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After $182 billion taxpayer rescue, is AIG on the verge of collapse?

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You may remember American International Group (AIG). The U.S. government gave it **$182 billion** of taxpayer money last fall in exchange for a 78 percent stake. Of that money, **$165 million** went for bonuses to a handful of people in its Financial Products Group (FPG), which sold Credit Default Swaps (CDSs) on which AIG lacked the capital to make good. And $200 million more is slated for those good folks in 2009.

Another **$12.9 billion** of our taxpayer money went to Goldman Sachs Group (GS) so AIG could pay Goldman 100 cents on the dollar for its CDSs. Hank Paulson wanted to keep the names of Goldman and the other recipients secret -- since so many of them were foreign banks, but the information leaked out in March 2009 after Paulson left office.

Now, **thanks to some solid reporting in *The New York Times***, it looks like the rot at AIG is not limited to FPG. While AIG officials have claimed that its problems were isolated to FPG, the reality is that AIG seems to have been running something akin to a shell game of massive proportions. Its shell game version took the form of selling insurance and assigning the resultant risks among its 71 different North American insurance companies.

Thanks to AIG's regulatory arbitrage -- taking advantage of the fact that its 19 state insurance regulators never conduct examinations at the same time -- AIG may have been able to shift assets among the companies to fool state regulators. If one its companies did not have enough money set aside as reserves against future claims, AIG could move assets to that reserve-deficient company right before the state insurance examiner moved in. And once that examiner was gone, AIG could in theory shift the extra cash to the next reserves-deficient company.

Want an example? Consider AIG affiliate National Union (NU). AIG indicated to Pennsylvania state insurance investigators that it had $33.7 billion in assets at the end of 2008 -- more than enough to protect against $21.9 billion in liabilities. But what the Pennsylvania regulators did not see is that $10.9 billion worth of NU's assets were investments in other AIG affiliates, which are not publicly traded and whose value is hard to measure. Subtract that and you have only $22.8 billion in assets.

But wait -- there's more. NU had $42 billion more in liabilities that the Pennsylvania regulators missed. How so? NU had obligations to pay claims of other AIG insurance affiliates -- the biggest of which was $23.1 billion that it owed AIG affiliate American Home (AH). NU owed another $19 billion to several other AIG afiiliates.

Meanwhile, AH had crushing obligations of its own. While the New York state regulators thought it had $26.3 billion in assets to a mere $19.9 billion in liabilities, the reality was far more dire. How so? AH was on the hook for an additional $120.7 billion in guarantees to 16 other AIG affiliates. Thus AH's liabilities really exceeded its assets by $114 billion.

To summarize, AIG's core insurance companies seem to be like a shell game which AIG was able to continue operating because it was able to keep the cash moving from the affiliate that one state regulator *had just examined* to the one that another state regulator was *about to examine*.

Unfortunately, it would not surprise me if this was happening and continues to happen at all big U.S. insurance companies. Moreover, I would be shocked if former AIG CEO Hank Greenberg -- who has heaped scorn on his successors -- was unaware of this practice.

Is it too early to write off that $182 billion?

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