

Congress of the United States
House of Representatives

COMMITTEE ON OVERSIGHT AND GOVERNMENT REFORM

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October 9, 2009

MEMORANDUM

TO: Members of the Committee on Oversight and Government Reform

FROM: Majority Staff, Committee on Oversight and Government Reform

SUBJECT: Full Committee Hearing entitled, "AIG Bonuses: Audit of the Special Inspector General for the Troubled Asset Relief Program (SIGTARP)"

On Wednesday, October 14, 2009, at 10:00 a.m. in room 2154 of the Rayburn House Office Building, the Committee on Oversight and Government Reform will hold a hearing entitled, "AIG Bonuses: Report of the Special Inspector General for the Troubled Asset Relief Program." At the hearing, Mr. Neil M. Barofsky, the Special Inspector General for the Troubled Asset Relief Program (SIGTARP), will report the results of his audit of bonus payments made to American International Group (AIG) executives in March 2009.

Background

At the beginning of 2008, AIG was the world's largest insurance company, with 116,000 employees, 74 million clients, operations in 130 countries, and more than \$1 trillion in assets.¹ However, beginning in 1998, AIG expanded beyond traditional insurance products, selling nearly \$500 billion worth of credit default swaps.² Credit default swaps insure against the default of debts, including debts tied to subprime mortgages. By August 2008, the rise in home foreclosures in the United States had reduced the market value of AIG's credit default swaps by more than \$25 billion, leading to net losses and declining share values for AIG.³

On September 15, 2008, Standard & Poor's downgraded AIG's credit rating and AIG determined that it needed to raise at least \$80 billion in capital to prevent bankruptcy.⁴ On September 16, after AIG failed to secure the necessary capital from private sources, the Federal Reserve Bank of New York (NY Fed) agreed to loan AIG

¹ AIG, *Annual Report* (2007); AIG, Form 10-Q (Mar. 31, 2008).

² AIG Residential Mortgage Presentation (Aug 9, 2007).

³ AIG Conference Call Credit Presentation (Aug. 7, 2008).

⁴ *Bad Bets and Cash Crunch Pushed Ailing AIG to Brink*, Wall Street Journal (Sept. 18, 2008).

\$85 billion to prevent the company from filing for bankruptcy.⁵ In return, the NY Fed received a 79.9 percent ownership stake in AIG. The NY Fed also replaced AIG's CEO with Edward Liddy, the former CEO of Allstate.

A timeline showing major events related to the AIG bonuses is attached.

AIG Compensation Policies

Following the Federal bailout, AIG's executive compensation came under intense public scrutiny when, on March 15, 2009, the company announced the payment of \$165 million in "retention bonuses" to employees of its troubled financial products division, AIGFP. AIG and the Treasury Department defended the bonuses as being required under current employment contracts and necessary to retain key employees. However, in a letter to Treasury Secretary Geithner dated March 14, 2009, Mr. Liddy pledged to use "best efforts" to reduce the bonus payments by "at least 30 percent."⁶ Secretary Geithner then wrote to House Speaker Pelosi, outlining what Treasury had done to date, its efforts to recoup "the retention payments" already made, and how Treasury planned to deal with future payments of executive compensation at AIG.⁷

The SIGTARP Audit

On March 20, 2009, the Special Inspector General for the Troubled Asset Relief Program (SIGTARP) initiated an audit of the AIG bonuses to review: (1) the extent of knowledge and oversight by Federal Reserve and Treasury officials over AIG compensation programs and, specifically, retention payments to AIGFP executives; (2) the extent to which AIGFP retention payments were governed by executive compensation restrictions or pre-existing contractual obligations; and (3) whether additional AIG compensation issues require resolution.

The SIGTARP's report will be the focus of the hearing. Copies of the report will be made available when they are received from the SIGTARP.

Witness

Mr. Neil M. Barofsky
Special Inspector General
for the Troubled Asset Relief Program

Should you have any questions, please contact John Arlington or Joanne Royce of the Committee Staff at 5-5051.

⁵ Credit Agreement between AIG and Federal Reserve Bank of New York (Sept. 22, 2008) (online at www.sec.gov/Archives/edgar/data/5272/000095012308011496/y71452exv99w1.htm).

⁶ Letter from Edward Liddy to Secretary Geithner (Mar. 14, 2009).

⁷ Letter from Secretary Geithner to Speaker Pelosi (Mar. 17, 2009).

AIG Bonus Timeline

May 8, 2008: AIG discloses, in an SEC filing, a plan to pay retention bonuses to AIG Financial Products employees.

Sept. 16: The Federal Reserve extends AIG a two-year loan of up to \$85 billion, and receives a 79.9% stake in return.

Oct. 8: Federal bailout loans increase to nearly \$123 billion due to problems in AIG's securities-lending program.

Nov. 9: The Federal rescue package increases to \$150 billion, including a new \$40 billion investment.

March 2, 2009: The Treasury Department makes an additional \$30 billion in TARP money available to AIG.

March 10: The Treasury Department receives from the New York Fed a list of bonus payments due to AIG executives.

March 11: Treasury Secretary Geithner discusses bonuses and compensation with AIG's CEO Edward Liddy.

March 14: In a letter to Secretary Geithner, Mr. Liddy says AIG will "use best efforts" to reduce the bonus payments by "at least 30%."

March 15: AIG announces to the public the payment of \$165 million in "retention bonuses" to employees of AIG Financial Products.

March 17: In a letter to House Speaker Pelosi, Secretary Geithner outlines what Treasury has done to date, its efforts to recoup "the retention payments" already made, and how Treasury plans to deal with future payments of executive compensation at AIG.

March 20: The Special Inspector General for the Troubled Asset Relief Program (SIGTARP) begins an audit of AIG bonuses.