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BACKGROUNDER

Longtime AIG Chairman Maurice "Hank" Greenberg Forced Out After Evidence Company Manipulated Reserves

Same Practice Used by Medical Malpractice Insurers to Justify Excessive Rates for Doctors

The Chairman of American International Group (AIG), one of the largest insurance companies in the world and a major medical malpractice insurer, has reportedly been forced to resign as the company's chief executive after New York Attorney General Eliot Spitzer sought to depose Greenberg in its investigation of company practices.

According to the March 15, 2005, *New York Times,* "Investigators want to question Mr. Greenberg over a transaction he personally struck in late 2000 and early 2001. The transaction -- between A.I.G. and Cologne Re, a subsidiary of Gen Re -- *bolstered A.I.G.'s reserves, making its financial position look better than it actually was,* regulators said. Reserves are the money an insurance company sets aside to pay future claims; their levels are watched closely by investors." (emphasis added).

Manipulation of reserves set aside to pay claims has been considered a major factor precipitating the medical malpractice insurance "crisis" for doctors in recent years. In hard markets (i.e. dropping investment income, rising insurance premiums), as we have recently experienced, insurers increase reserves as a way to justify premium increases. In fact, the recent insurance "crisis" rests significantly on a jump in reserves in 2001.

In June 2002, a front page *Wall Street Journal* article exposed the widely used insurance accounting practice of manipulating reserves in the early 1990s, which made the medical malpractice insurance business appear far more profitable than it really was - precisely the allegation now being made against AIG.[1]

Specifically, during the 1980s, one of the country's largest medical malpractice insurers, St. Paul, set aside too much money in reserves. Then, in the 1990s, the company "'released' $1.1 billion in reserves," which flowed through St. Paul's income statements. According to the *Journal*, this accounting practice made St. Paul appear to be "a model for big, quick profits" causing many new companies to enter the medical malpractice insurance market. Competition led to severe price cuts during this period, which were inadequate to cover claims. Then, when investment income declined, rates shot up. Many companies, including St. Paul, left the med mal insurance market altogether, creating a huge supply and demand problem for doctors in a number of states, like Nevada. In other words, manipulation of reserves precipitated today's medical malpractice insurance crisis.

Additional interesting facts about AIG include:

- In 2004, the company, a major medical malpractice insurer, experienced record profits "despite a year marked by catastrophe losses, a run-in with the U.S. authorities over its finite risk business and allegations of bid rigging." Net income for 2004 was $11.05 billion, an increase of 19.1% over 2003.[2]

- According to Texans for Public Justice, Hank Greenberg was a member of the elite group of George W. Bush fundraisers called "Pioneers" – people who raised at least $100,000 for Bush's original presidential run.[3]

- Greenberg was part of a group of 15 insurance executives brought into the White House for a private meeting with Bush and Commerce Secretary Donald L. Evans shortly after 9/11 to push for a taxpayer bailout of insurance companies in the event of future terrorist attacks.[4] In November 2002, Congress passed this bill, legislation that would have the government covering 90 percent of all terrorism-related losses after insurers pay a relatively small amount. This passed is despite then over a year's worth of evidence that the economic crisis that insurers promised due to the lack of a federal terrorism insurance backup never materialized.[5]

For more information, contact the Center for Justice & Democracy, http://centerjd.org

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NOTES

[1] Rachel Zimmerman And Christopher Oster, "Insurers' Price Wars Contributed To Doctors Facing Soaring Costs; Lawsuits Alone Didn't Inflate Malpractice Premiums; Reserves at St. Paul Distorted Pricing Picture in 1990s," *Wall St. Journal,* June 24, 2002.
[2] *Insurance Day,* February 10, 2005.
[3] Texans for Public Justice, *The Pioneers: George W. Bush's $100,000 Club*, found at http://www.tpj.org/pioneers.
[4] Stephen Labaton and Joseph B. Treaster, "Insurers Push for Cap on Future Payouts," *New York Times*, October 22, 2001; Center for Responsive Politics, "After the Attacks: A Special Report on America's Changed Political and Legislative Landscape," September 26, 2001, found at http://www.opensecrets.org/alerts/v6/postterrorism.asp#04. *See also*, Texans for Public Justice, "Pioneer Profiles: Industry Index," found at http://www.tpj.org/pioneers/industry_index.html#in.
[5] *See, e.g.,* Consumer Federation of America, "CFA Study Finds Fewer Terror Insurance Problems, Lower Losses Than Predicted," January 23, 2002, found at http://www.consumerfed.org/disaster_terror_insurance_1_02reportrelease.pdf

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