

Aon Benfield Analytics

US P&C Industry Statutory Reserve Study

Based on Schedule P data as of December 31, 2010

For Public Distribution

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Executive Summary

Reserve Summary (\$B)

Line	Estimated Reserves	Booked Reserves	Remaining Redundancy	Favorable / (Adverse) Development					Years at Run Rate
				2007	2008	2009	2010	Average	
Personal Lines	127.1	133.6	6.5	5.9	5.4	5.8	6.7	5.9	1.1
Commercial Property	40.5	41.9	1.5	1.7	2.6	2.4	2.7	2.3	0.6
Commercial Liability	227.0	236.8	9.9	1.0	5.2	3.8	2.4	3.1	3.2
Workers Compensation	111.2	117.7	6.5	1.0	1.1	(0.5)	(1.6)	0.0	N/A
Total Excl. Financial Guaranty	505.7	530.1	24.4	9.5	14.4	11.5	10.1	11.4	2.1
Financial Guaranty	32.6	30.2	(2.4)	(1.2)	(12.6)	7.0	0.4	(1.6)	N/A
Total	538.3	560.2	22.0	8.3	1.7	18.6	10.5	9.8	2.2

- P&C Industry undiscounted statutory reserves as of December 31, 2010 estimated to be USD22.0 Billion redundant
- USD10.5 Billion reserves released in calendar year 2010
- At the current average run rate, the redundancy will be eliminated in 2.2 years

Data Sources

- Schedule P parts 1 – 5 were used to obtain the following:
 - Earned Premiums
 - Paid Loss Triangle
 - Case Incurred Loss Triangle
 - Claim Count Triangles
 - Incurred (Ultimate) Loss Triangle

- P&C Industry 2010 data based on aggregation by SNL Financial
 - Data as of May 9, 2011 is based on majority of industry, but may change as additional annual statements are filed and aggregated

- AIG 2010 data based on Combined statutory annual statement
 - Includes disclosed data adjustments in the following lines
 - Workers' Compensation
 - Other Liability Occurrence
 - Private Passenger Auto Liability

Reserve Methods Applied

- Determine reserve levels indicated by mechanical application of standard actuarial techniques
 - Three and five year weighted average link ratios applied to paid loss triangles
 - Three and five year weighted average link ratios applied to case incurred loss triangles
 - Tail factors based on current booked tail factor (Booked Ultimate Loss for AY 2001 divided by most recent Case-Incurred or Paid Loss for AY 2001)

- Accident Years Prior to 2001
 - Prior year reserves estimated based on observed decay rate of prior year paid losses
 - Methodology makes no explicit provision for Asbestos & Environmental (A&E) reserves

- Reserve data are subject to considerable uncertainty and actual reserve emergence could vary materially from the amounts indicated by these methods

- For workers compensation, the analysis is based on nominal data
 - Other industry studies on workers compensation reserves may include tabular and/or non-tabular discounts as part of the industry's reserve adequacy (i.e., discounts reduce the industry's reserve adequacy)
 - This study does not include discounts as a reduction in reserve adequacy

Reserve Methods Applied – Prior Accident Years

- Prior year reserves estimated based on observed decay rate of prior year paid losses
- Determines amount of reserves needed now if selected annual paid loss decays over time according to the selected decay rate
- Estimated reserve = Selected Annual Paid Loss * Decay Rate / (1 – Decay Rate)
- Methodology makes no explicit provision for Asbestos & Environmental (A&E) reserves

Reserve Methods Applied to Industry by Line of Business

Summary of Reserve Methodology by LOB

LOB	LDF Selection	Tail Factor	Ultimate Loss Selection	
			2001 - 2008	2009 - 2010
Homeowners	3 Wtd and 5 Wtd	Current Booked	Avg Paid LDF & Incurred LDF	Max of LDF Methods
Private Passenger Auto	3 Wtd and 5 Wtd	Current Booked	Avg Paid LDF & Incurred LDF	Max of LDF Methods
Commercial Auto	3 Wtd and 5 Wtd	Current Booked	Avg Paid LDF & Incurred LDF	Max of LDF Methods
Workers Compensation	3 Wtd and 5 Wtd	Current Booked	Avg Paid LDF & Incurred LDF	Max of LDF Methods
Commercial Multi Peril	3 Wtd and 5 Wtd	Current Booked	Avg Paid LDF & Incurred LDF	Max of LDF Methods
Medical PL - Occ	3 Wtd and 5 Wtd	Current Booked	Avg Paid LDF & Incurred LDF	Max of LDF Methods
Medical PL - CM	3 Wtd and 5 Wtd	Current Booked	Avg Paid LDF & Incurred LDF	Max of LDF Methods
Special Liability	3 Wtd and 5 Wtd	Current Booked	Avg Paid LDF & Incurred LDF	Max of LDF Methods
Other Liability - Occ	3 Wtd and 5 Wtd	Current Booked	Avg Paid LDF & Incurred LDF	Max of LDF Methods
Other Liability - CM	3 Wtd and 5 Wtd	Current Booked	Avg Paid LDF & Incurred LDF	Max of LDF Methods
International	3 Wtd and 5 Wtd	Current Booked	Avg Paid LDF & Incurred LDF	Max of LDF Methods
Reinsurance - Property	3 Wtd and 5 Wtd	Current Booked	Avg Paid LDF & Incurred LDF	Max of LDF Methods
Reinsurance - Liability	3 Wtd and 5 Wtd	Current Booked	Avg Paid LDF & Incurred LDF	Max of LDF Methods
Reinsurance - Financial	3 Wtd and 5 Wtd	Current Booked	Avg Paid LDF & Incurred LDF	Max of LDF Methods
Products Liability - Occ	3 Wtd and 5 Wtd	Current Booked	Avg Paid LDF & Incurred LDF	Max of LDF Methods
Products Liability - CM	3 Wtd and 5 Wtd	Current Booked	Avg Paid LDF & Incurred LDF	Max of LDF Methods
All Other 2 Year Lines	3 Wtd and 5 Wtd	Current Booked	Avg Paid LDF & Incurred LDF	Max of LDF Methods
Financial Guaranty	Manual Selection	Current Booked	Avg Paid LDF & Incurred LDF	Max of LDF Methods

- Methodology above applied to P&C Industry excluding AIG data
- Adjusted AIG estimate based on the average of 3 year and 5 year weighted paid and incurred LDF methods
 - No provision made for prior year AIG reserves

AIG Data Adjustments

- As part of their 2010 Combined Annual Statement, AIG published additional disclosures outlining adjustments to their statutory Schedule P triangles

- The adjustments cover
 - Changes in mix of business
 - Excess workers compensation and warranty
 - Reinsurance Commutations and Novations
 - Foreign Branch Restructure
 - UK Quota Share

- Each of these adjustments can cause material distortions in mechanically generated reserve indications

- Aon Benfield incorporated the published adjustments for the following lines of business in its review
 - Workers' Compensation
 - Other Liability Occurrence
 - Private Passenger Auto Liability

- Total industry reserve position was estimated based on separate analysis of
 - P&C Industry excluding AIG
 - AIG with disclosed data adjustments

Comparison to 2009 Industry Reserve Study

2009 vs. 2010 Industry Reserve Studies (\$B)

Line	2009 Redundancy/ (Deficiency)	2010	2010
		Without AIG Disclosures Redundancy/ (Deficiency)	With AIG Disclosures Redundancy/ (Deficiency)
Personal Lines	6.0	6.4	6.5
Commercial Property	3.8	1.5	1.5
Commercial Liability	14.2	11.1	9.9
Workers Compensation	(0.8)	(2.6)	6.5
Total Excl. Financial Guaranty	23.2	16.3	24.4
Financial Guaranty	(1.4)	(2.4)	(2.4)
Total	21.9	13.9	22.0

- Overall industry redundancy at year-end 2010 similar to year-end 2009
- However, without adjustments based on AIG disclosures, the reserve redundancy from 2009 to 2010 drops by USD8 billion to USD13.9 billion
- Workers compensation sees a material impact when adjusting for AIG's change in mix of business out of excess workers compensation
 - Analysis based on nominal losses, and tabular and/or non-tabular discounts do not reduce reserve adequacy

Reserve Summary by Entity

Reserve Summary by Entity (\$B)

Line	Industry Excluding AIG Redundancy/ (Deficiency)	AIG With Disclosures Redundancy/ (Deficiency)	Total Industry Redundancy/ (Deficiency)
Personal Lines	7.3	(0.7)	6.5
Commercial Property	1.5	(0.1)	1.5
Commercial Liability	10.6	(0.7)	9.9
Workers Compensation	4.9	1.6	6.5
Total Excl. Financial Guaranty	24.3	0.1	24.4
Financial Guaranty	(2.8)	0.4	(2.4)
Total	21.5	0.5	22.0

- Personal lines and workers compensation each contribute about 25% to the total industry redundancy before accounting for Financial Guaranty
- Commercial property contributes only 6% to the total industry redundancy before accounting for Financial Guaranty
- Commercial liability contributes about 40% to the total industry redundancy before accounting for Financial Guaranty

Summary by Accident Year

Reserve Summary by AY (\$B)

AY	As of 12/31/2009			CY 2010 Reserve Change	As of 12/31/2010		
	Estimated Reserves	Booked Redundancy/ Reserves	(Deficiency)		Estimated Reserves	Booked Redundancy/ Reserves	(Deficiency)
Prior	105.1	94.3	(10.8)	5.2	97.1	90.2	(6.9)
2001	11.4	11.9	0.5	0.1	10.6	10.6	0.0
2002	12.6	12.6	(0.0)	0.1	10.7	10.7	(0.0)
2003	14.4	15.0	0.5	(0.4)	11.8	11.9	0.1
2004	18.0	19.0	1.0	(1.0)	14.0	14.7	0.7
2005	26.0	27.0	1.0	(1.5)	19.2	19.7	0.5
2006	35.0	41.1	6.1	(4.1)	23.9	27.1	3.3
2007	56.2	63.3	7.1	(1.8)	37.9	42.9	5.0
2008	98.3	108.9	10.6	(3.4)	66.7	74.9	8.2
2009	155.7	161.6	5.9	(3.7)	91.8	97.7	5.8
2010					154.7	159.9	5.2
Total	532.9	554.7	21.9	(10.5)	538.3	560.2	22.0

- Prior year reserve deficiency reduced from 2009 to 2010 by almost USD4 billion
- Remaining redundancies still apparent in AY 2006 to 2010

Reserve Ranges

- The 2010 emergence of USD10.5 billion was at the 36th percentile of the estimated range of outcomes
- The 90th percentile range for 2010 emergence is from USD22 billion favorable to USD9 billion adverse emergence
- The 90th percentile range for 2011 is similar, at USD21 billion favorable to USD8 billion adverse

One Year Reserve Range Summary (\$B)

Year	Reserve Volatility	90th Percentile Range	
		Lower Bound	Upper Bound
2009	2.7%	-9.1	22.1
2010	2.5%	-8.3	21.3

- The reserve ranges were developed using a Modified Wacek Reserve Risk Method, which estimates the 1 year development distribution calibrated to the P&C Industry All Lines Schedule P Incurred triangles
 - Assumes the selected ultimate loss is an average of the Chain Ladder and Bornhuetter-Ferguson methods
 - Simulates the next year development based upon the volatility of the triangle's link ratios
 - Estimates the resulting change in reserves due to the next year's simulated development

Aon Benfield Wacek Reserve Risk Method

- Reserve Risk based upon Company's Schedule P information
 - Use Schedule P to determine link ratios
 - Assume current ultimate is an average of Incurred Chain Ladder and BF methods.
 - Simulate expected loss emergence for next year by accident year
 - Record the implied change to ultimate from simulated loss emergence
- Methodology based upon “The Path of the Ultimate Loss Ratio Estimate,” by M. Wacek, CAS Winter Forum (2007)
 - <http://www.casact.org/pubs/forum/07wforum/07w345.pdf>
- Key Steps
 - Select loss development factors, and parameterize the observed link ratio volatility from Schedule P triangle
 - Calculate the implied BF a priori loss ratio assuming the selected ultimate is the average of the Chain Ladder, and BF loss development methods.
 - Simulate the next diagonal link ratios
 - Observe simulated actual vs. expected development
 - Calculate new ultimate based upon observed loss emergence
- Advantages of methodology
 - Reflects company's actual historical experience
 - Sensitive to changes in conservatism in ultimate loss selections

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About Aon Benfield

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