



RISKTHINKERS

**AMERICAN INTERNATIONAL GROUP AUSTRALASIA AND AIG INC.  
IS THERE A DIFFERENCE IN THIS REGION? THE FORMATION OF AIU HOLDINGS.  
INTERVIEW WITH THE CEO OF AIG AUSTRALASIA, CHRIS TOWNSEND.**

Following up on many enquiries from our clients I recently interviewed Chris Townsend, the CEO Australasia of AIG.

In September last year when the news broke that AIG Inc had to be supported by the US Government, I like many insurance professionals was alarmed at the potential of an AIG collapse. One of the few insurance groups to achieve a AAA rating from Standard & Poor's suddenly needed government assistance.

At the centre of AIG Inc's problems were Commercial Mortgage Backed Security (CMBS) investments which the AIG Financial Products division invested in. The position was not reached as a consequence of AIG's insurance underwriting operations, which have continued to operate profitably around the world.

Within AIG Inc is the American International Underwriters (AIU) group of companies of which *the Australian operation* is a member. To assist our clients in assessing any policies underwritten by AIG Australia I put the following questions to Chris and record his answers below each question.

**Question / Answers**

**Q.1. Do you issue policies in Australia as AIG Australia?**

**A.** Our trading name is AIG Australia, but the insurance company we issue paper under is American Home Assurance Company (AHAC) which is a New York registered and New York regulated entity. AIG Australia is a branch of this business and is therefore subject to regulation by both APRA and the insurance of commissioner of NY. AHAC is Standard & Poor's A+ rated and currently has surplus capital of US\$ 5.7B.

**Q.2. If AHA issues policies under the AIG Australia brand, is AHA authorised by APRA to transact insurance business in Australia?**

**A.** Yes, AHAC is authorised by APRA to conduct General Insurance business pursuant to the Insurance Act. We are regulated by APRA.

**Q.3. To achieve APRA approval, does AHA lodge separate assets in Australia which cannot be accessed by the AIG parent company?**

**A:** Under GPS 110 of the APRA Standards, AHAC is required to retain assets in Australia which exceed its liabilities in Australia. As AHAC, we comfortably exceed this minimum requirement. In fact, we had 2.05 times the minimum capital that we are required to hold as at 31st December 2008. In terms of our asset base, we have gross assets of a little over A\$1.7B in Australia, including a A\$1B

investment portfolio. Of this, 94% is in fixed income securities of which 90% is AA- rated or better. It is a highly conservative investment portfolio. .

GPS110 also prohibits AIG Australia and its senior officers in Australia from remitting any surplus capital back to its head office without obtaining APRA's prior written consent. Individuals who breach this requirement face substantial fines, jail, and life disqualification, from acting as a senior manager of an insurance company. Please note that since second quarter of 2008 we have not sought APRA approval to remit surplus funds to American Home Assurance Company.

**Q.4. What Surplus is required by APRA and how does the surplus of AHA compare?**

- A. APRA's guidance is for us to carry 1.5 times the minimum capital requirement that applies to AIG Australia. As mentioned above, as of 31st December when we submitted our last quarterly return to APRA we had coverage of 2.05 times our minimum capital. This leaves us with a surplus (assets in excess of our liabilities) of A\$ 345m in Australia.

APRA published comparative minimum capital requirements so it is a matter of public record.

**Q.5. Has AHA been directly affected by CMBS investments? What is the current investment structure and strategy of AHA in Australia?**

- A. As mentioned above, we hold a very conservative investment portfolio which is dominated by highly rated fixed income securities. Other assets include cash, a property in Melbourne and a small equity portfolio. We have no residential or commercial mortgage backed securities, we have no alternative investments and do not engage in any form of equities lending. Our intention is to take risk on the liability side of the balance sheet and not on the asset side of the balance sheet

**Q.6. Do you have to seek approval outside Australia to settle any claims? If Yes, at what level and what is the process?**

- A. Like most international insurers, we capitalise on our global buying power to secure competitive global reinsurance support. This requires AIG Australasia to collaborate on very large claims. However, it is noteworthy that these arrangements have been in place for at least ten years and have not changed since the US Government became a shareholder in AIG Inc. We will almost certainly have similar arrangements when AIU is in operation.

**Q.7. Has your claims paying ability been diminished or delayed since the developments of September last year?**

- A. Absolutely not. The insurance companies were never part of the problem but are the solution to AIG's parent companies issues. The general insurance companies around the world operate in highly regulated markets and meet (as they always have done) the local capital and claims paying requirements. In fact, AIU (the international - non US general insurance business) paid over US\$7.5B in claims in 2008 financial year. Our claims technical and service skill set has always been a key differentiator to our competitors in our chosen market segments and we have every intention of maintaining that position.

**Q.8. What is the current Standard & Poor's(S&P) rating for the Australian operations of AHA?**

- A. AHAC is rated by S&P as A+ secure

- Q.9. It has been announced that AIU Holdings Inc will be formed within the next two months and that AIG Australasia (AHAC) will be a member. Will this have any impact on:
- Your APRA approval
  - Your Minimum Capital Ratio
  - Your net Assets
  - Your claims settling authority

Colin, it is too early to provide this level of detail. The announcement of the creation of AIU Holdings Inc was released on 2nd March. We have a number of our senior executives in both the US and the International general insurance business working on a 45 day project to work out what this business will look like. What I can say is the establishment of AIU Holdings, Inc is much more than just a re-brand. The geographic reach of over 40 million commercial / individual customers world wide, with approx 44,000 employees, 500 products and services, through 130 countries and jurisdictions. On scale the net written premium (NPW) over US\$40B, Equity over US\$43B, in 2008 paid over US\$26B in claims - as a single, transparently managed and distinctly branded global insurance organisation – will deliver even greater value for our customers and distribution partners. This transition will allow us to have direct access to the capital markets and with time will allow us our own credit rating which is separate and distinct from that of our parent.

- Q.10. Finally Chris, would you like to briefly sum up how you would like your clients and prospective customers to view AIG Australasia now and in the future?

- A. AIG Australia is not standing still. The team is developing new opportunities to lead the market. In February we launched an enhanced D&O Gold policy offering dedicated director indemnity cover and a separate Company Securities 'companion' policy. This approach is designed to address the needs of both the directors and the company. AIG is launching this at a time when many other insurers are reviewing their coverage and capacity for a policy that is generating large losses from an increasingly severe and frequent incidence of shareholder class actions. We are referring to this initiative as a new direction in D&O, but it is essentially what many policyholders and their advisers are demanding.

The enhanced D&O Gold policy has coverage that puts real distance between AIG and its competitors. It is untainted by and ring-fenced from the entity cover which was previously offered under the one 'D&O' umbrella policy. The separate Company Securities policy offers entity cover that can now be valued in its own right (without the issue of priority of payments, shared indemnity limits or conflicts arising).

## **In Conclusion**

We have undoubtedly suffered a significant amount of brand damage by being part of AIG. The move to AIU Holdings provides us with a clear roadmap for our future. AIG Australia has a well defined set of strategic pillars which we are busy executing in the marketplace. Our staff has been nothing short of heroic over the past six months in the manner in which they have rallied round to support the business. I am proud of their efforts and our collective achievements.

### **COLIN SMITH**

Managing Director

01 April 2009

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