

**REPORT ON EXAMINATION**  
**OF THE**  
**AMERICAN LIFE INSURANCE COMPANY**  
**AS OF**  
**DECEMBER 31, 2004**

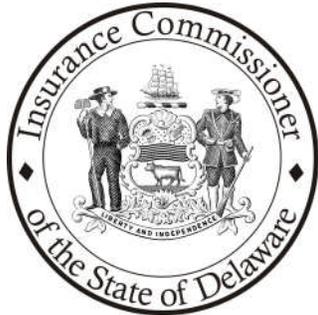
I, Matthew Denn, Insurance Commissioner of the State of Delaware, do hereby certify that the attached REPORT ON EXAMINATION, made as of DECEMBER 31, 2004 of the

**AMERICAN LIFE INSURANCE COMPANY**

is a true and correct copy of the document filed with this Department.

ATTEST BY: *Antoinette Handy*

DATE: 30 JUNE 2006



*In Witness Whereof*, I HAVE HEREUNTO SET MY HAND AND AFFIXED THE OFFICIAL SEAL OF THIS DEPARTMENT AT THE CITY OF DOVER, THIS 30TH DAY OF JUNE 2006.

*Matthew Denn*  
Insurance Commissioner

**REPORT ON EXAMINATION**  
OF THE  
**AMERICAN LIFE INSURANCE COMPANY**  
AS OF  
**December 31, 2004**

The above captioned Report was completed by examiners of the Delaware Insurance Department.

Consideration has duly been given to the comments, conclusions, and recommendations of the examiners regarding the status of the Company as reflected in the Report.

This Report is hereby accepted, adopted, and filed as an official record of this Department.

A handwritten signature in black ink, appearing to read "Matt Denn", written in a cursive style.

---

MATTHEW DENN  
INSURANCE COMMISSIONER

DATED this 30TH Day of JUNE 2006.

**TABLE OF CONTENTS**

	Page
SALUTATION	1
SCOPE OF EXAMINATION	1
HISTORY	4
CAPITALIZATION	5
DIVIDENDS TO STOCKHOLDERS	6
HOLDING COMPANY SYSTEM	6
MANAGEMENT AND CONTROL	9
GROWTH OF COMPANY	13
TERRITORY AND PLAN OF OPERATION	15
REINSURANCE	27
INTERCOMPANY AGREEMENTS	33
ACCOUNTS AND RECORDS	34
FINANCIAL STATEMENTS	35
Assets	36
Liabilities, Surplus and Other Funds	37
Summary of Operations	38
Capital and Surplus Account	39
Schedule of Examination Adjustments	39
NOTES TO FINANCIAL STATEMENTS	40
STATUS OF PREVIOUS EXAMINATION RECOMMENDATIONS	53
RECOMMENDATIONS	55
SUMMARY COMMENTS	59
CONCLUSION	61
ADDENDUM-Organizational Chart	63

February 22, 2006

**SALUTATION**

Honorable Mathew Denn  
Insurance Commissioner  
State of Delaware  
Rodney Building  
841 Silver Lake Building  
Dover, Delaware, 19901

Dear Commissioner:

In compliance with instructions contained in Certificate of Authority No. 04.024, an examination has been made of the affairs, financial condition and management of the

**AMERICAN LIFE INSURANCE COMPANY**

hereinafter referred to as "ALICO" or "Company", incorporated under the laws of the State of Delaware. The examination was conducted at the Home Office of the Company, located at One ALICO Plaza, 600 King Street, Wilmington, Delaware, 19801.

The report of such examination is respectfully submitted herewith.

**SCOPE OF EXAMINATION**

The last examination was conducted as of December 31, 2000. This examination covered the four year period of January 1, 2000 to December 31, 2004, and consisted of a general survey of the Company's business policies and practices; management, any corporate matters incident thereto; a verification and evaluation of assets and a determination of liabilities. Transactions subsequent to the latter date were reviewed where deemed necessary.

The format of this report is designed to explain the procedures employed on examination and the text will explain changes wherever made. If necessary, comments and recommendations have been made in those areas in need of correction or improvement. In such cases, these

## American Life Insurance Company

matters were thoroughly discussed with responsible Company officers during the course of the examination.

The general procedures of the examination followed the rules established by the National Association of Insurance Commissioners' (NAIC) Committee on Financial Condition Examiners Handbook, and generally accepted statutory insurance examination standards. The State of Delaware Insurance Code has provisions that specifically affect insurance companies conducting business solely outside of the United States, and these provisions impacted the examination.

Due to ALICO's international operations, the examination performed procedures on site at the Company's two largest branches, in Japan and the United Kingdom (U.K.). The examination reviewed the assets, liabilities and operations administered from the Wilmington Home Office. For the following branches, the examination reviewed and reconciled local audited financial statements to the amounts reported for those branches on the 2004 Annual Statement:

Greece	Spain
Portugal	Cyprus
Lebanon	Bangladesh
United Arab Emirates (UAE)	

For these branches, as well as Japan, the U.K. and the Home Office operations, the examination reviewed reports issued by the American International Group's Internal Audit Department.

The following chart provides a breakdown of the assets reported at year end 2004 and the net premiums reported for 2004 for the above branches and the Home Office:

American Life Insurance Company

<u>Branch</u>	<u>Assets</u>	<u>Premiums and Annuity Considerations</u>
Japan	\$34,459,236,467	\$7,418,053,584 (*)
United Kingdom (**)	11,993,415,206	5,672,364,995
Home Office	6,459,988,630	189,740,583
Greece	1,233,478,562	245,120,583
Spain	392,118,170	80,031,132
Portugal	469,627,026	43,551,154
Lebanon	288,801,139	74,824,172
Cyprus	265,912,935	33,248,801
Bangladesh	258,555,876	71,793,909
UAE	<u>56,092,354</u>	<u>71,356,200</u>
Totals	<u>\$55,877,226,365</u>	<u>\$13,900,085,113</u>
Annual Statement	\$56,392,883,894	\$14,139,746,759

(\*) An error was noted in the Company's reporting of premiums for the Japan Branch. See the Territory and Plan of Operation section of this report.

(\*\*) The United Kingdom branch amounts are reported in a Separate Accounts Annual Statement blank. The Company began this reporting in 1992 in accordance with Section 1321 of the Delaware Insurance Code, which allows an insurer to segregate the assets of a jurisdiction for the protection of the policyholders of that jurisdiction. See the paragraph below for an explanation of the annual statement blanks filed by ALICO.

During the period under examination, the Company's operations were audited by the firm of PricewaterhouseCoopers (PwC), Certified Public Accountants. As part of the audit procedures supporting the statutory audit opinion, PwC relied on work performed by several of its affiliated foreign branches. For the Japan and United Kingdom branches, the examination retained the firm of Jefferson Well International (JWI) to perform procedures to validate the branches' reported balances. Part of JWI's analysis was to be a review of PwC's local audit workpapers. For the United Kingdom branch, the local PwC office refused to cooperate with the examination, a violation of the Delaware Insurance Code which is discussed in detail in the Accounts and Records section of this report.

In addition to items hereinafter incorporated as part of the written report, the following were checked and made a part of the workpapers of this examination:

## American Life Insurance Company

Corporate Records  
Corporate Insurance  
Conflict of Interest  
All asset and liability items not mentioned

ALICO filed five (5) annual statement blanks for 2004: a “Blue Book” statement reflecting the operations of its general account for all the branches except the United Kingdom (U.K.) Branch. The Company also filed three Separate Account annual statements: one for variable life insurance and annuity business written in Japan; a second statement for all other variable business written worldwide; and a third statement for all the operations, both general account and variable, written by the U.K. Branch. The Separate Account annual statement filed for the U.K. Branch is referred to in this report as the “Green Book.” Finally, ALICO is unique in that it is permitted to write property and casualty insurance through the Certificate of Authority issued by the Delaware Insurance Department. To report the property and casualty business written in several Mid-Eastern branches, ALICO filed the standard property/casualty annual statement blank that is referred to in this report as the “Yellow Book.”

It should be noted that during the period under examination, ALICO adopted a November 30<sup>th</sup> year end for all of its operations. In this report all references to “Year- End 2004” refer to amounts or conditions applicable as of November 30, 2004.

### **HISTORY**

The Company was incorporated under the laws of the State of Delaware on August 18, 1921 as Asia Life insurance Company, with the principal office located in Shanghai, China. In 1951, the Company amended its Certificate of Incorporation, changing the corporate name to American Life Insurance Company and changing the principal office to Bermuda. In 1969, the Company relocated its principal office to Wilmington, Delaware. The Company is a wholly-owned subsidiary of American International Group, Inc. (AIG).

## American Life Insurance Company

The Company's Certificate of Authority from the Delaware Insurance Department authorizes the Company to transact the following types of insurance business: Life, including Annuities, Variable Annuities, Variable Life, Credit Life, Health, Credit Health, Property, Surety, Marine and Transportation, Casualty, including: Vehicle, Liability, Burglary & Theft, Personal Property Floater, Glass, Boiler & Machinery, Credit, Leakage & Fire Extinguisher Equipment, Malpractice, Elevator, Congenital Defects, Livestock, Entertainments and Miscellaneous. In May of 2002, the Company's Certificate of Authority was amended to permit ALICO to write workers' compensation and employers' liability insurance.

The Company reports all of its business as being written outside the United States.

### **CAPITALIZATION**

The following changes occurred in the capital accounts since the previous examination as reported in the Company's Annual Statements:

	Common Capital Stock (1)	Gross paid in and contributed Surplus	Unassigned (surplus)	Totals
December 31, 2000	\$3,000,000	\$550,562,542	\$5,348,971,390	\$5,902,533,932
Net income			975,484,614	
Net unrealized capital- Gains/(Losses)			(1,782,472,710)	
Change in Asset Valuation Reserve			393,673,787	
Change in nonadmitted Assets			(46,119,586)	
Change in net deferred Income taxes			(636,673,286)	
Surplus Contributions		152,431,771 (2)		
Dividends to Stockholders			(204,897,054)	
Foreign Exchange			(296,357,788)	
Separate Accounts-Contributions /Results			(190,378,883)	
Other Changes			(34,589,181)	
December 31, 2004	<u>\$ 3,000,000</u>	<u>\$702,994,313</u>	<u>\$3,526,641,303</u>	<u>\$4,232,635,616</u>

## American Life Insurance Company

- (1) Common stock, \$10 par value, 500,000 shares authorized; 300,000 shares issued and outstanding.
- (2) In 2001, ALICO received a contribution from AIG of the stock of AIG Life Ireland, valued at \$2,431,771. In 2004, ALICO received a surplus contribution of \$150 million from AIG to fund the Company's investment of AIG Financial Assurance Japan KK, which had purchased part of GE Edison in Japan.

See the Growth of Company\_section of this Report for information on Net Income, Unrealized Capital Gains and Deferred Taxes.

### **DIVIDENDS TO STOCKHOLDERS**

For the period under examination, the Company paid the following ordinary dividends:

2001	\$48,897,054
2002	50,000,000
2003	56,000,000
2004	50,000,000

All dividends were paid to ALICO's sole shareholder, American International Group Inc. and were approved by the Delaware Insurance Department.

### **HOLDING COMPANY SYSTEM**

ALICO is a member of an insurance Holding Company system as defined in Section 5001, of the Delaware Insurance Code. Registration statements have been filed with the State of Delaware as required. American International Group, Inc. (AIG) is named as the ultimate controlling person of the Holding Company System.

AIG reported the following as of December 31, 2004:

Total Assets	\$789,660,000,000
Stockholders' Equity	80,607,000,000
Total Revenue (for 2004)	\$97,987,000,000
Net Income (for 2004)	9,731,000,000

AIG, a Delaware corporation, is the leading international insurance organization with operations in more than 130 countries and jurisdictions. AIG companies serve commercial,

## American Life Insurance Company

institutional and individual customers through the most extensive worldwide property-casualty and life insurance networks of any insurer. In addition, AIG companies are leading providers of retirement services, financial services and asset management around the world.

Organizationally, AIG operates through four major business segments:

General Insurance- AIG's General Insurance operations include the largest U.S. underwriters of commercial and industrial insurance, the most extensive international property-casualty network of any insurer; a personal lines business with an emphasis on auto insurance and high-net-worth clients, and mortgage guaranty insurance operations.

Life Insurance & Retirement Services- AIG's global life insurance businesses make up the most extensive network of any life insurer. AIG has one of the premier Retirement Services businesses in the United States. AIG also has an extensive international retirement services network to meet the growing needs of groups and individuals in countries worldwide.

Financial Services - AIG's Financial Services businesses specialize in aircraft leasing, capital markets, consumer finance and insurance premium finance. These businesses complement AIG's core insurance operations and achieve a competitive advantage by capitalizing on opportunities throughout the AIG global network.

Asset Management - AIG's Asset Management Group manages institutional, retail and private fund assets, in addition to AIG insurance invested assets. Businesses in this group leverage AIG's deep knowledge of markets around the world and expertise in a wide range of asset classes. AIG Global Investment Group ranks among the top five institutional asset managers in the world.

Revenues by the major operating segments in 2004 were as follows:

General Insurance	\$41,897,000,000
Life Insurance & Retirement Services	43,386,000,000
Financial Services	7,982,000,000
Asset Management and Other	<u>4,722,000,000</u>
Total	<u>\$97,987,000,000</u>

Internationally, AIG's principal life operations are:

- American International Assurance Company Ltd. (AIA) is Southeast Asia's premier life insurance company. AIA is the largest life insurer in Hong Kong and Singapore and its subsidiaries operate in Malaysia, Thailand and Vietnam.
- Nan Shan Life Insurance Company, which is the second largest life insurer in Taiwan.

## American Life Insurance Company

- American Life Insurance Company (ALICO), AIG's largest international life insurer, operating in fifty-four (54) countries either through branches or subsidiaries. It should be noted that in Japan, ALICO's largest market, the Company operates in tandem with two affiliates, AIG Star Life Insurance Company and AIG Edison Life Insurance Company.

In twenty-three (23) countries, ALICO operates through subsidiaries, and in several countries, owns more than one subsidiary. At December 31, 2004, the Company also maintained investments in several related companies including a substantial investment in the stock of the parent, AIG. In total, ALICO reported investments in forty-six (46) companies within the AIG group at year end 2004.

An organizational chart, showing the major companies in the AIG Holding Company System, is attached as an addendum to this Report.

The 2000 examination noted an exception on Schedule Y, Part 2 Summary of Insurer's Transactions with Any Affiliates that continued during the current examination. The Annual Statement instructions require that for three types of transactions, Shareholder Dividends, Capital Contributions, and Reinsurance Recoverables/Credits, an insurer shall provide the dollar amounts of all inter-company transactions. ALICO did not provide any information for dividends received from subsidiaries or amounts contributed to subsidiaries. In 2004, ALICO received \$55.5 million in dividends from its subsidiary in Brazil. In 2003, ALICO contributed \$150 million to purchase GE Financial Assurance, renamed to AIG Financial Assurance, a subsidiary in Japan. These transactions are significant and should be disclosed. Due to the multitude of inter-company reinsurance transactions throughout the AIG Holding Company System, it is necessary that a central unit of AIG prepare Column 13, the section of Schedule Y that reports inter-company reinsurance transactions. For 2004, due to AIG restating the results for several reinsurance treaties (though none affected ALICO), Column 13 of Schedule Y Part 2

American Life Insurance Company

was not prepared for ALICO or any AIG companies. Therefore, because of the deficiencies noted:

**It is again recommended the Company fill out Schedule Y in compliance with Annual Statement instructions.**

### **MANAGEMENT AND CONTROL**

The management of the Company is vested in a Board of Directors which shall consist of not less than 4 or more than 22 directors with the Directors being elected annually by the stockholder. The Company's Board of Directors consisted of the following 19 members as of December 31, 2004:

<u>Board of Directors</u>	<u>Principal Occupation</u>
Merton Bernard Aidinoff	Senior Counsel- Sullivan & Cromwell
Bruce Emmitt Dozier	Senior Vice President & General Counsel- ALICO
Michael Henry Buthe	Vice President- ALICO
Maurice Raymond Greenberg *	Chairman & CEO- AIG
David Lawrence Herzog	Vice President & Treasurer- ALICO
Donald Perry Kanak, Jr.*	Director- ALICO; Executive Vice Chairman and Chief Operating Officer, AIG
Edward Easton Matthews *	Vice Chairman- AIG
George Burrell McClennen	Senior Vice President, Chief Financial Officer- ALICO
Win Jay Neuger	Executive Vice President and Chief Investment Officer- AIG
Robinson Kendall Nottingham	Chairman, President & CEO- ALICO
Ernest Theodore Patrikis	Senior Vice President & General Counsel- AIG

## American Life Insurance Company

Paul Stuart Rix	Director- ALICO
Howard Ian Smith *	Executive Vice President & CFO- AIG
Ernest Edward Stempel	Senior Advisor (Life Management Division)- AIG
Raymond Michael Terne	Vice President & Chief Actuary- ALICO
Seiki Tokuni	Director- ALICO
Edmund Sze-Wing Tse	Senior Vice Chairman, Life Insurance- AIG
Andreas Vassiliou	Executive Vice President- ALICO and President & CEO- Central & Eastern Europe
Frank George Wisner	Vice Chairman, External Affairs- AIG

- Mssrs. Greenberg, Mathews and Smith were not re-elected directors in 2005.
- Mr. Kanak resigned in 2005.

### Committees

The Board of Directors had the following standing committees at December 31, 2004:

<u>Executive</u>	<u>Investment</u>
Maurice Raymond Greenberg (Chairman)*	Michael Henry Buthe (Chairman)
Robinson Kendall Nottingham	George Burrell McClennen
Ernest Edward Stempel	Win Jay Neuger
Edmund Sze-Wing Tse	Robinson Kendall Nottingham
	Raymond Michael Terne

- Mr. Greenberg was not reappointed to the Company's Executive Committee in 2005. In 2005, the Executive Committee consisted of Win Jay Neuger, Robinson Kendall Nottingham, and Edmund Sze-Wing Tse.

During the examination period the Finance Committee was dissolved and the Investment Committee was created in its place. In addition, while ALICO does not have its own Audit Committee, the Audit Committee of AIG covers audit issues on behalf of all AIG entities.

The examination noted three (3) exceptions in the review of committees:

- In 2003, the ALICO Board of Directors appointed an Executive Committee just for the Japan Branch. This Executive Committee is described as a "decision-making"

body and consists of officers in Japan that are vice-presidents and above. The examination was provided with minutes of meetings of the Japan Executive Committee; however, it was noted that the actions of this committee are not reviewed and approved by the ALICO Board of Directors. Therefore:

**It is recommended the Executive Committee of the Japan Branch report to the ALICO Board of Directors and have the actions of the Japan Executive Committee approved by the ALICO Board.**

- The previous examination noted that the Board of Directors appointed a Banking Committee; however, this Committee did not hold formal meetings and, more importantly, the actions of the Banking Committee were not reviewed and approved by the Board of Directors. The current examination noted this situation continued during the period under examination. Therefore:

**It is again recommended that minutes of meetings of the Banking Committee be maintained and it is further recommended that all actions of the Banking Committee be approved by the ALICO Board of Directors.**

- It was noted that minutes of the Executive Committee meetings held November 29, 2001 and December 10, 2003, were not subsequently approved by the ALICO Board of Directors. At both Executive Committee meetings, stockholder dividends were declared. The 2000 examination also noted this deficiency. Therefore:

**It is again recommended that any action taken by the Executive Committee be reported to and approved by the Board of Directors at the next meeting following the Executive Committee action.**

Subsequent Event:

In 2005, the Company's Board of Directors appointed two new committees:

Corporate Governance and Compliance Committee. This committee is charged with investigating and reviewing all compliance matters that arise from the Sarbanes-Oxley

## American Life Insurance Company

Act of 2002 and all other laws and regulations applicable to ALICO. The members of this committee are: Bruce Emmitt Dozier, George Burrell McClennen, and Robinson Kendall Nottingham.

### Complex Structured Financial Transactions Committee

This committee will review transactions and agreements in numerous areas, with an emphasis that proper accounting and reporting treatment will be observed. The members of this committee are: Michael Henry Buthe, Bruce Emmitt Dozier, George Burrell McClennen, Robinson Kendall Nottingham, and Michael Terne.

### Officers

The following officers were elected and serving at December 31, 2004:

Robinson Kendall Nottingham	Chairman, President & CEO
Edmund Sze-Wing Tse	Vice Chairman
Andreas Vassiliou	Executive Vice President
George Burrell McClennen	Senior Vice President & CFO
Bruce Emmitt Dozier	Senior Vice President & General Counsel
Raymond Michael Terne	Vice President & Chief Actuary
Joanne Marie Warren	Vice President & CAO
Leslie Earl Burlew	Vice President & Controller
Elizabeth Margaret Tuck	Secretary
Jeffery Merton Kestenbaum	Senior Vice President
Ernest Sigmund Auerbach	Vice President
Patricia Anne Cameron	Vice President
Ralph Joseph Gaudio	Vice President
Frederick Harold Hemphill	Vice President
Thomas Martin Hoffman	Vice President
Michael Henry Buthe	Vice President
Gustavo Covacevich Ruiz	Vice President
Frederick Augustus Hegner	Vice President
David Lawrence Herzog	Vice President
Joseph William Thurstlic	Vice President

Note: As stated in the Territory and Plan of Operation section of this Report, ALICO conducts business in fifty-four (54) countries. In addition to the individuals listed above, ALICO appoints additional officers on a country specific or regional basis.

**GROWTH OF COMPANY**

The following information was obtained from the Company's filed Annual Statements and covers the five preceding years. The amounts below are prior to any examination adjustments:

<u>Year</u>	<u>Admitted Assets Excluding Separate Accounts Business</u>	<u>Separate Account Assets</u>	<u>Capital and Surplus</u>
2000	\$19,251,079,249	\$9,605,236,134	\$5,902,533,932
2001	18,681,846,643	9,789,301,350	4,703,916,840
2002	20,617,346,944	11,839,473,028	4,363,930,282
2003	27,067,202,917	12,560,364,257	4,127,015,461
2004	39,790,722,108	16,602,161,781	4,232,635,616

<u>Year</u>	<u>Premiums and Annuity Considerations</u>	<u>Net Income</u>
2000	\$10,215,255,733	\$271,420,264
2001	8,254,163,584	273,674,101
2002	10,267,416,008	178,901,267
2003	10,624,314,139	254,345,430
2004	20,123,246,084*	268,563,816

See the Capitalization section of this Report for detailed information on change in Capital and Surplus during the examination period.\* Also, the Company included the MODCO reserve adjustment in ceded premium, in error, instead of reporting as a separate revenue item in the Summary of Operations. As a result, premium was inflated, but there was no effect on total revenue or surplus. See the Territory and Plan of Operation section of this Report for details on this error.

All amounts are in U.S. dollars.

Assets, exclusive of the Separate Accounts business, have grown approximately 107% since the last examination. Separate Accounts assets grew 73% since 2000. The increase in assets is due primarily to the significant increase in revenues generated from the Company's operations in Japan, where admitted assets (excluding separate accounts) increased \$20.3 billion

## American Life Insurance Company

or 205%. The most prominent increase occurred in Japan from 2003 to 2004. The Company began issuing single premium annuities through banks in Japan. The Japan Branch increased its annuity sales in 2004 alone by almost \$6 billion.

Capital and Surplus decreased (\$1,670) million since 2000 representing a decrease of (28.3%). Two points are particularly noteworthy:

- Since 1967, ALICO has held a significant block of common stock of its parent, AIG. From a cost of \$2,241,437 in 1967, the value of the Company's AIG stock had risen to \$6,060,937,324 as of December 31, 2000.

However, effective January 1, 2001, under the NAIC's Codification requirements, insurance companies were required to accrue a tax liability on unrealized capital gains. As of January 1, 2001, ALICO accrued a deferred tax liability of \$2,120,543,569 on the appreciation in value on the AIG stock.

- The market value of the AIG stock was \$99.563 per share as of year end 2000. The market value fell to \$79.40 per share by December 31, 2001 and was \$63.35 as of year end 2004. The sizable decline in the value of the Company's AIG stock impacted the Company's financial reporting in several areas: in addition to the decrease in cumulative unrealized capital gains, the decline reduced the deferred tax liability noted above, and also triggered a decrease in the Asset Valuation Reserve. As of year end 2000, ALICO had accrued Asset Valuation Reserve equal to 25% of the cumulative appreciation on the AIG stock.

## American Life Insurance Company

ALICO reported \$975,484,614 in Net Income during the four (4) year period under review and reported positive Net Income in each year. During the same period, the Company paid \$204,897,054 in dividends to stockholders.

### **TERRITORY AND PLAN OF OPERATION**

ALICO transacts the business of insurance worldwide having representatives, branch offices or subsidiaries in fifty-four (54) jurisdictions. The following is a schedule of countries in which the Company was licensed to write business as of year end 2004:

Antigua	Argentina *	Aruba
Bahrain	Bangladesh	Barbados
Bermuda	Brazil *	Bulgaria*
Cayman Islands	Chile*	Colombia*
Cyprus **	Czech Republic *	Dominica
Egypt*	France *	Germany *
Greece ***	Grenada	Hungary *
Ireland *	Italy *	Japan
Jordan	Kenya *	Kuwait
Lebanon	Mexico	Nepal
Netherlands Antilles	Oman	Pakistan
Palestine	Panama	Peru *
Poland *	Portugal ***	Qatar
Romania *	Saudi Arabia	Slovak Republic *
Spain ***	St. Kitts	St. Lucia
St. Vincent	Taiwan	Trinidad & Tobago
Turkey *	Ukraine *	United Arab Emirates
United Kingdom	Uruguay *	Venezuela *
United States of America (Delaware)		

(\*) Insurance business conducted through an ALICO subsidiary

(\*\*) Insurance business conducted through a branch and subsidiary.

(\*\*\*) Insurance business conducted through a branch. Non-insurance business is also conducted through an ALICO subsidiary.

Since the December 31, 2000, examination date the Company no longer writes new business in: Belize, Haiti, Hong Kong, Liberia, Malta, Montserrat, Tanzania, Turks & Caicos Islands, and the Yemen Arab Republic, but had run-off business in these operations at December 31, 2004. Also, on December 31, 2004, the Company transferred to Parent via a dividend, its

American Life Insurance Company

investment in American Security Life Liechtenstein. The value of the dividend was \$13, 987, 054. Since December 31, 2000, the Company began writing business through subsidiaries in Germany, Ireland, Mexico, and Ukraine. While the countries in which ALICO ceased operations during the examination period represented minimal amounts of premium dollars, the Company has high expectations for the countries it recently entered. In particular, ALICO intends to use its subsidiaries in Ireland and France to write direct response business in several countries as permitted by European Union directives.

The examination requested documentation to support the licenses or authorities to write insurance in the countries noted above. The Company could not provide current information on its licenses. Therefore:

**It is recommended the Company undertake a project to update the Home Office files for certificates of authority or licenses in every country in which ALICO operates.**

ALICO operates exclusively outside the United States. ALICO branches and subsidiaries market an extensive range of life and health products, including traditional life, variable life, annuities, pensions, personal accident insurance and group insurance for large and small organizations.

On the 2004 Blue Book, the Company reported the following breakdown of premiums:

Direct	\$21,711,195,091
Assumed	223,707,044
Ceded	<u>1,811,656,051</u>
Net	<u>\$20,123,246,084</u>

American Life Insurance Company

The amounts that should have been reported were:

Direct	\$21,711,195,091
Assumed	223,707,044
Ceded	<u>7,795,155,376</u>
Net	<u>\$14,139,746,759</u>

In the review of Reinsurance (see following section of this Report), it was noted that in reporting premiums ceded in 2004 to RGA Reinsurance Company, ALICO erroneously deducted a Modified Coinsurance Reserve of \$5,983,499,325. This amount should have been properly reported on Line 7 of the Summary of Operations in the 2004 Blue Book, instead of distorting the Company's Premiums and Annuity Considerations. Therefore:

**It is recommended the Company report premiums on ceded reinsurance contracts in accordance with the NAIC Annual Statement Instructions.**

For 2004, ALICO reported the following geographical distribution of its direct premiums and annuity considerations (as reported on Schedule T of the 2004 Blue Book):

	2004 <u>Premiums</u>	% of <u>Total</u>	2000 <u>Premiums</u>	% Change During <u>Exam Period</u>
Japan	\$14,965,030,492	69.2%	\$3,633,370,507	311.9%
United Kingdom	5,584,228,181	25.8	6,105,730,611	-8.5
Greece	263,036,130	1.2	125,528,912	108.7
U.A.E.	98,621,800	.5	52,880,387	86.4
Spain	94,312,169	.4	50,336,501	87.5
Portugal	92,576,831	.4	45,380,110	104.4
Corporate	83,760,612	.4	81,369,365	3.1
Lebanon	83,275,067	.4	65,989,148	26.2
Taiwan	77,279,298	.4	14,625,107	429.5
Bangladesh	68,787,052	.3	43,374,198	58.5
Saudi Arabia	50,341,020	.2	35,512,703	41.7
Cyprus	37,802,678	.2	35,126,589	6.5
Jordan	24,846,394	.1	21,317,823	16.4
Panama	<u>23,644,740</u>	.1	20,748,782	14.0
Subtotal	\$21,547,542,464	99.6%		

American Life Insurance Company

Branches with  
writings of less  
than \$20 million                    87,115,432                    .4%

Total Direct Premiums  
and Annuity  
Considerations                    \$21,634,657,896

The Company's direct 2004 premiums were written in the following lines of business:

<u>Lines of Business</u>	<u>2004 Premiums</u>	<u>% of Total</u>
Ordinary Life	\$8,715,125,876	40.1%
Individual Annuities	10,130,047,312	46.7
Credit	71,341,137	.3
Group Life	206,187,771	.9
Group Annuities	142,660,306	.7
Group Accident & Health	144,228,127	.7
Other Accident & Health	<u>2,301,604,562</u>	<u>10.6</u>
Totals	<u>\$21,711,195,091*</u>	100.0%

\* This is the amount of direct premiums collected plus the change in uncollected premiums.

ALICO reported Gains from Operations in each of the years under examination. The following chart provides premium income and Net Gain from Operations for the four year period under examination:

	<u>Premium Income</u>	<u>Net Gain (Loss) from Operations</u>
Ordinary Life	\$29,303,649,590	\$570,715,750
Individual Annuities	12,031,578,430	(173,994,958)
Credit	162,395,495	(4,780,967)
Group Life	573,969,058	55,077,571
Group Annuities	462,772,053	8,320,616
Group Accident & Health	417,970,592	24,185,076
Other Accident & Health	6,316,804,107	525,167,832
Supplementary Contracts	_____	<u>42,018</u>
Totals	<u>\$49,269,139,325</u>	<u>\$1,004,732,938</u>

For the previous three year examination period, (1998 to 2000), ALICO reported premium for Individual Annuities of \$662,627,431. The loss on the Individual Annuities

## American Life Insurance Company

reported above was due to the acquisition costs incurred in writing massive amounts of new business. ALICO continues to report sizable profit margins on its Other Accident and Health business, which is referred to as “Personal Accident” business within ALICO and is traditionally the Company’s most profitable line of business. As noted below, the Company’s Japan Branch is facing increased competition in this very lucrative business area.

### **Operations in Japan**

For 2004, the business produced by ALICO’s Japan branch accounted for 69.2% of the Company’s total direct premiums and annuity considerations. The following chart provides a more specific breakdown along with a comparison to amounts reported for 2000:

<u>Line of Business</u>	<u>2004 Premiums</u>	<u>2000 Premiums</u>
Ordinary Life	\$2,785,179,000	\$1,949,755,000
Individual Annuities	10,034,048,000	467,625,000
Credit Life	9,118,000	7,939,000
Group Life	61,516,000	42,450,000
Group Accident & Health	5,391,000	1,700,000
Other Accident & Health	<u>2,069,778,000</u>	<u>1,163,902,000</u>
Totals	<u>\$14,965,030,000</u>	<u>\$ 3,633,371,000</u>

At year end (November 30<sup>th</sup>) 2004, the Japanese Yen translated at .009692 of the U.S. dollar or approximately 103.178 Yen equaling one U.S. dollar.

In reviewing the operations of the Japan Branch during the examination period, two (2) salient events stand out:

- The regulatory body in Japan, the FSA, allowed banks to begin selling insurance. Starting in 2000, ALICO has worked with an affiliate, SunAmerica, to develop a single premium annuity product for use in Japan.

This annuity became a natural product for banks to offer using ALICO as the underwriter. ALICO then brought two additional annuity products to the market. As indicated in the chart above, the popularity of the single premium annuity products in Japan has been phenomenal. ALICO sells its annuities through virtually all the large banks in Japan. Sales of the annuities remained strong in 2005.

## American Life Insurance Company

- At the time of the last exam, the FSA limited the percentage of assets that any insurance company could hold in non-yen currencies to 20% of total assets. During the exam period, the FSA raised the ratio for non-yen assets to 30%. More importantly, the FSA also permitted insurers to issue policies in non-yen currencies. Almost all of the recent single premium annuities issued by the Company are denominated in US dollars. A small percent is in Euros. The assets matching these non-yen denominated policy liabilities are exempt from the 30% limit. The easing of the currency restrictions has significantly aided ALICO in its efforts to sell the single premium annuities.

The examination noted that the FSA requires that insurers reserve the full account value for the single premium annuities. Though the commissions paid to the banks are not excessive, the sheer volume of business written by ALICO-Japan has created a huge surplus strain that affects all the business ALICO writes. The Company began to use ceded reinsurance to cushion the surplus strain. See the following Report Section for details on the ceded reinsurance program for the Japan Branch. In addition, the Home Office has transferred shares of the Company's AIG stock to the Japan Branch. Having these assets being held in Japan has bolstered ALICO-Japan's Solvency Margin score, which is roughly equivalent to Risk Based Capital in the U.S. The size of the Company's operation in Japan can be demonstrated by three (3) facts:

- ALICO Japan has 248 field offices
- The Japan branch had in excess of 200,000 agents or producers at year end 2004. This reflects the large number of banks selling ALICO's annuity products.
- In a roughly one year period from 2003 to 2004, ALICO-Japan registered approximately 40,000 new agents or producers.

In addition to banks, ALICO utilizes career agents, independent agents and mass marketing to generate business in Japan.

The products sold by the Japan Branch can be summarized as follows:

### Ordinary

ALICO Japan sells the basic products of whole life, endowment and term life. In addition, the Branch sells Savings Plans on a level or single premium basis, often serving a special purpose such as savings for education. Guaranteed Issue Whole Life is a direct sale whole life plan with premiums payable for life. Interest Sensitive Whole Life (ISWL) is a fixed premium universal life product with various payment periods, available from 3 years to life. The ISWL products are available in two currencies, yen and U.S. dollar.

## Health

The Full-in Hospital (FIH) plans provide benefits upon death, total disability and hospitalization. Different levels of hospitalization coverage are provided depending on whether the covered event resulted from sickness or accident. The Japan Branch has introduced several variations of this popular product. The Branch offers a FIH product that includes a death benefit, while another plan pays an endowment at the end of the term, depending on claim experience.

The Cancer plans provide indemnity benefits (either lump sum or daily) upon diagnosis, hospitalization, outpatient treatment, or surgery for cancer. Death benefits are also provided, with a much higher amount if the cause of death is cancer. Cancer plans are offered that pay an endowment.

Long-Term Personal Accident (LTPA) covers accidental death and physical impediments arising from accidents. The LTPA product is primarily sold to the corporate market.

During prior examination periods, accident and health products in Japan were marketed primarily by foreign insurance companies. To promote competition, the FSA has lifted that restriction on domestic Japanese companies. Also, the FSA permitted property-casualty insurance companies to write accident and health products. Many of ALICO's traditionally profitable accident and health products have been targeted by the Company's competitors. As a result, it is unlikely the Company will report the profit margins for accident and health business that it has in the past.

## Retirement Assurance

Retirement Assurance (RA) is a pure endowment product with death and surrender benefits which can be purchased with maturity dates at age 65, 70, 75 and 80. These products can be funded with a single premium payment or with level premiums over a variety of durations. There is a tontine-type feature to the RA products which distributes to persisting policies, the portion of the account values that is forfeited by terminations due to death or surrender.

## Fixed Annuity

ALICO Japan sells single-premium fixed annuities, denominated in U.S. dollars or Euros. The Regulus, denominated in U.S. dollars, is available as a 7 year contract with a 7 year interest guarantee, or a 10 year contract, with a 5 or 10 year interest guarantee. The Dual Currency Fixed Annuity has the same design as the Regulus, but also permits the policyholder to choose between Euros and U.S. dollars.

## American Life Insurance Company

### Variable Annuity

The Japan Branch offers a single-premium deferred Variable Annuity which allows policyholders to invest additional amounts on an unscheduled basis. The guaranteed minimum death benefit (GMDB) is return of premium. Bank variable annuity contracts offer higher optional ratchet GMDB for an additional charge.

### **Operations in the United Kingdom (U.K.)**

ALICO's U.K. Branch is the Company's second largest operation in terms of both assets and premium and annuity considerations.

Under the Delaware Insurance Code, insurance companies operating exclusively overseas, may segregate or "ringfence" the business and assets of a particular branch by reporting the assets, liabilities, surplus and operations of that branch utilizing the NAIC Separate Accounts Annual Statement blank.

During the previous examination period (1998 to 2000), the U.K. Branch reported significant growth. Premiums that were \$1.7 billion USD in 1997 rose to \$6.1 billion USD in 2000. As the chart below indicates, while the premiums reported by the U.K. Branch remained formidable, there were sizable fluctuations due to interest rate and stock market conditions:

<u>Year</u>	<u>Branch Assets</u>	<u>Premiums Annuity Considerations</u>
2004	\$11,997,819,581	\$5,672,364,995
2003	9,380,323,240	3,850,113,646
2002	9,954,842,227	5,780,007,993
2001	8,329,772,149	4,225,962,481
2000	8,049,272,037	6,105,730,611

One of the limitations of the Separate Account annual statement blank used to report the U.K. Branch's operation is the lack of premium information by source. In 2004, the U.K. Branch reported the following distribution of premiums:

American Life Insurance Company

Direct	\$5,584,281,000
Assumed	119,650,000
Ceded	<u>31,566,000</u>
Net premiums	<u>\$5,672,365,000</u>

Of the U.K. Branch's premiums for 2004, \$1,278,873,000 represented general account business where ALICO assumes the risk while the remaining \$4,393,492,000 premiums were written through products wherein the policyholder assumes a significant amount of the risk. This distinction is important in calculating the Branch's statutory Required Minimum Margin, which is discussed below.

Of all the Company's operations, the U.K. Branch is unique as per the products offered. This is reflected in the chart below providing direct premiums for 2004 by product:

Investment Products	\$5,317,647,000
Individual Annuities	41,708,000
Single Premium Pension	12,981,000
Ordinary Life	15,878,000
Personal Accident	74,979,000
Variable Life	3,374,000
Credit Life	32,243,000
Employee Benefits	<u>85,471,000</u>
Total Direct Premiums	<u>\$5,584,281,000</u>

As indicated by the breakdown of premiums by product, the U.K. Branch's operations are primarily dedicated to selling Investment Products, which are offered to customers through stock brokers and banks. Two products accounted for 87% of the Branch's writings in 2004:

- 1) Guaranteed Investment Bonds (GIBs). Writings of \$1,065,216 in 2004.

GIBs are comparable to Guaranteed Investment Contracts in the United States. The policyholder pays a single premium at the outset and receives a bond with a guaranteed rate of return and a guaranteed repayment of capital invested, payable at the maturity of the bond, or at death. The death benefit is set at 101% of the original investment. The term of the bond can vary from a maximum of five (5) years to one (1) month. These policies carry market value adjustment rights in the event of early surrender.

While the ALICO U.K. Branch guarantees the investment return on the GIB, the exposure is mitigated by the Branch offering returns that can be justified by the

## American Life Insurance Company

immediate purchasing of fixed interest securities that match or exceed the interest rate and maturity of the GIB. Traditionally, the Branch has been able to offer returns that exceed market conditions in the U.K. because of the AIG corporate tax agreement, which is discussed below.

- 2) Premier Access Bonds (PABs). For 2004, writings of \$3,794,155,000 in 2004 were reported.

PABs are unique products. The policyholder deposits a single premium with the Company. There is no fixed period for the bond. The U.K. Branch offers a fixed rate of return but can vary the interest rate on the bond at any time without prior notice to the policyholder. Concurrently, the policyholder can surrender all or part of the bond at any time without incurring surrender penalties. (This is one reason why the Surrender Benefits and Withdrawals for the U.K. Branch appear unusually large). And, the bond is linked to a separate account with the risk of the underlying investment being borne by the policyholder.

For both the PAB and other Investment Products, ALICO-U.K. utilizes derivatives to lock in investment returns. The U.K. Branch has also offered Investment Products that employ derivatives to generate additional income. For these types of products, the investment risk is borne by the policyholder.

The examination noted that U.K. taxes paid by ALICO to Inland Revenue (the U.K. equivalent of the IRS in the U.S.) are utilized as foreign tax credits by ALICO's parent, American International Group Inc., (AIG) in preparing AIG's U.S. federal income tax return. Under an agreement between ALICO and AIG (which is discussed in the Inter-Company Agreement Section of this Report), all foreign tax credits utilized by AIG on its U.S. tax return will be paid in cash to ALICO. Prior to 2003, when ALICO received payment from AIG for tax credits generated by the U. K. Branch, those funds were remitted to the U. K. Branch. In 2003, an amendment to the tax regulations of the Inland Revenue was proposed that could have had the impact of taxing this cash remittance received by the U. K. Branch. Therefore, in 2003, ALICO's Home Office began making tax payments directly to the Inland Revenue for the local tax provision of the U. K. Branch. The Inland Revenue amended the tax regulations in 2004 (s83(2B)FA 1989) and this amendment ultimately would not have imposed taxes on cash

## American Life Insurance Company

remittances received by the U. K. Branch. Whether the U.K. Branch pays its own taxes and seeks reimbursement, or the Home Office pays the U.K. taxes directly, the effect of the tax agreement with AIG is positive for the U.K. Branch. ALICO-UK can offer interest rates on its products on a pre-tax basis. This provides an advantage over competing companies who must take corporate taxes into consideration when determining if a product is profitable.

The examination reviewed the U.K. Branch's compliance with the regulatory surplus requirement, which in the U.K. is known as the "Required Minimum Margin" or "Solvency Margin." The U.K. Regulators classify business as two types: general or short-term insurance (where A&H insurance is reported), and long-term insurance, which covers life insurance. For the products where ALICO guarantees a rate of return, (such as Guaranteed Investment Bonds), the Company is required to hold excess assets equal to 4% of policy reserves as a solvency margin.

To offset the surplus strain of the 4% solvency margin, the Company has sought to offer products where all or most of the risk is transferred to the policyholder. For the Premier Access Bond, there is sufficient policyholder risk that the solvency margin is 0%.

The U.K. regulatory body, the Financial Services Authority (FSA), imposes additional requirements in that insurance companies are required to segregate assets to match the solvency margin. However, the value of the matching assets is a multiple of the solvency margin accrual. The FSA recommends that insurance companies maintain excess assets equal to 150% of the solvency margin. The insurer's segregated assets are determined on a case by case basis.

At year end 2004, the ALICO U.K. Branch reported the following solvency margin for its long-term business:

## American Life Insurance Company

Required Minimum Margin	\$194,044,960
Assets available to meet RMM	512,457,383
Ratio of assets to RMM	264%

For the Company's general business:

Required Minimum Margin	\$ 5,218,122
Assets available to meet RMM	27,498,794
Ratio of assets to RMM	527%

No exceptions were noted in the review of the Required Minimum Margin.

### **Property-Casualty Business**

As noted in the History section of this Report, ALICO has the authority from the Delaware Insurance Department to write both Life-Health and Property-Casualty insurance. In 2000, the Company began writing personal auto insurance in the United Arab Emirates (UAE) with total premiums for that year of \$1,713,000. In 2001, the Company began writing other property-casualty business in both the UAE and Oman, reporting gross and net premiums of \$9,516,000 and \$2,261,000 respectively.

Initially, ALICO reported the property-casualty business as a write-in item on the Blue Book Life Annual Statement. This presentation was inappropriate and was the subject of a recommendation in the 2000 Report of Examination.

The Company began filing a Yellow Book Property-Casualty Annual Statement in 2002 and reported the following financial results through year end 2004:

American Life Insurance Company

	<u>2004</u>	<u>2003</u>	<u>2002</u>
Assets	\$26,328,777	\$21,862,348	\$13,736,201
Policyholder Surplus	2,998,819	1,665,046	(753,036)
Net Income	1,096,349	2,635,717	179,403
Premiums			
Direct	\$22,832,079	\$16,311,036	\$9,556,720
Assumed			
Non-affiliates	2,939,755	2,411,561	1,280,123
Affiliates	13,600,961	14,457,155	7,537,997
Ceded			
to Affiliates	(38,790,227)	(33,050,890)	(17,085,156)
to Non-Affil	<u>(637,491)</u>	<u>(128,862)</u>	<u>(361,858)</u>
Net Premiums	<u>\$(54,923)</u>	<u>\$0</u>	<u>\$927,828</u>

As indicated by the above premium amounts, the Company cedes almost all of its net property-casualty business to affiliates. The examination sought to review the Company's property-casualty ceded reinsurance contracts with affiliates. The examiners were informed that no written reinsurance contracts are in place covering the property-casualty business and that no memorandums or other documentation stating the terms of the reinsurance are available.

Without executed, written reinsurance contracts ALICO cannot demonstrate compliance with the Delaware Insurance Code and SSAP 62 as per the recognition of ceded reinsurance credits. Therefore:

**It is recommended the Company reduce the ceded reinsurance coverage on the property-casualty business in the Mid-East to writing. The ceded reinsurance contracts must contain all clauses required by the Delaware Insurance Code and SSAP 62, and must demonstrate transfer of risk.**

### REINSURANCE

As noted in the previous section, for 2004, ALICO reported an incorrect amount for ceded reinsurance premiums on the 2004 Blue Book. The Company netted a Modified Coinsurance Reserve amount of \$5,983,499,325 against ceded premiums in violation of the NAIC Annual Statement Instructions. This exception promulgated an examination

## American Life Insurance Company

recommendation in the Territory and Plan of Operation section of this Report. The correct distribution of premiums and annuity considerations for 2004 is as follows:

Direct	\$21,711,195,091
Assumed	223,707,044
Ceded	<u>7,795,155,376</u>
Net	<u>\$14,139,746,759</u>

The examination noted two important points in evaluating ALICO's reinsurance program. First, the Company operates as an integral part of the American International Group (AIG). It is the traditional philosophy of AIG to spread risks among affiliated parties before ceding business outside the group. As will be detailed in the summaries below of the assumed and ceded reinsurance programs, the vast majority of the Company's assumed and ceded contracts are with subsidiaries and affiliates. An exception to this practice occurred during the examination period when the unprecedented premium growth of ALICO's Japan Branch triggered several massive reinsurance contracts. Because of capacity issues, one of these contracts was with an outside reinsurer. Second, the Company and its subsidiaries operate in fifty-four countries around the world. In evaluating this worldwide business, ALICO encounters wide ranges in both standards of living and mortality-morbidity experience. It would be unrealistic for the Company to have a uniform exposure (net retention after reinsurance ceded) throughout the world. And, if local branches or subsidiaries were permitted to retain high exposures, ALICO would constantly need to inject surplus funds into these countries to support the retained business. ALICO addresses this situation by evaluating each country individually. For subsidiaries, the Company seeks to act as the primary reinsurer. For branch operations, premiums are ceded to affiliates, which in turn retrocede the business to ALICO. In this way, premiums are retained "in-house" and branches and subsidiaries have the capacity to write larger

## American Life Insurance Company

amounts of premium. Thereafter, premiums are ceded to affiliates for excess coverages on a YRT basis and for catastrophe coverages, including those with third party reinsurers.

### Assumed

The Company's reinsurance assumed premiums for 2004 were distributed as follows:

	<u>Life &amp; Annuities</u>	<u>Accident &amp; Health</u>	<u>Total</u>
Affiliates	\$170,003,351	\$52,938,353	\$222,941,704
Non-affiliates	<u>819,175</u>	<u>(53,835)</u>	<u>765,340</u>
Totals	<u>\$170,822,526</u>	<u>\$52,884,518</u>	<u>\$223,707,044</u>

The Company's assumed premiums for 2004 had three major components:

- In 2004, ALICO assumed \$119,218,722 in premiums from American Security International (ASI), an alien affiliated insurer domiciled in the Isle of Man. ASI writes investment-type products on a non-admitted basis in the United Kingdom and retrocedes the business to ALICO via the Company's UK Branch.
- As noted above, ALICO's branches routinely cede business to affiliated insurers for the purpose of retroceding the same premiums to ALICO's Home Office, thereby keeping the business within the Company. In 2004, the Company assumed \$26,163,880 from American International Reinsurance Company (AIRCO) and American International Underwriting Overseas under this program.
- Of the remaining \$77,559,102 assumed from affiliates in 2004, the vast majority relates to ALICO providing primary coverage to its subsidiaries. The largest amounts assumed were \$18,667,456 from First American Polish Life Insurance and Reinsurance Company, and \$15,669,874 from Interamericana, ALICO's subsidiary in Chile. The Company also assumed sizable amounts from its subsidiaries in Venezuela, Slovakia and the Czech Republic.

### Ceded

The Company's ceded reinsurance program underwent a massive change during the period under examination; a change predicated by the increase in writings reported by the Company's Japan Branch (as noted above). As of the 2000 examination date, for life insurance, ceded premiums were \$226,478,005 while reserve credits were \$74,048,550. For 2004, life

American Life Insurance Company

ceded premiums were \$7,474,583,900 while reserve credits increased to \$4,452,550,587 and surplus relief was \$487,869,517.

The following chart provides a comparison of the five previous years:

	<u>2000</u>	<u>2001</u>	<u>2002</u>	<u>2003</u>	<u>2004</u>
Premiums					
Life	\$226,478,005	\$349,395,467	\$497,901,769	\$2,550,964,546	\$7,474,583,900
Acc & health	26,458,365	23,353,503	25,134,550	185,955,749	320,571,480
Reserve Credits					
Life	74,048,550	305,850,105	664,212,551	3,005,083,095	4,452,550,587
Acc & health	5,454,805	5,141,246	5,991,283	71,344,427	223,279,001
Surplus Relief					
Life	0	0	0	146,053,464	487,869,517
Acc & health	0	0	0	61,539,715	166,868,392
Funds Held					
Life	96,403,474	294,668,828	620,687,175	2,878,298,801	3,951,846,078
Acc & health	0	0	0	5,319,385	33,778,065

The four (4) ceded treaties below, all covering business written by ALICO's Japan Branch, account for a significant amount of the premiums, reserve credits, funds held liability and surplus relief reported by the Company at year end 2004:

1. Swiss Re of Zurich; effective August 1, 1999. Covers single premium deferred annuities (SPDA) denominated in US dollars (USD) in Japan. This treaty had no premiums in 2004 as it was succeeded by the AIG Life of Bermuda and RGA Re treaties noted below. Reserve credits were \$1,333,738,508 on the 2004 Blue Book, funds held were \$1,284,031,679 and surplus relief was \$49,706,830.

2. AIG Life of Bermuda; effective April 1, 2003. Covers SPDA products "A" and "B" written in Japan and denominated in USD. Ceded premiums for 2004 were \$754,257,070 and reserve credits were \$2,401,026,749. The ceded reserves were secured by funds held under this treaty of \$2,290,751,461. Outstanding surplus relief was \$110,275,288 as per the 2004 Blue Book.

3. AIG Life of Bermuda; effective April 1, 2003. Covers the Full in Hospital (A&H) business written in Japan. Premiums for 2004 were \$281,995,623, reserve credits were \$222,849,648, and outstanding surplus relief was \$166,868,392.

4. RGA Reinsurance Company; effective December 1, 2003. Covers SPDA product "C" written in Japan and denominated in foreign (non-yen) currencies. Premiums for 2004 were \$6,556,165,387, reserve credits were \$664,835,501 and outstanding surplus relief was \$326,093,039. The modified coinsurance reserve on this treaty at year end 2004 was \$5,983,499,325.

American Life Insurance Company

As disclosed in the Notes to the Financial Statements of the 2004 Blue Book, an affiliate of the Company, AIGTI, has provided RGA Reinsurance “credit enhancement” on the above treaty. A review of the Indemnity Agreement between AIGTI and RGA Reinsurance would indicate that AIGTI is guaranteeing an unstated minimum return on the Experience Account Balance contained in the treaty between ALICO and RGA Reinsurance. This examination notes that any amounts paid to RGA Reinsurance by AIGTI would result from the performance of ALICO’s Japan Branch as per investment yields and benefits paid on the underlying annuity business. Therefore:

**It is recommended that the guarantees to RGA Reinsurance as per the side agreement with AIGTI be more clearly quantified. The management of ALICO’s Japan Branch should be cognizant of the performance guarantees contained in the side agreement.**

The four above treaties accounted for \$7,592,418,080 in ceded premium in 2004, or 97.4% of the Company’s total. While the new ceded treaties were designed specifically for the single premium deferred annuity business in Japan, the surplus strain from writing huge amounts of new premium was so great that the accident and health products in Japan also had to be reinsured.

On a world-wide basis, the Company’s primary reinsurer is AIRCO, an affiliate domiciled in Bermuda. In 2004, ALICO ceded premiums of \$93,465,675 to AIRCO under three programs:

- ALICO branches ceding business to AIRCO and the premiums being retroceded back to the Company’s Home Office.	\$19,059,229
- AIRCO providing YRT coverage world-wide	63,242,239
- AIRCO providing various catastrophe coverages	<u>11,164,207</u>
Total	<u>\$93,465,675</u>

The YRT treaty with AIRCO has been the centerpiece of ALICO’s ordinary life reinsurance program for approximately twenty (20) years. In general, the treaty calls for the

## American Life Insurance Company

local branches to retain \$50,000 to \$200,000 per life with the reinsurer providing \$1,500,000 in life insurance, accidental death benefits and waiver of premium benefit coverages on most standard lives; however, the retentions and coverage vary from branch to branch.

In 2004, ALICO Japan's retention on individual life insurance was 50 million yen (or approximately \$450,000 at the 2004 year-end foreign exchange rate) and the retention was increased to 75 million yen (approximately \$725,000) effective December 1, 2005.

ALICO Japan's retention on individual life insurance was 50 million yen in 2004 (approximately \$450,000 at the year-end 2004 foreign exchange rate) and the retention was increased to 75 million yen (approximately \$725,000) effective December 1, 2005.

### United Kingdom Branch

ALICO's United Kingdom Branch files a Separate Account annual statement blank that is referred to as the "Green Book" in this Report. One of the drawbacks in using the separate account blank is the lack of information on reinsurance. Reinsurance premiums for the U.K. Branch are reported on the Blue Book annual statement; however, reinsurance reserves, whether assumed or ceded, are not reported on any annual statement. An extensive review of the U.K. Branch ceded reinsurance program noted the following:

In 2004, ALICO's United Kingdom Branch entered into a ceded reinsurance contract for health insurance with AIRCO that did not transfer morbidity risk, as required by Delaware Insurance Department Regulation 1002. The treaty provided ALICO with coverage only if the lapse rate on the subject block of business reported lower lapse rates than provided in the reinsurance contract. The examination permitted the treaty under Section 1104 of the Delaware Insurance Code but will also make the following recommendation:

**It is recommended the Company amend the reinsurance treaty between the United Kingdom Branch and AIRCO, that currently covers just lapse rates on health insurance, to include the transfer of morbidity risk as required by Regulation 1002 of Delaware Insurance Code.**

### **INTER-COMPANY AGREEMENTS**

ALICO operates on a large scale internationally and has approximately sixty (60) inter-company agreements. The Company's branch in Japan alone has in effect over two dozen such agreements, covering the Branch's operations from investments to sharing the expenses of a cafeteria. Virtually all services provided to the Company, particularly investment services, come from affiliates.

The more significant inter-company contracts are detailed below:

- ALICO is a participant in a Service and Expense Agreement, originally dated February, 1, 1974, among AIG and numerous subsidiaries. The parties to the agreement desire to share among themselves certain expenses such as equipment, office space, management services and personnel. The shared expenses are paid quarterly at cost. Allocation is to be made, on an item by item basis, by either specific identification or on a proportional basis. For 2004, ALICO paid \$18,825,918 under the Service and Expense Agreement.
- The Company participates in the Consolidated Federal Income Tax Return of AIG and its domestic subsidiaries, based upon a Tax Payment Allocation Agreement effective January 1, 1992. Basically, the agreement calls for the parent to charge ALICO for that portion of the consolidated tax liability that would have been paid by ALICO if a separate return had been filed. In addition, and of great importance to ALICO, AIG agrees under the terms of the tax sharing agreement to reimburse ALICO for the use of any losses and tax credits to the extent used by AIG in the consolidated tax return. As an insurer operating exclusively overseas, ALICO pays considerable taxes to foreign governments. These foreign tax payments are dollar for dollar tax credits on the U.S. federal Tax return of AIG. The parent reimburses ALICO for all foreign taxes utilized on the U.S. return. This situation means that ALICO basically doesn't pay any U.S. taxes.

In the investment area, ALICO has the following inter-company agreements:

-For the Home Office portfolios:

Management - AIG Global Investment Corp (Ireland)

American Life Insurance Company

Custodian - AIG Global Investment Trust Services

Securities Lending- AIG Global Securities Lending Corp.

-For the Japan Branch

Management- Two Agreements: AIG Global Investment Corp (Japan)

and AIG Investment Co.

### **ACCOUNTS AND RECORDS**

As noted in the Scope of Examination section of this Report, for the period under examination, ALICO's operations were audited by the firm of PricewaterhouseCoopers (PwC), Certified Public Accountants.

Regulation 301, Section 13.2 of the Delaware Insurance Codes states the following: "Every insurer required to file an Audited Financial Report pursuant to this regulation, shall require the accountant to make available for review by Department examiners, all workpapers prepared in the conduct of his examination"

During the examination review of ALICO's United Kingdom Branch, PwC's United Kingdom office refused to provide any audit workpapers for review by the examiners. This non-action by PwC was not only a violation of Regulation 301, it led to duplication of effort and greatly increased the time and cost of the examination.

**It is recommended that the Company work with PwC prior to the next examination to resolve the issues that resulted in PwC not providing the Department's examiners access to the workpapers from their annual audit as required by Regulation 301. If the Company is unable to resolve the issues with PwC in order for the Department's examiners to have access to the workpapers in the next examination, it is recommended that the Company find and utilize a CPA firm that will provide access to their workpapers in compliance with Regulation 301.**

Several discussions were held by the Department with representatives of PwC and the Company subsequent to the completion of the examination. As a result of these discussions, PwC and the

American Life Insurance Company

Company have assured the Department that its examiners will have access to PwC's workpapers in the next examination.

### **FINANCIAL STATEMENTS**

The Company's financial position on December 31, 2004, and the results of operations for 2004 are presented in the following statements. Differences of \$1.00 are due to rounding.

American Life Insurance Company

**ASSETS**

	Ledger <u>Assets</u>	Non-admitted <u>Assets</u>	Net Admitted <u>Assets</u>	<u>Notes</u>
Bonds	\$29,437,332,390		\$29,437,332,390	1
Preferred stocks	15,948,218		15,948,218	
Common stocks	5,636,071,456	\$33,638,995	5,602,432,461	2
Mortgage loans on real estate	904,678,492	38,565,118	866,113,374	3
Real estate:				
Properties occupied by the Company	46,236,213		46,236,213	
Properties held for income or sale	6,779,357		6,779,357	
Cash and short-term investments	1,240,850,610		1,240,850,610	
Contract loans	819,604,035		819,604,035	
Other invested assets	339,078,960		339,078,960	
Receivable for securities	14,186,922		14,186,922	
Aggregate write-ins for invested assets	55,761,117		55,761,117	
Investment income due and accrued	423,265,753		423,265,753	
Premiums and considerations:				
Uncollected premiums and agents' balances in course of collection	248,479,086	7,468,570	241,010,516	
Premiums deferred	22,308,055		22,308,055	
Reinsurance:				
Amounts recoverable from reinsurers	18,338,488		18,338,488	
Funds held by reinsured companies	48,677,652		48,677,652	
Other amounts recoverable	33,469,900		33,469,900	
Current federal/foreign tax recoverable	3,968,044		3,968,044	
Electronic data processing equipment and Software	65,852,145	42,063,652	23,788,493	
Furniture and equipment	27,255,580	27,255,580	0	
Receivable from parent, subsidiaries and Affiliates	201,545,358	79,964,483	121,580,874	4
Other asset non-admitted	1,927,983	1,927,983	0	
Premiums/insurance balances receivable	159,452,270	377,711	159,074,559	
Federal income taxes recoverable-parent	70,340,401		70,340,401	
Other assets	71,729,822	31,783,704	39,946,118	
Prepaid Expenses	<u>23,227,881</u>	<u>23,227,881</u>	<u>0</u>	
Total assets before Separate Accounts	\$39,936,366,184	\$286,273,677	\$39,650,092,507	
Separate Accounts	<u>16,602,161,782</u>		<u>0 16,602,161,782</u>	
TOTALS	<u>\$56,538,527,965</u>	<u>\$286,273,677</u>	<u>\$56,252,254,288</u>	

**LIABILITIES, SURPLUS AND OTHER FUNDS**

		Notes
Aggregate reserve for life contracts	\$ 24,244,847,413	5
Aggregate reserve for accident and Health contracts	2,383,951,764	
Liability for deposit-type contracts	1,221,499,156	
Contract claims:		
Life	184,999,221	
Accident and Health	232,283,157	
Policyholders' dividends due and unpaid	8,376	
Policyholders' dividends apportioned for payment in following year	40,664,461	
Provision for experience rated refunds	41,849,309	
Interest Maintenance Reserve	117,661,829	
Commissions to agents due and accrued	94,432,687	
General Insurance Expenses	105,544,964	
Transfers to Separate Accounts	27,401,243	
Taxes, licenses and fees	83,593,917	
Current federal and foreign taxes	108,430,593	
Net deferred tax liability	1,105,852,396	
Unearned investment income	4,281,387	
Amounts held for agents' account	4,444,745	
Remittances and items not allocated	201,859,588	
Liability for benefits to employees	233,114,486	
Asset Valuation Reserve	873,258,714	
Reinsurance in unauthorized companies	10,271,234	
Funds held for unauthorized reinsurers	55,167,358	
Payable to parent, subsidiaries and affiliates	190,072,480	
Funds held under coinsurance	3,985,624,143	
Payable for securities	475,675,804	
Reinsurance balance payable	44,882,200	
Accounts payable	<u>24,407,105</u>	
Total liabilities before Separate Accounts	\$36,096,079,730	
Separate Accounts	<u>16,064,168,543</u>	
Total Liabilities	\$52,160,248,273	
Common capital stock	3,000,000	
Gross paid in and contributed surplus	702,994,313	
Unassigned funds (surplus)	<u>3,386,011,702</u>	
Capital and Surplus	<u>\$4,092,006,015</u>	6
TOTAL	<u>\$56,252,254,288</u>	

American Life Insurance Company

**SUMMARY OF OPERATIONS**

Premiums and annuity considerations	\$14,139,746,759
Considerations for supplementary contracts	870,154
Net investment income	896,063,827
Amortization of Interest Maintenance Reserve	17,528,515
Separate Accounts net gain from operations	43,947,263
Commissions and expense allowances on reinsurance ceded	635,832,644
Reserve adjustment on reinsurance ceded	5,983,499,325
Other income	<u>7,855,968</u>
Totals	\$21,725,344,454
Death benefits	514,241,463
Matured endowments	214,494,249
Annuity benefits	48,013,494
Disability and accident & health benefits	590,610,942
Surrenders and withdrawals	5,501,457,507
Interest on deposit-type contracts	18,401,810
Payments on supplementary contracts	622,323
Increase in aggregate reserves for life and accident & health contracts	<u>9,803,316,174</u>
Totals	\$16,691,157,962
Commissions on premiums and annuities	1,039,877,816
Commissions on reinsurance assumed	30,571,377
General insurance expenses	1,493,530,283
Insurance taxes, licenses and fees	48,536,498
Increase in loading on deferred and uncollected premiums	23,326,179
Net transfers to separate accounts	1,913,485,237
Aggregate write-ins for deductions	<u>60,665,867</u>
Totals	<u>\$21,301,151,219</u>
Net gain from operations before policyholder dividends and federal income taxes	424,193,235
Dividends to policyholders	9,830,854
Federal and foreign income taxes	<u>171,426,008</u>
Net gain from operations before realized capital gains	\$242,936,373
Net realized capital gains	<u>25,627,443</u>
Net Income	<u>\$268,563,816</u>

American Life Insurance Company

**CAPITAL AND SURPLUS ACCOUNT**

Capital and Surplus, December 31, 2003		\$4,127,015,461
Net income	\$268,563,816	
Change in unrealized capital gains	505,020,669	
Change in net deferred income tax	(69,758,964)	
Change in nonadmitted assets	(129,586,868)	
Change in unrealized foreign exchange	(81,742,874)	
Change in liability for unauthorized reinsurance	1,298,668	
Change in asset valuation reserve	(443,755,606)	
Surplus contributed to Separate Accounts	(68,982,761)	
Other changes in surplus in Separate Accounts	34,718,120	
Dividends to stockholders	(50,000,000)	
Surplus paid in	150,000,000	
Correction of accounting error	(149,711,363)	
Other adjustments	(1,072,283)	
Change in Capital and Surplus for the year		<u>(35,009,446)</u>
Capital and Surplus, December 31, 2004		<u>\$4,092,006,015</u>

**SCHEDULE OF EXAMINATION ADJUSTMENTS**

	<u>Company Amount</u>	<u>Examination Amount</u>	Capital & Surplus Increase/ (Decrease)
Common Stocks	\$5,624,532,461	\$5,602,432,461	(\$22,100,000)
Mortgage Loans on Real Estate	904,678,492	866,113,374	(\$38,565,118)
Receivable from parent, subsidiaries and affiliates	201,545,358	121,580,875	<u>(\$79,964,483)</u>
Total Examination Adjustments			(\$140,629,601)
Company Capital and Surplus			<u>\$4,232,635,616</u>
Examination Capital and Surplus			<u>\$4,092,006,015</u>

**NOTES TO FINANCIAL STATEMENTS**

Note 1. Bonds

The Company reported \$29,437,332,387 for bonds on the 2004 Blue Book Annual Statement. In total amounts, ALICO reported the following for its bond portfolio:

Par Value	\$28,998,210,321
Cost	29,616,328,325
Fair Value	30,069,046,157
Book/Carrying Value	29,437,332,388

During the previous examination period, the NAIC's Securities Valuation Office (SVO) adopted guidelines which impacted ALICO. The SVO recognized that there are "foreign" securities (from issuers outside the United States) for which the required information needed to value the security might not be available. If these securities are owned by an insurance company that does no more than 20% of its business in the United States (such companies are referred to as "subparagraph D companies"), the following rules apply:

- the insurance company may determine the NAIC designation
- all securities so designated must be affixed with an "F" to denote a foreign security
- the insurance company must provide its domestic regulator with a description of the procedures used to evaluate and assign ratings to foreign securities

ALICO qualifies as a Subparagraph D company. If the Company rates a security using a Nationally Recognized Securities Rating Organization (NRSRO), the NAIC designation shall be the NAIC equivalent of the NRSRO rating. Such securities shall be listed as FE on Schedule D of the Annual Statement. If no NRSRO rating is available, the security shall be listed as simply an F, and the Company has to be able to defend its designation. The SVO also states that no security issued in a country can have a higher NAIC designation than the Sovereign Rating assigned to the government of that country. Approximately 98% of the Bonds reported by ALICO on the 2004 Blue Book carry the F or FE designation. ALICO reported only 14

## American Life Insurance Company

securities without the F or FE designation that were not U. S. Government securities. No exceptions were noted in the review of NAIC designations.

### Home Office Portfolios

The examination noted that bonds totaling \$2,133,596,082 are assigned to the Wilmington Home Office. The Home Office bonds are composed of several types of portfolios:

- the surplus of ALICO
- portfolios of branches where ALICO has been able to move funds out of the country to the Home Office.
- portfolios representing insurance products that cannot be assigned to any specific branch.

The Home Office portfolios are managed by an affiliate, AIG Global Investment Company-Ireland, which also manages the investments of the Company's U.K. Branch. The custodian of the Home Office portfolios is also an affiliate, AIG Global Trust Services (AIGGTS) also located in Ireland.

The examination noted three exceptions as in the Home Office portfolios:

- The custodian agreement with AIG Global Trust Services does not contain all the safeguard language ("the Indemnification Clause) recommended by the NAIC Financial Examiners Handbook. The examination notes that the custodian agreement with AIGGTS was previously amended to include some of the NAIC safeguards.

**It is recommended the Company's custodian agreement with AIG Global Trust Services be amended to include all of the safeguard language recommended in the NAIC Financial Examiners Handbook.**

- The Home Office portfolios were utilized in two Securities Lending arrangements. The first securities lending program was managed by an affiliate, AIG Global Securities Lending Corporation, and this program also involved the securities of the Company's U.K. Branch. The total amount of securities involved in the lending program at year end 2004 was \$2,579,366,076. SSAP #18 states that the reporting (or lending) entity shall receive collateral equal to at least 102% or 105% of the fair value

of the loaned securities. Despite several requests by the examination, the Company failed to provide evidence of collateral held for loaned securities.

**It is recommended the Company obtain evidence of collateral provided for loaned securities to demonstrate compliance with Statements of Statutory Accounting Principles 18, which states that the reporting (or lending) entity shall receive collateral equal to 102% or 105% of the fair value of loaned securities.**

- The Company supplied an additional list of loaned securities at year end 2004. This list indicated that \$16,026,138 had been loaned by the Company's custodian, AIGGTS, through an amendment to the custodian agreement. The Delaware Insurance Department has no record of reviewing that amendment. The examination noted that ALICO has already appointed an affiliate, AIGGSL, as its exclusive agent for securities lending. The securities lending by AIGGTS would seem to violate that agreement. In addition, the primary role of a custodian is to safeguard a client's assets; engaging in loaning those same assets would seem to contradict that mandate.

**It is recommended the Company's amended custodian agreement with AIGGTS be submitted to the Insurance Department for approval. It is additionally recommended that AIGGTS cease loaning ALICO's securities. ALICO already has appointed AIGGSL as its exclusive agent for the securities lending program; furthermore, it is the function of a custodian to safeguard an insurers assets, not engage in lending its securities.**

### Note #2 Common Stocks

The Company's common stock portfolio at year end 2004 consisted of the following three segments:

Stock of the parent, AIG Inc.	\$3,688,635,443
Stock of subsidiaries & affiliates	1,205,374,549
Other common stocks	<u>730,522,469</u>
Total	\$5,624,532,461

### AIG Stock.

ALICO's holding of the stock of its parent, AIG, dates to 1967 and has continually exerted a major influence on the Company's balance sheet. From a cost of \$2,241,437, the AIG stock appreciated by 164,566% through year end 2004. (It should be noted that in addition to the above Blue Book amounts, ALICO held at year end 2004 shares of the AIG stock at the U.K. branch at a value of \$113,868,251.) (It should be additionally noted that ALICO's ownership of

## American Life Insurance Company

its parent's stock pre-dates the modern Delaware Insurance Code and is therefore permitted under the "grandfather" provisions of the law.

However, the current four year examination period saw dramatic changes and events which significantly impacted ALICO. As of year end 2000, the AIG stock traded at a per share value of \$98.563. That value fell to \$63.35 per share as of year end 2004, reflecting a decrease in value of \$2,372,597,537 during the examination period.

Effective January 1, 2001, under the NAIC's Codification requirements, insurance companies were required to accrue a tax liability on unrealized capital gains. As of January 1, 2001, ALICO accrued a deferred tax liability of \$2,120,543,569 on the appreciation in value on the AIG stock. Because of the decline in the value of the AIG stock, the deferred tax liability also decreased, to \$1,290,237,902 as per the 2004 Blue Book. The Asset Valuation Reserve calculation on the AIG also went through a similar decline as the AIG stock decreased in value. Finally, in accordance with Statement of Statutory Accounting Principles No. 46, ALICO reduced the value of its AIG stock portfolio by a net amount of \$149,711,363 to account for the Company's reciprocal ownership of the AIG stock.

### Subsidiaries-Affiliates

ALICO reported values for forty-five (45) subsidiaries or affiliates at year end 2004. The total cost was \$1,234,179,628, reflecting an unrealized loss of \$28,805,079. At the time of the 2000 examination, the Company's unrealized loss on its subsidiaries and affiliates was \$253,434,508.

The Company's largest subsidiary is Unibanco Seguros S.A, a Brazilian company formerly known as AIG Participacoes do Brazil S.A. While the cost of the subsidiary is \$564,287,985, Unibanco Seguros's reported value was \$258,597,492 at year end 2004,

## American Life Insurance Company

indicating an unrealized loss of \$305,690,493. At the time of the 2000 examination, ALICO reported an unrealized capital loss of \$193,003,310 for this subsidiary.

A review of Unibanco Seguros' operations indicates profitable results. In 2004, the subsidiary paid dividends of \$55.5 million to the Company. One area of concern is the currency of Brazil, the Real. During the examination period, the Real was devalued. From an exchange rate of .51151 versus the US dollar at year end 2000, the exchange rate fell to .36499 at year end 2004. The decline in exchange rates was a major factor in the increase of the unrealized capital loss for Unibanco Seguros.

The examination reviewed the local audit report for the subsidiary operations in Brazil and noted several reconciling items that would decrease the value of Unibanco Seguros by \$22,100,000. The examination will reduce the value of common stocks by that amount in the financial statements of this Report.

During the period under examination, AIG acquired two large life insurance operations in Japan. ALICO participated in this acquisition through a subsidiary, AIG Financial Assurance Japan KK, which owns a portion of the former GE Edison Life (re-named AIG Edison Life). The Company reported a value of \$196,487,947 for AIG Financial Assurance at year end 2004.

Two of the Company's subsidiaries in former Iron Curtain countries have consistently reported profitable margins. ALICO's subsidiary in Poland, from a cost of \$24,801,281, reported a fair value of \$263,000,180. The Company's subsidiary in Slovakia, which has not been operational as long as Poland, reported a fair value of \$51,776,403 at year end 2004, against a cost of just \$4,881,000.

### Other Common Stocks

Of the \$730,522,469 in Other Common Stocks reported by the Company on the 2004 Blue Book, \$598,990,542 was reported by the Japan Branch. This amount was divided between

## American Life Insurance Company

individual common stocks amounting to \$256,355,343 and twenty-three (23) mutual funds that totaled \$342,635,199. Of the Japan Branch's mutual funds, eight (8) were held by banks which provided independent verification of both shares held and the per share price. The remaining fifteen (15) mutual funds, with a value of \$156,219,755 were held internally by ALICO-Japan, in a "Non-Custody Report". Nine of these mutual funds are AIG-sponsored funds while the other six are non-related funds. (It should be noted that the Japan Branch also holds bonds and loans with a value of \$121,742,326 internally, meaning the assets are not held by a custodian bank or trust company).

Holding the mutual funds internally is particularly an undesirable situation. The investment department of ALICO-Japan reports on the number of shares held in each fund, and an affiliate of ALICO, AIG Global Investment Company (which is also the Company's investment advisor) provides the share price of each fund. As noted above, nine of the mutual funds held internally are AIG sponsored and administered funds. Because the Company was able to provide a SAS 70 report that demonstrated strong internal controls in place at AIGGIC's Japan operations, the examination will admit the mutual funds held internally at the Japan Branch. The examination will make the recommendations below for corrective action. It should be noted that in Japan, the Company's separate account invested assets (of which large portions are mutual funds) are held by a third party custodian, which provides an independent valuation of the mutual funds.

**It is recommended that all common stock mutual funds held internally by the ALICO-Japan Branch be held at a third party custodian. The examination noted that the Japan Branch's separate account or variable mutual fund assets are held by custodians who provide an independent valuation of the shares prices. Additionally, it was noted that the Japan Branch holds bonds, loans, mortgages and other invested assets internally in the "Non-Custody Report." It is further recommended that, wherever possible, invested assets should be held by a third party custodian.**

## American Life Insurance Company

An error was noted in the Company's reporting on Schedule D of the 2004 Blue Book for Japan Branch common stocks. Initially, it appeared the Company combined five (5) funds for annual statement reporting purposes and did not use the respective individual fund share prices. Upon further investigation, it was noted that the Company had included two additional securities in this erroneous entry. In total, the Company reported a Blue Book entry of 3,500,311,554 shares for the AIGGIC Money Market Fund-New Hokuto, at a USD value of \$66,583,575. The Company doesn't own 3,500,311,554 shares of the New Hokuto mutual fund. Instead, the Company combined five AIGGIC funds, one outside mutual fund and one common stock into the Blue Book entry and backed into the share price reported in Schedule D. Overall, it appears that the dollar value was correct; however, this exception underscores the comment above that all investment securities should be held by custodians that can provide an independent verification of shares held and per share prices.

**It is recommended the Company accurately compile Schedule D and not combine several securities for Annual Statement reporting purposes.**

### **Note #3 Mortgage Loans on Real Estate**

The Company reported an amount of \$904,678,492 for Mortgage Loans on the 2004 Blue Book Annual Statement, a significant increase from the \$142,402,007 reported for the same item on the 2000 Annual Statement. Activity in the Company's Japan Branch accounted for the increase. During the period under examination, the Japan Branch issued ten (10) new mortgage loans to downstream subsidiary "specialty companies". At year end 2004, the Japan Branch had thirteen (13) loans to subsidiaries, at a value of \$897,396,450 or 99.2% of the Annual Statement balance.

In reviewing the mortgages issued by the Japan Branch, two (2) exceptions were noted:

## American Life Insurance Company

- For two mortgages, the balance of the loan exceeded the appraised value of the underlying real estate securing the loan. Moreover, Section 1118 of the Delaware Insurance Code states that mortgages on real property shall be reported at an amount not to exceed 90% of the fair value of the underlying property. The Company had eight (8) mortgages whose book value exceeded 90% of the fair value of the underlying property, in violation of Section 1118. The total amount that the eight (8) mortgages exceeded 90% was \$38,565,118. This amount will be reflected as an adjustment to the financial statement of this Report. In addition:

**It is recommended that the Company comply with Section 1118 of the Delaware Insurance Code and report values for mortgages that do not exceed 90% of the fair value of the underlying property supporting the mortgage loan.**

- The examination also noted that Section 1323 of the Delaware Code states that, upon issuance of the mortgage loan, no loan shall be issued in excess of 75% of the appraised value of the underlying property. A review of mortgage activity indicated that in 2003, the Company issued three mortgages well in excess of 75% of the appraised value.

**It is recommended that the Company comply with Section 1323 of the Delaware Insurance Code and issue no new mortgages for amounts in excess of 75% of the appraised value of the underlying property supporting the mortgage loan.**

### **Note #4 Receivables from parent, subsidiaries and affiliates.**

ALICO reported the amount of \$201,545,358 for the above captioned asset on the 2004 Blue Book Annual Statement. Included in the Company's receivable was the amount of \$79,964,483 for an "Indemnity Receivable" from AIG. During prior examination periods, ALICO engaged in several "Yen Swap" transactions by which funds in Japanese Yen were converted into U.S. dollars and subsequently invested in U.S. dollar-denominated investments. In these transactions, ALICO lent to and immediately borrowed back Yen from six financial institutions. In order to insure that ALICO suffered no foreign currency exchange losses when the loans matured, AIG provided the Company with an Indemnity Agreement. Any loss due to the decline in the exchange rates from the inception of a loan to its maturity would be reimbursed by AIG.

## American Life Insurance Company

During the period of the current examination, the Japanese regulators loosened restrictions on insurance companies holding assets in non-yen currencies. This development negated the need for the Yen Swap loans. ALICO moved assets of approximately 105 billion yen into U.S. dollar investments of approximately \$943 million. The Indemnity Agreement between ALICO and AIG was amended to no longer apply to the Yen Swap loans, but to apply to the 105 billion yen noted above. It was in this regard that the \$79,964,483 Indemnity Receivable was accrued at year end 2004.

The examination noted several exceptions in the review of the amended Indemnity Agreement:

- The Indemnity Agreement only applies if the 105 billion yen that was moved to U.S. dollars is exchanged back into yen. However, ALICO moved the funds into U.S. dollars to obtain significantly higher yields on fixed income securities. These higher yields and the long-term duration of the U.S. dollar denominated securities allowed the Company to achieve the matching of assets and liabilities required by Japanese regulators. These factors would make it very difficult for the Company to move any of its U.S. dollar securities back into yen. If there is no conversion of US dollars back into yen, there is no Indemnity Receivable.
- In conjunction with the first exception, the Indemnity Agreement has no termination date. It is “continuous” and contains no mandatory date or condition where funds will be translated from yen to U.S. dollars.

Because of these exceptions, the examination has non-admitted the Indemnity Receivable of \$79,964,483. This adjustment will reduce Capital and Surplus by a like amount in the financial statements of this report. Furthermore:

**It is recommended that any Indemnity Agreement between the Company and its parent provide for settlement dates or a termination date when any amounts due the Company will be promptly paid or settled.**

Additionally, the examination noted that on Holding Company filings and the Notes to the Financial Statements of the 2004 Blue Book, the Company continues to report that the Indemnity Agreement with AIG applies to the Yen Swap loan agreements As stated above, when

American Life Insurance Company

the Japanese regulators loosened restrictions on insurance companies holding assets in non-yen currencies, the Yen Swap loans were no longer needed. ALICO's Indemnity Agreement with AIG was amended to apply only to the 105 billion yen exchanged into U.S. dollars and invested in U.S. dollar-denominated investments.

**It is recommended the Company accurately complete the Holding Company Statement and Annual Statement. The disclosures regarding the Indemnity agreement covering the Yen Swap Loans are inaccurate as the Indemnity Agreement was amended and no longer covers the Yen Swap Loans.**

**Note #5 Aggregate Reserve for Life Policies and Contracts**

At year end 2004, ALICO reported the following amounts for Aggregate Life Policy Reserves on the Blue Book Annual Statement:

Life Insurance	\$13,485,592,587
Individual Annuities	9,543,374,154
Group Annuities	752,598,890
Supplemental Contracts	7,128,165
Accidental Death	17,300,493
Active and Disabled Lives	12,023,097
Miscellaneous Reserves	
Japan Contingency Fund	323,232,430
Terminal Benefits	52,076,392
Other	<u>51,521,204</u>
Total	<u>\$24,244,847,413</u>

As noted previously, the Company reports assets and liabilities of its United Kingdom (U.K.) Branch in the Green Book Separate Account Statement. The U.K reported the following at year end 2004:

Aggregate reserve for life, annuity and accident and health policies and contracts	\$10,982,236,636
--	------------------

ALICO also files two other separate account annual statements, for variable business written in Japan, and all other branches. The Japan Branch reported aggregate reserves for life,

American Life Insurance Company

annuity and accident and health policies and contracts of \$4,309,938,397 as of year end 2004, while the Other Branches reported similar reserves of \$194,205,038.

In accordance with the parameters detailed in the Scope of Examination Section of this report, the examination concentrated its review of ALICO's policy reserves in two phases:

Japan Branch/ United Kingdom Branch	On site review. Detailed testing of the Branch's Policy Master File was conducted. In Japan, the audit workpapers of Price WaterhouseCoopers were reviewed. In both branches, reports of AIG's Internal Audit Department were reviewed.
Greece, Spain, Portugal Lebanon, Cyprus, Bangladesh and UAE:	Amounts reported by the Branches and reflected on the 2004 Blue Book Annual Statements were reconciled to the local statutory audit reports. Reports of AIG's Internal Audit Department were reviewed for each branch.

These branches reported total policy reserves of \$38,257,000,000 or 96.3% of the total policy reserves reported on the combined 2004 Blue and Green Books and other Separate Accounts Annual Statements.

No exceptions were noted in the review of premium data during the examination on-site visits and no exceptions were noted in the review of the policy reserves reported by the seven "second phase" branches.

The examination retained the firm of INS Consultants Inc. (INS) for actuarial analysis.

INS Consultants reviewed ALICO's workpapers and electronic data files supporting the 2004 Blue Book and Green Book reserves and noted no exceptions. ALICO's decentralized administration led to the primary examination focus being a thorough review of asset adequacy/CFT (cash flow testing) analysis. Because the Japan Branch reported 80% of the Blue Book policy reserves, INS limited substantive analysis to the Japan Branch segment. No

## American Life Insurance Company

exceptions were noted. The remaining branch office reserve segments were analyzed by trend analysis, with reasonable results. The examination actuaries also performed a thorough review of the Company's Actuarial Opinion Memorandums (AOM) for the period under examination.

As a result of the examination analysis, the following findings are noted:

- In the previous (2000) examination, INS Consultants recommended the Company include in the Actuarial Opinion Memorandums a discussion of asset adequacy or Cash Flow Testing analysis of any business segment whose reserve exceeds 2.5% of statutory surplus. ALICO complied with that recommendation. For this exam, INS Consultants is recommending that the aggregate of reserves and actuarial liabilities NOT subject to cash flow testing or other asset adequacy analysis should not exceed 2.5% of statutory surplus.

**It is recommended that in the future, the aggregate of reserves and/or actuarial liabilities not subject to cash flow testing or other asset adequacy analysis, should not exceed 2.5% of statutory capital and surplus.**

- In the previous report of examination, INS Consultants recommended that the Company include a discussion in the Actuarial Opinion Memorandums of the adequacy of assets supporting any actuarial liabilities excluded from Cash Flow Testing analysis. For this examination, INS Consultants found that the Company had not fully complied with this recommendation. Therefore,

**It is recommended that future Actuarial Opinion Memorandums include the specific identification of assets supporting any actuarial liabilities excluded from Cash Flow-Testing analysis.**

- INS Consultants noted that, in the UK Branch, \$10.7 billion of the actuarial reserves are related to "indexed" products. INS Consultants noted that ALICO has immunized itself against the risk of disintermediation but believes there may be other risks that

remain the obligation of ALICO. These risks need to be evaluated and discussed.

Therefore:

**It is recommended that future Actuarial Opinion Memorandums evaluate and discuss all risks inherent in the United Kingdom indexed products.**

ALICO files three Separate Account annual statements: U.K. general and separate accounts, Japan separate account, and a third statement for all other branch's separate accounts. In reviewing the separate account statement all other branch's separate accounts, INS Consultants noted that while the policyholders bear the investment risk on these reserves, ALICO is responsible for mortality and expense charges. No AOM was provided in support of the asset adequacy of these segments. Therefore:

**It is recommended that a separate Actuarial Opinion Memorandum be compiled for the Separate Accounts - All Other Branches. Alternatively, the Statement of Actuarial Opinion for All Other Branches Separate Accounts should be required to identify the source of each liability, branch by branch, and to indicate whether that liability has been subjected to asset adequacy analysis.**

#### **Note #6-Capital and Surplus**

As noted throughout this Report, ALICO owns a significant block of its parent AIG, which has traditionally exerted a material impact on the Company's financial statements. Prior to the examination financial adjustments, ALICO reported Capital and Surplus of \$4,232,635,616 on the 2004 Blue Book Annual Statement. The following chart demonstrates the impact of the AIG stock on ALICO's Capital and Surplus:

-Value of the AIG stock, after deduction of deferred tax liability, asset valuation reserve and ALICO's reciprocal ownership per cent of AIG	\$2,120,420,579
-The Company's capital, contributed surplus and remaining unassigned funds	<u>2,112,215,037</u>
Total Reported Capital and Surplus	<u>\$4,232,635,616</u>

## American Life Insurance Company

As indicated above, the portion of the Company's Capital and Surplus represented by the AIG stock is a fraction over 50%. At the time of the 2000 examination, the AIG stock represented 79% of the Company's Capital and Surplus. More importantly, the value of the Company's Capital and Surplus not represented by appreciation on the AIG stock was \$1,216,494,916 at year end 2000. That value increased by 73.6% to the \$2,112,215,037 noted above.

Another area that impacts the Company's Capital and Surplus is foreign exchange. As of year end 2004, ALICO included in its Capital and Surplus a cumulative loss of \$318,022,744 due to changes in foreign exchange rates. Like many of the Company's results, the operations in Japan influence the overall results. Through year end 2004, ALICO has experienced a cumulative loss of \$489,997,203 on the exchange rates between the Yen and the U.S. dollar. This loss has been partially offset by a cumulative gain of \$149,403,092 for the U.S. dollar versus the Euro.

### **STATUS OF PRIOR EXAMINATION RECOMMENDATIONS**

The prior examination report as of December 31, 2000, contained sixteen (16) recommendations. Those findings with their current status are as follows:

#### **R1. The Company should fill out Schedule Y Properly**

The NAIC Annual Statement instructions state that all shareholder dividends and surplus contributions should be reported on Schedule Y. ALICO's subsidiary in Brazil paid 55.5 million in dividends in 2004. Also in 2004, ALICO contributed \$150 million to a subsidiary in Japan. These amounts are material and should be disclosed. This recommendation has been repeated in the current Report of Examination.

#### **R2. The Board of Directors should approve the actions of its committees**

The current examination noted instances where Executive Committee meetings were not reviewed by the ALICO Board of Directors. At both Executive Committee meetings, stockholder dividends were declared. This recommendation is repeated by the current examination.

**R3. The Board should elect the Investment Committee and define the role of the Finance Committee.**

During the current examination period, the ALICO Board elected the Investment Committee. The Finance Committee was discontinued.

**R4. The Board should review and approve the actions of the Banking Committee**

The current examination noted non-compliance with the previous exam recommendation. The recommendation is repeated in this Report of Examination.

**R5. All reinsurance contracts should be reported on Schedule F. All bulk reinsurance contracts should be submitted to the Insurance Department as required by Section 4944.**

The current examination noted no exceptions in this area.

**R6. ALICO should file a P&C annual statement to report its property-casualty business.**

The Company began filing a P&C annual statement during the current examination period.

**R7. The Company's custodian agreements should contain the NAIC recommended Indemnification Language.**

The previous examination's recommendations addressed deficiencies in the custodian agreements in place at the Japan and UK Branches. During the current examination period, ALICO changed custodians at both branches. No exceptions were noted in the review of the present custodian agreements used at the Japan and UK Branches. The examination will comment on the lack of complete compliance in the custodian agreement with AIGGTS, the custodian of the Home Office investment portfolios.

**R8. The Company should disclose Loaned Securities**

The recommendation in the 2000 Examination Report concerned securities lending at the Japan Branch. During the examination period, securities lending in Japan was limited to Separate Account common stocks. In 2004, Japan sold all individual common stocks held for the Separate Account and invested in common stock mutual funds. Due to this switch in investment vehicles, securities lending in Japan ceased. The Company still has in place the lending agreements in Japan that would trigger a violation of the annual statement instructions; however, due to the lack of securities lending, the previous recommendation is no longer applicable.

**R9. An audit of a Company subsidiary in Brazil should be performed. Also, audits should be performed of the numerous special purpose down-stream subsidiaries in Japan.**

During the current examination period, ALICO consolidated its holding company structure in Brazil. The intermediate holding company that was the subject of the examination recommendation was merged into a subsidiary (on which an audit is performed). Hence, the need for the recommendation was eliminated.

**R10. An audit of a large joint venture should be performed.**

The Company sold its interest in CEH Balkan Holdings in 2004. The recommendation is no longer applicable.

**R11. The Company's AOM should discuss asset adequacy for the liabilities excluded from Cash Flow Testing.**

The current examination noted some but not complete compliance with this recommendation. The recommendation is repeated by the current examination.

**R12. Cash Flow testing should be performed on all segments reported by the UK Branch.**

The current examination noted no exceptions in this area.

**R13. The Company should document the reserving requirements for all its branches.**

The current examination noted that the Company made an effort to comply with the recommendation but is still deficient for some branches. Because the undocumented areas involve smaller branches of the Company, an ECM comment will be made that the Company continue its documentation efforts.

**R14. The Company should annually submit a valuation report to the Department.**

The current examination noted compliance with this recommendation.

**R15. On the Annual Statements filed with the Department, the Company should report the reserves required by foreign jurisdictions.**

The current examination noted no exceptions in this area.

**R16. All stockholder dividends should be approved by the Board of Directors.**

The current examination noted situations where the Executive Committee of the Board of Directors approved stockholder dividends in 2001 and 2003. The actions of the Executive Committee were not subsequently approved by the Board of Directors.

**RECOMMENDATIONS**

The Company's attention is directed to the following examination recommendations:

It is again recommended the Company fill out Schedule Y in compliance with Annual Statement instructions. (See Holding Company System, page 9)

## American Life Insurance Company

It is recommended the Executive Committee of the Japan Branch report to the ALICO Board of Directors and have the actions of the Japan Executive Committee approved by the ALICO Board. (See Management and Control, page 11)

It is again recommended that the minutes of meetings of the Banking Committee be maintained and it is further recommended that all actions of the Banking Committee be approved by the ALICO Board of Directors. (See Management and Control, page 11)

It is again recommended that any action taken by the Executive Committee be reported to and approved by the Board of Directors at the next meeting following the Executive Committee action. (See Management and Controls, page 11)

It is recommended the Company undertake a project to update the Home Office files for certificates of authority or licenses in every country in which ALICO operates. (See Territory and Plan of Operation, page 16)

It is recommended the Company report premiums on ceded reinsurance contracts in accordance with the NAIC Annual Statement Instructions. (See Territory and Plan of Operation, page 17)

It is recommended the Company reduce the ceded reinsurance coverage on the property-casualty business in the Mid-East to writing. The ceded reinsurance contracts must contain all clauses required by the Delaware Insurance Code and Statement of Statutory Accounting Principles No.62, and must demonstrate transfer of risk. (See Territory and Plan of Operation, page 27)

It is recommended that the guarantees to RGA Reinsurance as per the side agreement with AIGTI be more clearly quantified. The management of ALICO's Japan Branch should be cognizant of the performance guarantees contained in the side agreement. (See Reinsurance, page, 31)

## American Life Insurance Company

It is recommended the Company amend the reinsurance treaty between the United Kingdom Branch and AIRCO that currently covers just lapse rates on health insurance, to include the transfer of morbidity risk as required by Regulation 1002 of Delaware Insurance Code. (See Reinsurance, page 32)

It is recommended that the Company work with PwC prior to the next examination to resolve the issues that resulted in PwC not providing the Department's examiners access to the workpapers from their annual audit as required by Regulation 301. If the Company is unable to resolve the issues with PwC in order for the Department's examiners to have access to the workpapers in the next examination, it is recommended that the Company find and utilize a CPA firm that will provide access to their workpapers in compliance with Regulation 301. (See Accounts and Records, page 34)

It is recommended the Company's custodian agreement with AIG Global Trust Services should be amended to include all of the safeguard language recommended in the NAIC Financial Examiners Handbook. (See Note #1, Bonds, page 41)

It is recommended the Company obtain evidence of collateral provided for loaned securities to demonstrate compliance with Statement of Statutory Accounting Principles 18, which states that the reporting (or lending) entity shall receive collateral equal to 102% or 105% of the fair value of loaned securities. (See Note #1, Bonds, page 42)

It is recommended the Company's amended custodian agreement with AIGGTS be submitted to the Delaware Department of Insurance for approval. It is additionally recommended that AIGGTS cease loaning ALICO's securities. ALICO already has appointed AIGGSL as its exclusive agent for the securities lending program; furthermore, it is the function of a custodian

American Life Insurance Company

to safeguard an insurers assets, not engage in lending its securities. (See Note #1, Bonds, page 42)

It is recommended that all common stock mutual funds held internally by the ALICO-Japan Branch be held at a third party custodian. The examination noted that the Japan Branch's separate account or variable mutual fund assets are held by custodians who provide an independent valuation of the shares prices. Additionally, it was noted that the Japan Branch holds bonds, loans, mortgages and other invested assets internally in the "Non-Custody Report." It is further recommended that, wherever possible, invested assets should be held by a third party custodian. (See Note #2, Common Stocks, page 45)

It is recommended the Company accurately compile Schedule D and not combine several securities for Annual Statement reporting purposes. (See Note #2, Common Stocks, page 46)

It is recommended that the Company comply with Section 1118 of the Delaware Insurance Code and report values for mortgages that do not exceed 90% of the fair value of the underlying property supporting the mortgage loan. (See Note #3, Mortgages, page 47)

It is recommended that the Company comply with Section 1323 of the Delaware Insurance Code and issue no new mortgages for amounts in excess of 75% of the appraised value of the underlying property supporting the mortgage loan. (See Note #3, Mortgages, page 47)

It is recommended that any Indemnity Agreement between the Company and its parent provide for settlement dates or a termination date when any amounts due the Company will be promptly paid or settled. (See Note #4, Receivable from parent, etc, page 48)

It is recommended the Company accurately complete the Holding Company Statement and Annual Statement. The disclosures regarding the Indemnity Agreement covering the Yen

American Life Insurance Company

Swap Loans are inaccurate as the Indemnity Agreement was amended and no longer covers the Yen Swap Loans. (See Note #4, Receivable from Parent, Subsidiaries, and Affiliates, page 49)

It is recommended that in the future, the aggregate of reserves and/or actuarial liabilities not subject to cash flow testing or other asset adequacy analysis, should not exceed 2.5% of statutory capital and surplus. (See Note #5, Aggregate policy reserves, page 51)

It is recommended that future Actuarial Opinion Memorandums include the specific identification of assets supporting any actuarial liabilities excluded from Cash Flow Testing analysis. (See Note #5, Aggregate policy reserves, page 51)

It is recommended that future Actuarial Opinion Memorandums evaluate and discuss all risks inherent in the United Kingdom indexed products. (See Note #5, Aggregate policy reserves, page 52)

It is recommended that a separate Actuarial Opinion Memorandum be compiled for the Separate Accounts - All Other Branches. Alternatively, the Statement of Actuarial Opinion for All Other Branches Separate Accounts should be required to identify the source of each liability, branch by branch, and to indicate whether that liability has been subjected to asset adequacy analysis. (See Note #5, Aggregate policy reserves, page 52)

### **SUMMARY COMMENTS**

ALICO operates in fifty-four (54) countries as a truly global insurance operation. During the examination period, the Company discontinued operations in ten (10) countries and began or resumed operation in four (4) countries.

Assets, exclusive of the Separate Accounts business, have grown approximately 107% since the last examination. Separate Accounts assets grew 73% since 2000. The increase in assets is due primarily to the significant increase in revenues generated from the Company's

## American Life Insurance Company

operations in Japan, where admitted assets (excluding separate accounts) increased \$20.3 billion or 205% in four years. The most prominent increase occurred in Japan from 2003 to 2004. The Company began issuing single premium deferred annuities through banks in Japan. The Japan Branch increased its annuity sales in 2004 alone by almost \$6 billion.

ALICO's Capital and Surplus decreased -\$1,669,898,316 (before examination adjustments) since 2000 representing a decrease of (28.3%). Two points are particularly noteworthy:

- Since 1967, ALICO has held a significant block of common stock of its parent, AIG. From a cost of \$2,241,437 in 1967, the value of the Company's AIG stock rose to \$6,060,937,324 as of December 31, 2000.

However, effective January 1, 2001, under the NAIC's Codification requirements, insurance companies were required to accrue a tax liability on unrealized capital gains. As of January 1, 2001, ALICO accrued a deferred tax liability of \$2,120,543,569 on the appreciation in value on the AIG stock.

- The market value of the AIG stock was \$99.563 per share as of year end 2000.

The market value fell to \$79.40 per share by December 31, 2001 and was \$63.35 as of year end 2004. The sizable decline in the value of the Company's AIG stock impacted the Company's financial reporting in several areas: besides the decrease in cumulative unrealized capital gains, the decline reduced the deferred tax liability noted above, and also triggered a decrease in the Asset Valuation Reserve. As of year end 2000, ALICO had accrued an Asset Valuation Reserve equal to 25% of the cumulative appreciation on the AIG stock.

## American Life Insurance Company

ALICO reported \$975,484,614 in Net Income during the four-(4) year period under review and reported positive Net Income in each year. During the same period, the Company paid \$204,897,054 in dividends to stockholders.

Prior to the examination financial adjustments, ALICO reported Capital and Surplus of \$4,232,635,616 on the 2004 Blue Book Annual Statement. The following chart demonstrates the impact of the AIG stock on ALICO's Capital and Surplus:

-Value of the AIG stock, after deduction of deferred tax liability, asset valuation reserve and ALICO's reciprocal ownership per cent of AIG	\$2,120,420,579
-The Company's capital, contributed surplus and remaining unassigned funds	<u>2,112,215,037</u>
Total Reported Capital and Surplus	<u>\$4,232,635,616</u>

As indicated above, the portion of the Company's Capital and Surplus represented by the AIG stock is a fraction over 50%. At the time of the 2000 examination, the AIG stock represented 79% of the Company's Capital and Surplus. More importantly, the value of the Company's Capital and Surplus not represented by appreciation on the AIG stock was \$1,216,494,916 at year end 2000. That value increased by 73.6% to the \$2,112,215,037 noted above.

### **CONCLUSION**

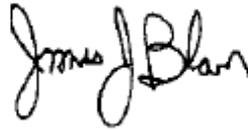
The following schedule shows the results of this examination and the results of the prior examination with changes between the examination periods:

<u>Description</u>	<u>Current Examination</u>	<u>12/31/2000 Examination</u>	<u>Changes Increases (Decreases)</u>
Assets	\$56,252,254,288	\$28,911,262,715	\$27,340,991,573
Liabilities	52,160,248,273	22,891,083,020	29,269,165,253
Capital and Surplus	4,092,006,015	6,020,179,695	(\$1,928,173,680)

American Life Insurance Company

In addition to the undersigned, Gregg Bealuk, CFE, John White, AFE and Thomas Bickerstaff, FSA, MAAA, of INS Consultants Inc., participated in the examination.

Respectfully submitted,

A handwritten signature in black ink that reads "James J. Blair". The signature is written in a cursive style with a large initial "J" and "B".

---

James J. Blair CFE, CPA  
Examination Supervisor  
Insurance Department  
State of Delaware

## SUBSIDIARIES OF REGISTRANT

	Jurisdiction of Incorporation or Organization	Percentage of Voting Securities Owned by Its Immediate Parent <sup>(2)</sup>
American International Group, Inc. (Registrant) <sup>(1)</sup>	Delaware	(3)
AIG Aviation, Inc.	Georgia	100
AIG Bulgaria Insurance and Reinsurance Company EAD	Bulgaria	100
AIG Capital Corporation	Delaware	100
AIG Consumer Finance Group, Inc.	Delaware	100
AIG Bank Polska S.A.	Poland	97.23
AIG Credit S.A.	Poland	80
Compania Financiera Argentina S.A.	Argentina	92.7
AIG Finance Holdings, Inc.	New York	100
AIG Finance (Hong Kong) Limited	Hong Kong	100
AIG Global Asset Management Holdings Corp.	Delaware	100
AIG Asset Management Services, Inc.	Delaware	100
Brazos Capital Management, L.P.	Delaware	92
AIG Capital Partners, Inc.	Delaware	100
AIG Equity Sales Corp.	New York	100
AIG Global Investment Corp.	New Jersey	100
International Lease Finance Corporation	California	64.85 <sup>(4)</sup>
AIG Global Real Estate Investment Corp.	Delaware	100
AIG Credit Corp.	Delaware	100
A.I. Credit Corp.	New Hampshire	100
Imperial Premium Finance, Inc.	California	100
Imperial Premium Finance, Inc.	Delaware	100
AIG Egypt Insurance Company, S.A.E.	Egypt	89.98
AIG Federal Savings Bank	Delaware	100
AIG Financial Advisor Services, Inc.	Delaware	100
AIG Financial Advisor Services (Europe), S.A.	Luxembourg	100
AIG Financial Products Corp.	Delaware	100
AIG Matched Funding Corp.	Delaware	100
Banque AIG	France	90 <sup>(5)</sup>
AIG Funding, Inc.	Delaware	100
AIG Global Trade & Political Risk Insurance Company	New Jersey	100
A.I.G. Golden Insurance Ltd.	Israel	50.01
AIG Life Insurance Company	Delaware	79 <sup>(6)</sup>
AIG Life Insurance Company of Canada	Canada	100
AIG Life Insurance Company of Puerto Rico	Puerto Rico	100
AIG Liquidity Corp.	Delaware	100
AIG Marketing, Inc.	Delaware	100
AIG Memsas, Inc.	Delaware	100 <sup>(7)</sup>
Tata AIG General Insurance Company Limited	India	26
AIG Private Bank Ltd.	Switzerland	100
AIG Retirement Services, Inc.	Delaware	100 <sup>(8)</sup>
SunAmerica Life Insurance Company	Arizona	100
SunAmerica Investments, Inc.	Georgia	70 <sup>(9)</sup>
AIG Advisor Group, Inc.	Maryland	100
Advantage Capital Corporation	New York	100
FSC Securities Corporation	Delaware	100
Royal Alliance Associates, Inc.	Delaware	100
Sentra Securities Corporation	California	100
Spelman & Co., Inc.	California	100
SunAmerica Securities, Inc.	Delaware	100
AIG SunAmerica Life Assurance Company	Arizona	100 <sup>(10)</sup>
AIG SunAmerica Asset Management Corp.	Delaware	100
AIG SunAmerica Capital Services, Inc.	Delaware	100
First SunAmerica Life Insurance Company	New York	100
AIG Risk Management, Inc.	New York	100
AIG Technologies, Inc.	New Hampshire	100

## SUBSIDIARIES OF REGISTRANT

	Jurisdiction of Incorporation or Organization	Percentage of Voting Securities Owned by its Immediate Parent <sup>(2)</sup>
American International Reinsurance Company, Ltd.	Bermuda	100
AIG Edison Life Insurance Company	Japan	90 <sup>(17)</sup>
American International Assurance Company, Limited	Hong Kong	100
American International Assurance Company (Australia) Limited	Australia	100
American International Assurance Company (Bermuda) Limited	Bermuda	100
American International Assurance Co. (Vietnam) Limited	Vietnam	100
Tata AIG Life Insurance Company Limited	India	26
Nan Shan Life Insurance Company, Ltd.	Taiwan	95
American International Underwriters Corporation	New York	100
American International Underwriters Overseas, Ltd.	Bermuda	100
AIG Europe (Ireland) Limited	Ireland	100
AIG Europe (U.K.) Limited	England	100
AIG Brasil Companhia de Seguros	Brazil	50
Universal Insurance Co., Ltd.	Thailand	100
La Seguridad de Centroamerica, Compania de Seguros S.A.	Guatemala	100
La Meridional Compania Argentina de Seguros	Argentina	100
American International Insurance Company of Puerto Rico	Puerto Rico	100
A.I.G. Colombia Seguros Generales S.A.	Colombia	100
American International Underwriters GmBH	Germany	100
Underwriters Adjustment Company, Inc.	Panama	100
American Life Insurance Company	Delaware	100
AIG Life (Bulgaria) Z.D. A.D	Bulgaria	100
ALICO, S.A	France	100
First American Polish Life Insurance and Reinsurance Company, S.A.	Poland	100
Inversiones Interamericana S.A. (Chile)	Chile	100
Pharaonic American Life Insurance Company	Egypt	71.63
Unibanco AIG Seguros S.A.	Brazil	47.81 <sup>(18)</sup>
AIG Life Insurance Company (Switzerland) Ltd.	Switzerland	100
American Security Life Insurance Company, Ltd.	Lichtenstein	100
Birmingham Fire Insurance Company of Pennsylvania	Pennsylvania	100
China America Insurance Company, Ltd.	Delaware	50
Commerce and Industry Insurance Company	New York	100
Commerce and Industry Insurance Company of Canada	Ontario	100
Delaware American Life Insurance Company	Delaware	100
Hawaii Insurance Consultants, Ltd.	Hawaii	100
HSB Group, Inc.	Delaware	100
The Hartford Steam Boiler Inspection and Insurance Company	Connecticut	100
The Hartford Steam Boiler Inspection and Insurance Company of Connecticut	Connecticut	100
HSB Engineering Insurance Limited	England	100
The Boiler Inspection and Insurance Company of Canada	Canada	100
The Insurance Company of the State of Pennsylvania	Pennsylvania	100
Landmark Insurance Company	California	100
Mt. Mansfield Company, Inc.	Vermont	100

## SUBSIDIARIES OF REGISTRANT

	Jurisdiction of Incorporation or Organization	Percentage of Voting Securities Owned by its Immediate Parent <sup>(2)</sup>
AIGTI, Inc.	Delaware	100
AIG Trading Group Inc.	Delaware	100
AIG International, Inc.	Delaware	100
AIU Insurance Company	New York	52 <sup>(11)</sup>
AIU North America, Inc.	New York	100
American General Corporation	Texas	100
American General Bancassurance Services, Inc.	Illinois	100
AGC Life Insurance Company	Missouri	100
AIG Assurance Canada	Canada	100 <sup>(7)</sup>
AIG Life of Bermuda, Ltd.	Bermuda	100
American General Life and Accident Insurance Company	Tennessee	100
American General Life Insurance Company	Texas	100
American General Annuity Service Corporation	Texas	100
AIG Enterprise Services, LLC	Delaware	100
American General Equity Services Corporation	Delaware	100
American General Life Companies, LLC	Delaware	100
The Variable Annuity Life Insurance Company	Texas	100
VALIC Retirement Services Company	Texas	100
VALIC Trust Company	Texas	100
American General Property Insurance Company	Tennessee	51.85 <sup>(12)</sup>
American General Property Insurance Company of Florida	Florida	100
AIG Annuity Insurance Company	Texas	100
The United States Life Insurance Company in the City of New York	New York	100
American General Finance, Inc.	Indiana	100
American General Auto Finance, Inc.	Delaware	100
American General Finance Corporation	Indiana	100
MorEquity, Inc.	Nevada	100
Wilmington Finance, Inc.	Delaware	100
Merit Life Insurance Co.	Indiana	100
Yosemite Insurance Company	Indiana	100
CommoLoCo, Inc.	Puerto Rico	100
American General Financial Services of Alabama, Inc.	Alabama	100
American General Investment Management Corporation	Delaware	100
American General Realty Investment Corporation	Texas	100
American General Assurance Company	Illinois	100
American General Indemnity Company	Illinois	100
USLIFE Credit Life Insurance Company of Arizona	Arizona	100
Knickerbocker Corporation	Texas	100
American Home Assurance Company	New York	100
AIG Domestic Claims, Inc.	Delaware	50 <sup>(13)</sup>
AIG Hawaii Insurance Company, Inc.	Hawaii	100
American Pacific Insurance Company, Inc.	Hawaii	100
American International Insurance Company	New York	100
American International Insurance Company of California, Inc.	California	100
American International Insurance Company of New Jersey	New Jersey	100
Minnesota Insurance Company	Minnesota	100
American International Realty Corp.	Delaware	31.5 <sup>(14)</sup>
Pine Street Real Estate Holdings Corp.	New Hampshire	31.47 <sup>(14)</sup>
Transatlantic Holdings, Inc.	Delaware	33.45 <sup>(15)</sup>
Transatlantic Reinsurance Company	New York	100
Putnam Reinsurance Company	New York	100
Trans Re Zurich	Switzerland	100
American International Insurance Company of Delaware	Delaware	100
American International Life Assurance Company of New York	New York	77.52 <sup>(16)</sup>

## SUBSIDIARIES OF REGISTRANT

	Jurisdiction of Incorporation or Organization	Percentage of Voting Securities Owned by its Immediate Parent <sup>(2)</sup>
National Union Fire Insurance Company of Pittsburgh, Pa.	Pennsylvania	100
American International Specialty Lines Insurance Company	Alaska	70 <sup>(19)</sup>
Lexington Insurance Company	Delaware	70 <sup>(19)</sup>
AIG Centennial Insurance Company	Pennsylvania	100
AIG Premier Insurance Company	Pennsylvania	100
AIG Indemnity Insurance Company	Pennsylvania	100
AIG Preferred Insurance Company	Pennsylvania	100
AIG Auto Insurance Company of New Jersey	New Jersey	100
JI Accident & Fire Insurance Co. Ltd.	Japan	50
National Union Fire Insurance Company of Louisiana	Louisiana	100
National Union Fire Insurance Company of Vermont	Vermont	100
21st Century Insurance Group	California	33.03 <sup>(20)</sup>
21st Century Insurance Company	California	100
21st Century Casualty Company	California	100
21st Century Insurance Company of the Southwest	Texas	100
Starr Excess Liability Insurance Company, Ltd.	Delaware	100
Starr Excess Liability Insurance International Ltd.	Ireland	100
NHIG Holding Corp.	Delaware	100
Audubon Insurance Company	Louisiana	100
Audubon Indemnity Company	Mississippi	100
Agency Management Corporation	Louisiana	100
The Gulf Agency, Inc.	Alabama	100
New Hampshire Insurance Company	Pennsylvania	100
AIG Europe, S.A.	France	<sup>(21)</sup>
AI Network Corporation	Delaware	100
American International Pacific Insurance Company	Colorado	100
American International South Insurance Company	Pennsylvania	100
Granite State Insurance Company	Pennsylvania	100
New Hampshire Indemnity Company, Inc.	Pennsylvania	100
AIG National Insurance Company, Inc.	New York	100
Illinois National Insurance Co.	Illinois	100
New Hampshire Insurance Services, Inc.	New Hampshire	100
AIG Star Life Insurance Co., Ltd	Japan	100
The Philippine American Life and General Insurance Company	Philippines	99.78
Pacific Union Assurance Company	California	100
Philam Equitable Life Assurance Company, Inc.	Philippines	95.31
Philam Insurance Company, Inc.	Philippines	100
Risk Specialist Companies, Inc.	Delaware	100
United Guaranty Corporation	North Carolina	36.31 <sup>(22)</sup>
United Guaranty Insurance Company	North Carolina	100
United Guaranty Mortgage Insurance Company	North Carolina	100
United Guaranty Mortgage Insurance Company of North Carolina	North Carolina	100
United Guaranty Partners Insurance Company	Vermont	80
United Guaranty Residential Insurance Company of North Carolina	North Carolina	100
United Guaranty Residential Insurance Company	North Carolina	75.03 <sup>(23)</sup>
United Guaranty Commercial Insurance Company of North Carolina	North Carolina	100
United Guaranty Mortgage Indemnity Company	North Carolina	100
United Guaranty Credit Insurance Company	North Carolina	100
United Guaranty Services, Inc.	North Carolina	100

(1) All subsidiaries listed are consolidated in the accompanying financial statements. Certain subsidiaries have been omitted from the tabulation. The omitted subsidiaries, when considered in the aggregate as a single subsidiary, do not constitute a significant subsidiary.

(2) Percentages include directors' qualifying shares.

(3) The common stock is owned approximately 12.0 percent by Starr International Company, Inc., 1.8 percent by C.V. Starr & Co., Inc. and 2.0 percent by The Starr Foundation.

(4) Also owned 35.15 percent by National Union Fire Insurance Company of Pittsburgh, Pa.

(5) Also owned 10 percent by AIG Matched Funding Corp.

(6) Also owned 21 percent by Commerce and Industry Insurance Company.

(7) Indirect wholly-owned subsidiary.

## SUBSIDIARIES OF REGISTRANT

- (8) Formerly known as AIG SunAmerica Inc.*
- (9) Also owned 30 percent by AIG Retirement Services, Inc.*
- (10) Formerly known as Anchor National Life Insurance Company.*
- (11) Also owned eight percent by The Insurance Company of the State of Pennsylvania, 32 percent by National Union Fire Insurance Company of Pittsburgh, Pa. and eight percent by Birmingham Fire Insurance Company of Pennsylvania.*
- (12) Also owned 48.15 percent by American General Life and Accident Insurance Company.*
- (13) Also owned 50 percent by The Insurance Company of the State of Pennsylvania.*
- (14) Also owned by 11 other AIG subsidiaries.*
- (15) Also owned 25.95 percent by AIG.*
- (16) Also owned 22.48 percent by American Home Assurance Company.*
- (17) Also owned ten percent by a subsidiary of American Life Insurance Company.*
- (18) Also owned 1.7 percent by American International Underwriters Overseas, Ltd. and .48 percent by American Home Assurance Company.*
- (19) Also owned 20 percent by The Insurance Company of the State of Pennsylvania and ten percent by Birmingham Fire Insurance Company of Pennsylvania.*
- (20) Also owned 16.85 percent by American Home Assurance Company, 6.34 percent by Commerce and Industry Insurance Company and 6.34 percent by New Hampshire Insurance Company.*
- (21) 100 percent to be held with other AIG companies.*
- (22) Also owned 45.88 percent by National Union Fire Insurance Company of Pittsburgh, Pa., 16.95 percent by New Hampshire Insurance Company and 0.86 percent by The Insurance Company of the State of Pennsylvania.*
- (23) Also owned 24.97 percent by United Guaranty Residential Insurance Company of North Carolina.*