IN THE UNITED STATES COURT OF FEDERAL CLAIMS

STARR INTERNATIONAL COMPANY, INC., on its behalf and on behalf of a class of others similarly situated	)	
Plaintiff,	)	No. 11-779C (Judge Thomas C. Wheeler)
v.	)	
UNITED STATES,	)	Filed under seal
Defendant,	)	

DEFENDANT'S STATEMENT OF CONTESTED FACTS

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DEFENDANT'S STATEMENT OF CONTESTED FACTS

Pursuant to Paragraph 4(b) of this Court's August 2, 2013 Pretrial Order, defendant, the United States, respectfully submits this pretrial statement of contested factual issues (reflected in outline headings) and contentions of fact (reflected in numbered paragraphs) that the United States expects to prove at trial. These facts supplement the parties' previously filed Joint Stipulation of Uncontroverted Facts, Dkt. No. 258-2.

THE EQUITY CLAIM

I. By AIG's Own Doing, AIG's Financial Condition Deteriorated In Late 2007 And Early 2008

1. The Government did not cause the financial distress AIG experienced in 2007 and 2008.

A. AIG Exposed Itself To Risk Through Its Credit Default Swap Portfolio And Securities Lending

2. By the beginning of 2008, AIG had massive exposure to the mortgage and housing markets, which created an enormous risk for AIG. This exposure was a result of AIG's strategy in 2005, 2006 and 2007 to invest in assets that were expected to offer returns that were higher than other lower-risk assets.

1. Credit Default Swap

3. AIG, through its wholly-owned subsidiary, AIGFP, had credit default swap (CDS) contracts exposing AIG to potential liability for notional amounts totaling hundreds of billions of dollars, including tens of billions in multi-sector collaterized debt obligations (CDOs). AIG reported revenue of $3.3 billion from AIGFP in 2005 and $5.1 billion from 2003 through 2005.

4. A CDO is an asset-backed security that provides investors with a contractual right to certain payment streams from a pool of debt instruments, such as mortgages.

5. A CDS is akin to financial insurance, whereby the CDS seller effectively guarantees the performance of CDOs.

6. If the debt referenced by a CDS is in default, the CDS seller must pay the purchaser of the CDS the amount required by the CDS contract. Specifically, if the debt referenced by a CDS undergoes a "credit event," as defined in the CDS contract, the protection buyer is entitled to payments of a specified face value, referred to as the notional amount of the reference entity debt.

7. AIG's CDS business was not subject to significant regulation, nor was AIG required to maintain reserves for this business.

8. Many of the CDSs that AIGFP sold required AIGFP to post collateral (*i.e.*, give collateral to AIG's counterparty) if (a) AIG's credit rating dropped, or (b) if the referenced CDO lost value or was downgraded.

9. The terms of AIGFP's CDS contracts exposed AIG to liquidity risk if AIG's credit rating dropped or if the referenced CDO lost value or was downgraded. Liquidity risk is the risk a firm will not be able to meet its current and future obligations including collateral calls.

10. At various times between 2003 and 2006, AIG was the largest writer of CDS contracts in the United States.

11. By December 2005, AIG decided to cease writing new CDSs on CDOs containing subprime residential mortgage-backed securities (RMBS) exposure. Despite this decision and through September 16, 2008, AIGFP continued to carry billions of dollars of risk on its existing CDS portfolio.

12. In 2007 and 2008, AIG chose not to hedge or mitigate its CDS exposure. That decision increased AIG's profit potential but also increased its risk.

13. Before September 2008, AIG did not set aside reserves to cover potential losses on its CDS portfolio.

14. AIG senior management either did not know or did not fully appreciate the significant risks presented by AIGFP.

2. Securities Lending

15. Through its securities lending program, AIG's insurance subsidiaries lent stocks and bonds on a short-term basis in exchange for cash collateral. The securities on loan were principally corporate bonds with the next two largest asset types being collateralized mortgage obligations and mortgage-backed securities.

16. All of AIG's securities lending was centralized in one subsidiary, AIG Securities Lending Corp., which invested the cash collateral on behalf of all of AIG's insurance subsidiaries.

17. AIG's securities lending business was not subject to significant regulation, and it was not required to maintain loss reserves.

18. When lending securities, AIG regularly agreed to receive collateral with a fair value less than the industry standard of 102 percent of the loaned security. This practice increased the attractiveness of AIG's securities lending program to potential customers, but significantly increased the risk to AIG.

19. Under AIG's standard securities-lending agreements, a party borrowing securities from AIG could return the securities at any time and demand the immediate return of the party's cash collateral.

20. Also under AIG's standard securities-lending agreements, if a loaned security dropped in value, AIG was responsible for returning cash collateral in an amount equal to the decline in value (*i.e.*, the negative mark).

21. AIG Securities Lending Corp. invested the cash collateral associated with the short-term, securities lending into longer-term RMBS, including both subprime and Alt-A RMBS, which is a category of mortgages of RMBS with a risk profile between prime and subprime.

22. AIG Securities Lending Corp.'s short-term securities lending and the longer-term RMBS investment created a maturity mismatch between liabilities and assets, which created risk.

23. AIG's practice of investing its securities lending collateral in RMBS continued through late 2007, even after AIG had decided against taking on additional subprime exposure in its other businesses. There was no material change in AIG's holding of RMBS securities in 2008, other than those due to valuation declines.

24. AIG's subsidiaries were exposed to significant securities lending losses.

25. As of the first quarter of 2008, AIG was exposed to a potential $9.3 billion loss on the invested, securities-lending collateral.

B. <u>AIG Suffered Losses From Its Aggressive Investments</u>

26. Before 2005, Standard & Poor's Financial Services, LLC (S&P) – a ratings agency, which publishes credit ratings on AIG – gave AIG an AAA credit rating – the highest rating available. This rating allowed AIG and its subsidiaries to borrow money at favorable terms and increased the company's profits.

27. In March 2005, S&P downgraded AIG from AAA to AA+.

28. In June 2005, S&P downgraded AIG from AA+ to AA.

29. As a result of the 2005 downgrades, AIG was required to post $1.16 billion in collateral to its CDS counterparties.

30. Over the second half of 2007, AIG realized capital losses primarily on its insurance investment portfolio totaling $3.56 billion on a pre-tax basis, and $2.31 billion on an after-tax basis. During the same period, AIG recognized a valuation loss of $11.5 billion in connection with the deteriorating market value of the mortgage-related securities referenced by AIGFP's CDS portfolio.

31. By the end of 2007, AIGFP had posted $2.9 billion of collateral to its CDS counterparties. Nonetheless, in December 2007, AIG's management did not expect to incur any material realized economic losses on AIGFP's CDS portfolio due to credit events.

32. In February 2008, AIG's independent auditor found tens of billions of dollars in projected losses due to AIG's unhedged CDS portfolio. In February 2008, AIG's auditor concluded that AIG had insufficient controls and oversight in its investments. After this finding by AIG's independent auditor, all four major rating agencies revised their outlook on AIG to negative.

33. In the first quarter 2008, AIG reported a net loss of $7.81 billion.

34. On May 8, 2008, S&P downgraded AIG's issuer credit rating to "AA-/A-1+" from "AA/A-1+".

35. On May 9, 2008, Moody's Investors Service (Moody's), another ratings agency, put AIG on review for possible downgrade, citing persistent volatility in AIG's reported results and concerns over the capital and liquidity levels of subsidiaries that hold mortgage-related positions.

36. On May 8, 2008, Fitch Ratings, Inc. (Fitch), another ratings agency, downgraded AIG's issuer default ratings and senior debt ratings to "AA-" from "AA".

37. On May 22, 2008, Moody's downgraded AIG's long-term-issuer rating and senior-unsecured-debt rating to Aa3 from Aa2.

38. AIG's May 2008 downgrades required the company to provide its CDS counterparties with additional collateral to cover anticipated losses.

39. In June 2008, A.M. Best Company, another ratings agency, downgraded AIG and its domestic life and retirement services subsidiaries based on AIG's management changes and future uncertainty given AIG's "risk appetite, exposure accumulations and capital management."

40. By June 2008, a one-notch downgrade by S&P and Moody's permitted AIGFP's CDS counterparties to make additional collateral calls for up to $13.3 billion of collateral.

41. By June 30, 2008, AIG reported that the reinvestment portfolio of its $75.1 billion securities lending operations had a fair value of just $59.5 billion, of which $36.2 billion (61 percent of the $59.5 billion fair value) consisted of "[m]ortgage-backed, asset-backed and collateralized" debt instruments.

42. AIG reported an after-tax net loss of $5.36 billion for the second quarter of 2008. AIG's loss before taxes and minority interest income for the second quarter of 2008 was $8.76 billion.

43. On the first trading day of 2007, AIG's stock price was $72.15 per share. AIG ended 2007 with a stock price of $58.30 and closed the second quarter of 2008 with a stock price of $26.46, a decline of almost 55 percent in six months.

44. In the summer of 2008, continuing calls for collateral from AIG's CDS and securities lending counterparties were rapidly draining AIG's liquidity.

45. By June 30, 2008, AIGFP had posted $13.8 billion of collateral to its CDS counterparties and by August 31, 2008, AIGFP had posted $19.7 billion of collateral to its CDS counterparties.

46. In August 2008, credit rating agencies began considering another downgrade for AIG.

47. On September 12, 2008, S&P placed AIG on CreditWatch with negative implications and noted the possibility of lowering the company's credit rating (which was "AA-" at the time) by up to three notches.

48. In the afternoon of September 15, 2008, AIG's credit ratings were downgraded by A.M. Best, S&P, Moody's, and Fitch, which triggered additional collateral calls.

49. On September 15, 2008, A.M. Best, S&P, Moody's, and Fitch also downgraded the financial strength ratings of many of AIG's insurance companies.

50. As of the evening of September 16, 2008, prior to receiving financial assistance from Federal Reserve Bank of New York (FRBNY), AIG was unable to meet its obligations as they came due the next morning.

II. <u>AIG Requested Assistance From FRBNY In September 2008</u>

51. Timothy Geithner, then-president of FRBNY, met with Robert B. Willumstad, AIG's CEO, twice in July 2008. Mr. Willumstad did not request lending assistance, and intentionally tried to avoid leaving Mr. Geithner with the impression that AIG was in need of such assistance at that time.

52. On September 9, 2008, Mr. Willumstad met with President Geithner to inform him that AIG was considering seeking to become a primary dealer. In that same meeting, Mr. Willumstad assured President Geithner that AIG had sufficient liquidity.

53. Prior to September 12, 2008, AIG had not informed FRBNY of the extent of its financial needs.

54. On Friday, September 12, 2008, senior officials at AIG met with FRBNY employees and, for the first time, informed FRBNY that AIG was facing a serious liquidity situation. AIG told FRBNY that the rating agencies might downgrade the company again later that day or on Monday, September 15. AIG assured FRBNY, however, that the company had at least two weeks of liquidity.

55. On the evening of Friday, September 12, 2008, FRBNY sent employees to AIG to seek to understand more about AIG and its needs. Over the weekend of September 13-14, 2008, FRBNY continued to discuss with AIG and analyze AIG's liquidity needs and financial condition.

56. On September 13 and 14, 2008, the Federal Reserve Board's staff met with AIG's management to understand the company's financial condition.

57. In the evening on September 13, 2008, Mr. Willumstad met with FRBNY President Geithner and Secretary of the Treasury Henry Paulson to inform them of AIG's financial condition and its ongoing attempts to secure private funding.

58. Over the weekend of September 13-14, FRBNY President Geithner asked his staff to evaluate the systemic implications of an AIG failure.

59. Throughout the morning and afternoon of Saturday, September 13, 2008, the Board of Governors and FRBNY encouraged AIG to pursue private-sector sources of funding.

III. FRBNY And The Board Of Governors Sought To Assist, Not Prevent, A Private-Sector Solution For AIG's Crisis, But The Potential Private Sector Solutions Failed

60. During the weekend of September 13-14, 2008, a number of bank presidents gathered at FRBNY to consider how Lehman Brothers could be saved. Through that same weekend, FRBNY and the Board of Governors continued to encourage AIG to pursue private-sector sources of funding.

61. AIG hired JPMorgan Chase and Blackstone Advisory Services, L.P. (Blackstone) as financial advisors to help develop funding options and strategic alternatives.

62. Blackstone canvassed the market for potential private investors in AIG during the weekend of September 13-14, 2008.

63. JPMorgan canvassed the market for potential private investors in AIG before September 15, 2008.

64. JPMorgan told AIG on September 14, 2008 that it could not "raise private equity capital" and would not itself provide financing to the company.

65. During the weekend of September 13-14, 2008, J.C. Flowers and Allianz considered a joint investment in AIG.

66. On September 14, 2008, J.C. Flowers and Allianz submitted an investment proposal to AIG (the J.C. Flowers proposal). The J.C. Flowers proposal provided for a $10 billion investment in insurance subsidiaries of AIG, with Allianz providing $5 billion and Flowers providing $5 billion. In return, J.C. Flowers and Allianz would receive 19.9 percent of the common stock of certain AIG subsidiaries, convertible into a majority of AIG's common stock.

67. The J.C. Flowers proposal was contingent on (1) AIG gaining access to the discount window, (2) a signal from the rating agencies that they would not downgrade AIG, (3) state regulatory approval to upstream $20 billion in assets from AIG's insurance subsidiaries, (4) the replacement of AIG's CEO, and (5) the new investors receiving the right to appoint two of AIG's directors.

68. J.C. Flowers and Allianz conditioned the proposal on AIG gaining access to the discount window because they could not address AIG's liquidity needs, and so planned to rely on FRBNY to "stabilize" AIG.

69. AIG rejected the $10 billion J.C. Flowers/Allianz proposal, in part because it was inadequate to meet AIG's liquidity needs, which had grown to at least $60 billion by the time the company evaluated the proposal.

70. AIG initiated a call with Warren Buffett on September 12, 2008, and faxed materials to Mr. Buffett in the hopes that Berkshire Hathaway would invest in AIG. Mr. Buffet called AIG back that night to tell Mr. Willumstad that a deal was "not feasible."

71. JPMorgan contacted KKR about a potential investment in AIG on September 12, 2008.

72. On September 13, 2008, KKR concluded that it would be too risky to invest in the AIG parent company because KKR could not determine the company's liquidity needs on such short notice.

73. On September 14, 2008, KKR told AIG that it "could [not] come up with the amount of financing required to stabilize [AIG's] balance sheet in the time available," and suggested that AIG seek financing from the Federal Reserve.

74. KKR never made a proposal to invest in AIG.

75. No sovereign wealth fund signed a letter of intent or began the steps necessary to perform due diligence on AIG's holdings.

76. Before any sovereign wealth fund could invest in AIG, the fund would need to perform weeks or months of due diligence to understand the risks involved in such an investment and obtain necessary approvals.

77. In September 2008, the China Investment Corporation (CIC) did not offer to invest in AIG or to loan the company money that was sufficient to resolve AIG's liquidity needs.

78. Neither the Government nor FRBNY sought to discourage CIC's – or any other entity's – investment in AIG.

79. On September 14, 2008, Mr. Willumstad called President of FRBNY Geithner regarding the status of private-sector efforts to assist AIG.

80. After AIG's own efforts to raise private capital failed, FRBNY sought to encourage a private-sector solution to AIG's financial needs. On September 15, 2008, in the wake of Lehman announcing its intent to file for bankruptcy, FRBNY asked JPMorgan and Goldman Sachs to attempt to syndicate private-sector funding for AIG.

81. On September 15, 2008, in developing a possible syndicated loan for AIG, JPMorgan and Goldman Sachs used a structure containing a 79.9 percent "equity kicker," *i.e.*, it contemplated that the consideration for the loan would include ownership of 79.9 percent of the equity in AIG.

82. The JPMorgan draft private-sector term sheet called for a $75 billion loan to AIG to be syndicated to 15 lenders at $5 billion each; an interest rate of LIBOR +650 basis points; a commitment fee of 500 basis points; and a 79.9 percent equity interest, in the form of warrants.

83. Late in the evening on September 15, 2008, JPMorgan and Goldman Sachs concluded that there was no possible private sector solution for AIG.

84. JPMorgan and Goldman Sachs concluded that there was not enough value in AIG to support the loan amount AIG would need. One estimate by JPMorgan was that AIG was worth, at most, $72 billion, but that AIG's liquidity needs could be $100 billion.

85. The ratings agency actions on the afternoon of September 15, 2008, described in paragraphs 48 and 49 above, greatly exacerbated AIG's anticipated liquidity needs and created further uncertainty about how much funding AIG would need. On September 5, 2008, Mr. Willumstad estimated that AIG's liquidity needs were between $13 and $18 billion depending on the magnitude of a possible downgrade. By September 16, 2008, JPMorgan estimated the liquidity need through year-end was between $80 and $100 billion and a presentation to the AIG board estimated the liquidity needs were $93 billion.

86. Ultimately, the urgency and uncertain size of AIG's financial needs made a private-sector rescue impossible.

87. As of September 16, 2008, AIG was insolvent. Without assistance from FRBNY, AIG would have had to file for bankruptcy.

88. On September 16, 2008, AIG did not expect to be able to meet its obligations as they came due the following day.

IV. The Board Of Governors Properly Authorized And FRBNY Offered The Revolving Credit Facility

A. The Board Of Governors And FRBNY Decided To Offer A Section 13(3) Loan To AIG

89. Starting on September 12, 2008, Federal Reserve officials initially indicated to AIG their sincere expectation that it was unlikely that FRBNY and the Board of Governors would provide AIG with lending. Consistent with the requirements of Section 13(3), FRBNY and the Board of Governors believed that AIG should seek private-sector solutions before turning to FRBNY as the lender of last resort. As FRBNY's and the Board of Governors' understanding of the potential systemic impacts of an AIG failure grew, however, FRBNY and the Board of Governors personnel began to reconsider their willingness to lend to AIG.

90. Section 13(3) required that FRBNY determine that AIG lacked adequate alternative credit accommodations before FRBNY could lend to AIG. Until late in the evening of September 15, 2008, FRBNY believed that AIG still had adequate, private-sector options available to it. By the morning of September 16, 2008, JPMorgan and Goldman Sachs informed Fed officials that there was no possibility of a private-sector loan.

91. During a morning meeting on September 16, 2008, FRBNY and the Board of Governors discussed the potential impact of AIG's likely failure on the broader economy and agreed that the Fed would propose a rescue loan to AIG.

92. After the discussion, FRBNY President Geithner and Federal Reserve Chairman Ben Bernanke decided to propose to the Board of Governors a Section 13(3) loan for AIG.

Treasury Secretary Paulson supported the decision to use Section 13(3) authority to provide a loan to AIG.

93. On the afternoon of September 16, 2008, the Board of Governors held a meeting to consider whether to authorize FRBNY to make a Section 13(3) loan to AIG.

94. On September 16, 2008, the Board of Governors unanimously approved a resolution that authorized FRBNY to offer an $85 billion loan to AIG pursuant to Section 13(3) of the Federal Reserve Act. The Department of the Treasury supported that decision.

95. In proposing a loan to AIG to the Board of Governors for authorization, and in subsequently making the loan that was authorized, FRBNY was not acting as an agent of the Board of Governors, subject to the Board of Governors' direction and control, but was exercising its own independent grant of discretionary authority pursuant to Section 13(3).

B. The Terms Authorized By The Board Of Governors Included An 79.9 Percent Equity Term And Did Not Limit The Form Of The Equity That Could Be Required

96. In order to assist FRBNY and the Government, on September 16, 2008, Morgan Stanley prepared a draft term sheet for a possible FRBNY revolving credit facility for AIG. The draft was based on Morgan Stanley's knowledge of the contents of the term sheet prepared on behalf of a private sector consortium that had considered lending, but ultimately did not lend, to AIG. The term sheet prepared on behalf of the private sector consortium included 79.9 percent equity consideration in the form of warrants.

97. FRBNY then asked Davis Polk & Wardwell LLP (Davis Polk) to advise it in the preparation of the term sheet.

98. After further revisions, FRBNY sent a draft of the term sheet to the Board of Governors for its review. The Board of Governors authorized an $85 billion loan to AIG

pursuant to Section 13(3) on terms "such as" those in the term sheet it reviewed, including the 79.9 percent equity term.

99. The Board of Governors minutes provided that "[t]he New York Reserve Bank may, as it deems appropriate, impose conditions on its extension of credit to AIG, such as those described in the proposed Summary of Terms for Senior Bridge Facility (Agreement)."

100. The Board of Governors resolution provided that "[t]he New York Reserve Bank may, as it deems appropriate, impose conditions, such as those in its proposed lending facility term sheet, on its extension of credit to AIG." There was no exercise price specified in the draft term sheet referenced by the Board of Governors September 16, 2008 resolution.

101. The form of the 79.9 percent equity term finalized in the Credit Agreement was consistent with FRBNY's proposal to the Board of Governors on September 16, 2008, and within the scope of the Board of Governors' prior authorization of that proposal.

V. AIG Voluntarily Accepted The Revolving Credit Facility And Its Terms

A. AIG Was Informed Of All Material Conditions Of The Loan FRBNY Was Authorized And Willing To Provide

102. Over the course of several hours on September 16, 2008, FRBNY and Treasury, along with lawyers from Davis Polk and Wachtell, Lipton, Rosen & Katz (Wachtell), made revisions to the term sheet provided to the Board of Governors, resulting in the term sheet that was offered to AIG.

103. The group drafting the FRBNY term sheet concluded that there was not enough time on September 16 to determine the form of equity.

104. The FRBNY term sheet was provided to AIG's counsel at around 4:00 p.m. on September 16, 2008, for the attorneys' consideration in advance of an AIG board meeting.

105. On September 16, 2008, Secretary Paulson and FRBNY President Geithner called Mr. Willumstad to tell him that that one condition of the FRBNY loan offer would be Mr. Willumstad's resignation.

106. The FRBNY term sheet provided to AIG's counsel did not specify the form that the equity would take. It stated that the equity participation would be "equivalent to 79.9% of the common stock of AIG on a fully-diluted basis" in a "[f]orm to be determined."

107. The FRBNY term sheet provided to AIG's counsel in advance of the AIG board meeting was the basis for the AIG board's discussions of the loan terms offered by FRBNY.

108. Neither the Government nor FRBNY ever provided AIG with a term sheet specifying that the form of equity would be warrants.

B. AIG's Board Voluntarily Decided To Accept FRBNY's Offer On September 16, 2008

109. At about 5:00 p.m. on September 16, all eleven AIG directors met to consider the terms offered by FRBNY in response to AIG's request for assistance. AIG's top management and its legal and financial advisers also attended.

110. All of AIG's directors were independent of the Government and FRBNY. The majority of AIG's directors were independent of AIG's management.

111. AIG's shareholders elected or reelected the AIG board members sitting on September 16, 2008, months or years before September 2008, with the exception of Suzanne Nora Johnson, who was elected by AIG's board on July 16, 2008.

112. Before voting to accept FRBNY's loan offer, AIG's board discussed the terms of the loan.

113. Before voting to accept FRBNY's loan offer, the members of AIG's board understood that the form of the 79.9 percent equity sought by FRBNY in exchange for the revolving credit facility was "to be determined."

114. On September 16, 2008, before voting to accept FRBNY's loan offer, AIG's board was informed by Mr. Willumstad that his resignation was a condition of FRBNY's offer.

115. On September 16, 2008, before AIG's board voted to accept FRBNY's loan offer, AIG's advisors told AIG's board that they had made extensive efforts to find a private-sector solution.

116. On September 16, 2008, before AIG's board voted to accept FRBNY's loan offer, AIG's outside counsel, H. Rodgin Cohen, informed AIG's board that, because AIG was insolvent, the board had fiduciary duties to the creditors as well as common shareholders.

117. On September 16, 2008, before AIG's board voted to accept FRBNY's loan offer, Mr. Cohen told the board that FRBNY's offer was the only alternative to bankruptcy.

118. On September 16, 2008, before AIG's board voted to accept FRBNY's loan offer, AIG's directors engaged in discussions of their duties to the company, its shareholders, and its creditors.

119. On September 16, 2008, before AIG's board voted to accept FRBNY's loan offer, AIG's directors engaged in lengthy discussions of the value of AIG's assets and AIG's liquidity needs.

120. On September 16, 2008, before voting on whether to accept FRBNY's terms, AIG's directors discussed the terms at length.

121. On September 16, 2008, before voting on whether to accept FRBNY's terms, AIG's directors engaged in lengthy discussions of the bankruptcy alternative. The directors were

advised that an AIG bankruptcy filing would cause further downgrades to AIG's credit rating and the financial strength rating of AIG's insurance subsidiaries and that an AIG bankruptcy filing would result in a surrender of existing policies and a loss due to CDS terminations.

122. On September 16, 2008, AIG's board directed Mr. Willumstad to ask FRBNY's President if the terms for the offered loan were negotiable. During a break in the AIG board meeting on September 16, 2008, before AIG's board voted to accept FRBNY's loan offer, Mr. Willumstad and AIG's attorneys called President Geithner to discuss the revolving credit facility terms and asked if FRBNY would negotiate on the equity consideration.
FRBNY President Geithner told AIG that the equity participation terms were not negotiable.

123. During the break in the AIG board meeting, Mr. Willumstad also asked FRBNY President Geithner about private-sector replacement of the loan. FRBNY President Geithner told Mr. Willumstad that if private financing was found that would pay off the FRBNY facility, and if private funds were sufficient to ensure AIG's continued viability, then the private sector could replace FRBNY.

124. On September 16, 2008, AIG's board concluded that AIG would have had a lower enterprise value in bankruptcy than under the revolving credit facility offered by FRBNY.

125. On September 16, 2008, AIG's board concluded that FRBNY's terms were preferable to the alternative of bankruptcy.

126. AIG's board members were not coerced to accept FRBNY's terms. No statute, regulation, or direct order required or coerced AIG to accept FRBNY's terms. Neither FRBNY nor the Government ever required, or suggested they required, AIG to enter into the September 16, 2008 loan agreement.

127. AIG's board members voted to accept FRBNY's loan offer.

128. On September 16, 2008, when AIG's board voted to accept FRBNY's loan offer, AIG's board knowingly authorized AIG to accept FRBNY's offer "to provide a revolving credit facility of up to $85 billion on terms consistent with those described at this meeting, including equity participation equivalent to 79.9% of the common stock of the Corporation on a fully-diluted basis (the 'Credit Facility')."

129. On September 16, 2008, when AIG's board voted to accept FRBNY's loan offer, AIG's board authorized AIG's CEO and other officers to execute and deliver all documents, contracts, and instruments evidencing or representing the Credit Facility and any arrangements related thereto.

130. AIG's board understood that by authorizing Mr. Willumstad to sign the term sheet, AIG was entering into a contract with FRBNY pursuant to which FRBNY would provide an $85 billion revolving credit facility to AIG in exchange for 79.9 percent of the equity of AIG, among other terms.

131. On September 16, 2008, upon authority of the AIG board, Mr. Willumstad executed a signature page signifying that AIG "hereby agrees to and accepts" the terms of FRBNY's offer.

132. AIG's counsel faxed the signature page of the term sheet with Mr. Willumstad's signature to FRBNY at 8:44 p.m.

C. <u>All Terms Of The Credit Facility Were Justified</u>

133. The terms and conditions of FRBNY's rescue loan, including the equity condition, were not intended to "punish" AIG but to address several important policy considerations inherent in Section 13(3) rescue lending. In particular, the terms of the loan were influenced by a desire to mitigate the moral hazard costs of rescuing AIG from bankruptcy on

highly favorable terms, and by a desire to compensate the taxpayers who ultimately bore the risk of FRBNY's assistance to AIG for the risks and costs of that loan and to allow the taxpayers to share in any value created and preserved by a successful rescue.

134. The terms and conditions of the loan addressed moral hazard concerns by seeking to minimize the windfall that AIG and its shareholders otherwise would have received from FRBNY's extraordinary assistance, which saved AIG from value-destroying bankruptcy. Minimizing the windfall that borrowers and their shareholders would otherwise receive mitigates moral hazard costs by incentivizing all market actors to prudently manage their capital and liquidity and proactively seek private-sector solutions instead of assuming that the Federal Reserve will provide rescue lending on favorable terms.

135. The terms and conditions of the loan also compensated taxpayers for the risks and costs of lending to AIG. FRBNY, and therefore ultimately taxpayers, took on significant credit risk given the size of the loan, the Federal Reserve's prior unfamiliarity with AIG, and the uncertainty of the Federal Reserve's information about AIG's solvency, financial condition, and funding needs (including AIG's inability to reliably estimate its financial needs, which ballooned from approximately $18 billion on September 12 to $85 billion just days later); uncertainty regarding the direction of the general economy; and the risk that the value of the collateral securing the loan would decrease in value in the future should AIG's financial condition continue to deteriorate notwithstanding the huge amount of financial assistance received by AIG from the FRBNY loan.

136. Equity kickers are commonly used and not unusual in lending to distressed, private entities.

137. The terms and conditions of FRBNY's rescue loan included a 79.9 percent equity interest. The market's understanding of the high risk of lending to AIG is reflected in private lenders' consideration of lending to AIG on comparable terms including a 79.9 percent equity interest, Berkshire Hathaway's decision not to make any offer, and JPMorgan and Goldman Sachs' conclusion that a loan could not be syndicated because AIG did not have enough value to justify a loan of the size AIG needed.

138. That a loan is secured, or even over-collateralized, does not make the loan risk-free, and particular features of the collateral securing the AIG loan heightened the risk of taxpayer loss even further. The loan to AIG was secured almost entirely by AIG's pledge of ownership interests in its regulated subsidiaries. This type of collateral was entirely unfamiliar to FRBNY and difficult to reliably value, particularly on the basis of the incomplete and uncertain information concerning those subsidiaries' financial strength and future business prospects. The value of ownership interests in AIG's subsidiaries was also highly correlated to AIG's risk of default. If AIG had defaulted, the value of this collateral would have dropped dramatically and immediately, leaving insufficient value to repay FRBNY's loan through asset sales.

139. The equity stake also served as a substitute for a higher interest rate and reduced the pressure on AIG's cash flow. Even the 12 percent interest rate initially charged on the revolving credit facility – which was reduced two months later – was well below comparable market yields at the time, was below the yields on AIG debt of similar maturity on September 16, 2008, and would not have fully compensated the American taxpayer for the risks of lending to AIG.

140. Because of its concern about a possible loss on the loan to AIG, the Board of Governors asked for and received a letter from Treasury acknowledging the potential reduced Federal Reserve revenues to Treasury in the event of a loss to FRBNY on the loan.

D. AIG And FRBNY Immediately Began Performance Of Their Agreement

141. After receiving the signed term sheet on the evening of September 16, 2008, FRBNY provided AIG with $14 billion to meet AIG's immediate financial needs for the next day. FRBNY provided these funds on the basis of the AIG board of directors' acceptance of the terms offered by FRBNY in the term sheet and would not have done so in the absence of that acceptance.

142. As of September 16, 2008, multiple members of the AIG board knew and respected Edward Liddy based on his experience as CEO of Allstate.

143. After AIG's board of directors vetted Mr. Liddy as a proposed candidate to replace Mr. Willumstad, Mr. Willumstad tendered his resignation to AIG's board on September 18, 2008, pursuant to the agreement between AIG and FRBNY.

144. On September 18, 2008, AIG's board appointed Mr. Liddy as Chairman and CEO, consistent with the terms to which it had agreed on September 16, 2008.

145. When AIG's board members voted to appoint Mr. Liddy the CEO on September 18, 2008, AIG's board members were independent of FRBNY and the Government.

146. On September 18, 2008, AIG filed a Form 8-K that erroneously stated that (1) AIG had entered into the Credit Agreement, (2) AIG had issued a warrant, and (3) AIG had agreed to an equity transfer that would be subject to shareholder approval. AIG and its counsel independently recognized that the 8-K was erroneous and drafted an amended 8-K to correct the errors.

147. Between September 17 and September 21, 2008, AIG borrowed another $23 billion. FRBNY would not have provided this additional funding in the absence of AIG's acceptance of the terms offered by FRBNY in the term sheet on September 16, 2008, and performance under that agreement by Mr. Willumstad's resignation.

E. AIG's Board Voluntarily Agreed To The Credit Agreement On September 21, Which Implemented The Deal Reached On September 16

148. From September 17 to September 21, 2008, AIG and FRBNY negotiated the terms of the Credit Agreement.

149. A draft of the Credit Agreement was circulated between AIG and FRBNY on September 19, 2008. The terms in the draft were consistent with the terms accepted by the AIG board on September 16, 2008.

150. A draft of Exhibit D to the Credit Agreement, which proposed that the equity term would be satisfied by preferred stock, was sent by FRBNY to AIG's counsel at 3:22 p.m. on September 21, 2008. The terms of Exhibit D to the Credit Agreement between FRBNY and AIG were further negotiated and revised before the exhibit was finalized.

151. A draft of Exhibit D to the Credit Agreement was provided to AIG's board at 6:31 p.m. on September 21, 2008.

152. The draft Credit Agreement provided for convertible preferred stock with dividend and voting rights equivalent to 79.9 percent of AIG's equity.

153. On the evening of September 21, 2008, AIG held a board of directors meeting to consider the proposed Credit Agreement. Members of AIG's senior management and its legal and financial advisers also attended.

154. With the exception of Mr. Liddy, who replaced Mr. Willumstad, AIG's board members on September 21, 2008 were the same as on September 16, 2008. All the board members, including Mr. Liddy, were independent from FRBNY and the Government.

155. On September 21, 2008, before the AIG board voted on the Credit Agreement, AIG's advisors told AIG's board that the proposed Credit Agreement was the only alternative to bankruptcy.

156. Before voting on whether to accept the terms of the Credit Agreement, AIG's directors engaged in lengthy discussions of their duties to the company, its shareholders, and its creditors.

157. Before voting on whether to accept the terms of the Credit Agreement, AIG's directors engaged in lengthy discussions regarding the alternative of bankruptcy.

158. On September 21, 2008, AIG's advisors told AIG's board that bankruptcy would be devastating for the company.

159. Blackstone advised AIG's board that FRBNY's rescue offer would give existing AIG shareholders 20 percent of the company, whereas the alternative would leave shareholders with 100 percent of a bankrupt corporation, advising that "20 percent of something was better than 100 percent of nothing."

160. Counsel to AIG advised AIG's board that, in his opinion, the board would properly exercise its business judgment if the board decided to approve the Credit Agreement; counsel to AIG advised AIG's board that he was not prepared to offer an opinion that the board had properly exercised its business judgment if the board decided to reject the Credit Agreement.

161. On September 21, 2008, when AIG's board members voted unanimously to approve the terms in the proposed Credit Agreement, neither FRBNY nor the Government held any shares of AIG.

162. Although FRBNY tracked AIG's use of FRBNY funds and overall performance between September 17 and 23, 2008, FRBNY did not control the company's decision-making between September 17 and September 23, 2008, or at any time thereafter.

163. AIG's board members were not coerced to accept the terms in the Credit Agreement. No statute, regulation, or direct order required or coerced AIG to accept the Credit Agreement's terms.

164. On September 21, 2008, AIG's board voted unanimously to accept the terms in the proposed Credit Agreement. When AIG's board took this vote, AIG's board understood the Credit Agreement's terms. AIG's board did not view the specific form of equity in the Credit Agreement as a material difference from the equity commitment in AIG's September 16 agreement.

165. AIG's board voted to approve the Credit Agreement because the board members believed that it was in the company's best interests. AIG's board members believed that the terms in the Credit Agreement were better than what would happen to the company in bankruptcy.

166. After the AIG board meeting on September 21, 2008, AIG's Audit Committee held a conference call and approved the issuance of preferred stock without a shareholder vote as provided for by New York Stock Exchange (NYSE) Listed Company Manual Rule 312.05, invoking an exemption on the ground that the delay in securing shareholder approval for the issuance of the preferred stock would seriously jeopardize AIG's financial viability.

167. AIG's Audit Committee invoked the NYSE exception for issuance of the preferred stock without a shareholder vote to prevent AIG's common stock from being delisted.

168. In 2008, AIG recorded the revolving credit facility as consideration for the Series C stock on its balance sheet. The Credit Agreement also stated that that the consideration paid for the Series C preferred stock consisted of "$500,000 plus the lending commitment of the Federal Reserve Bank of New York."

169. According to AIG's Form 10-Q for the third quarter in 2008, AIG recorded the fair value of the Series C preferred ($23 billion) as an increase to additional paid-in capital and the "value, net of the $500,000 cash portion of the consideration, was recognized as an addition to the prepaid commitment fee asset associated with the Fed Facility."

170. According to AIG's 2008 10-K, the aggregate purchase price for the Series C preferred stock was $500,000, with an understanding that additional and independently sufficient consideration was also furnished in September 2008 by FRBNY in the form of its $85 billion lending commitment under the Fed Credit Agreement.

171. According to AIG's 2008 10-K, the prepaid commitment fee asset of $23 billion associated with the Series C preferred stock was capitalized and amortized through interest expense over the five-year term of the Fed Facility. In 2008, AIG recorded an interest expense for the accelerated amortization of the prepaid commitment fee of $6.6 billion ($4.3 billion after tax).

172. AIG believed that the post-Credit Agreement transactions would "enhance AIG's ability to generate taxable income from the sales of businesses under its asset disposition plan, continue the earnings strength of the insurance businesses it intends to sell, and underscore the

United States Government's commitment to the orderly restructuring of AIG over time in the face of continuing market dislocations and economic deterioration."

173. AIG's certificate of incorporation included a provision expressly permitting AIG's board without a shareholder vote to issue "blank check preferred" stock, which could include rights upon liquidation or dilution, super voting rights, priority dividend rights, priority redemption rights, and rights of conversion.

174. When they purchased their shares, none of the Credit Agreement class members had any reasonable, investment-backed expectation that the Government would provide AIG with rescue lending at preferential rates that would keep the company from having to file for bankruptcy in the event it became unable to meet its obligations as they came due.

VI. There Could Be No Illegal Exaction Because The Board Of Governors And FRBNY Had The Authority To Seek The Conditions To Which AIG Agreed

A. Well In Advance Of FRBNY's Assistance To AIG, Both The Board Of Governors And FRBNY Concluded That They Could Seek Conditions On Section 13(3) Lending

175. The Board of Governors and FRBNY carefully considered their authority to require particular terms and conditions on Section 13(3) lending, including terms and conditions not expressly enumerated in the text of the Federal Reserve Act, in connection with FRBNY's March 2008 lending in connection with Bear Stearns.

176. In March 2008, FRBNY attorneys, including General Counsel Thomas Baxter, considered FRBNY's authority under the Federal Reserve Act and concluded that FRBNY could permissibly condition its lending on a borrower's agreement to convey a majority equity interest. FRBNY's attorneys informed FRBNY President Geithner of their analysis, and explained how conditioning lending on the provision of equity was permissible under the Federal Reserve Act.

177. In April 2008, FRBNY attorneys memorialized their analysis underlying FRBNY's lending in connection with Bear Stearns, the consideration for which had included, in addition to interest payments, the right to the residual value of the assets held by a special purpose vehicle called Maiden Lane ("Maiden Lane I"). In a formal legal opinion, the attorneys concluded that the Federal Reserve Act permitted FRBNY to obtain the right to the residual value of these assets, which they noted was very similar to an equity interest.

178. Also in April 2008, Board of Governors attorneys, including General Counsel Scott Alvarez, similarly concluded in a formal legal opinion that the Federal Reserve Act permitted the Federal Reserve to condition its lending on receiving the right to the residual value of the assets held by Maiden Lane I when so authorized by the Board of Governors. In particular, the attorneys concluded that "Section 13(3) allows the Board to authorize any Federal Reserve Bank to extend credit to any IPC . . . 'subject to such limitations, restrictions and regulations as the [Board] may prescribe.' The Board, therefore, has complete statutory discretion to determine the timing and the conditions of lending under section 13(3)."

179. In early July 2008, in connection with a series of meetings convened by President Geithner to consider potential options to avoid or mitigate the failure of a non-bank institution that could have systemic effects on the economy, FRBNY attorneys revisited the Federal Reserve's authority to impose particular terms and conditions on lending. FRBNY attorneys prepared a formal legal opinion again concluding that FRBNY could permissibly obtain an equity interest as a condition of lending under Section 13(3), and again presented their conclusions and analysis to President Geithner.

180. In conversations with President Geithner and the Board of Governors on September 16, 2008, Messrs. Baxter and Alvarez both confirmed their conclusions that the

Federal Reserve could permissibly condition lending on AIG's agreement to convey an equity interest as partial consideration for the proposed loan.

B. The Decision To Use A Trust Structure Was Intended To Address Policy And Prudential Concerns, But Also Had the Collateral Benefit of Obviating The Need For Further Consideration Of FRBNY's Or Treasury's Authority To Hold Equity

181. After the Board of Governors and FRBNY concluded on September 16, 2008 that FRBNY's lending to AIG could permissibly be conditioned on AIG's agreement to provide equity, FRBNY and the Government continued over the following week to consider what form that equity should take and what entity should hold the equity. These discussions raised prudential, policy, and legal considerations, including some questions related to legal authority.

182. FRBNY had concluded through its analyses over the spring and summer of 2008 that it could not only permissibly condition its lending on a borrower's agreement to provide equity, but also could hold that equity itself. FRBNY, nonetheless, preferred not to hold AIG's equity for various policy and prudential reasons. In particular, in its role as a component of the central bank, FRBNY typically has access to highly-sensitive, material, non-public information about companies, markets, economic trends, and market policies. FRBNY was concerned that access to this information would create a conflict of interest if it also held a majority economic or voting interest in AIG. The Board of Governors shared these concerns. The Board of Governors and FRBNY were also concerned with the possible public perception of the Government owning a portion of AIG and possibly providing the company with preferential treatment.

183. In September 2008, FRBNY suggested using a trust structure to address these policy and prudential concerns by placing control of the AIG equity interest with an independent entity that was not subject to potential conflicts. FRBNY had used trust structures in the past to separate legal ownership from control.

184. Although the reason for using a trust structure was to address these policy and prudential concerns, doing so also had the collateral benefit of obviating the need for further consideration of FRBNY's or Treasury's authority to hold equity, as both FRBNY and the Government agreed that using a trust structure was legally permissible.

185. The decision to use a trust structure was not intended to wrongfully circumvent any purported prohibition on FRBNY's or Treasury's ability to hold shares.

186. The Trust was intended to be independent from FRBNY and the Government.

187. To protect the taxpayers' interest in the trust equity, FRBNY recruited trustees for the Trust that FRBNY believed to be competent, trustworthy, and independent.

188. The Credit Facility Trust Agreement, which created the Trust, was the result of arms-length negotiations between FRBNY and the potential trustees, and granted the trustees full discretionary authority to vote the Trust stock.

189. The Trust was, in fact, independent from FRBNY and the Government. The trustees were likewise independent.

190. The Trust Agreement unremarkably provided for indemnification of the trustees so long as they acted consistently with the best interests of the U.S. Treasury (that is, the public fisc), the Trust's sole beneficiary, but in no way required the trustees to act at the direction of FRBNY or the United States.

191. Pursuant to the Trust Agreement (and the Series C Stock Purchase Agreement), AIG issued the Series C directly to the Trust in March 2008.

192. Although the trustees discussed AIG with FRBNY and the Government, they retained their own independent advisors, including legal counsel, and also met directly with

AIG's board, management, and outside advisors. The trustees always acted pursuant to the exercise of their own independent judgment.

193. The new directors elected to AIG's board of directors at AIG's 2009 annual shareholder meeting were initially identified by the trustees, with the assistance of an independent executive search firm, and then went through AIG's standard nominating process, including review by AIG's nominating committee.

VII. The Credit Agreement Class Members Did Not Suffer An Economic Loss, And Received A Net Economic Benefit From The Government's And FRBNY's Actions

A. An AIG bankruptcy Would Have Destroyed The Company's Remaining Value, And Made Plaintiffs' Investments Worthless

194. On September 16, AIG understood that no private-sector solution existed for its liquidity problems; to continue operating outside of bankruptcy, AIG would require Federal assistance.

195. As of September 16, AIG did not have the ability to execute an orderly chapter 11 bankruptcy through which the company might have survived as a going concern.

196. Because AIG had not planned for bankruptcy, there was an increased chance of a "free fall" bankruptcy that would have resulted in an even lower enterprise value for AIG than if it had filed bankruptcy with proper planning.

197. In bankruptcy, the holders of AIG's common stock would have been the lowest priority claimants, and would have stood behind all of AIG's creditors, holders of preferred stock, and any other claimants in priority of payment. In an unplanned bankruptcy, AIG's common stock would have continued to lose value.

198. Bankruptcies are disruptive and expensive, especially for insurance companies, whose business models depend on consumer confidence and succeed based on their ability to write and renew coverage policies.

199. An AIG bankruptcy would have destroyed the company's reputation and crippled AIG's core business operations through a loss of consumer confidence, the departure of qualified personnel from the company, an inability to write new coverage policies, and a flood of policy cancellations (including in AIG's key property and casualty businesses).

200. AIG's inability to pay its debts as they came due on September 17, and the resulting bankruptcy, would have forced the rating agencies to downgrade the company to a "D" (default). Such a severe downgrade of AIG would have had negative effects on AIG's operating subsidiaries through regulatory requirements and counterparty agreements referencing the parent-company's credit ratings.

201. If AIG had filed for bankruptcy, there was a high likelihood that state and foreign insurance regulators – who are responsible for and primarily concerned with protecting policy holders in their jurisdictions – would have eventually seized many of AIG's insurance subsidiaries to protect them from the risk of losses elsewhere in the company.

202. In bankruptcy, the transfer of capital and cash between AIG's insurance subsidiaries and the AIG parent would have ceased or been delayed, causing a significant liquidity strain on AIG's insurance subsidiaries and AIG parent.

203. In bankruptcy, AIG's securities lending counterparties would have accelerated their demands to end their securities lending contracts with AIG Securities Lending Corp., requiring the return of cash collateral and forcing AIG to liquidate its investments at fire-sale

prices. This would have led to significant, realized losses for AIG, as well as further liquidity issues for AIG's insurance subsidiaries.

204. In bankruptcy, AIG's counterparties would have filed deficiency claims on CDS contracts well in excess of accounting-based liabilities and would have asserted deficiency claims based on a contract close-out at the lower "bid" price, while AIG had previously posted collateral based on the mid-market price (the mid-point between bid and ask).

B. The Government's And FRBNY's Intervention Saved AIG from Bankruptcy and Gave the Shareholders A Net Economic Benefit

205. The revolving credit facility not only allowed AIG and its shareholders to avoid the catastrophic consequences of bankruptcy, it added additional value to the company by providing a below-market-rate loan as well as an ongoing, implicit indication of expected Government support.

206. The Credit Agreement class members – when they purchased their shares – did not possess a reasonable, investment-backed expectation that AIG was entitled to a below-market rescue loan from FRBNY.

207. The value created by the revolving credit facility to the shareholders was immediately reflected in the price of the AIG's common stock.

208. By September 2008, AIG's common stock had been in a state of steady decline since at least the fourth quarter of 2007, losing over 90 percent of its value between January 1, 2008, and September 1, 2008.

209. AIG's stock continued to fall until September 16, 2008, when the possibility of a Government rescue leaked to the market. In response to the news, the price of AIG's common stock immediately began to rise.

210. AIG's stock price continued to climb over the following days as FRBNY continued providing liquidity to the company.

211. By the time the Credit Agreement was signed, the price of the company's common stock was priced more than four times than what it had been at its lowest on September 16, when the company faced bankruptcy.

212. The company's total market value of equity, which increased as a result of the rescue, reflects the value created by the revolving credit facility.

213. Because of the value added by FRBNY's loan, the shareholders' remaining 20 percent share of the company at the end of the class period was worth more than their 100 percent share of the company at the beginning of the class period.

C. Even With The Credit Facility, AIG Teetered Near Bankruptcy In 2008 And Later, And Required More Federal Assistance That Would Not Have Been Provided If AIG Had Failed On September 16, 2008

214. Even after entering into the revolving credit facility, AIG's financial needs continued to be substantial.

215. Beginning on September 17, 2008, FRBNY placed FRBNY representatives on-site at AIG to track AIG's use of FRBNY funds and overall performance.

216. As is common for lenders to distressed companies, FRBNY and Treasury representatives attended certain AIG board meetings. However, neither FRBNY nor Treasury representatives had any voting power at AIG board meetings.

217. FRBNY asked AIG for the opportunity to review SEC filings and "broadly [distributed] communications that refer to or describe the credit arrangements." FRBNY did not generally review AIG's statements.

218. Mr. Liddy kept FRBNY apprised of AIG's significant plans, but did not seek or obtain approval from FRBNY for his business decisions.

219. FRBNY did not usurp the business judgment of AIG's management.

220. AIG's financial needs continued to increase in late September and early October 2008, in large part because of the company's securities lending program and CDS portfolio.

221. In October 2008, FRBNY sought to provide additional financing to AIG but the Board of Governors was reluctant to lend additional money to AIG because it was concerned about AIG's financial prospects, even with Government assistance. The Board of Governors nonetheless authorized a securities lending facility on October 6, 2008, whereby AIG would lend up to $37.6 billion in investment-grade, fixed income securities to FRBNY in return for cash collateral.

222. To alleviate continuing financial pressure on AIG, in October 2008, FRBNY and AIG agreed that AIG could lend securities to FRBNY for cash. This temporarily slowed the financial drain from AIG's securities lending.

223. To obtain liquidity in October 2008, AIG loaned residential mortgage-backed securities – where AIG's reinvested collateral was tied up – to FRBNY in exchange for cash collateral.

224. FRBNY's securities borrowing program was subsequently replaced by Maiden Lane II, which permanently resolved AIG's securities-lending liquidity issues.

225. Prior to November 2008, AIG sought to restructure its CDS portfolio, but AIG's counterparties would not agree to any concessions on AIG's contractual obligations under the CDS agreements.

226. On November 6, 2008, AIG asked FRBNY to negotiate with AIG's counterparties on AIG's behalf. FRBNY's efforts to negotiate counterparty concessions were not successful.

227. Before the November 10, 2008 deadline for AIG to announce its third-quarter earnings, the ratings agencies indicated that the expected losses would result in another downgrade, which would result in further collateral calls by AIG's CDS counterparties.

228. On November 10, 2008, AIG reported a 2008 third-quarter loss of $24.5 billion.

229. If downgraded in October or November 2008, AIG would have been required to post over $40 billion of cash collateral under its CDSs and likely would have had to file for bankruptcy.

230. On November 10, 2008, the Government, FRBNY, and AIG agreed to a restructuring of the revolving credit facility to help AIG avoid downgrades and bankruptcy.

231. In November 2008, as part of the November 2008 restructuring, Treasury exercised its authority under the Troubled Asset Relief Program (TARP) to purchase $40 billion of AIG Series D Cumulative Preferred, which was senior to the Series C preferred stock that subsequently was issued to the AIG Credit Facility Trust.

232. In connection with its $40 billion TARP investment, Treasury received warrants to purchase two percent of AIG common stock.

233. As part of the November 2008 assistance, the initial credit facility was restructured. The Credit Agreement was revised to reduce the fees and interest rate charged to AIG, and to extend the revolving credit facility's maturity to September 2013.

234. Also as part of the November 2008 assistance, FRBNY agreed to lend up to $30 billion to Maiden Lane III LLC ("Maiden Lane III"), a special purpose vehicle that used the proceeds of FRBNY's loan to purchase certain multi-sector CDOs underlying CDSs written by

AIGFP. Upon purchase of the underlying CDOs, the CDS contracts were terminated. By December 31, 2008, Maiden Lane III had purchased a total of $62.1 billion in par amount of CDO securities, terminated the associated CDSs, and thus eliminated AIG's exposure to its volatile CDS portfolio.

235. Even after the November 2008 restructuring, AIG continued to lose billions of dollars in the fourth quarter of 2008. AIG reported $61.7 billion in losses for the fourth quarter of 2008.

236. Without further Government assistance, AIG's fourth quarter losses would have caused a ratings agency downgrade.

237. If AIG had been downgraded in March 2009 after it announced its fourth quarter losses, it would have been forced into bankruptcy.

238. In March 2009, Treasury made $30 billion of TARP funds available to AIG in exchange for non-cumulative Series F Preferred Stock.

239. The Series F Preferred Stock was senior to the Series C stock held by the AIG Credit Facility Trust.

240. In April 2009, the Credit Agreement was revised again to drop the effective interest rate to 4.25 percent.

D. The January 2011 Recapitalization Provided Significant Value For AIG's Common Shareholders

241. In 2010, Treasury, FRBNY, the Trust, and AIG, engaged in extensive negotiations regarding the Government's exit from its AIG investments. These negotiations closed in January 2011 and resulted in a recapitalization of AIG. The goal of the January 2011 recapitalization was to deleverage AIG so that it could maintain an "A" rating without Government support.

242. One of the issues considered during the negotiations preceding the January 2011 recapitalization was the ultimate disposition of the Series C preferred stock. At one point, the parties considered canceling the Series C shares for no compensation.

243. During the negotiations preceding the 2011 recapitalization, the Trust insisted that the Series C shares not be canceled. Instead, the Trust demanded that the number of common shares to be exchanged for the Series C be broken out in the Recapitalization Term Sheet to reflect the formula for the number of shares that would have been obtained upon conversion according to the Credit Agreement and Certificate of Designations.

244. AIG's exchange of common shares for the Trust's Series C was made according to a predetermined formula, as disclosed by AIG to the SEC.

245. The Trust had the right both to transfer the Series C shares and to require AIG to issue depository shares in connection with the Series C that could have traded publicly. The 2011 recapitalization benefited AIG's public shareholders relative to these other potential ways of making the Series C preferred shares more liquid.

246. During the negotiations preceding the January 2011 recapitalization, Treasury made a concession to leave 7.9 percent of the post-exchange equity in the hands of the common shareholders.

VIII. Starr Waited To Receive The Full Benefit From FRBNY And The Government's Many Forms Of Assistance

247. Although Starr claims the terms of FRBNY's September 2008 rescue of AIG were illegal, it waited years, until AIG had received the full benefit of that rescue, before filing suit. Between September 2008 and January 2011, FRBNY and the United States collectively provided about $182 billion in emergency support to prevent AIG from failing. Starr never took

action during that time to challenge the Board of Governors' or FRBNY's conduct as beyond their statutory authority or as a taking of private property without just compensation.

248. Instead, Starr repeatedly asked FRBNY and the United States to *voluntarily* reduce the size of the equity interest to facilitate potential private capital raises by AIG. Starr never asserted as part of these requests that the equity interest was legally invalid or exceeded FRBNY's or the Board of Governors' authority, or that AIG's agreement to provide the equity interest violated Constitutional standards.

IX. Even If The 79.9 Equity Interest Exceeded FRBNY's And The Board of Governors' Statutory Authority, AIG Agreed to Convey The Economic Equivalent Of 79.9 Equity Interest

249. AIG agreed that, in return for its rescue, it would convey the economic equivalent of what it agreed to, in the event any term proved to be invalid, illegal or unenforceable.

250. Specifically, Section 8.12 of the Credit Agreement, to which AIG agreed, provides: "[i]n the event that any one or more of the provisions contained in this Agreement . . . should be held invalid, illegal or unenforceable in any respect . . . [t]he parties shall endeavor in good faith negotiations to replace the invalid, illegal or unenforceable provisions with valid provisions the economic effect of which comes as close as possible to that of the invalid, illegal or unenforceable provisions."

251. There are numerous alternative forms of economically equivalent consideration common in banking and in financing of distressed entities that would have been legally valid even if Starr were to establish that FRBNY and the Board of Governors exceeded their authority in conditioning lending on AIG's conveyance of preferred shares.

252. Even if FRBNY and the Board of Governors exceeded their authority, Starr did not suffer a compensable injury because AIG was contractually bound to provide an economically equivalent alternative.

THE DISMISSED EQUAL PROTECTION CLAIM

X. At The Time That AIG Needed A Rescue In September 2008, AIG Was Not Eligible For, Or Able To Be Rescued By, Alternative Federal Funding Or Lending Facilities

A. AIG Could Not Borrow Sufficient Funds From The Discount Window To Alleviate Its Financial Crisis In September 2008

253. Access to discount window lending, which allows eligible institutions to borrow money on a short-term basis, is limited by Section 19(b) of the Federal Reserve Act to depository institutions that maintain reservable accounts with the Federal Reserve.

254. In September 2008, AIG was statutorily ineligible to access FRBNY's discount window because it was not an eligible depository institution as defined in section 19(b) of the Federal Reserve Act.

255. Even if AIG had been statutorily eligible to access the discount window, it did not have sufficient collateral to secure a discount window loan of the size necessary to meet AIG's enormous financial needs in September 2008. Ownership interests in wholly-owned subsidiaries of a borrower – the collateral that secured FRBNY's $85 billion Section 13(3) rescue loan to AIG – are ineligible for pledge at the discount window.

256. Even if AIG had been statutorily eligible to access the discount window, AIG required a credit facility with a longer term than the 90-day maximum available under the discount window because there was no expectation that any of AIG's liquidity outflows related to its CDS or securities lending portfolios would be returned to AIG in the short-term, if at all.

257. In September 2008, AIG owned a small thrift that was an eligible depository institution with access to the discount window. The potential assistance that AIG's thrift could provide to AIG by borrowing from the discount window was significantly less than AIG's financial needs, as it only had available assets sufficient to collateralize a discount window loan of several million dollars.

B. AIG Was Ineligible To Become A Bank Holding Company, And Becoming A Bank Holding Company Would Not Have Alleviated AIG's Financial Crisis

258. In September 2008, AIG was not a bank holding company and did not own a bank.

259. AIG never applied to become a bank holding company. Unlike other entities that became bank holding companies in September 2008, AIG could not quickly have altered its structure to meet the requirements of the Bank Holding Company Act.

260. Even if AIG could have become a bank holding company, doing so would not have increased AIG's borrowing ability. Bank holding company status does not provide access to the discount window or any other source of Federal Reserve lending.

261. The benefit of becoming a bank holding company is not direct access to additional funding but possibly enhanced market confidence, resulting in part from becoming subject to heightened regulation and supervision by the Board of Governors.

262. Becoming a bank holding company would not have been sufficient to address AIG's funding needs. AIG required billions of dollars of emergency funding, not enhanced market confidence.

C. AIG Was Ineligible To Borrow From The Primary Dealer Credit Facility, And Even If It Had Been Eligible, It Did Not Have Adequate Collateral To Borrow Enough To Alleviate Its Financial Crisis

263. On March 16, 2008, the Board of Governors authorized FRBNY to establish the Primary Dealer Credit Facility (PDCF). The purpose of the PDCF was to enhance liquidity in the overnight repo markets, an important part of the national financial system, by providing overnight loans against a specified range of collateral to eligible entities that had an established trading relationship with FRBNY, known as primary dealers.

264. Primary dealers are banks or securities broker-dealers that do large-scale business trading in Treasury securities and act as FRBNY's counterparties in open market operations. Primary dealers are required to submit meaningful bids when new Treasury securities are auctioned and to provide the Federal Reserve's trading desk with helpful market information. In 2008, there were fewer than 20 primary dealers, none of which were insurance companies.

265. Because the scope of the Board of Governors' March 16, 2008 resolution authorizing the creation of the PDCF was limited to primary dealers, FRBNY could not extend PDCF lending to institutions that were not primary dealers. AIG was not a primary dealer in 2008, and never applied to become one.

266. AIG did not meet the eligibility criteria for becoming a primary dealer. The only entities eligible to become primary dealers were (1) United States chartered banks that were subject to official supervision by bank supervisors, and (2) broker-dealers registered with and supervised by the Securities and Exchange Commission (SEC).

267. Primary dealer applicants were required to demonstrate their activity levels in the various markets in which the FRBNY's domestic trading desk transacted and their ability to provide sizable, sustained performance in operations in those markets. AIG's internal planning

documents in August and September of 2008 reveal that AIG realized it would not be able to have the necessary resources and infrastructure in place to act as a primary dealer until well into 2009, many months after it would have failed in September 2008.

268. AIG also could not meet the minimum capital requirements required of primary dealers. AIG's consolidated GAAP capital in September 2008 was negative $13.5 billion, largely as a result of the huge capital hole at AIG's Financial Products subsidiary, the very entity AIG had previously contemplated having apply for primary dealer status.

269. Even if AIG had been eligible to access the PDCF, AIG did not have sufficient PDCF-eligible collateral to pledge in the amount necessary to meet AIG's massive needs in September 2008. Initially, PDCF-eligible collateral was limited to investment grade debt securities such as Treasuries, corporate debt securities, and certain mortgage-backed securities. On September 14, 2008, the Board of Governors approved an expansion of PDCF-eligible collateral to permit lending against collateral that could be pledged in the tri-party repo systems of the two major clearing banks. Although this expansion of PDCF-eligible collateral permitted the pledge of certain publicly traded equities with readily determinable market values, ownership interests in wholly-owned subsidiaries of a borrower remained ineligible for pledge.

270. Additionally, even if AIG had been eligible to access the PDCF, the overnight loans available under that facility could not have provided AIG with the long-term, massive support of the type that AIG needed and ultimately received. As with short-term discount window lending, overnight PDCF loans could not have met AIG's needs because there was no expectation that AIG's liquidity outflows related to its CDS or securities lending portfolios would be returned to AIG in the short-term, if at all.

D. FRBNY And Treasury Did Not Have Authority To Offer Other Potential Assistance To AIG

271. In September 2008, FRBNY did not have the authority to guarantee AIG's obligations.

272. In September 2008, Treasury did not have the authority to inject equity into companies.

273. On October 3, 2008, the Emergency Economic Stabilization Act (EESA) was signed into law.

274. EESA authorized the Secretary of the Treasury to establish TARP.

275. TARP provided Treasury with new tools to address the financial crisis.

276. Treasury's Asset Guarantee Program was created pursuant to EESA, and did not exist in September 2008.

THE REVERSE STOCK SPLIT CLAIM

XI. No One Represented To The Court In The *Walker* Litigation That Common Shareholders Would Have A Separate Class Vote On A Reverse Stock Split Or Before The Trust Disposed Of Its Preferred Shares

277. On November 4, 2008, AIG shareholder Wilma Walker sued AIG and its directors in the Delaware Court of Chancery, seeking a declaration that the preferred shares AIG agreed to issue to the Trust were not convertible unless the common stockholders had a class-only vote to increase the number of authorized shares and/or to decrease the par value of common stock.

278. During a November 7, 2008 telephonic conference with the Court of Chancery, counsel for AIG confirmed that, as Delaware law required, "any amendment to its certificate of incorporation to increase the number of authorized shares of common stock or to change the par value of that stock requires a class vote of holders of record of a majority of the shares of common stock outstanding on the record date of that vote," and that "to the extent the separate

class vote is required, [the Series C preferred shares] do not get to vote on that class vote."

279. On January 22, 2009, Ms. Walker's counsel submitted "a proposed Stipulation and Order of Dismissal" on behalf of all parties, which the Court of Chancery signed on February 5, 2009.

280. The Court of Chancery February 5, 2009 order recited that "based on" AIG's representation that "any amendment to the Restated Certificate of Incorporation to increase the number of authorized common shares or to decrease the par value of the common shares would be the subject of a class vote by the holders of the common stock," "plaintiff's counsel agreed that the plaintiff's request for an order granting this relief is moot."

281. At no point did AIG — or the Government, FRBNY, or the Trust — represent that there would be a separate class vote on any proposed amendment to AIG's certificate of incorporation to change the number of AIG's outstanding common shares, or to allow the Series C preferred shares to be traded for common shares.

282. Neither FRBNY nor the Government nor the Trust was a party to, made an appearance in, or made any representation to the Court during the *Walker* lawsuit.

283. AIG represented to the Court of Chancery only that the company would adhere to its statutory obligations if it proposed an amendment — not that it would propose any particular amendment, or that it would afford shareholders any other voting rights not provided for by Delaware law.

284. AIG held a class-only vote on the authorization of additional shares of common stock at its June 2009 annual shareholders meeting.

285. The reverse stock split proposal did not change the number of authorized shares.

XII. The Vote Called For In the Credit Agreement Reflected Delaware Law Requirements In The Event Of A Conversion And Did Not Give Shareholders A Right To Vote On Any Other Way The Trust Might Monetize Its Equity Interest

286. Annex D to the Credit Agreement contemplated that AIG would call a shareholder meeting to vote on charter amendments increasing the number of authorized shares of common stock and reducing the par value of AIG's common stock as well as any other measures necessary for the conversion of the preferred stock.

287. The shareholder vote provision of Annex D reflects Delaware law, which gives common shareholders a right to vote as a class on any amendments to the AIG charter that would increase or decrease the number or par value of authorized shares of common stock.

288. The Trust had several options to monetize its equity interest other than conversion of the preferred C shares; these other options did not require a class-only vote of the common shareholders.

289. The Credit Agreement contained no promises to AIG common shareholders, as it was an agreement between AIG and FRBNY and explicitly stated that nothing in the agreement was intended to confer upon any third parties any rights, remedies, obligations, or liabilities.

XIII. AIG Decided To Put Off A Charter Amendment Vote

290. Although AIG considered holding a special shareholders meeting to put to a shareholder vote the charter amendments necessary for conversion of the Series C preferred stock into common stock, AIG informed counsel for the Government in January 2009 that AIG was no longer prioritizing this meeting.

291. Thus, AIG informed the Government that it intended to put off shareholder meetings that AIG had initially planned.

292. At that point in time, the Series C had not been issued, and there were no present

plans to convert the Series C into common stock.

293. The Series C Securities Purchase Agreement and Certificate of Designations were drafted, and the Credit Agreement amended for the third time, to confer on the Trust the sole discretion to direct AIG at some future time to hold votes to increase the number of authorized shares of AIG common stock and decrease the common stock's par value.

294. AIG and FRBNY voluntarily agreed to terms in the Series C Securities Purchase Agreement and Certificate of Designations and in the amended Credit Agreement that the Trust had the sole discretion to direct AIG at some future time to hold the votes to increase the number of authorized shares of AIG common stock and decrease the common stock's par value.

295. AIG publicly disclosed in Form 10-K for the 2008 fiscal year, filed with the SEC on March 2, 2009, that the Trust had the sole discretion to direct AIG at some future time to hold the votes to increase the number of authorized shares of common stock and decrease the common stock's par value. In a Form 8-K, AIG also disclosed the third amendment to the Credit Agreement.

XIV. AIG — Not The Government, FRBNY, Or The Trust — Decided To Propose The Reverse Stock Split And Decided The Split's Terms

296. In October 2008, the NYSE sent a letter to AIG warning that the company was at risk of being delisted under NYSE rules because the company's common stock was trading at a low price per share. NYSE "noted that [AIG's] common stock has recently been trading at levels below $5.00 per share," and "[a]ccordingly, [NYSE] wanted to draw [AIG's] attention to" the requirement that NSYE-listed companies have an "[a]verage closing share price of not less than $1.00 over a 30 day trading period."

297. AIG decided to propose a reverse stock split because it wanted to raise its share price and avoid the adverse consequences of delisting. AIG also sought to raise its stock price

through a reverse stock split because many institutional investors would not invest in stocks that traded below a certain level, such as $5.00 or $10.00 a share.

298. David Herzog, AIG's Chief Financial Officer, developed the idea of a reverse stock split to increase the trading price of AIG common stock and thereby prevent delisting. AIG told officials at FRBNY that the reverse stock split was intended to increase trading price so as to avoid delisting.

299. The concept of a reverse stock split first appeared in writing in a draft proxy statement circulated by AIG's counsel Sullivan & Cromwell in December 2008, with a proposed 1:10 ratio – before AIG decided to postpone the shareholder votes to increase the number of authorized shares of AIG common stock and to decrease the common stock's par value.

300. In December 2008, AIG's draft proxy included *both* (1) a proposal that would increase authorized shares and decrease the common stock's par value to permit the conversion of the preferred shares to be issued to the AIG Credit Facility Trust and (2) a reverse stock split proposal.

301. Based on its internal analysis and external advice, AIG determined to propose a stock split ratio of 1:20 to achieve a desired price range for its common stock.

302. AIG decided to apply the reverse stock split only to issued shares, and not to authorized shares, due to the already complex nature of the June 2009 proxy statement.

303. On May 20, 2009, AIG's board of directors approved the proxy statement, which was filed on June 5, 2009.

304. In the proxy statement, AIG explained:

> The primary purpose of the reverse stock split is to increase the per share trading price of AIG Common Stock. AIG believes a reverse stock split will increase the price of AIG Common Stock and thus allow a broader range of institutional investors to invest in AIG

> Common Stock, increase other investor interest in AIG Common Stock and help ensure the continued listing of AIG Common Stock on the NYSE.

305. The proxy statement also expressly disclosed:

> An overall effect of the reverse stock split of the outstanding AIG Common Stock will be a reduction of the total number of outstanding shares of AIG Common Stock approximately in proportion to the one-for-twenty reverse stock split ratio and therefore an increase in authorized but unissued shares of AIG Common Stock. *AIG currently has no plans for these authorized but unissued shares of AIG Common Stock* other than those shares previously reserved for issuance under AIG's Equity Units, the Warrants and AIG's employee benefit plans. (Emphasis added.)

306. On June 18, 2009, Glass Lewis, a proxy advisory service, recommended voting in favor of the reverse stock split.

307. The Government, FRBNY, or the Trust had no involvement in (1) the decision to propose a reverse stock split, (2) the split's ratio, or (3) whether the split would apply only to issued shares. AIG independently made those decisions. The Government, FRBNY, or the Trust did not initiate, orchestrate, or press for those decisions.

308. The Government, FRBNY, and the Trust's involvement in the June 2009 shareholder vote was limited to reviewing drafts of the proxy statement that AIG sent them, but neither the Government, nor FRBNY, nor the Trust provided substantive comments or proposed changes concerning the reverse stock split.

XV. The Common Shareholders Were Aware Of The Potential Effects Of The Reverse Stock Split And Voted In Favor Of It

309. The June 30, 2009 AIG proxy statement contained a table disclosing the number of common shares that would be authorized, issued, and unissued if the reverse stock split (Proposal 4) was approved:

Number of shares of AIG Common Stock	If Proposal 3 is approved, but Proposal 4 is not	If Proposal 4 is approved, but Proposal 3 is not	If Proposals 3 and 4 are both approved
Authorized	9,225,000,000	5,000,000,000	5,211,250,000
Issued	2,948,018,614	147,400,931	147,400,931
Reserved but unissued	395,343,040	19,767,152	19,767,152
Authorized but unissued and unreserved	5,881,638,346	4,832,831,917	5,044,081,917

310. These disclosures informed common shareholders that — although the reverse split would not change their current percentage ownership of AIG common stock — approving the split would have the effect of making available for future issuance approximately 5 billion shares of common stock, nearly 97 percent of the total number of authorized shares.

311. The proxy statement also explained that, if the reverse stock split passed, "[i]n the future, these [authorized but unissued] shares may be issued by AIG's Board of Directors in its sole discretion. Any future issuance will have the effect of diluting the percentage of stock ownership and voting rights of the present holders of AIG Common Stock."

312. The preferred and common shareholders voted to approve the reverse stock split on June 30, 2009. Although the common shareholders did not vote as a separate class, a majority of common shareholders, including Starr itself, voted for the reverse stock split.

XVI. The Reverse Stock Split Was Not Related To Converting Or Exchanging The Trust's Series C Preferred Stock

313. AIG's decision to propose the reverse stock split was unrelated to its plans for the Trust's Series C preferred stock.

314. The $2.50 par value of AIG's common stock created an independent obstacle to converting the preferred shares to common stock, as the par value was too high relative to the par value of the preferred shares to allow conversion. The reverse stock split did not remove this obstacle.

315. The Series C preferred stock was never converted to common shares – instead it was exchanged.

316. Exchange of the Series C for common shares was not considered until 2010, months after the reverse stock split.

317. AIG had no intention in June 2009 to issue these authorized but unissued shares, and the plan to exchange Series C preferred shares for common shares did not emerge for more than a year after the June 2009 shareholders meeting. Likewise, at the time of the June 2009 shareholder meeting, the Government was not considering what it would do with the Trust's Series C preferred shares.

318. In January 2010, AIG and the Government each presented to the AIG board proposals for the Government to divest from AIG; neither plan involved an exchange of the Series C preferred stock for common shares.

319. The exchange did not require an increase in the number of authorized shares.

XVII. <u>The Stock Split Class Did Not Suffer An Economic Impact</u>

320. The reverse stock split benefited AIG's shareholders by preventing AIG's stock from being delisted and by raising AIG's common stock price, which allowed the stock to be more widely held.

321. Following the filing of the preliminary proxy containing the reverse stock split on May 22, 2009, AIG's stock price did not reflect a loss in value due to the filing.

322. Following the filing of the final proxy containing the reverse stock split on June 8, 2009, AIG's stock price did not reflect a loss in value due to the filing.

323. When the news of the shareholder vote approving the reverse stock split was reported on June 30, 2009, AIG's stock price did not reflect a loss in value due to the announcement.

324. AIG's common stock price did not decrease as a result of any information related

to the reverse stock split because the reverse stock split did not cause any dilution of the economic value, voting power, or ownership interests associated with the shares held by the members of the stock split class.

325. Any possible dilution due to the reverse stock split would have been reflected in the value of AIG's common stock immediately after the reverse stock split, at the latest.

326. Events related to the recapitalization in 2010 and 2011 – including the exchange of the Series C, E, and F preferred stock – cannot possibly have caused any dilution of AIG's common stock at the time of the reverse stock split in June 2009.

327. The January 14, 2011 exchange of the Series C, E and F preferred stock for common stock did not dilute the shareholders in the stock split class.

328. When they purchased their shares, none of the reverse stock split class members had any reasonable, investment-backed expectation that they could prevent AIG from proposing a lawful reverse stock split that would result in making enough shares available that the Government could exchange its preferred stock for an equivalent ownership interest in AIG common stock.

PREJUDGMENT INTEREST

XVIII. Any Prejudgment Interest For A Taking Without Just Compensation Should Be At A Rate Equal To The Return On One-Year Treasury Bills

329. The return on one-year Treasury Bills properly reflects the cost of carrying a debt obligation from the Government.

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