IS AIG'S REINSURANCE SIDE A HOUSE OF CARDS, TOO?

The other day, Atrios pointed to this passage, explaining that AIG was reinsuring some of its own insurance businesses.

> Thomas Gober, a former Mississippi state insurance examiner who has tracked fraud in the industry for 23 years and served previously as a consultant to the FBI and the Department of Justice, says he believes AIG's supposedly solvent insurance business may be at least as troubled as its reckless financial-products unit. Far from being "healthy," as state insurance regulators, ratings agencies and other experts have repeatedly described the insurance side, Gober calls it "a house of cards." Citing numerous documents he has obtained from state insurance regulators and obscure data buried in AIG's own 300-page annual reports, Gober argues that AIG's 71 interlocking domestic U.S. insurance subsidiaries are in hock to each other to an astonishing degree.
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> Most of this as-yet-undiscovered problem, Gober says, lies in the area of reinsurance, whereby **one insurance company insures the liabilities of another so that the latter doesn't have to carry all the risk on its books. Most major insurance companies use outside firms to reinsure, but the vast majority of AIG's reinsurance contracts are negotiated internally among its affiliates, Gober says, and these internal balance sheets don't add up**. The annual report of one major AIG subsidiary, American Home Assurance, shows that it owes $25 billion to another AIG affiliate, National Union

> Fire, Gober maintains. But American has only $22 billion of total invested assets on its balance sheet, he says, and it has issued another $22 billion in guarantees to the other companies. "The American Home assets and liquidity raise serious questions about their ability to make good on their promise to National Union Fire," says Gober, who has a consulting business devoted to protecting policyholders. Gober says there are numerous other examples of "cooked books" between AIG subsidiaries. Based on the state insurance regulators' own reports detailing unanswered questions, the tally in losses could be hundreds of billions of dollars more than AIG is now acknowledging. [my emphasis]

Masaccio pointed me to these two passages in AIG's 10K, which sound like they may describe what Gober is talking about:

> Various AIG profit centers, including DBG, AIU, AIG Reinsurance Advisors, Inc. and AIG Risk Finance, as well as certain Foreign Life subsidiaries, use AIRCO as a reinsurer for certain of their businesses, and AIRCO also receives premiums from offshore captives of AIG clients. **In accordance with permitted accounting practices in Bermuda, AIRCO discounts reserves attributable to certain classes of business assumed from other AIG subsidiaries**. (10)
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> **AIRCO acts primarily as an internal reinsurance company for AIG's insurance operations**. This facilitates insurance risk management (retention, volatility, concentrations) and capital planning locally (branch and subsidiary). It also allows AIG to pool its insurance risks and purchase reinsurance more efficiently at a consolidated level, manage global counterparty risk and

> relationships and manage global life catastrophe risks. [my emphasis]

So AIG admits that its got a company, AIRCO, that is reinsuring its own insurance, and AIRCO is using a Bermuda accounting trick to limit the reserves it holds for this reinsurance.

In the Newsweek article above, AIG points to state insurance regulators giving AIG a clean bill of health, but as one of them admits, state regulators only regulate state-based contracts–not shit created to exploit Bermuda loopholes.

> In response, Eric Dinallo, New York state's superintendent of insurance, said he thought "the operating companies of AIG, particularly the property companies, are in excellent condition." But Dinallo admitted he had examined only 25 of the domestic AIG companies and added: "There are problems with state insurance regulation. I've been a proponent of us revisiting it."

So it sure sounds like AIG may be hiding its own special version of reinsurance shitpile in Bermuda.

Which is why I was concerned about this paragraph in a letter Edward Liddy sent to Elijah Cummings in December explaining why AIG is offering bonuses to its "healthy" insurance side (these are the bonuses to some 4500 people above and beyond the bonuses to AIGFP people).

> Recently, some reinsurers have begun requesting provisions which would allow them to cancel reinsurance contracts upon the departure of critical AIG employees. Having appropriate reinsurance coverage in place is essential to the risk control for AIG's operations. Without appropriate reinsurance cover, the magnitude of losses on catastrophic events would

> seriously injure the financial strength of the company. In addition, AIG plays a vital role in providing risk coverage to many institutions around the world. AIG’s risk appetite would be severely impacted without appropriate reinsurance.

Of course, what Liddy didn’t tell Cummings is that some of these reinsurance companies are shell games constructed within AIG.

I’m developing an increasingly gloomy belief that every single one of these bonuses–the AIGFP ones we’re all talking about, but also the 4500 bonuses to people in the so-called "healthy" insurance side–are tied to an amazing financial fraud. And we, the taxpayers, are bribing these people to stick around their fraud long enough to try to undo it.