet date.

OTC derivatives are valued using market transactions and other market evidence whenever possible, including market-based inputs to models, model calibration to market clearing transactions, broker or dealer quotations or alternative pricing sources with reasonable levels of price transparency. When models are used, the selection of a particular model to value an OTC derivative depends on the contractual terms of, and specific risks inherent in, the instrument as well as the availability of pricing information in the market. AIG generally uses similar models to value similar instruments. Valuation models require a variety of inputs, including contractual terms, market prices and rates, yield curves, credit curves, measures of volatility, prepayment rates and correlations of such inputs. For OTC derivatives that trade in liquid markets, such as generic forwards, swaps and options, model inputs can generally be corroborated by observable market data by correlation or other means, and model selection does not involve significant management judgment.

Certain OTC derivatives trade in less liquid markets with limited pricing information, and the determination of fair value for these derivatives is inherently more difficult. When AIG does not have corroborating market evidence to support significant model inputs and cannot verify the model to market transactions, the transaction price is initially used as the best estimate of fair value. Accordingly, when a pricing model is used to value such an instrument, the model is adjusted so the model value at inception equals the transaction price. Subsequent to initial recognition, AIG updates valuation inputs when corroborated by evidence such as similar market transactions, third-party pricing services and/or broker or dealer quotations, or other empirical market data. When appropriate, valuations are adjusted for various factors such as liquidity, bid/offer spreads and credit considerations. Such adjustments are generally based on available market evidence. In the absence of such evidence, management's best estimate is used.

With the adoption of FAS 157 on January 1, 2008, AIG's own credit risk has been considered and is incorporated into the fair value measurement of its freestanding derivative liabilities.

Embedded Policy Derivatives

The fair value of embedded policy derivatives contained in certain variable annuity and equity-indexed annuity and life contracts is measured based on actuarial and capital market assumptions related to projected cash flows over the expected lives of the contracts. These cash flow estimates primarily include benefits and related fees assessed, when applicable, and incorporate expectations about policyholder behavior. Estimates of future policyholder behavior are subjective and based primarily on AIG's historical experience. With respect to embedded policy derivatives in AIG's variable annuity contracts, because of the dynamic and complex nature of the expected cash flows, risk neutral valuations are used. Estimating the underlying cash flows for these products involves many estimates and judgments, including those regarding expected market rates of return, market volatility, correlations of market index returns to funds, fund performance, discount rates and policyholder behavior. With respect to embedded policy derivatives in AIG's equity-indexed annuity and life contracts, option pricing models are used to estimate fair value, taking into account assumptions for future

3. Fair Value Measurements *(continued)*

equity index growth rates, volatility of the equity index, future interest rates, and determinations on adjusting the participation rate and the cap on equity indexed credited rates in light of market conditions and policyholder behavior assumptions. With the adoption of FAS 157, these methodologies were not changed, with the exception of incorporating an explicit risk margin to take into consideration market participant estimates of projected cash flows and policyholder behavior.

AIGFP's Super Senior Credit Default Swap Portfolio

AIGFP values its credit default swaps written on the most senior (super senior) risk layers of designated pools of debt securities or loans using internal valuation models, third-party prices and market indices. The principal market was determined to be the market in which super senior credit default swaps of this type and size would be transacted, or have been transacted, with the greatest volume or level of activity. AIG has determined that the principal market participants, therefore, would consist of other large financial institutions who participate in sophisticated over-the-counter derivatives markets. The specific valuation methodologies vary based on the nature of the referenced obligations and availability of market prices.

The valuation of the super senior credit derivatives continues to be challenging given the limitation on the availability of market observable information due to the limited trading and lack of price transparency in the structured finance market, particularly during and since the fourth quarter of 2007. These market conditions have increased the reliance on management estimates and judgments in arriving at an estimate of fair value for financial reporting purposes. Further, disparities in the valuation methodologies employed by market participants when assessing illiquid markets have increased the likelihood that the various parties to these instruments may arrive at significantly different estimates as to their fair values.

AIGFP's valuation methodologies for the super senior credit default swap portfolio have evolved in response to the deteriorating market conditions and the lack of sufficient market observable information. AIG has sought to calibrate the model to available market information and to review the assumptions of the model on a regular basis.

In the case of credit default swaps written to facilitate regulatory capital relief, AIGFP estimates the fair value of these derivatives by considering observable market transactions. The transactions with the most observability are the early terminations of these transactions by counterparties. AIG expects that the majority of these transactions will be terminated within the next 6 to 18 months by AIGFP's counterparties. AIGFP also considers other market data, to the extent available.

AIGFP uses a modified version of the Binomial Expansion Technique (BET) model to value its credit default swap portfolio written on super senior tranches of multi-sector collateralized debt obligations (CDOs) of asset-backed securities (ABS), including maturity-shortening puts that allow the holders of the securities issued by certain CDOs to treat the securities as short-term eligible 2a-7 investments under the Investment Company Act of 1940 (2a-7 Puts).

The BET model uses the prices for the securities comprising the portfolio of a CDO as an input and converts those prices to credit spreads over current LIBOR-based interest rates. These credit spreads are used to determine implied probabilities of default and expected losses on the underlying securities. This data is then aggregated and used to estimate the expected cash flows of the super senior tranche of the CDO. The most significant assumption used in the BET model is the pricing of the individual securities within the CDO collateral pools. The BET model also uses diversity scores, weighted average lives, recovery rates and discount rates.

Prices for the individual securities held by a CDO are obtained in most cases from the CDO collateral managers, to the extent available. For the quarter ended September 30, 2008, CDO collateral managers provided market prices for approximately 70 percent of the underlying securities. When a price for an individual security is not provided by a CDO collateral manager, AIGFP derives the price through a pricing matrix using prices from CDO collateral managers for similar securities. Matrix pricing is a mathematical technique used principally to value debt securities without relying exclusively on quoted prices for the specific securities, but rather by relying on the relationship of the security to other benchmark quoted securities. Substantially all of the CDO collateral managers who provided prices used dealer prices for all or part of the underlying securities, in some cases supplemented by third party pricing services.

AIGFP also employs a Monte Carlo simulation to assist in quantifying the effect on the valuation of the CDOs of the unique aspects of the CDOs' structure such as triggers that divert cash flows to the most senior part of the capital structure. The Monte Carlo simulation is used to determine whether an underlying security defaults in a given simulation scenario and, if it does, the security's implied random default time and expected loss. This information is used to project cash flow streams and to determine the expected losses of the portfolio.

In addition to calculating an estimate of the fair value of the super senior CDO security referenced in the credit default swaps using its internal model, AIGFP also considers the price estimates for the super senior CDO securities provided by

3. Fair Value Measurements *(continued)*

third parties, including counterparties to these transactions, to validate the results of the model and to determine the best available estimate of fair value. In determining the fair value of the super senior CDO security referenced in the credit default swaps, AIGFP uses a consistent process which considers all available pricing data points and eliminates the use of outlying data points. When pricing data points are within a reasonable range an averaging technique is applied.

In the case of credit default swaps written on portfolios of investment-grade corporate debt, AIGFP estimates the fair value of its obligations by comparing the contractual premium of each contract to the current market levels of the senior tranches of comparable credit indices, the iTraxx index for European corporate issuances and the CDX index for U.S. corporate issuances. These indices are considered to be reasonable proxies for the referenced portfolios. In addition, AIGFP compares these valuations to third party prices and makes adjustments as necessary to arrive at the best available estimate of fair value.

AIGFP estimates the fair value of its obligations resulting from credit default swaps written on collateralized loan obligations to be equivalent to the par value less the current market value of the referenced obligation. Accordingly, the value is determined by obtaining third-party quotes on the underlying super senior tranches referenced under the credit default swap contract.

Policyholders' Contract Deposits

Policyholders' contract deposits accounted for at fair value beginning January 1, 2008 are measured using an income approach by taking into consideration the following factors:

- Current policyholder account values and related surrender charges;
- The present value of estimated future cash inflows (policy fees) and outflows (benefits and maintenance expenses) associated with the product using risk neutral valuations, incorporating expectations about policyholder behavior, market returns and other factors; and
- A risk margin that market participants would require for a market return and the uncertainty inherent in the model inputs.

The change in fair value of these policyholders' contract deposits is recorded as incurred policy losses and benefits in the consolidated statement of income (loss).

Fair Value Measurements on a Non-Recurring Basis

AIG also measures the fair value of certain assets on a non-recurring basis, generally quarterly, annually, or when events or changes in circumstances indicate that the carrying amount of the assets may not be recoverable. These assets include held to maturity securities (in periods prior to the third quarter of 2008), cost and equity-method investments, life settlement contracts, flight equipment, collateral securing foreclosed loans and real estate and other fixed assets, goodwill, and other intangible assets. AIG uses a variety of techniques to measure the fair value of these assets when appropriate, as described below:

- *Held to Maturity Securities, Cost and Equity-Method Investments:* When AIG determines that the carrying value of these assets may not be recoverable, AIG records the assets at fair value with the loss recognized in income. In such cases, AIG measures the fair value of these assets using the techniques discussed above for fixed maturities and equity securities. During the third quarter of 2008, AIG transferred all securities previously classified as held to maturity to the available for sale category (see Note 1 for further discussion).
- *Life Settlement Contracts:* AIG measures the fair value of individual life settlement contracts (which are included in other invested assets) whenever the carrying value plus the undiscounted future costs that are expected to be incurred to keep the life settlement contract in force exceed the expected proceeds from the contract. In those situations, the fair value is determined on a discounted cash flow basis, incorporating current life expectancy assumptions. The discount rate incorporates current information about market interest rates, the credit exposure to the insurance company that issued the life settlement contract and AIG's estimate of the risk margin an investor in the contracts would require.
- *Flight Equipment Primarily Under Operating Leases:* When AIG determines the carrying value of its commercial aircraft may not be recoverable, AIG records the aircraft at fair value with the loss recognized in income. AIG measures the fair value of its commercial aircraft using an income approach based on the present value of all cash flows from existing and projected lease payments (based on historical experience and current expectations regarding market participants) including net contingent rentals for the period extending to the end of the aircraft's economic life in its highest and best use configuration, plus its disposition value.
- *Collateral Securing Foreclosed Loans and Real Estate and Other Fixed Assets:* When AIG takes collateral in connection with foreclosed loans, AIG generally bases its estimate

3. Fair Value Measurements *(continued)*

of fair value on the price that would be received in a current transaction to sell the asset by itself.

- *Goodwill:* AIG tests goodwill for impairment whenever events or changes in circumstances indicate the carrying amount of goodwill may not be recoverable, but at least annually. When AIG determines goodwill may be impaired, AIG uses techniques that consider market-based earnings multiples of the unit's peer companies or discounted cash flow techniques based on the price that could be received in a current transaction to sell the asset assuming the asset would be used with other assets as a group (in-use premise). See Fair Value Measured on a Non-Recurring Basis below for additional information.
- *Intangible Assets:* AIG tests its intangible assets for impairment whenever events or changes in circumstances indicate the carrying amount of an intangible asset may not be recoverable. AIG measures the fair value of intangible assets based on an in-use premise that considers the same factors used to estimate the fair value of its real estate and other fixed assets under an in-use premise discussed above.

See Notes 1(c), (d), (e), (t), and (v) to Consolidated Financial Statements included in the 2007 Annual Report on Form 10-K for additional information about how AIG tests various asset classes for impairment.

Fair Value Hierarchy

Beginning January 1, 2008, assets and liabilities recorded at fair value in the consolidated balance sheet are measured and classified in a hierarchy for disclosure purposes consisting of three "levels" based on the observability of inputs available in the marketplace used to measure the fair values as discussed below:

- *Level 1:* Fair value measurements that are quoted prices (unadjusted) in active markets that AIG has the ability to access for identical assets or liabilities. Market price data generally is obtained from exchange or dealer markets. AIG does not adjust the quoted price for such instruments. Assets and liabilities measured at fair value on a recurring basis and classified as Level 1 include certain government and agency securities, actively traded listed common stocks and derivative contracts, most separate account assets and most mutual funds.
- *Level 2:* Fair value measurements based on inputs other than quoted prices included in Level 1 that are observable for the asset or liability, either directly or indirectly. Level 2 inputs include quoted prices for similar assets and liabilities in active markets, and inputs other than quoted prices that are observable for the asset or liability, such as interest rates and yield curves that are observable at commonly quoted intervals. Assets and liabilities measured at fair value on a recurring basis and classified as Level 2 generally include certain government securities, most investment-grade and high-yield corporate bonds, certain ABS, certain listed equities, state, municipal and provincial obligations, hybrid securities, mutual fund and hedge fund investments, derivative contracts, GIAs at AIGFP and physical commodities.
- *Level 3:* Fair value measurements based on valuation techniques that use significant inputs that are unobservable. These measurements include circumstances in which there is little, if any, market activity for the asset or liability. In certain cases, the inputs used to measure fair value may fall into different levels of the fair value hierarchy. In such cases, the level in the fair value hierarchy within which the fair value measurement in its entirety falls is determined based on the lowest level input that is significant to the fair value measurement in its entirety. AIG's assessment of the significance of a particular input to the fair value measurement in its entirety requires judgment. In making the assessment, AIG considers factors specific to the asset or liability. Assets and liabilities measured at fair value on a recurring basis and classified as Level 3 include certain distressed ABS, structured credit products, certain derivative contracts (including AIGFP's super senior credit default swap portfolio), policyholders' contract deposits carried at fair value, private equity and real estate fund investments, and direct private equity investments. AIG's non-financial-instrument assets that are measured at fair value on a non-recurring basis generally are classified as Level 3.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

3. Fair Value Measurements *(continued)*

Assets and Liabilities Measured at Fair Value on a Recurring Basis

The following table presents information about assets and liabilities measured at fair value on a recurring basis at September 30, 2008, and indicates the level of the fair value measurement based on the levels of the inputs used:

(in millions)	Level 1	Level 2	Level 3	Counterparty Netting[(a)]	Total September 30, 2008
Assets:					
Bonds available for sale	$ 891	$375,021	$18,582	$ –	$394,494
Bond trading securities	–	7,355	197	–	7,552
Common stocks available for sale	11,113	271	75	–	11,459
Common and preferred stocks trading	19,751	922	1	–	20,674
Preferred stocks available for sale	1	1,393	70	–	1,464
Mortgage and other loans receivable	–	324	4	–	328
Financial Services assets:					
Securities available for sale	1	762	1,563	–	2,326
Trading securities	1,388	28,710	6,038	–	36,136
Spot commodities	–	34	–	–	34
Unrealized gain on swaps, options and forward transactions	–	54,108	3,307	(47,381)	10,034
Securities purchased under agreements to resell	–	12,100	–	–	12,100
Securities lending invested collateral[(b)]	–	23,648	12,173	–	35,821
Other invested assets[(c)]	2,334	7,406	11,788	–	21,528
Short-term investments	4,320	18,201	69	–	22,590
Separate and variable accounts	61,405	2,953	1,114	–	65,472
Other assets	110	3,057	354	(1,898)	1,623
Total	$101,314	$536,265	$55,335	$(49,279)	$643,635
Liabilities:					
Policyholders' contract deposits	$ –	$ –	$ 4,282	$ –	$ 4,282
Other policyholders' funds					
Financial Services liabilities:					
Securities sold under agreements to repurchase	–	7,143	50	–	7,193
Securities and spot commodities sold but not yet purchased	715	1,851	–	–	2,566
Unrealized loss on swaps, options and forward transactions[(d)]	–	47,066	34,949	(75,690)	6,325
Trust deposits and deposits due to banks and other depositors	–	215	–	–	215
Other long-term borrowings	–	38,347	802	–	39,149
Other liabilities	7	3,501	60	(179)	3,389
Total	$ 722	$ 98,123	$40,143	$(75,869)	$ 63,119

(a) Represents netting of derivative exposures covered by a qualifying master netting agreement in accordance with FIN 39 of $42.8 billion, offset by cash collateral posted and received by AIG of $33.1 billion and $6.5 billion, respectively.

(b) Amounts exclude short-term investments that are carried at cost, which approximates fair value of $5.7 billion.

(c) Approximately 11 percent of the fair value of the assets recorded as Level 3 relates to various private equity, real estate, hedge fund and fund-of-funds investments. AIG's ownership in these funds represented 27 percent, or $1.7 billion of the Level 3 amount.

(d) Included in Level 3 is the fair value derivative liability of $32.3 billion on AIGFP super senior credit default swap portfolio.

At September 30, 2008, Level 3 assets were 5.4 percent of total assets, and Level 3 liabilities were 4.2 percent of total liabilities.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

3. Fair Value Measurements *(continued)*

The following tables present changes during the three- and nine-month periods ended September 30, 2008 in Level 3 assets and liabilities measured at fair value on a recurring basis, and the realized and unrealized gains (losses) recorded in income during the three- and nine-month periods ended September 30, 2008 related to the Level 3 assets and liabilities that remained in the consolidated balance sheet at September 30, 2008:

(in millions)	Balance Beginning of Period[(a)]	Net Realized and Unrealized Gains (Losses) Included in Income[(b)]	Accumulated Other Comprehensive Income (Loss)	Purchases, Sales, Issuances and Settlements-net	Transfers In (Out)	Balance at September 30, 2008	Changes in Unrealized Gains (Losses) on Instruments Held at September 30, 2008
Three Months Ended September 30, 2008:							
Assets:							
Bonds available for sale	$ 18,480	$ (696)	$ (255)	$ (646)	$1,699	$ 18,582	$ –
Bond trading securities	195	(11)	(2)	20	(5)	197	(6)
Common stocks available for sale	227	1	1	(196)	42	75	–
Common and preferred stocks trading	5	–	(3)	5	(6)	1	–
Preferred stocks available for sale	258	(7)	(50)	(9)	(122)	70	–
Mortgage and other loans receivable	4	–	–	–	–	4	–
Financial Services assets:							
Securities available for sale	372	(3)	(180)	1,341	33	1,563	–
Trading securities	3,680	(1,510)	–	3,865	3	6,038	(919)
Securities lending invested collateral	8,489	(2,091)	829	(706)	5,652	12,173	–
Other invested assets	11,868	77	(126)	131	(162)	11,788	293
Short-term investments	–	–	–	69	–	69	–
Separate and variable accounts	1,178	(75)	–	11	–	1,114	(75)
Other assets	334	(4)	–	13	–	343	(4)
Total	$ 45,090	$ (4,319)	$ 214	$ 3,898	$7,134	$ 52,017	$ (711)
Liabilities:							
Policyholders' contract deposits	$ (4,179)	$ 113	$ 43	$ (259)	$ –	$ (4,282)	$ 235
Financial Services liabilities:							
Securities sold under agreements to repurchase	(40)	5	–	(15)	–	(50)	(5)
Unrealized loss on swaps, options and forward transactions, net	(26,674)	(5,223)	–	207	48	(31,642)	(6,032)
Other long-term borrowings	(2,689)	1,030	–	630	227	(802)	(500)
Other liabilities	(25)	(15)	(2)	2	(9)	(49)	4
Total	$(33,607)	$ (4,090)	$ 41	$ 565	$ 266	$(36,825)	$ (6,298)
Nine Months Ended September 30, 2008:							
Assets:							
Bonds available for sale	$ 18,786	$ (2,140)	$ (805)	$ (870)	$3,611	$ 18,582	$ –
Bond trading securities	141	(31)	–	35	52	197	(16)
Common stocks available for sale	224	(4)	1	(185)	39	75	–
Common and preferred stocks trading	30	(1)	(1)	(14)	(13)	1	–
Preferred stocks available for sale	135	(9)	(44)	(76)	64	70	–
Mortgage and other loans receivable	–	–	–	–	4	4	–
Financial Services assets:							
Securities available for sale	285	(6)	(172)	1,423	33	1,563	–
Trading securities	4,422	(2,943)	–	4,567	(8)	6,038	(2,408)
Securities lending invested collateral	11,353	(5,229)	1,916	(1,524)	5,657	12,173	–
Other invested assets	10,373	269	11	1,279	(144)	11,788	862
Short-term investments	–	–	–	69	–	69	–
Separate and variable accounts	1,003	(48)	–	159	–	1,114	(48)
Other assets	141	(4)	–	206	–	343	(4)
Total	$ 46,893	$(10,146)	$ 906	$ 5,069	$9,295	$ 52,017	$ (1,614)
Liabilities:							
Policyholders' contract deposits	$ (3,674)	$ 56	$ (8)	$ (656)	$ –	$ (4,282)	$ 398
Financial Services liabilities:		–					
Securities sold under agreements to repurchase	(208)	(15)	–	(49)	222	(50)	(5)
Unrealized loss on swaps, options and forward transactions, net	(11,718)	(19,785)	–	(222)	83	(31,642)	(20,631)
Other long-term borrowings	(3,578)	1,120	–	1,268	388	(802)	(522)
Other liabilities	(503)	(70)	(2)	534	(8)	(49)	33
Total	$(19,681)	$(18,694)	$ (10)	$ 875	$ 685	$(36,825)	$(20,727)

(a) Total Level 3 derivative exposures have been netted on these tables for presentation purposes only.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

3. Fair Value Measurements *(continued)*

(b) Net realized and unrealized gains and losses shown above are reported in the consolidated statement of income (loss) primarily as follows:

Major category of Assets/Liabilities	Consolidated Statement of Income (Loss) Line Items
Financial Services assets and liabilities	• Other income • Unrealized market valuation losses on AIGFP super senior credit default swap portfolio
Securities lending invested collateral	• Net realized capital gains (losses)
Other invested assets	• Net realized capital gains (losses)
Policyholders' contract deposits	• Incurred policy losses and benefits • Net realized capital gains (losses)

Both observable and unobservable inputs may be used to determine the fair values of positions classified in Level 3 in the tables above. As a result, the unrealized gains (losses) on instruments held at September 30, 2008 may include changes in fair value that were attributable to both observable (e.g., changes in market interest rates) and unobservable inputs (e.g., changes in unobservable long-dated volatilities).

AIG uses various hedging techniques to manage risks associated with certain positions, including those classified within Level 3. Such techniques may include the purchase or sale of financial instruments that are classified within Level 1 and/or Level 2. As a result, the realized and unrealized gains (losses) for assets and liabilities classified within Level 3 presented in the table above do not reflect the related realized or unrealized gains (losses) on hedging instruments that are classified within Level 1 and/or Level 2.

Changes in the fair value of separate and variable account assets are completely offset in the consolidated statement of income (loss) by changes in separate and variable account liabilities, which are not carried at fair value and therefore not included in the tables above.

Fair Value Measured on a Non-Recurring Basis

AIG measures the fair value of certain assets on a non-recurring basis, generally quarterly, or when events or changes in circumstances indicate that the carrying amount of the asset may not be recoverable. These assets include goodwill, real estate owned, real estate loans held for sale, and other intangible assets.

Assets measured at fair value on a non-recurring basis on which impairment charges were recorded were as follows:

(in millions)	Level 1	Level 2	Level 3	Total	Three Months Ended September 30, 2008	Nine Months Ended September 30, 2008
Goodwill	**$–**	**$–**	**$ –**	**$ –**	**$432**	**$477**
Real estate owned	**–**	**–**	**1,358**	**1,358**	**100**	**102**
Other investments	**–**	**–**	**3,883**	**3,883**	**75**	**85**
Other assets	**–**	**7**	**190**	**197**	**2**	**53**
Total	**$–**	**$7**	**$5,431**	**$5,438**	**$609**	**$717**

AIG recognized goodwill impairment charges of $432 million and $477 million for the three and nine months ended September 30, 2008, which were primarily related to the domestic Consumer Finance and the Capital Markets businesses.

AIG recognized an impairment charge on certain investment real estate and other real estate owned of $100 million and $102 million for the three and nine months ended September 30, 2008, respectively, which was included in other income. As required by FAS 157, the fair value disclosed in the table above is unadjusted for transaction costs. The amounts recorded on the consolidated balance sheet are net of transaction costs.

Fair Value Option

FAS 159 permits a company to choose to measure at fair value many financial instruments and certain other assets and liabilities that are not required to be measured at fair value. Subsequent changes in fair value for designated items are required to be reported in income. Unrealized gains and losses on financial instruments in AIG's insurance businesses and in AIGFP for which the fair value option was elected under FAS 159 are classified in incurred policy losses and benefits and in other income, respectively, in the consolidated statement of income (loss).

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

The following table presents the gains or losses recorded during the three- and nine-month periods ended September 30, 2008 related to the eligible instruments for which AIG elected the fair value option and the related transition adjustment recorded as a decrease to opening shareholders' equity at January 1, 2008:

(in millions)	January 1, 2008 prior to Adoption	Transition Adjustment upon Adoption	January 1, 2008 after Adoption	Gain (Loss) Three Months Ended September 30, 2008	Gain (Loss) Nine Months Ended September 30, 2008
Mortgage and other loans receivable	$ 1,109	$ –	$ 1,109	$ (74)	$ 5
Financial Services assets[(a)]:					
Trading securities (formerly available for sale)	39,278	5	39,283	(3,886)	(5,037)
Securities purchased under agreements to resell	20,950	1	20,951	(180)	395
Other invested assets	321	(1)	320	(24)	(12)
Short-term investments	6,969	–	6,969	(2)	65
Deferred policy acquisition costs	1,147	(1,147)	–	–	–
Other assets	435	(435)	–	–	–
Future policy benefits for life, accident and health insurance contracts	299	299	–	–	–
Policyholders' contract deposits[(b)]	3,739	360	3,379	416	534
Financial Services liabilities[(a)]:					
Securities sold under agreements to repurchase	6,750	(10)	6,760	339	(77)
Securities and spot commodities sold but not yet purchased	3,797	(10)	3,807	157	144
Trust deposits and deposits due to banks and other depositors	216	(25)	241	24	13
Long-term borrowings	57,968	(675)	58,643	294	(97)
Other liabilities	1,792	–	1,792	1,266	947
Total gain (loss) for the three- and nine-month periods ended September 30, 2008 [(c)]				$(1,670)	$(3,120)
Pre-tax cumulative effect of adopting the fair value option		(1,638)			
Decrease in deferred tax liabilities		526			
Cumulative effect of adopting the fair value option		$(1,112)			

(a) Effective January 1, 2008, AIGFP elected to apply the fair value option under FAS 159 to all eligible assets and liabilities (other than equity method investments, trade receivables and trade payables) because electing the fair value option allows AIGFP to more closely align its earnings with the economics of its transactions by recognizing concurrently through earnings the change in fair value of its derivatives and the offsetting change in fair value of the assets and liabilities being hedged as well as the manner in which the business is evaluated by management. Substantially all of the gain (loss) amounts shown above are reported in other income on the consolidated statement of income (loss). In August 2008, AIGFP modified prospectively this election as management believes it is appropriate to exclude from the automatic election securities purchased in connection with existing structured credit transactions and their related funding obligations. AIGFP will evaluate whether to elect the fair value option on a case-by-case basis for securities purchased in connection with existing structured credit transactions and their related funding obligations.

(b) AIG elected to apply the fair value option to certain single premium variable life products in Japan and an investment-linked life insurance product sold principally in Asia, both classified within policyholders' contract deposits in the consolidated balance sheet. AIG elected the fair value option for these liabilities to more closely align its accounting with the economics of its transactions. For the investment-linked product sold principally in Asia, the election more effectively aligns changes in the fair value of assets with a commensurate change in the fair value of policyholders' liabilities. For the single premium life products in Japan, the fair value option election allows AIG to economically hedge the inherent market risks associated with this business in an efficient and effective manner through the use of derivative instruments. The hedging program, which was completed in the third quarter of 2008, results in an accounting presentation for this business that more closely reflects the underlying economics and the way the business is managed, with the change in the fair value of derivatives and underlying assets largely offsetting the change in fair value of the policy liabilities. AIG did not elect the fair value option for other liabilities classified in policyholders' contract deposits because other contracts do not share the same contract features that created the disparity between the accounting presentation and the economic performance.

(c) Not included in the table above were losses of $9.6 billion and $23.2 billion for the three- and nine-month periods ended September 30, 2008, respectively, that were primarily due to changes in the fair value of derivatives, trading securities and certain other invested assets for which the fair value option under FAS 159 was not elected. Included in these amounts were unrealized market valuation losses of $7.1 billion and $21.7 billion for the three- and nine-months periods ended September 30, 2008, respectively, related to AIGFP's super senior credit default swap portfolio.

3. Fair Value Measurements *(continued)*

Interest income and expense and dividend income on assets and liabilities elected under the fair value option are recognized and classified in the consolidated statement of income (loss) depending on the nature of the instrument and related market conventions. For AIGFP related activity, interest, dividend income, and interest expense are included in other income. Otherwise, interest and dividend income are included in net investment income in the consolidated statement of income (loss). See Note 1(a) to the Consolidated Financial Statements included in the 2007 Annual Report on Form 10-K for additional information about AIG's policies for recognition, measurement, and disclosure of interest and dividend income and interest expense.

During the three- and nine-month periods ended September 30, 2008, AIG recognized a loss of $184 million and a gain of $1.1 billion, respectively, attributable to the observable effect of changes in credit spreads on AIG's own liabilities for which the fair value option was elected. AIG calculates the effect of these credit spread changes using discounted cash flow techniques that incorporate current market interest rates, AIG's observable credit spreads on these liabilities and other factors that mitigate the risk of nonperformance such as collateral posted.

The following table presents the difference between fair values and the aggregate contractual principal amounts of mortgage and other loans receivable and long-term borrowings, for which the fair value option was elected:

(in millions)	Fair Value at September 30, 2008	Principal Amount Due Upon Maturity	Difference
Assets:			
Mortgage and other loans receivable	$ 328	$ 378	$ (50)
Liabilities:			
Long-term borrowings	$36,464	$36,065	$399

At September 30, 2008, there were no mortgage and other loans receivable for which the fair value option was elected, that were 90 days or more past due and in non-accrual status.

4. Revolving Credit Agreement and Guarantee and Pledge Agreement between AIG and the Federal Reserve Bank of New York

On September 22, 2008, AIG entered into the $85 billion Fed Credit Agreement and a Guarantee and Pledge Agreement (the Pledge Agreement) with the NY Fed.

The Fed Facility has a two-year term. Outstanding borrowings bear interest at 3-month LIBOR (not less than 3.5 percent per annum) plus 8.5 percent per annum. AIG incurred, in the form of an increase in the outstanding loan balance under the Fed Credit Agreement, a gross commitment fee of $1.7 billion, which was paid in kind and was recognized as a prepaid commitment asset. Pursuant to the Fed Credit Agreement, in consideration for the NY Fed's extension of credit under the Fed Facility and the payment of $500,000, AIG agreed to issue 100,000 shares, liquidation preference $5.00 per share, of the Series C Preferred Stock to the Trust. The Series C Preferred Stock was not yet issued as of September 30, 2008. Accordingly, additional paid-in capital has been increased to reflect a prepaid commitment fee which represents AIG's obligation to issue the Series C Preferred Stock in the fourth quarter of 2008. The value of the Series C Preferred Stock was also recognized as part of the prepaid commitment asset. The total prepaid commitment fee asset of $24.7 billion is being amortized as interest expense through the term of the facility. AIG also incurs a commitment fee on undrawn amounts at the rate of 8.5 percent per annum, which is recognized as interest expense when incurred.

Interest and the commitment fees are payable in kind and generally recognized through an increase in the outstanding balance under the Fed Facility.

AIG is required to repay the Fed Facility primarily from proceeds on sales of assets, including businesses. These mandatory repayments permanently reduce the maximum amount available to be borrowed under the Fed Facility. Additionally, AIG is permitted to repay any portion of the amounts borrowed at any time prior to the maturity of the Fed Facility, without penalty. Voluntary repayments do not reduce the maximum amount available to be borrowed.

The Fed Credit Agreement contains customary affirmative and negative covenants, including a requirement to maintain a minimum amount of liquidity and a requirement to use reasonable efforts to cause the composition of the Board of Directors of AIG to be satisfactory to the Trust within 10 days after the establishment of the Trust. Borrowings under the Fed Facility are conditioned, among other things, on the NY Fed being satisfied with AIG's corporate governance and the value of the collateral.

The Fed Facility is secured by a pledge of the capital stock and assets of certain of AIG's subsidiaries, subject to exclusions of certain property not permitted to be pledged under AIG debt agreements and its Restated Certificate of Incorporation, as well as exclusions of assets of regulated subsidiaries, assets of foreign subsidiaries and assets of special purpose vehicles. The exclusion of these assets from the pledge assures that AIG has not pledged all or substantially all of its assets to the NY Fed.

4. Revolving Credit Agreement and Guarantee and Pledge Agreement between AIG and the Federal Reserve Bank of New York *(continued)*

At September 30, 2008, the amount owed under the Fed Facility totaled $63 billion, which included accrued fees and interest of $2 billion added to the principal of cash borrowings. The amount available to be borrowed under the Fed Facility is not generally reduced for the amount of fees and interest added to cash borrowings.

See Note 11 to the Consolidated Financial Statements, regarding borrowings under the Fed Facility and amendments to the Fed Credit Agreement subsequent to September 30, 2008.

5. Shareholders' Equity and Earnings (Loss) Per Share

Shareholders' Equity

Series C Perpetual, Convertible, Participating Preferred Stock

Pursuant to the Fed Credit Agreement, AIG agreed to issue 100,000 shares of Series C Preferred Stock to the Trust in the fourth quarter of 2008.

Under the terms of the Fed Credit Agreement prior to its amendment on November 9, 2008, the terms of the Series C Preferred Stock were as follows: The Series C Preferred Stock will have voting rights commensurate with an approximately 79.9 percent holding of all outstanding shares of common stock. Holders of the Series C Preferred Stock will be entitled to participate in dividends paid on the common stock, receiving up to 79.9 percent of the aggregate amount of dividends paid on the shares of common stock then outstanding. After the Series C Preferred Stock is issued, AIG will be required to hold a special shareholders' meeting to amend its restated certificate of incorporation to increase the number of authorized shares of common stock to 19 billion and to reduce the par value per share. The holders of the common stock will be entitled to vote as a class separate from the holders of the Series C Preferred Stock on these changes to AIG's Restated Certificate of Incorporation. If the increase in the number of authorized shares and change in par value is approved, the Series C Preferred Stock will become convertible into common stock. The number of shares into which the Series C Preferred Stock will be convertible is that which will result in a 79.9 percent holding, after conversion, based upon the number of common shares outstanding on the issue date of the Series C Preferred Stock, plus the number of common shares that are subsequently issued in settlement of Equity Units. Subject to certain exceptions, while the United States Treasury beneficially owns at least 50 percent of the Series C Preferred Stock (or the shares into which the Series C Preferred Stock is convertible), AIG will be prohibited from issuing any capital stock, or any securities or instruments convertible or exchangeable into, or exercisable for, capital stock, without the Trust's consent. In addition, AIG is required to enter into a registration rights agreement that will provide demand registration rights for the Series C Preferred Stock and will require AIG to apply for the listing on the NYSE of the common stock underlying the Series C Preferred Stock. As described in Note 11 to the Consolidated Financial Statements, the November 9, 2008 agreement in principle provides that AIG will issue 10-year warrants to the United States Treasury, and the number of shares into which the Series C Preferred Stock will be convertible will be reduced so as not to exceed 77.9 percent of the outstanding shares of common stock.

AIG received the consideration in the form of the Fed Facility for the Series C Preferred Stock in the third quarter of 2008 and recorded the fair value of the Series C Preferred Stock, $23 billion, as an increase to additional paid-in capital. The value, net of the $500,000 cash portion of the consideration, was recognized as an addition to the prepaid commitment fee asset associated with the Fed Facility.

The valuation of the consideration received for the Series C Preferred Stock that AIG agreed to issue was determined by AIG and was primarily based on the implied value of 79.9 percent of AIG indicated by AIG's common stock price after the terms of the Fed Credit Agreement were publicly announced. Other valuation techniques were employed to corroborate this value, taking into consideration both market observable inputs, such as AIG credit spreads, and other inputs. The following key assumptions were utilized in the valuation:

- The valuation date for the Series C Preferred Stock was the date at which consideration was received for the obligation to issue the Series C Preferred Stock, that is, the date borrowings were made available to AIG pursuant to the NY Fed's agreement to enter into the Fed Credit Agreement.
- The Series C Preferred Stock will be economically equivalent to the common stock, will have voting rights commensurate with the common stock, and will be convertible into shares of common stock.
- The price of AIG common stock the day after the announcement of the terms of the NY Fed's agreement to enter into the Fed Credit Agreement provided the most observable market evidence of the valuation of AIG.

Basic and diluted EPS will be affected in any period in which AIG has net income. The effect on basic EPS will be

computed using the two-class method, pursuant to which the earnings of the period will be allocated between the preferred shareholders and the common shareholders, determined on the same basis as if all the earnings were distributed. Prior to any partial conversion of the Series C Preferred Stock, this will result in 79.9 percent of the earnings for the period being allocated to the Series C Preferred Stock, directly reducing the net income available for common shareholders. Diluted EPS will be computed on the more dilutive of the if-converted method and the two-class method. Under the if-converted method, conversion of the Series C Preferred Stock is assumed to have occurred as of the beginning of the period, and the number of common shares that would be issued on conversion is assumed to be the number of additional shares outstanding for the period. Because AIG had losses for the three- and nine-month periods ended September 30, 2008, the Series C Preferred Stock was anti-dilutive to basic and diluted EPS.

Dividends

The quarterly dividend per common share declared in May 2008 and paid on September 19, 2008 was $0.22. Effective September 23, 2008, AIG's Board of Directors suspended the declaration of dividends on AIG's common stock. Pursuant to the Fed Credit Agreement, AIG is restricted from paying dividends on its common stock.

Share Issuance and Repurchase

In February 2007, AIG's Board of Directors increased AIG's share repurchase program by authorizing the purchase of shares with an aggregate purchase price of $8 billion. In November 2007, AIG's Board of Directors authorized the purchase of an additional $8 billion in common stock. In 2007, AIG entered into structured share repurchase arrangements providing for the purchase of shares over time with an aggregate purchase price of $7 billion.

A total of 37,926,059 shares were purchased during the first six months of 2008 to meet commitments that existed at December 31, 2007. There were no repurchases during the third quarter of 2008. At October 31, 2008, $9 billion was available for purchases under the aggregate authorizations.

Pursuant to the Fed Credit Agreement, AIG is restricted from repurchasing shares of its common stock.

In May 2008, AIG sold 196,710,525 shares of common stock at a price per share of $38 for gross proceeds of $7.47 billion and 78,400,000 equity units (the Equity Units) at a price per unit of $75 for gross proceeds of $5.88 billion. The Equity Units, the key terms of which are summarized below, are recorded as long-term borrowings in the consolidated balance sheet.

Equity Units

Each Equity Unit has an initial stated amount of $75 and consists of a stock purchase contract issued by AIG and, initially, a 1/40th or 2.5 percent undivided beneficial ownership interest in three series of junior subordinated debentures (Series B-1, B-2 and B-3), each with a principal amount of $1,000.

Each stock purchase contract requires its holder to purchase, and requires AIG to sell, a variable number of shares of AIG common stock for $25 in cash on each of the following dates: February 15, 2011, May 1, 2011 and August 1, 2011. The number of shares that AIG is obligated to deliver on each stock purchase date is set forth in the chart below (where the "applicable market value" is an average of the trading prices of AIG's common stock over the 20-trading-day period ending on the third business day prior to the relevant stock purchase date).

If the applicable market value is:	then AIG is obligated to issue:
• Greater than or equal to $45.60	• 0.54823 shares per stock purchase contract
• Between $45.60 and $38.00	• Shares equal to $25 divided by the applicable market value
• Less than or equal to $38.00	• 0.6579 shares per stock purchase contract

Basic earnings (loss) per share (EPS) will not be affected by outstanding stock purchase contracts. Diluted EPS will be determined considering the potential dilution from outstanding stock purchase contracts using the treasury stock method, and therefore diluted EPS will not be affected by outstanding stock purchase contracts until the applicable market value exceeds $45.60.

AIG is obligated to pay quarterly contract adjustment payments to the holders of the stock purchase contracts, at an initial annual rate of 2.7067 percent applied to the stated amount. The present value of the contract adjustment payments, $431 million, was recognized at inception as a liability (a component of other liabilities), and was recorded as a reduction to additional paid-in capital.

In addition to the stock purchase contracts, as part of the Equity Units, AIG issued $1.96 billion of each of the Series B-1, B-2 and B-3 junior subordinated debentures, which initially pay interest at rates of 5.67 percent, 5.82 percent and 5.89 percent, respectively. For accounting purposes, AIG allocated the proceeds of the Equity Units between the stock purchase contracts and the junior subordinated debentures on a relative fair value basis. AIG determined that the fair value of the stock purchase contract at issuance was zero, and therefore all of the proceeds were allocated to the junior subordinated debentures.

Share-based Employee Compensation Plans

During the first quarter of 2008, AIG reviewed the vesting schedules of its share-based employee compensation plans, and on March 11, 2008, AIG's management and the Compensation and Management Resources Committee of AIG's Board of Directors determined that, to fulfill the objective of attracting and retaining high quality personnel, the vesting schedules of certain awards outstanding under these plans and all awards made in the future under these plans should be shortened.

For accounting purposes, a modification of the terms or conditions of an equity award is treated as an exchange of the original award for a new award. As a result of this modification, the incremental compensation cost related to the affected awards totaled $24 million and will, together with the unamortized originally-measured compensation cost, be amortized over shorter periods. AIG estimates the modifications will increase the amortization of this cost by $106 million and $46 million in 2008 and 2009, respectively, with a related reduction in amortization expense of $128 million in 2010 through 2013.

In the second quarter of 2008, reversals of previously accrued costs related to certain performance-based compensation plans were made, as performance to date was below the performance thresholds set forth in those plans.

Earnings (Loss) Per Share (EPS)

Basic EPS is based on the weighted average number of common shares outstanding. Diluted EPS is based on those shares used in basic EPS plus shares that would have been outstanding assuming issuance of common shares for all dilutive potential common shares outstanding.

The computation of basic and diluted EPS was as follows:

	Three Months Ended September 30,		Nine Months Ended September 30,	
(in millions, except per share data)	**2008**	2007	**2008**	2007
Numerator for EPS:				
Net income (loss)	**$(24,468)**	$3,085	**$(37,630)**	$11,492
Denominator for EPS:				
Weighted average shares outstanding used in the computation of EPS:				
Common stock issued	**2,948**	2,751	**2,850**	2,751
Common stock in treasury	**(259)**	(189)	**(251)**	(168)
Deferred shares	**14**	14	**14**	13
Weighted average shares outstanding – basic*	**2,703**	2,576	**2,613**	2,596
Incremental shares arising from awards outstanding under share-based employee compensation plans*	**–**	13	**–**	13
Weighted average shares outstanding – diluted*	**2,703**	2,589	**2,613**	2,609
EPS:				
Basic	**$ (9.05)**	$ 1.20	**$ (14.40)**	$ 4.43
Diluted	**$ (9.05)**	$ 1.19	**$ (14.40)**	$ 4.40

* *Calculated using the treasury stock method. Certain potential common shares arising from share-based employee compensation plans were not included in the computation of diluted EPS because the effect would have been anti-dilutive. The number of potential shares excluded was 7 million for the nine-month period ended September 30, 2007. Additionally, the Preferred Stock to be issued was not included in the computation of basic or diluted EPS because the effect would have been anti-dilutive.*

6. Ownership

According to the Schedule 13D/A filed on October 30, 2008, by C.V. Starr & Co., Inc. (Starr), Starr International Company, Inc. (SICO), Edward E. Matthews, Maurice R. Greenberg, the Maurice R. and Corinne P. Greenberg Family Foundation, Inc., the Universal Foundation, Inc., the Maurice R. and Corinne P. Greenberg Joint Tenancy Company, LLC and the C.V. Starr & Co., Inc. Trust, these reporting persons could be considered to beneficially own 278,430,935 shares or approximately 10 percent of AIG's common stock at that date. Although these reporting persons may have made filings under Section 16 of the Exchange Act, reporting sales of shares of common stock, no amendment to the Schedule 13D has been filed to report a change in ownership subsequent to October 30, 2008.

7. Commitments, Contingencies and Guarantees

(a) Litigation and Investigations

AIG and its subsidiaries, in common with the insurance and financial services industries in general, are subject to litigation, including claims for punitive damages, in the normal course of their business. At the current time, AIG cannot predict the outcome of the matters described below, or estimate any potential additional costs related to these matters, unless otherwise indicated. In AIG's insurance operations,

7. Commitments, Contingencies and Guarantees *(continued)*

litigation arising from claims settlement activities is generally considered in the establishment of AIG's reserve for losses and loss expenses. However, the potential for increasing jury awards and settlements makes it difficult to assess the ultimate outcome of such litigation.

Various federal, state and foreign regulatory and governmental agencies are reviewing certain public disclosures, transactions and practices of AIG and its subsidiaries in connection with industry wide and other inquiries. These reviews include the inquiries by the SEC and U.S. Department of Justice (DOJ), previously confirmed by AIG, with respect to AIG's valuation of and disclosures relating to the AIGFP super senior credit default swap portfolio. AIG has cooperated, and will continue to cooperate, in producing documents and other information in response to subpoenas and other requests.

In connection with some of the SEC investigations, AIG understands that some of its employees have received Wells notices and it is possible that additional current and former employees could receive similar notices in the future. Under SEC procedures, a Wells notice is an indication that the SEC staff has made a preliminary decision to recommend enforcement action that provides recipients with an opportunity to respond to the SEC staff before a formal recommendation is finalized.

Although AIG cannot currently quantify its ultimate liability for the unresolved litigation and investigation matters referred to below, it is possible that such liability could have a material adverse effect on AIG's consolidated financial condition, or consolidated results of operations for an individual reporting period.

Litigation Relating to AIGFP's Super Senior Credit Default Swap Portfolio

Securities Actions – Southern District of New York. On May 21, 2008, a purported securities fraud class action complaint was filed against AIG and certain of its current and former officers and directors in the United States District Court for the Southern District of New York (the Southern District of New York). The complaint alleges that defendants made statements during the period May 11, 2007 through May 9, 2008 in press releases, AIG's quarterly and year-end filings and during conference calls with analysts which were materially false and misleading and which artificially inflated the price of AIG's stock. The alleged false and misleading statements relate to, among other things, unrealized market valuation losses on AIGFP's super senior credit default swap portfolio as a result of severe credit market disruption. The complaint alleges claims under Sections 10(b) and 20(a) of the Exchange Act. Three additional purported securities class action complaints were subsequently filed in the Southern District of New York, all containing similar allegations. One of the additional complaints filed on June 19, 2008, alleges a purported class period of November 10, 2006 through June 6, 2008. The Court has not yet appointed a lead plaintiff in these actions.

On October 9, 2008, a purported securities class action complaint was filed in the Southern District of New York on behalf of purchasers of 7.70 percent Series A-5 Junior Subordinated Debentures in connection with AIG's public offering on December 11, 2007 against AIG, certain of its current and former officers and directors, and the offering underwriters. The complaint alleges that defendants made statements in AIG's registration statement, prospectus and quarterly and year-end filings which were materially false and misleading, in violation of Sections 11, 12(a) and 15 of the Securities Act of 1933. The claims are based generally on the same allegations as the securities fraud class actions described above. One additional purported securities class action complaint was filed in the Southern District of New York on October 24, 2008, containing identical allegations.

ERISA Actions – Southern District of New York. On June 25, 2008, the Company, certain of its executive officers and directors, and unnamed members of the Company's Retirement Board and Investment Committee were named as defendants in two separate, though nearly identical, actions filed in the Southern District of New York. The actions purport to be brought as class actions on behalf of all participants in or beneficiaries of certain pension plans sponsored by AIG or its subsidiaries (the Plans) during the period May 11, 2007 through the present and whose participant accounts included investments in the Company's common stock. Plaintiffs allege, among other things, that the defendants breached their fiduciary responsibilities to Plan participants and their beneficiaries under the Employee Retirement Income Security Act of 1974, as amended (ERISA), by: (i) failing to prudently and loyally manage the Plans and the Plans' assets; (ii) failing to provide complete and accurate information to participants and beneficiaries about the Company and the value of the Company's stock; (iii) failing to monitor appointed Plan fiduciaries and to provide them with complete and accurate information; and (iv) breaching their duty to avoid conflicts of interest. The alleged ERISA violations relate to, among other things, the defendants' purported failure to monitor and/or disclose unrealized market valuation losses on AIGFP's super senior credit default swap portfolio as a result of severe credit market disruption. Six additional purported ERISA class action complaints were subsequently filed in the Southern District of New York, each containing similar allegations. It is anticipated that these actions will all be consolidated and that

7. Commitments, Contingencies and Guarantees *(continued)*

the Court will then appoint a lead plaintiff in the consolidated action.

Derivative Actions – Southern District of New York. On November 20, 2007, two purported shareholder derivative actions were filed in the Southern District of New York naming as defendants the then current directors of AIG and certain senior officers of AIG and its subsidiaries. Plaintiffs assert claims for breach of fiduciary duty, waste of corporate assets and unjust enrichment, as well as violations of Section 10(b) of the Exchange Act and Rule 10b-5 promulgated thereunder, and Section 20(a) of the Exchange Act, among other things, in connection with AIG's public disclosures regarding its exposure to what the lawsuits describe as the subprime market crisis. The actions were consolidated as In re American International Group, Inc. 2007 Derivative Litigation (the Consolidated 2007 Derivative Litigation). On February 15, 2008, plaintiffs filed a consolidated amended complaint alleging the same causes of action. On April 15, 2008, motions to dismiss the action were filed on behalf of all defendants. The motions to dismiss are pending.

On August 8, 2008, a purported shareholder derivative action was filed in the Southern District of New York asserting claims on behalf of AIG based generally on the same allegations as in the consolidated amended complaint in the Consolidated 2007 Derivative Litigation.

Derivative Action – Supreme Court of New York. On February 29, 2008, a purported shareholder derivative complaint was filed in the Supreme Court of Nassau County, asserting the same state law claims against the same defendants as in the consolidated amended complaint in the Consolidated 2007 Derivative Litigation. On May 19, 2008, defendants filed a motion to dismiss or to stay the proceedings in light of the pending Consolidated 2007 Derivative Litigation. The motion is pending.

Derivative Action – Delaware Court of Chancery. On September 17, 2008, a purported shareholder derivative complaint was filed in the Court of Chancery of Delaware naming as defendants certain directors and senior officers of AIG and its subsidiaries and asserting claims on behalf of AIG based generally on the same allegations as in the consolidated amended complaint in the Consolidated 2007 Derivative Litigation.

Action by the Starr Foundation – Supreme Court of New York. On May 7, 2008, the Starr Foundation filed a complaint in New York State Supreme Court against AIG, AIG's former Chief Executive Officer, Martin Sullivan, and AIG's then Chief Financial Officer, Steven Bensinger, asserting a claim for common law fraud. The complaint alleges that the defendants made materially misleading statements and omissions concerning alleged multi-billion dollar losses in AIG's portfolio of credit default swaps. The complaint asserts that if the Starr Foundation had known the truth about the alleged losses, it would have sold its remaining shares of AIG stock. The complaint alleges that the Starr Foundation has suffered damages of at least $300 million. On May 30, 2008, a motion to dismiss the complaint was filed on behalf of defendants. The motion to dismiss, which has been converted by the court into a motion for summary judgment, is still pending.

Litigation Relating to the Credit Agreement with the NY Fed

On November 4, 2008, a purported class action was filed in the Delaware Court of Chancery naming as defendants AIG, Chairman and Chief Executive Officer, Edward M. Liddy, and current and past AIG directors. Plaintiff alleges violations of Delaware General Corporation Law Section 242(b)(2) and breaches of fiduciary duty in connection with the Series C Preferred Stock to be issued to the Trust created for the benefit of the United States Treasury pursuant to the Fed Credit Agreement. Plaintiff seeks an order declaring that the Series C Preferred Stock is not convertible into common stock absent a class vote by the holders of the common stock to amend the Restated Certificate of Incorporation to increase the number of authorized common shares and decrease the par value of the common shares, an order declaring that AIG's directors are breaching their fiduciary duties in not seeking alternative or supplemental financing in advance of a stockholder vote on such an amendment to the Restated Certificate of Incorporation, and damages. During a conference with the Court on November 7, 2008, AIG's counsel stated that any amendment to the Restated Certificate of Incorporation to increase the number of authorized common shares or to decrease the par value of the common shares would be the subject of a class vote by the holders of the common stock, and plaintiff's counsel agreed that the plaintiff's request for an order granting this relief is moot.

2006 Regulatory Settlements and Related Matters

2006 Regulatory Settlements. In February 2006, AIG reached a resolution of claims and matters under investigation with the DOJ, the SEC, the Office of the New York Attorney General (NYAG) and the New York State Department of Insurance (DOI). AIG recorded an after-tax charge of $1.15 billion relating to these settlements in the fourth quarter of 2005. The settlements resolved investigations conducted by the SEC, NYAG and DOI in connection with the accounting, financial reporting and insurance brokerage practices of AIG and its subsidiaries, as well as claims relating to the underpayment of certain workers compensation premium taxes and other assessments. These settlements did not, however, resolve

7. Commitments, Contingencies and Guarantees *(continued)*

investigations by regulators from other states into insurance brokerage practices related to contingent commissions and other broker-related conduct, such as alleged bid rigging. Nor did the settlements resolve any obligations that AIG may have to state guarantee funds in connection with any of these matters.

As a result of these settlements, AIG made payments or placed amounts in escrow in 2006 totaling approximately $1.64 billion, $225 million of which represented fines and penalties. Amounts held in escrow totaling approximately $337 million, including interest thereon, are included in other assets at September 30, 2008. At that date, all of the funds were escrowed for settlement of claims resulting from the underpayment by AIG of its residual market assessments for workers' compensation.

In addition to the escrowed funds, $800 million was deposited into a fund under the supervision of the SEC as part of the settlements to be available to resolve claims asserted against AIG by investors, including the securities class action shareholder lawsuits described below.

Also, as part of the settlements, AIG agreed to retain, for a period of three years, an independent consultant to conduct a review that will include, among other things, the adequacy of AIG's internal control over financial reporting, the policies, procedures and effectiveness of AIG's regulatory, compliance and legal functions and the remediation plan that AIG has implemented as a result of its own internal review.

Other Regulatory Settlements. AIG's 2006 regulatory settlements with the SEC, DOJ, NYAG and DOI did not resolve investigations by regulators from other states into insurance brokerage practices. AIG entered into agreements effective January 29, 2008 with the Attorneys General of the States of Florida, Hawaii, Maryland, Michigan, Oregon, Texas and West Virginia; the Commonwealths of Massachusetts and Pennsylvania; and the District of Columbia; as well as the Florida Department of Financial Services and the Florida Office of Insurance Regulation, relating to their respective industry wide investigations into producer compensation and insurance placement practices. The settlements call for total payments of $12.5 million to be allocated among the ten jurisdictions representing restitution to state agencies and reimbursement of the costs of the investigation. During the term of the settlement agreements, AIG will continue to maintain certain producer compensation disclosure and ongoing compliance initiatives. AIG will also continue to cooperate with the industry wide investigations. The agreement with the Texas Attorney General also settles allegations of anticompetitive conduct relating to AIG's relationship with Allied World Assurance Company and includes an additional settlement payment of $500,000 related thereto.

AIG entered into an agreement effective March 13, 2008 with the Pennsylvania Insurance Department relating to the Department's investigation into the affairs of AIG and certain of its Pennsylvania-domiciled insurance company subsidiaries. The settlement calls for total payments of approximately $13.5 million, of which approximately $4.4 million was paid under previous settlement agreements. During the term of the settlement agreement, AIG will provide annual reinsurance reports, as well as maintain certain producer compensation disclosure and ongoing compliance initiatives.

NAIC Examination of Workers Compensation Premium Reporting. During 2006, the Settlement Review Working Group of the National Association of Insurance Commissioners (NAIC), under the direction of the states of Indiana, Minnesota and Rhode Island, began an investigation into AIG's reporting of workers' compensation premiums. In late 2007, the Settlement Review Working Group recommended that a multi-state targeted market conduct examination focusing on workers' compensation insurance be commenced under the direction of the NAIC's Market Analysis Working Group. AIG was informed of the multi-state targeted market conduct examination in January 2008. AIG has been advised that the lead states in the multi-state examination are Delaware, Florida, Indiana, Massachusetts, Minnesota, New York, Pennsylvania, and Rhode Island and that all other states (and the District of Columbia) have agreed to participate. AIG has also been advised that the examination will focus on both legacy issues and AIG's current compliance with legal requirements applicable to AIG's writing and reporting of workers' compensation insurance, but as of October 31, 2008 no determinations had been made with respect to these issues.

Securities Action – Southern District of New York. Beginning in October 2004, a number of putative securities fraud class action suits were filed in the Southern District of New York against AIG and consolidated as In re American International Group, Inc. Securities Litigation. Subsequently, a separate, though similar, securities fraud action was also brought against AIG by certain Florida pension funds. The lead plaintiff in the class action is a group of public retirement systems and pension funds benefiting Ohio state employees, suing on behalf of themselves and all purchasers of AIG's publicly traded securities between October 28, 1999 and April 1, 2005. The named defendants are AIG and a number of present and former AIG officers and directors, as well as Starr, SICO, General Reinsurance Corporation (General Re), and PricewaterhouseCoopers LLP (PwC), among others. The lead plaintiff alleges, among other things, that AIG: (1) concealed that it engaged in anti-competitive conduct through alleged payment of contingent commissions to brokers and participation in illegal bid-rigging; (2) concealed that it used

7. Commitments, Contingencies and Guarantees *(continued)*

"income smoothing" products and other techniques to inflate its earnings; (3) concealed that it marketed and sold "income smoothing" insurance products to other companies; and (4) misled investors about the scope of government investigations. In addition, the lead plaintiff alleges that AIG's former Chief Executive Officer, Maurice R. Greenberg, manipulated AIG's stock price. The lead plaintiff asserts claims for violations of Sections 11 and 15 of the Securities Act of 1933, Section 10(b) of the Exchange Act and Rule 10b-5 promulgated thereunder, Section 20(a) of the Exchange Act, and Section 20A of the Exchange Act. In April 2006, the court denied the defendants' motions to dismiss the second amended class action complaint and the Florida complaint. In December 2006, a third amended class action complaint was filed, which does not differ substantially from the prior complaint. Fact and class discovery is currently ongoing. On February 20, 2008, the lead plaintiff filed a motion for class certification. The class certification motion is pending.

ERISA Action – Southern District of New York. Between November 30, 2004 and July 1, 2005, several ERISA actions were filed in the Southern District of New York on behalf of purported class participants and beneficiaries of three pension plans sponsored by AIG or its subsidiaries. A consolidated complaint filed on September 26, 2005 alleges a class period between September 30, 2000 and May 31, 2005 and names as defendants AIG, the members of AIG's Retirement Board and the Administrative Boards of the plans at issue, and present or former members of AIG's Board of Directors. The factual allegations in the complaint are essentially identical to those in the securities actions described above. The parties have reached an agreement to settle this matter for an amount within AIG's insurance coverage limits. On July 3, 2008, the Court granted preliminary approval of the settlement, and at a hearing on October 7, 2008 the Court issued an order finally approving the settlement, dismissing the action with prejudice. The deadline for filing an appeal from the approval order is November 7, 2008.

Derivative Action – Southern District of New York. Between October 25, 2004 and July 14, 2005, seven separate derivative actions were filed in the Southern District of New York, five of which were consolidated into a single action (the New York 2004/2005 Derivative Litigation). The complaint in this action contains nearly the same types of allegations made in the securities fraud action described above. The named defendants include current and former officers and directors of AIG, as well as Marsh & McLennan Companies, Inc. (Marsh), SICO, Starr, ACE Limited and subsidiaries (ACE), General Re, PwC, and certain employees or officers of these entity defendants. Plaintiffs assert claims for breach of fiduciary duty, gross mismanagement, waste of corporate assets, unjust enrichment, insider selling, auditor breach of contract, auditor professional negligence and disgorgement from AIG's former Chief Executive Officer, Maurice R. Greenberg, and former Chief Financial Officer, Howard I. Smith, of incentive-based compensation and AIG share proceeds under Section 304 of the Sarbanes-Oxley Act, among others. Plaintiffs seek, among other things, compensatory damages, corporate governance reforms, and a voiding of the election of certain AIG directors. AIG's Board of Directors has appointed a special committee of independent directors (Special Committee) to review the matters asserted in the operative consolidated derivative complaint. The court has entered an order staying this action pending resolution of the Delaware 2004/2005 Derivative Litigation discussed below. The court also has entered an order that termination of certain named defendants from the Delaware action applies to this action without further order of the court. On October 17, 2007, plaintiffs and those AIG officer and director defendants against whom the shareholder plaintiffs in the Delaware action are no longer pursuing claims filed a stipulation providing for all claims in this action against such defendants to be dismissed with prejudice. Former directors and officers Maurice R. Greenberg and Howard I. Smith have asked the court to refrain from so ordering this stipulation.

Derivative Actions – Delaware Chancery Court. From October 2004 to April 2005, AIG shareholders filed five derivative complaints in the Delaware Chancery Court. All of these derivative lawsuits were consolidated into a single action as In re American International Group, Inc. Consolidated Derivative Litigation (the Delaware 2004/2005 Derivative Litigation). The amended consolidated complaint named 43 defendants (not including nominal defendant AIG) who, as in the New York 2004/2005 Derivative Litigation, were current and former officers and directors of AIG, as well as other entities and certain of their current and former employees and directors. The factual allegations, legal claims and relief sought in this action are similar to those alleged in the New York 2004/2005 Derivative Litigation, except that the claims are only under state law. In early 2007, the court approved an agreement that AIG be realigned as plaintiff, and, on June 13, 2007, acting on the direction of the Special Committee, AIG filed an amended complaint against former directors and officers Maurice R. Greenberg and Howard I. Smith, alleging breach of fiduciary duty and indemnification. Also on June 13, 2007, the Special Committee filed a motion to terminate the litigation as to certain defendants, while taking no action as to others. Defendants Greenberg and Smith filed answers to AIG's complaint and brought third-party complaints against certain current and former AIG directors and officers, PwC and Regulatory Insurance Services, Inc. On September 28, 2007, AIG and the shareholder plaintiffs filed a combined amended complaint in which AIG continued to assert claims

7. Commitments, Contingencies and Guarantees *(continued)*

against defendants Greenberg and Smith and took no position as to the claims asserted by the shareholder plaintiffs in the remainder of the combined amended complaint. In that pleading, the shareholder plaintiffs are no longer pursuing claims against certain AIG officers and directors. On February 12, 2008, the court granted AIG's motion to stay discovery pending the resolution of claims against AIG in the New York consolidated securities action. The court also directed the parties to coordinate a briefing schedule for the motions to dismiss. On April 11, 2008, the shareholder plaintiffs filed the First Amended Combined Complaint, which added claims against former AIG directors and officers Maurice Greenberg, Edward Matthews, and Thomas Tizzio for breach of fiduciary duty based on alleged bid-rigging in the municipal derivatives market. On June 13, 2008, certain defendants filed motions to dismiss the shareholder plaintiffs' portions of the complaint. The motions to dismiss are pending.

AIG is also named as a defendant in a derivative action in the Delaware Chancery Court brought by shareholders of Marsh. On July 10, 2008, shareholder plaintiffs filed a second consolidated amended complaint, which contains claims against AIG for aiding and abetting a breach of fiduciary duty and contribution and indemnification in connection with alleged bid-rigging and steering practices in the commercial insurance market that are the subject of the Policyholder Antitrust and RICO Actions described below.

Policyholder Antitrust and RICO Actions. Commencing in 2004, policyholders brought multiple federal antitrust and Racketeer Influenced and Corrupt Organizations Act (RICO) class actions in jurisdictions across the nation against insurers and brokers, including AIG and a number of its subsidiaries, alleging that the insurers and brokers engaged in a broad conspiracy to allocate customers, steer business, and rig bids. These actions, including 24 complaints filed in different federal courts naming AIG or an AIG subsidiary as a defendant, were consolidated by the judicial panel on multi-district litigation and transferred to the United States District Court for the District of New Jersey (District of New Jersey) for coordinated pretrial proceedings. The consolidated actions have proceeded in that court in two parallel actions, In re Insurance Brokerage Antitrust Litigation (the Commercial Complaint) and In re Employee Benefit Insurance Brokerage Antitrust Litigation (the Employee Benefits Complaint, and, together with the Commercial Complaint, the Multi-district Litigation).

The plaintiffs in the Commercial Complaint are a group of corporations, individuals and public entities that contracted with the broker defendants for the provision of insurance brokerage services for a variety of insurance needs. The broker defendants are alleged to have placed insurance coverage on the plaintiffs' behalf with a number of insurance companies named as defendants, including AIG subsidiaries. The Commercial Complaint also named various brokers and other insurers as defendants (three of which have since settled). The Commercial Complaint alleges, among other things, that defendants engaged in a widespread conspiracy to allocate customers through bid-rigging and steering practices. Plaintiffs assert that the defendants violated the Sherman Antitrust Act, RICO, and the antitrust laws of 48 states and the District of Columbia, and are liable under common law breach of fiduciary duty and unjust enrichment theories. Plaintiffs seek treble damages plus interest and attorneys' fees as a result of the alleged RICO and Sherman Antitrust Act violations.

The plaintiffs in the Employee Benefits Complaint are a group of individual employees and corporate and municipal employers alleging claims on behalf of two separate nationwide purported classes: an employee class and an employer class that acquired insurance products from the defendants from August 26, 1994 to the date of any class certification. The Employee Benefits Complaint names AIG, as well as various other brokers and insurers, as defendants. The activities alleged in the Employee Benefits Complaint, with certain exceptions, track the allegations made in the Commercial Complaint.

The Court in connection with the Commercial Complaint granted (without leave to amend) defendants' motions to dismiss the federal antitrust and RICO claims on August 31, 2007 and September 28, 2007, respectively. The court declined to exercise supplemental jurisdiction over the state law claims in the Commercial Complaint and therefore dismissed it in its entirety. On January 14, 2008, the court granted defendants' motion for summary judgment on the ERISA claims in the Employee Benefits Complaint and subsequently dismissed the remaining state law claims without prejudice, thereby dismissing the Employee Benefits Complaint in its entirety. On February 12, 2008, plaintiffs filed a notice of appeal to the United States Court of Appeals for the Third Circuit with respect to the dismissal of the Employee Benefits Complaint. Plaintiffs previously appealed the dismissal of the Commercial Complaint to the United States Court of Appeals for the Third Circuit on October 10, 2007. Both appeals are pending.

A number of complaints making allegations similar to those in the Multi-district Litigation have been filed against AIG and other defendants in state and federal courts around the country. The defendants have thus far been successful in having the federal actions transferred to the District of New Jersey and consolidated into the Multi-district Litigation. These additional consolidated actions are still pending in the District of New Jersey, but are currently stayed pending

7. Commitments, Contingencies and Guarantees *(continued)*

a decision by the court on whether they will proceed during the appeal of the dismissal of the Multi-district Litigation. On August 20, 2008, the District Court, however, granted plaintiff's motion to lift the stay in one tag-along matter and suggested that the case be remanded to the transferor court, and on September 17, 2008, the Judicial Panel on Multidistrict Litigation filed a Conditional Transfer Order with respect to this matter. The AIG defendants have also sought to have state court actions making similar allegations stayed pending resolution of the Multi-district Litigation proceeding. These efforts have generally been successful, although plaintiffs in one case pending in Texas state court have moved to re-open discovery; a hearing on that motion was held on April 9, 2008. The court subsequently issued an order deferring a ruling on the motion until the Court holds a hearing on defendants' Special Exceptions. A hearing date has not yet been set. AIG has recently settled several of the various federal and state actions alleging claims similar to those in the Multi-district Litigation, including a state court action pending in Florida in which discovery had been allowed to proceed.

Ohio Attorney General Action – Ohio Court of Common Pleas. On August 24, 2007, the Ohio Attorney General filed a complaint in the Ohio Court of Common Pleas against AIG and a number of its subsidiaries, as well as several other broker and insurer defendants, asserting violation of Ohio's antitrust laws. The complaint, which is similar to the Commercial Complaint, alleges that AIG and the other broker and insurer defendants conspired to allocate customers, divide markets, and restrain competition in commercial lines of casualty insurance sold through the broker defendant. The complaint seeks treble damages on behalf of Ohio public purchasers of commercial casualty insurance, disgorgement on behalf of both public and private purchasers of commercial casualty insurance, as well as a $500 per day penalty for each day of conspiratorial conduct. AIG, along with other co-defendants, moved to dismiss the complaint on November 16, 2007. On June 30, 2008, the Court denied defendants' motion to dismiss. On August 18, 2008, defendants filed their answers to the complaint. Discovery is ongoing.

Action Relating to Workers Compensation Premium Reporting – Northern District of Illinois. On May 24, 2007, the National Workers Compensation Reinsurance Pool (the NWCRP), on behalf of its participant members, filed a lawsuit in the United States District Court for the Northern District of Illinois against AIG with respect to the underpayment by AIG of its residual market assessments for workers compensation. The complaint alleges claims for violations of RICO, breach of contract, fraud and related state law claims arising out of AIG's alleged underpayment of these assessments between 1970 and the present and seeks damages purportedly in excess of $1 billion. On August 6, 2007, the court denied AIG's motion seeking to dismiss or stay the complaint or, in the alternative, to transfer to the Southern District of New York. On December 26, 2007, the court denied AIG's motion to dismiss the complaint. On March 17, 2008, AIG filed an amended answer, counterclaims and third-party claims against the National Council on Compensation Insurance (in its capacity as attorney-in-fact for the NWCRP), the NWCRP, its board members, and certain of the other insurance companies that are members of the NWCRP alleging violations of RICO, as well as claims for conspiracy, fraud, and other state law claims. The counterclaim-and third-party defendants filed motions to dismiss on June 9, 2008. The motions are scheduled for decision on November 20, 2008. Discovery is currently ongoing while the motions are pending.

Action Relating to Workers Compensation Premium Reporting – Minnesota. On February 16, 2006, the Attorney General of the State of Minnesota filed a complaint against AIG with respect to claims by the Minnesota Department of Revenue and the Minnesota Special Compensation Fund, alleging that AIG made false statements and reports to Minnesota agencies and regulators, unlawfully reducing AIG's contributions and payments to Minnesota and certain state funds relating to its workers' compensation premiums. While AIG settled that litigation in December 2007, a similar lawsuit was filed by the Minnesota Workers Compensation Reinsurance Association and the Minnesota Workers Compensation Insurers Association in the United States District Court for the District of Minnesota. On March 28, 2008, the court granted AIG's motion to dismiss the case in its entirety. On April 25, 2008, plaintiffs appealed to the United States Court of Appeals for the Eighth Circuit and also filed a new complaint making similar allegations in Minnesota state court. On April 30, 2008, substantially identical claims were also filed in Minnesota state court by the Minnesota Insurance Guaranty Association and Minnesota Assigned Risk Plan. On September 11, 2008, the parties to both actions entered into a settlement, resulting in the dismissal of all claims against AIG. In exchange for the dismissal and a broad release of claims, the financial terms of the settlement provided for AIG's payment of $21.5 million to plaintiffs and waiver of its right to collect $3.5 million in payments due from the plaintiffs.

Action Relating to Workers Compensation Premium Reporting – District of South Carolina. A purported class action was also filed in the United States District Court for the District of South Carolina on January 25, 2008 against AIG and certain of its subsidiaries, on behalf of a class of employers that obtained workers' compensation insurance from AIG companies and allegedly paid inflated premiums as a result of AIG's alleged underreporting of workers'

7. Commitments, Contingencies and Guarantees *(continued)*

compensation premiums. An amended complaint was filed on March 24, 2008, and AIG filed a motion to dismiss the amended complaint on April 21, 2008. On July 8, 2008, the court granted AIG's motion to dismiss all claims without prejudice and granted plaintiff leave to refile subject to certain conditions. Plaintiffs filed their second amended complaint on July 22, 2008. AIG moved to dismiss the second amended complaint on August 22, 2008. Discovery is stayed pending resolution of the motion to dismiss.

Litigation Relating to SICO and Starr

SICO Action. In July, 2005 SICO filed a complaint against AIG in the Southern District of New York, claiming that AIG had refused to provide SICO access to certain artwork, and asking the court to order AIG immediately to release the property to SICO. AIG filed an answer denying SICO's allegations and setting forth defenses to SICO's claims. In addition, AIG filed counterclaims asserting breach of contract, unjust enrichment, conversion, breach of fiduciary duty, a constructive trust and declaratory judgment, relating to SICO's breach of its commitment to use its AIG shares only for the benefit of AIG and AIG employees. On June 23, 2008, the Court denied in part and granted in part SICO's motion for summary judgment, and on July 31, 2008 the parties submitted a joint pre-trial order. Trial is scheduled to commence on March 2, 2009.

Derivative Action Relating to Starr and SICO. On December 31, 2002, a derivative lawsuit was filed in the Delaware Chancery Court against twenty directors and executives of AIG as well as against AIG as a nominal defendant that alleges, among other things, that the directors of AIG breached the fiduciary duties of loyalty and care by approving the payment of commissions to insurance managing general agencies owned by Starr and of rental and service fees to SICO and the executives breached their duty of loyalty by causing AIG to enter into contracts with Starr and SICO and their fiduciary duties by usurping AIG's corporate opportunities. The complaint further alleges that the Starr agencies did not provide any services that AIG was not capable of providing itself, and that the diversion of commissions to these entities was solely for the benefit of Starr's owners. The complaint also alleges that the service fees and rental payments made to SICO and its subsidiaries were improper. Under the terms of a stipulation approved by the Court on February 16, 2006, the claims against the outside independent directors were dismissed with prejudice, while the claims against the other directors were dismissed without prejudice. In an opinion dated June 21, 2006, the Court denied defendants' motion to dismiss, except with respect to plaintiff's challenge to payments made to Starr before January 1, 2000. On July 21, 2006, plaintiff filed its second amended complaint, which alleges that, between January 1, 2000 and May 31, 2005, individual defendants breached their duty of loyalty by causing AIG to enter into contracts with Starr and SICO and breached their fiduciary duties by usurping AIG's corporate opportunity. Starr is charged with aiding and abetting breaches of fiduciary duty and unjust enrichment for its acceptance of the fees. SICO is no longer named as a defendant. On June 27, 2007, Starr filed a cross-claim against AIG, alleging one count that includes contribution, unjust enrichment and setoff. On November 15, 2007, the Court granted AIG's motion to dismiss the cross-claim by Starr to the extent that it sought affirmative relief from AIG. On February 14, 2008, the Court granted a motion to add former AIG officer Thomas Tizzio as a defendant. As a result, the remaining defendants in the case are AIG (the nominal defendant), Starr and former directors and officers Maurice Greenberg, Howard Smith, Edward Matthews and Thomas Tizzio. On September 30, 2008, the parties filed a stipulation of settlement, and the court scheduled a settlement hearing for December 17, 2008. Pursuant to the settlement, defendants have agreed to payment of $115 million to AIG, net of attorneys' fees and costs, in exchange for receipt of a broad release of claims relating to the allegations in the complaint.

Litigation Matters Relating to AIG's General Insurance Operations

Caremark. AIG and certain of its subsidiaries have been named defendants in two putative class actions in state court in Alabama that arise out of the 1999 settlement of class and derivative litigation involving Caremark Rx, Inc. (Caremark). The plaintiffs in the second-filed action have intervened in the first-filed action, and the second-filed action has been dismissed. An excess policy issued by a subsidiary of AIG with respect to the 1999 litigation was expressly stated to be without limit of liability. In the current actions, plaintiffs allege that the judge approving the 1999 settlement was misled as to the extent of available insurance coverage and would not have approved the settlement had he known of the existence and/or unlimited nature of the excess policy. They further allege that AIG, its subsidiaries, and Caremark are liable for fraud and suppression for misrepresenting and/or concealing the nature and extent of coverage. In addition, the intervenor-plaintiffs allege that various lawyers and law firms who represented parties in the underlying class and derivative litigation (the Lawyer Defendants) are also liable for fraud and suppression, misrepresentation, and breach of fiduciary duty. The complaints filed by the plaintiffs and the intervenor-plaintiffs request compensatory damages for the 1999 class in the amount of $3.2 billion, plus punitive damages. AIG and its subsidiaries deny the allegations of fraud and suppression and have asserted that information concerning the excess policy was publicly disclosed months prior to the approval

7. Commitments, Contingencies and Guarantees *(continued)*

of the settlement. AIG and its subsidiaries further assert that the current claims are barred by the statute of limitations and that plaintiffs' assertions that the statute was tolled cannot stand against the public disclosure of the excess coverage. The plaintiffs and intervenor-plaintiffs, in turn, have asserted that the disclosure was insufficient to inform them of the nature of the coverage and did not start the running of the statute of limitations. On November 26, 2007, the trial court issued an order that dismissed the intervenors' complaint against the Lawyer Defendants and entered a final judgment in favor of the Lawyer Defendants. The matter was stayed pending appeal to the Alabama Supreme Court. In September 2008 the Alabama Supreme Court affirmed the trial court's dismissal of the Lawyer Defendants. It is anticipated that the next steps will be class discovery and a hearing on class certification. AIG cannot reasonably estimate either the likelihood of its prevailing in these actions or the potential damages in the event liability is determined.

(b) Commitments

Flight Equipment

At September 30, 2008, International Lease Finance Corporation (ILFC) had committed to purchase 174 new aircraft deliverable from 2008 through 2019 at an estimated aggregate purchase price of $16.9 billion. ILFC will be required to find customers for any aircraft acquired, and it must arrange financing for portions of the purchase price of such equipment.

ILFC has ordered 74 Boeing 787 aircraft with the first aircraft now scheduled to be delivered in late 2011. Boeing has made several announcements concerning the delays in the deliveries of the 787s. Boeing has informed ILFC that its 787 deliveries will be delayed, on average, an excess of 27 months per aircraft. Such delays will span across ILFC's entire order, with the original contracted deliveries running from 2010 through 2017. ILFC expects further delays on its future Boeing aircraft deliveries resulting from the recent labor strike.

Other Commitments

In the normal course of business, AIG enters into commitments to invest in limited partnerships, private equities, hedge funds and mutual funds and to purchase and develop real estate in the U.S. and abroad. These commitments totaled $8.4 billion at September 30, 2008.

On June 27, 2005, AIG entered into an agreement pursuant to which AIG agreed, subject to certain conditions, to make any payment that is not promptly paid with respect to the benefits accrued by certain employees of AIG and its subsidiaries under the SICO Plans (as discussed below under "Benefits Provided by Starr International Company, Inc. and C.V. Starr & Co., Inc.").

(c) Contingencies

Loss Reserves

Although AIG regularly reviews the adequacy of the established reserve for losses and loss expenses, there can be no assurance that AIG's ultimate loss reserves will not develop adversely and materially exceed AIG's current loss reserves. Estimation of ultimate net losses, loss expenses and loss reserves is a complex process for long-tail casualty lines of business, which include excess and umbrella liability, directors and officers liability, professional liability, medical malpractice, workers' compensation, general liability, products liability and related classes, as well as for asbestos and environmental exposures. Generally, actual historical loss development factors are used to project future loss development. However, there can be no assurance that future loss development patterns will be the same as in the past. Moreover, any deviation in loss cost trends or in loss development factors might not be discernible for an extended period of time subsequent to the recording of the initial loss reserve estimates for any accident year. Thus, there is the potential for reserves with respect to a number of years to be significantly affected by changes in loss cost trends or loss development factors that were relied upon in setting the reserves. These changes in loss cost trends or loss development factors could be attributable to changes in inflation, in labor and material costs or in the judicial environment, or in other social or economic phenomena affecting claims.

Deferred Tax Assets

AIG's determination of the realizability of deferred tax assets requires estimates of future taxable income. Such estimates could change in the near term, perhaps materially, which may require AIG to adjust its valuation allowance. Such adjustment, either positive or negative, could be material to AIG's consolidated financial condition or its results of operations. See Note 9 to the Consolidated Financial Statements.

Benefits Provided by Starr International Company, Inc. and C.V. Starr & Co., Inc.

SICO has provided a series of two-year Deferred Compensation Profit Participation Plans (SICO Plans) to certain AIG employees. The SICO Plans were created in 1975 when the voting shareholders and Board of Directors of SICO, a private holding company whose principal asset is AIG common stock, decided that a portion of the capital value of SICO should be used to provide an incentive plan for the current and

7. Commitments, Contingencies and Guarantees *(continued)*

succeeding managements of all American International companies, including AIG.

None of the costs of the various benefits provided under the SICO Plans has been paid by AIG, although AIG has recorded a charge to reported earnings for the deferred compensation amounts paid to AIG employees by SICO, with an offsetting amount credited to additional paid-in capital reflecting amounts considered to be contributed by SICO. The SICO Plans provide that shares currently owned by SICO are set aside by SICO for the benefit of the participant and distributed upon retirement. The SICO Board of Directors currently may permit an early payout of units under certain circumstances. Prior to payout, the participant is not entitled to vote, dispose of or receive dividends with respect to such shares, and shares are subject to forfeiture under certain conditions, including but not limited to the participant's voluntary termination of employment with AIG prior to normal retirement age. Under the SICO Plans, SICO's Board of Directors may elect to pay a participant cash in lieu of shares of AIG common stock. Following notification from SICO to participants in the SICO Plans that it will settle specific future awards under the SICO Plans with shares rather than cash, AIG modified its accounting for the SICO Plans from variable to fixed measurement accounting. AIG gave effect to this change in settlement method beginning on December 9, 2005, the date of SICO's notice to participants in the SICO Plans.

(d) Guarantees

AIG and certain of its subsidiaries are parties to derivative financial instruments with market risk resulting from both dealer and end-user activities to reduce currency, interest rate, equity and commodity exposures. These instruments are carried at their fair value in the consolidated balance sheet. The majority of AIG's derivative activity is transacted by AIGFP. See Note 8 to the Consolidated Financial Statements included in the 2007 Annual Report on Form 10-K.

AIG has issued unconditional guarantees with respect to the prompt payment, when due, of all present and future payment obligations and liabilities of AIGFP arising from transactions entered into by AIGFP.

SAI Deferred Compensation Holdings, Inc., a wholly owned subsidiary of AIG, has established a deferred compensation plan for registered representatives of certain AIG subsidiaries, pursuant to which participants have the opportunity to invest deferred commissions and fees on a notional basis. The value of the deferred compensation fluctuates with the value of the deferred investment alternatives chosen. AIG has provided a full and unconditional guarantee of the obligations of SAI Deferred Compensation Holdings, Inc. to pay the deferred compensation under the plan.

See also Note 11 to the Consolidated Financial Statements for information on the termination of selected AIG voluntary non-qualified deferred compensation plans.

8. Employee Benefits

The components of the net periodic benefit cost with respect to pensions and other postretirement benefits were as follows:

	Pensions			Postretirement		
(in millions)	Non-U.S. Plans	U.S. Plans	Total	Non-U.S. Plans	U.S. Plans	Total
Three Months Ended September 30, 2008						
Components of net periodic benefit cost:						
Service cost	**$ 34**	**$ 32**	**$ 66**	**$2**	**$ 2**	**$ 4**
Interest cost	**16**	**49**	**65**	**1**	**4**	**5**
Expected return on assets	**(11)**	**(59)**	**(70)**	–	–	–
Amortization of prior service cost	**(3)**	–	**(3)**	–	–	–
Amortization of net loss	**15**	**3**	**18**	–	–	–
Curtailment gain	**(6)**	–	**(6)**	–	–	–
Settlement gain	**(1)**	–	**(1)**	–	–	–
Net periodic benefit cost	**$ 44**	**$ 25**	**$ 69**	**$3**	**$ 6**	**$ 9**
Three Months Ended September 30, 2007						
Components of net periodic benefit cost:						
Service cost	$ 22	$ 30	$ 52	$1	$ 3	$ 4
Interest cost	12	45	57	1	3	4
Expected return on assets	(9)	(53)	(62)	–	–	–
Amortization of prior service cost	(2)	(1)	(3)	–	–	–
Amortization of net loss	2	9	11	–	–	–
Amortization of initial net obligation	1	–	1	–	–	–
Settlement loss	–	3	3	–	–	–
Net periodic benefit cost	$ 26	$ 33	$ 59	$2	$ 6	$ 8
Nine Months Ended September 30, 2008						
Components of net periodic benefit cost:						
Service cost	**$ 84**	**$ 96**	**$ 180**	**$6**	**$ 6**	**$12**
Interest cost	**44**	**149**	**193**	**3**	**12**	**15**
Expected return on assets	**(34)**	**(178)**	**(212)**	–	–	–
Amortization of prior service cost	**(8)**	**(1)**	**(9)**	–	–	–
Amortization of net loss	**22**	**12**	**34**	–	–	–
Curtailment gain	**(6)**	–	**(6)**	–	–	–
Settlement loss	**1**	–	**1**	–	–	–
Net periodic benefit cost	**$103**	**$ 78**	**$ 181**	**$9**	**$18**	**$27**
Nine Months Ended September 30, 2007						
Components of net periodic benefit cost:						
Service cost	$ 66	$ 90	$ 156	$4	$ 8	$12
Interest cost	36	134	170	2	11	13
Expected return on assets	(27)	(160)	(187)	–	–	–
Amortization of prior service cost	(7)	(2)	(9)	–	(1)	(1)
Amortization of net loss	7	27	34	–	–	–
Amortization of initial net obligation	1	–	1	–	–	–
Settlement loss	1	3	4	–	–	–
Net periodic benefit cost	$ 77	$ 92	$ 169	$6	$18	$24

Expected Cash Flows

As disclosed in its 2007 Annual Report on Form 10-K, AIG expected to contribute $118 million to its U.S. and non-U.S. pension plans in 2008. For the nine months ended September 30, 2008, AIG had contributed $122 million to its U.S. and non-U.S. pension plans. Based upon the current funded status of the plans, the current interest rate environment, and the

projected performance of pension plan assets, additional expected contributions for the U.S. and non-U.S. pension plans in the 2008 fourth quarter range from approximately $168 million to $532 million. Actual contributions will depend on asset performance, foreign exchange rates, and the interest rate environment as of December 31, 2008. Actual contributions may also vary as a result of anticipated business dispositions.

9. Federal Income Taxes

Interim Period Tax Assumptions and Effective Tax Rates

AIG's interim period tax expense or benefit is measured using an estimated annual effective tax rate. To the extent that a portion of AIG's annual pretax income or loss cannot be reliably estimated, the actual tax expense or benefit applicable to that income or loss is reported in the interim period in which the related income or loss is reported. AIG is unable to reliably estimate impairments of goodwill, other-than-temporary impairments, realized capital gains and losses, and the operating results of AIGFP. Therefore, the tax effects of these items, to the extent deductible, are calculated at the applicable local statutory rate (predominantly 35 percent) and are reported as discrete adjustments to the estimated annual effective tax rate that AIG applies to all other pretax income.

The effective tax rate on the pre-tax loss for the three-month period ended September 30, 2008 was 12.3 percent. The effective tax rate was lower than the statutory rate of 35 percent due primarily to $6.9 billion of deferred tax expense recorded during the third quarter, comprising $3.6 billion of deferred tax expense attributable to the potential sale of foreign businesses, and a $3.3 billion valuation allowance to reduce tax benefits on capital losses to the amount that AIG believes is more likely than not to be realized.

The effective tax rate on the pre-tax loss for the nine-month period ended September 30, 2008 was 21.5 percent and was also lower than the statutory rate primarily due to the $6.9 billion of deferred tax expense, which is discussed above, as well as other tax charges previously recorded.

The effective tax rates on pre-tax income for the three- and nine-month periods ended September 30, 2007 were 30.0 percent and 28.0 percent, respectively. These effective tax rates were lower than the statutory rate due primarily to benefits from remediation adjustments and the recognition of tax benefits associated with the SICO Plan for which the compensation expense was recognized in prior years.

Valuation Allowances

In general, realization of deferred tax assets depends on a company's ability to generate sufficient taxable income of the appropriate character within the carryforward periods of the jurisdictions in which the net operating losses and deductible temporary differences were incurred. AIG assessed its ability to realize the deferred tax asset of $19.1 billion and concluded a $3.3 billion valuation allowance was required to reduce the deferred tax asset to an amount AIG believes is more likely than not to be realized.

When making its assessment, AIG considered all available evidence, including future reversals of existing taxable temporary differences, estimated future GAAP taxable income, and tax-planning strategies AIG would implement, if necessary, to realize the net deferred tax asset.

In assessing future GAAP taxable income, AIG considered its strong earnings history exclusive of the recent losses on the super senior credit default swap portfolio and from the securities lending program, because AIG expects to enter into transactions with the NY Fed to limit exposure to future losses. AIG also considered taxable income from the sales of businesses under its asset disposition plan, the continuing earnings strength of the insurance businesses it intends to retain and its recently announced debt and preferred stock transactions with the NY Fed and United States Treasury, respectively, together with other actions AIG is taking, when assessing the ability to generate sufficient future taxable income during the relevant carryforward periods to realize the deferred tax asset. See Note 11 to the Consolidated Financial Statements.

In evaluating the realizability of the loss carryforwards, AIG considered the relief provided by IRS Notice 2008-84 which provides that the limitation on loss carryforwards that can arise as a result of one or more acquisitions of stock of a loss company will not apply to such stock acquisitions for any period during which the United States becomes a direct or indirect owner of a more than 50 percent interest in the loss company.

At September 30, 2008, AIG has recorded deferred tax assets related to stock compensation of $200 million. Due to the significant decline in AIG's stock price, these deferred tax assets may not be realizable in the future. FAS 123(R) precludes AIG from recognizing an impairment charge on these assets until the related stock awards are either exercised, vested or expired. Any charge associated with the deferred tax asset would be reflected in additional paid-in capital rather than income tax expense.

Undistributed Earnings

During the three months ended September 30, 2008, AIG recorded $3.6 billion of deferred tax expense attributable to foreign businesses. This deferred tax, primarily related to GAAP and tax differences such as DAC, has not been previously recorded because the earnings from certain

9. Federal Income Taxes *(continued)*

non-U.S. subsidiaries had been reinvested abroad indefinitely. At September 30, 2008, AIG continues to maintain permanent reinvestment assertions with respect to foreign general insurance and related companies. Approximately $7 billion of GAAP earnings related to such foreign general insurance and related companies has not been subject to U.S. tax under Accounting Principles Board Opinion No. 23, "Accounting for Income Taxes — Special Areas".

Tax Filings and Examinations

On March 20, 2008, AIG received a Statutory Notice of Deficiency from the IRS for years 1997 to 1999. The Notice asserted that AIG owes additional taxes for these years primarily due to the disallowance of foreign tax credits. AIG has paid the assessed tax plus interest and penalties for 1997 and has filed a claim for refund. AIG has also paid the additional taxes, interest, and penalties assessed for 1998 and 1999. AIG will vigorously defend its position, and continues to believe that it has adequate reserves for any liability that could result from the IRS actions.

During the third quarter, the IRS announced a settlement initiative with respect to certain taxpayers that participated in targeted leasing transactions. On October 6, 2008, AIG notified the IRS of its decision to participate in the settlement offer. In accordance with FIN 48 and FSP 13-2, AIG anticipates recording an after-tax charge of approximately $34 million to $100 million for this matter in the fourth quarter of 2008.

FIN 48

As of September 30, 2008 and December 31, 2007, AIG's unrecognized tax benefits, excluding interest and penalties, were $2.4 billion and $1.3 billion, respectively. As of September 30, 2008 and December 31, 2007, AIG's unrecognized tax benefits included $689 million and $299 million, respectively, related to tax positions the disallowance of which would not affect the effective tax rate. Accordingly, as of September 30, 2008 and December 31, 2007, the amounts of unrecognized tax benefits that, if recognized, would favorably affect the effective tax rate were $1.7 billion and $1.0 billion, respectively. Substantially all of the increase as of September 30, 2008 was attributable to the quarter ended March 31, 2008.

At September 30, 2008, AIG had accrued $420 million for the payment of interest (net of the federal benefit) and penalties.

AIG continually evaluates proposed adjustments by taxing authorities. At September 30, 2008, such proposed adjustments would not result in a material change to AIG's consolidated financial condition, although it is possible that the effect could be material to AIG's consolidated results of operations for an individual reporting period. Although it is reasonably possible that a significant change in the balance of unrecognized tax benefits may occur within the next twelve months, at this time it is not possible to estimate the range of the change due to the uncertainty of the potential outcomes.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

10. Information Provided in Connection with Outstanding Debt

The following condensed consolidating financial statements reflect the results of AIG Life Holdings (US), Inc. (AIGLH), formerly known as American General Corporation, a holding company and a wholly owned subsidiary of AIG. AIG provides a full and unconditional guarantee of all outstanding debt of AIGLH.

In addition, AIG Liquidity Corp. and AIG Program Funding, Inc. are both wholly owned subsidiaries of AIG. AIG provides a full and unconditional guarantee of all obligations of AIG Liquidity Corp. and AIG Program Funding, Inc. There are no reportable amounts for these entities.

Condensed Consolidating Balance Sheet

(in millions)	American International Group, Inc. (As Guarantor)	AIGLH	Other Subsidiaries	Eliminations	Consolidated AIG
September 30, 2008					
Assets:					
Investments and Financial Services assets	**$ 11,394**	**$ 40**	**$ 869,197**	**$(117,148)**	**$ 763,483**
Loans to subsidiaries	**61,470**	**–**	**(61,470)**	**–**	**–**
Cash	**1,260**	**–**	**17,310**	**–**	**18,570**
Carrying value of subsidiaries and partially owned companies, at equity	**83,608**	**27,740**	**35,616**	**(146,373)**	**591**
Other assets	**43,812**	**2,629**	**191,936**	**1,216**	**239,593**
Total assets	**$201,544**	**$30,409**	**$1,052,589**	**$(262,305)**	**$1,022,237**
Liabilities:					
Insurance liabilities	**$ –**	**$ –**	**$ 547,857**	**$ (108)**	**$ 547,749**
Federal Reserve Bank of New York credit facility	**62,960**	**–**	**–**	**–**	**62,960**
Other long-term borrowings	**48,285**	**2,136**	**227,226**	**(116,057)**	**161,590**
Other liabilities	**19,117**	**3,040**	**155,888**	**611**	**178,656**
Total liabilities	**130,362**	**5,176**	**930,971**	**(115,554)**	**950,955**
Preferred shareholders' equity in subsidiary companies	**–**	**–**	**100**	**–**	**100**
Total shareholders' equity	**71,182**	**25,233**	**121,518**	**(146,751)**	**71,182**
Total liabilities, preferred shareholders' equity in subsidiary companies and shareholders' equity	**$201,544**	**$30,409**	**$1,052,589**	**$(262,305)**	**$1,022,237**
December 31, 2007					
Assets:					
Investments and Financial Services assets	$ 13,378	$ 40	$ 850,414	$ (21,790)	$ 842,042
Cash	84	1	2,199	–	2,284
Carrying value of subsidiaries and partially owned companies, at equity	111,714	24,396	18,542	(153,998)	654
Other assets	10,684	2,592	189,950	155	203,381
Total assets	$135,860	$27,029	$1,061,105	$(175,633)	$1,048,361
Liabilities:					
Insurance liabilities	$ 43	$ –	$ 528,059	$ (75)	$ 528,027
Long-term borrowings	36,045	2,136	156,003	(18,135)	176,049
Other liabilities	3,971	2,826	244,672	(3,085)	248,384
Total liabilities	40,059	4,962	928,734	(21,295)	952,460
Preferred shareholders' equity in subsidiary companies	–	–	100	–	100
Total shareholders' equity	95,801	22,067	132,271	(154,338)	95,801
Total liabilities, preferred shareholders' equity in subsidiary companies and shareholders' equity	$135,860	$27,029	$1,061,105	$(175,633)	$1,048,361

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

10. Information Provided in Connection with Outstanding Debt *(continued)*

Condensed Consolidating Statement of Income (Loss)

(in millions)	American International Group, Inc. (As Guarantor)	AIGLH	Other Subsidiaries	Eliminations	Consolidated AIG
Three Months Ended September 30, 2008					
Operating income (loss)	**$ (3,250)**	**$ (24)**	**$(24,911)**	**$ –**	**$(28,185)**
Equity in undistributed net income of consolidated subsidiaries	**(17,803)**	**(7,858)**	**–**	**25,661**	**–**
Dividend income from consolidated subsidiaries	**881**	**75**	**–**	**(956)**	**–**
Income taxes (benefits)	**4,296***	**(1)**	**(7,775)**	**–**	**(3,480)**
Minority interest	**–**	**–**	**237**	**–**	**237**
Net income (loss)	**$(24,468)**	**$ (7,806)**	**$(16,899)**	**$ 24,705**	**$(24,468)**
Three Months Ended September 30, 2007					
Operating income (loss)	$ (587)	$ (37)	$ 5,503	$ –	$ 4,879
Equity in undistributed net income of consolidated subsidiaries	2,343	55	–	(2,398)	–
Dividend income from consolidated subsidiaries	1,109	320	–	(1,429)	–
Income taxes (benefits)	(220)	256	1,427	–	1,463
Minority interest	–	–	(331)	–	(331)
Net income (loss)	$ 3,085	$ 82	$ 3,745	$ (3,827)	$ 3,085
Nine Months Ended September 30, 2008					
Operating income (loss)	**$ (4,135)**	**$ (65)**	**$(44,005)**	**$ –**	**$(48,205)**
Equity in undistributed net income of consolidated subsidiaries	**(31,721)**	**(10,833)**	**–**	**42,554**	**–**
Dividend income from consolidated subsidiaries	**2,354**	**75**	**–**	**(2,429)**	**–**
Income taxes (benefits)	**4,128***	**(8)**	**(14,494)**	**–**	**(10,374)**
Minority interest	**–**	**–**	**201**	**–**	**201**
Net income (loss)	**$(37,630)**	**$(10,815)**	**$(29,310)**	**$ 40,125**	**$(37,630)**
Nine Months Ended September 30, 2007					
Operating income (loss)	$ (1,130)	$ (123)	$ 18,632	$ –	$ 17,379
Equity in undistributed net income of consolidated subsidiaries	9,192	546	–	(9,738)	–
Dividend income from consolidated subsidiaries	3,274	978	–	(4,252)	–
Income taxes (benefits)	(156)	249	4,775	–	4,868
Minority interest	–	–	(1,019)	–	(1,019)
Net income (loss)	$ 11,492	$ 1,152	$ 12,838	$(13,990)	$ 11,492

* *Income taxes recorded by the Parent company include deferred tax expense attributable to the potential sale of foreign businesses and a valuation allowance on capital losses. See Note 9 to the Consolidated Financial Statements for additional information.*

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(unaudited) (continued)*

10. Information Provided in Connection with Outstanding Debt *(continued)*

Condensed Consolidating Statement of Cash Flows

(in millions)	American International Group, Inc. (As Guarantor)	AIGLH	Other Subsidiaries	Consolidated AIG
Nine Months Ended September 30, 2008				
Net cash provided by (used in) operating activities	**$ (238)**	**$ 179**	**$ 2,241**	**$ 2,182**
Cash flows from investing:				
Invested assets disposed	**1,014**	**–**	**118,971**	**119,985**
Invested assets acquired	**(3,925)**	**–**	**(136,156)**	**(140,081)**
Loans to subsidiaries	**(75,290)**	**–**	**75,290**	**–**
Other	**465**	**(180)**	**12,351**	**12,636**
Net cash provided by (used in) investing activities	**(77,736)**	**(180)**	**70,456**	**(7,460)**
Cash flows from financing activities:				
Federal Reserve Bank of New York credit facility borrowings	**61,000**		**–**	**61,000**
Issuance of long-term borrowings	**21,586**		**89,972**	**111,558**
Repayments of long-term borrowings	**(4,771)**		**(109,280)**	**(114,051)**
Proceeds from common stock issued	**7,343**		**–**	**7,343**
Payments advanced to purchase shares	**(1,000)**		**–**	**(1,000)**
Cash dividends paid to shareholders	**(1,629)**		**–**	**(1,629)**
Other	**(3,379)**	**–**	**(38,283)**	**(41,662)**
Net cash provided by (used in) financing activities	**79,150**	**–**	**(57,591)**	**21,559**
Effect of exchange rate changes on cash	**–**		**5**	**5**
Change in cash	**1,176**	**(1)**	**15,111**	**16,286**
Cash at beginning of period	**84**	**1**	**2,199**	**2,284**
Cash at end of period	**$ 1,260**	**$ –**	**$ 17,310**	**$ 18,570**
Nine Months Ended September 30, 2007				
Net cash provided by (used in) operating activities	$ (95)	$ 375	$ 27,269	$ 27,549
Cash flows from investing:				
Invested assets disposed	2,129	–	124,600	126,729
Invested assets acquired	(8,634)	–	(152,187)	(160,821)
Other	(1,199)	(220)	(30,351)	(31,770)
Net cash provided by (used in) investing activities	(7,704)	(220)	(57,938)	(65,862)
Cash flows from financing activities:				
Issuance of long-term borrowings	13,540	–	58,499	72,039
Repayments of long-term borrowings	(1,143)	–	(48,500)	(49,643)
Payments advanced to purchase shares	(5,000)	–	–	(5,000)
Cash dividends paid to shareholders	(1,372)	–	–	(1,372)
Other	1,723	(154)	21,371	22,940
Net cash provided by (used in) financing activities	7,748	(154)	31,370	38,964
Effect of exchange rate changes on cash			8	8
Change in cash	(51)	1	709	659
Cash at beginning of period	76	–	1,514	1,590
Cash at end of period	$ 25	$ 1	$ 2,223	$ 2,249

10. Information Provided in Connection with Outstanding Debt *(continued)*

Supplementary disclosure of cash flow information:

(in millions)	Nine Months Ended September 30, **2008**	2007
Intercompany non-cash financing activities:		
Settlement of repurchase agreement with loan receivable	**$ 3,160**	–
Intercompany non-cash investing activities:		
Capital contributions to subsidiaries through forgiveness of loans	**$14,510**	–

During the second quarter of 2008, AIG made certain revisions to the American International Group, Inc. (as Guarantor) Condensed Statement of Cash Flows, primarily relating to the effect of reclassifying certain intercompany and securities lending balances. Accordingly, AIG revised the previous period presented to conform to the revised presentation. There was no effect on the Consolidated Statement of Cash Flows or ending cash balances.

The revisions and their effect on the American International Group, Inc. (as Guarantor) Condensed Statement of Cash Flows for the nine months ended September 30, 2007 were as follows:

(in millions)	Originally Reported September 30, 2007	Revisions	As Revised
Cash flows provided by (used in) operating activities	$ 1,627	$(1,722)	$ (95)
Cash flows provided by (used in) investing activities	(7,799)	95	(7,704)
Cash flows provided by (used in) financing activities	6,121	1,627	7,748

11. Subsequent Events

Utilization of the Fed Facility

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

(in millions)	Inception Through September 30, 2008	Inception Through November 5, 2008
Borrowings:		
Loans to AIGFP for collateral postings, GIA and other maturities	**$35,340**	**$43,100**
Capital contributions to insurance companies [(a)]	**13,341**	**13,687**
Repayment of obligations to securities lending program	**3,160**	**3,160**
AIG Funding commercial paper maturities	**2,717**	**3,714**
Repayment of intercompany loans	**1,528**	**1,528**
Contributions to AIGCFG subsidiaries	**1,094**	**1,591**
Debt repayments	**1,038**	**1,578**
Other borrowings [(a)]	**2,782**	**8,642**
Total borrowings	**61,000**	**77,000**
Repayments:		
Repayments not reducing available amounts	**–**	**16,000** [(b)]
Repayments reducing available amounts	**–**	**–**
Total repayments	**–**	**16,000**
Net borrowings	**61,000**	**61,000**
Total Fed Facility	**85,000**	**85,000**
Remaining available amount	**24,000**	**24,000**
Net borrowings	**61,000**	**61,000**
Paid in kind interest and fees	**1,960**	**1,960**
Total balance outstanding	**$62,960**	**$62,960**

(a) Includes securities lending activities.

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

11. Subsequent Events *(continued)*

Preferred Equity Investment by the United States Treasury Pursuant to TARP

On November 9, 2008, AIG and the United States Treasury agreed in principle to a transaction pursuant to which the United States Treasury will purchase from AIG $40 billion liquidation preference of newly issued perpetual preferred stock (Series D Preferred Shares) under the United States Treasury's Troubled Asset Relief Program (TARP). The Series D Preferred Shares will be in addition to the Series C Preferred Stock related to the Fed Credit Agreement. AIG is required to use the net proceeds from the sale of the Series D Preferred Shares to repay a portion of the outstanding balance under the Fed Facility.

The Series D Preferred Shares will rank *pari passu* with the Series C Preferred Stock and senior to AIG's common stock. The Series D Preferred Shares will have limited class voting rights and will accumulate cumulative compounding dividends at a rate equal to 10 percent per annum. The dividends will be payable when, as and if declared by AIG's Board of Directors. AIG will not be able to declare or pay any dividends on AIG's common stock or on any AIG preferred stock ranking *pari passu* with or junior to the Series D Preferred Shares until dividends on the Series D Preferred Shares have been paid. AIG may redeem the Series D Preferred Shares at the stated liquidation preference, plus accumulated but unpaid dividends, at any time that the Trust or a successor entity beneficially owns less than 30 percent of AIG's voting securities and no holder of the Series D Preferred Shares controls or has the potential to control AIG.

Pursuant to the agreement between AIG and the United States Treasury in connection with the Series D Preferred Shares, for as long as the United States Treasury owns any of the Series D Preferred Shares, AIG will be subject to restrictions on its ability to repurchase capital stock, and will be required to adopt and maintain policies limiting corporate expenses, lobbying activities and executive compensation.

In connection with the issuance of the Series D Preferred Shares, AIG will also issue a 10-year warrant to the United States Treasury exercisable for a number of shares of common stock of AIG equal to two percent of the issued and outstanding shares of common stock on the date of the issuance (in connection with the issuance of the warrant, the voting, dividend and conversion rights of the Series C Preferred Stock will be reduced from 79.9 percent to 77.9 percent.) The warrant will be exercisable at any time and will have an exercise price equal to the par value of AIG's common stock at the time of exercise. The United States Treasury has agreed that it will not exercise any voting rights with respect to the common stock issued upon exercise of the warrant. The warrant will not be subject to contractual transfer restrictions other than restrictions necessary to comply with U.S. federal and state securities laws. AIG will be obligated, at the request of the United States Treasury, to file a registration statement with respect to the warrant and the common stock for which the warrant can be exercised. During the 10-year term of the warrant, if the shares of common stock of AIG are no longer listed or trading on a national securities exchange, AIG may be obligated, at the direction of the United States Treasury, to exchange all or a portion of the warrant for another economic interest of AIG classified as permanent equity under U.S. GAAP with an equivalent fair value. If the Series D Preferred Shares issued in connection with the warrant are redeemed in whole or transferred to third parties, AIG may repurchase the warrant then held by the United States Treasury at any time for its fair market value so long as no holder of the warrant controls or has the potential to control AIG. As a result of the issuance of the warrant, the number of shares into which the Series C Preferred Stock will be convertible will be reduced to 77.9 percent of the outstanding shares of common stock.

Amending the Fed Credit Agreement

On November 9, 2008, AIG and the NY Fed agreed, subject to the issuance of the Series D Preferred Shares, to amend the Fed Credit Agreement to, among other things, (i) provide that the total commitment under the Fed Facility following the issuance of the Series D Preferred Shares shall be $60 billion; (ii) reduce the interest rate payable on outstanding borrowings under the Fed Facility from three-month LIBOR (not less than 3.5 percent) plus 8.5 percent per annum to three-month LIBOR (not less than 3.5 percent) plus 3.0 percent per annum; (iii) reduce the fee payable on undrawn amounts from 8.5 percent per annum to 0.75 percent per annum; and (iv) extend the term of the Fed Facility from two years to five years.

Securities Lending Agreement with the Federal Reserve Bank of New York

On October 8, 2008, certain of AIG's life insurance and retirement services subsidiaries entered into a securities lending agreement with the NY Fed, providing that the NY Fed will borrow, on an overnight basis on commercial terms and conditions, investment grade fixed maturity securities from these AIG subsidiaries in return for cash collateral. Prior to this arrangement, draw downs under the existing Fed Facility were used, in part, to settle securities lending transactions. The NY Fed has been borrowing securities pursuant to the securities lending agreement, which has allowed AIG to replenish liquidity in the securities lending program on an as-needed basis, while providing possession and control of these third-party securities to the NY Fed.

As of November 5, 2008, the total value of securities lending payables amounted to $34.2 billion, with $19.9 billion of this amount payable to the NY Fed under this agreement.

AIG's U.S. securities lending program is scheduled to be terminated in the fourth quarter of 2008 as further described below.

Transfer of RMBS by Certain AIG Insurance Subsidiaries

AIG and the NY Fed expect to establish a facility under which approximately $40 billion principal amount of residential mortgage-backed securities (RMBS) related to AIG's U.S. securities lending program will be transferred by certain AIG insurance subsidiaries to a newly-formed limited liability company (the RMBS LLC) that will be financed by the NY Fed and AIG. Proceeds to the insurance company subsidiaries, together with other AIG funds, will be used to return all cash collateral posted by securities borrowers, including approximately $19.9 billion to be returned to the NY Fed. After all collateral is returned, AIG's U.S. securities lending program will be terminated.

The aggregate proceeds to the AIG insurance company subsidiaries will be equal to the estimated fair value of the RMBS at October 31, 2008, adjusted for collections and certain other events between such date and the closing date of the purchase, which is expected to be prior to November 30, 2008. At September 30, 2008, the fair value of the RMBS being transferred was $23.5 billion. AIG will provide $1 billion of proceeds to the AIG entities and the NY Fed will provide the remainder of the proceeds up to $22.5 billion.

Interest on both the NY Fed's senior loan and AIG's subordinated loan will be capitalized (converted to principal of the related loan instead of being paid in cash). Payments of interest on, and principal of, the RMBS and the net sale proceeds, if any, on the RMBS received by the RMBS LLC will be used to pay principal of the NY Fed's senior loan in full before any payments are made on AIG's subordinated loan. None of the obligations of RMBS LLC have recourse to AIG, although AIG's subordinated loan will be exposed to losses of the RMBS LLC up to $1 billion plus the amount of capitalized interest thereon. After the loans have returned amounts equal to their principal and capitalized interest, payments with respect to the remaining RMBS received by the RMBS LLC will be allocated as contingent interest on both of the loans. There are no economic interests in the RMBS LLC other than the NY Fed's senior loan and AIG's subordinated loan.

The implementation of RMBS LLC is subject to approval of the relevant state insurance commissioners.

Terminations of Multi-Sector Credit Default Swap Transactions and Sale of Underlying CDOs

AIGFP has currently outstanding multi-sector credit default swaps with third-party counterparties related to CDOs. Such credit default swaps require that AIGFP post collateral with the counterparties to secure its obligations based on fair value deterioration, ratings downgrades of referenced obligations and downgrades of AIG's ratings. As of November 5, 2008, AIGFP had either agreed to post or posted collateral based on exposures calculated in respect of multi-sector credit default swaps in an aggregate net amount of $37.3 billion.

AIG and the NY Fed expect to establish a facility in which a newly-formed limited liability company (the CDO LLC) will offer to purchase CDOs from the counterparties, who will concurrently with such purchase terminate the related credit default swaps. AIGFP and the NY Fed have begun negotiating the terminations; depending on the level of counterparty participation, on the closing date, the NY Fed will advance up to $30 billion (the Tranche A Loan) and AIG will advance $5 billion (the Tranche B Loan) to the CDO LLC to fund the purchase price of such CDOs. Separately, AIG will pay the costs associated with the unwind of the related CDSs, and so will bear the risk of declines in the market value of the CDOs through October 31, 2008. After the closing date, AIGFP will not be subject to any further collateral calls related to the terminated credit default swaps.

Interest on both the Tranche A Loan and the Tranche B Loan will be capitalized. Payments of interest on, and principal of, the CDOs received by the CDO LLC will be used to pay principal and interest of the Tranche A Loan in full before any payments may be made on the Tranche B Loan. None of the obligations of the CDO LLC have recourse to AIG, although AIG's Tranche B Loan will be exposed to losses of the CDO LLC up to its principal amount plus the amount of capitalized interest thereon. After the loans have returned amounts equal to their principal and capitalized interest, payments with respect to the remaining CDOs received by the CDO LLC will be allocated as contingent interest on both of the loans. There are no economic interests in the CDO LLC other than the Tranche A Loan and Tranche B Loan.

Because the successful implementation of the proposed establishment of CDO LLC depends on the agreement of counterparties to terminate their super senior credit default swaps, no assurance can be given that this facility will be completed or, if completed, on the level of participation.

Commercial Paper Funding Facility

On October 27, 2008, four AIG affiliates applied for participation in the NY Fed's Commercial Paper Funding Facility (CPFF). AIG Funding, Inc., ILFC, Curzon Funding LLC and Nightingale Finance LLC may issue up to approximately

$6.9 billion, $5.7 billion, $7.2 billion and $1.1 billion, respectively, of commercial paper under the CPFF. As of November 5, 2008, these entities had borrowed a total of approximately $15.2 billion under this facility, which allowed AIG to repay borrowings under the Fed Facility.

These AIG affiliates are participating in the CPFF on the same terms and conditions as other non-AIG companies.

Proceeds from the issuance of the commercial paper will be used to refinance AIG's outstanding commercial paper as it matures, meet other working capital needs and make voluntary prepayments under the Fed Facility. The voluntary repayments of the Fed Facility will not reduce the amount available to be borrowed thereunder.

Asset Disposition Plan

AIG has recently hired a Vice Chairman and Chief Restructuring Officer to oversee the asset disposition plan to sell assets and businesses to repay the Fed Facility.

AIG intends to retain the majority of its U.S. property and casualty and foreign general insurance businesses, and to retain an ownership interest in certain of its foreign life insurance operations. AIG is exploring divestiture opportunities for its remaining businesses. Proceeds from these sales are contractually required to be applied toward the repayment of the Fed Facility. None of the businesses under consideration for sale at September 30, 2008 met the criteria in FAS 144, "Accounting for the Impairment or Disposal of Long-Lived Assets" to qualify as "held for sale." Management continues to evaluate the status of its asset sales with respect to these criteria.

In connection with AIG's asset disposition plan, subsequent to September 30, 2008, AIG entered into negotiations to sell certain operations in its General Insurance, Life Insurance and Retirement Services, Financial Services and Asset Management operating segments. These operations had total assets and liabilities with carrying values of approximately $9 billion and $6 billion, respectively, at September 30, 2008. AIG expects to enter into purchase agreements with respect to these assets during the fourth quarter of 2008.

Dispositions of certain businesses may be subject to regulatory approval.

Termination of Voluntary Deferred Compensation Plans

In October 2008, the Compensation and Management Resources Committee of the Board of Directors approved the termination of 14 voluntary deferred compensation plans. In accordance with the provisions of Section 409A of the Code, these plans will terminate and approximately $503 million in deferred compensation, which had been previously accrued, will be paid out to employees, agents and registered representatives during the first quarter of 2009.

ITEM 2. Management's Discussion and Analysis of Financial Condition and Results of Operations

Management's Discussion and Analysis of Financial Condition and Results of Operations is designed to provide the reader a narrative with respect to AIG's operations, financial condition and liquidity and certain other significant matters.

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Cautionary Statement Regarding Projections and Other Information About Future Events

This Quarterly Report on Form 10-Q and other publicly available documents may include, and AIG's officers and representatives may from time to time make, projections concerning financial information and statements concerning future economic performance and events, plans and objectives relating to the establishment of special purpose vehicles with the NY Fed, asset dispositions, liquidity, collateral posting requirements, management, operations, products and services, and assumptions underlying these projections and statements. These projections and statements are not historical facts but instead represent only AIG's belief regarding future events, many of which, by their nature, are inherently uncertain and outside AIG's control. These projections and statements may address, among other things, the number, size, terms and timing of dispositions and their potential effect on AIG's businesses, financial condition, results of operations, cash flows and liquidity (and AIG at any time and from time to time may change its plans with respect to the sale of one or more businesses), the effect on AIG's liquidity of the establishment of two special purpose vehicles with the NY Fed, AIG's exposures to subprime mortgages, monoline insurers and the residential and commercial real estate markets and AIG's strategy for growth, product development, market position, financial results and reserves. It is possible that AIG's actual results and financial condition may differ, possibly materially, from the anticipated results and financial condition indicated in these projections and statements. Factors that could cause AIG's actual results to differ, possibly materially, from those in the specific projections and statements are discussed in Risk Factors, and throughout this Management's Discussion and Analysis of Financial Condition and Results of Operations (MD&A) and in Item 1A. Risk Factors of this Quarterly Report on Form 10-Q and Item 1A. Risk Factors of AIG's Annual Report on Form 10-K for the year ended December 31, 2007 (2007 Annual Report on Form 10-K). AIG is not under any obligation (and expressly disclaims any such obligations) to update or alter any projection or other statement, whether written or oral, that may be made from time to time, whether as a result of new information, future events or otherwise.

In addition to reviewing AIG's results for the three and nine months ended September 30, 2008, this MD&A supplements and updates the information and discussion included in the 2007 Annual Report on Form 10-K to reflect developments in or affecting AIG's business to date during 2008. Throughout this MD&A, AIG presents its operations in the way it believes will be most meaningful. Statutory loss ratios and combined ratios are presented in accordance with accounting principles prescribed by insurance regulatory authorities because these are standard measures of performance filed with insurance regulatory authorities and used for analysis in the insurance industry and thus allow more meaningful comparisons with AIG's insurance competitors. AIG also uses cross-references to additional information included in this Quarterly Report on Form 10-Q and in the 2007 Annual Report on Form 10-K to assist readers seeking related information on a particular subject.

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

In connection with the preparation of its third quarter Form 10-Q, management has assessed whether AIG has the ability to continue as a going concern. In making this assessment, AIG has considered:

- The liquidity events leading up to September 22, 2008;
- AIG's liquidity-related actions and plans to stabilize its businesses and repay the facility (Fed Facility) created pursuant to the $85 billion credit agreement, dated September 22, 2008 (Fed Credit Agreement), between AIG and the Federal Reserve Bank of New York (NY Fed);
- The negative effects of the liquidity events on AIG's businesses and AIG's efforts to address such effects; and
- The substantial risks to which AIG is subject.

Each of these items is discussed in more detail below.

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

It is possible that the actual outcome of one or more of management's plans could be materially different or that one or more of management's significant judgments or estimates about the potential effects of the risks and uncertainties could be prove to be materially incorrect or that the principal transactions disclosed in Note 11 to the Consolidated Financial Statements (and as discussed below) do not result in completed transactions. If one or more of these possible outcomes were realized, AIG may not have sufficient cash to meet its obligations. If AIG needs funds in excess of amounts available from the sources described below, AIG would need to find additional financing and, if such additional financing were to be unavailable, there could be substantial doubt about AIG's ability to continue as a going concern.

Liquidity Events Leading Up to September 22, 2008

Liquidity Entering the Third Quarter

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

Strategic Review and Proposed Liquidity Measures

From mid-July and throughout August 2008, AIG's then Chief Executive Officer, Robert Willumstad, was engaged in a review of AIG's businesses. Mr. Willumstad had announced that he would hold an investor meeting on September 25, 2008 to present the results of his review.

During this same time period, AIG was engaged in a review of measures to address the liquidity concerns in AIG's securities lending portfolio discussed in previous SEC filings and to address the ongoing collateral calls with respect to AIGFP's super senior multi-sector credit default swap portfolio. To facilitate this process, AIG asked a number of investment banking firms to discuss possible solutions to these issues. In late August, AIG engaged J.P. Morgan Securities, Inc. (J.P. Morgan) to assist in developing alternatives, including a potential additional capital raise.

Continuing Liquidity Pressures

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

In addition, from July 1, 2008 to August 31, 2008, the continuing decline in value of the super senior collateralized debt obligations (CDO) securities protected by AIGFP's super senior credit default swap portfolio, together with ratings downgrades of such CDO securities, resulted in AIGFP posting or agreeing to post collateral in an aggregate net amount of $6.0 billion.

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

Rating Agencies

In early September 2008, AIG met with the representatives of the principal rating agencies to discuss Mr. Willumstad's

strategic review as well as the liquidity issues arising from AIG's securities lending program and AIGFP's super senior multi-sector CDO credit default swap portfolio. On Friday, September 12, 2008, S&P placed AIG on CreditWatch with negative implications and noted that upon completion of its review, the agency could affirm AIG parent's current rating of "AA-" or lower the rating by one to three notches. AIG understood that both S&P and Moody's would re-evaluate AIG's ratings early in the week of September 15, 2008. Also on Friday, September 12, 2008, AIG's subsidiaries ILFC and AGF were unable to replace all of their maturing commercial paper with new issuances of commercial paper. As a result, AIG advanced loans to these subsidiaries to meet their commercial paper obligations.

The Accelerated Capital Raise Attempt

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

AIG Attempts to Enter into a Syndicated Secured Lending Facility

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

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

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

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

The Private Sector Solution Fails

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

Also, on September 16, 2008, AIG was notified by its insurance regulators that it would no longer be permitted to borrow funds from its insurance company subsidiaries under a revolving credit facility that AIG had maintained with certain of its insurance subsidiaries acting as lenders. Subsequently, the insurance regulators required AIG to repay any outstanding loans under that facility and to terminate it. The intercompany facility was terminated effective September 22, 2008.

Fed Credit Agreement

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

$37 billion from the NY Fed before formally entering into the Fed Credit Agreement.

On September 22, 2008, AIG entered into the Fed Credit Agreement in the form of a two-year secured loan and a Guarantee and Pledge Agreement (the Pledge Agreement) with the NY Fed. See Notes 5 and 11 to the Consolidated Financial Statements for more information regarding the terms of and borrowings under the Fed Credit Agreement.

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

(in millions)	Inception Through September 30, 2008	Inception Through November 5, 2008
Borrowings:		
Loans to AIGFP for collateral postings, GIA and other maturities	$35,340	$43,100
Capital contributions to insurance companies[(a)]	13,341	13,687
Repayment of obligations to securities lending program	3,160	3,160
AIG Funding commercial paper maturities	2,717	3,714
Repayment of intercompany loans	1,528	1,528
Contributions to AIGCFG subsidiaries	1,094	1,591
Debt repayments	1,038	1,578
Other borrowings[(a)]	2,782	8,642
Total borrowings	61,000	77,000
Repayments:		
Repayments not reducing available amounts	–	16,000 [(b)]
Repayments reducing available amounts	–	–
Total repayments	–	16,000
Net borrowings	61,000	61,000
Total Fed Facility	85,000	85,000
Remaining available amount	24,000	24,000
Net borrowings	61,000	61,000
Paid in kind interest and fees	1,960	1,960
Total balance outstanding	$62,960	$62,960

(a) Includes securities lending activities.

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

Liquidity Related Actions and Plans

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

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

Preferred Equity Investment by the United States Treasury Pursuant to TARP

On November 9, 2008, AIG and the United States Treasury agreed in principle to a transaction pursuant to which the United States Treasury will purchase from AIG $40 billion liquidation preference of newly issued perpetual preferred stock (Series D Preferred Shares) under TARP. The Series D Preferred Shares will be in addition to the Series C Preferred Stock that AIG is obligated to issue to the Trust in connection with the Fed Credit Agreement. AIG is required to use the net proceeds from the sale of the Series D Preferred Shares to repay a portion of the outstanding balance under the Fed Facility.

The Series D Preferred Shares will rank *pari passu* with the Series C Preferred Stock and senior to AIG's common stock. The Series D Preferred Shares will have limited class voting rights and will accumulate cumulative compounding dividends at a rate equal to 10 percent per annum. The dividends will be payable when, as and if declared by AIG's Board of Directors. AIG will not be able to declare or pay any dividends on AIG's common stock or on any AIG preferred stock ranking *pari passu* with or junior to the Series D Preferred Shares until dividends on the Series D Preferred Shares have been paid. AIG may redeem the Series D Preferred Shares at the stated liquidation preference, plus accumulated but unpaid dividends, at any time that the Trust or any successor entity beneficially owns less than 30 percent of AIG's voting securities and no holder of Series D Preferred Shares controls or has the potential to control AIG.

Pursuant to the agreement between AIG and the United States Treasury in connection with the Series D Preferred Shares, for as long as the United States Treasury owns any of the Series D Preferred Shares, AIG will be subject to restrictions on its ability to repurchase capital stock and will

be required to adopt and maintain policies on corporate expenses, lobbying activities and executive compensation.

In connection with the issuance of the Series D Preferred Shares, AIG will also issue a 10-year warrant to the United States Treasury exercisable for a number of shares of common stock of AIG equal to two percent of the issued and outstanding shares of common stock on the date of the investment. In connection with the issuance of the warrant, the voting, conversion rights and dividend rights of the Series C Preferred Stock will be reduced from 79.9 percent to 77.9 percent. The warrant will be exercisable at any time and have an exercise price equal to the par value of AIG's common stock at the time of exercise. The United States Treasury has agreed that it will not exercise any voting rights with respect to the common stock issued upon exercise of the warrant. The warrant will not be subject to contractual transfer restrictions other than restrictions necessary to comply with U.S. federal and state securities laws. AIG will be obligated, at the request of the United States Treasury, to file a registration statement with respect to the warrant and the common stock for which the warrant can be exercised. During the 10-year term of the warrant, if the shares of common stock of AIG are no longer listed or trading on a national securities exchange, AIG may be obligated, at the direction of the United States Treasury, to exchange all or a portion of the warrant for another economic interest of AIG classified as permanent equity under U.S. GAAP with an equivalent fair value. If the Series D Preferred Shares issued in connection with the warrant are redeemed in whole, AIG may repurchase the warrant then held by the United States Treasury at any time for its fair value so long as no holder of a warrant controls or has the potential to control AIG. As a result of the issuance of the warrant, the number of shares into which the Series C Preferred Stock will be convertible will be reduced so as not to exceed 77.9 percent of the outstanding shares of common stock.

The Fed Securities Lending Program

On October 8, 2008, certain of AIG's domestic life insurance subsidiaries entered into the Fed Securities Lending Agreement, providing that the NY Fed will borrow, on an overnight basis, investment grade fixed maturity securities from these AIG subsidiaries in return for cash collateral. Prior to this arrangement, draw downs under the existing Fed Facility were used, in part, to settle securities lending transactions. The NY Fed has been borrowing securities under the Fed Securities Lending Agreement, which has allowed AIG to replenish liquidity in the securities lending program on an as-needed basis, while providing possession and control of these third-party securities to the NY Fed.

As of November 5, 2008, the total value of securities lending payables was $34.2 billion, with $19.9 billion of this amount payable to the NY Fed under this agreement. This program will be terminated on the closing of the RMBS sale as described below.

Transfer of RMBS by certain AIG Insurance Subsidiaries

AIG and the NY Fed expect to establish a facility under which approximately $40 billion principal amount of residential mortgage-backed securities (RMBS) related to AIG's U.S. securities lending program will be transferred by certain AIG insurance subsidiaries to a newly-formed limited liability company (the RMBS LLC) that will be financed by the NY Fed and AIG. Proceeds to the insurance company subsidiaries, together with other AIG funds, will be used to return all cash collateral posted by securities borrowers, including approximately $19.9 billion to be returned to the NY Fed. After all collateral is returned, AIG's U.S. Securities lending program will be terminated.

The aggregate proceeds to the AIG insurance subsidiaries will be equal to the estimated fair value of the RMBS at October 31, 2008, adjusted for collections and certain other events between such date and the closing date of the purchase, which is expected to be prior to November 30, 2008. At September 30, 2008, the fair value of the RMBS being transferred was $23.5 billion. AIG will provide $1 billion of proceeds to the AIG entities and the NY Fed will provide the remainder of the proceeds up to $22.5 billion.

Interest on both the NY Fed's senior loan and AIG's subordinated loan will be capitalized (converted to principal of the related loan instead of being paid in cash). Payments of interest on, and principal of, the RMBS and the net sale proceeds, if any, on the RMBS received by the RMBS LLC will be used to pay principal of the NY Fed's senior loan in full before any payments are made on AIG's subordinated loan. None of the obligations of RMBS LLC have recourse to AIG, although AIG's subordinated loan will be exposed to losses of the RMBS LLC up to $1 billion plus the amount of capitalized interest thereon. After the loans have returned amounts equal to their principal and capitalized interest, payments with respect to the remaining RMBS received by the RMBS LLC will be allocated as contingent interest on both of the loans. There are no economic interests in the RMBS LLC other than the NY Fed's senior loan and AIG's subordinated loan.

The implementation of RMBS LLC is subject to the approval of the relevant state insurance commissioners.

Terminations of Multi-Sector Credit Default Swap Transactions

AIGFP currently has outstanding multi-sector credit default swaps with third-party counterparties related to CDOs. Such credit default swaps require that AIGFP post collateral with the counterparties to secure its obligations based on fair value deterioration, ratings downgrades of referenced obligations and downgrades of AIG's ratings. As of November 5, 2008, AIGFP had either agreed to post or posted collateral based on exposures, calculated in respect of super senior credit default swaps in an aggregate net amount of $37.3 billion.

AIG and the NY Fed expect to establish a facility in which a newly-formed limited liability company (the CDO LLC) will offer to purchase CDOs from the counterparties, who will concurrently with such purchase terminate the related credit default swaps. AIGFP and the NY Fed have begun negotiating the terminations; depending on the level of counterparty participation, on the closing date, the NY Fed will advance up to $30 billion (the Tranche A Loan) and AIG will advance up to $5 billion (the Tranche B Loan) to the CDO LLC to fund the purchase price of such CDOs. Separately, AIG will pay the costs associated with the unwind of the related credit default swaps, and so will bear the risk of declines in the market value of the CDOs through October 31, 2008. After the closing date, AIGFP will not be subject to any further collateral calls related to the terminated credit default swaps.

Interest on both the Tranche A Loan and the Tranche B Loan will be capitalized. Payments of interest on, and principal of, the CDOs received by the CDO LLC will be used to pay principal and interest of the Tranche A Loan in full before any payments are made on the Tranche B Loan. None of the obligations of the CDO LLC have recourse to AIG, although AIG's Tranche B Loan will be exposed to losses of the CDO LLC up to its principal amount plus the amount of capitalized interest thereon. After the loans have returned amounts equal to their principal and capitalized interest, payments with respect to the remaining CDOs received by the CDO LLC will be allocated as contingent interest on both of the loans. There are no economic interests in the CDO LLC other than the Tranche A Loan and Tranche B Loan.

Because the successful implementation of the proposed establishment of the CDO LLC depends on the agreement of the counterparties to terminate their super senior credit default swaps, no assurance can be given that this facility will be completed or, if completed, on the level of participation.

Commercial Paper Funding Facility

On October 27, 2008, four AIG affiliates applied for participation in the NY Fed's Commercial Paper Funding Facility (CPFF). AIG Funding, Inc., ILFC, Curzon Funding LLC and Nightingale Finance LLC may issue up to approximately $6.9 billion, $5.7 billion, $7.2 billion and $1.1 billion, respectively, of commercial paper under the CPFF. As of November 5, 2008, these entities had borrowed a total of approximately $15.2 billion under this facility, which allowed AIG to repay borrowings under the Fed Facility.

These AIG affiliates are participating in the CPFF on the same terms and conditions as other non-AIG companies.

Proceeds from the issuance of the commercial paper will be used to refinance AIG's outstanding commercial paper as it matures, meet other working capital needs and make voluntary prepayments under the Fed Facility. The voluntary repayments of the Fed Facility will not reduce the amount available to be borrowed thereunder.

Asset Disposition Plan

AIG has recently hired a Vice Chairman and Chief Restructuring Officer to oversee the asset disposition plan and has developed a plan to sell assets and businesses to repay the Fed Facility.

AIG intends to retain the majority of its U.S. property and casualty and foreign general insurance businesses, and to retain an ownership interest in certain of its foreign life insurance operations. AIG is exploring divestiture opportunities for its remaining businesses. Proceeds from these sales are contractually required to be applied toward the repayment of the Fed Facility. None of the businesses under consideration for sale at September 30, 2008 met the criteria in Statement of Financial Accounting Standards (FAS) No. 144, "Accounting for the Impairment or Disposal of Long-Lived Assets" to qualify as "held for sale." AIG continues to evaluate the status of its asset sales with respect to these criteria.

In connection with AIG's asset disposition plan, subsequent to September 30, 2008, AIG entered into negotiations to sell certain operations in its General Insurance, Life Insurance and Retirement Services, Financial Services and Asset Management operating segments. These operations had total assets and liabilities with carrying values of approximately $9 billion and $6 billion, respectively, at September 30, 2008. AIG expects to enter into purchase agreements with respect to these assets during the fourth quarter of 2008.

Dispositions of certain businesses may be subject to regulatory approval.

Expense Reductions and Preservation of Cash and Capital

AIG has named a Vice Chairman, Transition Planning and Chief Administrative Officer to lead expense reduction initiatives and transition planning. AIG has developed a plan to review significant projects and will eliminate, delay, or curtail those that are discretionary or non-essential and to make available internal resources, reduce cash outflows to outside service providers to improve liquidity. AIG also suspended the dividend on its common stock to preserve capital.

Negative Effects of Liquidity Events

As a result of AIG's deteriorated financial condition and its announced strategies, AIG's businesses have been subjected to strained relationships with customers, brokers, agents, other business partners and employees as well as increased monitoring by regulatory agencies. Specific issues related to AIG's businesses are addressed below.

General Insurance

While the Commercial Insurance Group (CIG) has been generally successful in retaining clients, the amount of business AIG underwrites for clients has declined. Concern over AIG's

financial strength has a particularly adverse effect on CIG underwriting of directors' and officers' insurance, especially at the higher attachment points.

New business activity has been at lower levels, and AIG continues to see pricing pressure in its general insurance business.

The domestic property and casualty companies are beneficiaries of $5.7 billion of letters of credit arranged by AIG and its subsidiaries. Letters of credit totaling $4.2 billion will expire on December 31, 2008 and the remainder will expire on December 31, 2010. These letters of credit secure amounts recoverable from both affiliated and unaffiliated reinsurers. The inability of AIG to renew or replace these letters of credit or otherwise obtain equivalent financial support from AIG or a third-party would result in a significant reduction of the statutory surplus of these property and casualty insurance companies. AIG is pursuing alternatives to letters of credit such as trust agreements and other forms of credit support and is also pursuing opportunities to significantly reduce the need for such security after December 31, 2008.

Capital Maintenance

AIG has capital maintenance agreements with the companies included in the Commercial Insurance and Mortgage Guaranty reporting units under which AIG may be required to provide ongoing capital support.

Life Insurance & Retirement Services

Disruptions in markets throughout the world and AIG's recent liquidity issues have had, and AIG expects will continue to have, a significant adverse effect on Life Insurance & Retirement Services operating results, specifically its net investment income, deferred policy acquisition costs (DAC) and sales inducement asset (SIA) amortization and net realized capital losses in 2008. AIG expects that these events and AIG's previously announced asset disposition plan will continue to be key factors in the remainder of 2008 and into 2009. In addition, AIG parent's liquidity issues have affected certain operations through higher surrender activity, particularly in the U.S. domestic retirement service's fixed annuity business and foreign investment-oriented and retirement service's products in Japan and Asia. For Japan and Korea, surrenders are expected to continue to be higher than historic averages in the next quarter and possibly beyond due to the suspension of sales by some banks, equity market volatility and elevated levels of surrenders. While surrender levels have declined from their peaks in mid-September, they are still higher than historic levels and AIG expects them to remain at these higher than historic levels until the uncertainties relating to AIG are resolved.

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

Due to the high volume of surrender activity for certain investment-oriented products in the U.K., surrender payments were temporarily suspended in accordance with contract terms to provide time to develop an appropriate course of action with the respective distribution network and to protect the interests of the fund's policyholders.

During the three months ended September 30, 2008 and through October 29, 2008, AIG contributed capital totaling $16.6 billion ($11.8 billion of which was contributed using borrowings under the Fed Facility) to certain of its Domestic Life Insurance and Domestic Retirement Services subsidiaries to replace a portion of the capital lost as a result of net realized capital losses. Further capital contributions will be required to the extent additional net realized capital losses are incurred. In Taiwan, AIG expects to contribute approximately $1.4 billion to Nan Shan in November 2008 as a result of the continued declines in the Taiwan equity market. AIG made capital contributions of $1.3 billion to support foreign life operations in Hong Kong and Japan, principally due to the steep decline in AIG's common stock price. Additional capital contributions to certain operations may be necessary during the remainder of 2008, in large measure due to the continued effect of equity market volatility, declining bond prices and net realized capital losses resulting from other-than-temporary impairment charges.

Financial Services

International Lease Finance Corporation

As a result of AIG parent's liquidity issues and related credit rating downgrades, ILFC was unable to borrow in the public short-term and long-term debt markets, and therefore, ILFC borrowed $6.5 billion under its credit facilities in September 2008. ILFC expects to use these borrowings to repay maturing commercial paper and other obligations. AIG expects that ILFC may raise additional funds through secured lending transactions in early 2009. ILFC can also issue commercial paper under the CPFF. ILFC believes that these borrowings and cash from operations, which may include aircraft sales, will permit ILFC to meet its obligations through September 2009, after which AIG would rely upon additional asset sales and funding through the Fed Facility.

Capital Markets

Given the extreme market conditions during the third quarter of 2008, downgrades of AIG's credit ratings by the rating agencies, as well as AIG's intention to refocus on its core business, AIGFP began unwinding certain of its businesses and portfolios. AIG is only entering into new derivative transactions to maintain its current portfolio, reduce risk and hedge

the currency and interest rate risks associated with its affiliated businesses. AIG is also opportunistically terminating contracts. Due to the long-term duration of AIGFP's derivative contracts and the complexity of AIGFP's portfolio, AIG expects that an orderly wind-down will take a substantial period of time.

American General Finance

As a result of AIG parent's liquidity issues and the related credit ratings downgrades, AGF suspended its efforts to borrow in the public short-term and long-term debt markets. As a result, AGF borrowed approximately $4.6 billion under its primary credit facilities in September 2008. AGF anticipates that its primary sources of funds to support its operations and repay its obligations will be finance receivable collections from operations and secured financings, which will require it to limit its lending activities and focus on expense savings. AGF anticipates that its existing sources of funds will be sufficient to meet its debt and other obligations through the first quarter of 2009. AGF will need additional sources of funds at that time, including sales of AGF assets and funding through the Fed Facility.

AIG Consumer Finance Group

AIG's recent liquidity issues and related credit ratings downgrades have materially adversely affected AIG Consumer Finance Group, Inc. (AIGCFG). AIGCFG experienced significant deposit withdrawals in Hong Kong during September 2008. The inability of AIGCFG to access its traditional sources of funding resulted in AIG lending $1.6 billion to subsidiaries of AIGCFG in September and October of 2008. AIG expects that these businesses will continue to be materially adversely affected until the current uncertainties concerning AIG and the potential sale of these businesses are resolved.

Asset Management

The principal cash requirements in Asset Management are to fund warehousing activities, existing capital commitments and certain direct investments.

General disruption in the global equity and credit markets and the liquidity issues at AIG have negatively affected the Institutional Asset Management segment operating results. Distressed global markets have reduced the value of assets under management, translating to lower base management fees and reduced performance fees (carried interest). Tight credit markets have put pressure on the commercial and residential real estate markets, which has caused values in certain geographic locations to fall, resulting in impairment charges on real estate held for investment purposes.

AIG parent's liquidity issues and lower asset performance as a result of challenging market conditions have contributed to the loss of institutional and retail clients as well as higher redemptions from some of AIG's managed hedge and mutual funds. The continued uncertainty in the equity and credit markets, as well as AIG parent's liquidity issues and the proposed asset dispositions, will continue to adversely affect management and performance fees as well as AIG's ability to launch new funds and investment strategies.

Within the Spread-Based Investment business, distressed markets have resulted in significant loss of invested asset value and AIG expects such losses to continue through the remainder of 2008. In addition, given market conditions, AIG does not expect to issue any additional debt to fund the MIP for the foreseeable future.

Other Effects

As disclosed in its 2007 Annual Report on Form 10-K, AIG expected to contribute approximately $118 million to its U.S. and non-U.S. pension plans in 2008. For the nine months ended September 30, 2008, AIG had contributed $122 million to its U.S. and non-U.S. pension plans. Based upon the current funded status of the plans, the current interest rate environment, and the projected performance of pension plan assets, additional expected contributions for the U.S. and non-U.S. pension plans in the 2008 fourth quarter range from approximately $168 million to $532 million. Actual contributions, however, will depend on asset performance, foreign exchange rates, and the interest rate environment as of December 31, 2008. Actual contributions may also vary as a result of anticipated dispositions.

Regulators in various jurisdictions in which AIG entities operate have imposed additional requirements on the AIG entities. These requirements primarily require AIG to obtain prior approval from the regulator for transactions related to the dispositions of assets, transfers of cash or other transactions outside the normal course of business. In addition, certain regulators have requested additional capital or collateral to be posted. To date, these requirements have not had a significant effect on AIG's operations.

AIG conducted an annual goodwill impairment review as of June 30, 2008. In connection with the decline in the price of AIG's common stock during the third quarter of 2008, AIG conducted an updated goodwill impairment test as of September 30, 2008. As a result of the updated test AIG recognized goodwill impairment charges of $432 million for the three-month period ended September 30, 2008, which were primarily related to the domestic Consumer Finance and the Capital Markets businesses.

In addition, the excess of the fair value over the carrying value of AIG's Personal Lines and foreign Consumer Finance businesses narrowed subsequent to the June 30, 2008 test. As of September 30, 2008, goodwill related to these businesses totaled approximately $700 million and $344 million, respectively. A continuation of the decline in fair value of these

businesses could result in impairment of goodwill in the future.

Risk Factors

The following supplements the significant factors that may affect AIG's business and operations described under "Risk Factors" in Item 1A. of Part I of AIG's 2007 Annual Report on Form 10-K.

Business and Credit Environment

AIG's businesses, results of operations and financial condition have been materially and adversely affected by recent market conditions.

During the third quarter of 2008 continuing through November 2008, worldwide economic conditions significantly deteriorated. The decline in economic conditions has resulted in highly volatile markets, a steep decline in equity markets, further and continuing lack of liquidity, a widening of credit spreads, a lack of price transparency and the collapse of several prominent financial institutions. Global regulators and central banks have taken a number of unprecedented steps to address these issues, but it is unclear whether these measures will be effective or, if effective, when the markets will stabilize.

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

- severe and continued declines in its investment portfolio, leading to significant other-than-temporary impairments;
- significant credit losses due to the failure of, or governmental intervention with respect to, several prominent institutions; and
- a general decline in business activity.

The consequences of these conditions have been more severe for AIG than for other insurers. AIG expects its businesses, financial condition and results of operations will continue to be materially and adversely affected by these conditions for the foreseeable future.

AIG is subject to extensive litigation that may have a material adverse effect on its consolidated financial condition or its consolidated results of operations.

As described in Note 7(a) to the Consolidated Financial Statements, AIG is subject to extensive litigation, including securities class actions. Due to the nature of this litigation, the lack of precise damage claims and the type of claims made against AIG, AIG cannot currently quantify its ultimate liability for these actions. It is possible that such liability could have a material adverse effect on AIG's consolidated financial condition or consolidated results of operations for an individual reporting period.

Credit and Financial Strength Ratings

Adverse ratings actions regarding AIG's long-term debt ratings by Moody's or S&P would require AIG to make additional substantial collateral payments under existing derivative transactions to which AIGFP is a party, which could adversely affect AIG's business and its consolidated results of operations and financial condition.

On September 15, 2008, the following credit rating actions were taken:

- Standard & Poor's, a division of The McGraw-Hill Companies, Inc. (S&P), lowered its long-term debt rating on AIG to 'A-' from 'AA-', and its short-term debt rating to 'A-2' from 'A-1+'. S&P also downgraded the long-term debt and short-term debt ratings of International Lease Finance Corp. (ILFC) to 'A-' from 'A+' and to 'A-2' from 'A-1,' respectively and the long-term and short-term debt ratings of American General Finance Corporation (AGF Corp.) to 'BBB' from 'A+' and to 'A-3' from 'A-1,' respectively. At the same time, S&P lowered its counterparty credit and financial strength ratings on most of AIG's insurance operating subsidiaries to 'A+' from 'AA+'. All of the ratings remained on CreditWatch Negative.
- Moody's Investors Service (Moody's) lowered AIG's senior unsecured debt ratings to 'A2' from 'Aa3' and placed the long-term and short-term ratings on review for possible downgrade. In addition, Moody's downgraded the ratings of several AIG subsidiaries, including the Domestic Life Insurance and Retirement Services companies (Insurer Financial Strength Rating to 'Aa3' from 'Aa2'), and ILFC and AGF Corp. (Senior Unsecured Debt Rating to 'A3' from 'A1' and short-term debt rating to 'P-2' from 'P-1.') Nearly all of AIG's subsidiaries remained on review for possible downgrade.
- Fitch Ratings (Fitch) lowered AIG's long-term issuer rating to 'A' from 'AA-' and its short-term issuer rating to 'F1' from 'F1+'. In addition, Fitch downgraded nearly all of AIG's subsidiaries' Insurer Financial Strength Ratings to 'AA-' from 'AA+.' A majority of the ratings remained on Rating Watch Negative.
- A.M. Best Company (A.M. Best) lowered AIG's issuer credit rating to 'bbb' from 'a+'. In addition, A.M. Best downgraded most of AIG's Insurer Financial Strength Ratings to 'A' from 'A+' and placed the ratings under review with negative implications.

As a consequence of the rating actions, AIGFP estimated that it would need in excess of $20 billion in order to fund additional collateral demands and transaction termination payments in a short period of time. Subsequently, in a period of approximately 15 days following the rating actions, AIGFP was required to fund approximately $32 billion, reflecting not only the effect of the rating actions but also changes in market levels and other factors.

Following the agreement with the NY Fed announced on September 17, 2008, the following credit rating actions were taken:

- S&P upgraded AIG's and ILFC's short-term debt ratings to 'A-1' from 'A-2' and revised the CreditWatch status on all ratings from CreditWatch Negative to CreditWatch Developing.
- Fitch revised the rating watch status on all ratings from Rating Watch Negative to Rating Watch Evolving.

Following AIG's strategic review press release on October 3, 2008, the following credit rating actions were taken:

- S&P revised the CreditWatch status on AIG's and AGF Corp.'s ratings from CreditWatch Developing to CreditWatch Negative.
- Moody's downgraded AIG's Senior Unsecured Debt rating to 'A3' from 'A2' and ILFC and AGF Corp.'s Senior Unsecured Debt ratings to 'Baa1' from 'A3.' Most ratings remain under review for possible downgrade with ILFC revised to under review with direction uncertain.

Credit ratings measure a company's ability to repay its obligations and directly affect the cost and availability to that company of unsecured financing.

In the event of a further downgrade of AIG's long-term senior debt ratings, AIG would be required to post additional collateral and AIG or its counterparties would be permitted to elect early termination of contracts.

It is estimated that as of the close of business on October 27, 2008, based on AIGFP's outstanding municipal GIAs and financial derivative transactions at that date, a downgrade of AIG's long-term senior debt ratings to Baa1 by Moody's and BBB+ by S&P would permit counterparties to make additional calls and permit either AIG or the counterparties to elect early termination of contracts, resulting in up to approximately $5.2 billion of collateral and termination payments, while a downgrade to Baa2 by Moody's and BBB by S&P would result in approximately $0.3 billion in additional collateral and termination payments.

For the multi-sector super senior credit default swap portfolio, it is estimated based on the October 24, 2008 notional values a downgrade of AIG's long-term senior debt ratings to Baa1 by Moody's and BBB+ by S&P, would increase the amount of collateral posted by approximately $2.7 billion due to the adjustment of threshold and independent amount percentages. A downgrade to Baa2 by Moody's and BBB by S&P would allow the counterparties to certain 2a7 puts to elect early termination, resulting in a cash outflow of approximately $3.7 billion. In addition, at that rating level, counterparties to transactions representing approximately $47.8 billion in net notional amount have the right to elect early termination. In the event a counterparty elects to terminate a transaction early, such transaction will be terminated at its replacement value, less any previously posted collateral. Due to current market conditions, it is not possible to reliably estimate the replacement cost of these transactions.

The actual amount of collateral that AIGFP would be required to post to counterparties in the event of such downgrades, or the aggregate amount of payments that AIG could be required to make, depends on market conditions, the fair value of outstanding affected transactions and other factors prevailing at the time of the downgrade. Additional obligations to post collateral or the costs of assignment, repayment or alternative credit could exceed the amounts available under the Fed Credit Agreement. See discussion of the Fed Credit Agreement below.

A downgrade in the short-term credit ratings of the commercial paper programs of certain AIG affiliates could make these issuers ineligible for participation in the NY Fed's Commercial Paper Funding Facility (CPFF).

AIG's affiliates AIG Funding, Inc., ILFC, Curzon Funding LLC and Nightingale Finance LLC currently participate in the CPFF. However, in the event of a downgrade of the short-term credit ratings applicable to the commercial paper programs of these issuers, the affiliates may no longer qualify for participation in the CPFF. The CPFF only purchases U.S. dollar-denominated commercial paper (including asset-backed commercial paper) that is rated at least A-1/P-1/F1 by a major nationally recognized statistical rating organization (NRSRO) or, if rated by multiple major NRSROs, is rated at least A-1/P-1/F1 by two or more major NRSROs. Accordingly, these AIG affiliates will lose access to the CPFF if:

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

A downgrade in the Insurer Financial Strength ratings of AIG's insurance companies could prevent the companies from writing new business and retaining customers and existing business.

Financial strength ratings by the major ratings agencies are an important factor in establishing the competitive position of insurance companies. Financial strength ratings measure an insurance company's ability to meet its obligations to contract holders and policyholders, help maintain public confidence in a company's products, facilitate marketing of products and enhance a company's competitive position.

Further downgrades of the Insurer Financial Strength ratings of AIG's insurance companies may prevent these

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

Fed Facility

The Fed Credit Agreement and the Series D Preferred Shares will require AIG to devote significant resources to debt repayment and preferred dividends for the foreseeable future, thereby reducing capital available for other purposes.

AIG is required to repay the Fed Credit Agreement primarily from the proceeds of sales of assets, including businesses. These mandatory repayments permanently reduce the amount available under the Fed Credit Agreement.

In addition, American General Finance, Inc. (AGF) and ILFC have drawn the full amounts available under their revolving credit facilities and currently do not have access to their traditional sources of long-term or short-term financing through the public debt markets.

Unanticipated collateral calls, continued high surrenders, a downgrade in AIG's credit ratings or a further deterioration in AIGFP's super senior credit default swap portfolio may cause AIG to need additional funding in excess of the borrowings available under the Fed Credit Agreement. If AIG needs funds in excess of those available under the Fed Credit Agreement, AIG will need to find additional financing. Further, an inability to effect asset sales in accordance with its asset disposition plan may result in AIG not being able to timely repay its borrowings under the Fed Credit Agreement. See also Significant Liquidity Requirements — Asset Disposition Plan for a discussion of AIG's asset disposition plan.

The Series D Preferred Shares pay a 10 percent dividend which will not be deductible for tax purposes.

AIG's substantial obligations will require it to dedicate all of its proceeds from asset sales and a considerable portion of its cash flows from operations to the repayment of the Fed Facility, thereby reducing the funds available for other purposes. In addition, because AIG's debt service and preferred dividend obligations will be very high, AIG may be more vulnerable to competitive pressures and expects to have less flexibility to plan for or respond to changing business and economic conditions.

Borrowings under the Fed Credit Agreement are subject to the NY Fed being satisfied with the collateral pledged by AIG.

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

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

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

AIG must sell significant assets to service the debt under the Fed Credit Agreement.

AIG must make asset sales to repay the borrowings under the Fed Credit Agreement. A delay or inability to effect these sales at acceptable prices and terms could result in AIG being unable to repay the Fed Credit Agreement by its maturity date.

While AIG has adopted an asset disposition plan, as discussed under Significant Liquidity Requirements, this plan may not be successfully executed due to, among other things:

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

Further, due to AIG's need to dispose of assets, AIG may be unable to negotiate favorable terms.

If AIG is not able to execute its disposition plan, and cannot otherwise repay the Fed Facility in accordance with its terms, an event of default would result. If an event of default were to occur, the NY Fed could, among other things, declare outstanding borrowings under the Fed Facility immediately due and payable. In addition, an event of default or declaration of acceleration under the Fed Credit Agreement could also result in an event of default under other agreements.

The Fed Credit Agreement includes financial and other covenants that impose restrictions on AIG's financial and business operations.

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

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

AIG's results of operations will be materially adversely affected by a significant increase in interest expense.

AIG expects its results of operations in the fourth quarter of 2008 and in 2009 to be significantly adversely affected by the recognition of interest expense. AIG's initial $1.7 billion commitment fee will amortize over the term of the Fed Facility. Finally, the prepaid commitment fee asset of $23 billion associated with the Preferred Stock to be issued will be amortized through interest expense over the term of the Fed Facility. As a result, AIG anticipates that interest expense in the fourth quarter of 2008 and in the year ended December 31, 2009 will significantly increase as a result of these items. In addition, paid in kind interest expense under the Fed Facility is accrued over the term of the Fed Facility.

Liquidity

AIG's businesses have been adversely affected by AIG's reduced liquidity.

Many of AIG's businesses depend upon the financial stability (both actual and perceived) of AIG parent. Perceptions that AIG or its subsidiaries may not be able to meet their obligations can negatively affect AIG's businesses in many ways, including:

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

AIG's ability to access funds from its subsidiaries is limited.

As a holding company, AIG depends on dividends, distributions and other payments from its subsidiaries to fund payments on AIG's obligations, including its debt securities. In light of AIG's current financial situation, AIG expects that its regulated subsidiaries may be significantly restricted from making dividend payments, or advancing funds, to AIG. This restriction may hinder AIG's ability to access funds that AIG may need to make payments on its obligations, including those arising from day-to-day business activities.

Controlling Shareholder

As a result of the issuance of the Series C Preferred Stock, AIG will be controlled by a trust holding the Series C Preferred Stock for the benefit of the United States Treasury. AIG's interests and those of AIG's minority shareholders may not be the same as those of the United States Treasury.

In accordance with the Fed Credit Agreement, AIG will issue 100,000 shares of Series C Perpetual, Convertible, Participating Preferred Stock (the Series C Preferred Stock) to a trust that will hold the Series C Preferred Stock for the benefit of the United States Treasury (the Trust). Pursuant to the agreement in principle reached by AIG and the NY Fed on November 9, 2008 to amend the NY Fed Credit Agreement, the Series C Preferred Stock is entitled to:

- participate in any dividends paid on the common stock, with the payments attributable to the Series C Preferred Stock being approximately, but not in excess of, 77.9 percent of the aggregate dividends paid on AIG's common stock, treating the Series C Preferred Stock as converted; and
- to the extent permitted by law, vote with AIG's common stock on all matters submitted to AIG's shareholders and hold approximately, but not in excess of, 77.9 percent of the aggregate voting power of the common stock, treating the Series C Preferred Stock as converted.

The Series C Preferred Stock will remain outstanding even if the Fed Facility is repaid in full or otherwise terminates. In addition, upon shareholder approval to certain amendments to AIG's certificate of incorporation, the Trust can convert the Series C Preferred Stock into AIG common stock.

As a result of its ownership, the Trust will be able to elect all of AIG's directors and can control the vote on all matters, including:

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

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

The Trust may also transfer the Series C Preferred Stock to another person or entity and that person or entity may become AIG's controlling shareholder.

Possible future sales of Series C Preferred Stock or AIG common stock by the Trust could adversely affect the market for AIG common stock.

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

Employees

The decline in AIG's common stock price and the announcement of proposed asset dispositions may prevent AIG from retaining key personnel.

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

Change of Control

The issuance of the Series C Preferred Stock may have adverse regulatory consequences for AIG and its subsidiaries and may trigger contractual obligations to third parties.

The Trust will control AIG by virtue of its ownership of the Series C Preferred Stock. AIG and its subsidiaries are subject to various regulatory requirements and are a party to various contracts, agreements, licenses, permits, authorizations and other arrangements (collectively, Arrangements) that contain provisions that, upon a change of control, provide regulators and counterparties with rights to take actions that could have a material effect on AIG's consolidated financial condition, results of operations, or cash flows from an operational, regulatory, compliance, or economic standpoint.

AIG has initiated discussions and activities with regulators and counterparties to take necessary actions to remedy, amend, or comply with the provisions of these Arrangements. AIG has not been notified by regulators or counterparties of their intent to exercise their rights under the Arrangements to a material extent. However, AIG cannot presently predict the effects, if any, the change of control or the other recent events will have on the Arrangements or on AIG's consolidated financial condition, results of operations, or cash flows.

Results of Operations

AIG identifies its operating segments by product line, consistent with its management structure. These segments are General Insurance, Life Insurance & Retirement Services, Financial Services and Asset Management. Through these operating segments, AIG provides insurance, financial and investment products and services to both businesses and individuals in more than 130 countries and jurisdictions. AIG's Other category consists of items not allocated to AIG's operating segments.

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

Consolidated Results

AIG's consolidated statements of income (loss) were as follows:

(in millions)	Three Months Ended September 30, 2008	Three Months Ended September 30, 2007	Percentage Increase/ (Decrease)	Nine Months Ended September 30, 2008	Nine Months Ended September 30, 2007	Percentage Increase/ (Decrease)
Revenues:						
Premiums and other considerations	**$ 21,082**	$19,733	7%	**$ 63,489**	$58,908	8%
Net investment income	**2,946**	6,172	(52)	**14,628**	21,149	(31)
Net realized capital losses	**(18,312)**	(864)	–	**(30,482)**	(962)	–
Unrealized market valuation losses on AIGFP super senior credit default swap portfolio	**(7,054)**	(352)	–	**(21,726)**	(352)	–
Other income	**2,236**	5,147	(57)	**8,953**	12,888	(31)
Total revenues	**898**	29,836	(97)	**34,862**	91,631	(62)
Benefits and expenses:						
Incurred policy losses and benefits	**17,189**	15,595	10	**51,521**	47,962	7
Policy acquisition and other insurance expenses	**6,919**	5,357	29	**18,560**	15,508	20
Interest expense	**2,297**	1,232	86	**4,902**	3,425	43
Other expenses	**2,678**	2,773	(3)	**8,084**	7,357	10
Total benefits and expenses	**29,083**	24,957	17	**83,067**	74,252	12
Income (loss) before income taxes (benefits) and minority interest	**(28,185)**	4,879	–	**(48,205)**	17,379	–
Income taxes (benefits)	**(3,480)**	1,463	–	**(10,374)**	4,868	–
Income (loss) before minority interest	**(24,705)**	3,416	–	**(37,831)**	12,511	–
Minority interest	**237**	(331)	–	**201**	(1,019)	–
Net income (loss)	**$(24,468)**	$ 3,085	–%	**$(37,630)**	$11,492	–%

Premiums and Other Considerations

Premiums and other considerations increased in the three-month period ended September 30, 2008 compared to the same period in 2007 primarily due to increases of $854 million, $420 million and $219 million in premiums from Foreign Life Insurance & Retirement Services, Foreign General Insurance, and Domestic Life Insurance, respectively, partially offset by a decrease of $207 million in premiums from Commercial Insurance. Premiums and other considerations increased in the nine-month period ended September 30, 2008 compared to the same period in 2007 primarily due to increases of $2.9 billion, $1.7 billion, and $513 million in premiums from Foreign Life Insurance & Retirement Services, Foreign General Insurance, and Domestic Life Insurance, respectively, partially offset by a decrease of $855 million in premiums from Commercial Insurance. Foreign Life Insurance & Retirement Services premiums increased principally as a result of increased production and favorable foreign exchange rates. Foreign General Insurance premiums increased primarily due to the positive effect of changes in foreign currency exchange rates and new business from both established and new distribution channels. Domestic Life Insurance premium increased primarily due to an increase in sales of payout annuities. Commercial Insurance premiums decreased primarily due to declines in workers' compensation premiums and other casualty lines of business.

Net Investment Income

The components of consolidated net investment income were as follows:

(in millions)	Three Months Ended September 30, 2008	Three Months Ended September 30, 2007	Percentage Increase/ (Decrease)	Nine Months Ended September 30, 2008	Nine Months Ended September 30, 2007	Percentage Increase/ (Decrease)
Fixed maturities, including short-term investments	**$ 5,773**	$5,406	7%	**$16,691**	$15,976	4%
Equity securities	**277**	226	23	**496**	443	12
Interest on mortgage and other loans	**407**	371	10	**1,182**	1,056	12
Partnerships	**(813)**	274	–	**(641)**	1,444	–
Mutual funds	**(632)**	(19)	–	**(656)**	430	–
Trading account losses	**(501)**	(79)	–	**(722)**	(93)	–
Other investments	**228**	107	113	**768**	665	15
Total investment income before policyholder income and trading gains (losses)	**4,739**	6,286	(25)	**17,118**	19,921	(14)
Policyholder investment income and trading gains (losses)	**(1,561)**	149	–	**(1,729)**	2,026	–
Total investment income	**3,178**	6,435	(51)	**15,389**	21,947	(30)
Investment expenses	**232**	263	(12)	**761**	798	(5)
Net investment income	**$ 2,946**	$6,172	(52)%	**$14,628**	$21,149	(31)%

Net investment income decreased in the three- and nine-month periods ended September 30, 2008 compared to the same periods in 2007 due to losses from partnerships, hedge funds and mutual funds as well as policyholder trading losses and higher trading account losses related to certain investment-oriented products in the U.K. for Life Insurance & Retirement Services. Policyholder trading gains (losses) are offset by a charge or benefit to incurred policy losses and benefits expense. The policyholder trading losses for the three- and nine-month periods ended September 30, 2008 generally reflect the trends in equity markets, principally in Japan and Asia. The decline in net investment income also reflects the effects of higher cash balances for liquidity purposes.

Net Realized Capital Losses

The composition of net realized capital losses was as follows:

(in millions)	Three Months Ended September 30, 2008	Three Months Ended September 30, 2007	Nine Months Ended September 30, 2008	Nine Months Ended September 30, 2007
Sales of fixed maturity securities	**$ (768)**	$(403)	**$ (778)**	$(572)
Sales of equity securities	**288**	265	**608**	708
Sales of real estate and other assets	**97**	210	**422**	709
Other-than-temporary impairments:				
Severity	**(7,327)**	–	**(16,275)**	–
Lack of intent to hold to recovery	**(8,299)**	(240)	**(9,320)**	(614)
Trading at 25 percent or more discount for nine consecutive months	**–**	–	**–**	(6)
Foreign currency declines	**(50)**	(29)	**(1,084)**	(333)
Issuer-specific credit events	**(3,453)**	(124)	**(3,946)**	(316)
Adverse projected cash flows on structured securities	**(747)**	(151)	**(1,621)**	(159)
Foreign exchange transactions	**1,996**	(361)	**1,258**	(469)
Derivative instruments	**(49)**	(31)	**254**	90
Total	**$(18,312)**	$(864)	**$(30,482)**	$(962)

Net realized capital losses increased in the three- and nine-months ended September 30, 2008 compared to the same periods in 2007 primarily due to an increase in other-than-temporary impairment charges. Other-than-temporary impairment charges included the change in AIG's intent and ability to hold to recovery the securities, held as collateral in the securities lending program; an increase in severity losses primarily related to certain RMBS, other structured securities and securities of financial institutions due to rapid and severe market valuation declines where the impairment period was not deemed temporary; and issuer specific credit events; partially offset by the favorable effect of foreign exchange transactions due to

strengthening of the U.S. dollar. See Invested Assets — Portfolio Review — Other-Than-Temporary Impairments.

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

The unrealized market valuation losses on AIGFP's super senior credit default swap portfolio in the three- and nine-month periods ended September 30, 2008 increased compared to the same periods in 2007 due to significant widening in credit spreads and the downgrades of RMBS and CDO securities by rating agencies in the three-month period ended September 30, 2008 driven by the credit concerns resulting from U.S. residential mortgages and the severe liquidity crisis affecting the markets. (See Capital Markets Results and Critical Accounting Estimates — Valuation of Level 3 Assets and Liabilities.

Other Income

Other Income decreased in the three-month period ended September 30, 2008 compared to the same period in 2007 primarily due to a $2.0 billion decrease in Financial Services revenues and a $625 million decrease in Asset Management revenues. Financial Services revenues decreased principally as a result of a net $987 million credit valuation adjustment loss on AIGFP's assets and liabilities which are measured at fair value. AIGFP's revenues were also negatively affected by the disruption in the credit markets and the general decline in liquidity in the marketplace. Asset Management revenues decreased primarily as a result of lower partnership income related to the Spread-Based Investment Business.

Other Income decreased in the nine-month period ended September 30, 2008 compared to the same period in 2007 primarily due to a $1.7 billion decrease in Financial Services revenues and a $1.2 billion decrease in Asset Management revenues. Financial Services revenues decreased principally as a result of a net $1.4 billion credit valuation adjustment loss on AIGFP's assets and liabilities which are measured at fair value. Asset Management revenues decreased primarily as a result of lower guaranteed investment contract revenue due to lower partnership income.

Incurred Policy Losses and Benefits

Incurred policy losses and benefits increased in the three-month period ended September 30, 2008 compared to the same period in 2007 primarily due to a $1.2 billion increase in Commercial Insurance as a result of $1.1 billion of catastrophe-related losses principally from hurricanes Ike and Gustav in 2008, a $464 million increase in Foreign General Insurance as a result of an increase in frequency of smaller claims and higher catastrophe-related losses primarily from hurricanes Ike and Gustav and a $461 million increase in Mortgage Guaranty reflecting the deterioration of the U.S. housing market. Increases in incurred policy losses and benefits of $1.0 billion in Life Insurance & Retirement Services were more than offset by a reduction in losses and benefits arising from policyholder trading losses of $1.7 billion discussed above in Net Investment Income.

Incurred policy losses and benefits increased in the nine-month period compared to the same period in 2007 primarily due to a $1.6 billion increase in Commercial Insurance as a result of higher catastrophe-related losses principally from hurricanes Ike and Gustav in 2008, a $1.2 billion increase in Foreign General Insurance as a result of higher catastrophe-related losses and severe but non-catastrophic losses, and a $1.4 billion increase in Mortgage Guaranty reflecting the deterioration of the U.S. housing market. Increases in incurred policy losses and benefits of $2.7 billion in Life Insurance & Retirement Services were more than offset by a reduction in losses and benefits arising from policyholder trading losses of $3.8 billion discussed above in Net Investment Income.

Policy Acquisition and Other Insurance Expenses

Policy acquisition and other insurance expenses increased in the three-month period ended September 30, 2008 compared to the same period in 2007 primarily due to a $785 million increase in General Insurance expenses and a $777 million increase in Life Insurance & Retirement Services expenses. General Insurance expenses increased primarily due to the recognition of a premium deficiency reserve of $453 million related to United Guaranty Corporation's (UGC) second-lien business. Life Insurance & Retirement Services expenses increased principally as a result of the effect of foreign exchange, growth in the business and the effect of FAS 159 implementation.

Policy acquisition and other insurance expenses increased in the nine-month period ended September 30, 2008 compared to the same period in 2007 primarily due to a $1.6 billion increase in General Insurance expenses and a $1.5 billion increase in Life Insurance & Retirement Services expenses. General Insurance expenses increased primarily due to the recognition of a premium deficiency reserve of $453 million related to UGC's second-lien business, a $432 million increase in compensation-related expenses, and a $275 million change in DAC. Life Insurance & Retirement Services expenses increased primarily due to the effect of foreign exchange, growth in the business and the effect of FAS 159 implementation.

Interest Expense

Interest expense increased in the three- and nine-month periods ended September 30, 2008 compared to the same periods in 2007 reflecting higher borrowings, including interest on the debt and Equity Units from the dates of issuance in May 2008 and borrowings under the Fed facility. Interest expense also includes amortization of the prepaid commitment assets in connection with the Series C Preferred Stock.

Other Expenses

Other Expenses decreased in the three-month period ended September 30, 2008 compared to the same period in 2007 primarily due to a $563 million reversal of accrued compensation expense under AIGFP's various deferred compensation plans and special incentive plan as a result of significant losses recognized by AIGFP in 2008. Offsetting this reversal were goodwill impairment charges of $341 million and $91 million related to Consumer Finance and Capital Markets, respectively, recognized in the third quarter 2008, resulting from the downturn in the housing markets, the credit crisis and the intent to unwind certain AIGFP businesses. An increase in AGF's provision for finance receivable losses of $198 million also contributed to the decline.

Other Expenses increased in the nine-month period ended September 30, 2008 compared to the same period in 2007 primarily as a result of the goodwill impairment charges mentioned above, an increase in AIGFP's other operating expenses due to professional service fees and an increase in AGF's provision for finance receivable losses of $471 million. Partially offsetting these increases was the reversal of AIGFP deferred compensation and special incentive plan discussed above.

Income Taxes (Benefits)

The effective tax rate on the pre-tax loss for the three-month period ended September 30, 2008 was 12.3 percent. The effective tax rate was lower than the statutory rate of 35 percent due primarily to $6.9 billion of deferred tax expense recorded during the third quarter, comprising $3.6 billion of deferred tax expense attributable to the potential sale of foreign businesses, and a $3.3 billion valuation allowance to reduce tax benefits on capital losses to the amount that AIG believes is more likely than not to be realized.

The effective tax rate on the pre-tax loss for the nine-month period ended September 30, 2008 was 21.5 percent and was also lower than the statutory rate primarily due to the $6.9 billion of deferred tax expense, which is discussed above, as well as other tax charges recorded.

The effective tax rates on pre-tax income for the three- and nine-month periods ended September 30, 2007 were 30.0 percent and 28.0 percent, respectively. These effective tax rates were lower than the statutory rate due primarily to benefits from remediation adjustments and the recognition of tax benefits associated with the SICO Plan for which the compensation expense was recognized in prior years.

Realization of the deferred tax asset depends on AIG's ability to generate sufficient taxable income of the appropriate character within the carryforward periods of the jurisdictions in which the net operating losses and deductible temporary differences were incurred. AIG assessed its ability to realize the deferred tax asset of $19.1 billion and concluded a $3.3 billion valuation allowance was required to reduce the deferred tax asset to an amount AIG believes is more likely than not to be realized.

When making its assessment, AIG considered future reversals of existing taxable temporary differences, future GAAP taxable income and tax-planning strategies AIG would implement, if necessary, to realize the net deferred tax asset.

In assessing future GAAP taxable income, AIG considered its strong earnings history exclusive of the recent losses on the super senior credit default swap portfolio and from the securities lending program, with respect to which AIG is entering into transactions with the NY Fed to limit exposure to future losses. AIG also considered taxable income from the sales of businesses under its asset disposition plan, the continuing earnings strength of the insurance businesses it intends to retain and its recently announced debt and preferred stock transactions with the NY Fed, together with other actions AIG is taking, when assessing the ability to generate sufficient future taxable income during the relevant carryforward periods to realize the deferred tax asset.

Segment Results

The following table summarizes the operations of each operating segment. (See also Note 2 to the Consolidated Financial Statements.)

(in millions)	Three Months Ended September 30, **2008**	2007	Percentage Increase/ (Decrease)	Nine Months Ended September 30, **2008**	2007	Percentage Increase/ (Decrease)
Total revenues[(a)(b)(e)]:						
General Insurance	**$ 10,808**	$12,758	(15)%	**$ 35,854**	$38,589	(7)%
Life Insurance & Retirement Services	**(4,642)**	12,632	–	**14,271**	40,337	(65)
Financial Services[(c)(d)]	**(5,851)**	2,785	–	**(16,016)**	7,109	–
Asset Management	**10**	1,519	(99)	**658**	4,969	(87)
Other	**451**	13	–	**531**	407	30
Consolidation and eliminations	**122**	129	–	**(436)**	220	–
Total	**$ 898**	$29,836	(97)%	**$ 34,862**	$91,631	(62)%
Operating income (loss)[(a)(b)(e)]:						
General Insurance	**$ (2,557)**	$ 2,439	–%	**$ (393)**	$ 8,511	–%
Life Insurance & Retirement Services	**(15,329)**	1,999	–	**(19,561)**	6,900	–
Financial Services[(c)(d)]	**(8,203)**	669	–	**(22,880)**	1,008	–
Asset Management	**(1,144)**	121	–	**(2,709)**	1,806	–
Other	**(1,416)**	(627)	–	**(2,899)**	(1,557)	–
Consolidation and eliminations	**464**	278	–	**237**	711	–
Total	**$(28,185)**	$ 4,879	–%	**$(48,205)**	$17,379	–%

(a) Includes gains (losses) from hedging activities that did not qualify for hedge accounting treatment under FAS No. 133, "Accounting for Derivative Instruments and Hedging Activities" (FAS 133), including the related foreign exchange gains and losses. For the three-month periods ended September 30, 2008 and 2007, the effect was $1.2 billion and $(178) million, respectively, in both revenues and operating income (loss). For the nine-month periods ended September 30, 2008 and 2007, the effect was $705 million and $(1.1) billion, respectively, in both revenues and operating income (loss). These amounts result primarily from interest rate and foreign currency derivatives that are effective economic hedges of investments and borrowings.

(b) Includes other-than-temporary impairment charges. Refer to Invested Assets — Portfolio Review — Other-Than-Temporary Impairments for further discussion.

(c) Includes gains (losses) from hedging activities that did not qualify for hedge accounting treatment under FAS 133, including the related foreign exchange gains and losses. For the three-month periods ended September 30, 2008 and 2007, the effect was $217 million and $353 million, respectively, in both revenues and operating income (loss). For the nine-month periods ended September 30, 2008 and 2007, the effect was $18 million and $(250) million, respectively, in both revenues and operating income (loss). These amounts result primarily from interest rate and foreign currency derivatives that are effective economic hedges of investments and borrowings.

(d) Includes unrealized market valuation losses of $7.1 billion and $21.7 billion for the three- and nine-month periods ended September 30, 2008, respectively, and $352 million for the three- and nine-month periods ended September 30, 2007, on AIGFP's super senior credit default swap portfolio.

(e) To better align financial reporting with the manner in which AIG's chief operating decision maker manages the business, beginning in the third quarter of 2008, AIG's own credit risk valuation adjustments on intercompany transactions are excluded from segment revenues and operating income.

General Insurance Operations

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

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

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

Transatlantic Holdings, Inc. (Transatlantic) subsidiaries offer reinsurance capacity on both a treaty and facultative basis both in the U.S. and abroad. Transatlantic structures programs for a full range of property and casualty products with an emphasis on specialty risk.

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

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

On September 15, 2008, United Guaranty Residential Insurance Company (UGRIC) and United Guaranty Mortgage Indemnity Company (UGMIC) were downgraded from AA+ to A+ by S&P. As a result of the downgrade below the AA- level, the companies were required to submit a remediation plan to Fannie Mae and Freddie Mac. All U.S. based mortgage insurers are currently subject to a Government Sponsored Enterprise (GSE) remediation plan as a result of industry-wide rating agency downgrades. UGC's plan was timely submitted and is awaiting GSE approval. UGRIC and UGMIC continue to write new domestic first-lien mortgage insurance and remain as eligible mortgage insurers with Fannie Mae and Freddie Mac.

AIG's Foreign General Insurance Group writes both commercial and consumer lines of insurance which is primarily underwritten through American International Underwriters (AIU), a marketing unit consisting of wholly owned agencies and insurance companies. The Foreign General Insurance Group also includes business written by AIG's foreign-based insurance subsidiaries.

General Insurance Results

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

(in millions, except ratios)	Three Months Ended September 30, 2008	Three Months Ended September 30, 2007	Percentage Increase/ (Decrease)	Nine Months Ended September 30, 2008	Nine Months Ended September 30, 2007	Percentage Increase/ (Decrease)
Net premiums written:						
AIG Property Casualty Group						
Commercial Insurance	**$ 5,597**	$ 6,012	(7)%	**$16,698**	$18,460	(10)%
Transatlantic	**1,094**	985	11	**3,118**	2,952	6
Personal Lines	**1,108**	1,253	(12)	**3,626**	3,685	(2)
Mortgage Guaranty	**280**	303	(8)	**872**	841	4
Foreign General Insurance	**3,647**	3,270	12	**11,712**	10,130	16
Total	**$11,726**	$11,823	(1)%	**$36,026**	$36,068	–%
Net premiums earned:						
AIG Property Casualty Group						
Commercial Insurance	**$ 5,735**	$ 5,942	(3)%	**$17,064**	$17,919	(5)%
Transatlantic	**1,027**	960	7	**3,067**	2,873	7
Personal Lines	**1,183**	1,193	(1)	**3,591**	3,516	2
Mortgage Guaranty	**254**	226	12	**779**	657	19
Foreign General Insurance	**3,532**	3,112	13	**10,740**	9,050	19
Total	**$11,731**	$11,433	3%	**$35,241**	$34,015	4%
Net investment income:						
AIG Property Casualty Group						
Commercial Insurance	**$ 512**	$ 854	(40)%	**$ 1,842**	$ 2,871	(36)%
Transatlantic	**111**	113	(2)	**348**	348	–
Personal Lines	**53**	59	(10)	**166**	173	(4)
Mortgage Guaranty	**48**	42	14	**136**	118	15
Foreign General Insurance	**5**	325	(99)	**604**	1,071	(44)
Reclassifications and eliminations	**6**	1	–	**11**	4	175
Total	**$ 735**	$ 1,394	(47)%	**$ 3,107**	$ 4,585	(32)%
Net realized capital gains (losses)	**$ (1,658)**	$ (69)	–%	**$ (2,494)**	$ (11)	–%
Operating income (loss):						
AIG Property Casualty Group						
Commercial Insurance	**$ (1,109)**	$ 1,829	–%	**$ 57**	$ 5,662	(99)%
Transatlantic	**(155)**	189	–	**148**	508	(71)
Personal Lines	**23**	28	(18)	**47**	252	(81)
Mortgage Guaranty	**(1,118)**	(216)	–	**(1,990)**	(289)	–
Foreign General Insurance	**(209)**	607	–	**1,323**	2,383	(44)
Reclassifications and eliminations	**11**	2	450	**22**	(5)	–
Total	**$ (2,557)**	$ 2,439	–%	**$ (393)**	$ 8,511	–%
Statutory underwriting profit (loss)[(b)]:						
AIG Property Casualty Group						
Commercial Insurance	**$ (426)**	$ 1,014	–%	**$ 149**	$ 2,744	(95)%
Transatlantic	**(96)**	53	–	**24**	106	(77)
Personal Lines	**9**	(40)	–	**(96)**	49	–
Mortgage Guaranty	**(1,155)**	(270)	–	**(2,126)**	(438)	–
Foreign General Insurance	**74**	266	(72)	**881**	1,039	(15)
Total	**$ (1,594)**	$ 1,023	–%	**$ (1,168)**	$ 3,500	–%
AIG Property Casualty Group:						
Loss Ratio	**92.2**	69.2		**83.8**	68.8	
Expense Ratio	**28.6**	21.1		**24.7**	20.5	
Combined Ratio	**120.8**	90.3		**108.5**	89.3	
Foreign General Insurance:						
Loss Ratio	**59.3**	52.4		**54.9**	51.7	
Expense Ratio[(a)]	**37.4**	37.1		**33.8**	32.9	
Combined ratio	**96.7**	89.5		**88.7**	84.6	
Consolidated:						
Loss Ratio	**82.3**	64.7		**75.0**	64.3	
Expense Ratio	**31.3**	25.5		**27.7**	24.0	
Combined Ratio	**113.6**	90.2		**102.7**	88.3	

(a) Includes amortization of advertising costs.

(b) Statutory underwriting profit (loss) is a measure that U.S. domiciled insurance companies are required to report to their regulatory authorities. The following table reconciles statutory underwriting profit (loss) to operating income (loss) for General Insurance:

(in millions)	Commercial Insurance	Transatlantic	Personal Lines	Mortgage Guaranty	Foreign General Insurance	Reclassifications and Eliminations	Total
Three Months Ended September 30, 2008:							
Statutory underwriting profit (loss)	**$ (426)**	**$ (96)**	**$ 9**	**$(1,155)**	**$ 74**	$ –	**$(1,594)**
Increase (decrease) in DAC	**(53)**	**7**	**(10)**	**(9)**	**25**	–	**(40)**
Net investment income	**512**	**111**	**53**	**48**	**5**	**6**	**735**
Net realized capital gains (losses)	**(1,142)**	**(177)**	**(29)**	**(2)**	**(313)**	**5**	**(1,658)**
Operating income (loss)	**$(1,109)**	**$(155)**	**$ 23**	**$(1,118)**	**$ (209)**	**$11**	**$(2,557)**
Three Months Ended September 30, 2007:							
Statutory underwriting profit (loss)	$ 1,014	$ 53	$ (40)	$ (270)	$ 266	$ –	$ 1,023
Increase (decrease) in DAC	21	8	9	13	40	–	91
Net investment income	854	113	59	42	325	1	1,394
Net realized capital gains (losses)	(60)	15	–	(1)	(24)	1	(69)
Operating income (loss)	$ 1,829	$ 189	$ 28	$ (216)	$ 607	$ 2	$ 2,439
Nine Months Ended September 30, 2008:							
Statutory underwriting profit (loss)	**$ 149**	**$ 24**	**$ (96)**	**$(2,126)**	**$ 881**	$ –	**$(1,168)**
Increase (decrease) in DAC	**(57)**	**8**	**16**	**4**	**191**	–	**162**
Net investment income	**1,842**	**348**	**166**	**136**	**604**	**11**	**3,107**
Net realized capital gains (losses)	**(1,877)**	**(232)**	**(39)**	**(4)**	**(353)**	**11**	**(2,494)**
Operating income (loss)	**$ 57**	**$ 148**	**$ 47**	**$(1,990)**	**$1,323**	**$22**	**$ (393)**
Nine Months Ended September 30, 2007:							
Statutory underwriting profit (loss)	$ 2,744	$ 106	$ 49	$ (438)	$1,039	$ –	$ 3,500
Increase (decrease) in DAC	106	22	31	34	244	–	437
Net investment income	2,871	348	173	118	1,071	4	4,585
Net realized capital gains (losses)	(59)	32	(1)	(3)	29	(9)	(11)
Operating income (loss)	$ 5,662	$ 508	$252	$ (289)	$2,383	$ (5)	$ 8,511

AIG transacts business in most major foreign currencies. The effects of changes in foreign currency exchange rates on the growth of General Insurance net premiums written were as follows:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2008	2007	**2008**	2007
Growth in original currency*	**(2.9)%**	4.3%	**(2.8)%**	4.6%
Foreign exchange effect	**2.1**	1.0	**2.7**	1.1
Growth as reported in U.S. dollars	**(0.8)%**	5.3%	**(0.1)%**	5.7%

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

Quarterly General Insurance Results

General Insurance reported an operating loss in the three-month period ended September 30, 2008 compared to operating income in the same period in 2007 due to declines in underwriting results and net investment income as well as increased net realized capital losses in the three month-period ended September 30, 2008. The combined ratio for the three-month period ended September 30, 2008 increased to 113.6, an increase of 23.4 points compared to the same period in 2007, primarily due to an increase in the loss ratio of 17.6 points. The loss ratio for accident year 2008 recorded in the three-month period ended September 30, 2008 was 15.7 points higher than the loss ratio recorded in the three-month period ended September 30, 2007 for accident year 2007. Catastrophe related losses (primarily from hurricanes Ike and Gustav in 2008) were $1.4 billion in the three-month period ended September, 30, 2008, accounting for 11.6 points of the increase in the accident year loss ratio. Increases in first-lien Mortgage Guaranty losses accounted for 2.6 points of the increase in the 2008 accident year loss ratio. AIG expects that the downward cycle in the U.S. housing market will continue to adversely affect Mortgage Guaranty's loss ratios for the foreseeable future. The loss ratio also increased for other property and casualty lines due to premium rate decreases and changes in loss trends. Favorable prior year development and increases in the loss reserve discount reduced incurred losses by $169 million and $377 million in the three-month periods ended September 30, 2008 and 2007, respectively, accounting for 1.9 points of the increase in the loss ratio.

General Insurance net premiums written declined 0.8 percent in the three-month period ended September 30, 2008 compared to the same period in 2007, as a decline in AIG Property Casualty Group was partially offset by growth in Foreign General Insurance from both established and new distribution channels, and the positive effect of changes in foreign currency exchange rates.

General Insurance net investment income declined in the three-month period ended September 30, 2008 by $659 million or approximately 47 percent compared to the same period in 2007. Interest and dividend income increased $17 million in the three-month period ended September 30, 2008 compared to the

same period in 2007 as investments in fixed maturities and equity securities increased by $3.2 billion and the average yield was substantially unchanged for both periods. Partnership and mutual fund investment results were losses of $512 million in the three-month period ended September 30, 2008 compared to income of $241 million in the same period in 2007, primarily due to weaker equity market performance in 2008.

Net realized capital losses in the three-month period ended September 30, 2008 include other-than-temporary impairment charges of $1.8 billion principally on fixed maturity securities compared to $35 million in the same period of 2007. See also Capital Resources and Liquidity and Invested Assets herein.

Year-to-Date General Insurance Results

General Insurance reported an operating loss in the nine-month period ended September 30, 2008 compared to the same period in 2007 due to declines in underwriting results and net investment income as well as net realized capital losses in the nine month-period ended September 30, 2008 compared to net realized capital gains in the same period in 2007. The combined ratio for the nine-month period ended September 30, 2008, increased to 102.7, an increase of 14.4 points compared to the same period in 2007, primarily due to an increase in the loss ratio of 10.8 points. The loss ratio for accident year 2008 recorded in the nine-month period ended September 30, 2008 was 9.4 points higher than the loss ratio recorded in the nine-month period ended September 30, 2007 for accident year 2007. Catastrophe-related losses were $1.5 billion and $101 million in the nine-month periods ended September, 30, 2008, and 2007, respectively, accounting for 4.1 points of the increase in the accident loss ratio. Increases in Mortgage Guaranty losses accounted for 3.0 points of the increase in the 2008 accident year loss ratio. The loss ratio also increased for other property and casualty lines due to premium rate decreases and changes in loss trends. Favorable development from prior years and increases in the loss reserve discount reduced incurred losses by $254 million and $720 million in the nine-month periods ended September 30, 2008 and 2007, respectively. The favorable development in the nine-month period ended September 30, 2008 includes $339 million of favorable development recognized in the first three months of 2008, related to policies whose premiums vary with the level of losses incurred (loss sensitive policies). Loss sensitive policies did not have a significant effect in 2007. The favorable development on loss sensitive policies had no effect on underwriting profit as it was entirely offset by a reduction in earned premiums.

General Insurance net premiums written were essentially unchanged in the nine-month period ended September 30, 2008 compared to the same period in 2007, as a decline in Commercial Insurance rates was almost entirely offset by growth in Foreign General Insurance from both established and new distribution channels and the positive effect of changes in foreign currency exchange rates.

General Insurance net investment income declined in the nine-month period ended September 30, 2008 by $1.5 billion or approximately 32 percent compared to the same period in 2007. Interest and dividend income increased $186 million in the nine-month period ended September 30, 2008 compared to the same period in 2007 as investment in fixed maturities and equity securities increased by $4.5 billion and the average yield was substantially unchanged for both periods. Partnership and mutual fund investment results were losses of $496 million in the nine-month period ended September 30, 2008 compared to income of $1.2 billion in the same period in 2007, primarily due to poor performance in the equity markets in 2008. Investment expenses declined $64 million in the nine-month period ended September 30, 2008 compared to the same period in 2007, primarily due to decreased interest expense on deposit liabilities.

Net realized capital losses in the nine-month period ended September 30, 2008 were driven by other-than-temporary impairment charges of $2.7 billion compared to $165 million in the same period of 2007. See also Capital Resources and Liquidity and Invested Assets herein.

Quarterly Commercial Insurance Results

Commercial Insurance reported an operating loss of $1.1 billion in the three-month period ended September 30, 2008 compared to operating income of $1.8 billion in the same period in 2007, reflecting both underwriting losses and reduced net investment income as well as increased net realized capital losses in the three-month period ended September 30, 2008. The decline in underwriting results is also reflected in the combined ratio, which increased 25.2 points in the three-month period ended September 30, 2008 compared to the same period in 2007. The loss ratio for accident year 2008, recorded in the three-month period ended September 30, 2008 was 19.8 points higher than the loss ratio recorded in the three-month period ended September 30, 2007 for accident year 2007. The increase in the 2008 accident year loss ratio includes 18.8 points for losses related to the hurricanes with the remaining increase due to higher casualty losses and the effect of premium rate declines. Favorable prior year development and increases in the reserve discount decreased incurred losses by $181 million and $353 million in the three-month periods ended September 30, 2008 and 2007, respectively, accounting for 2.8 points of the increase in the loss ratio. Commercial Insurance's net premiums written declined in the three-month period ended September 30, 2008 compared to the same period in 2007 primarily due to declines in workers' compensation premiums and other casualty lines of business.

Commercial Insurance's expense ratio increased to 21.9 in the three-month period ended September 30, 2008 compared to 19.2 in the same period of 2007. Provision for uncollectible premiums increased by $82 million in the three-month period ended September 30, 2008 compared to the same period in 2007. In general, net premiums written

increased in lines of business with higher expense ratios and lower loss ratios compared to other Commercial Insurance lines of business, contributing to the increase in the expense ratio for the three-month period ended September 30, 2008 compared to the same period in 2007.

Commercial Insurance's net investment income declined in the three-month period ended September 30, 2008 compared to the same period in 2007, primarily due to losses of $230 million from partnership and mutual fund investments in the three-month period ended September 30, 2008 compared to income of $219 million in the same period in 2007.

Commercial Insurance recorded net realized capital losses of $1.1 billion in the three-month period ended September 30, 2008 compared to net realized capital losses of $60 million in the same period of 2007, primarily due to other-than-temporary impairment charges of $1.2 billion in the three-month period ended September 30, 2008 compared to charges of $26 million in the same period in 2007, principally related to fixed maturity securities.

Year-to-Date Commercial Insurance Results

Commercial Insurance's operating income decreased 99 percent in the nine-month period ended September 30, 2008 compared to the same period in 2007, primarily due to significant declines in underwriting results and net investment income, as well as significantly greater net realized capital losses in the nine-month period ended September 30, 2008. The decline in underwriting results is also reflected in the combined ratio, which increased 15.5 points in the nine-month period ended September 30, 2008 compared to the same period in 2007. The loss ratio for accident year 2008 recorded in the nine-month period ended September 30, 2008 included a 7.2 point effect related to the catastrophe losses, and was 11.1 points higher than the loss ratio recorded in the nine-month period ended September 30, 2007 for accident year 2007. Prior year development and increases in the loss reserve discount reduced incurred losses by $373 million and $630 million in the nine-month periods ended September 30, 2008 and 2007, respectively.

Commercial Insurance's net premiums written declined in the nine-month period ended September 30, 2008 compared to the same period in 2007 primarily due to declines in premiums from workers' compensation and other casualty lines of business including a reduction of $339 million related to loss sensitive policies as described above.

Commercial Insurance's expense ratio increased to 21.7 in the nine-month period ended September 30, 2008 compared to 18.6 in the same period of 2007. Return premiums on loss sensitive policies reduced net premiums written, without a corresponding reduction in expenses, increasing the expense ratio by 0.5 points for the nine-month period ended September 30, 2008 compared to the same period in 2007. The remaining increase in the expense ratio primarily resulted from changes in property reinsurance programs, increases in the provision for uncollectible premiums and changes in the mix of business as discussed above.

Commercial Insurance's net investment income declined significantly in the nine-month period ended September 30, 2008 compared to the same period in 2007, primarily due to a loss of $273 million from partnership and mutual fund investments in the nine-month period ended September 30, 2008 compared to a gain of $875 million in the same period in 2007.

Commercial Insurance recorded net realized capital losses of $1.9 billion in the nine-month period ended September 30, 2008 compared to net realized capital losses of $59 million in the same period in 2007, primarily due to other-than-temporary impairment charges of $2.0 billion in the nine-month period ended September 30, 2008, related to both fixed maturity and equity securities, compared to $139 million in the same period in 2007.

Quarterly Transatlantic Results

Transatlantic reported an operating loss of $155 million in the three-month period ended September 30, 2008 compared to income of $189 million in the same period in 2007, primarily due to a significant increase in net realized capital losses and a statutory underwriting loss. The increase in net realized capital losses is due principally to other-than-temporary impairment charges of $144 million. The statutory underwriting loss in the three-month period ended September 30, 2008 compared to the gain in the same period in 2007 reflects increased catastrophe losses resulting principally from hurricane Ike.

Year-to-Date Transatlantic Results

Transatlantic's operating income decreased to $148 million in the nine-month period ended September 30, 2008 compared to $508 million in the same period in 2007, primarily due to an increase in net realized capital losses and a decrease in statutory underwriting profit. The increase in net realized capital losses is due principally to other-than-temporary impairment charges of $202 million. The decrease in statutory underwriting profit in the nine-month period ended September 30, 2008 compared to the same period in 2007 reflects increased catastrophe losses resulting principally from hurricane Ike.

Quarterly Personal Lines Results

Personal Lines operating income decreased in the three-month period ended September 30, 2008 compared to the same period in 2007, primarily due to a decline in net investment income and other-than-temporary impairment charges related to the ongoing turmoil in the financial markets, which more than offset an improvement in statutory underwriting results.

Net premiums written decreased in the three-month period ended September 30, 2008 compared to the same period in 2007, primarily due to continued growth in the Private Client Group, offset by reductions in both the

aigdirect.com and Agency Auto businesses. The growth in the Private Client Group reflects the execution of a plan to expand its distribution network.

Year-to-Date Personal Lines Results

Personal Lines operating income decreased in the nine-month period ended September 30, 2008 compared to the same period in 2007, primarily due to a decline in statutory underwriting profit and other-than-temporary impairment charges.

Quarterly Mortgage Guaranty Results

In response to the worsening market conditions during the last several quarters, UGC has tightened underwriting standards and increased premium rates for its first- and second-lien business. As the credit markets tightened the second-lien business has seen a significant decline in activity and, combined with UGC's tightened underwriting standards, new business written for second-liens has dropped significantly. As a result of the decline in new business and in conjunction with the increasing loss experience UGC decided to withdraw from the second-lien market, cease selling new business and place its second-lien portfolio into run-off as of September 30, 2008.

Mortgage Guaranty's operating loss increased significantly in the three-month period ended September 30, 2008 compared to the same period in 2007 due to tightening credit markets, declining housing values and the recognition of a premium deficiency reserve on second-lien business.

Net premiums written declined by 8 percent to $280 million in the three-month period ended September 30, 2008 compared to the same period in 2007, primarily due to declines in private student loans and international mortgage businesses of 77 percent and 30 percent, respectively, primarily due to tightened underwriting standards. First-and second-lien business grew moderately due to increased persistency year over year. However, new insurance written, which is a measure of the amount of new insurance added to the portfolio, during the three-month period ended September 30, 2008 decreased 77 percent and 97 percent, respectively, when compared to the same period in 2007. This decline is primarily due to UGC's tightening of underwriting guidelines and rate increases during the period.

Losses and loss expenses incurred increased $461 million over the same period in 2007, driven by domestic first- and second-lien business due to the continuing decline in the domestic housing market. Domestic first- and second-lien losses incurred increased 189 percent and 35 percent respectively, compared to the same period in 2007, resulting in a loss ratio for the first-lien business of 308.1 in the three-month period ended September 30, 2008. Increases in both domestic and international losses incurred resulted in an overall loss ratio for Mortgage Guaranty (excluding in 2008 the second-lien business in run-off) of 279.4 in the three-month period ended September 30, 2008 compared to 197.0 in the same period in 2007. Limits on certain ceded reinsurance covering the domestic first lien business may result in increased net losses in future periods, if the current housing market decline continues.

Historically, Mortgage Guaranty included all mortgage insurance risks in a single premium deficiency test because the manner of acquiring, servicing and measuring the profitability of all Mortgage Guaranty contracts was consistent. With the decision to place the second-lien business in run-off, management no longer measures the profitability for the second-lien business in the same manner as that for Mortgage Guaranty's ongoing businesses, and will no longer report loss ratio or expense ratio information for the second-lien business. As a result, UGC performed a separate premium deficiency calculation for the second lien business as of September 30, 2008.

At September 30, 2008, the present value of expected second-lien future losses and expenses (net of expected future recoveries) was $1.6 billion, offset by the present value of expected second-lien future premium of $499 million and the already established loss reserves of $727 million, resulting in a premium deficiency reserve of $453 million. The second-lien risk in force at September 30, 2008 totaled $3.1 billion with 550 thousand second-lien policies in force, expected to run-off over the next 10 to 12 years. Risk in force represents the full amount of second-lien loans insured reduced for contractual aggregate loss limits on certain pools of loans, usually 10 percent of the full amount of loans insured in each pool. Mortgage Guaranty may record net losses on this business in future periods because the timing of future delinquencies may precede recognition of future premiums, in an amount in excess of the premium deficiency reserve.

As of September 30, 2008 there was no premium deficiency related to the remainder of the Mortgage Guaranty business.

Year-to-Date Mortgage Guaranty Results

Mortgage Guaranty's operating loss in the nine-month period ended September 30, 2008 increased significantly compared to the same period in 2007 due to deteriorating housing markets throughout the United States as well as in several international markets, a tightening domestic credit market and the premium deficiency reserve discussed above. Net premiums written increased 4 percent in the nine-month period ended September 30, 2008 compared to the same period in 2007, primarily due to increases in domestic first- and second-lien premiums during the first half of 2008, partially offset by declines in net premiums written in private student loans and international mortgage insurance businesses. Net premiums written for first-and second-lien businesses increased 22 percent and 14 percent, respectively, in the nine-month period ended September 30, 2008 compared to the same period in 2007, due mainly to increased persistency

year over year. Net premiums written for international mortgage insurance business declined 20 percent, primarily due to tightened underwriting standards. During the nine-month period in 2008, net premiums written have steadily declined due to UGC's steady tightening of underwriting guidelines and rate increases during the year. New insurance written during the nine-month period ended September 30, 2008 decreased 31 percent and 78 percent for first and second-lien business, respectively, when compared to the same period in 2007.

Domestic first- and second-lien losses incurred increased 247 percent and 75 percent, respectively, compared to the nine-month period ended September 30, 2007, resulting in a first-lien loss ratio of 255.3 in the nine-month period ended September 30, 2008. Increases in domestic and international losses incurred resulted in an overall loss ratio for Mortgage Guaranty (excluding in 2008 the second-lien business in run-off) of 225.0 in the nine-month period ended September 30, 2008, compared to 140.9 in the nine-month period ended September 30, 2007.

Quarterly Foreign General Insurance Results

Foreign General Insurance incurred an operating loss of $209 million in the three-month period ended September 30, 2008 compared to operating income of $607 million in the same period in 2007. The loss was due to a decline of $320 million in net investment income and an increase of $289 million in net realized capital losses, as well as a decrease in underwriting results, mainly due to catastrophe losses.

Net premiums written increased 12 percent (4 percent in original currency) in the three-month period ended September 30, 2008 compared to the same period in 2007, reflecting growth in commercial and consumer lines driven by new business from both established and new distribution channels, including the late 2007 acquisition of Württembergische und Badische Versicherungs – AG (WüBa) in Germany. Net premiums written for commercial lines increased due to new business, mainly in the U.K. and European markets, and decreases in the use of reinsurance, partially offset by declines in premium rates. Net premiums written for the Lloyd's syndicate and Aviation declined due to rate decreases, increased market competition and an increase in the use of reinsurance.

The loss ratio in the three-month period ended September 30, 2008 increased 6.9 points compared to the same period in 2007, primarily due to higher catastrophe losses and an increase in frequency of smaller claims partially offset by a reduction in severe but non-catastrophe losses. Catastrophe losses in Ascot from Hurricanes Ike and Gustav totaled $133 million for the three months ended September 30, 2008 and contributed 2.8 points to the increase in the loss ratio. In addition, higher claims frequency contributed 4.5 points to the loss ratio, which was partially offset by declines in severe but non-catastrophe losses.

Net investment income decreased $320 million or 99 percent in the three-month period ended September 30, 2008 compared to the same period in 2007 as continued weakness in the equity markets led to losses from partnership and mutual fund investments which collectively increased $296 million from the same period in 2007.

Foreign General Insurance net realized capital losses for the three-month period ended September 30, 2008 were $313 million compared to net realized capital losses of $24 million in the same period of 2007, primarily due to other-than-temporary impairment charges, which amounted to $433 million for the three-month period ended September 30, 2008, compared to $5 million in the same period in 2007.

Year-to-Date Foreign General Insurance Results

Foreign General Insurance operating income decreased in the nine-month period ended September 30, 2008 compared to the same period in 2007, due to net realized capital losses, decreases in underwriting results and net investment income.

Net premiums written increased 16 percent (7 percent in original currency) in the nine-month period ended September 30, 2008 compared to the same period in 2007, reflecting growth in commercial and consumer lines driven by new business from established and new distribution channels, including the WüBa acquisition. Net premiums written for commercial lines increased due to new business in the U.K. and Europe and decreases in the use of reinsurance, partially offset by declines in premium rates. Growth in personal accident business in Latin America, Asia and Europe also contributed to the increase. Net premiums written for the Lloyd's syndicate Ascot continued to decline due to rate decreases and increased market competition.

The loss ratio in the nine-month period ended September 30, 2008 increased 3.2 points compared to the same period in 2007 due to increases in catastrophe losses, frequency of smaller claims and severe but non-catastrophic losses. Catastrophe losses including Hurricanes Ike and Gustav totaled $138 million for the nine months ended September 30, 2008 compared to $91 million of U.K. flood losses in the same period in the prior year, which contributed 0.2 points to the increase in the loss ratio. Prior accident year development reduced incurred losses by $65 million and $108 million in the first nine months of 2008 and 2007, respectively, accounting for 0.6 points of the increase. The current accident year loss ratio excluding catastrophe losses increased by 2.4 points primarily due to increases in severe but non-catastrophic losses and the frequency of smaller claims.

Net investment income decreased $467 million in the nine-month period ended September 30, 2008 compared to the same period in 2007 primarily due to mutual fund income which was $361 million lower than the same period of 2007, reflecting weaker performance in the equity markets in 2008.

Foreign General Insurance net realized capital losses for the nine-month period ended September 30, 2008 were $353 million compared to net realized capital gains of $29 million in the same period of 2007, primarily due to other-than-temporary impairment charges, which amounted to $433 million for the nine-month period ended September 30, 2008, compared to $16 million in the same period in 2007.

Reserve for Losses and Loss Expenses

The following table presents the components of the General Insurance gross reserve for losses and loss expenses (loss reserves) by major lines of business on a statutory Annual Statement basis*:

(in millions)	**September 30, 2008**	December 31, 2007
Other liability occurrence	**$21,311**	$20,580
Workers' compensation	**15,242**	15,568
Other liability claims made	**13,802**	13,878
International	**8,452**	7,036
Auto liability	**6,211**	6,068
Property	**5,933**	4,274
Reinsurance	**3,610**	3,127
Products liability	**2,462**	2,416
Medical malpractice	**2,315**	2,361
Mortgage guaranty/credit	**2,779**	1,426
Accident and health	**1,783**	1,818
Commercial multiple peril	**1,796**	1,900
Aircraft	**1,705**	1,623
Fidelity/surety	**1,216**	1,222
Other	**2,260**	2,203
Total	**$90,877**	$85,500

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

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

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

At September 30, 2008, General Insurance net loss reserves increased $4.47 billion from the prior year-end to $73.75 billion. The net loss reserves represent loss reserves reduced by reinsurance recoverable, net of an allowance for unrecoverable reinsurance and applicable discount for future investment income.

The following table classifies the components of the General Insurance net loss reserve by business unit:

(in millions)	**September 30, 2008**	December 31, 2007
Commercial Insurance[(a)]	**$49,240**	$47,392
Transatlantic	**7,537**	6,900
Personal Lines[(b)]	**2,472**	2,417
Mortgage Guaranty	**2,545**	1,339
Foreign General Insurance[(c)]	**11,959**	11,240
Total Net Loss Reserve	**$73,753**	$69,288

(a) At September 30, 2008 and December 31, 2007, Commercial Insurance loss reserves include approximately $2.78 billion and $3.13 billion, respectively, ($2.96 billion and $3.34 billion, respectively, before discount), related to business written by Commercial Insurance but ceded to American International Reinsurance Company Limited (AIRCO) and reported in AIRCO's statutory filings. Commercial Insurance loss reserves also include approximately $601 million and $590 million related to business

included in AIUO's statutory filings at September 30, 2008 and December 31, 2007, respectively.

(b) At September 30, 2008 and December 31, 2007, Personal Lines loss reserves include approximately $1.07 billion and $894 million, respectively, related to business ceded to Commercial Insurance and reported in Commercial Insurance's statutory filings.

(c) At September 30, 2008 and December 31, 2007, Foreign General Insurance loss reserves include approximately $2.02 billion and $3.02 billion, respectively, related to business reported in Commercial Insurance's statutory filings.

The Commercial Insurance net loss reserve is comprised principally of the business of AIG subsidiaries participating in American Home/National Union pool (10 companies) and the surplus lines pool (Lexington Insurance Company, AIG Excess Liability Insurance Company and Landmark Insurance Company).

Commercial Insurance cedes a quota share percentage of its other liability occurrence and products liability occurrence business to AIRCO. The quota share percentage ceded was 10 percent in the nine-month period ended 2008 and 15 percent in 2007 and covered all business written in these years for these lines by participants in the American Home/National Union pool. AIRCO's loss reserves relating to these quota share cessions from Commercial Insurance are recorded on a discounted basis. As of September 30, 2008, AIRCO carried a discount of approximately $180 million applicable to the $2.96 billion in undiscounted reserves it assumed from the American Home/National Union pool via this quota share cession. AIRCO also carries approximately $499 million in net loss reserves relating to Foreign General Insurance business. These reserves are carried on an undiscounted basis.

The companies participating in the American Home/National Union pool have maintained a participation in the business written by AIU for decades. As of September 30, 2008, these AIU reserves carried by participants in the American Home/National Union pool totaled approximately $2.02 billion. The remaining Foreign General Insurance reserves are carried by American International Underwriter Overseas, Ltd. (AIUO), AIRCO, AIG U.K., and other smaller AIG subsidiaries domiciled outside the United States. Statutory filings in the United States by AIG companies reflect the business written by U.S. domiciled entities only, and therefore exclude business written by AIUO, AIRCO, and all other internationally domiciled subsidiaries. The total reserves carried at September 30, 2008 by AIUO and AIRCO were approximately $3.60 billion and $3.28 billion, respectively. AIRCO's $3.28 billion in total General Insurance reserves consist of approximately $2.78 billion from business assumed from the American Home/National Union pool and an additional $499 million relating to Foreign General Insurance business.

Discounting of Reserves

At September 30, 2008, AIG's overall General Insurance net loss reserves reflect a loss reserve discount of $2.50 billion, including tabular and non-tabular calculations. The tabular workers compensation discount is calculated using a 3.5 percent interest rate and the 1979-81 Decennial Mortality Table. The non-tabular workers compensation discount is calculated separately for companies domiciled in New York and Pennsylvania, and follows the statutory regulations for each state. For New York companies, the discount is based on a five percent interest rate and the companies' own payout patterns. For Pennsylvania companies, the statute has specified discount factors for accident years 2001 and prior, which are based on a six percent interest rate and an industry payout pattern. For accident years 2002 and subsequent, the discount is based on the yield of United States Treasury securities ranging from one to twenty years and the companies' own payout patterns, with the future expected payment for each year using the interest rate associated with the corresponding Treasury security yield for that time period. The discount is comprised of the following: $794 million — tabular discount for workers' compensation in Commercial Insurance; $1.53 billion — non-tabular discount for workers' compensation in Commercial Insurance; and $180 million — non-tabular discount for other liability occurrence and products liability occurrence in AIRCO. The total undiscounted workers' compensation loss reserve carried by Commercial Insurance is approximately $13.5 billion as of September 30, 2008. The other liability occurrence and products liability occurrence business in AIRCO that is assumed from Commercial Insurance is discounted based on the yield of United States Treasury securities ranging from one to twenty years and the Commercial Insurance payout pattern for this business. The undiscounted reserves assumed by AIRCO from Commercial Insurance totaled approximately $2.96 billion at September 30, 2008.

Quarterly Reserving Process

AIG believes that the General Insurance net loss reserves are adequate to cover General Insurance net losses and loss expenses as of September 30, 2008. While AIG regularly reviews the adequacy of established loss reserves, there can be no assurance that AIG's ultimate loss reserves will not develop adversely and materially exceed AIG's loss reserves as of September 30, 2008. In the opinion of management, such adverse development and resulting increase in reserves is not likely to have a material adverse effect on AIG's consolidated financial condition, although it could have a material adverse effect on AIG's consolidated results of operations for an individual reporting period.

The reconciliation of net loss reserves was as follows:

(in millions)	Three Months Ended September 30, 2008	Three Months Ended September 30, 2007	Nine Months Ended September 30, 2008	Nine Months Ended September 30, 2007
Net reserve for losses and loss expenses at beginning of period	**$72,331**	$65,197	**$69,288**	$62,630
Foreign exchange effect	**(765)**	224	**(502)**	438
Losses and loss expenses incurred:				
Current year	**9,723**	7,636	**26,364**	22,185
Prior years, other than accretion of discount	**(144)**	(337)	**(215)**	(605)
Prior years, accretion of discount	**79**	92	**255**	220
Losses and loss expenses incurred	**9,658**	7,391	**26,404**	21,800
Losses and loss expenses paid	**7,471**	5,875	**21,437**	17,931
Net reserve for losses and loss expenses at end of period	**$73,753**	$66,937	**$73,753**	$66,937

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

(in millions)	Three Months Ended September 30, 2008	Three Months Ended September 30, 2007	Nine Months Ended September 30, 2008	Nine Months Ended September 30, 2007
Prior Accident Year Development by Reporting Unit:				
Commercial Insurance	**$ (156)**	$ (313)	**$ (298)**	$ (465)
Personal Lines	**(9)**	32	**56**	(29)
Mortgage Guaranty	**69**	(27)	**127**	–
Foreign General Insurance	**(49)**	(40)	**(65)**	(108)
Subtotal	**(145)**	(348)	**(180)**	(602)
Transatlantic	**1**	11	**2**	47
Asbestos settlements	–	–	**(37)**	(50)
Prior years, other than accretion of discount	**$ (144)**	$ (337)	**$ (215)**	$ (605)

(in millions)	Calendar Year 2008	Calendar Year 2007
Prior Accident Year Development by Accident Year:		
2007	**$ (259)**	
2006	**(388)**	$ (898)
2005	**(396)**	(373)
2004	**(269)**	(248)
2003	**66**	143
2002	**78**	200
2001 and prior	**953**	571
Prior years, other than accretion of discount	**$ (215)**	$ (605)

In determining the quarterly loss development from prior accident years, AIG conducts analyses to determine the change in estimated ultimate loss for each accident year for each profit center. For example, if loss emergence for a profit center is different than expected for certain accident years, the actuaries examine the indicated effect such emergence would have on the reserves of that profit center. In some cases, the higher or lower than expected emergence may result in no clear change in the ultimate loss estimate for the accident years in question, and no adjustment would be made to the profit center's reserves for prior accident years. In other cases, the higher or lower than expected emergence may result in a larger change, either favorable or unfavorable, than the difference between the actual and expected loss emergence. Such additional analyses were conducted for each profit center, as appropriate, in the three-month period ended September 30, 2008 to determine the loss development from prior accident years for the three-month period ended September 30, 2008. As part of its quarterly reserving process, AIG also considers notices of claims received with respect to emerging issues, such as those related to the U.S. mortgage and housing market.

2008 Net Loss Development

In the three-month period ended September 30, 2008, net loss development from prior accident years was favorable by approximately $144 million, excluding approximately $79 million from accretion of loss reserve discount. The overall favorable development of $144 million consisted of approximately $473 million of favorable development from accident years 2004 through 2007, partially offset by approximately $329 million of adverse loss development from accident years 2003 and prior. In the three months ended September 30, 2008, AIG completed an update of its ground up projections of claims exposure for the directors and officers liability (D&O) and related management liability classes of business within AIG Executive Liability. AIG utilizes the ultimate loss estimates resulting from these claims projections as a benchmark in determining the appropriate loss reserves for this business. As a result of the updated claims projections, the quarterly review of reported loss experience as of September 30, 2008 and other relevant factors, AIG recognized approximately $105 million in favorable loss development from prior accident years for the D&O and related management liability classes of business in the three months ended September 30, 2008. This consisted of approximately $185 million of favorable development from accident years 2004 through 2006, partially offset by approximately $80 million of adverse development from accident years 2000 through 2002. The overall favorable development of $144 million reflects this $105 million in favorable development from the D&O and related management liability classes of business within AIG Executive Liability. The overall favorable development of $144 million also included approximately $140 million of favorable development from business written within Commercial Insurance by Lexington Insurance Company, including casualty, catastrophic casualty, healthcare and program business. Partially offsetting these favorable developments within Commercial Insurance was approximately $170 million of adverse development from business written

by AIG Excess Casualty, primarily from accident years 2003 and prior. This adverse development relating to excess casualty reflected continued emergence of latent claims such as construction defect, product aggregate, and pharmaceutical related exposures, as well as higher than expected large loss activity from these accident years. The commutation of one large account within Commercial Insurance resulted in approximately $120 million of favorable development from accident years 2001 and prior in the three months ended September 30, 2008.

Mortgage Guaranty experienced $69 million of adverse development in the three-month period ended September 30, 2008, reflecting the adverse claims environment (see Quarterly Mortgage Guaranty Results above), including approximately $77 million of adverse development from accident year 2007, partially offset by a minor amount of favorable development from earlier accident years.

In the nine-month period ended September 30, 2008, net loss development from prior accident years was favorable by approximately $215 million, including approximately $339 million of favorable development relating to loss sensitive business in the first three months of 2008 (which was offset by an equal amount of negative earned premium development), and excluding approximately $255 million from accretion of loss reserve discount. Excluding both the favorable development relating to loss sensitive business and accretion of loss reserve discount, net loss development from prior accident years in the nine-month period ended September 30, 2008, was adverse by approximately $124 million. The overall favorable development of $215 million consisted of approximately $1.31 billion of favorable development from accident years 2004 through 2007 partially offset by approximately $1.10 billion of adverse loss development from accident years 2003 and prior. Excluding the favorable development from loss sensitive business, the overall adverse development of $124 million consisted of approximately $1.03 billion of favorable development from accident years 2004 through 2007 offset by approximately $1.15 billion of adverse development from accident years 2003 and prior. The adverse development from accident years 2003 and prior was primarily related to excess casualty business within Commercial Insurance. The favorable development from accident years 2004 through 2007 included approximately $280 million in favorable development from loss sensitive business written by AIG Risk Management, and approximately $350 million in favorable development from business written by Lexington Insurance Company, including healthcare, catastrophic casualty, casualty and program businesses. AIG Executive Liability business contributed approximately $250 million to the favorable development from accident years 2004 and 2005, relating primarily to D&O. The adverse development from accident years 2003 and prior included approximately $200 million related to claims involving MTBE, a gasoline additive, primarily on excess casualty business within Commercial Insurance from accident years 2000 and prior. In addition, as described above for the three months ended September 30, 2008, the excess casualty adverse developments reflect a variety of other latent claims and large losses. AIG's exposure to these latent exposures was reduced after 2002 due to significant changes in policy terms and conditions as well as underwriting guidelines. Other segments throughout AIG contributed to the adverse developments from accident year 2003 and prior, including D&O and other professional liability classes within Commercial Insurance, and Transatlantic. Mortgage Guaranty contributed approximately $126 million of overall adverse development in the nine-month period ended September 30, 2008, with $119 million relating to accident year 2007. See Year-to-Date Mortgage Guaranty Results above.

2007 Net Loss Development

In the three months ended September 30, 2007, net loss development from prior accident years was favorable by approximately $337 million, including approximately $11 million of adverse development from the general reinsurance operations of Transatlantic, and excluding approximately $92 million from accretion of loss reserve discount. Excluding Transatlantic, as well as accretion of discount, net loss development in the three months ended September 30, 2007 from prior accident years was favorable by approximately $348 million. The overall favorable development of $337 million consisted of approximately $764 million of favorable development from accident years 2004 through 2006, partially offset by approximately $299 million of adverse development from accident years 2002 and prior and $128 million of adverse development from accident year 2003. For the three months ended September 30, 2007, most classes of AIG's business continued to experience favorable development for accident years 2004 through 2006. The majority of the adverse development from accident years 2002 and prior was related to developments from excess casualty business within Commercial Insurance and from Transatlantic. The adverse development from accident year 2003 was primarily related to developments from excess casualty business within Commercial Insurance, which represented less than a 1 percent change in the ultimate loss estimate for accident year 2003. In the three months ended September 30, 2007, as described above, AIG completed an update of its ground up projections of claims exposure for the D&O and related management liability classes of business. As a result of the updated claims projections, in addition to the quarterly review of reported loss experience as of September 30, 2007 and other relevant factors, AIG recognized approximately $150 million in favorable loss development from prior accident years for the D&O and related management liability classes of business in the three months ended September 30, 2007. This consisted of approximately $200 million of favorable development from accident years 2004 through 2006, partially offset by approximately

$50 million of adverse development from accident years 2002 and prior. The overall favorable development of $337 million reflects this $150 million from the D&O and related management liability classes of business within Commercial Insurance.

In the first nine months of 2007, net loss development from prior accident years was favorable by approximately $605 million, including approximately $47 million of adverse development from the general reinsurance operations of Transatlantic, and excluding approximately $220 million from accretion of loss reserve discount. Excluding Transatlantic, as well as accretion of discount, net loss development in the first nine months of 2007 from prior accident years was favorable by approximately $652 million. The overall favorable development of $605 million consisted of approximately $1.52 billion of favorable development from accident years 2004 through 2006, partially offset by approximately $771 million of adverse development from accident years 2002 and prior and $143 million of adverse development from accident year 2003. For the first nine months of 2007, most classes of AIG's business continued to experience favorable development for accident years 2004 through 2006. The majority of the adverse development from accident years 2002 and prior was related to development from excess casualty business within Commercial Insurance and from Transatlantic. The adverse development from accident year 2003 was primarily related to developments from excess casualty business within Commercial Insurance. The overall favorable development of $605 million includes approximately $200 million pertaining to the D&O and related management liability classes of business within Commercial Insurance, consisting of approximately $235 million of favorable development from accident years 2004 through 2006, partially offset by approximately $35 million of adverse development from accident years 2002 and prior.

Asbestos and Environmental Reserves

The estimation of loss reserves relating to asbestos and environmental claims on insurance policies written many years ago is subject to greater uncertainty than other types of claims due to inconsistent court decisions as well as judicial interpretations and legislative actions that in some cases have tended to broaden coverage beyond the original intent of such policies and in others have expanded theories of liability.

As described more fully in the 2007 Annual Report on Form 10-K, AIG's reserves relating to asbestos and environmental claims reflect a comprehensive ground-up analysis. In the nine-month period ended September 30, 2008, AIG maintained the ultimate loss estimates for asbestos and environmental claims resulting from the recently completed reserve analyses. A minor amount of adverse incurred loss development pertaining to asbestos was reflected in the nine-month period ended September 30, 2008, as presented in the table that follows. This development was primarily attributable to several large defendants, the effect of which was largely offset by one large favorable settlement. A moderate amount of favorable gross incurred loss development pertaining to environmental was reflected in the nine-month period ended September 30, 2008, as presented in the table that follows. This development was primarily attributable to recent favorable experience which was fully reinsured, resulting in no favorable net development on environmental net reserves.

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

	Nine Months Ended September 30,			
	2008		2007	
(in millions)	Gross	Net	Gross[a]	Net
Asbestos:				
Reserve for losses and loss expenses at beginning of year	**$3,864**	**$1,454**	$4,523	$1,889
Losses and loss expenses incurred[b]	**76**	**18**	18	7
Losses and loss expenses paid[b]	**(540)**	**(228)**	(614)	(363)
Reserve for losses and loss expenses at end of period	**$3,400**	**$1,244**	$3,927	$1,533
Environmental:				
Reserve for losses and loss expenses at beginning of year	**$ 515**	**$ 237**	$ 629	$ 290
Losses and loss expenses incurred[b]	**(40)**	**1**	2	(1)
Losses and loss expenses paid[b]	**(39)**	**(28)**	(89)	(46)
Reserve for losses and loss expenses at end of period	**$ 436**	**$ 210**	$ 542	$ 243
Combined:				
Reserve for losses and loss expenses at beginning of year	**$4,379**	**$1,691**	$5,152	$2,179
Losses and loss expenses incurred[b]	**36**	**19**	20	6
Losses and loss expenses paid[b]	**(579)**	**(256)**	(703)	(409)
Reserve for losses and loss expenses at end of period	**$3,836**	**$1,454**	$4,469	$1,776

(a) Gross amounts were revised from the presentation in prior periods to reflect the inclusion of certain reserves not previously identified as asbestos and environmental related. This revision had no effect on net reserves.

(b) All amounts pertain to policies underwritten in prior years, primarily to policies issued in 1984 and prior years.

The gross and net IBNR included in the reserve for losses and loss expenses, relating to asbestos and environmental claims separately and combined, were estimated as follows:

	Nine Months Ended September 30,			
	2008		2007	
(in millions)	Gross	Net	Gross*	Net
Asbestos	**$2,211**	**$ 989**	$2,801	$1,261
Environmental	**259**	**111**	328	127
Combined	**$2,470**	**$1,100**	$3,129	$1,388

* *Gross amounts were revised from the presentation in prior periods to reflect the inclusion of certain reserves not previously identified as asbestos and environmental related. This revision had no effect on net reserves.*

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

	Nine Months Ended September 30,					
	2008			2007		
	Asbestos	Environmental	Combined	Asbestos	Environmental	Combined
Claims at beginning of year	**6,563**	**7,652**	**14,215**	6,878	9,442	16,320
Claims during year:						
Opened	**514**	**864**	**1,378**	321	850	1,171
Settled	**(130)**	**(105)**	**(235)**	(113)	(101)	(214)
Dismissed or otherwise resolved	**(823)**	**(1,561)**	**(2,384)**	(745)	(2,138)	(2,883)
Claims at end of period	**6,124**	**6,850**	**12,974**	6,341	8,053	14,394

Survival Ratios — Asbestos and Environmental

The following table presents AIG's survival ratios for asbestos and environmental claims at September 30, 2008 and 2007. The survival ratio is derived by dividing the current carried loss reserve by the average payments for the three most recent calendar years for these claims. Therefore, the survival ratio is a simplistic measure estimating the number of years it would be before the current ending loss reserves for these claims would be paid off using recent year average payments. The September 30, 2008 survival ratio is lower than the ratio at September 30, 2007 because the more recent periods included in the rolling average reflect higher claims payments. In addition, AIG's survival ratio for asbestos claims was negatively affected by the favorable settlement described above, as well as several similar settlements during 2007. These settlements reduced gross and net asbestos survival ratios at

September 30, 2008 by approximately 1.2 years and 2.7 years, respectively, and reduced gross and net asbestos survival ratios at September 30, 2007 by approximately 1.4 years and 3.2 years, respectively. Many factors, such as aggressive settlement procedures, mix of business and level of coverage provided, have a significant effect on the amount of asbestos and environmental reserves and payments and the resultant survival ratio. Moreover, as discussed above, the primary basis for AIG's determination of its reserves is not survival ratios, but instead the ground-up and top-down analysis. Thus, caution should be exercised in attempting to determine reserve adequacy for these claims based simply on this survival ratio.

AIG's survival ratios for asbestos and environmental claims, separately and combined were based upon a three-year average payment. These ratios at September 30, 2008 and 2007 were as follows:

	Gross*	Net
2008		
Survival ratios:		
Asbestos	5.3	4.1
Environmental	4.6	3.7
Combined	5.2	4.0
2007		
Survival ratios:		
Asbestos	7.7	6.4
Environmental	5.1	3.8
Combined	7.2	5.8

* *Gross amounts for 2007 were revised from the presentation in prior periods to reflect the inclusion of certain reserves not previously identified as asbestos and environmental related. This revision had no effect on net reserves.*

Life Insurance & Retirement Services Operations

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

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

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

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

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

Foreign Life Insurance & Retirement Services

Japan and Other

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

Asia

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

Domestic Life Insurance

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

Domestic Retirement Services

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

Life Insurance & Retirement Services Results

Life Insurance & Retirement Services results were as follows:

(in millions)	Premiums and Other Considerations	Net Investment Income	Net Realized Capital Gains (Losses)	Total Revenues	Operating Income (Loss)
Three Months Ended September 30, 2008					
Foreign Life Insurance & Retirement Services	**$ 7,359**	**$ 474**	**$ (3,455)**	**$ 4,378**	**$ (2,493)**
Domestic Life Insurance	**1,714**	**973**	**(4,391)**	**(1,704)**	**(3,911)**
Domestic Retirement Services	**281**	**898**	**(8,495)**	**(7,316)**	**(8,925)**
Total	**$ 9,354**	**$ 2,345**	**$(16,341)**	**$ (4,642)**	**$(15,329)**
Three Months Ended September 30, 2007					
Foreign Life Insurance & Retirement Services	$ 6,505	$ 2,367	$ 138	$ 9,010	$ 1,736
Domestic Life Insurance	1,495	985	(295)	2,185	61
Domestic Retirement Services	300	1,471	(334)	1,437	202
Total	$ 8,300	$ 4,823	$ (491)	$12,632	$ 1,999
Percentage Increase/(Decrease) from Prior Year:					
Foreign Life Insurance & Retirement Services	13%	(80)%	–%	(51)%	–%
Domestic Life Insurance	15	(1)	–	–	–
Domestic Retirement Services	(6)	(39)	–	–	–
Total	13%	(51)%	–%	–%	–%
Nine Months Ended September 30, 2008					
Foreign Life Insurance & Retirement Services	**$22,497**	**$ 5,084**	**$ (5,086)**	**$22,495**	**$ (985)**
Domestic Life Insurance	**4,905**	**2,963**	**(7,055)**	**813**	**(5,786)**
Domestic Retirement Services	**855**	**3,687**	**(13,579)**	**(9,037)**	**(12,790)**
Total	**$28,257**	**$11,734**	**$(25,720)**	**$14,271**	**$(19,561)**
Nine Months Ended September 30, 2007					
Foreign Life Insurance & Retirement Services	$19,621	$ 8,611	$ (79)	$28,153	$ 4,674
Domestic Life Insurance	4,392	2,996	(323)	7,065	774
Domestic Retirement Services	882	4,861	(624)	5,119	1,452
Total	$24,895	$16,468	$ (1,026)	$40,337	$ 6,900
Percentage Increase/(Decrease) from Prior Year:					
Foreign Life Insurance & Retirement Services	15%	(41)%	–%	(20)%	–%
Domestic Life Insurance	12	(1)	–	(88)	–
Domestic Retirement Services	(3)	(24)	–	–	–
Total	14%	(29)%	–%	(65)%	–%

The gross insurance in force for Life Insurance & Retirement Services was as follows:

(In millions)	**September 30, 2008**	December 31, 2007
Foreign*	**$1,394,683**	$1,327,251
Domestic	**1,027,600**	984,794
Total	**$2,422,283**	$2,312,045

* *Includes an increase of $10.5 billion related to changes in foreign exchange rates at September 30, 2008.*

Premiums and other considerations in the three- and nine-month periods ended September 30, 2008 reflect growth primarily due to increased production and favorable foreign exchange rates in the Foreign Life Insurance & Retirement Services operations and sales of payout annuities in Domestic Life Insurance compared to the same periods in 2007.

Net investment income decreased in the three- and nine-month periods ended September 30, 2008 compared to the same periods in 2007 due to partnership and mutual fund losses in the 2008 periods compared to income in the 2007 periods, lower yield enhancement income, higher trading account losses in the U.K. associated with certain investment-linked products and increased levels of short-term investments. Policyholder investment income and trading losses (together, policyholder trading gains (losses)) were $(1.6) billion and $(1.7) billion in the three- and nine-month periods ended September 30, 2008, respectively, compared to gains of $150 million and $2.0 billion in the same periods in 2007, reflecting equity market declines. Policyholder trading gains (losses) are offset by a change in incurred policy losses and benefits expense. Policyholder trading gains (losses) generally reflect the trends in equity markets, principally in Japan and Asia.

The higher net realized capital losses in the three- and nine-month periods ended September 30, 2008 compared to the same periods in 2007 were primarily driven by impairments related to severity losses, credit events primarily in the financial institutions sector and changes in intent to hold until recovery as the credit market disruption continued. Net realized capital losses resulting from other-than-temporary impairment charges were $15.9 billion and $25.5 billion in the three- and nine-month periods ended September 30, 2008, respectively, compared to $349 million and $1.1 billion in the same periods of 2007. See Invested Assets for further details.

In addition to the higher net realized capital losses and lower net investment income noted above, the operating loss for the three- and nine-month periods ended September 30, 2008 increased as a result of DAC and SIA charges and related reserve strengthening of $728 million in the Domestic Retirement Services operations resulting from the continued weakness in the equity markets and the significantly higher surrender activity resulting from AIG parent's liquidity issues beginning in mid-September. The operating loss also included higher benefit costs in the Japan variable life level premium product resulting from a sharp decline in the Japanese equity market and a loss recognition charge in the Philippine operations. These decreases were partially offset by the favorable effect of foreign exchange rates and growth in the underlying business in force. The operating loss in the three-month period ended September 30, 2008 included a DAC and sales inducement asset (SIA) benefit of $478 million related to net realized capital losses compared to a benefit of $56 million in the same period in 2007. The operating loss in the nine-month period ended September 30, 2008 included a DAC and SIA benefit of $957 million related to net realized capital losses compared to a benefit of $170 million in the same period in 2007.

AIG adopted FAS 157 on January 1, 2008 and the most significant effect on the Life Insurance & Retirement Services results was the change in measurement of fair value for embedded policy derivatives. The pre-tax effect of adoption related to embedded policy derivatives was an increase in net realized capital losses of $155 million as of January 1, 2008, partially offset by a $47 million DAC benefit related to these losses. The effect of initial adoption was primarily due to an increase in the embedded policy derivative liability valuations resulting from the inclusion of explicit risk margins.

AIG adopted FAS 159 on January 1, 2008 and elected to apply the fair value option to a closed block of single premium variable life business in Japan and to an investment-linked product sold principally in Asia. The adoption of FAS 159 with respect to these fair value elections resulted in a decrease to 2008 opening retained earnings of $559 million, net of tax. The fair value of the liabilities for these policies totaled $3.3 billion at September 30, 2008 and is reported in policyholders' contract deposits.

Foreign Life Insurance & Retirement Services Results

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

(in millions)	Premiums and Other Considerations	Net Investment Income	Net Realized Capital Gains (Losses)	Total Revenues	Operating Income (Loss)
Three Months Ended September 30, 2008					
Life insurance	**$ 4,282**	**$ 164**	**$(3,078)**	**$ 1,368**	**$(2,490)**
Personal accident	**1,788**	**124**	**(71)**	**1,841**	**323**
Group products	**962**	**124**	**(47)**	**1,039**	**83**
Individual fixed annuities	**221**	**621**	**(258)**	**584**	**(33)**
Individual variable annuities	**106**	**(559)**	**(1)**	**(454)**	**(376)**
Total	**$ 7,359**	**$ 474**	**$(3,455)**	**$ 4,378**	**$(2,493)**
Three Months Ended September 30, 2007					
Life insurance	$ 3,992	$1,598	$ 74	$ 5,664	$ 1,048
Personal accident	1,519	91	12	1,622	353
Group products	744	162	(37)	869	81
Individual fixed annuities	141	533	89	763	286
Individual variable annuities	109	(17)	–	92	(32)
Total	$ 6,505	$2,367	$ 138	$ 9,010	$ 1,736
Percentage Increase/(Decrease) from Prior Year:					
Life insurance	7%	(90)%	–%	(76)%	–%
Personal accident	18	36	–	14	(8)
Group products	29	(23)	–	20	2
Individual fixed annuities	57	17	–	(23)	–
Individual variable annuities	(3)	–	–	–	–
Total	13%	(80)%	–%	(51)%	–%
Nine Months Ended September 30, 2008					
Life insurance	**$13,428**	**$2,896**	**$(4,395)**	**$11,929**	**$(2,007)**
Personal accident	**5,334**	**325**	**(137)**	**5,522**	**1,086**
Group products	**2,960**	**521**	**(88)**	**3,393**	**289**
Individual fixed annuities	**429**	**1,850**	**(486)**	**1,793**	**69**
Individual variable annuities	**346**	**(508)**	**20**	**(142)**	**(422)**
Total	**$22,497**	**$5,084**	**$(5,086)**	**$22,495**	**$ (985)**
Nine Months Ended September 30, 2007					
Life insurance	$12,264	$5,247	$ 47	$17,558	$ 2,855
Personal accident	4,479	261	6	4,746	1,046
Group products	2,187	558	(64)	2,681	233
Individual fixed annuities	387	1,681	(68)	2,000	487
Individual variable annuities	304	864	–	1,168	53
Total	$19,621	$8,611	$ (79)	$28,153	$ 4,674
Percentage Increase/(Decrease) from Prior Year:					
Life insurance	9%	(45)%	–%	(32)%	–%
Personal accident	19	25	–	16	4
Group products	35	(7)	–	27	24
Individual fixed annuities	11	10	–	(10)	(86)
Individual variable annuities	14	–	–	–	–
Total	15%	(41)%	–%	(20)%	–%

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

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

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2008	2007	**2008**	2007
Growth in original currency*	**5.5%**	7.5%	**6.6%**	6.8%
Foreign exchange effect	**7.6**	1.2	**8.1**	1.7
Growth as reported in U.S. dollars	**13.1%**	8.7%	**14.7%**	8.5%

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

Quarterly Japan and Other Results

First year premium, single premium and annuity deposits for Japan and Other were as follows:

	Three Months Ended September 30,		Percentage Increase/ (Decrease)	
(in millions)	**2008**	2007	U.S.$	Original Currency
First year premium	**$ 764**	$ 598	28%	15%
Single premium	**2,548**	3,606	(29)%	(30)%
Annuity deposits	**4,284**	5,308	(19)%	(19)%

First year premium sales in the three-month period ended September 30, 2008 reflected strong growth in U.S. dollar terms and on an original currency basis compared to the same period in 2007. First year premium life insurance sales in Japan rose principally from increased sales of an interest sensitive product. Personal accident first year premium sales were down slightly due to lower direct marketing sales and a shift to single premium products in Japan. First year premium sales of group products increased primarily due to higher pension deposits in Brazil.

Single premium sales reflected a significant decline as the life insurance product lines fell 37 percent in the three-month period ended September 30, 2008 compared to the same period last year. This decline was due to lower guaranteed income bond sales in the U.K. In Japan, a new single premium personal accident and health product was successfully launched during the first quarter of 2008 with the majority of sales coming through banks which were recently deregulated and are now able to sell accident and health products. Group products single premium sales increased substantially with higher production of credit life insurance products in Europe and higher pension deposits in Brazil.

Annuity deposits decreased in the three-month period ended September 30, 2008 compared to the same period in 2007 due to the continued market volatility which negatively affected individual variable annuities sales in Japan and the U.K. This decline more than offset the increase in individual fixed annuity deposits in Japan which grew as a result of an improved exchange rate environment and benefited from the volatile equity markets. Net flows for Japan fixed annuities increased from $163 million in the three-month period ended September 30, 2007 to $579 million in the three-month period ended September 30, 2008.

Japan and Other results on a sub – product basis were as follows:

(in millions)	Premiums and Other Considerations	Net Investment Income	Net Realized Capital Gains (Losses)	Total Revenues	Operating Income (Loss)
Three Months Ended September 30, 2008					
Life insurance	**$1,358**	**$ 331**	**$(1,372)**	**$ 317**	**$(1,058)**
Personal accident	**1,268**	**68**	**(10)**	**1,326**	**290**
Group products	**722**	**93**	**(11)**	**804**	**81**
Individual fixed annuities	**212**	**588**	**(225)**	**575**	**(13)**
Individual variable annuities	**104**	**(559)**	**(1)**	**(456)**	**(374)**
Total	**$3,664**	**$ 521**	**$(1,619)**	**$2,566**	**$(1,074)**
Three Months Ended September 30, 2007					
Life insurance	$1,219	$ 393	$ 81	$1,693	$ 429
Personal accident	1,049	48	5	1,102	267
Group products	563	131	(2)	692	76
Individual fixed annuities	137	499	101	737	290
Individual variable annuities	109	(18)	–	91	(32)
Total	$3,077	$1,053	$ 185	$4,315	$ 1,030
Percentage Increase/(Decrease) from Prior Year:					
Life insurance	11%	(16)%	–%	(81)%	–%
Personal accident	21	42	–	20	9
Group products	28	(29)	–	16	7
Individual fixed annuities	55	18	–	(22)	–
Individual variable annuities	(5)	–	–	–	–
Total	19%	(51)%	–%	(41)%	–%

Total revenues for Japan and Other in the three-month period ended September 30, 2008 decreased compared to the same period in 2007 primarily due to higher net realized capital losses and lower net investment income which were partially offset by growth in premiums and other considerations. Realized capital losses increased primarily due to higher other-than-temporary impairments. Net investment income declined in the period due to significantly higher trading account losses related to certain investment-linked products in the U.K., higher policyholder trading losses and losses on partnership investments.

Operating income declined in the three-month period ended September 30, 2008 compared to the same period in 2007 due to significantly higher realized capital losses and $422 million of higher trading account losses in the U.K. related to certain investment-linked products. These decreases were partially offset by the positive effect of foreign exchange. In addition, the three-month period ended September 30, 2007 operating income benefited from $37 million of DAC unlocking and other changes in actuarial estimates and $16 million of higher individual fixed annuities surrender charge income, net of DAC, compared to the same period in 2008.

Year-to-Date Japan and Other Results

First year premium, single premium and annuity deposits for Japan and Other were as follows:

(in millions)	Nine Months Ended September 30, 2008	Nine Months Ended September 30, 2007	Percentage Increase/(Decrease) U.S.$	Percentage Increase/(Decrease) Original Currency
First year premium	**$ 2,140**	$ 1,891	13%	2%
Single premium	**7,682**	7,724	(1)%	(3)%
Annuity deposits	**15,809**	13,520	17%	16%

First year premium sales for the nine-month period ended September 30, 2008 reflected steady growth in U.S. dollar terms, but were up slightly on an original currency basis compared to the same period in 2007. First year premium sales were bolstered by group products sales in Brazil, Europe and the Middle East. This increase was partially offset by the decline in life insurance and personal accident sales in Japan. Life insurance sales were negatively affected by the suspension of increasing term sales in 2007 while personal accident sales have declined due to lower direct marketing sales.

Single premium sales for the nine-month period ended September 30, 2008 were essentially flat in U.S. dollar terms and down slightly on an original currency basis compared to the same period in 2007. While interest sensitive life insurance sales increased in Japan, guaranteed income bond sales in the U.K. fell as deposits shifted to the variable annuity products. A new single premium personal accident and health product launched in Japan during the first quarter of 2008 continues to perform well and sales which started through banks are being

expanded to the agency channels. Group products produced favorable results as pension deposits in Brazil and credit sales in Europe grew significantly in the nine months ended September 30, 2008 compared to the same period last year.

Annuity deposits increased in the nine-month period ended September 30, 2008 compared to the same period in 2007 as individual fixed annuities in Japan and individual variable annuities in the U.K. performed well. In Japan, fixed annuity products improved due to the launch of new products and a favorable exchange rate environment for non-yen denominated products. Net flows for Japan individual fixed annuities increased from $219 million in the nine-month period ended September 30, 2007 to $2.4 billion in the nine-month period ended September 30, 2008. Variable annuity deposit growth in the U.K. was favorably affected by the launch of a new product; however, the growth rate in the U.K. has slowed as the current market volatility continued. This volatility continues to negatively affect the growth rate in Japan for the individual variable annuity sales.

Japan and Other results on a sub-product basis were as follows:

(in millions)	Premiums and Other Considerations	Net Investment Income	Net Realized Capital Gains (Losses)	Total Revenues	Operating Income (Loss)
Nine Months Ended September 30, 2008					
Life insurance	**$ 4,254**	**$1,311**	**$(1,917)**	**$ 3,648**	**$(857)**
Personal accident	**3,781**	**189**	**(45)**	**3,925**	**929**
Group products	**2,274**	**433**	**(28)**	**2,679**	**237**
Individual fixed annuities	**399**	**1,750**	**(421)**	**1,728**	**98**
Individual variable annuities	**341**	**(510)**	**20**	**(149)**	**(421)**
Total	**$11,049**	**$3,173**	**$(2,391)**	**$11,831**	**$(14)**
Nine Months Ended September 30, 2007 Life insurance	$ 3,785	$1,584	$ 96	$ 5,465	$1,219
Personal accident	3,118	150	7	3,275	799
Group products	1,677	482	4	2,163	212
Individual fixed annuities	354	1,591	(63)	1,882	471
Individual variable annuities	302	861	–	1,163	52
Total	$ 9,236	$4,668	$ 44	$13,948	$2,753
Percentage Increase/(Decrease) from Prior Year:					
Life insurance	12%	(17)%	–%	(33)%	–%
Personal accident	21	26	–	20	16
Group products	36	(10)	–	24	12
Individual fixed annuities	13	10	–	(8)	(79)
Individual variable annuities	13	–	–	–	–
Total	20%	(32)%	–%	(15)%	–%

Total revenues for Japan and Other in the nine-month period ended September 30, 2008 decreased compared to the same period in 2007 primarily due to net realized capital losses and lower net investment income. Net realized capital losses were recognized in the period primarily due to other-than-temporary impairment charges. Net investment income declined due to policyholder trading losses, lower partnership and mutual fund income and mark-to-market trading losses related to investment-linked products in the U.K. Policyholder trading losses were $242 million for the nine-month period ended September 30, 2008 compared to gains of $1.4 billion for the same period in 2007. Policyholder trading gains (losses) are offset by a change to incurred policy losses and benefits expense. Partnership and mutual fund income for the nine-month period ended September 30, 2008 was $87 million lower than the same period in 2007. Trading account losses in the U.K. on certain investment-linked products were $722 million for the nine-month period ended September 30, 2008 compared to a loss of $93 million in the same period in 2007.

Despite the continued growth in the underlying business and the positive effect of foreign exchange, the decline in total revenues resulted in an operating loss of $14 million for the nine-month period ended September 30, 2008 compared to income of $2.8 billion in the same period in 2007. The results reflected higher benefit costs of $55 million resulting from volatility in the Japanese equity market and interest rates which affect variable life fair value liabilities under FAS 159, lower DAC unlocking benefits and other changes in actuarial estimates of $51 million and $52 million of lower individual fixed annuities surrender charge income, net of DAC, compared to the same period in 2007. Operating income for the nine-month period ended September 30, 2007 included a $62 million charge related to the regulatory claims review in Japan.

Quarterly Asia Results

First year premium, single premium and annuity deposits for Asia were as follows:

(in millions)	Three Months Ended September 30, 2008	2007	Percentage Increase/ (Decrease) U.S.$	Original Currency
First year premium	**$721**	$ 757	**(5)%**	(6)%
Single premium	**383**	1,138	**(66)%**	(67)%
Annuity deposits	**215**	179	**20%**	25%

First year premium sales in the three-month period ended September 30, 2008 declined on a U.S. dollar basis and original currency basis compared to the same period in 2007 as the sales focus in Taiwan shifted to individual variable annuity products. This decline more than offset the increase in first year life insurance sales in Korea, Singapore and Thailand. First year personal accident premiums declined due to increased competition in the direct marketing channel in Korea, which offset positive growth in other parts of Asia. The group products business performed well, particularly in Australia.

Single premium sales in the three-month period ended September 30, 2008 decreased significantly as equity market volatility negatively affected the investment-oriented life insurance sales in Taiwan, Singapore, Hong Kong, China and Korea.

Annuity deposits in the three-month period ended September 30, 2008 increased compared to the same period in 2007 due to sales of variable annuity products in Taiwan.

Asia results, presented on a sub-product basis were as follows:

(in millions)	Premiums and Other Considerations	Net Investment Income	Net Realized Capital Gains (Losses)	Total Revenues	Operating Income
Three Months Ended September 30, 2008					
Life insurance	**$2,924**	**$ (167)**	**$(1,706)**	**$1,051**	**$(1,432)**
Personal accident	**520**	**56**	**(61)**	**515**	**33**
Group products	**240**	**31**	**(36)**	**235**	**2**
Individual fixed annuities	**9**	**33**	**(33)**	**9**	**(20)**
Individual variable annuities	**2**	**–**	**–**	**2**	**(2)**
Total	**$3,695**	**$ (47)**	**$(1,836)**	**$1,812**	**$(1,419)**
Three Months Ended September 30, 2007					
Life insurance	$2,773	$1,205	$ (7)	$3,971	$619
Personal accident	470	43	7	520	86
Group products	181	31	(35)	177	5
Individual fixed annuities	4	34	(12)	26	(4)
Individual variable annuities	–	1	–	1	–
Total	$3,428	$1,314	$ (47)	$4,695	$706
Percentage Increase/(Decrease) from Prior Year:					
Life insurance	5%	–%	–%	(74)%	–%
Personal accident	11	30	–	(1)	(62)
Group products	33	–	–	33	(60)
Individual fixed annuities	125	(3)	–	(65)	–
Individual variable annuities	–	–	–	100	–
Total	8%	–%	–%	(61)%	–%

Total revenues for Asia in the three-month period ended September 30, 2008 decreased significantly compared to the same period in 2007, primarily due to the negative effect of policyholder trading losses on net investment income and higher net realized capital losses, which more than offset the growth in premiums and other considerations. Premiums and other considerations increased in the three-month period ended September 30, 2008 compared to the same period in 2007 due to growth in the underlying in force business. Net investment income declined due to policyholder trading losses of $1.1 billion in 2008 compared to gains of $158 million in the same period in 2007 and partnership and mutual fund losses of $363 million compared to income of $16 million in the same period in 2007. Net realized capital losses in the three-month period ended September 30, 2008 included higher other-than-temporary impairment charges.

Asia reported an operating loss of $1.4 billion in the three-month period ended September 30, 2008 compared to income of $706 million in the same period in 2007. This loss was principally due to higher net realized capital losses, partnership and mutual fund losses and a $31 million loss recognition charge in the Philippine operations, which more than offset the favorable effect of foreign exchange.

Year-to-Date Asia Results

First year premium, single premium and annuity deposits for Asia were as follows:

(in millions)	Nine Months Ended September 30, 2008	2007	Percentage Increase/ (Decrease) U.S.$	Original Currency
First year premium	**$2,199**	$2,171	**1%**	(1)%
Single premium	**2,232**	2,708	**(18)%**	(22)%
Annuity deposits	**881**	550	**60%**	59%

First year premium sales in the nine-month period ended September 30, 2008 grew slightly compared to the same period in 2007 as the sales focus shifted more to single premium and annuity products. The increase in investment-oriented life insurance sales in Korea and Singapore was nearly offset by declines in Taiwan life insurance sales due to a shift to variable annuity products in early 2008. The group products business performed well in Australia, China and Singapore.

Single premium sales in the nine-month period ended September 30, 2008 declined compared to the same period in 2007 primarily due to the negative affect of equity market volatility on investment-oriented life insurance sales, particularly in Taiwan, Hong Kong, China and the Philippines. Group products increased due to sales of credit life insurance primarily in Thailand.

Annuity deposits in the nine-month period ended September 30, 2008 increased 60 percent compared to the same period in 2007 due to the variable annuity deposits in Taiwan. Fixed annuity deposits in Korea were down in the nine-month period ended September 30, 2008 compared to the same period last year due to a recent market shift toward variable universal life products.

Asia results, presented on a sub-product basis were as follows:

(in millions)	Premiums and Other Considerations	Net Investment Income	Net Realized Capital Gains (Losses)	Total Revenues	Operating Income (Loss)
Nine Months Ended September 30, 2008					
Life insurance	**$ 9,174**	**$1,585**	**$(2,478)**	**$ 8,281**	**$(1,150)**
Personal accident	**1,553**	**136**	**(92)**	**1,597**	**157**
Group products	**686**	**88**	**(60)**	**714**	**52**
Individual fixed annuities	**30**	**100**	**(65)**	**65**	**(29)**
Individual variable annuities	**5**	**2**	**–**	**7**	**(1)**
Total	**$11,448**	**$1,911**	**$(2,695)**	**$10,664**	**$ (971)**
Nine Months Ended September 30, 2007					
Life insurance	$ 8,479	$3,663	$ (49)	$12,093	$ 1,636
Personal accident	1,361	111	(1)	1,471	247
Group products	510	76	(68)	518	21
Individual fixed annuities	33	90	(5)	118	16
Individual variable annuities	2	3	–	5	1
Total	$10,385	$3,943	$ (123)	$14,205	$ 1,921
Percentage Increase/(Decrease) from Prior Year:					
Life insurance	8%	(57)%	–%	(32)%	–%
Personal accident	14	23	–	9	(36)
Group products	35	16	–	38	148
Individual fixed annuities	(9)	11	–	(45)	–
Individual variable annuities	150	(33)	–	40	–
Total	10%	(52)%	–%	(25)%	–%

Total revenues in Asia in the nine-month period ended September 30, 2008 decreased compared to the same period in 2007 primarily due to higher net realized capital losses and lower net investment income, which more than offset the growth in premiums and other considerations. Net investment income declined due to policyholder trading losses of $1.4 billion in 2008 compared to gains of $652 million in 2007 and partnership and mutual fund losses of $413 million in 2008 compared to income of $149 million in the same period in 2007. The higher realized capital losses were primarily due to other-than-temporary impairment charges.

Asia reported an operating loss of $971 million for the nine-month period ended September 30, 2008 compared to operating income of $1.9 billion in the same period in 2007. Results for the year were affected by lower total revenues, lower operating income in Taiwan and a $31 million loss recognition charge in the Philippine operations.

Quarterly Domestic Life Insurance Results

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

(in millions)	Premiums and Other Considerations	Net Investment Income	Net Realized Capital Gains (Losses)	Total Revenues	Operating Income (Loss)
Three Months Ended September 30, 2008					
Life insurance	**$ 667**	**$331**	**$(3,471)**	**$(2,473)**	**$(3,176)**
Home service	**189**	**161**	**(577)**	**(227)**	**(486)**
Group life/health	**211**	**49**	**(64)**	**196**	**(70)**
Payout annuities*	**639**	**327**	**(211)**	**755**	**(154)**
Individual fixed and runoff annuities	**8**	**105**	**(68)**	**45**	**(25)**
Total	**$1,714**	**$973**	**$(4,391)**	**$(1,704)**	**$(3,911)**
Three Months Ended September 30, 2007					
Life insurance	$ 586	$375	$ (253)	$ 708	$ (56)
Home service	189	160	(29)	320	52
Group life/health	211	48	(5)	254	53
Payout annuities*	494	287	(10)	771	(13)
Individual fixed and runoff annuities	15	115	2	132	25
Total	$1,495	$985	$ (295)	$ 2,185	$ 61
Percentage Increase/(Decrease) from Prior Year:					
Life insurance	14%	(12)%	–%	–%	–%
Home service	–	1	–	–	–
Group life/health	–	2	–	(23)	–
Payout annuities	29	14	–	(2)	–
Individual fixed and runoff annuities	(47)	(9)	–	(66)	–
Total	15%	(1)%	–%	–%	–%

* *Includes structured settlements, single premium immediate annuities and terminal funding annuities.*

Total Domestic Life Insurance revenues decreased in the three-month period ended September 30, 2008 compared to the same period in 2007 due to significantly higher net realized capital losses, partially offset by higher premiums and other considerations. The increase in net realized capital losses was primarily driven by other-than-temporary impairment charges related to AIG's securities lending program and of securities held in general account portfolios. See Invested Assets — Securities Lending Activities for further information. Domestic Life Insurance premiums and other considerations increased in the three-month period ended September 30, 2008 compared to the same period in 2007 primarily due to strong payout annuity premiums and growth in life insurance business in force. Life insurance premiums and other considerations were also positively affected by a $52 million decrease in the unearned revenue liability related to certain blocks of universal life business. The growth in payout annuity deposits was driven by structured settlements and terminal funding annuities in both the U.S. and Canada. Net investment income for the three-month period ended September 30, 2008 was lower than the same period in 2007 despite growth in the underlying business due to reduced overall investment yield from increased levels of short-term investments and higher policyholder trading losses of $82 million.

Domestic Life Insurance reported an operating loss of $3.9 billion for the three-month period ended September 30, 2008 compared to operating income of $61 million in the same period in 2007 due principally to higher net realized capital losses, partially offset by growth in the in-force block and favorable mortality experience in life insurance and payout annuities. Life insurance results were also affected by higher DAC amortization of $30 million due to the decrease in the unearned revenue liability described above, resulting in a net benefit of $22 million. Due to a projected decline in sales as a result of AIG parent's liquidity issues, the deferral of acquisition costs was limited during the three-month period ended September 30, 2008 resulting in additional acquisition expenses of $13 million. In addition, 2007 payout annuities operating income was adversely affected by a $30 million adjustment to increase group annuity reserves. Home service reported an operating loss due to higher net realized capital losses partially offset by improved margins on the in-force business. Group life/health reported an operating loss during the three-month period ended September 30, 2008 compared to the same period in 2007 primarily due to higher net realized capital losses and the strengthening of long-term disability reserves of $8 million. In addition, for the three-month period ended September 30, 2008, policyholder benefit reserves included an increase of $11 million related to the workers compensation reinsurance program compared to a reduction in expense of $52 million for the same period in 2007. The loss for the three-month period ended September 30, 2008 includes a DAC benefit related to realized capital losses of $36 million compared to a DAC benefit of $4 million in the same period in 2007.

Year-to-Date Domestic Life Insurance Results

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

(in millions)	Premiums and Other Considerations	Net Investment Income	Net Realized Capital Gains (Losses)	Total Revenues	Operating Income (Loss)
Nine Months Ended September 30, 2008					
Life insurance	**$1,877**	**$1,069**	**$(5,636)**	**$(2,690)**	**$(4,933)**
Home service	**563**	**477**	**(915)**	**125**	**(660)**
Group life/health	**633**	**144**	**(91)**	**686**	**(64)**
Payout annuities*	**1,797**	**950**	**(266)**	**2,481**	**(99)**
Individual fixed and runoff annuities	**35**	**323**	**(147)**	**211**	**(30)**
Total	**$4,905**	**$2,963**	**$(7,055)**	**$ 813**	**$(5,786)**
Nine Months Ended September 30, 2007					
Life insurance	$1,767	$1,149	$ (213)	$ 2,703	$ 393
Home service	576	479	(42)	1,013	200
Group life/health	637	152	(10)	779	57
Payout annuities*	1,370	852	(51)	2,171	55
Individual fixed and runoff annuities	42	364	(7)	399	69
Total	$4,392	$2,996	$ (323)	$ 7,065	$ 774
Percentage Increase/(Decrease) from Prior Year:					
Life insurance	6%	(7)%	–%	–%	–%
Home service	(2)	–	–	(88)	–
Group life/health	(1)	(5)	–	(12)	–
Payout annuities	31	12	–	14	–
Individual fixed and runoff annuities	(17)	(11)	–	(47)	–
Total	12%	(1)%	–%	(88)%	–%

* *Includes structured settlements, single premium immediate annuities and terminal funding annuities.*

Total Domestic Life Insurance revenues decreased in the nine-month period ended September 30, 2008 compared to the same period in 2007 due to higher net realized capital losses partially offset by higher premiums and other considerations. The increase in net realized capital losses was primarily driven by other-than-temporary impairment charges related to AIG's securities lending program and of securities held in general account portfolios. See Invested Assets — Securities Lending Activities. Domestic Life Insurance premiums and other considerations increased in the nine-month period ended September 30, 2008 compared to the same period in 2007 primarily due to strong payout annuity premiums and growth in life insurance business in force. Life insurance premiums and other considerations were also positively affected by a $52 million decrease in the unearned revenue liability related to certain blocks of universal life business. The growth in payout annuity deposits was driven by sales of structured settlements and terminal funding annuities in both the U.S. and Canada. Net investment income for the nine-month period ended September 30, 2008 was down slightly due to reduced overall investment yield from increased levels of short-term investments and higher policyholder trading losses of $94 million.

Domestic Life Insurance reported an operating loss of $5.8 billion for the nine-month period ended September 30, 2008 compared to operating income of $774 million in the same period in 2007 due principally to higher net realized capital losses. Partially offsetting this item was the growth in the in-force block and favorable mortality experience in the life insurance and payout annuities businesses. Life insurance results were also affected by higher DAC amortization of $30 million due to the decrease in the unearned revenue liability described above, resulting in a net benefit of $22 million. Due to a projected decline in sales as a result of AIG parent's liquidity issues, the deferral of acquisition costs was limited during the nine-month period ended September 30, 2008 resulting in additional acquisition expenses of $17 million. In addition, 2007 payout annuities operating income was adversely affected by a $30 million adjustment to increase group annuity reserves. Home service reported an operating loss due to higher net realized capital losses partially offset by improved margins on the in-force business. Group life/health reported an operating loss during the nine-month period ended September 30, 2008 compared to the same period in 2007 primarily due to higher net realized capital losses and the strengthening of long-term disability reserves of $8 million. In addition, for the nine-month period ended September 30, 2008, policyholder benefit reserves included an increase of $11 million related to the workers compensation reinsurance program compared to a reduction in expense of $52 million for the same period in 2007. The operating loss during the nine-month period ended September 30, 2008 includes a DAC benefit related to realized capital losses of $73 million compared to a DAC benefit of $8 million in the same period in 2007.

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

(in millions)	Three Months Ended September 30, 2008	Three Months Ended September 30, 2007	Percentage Increase/ (Decrease)	Nine Months Ended September 30, 2008	Nine Months Ended September 30, 2007	Percentage Increase/ (Decrease)
Life insurance						
Periodic premium by product:						
Universal life	**$ 42**	$ 52	(19)%	**$ 135**	$ 150	(10)%
Variable universal life	**9**	19	(53)	**51**	44	16
Term life	**58**	53	9	**171**	165	4
Whole life/other	**2**	2	–	**8**	7	14
Total periodic premiums by product	**111**	126	(12)	**365**	366	–
Unscheduled and single deposits	**52**	134	(61)	**225**	315	(29)
Total life insurance	**163**	260	(37)	**590**	681	(13)
Home service						
Life insurance and accident and health	**25**	22	14	**69**	71	(3)
Fixed annuities	**54**	28	93	**123**	73	68
Unscheduled and single deposits	**7**	4	75	**17**	12	42
Total home service	**86**	54	59	**209**	156	34
Group life/health	**28**	28	–	**100**	88	14
Payout annuities	**867**	711	22	**2,417**	1,996	21
Individual fixed and runoff annuities	**361**	163	121	**701**	351	100
Total sales and deposits	**$1,505**	$1,216	24%	**$4,017**	$3,272	23%

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

Total Domestic Life Insurance sales and deposits increased 24 percent and 23 percent for the three- and nine-month periods, respectively, over the same periods in 2007. This growth was principally driven by strong term life, fixed annuity and payout annuity sales. However, the ratings downgrades and recent negative publicity related to AIG and AIG American General are expected to have a significant adverse effect on future sales.

Domestic Life Insurance periodic premium sales decreased 12 percent in the three-month period ended September 30, 2008 compared to the same period in 2007 primarily as a result of lower variable universal life sales. Periodic premium sales were consistent with the nine month period ended September 30, 2008 compared to the same period in 2007 as lower universal life sales were offset by increased private placement variable universal life and term sales. The U.S. life insurance market remains highly competitive and Domestic Life's emphasis on maintaining new business margins has affected sales of term and universal life products, although recent enhancements to term products have resulted in an increase in sales. Group life/health growth was driven by increased sales of supplemental health and voluntary products. Payout annuities have experienced strong growth from terminal funding and structured settlement sales in both the U.S. and Canada. Home service growth was driven by a 14 percent increase in life insurance sales and by increased fixed annuity deposits. Individual fixed and runoff annuities sales and deposits have increased as a result of the current interest rate environment as credited rates offered during the quarter were more competitive with the rates offered by banks on certificates of deposit.

Domestic Life Insurance sales for the three-month period ended September 30, 2008 were up despite AIG parent's liquidity issues.

Quarterly Domestic Retirement Services Results

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

(in millions)	Premiums and Other Considerations	Net Investment Income	Net Realized Capital Gains (Losses)	Total Revenues	Operating Income (Loss)
Three Months Ended September 30, 2008					
Group retirement products	**$102**	**$ 307**	**$(2,533)**	**$(2,124)**	**$(2,487)**
Individual fixed annuities	**26**	**499**	**(5,209)**	**(4,684)**	**(5,239)**
Individual variable annuities	**150**	**14**	**(375)**	**(211)**	**(830)**
Individual annuities — runoff*	**3**	**78**	**(378)**	**(297)**	**(369)**
Total	**$281**	**$ 898**	**$(8,495)**	**$(7,316)**	**$(8,925)**
Three Months Ended September 30, 2007					
Group retirement products	$114	$ 510	$ (116)	$ 508	$ 120
Individual fixed annuities	24	828	(177)	675	42
Individual variable annuities	159	38	(22)	175	41
Individual annuities — runoff*	3	95	(19)	79	(1)
Total	$300	$1,471	$ (334)	$ 1,437	$ 202
Percentage Increase/(Decrease) from Prior Year:					
Group retirement products	(11)%	(40)%	–%	–%	–%
Individual fixed annuities	8	(40)	–	–	–
Individual variable annuities	(6)	(63)	–	–	–
Individual annuities — runoff	–	(18)	–	–	–
Total	(6)%	(39)%	–%	–%	–%

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

Domestic Retirement Services incurred a significant operating loss of $8.9 billion in the three-month period ended September 30, 2008 compared to operating income of $202 million in the same period in 2007, primarily due to significantly increased net realized capital losses and losses on partnership investments. Net realized capital losses for Domestic Retirement Services increased primarily due to other-than-temporary impairment charges of $8.0 billion in the three-month period ended September 30, 2008 compared to charges of $157 million in the same period in 2007, primarily driven by severity losses related to RMBS in AIG's securities lending program due to the change of intent and ability to hold those securities to recovery.

Group retirement products and individual fixed annuities reported a combined operating loss of $7.7 billion in the three-month period ended September 30, 2008 compared to operating income of $162 million in the same period in 2007, primarily as a result of increased net realized capital losses due to higher other-than-temporary impairment charges, losses on partnership investments, DAC and SIA charges and reduced overall investment yield from increased levels of short-term investments. DAC and SIA charges for group retirement products and individual fixed annuities totaled $31 million and $166 million, respectively, related to projected increases in surrenders. These negative effects were partially offset by decreases in DAC amortization and SIA costs of $337 million related to the net realized capital losses compared to $39 million in the same period in 2007.

Individual variable annuities reported an operating loss of $830 million in the three-month period ended September 30, 2008 compared to income of $41 million in the same period in 2007, primarily due to a $531 million DAC charges and related reserve strengthening as a result of continued weakness in the equity markets and, to a lesser extent, increases in anticipated surrenders in the fourth quarter 2008. In addition, net realized capital losses increased largely due to higher other-than-temporary impairment charges and $207 million of increased embedded policy derivative liability valuations, net of related hedges. These decreases were partially offset by decreases in DAC amortization and SIA costs of $54 million related to the net realized capital losses compared to $15 million in the same period in 2007.

Year-to-Date Domestic Retirement Services Results

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

(in millions)	Premiums and Other Considerations	Net Investment Income	Net Realized Capital Gains (Losses)	Total Revenues	Operating Income (Loss)
Nine Months Ended September 30, 2008					
Group retirement products	**$320**	**$1,289**	**$ (4,213)**	**$(2,604)**	**$ (3,679)**
Individual fixed annuities	**66**	**2,075**	**(8,046)**	**(5,905)**	**(7,469)**
Individual variable annuities	**459**	**83**	**(670)**	**(128)**	**(1,017)**
Individual annuities — runoff*	**10**	**240**	**(650)**	**(400)**	**(625)**
Total	**$855**	**$3,687**	**$(13,579)**	**$(9,037)**	**$(12,790)**
Nine Months Ended September 30, 2007					
Group retirement products	$331	$1,721	$ (229)	$ 1,823	$ 661
Individual fixed annuities	75	2,723	(346)	2,452	606
Individual variable annuities	460	123	(29)	554	146
Individual annuities — runoff*	16	294	(20)	290	39
Total	$882	$4,861	$ (624)	$ 5,119	$ 1,452
Percentage Increase/(Decrease) from Prior Year:					
Group retirement products	(3)%	(25)%	–%	–%	–%
Individual fixed annuities	(12)	(24)	–	–	–
Individual variable annuities	–	(33)	–	–	–
Individual annuities — runoff	(38)	(18)	–	–	–
Total	(3)%	(24)%	–%	–%	–%

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

Domestic Retirement Services incurred a significant operating loss of $12.8 billion in the nine-month period ended September 30, 2008 compared to operating income of $1.5 billion in the same period in 2007, primarily due to significantly increased net realized capital losses and losses on partnership investments. Net realized capital losses for Domestic Retirement Services increased primarily due to other-than-temporary impairment charges of $12.8 billion in the nine-month period ended September 30, 2008 compared to charges of $343 million in the same period in 2007, primarily driven by losses related to securities held in AIG's securities lending program due to the change of intent and ability to hold those securities to recovery.

Both group retirement products and individual fixed annuities reported operating losses in the nine-month period ended September 30, 2008 compared to the same period in 2007 primarily as a result of increased net realized capital losses due to higher other-than-temporary impairment charges, lower net investment income due to partnership losses, lower yield enhancement income and reduced overall investment yield from increased levels of short term investments. In addition, DAC and SIA charges for group retirement products and individual fixed annuities totaled $197 million as discussed above. These negative effects were partially offset by decreases in DAC amortization and SIA costs of $666 million related to the net realized capital losses compared to $94 million in the same period in 2007.

Individual variable annuities reported an operating loss of $1.0 billion in the nine-month period ended September 30, 2008 compared to operating income of $146 million in the same period in 2007 primarily as a result of significantly increased net realized capital losses, principally due to other-than-temporary impairment charges and $361 million of increased embedded policy derivative liability valuations, net of related hedges, as well as the $531 million DAC and related reserve strengthening charges described above. Operating losses also included DAC and SIA benefits of $110 million related to the net realized capital losses compared to $21 million in the same period in 2007.

The account value roll forward for Domestic Retirement Services by product was as follows:

	Three Months Ended September 30,		Nine Months Ended September 30,	
(in millions)	**2008**	2007	**2008**	2007
Group retirement products				
Balance at beginning of period	**$ 66,189**	$ 67,687	**$ 68,109**	$ 64,357
Deposits – annuities	**1,450**	1,533	**4,375**	4,414
Deposits – mutual funds	**379**	501	**1,174**	1,296
Total deposits	**1,829**	2,034	**5,549**	5,710
Surrenders and other withdrawals	**(1,637)**	(1,649)	**(4,409)**	(5,061)
Death benefits	**(56)**	(66)	**(179)**	(196)
Net inflows	**136**	319	**961**	453
Change in fair value of underlying investments, interest credited, net of fees	**(3,227)**	694	**(5,972)**	3,889
Other	–	(1)	–	–
Balance at end of period	**$ 63,098**	$ 68,699	**$ 63,098**	$ 68,699

(in millions)	Three Months Ended September 30, 2008	Three Months Ended September 30, 2007	Nine Months Ended September 30, 2008	Nine Months Ended September 30, 2007
Individual fixed annuities				
Balance at beginning of period	**$ 52,077**	$ 52,170	**$ 50,508**	$ 52,685
Deposits	**1,561**	993	**6,036**	3,857
Surrenders and other withdrawals	**(2,096)**	(2,092)	**(5,136)**	(5,611)
Death benefits	**(400)**	(436)	**(1,224)**	(1,293)
Net outflows	**(935)**	(1,535)	**(324)**	(3,047)
Change in fair value of underlying investments, interest credited, net of fees	**481**	501	**1,439**	1,498
Balance at end of period	**$ 51,623**	$ 51,136	**$ 51,623**	$ 51,136
Individual variable annuities				
Balance at beginning of period	**$ 30,667**	$ 33,051	**$ 33,108**	$ 31,093
Deposits	**1,051**	1,181	**3,190**	3,393
Surrenders and other withdrawals	**(1,254)**	(1,031)	**(3,127)**	(3,078)
Death benefits	**(131)**	(124)	**(381)**	(374)
Net inflows (outflows)	**(334)**	26	**(318)**	(59)
Change in fair value of underlying investments, interest credited, net of fees	**(2,804)**	700	**(5,261)**	2,743
Balance at end of period	**$ 27,529**	$ 33,777	**$ 27,529**	$ 33,777
Total Domestic Retirement Services				
Balance at beginning of period	**$148,933**	$152,908	**$151,725**	$148,135
Deposits	**4,441**	4,208	**14,775**	12,960
Surrenders and other withdrawals	**(4,987)**	(4,772)	**(12,672)**	(13,750)
Death benefits	**(587)**	(626)	**(1,784)**	(1,863)
Net inflows (outflows)	**(1,133)**	(1,190)	**319**	(2,653)
Change in fair value of underlying investments, interest credited, net of fees	**(5,550)**	1,895	**(9,794)**	8,130
Other	**–**	(1)	**–**	–
Balance at end of period, excluding runoff	**142,250**	153,612	**142,250**	153,612
Individual annuities runoff	**5,307**	5,829	**5,307**	5,829
Balance at end of period	**$147,557**	$159,441	**$147,557**	$159,441
General and separate account reserves and mutual funds				
General account reserve			**$ 91,472**	$ 89,595
Separate account reserve			**48,518**	61,696
Total general and separate account reserves			**139,990**	151,291
Group retirement mutual funds			**7,567**	8,150
Total reserves and mutual funds			**$147,557**	$159,441

The decrease in group retirement products deposits was due to a decline in both group annuity deposits and group mutual fund deposits. The improvement in individual fixed annuity deposits was due to a steepened yield curve, providing the opportunity to offer higher interest crediting rates than certificates of deposits and mutual fund money market rates available at the time. Although new individual variable annuity products and features were developed in 2007 and 2008, sales did not increase due to declines in the equity markets.

Domestic Retirement Services surrenders and other withdrawals decreased in the group retirement and individual fixed annuity product lines in the nine-month period ended September 30, 2008 compared to the same period in 2007. In general, surrenders and other withdrawals decreased as a result of the relative lack of attractive alternative investment products. However, Domestic Retirement Services surrenders and other withdrawals increased in September 2008 subsequent to the AIG ratings downgrades and the announcement of the Fed Credit Agreement.

Domestic Retirement Services reserves by surrender charge category and surrender rates were as follows:

(in millions)	Group Retirement Products*	Individual Fixed Annuities	Individual Variable Annuities
September 30, 2008			
No surrender charge	**$47,162**	**$11,362**	**$10,886**
0% – 2%	**2,301**	**3,303**	**3,906**
Greater than 2% – 4%	**2,492**	**7,272**	**3,207**
Greater than 4%	**2,666**	**26,399**	**8,944**
Non-surrenderable	**910**	**3,287**	**586**
Total reserves	**$55,531**	**$51,623**	**$27,529**
Surrender rates	**8.9%**	**13.3%**	**13.6%**
September 30, 2007			
No surrender charge	$46,193	$ 9,763	$13,142
0% – 2%	6,519	2,835	5,597
Greater than 2% – 4%	3,771	7,904	5,598
Greater than 4%	3,191	27,205	9,348
Non-surrenderable	875	3,429	92
Total reserves	$60,549	$51,136	$33,777
Surrender rates	10.2%	14.4%	12.7%

* *Excludes mutual funds of $7.6 billion and $8.2 billion at September 30, 2008 and 2007, respectively.*

Surrender rates were essentially flat for group retirement products and individual fixed annuities for the three-month period ended September 30, 2008 compared to the same period in 2007. Surrender rates decreased for group retirement products and individual fixed annuities in the nine-month period ended September 30, 2008 compared to the same period in 2007. The surrender rate for individual fixed annuities continues to be driven by the yield curve and the general aging of the in-force block. Surrender rates increased for individual variable annuities in both the three- and nine-month periods ended September 30, 2008 compared to the same periods in 2007 due to publicity concerning AIG's financial situation as well as significant declines in the equity markets. As mentioned above, surrenders have increased in all three product lines in September 2008 subsequent to the AIG ratings downgrades and the announcement of the Fed Credit Agreement.

Life Insurance & Retirement Services Net Investment Income and Net Realized Capital Gains (Losses)

The components of net investment income for Life Insurance & Retirement Services were as follows:

(in millions)	Three Months Ended September 30, 2008	2007	Nine Months Ended September 30, 2008	2007
Foreign Life Insurance & Retirement Services:				
Fixed maturities, including short-term investments	**$ 2,411**	$2,037	**$ 6,958**	$ 5,876
Equity securities	**214**	186	**325**	284
Interest on mortgage and other loans	**152**	119	**427**	346
Partnership income (loss)	**(40)**	–	**(29)**	86
Mutual funds	**(362)**	5	**(366)**	168
Trading account losses	**(501)**	(79)	**(722)**	(93)
Other[(a)]	**169**	65	**415**	193
Total investment income before policyholder income and trading gains (losses)	**2,043**	2,333	**7,008**	6,860
Policyholder investment income and trading gains (losses)[(b)]	**(1,489)**	141	**(1,645)**	2,017
Total investment income	**554**	2,474	**5,363**	8,877
Investment expenses	**80**	107	**279**	266
Net investment income	**$ 474**	$2,367	**$ 5,084**	$ 8,611
Domestic Life Insurance:				
Fixed maturities, including short-term investments	**$ 885**	$ 865	**$ 2,596**	$ 2,646
Equity securities	**25**	(4)	**66**	(7)
Interest on mortgage and other loans	**107**	110	**309**	312
Partnership income (loss) — excluding Synfuels	**(3)**	26	**22**	113
Partnership loss — Synfuels	**(2)**	(26)	**(10)**	(101)
Mutual funds	**(3)**	(1)	**(2)**	4
Other[(a)]	**55**	17	**117**	57
Total investment income before policyholder income and trading gains (losses)	**1,064**	987	**3,098**	3,024
Policyholder investment income and trading gains (losses)[(b)]	**(73)**	9	**(85)**	9
Total investment income	**991**	996	**3,013**	3,033
Investment expenses	**18**	11	**50**	37
Net investment income	**$ 973**	$ 985	**$ 2,963**	$ 2,996
Domestic Retirement Services:				
Fixed maturities, including short-term investments	**$ 1,229**	$1,325	**$ 3,577**	$ 4,089
Equity securities	**1**	4	**10**	28
Interest on mortgage and other loans	**147**	141	**444**	397
Partnership income (loss)	**(528)**	6	**(434)**	389
Other[(a)]	**64**	9	**136**	1
Total investment income	**913**	1,485	**3,733**	4,904
Investment expenses	**15**	14	**46**	43
Net investment income	**$ 898**	$1,471	**$ 3,687**	$ 4,861
Total:				
Fixed maturities, including short-term investments	**$ 4,525**	$4,227	**$13,131**	$12,611
Equity securities	**240**	186	**401**	305
Interest on mortgage and other loans	**406**	370	**1,180**	1,055
Partnership income (loss) — excluding Synfuels	**(571)**	32	**(441)**	588
Partnership loss — Synfuels	**(2)**	(26)	**(10)**	(101)
Mutual funds	**(365)**	4	**(368)**	172
Trading account losses	**(501)**	(79)	**(722)**	(93)
Other[(a)]	**288**	91	**668**	251
Total investment income before policyholder income and trading gains (losses)	**4,020**	4,805	**13,839**	14,788
Policyholder investment income and trading gains (losses)[(b)]	**(1,562)**	150	**(1,730)**	2,026
Total investment income	**2,458**	4,955	**12,109**	16,814
Investment expenses	**113**	132	**375**	346
Net investment income	**$ 2,345**	$4,823	**$11,734**	$16,468

(a) Includes real estate income, income on non-partnership invested assets, securities lending and Foreign Life Insurance & Retirement Services' equal share of the results of AIG Credit Card Company (Taiwan).

(b) Relates principally to assets held in various trading securities accounts that do not qualify for separate account treatment under AICPA SOP 03-1, "Accounting and Reporting by Insurance Enterprises for Certain Nontraditional Long-Duration Contracts and for Separate Accounts" (SOP 03-1). These amounts are principally offset by an equal change included in incurred policy losses and benefits.

Net investment income decreased $2.5 billion and $4.7 billion in the three- and nine-month periods ended September 30, 2008 compared to the same periods in 2007, respectively, reflective of the recent market volatility. For the three- and nine-month periods ended September 30, 2008, policyholder trading losses were $1.6 billion and $1.7 billion, respectively, compared to gains of $150 million and $2.0 billion in the same periods of 2007 reflecting equity market declines in Japan and Asia. In addition, net investment income was negatively affected by lower yield enhancement income from equity investments, and higher trading account losses. Domestic Life Insurance and Retirement Services held higher balances in cash and short-term investments which negatively affected investment income on fixed maturity securities. Historically, AIG generated income tax credits as a result of investing in Synfuels related to the partnership income (loss) shown in the table above. Synfuel production ceased effective December 31, 2007.

The components of net realized capital gains (losses) for Life Insurance & Retirement Services were as follows:

	Three Months Ended September 30,		Nine Months Ended September 30,	
(in millions)	**2008**	2007	**2008**	2007
Foreign Life Insurance & Retirement Services:				
Sales of fixed maturities	**$ (28)**	$(122)	**$ (12)**	$ (167)
Sales of equity securities	**337**	205	**608**	417
Other:				
Other-than-temporary impairments[(a)]	**(3,812)**	(90)	**(5,899)**	(552)
Foreign exchange transactions	**317**	247	**124**	337
Derivatives instruments	**(412)**	(130)	**(329)**	(195)
Other[(b)]	**143**	28	**422**	81
Total Foreign Life Insurance & Retirement Services	**$ (3,455)**	$ 138	**$ (5,086)**	$ (79)
Domestic Life Insurance:				
Sales of fixed maturities	**$ (256)**	$ (83)	**$ (266)**	$ (122)
Sales of equity securities	**(1)**	1	**2**	6
Other:				
Other-than-temporary impairments[(a)]	**(4,121)**	(102)	**(6,780)**	(170)
Foreign exchange transactions	**5**	5	**9**	7
Derivatives instruments	**(10)**	(121)	**(77)**	(91)
Other[(c)]	**(8)**	5	**57**	47
Total Domestic Life Insurance	**$ (4,391)**	$(295)	**$ (7,055)**	$ (323)
Domestic Retirement Services:				
Sales of fixed maturities	**$ (410)**	$(142)	**$ (473)**	$ (202)
Sales of equity securities	**18**	4	**41**	20
Other:				
Other-than-temporary impairments[(a)]	**(7,981)**	(157)	**(12,820)**	(343)
Foreign exchange transactions	**13**	6	**12**	13
Derivatives instruments	**(153)**	(34)	**(338)**	(81)
Other[(c)]	**18**	(11)	**(1)**	(31)
Total Domestic Retirement Services	**$ (8,495)**	$(334)	**$(13,579)**	$ (624)
Total:				
Sales of fixed maturities	**$ (694)**	$(347)	**$ (751)**	$ (491)
Sales of equity securities	**354**	210	**651**	443
Other:				
Other-than-temporary impairments[(a)]	**(15,914)**	(349)	**(25,499)**	(1,065)
Foreign exchange transactions	**335**	258	**145**	357
Derivatives instruments	**(575)**	(285)	**(744)**	(367)
Other[(b)(c)]	**153**	22	**478**	97
Total	**$(16,341)**	$(491)	**$(25,720)**	$(1,026)

(a) See Invested Assets — Portfolio Review — Other-Than-Temporary Impairments for additional information.

(b) Includes losses of $104 million and $16 million allocated to participating policyholders for the three-month periods ended September 30, 2008 and 2007, respectively, and losses of $282 million and $21 million for the nine-month periods ended September 30, 2008 and 2007, respectively.

(c) Includes losses of $12 million and $143 million for the nine-month period ended September 30, 2008 for Domestic Life Insurance and Domestic Retirement Services, respectively, related to the adoption of FAS 157 with respect to embedded policy derivatives.

Included in net realized capital gains (losses) are gains (losses) on sales of investments, derivative gains (losses) for transactions that did not qualify for hedge accounting treatment under FAS 133, foreign exchange gains and losses, other-than-temporary impairment charges and the effects of the adoption of FAS 157 further described below.

Foreign Life Insurance & Retirement Services' net realized capital losses were significantly higher in the nine months ended September 30, 2008 compared to the same period in 2007. The increased other-than-temporary impairment charges were primarily driven by severity losses, credit events and the change in AIG's intent and ability to hold until recovery. See Invested Assets — Portfolio Review herein for further information. Other-than-temporary impairment charges for credit events were primarily related to exposure to certain financial institutions. Other-than-temporary impairment charges of $1.4 billion for the nine months ended September 30, 2008 related to the change in AIG's intent and ability to hold to recovery were primarily driven by RMBS in AIG's securities lending portfolio and the need for additional liquidity for higher surrender activity in September, particularly in the Japan and Korea fixed annuity blocks. Foreign exchange transactions of $317 million and $124 million in the three and nine-month periods ended September 30, 2008, respectively, related to non-functional currency transactions, primarily in Japan and Asia. Derivatives in the Foreign Life Insurance & Retirement Services operations are primarily used to economically hedge cash flows related to U.S. dollar bonds back to the respective currency of the country, principally in Taiwan, Thailand and Singapore. These derivatives do not qualify for hedge accounting treatment under FAS 133 and are recorded in net realized capital gains (losses). The corresponding foreign exchange gain or loss with respect to the economically hedged bond is deferred in accumulated other comprehensive income (loss) until the bond is sold, matures or deemed to be other-than-temporarily impaired.

In the three- and nine-month periods ended September 30, 2008, the Domestic Life Insurance and Domestic Retirement Services operations incurred higher net realized capital losses primarily due to other-than-temporary impairment charges related to severity losses, credit events and the change in AIG's intent and ability to hold until recovery. Other-than-temporary impairment charges of $6.9 billion for the nine months ended September 30, 2008 related to the change in AIG's intent and ability to hold to recovery were primarily driven by securities held in AIG's securities lending portfolio. Derivatives in the Domestic Life Insurance operations include affiliated interest rate swaps used to economically hedge cash flows on bonds and option contracts used to economically hedge cash flows on indexed annuity and universal life products. These derivatives do not qualify for hedge accounting treatment under FAS 133 and are recorded in net realized capital gains (losses). The corresponding gain or loss with respect to the economically hedged bond is deferred in accumulated other comprehensive income (loss) until the bond is sold, matures or is deemed to be other-than-temporarily impaired.

The most significant effect of AIG's adoption of FAS 157 was the change in measurement of fair value for embedded policy derivatives. The pre-tax effect of adoption related to embedded policy derivatives was an increase in net realized capital losses of $155 million as of January 1, 2008. The effect of initial adoption was primarily due to an increase in the embedded policy derivative liability valuations resulting from the inclusion of explicit risk margins.

Deferred Policy Acquisition Costs and Sales Inducement Assets

DAC for Life Insurance & Retirement Services products arises from the deferral of costs that vary with, and are directly related to, the acquisition of new or renewal business. Policy acquisition costs for life insurance products are generally deferred and amortized over the premium paying period in accordance with FAS 60, "Accounting and Reporting by Insurance Enterprises" (FAS 60). Policy acquisition costs that relate to universal life and investment-type products are generally deferred and amortized, with interest in relation to the incidence of estimated gross profits to be realized over the estimated lives of the contracts in accordance with FAS 97. Value of Business Acquired (VOBA) is determined at the time of acquisition and is reported on the consolidated balance sheet with DAC and amortized over the life of the business, similar to DAC. AIG offers sales inducements to contract holders (bonus interest) on certain annuity and investment contracts. Sales inducements are recognized as an asset (SIA) with a corresponding increase to the liability for policyholders' contract deposits on the consolidated balance sheet and are amortized over the life of the contract similar to DAC. The deferral of acquisition and sales inducement costs increased $284 million in the nine-month period ended September 30, 2008 compared to the same period in 2007 primarily due to higher production in the Foreign Life Insurance operations and Domestic Retirement Services. Total amortization expense increased by $540 million in the nine-month period ended September 30, 2008 compared to the same period in 2007. The current year amortization includes a $957 million increase to operating income related to net realized capital losses in the first nine months of 2008 compared to $170 million in the same period of 2007 reflecting significantly higher other-than-temporary impairment charges. Current year amortization for Domestic Retirement Services also includes adjustments for DAC and SIA charges of $354 million related to the continued weakness in the equity markets, DAC and SIA charges of $71 million due to higher surrender activity in September 2008 and DAC and SIA charges of $199 million related to expected future higher surrender activity. There was no effect from higher surrender activity in Domestic Life and the Foreign Life operations as the write-off of the DAC was

offset by related policy charges. Annualized amortization expense levels in the first nine months of both 2008 and 2007 were approximately 13 percent of the opening DAC balance.

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

The major components of the changes in DAC/VOBA and SIA were as follows:

	Nine Months Ended September 30,					
	2008			2007		
(in millions)	DAC/VOBA	SIA	Total	DAC/VOBA	SIA	Total
Foreign Life Insurance & Retirement Services						
Balance at beginning of year	**$26,175**	**$ 681**	**$26,856**	$21,153	$ 404	$21,557
Acquisition costs deferred	**4,250**	**67**	**4,317**	4,047	99	4,146
Amortization (charged) or credited to operating income:						
Related to net realized capital gains (losses)	**105**	**3**	**108**	44	–	44
Related to unlocking future assumptions	**(24)**	**(2)**	**(26)**	53	4	57
All other amortization	**(2,864)**	**(50)**	**(2,914)**	(2,141)	(12)	(2,153)
Change in unrealized gains (losses) on securities	**2,216**	**7**	**2,223**	558	13	571
Increase (decrease) due to foreign exchange	**(70)**	**(11)**	**(81)**	125	4	129
Other*	**(1,088)**	**(298)**	**(1,386)**	68	–	68
Balance at end of period	**$28,700**	**$ 397**	**$29,097**	$23,907	$ 512	$24,419
Domestic Life Insurance						
Balance at beginning of year	**$ 6,432**	**$ 53**	**$ 6,485**	$ 6,006	$ 46	$ 6,052
Acquisition costs deferred	**656**	**11**	**667**	656	12	668
Amortization (charged) or credited to operating income:						
Related to net realized capital gains (losses)	**72**	**1**	**73**	8	–	8
All other amortization	**(472)**	**(6)**	**(478)**	(526)	(4)	(530)
Change in unrealized gains (losses) on securities	**415**	**–**	**415**	197	–	197
Increase (decrease) due to foreign exchange	**(40)**	**–**	**(40)**	80	–	80
Other*	**–**	**–**	**–**	(64)	–	(64)
Balance at end of period	**$ 7,063**	**$ 59**	**$ 7,122**	$ 6,357	$ 54	$ 6,411
Domestic Retirement Services						
Balance at beginning of year	**$ 5,838**	**$ 991**	**$ 6,829**	$ 5,651	$ 887	$ 6,538
Acquisition costs deferred	**654**	**163**	**817**	553	150	703
Amortization (charged) or credited to operating income:						
Related to net realized capital gains (losses)	**598**	**178**	**776**	96	22	118
Related to unlocking future assumptions	**(477)**	**(76)**	**(553)**	4	(17)	(13)
All other amortization	**(651)**	**(141)**	**(792)**	(677)	(120)	(797)
Change in unrealized gains (losses) on securities	**817**	**146**	**963**	314	62	376
Increase (decrease) due to foreign exchange	**–**	**–**	**–**	–	–	–
Balance at end of period	**$ 6,779**	**$1,261**	**$ 8,040**	$ 5,941	$ 984	$ 6,925
Total Life Insurance & Retirement Services						
Balance at beginning of year	**$38,445**	**$1,725**	**$40,170**	$32,810	$1,337	$34,147
Acquisition costs deferred	**5,560**	**241**	**5,801**	5,256	261	5,517
Amortization (charged) or credited to operating income:						
Related to net realized capital gains (losses)	**775**	**182**	**957**	148	22	170
Related to unlocking future assumptions	**(501)**	**(78)**	**(579)**	57	(13)	44
All other amortization	**(3,987)**	**(197)**	**(4,184)**	(3,344)	(136)	(3,480)
Change in unrealized gains (losses) on securities	**3,448**	**153**	**3,601**	1,069	75	1,144
Increase (decrease) due to foreign exchange	**(110)**	**(11)**	**(121)**	205	4	209
Other*	**(1,088)**	**(298)**	**(1,386)**	4	–	4
Balance at end of period	**$42,542**	**$1,717**	**$44,259**	$36,205	$1,550	$37,755

* *In 2008, primarily represents the cumulative effect of adoption of FAS 159. In 2007, primarily represents the cumulative effect of adoption of SOP 05-1.*

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

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

Future Policy Benefit Reserves

Periodically, the net benefit reserves (policy benefit reserves less DAC) established for Life Insurance & Retirement Services companies are tested to ensure that, including consideration of future expected premium payments, they are adequate to provide for future policyholder benefit obligations. The assumptions used to perform the tests are current best-estimate assumptions as to policyholder mortality, morbidity, terminations, company maintenance expenses and invested asset returns. For long duration traditional business, a "lock-in" principle applies, whereby the assumptions used to calculate the benefit reserves and DAC are set when a policy is issued and do not change with changes in actual experience. These assumptions include margins for adverse deviation in the event that actual experience might deviate from these assumptions. For business in force outside of North America, 47 percent of total policyholder benefit liabilities at September 30, 2008 represent traditional business where the lock-in principle applies. In most foreign locations, various guarantees are embedded in policies in force that may remain applicable for many decades into the future.

As experience changes over time, the best-estimate assumptions are updated to reflect observed changes. Because of the long-term nature of many of AIG's liabilities subject to the lock-in principle, small changes in certain of the assumptions may cause large changes in the degree of reserve adequacy. In particular, changes in estimates of future invested asset return assumptions have a large effect on the degree of reserve adequacy.

Taiwan

Beginning in 2000, the yield available on Taiwanese 10-year government bonds dropped from approximately 6 percent to 2.5 percent at September 30, 2008. Yields on most other invested assets have correspondingly dropped over the same period. Current sales are focused on products such as:

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

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

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

Future results of the reserve adequacy tests will involve significant management judgment as to mortality, morbidity, expense and termination rates and investment yields. Adverse changes in these assumptions could accelerate DAC amortization and necessitate reserve strengthening. The ability to maintain the current investment strategy is uncertain due to the recent significant declines in the Taiwan equity markets and the related effect on capital solvency and potential actions by the Taiwan regulators. Future results of the reserve adequacy tests will be affected by the nature, timing and duration of any potential change in investment strategy implemented for Nan Shan.

Financial Services Operations

AIG's Financial Services subsidiaries engage in diversified activities including aircraft and equipment leasing, capital markets, consumer finance and insurance premium finance.

Financial Services Results

Financial Services results were as follows:

(in millions)	Three Months Ended September 30, 2008	Three Months Ended September 30, 2007	Percentage Increase/ (Decrease)	Nine Months Ended September 30, 2008	Nine Months Ended September 30, 2007	Percentage Increase/ (Decrease)
Total revenues:						
Aircraft Leasing	**$ 1,367**	$1,237	11%	**$ 3,830**	$3,468	**10%**
Capital Markets[(a)]	**(8,337)**	540	**–**	**(23,168)**	701	**–**
Consumer Finance[(b)]	**1,029**	940	9	**2,988**	2,696	**11**
Other, including intercompany adjustments	**90**	68	32	**334**	244	**37**
Total	**$(5,851)**	$2,785	**–%**	**$(16,016)**	$7,109	**–%**
Operating income (loss):						
Aircraft Leasing	**$ 366**	$ 254	44%	**$ 921**	$ 625	**47%**
Capital Markets[(a)(c)(d)]	**(8,073)**	370	**–**	**(23,284)**	183	**–**
Consumer Finance[(b)(c)]	**(474)**	69	**–**	**(559)**	180	**–**
Other, including intercompany adjustments	**(22)**	(24)	**–**	**42**	20	**110**
Total	**$(8,203)**	$ 669	**–%**	**$(22,880)**	$1,008	**–%**

(a) Both revenues and operating income (loss) include unrealized market valuation losses on AIGFP's super senior credit default swap portfolio of $7.1 billion and $21.7 billion for the three- and nine-month periods ended September 30, 2008, respectively, and $352 million for the three- and nine-month periods ended September 30, 2007.

(b) The nine-month period ended September 30, 2007 included a pre-tax charge of $178 million related to domestic Consumer Finance's mortgage banking activities. Based on a current evaluation of the estimated cost of implementing the Supervisory Agreement entered into with the OTS, partial reversals of this prior year charge included in the three- and nine-month periods ended September 30, 2008 were $10 million and $53 million, respectively.

(c) The three- and nine-month periods ended September 30, 2008 include goodwill impairment charges of $341 million and $91 million related to Consumer Finance and Capital Markets, respectively, resulting from the downturn in the housing markets, the credit crisis and the decision to exit certain AIGFP businesses.

(d) The three- and nine-month periods ended September 30, 2008 include a $563 million reversal of accrued compensation expense under AIGFP's various deferred compensation plans and special incentive plan as a result of significant losses recognized by AIGFP in 2008.

Financial Services reported operating losses in the three- and nine-month periods ended September 30, 2008 compared to operating income in the same periods in 2007, primarily due to unrealized market valuation losses on AIGFP's super senior credit default swap portfolio of $7.1 billion and $21.7 billion in the three- and nine-month periods ended September 30, 2008, respectively, and $352 million for the three- and nine-month periods ended September 30, 2007. The remaining operating loss resulted from the change in credit spreads on AIGFP's other assets and liabilities and a decline in operating income for AGF. AGF's operating income declined in the three- and nine-month periods ended September 30, 2008 compared to the same periods in 2007 primarily due to increases in the provision for finance receivable losses and goodwill impairment. In addition, AGF recorded a pre-tax charge of $27 million in second quarter 2008 resulting from AGF's decision to cease its wholesale originations.

In the first nine months of 2007, AGF recorded a pre-tax charge of $178 million representing the estimated cost of implementing a supervisory agreement (the Supervisory Agreement) entered into with the Office of Thrift Supervision (OTS), which is discussed in the Consumer Finance results of operations section. Based on the evaluations of the estimated cost of implementing the Supervisory Agreement, AGF recorded partial reversals of this prior year charge of $10 million and $53 million for the three- and nine-month periods ended September 30, 2008, respectively.

ILFC generated strong operating income growth in the three-and nine-month periods ended September 30, 2008 compared to the same periods in 2007, driven to a large extent by a larger aircraft fleet, higher lease rates and higher utilization and lower composite borrowing rates.

Aircraft Leasing

Aircraft Leasing operations represent the operations of ILFC, which generates its revenues primarily from leasing new and used commercial jet aircraft to foreign and domestic airlines. Revenues also result from the remarketing of commercial aircraft for ILFC's own account, and remarketing and fleet management services for airlines and financial institutions. ILFC finances its aircraft purchases primarily through the issuance of debt instruments. ILFC economically hedges part of its floating rate and substantially all of its foreign currency denominated debt using interest rate and foreign currency derivatives. Starting in the second quarter of 2007, ILFC began applying hedge accounting to most of its derivatives. The composite borrowing rates, which include the effect of derivatives, at September 30, 2008 and 2007 were 5.01 percent and 5.28 percent, respectively.

ILFC typically contracts to re-lease aircraft before the end of the existing lease term. For aircraft returned before the end of the lease term, ILFC has generally been able to re-lease such aircraft within two to six months of their return. As a lessor, ILFC considers an aircraft "idle" or "off lease" when the

aircraft is not subject to a signed lease agreement or signed letter of intent. During the nine-month period ended September 30, 2008, 22 of ILFC's aircraft were returned by bankrupt lessees. As of October 27, 2008, ILFC has sold one and leased 18 of the 22 aircraft. As of October 31, 2008, all but three of the new aircraft scheduled for delivery through 2010 have been leased.

Quarterly Aircraft Leasing Results

ILFC's operating income increased in the three-month period ended September 30, 2008 compared to the same period in 2007. Rental revenues increased by $75 million or 6 percent, driven by a larger aircraft fleet, higher lease rates and higher utilization. As of September 30, 2008, 950 aircraft in ILFC's fleet were subject to operating leases compared to 894 aircraft as of September 30, 2007. Interest expense decreased by $19 million in the three-month period ended September 30, 2008 compared to the same period in 2007 as a result of lower short-term interest rates. The increases in revenues were offset by an increase in depreciation. Depreciation expense increased by $27 million, or 6 percent, in line with the increase in the size of the aircraft fleet. In the three-month period ended September 30, 2008 and 2007, the gains (losses) from hedging activities that did not qualify for hedge accounting treatment under FAS 133, including the related foreign exchange gains and losses, were $67 million and $(19) million, respectively, in both revenues and operating income.

Year-to-Date Aircraft Leasing Results

ILFC's operating income increased in the nine-month period ended September 30, 2008 compared to the same period in 2007. Rental revenues increased by $325 million or 10 percent, driven by a larger aircraft fleet, higher lease rates and higher utilization. As of September 30, 2008, 950 aircraft in ILFC's fleet were subject to operating leases compared to 894 aircraft as of September 30, 2007. Interest expense decreased by $70 million in the nine-month period ended September 30, 2008, compared to the same period in 2007, as a result of lower short-term interest rates. The increases in revenues were partially offset by an increase in depreciation. Depreciation expense increased by $102 million, or 8 percent, in line with the increase in the size of the aircraft fleet. In the nine-month period ended September 30, 2008 and 2007, the gains (losses) from hedging activities that did not qualify for hedge accounting treatment under FAS 133, including the related foreign exchange gains and losses, were $4 million and $(32) million, respectively, in both revenues and operating income.

Capital Markets

Capital Markets represents the operations of AIGFP, which has engaged as principal in a wide variety of financial transactions, including standard and customized financial products involving commodities, credit, currencies, energy, equities and rates. The credit products include credit protection written through credit default swaps on super senior risk tranches of diversified pools of loans and debt securities. AIGFP has also invested in a diversified portfolio of securities and principal investments and engaged in borrowing activities involving the issuance of standard and structured notes and other securities, and entering into GIAs. Given the extreme market conditions experienced during the third quarter of 2008, downgrades of AIG's credit ratings by the rating agencies, as well as AIG's intent to refocus on its core businesses, AIGFP began unwinding its businesses and portfolios.

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

AIGFP's products generally require sophisticated models and significant management assumptions to determine fair values and, particularly during times of market disruption, the absence of observable market data can result in fair values at any given balance sheet date that are not indicative of the ultimate settlement values of the products.

Quarterly Capital Markets Results

Capital Markets reported an operating loss in the three-month period ended September 30, 2008 compared to operating income in the same period of 2007, primarily due to a $7.1 billion unrealized market valuation loss related to AIGFP's super senior credit default swap portfolio principally written on multi-sector CDOs and credit valuation adjustments on AIGFP's assets and liabilities. During 2008, AIGFP instituted a number of measures to attempt to manage its liquidity in light of the deteriorating credit markets and its limited ability to access the capital markets. These measures ultimately were unsuccessful. These issues coupled with concerns regarding AIG's resulting financial condition and the subsequent downgrade of its ratings by rating agencies on September 15, 2008 have severely affected AIGFP's non-credit businesses resulting in a significant decline in revenue. AIGFP has not replaced revenues from certain structured transactions that were terminated or matured at the end of 2007 and early 2008.

The change in fair value of AIGFP's credit default swaps was caused by the significant widening in spreads and the downgrades of RMBS and CDO securities by rating agencies in the three-month period ended September 30, 2008 driven

by the credit concerns resulting from U.S. residential mortgages and the severe liquidity crisis affecting the markets. See Critical Accounting Estimates — Valuation of Level 3 Assets and Liabilities.

During the third quarter of 2008, AIGFP purchased super senior CDO securities with a net notional amount of $5.7 billion in connection with 2a-7 Puts. Upon purchase, $4.1 billion of these securities were included in AIGFP's trading securities portfolio and $1.6 billion of the securities were included in the available for sale portfolio at their fair value. Effective January 1, 2008 and until August 2008, AIGFP elected to apply the fair value option to all of its investment securities. In August 2008, AIGFP revised this election and now evaluates whether to elect the fair value option on a case by case basis for securities purchased in connection with the existing structured transaction. Approximately $840 million of the cumulative unrealized market valuation loss previously recognized on these derivatives was realized as a result of these purchases.

Capital Markets' operating loss for the three-month period ended September 30, 2008 includes a net loss of $987 million representing the effect of changes in credit spreads on the valuation of AIGFP's assets and liabilities, including $98 million of gains reflected in the unrealized market valuation loss on super senior credit default swaps. Historically, AIG's credit spreads and those on its assets moved in a similar fashion. This relationship began to diverge during second quarter of 2008 and the divergence continued through the third quarter. While AIG's credit spreads widened significantly more than the credit spreads on the ABS and CDO products, which represent a significant portion of AIGFP's investment portfolio, the losses on AIGFP's assets more than offset the net gain on its liabilities, which were driven by the significant widening in AIG's credit spreads. The net gain on AIGFP's liabilities was reduced by the effect of posting collateral and the early terminations of GIAs.

The following table presents AIGFP's credit valuation adjustment gains (losses) for the three-month period ended September 30, 2008 (excluding intercompany transactions):

(in millions)

Counterparty Credit Valuation Adjustment on Assets		AIG Inc.'s Own Credit Valuation Adjustment on Liabilities	
Trading securities	$(2,032)	Term notes	$ 1,003
Loans and other assets	(7)	Hybrid term notes	729
Derivative assets	(240)	GIAs	(1,272)
		Other liabilities	81
		Derivative liabilities*	751
Decrease in assets	$(2,279)	Decrease in liabilities	$ 1,292
Net pre-tax decrease to other income	$ (987)		

** Includes super senior credit default swap portfolio*

During the third quarter of 2008, AIGFP recognized a gain of $450 million on a sale of its interest in a private equity investment to a consolidated affiliate of AIG, which is eliminated in consolidation. This gain was partially offset by a $322 million loss recorded under the equity method of accounting reflecting AIGFP's share of a goodwill impairment charge recognized by this private equity investment in the third quarter of 2008.

During 2008, AIGFP's revenues from certain products have declined, in part, as a consequence of the continued disruption in the credit markets, the general decline in liquidity in the marketplace, and AIGFP's efforts to manage its liquidity.

The most significant component of Capital Markets operating expenses is compensation. Due to the significant losses recognized by AIGFP during 2008, the entire amount of $563 million accrued under AIGFP's various deferred compensation plans and special incentive plan was reversed in the third quarter of 2008. In the first quarter of 2008, AIGFP established an employee retention plan, which guarantees a broad group of AIGFP's employees and consultants a minimum level of compensation for each of the 2008 and 2009 compensation years, subject to mandatory partial deferral which, in certain circumstances, will be indexed to the price of AIG stock. The expense related to the retention plan is being recognized over the vesting period, beginning in the first quarter of 2008.

Year-to-Date Capital Markets Results

Capital Markets reported an increased operating loss in the nine-month period ended September 30, 2008 compared to the operating loss in the same period of 2007, primarily due to $21.7 billion in unrealized market valuation losses related to AIGFP's super senior credit default swap portfolio principally written on multi-sector CDOs and credit valuation adjustments on AIGFP's assets and liabilities. Financial market conditions in the nine-month period ended September 30, 2008 were characterized by widening credit spreads and declining interest rates.

During the second quarter of 2008, AIGFP implemented further refinements to the cash flow waterfall used by the BET model and the assumptions used therein. These refinements reflected the ability of a CDO to use principal proceeds to cover interest payment obligations on lower-rated tranches, the ability of a CDO to use principal proceeds to cure a breach of an over collateralization test, the ability of a CDO to amortize certain senior CDO tranches on a pro-rata or sequential basis and the preferential payment of management fees. To the extent there is a lag in the prices provided by the collateral managers, AIG refines those prices by rolling them forward to the end of the quarter using prices provided by a third party pricing service. The net effect of these refinements was an incremental unrealized market valuation loss of $342 million. Refinements made during the third quarter of 2008 had only a de minimis effect on the unrealized market valuation loss.

During the second quarter of 2008, AIGFP issued new 2a-7 Puts with a net notional amount of $5.4 billion on the super senior security issued by a CDO of AAA-rated commercial mortgage-backed securities (CMBS) pursuant to a facility that was entered into in 2005. At this time, AIGFP is not party to any commitments to enter into any new 2a-7 Puts.

During the nine month period ended September 30, 2008, AIGFP extinguished its obligations with respect to a credit default swap by purchasing the protected CDO security for $103 million, its principal amount outstanding related to this obligation. Additionally, AIGFP purchased other super senior CDO securities with a net notional amount of $6.6 billion in connection with 2a-7 Puts. Upon purchase, $5.0 billion of these securities were included in AIGFP's trading portfolio and $1.6 billion in available for sale portfolio at their fair value. Approximately $907 million of the cumulative unrealized market valuation loss previously recognized on these derivatives was realized as a result of these purchases.

The net loss recognized for the nine-month period ended September 30, 2007 included a $166 million reduction in fair value of certain derivatives that are an integral part of, and economically hedge, the structured transactions potentially affected by the proposed guidance by the United States Department of the Treasury affecting the ability to claim foreign tax credits.

Effective January 1, 2008, AIGFP adopted FAS 157. The most significant effect of adopting FAS 157 was a change in the valuation methodologies for hybrid financial instruments and derivative liabilities (both freestanding and embedded) historically carried at fair value. The changes were primarily to incorporate AIGFP's own credit risk, when appropriate, in the fair value measurements.

Effective January 1, 2008, AIGFP elected to apply the fair value option under FAS 159 to all eligible assets and liabilities (other than equity method investments trade receivables and trade payables) because electing the fair value option allows AIGFP to more closely align its earnings with the economics of its transactions by recognizing concurrently through earnings the change in fair value of its derivatives and the offsetting change in fair value of the assets and liabilities being hedged as well as the manner in which the business is evaluated by management. In August 2008, AIGFP prospectively modified this election as management believes it is appropriate to exclude the automatic election of securities purchased in connection with existing structured credit transactions and their related funding obligations. AIGFP will evaluate whether or not to elect the fair value option on a case-by-case basis for securities purchased in connection with existing structured credit transactions and their related funding obligations.

Capital Markets' operating loss for the nine-month period ended September 30, 2008 includes a loss of $1.4 billion representing the effect of changes in credit spreads on the valuation of AIGFP's assets and liabilities, including $207 million of gains reflected in the unrealized market valuation loss on super senior credit default swaps. Historically, AIG's credit spreads and those on its assets moved in a similar fashion. This relationship began to diverge during second quarter of 2008 and continued to diverge through the third quarter. While AIG's credit spreads widened significantly more than the credit spreads on the ABS and CDO products, which represent a significant portion of AIGFP's investment portfolio, the losses on AIGFP's assets more than offset the net gain on its liabilities, which were driven by the significant widening in AIG's credit spreads. The net gain on AIGFP's liabilities was reduced by the effect of posting collateral and the early terminations of GIAs. Included in the nine-month period ended September 30, 2008 operating loss is the transition amount of $291 million related to the adoption of FAS 157 and FAS 159.

The following table presents AIGFP's credit valuation adjustment gains (losses) for the nine-month period ended September 30, 2008 (excluding intercompany transactions):

(in millions)

Counterparty Credit Valuation Adjustment on Assets		AIG Inc.'s Own Credit Valuation Adjustment on Liabilities	
Trading securities	$(4,683)	Term notes	$1,185
Loans and other assets	(35)	Hybrid term notes	1,344
Derivative assets	(543)	GIAs	(200)
		Other liabilities	109
		Derivative liabilities*	1,390
Decrease in assets	$(5,261)	Decrease in liabilities	$3,828
Net pre-tax decrease to other income	$(1,433)		

** Includes super senior CDS portfolio*

Year to date results also reflect the reversal of amounts accrued under AIGFP's various deferred compensation plans in the third quarter of 2008 as discussed above.

Consumer Finance

AIG's Consumer Finance operations in North America are principally conducted through AGF. AGF derives most of its revenues from finance charges assessed on outstanding real estate loans, secured and unsecured non-real estate loans and retail sales finance receivables and credit-related insurance.

Effective February 29, 2008, AGF purchased a portion of Equity One, Inc.'s consumer branch finance receivable portfolio consisting of $1.0 billion of real estate loans, $290 million of non-real estate loans, and $156 million of retail sales finance receivables.

AIG's foreign consumer finance operations are principally conducted through AIGCFG. AIGCFG operates primarily in emerging and developing markets. AIGCFG has operations in Argentina, China, Brazil, Hong Kong, Mexico, Philippines, Poland, Taiwan, Thailand, India and Colombia. In April 2008, AIGCFG decided to sell or liquidate its existing

operations in Taiwan. In October 2008, AIGCFG decided to sell its existing operations in Europe and Asia.

Certain of the AIGCFG operations are partly or wholly owned by life insurance subsidiaries of AIG. Accordingly, the financial results of those companies are allocated between Financial Services and Life Insurance & Retirement Services according to their ownership percentages. While products vary by market, the businesses generally provide credit cards, unsecured and secured non-real estate loans, term deposits, savings accounts, retail sales finance and real estate loans. AIGCFG originates finance receivables through its branches and direct solicitation. AIGCFG also originates finance receivables indirectly through relationships with retailers, auto dealers, and independent agents.

Quarterly Consumer Finance Results

Consumer Finance reported a significant operating loss in the three-month period ended September 30, 2008 compared to operating income in the same period in 2007, primarily due to the write-down of AGF's goodwill of $341 million during the third quarter of 2008 and increases in the provision for finance receivable losses of $198 million.

During 2007 and the nine months ended September 30, 2008, the U.S. residential real estate and credit markets continued to experience significant turmoil as housing prices softened, unemployment increased, consumer delinquencies increased, and credit availability contracted and became more expensive for consumers and financial institutions. These market developments are reflected in AGF's decline in consumer real estate loan originations affecting both revenue and operating income in 2007 and 2008.

AGF's revenues decreased $18 million or 2 percent during the three-month period ended September 30, 2008 compared to the same period in 2007. Revenues from AGF's loan brokerage fees decreased during the three-month period reflecting the slower United Kingdom housing market. AGF's net finance receivables totaled $26.2 billion at September 30, 2008, an increase of approximately $678 million compared to its net finance receivables at December 31, 2007. This increase reflects the purchase of $1.5 billion of finance receivables from Equity One, Inc. on February 29, 2008. The increase in the net finance receivables resulted in an increase in revenues generated from these assets, partially offset by the reduced residential mortgage originations as a result of the slower U.S. housing market.

Revenues from foreign consumer finance operations increased by 73 percent in the three-month period ended September 30, 2008 compared to the same period in 2007, due primarily to loan growth, particularly in Poland and Latin America, and revenues from the recently acquired business in Colombia. The increase in revenues was partially offset by increases in the provision for finance receivable losses and operating expenses associated with branch expansions, acquisition activities and product promotion campaigns.

Year-to-Date Consumer Finance Results

Consumer Finance reported a significant operating loss in the nine-month period ended September 30, 2008 compared to operating income in the same period in 2007, primarily due to increases in the provision for finance receivable losses of $471 million and the write-down of AGF's goodwill of $341 million during the nine months ended September 30, 2008. The nine-month period ended September 30, 2007 reflected a charge of $178 million relating to the estimated cost of implementing the Supervisory Agreement.

AGF's revenues increased $34 million or 2 percent during the nine-month period ended September 30, 2008 compared to the same period in 2007. Revenues from AGF's finance receivables increased as a result of the $1.5 billion finance receivable purchase in the first quarter of 2008, but were partially offset by reduced residential mortgage originations due to the slower U.S. housing market. Revenues from AGF's mortgage banking activities increased $166 million in the nine-month period ended September 30, 2008 compared to the same period in 2007 (which included a charge of $178 million related to the Supervisory Agreement). AGF reversed $53 million of the previously recorded charge in the nine months ended September 30, 2008. The nine-month period ended September 30, 2007 included a recovery of $65 million from a favorable out of court settlement. Revenues from AGF's loan brokerage fees decreased during the nine-month period reflecting the slower United Kingdom housing market.

Revenues from the foreign consumer finance operations increased by 55 percent in the nine-month period ended September 30, 2008 compared to the same period in 2007, due primarily to loan growth, particularly in Poland and Latin America, and revenues from the recently acquired business in Colombia. The increase in revenues was more than offset by increases in the provision for finance receivable losses and operating expenses associated with branch expansions, acquisition activities and product promotion campaigns.

Credit Quality of Finance Receivables

The overall credit quality of AGF's finance receivables portfolio deteriorated during the nine-month period ended September 30, 2008 due to negative economic fundamentals, the aging of the real estate loan portfolio and a higher proportion of non-real estate loans and retail sales finance receivables.

At September 30, 2008, the 60-day delinquency rate for the entire portfolio increased by 171 basis points to 4.18 percent compared to September 30, 2007, while the 60-day delinquency rate for real estate loans increased by 197 basis points to 4.19 percent. For the three-month period ended September 30, 2008, AGF's net charge-off rate increased to 2.15 percent compared to 1.15 percent for the same period in

2007 and for the nine-month period ended September 30, 2008 increased to 1.81 percent compared to 1.05 percent for the same period in 2007.

AGF's allowance for finance receivable losses as a percentage of outstanding receivables was 3.66 percent at September 30, 2008 compared to 2.11 percent at September 30, 2007.

Asset Management Operations

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

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

Spread-Based Investment Business

AIG's Spread-Based Investment business includes the results of AIG's proprietary Spread-Based Investment operations, the Matched Investment Program (MIP), which was launched in September of 2005 to replace the Guaranteed Investment Contract (GIC) program, which is in runoff whereby no new GIC contracts are being written. The MIP is an investment strategy that involves investing in various asset classes with financing provided through third parties. This business uses various risk mitigating strategies designed to hedge interest rate and currency risk associated with underlying investments and related liabilities. The MIP undertakes various other types of investment risk, namely credit, duration and maturity risk.

Institutional Asset Management

AIG's Institutional Asset Management business, conducted through AIG Investments, provides an array of investment products and services globally to institutional investors, pension funds, AIG subsidiaries and high net worth investors. These products include traditional equity and fixed maturity securities, and a wide range of alternative asset classes. These services include investment advisory and subadvisory services, investment monitoring, securities lending and transaction structuring. Within the fixed maturity and equity asset classes, AIG Investments offers various forms of structured investments aimed at achieving superior returns or capital preservation. Within the alternative asset class, AIG Investments offers hedge and private equity funds and fund-of-funds, direct investments and distressed debt investments.

AIG Global Real Estate provides a wide range of real estate investment and management services for AIG subsidiaries, as well as for third-party institutional investors, high net worth investors and pension funds. Through a strategic network of local real estate ventures, AIG Global Real Estate actively invests in and develops office, industrial, multi-family residential, retail, mixed-use hotel and resort properties located around the world.

AIG Private Bank offers banking, trading and investment management services to private clients and institutions globally. To further focus on its wealth management expansion efforts, AIG Private Bank Ltd. entered into a joint venture agreement with Bank Sarasin & Co. Ltd. Under this agreement, a new Swiss bank was established, into which both AIG Private Bank Ltd. and Bank Sarasin & Co. Ltd. contributed their retail banking businesses. The new bank commenced operations on July 1, 2008 with assets under management of approximately $8 billion.

From time to time, AIG Investments acquires warehoused assets. During the warehousing period, AIG bears the cost and risks associated with carrying these investments, consolidates them on its balance sheet and records the operating results until the investments are transferred, sold or otherwise divested. Changes in market conditions may negatively affect the fair value of these warehoused investments. Market conditions may impede AIG from launching new investment products for which these warehoused assets are being held and may prevent AIG from recovering its investment upon transfer or divestment. In the event that AIG is unable to transfer or otherwise divest its interest in the warehoused investment to third parties, AIG could be required to hold these investments indefinitely. In certain instances, the consolidated warehoused investments are not wholly owned by AIG. In such cases, AIG shares the risk associated with warehousing the asset with the minority interest investors.

Brokerage Services and Mutual Funds

AIG's Brokerage Services and Mutual Funds business, conducted through AIG Advisor Group, Inc. and AIG SunAmerica Asset Management Corp., provides broker-dealer related services and mutual funds to retail investors, group trusts and corporate accounts through an independent network of financial advisors. AIG Advisor Group, Inc., a subsidiary of AIG Retirement Services, Inc., is comprised of several broker-dealer entities that provide these services to clients primarily in the U.S. marketplace. AIG SunAmerica Asset Management Corp. manages, advises and/or administers retail mutual funds, as well as the underlying assets of variable annuities sold by AIG SunAmerica and VALIC to individuals and groups throughout the United States.

Other Asset Management

Included in Other Asset Management is income or loss from certain AIG SunAmerica sponsored partnerships and partnership investments. Partnership assets consist of investments in a diversified portfolio of private equity funds, affordable housing partnerships and hedge fund investments.

Asset Management Results

Asset Management results were as follows:

(in millions)	Three Months Ended September 30, 2008	Three Months Ended September 30, 2007	Percentage Increase/ (Decrease)	Nine Months Ended September 30, 2008	Nine Months Ended September 30, 2007	Percentage Increase/ (Decrease)
Total revenues:						
Spread-Based Investment business	**$ (903)**	$ 555	–%	**$(1,710)**	$2,304	–%
Institutional Asset Management	**782**	815	(4)	**1,993**	2,113	(6)
Brokerage Services and Mutual Funds	**67**	83	(19)	**215**	243	(12)
Other Asset Management	**64**	66	(3)	**160**	309	(48)
Total	**$ 10**	$1,519	(99)%	**$ 658**	$4,969	(87)%
Operating income (loss):						
Spread-Based Investment business	**$(1,229)**	$ 24	–%	**$(2,900)**	$ 759	–%
Institutional Asset Management	**10**	5	100	**(10)**	671	–
Brokerage Services and Mutual Funds	**10**	27	(63)	**46**	74	(38)
Other Asset Management	**65**	65	–	**155**	302	(49)
Total	**$(1,144)**	$ 121	–%	**$(2,709)**	$1,806	–%

Asset Management recognized operating losses in the three-and nine-month periods ended September 30, 2008 compared to operating income in the same periods in 2007, primarily due to other-than-temporary impairment charges on fixed maturity securities, significantly lower partnership income, lower securities lending fees, lower net carried interest revenues and impairments on real estate investments. Partially offsetting these declines were increases in net foreign exchange gains on foreign currency denominated GIC and MIP liabilities. Included in operating income (loss) for the three-month period ended September 30, 2008, was the positive effect of excluding the credit valuation adjustment on intercompany derivatives, which had no effect on AIG's consolidated results. The effect of this change on Asset Management was an increase of $155 million to operating income for the three- and nine-month periods ended September 30, 2008, and has been included in the net mark to market gains/losses related to interest rate and foreign exchange hedges, as well as the losses on credit default swaps, identified below. Included in the operating income during the nine-month period ended September 30, 2007 was a gain on the sale of a portion of AIG's investment in The Blackstone Group L.P. (Blackstone) in connection with its initial public offering.

Quarterly Spread-Based Investment Business Results

The Spread-Based Investment business reported an operating loss in the three-month period ended September 30, 2008 compared to marginal operating income in the same period in 2007 due to significantly higher net realized capital losses and lower partnership income. Net realized capital losses for the three-month period ended September 30, 2008, were $1.3 billion compared to $239 million in the same period of 2007 . The increase in net realized capital losses primarily consists of an increase of $1.8 billion in other-than-temporary impairment charges on fixed maturity securities for both the GIC and MIP portfolios and higher mark to market losses on credit default swaps in the MIP. Partially offsetting these increases was a $995 million increase in net foreign exchange gains on foreign currency denominated GIC and MIP liabilities and higher net mark to market gains of $125 million on interest rate and foreign exchange hedges not qualifying for hedge accounting treatment for both the GIC and MIP. Included in the net mark-to-market gains is a credit valuation adjustment on swaps in a liability position.

The other-than-temporary impairment charges on fixed maturity securities held in the GIC and MIP portfolios were $1.4 billion for the GIC and $579 million for the MIP for the three-month period ended September 30, 2008. These impairments primarily resulted from severity losses and the change in AIG's intent and ability to hold securities to recovery related to the Securities Lending portfolio. See Invested Assets — Portfolio Review — Other-Than-Temporary Impairments.

In the GIC program, income from partnership investments declined $330 million for the three-month period ended September 30, 2008, compared to the same period of 2007, reflecting higher returns in the 2007 period and weaker market conditions in 2008. Partially offsetting this decline were foreign exchange gains on foreign currency denominated GIC reserves, which increased by $916 million in the three-month period ended September 30, 2008 compared to the same period in 2007 as a result of the strengthening of the U.S. dollar. As noted below, a significant portion of these GIC reserves mature in the next twelve months.

Operating income for the MIP increased in the three-month period ended September 30, 2008 compared to the same period in 2007, primarily due to higher net interest income resulting from the effect of lower funding costs related to interest rate swaps on debt not receiving hedge accounting treatment and interest accretion related to certain securities that were impaired in prior periods. The MIP net mark to market gains increased $88 million in the third quarter of 2008 compared to the same period in 2007 due primarily to interest rate and foreign exchange derivative positions that, while partially effective in hedging interest rate and foreign exchange risk, did not qualify for hedge accounting treatment. Partially offsetting these increases were higher net mark to market losses of $135 million related to credit default swap investments. The MIP invests in credit default swaps comprised predominantly of single-name high-grade corporate exposures. These losses were partially driven by the widening of corporate credit spreads. AIG enters into hedging arrangements to mitigate the effect of changes in currency and interest rates associated with the fixed and floating rate and foreign currency denominated obligations issued under these programs. Some of these hedging relationships qualify for hedge accounting treatment, while others do not. Income or loss from these hedges not qualifying for hedge accounting treatment are classified as net realized capital gains (losses) in AIG's consolidated statement of income (loss). AIG did not issue any additional debt to fund the MIP in the three-month period ended September 30, 2008 and does not intend to issue any additional debt to fund the MIP.

Year-to-Date Spread-Based Investment Business Results

The Spread-Based Investment business reported an operating loss in the nine-month period ended September 30, 2008 compared to operating income in the same period in 2007 due to significantly higher net realized capital losses and lower partnership income. Included in the operating loss were net realized capital losses of $3.1 billion for the nine-month period ended September 30, 2008, compared to $326 million in the same period in 2007. The increase in net realized capital losses for the nine-month period ended September 30, 2008 primarily consist of an increase of $3.7 billion in other-than-temporary impairment charges on fixed maturity securities for both the GIC and MIP and higher net mark to market losses of $244 million on credit default swap investments held by the MIP due to the widening of corporate credit spreads. Partially offsetting these declines were increased net mark to market gains of $530 million on interest rate and foreign exchange hedges not qualifying for hedge accounting treatment for both the GIC and MIP and a $757 million increase in foreign exchange related gains on foreign denominated GIC reserves and MIP liabilities. Included in the net mark-to-market gains is a credit valuation adjustment on swaps in a liability position.

The other-than-temporary impairment charges on fixed maturity securities held in the GIC and MIP portfolios were $2.5 billion for the GIC and $1.4 billion for the MIP for the nine-month period ended September 30, 2008, primarily resulting from severity losses and the change in AIG's intent and ability to hold securities to recovery related to the Securities Lending portfolio. See Invested Assets — Portfolio Review — Other-Than-Temporary Impairments.

In the GIC program, income from partnership investments decreased $984 million for the nine-month period ended September 30, 2008, compared to the same period of 2007 due to significantly higher returns in the 2007 period and weaker market conditions in 2008. Also contributing to the decline was the one-time distribution from a single partnership of $164 million in the nine-month period ended September 30, 2007. Offsetting these declines were foreign exchange gains on foreign-denominated GIC reserves which increased by $694 million in the nine-month period ended September 30, 2008 as a result of the strengthening of the U.S. dollar compared to the 2007 period and an increase in net mark to market gains on derivative positions of $501 million. As noted below, a significant portion of these GIC reserves mature in the next twelve months. The derivative gains included net mark to market gains on interest rate and foreign exchange derivatives used to economically hedge the effect of interest rate and foreign exchange rate movements on GIC reserves. Although these economic hedges are partially effective in hedging the interest rate and foreign exchange risk, AIG has not applied hedge accounting treatment.

The MIP recognized higher operating income in the nine-months ended September 30, 2008 compared to the same period in 2007 due to higher net interest income due to a larger average asset base, the effect of lower funding costs related to interest rate swaps on debt not receiving hedge accounting treatment and interest accretion related to certain securities that were impaired in prior periods.

AIG did not issue any additional debt to fund the MIP in the nine-month period ended September 30, 2008 and does not intend to issue any additional debt to fund the MIP. Through September 30, 2008, the MIP had cumulative debt issuances of $13.4 billion.

The GIC is in runoff with no new GICs issued subsequent to 2005. The anticipated runoff of the domestic GIC portfolio at September 30, 2008 was as follows:

(in billions)	Less Than One Year	1-3 Years	3+-5 Years	Over Five Years	Total
Domestic GICs	$9.9	$3.3	$3.1	$4.3	$20.6

Quarterly Institutional Asset Management Results

Institutional Asset Management recorded higher operating income in the three-month period ended September 30, 2008 compared to the same period in 2007. The increase primarily reflects an increase in operating income of

$174 million related to a credit valuation adjustment on credit default swaps in a liability position. Excluding this effect, Institutional Asset Management recorded an operating loss for the three-month period ended September 30, 2008, compared to operating income in the same period in 2007. This negative variance was driven by impairment losses on proprietary real estate investments of $102 million, a decrease of $36 million in securities lending revenues, a decrease of $22 million in net carried interest revenues and lower trading gains on market-making activities at AIG Private Bank. Also contributing to the decline were net mark-to-market losses on economic interest rate swap hedges associated with warehouse investments, net mark-to-market losses on non-hedge derivatives and higher net foreign exchange losses.

Due to the current real estate market conditions across the globe, several of AIG Global Real Estate's investments were deemed to be impaired for the third quarter of 2008. The impaired investments were written down to their fair value (or fair value less cost to sell for those assets held for sale). AIG recognizes carried interest revenues on an unrealized basis by reflecting the amount owed to AIG as of the balance sheet date based on the related funds' performance. The reduction in carried interest revenues was driven by lower unrealized carry due to weaker fund performance in the three-month period ended September 30, 2008 compared to the same period in 2007. Partially offsetting these amounts were higher net realized capital gains on the sale of proprietary real estate investments of $31 million.

Base management fees decreased in the three-months ended September 30, 2008 as compared to the 2007 period on a lower average asset base. AIG's unaffiliated client assets under management, including retail mutual funds and institutional accounts, were $80.2 billion, $97.6 billion and $96.8 billion at September 30, 2008, December 31, 2007 and September 30, 2007, respectively. The decline from December 31, 2007 reflects lower asset values due to the significant deterioration in the credit and equity markets during 2008 as well as the loss of some third party institutional clients and redemptions in managed funds.

Total operating loss from various consolidated warehoused investments for the three-month periods ended September 30, 2008 and 2007 was $42 million and $33 million, respectively. A portion of these amounts is offset in minority interest expense, which is not a component of operating income (loss).

Year-to-Date Institutional Asset Management Results

Institutional Asset Management recognized an operating loss in the nine-month period ended September 30, 2008 compared to operating income in the same period in 2007 reflecting lower carried interest of $140 million, impairments on real estate investments of $102 million, reduced securities lending revenues of $60 million, and lower income on fund investments of $112 million. Also included in the 2007 nine month results was a $398 million gain related to the sale of a portion of AIG's investment in Blackstone. The reduction in carried interest revenues was driven by lower net unrealized carry due to significantly higher fund performance in the nine-month period ended September 30, 2007. Partially offsetting the reduction was the positive effect on operating income of $174 million related to a credit valuation adjustment on credit default swaps in a liability position.

Average assets under management increased in the nine-month period ended September 30, 2008 compared to the same period in 2007 and resulted in higher base management fees. However, assets under management at September 30, 2008 declined compared to September 30, 2007 reflecting lower asset values due to the significant deterioration in the credit and equity markets during 2008 as well as the loss of some third party institutional clients and redemptions in managed funds.

Total operating losses from various consolidated warehoused investments for the nine-month periods ended September 30, 2008 and 2007 were $119 million and $72 million, respectively. A portion of these amounts is offset in minority interest expense, which is not a component of operating income (loss).

Brokerage Services and Mutual Funds

Revenues and operating income related to Brokerage Services and Mutual Fund activities decreased due to lower fee income as a result of a lower asset base and a decline in commission income resulting from negative market conditions in the three and nine-month periods ended September 30, 2008 compared to the same periods in 2007.

Other Asset Management Results

Revenues and operating income related to the Other Asset Management activities were unchanged in the three-month period ended September 30, 2008 compared to the same period in 2007. Revenues and operating income decreased by $149 million and $147 million, respectively, in the nine-month period ended September 30, 2008 compared to the same period in 2007 due to significantly higher returns on partnership income during 2007 and weaker market conditions in 2008.

Other Operations

The operating loss of AIG's Other category was as follows:

(in millions)	Three Months Ended September 30, 2008	Three Months Ended September 30, 2007	Nine Months Ended September 30, 2008	Nine Months Ended September 30, 2007
Operating income (loss):				
Equity earnings in partially owned companies	**$ (13)**	$ 37	**$ 3**	$ 128
Interest expense on Fed Facility[(a)]	**(802)**	–	**(802)**	–
Other interest expense	**(571)**	(315)	**(1,391)**	(869)
Unallocated corporate expenses[(b)]	**(154)**	(166)	**(529)**	(548)
Net realized capital gains (losses)	**139**	(199)	**(96)**	(226)
Other miscellaneous, net	**(15)**	16	**(84)**	(42)
Total Other	**$(1,416)**	$(627)	**$(2,899)**	$(1,557)

(a) Includes $515 million of amortization of prepaid commitment fee asset.

(b) Includes a charge for settlement of a dispute, expenses of corporate staff not attributable to specific operating segments, expenses related to efforts to improve internal controls, corporate initiatives and certain compensation plan expenses.

The operating loss in the three- and nine-month periods ended September 30, 2008 increased compared to the same periods in 2007 primarily due to higher interest expense that resulted from increased borrowings, including interest on the debt and Equity Units from the dates of issuance in May 2008 and borrowings under the Fed Facility. Unallocated corporate expenses included a charge of $24 million and $125 million for the three- and nine-month periods ended September 30, 2008, respectively, for the settlement of a dispute in connection with the July 2008 purchase of the balance of Ascot Underwriting Holdings, Ltd. The decrease in net realized capital losses in the three- and nine-month periods ended September 30, 2008 reflected lower foreign exchange losses on foreign-denominated debt, a portion of which was economically hedged but did not qualify for hedge accounting treatment under FAS 133. Other miscellaneous, net included a $45 million write-off of goodwill related to Mortgage Guaranty in the nine-month period ended September 30, 2008.

Executive Management

On September 18, 2008, AIG's Board of Directors elected Edward M. Liddy as Chief Executive Officer and a director of AIG and appointed him as Chairman of the Board. Simultaneously, Robert B. Willumstad resigned as Chairman and as a director of AIG, and his employment as Chief Executive Officer was terminated without cause.

On October 16, 2008, David L. Herzog was named Executive Vice President and Chief Financial Officer. Steven J. Bensinger, who had served since May 2008 as Vice Chairman — Financial Services and acting Chief Financial Officer, left AIG.

AIG has recently hired a Vice Chairman and Chief Restructuring Officer to oversee the asset disposition plan to sell assets and businesses to repay the Fed Facility.

On September 22, 2008, a $148 million retention program became effective. The program applies to approximately 130 executives and consists of cash awards payable 60 percent in December 2008 and 40 percent in December 2009.

Subsequent to September 30, 2008, AIG implemented two additional retention programs, totaling approximately $321 million covering 2,101 employees. In addition, several business units have adopted their own retention plans; the cost of these plans is included in consolidated results and is being paid by the respective business units.

Critical Accounting Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America (GAAP) requires the application of accounting policies that often involve a significant degree of judgment. AIG considers that its accounting policies that are most dependent on the application of estimates and assumptions, and therefore viewed as critical accounting estimates, to be those relating to reserves for losses and loss expenses, future policy benefits for life and accident and health contracts, recoverability of DAC, estimated gross profits for investment-oriented products, the allowance for finance receivable losses, flight equipment recoverability, other-than-temporary impairments, estimates with respect to income taxes and fair value measurements of certain financial assets and liabilities, including credit default swaps. These accounting estimates require the use of assumptions about matters, some of which are highly uncertain at the time of estimation. To the extent actual experience differs from the assumptions used, AIG's results of operations would be directly affected.

The major categories for which assumptions are developed and used to establish each critical accounting estimate are highlighted below.

Reserves for Losses and Loss Expenses (General Insurance):

- *Loss trend factors:* used to establish expected loss ratios for subsequent accident years based on premium rate adequacy and the projected loss ratio with respect to prior accident years.
- *Expected loss ratios for the latest accident year:* in this case, accident year 2008 for the year-end 2008 loss reserve analysis. For low-frequency, high-severity classes such as excess casualty, expected loss ratios generally are utilized for at least the three most recent accident years.
- *Loss development factors:* used to project the reported losses for each accident year to an ultimate amount.

- *Reinsurance recoverable on unpaid losses:* the expected recoveries from reinsurers on losses that have not yet been reported and/or settled.

Future Policy Benefits for Life and Accident and Health Contracts (Life Insurance & Retirement Services):

- *Interest rates:* which vary by geographical region, year of issuance and products.
- *Mortality, morbidity and surrender rates:* based upon actual experience by geographical region modified to allow for variation in policy form, risk classification and distribution channel.

Deferred Policy Acquisition Costs (Life Insurance & Retirement Services):

- *Recoverability:* based on current and future expected profitability, which is affected by interest rates, foreign exchange rates, mortality/morbidity experience, expenses, investment returns and policy persistency.

Deferred Policy Acquisition Costs (General Insurance):

- *Recoverability:* based upon the current terms and profitability of the underlying insurance contracts.

Estimated Gross Profits for Investment-Oriented Products (Life Insurance & Retirement Services):

- *Estimated gross profits:* to be realized over the estimated duration of the contracts (investment-oriented products) affect the carrying value of DAC, unearned revenue liability, SIAs and associated amortization patterns. Estimated gross profits include investment income and gains and losses on investments less required interest, actual mortality and other expenses.

Allowance for Finance Receivable Losses (Financial Services):

- *Historical defaults and delinquency experience:* utilizing factors, such as delinquency ratio, allowance ratio, charge-off ratio and charge-off coverage.
- *Portfolio characteristics:* portfolio composition and consideration of the recent changes to underwriting criteria and portfolio seasoning.
- *External factors:* consideration of current economic conditions, including levels of unemployment and personal bankruptcies.
- *Migration analysis:* empirical technique measuring historical movement of similar finance receivables through various levels of repayment, delinquency, and loss categories to existing finance receivable pools.

Flight Equipment Recoverability (Financial Services):

- *Expected undiscounted future net cash flows:* based upon current lease rates, projected future lease rates and estimated terminal values of each aircraft based on expectations of market participants.

Other-Than-Temporary Impairments:

AIG evaluates its investments for impairment such that a security is considered a candidate for other-than-temporary impairment if it meets any of the following criteria:

- Trading at a significant (25 percent or more) discount to par, amortized cost (if lower) or cost for an extended period of time (nine consecutive months or longer);
- The occurrence of a discrete credit event resulting in (i) the issuer defaulting on a material outstanding obligation; (ii) the issuer seeking protection from creditors under the bankruptcy laws or any similar laws intended for court supervised reorganization of insolvent enterprises; or (iii) the issuer proposing a voluntary reorganization pursuant to which creditors are asked to exchange their claims for cash or securities having a fair value substantially lower than par value of their claims; or
- AIG may not realize a full recovery on its investment, regardless of the occurrence of one of the foregoing events.

The determination that a security has incurred an other-than-temporary decline in value requires the judgment of management and consideration of the fundamental condition of the issuer, its near-term prospects and all the relevant facts and circumstances. The above criteria also consider circumstances of a rapid and severe market valuation decline, such as that experienced in current credit markets, in which AIG could not reasonably assert that the impairment period would be temporary (severity losses). For further discussion, see Invested Assets — Portfolio Review — Other-Than-Temporary Impairments.

At each balance sheet date, AIG evaluates its securities holdings with unrealized losses. When AIG does not intend to hold such securities until they have recovered their cost basis, AIG records the unrealized loss in income. If a loss is recognized from a sale subsequent to a balance sheet date pursuant to changes in circumstances, the loss is recognized in the period in which the intent to hold the securities to recovery no longer existed.

In periods subsequent to the recognition of an other-than-temporary impairment charge for fixed maturity securities, which is not credit or foreign exchange related, AIG generally accretes into income the discount or amortizes the reduced premium resulting from the reduction in cost basis over the remaining life of the security.

Valuation Allowance on Deferred Tax Assets:

Recognition of deferred tax assets and the related valuation allowance is influenced by management's assessment of AIG's historic and estimated future profitability profile, including

the character and amount of historic and estimated future taxable income. AIG records a valuation allowance to reduce deferred tax assets to the amount AIG believes is more likely than not to be realized. At each balance sheet date, existing assessments are reviewed and, if necessary, revised to reflect changed circumstances.

Income Taxes on Earnings of Certain Foreign Subsidiaries:

In connection with AIG's asset disposition plan, AIG determined it can no longer assert that earnings of certain foreign subsidiaries will be indefinitely reinvested. Due to the complexity of the U.S. federal income tax laws involved in determining the amount of income taxes incurred on these potential dispositions, as well as AIG's reliance on reasonable assumptions and estimates in calculating this liability, AIG considers the U.S. federal income taxes accrued on the earnings of certain foreign subsidiaries to be a critical accounting estimate.

Fair Value Measurements of Certain Financial Assets and Liabilities:

Overview

AIG measures at fair value on a recurring basis financial instruments in its trading and available for sale securities portfolios, certain mortgage and other loans receivable, certain spot commodities, derivative assets and liabilities, securities purchased (sold) under agreements to resell (repurchase), securities lending invested collateral, non-marketable equity investments, included in other invested assets, certain policyholders' contract deposits, securities and spot commodities sold but not yet purchased, certain trust deposits and deposits due to banks and other depositors, certain long-term borrowings, and certain hybrid financial instruments included in other liabilities. The fair value of a financial instrument is the amount that would be received to sell an asset or paid to transfer a liability in an orderly transaction between willing, able and knowledgeable market participants at the measurement date.

The degree of judgment used in measuring the fair value of financial instruments generally correlates with the level of pricing observability. Financial instruments with quoted prices in active markets generally have more pricing observability and less judgment is used in measuring fair value. Conversely, financial instruments traded in other-than-active markets or that do not have quoted prices have less observability and are measured at fair value using valuation models or other pricing techniques that require more judgment. An active market is one in which transactions for the asset or liability being valued occur with sufficient frequency and volume to provide pricing information on an ongoing basis. An other-than-active market is one in which there are few transactions, the prices are not current, price quotations vary substantially either over time or among market makers, or in which little information is released publicly for the asset or liability being valued. Pricing observability is affected by a number of factors, including the type of financial instrument, whether the financial instrument is new to the market and not yet established, the characteristics specific to the transaction and general market conditions.

AIG management is responsible for the determination of the value of the financial assets and financial liabilities carried at fair value and the supporting methodologies and assumptions. With respect to securities, AIG employs independent third-party valuation service providers to gather, analyze, and interpret market information and derive fair values based upon relevant methodologies and assumptions for individual instruments. When AIG's valuation service providers are unable to obtain sufficient market observable information upon which to estimate the fair value for a particular security, fair value is determined either by requesting brokers who are knowledgeable about these securities to provide a quote, which is generally non-binding, or by employing widely accepted internal valuation models.

Valuation service providers typically obtain data about market transactions and other key valuation model inputs from multiple sources and, through the use of widely accepted internal valuation models, provide a single fair value measurement for individual securities for which a fair value has been requested under the terms of service agreements. The inputs used by the valuation service providers include, but are not limited to, market prices from recently completed transactions and transactions of comparable securities, interest rate yield curves, credit spreads, currency rates, and other market-observable information, as applicable. The valuation models take into account, among other things, market observable information as of the measurement date as well as the specific attributes of the security being valued including its term, interest rate, credit rating, industry sector, and when applicable, collateral quality and other issue or issuer specific information. When market transactions or other market observable data is limited, the extent to which judgment is applied in determining fair value is greatly increased.

AIG employs specific control processes to determine the reasonableness of the fair values of AIG's financial assets and financial liabilities. AIG's processes are designed to ensure that the values received or internally estimated are accurately recorded and that the data inputs and the valuation techniques utilized are appropriate, consistently applied, and that the assumptions are reasonable and consistent with the objective of determining fair value. AIG assesses the reasonableness of individual security values received from valuation service providers through various analytical techniques. In addition, AIG may validate the reasonableness of fair values by comparing information obtained from AIG's valuation service providers to other third party valuation sources for selected securities. AIG also validates prices for selected securities

obtained from brokers through reviews by members of management who have relevant expertise and who are independent of those charged with executing investing transactions.

The following table quantifies the fair value of fixed income and equity securities by source of value determination as of September 30, 2008:

(in billions)	Fair Value	Percent of Total
Fair value based on external sources[(a)]	$481.1	94.4%
Fair value based on internal sources	28.8	5.6
Total fixed income and equity securities[(b)]	$509.9	100.0%

(a) Includes $45.6 billion whose primary source is broker quotes.

(b) Includes available for sale, trading and securities lending invested collateral securities.

For more detailed information about AIG's accounting policy for the measurement of fair value of financial assets and financial liabilities and information about the financial assets and financial liabilities, see Note 3 to the Consolidated Financial Statements.

Incorporation of Credit Risk in Fair Value Measurements

- *AIG's Own Credit Risk.* Fair value measurements for debt, GIAs, and structured note liabilities at AIGFP incorporate AIG's own credit risk by discounting cash flows at rates that incorporate AIG's currently observable credit default swap spreads and takes into consideration collateral posted by AIG with counterparties at the balance sheet date.

  Fair value measurements for freestanding derivatives incorporate AIG's own credit risk by determining the explicit cost for each counterparty to protect against its net credit exposure to AIG at the balance sheet date by reference to observable AIG credit default swap spreads. A counterparty's net credit exposure to AIG is determined based on master netting agreements, which take into consideration all derivative positions with AIG, as well as cash collateral posted by AIG with the counterparty at the balance sheet date.

  Fair value measurements for embedded policy derivatives and policyholders' contract deposits take into consideration that policyholder liabilities are senior in priority to general creditors of AIG and therefore are much less sensitive to changes in AIG credit default swap or cash issuance spreads.

- *Counterparty Credit Risk.* Fair value measurements for freestanding derivatives incorporate the counterparty credit by determining the explicit cost for AIG to protect against its net credit exposure to each counterparty at the balance sheet date by reference to observable counterparty credit default swap spreads. AIG's net credit exposure to a counterparty is determined based on master netting agreements, which take into consideration all derivative positions with the counterparty, as well as cash collateral posted by the counterparty at the balance sheet date.

  Fair values for fixed maturity securities based on observable market prices for identical or similar instruments implicitly include the incorporation of counterparty credit risk. Fair values for fixed maturity securities based on internal models incorporate counterparty credit risk by using discount rates that take into consideration cash issuance spreads for similar instruments or other observable information.

Fixed Maturity Securities — Trading and Available for Sale

AIG maximizes the use of observable inputs and minimizes the use of unobservable inputs when measuring fair value. Whenever available, AIG obtains quoted prices in active markets for identical assets at the balance sheet date to measure at fair value fixed maturity securities in its trading and available for sale portfolios. Market price data generally is obtained from exchange or dealer markets.

AIG estimates the fair value of fixed maturity securities not traded in active markets, including securities purchased (sold) under agreements to resell (repurchase) and mortgage and other loans receivable, for which AIG elected the fair value option by referring to traded securities with similar attributes, using dealer quotations and matrix pricing methodologies, discounted cash flow analyses, or internal valuation models. This methodology considers such factors as the issuer's industry, the security's rating and tenor, its coupon rate, its position in the capital structure of the issuer, yield curves, credit curves, prepayment rates and other relevant factors. For fixed maturity securities that are not traded in active markets or that are subject to transfer restrictions, valuations are adjusted to reflect illiquidity and/or non-transferability, and such adjustments generally are based on available market evidence. In the absence of such evidence, management's best estimate is used.

Equity Securities Traded in Active Markets — Trading and Available for Sale

AIG maximizes the use of observable inputs and minimizes the use of unobservable inputs when measuring fair value. Whenever available, AIG obtains quoted prices in active markets for identical assets at the balance sheet date to measure at fair value marketable equity securities in its trading and available for sale portfolios. Market price data generally is obtained from exchange or dealer markets.

Non-Traded Equity Investments — Other Invested Assets

AIG initially estimates the fair value of equity securities not traded in active markets by reference to the transaction price. This valuation is adjusted only when changes to inputs and assumptions are corroborated by evidence such as transactions in similar instruments, completed or pending third-party transactions in the underlying investment or comparable entities, subsequent rounds of financing, recapitalizations and

other transactions across the capital structure, offerings in the equity capital markets, and changes in financial ratios or cash flows. For equity securities that are not traded in active markets or that are subject to transfer restrictions, valuations are adjusted to reflect illiquidity and/or non-transferability and such adjustments generally are based on available market evidence. In the absence of such evidence, management's best estimate is used.

Private Limited Partnership and Hedge Fund Investments — Other Invested Assets

AIG initially estimates the fair value of investments in certain private limited partnerships and certain hedge funds by reference to the transaction price. Subsequently, AIG obtains the fair value of these investments generally from net asset value information provided by the general partner or manager of the investments, the financial statements of which generally are audited annually.

Separate and Variable Account Assets

Separate and variable account assets are composed primarily of registered and unregistered open-end mutual funds that generally trade daily and are measured at fair value in the manner discussed above for equity securities traded in active markets.

Freestanding Derivatives

Derivative assets and liabilities can be exchange-traded or traded over the counter (OTC). AIG generally values exchange-traded derivatives within portfolios using models that calibrate to market clearing levels and eliminate timing differences between the closing price of the exchange-traded derivatives and their underlying instruments.

OTC derivatives are valued using market transactions and other market evidence whenever possible, including market-based inputs to models, model calibration to market clearing transactions, broker or dealer quotations or alternative pricing sources with reasonable levels of price transparency. When models are used, the selection of a particular model to value an OTC derivative depends on the contractual terms of, and specific risks inherent in, the instrument as well as the availability of pricing information in the market. AIG generally uses similar models to value similar instruments. Valuation models require a variety of inputs, including contractual terms, market prices and rates, yield curves, credit curves, measures of volatility, prepayment rates and correlations of such inputs. For OTC derivatives that trade in liquid markets, such as generic forwards, swaps and options, model inputs can generally be corroborated by observable market data by correlation or other means and model selection does not involve significant management judgment.

Certain OTC derivatives trade in less liquid markets with limited pricing information and the determination of fair value for these derivatives is inherently more difficult. When AIG does not have corroborating market evidence to support significant model inputs and cannot verify the model to market transactions, the transaction price is initially used as the best estimate of fair value. Accordingly, when a pricing model is used to value such an instrument, the model is adjusted so the model value at inception equals the transaction price. Subsequent to initial recognition, AIG updates valuation inputs when corroborated by evidence such as similar market transactions, third-party pricing services and/or broker or dealer quotations, or other empirical market data. When appropriate, valuations are adjusted for various factors such as liquidity, bid/offer spreads and credit considerations. Such adjustments are generally based on available market evidence. In the absence of such evidence, management's best estimate is used.

With the adoption of FAS 157 on January 1, 2008, AIG's own credit risk has been considered and is incorporated into the fair value measurement of freestanding derivative liabilities.

Embedded Policy Derivatives

The fair value of embedded policy derivatives contained in certain variable annuity and equity-indexed annuity and life contracts is measured based on actuarial and capital market assumptions related to projected cash flows over the expected lives of the contracts. These cash flow estimates primarily include benefits and related fees assessed, when applicable, and incorporate expectations about policyholder behavior. Estimates of future policyholder behavior are subjective and based primarily on AIG's historical experience. With respect to embedded policy derivatives in AIG's variable annuity contracts, because of the dynamic and complex nature of the expected cash flows, risk neutral valuations are used. Estimating the underlying cash flows for these products involves many estimates and judgments, including those regarding expected market rates of return, market volatility, correlations of market index returns to funds, fund performance, discount rates and policyholder behavior. With respect to embedded policy derivatives in AIG's equity-indexed annuity and life contracts, option pricing models are used to estimate fair value, taking into account assumptions for future equity indexed growth rates, volatility of the equity index, future interest rates, and determination on adjusting the participation rate and the cap on equity indexed credited rates in light of market conditions and policyholder behavior assumptions. With the adoption of FAS 157, these methodologies were not changed, with the exception of incorporating an explicit risk margin to take into consideration market participant estimates of projected cash flows and policyholder behavior.

AIGFP's Super Senior Credit Default Swap Portfolio

See Valuation of Level 3 Assets and Liabilities below for a comprehensive discussion of AIGFP's super senior credit default swap portfolio.

Policyholders' Contract Deposits

Policyholders' contract deposits accounted for at fair value beginning January 1, 2008 are measured using an income approach by taking into consideration the following factors:

- Current policyholder account values and related surrender charges,
- The present value of estimated future cash inflows (policy fees) and outflows (benefits and maintenance expenses) associated with the product using risk neutral valuations, incorporating expectations about policyholder behavior, market returns and other factors, and
- A risk margin that market participants would require for a market return and the uncertainty inherent in the model inputs.

The change in fair value of these policyholders' contract deposits is recorded as incurred policy losses and benefits in the consolidated statement of income (loss).

Level 3 Assets and Liabilities

Under FAS 157, assets and liabilities recorded at fair value in the consolidated balance sheet are classified in a hierarchy for disclosure purposes consisting of three "levels" based on the observability of inputs available in the marketplace used to measure the fair value. See Note 3 to the Consolidated Financial Statements for additional information about fair value measurements.

At September 30, 2008, AIG classified $55.3 billion and $40.0 billion of assets and liabilities, respectively, measured at fair value on a recurring basis as Level 3. This represented 5.4 percent and 4.2 percent of the total assets and liabilities, respectively, measured at fair value on a recurring basis. Level 3 fair value measurements are based on valuation techniques that use at least one significant input that is unobservable. These measurements are made under circumstances in which there is little, if any, market activity for the asset or liability. AIG's assessment of the significance of a particular input to the fair value measurement in its entirety requires judgment.

In making the assessment, AIG considers factors specific to the asset or liability. In certain cases, the inputs used to measure fair value of an asset or a liability may fall into different levels of the fair value hierarchy. In such cases, the level in the fair value hierarchy within which the fair value measurement in its entirety is classified is determined based on the lowest level input that is significant to the fair value measurement in its entirety.

Valuation of Level 3 Assets and Liabilities

AIG values its assets and liabilities classified as Level 3 using judgment and valuation models or other pricing techniques that require a variety of inputs including contractual terms, market prices and rates, yield curves, credit curves, measures of volatility, prepayment rates and correlations of such inputs, some of which may be unobservable. The following paragraphs describe the methods AIG uses to measure on a recurring basis the fair value of the major classes of assets and liabilities classified in Level 3.

Private equity and real estate fund investments: These assets initially are valued at the transaction price, i.e., the price paid to acquire the asset. Subsequently, they are measured based on net asset value using information provided by the general partner or manager of these investments, the accounts of which generally are audited on an annual basis.

Corporate bonds and private placement debt: These assets initially are valued at the transaction price. Subsequently, they are valued using market data for similar instruments (e.g., recent transactions, bond spreads or credit default swap spreads), comparisons to benchmark derivative indices or movements in underlying credit spreads. When observable price quotations are not available, fair value is determined based on cash flow models with yield curves, bond or single-name credit default swap spreads and estimated recovery rates.

Certain Residential Mortgage-Backed Securities (RMBS): These assets initially are valued at the transaction price. Subsequently, they may be valued by comparison to transactions in instruments with similar collateral and risk profiles, remittances received and updated cumulative loss data on underlying obligations, discounted cash flow techniques, and/or option adjusted spread analyses.

Certain Asset-Backed Securities — non-mortgage: These assets initially are valued at the transaction price. Subsequently, they may be valued based on external price/spread data. When position-specific external price data are not observable, the valuation is based on prices of comparable securities.

CDOs: These assets initially are valued at the transaction price. Subsequently, they are valued based on external price/spread data from independent third parties, dealer quotations, matrix pricing, the BET model or a combination thereof.

AIGFP's Super Senior Credit Default Swap Portfolio: AIGFP wrote credit protection on the super senior risk layer of diversified portfolios of corporate debt, prime residential mortgages, collaterized loan obligations (CLOs) and multi-sector CDOs. In these transactions, AIGFP is at risk of credit performance on the super senior risk layer related to a diversified portfolio referenced to loans or debt securities. Further, these transactions have placed a significant demand on AIGFP's liquidity during 2008, primarily as a result of their

collateral posting provisions. See General Contractual Terms below. To a lesser extent, AIGFP also wrote protection on tranches below the super senior risk layer, primarily in respect of regulatory capital transactions.

At September 30, 2008, the net notional amount, fair value and unrealized market valuation loss of the AIGFP super senior credit default swap portfolio, including certain regulatory capital relief transactions, by asset class were as follows:

	Net Notional Amount			Fair Value Of Derivative Liability at September 30, 2008[b]	Unrealized Market Valuation Loss (Gain)	
(in millions)	June 30, 2008[a]	**Decrease**	**September 30, 2008[a]**		**Three Months Ended September 30, 2008[c]**	**Nine Months Ended September 30, 2008[c]**
Regulatory Capital:						
Corporate loans	$172,717	**$(40,928)**	**$131,789**	**$ –**	**$ –**	**$ –**
Prime residential mortgages	132,612	**(16,054)**	**116,558**	**–**	**–**	**–**
Other[d]	1,619	**(19)**	**1,600**	**397**	**272**	**397**
Total	306,948	**(57,001)[f]**	**249,947**	**397**	**272**	**397**
Arbitrage:						
Multi-sector CDOs, including 2a-7 Puts	80,301	**(8,657)[g]**	**71,644**	**30,207**	**6,262**	**19,868**
Corporate debt/CLOs	53,767	**(3,089)[h]**	**50,678**	**1,534**	**538**	**1,308**
Total	134,068	**(11,746)**	**122,322**	**31,741**	**6,800**	**21,176**
Mezzanine tranches[e]	5,824	**(811)**	**5,013**	**153**	**(18)**	**153**
Total	$446,840	**$(69,558)**	**$377,282**	**$32,291**	**$7,054**	**$21,726**

(a) Notional amounts presented are net of all structural subordination below the covered tranches.

(b) Fair value amounts are shown before the effects of counterparty netting adjustments and offsetting cash collateral in accordance with FIN 39.

(c) Includes credit valuation adjustment gains of $98 million and $207 million, respectively, for the three- and nine-month periods ended September 30, 2008.

(d) Represents transactions where AIGFP believes the counterparties are no longer using the transactions to obtain regulatory capital relief. During the second quarter of 2008, a European RMBS regulatory capital relief transaction with a net notional amount of $1.6 billion was not terminated as expected when it no longer provided regulatory capital relief to the counterparty.

(e) Represents credit default swaps written by AIGFP on tranches below super senior on certain regulatory capital relief trades.

(f) The decline includes terminations of $29.5 billion and the effect of foreign exchange rates of $26.4 billion resulting from the strengthening of the U.S. dollar, primarily against the Euro and the British Pound.

(g) The decline includes purchases of $5.7 billion of super senior CDO securities in connection with 2a-7 Puts and amortization of $2.5 billion.

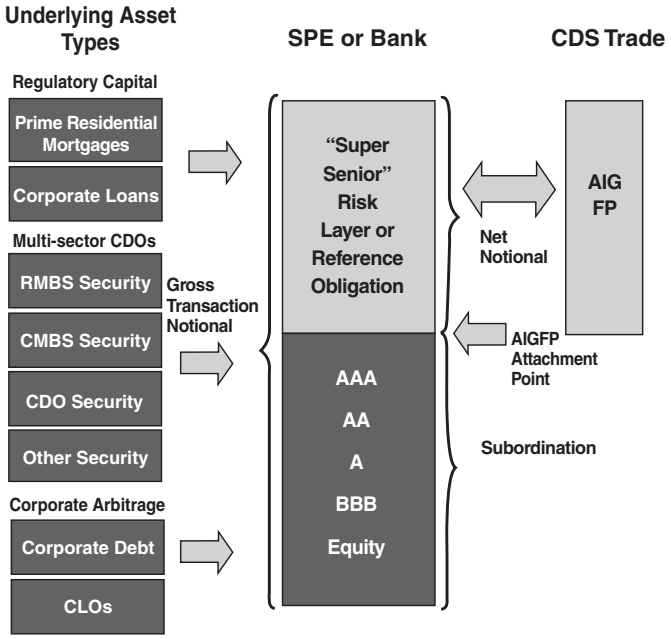
(h) Includes the effect of foreign exchange rates of $2.0 billion resulting from the strengthening of the U.S. dollar, primarily against the Euro.

General Contractual Terms

AIGFP entered into credit default swap and other credit derivative transactions (collectively, CDS) in the ordinary course of its business. In the majority of AIGFP's credit derivatives transactions, AIGFP sold credit protection on a designated portfolio of loans or debt securities. Generally, AIGFP provides such credit protection on a "second loss" basis, meaning that AIGFP will incur credit losses only after a shortfall of principal and/or interest, or other credit events, in respect of the protected loans and debt securities, exceed a specified threshold amount or level of "first loss."

Typically, the credit risk associated with a designated portfolio of loans or securities has been tranched into different layers of risk, which are then analyzed and rated by the credit rating agencies. At origination, there is usually an equity layer covering the first credit losses in respect of the portfolio up to a specified percentage of the total portfolio, and then successive layers ranging from generally a BBB-rated layer to one or more AAA-rated layers. A significant majority of transactions that are rated by rating agencies have risk layers or tranches that were rated AAA at origination and are immediately junior to the threshold level above which AIGFP's payment obligation would generally arise. In transactions that were not rated, AIGFP applied equivalent risk criteria for setting the threshold level for its payment obligations. Therefore, the risk layer assumed by AIGFP with respect to the designated portfolio of loans or securities in these transactions is often called the "super senior" risk layer, defined as a layer of credit risk senior to one or more risk layers that have been rated AAA by the credit rating agencies, or if the transaction is not rated, structured to the equivalent thereto.

The following graphic represents a typical structure of a transaction including the super senior risk layer:



Regulatory Capital Portfolio

Approximately $250 billion (consisting of corporate loans and prime residential mortgages) of the $377 billion in net notional exposure of AIGFP's super senior credit default swap portfolio as of September 30, 2008 represented derivatives written for financial institutions, principally in Europe, for the purpose of providing regulatory capital relief rather than risk mitigation. In exchange for a periodic fee, the counterparties receive credit protection with respect to diversified loan portfolios they own, thus improving their regulatory capital position. These transactions generally provide for cash settlement (see Triggers and Settlement Alternatives below); however, AIGFP does not expect to be required to make payments under these contracts during their estimated life as these transactions are generally expected to terminate at no additional cost to AIGFP when the transactions no longer provide such regulatory capital benefit. See Regulatory Models and Modeling — Regulatory Capital Portfolio.

Arbitrage Portfolio

Approximately $122 billion of the $377 billion in net notional exposure on AIGFP's super senior credit default swaps as of September 30, 2008 are arbitrage-motivated transactions written on multi-sector CDOs or designated pools of investment grade corporate debt or CLOs. While certain credit default swaps written on corporate debt and multi-sector CDOs provide for cash settlement, the large majority of the AIGFP credit default swaps written on multi-sector CDOs and CLOs require physical settlement (see Triggers and Settlement Alternatives below).

The most significant portfolio, in terms of unrealized market valuation losses, is the super senior multi-sector CDO credit default swap portfolio.

At September 30, 2008, the gross transaction notional amount of the multi-sector CDOs on which AIGFP wrote protection on the super senior tranche, subordination below the super senior risk layer and AIGFP net notional exposure were as follows:

(in millions)	Gross Transaction Notional Amount[(a)]	Subordination Below Super Senior Risk Layer	Net Notional Amount[(b)]	Fair Value of Derivative Liability at September 30, 2008
High grade with sub-prime collateral	$ 50,582	$ 9,751	$40,831	$18,201
High grade with no sub-prime collateral	30,284	14,581	15,703	4,195
Total high grade[(c)]	80,866	24,332	56,534	22,396
Mezzanine with sub-prime	25,888	11,575	14,313	7,487
Mezzanine with no sub-prime	1,698	901	797	324
Total mezzanine[(d)]	27,586	12,476	15,110	7,811
Total	$108,452	$36,808	$71,644	$30,207

(a) Total outstanding principal amount of securities held by a CDO.

(b) Notional size on which AIGFP wrote credit protection.

(c) "High grade" refers to transactions in which the underlying collateral credit ratings on a stand-alone basis were predominantly AA or higher at origination.

(d) "Mezzanine" refers to transactions in which the underlying collateral credit ratings on a stand-alone basis were predominantly A or lower at origination.

At September 30, 2008, the gross notional amount, percentage of the total CDO collateral pools, and ratings and vintage breakdown of collateral securities in the multi-sector CDOs, by ABS category, were as follows:

(dollars in millions)

ABS Category	Gross Transaction Notional Amount	Percent of Total	RATINGS BREAKDOWN							VINTAGE				
			AAA	AA	A	BBB	BB	<BB	NR	2008	2007	2006	2005	2004+P
RMBS PRIME	$ 12,280	11.33%	8.13%	0.97%	0.88%	0.68%	0.17%	0.49%	0.01%	0.08%	2.39%	2.37%	3.36%	3.13%
RMBS ALT-A	17,086	15.75%	6.99%	2.48%	1.87%	1.34%	0.78%	2.29%	0.00%	0.16%	1.40%	3.41%	7.92%	2.86%
RMBS SUBPRIME	40,262	37.12%	2.07%	8.11%	5.56%	5.05%	3.44%	12.89%	0.00%	0.01%	2.48%	2.61%	20.55%	11.47%
CMBS	23,271	21.46%	15.88%	0.99%	1.25%	2.38%	0.51%	0.12%	0.33%	0.08%	5.73%	3.55%	2.77%	9.33%
CDO	10,196	9.40%	1.27%	1.61%	1.37%	1.04%	0.66%	3.41%	0.04%	0.00%	0.32%	1.12%	3.20%	4.76%
OTHER	5,357	4.94%	1.18%	1.06%	1.38%	1.23%	0.02%	0.06%	0.01%	0.12%	0.24%	0.86%	1.46%	2.26%
Total	$108,452	100.00%	35.52%	15.22%	12.31%	11.72%	5.58%	19.26%	0.39%	0.45%	12.56%	13.92%	39.26%	33.81%

Triggers and Settlement Alternatives

CDS transactions entered into by counterparties for regulatory capital purposes, together with a number of arbitrage transactions (comprising approximately $47 billion or 38.6 percent of the net notional amount for the arbitrage portfolio at September 30, 2008), have cash-settled structures (see Cash Settlement below) in respect of a basket of reference obligations, where AIGFP's payment obligations may be triggered by payment shortfalls, bankruptcy and certain other events such as write-downs of the value of underlying assets as further described below. By contrast, under the large majority of CDS transactions in respect of multi-sector CDOs (comprising approximately $57 billion or 46.5 percent of the net notional amount for the arbitrage portfolio at September 30, 2008) AIGFP's payment obligations are triggered by the occurrence of a non-payment event under a single reference CDO security, and performance is limited to a single payment by AIGFP in return for physical delivery by the counterparty of the reference security. See Physical Settlement below. A number of CDS transactions in respect of CLOs have similar settlement mechanisms. In addition, the arbitrage portfolio includes transactions with a net notional amount of $4.9 billion that allow holders to put securities to AIGFP at par in the event of a failed remarketing of the referenced security. AIGFP cannot currently determine if and when it may be required to perform its obligations in the future including the timing of any future triggering events or the amount of any additional purchases, individually or in the aggregate, that might be required.

Physical Settlement. For CDS transactions requiring physical settlement, AIGFP is required to pay unpaid principal and accrued interest for the relevant reference obligation in return for physical delivery of such reference obligation by the CDS buyer upon the occurrence of a credit event. After purchasing the reference obligation, AIGFP may sell the security and recover all or a portion of the purchase price paid under the CDS, or hold such security and be entitled to receive subsequent collections of principal and interest. There can be no assurance that the satisfaction of these obligations by AIGFP will not have a material effect on AIG's liquidity. AIGFP generally is required to settle such a transaction only if the following conditions are satisfied:

- A "Credit Event" (as defined in the relevant CDS transaction confirmation) must have occurred. In all CDS transactions subject to physical settlement, "Failure to Pay" is specified as a Credit Event and is generally triggered if there is a failure by the issuer under the related CDO to make a payment under the reference obligation (after the expiration of any applicable grace period and, in certain transactions, subject to a nominal non-payment threshold having been met).

  In addition, certain of the AIGFP CDSs, with an aggregate net notional amount totaling $7.7 billion, provide credit protection in respect of CDOs that require minimum amounts of collateral to be maintained to support the CDO debt, where the value of such collateral is affected by among other things the ratings of the securities and other obligations comprising such collateral. In the event that the issuer of such a CDO fails to maintain the minimum levels of collateral, an event of default would occur, triggering a right by a specified controlling class of CDO note holders to accelerate the payment of principal and interest on the protected reference obligations. Under certain of the CDSs, upon acceleration of the reference obligations underlying a CDS, AIGFP may be required to purchase such reference obligations for a purchase price equal to unpaid principal and accrued interest of the CDO in settlement of the CDS. As a result of this over-collaterization feature of these CDOs, AIGFP potentially may be required to purchase such CDO securities in settlement of the related CDS sooner than it would be required to if such CDOs did not have an over-collaterization feature. As of November 5, 2008, eight CDOs for which AIGFP had written credit protection on the super senior layer had experienced over-collaterization related events of default. One of these CDOs was accelerated in the second quarter of 2008, and AIGFP extinguished a portion of its CDS obligations by purchasing the protected CDO security for $103 million, which equaled the principal amount

outstanding related to this CDS. AIGFP extinguished the remainder of its CDS obligations related to this CDO on November 6, 2008 by purchasing the protected CDO security for $59 million, which equaled the remaining principal amount of this CDO security subject to CDS protection. AIGFP's remaining CDS net notional exposure with respect to CDOs that have experienced over-collateralization events of default was $2.4 billion at November 5, 2008. While AIGFP believes that these defaulted transactions are most likely to result in a payment by AIGFP, AIG cannot estimate the timing of any required payments since the timing of a Credit Event may be outside of AIGFP's control.

In addition, certain of AIGFP's CDSs provide credit protection in respect of CDOs that provide if the CDO issuer fails to pay amounts due on classes of CDO securities that rank *pari passu* with or subordinate to such referenced obligations, an event of default would occur, triggering a right by a specified controlling class of CDO noteholders to accelerate the payment of principal and interest on the protected reference obligations. As in the case of CDOs with the over-collateralization feature, the existence of such an acceleration feature potentially may result in AIGFP being required to purchase the super senior reference obligation in settlement of the related CDS sooner than would be required if such CDO did not have such acceleration feature.

- The CDS buyer must deliver the reference obligation within a specified period, generally within 30 days. There is no payment obligation if delivery is not made within this period.
- Upon completion of the physical delivery and payment by AIGFP, AIGFP would be the holder of the relevant reference obligation and have all rights associated with a holder of such securities.

Cash Settlement. Transactions requiring cash settlement (also known as "pay as you go") are in respect of protected baskets of reference credits (which may also include single name CDSs in addition to securities and loans) rather than a single reference obligation as in the case of the physically-settled transactions described above. Under these credit default swaps:

- Each time a "triggering event" occurs a "loss amount" is calculated. A triggering event is generally a failure by the relevant obligor to pay principal of or, in some cases, interest on one of the reference credits in the underlying protected basket. Triggering events may also include bankruptcy of reference credits, write-downs or postponements with respect to interest or to the principal amount of a reference credit payable at maturity. The determination of the loss amount is specific to each triggering event. It can represent the amount of a shortfall in ordinary course interest payments on the reference credit, a write-down in the interest on or principal of such reference credit or any amount postponed in respect thereof. It can also represent the difference between the notional or par amount of such reference credit and its market value, as determined by reference to market quotations.
- Triggering events can occur multiple times, either as a result of continuing shortfalls in interest or write-downs or postponements on a single reference credit, or as a result of triggering events in respect of different reference credits included in a protected basket. In connection with each triggering event, AIGFP is required to make a cash payment to the buyer of protection under the related CDS only if the aggregate loss amounts calculated in respect of such triggering event and all prior triggering events exceed a specified threshold amount (reflecting AIGFP's attachment point). In addition, AIGFP is typically entitled to receive amounts recovered, or deemed recovered, in respect of loss amounts resulting from triggering events caused by interest shortfalls, postponements or write-downs on reference credits.
- To the extent that there are reimbursements received (actual or deemed) by the CDS buyer in respect of prior triggering events, AIGFP will be entitled to receive equivalent amounts from the counterparty to the extent AIGFP has previously made a related payment.

2a-7 Puts. Included in the multi-sector CDO portfolio are maturity-shortening puts with a net notional amount of $4.9 billion as of September 30, 2008 that allow the holders of the securities issued by certain CDOs to treat the securities as short-term eligible 2a-7 investments under the Investment Company Act of 1940 (2a-7 Puts). The general terms of these transactions differ from those referenced above. Holders of securities are required, in certain circumstances, to tender their securities to the issuers at par. If an issuer's remarketing agent is unable to resell the securities so tendered, AIGFP must purchase the securities at par as long as the security has not experienced a payment default or certain bankruptcy events with respect to the issuer of such security have not occurred. During the nine-month period ended September 30, 2008, AIGFP repurchased securities with a principal amount of approximately $6.6 billion in connection with these obligations, of which $5.4 billion were funded using existing liquidity facilities. AIGFP repurchased securities with a principal amount of approximately $1.4 billion from September 30, 2008 to October 27, 2008, which were funded using existing liquidity facilities. AIGFP expects to repurchase within the next two years the majority of securities under the remaining 2a-7 Puts having a net notional exposure of $3.5 billion at October 27, 2008. In certain transactions, AIGFP has contracted with third parties to provide liquidity for the purchase of such securities if they are put to AIGFP for up to a three-year period. Such unused liquidity facilities

totaled $1.7 billion at October 27, 2008. AIG expects to use these facilities to fund future purchases of these securities.

Termination Events. A majority of the super senior credit default swaps written on multi-sector CDOs provide the counterparties with an additional termination right once AIG's rating level falls to BBB or Baa. At that level, counterparties have the right to terminate the transactions early. This aggregate net notional amount of such super senior credit default swaps written on multi-sector CDOs is approximately $47.8 billion as of October 27, 2008. If counterparties exercise this right, the contracts provide for the counterparties to be compensated for the cost to replace the trades, or an amount reasonably determined in good faith to estimate the losses the counterparties would incur as a result of the termination of the trades.

Many of the super senior credit default swaps written for regulatory capital relief, having a net notional amount of $130 billion, include triggers that require certain actions to be taken by AIG upon such a downgrade, which, if not taken, will give rise to a right of the counterparties to terminate the swaps. Such actions include posting collateral, transferring the swap or providing a guarantee from a more highly rated entity. Through October 27, 2008, AIGFP has elected to post collateral in such cases, and, as a result, the counterparty has not had the right to terminate the swaps.

Given the level of uncertainty in estimating both the number of counterparties who may elect to exercise their right to terminate and the payment that may be triggered in connection with any such exercise, AIG is unable to reasonably estimate the aggregate amount that it would be required to pay under the super senior credit default swaps in the event of any such downgrade.

Collateral

Most of AIGFP's credit default swaps are subject to collateral posting provisions. These provisions differ among counterparties and asset classes. Although AIGFP has collateral posting obligations associated with both regulatory capital relief transactions and arbitrage transactions, the large majority of these obligations are associated with arbitrage transactions in respect of multi-sector CDOs.

The collateral arrangements in respect of the multi-sector CDO, regulatory capital and corporate arbitrage transactions are nearly all documented under a Credit Support Annex (CSA) to an International Swaps and Derivatives Association, Inc (ISDA) Master Agreement (Master Agreement). The Master Agreement and CSA forms are standardized form agreements published by the ISDA, which market participants have adopted as the primary contractual framework for various kinds of derivatives transactions, including CDS. The Master Agreement and CSA forms are designed to be customized by counterparties to accommodate their particular requirements for the anticipated types of swap transactions to be entered into. Elective provisions and modifications of the standard terms are negotiated in connection with the execution of these documents. The Master Agreement and CSA permit any provision contained in these documents to be further varied or overridden by the individual transaction confirmations, providing flexibility to tailor provisions to accommodate the requirements of any particular transaction. A CSA, if agreed by the parties to a Master Agreement, supplements and forms part of the Master Agreement and contains provisions (among others) for the valuation of the covered transactions, the delivery and release of collateral, the types of acceptable collateral, the grant of a security interest (in the case of a CSA governed by New York law) or the outright transfer of title (in the case in a CSA governed by English law) in the collateral that is posted, the calculation of the amount of collateral required, the valuation of the collateral provided, the timing of any collateral demand or return, dispute mechanisms, and various other rights, remedies and duties of the parties with respect to the collateral provided.

In general, each party has the right under a CSA to act as the "Valuation Agent" and initiate the calculation of the exposure of one party to the other (Exposure) in respect of transactions covered by the CSA. The valuation calculation may be performed daily, weekly or at some other interval, and the frequency is one of the terms negotiated at the time the CSA is signed. The definition of Exposure under a standard CSA is the amount that would be payable to one party by the other party upon a hypothetical termination of that transaction. This amount is determined, in most cases, by the Valuation Agent using its estimate of mid-market quotations (i.e., the average of hypothetical bid and ask quotations) of the amounts that would be paid for a replacement transaction. AIGFP determines Exposure typically by reference to the mark-to-market valuation of the relevant transaction produced by its systems and specialized models. Exposure amounts are typically determined for all transactions under a Master Agreement (unless the parties have specifically agreed to exclude certain transactions, not to apply the CSA or to set a specific transaction Exposure to zero). The aggregate Exposure less the value of collateral already held by the relevant party (and following application of certain thresholds) results in a net exposure amount (Delivery Amount). If this amount is a positive number, then the other party must deliver collateral with a value equal to the Delivery Amount. Under the standard CSA, the party not acting as Valuation Agent for any particular Exposure calculation may dispute the Valuation Agent's calculation of the Delivery Amount. If the parties are unable to resolve this dispute, the terms of the standard CSA provide that the Valuation Agent is required to recalculate Exposure using, in substitution for the disputed Exposure amounts, the average of actual quotations at mid-market from four leading dealers in the relevant market.

Regulatory Capital Transactions

As of September 30, 2008, approximately 27 percent of AIGFP's regulatory capital transactions (measured by net notional amount) were subject to a CSA. In other transactions, which represent approximately 39 percent of the total net notional amount of the outstanding regulatory capital transactions, AIGFP is obligated to put a CSA or alternative collateral arrangement in place if AIG's ratings fall below certain levels (typically, AA-/Aa3). In light of the rating actions taken in respect of AIG on September 15, 2008, AIGFP has implemented a CSA or alternative collateral arrangement in a large majority of these transactions. In some cases, AIGFP may not reach agreement with a counterparty on the terms of a collateral arrangement, and as a result, the counterparty may be entitled to terminate the transaction. In general, each regulatory capital transaction is subject to a stand-alone Master Agreement or similar agreement, which means that aggregate Exposure for the given Master Agreement or similar agreement is calculated only with reference to a single transaction.

There are diverse mechanisms for calculating Exposure in these transactions. A small minority relies on the standard CSA approach described above under "Collateral"; the large majority uses a formula to calculate Exposure. In most cases, the formula is unique to that transaction or counterparty. These unique formulas typically depend on either credit ratings (including the ratings of AIG and, in some cases, the ratings of notes that have been issued with respect to different tranches of the transaction), rating agency expected loss models, or changes in spreads on identified credit indices (but do not depend on the value of any underlying reference obligations).

Arbitrage Portfolio — Multi-Sector CDOs

In the large majority of the CDS transactions in respect of multi-sector CDOs, the standard CSA provisions for the calculation of Exposure have been modified, with the Exposure amount determined pursuant to an agreed formula that is based on the difference between the net notional amount of such transaction and the market value of the relevant underlying CDO security, rather than the replacement value of the transaction. In cases where a formula is utilized, a transaction-specific threshold is generally factored into the calculation of Exposure, which reduces the amount of collateral required to be posted. These thresholds typically vary based on the credit ratings of AIG and/or the reference obligations, with greater posting obligations arising in the context of lower ratings. For the large majority of counterparties to these transactions, the Master Agreement and CSA cover non-CDS transactions (e.g., interest rate and cross currency swap transactions) as well as CDS transactions.

Arbitrage Portfolio — Corporate Debt/CLOs

Almost all of AIGFP's corporate arbitrage transactions are subject to CSAs. Approximately 47 percent (measured by net notional amount) of these transactions contain no special collateral posting provisions, but are subject to a Master Agreement that includes a CSA. These transactions are treated the same as other trades subject to the same Master Agreement and CSA, with the calculation of collateral in accordance with the standard CSA procedures outlined above. Approximately 53 percent (measured by net notional amount) of these transactions, although subject to a Master Agreement and CSA, have specific valuation and threshold provisions. These thresholds are typically based on a combination of the credit rating of AIG and a Moody's model rating of the transaction (and not based on the value of any underlying reference obligations). Thus, as long as AIG maintains a rating above a specified threshold and the Moody's model of the underlying transaction exceeds a specified rating, the collateral provisions do not apply.

Collateral Calls

AIGFP has received collateral calls from counterparties in respect of certain super senior credit default swaps, of which a large majority relate to multi-sector CDOs. To a significantly lesser extent, AIGFP has also received collateral calls in respect of certain super senior credit default swaps entered into by counterparties for regulatory capital relief purposes and in respect of corporate debt/CLOs. Frequently, valuation estimates made by counterparties with respect to certain super senior credit default swaps or the underlying reference CDO securities, for purposes of determining the amount of collateral required to be posted by AIGFP in connection with such instruments, have differed, at times significantly, from AIGFP's estimates. In almost all cases, AIGFP has been able to successfully resolve the differences or otherwise reach an accommodation with respect to collateral posting levels, including in certain cases by entering into compromise collateral arrangements. Due to the ongoing nature of these collateral calls, AIGFP may engage in discussions with one or more counterparties in respect of these differences at any time. As of September 30, 2008, AIGFP had either agreed to post or posted collateral based on exposures, calculated in respect of super senior credit default swaps, in an aggregate net amount of $32.8 billion. Valuation estimates made by counterparties for collateral purposes were, like any other third-party valuation, considered in the determination of the fair value estimates of AIGFP's super senior credit default swap portfolio.

Through June 30, 2007, AIGFP had not received any collateral calls related to this credit default swap portfolio. Since that date and through October 27, 2008, counterparties have made large collateral calls against AIGFP, in particular related to the multi-sector CDO portfolio. This was largely driven by deterioration in the market value of the reference obligations. As of July 31, 2008, AIGFP had either agreed to

post or posted collateral based on exposures, calculated in respect of super senior credit default swaps, in an aggregate net amount of $16.5 billion. Since that date and up to November 5, 2008, AIG has agreed to post or posted an additional $23.4 billion, for a total of $39.9 billion, resulting from continued deterioration in the market valuation of the referenced obligations, rating downgrades of reference obligations and the downgrade of AIG's ratings. The amount of future collateral posting requirements is a function of AIG's credit ratings, the rating of the reference obligations and any further decline in the market value of the relevant reference obligations, with the latter being the most significant factor. Given the severe market disruption, lack of observable data and the uncertainty regarding the potential effects on market prices of the TARP and other measures recently undertaken by the federal government to address the credit market disruption, AIGFP is unable to reasonably estimate the amounts of collateral that it would be required to post. The maximum amount of collateral that AIGFP could be required to post is the net notional amount of the super senior credit default swap portfolio.

Models and Modeling

AIGFP values its credit default swaps written on the most senior (super senior) risk layers of designated pools of debt securities or loans using internal valuation models, third-party prices and market indices. The principal market was determined to be the market in which super senior credit default swaps of this type and size would be transacted, or have been transacted, with the greatest volume or level of activity. AIG has determined that the principal market participants, therefore, would consist of other large financial institutions who participate in sophisticated over-the-counter derivatives markets. The specific valuation methodologies vary based on the nature of the referenced obligations and availability of market prices.

The valuation of the super senior credit derivatives continues to be challenging given the limitation on the availability of market observable information due to the lack of trading and price transparency in the structured finance market, particularly during and since the fourth quarter of 2007. These market conditions have increased the reliance on management estimates and judgments in arriving at an estimate of fair value for financial reporting purposes. Further, disparities in the valuation methodologies employed by market participants and the varying judgments reached by such participants when assessing volatile markets have increased the likelihood that the various parties to these instruments may arrive at significantly different estimates as to their fair values.

AIGFP's valuation methodologies for the super senior credit default swap portfolio have evolved in response to the deteriorating market conditions and the lack of sufficient market observable information. AIG has sought to calibrate the model to available market information and to review the assumptions of the model on a regular basis.

Arbitrage Portfolio — Multi-Sector CDOs

The underlying assumption of the valuation methodology for AIGFP's credit default swap portfolio wrapping multi-sector CDOs is that, to be willing to assume the obligations under a credit default swap, a market participant would require payment of the full difference between the cash price of the underlying tranches of the referenced securities portfolio and the net notional amount specified in the credit default swap.

AIGFP uses a modified version of the Binomial Expansion Technique (BET) model to value its credit default swap portfolio written on super senior tranches of CDOs of ABS, including the 2a-7 Puts. The BET model was developed in 1996 by a major rating agency to generate expected loss estimates for CDO tranches and derive a credit rating for those tranches, and has been widely used ever since.

AIG selected the BET model for the following reasons:

- it is known and utilized by other institutions;
- it has been studied extensively, documented and enhanced over many years;
- it is transparent and relatively simple to apply;
- the parameters required to run the BET model are generally observable; and
- it can easily be modified to use probabilities of default and expected losses derived from the underlying collateral securities market prices instead of using rating-based historical probabilities of default.

The BET model has certain limitations. A well known limitation of the BET model is that it can understate the expected losses for super senior tranches when default correlations are high. The model uses correlations implied from diversity scores which do not capture the tendency for correlations to increase as defaults increase. Recognizing this concern, AIG tested the sensitivity of the valuations to the diversity scores. The results of the testing demonstrated that the valuations are not very sensitive to the diversity scores because the expected losses generated from the prices of the collateral pool securities are currently high, breaching the attachment point in most transactions. Once the attachment point is breached by a sufficient amount, the diversity scores, and their implied correlations, are no longer a significant driver of the valuation of a super senior tranche.

AIGFP has adapted the BET model to estimate the price of the super senior risk layer or tranche of the CDO. AIG modified the BET model to imply default probabilities from market prices for the underlying securities and not from rating agency assumptions. To generate the estimate, the model uses the prices for the securities comprising the portfolio of a CDO as an input and converts those prices to credit spreads over current LIBOR-based interest rates. These credit spreads are used to determine implied probabilities of default and

expected losses on the underlying securities. This data is then aggregated and used to estimate the expected cash flows of the super senior tranche of the CDO.

The application of the modified BET model involves the following steps for each individual super senior tranche of a CDO in the portfolio:

1) Calculation of the cash flow pattern that matches the weighted average life for each underlying security of the CDO;

2) Calculation of an implied credit spread for each security from the price and cash flow pattern determined in step 1. This is an arithmetic process which converts prices to yields (similar to the conversion of United States Treasury security prices to yields), and then subtracts LIBOR-based interest rates to determine the credit spreads;

3) Conversion of the credit spread into its implied probability of default. This also is an arithmetic process that determines the assumed level of default on the security that would equate the present value of the expected cash flows discounted at a risk free rate with the present value of the contractual cash flows discounted using LIBOR-based interest rates plus the credit spreads;

4) Generation of expected losses for each underlying security using the probability of default and recovery rate;

5) Aggregation of the cash flows for all securities to create a cash flow profile of the entire collateral pool within the CDO;

6) Division of the collateral pool into a number of hypothetical independent identical securities based on the CDO's diversity score so that the cash flow effects of the portfolio can be mathematically aggregated properly. The purpose of dividing the collateral pool into hypothetical securities is a simplifying assumption used in all BET models as part of a statistical technique that aggregates large amounts of homogeneous data;

7) Simulation of the default behavior of the hypothetical securities using a Monte Carlo simulation and aggregation of the results to derive the effect of the expected losses on the cash flow pattern of the super senior tranche taking into account the cash flow diversion mechanism of the CDO;

8) Discounting of the expected cash flows determined in step 7 using LIBOR-based interest rates to estimate the value of the super senior tranche of the CDO; and

9) Adjustment of the model value for the super senior multi-sector CDO credit default swap for the effect of the risk of non-performance by AIG using the credit spreads of AIG available in the marketplace and considering the effects of collateral and master netting arrangements.

AIGFP employs a Monte Carlo simulation in step 7 above to assist in quantifying the effect on the valuation of the CDO of the unique aspects of the CDO's structure such as triggers that divert cash flows to the most senior part of the capital structure. The Monte Carlo simulation is used to determine whether an underlying security defaults in a given simulation scenario and, if it does, the security's implied random default time and expected loss. This information is used to project cash flow streams and to determine the expected losses of the portfolio.

In addition to calculating an estimate of the fair value of the super senior CDO security referenced in the credit default swaps using its internal model, AIGFP also considers the price estimates for the super senior CDO securities provided by third parties, including counterparties to these transactions, to validate the results of the model and to determine the best available estimate of fair value. In determining the fair value of the super senior CDO security referenced in the credit default swaps, AIGFP uses a consistent process which considers all available pricing data points and eliminates the use of outlying data points. When pricing data points are within a reasonable range an averaging technique is applied.

The following table presents the net notional amount and fair value derivative liability of the multi-sector super senior credit default swap portfolio using AIGFP's fair value methodology at September 30, 2008:

(in millions)	Net Notional Amount	Fair Value Derivative Liability at September 30, 2008
BET model	$ 9,010	$ 3,920
Third party price	21,050	9,297
Average of BET model and third party price	36,966	15,185
Other	4,618	1,805
Total	$71,644	$30,207

The fair value derivative liability of $30.2 billion recorded on AIGFP's super senior multi-sector CDO credit default swap portfolio represents the cumulative change in fair value of these derivatives, which represents AIG's best estimate of the amount it would need to pay to a willing, able and knowledgeable third party to assume the obligations under AIGFP's super senior multi-sector credit default swap portfolio as of September 30, 2008.

Arbitrage Portfolio — Corporate Debt/CLOs

The valuation of credit default swaps written on portfolios of investment-grade corporate debt and CLOs is less complex than the valuation of super senior multi-sector CDO credit default swaps and the valuation inputs are more transparent and readily available.

In the case of credit default swaps written on portfolios of investment-grade corporate debt, AIGFP estimates the fair value of its obligations by comparing the contractual premium of each contract to the current market levels of the

senior tranches of comparable credit indices, the iTraxx index for European corporate issuances and the CDX index for U.S. corporate issuances. These indices are considered reasonable proxies for the referenced portfolios. In addition, AIGFP compares these valuations to third party prices and makes adjustments as necessary to determine the best available estimate of fair value.

AIGFP estimates the fair value of its obligations resulting from credit default swaps written on CLOs to be equivalent to the par value less the current market value of the referenced obligation. Accordingly, the value is determined by obtaining third-party quotes on the underlying super senior tranches referenced under the credit default swap contract.

No assurance can be given that the fair value of AIGFP's arbitrage credit default swap portfolio would not change materially if other market indices or pricing sources were used to estimate the fair value of the portfolio.

Regulatory Capital Portfolio

In the case of credit default swaps written to facilitate regulatory capital relief, AIGFP estimates the fair value of these derivatives by considering observable market transactions. The transactions with the most observability are the early terminations of these transactions by counterparties. AIG expects that the majority of these transactions will be terminated within the next 6 to 18 months by AIGFP's counterparties. From January 1, 2008 through September 30, 2008, $94.9 billion in net notional exposures have been terminated. Since that date and through October 27, 2008, $4.5 billion in net notional exposures have been terminated. AIGFP has not been required to make any payments as part of these terminations and in certain cases was paid a fee upon termination. In all cases, terminations were initiated by the counterparties prior to the transactions maturing. AIGFP also considers other market data, to the extent relevant and available.

In light of early termination experience to date and after other analyses, AIG determined that there was no unrealized market valuation adjustment for this regulatory capital relief portfolio for the nine-month period ended September 30, 2008 other than for one transaction where AIGFP believes the counterparty is no longer using the transaction to obtain regulatory capital relief. During the second quarter of 2008, a regulatory capital relief transaction with a net notional amount of $1.6 billion and a fair value loss of $125 million was not terminated as expected when it no longer provided regulatory capital benefit to the counterparty. This transaction provided protection on an RMBS, unlike the other regulatory transactions, which provide protection on loan portfolios held by the counterparties. The documentation for this transaction contains provisions not included in AIGFP's other regulatory capital relief transactions, which enable the counterparty to arbitrage a specific credit exposure.

AIG will continue to assess the valuation of this portfolio and monitor developments in the marketplace. Given the significant deterioration in the credit markets and the risk that AIGFP's expectations with respect to the termination of these transactions by its counterparties may not materialize, there can be no assurance that AIG will not recognize unrealized market valuation losses from this portfolio in future periods, and recognition of even a small percentage decline in the fair value of this portfolio could be material to AIG's consolidated results of operations for an individual reporting period or to AIG's consolidated financial condition.

Key Assumptions Used in the BET model — Multi-Sector CDOs

The most significant assumption used in the BET model is the pricing of the individual securities within the CDO collateral pools. The following table summarizes the gross transactional notional weighted average price at June 30, 2008 and September 30, 2008, by ABS category.

ABS Category	Gross Transaction Notional Weighted Average Price September 30, 2008	Gross Transaction Notional Weighted Average Price June 30, 2008
RMBS Prime	71.54%	81.23%
RMBS Alt-A	46.12	58.06
RMBS Subprime	38.83	48.44
CMBS	81.40	87.46
CDOs	29.83	32.24
Other	78.36	85.03
Total	52.33%	60.38%

The decrease in the weighted average prices reflects continued deterioration in the markets for RMBS and CMBS and further downgrades in RMBS and CMBS credit ratings.

Prices for the individual securities held by a CDO are obtained in most cases from the CDO collateral managers, to the extent available. For the quarter ended September 30, 2008, CDO collateral managers provided market prices for approximately 70 percent of the underlying securities. When a price for an individual security is not provided by a CDO collateral manager, AIGFP derives the price through a pricing matrix using prices from CDO collateral managers for similar securities. Matrix pricing is a mathematical technique used principally to value debt securities without relying exclusively on quoted prices for the specific securities, but rather by relying on the relationship of the security to other benchmark quoted securities. Substantially all of the CDO collateral managers who provided prices used dealer prices for all or part of the underlying securities, in some cases supplemented by third party pricing services.

The BET model also uses diversity scores, weighted average lives, recovery rates and discount rates. The determination of some of these inputs requires the use of judgment

and estimates, particularly in the absence of market observable data. Diversity scores (which reflect default correlations between the underlying securities of a CDO) are obtained from CDO trustees or implied from default correlations. Weighted average lives of the underlying securities are obtained, when available, from external subscription services such as Bloomberg and Intex and, if not available, AIGFP utilizes an estimate reflecting known weighted average lives. Collateral recovery rates are obtained from the multi-sector CDO recovery data of a major rating agency. AIGFP utilizes a LIBOR-based interest rate curve to derive its discount rates.

AIGFP employs similar control processes to validate these model input as those used to value AIG's investment portfolio as described in Critical Accounting Estimates — Fair Value Measurements of Certain Financial Assets and Liabilities — Overview. The effects of the adjustments resulting from the validation process were de minimis for each period presented.

Valuation Sensitivity — Arbitrage Portfolio

Multi-Sector CDOs

AIG utilizes sensitivity analyses that estimate the effects of using alternative pricing and other key inputs on AIG's calculation of the unrealized market valuation loss related to the AIGFP super senior credit default swap portfolio. While AIG believes that the ranges used in these analyses are reasonable, given the current difficult market conditions, AIG is unable to predict which of the scenarios is most likely to occur. Actual results in any period are likely to vary, perhaps materially, from the modeled scenarios, and there can be no assurance that the unrealized market valuation loss related to the AIGFP super senior credit default swap portfolio will be consistent with any of the sensitivity analyses.

For the purposes of estimating sensitivities for the super senior multi-sector CDO credit default swap portfolio, the change in valuation derived using the BET model is used to estimate the change in the fair value of the derivative liability. As mentioned above, the most significant assumption used in the BET model is the pricing of the securities within the CDO collateral pools. If the actual pricing of the securities within the collateral pools differs from the pricing used in estimating the fair value of the super senior credit default swap portfolio, there is potential for material variation in the fair value estimate. A decrease by five points (for example, from 87 cents per dollar to 82 cents per dollar) in the aggregate price of the underlying collateral securities would increase the fair value derivative liability by approximately $3.7 billion, while an increase in the aggregate price of the underlying collateral securities by five points (for example, from 90 cents per dollar to 95 cents per dollar) would reduce the fair value derivative liability by approximately $3.8 billion. Any further declines in the value of the underlying collateral securities held by a CDO will similarly affect the value of the super senior CDO securities given their significantly depressed valuations. Given the current difficult market conditions, AIG cannot predict reasonably likely changes in the prices of the underlying collateral securities held within a CDO at this time.

The following table presents other key inputs used in the BET model, and the potential increase (decrease) to the fair value of the derivative liability at September 30, 2008 corresponding to changes in these key inputs:

(in millions)	Increase (Decrease) To Fair Value Derivative Liability
Weighted average lives	
Effect of an increase of 1 year	$ 426
Effect of a decrease of 1 year	(968)
Recovery rates	
Effect of an increase of 10%	(21)
Effect of a decrease of 10%	119
Diversity scores	
Effect of an increase of 5	(80)
Effect of a decrease of 5	207
Discount curve	
Effect of an increase of 100 basis points	158

These results are calculated by stressing a particular assumption independently of changes in any other assumption. No assurance can be given that the actual levels of the key inputs will not exceed, perhaps significantly, the ranges assumed by AIG for purposes of the above analysis. No assumption should be made that results calculated from the use of other changes in these key inputs can be interpolated or extrapolated from the results set forth above.

Corporate Debt

The following table represents the relevant market credit indices and index CDS maturity used to estimate the sensitivity for the credit default swap portfolio written on investment-grade corporate debt and the estimated increase (decrease) to the fair value of the derivative liability at September 30, 2008 corresponding to changes in these market credit indices and maturity:

(in millions)	Increase (Decrease) To Fair Value Derivative Liability		
CDS maturity (in years)	5	7	10
CDX Index			
Effect of an increase of 10 basis points	$(19)	$(46)	$ (9)
Effect of a decrease of 10 basis points	19	46	9
iTraxx Index			
Effect of an increase of 10 basis points	(9)	(32)	(7)
Effect of a decrease of 10 basis points	9	32	7

These results are calculated by stressing a particular assumption independently of changes in any other assumption. No assurance can be given that the actual levels of the indices and maturity will not exceed, perhaps significantly, the ranges assumed by AIGFP for purposes of the above

analysis. No assumption should be made that results calculated from the use of other changes in these indices and maturity can be interpolated or extrapolated from the results set forth above.

Stress Testing of Potential Realized Credit Losses — Multi-Sector CDOs

In addition to performing sensitivity analyses around the valuation of the AIGFP super senior credit default swap portfolio, AIG performed a roll rate analysis to stress the AIGFP super senior multi-sector CDO credit default swap portfolio for potential pre-tax realized credit losses without taking into consideration either sales of securities or early terminations of the contracts. Credit losses represent the shortfall of principal and/or interest cash flows on the referenced super senior risk layers underlying the portfolio.

Two scenarios illustrated in this process resulted in potential pre-tax realized credit losses of approximately $7.8 billion (Scenario A) and approximately $12.0 billion (Scenario B). Comparable amounts at June 30, 2008 were $5.0 billion and $8.5 billion, respectively. At September 30, 2008, AIG used the same set of roll rate and loss severity assumptions in its roll rate analysis as those used at June 30, 2008. However, the estimated potential credit losses illustrated by Scenarios A and B increased significantly over the amounts reported at June 30, 2008. The increases in the estimated potential credit losses were principally attributable to three factors:

- approximately $1.5 billion in each scenario was attributable to the increase in the LIBOR interest rate, caused by tight money market conditions, which increased the modeled amounts of cash flow diversion to lower rated tranches within the multi-sector CDOs;
- approximately $600 million in scenario A and $700 million in scenario B were attributable to enhancements used in the analysis to reflect more accurately the attributes of the portfolio; and
- approximately $600 million in scenario A and $1.2 billion in scenario B were due to larger actual delinquencies in the performing mortgage pools and greater credit deterioration in other collateral securities.

Other factors, such as applying the pool losses determined based on the above factors up through the capital structures of the RMBS as well as the cash flow waterfall effects within the CDOs, account for the remainder of the increase.

The significant assumptions for subprime mortgages used in Scenario A are provided below. Scenario B illustrates the effect of a 20 percent relative increase (but not in excess of 100 percent) in all Scenario A roll rate default frequency assumptions and in all Scenario A loss severity assumptions across all mortgage collateral (for example, 60 percent increased to 72 percent). Actual ultimate realized credit losses are likely to vary, perhaps materially, from these scenarios, and there can be no assurance that the ultimate realized credit losses related to the AIGFP super senior multi-sector CDO credit default swap portfolio will be consistent with either scenario or that such realized credit losses will not exceed the potential realized credit losses illustrated by Scenario B.

In the second quarter of 2008, AIG stressed the AIGFP super senior multi-sector CDO credit default swap portfolio using the roll rate analysis enhanced to apply to all RMBS collateral including subprime, Alt-A and prime residential mortgages that comprise the subprime, Alt-A and prime RMBS. This analysis assumed that certain percentages of actual delinquent mortgages will roll into default and foreclosure. It also assumed that certain percentages of non-delinquent mortgages will become delinquent and default over time, with those delinquency percentages depending on the age of the mortgage pool. To those assumed defaults AIG applied loss severities (one minus recovery) to derive estimated ultimate losses for each mortgage pool comprising a subprime, Alt-A and prime RMBS. Because subprime, Alt-A and prime RMBS have differing characteristics, the roll rates and loss severities differed. AIG then estimated tranche losses from these roll rate losses by applying the pool losses up through the capital structure of the RMBS. In this estimate of tranche losses, AIG introduced in the second quarter of 2008 an enhancement to the roll rate analysis to take into account the cash flow waterfall and to capture the potential effects, both positive and negative, of cash flow diversion within each CDO. To these estimated subprime, Alt-A and prime RMBS losses AIG added estimated credit losses on the inner CDOs and other ABS, such as CMBS, credit card and auto loan ABS held by the CDOs, calculated by using rating-based static percentages, in the case of inner CDOs varying by vintage and type of CDO, and, in the case of other ABS, by rating. In addition to the foregoing, the analysis incorporates the effects of certain other factors such as mortgage prepayment rates, excess spread and delinquency triggers.

Subprime RMBS comprise the majority of collateral securities within the multi-sector CDOs. Given adverse real estate market conditions, subprime mortgage losses comprise the largest percentage of AIG's pre-tax credit impairment losses in scenarios A and B.

The roll rate analysis, as mentioned above, consists of projecting credit losses by projecting mortgage defaults and applying loss severities to these defaults. Mortgage defaults are estimated by applying roll rate frequencies to each segment of existing delinquent mortgages and by using loss timing curves to forecast future defaults from currently performing mortgages.

The roll rate default frequency assumptions for subprime mortgages by vintage used in the scenario A roll rate analysis are as follows:

Segment	Pre-2005	2005	2006	2007
30+ days delinquent	60%	70%	80%	80%
60+ days delinquent	70%	80%	80%	80%
90+ days delinquent + borrower bankruptcies	70%	80%	90%	90%
Foreclosed/REO mortgages	100%	100%	100%	100%

The subprime mortgage loss severity assumptions by vintage used in the scenario A roll rate analysis are as follows:

Pre 2H 2004	2H 2004	1H 2005	2H 2005	2006/2007
50%	50%	55%	55%	60%

Prior to June 30, 2008, AIG conducted risk analyses of the AIGFP super senior multi-sector CDO credit default swap portfolio using certain ratings-based static stress tests, which centered around scenarios of further stress on the portfolio resulting from downgrades by the rating agencies from current levels on the underlying collateral in the CDO structures supported by AIGFP's credit default swaps. During the first quarter of 2008, AIG developed and implemented its roll rate analysis. Commencing in the second quarter of 2008, AIG discontinued use of the rating-based static stress test and used only the roll rate stress test because it believed that the roll rate stress test provided a more reasonable methodology to illustrate potential realized credit losses than the rating-based static stress test used previously.

Due to the dislocation in the market for CDO and RMBS collateral, AIG does not use the market values of the underlying CDO collateral in estimating its potential realized credit losses. The use of factors derived from market-observable prices in models used to determine the estimates for future realized credit losses could result in materially higher estimates of potential realized credit losses.

Under the terms of most of these credit derivatives, credit losses to AIG would generally result from the credit impairment of the referenced obligations that AIG would acquire in extinguishing its swap obligations. Other types of analyses or models could result in materially different estimates. AIG is aware that other market participants have used different assumptions and methodologies to estimate the potential realized credit losses on AIGFP's super senior multi-sector CDO credit default swap portfolio, resulting in significantly higher estimates than those resulting from AIG's roll rate stress testing scenarios. Actual ultimate realized credit losses are likely to vary, perhaps materially, from AIG's roll rate stress testing scenarios, and there can be no assurance that the ultimate realized credit losses related to the AIGFP super senior multi-sector CDO credit default swap portfolio will be consistent with either scenario or that such realized credit losses will not exceed the potential realized credit losses illustrated by Scenario B.

The potential realized credit losses illustrated in Scenarios A and B are lower than the $30.2 billion fair value derivative liability of AIGFP's super senior multi-sector CDO credit default swap portfolio at September 30, 2008. The fair value of AIGFP's super senior multi-sector CDO credit default swap portfolio is based upon fair value accounting principles, which rely on third-party prices for both the underlying collateral securities and the CDOs that AIGFP's super senior credit default swaps wrap. These prices currently incorporate liquidity premiums, risk aversion elements and credit risk modeling, which in some instances may use more conservative assumptions than those used by AIG in its roll rate stress testing. Due to the ongoing disruption in the U.S. residential mortgage market and credit markets and the downgrades of RMBS and CDOs by the rating agencies, the market continues to lack transparency around the pricing of these securities. These prices are not necessarily reflective of the ultimate potential realized credit losses AIGFP could incur in the future related to the AIGFP super senior multi-sector CDO credit default swap portfolio, and AIG believes they incorporate a significant amount of market-driven risk aversion.

Other derivatives. Valuation models that incorporate unobservable inputs initially are calibrated to the transaction price. Subsequent valuations are based on observable inputs to the valuation model (e.g., interest rates, credit spreads, volatilities, etc.). Model inputs are changed only when corroborated by market data.

Transfers into Level 3

During the three-months ended September 30, 2008, AIG transferred from Level 2 to Level 3 approximately $7.1 billion of assets, primarily representing fixed maturity securities for which the significant inputs used to measure the fair value of the securities became unobservable primarily as a result of the significant disruption in the credit markets. See Note 3 to the Consolidated Financial Statements for additional information about transfers into Level 3.

Valuation Controls

AIG is actively implementing its remediation plan to address the material weakness in internal control relating to the fair value valuation of the AIGFP super senior credit default swap portfolio, and oversight thereof as described in Item 9A. of the 2007 Annual Report on Form 10-K. AIG is developing new systems and processes to reduce reliance on certain manual controls that have been established as compensating controls over valuation of this portfolio and in other areas, and is strengthening the resources required to remediate this weakness. Notwithstanding this need to continue strengthening these controls, AIG has an oversight structure that includes appropriate segregation of duties with respect to the valuation of its financial instruments. Senior management, independent of the trading and investing functions, is responsible for the

oversight of control and valuation policies and for reporting the results of these controls and policies to AIG's Audit Committee. AIG employs procedures for the approval of new transaction types and markets, price verification, periodic review of profit and loss, and review of valuation models by personnel with appropriate technical knowledge of relevant products and markets. These procedures are performed by personnel independent of the trading and investing functions. For valuations that require inputs with little or no market observability, AIG compares the results of its valuation models to actual subsequent transactions.

Capital Resources and Liquidity

Liquidity

During the third quarter of 2008, AIG experienced liquidity issues as described under Current Events Related to Liquidity. As a result of these events, AIG, ILFC and AGF have not had access to their traditional sources of long-term or short-term financing through the public debt markets. AIG parent's sources of liquidity currently consist of borrowings under the Fed Facility, issuances of commercial paper under the CPFF and borrowings under its other revolving credit facilities and dividends, distributions and other payments from its subsidiaries.

On November 10, 2008, AIG announced several transactions that will help stabilize AIG's liquidity. Subject to the issuance of the Series D Preferred Shares described below, the Fed Credit Agreement will be amended to, among other things:

- provide that the total commitment under the Fed Facility following the issuance of the Series D Preferred Shares shall be $60 billion;
- reduce the interest rate payable on outstanding borrowings under the Fed Facility from three-month LIBOR (not less than 3.5 percent) plus 8.5 percent per annum to three-month LIBOR (not less than 3.5 percent) plus 3.0 percent per annum;
- reduce the fee payable on undrawn amounts from 8.5 percent per annum to 0.75 percent per annum;
- reduce the number of shares of common stock of AIG to be issued upon conversion of the Series C Preferred Stock to be held by the Trust to 77.9 percent; and
- extend the term of the Fed Facility from two years to five years.

Pursuant to an agreement, AIG will issue $40 billion liquidation preference of Series D Preferred Shares and a 10-year warrant exercisable for shares of AIG common stock equal to 2 percent of the outstanding shares of common stock to the United States Treasury, the net proceeds of which will be used to repay a portion of the outstanding balance under the Fed Facility. AIG expects during the fourth quarter to form a limited liability company with the NY Fed that will acquire RMBS owned by certain AIG insurance company subsidiaries. These proceeds together with other AIG funds, will be used to return all cash collateral posted by securities borrowers, including approximately $19.9 billion to be returned to the NY Fed. After all collateral is returned, AIG's U.S. securities lending program will be terminated. AIG also expects during the fourth quarter to establish a limited liability company with the NY Fed that will purchase up to approximately $70 billion of the CDO exposures protected by AIGFP's multi-sector credit default swap portfolio. These actions are expected to:

- increase AIG's effective borrowing capacity under the Fed Facility;
- limit AIG's exposure to the RMBS securities in the securities lending pool; and
- limit AIG's exposure to the CDOs underlying its multi-sector credit default swap portfolio.

At the subsidiary level, in September 2008, both AGF and ILFC borrowed under their credit facilities ($4.6 billion and $6.5 billion, respectively) and certain U.S. life insurance companies entered into the Fed Securities Lending Agreement with the NY Fed.

Proceeds from announced asset sales are required to pay down the Fed Facility.

AIG Parent

At November 5, 2008, AIG parent had the following sources of liquidity:

- $24 billion of available borrowings under the September 22, 2008 Fed Facility;
- $5.6 billion of available commercial paper borrowings under all programs under the CPFF; and
- $3.8 billion of available borrowings under its revolving credit facilities, as described under Revolving Credit Facilities below.

As a result, AIG believes that it has sufficient liquidity at the parent level to meet its obligations through at least the next twelve months. However, no assurance can be given that AIG's cash needs will not exceed projected amounts. Additional collateral calls at AIGFP, a failure to consummate either the establishment of the RMBS limited liability company or CDO security limited liability company, a further downgrade of AIG's credit ratings or unexpected capital or liquidity needs of AIG's subsidiaries may result in significant cash needs. For a further discussion of this risk, see Item 1A. Risk Factors.

Domestic Life Insurance Companies

AIG's Domestic Life Insurance and Retirement Services companies have three primary liquidity needs: the funding of

surrenders; returning cash collateral under the securities lending program; and obtaining capital to offset other-than-temporary impairment charges. At the current rate of surrenders, AIG believes that its Domestic Life Insurance and Retirement Services companies will have sufficient resources to meet these obligations. A substantial increase in surrender activity could, however, place stress on the liquidity of these companies and require asset sales.

AIG's securities lending payables totaled $34.2 billion at November 5, 2008. When necessary, the NY Fed is providing liquidity to the securities lending pool through borrowings of securities from the pool. AIG anticipates repaying the Fed Securities Lending Agreement in full upon the establishment of the limited liability company to repurchase the RMBS in the securities lending pool.

AIG parent contributed $16.6 billion to Domestic Life Insurance and Retirement Services companies during the first nine months of 2008, largely to offset the reduction in capital due to the significant other-than-temporary impairment charges. To the extent the investment portfolios of the Domestic Life Insurance and Retirement Services companies continue to be adversely affected by market conditions, AIG may need to make additional capital contributions to these companies.

Foreign Life Insurance Companies

AIG's Foreign Life Insurance companies (including ALICO) have had significant capital needs following publicity of AIG parent's liquidity issues and related credit ratings downgrades and reflecting the decline in the equity markets. AIG contributed $1.6 billion to the Foreign Life Insurance companies in September 2008, and $339 million in October 2008 to meet these needs. AIG expects to contribute approximately $1.4 billion to Nan Shan in November 2008.

AIG believes that its Foreign Life Insurance subsidiaries will have adequate capital to support their business plans through the remainder of 2008; however, to the extent the investment portfolios of the Foreign Life Insurance companies continue to be adversely affected by market conditions, AIG may need to make additional capital contributions to these companies.

Commercial Insurance Group

AIG expects CIG to be able to continue to meet its obligations as they come due through cash from operations and, to the extent necessary, asset dispositions. One or more large catastrophes, however, may require AIG to provide additional support to CIG.

AIG has provided letters of credit that totaled $5.7 billion at October 27, 2008, to allow subsidiaries of CIG to obtain admitted surplus credit for reinsurance provided by non-admitted carriers. Approximately $4.2 billion of these letters of credit will expire on December 31, 2008. The inability of AIG to renew or replace these letters of credit or otherwise obtain equivalent financial support would result in a significant reduction of the statutory surplus of these property and casualty companies and would require AIG to make additional capital contributions.

International Lease Finance Corporation

To assure maximum liquidity for its operations, ILFC borrowed the full amount available under its credit facilities, $6.5 billion, in September 2008. ILFC can also borrow up to $5.7 billion under the CPFF. At November 5, 2008, ILFC had borrowed $1.7 billion under the CPFF. Funding under the CPFF terminates in April 30, 2009, with funds outstanding at that date maturing through July 2009. In addition, ILFC is seeking secured financings. ILFC currently has the capacity under their present facilities and indentures to enter into secured financings in excess of $4.0 billion. AIG expects that these borrowings and cash flows from operations, which may include aircraft sales, will permit ILFC to meet its obligations through September 2009, after which AIG would rely upon additional asset sales and funding through the Fed Facility.

American General Finance

To assure maximum liquidity for its operations, AGF borrowed the full amount available under its primary credit facilities, $4.6 billion, in September 2008. AGF anticipates that its primary sources of funds to support its operations and repay its obligations will be finance receivable collections from operations, while limiting its lending activities and focusing on expense savings. In addition, AGF is seeking secured financing. AGF anticipates that its existing sources of funds will be sufficient to meet its debt and other obligations through the first quarter of 2009. At that time, AIG will need to find other sources of liquidity for AGF, including sales of AGF assets and funding through the Fed Facility.

AIGCFG

As a result of AIG parent's liquidity issues and related credit ratings downgrades, AIGCFG experienced significant deposit withdrawals in Hong Kong during September 2008. AIGCFG subsidiaries borrowed $1.6 billion from AIG in September and October of 2008 to meet these withdrawals and other cash needs.

AIG believes that the funding needs of AIGCFG have stabilized, but it is possible that AIGCFG's liquidity needs could increase substantially. AIG is working to sell these businesses on an expedited basis and believes that entering into sale agreements will help stabilize AIGCFG's liquidity.

Debt maturities in next twelve months

The following sets forth AIG's debt maturities by quarter for the twelve months ended September 30, 2009:

(in billions)	4th Quarter 2008	1st Quarter 2009	2nd Quarter 2009	3rd Quarter 2009
Debt Maturities	$9	$3	$4	$12

AIG expects to meet these obligations through borrowings from the Fed Facility, sales of commercial paper pursuant to the CPFF, and cash received from subsidiaries. See Notes 4, 5, and 11 to the Consolidated Financial Statements for additional information regarding the terms of the Fed Credit Agreement and the Pledge Agreement.

Third Quarter and Nine Month Capital Resources and Liquidity

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

(in millions)	Inception through September 30, 2008	Inception through November 5, 2008
Borrowings:		
Loans to AIGFP for collateral postings, GIA and other maturities	**$35,340**	**$43,100**
Capital contributions to insurance companies[(a)]	**13,341**	**13,687**
Repayment of obligations to securities lending program	**3,160**	**3,160**
AIG Funding commercial paper maturities	**2,717**	**3,714**
Repayment of intercompany loans	**1,528**	**1,528**
Contributions to AIGCFG subsidiaries	**1,094**	**1,591**
Debt repayments	**1,038**	**1,578**
Other borrowings[(a)]	**2,782**	**8,642**
Total borrowings	**61,000**	**77,000**
Repayments:		
Repayments not reducing available amounts	**–**	**16,000** [(b)]
Repayments reducing available amounts	**–**	**–**
Total repayments	**–**	**16,000**
Net borrowings	**61,000**	**61,000**
Total Fed Facility	**85,000**	**85,000**
Remaining available amount	**24,000**	**24,000**
Net borrowings	**61,000**	**61,000**
Paid in kind interest and fees	**1,960**	**1,960**
Total balance outstanding	**$62,960**	**$62,960**

(a) Includes securities lending activities.

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

Borrowings

AIG's total borrowings were as follows:

(in millions)	**September 30, 2008**	December 31, 2007
Borrowings issued by AIG:		
Fed Facility	**$ 62,960**	$ –
Notes and bonds payable	**12,036**	14,588
Junior subordinated debt	**12,224**	5,809
Junior subordinated debt attributable to equity units	**5,880**	–
Loans and mortgages payable	**376**	729
MIP matched notes and bonds payable	**13,871**	14,267
AIGFP matched notes and bonds payable	**4,204**	874
Total AIG borrowings	**111,551**	36,267
Borrowings guaranteed by AIG:		
AIGFP[(a)]		
GIAs	**13,608**	19,908
Notes and bonds payable	**16,229**	36,676
Loans and mortgages payable	**6,627**	1,384
Hybrid financial instrument liabilities[(b)]	**2,685**	7,479
Total AIGFP borrowings	**39,149**	65,447
AIG Funding, Inc. commercial paper	**1,944**	4,222
AIGLH notes and bonds payable	**798**	797
Liabilities connected to trust preferred stock	**1,414**	1,435
Total borrowings issued or guaranteed by AIG	**154,856**	108,168
Borrowings not guaranteed by AIG:		
ILFC		
Commercial paper	**1,562**	4,483
Junior subordinated debt	**999**	999
Notes and bonds payable[(c)]	**32,005**	25,737
Total ILFC borrowings	**34,566**	31,219
AGF		
Commercial paper and extendible commercial notes	**1,918**	3,801
Junior subordinated debt	**349**	349
Notes and bonds payable	**24,098**	22,369
Total AGF borrowings	**26,365**	26,519
AIGCFG		
Commercial paper	**168**	287
Loans and mortgages payable	**2,035**	1,839
Total AIGCFG borrowings	**2,203**	2,126
AIG Finance Taiwan Limited commercial paper	**8**	–
Other subsidiaries	**694**	775
Borrowings of consolidated investments:		
A.I. Credit[(d)]	**–**	321
AIG Investments	**1,305**	1,636
AIG Global Real Estate Investment	**4,548**	5,096
AIG SunAmerica	**5**	186
ALICO	**–**	3
Total borrowings of consolidated investments	**5,858**	7,242
Total borrowings not guaranteed by AIG	**69,694**	67,881
Consolidated:		
Total commercial paper and extendible commercial notes	**5,600**	13,114
Total long-term borrowings	**218,950**	162,935
Total borrowings	**$224,550**	$176,049

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

(b) Represents structured notes issued by AIGFP that are accounted for using the fair value option at 2008 and 2007.

(c) Includes borrowings under Export Credit Facility of $2.5 billion at September 30, 2008 and December 31, 2007, respectively.

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

The roll forward of long-term borrowings, excluding borrowings of consolidated investments, for the nine months ended September 30, 2008 was as follows:

(in millions)	Balance at December 31, 2007	Issuances	Maturities and Repayments	Effect of Foreign Exchange	Other Changes[b]	**Balance at September 30, 2008**
AIG						
Fed Facility	$ –	$ 61,000	$ –	$ –	$ 1,960	**$ 62,960**
Notes and bonds payable	14,588	–	(2,386)	(161)	(5)	**12,036**
Junior subordinated debt	5,809	6,953	–	(539)	1	**12,224**
Junior subordinated debt attributable to equity units	–	5,880	–	–	–	**5,880**
Loans and mortgages payable	729	297	(642)	8	(16)	**376**
MIP matched notes and bonds payable	14,267	–	(200)	(12)	(184)	**13,871**
AIGFP matched notes and bonds payable	874	3,464	(135)	–	1	**4,204**
AIGFP[a]						
GIAs	19,908	4,708	(13,247)	–	2,239	**13,608**
Notes and bonds payable and hybrid financial instrument liabilities	44,155	66,874	(89,660)	–	(2,455)	**18,914**
Loans and mortgages payable	1,384	5,489	(242)	–	(4)	**6,627**
AIGLH notes and bonds payable	797	–	–	–	1	**798**
Liabilities connected to trust preferred stock	1,435	–	(19)	–	(2)	**1,414**
ILFC notes and bonds payable	25,737	9,311	(2,791)	(253)	1	**32,005**
ILFC junior subordinated debt	999	–	–	–	–	**999**
AGF notes and bonds payable	22,369	5,691	(3,730)	(198)	(34)	**24,098**
AGF junior subordinated debt	349	–	–	–	–	**349**
AIGCFG loans and mortgages payable	1,839	1,800	(1,744)	3	137	**2,035**
Other subsidiaries	775	29	(116)	4	2	**694**
Total	$156,014	$171,496	$(114,912)	$ (1,148)	$ 1,642	**$213,092**

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

(b) Includes the cumulative effect of the adoption of FAS 159. Also includes commitment fee and payment in kind interest of $1.96 billion on the Fed Facility.

Maturities of long-term borrowings at September 30, 2008, excluding borrowings of consolidated investments, are as follows:

	Twelve Months Ended September 30,						
(in millions)	Total	2009	2010	2011	2012	2013	Thereafter
AIG:							
Fed Facility	$ 62,960	$ –	$62,960	$ –	$ –	$ –	$ –
Notes and bonds payable	12,036	639	1,850	500	503	997	7,547
Junior subordinated debt	12,224	–	–	–	–	–	12,224
Junior subordinated debt attributable to equity units	5,880	–	–	–	–	–	5,880
Loans and mortgages payable	376	36	–	–	–	292	48
MIP matched notes and bonds payable	13,871	1,207	2,217	3,069	2,024	871	4,483
AIGFP matched notes and bonds payable	4,204	252	39	12	64	6	3,831
Total AIG	111,551	2,134	67,066	3,581	2,591	2,166	34,013
AIGFP:							
GIAs	13,608	1,586	981	545	552	430	9,514
Notes and bonds payable	16,229	12,048	894	142	418	86	2,641
Loans and mortgages payable	6,627	43	506	121	1,251	2,230	2,476
Hybrid financial instrument liabilities	2,685	520	1,150	199	84	175	557
Total AIGFP	39,149	14,197	3,531	1,007	2,305	2,921	15,188
AIGLH notes and bonds payable	798	–	500	–	–	–	298
Liabilities connected to trust preferred stock	1,414	–	–	–	–	–	1,414
ILFC:							
Notes and bonds payable	21,948	3,824	4,480	4,756	3,574	2,806	2,508
Junior subordinated debt	999	–	–	–	–	–	999
Export credit facility	2,492	520	419	331	275	275	672
Bank financings	7,565	473	2,107	2,160	2,650	175	–
Total ILFC	33,004	4,817	7,006	7,247	6,499	3,256	4,179
AGF:							
Notes and bonds payable	24,098	5,831	5,777	2,517	1,809	2,398	5,766
Junior subordinated debt	349	–	–	–	–	–	349
Total AGF	24,447	5,831	5,777	2,517	1,809	2,398	6,115
AIGCFG Loans and mortgages payable	2,035	1,061	768	161	22	13	10
Other subsidiaries	694	17	2	4	4	2	665
Total	$213,092	$28,057	$84,650	$14,517	$13,230	$10,756	$61,882

AIG (Parent Company)

AIG has not had access to its traditional sources of long-term or short-term financing through the public debt markets. Further, in light of AIG's current common stock price, AIG does not expect to be able to issue equity securities in the public markets in the foreseeable future. AIG's affiliates, AIG Funding Inc., ILFC, Curzon Funding LLC and Nightingale Finance LLC, may issue up to approximately $6.9 billion, $5.7 billion, $7.2 billion and $1.1 billion, respectively, of commercial paper under the CPFF.

AIG traditionally issued debt securities from time to time to meet its financing needs and those of certain of its subsidiaries, as well as to opportunistically fund the MIP. The maturities of the debt securities issued by AIG to fund the MIP are generally expected to be paid using the cash flows of assets held by AIG as part of the MIP portfolio.

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

As of September 30, 2008, approximately $7.4 billion principal amount of senior notes were outstanding under AIG's medium-term note program, of which $3.2 billion was used for AIG's general corporate purposes, $1.0 billion was used by AIGFP (included within "AIGFP matched notes bonds and payable" in the preceding tables) and $3.2 billion was used to fund the MIP. The maturity dates of these notes range from 2008 to 2052. To the extent considered appropriate, AIG may enter into swap transactions to manage its effective borrowing rates with respect to these notes.

AIG also maintains a Euro medium-term note program under which an aggregate nominal amount of up to $31.5 billion of senior notes may be outstanding at any one time. As of September 30, 2008, the equivalent of $12.0 billion of notes were outstanding under the program, of which $9.3 billion were used to fund the MIP and the remainder was used for AIG's general corporate purposes. The aggregate amount outstanding includes a $678 million increase resulting from

foreign exchange translation into U.S. dollars, of which $167 million relates to notes issued by AIG for general corporate purposes and $511 million relates to notes issued to fund the MIP. AIG has economically hedged the currency exposure arising from its foreign currency denominated notes.

AIG maintains a shelf registration statement in Japan, providing for the issuance of up to Japanese yen 300 billion principal amount of senior notes, of which the equivalent of $476 million was outstanding as of September 30, 2008 and was used for AIG's general corporate purposes. In October 2008, $282 million of senior notes matured and were paid.

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

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

AIGFP

AIGFP used the proceeds from the issuance of notes and bonds and GIA borrowings to invest in a diversified portfolio of securities and derivative transactions. The borrowings may also be temporarily invested in securities purchased under agreements to resell. AIGFP's notes and bonds include structured debt instruments whose payment terms are linked to one or more financial or other indices (such as an equity index or commodity index or another measure that is not considered to be clearly and closely related to the debt instrument). These notes contain embedded derivatives that otherwise would be required to be accounted for separately under FAS 133. Upon AIG's adoption of FAS 155 in 2006, AIGFP elected the fair value option for these notes. The notes that are accounted for using the fair value option are reported separately under hybrid financial instrument liabilities. AIG guarantees the obligations of AIGFP under AIGFP's notes and bonds and GIA borrowings.

Approximately $8.7 billion of AIGFP's debt maturities through September 30, 2009 are fully collateralized with assets backing the corresponding liabilities.

ILFC

ILFC has not had access to its traditional sources of long-term or short-term financing through the public debt markets. ILFC can currently issue up to $5.7 billion in commercial paper under the CPFF and has the capacity under its present facilities and indentures to enter into secured financings in excess of $4.0 billion.

As a well-known seasoned issuer, ILFC has an automatic shelf registration statement with the SEC allowing ILFC immediate access to the U.S. public debt markets. At September 30, 2008, $6.9 billion of debt securities had been issued under this registration statement and $6.1 billion had been issued under a prior registration statement. In addition, ILFC has a Euro medium-term note program for $7.0 billion, under which $3.8 billion in notes were outstanding at September 30, 2008. Notes issued under the Euro medium-term note program are included in ILFC notes and bonds payable in the preceding table of borrowings. The cumulative foreign exchange adjustment loss for the foreign currency denominated debt was $715 million at September 30, 2008 and $969 million at December 31, 2007. ILFC has substantially eliminated the currency exposure arising from foreign currency denominated notes by economically hedging the note exposure.

ILFC had a $4.3 billion Export Credit Facility for use in connection with the purchase of approximately 75 aircraft delivered through 2001. This facility was guaranteed by various European Export Credit Agencies. The interest rate varies from 5.75 percent to 5.90 percent on these amortizing ten-year borrowings depending on the delivery date of the aircraft. At September 30, 2008, ILFC had $445 million outstanding under this facility. The debt is collateralized by a pledge of the shares of a subsidiary of ILFC, which holds title to the aircraft financed under the facility.

In May 2004, ILFC entered into a similarly structured Export Credit Facility for up to a maximum of $2.6 billion for Airbus aircraft to be delivered through May 31, 2005. The facility was subsequently increased to $3.6 billion and extended to include aircraft to be delivered through May 31, 2009. The facility becomes available as the various European Export Credit Agencies provide their guarantees for aircraft based on a forward-looking calendar, and the interest rate is determined through a bid process. The interest rates are either LIBOR based with spreads ranging from (0.04) percent to 0.02 percent or at fixed rates ranging from 4.2 percent to 4.7 percent. At September 30, 2008, ILFC had $2.0 billion outstanding under this facility. At September 30, 2008, the interest rate of the loans outstanding ranged from 2.83 percent to 4.71 percent. The debt is collateralized by a pledge of shares of a subsidiary of ILFC, which holds title to the aircraft financed under the facility. Borrowings with respect to these facilities are included in ILFC's notes and bonds payable in the preceding table of borrowings.

Under these Export Credit Facilities, ILFC may be required to segregate deposits and maintenance reserves for particular aircraft into separate accounts in connection with certain credit rating downgrades. As a result of Moody's October 3, 2008 downgrade of ILFC's long-term debt rating to Baa1, ILFC has received notice from the security trustee of the 2004 facility to segregate into separate accounts security deposits and maintenance reserves aggregating $148.8 million related to aircraft funded under the facility. ILFC has 90 days from the notice to comply. Further credit rating declines could impose additional restrictions under the Export Credit Facilities and make it more difficult for ILFC to borrow under the 2004 facility.

From time to time, ILFC enters into funded financing agreements. As of September 30, 2008, ILFC had a total of $1.1 billion outstanding, which has varying maturities through February 2012. The interest rates are LIBOR-based, with spreads ranging from 0.33 percent to 1.625 percent. At September 30, 2008, the interest rates ranged from 3.113 percent to 5.375 percent. AIG does not guarantee any of the debt obligations of ILFC.

AGF

In the current environment, AGF has not had access to its traditional sources of long-term or short-term financing through the public debt markets.

As of September 30, 2008, notes and bonds aggregating $24.1 billion were outstanding with maturity dates ranging from 2008 to 2031 at interest rates ranging from 1.46 percent to 9 percent. To the extent considered appropriate, AGF has entered into swap transactions to manage its effective borrowing rates with respect to these notes and bonds. AIG does not guarantee any of the debt obligations of AGF.

Revolving Credit Facilities

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

As previously discussed under Item 1A. Risk Factors — New Credit Facility, both ILFC and AGF have drawn the full amount available under their revolving credit facilities. AIG's syndicated facilities contain a covenant requiring AIG to maintain total shareholders' equity (calculated on a consolidated basis consistent with GAAP) of at least $50 billion at all times. If AIG fails to maintain this level of total shareholders' equity at any time, it will lose access to those facilities.

As of September 30, 2008 (in millions)

Facility	Size	Borrower(s)	Available Amount	Expiration	One-Year Term-Out Option
AIG:					
364-Day Syndicated Facility	$2,125	AIG/AIG Funding[(a)]	$2,125	July 2009	Yes
5-Year Syndicated Facility	1,625	AIG/AIG Funding[(a)]	1,625	July 2011	No
364-Day Bilateral Facility [(b)]	3,200	AIG/AIG Funding[(a)]	70	December 2008	Yes
Total AIG	$6,950		$3,820		
ILFC:					
5-Year Syndicated Facility	$2,500	ILFC	$ –	October 2011	No
5-Year Syndicated Facility	2,000	ILFC	–	October 2010	No
5-Year Syndicated Facility	2,000	ILFC	–	October 2009	No
Total ILFC	$6,500		$ –		
AGF:					
364-Day Syndicated Facility	$2,450	American General Finance Corporation American General Finance, Inc.[(c)]	$ –	July 2009	Yes
5-Year Syndicated Facility	2,125	American General Finance Corporation	–	July 2010	No
Total AGF	$4,575		$ –		

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

(b) This facility can be drawn in the form of loans or letters of credit. All drawn amounts shown above are in the form of letters of credit.

(c) American General Finance, Inc. was an eligible borrower for up to $400 million only.

Credit Ratings

The cost and availability of unsecured financing for AIG and its subsidiaries are generally dependent on their short-and long-term debt ratings. The following table presents the credit ratings of AIG and certain of its subsidiaries as of October 27, 2008. In parentheses, following the initial occurrence in the table of each rating, is an indication of that rating's relative rank within the agency's rating categories. That ranking refers only to the generic or major rating category and not to the modifiers appended to the rating by the rating agencies to denote relative position within such generic or major category.

	Short-term Debt			Senior Long-term Debt		
	Moody's	S&P	Fitch[j]	Moody's[a]	S&P[b]	*Fitch[c][j]*
AIG	P-1 (1st of 3)[g]	A-1 (1st of 6)[e]	F1 (1st of 5)	A3 (3rd of 9)[g]	A- (3rd of 8)[e]	A (3rd of 9)
AIG Financial Products Corp.[d]	P-1[g]	A-1[e]	–	A3[g]	A-[e]	–
AIG Funding, Inc.[d]	P-1[g]	A-1[e]	F1	–	–	–
ILFC	P-2 (2nd of 3)[h]	A-1[f]	F1	Baa1 (4th of 9)[h]	A-[f]	A
American General Finance Corporation	P-2[i]	A-3 (3rd of 6)	F1	Baa1[g]	BBB(4th of 8)[e]	A
American General Finance, Inc.	P-2[g]	A-3	F1	–	–	A

(a) Moody's appends numerical modifiers 1, 2 and 3 to the generic rating categories to show relative position within rating categories.
(b) S&P ratings may be modified by the addition of a plus or minus sign to show relative standing within the major rating categories.
(c) Fitch ratings may be modified by the addition of a plus or minus sign to show relative standing within the major rating categories.
(d) AIG guarantees all obligations of AIG Financial Products Corp. and AIG Funding, Inc.
(e) Credit Watch Negative.
(f) Credit Watch Developing.
(g) Under Review for Possible Downgrade.
(h) Under Review with Direction Uncertain.
(i) Negative Outlook.
(j) Rating Watch Evolving.

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

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

A significant portion of AIGFP's GIAs and financial derivative transactions include provisions that require AIGFP, upon a downgrade of AIG's long-term debt ratings, to post collateral or, with the consent of the counterparties, assign or repay its positions or arrange a substitute guarantee of its obligations by an obligor with higher debt ratings.

Furthermore, certain downgrades of AIG's long-term senior debt ratings would permit either AIG or the counterparties to elect early termination of contracts.

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

Contractual Obligations

Contractual obligations in total, and by remaining maturity at September 30, 2008 were as follows:

(in millions)	Total Payments	Payments due by Period: Less Than One Year	1-3 Years	3+-5 Years	More Than Five Years
Borrowings[(a)]	$ 150,132	$ 28,057	$ 36,207	$23,986	$ 61,882
Fed Facility	62,960	–	62,960	–	–
Interest payments on borrowings	76,692	5,556	11,535	9,131	50,470
Loss reserves[(b)]	90,877	24,991	27,717	13,178	24,991
Insurance and investment contract liabilities[(c)]	698,107	31,815	47,027	44,436	574,829
GIC liabilities[(d)]	23,998	10,432	3,951	3,467	6,148
Aircraft purchase commitments	16,902	735	3,155	3,180	9,832
Other long-term obligations	683	248	393	28	14
Total[(e)(f)]	$1,120,351	$101,834	$192,945	$97,406	$728,166

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

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

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

(d) Represents guaranteed maturities under GICs.

(e) Does not reflect unrecognized tax benefits of $2.5 billion, the timing of which is uncertain.

(f) The majority of AIGFP's credit default swaps require AIGFP to provide credit protection on a designated portfolio of loans or debt securities. At September 30, 2008, the fair value derivative liability was $30.2 billion relating to AIGFP's super senior multi-sector CDO credit default swap portfolio, net of amounts realized in extinguishing derivative obligations. However, AIG's credit-based stress testing scenarios illustrate potential pre-tax realized credit losses from these contracts at approximately $7.8 billion and approximately $12.0 billion at that date. Due to the long-term maturities of these credit default swaps, AIG is unable to make reasonable estimates of the periods during which any payments would be made.

Off Balance Sheet Arrangements and Commercial Commitments

Off balance sheet arrangements and commercial commitments in total, and by remaining maturity at September 30, 2008 were as follows:

(in millions)	Total Amounts Committed	Amount of Commitment Expiration: Less Than One Year	1-3 Years	3+-5 Years	More Than Five Years
Guarantees:					
Liquidity facilities[(a)]	$ 1,942	$ 8	$ 883	$ 813	$ 238
Standby letters of credit	1,698	1,483	45	28	142
Construction guarantees[(b)]	162	–	–	–	162
Guarantees of indebtedness	1,206	2	214	500	490
All other guarantees	617	52	54	13	498
Commitments:					
Investment commitments[(c)]	8,444	2,890	3,551	1,847	156
Commitments to extend credit	1,760	1,315	348	94	3
Letters of credit	1,229	959	120	–	150
Maturity shortening puts[(d)]	1,000	136	864	–	–
Other commercial commitments[(e)]	1,034	10	–	79	945
Total	$ 19,092	$ 6,855	$ 6,079	$ 3,374	$ 2,784

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

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

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

(d) Represents obligations under 2a-7 Puts to purchase certain multi-sector CDOs at pre-determined contractual prices.

(e) Includes options to acquire aircraft. Excludes commitments with respect to pension plans. The annual pension contribution for 2008 is expected to be approximately $654 million for U.S. and non-U.S. plans.

Arrangements with Variable Interest Entities and Structured Investment Vehicles

AIG enters into various off-balance-sheet (unconsolidated) arrangements with variable interest entities (VIEs) in the normal course of business. AIG's involvement with VIEs ranges from being a passive investor to designing and structuring, warehousing and managing the collateral of VIEs. AIG engages in transactions with VIEs as part of its investment activities to obtain funding and to facilitate client needs. AIG purchases debt securities (rated and unrated) and equity interests issued by VIEs, makes loans and provides other credit support to VIEs, enters into insurance, reinsurance and derivative transactions and leasing arrangements with VIEs, and acts as the warehouse agent and collateral manager for VIEs. Interest holders in the VIEs generally have recourse only to the assets and cash flows of the VIEs and do not have recourse to AIG, except when AIG has provided a guarantee to the VIEs' interest holders. AIGFP has written regulatory relief super senior credit default swaps on VIE's used by lenders to fund their corporate loan and residential mortgage loan portfolios.

Under FIN 46(R), AIG consolidates a VIE when it is the primary beneficiary of the entity. The primary beneficiary is the party that either (i) absorbs a majority of the VIE's expected losses; (ii) receives a majority of the VIEs' expected residual returns; or (iii) both. For a further discussion of AIG's involvement with VIEs, see Note 7 of Notes to Consolidated Financial Statements in the 2007 Annual Report on Form 10-K.

A significant portion of AIG's overall exposure to VIEs results from AIG Investment's real estate and investment funds.

In certain instances, AIG Investments acts as the collateral manager or general partner of an investment fund, private equity fund or hedge fund. Such entities are typically registered investment companies or qualify for the specialized investment company accounting in accordance with the AICPA Investment Company Audit and Accounting Guide. For investment partnerships, hedge funds and private equity funds, AIG acts as the general partner or manager of the fund and is responsible for carrying out the investment mandate of the VIE. Often, AIG's insurance operations participate in these AIG managed structures as a passive investor in the debt or equity issued by the VIE. Typically, AIG does not provide any guarantees to the investors in the VIE.

AIG's primary exposure to unconsolidated VIEs at September 30, 2008 consists of debt and equity investments of approximately $17 billion which are included in AIG's Total Investments and Financial Services assets on the consolidated balance sheet. AIG's total maximum exposure to loss on unconsolidated VIEs continued to decline as a result of the termination of certain of AIGFP's transactions and the effects of overall market deterioration. In addition, AIG has certain regulatory capital relief CDSs written by AIGFP with VIEs, including CDSs with VIEs where AIG also has a debt or equity interest. These regulatory capital relief CDSs continue to have a zero fair value and AIGFP's exposure is included in the total net notional amount of AIGFP's regulatory capital CDS portfolio of $250 billion. See Critical Accounting Estimates — AIGFP's Super Senior Credit Default Swap Portfolio — Regulatory Capital Portfolio.

Potential Amendment to FIN 46(R)

In September 2008, the FASB issued an exposure draft of an FAS that would amend FIN 46(R) to change the criteria for determining the primary beneficiary of a VIE. The primary beneficiary is the party that consolidates the VIE. The amendment would identify the party that has the ability to direct matters that most significantly affect the activities of the VIE as the primary beneficiary. The majority of AIG's involvement with VIE's results from being a passive investor. AIG is currently assessing the effect that adopting this potential amendment would have on its consolidated financial statements.

Shareholders' Equity

The changes in AIG's consolidated shareholders' equity were as follows:

(in millions)	Nine Months Ended September 30, 2008
Beginning of year	**$ 95,801**
Net income (loss)	**(37,630)**
Unrealized depreciation of investments, net of tax	**(13,383)**
Cumulative translation adjustment, net of tax	**(579)**
Dividends to shareholders	**(1,105)**
Payments advanced to purchase shares, net	**912**
Common share issuance	**7,343**
Consideration received for preferred stock not yet issued	**23,000**
Share purchases	**(1,912)**
Cumulative effect of accounting changes, net of tax	**(1,108)**
Other*	**(157)**
End of period	**$ 71,182**

* *Reflects the effects of employee stock transactions and the present value of future contract adjustment payments related to the issuance of Equity Units.*

New Share Issuance

In May 2008, AIG sold in a public offering 196,710,525 shares of its common stock at a price per share of $38. Concurrent with the common stock offering, AIG sold 78.4 million Equity Units at a price per unit of $75. The Equity Units consist of an ownership interest in AIG junior subordinated debentures and a stock purchase contract obligating the holder of an equity unit to purchase, and obligating AIG to sell, on each of February 15, 2011, May 1, 2011 and August 1, 2011, for a price of $25, a variable number of shares of AIG common stock, that is not less than 0.54823 shares and not more than 0.6579 shares, subject to anti-dilution adjustments. Accordingly, a maximum number of 154,738,080 shares and a

minimum number of 128,944,480 shares of AIG common stock will be issued in the year 2011 under the stock purchase contracts, subject to anti-dilution adjustments.

On May 7, 2008, AIG's Board of Directors declared a quarterly cash dividend on the common stock of $0.22 per share, that was paid on September 19, 2008 to shareholders of record on September 5, 2008. Effective September 23, 2008, AIG's Board of Directors suspended the declaration of dividends on AIG's common stock. Pursuant to the Fed Credit Agreement, AIG is restricted from paying dividends on its common stock.

See Note 5 to the Consolidated Financial Statements.

Share Repurchases

In February 2007, AIG's Board of Directors increased AIG's share repurchase program by authorizing the purchase of shares with an aggregate purchase price of $8 billion. In November 2007, AIG's Board of Directors authorized the purchase of an additional $8 billion in common stock. In 2007, AIG entered into structured share repurchase arrangements providing for the purchase of shares over time with an aggregate purchase price of $7 billion.

A total of 37,926,059 shares were purchased during the nine-month period ended September 30, 2008 to meet commitments that existed at December 31, 2007. All shares purchased are recorded as treasury stock at cost.

At October 27, 2008, $9 billion was available for purchases under the aggregate authorization. Pursuant to the Fed Credit Agreement, AIG is restricted from repurchasing shares of its common stock.

Invested Assets

The following tables summarize the composition of AIG's invested assets by segment:

(in millions)	General Insurance	Life Insurance & Retirement Services	Financial Services	Asset Management	Other	Total
September 30, 2008						
Fixed maturity securities:						
Bonds available for sale, at fair value	$ 89,555	$284,886	$ 1,199	$18,854	$ —	$394,494
Bond trading securities, at fair value	—	7,545	—	7	—	7,552
Equity securities:						
Common stocks available for sale, at fair value	3,028	7,793	2	654	(18)	11,459
Common and preferred stocks trading, at fair value	228	20,421	—	25	—	20,674
Preferred stocks available for sale, at fair value	1,111	348	5	—	—	1,464
Mortgage and other loans receivable, net of allowance	16	25,937	621	7,114	36	33,724
Financial Services assets:						
Flight equipment primarily under operating leases, net of accumulated depreciation	—	—	43,561	—	—	43,561
Securities available for sale, at fair value	—	—	2,326	—	—	2,326
Trading securities, at fair value	—	—	36,136	—	—	36,136
Spot commodities, at fair value	—	—	34	—	—	34
Unrealized gain on swaps, options and forward transactions, at fair value	—	—	11,663	—	(1,629)	10,034
Trade receivables	—	—	4,617	—	—	4,617
Securities purchased under agreements to resell, at fair value	—	—	12,100	—	—	12,100
Finance receivables, net of allowance	—	5	32,585	—	—	32,590
Securities lending invested collateral, at fair value	2,910	35,176	—	3,425	—	41,511
Other invested assets	12,341	19,670	2,756	16,042	7,914	58,723
Short-term investments	9,687	27,119	8,846	5,595	1,237	52,484
Total Investments and Financial Services assets as shown on the balance sheet	118,876	428,900	156,451	51,716	7,540	763,483
Cash	1,743	5,324	9,795	545	1,163	18,570
Investment income due and accrued	1,376	5,322	29	282	(1)	7,008
Real estate, net of accumulated depreciation	306	926	34	87	225	1,578
Total invested assets*	$122,301	$440,472	$166,309	$52,630	$ 8,927	$790,639

**At September 30, 2008, approximately 62 percent and 38 percent of invested assets were held in domestic and foreign investments, respectively.*

(in millions)	General Insurance	Life Insurance & Retirement Services	Financial Services	Asset Management	Other	Total
December 31, 2007						
Fixed maturity securities:						
Bonds available for sale, at fair value	$ 74,057	$294,162	$ 1,400	$27,753	$ —	$397,372
Bonds held to maturity, at amortized cost	21,355	1	—	225	—	21,581
Bond trading securities, at fair value	—	9,948	—	34	—	9,982
Equity securities:						
Common stocks available for sale, at fair value	5,599	11,616	—	609	76	17,900
Common and preferred stocks trading, at fair value	321	21,026	—	29	—	21,376
Preferred stocks available for sale, at fair value	1,885	477	8	—	—	2,370
Mortgage and other loans receivable, net of allowance	13	24,851	1,365	7,442	56	33,727
Financial Services assets:						
Flight equipment primarily under operating leases, net of accumulated depreciation	—	—	41,984	—	—	41,984
Securities available for sale, at fair value	—	—	40,305	—	—	40,305
Trading securities, at fair value	—	—	4,197	—	—	4,197
Spot commodities	—	—	238	—	—	238
Unrealized gain on swaps, options and forward transactions, at fair value	—	—	13,010	—	(692)	12,318
Trade receivables	—	—	672	—	—	672
Securities purchased under agreements to resell, at contract value	—	—	20,950	—	—	20,950
Finance receivables, net of allowance	—	5	31,229	—	—	31,234
Securities lending invested collateral, at fair value	5,031	57,471	148	13,012	—	75,662
Other invested assets	11,895	19,015	3,663	17,261	6,989	58,823
Short-term investments	7,356	25,236	12,249	4,919	1,591	51,351
Total Investments and Financial Services assets as shown on the balance sheet	127,512	463,808	171,418	71,284	8,020	842,042
Cash	497	1,000	389	269	129	2,284
Investment income due and accrued	1,431	4,728	29	401	(2)	6,587
Real estate, net of accumulated depreciation	349	976	17	89	231	1,662
Total invested assets*	$129,789	$470,512	$171,853	$72,043	$8,378	$852,575

**At December 31, 2007, approximately 65 percent and 35 percent of invested assets were held in domestic and foreign investments, respectively.*

Investment Strategy

AIG's investment strategies are tailored to the specific business needs of each operating unit. The investment objectives are driven by the business model for each of the businesses: General Insurance, Life Insurance, Retirement Services and Asset Management's Spread-Based Investment business. The primary objectives are liquidity, preservation of capital, growth of surplus and generation of investment income to support the insurance products. Difficult market conditions in recent quarters have significantly hindered AIG's ability to achieve these objectives, and these challenges are expected to persist for the foreseeable future.

At the local operating unit level, investment strategies are based on considerations that include the local market, liability duration and cash flow characteristics, rating agency and regulatory capital considerations, legal investment limitations, tax optimization and diversification.

The majority of assets backing insurance liabilities at AIG consist of intermediate and long duration fixed maturity securities. In the case of Life Insurance & Retirement Services companies, as well as in the GIC and MIP portfolios of the Asset Management segment, the fundamental investment strategy is, as nearly as is practicable, to match the duration characteristics of the liabilities with comparable duration assets. Fixed maturity securities held by the insurance companies included in the AIG Property Casualty Group historically have consisted primarily of laddered holdings of tax-exempt municipal bonds, which provided attractive after-tax returns and limited credit risk. In light of AIG's net operating position, AIG changed its intent to hold to maturity certain tax-exempt municipal securities held by its insurance subsidiaries. Fixed maturity securities held by Foreign General Insurance companies consist primarily of intermediate duration high grade securities.

The market price of fixed maturity securities reflects numerous components, including interest rate environment, credit spread, embedded optionality (such as call features), liquidity, structural complexity, foreign exchange risk, and

other credit and non-credit factors. However, in most circumstances, pricing is most sensitive to interest rates, such that the market price declines as interest rates rise, and increases as interest rates fall. This effect is more pronounced for longer duration securities.

AIG marks to market the vast majority of the invested assets held by its insurance companies pursuant to FAS 115, "Accounting for Certain Investments in Debt and Equity Securities," and related accounting pronouncements. However, with limited exceptions (primarily with respect to separate account products consolidated on AIG's balance sheet pursuant to SOP 03-01), AIG does not mark to market its insurance liabilities for changes in interest rates, even though rising interest rates have the effect of reducing the fair value of such liabilities, and falling interest rates have the opposite effect. This results in the recording of changes in unrealized gains (losses) on securities in Accumulated other comprehensive income resulting from changes in interest rates without any correlative, inverse changes in gains (losses) on AIG's liabilities. Because AIG's asset duration in certain low-yield currencies, particularly Japan and Taiwan, is shorter than its liability duration, AIG views increasing interest rates in these countries as economically advantageous, notwithstanding the effect that higher rates have on the market value of its fixed maturity portfolio.

The majority of AIG's non-floating rate fixed maturity portfolio is held to support intermediate and long duration liabilities. Assuming no other changes in factors affecting the valuation of fixed maturity securities, each 10 basis point (1/10 of 1 percent) increase in interest rates results in a decline of approximately $2.2 billion in the pre-tax fair value of the fixed maturity portfolio. In most jurisdictions in which AIG operates, including the United States, such interest rate related changes in portfolio value are ignored for purposes of measuring regulatory capital adequacy.

The amortized cost or cost and fair value of AIG's available for sale and held to maturity securities were as follows:

	September 30, 2008				December 31, 2007			
(in millions)	Amortized Cost or Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value	Amortized Cost or Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Bonds — available for sale:[a]								
U.S. government and government sponsored entities	**$ 4,689**	**$ 162**	**$ (63)**	**$ 4,788**	$ 7,956	$ 333	$ (37)	$ 8,252
Obligations of states, municipalities and political subdivisions	**66,491**	**506**	**(3,278)**	**63,719**	46,087	927	(160)	46,854
Non-U.S. governments	**70,554**	**4,140**	**(1,610)**	**73,084**	67,023	3,920	(743)	70,200
Corporate debt	**213,588**	**3,020**	**(14,421)[b]**	**202,187**	239,822	6,216	(4,518)	241,520
Mortgage-backed, asset-backed and collateralized	**95,712**	**916**	**(7,823)**	**88,805**	140,982	1,221	(7,703)	134,500
Total bonds	**$451,034**	**$ 8,744**	**$(27,195)**	**$432,583**	$501,870	$12,617	$(13,161)	$501,326
Equity securities	**12,945**	**1,526**	**(1,548)**	**12,923**	15,188	5,545	(463)	20,270
Total	**$463,979**	**$10,270**	**$(28,743)**	**$445,506**	$517,058	$18,162	$(13,624)	$521,596
Held to maturity:[c]	**$ –**	**$ –**	**$ –**	**$ –**	$ 21,581	$ 609	$ (33)	$ 22,157

(a) At December 31, 2007, included AIGFP available for sale securities with a fair value of $39.3 billion, for which AIGFP elected the fair value option effective January 1, 2008, consisting primarily of corporate debt, mortgage-backed, asset-backed and collateralized securities. At September 30, 2008, the fair value of these securities were $33.6 billion. At September 30, 2008 and December 31, 2007, fixed maturities held by AIG that were below investment grade or not rated totaled $20.5 billion and $27.0 billion, respectively. During the third quarter of 2008, AIG changed its intent to hold until maturity certain tax-exempt municipal securities held by its insurance subsidiaries. As a result, all securities previously classified as held to maturity are now classified in the available for sale category. See Note 1 to the Consolidated Financial Statements for additional information.

(b) Financial institutions represent approximately 54 percent of the total gross unrealized losses at September 30, 2008.

(c) Represents obligations of states, municipalities and political subdivisions.

At September 30, 2008, approximately 54 percent of the fixed maturity securities were held by domestic entities. Approximately 38 percent of such domestic securities were rated AAA by one or more of the principal rating agencies. Approximately five percent were below investment grade or not rated. AIG's investment decision process relies primarily on internally generated fundamental analysis and internal risk ratings. Third-party rating services' ratings and opinions provide one source of independent perspectives for consideration in the internal analysis. A significant portion of the foreign fixed maturity portfolio is rated by Moody's, S&P or similar foreign rating services. Rating services are not available in all overseas locations. AIG's Credit Risk Committee closely reviews the credit quality of the foreign portfolio's non-rated fixed maturity securities. At September 30, 2008, approximately 18 percent of the foreign fixed maturity securities were either rated AAA or, on the basis of AIG's internal analysis, were equivalent from a credit standpoint to securities so rated. Approximately three percent were below investment grade or not rated at that date. Approximately one third of the foreign

fixed maturity portfolio is sovereign fixed maturity securities supporting policy liabilities in the country of issuance.

The credit ratings of AIG's fixed maturity securities, other than those of AIGFP, were as follows:

	September 30, 2008	December 31, 2007
Rating		
AAA	**29%**	38%
AA	**29**	28
A	**23**	18
BBB	**14**	11
Below investment grade	**4**	4
Non-rated	**1**	1
Total	**100%**	100%

The industry categories of AIG's available for sale corporate debt securities, other than those of AIGFP, were as follows:

Industry Category	**September 30, 2008**	December 31, 2007
Financial institutions:		
Money Center / Global Bank Groups	**17%**	16%
Regional banks — other	**6**	6
Life insurance	**5**	5
Securities firms and other finance companies	**4**	6
Insurance non-life	**3**	2
Regional banks — North America	**3**	4
Other financial institutions	**3**	3
Utilities	**12**	11
Communications	**8**	8
Consumer noncyclical	**7**	7
Capital goods	**6**	6
Consumer cyclical	**5**	5
Energy	**5**	4
Other	**16**	17
Total*	**100%**	100%

** At both September 30, 2008 and December 31, 2007, approximately 95 percent of these investments were rated investment grade.*

Investments in RMBS, CMBS, CDOs and ABS

The amortized cost, gross unrealized gains (losses) and fair value of AIG's investments in RMBS, CMBS, CDOs and ABS were as follows:

	September 30, 2008				December 31, 2007			
(in millions)	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Bonds — available for sale:								
AIG, excluding AIGFP:								
RMBS	**$64,733**	**$620**	**$(3,745)**	**$61,608**	$ 89,851	$ 433	$(5,504)	$ 84,780
CMBS	**20,021**	**187**	**(2,657)**	**17,551**	23,918	237	(1,156)	22,999
CDO/ABS	**9,609**	**96**	**(1,230)**	**8,475**	10,844	196	(593)	10,447
Subtotal, excluding AIGFP	**94,363**	**903**	**(7,632)**	**87,634**	124,613	866	(7,253)	118,226
AIGFP*	**1,349**	**13**	**(191)**	**1,171**	16,369	355	(450)	16,274
Total	**$95,712**	**$916**	**$(7,823)**	**$88,805**	$140,982	$1,221	$(7,703)	$134,500

**The December 31, 2007 amounts represent total AIGFP investments in mortgage-backed, asset-backed and collateralized securities for which AIGFP has elected the fair value option effective January 1, 2008. At September 30, 2008, the fair value of these securities were $20.2 billion. The September 30, 2008 amounts represent securities for which AIGFP has not elected the fair value option. An additional $1.6 billion related to insurance company investments is included in Bonds — trading.*

Investments in RMBS

The amortized cost, gross unrealized gains (losses) and fair value of AIG's investments in RMBS securities, other than those of AIGFP, were as follows:

	September 30, 2008					December 31, 2007				
(in millions)	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value	Percent of Total	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value	Percent of Total
RMBS:										
U.S. agencies	**$17,419**	**$255**	**$ (170)**	**$17,504**	**28%**	$14,575	$320	$ (70)	$14,825	17%
Prime non-agency[(a)]	**15,698**	**41**	**(2,019)**	**13,720**	**22**	21,552	72	(550)	21,074	25
Alt-A	**14,984**	**177**	**(1,197)**	**13,964**	**23**	25,349	17	(1,620)	23,746	28
Other housing-related[(b)]	**2,111**	**37**	**(93)**	**2,055**	**3**	4,301	2	(357)	3,946	5
Subprime	**14,521**	**110**	**(266)**	**14,365**	**24**	24,074	22	(2,907)	21,189	25
Total	**$64,733**	**$620**	**$(3,745)**	**$61,608**	**100%**	$89,851	$433	$(5,504)	$84,780	100%

(a) Includes foreign and jumbo RMBS-related securities.
(b) Primarily wrapped second-lien.

AIG's operations, other than AIGFP, held investments in RMBS with an estimated fair value of $61.6 billion at September 30, 2008, or approximately 8 percent of AIG's total invested assets. In addition, AIG's insurance operations held investments with a fair value totaling $8.5 billion in CDOs/ABS, of which $27 million included some level of subprime exposure. AIG's RMBS investments are predominantly in highly-rated tranches that contain substantial protection features through collateral subordination. At September 30, 2008, approximately 82 percent of these investments were rated AAA, and approximately 9 percent were rated AA by one or more of the principal rating agencies. AIG's investments rated BBB or below totaled $3.3 billion, or less than 0.5 percent of AIG's total invested assets at September 30, 2008. As of October 27, 2008, $14.8 billion of AIG's RMBS backed primarily by subprime collateral had been downgraded as a result of rating agency actions since January 1, 2008, and $184 million of such investments had been upgraded. Of the downgrades, $13.9 billion were AAA rated securities. In addition to the downgrades, as of October 27, 2008, the rating agencies had $5.7 billion of RMBS on watch for downgrade.

The amortized cost of AIG's RMBS investments, other than those of AIGFP, at September 30, 2008 by year of vintage and credit rating were as follows:

	Year of Vintage						
(in billions)	Prior	2004	2005	2006	2007	**2008**	Total
Rating:							
Total RMBS							
AAA	$8,479	$5,528	$10,471	$13,591	$11,460	**$3,785**	$53,314
AA	975	555	1,066	2,380	1,135	**–**	6,111
A	215	230	304	1,037	185	**69**	2,040
BBB and below	98	218	301	1,450	1,178	**23**	3,268
Total RMBS	$9,767	$6,531	$12,142	$18,458	$13,958	**$3,877**	$64,733
Alt-A RMBS							
AAA	$ 736	$ 763	$ 2,929	$ 4,150	$ 3,646	**$ –**	$12,224
AA	242	106	221	628	311	**–**	1,508
A	25	33	99	506	18	**–**	681
BBB and below	10	22	50	363	126	**–**	571
Total Alt-A	$1,013	$ 924	$ 3,299	$ 5,647	$ 4,101	**$ –**	$14,984
Subprime RMBS							
AAA	$ 381	$ 336	$ 3,261	$ 4,307	$ 2,217	**$ –**	$10,502
AA	122	96	289	1,152	235	**–**	1,894
A	72	50	51	425	117	**–**	715
BBB and below	2	67	63	722	556	**–**	1,410
Total Subprime	$ 577	$ 549	$ 3,664	$ 6,606	$ 3,125	**$ –**	$14,521

AIG's underwriting practices for investing in RMBS, other ABS and CDOs take into consideration the quality of the originator, the manager, the servicer, security credit ratings, underlying characteristics of the mortgages, borrower characteristics, and the level of credit enhancement in the transaction. AIG's strategy is typically to invest in securities rated AA or better and create diversification across multiple underlying asset classes.

Investments in CMBS

The amortized cost of AIG's CMBS investments, other than those of AIGFP, at September 30, 2008 was as follows:

(in millions)	Amortized Cost	Percent of Total
CMBS (traditional)	$18,263	91%
ReRemic/CRE CDO	1,164	6
Agency	202	1
Other	392	2
Total	$20,021	100%

The percentage of AIG's CMBS investments, other than those of AIGFP, at September 30, 2008 by credit rating was as follows:

	Percentage
Rating:	
AAA	79%
AA	12
A	7
BBB and below	2
Total	100%

The percentage of AIG's CMBS investments, other than those of AIGFP, by year of vintage at September 30, 2008 was as follows:

	Percentage
Year:	
2008	1%
2007	24
2006	14
2005	19
2004	17
2003 and prior	25
Total	100%

The percentage of AIG's CMBS investments, other than those of AIGFP, by geographic region at September 30, 2008 was as follows:

	Percentage
Geographic region:	
New York	17%
California	13
Texas	7
Florida	6
Virginia	3
Illinois	3
New Jersey	3
Pennsylvania	3
Maryland	3
Georgia	2
All Other	40
Total	100%

At September 30, 2008, AIG held $20 billion in cost basis of CMBS. Approximately 79 percent of such holdings were rated AAA, approximately 19 percent were rated AA or A, and approximately 2 percent were rated BBB or below at September 30, 2008.

There have been disruptions in the commercial mortgage markets in general, and the CMBS market in particular, with credit default swaps indices and quoted prices of securities at levels consistent with a severe correction in lease rates, occupancy and fair value of properties. In addition, spreads in the primary mortgage market have widened significantly.

Pricing of CMBS has been adversely affected by market perceptions that underlying mortgage defaults will increase. As a result, AIG recognized $474 million of other-than-temporary impairment charges in the three-month period ended September 30, 2008 on CMBS valued at a severe discount to cost, despite the absence of any deterioration in performance of the underlying credits, because AIG concluded that it could not reasonably assert that the impairment period was temporary. At this time, AIG anticipates substantial recovery of principal and interest on the securities to which such other-than-temporary impairment charges were recorded. In addition, AIG recognized $485 million in other-than-temporary impairment charges due to the change in intent to hold these CMBS until they recover in value.

Investments in CDOs

The amortized cost of AIG's CDO investments, other than those of AIGFP, by collateral type at September 30, 2008 was as follows:

(in millions)	Amortized Cost	Percent of Total
Collateral Type:		
Bank loans (CLO)	$2,111	58%
Synthetic investment grade	878	24
Other	633	17
Subprime ABS	34	1
Total	$3,656	100%

Amortized cost of the AIG's CDO investments, other than those of AIGFP, by credit rating at September 30, 2008 was as follows:

(in millions)	Amortized Cost	Percent of Total
Rating:		
AAA	$ 748	20%
AA	613	17
A	1,926	53
BBB	285	8
Below investment grade and equity	84	2
Total	$3,656	100%

Commercial Mortgage Loan Exposure

At September 30, 2008, AIG had direct commercial mortgage loan exposure of $17.2 billion, with $15.8 billion representing

U.S. loan exposure. At that date, substantially all of the U.S. loans were current. Foreign commercial mortgage loans are secured predominantly by properties in Japan. In addition, at September 30, 2008, AIG had $2.3 billion in residential mortgage loans in jurisdictions outside the United States, primarily backed by properties in Taiwan and Thailand.

AIGFP Trading Investments

The fair value of AIGFP's trading investments at September 30, 2008 was as follows:

(In millions)	Fair Value	Percent of Total
U.S. government and government sponsored entities	$ 8,000	24%
Non-U.S. governments	472	1
Corporate debt	4,993	15
Mortgage-backed, asset- backed and collateralized	20,175	60
Total	$33,640	100%

The credit ratings of AIGFP's trading investments at September 30, 2008 were as follows:

Rating	Percentage
AAA	70%
AA	10
A	18
BBB	2
Total	100%

The fair value of AIGFP's trading investments in RMBS, CDO, ABS and other collateralized securities at September 30, 2008 was as follows:

(In millions)	Fair Value	Percent of Total
RMBS	$ 4,272	21%
CMBS	4,703	23
CDO/ABS and collateralized	11,200	56
Total	$20,175	100%

Securities Lending Activities

AIG's securities lending program historically operated as centrally managed by AIG Investments for the benefit of certain of AIG's insurance companies. Under this program, securities are loaned to various financial institutions, primarily major banks and brokerage firms. Cash collateral is received and is invested in fixed maturity securities to earn a net spread. Historically, AIG had received cash collateral from borrowers between 100-102 percent of the value of the loaned securities. The amount of cash advanced by borrowers has been declining, in light of the availability of alternative transactions requiring less collateral. If amounts received are insufficient to fund substantially all of the cost of purchasing identical replacements for the loaned securities, these transactions will cease to be accounted for as secured borrowings and will instead be accounted for as sales and forward purchases.

AIG's liability to the borrowers for collateral received was $42.8 billion and the fair value of the collateral reinvested was $41.5 billion as of September 30, 2008. In addition to the invested collateral, the securities on loan as well as all of the assets of the lending companies are generally available to satisfy the liability for collateral received.

A significant portion of the collateral received was invested in RMBS with cash flows with tenors longer than the liabilities to the counterparties. The value of those collateral securities declined over the last 12 months and trading in such securities has been extremely limited. Given these events, AIG began increasing liquidity in the collateral accounts by increasing the amount of cash and overnight investments that comprise the securities lending invested collateral in the third quarter of 2007.

The composition of the securities lending invested collateral by credit rating at September 30, 2008 was as follows:

(in millions)	AAA	AA	A	BBB/Not Rated	Short-Term	Total
Corporate debt	$ 472	$3,232	$2,508	$ 305	$ –	$ 6,517
Mortgage-backed, asset-backed and collateralized	21,660	4,036	1,140	2,410	–	29,246
Cash and short-term investments	–	–	–	–	5,748	5,748
Total	$22,132	$7,268	$3,648	$2,715	$5,748	$41,511

Participation in the securities lending program by reporting unit at September 30, 2008 was as follows:

	Percent Participation
Domestic Life Insurance and Domestic Retirement Services	73%
Foreign Life Insurance	13
AIG Property Casualty Group	2
Foreign General Insurance	5
Asset Management	7
Total	100%

Due to AIG-specific credit concerns and systemic issues in the financial markets in the third quarter, counterparties began curtailing their participation in the program by returning lent securities and requiring the return of cash collateral. As a result, the collateral pools did not have sufficient liquidity to satisfy these obligations. As of September 30, 2008, AIG had borrowed approximately $11.5 billion under the Fed Facility to provide liquidity to the securities lending program. As the funding from the Fed Facility and other available cash was used to satisfy liabilities to borrowers rather than sales of securities lending invested collateral, the liabilities declined more significantly than the invested collateral.

The recognition of other-than-temporary impairment charges for the securities lending collateral investments placed significant stress on the statutory surplus of the participating insurance companies. During the third quarter of 2008, AIG recognized other-than-temporary impairment charges of $11.7 billion related to these investments, including $6.9 billion of charges related to AIG's change in intent to hold these securities to maturity as it winds this program down. During the three months ended September 30, 2008, AIG contributed $14.9 billion to certain of its domestic life and retirement services subsidiaries, largely related to these charges.

On October 8, 2008, certain of AIG's domestic life insurance subsidiaries entered into the Fed Securities Lending Agreement, providing that the NY Fed will borrow, on an overnight basis on commercial terms and conditions, investment grade fixed income securities from these AIG subsidiaries in return for cash collateral. Prior to this arrangement, draw downs under the existing Fed Facility were used, in part, to settle securities lending transactions. AIG understands that the NY Fed is prepared to borrow securities to extend AIG's currently outstanding lending obligations when those obligations are not rolled over or replaced by transactions with other private market participants. These securities borrowings by the NY Fed will allow AIG to replenish liquidity to the securities lending program on an as-needed basis, while providing the NY Fed with a perfected security interest in these third party securities.

As of November 5, 2008, the total value of securities lending payables amounted to $34.2 billion, with $19.9 billion of this amount payable to the NY Fed under this agreement.

AIG and the NY Fed expect to establish a limited liability company to hold RMBS securities in the domestic securities lending program and to terminate the Fed Securities Lending Agreement and AIG's U.S. securities lending program. See Note 11 to the Consolidated Financial Statements.

Portfolio Review

Other-Than-Temporary Impairments

AIG assesses its ability to hold any fixed maturity security in an unrealized loss position to its recovery, including fixed maturity securities classified as available for sale, at each balance sheet date. The decision to sell any such fixed maturity security classified as available for sale reflects the judgment of AIG's management that the security sold is unlikely to provide, on a relative value basis, as attractive a return in the future as alternative securities entailing comparable risks. With respect to distressed securities, the sale decision reflects management's judgment that the risk-discounted anticipated ultimate recovery is less than the value achievable on sale.

AIG evaluates its investments for impairments in valuation as well as credit. The determination that a security has incurred an other-than-temporary decline in value requires the judgment of management and consideration of the fundamental condition of the issuer, its near-term prospects and all the relevant facts and circumstances. See Critical Accounting Estimates — Other-Than-Temporary Impairments herein for further information on AIG's policy.

Once a security has been identified as other-than-temporarily impaired, the amount of such impairment is determined by reference to that security's contemporaneous fair value and recorded as a charge to earnings.

As a result of AIG's periodic evaluation of its securities for other-than-temporary impairments in value, AIG recorded other-than-temporary impairment charges of $19.9 billion and $544 million in the three-month periods ended September 30, 2008 and 2007, respectively, and $32.2 billion

and $1.4 billion in the nine-month periods ended September 30, 2008 and 2007, respectively.

In light of the recent significant disruption in the U.S. residential mortgage and credit markets, AIG has recognized an other-than-temporary impairment charge (severity loss) of $7.3 billion and $16.3 billion in the three- and nine-month periods ended September 30, 2008, primarily related to certain RMBS, other structured securities and securities of financial institutions. Notwithstanding AIG's intent and ability to hold such securities indefinitely (except for securities lending invested collateral comprising $3.4 billion and $9.2 billion of the severity loss for the three- and nine-month periods ended September 30, 2008), and despite structures that indicate that a substantial amount of the securities should continue to perform in accordance with original terms, AIG concluded that it could not reasonably assert that the impairment period would be temporary.

In addition to the above severity losses, AIG recorded other-than-temporary impairment charges in the three- and nine-month periods ended September 30, 2008 and 2007 related to:

- securities that AIG does not intend to hold until recovery;
- declines due to foreign exchange rates;
- issuer-specific credit events;
- certain structured securities impaired under Emerging Issues Task Force Issue No. 99-20, "Recognition of Interest Income and Impairment on Purchased Beneficial Interests and Beneficial Interests that Continue to be Held by a Transferor in Securitized Financial Assets"; and
- other impairments, including equity securities and partnership investments.

Other-than-temporary impairment charges by reporting segment were as follows:

(in millions)	General Insurance	Life Insurance & Retirement Services	Financial Services	Asset Management	Other	Total
Three months ended September 30, 2008						
Impairment Type:						
Severity	**$ 649**	**$ 5,530**	**$ 15**	**$ 1,133**	**$ –**	**$ 7,327**
Trading at 25 percent or more discount for nine consecutive months	–	–	–	–	–	–
Lack of intent to hold to recovery	**271**	**7,462**	**6**	**560**	–	**8,299**
Foreign currency declines	**–**	**50**	–	–		**50**
Issuer-specific credit events	**908**	**2,222**	**2**	**194**	**127**	**3,453**
Adverse projected cash flows on structured securities	–	**650**	**4**	**93**	–	**747**
Total	**$ 1,828**	**$15,914**	**$ 27**	**$ 1,980**	**$ 127**	**$19,876**
Three months ended September 30, 2007						
Impairment Type:						
Severity	$ –	$ –	$ –	$ –	$ –	$ –
Trading at 25 percent or more discount for nine consecutive months	–	–	–	–	–	–
Lack of intent to hold to recovery	1	183	1	34	21	240
Foreign currency declines		29	–	–	–	29
Issuer-specific credit events	34	82	–	8	–	124
Adverse projected cash flows on structured securities	–	55	–	96	–	151
Total	$ 35	$ 349	$ 1	$ 138	$ 21	$ 544
Nine months ended September 30, 2008						
Impairment Type:						
Severity	**$ 1,394**	**$12,060**	**$ 42**	**$ 2,778**	**$ 1**	**$16,275**
Trading at 25 percent or more discount for nine consecutive months	–	–	–	–	–	–
Lack of intent to hold to recovery	**292**	**8,390**	**8**	**630**	–	**9,320**
Foreign currency declines	–	**1,084**	–	–	–	**1,084**
Issuer-specific credit events	**975**	**2,610**	**2**	**232**	**127**	**3,946**
Adverse projected cash flows on structured securities	**7**	**1,355**	**4**	**255**	–	**1,621**
Total	**$ 2,668**	**$25,499**	**$ 56**	**$ 3,895**	**$ 128**	**$32,246**
Nine months ended September 30, 2007						
Impairment Type:						
Severity	$ –	$ –	$ –	$ –	$ –	$ –
Trading at 25 percent or more discount for nine consecutive months	–	6	–	–	–	6
Lack of intent to hold to recovery	73	481	3	36	21	614
Foreign currency declines	–	333	–	–	–	333
Issuer-specific credit events	92	183	–	35	6	316
Adverse projected cash flows on structured securities	–	62	–	97	–	159
Total	$ 165	$ 1,065	$ 3	$ 168	$ 27	$ 1,428

Financial institutions industry other-than-temporary impairment charges by industry classification were as follows:

(in millions)	Severity	Lack of Intent to Hold to Recovery	Issuer-Specific Credit Events	Total
Three months ended September 30, 2008				
Industry Classification:				
Banking	$ 719	$1,032	$ 399	$2,150
Brokerage	152	172	1,324	1,648
Insurance	9	79	56	144
Other	153	95	87	335
Total	$1,033	$1,378	$1,866	$4,277
Nine months ended September 30, 2008				
Industry Classification:				
Banking	$ 734	$1,086	$ 405	$2,225
Brokerage	193	172	1,330	1,695
Insurance	14	85	61	160
Other	245	223	125	593
Total	$1,186	$1,566	$1,921	$4,673

Other-than-temporary severity-related impairment charges for the three- and nine-month periods ended September 30, 2008 by type of security and credit rating were as follows:

Rating: *(in millions)*	RMBS	CDO	CMBS	Financial Institutions	Other Securities	Total
Three months ended September 30, 2008						
Fixed Maturities:						
AAA	**$ 3,005**	**$ 37**	**$ 150**	**$ 18**	**$ 71**	**$ 3,281**
AA	**949**	**168**	**96**	**48**	**–**	**1,261**
A	**335**	**189**	**154**	**589**	**20**	**1,287**
BBB and below	**326**	**105**	**75**	**141**	**38**	**685**
Nonrated	**–**	**–**	**–**	**–**	**12**	**12**
Equities	**–**	**–**	**–**	**237**	**564**	**801**
Total	**$ 4,615**	**$499**	**$ 475**	**$1,033**	**$ 705**	**$ 7,327**
Nine months ended September 30, 2008*						
Fixed Maturities:						
AAA	**$ 7,465**	**$ 59**	**$ 373**	**$ 18**	**$ 83**	**$ 7,998**
AA	**2,505**	**209**	**167**	**48**	**1**	**2,930**
A	**817**	**244**	**639**	**593**	**20**	**2,313**
BBB and below	**1,076**	**144**	**200**	**144**	**55**	**1,619**
Nonrated	**–**	**–**	**–**	**–**	**29**	**29**
Equities	**–**	**–**	**–**	**383**	**1,003**	**1,386**
Total	**$11,863**	**$656**	**$1,379**	**$1,186**	**$1,191**	**$16,275**

** Ratings are as of the date of the impairment charge.*

No other-than-temporary impairment charge with respect to any one single counterparty was significant to AIG's consolidated financial condition or results of operations, and no individual other-than-temporary impairment charge exceeded five percent of the consolidated net loss in the nine-month period ended September 30, 2008.

In periods subsequent to the recognition of an other-than-temporary impairment charge for fixed maturity securities that is not credit or foreign exchange related, AIG generally accretes into income the discount or amortizes the reduced premium resulting from the reduction in cost basis over the remaining life of the security. The amount of accretion recognized in earnings for the three- and nine-month periods ended September 30, 2008 was $196 million and $283 million, respectively.

An aging of the pre-tax unrealized losses of fixed maturity and equity securities, distributed as a percentage of cost relative to unrealized loss (the extent by which the fair value is less than amortized cost or cost), including the number of respective items, at September 30, 2008 was as follows:

	Less than or equal to 20% of Cost[b]			Greater than 20% to 50% of Cost[b]			Greater than 50% of Cost[b]			Total		
Aging[a] *(dollars in millions)*	Cost[c]	Unrealized Loss	Items	Cost[c]	Unrealized Loss	Items	Cost[c]	Unrealized Loss	Items	Cost[c]	Unrealized Loss[d]	Items
Investment grade bonds												
0-6 months	$160,907	$ 7,575	21,711	$ 3,722	$ 1,620	660	$–	$–	–	$164,629	$ 9,195	22,371
7-12 months	41,320	4,056	12,637	5,960	1,926	4,827	–	–	–	47,280	5,982	17,464
>12 months	55,073	5,624	8,205	17,160	5,543	1,874	–	–	–	72,233	11,167	10,079
Total	$257,300	$17,255	42,553	$26,842	$ 9,089	7,361	$–	$–	–	$284,142	$26,344	49,914
Below investment grade bonds												
0-6 months	$ 7,625	$ 271	2,147	$ 281	$ 76	24	$–	$–	–	$ 7,906	$ 347	2,171
7-12 months	933	91	339	253	85	21	–	–	–	1,186	176	360
>12 months	1,432	107	224	652	221	14	–	–	–	2,084	328	238
Total	$ 9,990	$ 469	2,710	$ 1,186	$ 382	59	$–	$–	–	$ 11,176	$ 851	2,769
Total bonds												
0-6 months	$168,532	$ 7,846	23,858	$ 4,003	$ 1,696	684	$–	$–	–	$172,535	$ 9,542	24,542
7-12 months	42,253	4,147	12,976	6,213	2,011	4,848	–	–	–	48,466	6,158	17,824
>12 months	56,505	5,731	8,429	17,812	5,764	1,888	–	–	–	74,317	11,495	10,317
Total[e]	$267,290	$17,724	45,263	$28,028	$9,471[f]	7,420	$–	$–	–	$295,318	$27,195	52,683
Equity securities												
0-6 months	$ 6,027	$ 629	40,617	$ 1,507	$ 761	1,139	$–	$–	–	$ 7,534	$ 1,390	41,756
7-12 months	561	69	486	244	89	329	–	–	–	805	158	815
>12 months	–	–	–	–	–	–	–	–	–	–	–	–
Total	$ 6,588	$ 698	41,103	$ 1,751	$ 850	1,468	$–	$–	–	$ 8,339	$ 1,548	42,571

(a) Represents the number of consecutive months that fair value has been less than cost by any amount.

(b) Represents the percentage by which fair value is less than cost at the balance sheet date.

(c) For bonds, represents amortized cost.

(d) The effect on net income of unrealized losses after taxes will be mitigated upon realization because certain realized losses will be charged to participating policyholder accounts, or realization will result in current decreases in the amortization of certain DAC.

(e) Includes securities lending invested collateral.

(f) Of this $9.5 billion, $3.7 billion relates to RMBS, CMBS, CDOs and ABS with unrealized losses between 25 percent and 50 percent; and $1.1 billion relates to RMBS, CMBS, CDOs and ABS with unrealized losses between 20 percent and 25 percent. The balance represents all other classes of fixed maturity securities.

The aging of the unrealized losses of RMBS, CMBS, CDOs and ABS with fair values between 20 percent and 50 percent less than their cost at September 30, 2008 (in footnote (f) to the table above) is shown in the table below, which provides the period in which those securities in unrealized loss positions would become candidates for impairment solely because they have been trading at a discount for nine consecutive months (AIG's other-than-temporary aging guideline) without regard to the level of discount (AIG's other-than-temporary trading level guideline), assuming prices remained unchanged.

(In millions) Unrealized loss percent	Fourth Quarter 2008	First Quarter 2009	Second Quarter 2009	Total
25 to 50 percent	$207	$403	$3,059	$3,669
20 to less than 25 percent	$–	$1	$1,134	$1,135

Given the current difficult market conditions, AIG is not able to predict reasonably likely changes in the prices of these securities. Moreover, AIG is unable to assess the effect, if any, that potential sale of securities pursuant to TARP will have on the pricing of its available for sale securities.

Unrealized gains and losses

At September 30, 2008, the carrying value of AIG's available for sale fixed maturity and equity securities aggregated $445.5 billion. At September 30, 2008, aggregate pre-tax unrealized gains for fixed maturity and equity securities were $10.3 billion ($6.7 billion after tax).

At September 30, 2008, the aggregate pre-tax gross unrealized losses on fixed maturity and equity securities were $28.7 billion ($18.7 billion after tax). Additional information about these securities is as follows:

- These securities were valued, in the aggregate, at approximately 91 percent of their current amortized cost.
- Approximately 10 percent of these securities were valued at less than 20 percent of their current cost, or amortized cost.
- Approximately four percent of the fixed maturity securities had issuer credit ratings that were below investment grade.

AIG did not consider these securities in an unrealized loss position to be other-than-temporarily impaired at September 30, 2008, because management has the intent and ability to hold these investments until they recover their cost basis within a recovery period deemed temporary. AIG believes the securities will generally continue to perform in accordance with the original terms, notwithstanding the present price declines.

For the three- and nine-month periods ended September 30, 2008, unrealized losses related to investment grade bonds increased $3.0 billion ($2.0 billion after tax) and $13.5 billion ($8.8 billion after tax), respectively, reflecting the widening of credit spreads, partially offset by the effects of a decline in risk-free interest rates.

The amortized cost and fair value of fixed maturity securities available for sale in an unrealized loss position at September 30, 2008, by contractual maturity, were as follows:

(in millions)	Amortized Cost	Fair Value
Due in one year or less	$ 9,257	$ 8,914
Due after one year through five years	49,370	45,950
Due after five years through ten years	67,864	62,968
Due after ten years	100,805	90,092
Mortgage-backed, asset-backed and collateralized	68,022	60,199
Total	$295,318	$268,123

For the nine-month period ended September 30, 2008, the pre-tax realized losses incurred with respect to the sale of fixed maturities and equity securities were $1.7 billion. The aggregate fair value of securities sold was $20.6 billion, which was approximately 92 percent of amortized cost. The average period of time that securities sold at a loss during the nine-month period ended September 30, 2008 were trading continuously at a price below book value was approximately five months. See Risk Management — Corporate Risk Management — Credit Risk Management in the 2007 Annual Report on Form 10-K for an additional discussion of investment risks associated with AIG's investment portfolio.

Certain of AIG's foreign subsidiaries included in the consolidated financial statements report on a fiscal period ended August 31. The effect on AIG's consolidated financial condition and results of operations of all material events occurring between August 31 and September 30 for all periods presented has been recorded. Due to the significant and rapid world-wide market decline, in September 2008, AIG determined this to be an intervening event that had a material effect on its consolidated financial position and results of operations. AIG reflected this recent market decline throughout its investment portfolio. Accordingly, AIG recorded $1.3 billion ($845 million after tax) of hedge and mutual fund investment losses in net investment income, $1.1 billion ($910 million after tax) of other than temporary impairment charges, and $5.4 billion ($3.2 billion after tax) of unrealized depreciation on investments.

Risk Management

For a complete discussion of AIG's risk management program, see Risk Management in the 2007 Annual Report on Form 10-K.

The recent unprecedented market turmoil, particularly in the residential mortgage-backed securities market, led to severe declines in the prices of highly-rated asset backed securities and reduced liquidity for these securities. The unanticipated price declines and reduction of liquidity exceeded the parameters historically used by AIG for purposes of asset-liability and liquidity management processes. AIG is responding to these developments by enhancing its risk management processes and stress testing. The continuation of such market turmoil and associated price declines and limited liquidity have severely constrained AIG's alternatives for mitigating its exposure to credit, market and liquidity risks.

AIG has continued to invest in human resources, systems and processes in the enterprise risk management functions, both at the corporate and business unit levels. These efforts include implementing systems and processes to ensure the aggregation of the various categories of risk across business units and as a whole, and incorporating forward-looking analyses and stress tests. These initiatives are ongoing and will take time to implement. As AIG divests of certain operations, enterprise risk management will be focused on maintaining appropriate human resources, oversight and controls for the remaining operations.

Credit Risk Management

AIG defines its aggregate credit exposures to a counterparty as the sum of its fixed maturities, loans, finance leases, derivatives (mark to market), deposits (in the case of financial institutions) and the specified credit equivalent exposure to certain insurance products which embody credit risk.

The following table presents AIG's largest credit exposures at September 30, 2008 as a percentage of total consolidated shareholders' equity:

Category	Risk Rating[(a)]	Credit Exposure as a Percentage of Total Consolidated Shareholders' Equity
Investment Grade:		
10 largest combined	A+ (weighted) average[(b)]	128.9%
Single largest non-sovereign (financial institution)	A-	17.9
Single largest corporate	AAA	7.4
Single largest sovereign	A	23.3
Non-Investment Grade:		
Single largest sovereign	BB-	2.5
Single largest non-sovereign	BB	0.7

(a) Risk rating is based on AIG's internal risk ratings process.

(b) Five of the ten largest credit exposures are to highly-rated financial institutions and four are to investment-grade rated sovereigns; none is rated lower than BBB or its equivalent.

AIG monitors its aggregate cross-border exposures by country and regional group of countries. AIG defines its cross-border exposure to include both cross-border credit exposures and its large cross-border investments in its own international subsidiaries. Fourteen countries had cross-border exposures in excess of 10 percent of total consolidated shareholders' equity at September 30, 2008. At that date nine were AAA-rated, two were AA-rated and three were A-rated.

In addition, AIG reviews its industry concentrations. Excluding the U.S. residential and commercial mortgage sectors, AIG's single largest industry credit exposure is to the global financial institutions sector comprised of banks, securities firms, insurance companies and finance companies.

The following table presents AIG's largest credit exposures to the global financial institution sector at September 30, 2008 as a percentage of total consolidated shareholders' equity:

Industry Category	Credit Exposure as a Percentage of Consolidated Shareholders' Equity
Money Center / Global Bank Groups	121.0%
Global Life Insurance Carriers	24.8
European Regional Financial Institutions	21.6
Global Securities Firms and Exchanges	17.2
Global Reinsurance Firms	16.2
North American Based Regional Financial Institutions	15.5
Asian Regional Financial Institutions	10.7

AIG's exposure to the five largest money center/global bank group institutions was 59 percent of shareholders' equity.

AIG's other industry credit concentrations in excess of 10 percent of total consolidated shareholders' equity are in the following industries (in descending order by approximate size):

- Oil and gas;
- Electric and water utilities;
- Global telecommunications companies;
- Conglomerates;
- Pharmaceutical and healthcare companies;
- Government sponsored entities;
- Retail companies; and
- Food and beverage companies.

Other than as described above, there were no significant changes to AIG's credit exposures as set forth in Risk Management — Corporate Risk Management — Credit Risk Management in the 2007 Annual Report on Form 10-K.

Market Risk Management

Insurance, Asset Management and Non-Trading Financial Services Value at Risk (VaR)

AIG performs a VaR analysis across all of its non-trading businesses, and a separate VaR analysis for its trading business at AIGFP. The comprehensive VaR is categorized by AIG business segment (General Insurance, Life Insurance & Retirement Services, Financial Services and Asset Management) and also by market risk factor (interest rate, currency and equity). AIG's market risk VaR calculations include exposures to benchmark Treasury or swap interest rates, but do not include exposures to credit-based factors such as credit spreads. AIG's credit exposures within its invested assets and credit derivative portfolios are discussed in Risk Management — Segment Risk Management — Financial Services in the 2007 Annual Report on Form 10-K.

For the insurance segments, assets included are invested assets (excluding direct holdings of real estate) and liabilities included are reserve for losses and loss expenses, reserve for unearned premiums, future policy benefits for life and accident and health insurance contracts and other policyholders' funds. For financial services companies, loans and leases represent the majority of assets represented in the VaR calculation, while bonds and notes issued represent the majority of liabilities. Parent company assets and liabilities (other than those pertaining to funding under the Fed Facility and consideration received for Series C Preferred Stock not yet issued) are included in the Total AIG VaR figures.

AIG calculated the VaR with respect to net fair values as of September 30, 2008 and December 31, 2007. The VaR number represents the maximum potential loss as of those dates that could be incurred with a 95 percent confidence (i.e., only five percent of historical scenarios show losses greater than the VaR figure) within a one-month holding

period. AIG uses the historical simulation methodology that entails repricing all assets and liabilities under explicit changes in market rates within a specific historical time period. AIG uses the most recent three years of historical market information for interest rates, foreign exchange rates, and equity index prices. For each scenario, each transaction was repriced. Segment and AIG-wide scenario values are then calculated by netting the values of all the underlying assets and liabilities.

The following table presents the period-end, average, high and low VaRs on a diversified basis and of each component of market risk for AIG's non-trading businesses. The diversified VaR is usually smaller than the sum of its components due to correlation effects.

	2008				2007			
		Nine Months Ended September 30,				Year Ended December 31,		
(in millions)	As of September 30,	Average	High	Low	As of December 31,	Average	High	Low
Total AIG non-trading market risk:								
Diversified	**$7,347**	**$6,609**	**$7,347**	**$5,593**	$5,593	$5,316	$5,619	$5,073
Interest rate	**5,380**	**4,944**	**5,380**	**4,383**	4,383	4,600	4,757	4,383
Currency	**772**	**856**	**1,022**	**772**	785	729	785	685
Equity	**3,410**	**3,111**	**3,410**	**2,627**	2,627	2,183	2,627	1,873
General Insurance:								
Diversified	**$1,330**	**$1,357**	**$1,377**	**$1,330**	$1,363	$1,637	$1,892	$1,363
Interest rate	**1,279**	**1,173**	**1,279**	**1,078**	1,117	1,492	1,792	1,117
Currency	**147**	**259**	**328**	**147**	255	222	255	205
Equity	**971**	**961**	**1,030**	**835**	835	659	835	573
Life Insurance & Retirement Services:								
Diversified	**$6,698**	**$6,064**	**$6,698**	**$5,180**	$5,180	$4,848	$5,180	$4,574
Interest rate	**5,351**	**4,850**	**5,351**	**4,405**	4,405	4,465	4,611	4,287
Currency	**752**	**707**	**807**	**621**	649	621	678	568
Equity	**2,332**	**2,137**	**2,332**	**1,810**	1,810	1,512	1,810	1,293
Non-Trading Financial Services:								
Diversified	**$ 165**	**$ 140**	**$ 167**	**$ 99**	$ 99	$ 117	$ 170	$ 85
Interest rate	**166**	**137**	**166**	**95**	95	116	168	76
Currency	**17**	**15**	**17**	**13**	13	12	13	11
Equity	**2**	**1**	**2**	**1**	1	1	1	1
Asset Management:								
Diversified	**$ 141**	**$ 73**	**$ 141**	**$ 38**	$ 38	$ 49	$ 74	$ 26
Interest rate	**138**	**67**	**138**	**32**	32	45	72	22
Currency	**12**	**4**	**12**	**2**	2	3	5	2
Equity	**8**	**11**	**13**	**8**	13	11	13	8

AIG's total non-trading market risk VaR increased from $5.6 billion at year-end 2007 to $7.3 billion at September 30, 2008. The VaR increase was driven primarily by higher volatilities in equity markets globally and interest rates in the U.S.

Capital Markets Trading VaR

AIGFP attempts to minimize risk in benchmark interest rates, equities, commodities and foreign exchange. Market exposures in option implied volatilities, correlations and basis risks are also minimized over time.

AIGFP's minimal reliance on market risk driven revenue is reflected in its VaR. AIGFP's VaR calculation is based on the interest rate, equity, commodity and foreign exchange risk arising from its portfolio. Credit-related factors, such as credit spreads or credit default, are not included in AIGFP's VaR calculation. Because the market risk with respect to securities available for sale, at market, is substantially hedged, segregation of the financial instruments into trading and other than trading was not considered necessary. AIGFP operates under established market risk limits based upon this VaR calculation. In addition, AIGFP backtests its VaR.

In the calculation of VaR for AIGFP, AIG uses the historical simulation methodology based on estimated changes to the value of all transactions under explicit changes in market rates and prices within a specific historical time period. AIGFP attempts to secure reliable and independent current market prices, such as published exchange prices, external subscription services such as Bloomberg or Reuters, or third-party or broker quotes. When such prices are not available, AIGFP uses an internal methodology that includes extrapolation from observable and verifiable prices nearest to the dates of the transactions. Historically, actual results have not deviated from these models in any material respect.

AIGFP reports its VaR level using a 95 percent confidence level and a one-day holding period, facilitating risk comparison

with AIGFP's trading peers and reflecting the fact that market risks can be actively assumed and offset in AIGFP's trading portfolio.

The following table presents the year-end, average, high, and low VaRs on a diversified basis and of each component of market risk for Capital Markets operations. The diversified VaR is usually smaller than the sum of its components due to correlation effects.

(in millions)	As of September 30,	Nine Months Ended September 30, Average	High	Low	As of December 31,	Year Ended December 31, Average	High	Low
Capital Markets trading market risk:								
Diversified	**$5**	**$6**	**$9**	**$4**	$5	$5	$8	$4
Interest rate	**3**	**2**	**4**	**1**	3	2	3	2
Currency	**3**	**1**	**4**	**–**	1	1	2	1
Equity	**2**	**2**	**4**	**2**	3	3	5	2
Commodity	**2**	**4**	**7**	**2**	3	3	7	2

See Valuation of Level 3 Assets and Liabilities for a comprehensive discussion of AIGFP's super senior credit default swap portfolio.

Insurance Risk Management

Catastrophe Exposures

The nature of AIG's business exposes it to various catastrophic events in which multiple losses across multiple lines of business can occur in any calendar year. To control this exposure, AIG uses a combination of techniques, including setting aggregate limits in key business units, monitoring and modeling accumulated exposures, and purchasing catastrophe reinsurance to supplement its other reinsurance protections.

Natural disasters such as hurricanes, earthquakes and other catastrophes have the potential to adversely affect AIG's operating results. Other risks, such as an outbreak of a pandemic disease, such as the Avian Influenza A Virus (H5N1), could adversely affect AIG's business and operating results to an extent that may be only partially offset by reinsurance programs.

AIG evaluates catastrophic events and assesses the probability of occurrence and magnitude of catastrophic events through the use of industry recognized models, among other techniques. AIG updates these models by periodically monitoring the exposure risks of AIG's worldwide General Insurance operations. Following is an overview of modeled losses associated with the more significant natural perils, which includes exposures for AIG Property Casualty Group and Foreign General (other than Ascot). Transatlantic and Ascot utilize a different model, and their results are presented separately below. Significant Life Insurance and accident and health exposures have been added to these results as well. The modeled results assume that all reinsurers fulfill their obligations to AIG in accordance with their terms.

It is important to recognize that there is no standard methodology to project the possible losses from total property and workers' compensation exposures. Further, there are no industry standard assumptions to be utilized in projecting these losses. The use of different methodologies and assumptions could materially change the projected losses. Therefore, these modeled losses may not be comparable to estimates made by other companies. These estimates are inherently uncertain and may not reflect AIG's maximum exposures to these events. It is highly likely that AIG's losses will vary, perhaps significantly, from these estimates.

AIG has revised the catastrophe exposure disclosures presented below from that presented in the 2007 Annual Report on Form 10-K to reflect more recent data for AIG's Property Casualty Group, as well as reinsurance programs in place as of September 1, 2008. The modeled results provided in the table below were based on the aggregate exceedence probability (AEP) losses which represent total property, workers' compensation, life, and accident and health losses that may occur in any single year from one or more natural events. The updated Property Casualty Group property exposures were modeled with exposure data as of June 2008. The values provided were based on 100-year return period losses, which have a one percent likelihood of being exceeded in any single year. Thus, the model projects that there is a one percent probability that AIG could incur in any year losses in excess of the modeled amounts for these perils. Losses include loss adjustment expenses and the net values include reinstatement premiums.

(in millions)	Gross	Net of 2008 Reinsurance	Net After Income Tax	% of Consolidated Shareholders' Equity at September 30, 2008
Natural Peril:				
Earthquake	$6,627	$4,098	$2,664	3.7%
Tropical Cyclone*	$6,850	$4,094	$2,661	3.7%

** Includes hurricanes, typhoons and European Windstorms.*

Both gross earthquake and tropical cyclone modeled losses increased $1.0 billion compared to estimates included in the 2007 Annual Report on Form 10-K while net after tax losses increased $456 million and $431 million, respectively. These increases are mainly attributable to growth in Lexington, Private Client Group and energy.

In addition to the return period loss, AIG evaluates potential single event earthquake and hurricane losses that may be incurred. The single events utilized are a subset of potential events identified and utilized by Lloyd's *(see Lloyd's Realistic Disaster Scenarios, Scenario Specifications, April 2006)* and referred to as Realistic Disaster Scenarios (RDSs). The purpose of this analysis is to utilize these RDSs to provide a reference frame and place into context the model results. However, it is important to note that the specific events used for this analysis do not necessarily represent the worst case loss that AIG could incur from this type of an event in these regions. The losses associated with the RDSs are included in the following table.

Single event modeled property and workers' compensation losses to AIG's worldwide portfolio of risk for key geographic areas are set forth below. Gross values represent AIG's liability after the application of policy limits and deductibles, and net values represent losses after reinsurance is applied; net losses also include reinsurance reinstatement premiums. Both gross and net losses include loss adjustment expenses.

(in millions)	Gross	Net of 2008 Reinsurance
Natural Peril:		
San Francisco Earthquake	$7,294	$4,573
Miami Hurricane	$7,335	$3,834
Los Angeles Earthquake	$6,336	$3,986
Northeast Hurricane	$5,012	$2,978
Gulf Coast Hurricane	$4,376	$2,476
Japanese Earthquake	$1,109	$ 406
European Windstorm	$ 252	$ 89
Japanese Typhoon	$ 177	$ 103

AIG also monitors key international property risks utilizing modeled statistical return period losses as well. Based on these simulations, the 100-year return period loss for Japanese Earthquake is $510 million gross, and $170 million net, the 100-year return period loss for European Windstorm is $448 million gross, and $154 million net, and the 100-year return period loss for Japanese Typhoon is $340 million gross, and $212 million net.

The losses provided above do not include Transatlantic or Ascot. The one in 100 year AEP amounts for Ascot and AIG's share (59 percent) of Transatlantic are as follows:

(in millions)	Gross	Net of 2008 Reinsurance	Net After Income Tax
Natural Peril:			
Ascot Earthquake	$380	$ 76	$ 49
Ascot Tropical Cyclone*	$422	$169	$110
AIG's Share of Transatlantic Earthquake	$452	$406	$264
AIG's Share of Transatlantic Tropical Cyclone*	$618	$577	$375

* *The Ascot amounts are based on data as of June 30, 2008 and the Transatlantic amounts are based on data as of July 1, 2008.*

Terrorism

Exposure to loss from terrorist attack is controlled by limiting the aggregate accumulation of workers' compensation and property insurance that is underwritten within defined target locations. Modeling is used to provide projections of probable maximum loss by target location based upon the actual exposures of AIG policyholders.

Terrorism risk is monitored to manage AIG's exposure. AIG shares its exposures to terrorism risks under the Terrorism Risk Insurance Act (TRIA). During 2007, AIG's deductible under TRIA was approximately $4.0 billion, with a 15 percent share of certified terrorism losses in excess of the deductible. As of January 1, 2008, the deductible increased to approximately $4.2 billion, with a 15 percent share of certified terrorism losses in excess of the deductible.

ITEM 3. Quantitative and Qualitative Disclosures About Market Risk

Included in Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations.

ITEM 4. Controls and Procedures

In connection with the preparation of this Quarterly Report on Form 10-Q, an evaluation was carried out by AIG's management, with the participation of AIG's Chief Executive Officer and Chief Financial Officer, of the effectiveness of AIG's disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934 (Exchange Act)). Disclosure controls and procedures are designed to ensure that information required to be disclosed in reports filed or submitted under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in SEC rules and forms and that such information is accumulated and communicated to management, including the Chief Executive Officer and Chief Financial Officer, to allow timely decisions regarding required disclosures. Solely as a result of the previously identified material weakness in internal control over the fair value valuation of the AIGFP super senior credit default swap portfolio and oversight thereof as described in the 2007 Annual Report on Form 10-K, AIG's Chief Executive Officer and Chief Financial Officer have concluded that, as of September 30, 2008, AIG's disclosure controls and procedures were ineffective. Notwithstanding the existence of this material weakness, AIG believes that the consolidated financial statements in this Quarterly Report on Form 10-Q fairly present, in all material respects, AIG's consolidated financial condition as of September 30, 2008 and December 31, 2007 and consolidated results of operations for the three- and nine-month periods ended September 30, 2008 and 2007 and consolidated cash flows for the nine-month periods ended September 30, 2008 and 2007, in conformity with GAAP. In addition, there has been no change in AIG's internal control over financial reporting (as defined in Rule 13a-15(f) under the Exchange Act) that occurred during the quarter ended September 30, 2008 that has materially affected, or is reasonably likely to materially affect, AIG's internal control over financial reporting.

Throughout 2008 and 2007, AIG recorded out of period adjustments, many of which were detected as part of continuing remediation efforts. It is AIG's policy to record all error corrections, without regard to materiality, and AIG has an established, formal process for the identification, evaluation and recording of all out of period adjustments. This process includes a heightened sensitivity for potential errors related to the internal control matters discussed in Item 9A. of the 2007 Annual Report on Form 10-K. AIG distinguishes error corrections from changes in estimates by evaluating the facts and circumstances of such items, including considering whether information was capable of being known at the time of original recording. AIG has evaluated the adjustments recorded in 2008 and 2007 from a qualitative and quantitative perspective and concluded that such adjustments are immaterial individually and in the aggregate to the current and prior periods.

Part II – OTHER INFORMATION

ITEM 1. Legal Proceedings

Included in Note 7(a) to the Consolidated Financial Statements.

ITEM 1A. Risk Factors

Included in Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations.

ITEM 6. Exhibits

See accompanying Exhibit Index.

SIGNATURE

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

AMERICAN INTERNATIONAL GROUP, INC.
(Registrant)

/s/ David L. Herzog

David L. Herzog
Executive Vice President
Chief Financial Officer
Principal Accounting Officer

Dated: November 10, 2008

EXHIBIT INDEX

Exhibit Number	Description	Location
10.1	Release agreement with Steven J. Bensinger	
10.2	Letter from Robert B. Willumstad to Edward M. Liddy	
10.3	Letter Agreement, dated November 9, 2008, between American International Group, Inc. and the United States Department of the Treasury	
10.4	Amendment No. 2, dated as of November 9, 2008, to Credit Agreement, dated as of September 22, 2008, between American International Group, Inc. and the Federal Reserve Bank of New York	
11	Statement re computation of per share earnings	Included in Note 5 of Notes to Consolidated Financial Statements.
12	Computation of ratios of earnings to fixed charges	Filed herewith.
31	Rule 13a-14(a)/15d-14(a) Certifications	Filed herewith.
32	Section 1350 Certifications	Filed herewith.

Exhibit 12

American International Group, Inc.
Computation of Ratios of Earnings to Fixed Charges

(in millions, except ratios)	Three Months Ended September 30, **2008**	2007	Nine Months Ended September 30, **2008**	2007
Income (loss) before income taxes and minority interest	**$(28,185)**	$ 4,879	**$(48,205)**	$17,379
Less – Equity income of less than 50% owned persons	**(2)**	39	**15**	130
Add – Dividends from less than 50% owned persons	**1**	3	**22**	28
	(28,182)	4,843	**(48,198)**	17,277
Add – Fixed charges	**2,048**	3,153	**7,141**	8,267
Less – Capitalized interest	**6**	8	**21**	28
Income (loss) before income taxes, minority interest and fixed charges	**$(26,140)**	$ 7,988	**$(41,078)**	$25,516
Fixed charges:				
Interest costs	**$ 1,973**	$ 3,093	**$ 6,916**	$ 8,086
Rental expense[(a)]	**75**	60	**225**	181
Total fixed charges	**$ 2,048**	$ 3,153	**$ 7,141**	$ 8,267
Ratio of earnings to fixed charges	[(b)]	2.53	[(b)]	3.09
Secondary Ratio				
Interest credited to GIC and GIA policy and contract holders	**$ (551)**	$(1,949)	**$ (3,071)**	$ (4,796)
Total fixed charges excluding interest credited to GIC and GIA policy and contract holders	**$ 1,497**	$ 1,204	**$ 4,070**	$ 3,471
Secondary ratio of earnings to fixed charges	[(b)]	5.02	[(b)]	5.97

(a) The proportion considered representative of the interest factor.

(b) Earnings were inadequate to cover total fixed charges by $28,188 million and $48,219 million for the three- and nine-month periods ended September 30, 2008. The coverage deficiency for total fixed charges excluding interest credited to GIC and GIA policy and contract holders was $27,637 million and $45,148 million for the three- and nine-month periods ended September 30, 2008.

The secondary ratio is disclosed for the convenience of fixed income investors and the rating agencies that serve them and is more comparable to the ratios disclosed by all issuers of fixed maturity securities. The secondary ratio removes interest credited to guaranteed investment contract (GIC) policyholders and guaranteed investment agreement (GIA) contract holders. Such interest expenses are also removed from income (loss) before income taxes and minority interest used in this calculation. GICs and GIAs are entered into by AIG's insurance subsidiaries, principally SunAmerica Life Insurance Company and AIG Financial Products Corp. and its subsidiaries, respectively. The proceeds from GICs and GIAs are invested in a diversified portfolio of securities, primarily investment grade bonds. The assets acquired yield rates greater than the rates on the related policyholders obligation or agreement, with the intent of earning operating income from the spread.

Exhibit 31

CERTIFICATIONS

I, Edward M. Liddy, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q of American International Group, Inc.;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:

(a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

(b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

(c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

(d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):

(a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

(b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

/s/ Edward M. Liddy

Edward M. Liddy
Chairman and Chief Executive Officer

Date: November 10, 2008

CERTIFICATIONS

I, David L. Herzog, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q of American International Group, Inc.;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:

(a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

(b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

(c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

(d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):

(a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

(b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

/s/ David L. Herzog

David L. Herzog
Executive Vice President and
Chief Financial Officer

Date: November 10, 2008

Exhibit 32

CERTIFICATION

In connection with the Quarterly Report on Form 10-Q of American International Group, Inc. (the "Company") for the quarter ended September 30, 2008, as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, Edward M. Liddy, Chairman and Chief Executive Officer of the Company, certify, pursuant to 18 U.S.C. Section 1350, that to my knowledge:

1. The Report fully complies with the requirements of Section 13(a) or 15(d), as applicable, of the Securities Exchange Act of 1934; and

2. The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

/s/ Edward M. Liddy

Edward M. Liddy
Chairman and Chief Executive Officer

Date: November 10, 2008

The foregoing certification is being furnished solely pursuant to 18 U.S.C. Section 1350 and is not being filed as part of the Report or as a separate disclosure document.

CERTIFICATION

In connection with the Quarterly Report on Form 10-Q of American International Group, Inc. (the "Company") for the quarter ended September 30, 2008, as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, David L. Herzog, Executive Vice President and Chief Financial Officer of the Company, certify, pursuant to 18 U.S.C. Section 1350, that to my knowledge:

1. The Report fully complies with the requirements of Section 13(a) or 15(d), as applicable, of the Securities Exchange Act of 1934; and

2. The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

/s/ David L. Herzog

David L. Herzog
Executive Vice President and Chief Financial Officer

Date: November 10, 2008

The foregoing certification is being furnished solely pursuant to 18 U.S.C. Section 1350 and is not being filed as part of the Report or as a separate disclosure document.