Memorandum

PLAINTIFF'S EXHIBIT 19

To: M. R. Greenberg

From: Frank H. Douglas

Date: 09/10/99

Re: Auto Warranty

Per your request, the attached report provides a recap of our warranty business since its inception.

You might want to review to Exhibit 1 to the attached note, which provides the actual results booked over the years for this business. Note the large amount of reinsurance and the extremely low net earned prior to 1997. For example, of the 93M of gross written in 1996 there was about only 7M net earned. This is because the premium earns very slowly and the net retention was low for this business. As the attached note highlights, we did not begin to develop any credible data until 1997. Additionally, the loss of the reinsurance essentially made all the exposure net.

Actuarial supported Evan's suggestion to hire a consulting actuary. The only consultant we felt could bring significant additional input to our review was Roger Hayne of Milliman & Robertson. We knew Hayne had done consulting work for many other writers of Auto Warranty business (including our reinsurer OPL) and that he therefore would be able to bring into his review all the data and rate making experience of his other clients. In actuarial circles he is considered the actuarial authority on Auto Warranty business. His report on our results suggests there will be an underwriting loss of close to 400M against our unearned premium reserve as of 12/31/98 of 244M. His projected loss ratio is about 265% and he said this is the worst he has ever seen other than one account he reviewed many years ago.

It appears to us that several of the assumptions made by Milliman & Robertson are conservative. For example, they are assuming an annual increase in loss costs of about 9% per year whereas their normal assumption is close to zero. Their assumption is based on our own data as provided by our administrators which indicates this high loss trend. It is our hope and the profit center's belief that this trend can be eliminated if not reversed by our implementation of good claims management control. As this underwriting loss is entirely in the future, it is clear that to the extent our poor results are driven by claim or administrator control problems significant improvement would be indeed be possible.

CC: E. G. Greenberg

American International Group

70 Pine Street New York, N.Y. 10270

To: Frank H. Douglas Date: September 10,1999

From: Jay Morrow

Re: **Auto Warranty**

DBG Division 16 started writing automobile warranty business as a separate Profit Center in 1993. There was one small MBI program written in Division 31 for many years prior to this. It was rolled into the new Profit Center at this time. The rates and earnings curves originally used were based on highly summarized data provided by the various administrators. There were two major judgemental adjustments that had to be made to this data in arriving at the rates and earnings curves: changes in the underlying manufacturers warranty period, and a significant increase in the amount of extended eligibility sales.

From March 1993 through April 1995 there was an 80% quota share with Lloyd's of London. From May 1995 through September of 1996 there was an 80% quota share with OPL. There are some problems with collectability on the Lloyds reinsurance and in early 1998 we agreed to provide OPL with a stop loss treaty at a 120% combined ratio because of the high level of loss and our historical business relationship. At this time, we also had to reverse premium erroneously ceded to OPL from October 1996 through October 1997.

The attached Exhibit I shows the calendar year results booked for this business. Exhibits II through V show the gross reported results by contract sale year as of 3/31/99 split between new and used VSC contracts and new and used MBI contracts. Keep in mind that VSC contracts have a zero commission while MBI has about a 50% commission. The earned premium is based on our current earning curves except for cancellations which are fully earned at the time of cancellation. The cancellation issue results in the reported loss ratio being lower than the expected ultimate loss ratio, especially for the latest couple of years.

This business was initially booked to around an 80% loss ratio based on the initial rating assumptions of the Profit Center. This allowed for a small IBNR reserve for the inherent processing delay. Other than this small IBNR, this business runs on a reported paid loss basis. In 1997, the reported loss ratio exceeded 80% and has continued upward ever since.

There was substantial effort by the Profit Center for several years to get data out of the administrators that could be used for analysis. This data was finally received late in 1997. The initial reports indicated the results were much worse than the initial 80% loss ratio assumption, but required more refined reports to drill down to the specific problems. As these reports were refined over the course of 1998, it was discovered that the biggest problem was the extended eligibility business. The other problem noted is that in each quarters update, the trend in both frequency and severity has been significantly higher than any reasonable assumption would have suggested. The current Milliman and Robertson draft report has extrapolated this trend into the future to arrive at very high ultimate loss ratios. It indicates a gross underwriting loss of about $400 million for the 12/31/98 UEPR. The attached report from Steve Gapp shows the detail of this projected loss by administrator.

Attachment

Exhibit I

New Hampshire Insurance Company
Domestic Warranty Group - Automobile
Annual Results - (000) Omitted

Calendar Year	Gross Written Premium	Net Written Premium	Net Earned Premium	Incurred Losses & LAE	Stat P&L	Incurred Loss & LAE Ratio	Expense Ratio	Combined Ratio
1994	45,402	8,829	1,412	1,078	334	76.3%	3.6%	80.0%
1995	51,187	9,604	3,375	2,807	568	83.2%	7.7%	90.8%
1996	93,112	20,187	7,365	5,653	1,712	76.8%	4.9%	81.6%
1997	160,633	97,089	23,311	24,454	-1,143	104.9%	-1.1%	103.8%
1998	176,443	206,497	83,310	103,446	-20,136	124.2%	3.6%	127.8%
1999-1	36,857	31,765	21,478	31,661	-10,183	147.4%	-9.0%	138.4%
1999-2	32,856	30,337	21,252	41,200	-19,948	193.9%	-30.9%	162.9%
Fisrt Six Months 1999	69,713	62,102	42,730	72,861	-30,131	170.5%	-19.7%	150.8%
Total	596,490	404,308	161,503	210,299	-48,796	130.2%	-0.9%	129.3%

Note net earned immaterial until 1997

New VSC Business For All TPAs by Sale Year
Data From NAT As of March 31, 1999

Exhibit II

Sale Year	Net Units Sold	Gross Written Premium	Earned Premium	Unearned Premium	Average Premium	Percent Premium Earned	Claim Count	Claims Paid	Net Frequency	Severity	Net Loss Cost	Earned Premium Loss Ratio
1991	1	390	390	0	390	100.00%	5	4,030	500%	806	4,030	1032%
1992	573	105,826	102,074	3,752	185	96.45%	140	59,818	25%	427	108	59%
1993	21,979	5,347,439	4,862,882	484,557	243	90.94%	14,918	6,155,120	75%	413	308	127%
1994	40,221	10,051,938	7,707,316	2,344,622	250	76.67%	30,224	12,552,608	98%	415	407	163%
1995	61,447	17,884,012	10,560,485	7,323,528	291	59.05%	45,125	19,969,087	124%	443	550	189%
1996	97,486	33,353,890	13,636,730	19,717,160	342	40.88%	60,232	28,747,229	151%	477	721	211%
1997	184,948	71,058,461	15,673,191	55,385,270	384	22.06%	62,198	30,202,116	152%	486	740	193%
1998	209,089	82,751,134	7,052,720	75,698,414	396	8.52%	18,105	7,948,267	102%	439	446	113%
1999	28,805	12,089,284	416,620	11,672,665	420	3.45%	97	32,110	10%	331	32	8%
Grand Total	644,549	232,642,375	60,012,408	172,629,967	361	25.80%	231,044	105,670,385	139%	457	636	176%

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Exhibit III

Used VSC Business For All TPAs by Sale Year
Data From NAT As of March 31, 1999

Sale Year	Net Units Sold	Gross Written Premium	Earned Premium	Unearned Premium	Average Premium	Percent Premium Earned	Claim Count	Claims Paid	Net Frequency	Severity	Net Loss Cost	Earned Premium Loss Ratio
1992	151	46,939	46,939	0	311	100.00%	13	5,597	9%	431	37	12%
1993	15,543	5,250,819	5,250,819	0	338	100.00%	8,454	4,456,539	54%	527	287	85%
1994	31,378	9,954,597	9,954,579	18	317	100.00%	18,611	9,349,090	59%	502	298	94%
1995	51,953	19,135,996	19,058,976	77,019	368	99.60%	40,313	20,545,245	78%	510	397	108%
1996	89,770	37,289,853	35,460,228	1,829,625	415	95.09%	70,969	41,148,898	83%	580	482	116%
1997	166,429	72,564,100	56,604,083	15,960,017	436	78.01%	109,368	66,647,255	84%	609	513	118%
1998	171,199	76,373,939	27,348,287	49,025,652	446	35.81%	59,315	36,020,716	97%	607	588	132%
1999	23,148	10,629,066	277,490	10,351,577	459	2.61%	897	524,176	148%	584	867	189%
Grand Total	549,571	231,245,309	154,001,400	77,243,909	421	66.60%	307,940	178,697,515	84%	580	488	116%

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Exhibit IV

New MBI Business For All TPAs by Sale Year

Data From NAT As of March 31, 1999

Sale Year	Net Units Sold	Gross Written Premium	Earned Premium	Unearned Premium	Average Premium	Percent Premium Earned	Claim Count	Claims Paid	Net Frequency	Severity	Net Loss Cost	Earned Premium Loss Ratio
1985	2,335	618,697	618,697	0	132	100.00%	1,254	404,366	54%	322	173	65%
1986	5,170	1,474,877	1,474,877	0	143	100.00%	2,936	1,028,963	57%	350	199	70%
1987	6,238	1,832,758	1,832,758	0	147	100.00%	3,286	908,353	53%	276	146	50%
1988	10,783	3,053,334	3,053,334	0	142	100.00%	7,580	1,906,541	70%	252	177	62%
1989	8,707	2,754,977	2,754,977	0	158	100.00%	7,085	2,003,398	81%	283	230	73%
1990	11,500	4,182,611	4,182,611	0	182	100.00%	10,718	3,780,149	93%	353	329	90%
1991	7,985	3,211,342	3,211,342	0	201	100.00%	7,684	3,162,868	96%	412	396	98%
1992	6,231	2,875,982	2,874,742	1,240	231	99.96%	7,688	3,546,475	123%	461	569	123%
1993	12,092	5,445,225	4,906,324	538,902	225	90.10%	13,280	6,276,022	122%	473	576	128%
1994	18,333	8,249,703	5,454,263	2,795,440	225	66.11%	15,901	7,194,571	131%	452	594	132%
1995	18,576	8,502,000	3,564,165	4,937,835	229	41.92%	11,486	5,291,996	147%	461	680	148%
1996	21,230	12,505,974	2,472,817	10,033,157	295	19.77%	10,114	3,995,683	241%	395	952	162%
1997	24,417	15,517,563	883,643	14,633,919	318	5.69%	6,177	2,299,768	444%	372	1,654	260%
1998	18,312	11,439,551	109,345	11,330,206	312	0.96%	1,079	513,898	616%	476	2,936	470%
1999	391	299,341	29	299,313	383	0.01%	1	203	2685%	203	5,442	711%
Grand Total	172,300	81,963,934	37,393,923	44,570,011	476	45.62%	106,269	42,313,253	135%	398	538	113%

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Used MBI Business For All TPAs by Sale Year

Data From NAT As of March 31, 1999

Exhibit II

Sale Year	Net Units Sold	Gross Written Premium	Earned Premium	Unearned Premium	Average Premium	Percent Premium Earned	Claim Count	Claims Paid	Net Frequency	Severity	Net Loss Cost	Earned Premium Loss Ratio
1985	157	40,474	40,474	0	129	100.00%	45	16,188	29%	360	103	40%
1986	788	222,520	222,520	0	141	100.00%	251	85,510	32%	341	109	38%
1987	913	347,742	347,742	0	190	100.00%	253	105,183	28%	416	115	30%
1988	1,112	513,039	513,039	0	231	100.00%	371	139,785	33%	377	126	27%
1989	984	451,922	451,922	0	230	100.00%	358	138,647	36%	387	141	31%
1990	1,187	558,354	558,354	0	235	100.00%	546	210,495	46%	386	177	38%
1991	1,047	504,091	504,091	0	241	100.00%	455	170,636	43%	375	163	34%
1992	1,012	500,720	500,720	0	247	100.00%	472	184,646	47%	391	182	37%
1993	2,759	1,353,124	1,353,124	0	245	100.00%	1,619	744,990	59%	460	270	55%
1994	5,093	2,470,135	2,466,926	3,209	243	99.87%	3,324	1,703,131	65%	512	335	69%
1995	5,347	2,692,371	2,682,779	9,591	252	99.64%	4,063	2,275,987	76%	560	427	85%
1996	9,608	6,661,391	6,438,843	222,548	347	96.66%	15,782	5,484,715	170%	348	591	85%
1997	12,599	9,385,064	7,339,772	2,045,292	372	78.21%	16,838	5,516,978	171%	328	560	75%
1998	10,109	7,187,094	3,009,142	4,177,952	355	41.87%	3,978	2,328,086	94%	585	550	77%
1999	131	112,824	1,848	110,975	431	1.64%	11	6,709	513%	610	3,126	363%
Grand Total	52,846	33,000,863	26,431,295	6,569,568	624	80.09%	48,366	19,111,687	114%	395	452	72%

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