**EXHIBIT M**

**HARTFORD CASE DOCUMENTS**

SUPREME COURT OF THE STATE OF NEW YORK
COUNTY OF NEW YORK

TWIN CITY FIRE INSURANCE COMPANY, HARTFORD INSURANCE COMPANY OF ILLINOIS, HARTFORD INSURANCE COMPANY OF THE MIDWEST, TRUMBULL INSURANCE COMPANY, HARTFORD INSURANCE COMPANY OF THE SOUTHEAST, NUTMEG INSURANCE COMPANY, PROPERTY AND CASUALTY INSURANCE COMPANY OF HARTFORD, HARTFORD FIRE INSURANCE COMPANY, HARTFORD CASUALTY INSURANCE COMPANY, HARTFORD ACCIDENT AND INDEMNITY INSURANCE COMPANY, HARTFORD UNDERWRITERS INSURANCE COMPANY, PACIFIC INSURANCE COMPANY, LIMITED, THE HARTFORD FINANCIAL SERVICES GROUP, INC.,

Plaintiffs,

-against-

ARCH INSURANCE GROUP, INC., ARCH CAPITAL GROUP LTD., DAVID McELROY, JOHN RAFFERTY and MICHAEL PRICE,

Defendants.

Index No. 09/602062

Plaintiff designates New York County as the place of trial.

**SUMMONS**

The basis of venue is CPLR § 503(a), (c).



*TO:* ***ARCH INSURANCE GROUP, INC.***
***One Liberty Plaza***
***New York, New York***

You are hereby summoned and required to serve upon Plaintiffs' attorney an Answer to the Complaint in this action within twenty (20) days after the service of this Summons, exclusive of the day of service, or within thirty (30) days after service is complete if this Summons is not personally delivered to you within the State of New York. In case of your failure to answer, judgment will be taken against you by default for the relief demanded in the Complaint.

Dated: New York, New York
July 2, 2009

DEWEY PEGNO & KRAMARSKY LLP

By _____

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Stephen M. Kramarsky
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*Attorneys for Plaintiffs*

SUPREME COURT OF THE STATE OF NEW YORK
COUNTY OF NEW YORK

TWIN CITY FIRE INSURANCE COMPANY, HARTFORD INSURANCE COMPANY OF ILLINOIS, HARTFORD INSURANCE COMPANY OF THE MIDWEST, TRUMBULL INSURANCE COMPANY, HARTFORD INSURANCE COMPANY OF THE SOUTHEAST, NUTMEG INSURANCE COMPANY, PROPERTY AND CASUALTY INSURANCE COMPANY OF HARTFORD, HARTFORD FIRE INSURANCE COMPANY, HARTFORD CASUALTY INSURANCE COMPANY, HARTFORD ACCIDENT AND INDEMNITY INSURANCE COMPANY, HARTFORD UNDERWRITERS INSURANCE COMPANY, PACIFIC INSURANCE COMPANY, LIMITED, and THE HARTFORD FINANCIAL SERVICES GROUP, INC.

Plaintiffs,

-against-

ARCH INSURANCE GROUP, INC., ARCH CAPITAL GROUP LTD., DAVID McELROY, JOHN RAFFERTY and MICHAEL PRICE,

Defendants.

Index No. 09/602062

**COMPLAINT**
**JURY TRIAL DEMANDED**



Twin City Fire Insurance Company, Hartford Insurance Company of Illinois, Hartford Insurance Company of the Midwest, Trumbull Insurance Company, Hartford Insurance Company of the Southeast, Nutmeg Insurance Company, Property and Casualty Insurance Company of Hartford, Hartford Fire Insurance Company, Hartford Casualty Insurance Company, Hartford Accident and Indemnity Company, Hartford Underwriters Insurance Company, Pacific Insurance Company, Limited, and The Hartford Financial Services Group, Inc. (collectively

"The Hartford"), by their attorneys, Dewey, Pegno & Kramarsky LLP, as and for their Complaint allege, upon knowledge as to their own actions and upon information and belief as to the actions of others, as follows:

## Preliminary Statement

1. The Hartford brings this action to address egregious, ongoing misconduct orchestrated by a competitor and several former senior executives of The Hartford's Financial Products division.

2. On Monday June 1, 2009, David McElroy—a Senior Vice President of The Hartford and President of its Hartford Financial Products division ("HFP")—announced his "retirement," receiving a large compensation package from The Hartford. He "retired" from the company effective Friday, June 5, 2009.

3. McElroy's "retirement" was short-lived: on Monday, June 8, 2009, Defendants Arch Insurance Group, Inc. and Arch Capital Group Ltd. (collectively "Arch") announced that McElroy had joined Arch. Shortly thereafter, Arch announced that McElroy would head a new division of Arch—a new division evidently created to service the business that Arch and McElroy intended to steal from The Hartford by any necessary means.

4. What quickly followed was an unlawful corporate "raid" of unprecedented proportions, characterized by threats, bullying and repeated disparagement of The Hartford to employees, clients and other business partners. Plaintiffs have overcome the effects of this misconduct at great cost, and only through the hard work, perseverance and resourcefulness of remaining HFP personnel.

5. Since June 8, 2009, more than 60 HFP employees, including several of its most senior executives and the vast majority of its underwriting staff, have resigned and accepted employment with Arch.

6. Arch executives and employees have bombarded current HFP employees with threatening and bullying emails, telephone calls and text messages falsely stating, in words or in effect, among other things, that HFP is a "sinking ship"; that HFP employees better "jump ship" fast; that "[t]here isn't going to be an HFP anymore"; and that HFP employees "better come to Arch" or they "will never work in this industry again".

7. Further, unsatisfied with bullying scores of HFP employees into resigning, Arch has endeavored to destroy HFP's business and its ability to compete: for example, Arch has solicited virtually *all* HFP underwriting employees—even those who are currently still being trained.

8. Arch has also aggressively recruited HFP Information Technology employees in an effort to interfere with HFP's daily technology operations, and potentially to steal technological information from HFP.

9. Nor was the timing of the raid coincidental. Reinsurance of HFP's insurance obligations is an integral component of HFP's underwriting operations. The resignations of McElroy and other HFP executives were orchestrated to occur during a significant period—the period during which HFP renegotiates its reinsurance contracts with reinsurers.

10. This egregious conduct makes a mockery of Arch's Code of Business Conduct, which purports to set a high ethical bar for Arch employees. "It is the responsibility of each [Arch] Employee to conduct himself or herself in a manner that will support and maintain the Company's reputation for fairness and a high level of integrity. . . . In every case, an Employee

should ask himself or herself if the conduct being contemplated would comply with Company policies and would withstand public disclosure and scrutiny." In this case, it plainly does not.

11. Moreover, despite its purported commitment to "integrity", Arch's conduct in fact appears to be business as usual: In late 2007, a Connecticut court found that Arch had raided a reinsurance division of General Reinsurance Corporation ("Gen Re"), agreeing with Gen Re that "the individual defendants plotted to move a substantial portion of GPF's business to Arch along with GPF personnel, trade secrets, proprietary information and business plan . . . and are . . . planning to use these assets to unfairly create and operate out of whole cloth a business to competitive to Gen Re's GPF division."

12. Although The Hartford has effectively managed and contained the damage from Defendants' onslaught, such egregious behavior cannot go unchecked. The Hartford accordingly brings this action to enjoin Defendants' unlawful conduct and to recover the damages caused by that conduct.

**The Parties, Jurisdiction and Venue**

13. Plaintiff The Hartford Financial Services Group, Inc. ("HFSG"), one of the nation's leading financial services companies, is organized under the laws of the State of Delaware with its principal place of business at One Hartford Plaza, Hartford, Connecticut. The subsidiaries of HFSG, including as set forth below, operate collectively under the trade name "The Hartford" and are engaged in the business of selling investment and insurance products to their clients.

14. Plaintiff Twin City Fire Insurance Company, a direct or indirect subsidiary of HFSG, is a company organized under the laws of the State of Indiana, with its primary place of business in Connecticut.

15. Plaintiff Hartford Insurance Company of Illinois, a direct or indirect subsidiary of HFSG, is a company organized under the laws of the State of Illinois, with its primary place of business in Connecticut.

16. Plaintiff Hartford Insurance Company of the Midwest, a direct or indirect subsidiary of HFSG, is a company organized under the laws of the State of Indiana, with its primary place of business in Connecticut.

17. Plaintiff Trumbull Insurance Company, a direct or indirect subsidiary of HFSG, is a company organized under the laws of the State of Connecticut, with its primary place of business in Connecticut.

18. Plaintiff Hartford Insurance Company of the Southeast, a direct or indirect subsidiary of HFSG, is a company organized under the laws of the State of Connecticut, with its primary place of business in Connecticut.

19. Plaintiff Nutmeg Insurance Company, a direct or indirect subsidiary of HFSG, is a company organized under the laws of the State of Connecticut, with its primary place of business in Connecticut.

20. Plaintiff Property and Casualty Insurance Company of Hartford, a direct or indirect subsidiary of HFSG, is a company organized under the laws of the State of Indiana, with its primary place of business in Connecticut.

21. Plaintiff Hartford Fire Insurance Company, a direct or indirect subsidiary of HFSG, is a company organized under the laws of the State of Connecticut, with its primary place of business in Connecticut.

22. Plaintiff Casualty Insurance Company, a direct or indirect subsidiary of HFSG, is a company organized under the laws of the State of Indiana, with its primary place of business in Connecticut.

23. Plaintiff Accident & Indemnity Company, a direct or indirect subsidiary of HFSG, is a company organized under the laws of the State of Connecticut, with its primary place of business in Connecticut.

24. Plaintiff Hartford Underwriters Insurance Company, a direct or indirect subsidiary of HFSG, is a company organized under the laws of the State of Connecticut, with its primary place of business in Connecticut.

25. Plaintiff Pacific Insurance Company Limited, a subsidiary of HFSG, is a company organized under the laws of the State of Connecticut, with its primary place of business in Connecticut.

26. Defendant Arch Capital Group, Ltd. is a Bermuda public limited liability company that writes insurance and reinsurance on a worldwide basis through operations in Bermuda, the United States, Europe and Canada. Its principal place of business is Wessex House, 45 Reid Street, Hamilton, Bermuda.

27. Defendant Arch Insurance Group, Inc., a corporation organized under the laws of the State of Delaware, is a subsidiary of Arch Capital Group, Ltd. Arch Insurance Group writes insurance and reinsurance to North American clients. Its principal place of business is One Liberty Plaza, New York, New York.

28. Defendant David McElroy is a resident of the State of Connecticut. McElroy was employed as the Senior Vice President of Plaintiffs Hartford Casualty Insurance Company, Hartford Insurance Company of Illinois, Hartford Insurance Company of the Midwest, Hartford

Insurance Company of the Southeast, Nutmeg Insurance Company and Twin City Fire Insurance, and President of HFP from September 2000 to June 5, 2009. McElroy worked in HFP's headquarters in New York, New York.

29. Defendant John Rafferty is a resident of the State of Illinois. Rafferty was an officer of Plaintiffs Nutmeg Insurance Company and Twin City Fire Insurance Company, and Vice President of HFP until June 9, 2009. Rafferty traveled frequently to HFP's New York headquarters.

30. Defendant Michael Price is a resident of the State of New Jersey. Price was a Vice President of HFP until June 10, 2009. Price worked in HFP's headquarters in New York.

31. Jurisdiction and venue in this Court are proper because Arch Insurance Group, Inc. is a resident of New York, HFP is headquartered in New York, all the defendants transacted business in New York, and the acts and omissions at issue occurred in New York.

## Background

### *McElroy's Employment at The Hartford*

32. HFP makes The Hartford one of the largest providers of Directors and Officers, Employment Practices, Liability, Errors and Omissions, and crime insurance in the nation.

33. In September 2000, The Hartford purchased the business that became HFP from Reliance Group Holdings. This business, at the time of The Hartford's purchase, had approximately $295 million in premiums in force; as of December 2008, HFP's business had more than doubled, and it had approximately $720 million in premiums in force.

34. When the Hartford purchased the business, it purchased the books and records of the business, including marketing materials, rating and pricing information and materials, policyholder lists, policy forms, and underwriting files. The foregoing constitute valuable trade

secrets and intellectual property for which The Hartford paid a substantial premium. Hartford's purchase also included in-force, new and renewal business.

35. In connection with this transaction, McElroy was hired by The Hartford as Senior Vice President, and was appointed President of the HFP division.

36. Rafferty and Price were also hired and appointed Vice Presidents of HFP.

37. In those roles, McElroy, Rafferty and Price (the "Individual Defendants") held positions of trust: they were privy to substantial confidential, proprietary and trade secret information belonging to The Hartford, including (for example) the names and contact information of brokers and clients; strategies to develop and expand HFP's customer base; unique features and advantages of HFP's insurance products, including insurance forms and marketing documents; and information about the needs and preferences of HFP clients, including the renewal schedules for those clients.

38. In addition to substantial monetary compensation, The Hartford provided the Individual Defendants with ongoing training; paid for and sponsored their industry registrations; reimbursed them for travel and entertainment expenses associated with business development; and expended considerable resources developing the clients they serviced, as well as the products they sold.

39. Indeed, The Hartford paid for Price to receive a master's degree from New York University. The Hartford provided McElroy, Rafferty and Price with benefits, systems, resources and support at all times throughout their employment.

40. Through these efforts, The Hartford was able to build HFP into a very robust business. Although many of McElroy's colleagues also joined The Hartford from Reliance, the vast majority of HFP's staff was built at The Hartford.

41. Moreover, many new clients and client contacts were developed at The Hartford. Since 2000, several new insurance products were developed, and all of HFP's products have been substantially rewritten and re-filed with the relevant state authorities using the resources of The Hartford.

42. McElroy has acknowledged publicly that The Hartford's unique position and reputation created significant growth for HFP. As he stated in a 2001 interview, "Thanks to [The Hartford's] financial strength and strong reputation, we're seeing more and better opportunities."

***Defendants' Contractual Commitments to The Hartford***

43. While employed at The Hartford, McElroy signed two Employee Confidentiality and Work Product Ownership Agreements (the "Confidentiality Agreements"), one in 2000 and one in 2001. Both contain identical provisions concerning the use of confidential information belonging to The Hartford.

44. Price also signed a Confidentiality Agreement in 2003 that contained identical provisions regarding the use of confidential information belonging to The Hartford.

45. The Confidentiality Agreements provide, among other things, that McElroy and Price would

> keep in the strictest confidence and not disclose to persons outside of The Hartford (i) all information that is confidential to and/or a trade secret of The Hartford, that I may learn about, develop or otherwise gain access to by any means, in connection with or as a result of my employment with The Hartford, and (ii) all information with which I come in contact during my employment with The Hartford that under the circumstances should be treated as confidential, because it is information that is not generally known outside of The Hartford and is of significant value to The Hartford ("Confidential Information") . . . .

The Confidentiality Agreements further provide that:

> At the termination of my employment, I will make a diligent search for and immediately return all Confidential Information in

> my possession to The Hartford without any demand therefor, including, but not limited to, original versions and copies of all such information, and written notes or other materials from which Confidential Information could be reproduced.

46. McElroy and Price also agreed that they would assign to The Hartford "all inventions, designs, developments, patents, copyrights, trademarks and service marks ('Work Product')" developed while employed at The Hartford, as well as any "Work Product" developed within six months after the termination of their employment.

47. In the Confidentiality Agreements, McElroy and Price also agreed that "in the event of litigation between The Hartford and me concerning an alleged violation of this Agreement, I agree that I will pay The Hartford's reasonable attorneys' fees, costs and expenses associated with such litigation, if a court with jurisdiction over the litigation finds that I have violated the agreement."

48. Further, the Hartford's Code of Ethics and Business Conduct (the "Code of Ethics") also contained relevant restrictions on the use of The Hartford's information. Every employee, including the Individual Defendants, annually certified that he or she had reviewed and agreed to abide by the Code of Ethics, and such certification was a condition to continued employment at The Hartford.

49. The Code of Ethics provided that employees "have a responsibility to use and disclose information assets only as necessary to perform their job-related duties." It also provided that "Employees leaving the Company, voluntarily or otherwise, are prohibited from removing, copying or disclosing any Company or customer information, in whatever form, that is proprietary or confidential."

***McElroy and Arch Conspire to Gut HFP***

50. Despite the considerable growth of the HFP business and The Hartford's commitment to that division, starting in at least March 2009, McElroy met and spoke with Arch representatives about leaving The Hartford and taking the entire HFP business with him.

51. McElroy and Arch were well aware that the hiring of McElroy alone would not be sufficient to develop the specialty products business that both envisioned at Arch—a business they both wanted, but for which Arch was unwilling to pay. To develop such a division would require that the *entire* business—its major employees, its relationships, its information and its contracts—be moved from The Hartford. As McElroy himself acknowledged, when speaking about HFP, "this is a very tough business to start from scratch. You need critical mass."

52. So, upon information and belief, McElroy and Arch developed a plan that allowed Arch to grow a new business without having to "build it from scratch"—and without ever paying for it.

53. McElroy and Arch further determined that they also would destroy The Hartford's business by attempting to strip away HFP's personnel at all levels, dissuading clients from renewing their contracts with HFP, and attempting to undermine the reinsurance contracts that are integral to HFP's business.

54. Arch agreed to hire McElroy, offering significant sums of money for McElroy's expertise and his promise to move the entire HFP business to Arch. Both Arch and McElroy knew that McElroy would, in violation of his Confidentiality Agreements and the Code of Ethics, bring with him to Arch and use for Arch's benefit, confidential, proprietary and trade secret information belonging to The Hartford, including but not limited to the names and contact information of The Hartford's clients and the brokers servicing those clients, confidential

information concerning HFP's internal structure and personnel, and information about the insurance needs of HFP's clients and the products they bought.

55. Moreover, as another element of their plan to destroy The Hartford's HFP business by improper means, Arch and McElroy timed McElroy's resignation, and their plan to lure away scores of other HFP employees, to coincide with the time when HFP needed to renegotiate its reinsurance agreements: these departures were calculated by Arch and McElroy to leave The Hartford with no employee sufficiently senior to negotiate these critical agreements. Arch intended, and upon information and belief still intends, to leverage that position in an effort to prevent HFP from securing reinsurance commitments.

***The Events of June 2009***

56. On June 1, 2009, a Monday, McElroy announced to The Hartford that he was "retiring", and would be leaving the company as of that Friday, June, 5, less than a month before HFP had to renegotiate and finalize its reinsurance contracts.

57. McElroy's "retirement" permitted him to collect a large compensation package.

58. Despite his purported "retirement", on June 3, 2009—before McElroy had even left HFP—Arch announced on its trading floor that McElroy would be joining Arch.

59. McElroy started at Arch on June 8, 2009, the Monday following his "retirement" from HFP.

60. The very next day, June 9, 2009, Rafferty tendered his resignation from HFP. On June 10, 2009, Price resigned.

61. A week after McElroy started at Arch, Arch announced that it was forming a new division called the Financial and Professional Liability group, headed by McElroy—a move that evidently had been planned for some time. Arch stated that it was starting its new business to

"maximize underwriting opportunities as the market transitions"; in other words, it specifically designed its operation to take on business that would become available if it was able to execute its plan to destroy HFP. Rafferty was named head of the "Executive Assurance" division of Arch's new group, reporting directly to McElroy, the same role he had had at The Hartford.

62. Starting the week after the Individual Defendants began working at Arch, scores of HFP employees began defecting to Arch.

63. In a particularly brazen tactic, Arch began soliciting HFP employees with emails sent directly to their email addresses at The Hartford.

64. Determined to steal the entire HFP business, Defendants resorted to bullying and threats to ensure that their plans to eviscerate HFP were successful. HFP employees were told, in words or in effect, by Arch employees, including Price, that they should move to Arch or "they would never work in this industry again"; if they did not move immediately, they were told, the job offer would no longer be available.

65. Arch continued to frighten HFP employees into resigning, making phone calls to HFP employees, and sending text messages directly to HFP employees' cell phones falsely stating, in words or in effect, that "HFP is sinking fast" and telling the employees "they better jump" and also stating, falsely, that "Arch is buying HFP's book." At least one employee was told falsely that "there isn't going to be an HFP anymore."

66. In addition, Arch was actually willing to take on *redundant* costs simply to execute McElroy's vendetta against his former employer. For example, guided by McElroy, Arch aggressively solicited and extended offers to underwriting employees from the most senior, to junior underwriters and underwriting trainees. The *only* purpose of this aggressive

solicitation, given Arch's lack of a need for these services, was to attempt to cause harm and disruption within HFP.

67. Arch also aggressively solicited HFP Information Technology employees in an effort to hire away the few individuals trained to maintain and service HFP's technology systems.

68. As of today, more than 60 of HFP's 250 employees, including significant numbers of senior employees, and the vast majority of the underwriting staff who were employed as of June 8, 2009, have resigned and accepted employment with Arch. Plaintiffs have overcome these losses at great cost, and only through the hard work, perseverance and resourcefulness of their remaining personnel.

***Arch's Attempts to Undermine HFP***

69. Arch's and McElroy's efforts, however, did not stop with HFP employees. Arch employees had conversations with at least one insurance broker, advising that broker, upon information and belief, that The Hartford was crippled and would not be able to effectively service his business; the solution, the broker was told, was to transition the business to Arch. Upon information and belief, Arch employees had similar conversations with other brokers and clients of The Hartford.

70. Arch also attempted to undermine HFP's ability to enter into reinsurance contracts, which HFP was preparing to renegotiate when the Individual Defendants—and scores of other former HFP employees—resigned to go to Arch. As Defendants are well aware, reinsurance is an integral part of HFP's underwriting operations. None of the Defendants stands to gain anything from undermining HFP's ability to reinsure its commitments.

## COUNT ONE
## BREACH OF FIDUCIARY DUTY (against the Individual Defendants)

71. Plaintiffs repeat and reallege Paragraphs 1-70 as if fully set forth herein.

72. The Individual Defendants were senior employees of The Hartford in whom The Hartford reposed significant and unique trust.

73. The Individual Defendants owed The Hartford a fiduciary duty not to act in any manner inconsistent with their employment and to exercise good faith and loyalty in performing their duties.

74. The Individual Defendants breached their fiduciary duties to The Hartford in numerous ways, including but not limited to by: taking confidential and proprietary information from The Hartford and providing it to Arch; utilizing the confidential and proprietary information of The Hartford to aid Arch in its efforts to solicit and recruit employees of The Hartford; planning with Arch to solicit employees and clients of The Hartford; planning to move and moving an entire business from The Hartford to Arch without Arch paying for the business; planning to gut the HFP business by attempting to persuade clients not to renew their contracts with HFP; and undermining the reinsurance contracts that are an integral part of HFP's business.

75. These breaches caused damage to Plaintiffs amounting to millions of dollars, plus related transaction costs, interest and fees.

## COUNT TWO
## AIDING AND ABETTING BREACH OF FIDUCIARY DUTY (against Arch)

76. Plaintiffs repeat and reallege Paragraphs 1-75 as if fully set forth herein.

77. The Individual Defendants had a fiduciary duty to The Hartford, which they breached as set forth above in Paragraphs 71 through 75.

78. Defendant Arch knew that the Individual Defendants were senior employees of The Hartford in which The Hartford reposed significant and unique trust, and thus that they owed The Hartford fiduciary duties.

79. Despite this knowledge, Arch knowingly and substantially assisted and induced the Individual Defendants' breaches of their fiduciary duty by:

a. providing a substantial payment to McElroy for agreeing to bring the HFP business, including all HFP senior employees as well as HFP underwriting employees, to Arch;

b. planning with McElroy to move and attempting to move an entire business from The Hartford to Arch without paying for the business;

c. providing a substantial payment to McElroy, Rafferty and Price for providing Arch with The Hartford's confidential, proprietary and trade secret information;

d. planning with McElroy, Rafferty and Price to sabotage the HFP business by undermining the reinsurance contracts that are an integral part of HFP's business.

80. Arch has knowingly and substantially profited from the Individual Defendants' breach.

81. These breaches caused damage to Plaintiffs amounting to millions of dollars, plus related transaction costs, interest and fees.

## COUNT THREE
## BREACH OF CONTRACT
**(against McElroy and Price for breach of the Confidentiality Agreements)**

82. Plaintiffs repeat and reallege Paragraphs 1-81 as if fully set forth herein.

83. The Confidentiality Agreements are valid and enforceable contracts.

84. The Confidentiality Agreements provided, among other things, that McElroy and Price would

> keep in the strictest confidence and not disclose to persons outside of The Hartford (i) all information that is confidential to and/or a trade secret of The Hartford, that I may learn about, develop or otherwise gain access to by any means, in connection with or as a result of my employment with The Hartford, and (ii) all information with which I come in contact during my employment with The Hartford that under the circumstances should be treated as confidential, because it is information that is not generally known outside of The Hartford and is of significant value to The Hartford ("Confidential Information") . . . .

The Confidentiality Agreements further provided that:

> At the termination of my employment, I will make a diligent search for and immediately return all Confidential Information in my possession to The Hartford without any demand therefor, including, but not limited to, original versions and copies of all such information, and written notes or other materials from which Confidential Information could be reproduced."

85. In the Confidentiality Agreements, McElroy and Price also agreed to assign to The Hartford "all inventions, designs, developments, patents, copyrights, trademarks and service marks ('Work Product')" developed while employed at the Hartford, as well as any "Work Product" developed within six months of the termination of their employment.

86. The Hartford substantially performed its duties and obligations under the Confidentiality Agreements.

87. McElroy and Price breached their obligations under the Confidentiality Agreements by, upon information and belief, (a) utilizing The Hartford's confidential, proprietary and trade secret information for purposes contrary to the interests of The Hartford, including the solicitation of employees and clients and the planning of a raid on HFP, while still employed by The Hartford; and (b) bringing with them to Arch and using for Arch's benefit

confidential, proprietary and trade secret information belonging to The Hartford, including but not limited to the names and contact information for The Hartford's clients and the brokers servicing those clients, and information about the insurance needs of The Hartford's clients, as well as other confidential information relating to the internal structure, operations and products of The Hartford and HFP.

88. McElroy's and Price's breaches were neither justified nor excused.

89. These breaches caused damage to Plaintiffs amounting to millions of dollars, plus related transaction costs, interest and fees.

**COUNT FOUR**
**BREACH OF CONTRACT**
**(against the Individual Defendants for breach of the Code of Ethics)**

90. Plaintiffs repeat and reallege Paragraphs 1-89 as if fully set forth herein.

91. The Code of Ethics was part of the Individual Defendants' valid and enforceable employment contracts.

92. The Code of Ethics provided that The Hartford employees "have a responsibility to use and disclose information assets only as necessary to perform their job-related duties." It also provided that "Employees leaving the Company, voluntarily or otherwise, are prohibited from removing, copying or disclosing any Company or customer information, in whatever form, that is proprietary or confidential."

93. The Hartford substantially performed it duties and obligations under its employment contracts with the Individual Defendants.

94. The Individual Defendants breached their obligations under the Code of Ethics as set forth in Paragraph 87 above.

95. The Individual Defendants' breaches were neither justified nor excused.

96. These breaches caused damage to Plaintiffs amounting to millions of dollars, plus related transaction costs, interest and fees.

## COUNT FIVE
## TORTIOUS INTERFERENCE WITH CONTRACT (against Arch)

97. Plaintiffs repeat and reallege Paragraphs 1-96 as if fully set forth herein.

98. The Confidentiality Agreements McElroy and Price had with The Hartford were and are valid and enforceable contracts.

99. Arch knew of the existence and terms of these agreements.

100. Arch has knowingly, intentionally, improperly, tortiously and in bad faith caused or aided McElroy's and Price's breaches of the Confidentiality Agreements set forth above in Paragraph 87, or otherwise knowingly, intentionally, improperly, tortiously and in bad faith procured or induced such breaches of agreements by McElroy.

101. McElroy and Price have in fact breached the Confidentiality Agreements as set out above, and Plaintiffs have thereby been damaged by such breaches.

102. Arch has undertaken the tortious conduct set out herein and secured or induced breaches of McElroy's and Price's Confidentiality Agreements without claim of right or privilege, and has substantially profited thereby.

103. Defendants' tortious interference with McElroy's and Price's Confidentiality Agreements has caused damage to Plaintiffs amounting to million of dollars, plus related transaction costs, interests and fees.

## COUNT SIX
## TORTIOUS INTERFERENCE WITH PROSPECTIVE CONTRACT
## (against all Defendants)

104. Plaintiffs repeat and reallege Paragraphs 1-103 as if fully set forth herein.

105. McElroy, Rafferty and Price, as former employees of The Hartford, and Arch, both through the Individual Defendants and as another entity in the insurance business, knew of The Hartford's relationships with clients.

106. Defendants deliberately and without legitimate business justification, for the sole purpose of harming The Hartford, interfered with these relationships in an attempt to ensure that HFP would be unable to service its clients.

107. Defendants interfered with these business relationships in a wrongful manner, including but not limited to by making threats and/or defamatory and disparaging comments about The Hartford to brokers who service clients of The Hartford and to clients of The Hartford whose contracts need to be or will need to be renewed.

108. Clients would have renewed their insurance contracts but for Defendants' interference.

109. Defendants' tortious interference has caused damage to Plaintiffs amounting to million of dollars, plus related transaction costs, interests and fees.

**COUNT SEVEN**
**RAIDING/UNFAIR COMPETITION (against Arch)**

110. Plaintiffs repeat and reallege Paragraphs 1-109 as if fully set forth herein.

111. Upon information and belief, Arch used dishonest and unfair means to gain access to confidential, proprietary trade secret information belonging to The Hartford, including but not limited to information about The Hartford's clients and their insurance needs and preferences and the internal structure and operations of The Hartford's business.

112. Arch then used that confidential and proprietary information and trade secrets, including information about Plaintiffs' corporate structure and its clients and, through dishonest

and unfair means, including but not limited to threats, bullying, and the employment of a strategy designed to decimate HFP's business, Arch lured away scores of employees of The Hartford.

113. To date, in an effort to keep The Hartford from servicing its clients, Arch has lured away a significant percentage of the HFP employees by headcount, including many of its senior employees and virtually all underwriting employees at all levels. Arch also attempted to lure away HFP Information Technology staff in an effort to interfere with HFP's daily operations.

114. Arch had no business justification for its actions, and Arch's actions were done in bad faith and with the intent to harm Plaintiffs.

115. The Hartford has suffered damages as a result of the unfair competition by Arch amounting to millions of dollars, plus related transaction costs, interest and fees.

**COUNT EIGHT**
**UNJUST ENRICHMENT (against Arch)**

116. Plaintiffs repeat and reallege Paragraphs 1-115 as if fully set forth herein.

117. Arch was enriched by its misappropriation and use of The Hartford's confidential, proprietary and trade secret information including but not limited to the names and contact information of The Hartford's clients and the brokers servicing those clients, confidential information related to HFP's internal structure and personnel, and information about the insurance needs of HFP's clients and the products they bought.

118. This information was obtained improperly and at The Hartford's expense.

119. Equity and good conscience militate against permitting Arch to retain the benefits of the confidential, proprietary and trade secret information belonging to The Hartford.

## COUNT NINE
## MISAPPROPRIATION OF TRADE SECRETS (against all Defendants)

120. Plaintiffs repeat and reallege Paragraphs 1-119 as if fully set forth herein.

121. As set forth above in Paragraphs 37 and 87, Plaintiffs' client lists, including the names and contact information of The Hartford's clients and the brokers servicing those clients, confidential information concerning HFP's internal structure and personnel, and information about the insurance needs of HFP's clients and the products they bought constitute valuable trade secrets of Plaintiffs' not generally known in the industry or otherwise.

122. Defendants have breached their common law and contractual obligations by misappropriating Plaintiffs' trade secrets for their own use and disclosing those trade secrets to others.

123. As a result of Defendants' misappropriation of Plaintiffs' trade secrets, Plaintiffs have sustained, and expect to continue to sustain, substantial financial harm amounting to millions of dollars, plus related transaction costs, interest and fees.

## PRAYER FOR RELIEF

Wherefore, Plaintiffs pray for relief and judgment as follows:

A. Ordering Defendants McElroy, Rafferty, and Price to return to The Hartford all compensation earned during the period of or in connection with their disloyalty to The Hartford;

B. Ordering Defendants McElroy and Price to disclose and assign to The Hartford all "Work Product" created since their resignation from The Hartford, as called for by the Confidentiality Agreements;

C. Awarding compensatory damages in favor of Plaintiffs for all damages sustained as a result of Defendants' wrongdoing, in an amount to be proven at trial, but in no event less than many millions of dollars plus related transaction costs, interest, fees and litigation costs;

D. Immediately and permanently enjoining Defendants' use of Plaintiffs' confidential, proprietary and trade secret information, and Defendants' use of unfair and dishonest trade practices;

E. Awarding punitive damages for Defendants' egregious conduct that caused Plaintiffs' damages;

F. Awarding Plaintiffs attorneys' fees, as well as costs and expenses associated with this litigation, as provided for in the Confidentiality Agreements and as otherwise provided for by applicable law; and

G. Any other and further relief the Court deems just and proper.

Dated: New York, New York
July 2, 2009

DEWEY PEGNO & KRAMARSKY LLP

By: _____

Thomas E.L. Dewey
Stephen M. Kramarsky
Ariel P. Cannon
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New York, New York 10017
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*Attorneys for Plaintiffs The Hartford Financial Services Group, Inc., et al*

SUPREME COURT OF THE STATE OF NEW YORK
COUNTY OF NEW YORK/IAS Part 56

| | | |
|---|---|---|
| TWIN CITY FIRE INSURANCE COMPANY, HARTFORD INSURANCE COMPANY OF ILLINOIS, HARTFORD INSURANCE COMPANY OF THE MIDWEST, TRUMBULL INSURANCE COMPANY, HARTFORD INSURANCE COMPANY OF THE SOUTHEAST, NUTMEG INSURANCE COMPANY, PROPERTY AND CASUALTY INSURANCE COMPANY OF HARTFORD, HARTFORD FIRE INSURANCE COMPANY, HARTFORD CASUALTY INSURANCE COMPANY, HARTFORD ACCIDENT AND INDEMNITY INSURANCE COMPANY, HARTFORD UNDERWRITERS INSURANCE COMPANY, PACIFIC INSURANCE COMPANY, LIMITED, and THE HARTFORD FINANCIAL SERVICES GROUP, INC., | : | Index No. 602062/09<br><br>Hon. Richard B. Lowe, J.S.C. |
| Plaintiffs,<br><br>-against-<br><br>ARCH INSURANCE GROUP, INC., ARCH CAPITAL GROUP LTD., DAVID McELROY, JOHN RAFFERTY and MICHAEL PRICE,<br><br>Defendants. | : | **AMENDED ANSWER, DEFENSES AND COUNTERCLAIMS OF DEFENDANTS ARCH INSURANCE GROUP INC. AND ARCH CAPITAL GROUP LTD.** |

Defendants Arch Insurance Group Inc. ("AIGI"), sued as "Arch Insurance Group, Inc.," and Arch Capital Group Ltd. (together with AIGI, "Arch"), by their attorneys, Foley & Lardner LLP, for their Amended Answer to the Complaint of the plaintiffs (together, "Hartford") and Counterclaims, allege as follows:

1. Deny each and every allegation contained in Paragraph 1 of the Complaint.

2. Deny knowledge or information sufficient to form a belief as to the truth of the allegations contained in Paragraph 2 of the Complaint, except admit, upon information and belief, that defendant David McElroy ("McElroy") retired from his position at the Hartford Financial Products division of Hartford ("HFP") prior to June 8, 2009.

3. Deny each and every allegation contained in Paragraph 3 of the Complaint, except admit that, on Monday, June 8, 2009, and on Monday, June 15, 2009, AIGI made certain public announcements, and refer to those press releases for the full contents thereof.

4. Deny each and every allegation contained in Paragraph 4 of the Complaint, except admit, upon information and belief, that Hartford has not been damaged by the alleged conduct of which it complains in the Complaint and that, even if it had been damaged, it had overcome these alleged losses by the date of the Complaint.

5. Deny knowledge or information sufficient to form a belief as to the truth of the allegations contained in Paragraph 5 of the Complaint, except admit that since June 8, 2009, more than 60 former employees of Hartford have chosen to leave Hartford and to accept offers of employment from AIGI.

6. Deny each and every allegation contained in Paragraph 6 of the Complaint, except deny knowledge or information sufficient to form a belief as to the truth of the allegation that Arch employees may have communicated with employees of HFP concerning the possibility of their employment at AIGI, their employment prospects, and the status and stability of HFP.

7. Deny each and every allegation contained in Paragraph 7 of the Complaint.

8. Deny each and every allegation contained in Paragraph 8 of the Complaint.

9. Deny each and every allegation contained in Paragraph 9 of the Complaint, except deny knowledge or information sufficient to form a belief as to the truth of the allegations that reinsurance is an integral part of HFP's underwriting operations.

10. Deny each and every allegation contained in Paragraph 10 of the Complaint, except admit that there is an Arch Capital Group Ltd. and Subsidiaries Code of Business Conduct, and refer to that document for the contents thereof.

11. Deny each and every allegation contained in Paragraph 11 of the Complaint.

12. Deny each and every allegation contained in Paragraph 12 of the Complaint, except admit, upon information and belief, that Hartford has not been damaged by the alleged conduct of which it complains in the Complaint and that, even if it had been damaged, it had overcome these alleged losses by the date of the Complaint.

13. Deny knowledge or information sufficient to form a belief as to the truth of the allegations contained in Paragraph 13 of the Complaint.

14. Deny knowledge or information sufficient to form a belief as to the truth of the allegations contained in Paragraph 14 of the Complaint.

15. Deny knowledge or information sufficient to form a belief as to the truth of the allegations contained in Paragraph 15 of the Complaint.

16. Deny knowledge or information sufficient to form a belief as to the truth of the allegations contained in Paragraph 16 of the Complaint.

17. Deny knowledge or information sufficient to form a belief as to the truth of the allegations contained in Paragraph 17 of the Complaint.

18. Deny knowledge or information sufficient to form a belief as to the truth of the allegations contained in Paragraph 18 of the Complaint.

19. Deny knowledge or information sufficient to form a belief as to the truth of the allegations contained in Paragraph 19 of the Complaint.

20. Deny knowledge or information sufficient to form a belief as to the truth of the allegations contained in Paragraph 20 of the Complaint.

21. Deny knowledge or information sufficient to form a belief as to the truth of the allegations contained in Paragraph 21 of the Complaint.

22. Deny knowledge or information sufficient to form a belief as to the truth of the allegations contained in Paragraph 22 of the Complaint.

23. Deny knowledge or information sufficient to form a belief as to the truth of the allegations contained in Paragraph 23 of the Complaint.

24. Deny knowledge or information sufficient to form a belief as to the truth of the allegations contained in Paragraph 24 of the Complaint.

25. Deny knowledge or information sufficient to form a belief as to the truth of the allegations contained in Paragraph 25 of the Complaint.

26. Admit the allegations contained in Paragraph 26 of the Complaint, except deny that the correct name of the referenced entity is "Arch Capital Group, Ltd."

27. Admit the allegations contained in Paragraph 27 of the Complaint, except deny that the correct name of the referenced entities are "Arch Capital Group, Ltd." or "Arch Insurance Group, Inc." and that AIGI writes insurance or reinsurance.

28. Deny knowledge or information sufficient to form a belief as to the truth of the allegations contained in Paragraph 28 of the Complaint, except admit, upon information and belief, that McElroy resides in Connecticut and previously was employed at HFP.

29. Deny knowledge or information sufficient to form a belief as to the truth of the allegations contained in Paragraph 29 of the Complaint, except admit, upon information and belief, the allegations that defendant John Rafferty ("Rafferty") resides in Illinois and previously was employed at HFP.

30. Deny knowledge or information sufficient to form a belief as to the truth of the allegations contained in Paragraph 30 of the Complaint, except admit, upon information and belief, that defendant Michael Price ("Price") resides in New Jersey and previously was employed at HFP.

31. Make no response to the allegations contained in Paragraph 31 of the Complaint on the ground that it states legal conclusions, except admit that AIGI has its principal place of business, and has transacted business, in New York.

32. Deny knowledge or information sufficient to form a belief as to the truth of the allegations contained in Paragraph 32 of the Complaint.

33. Deny knowledge or information sufficient to form a belief as to the truth of the allegations contained in Paragraph 33 of the Complaint.

34. Deny each and every allegation contained in Paragraph 34 of the Complaint, except deny knowledge or information sufficient to form a belief as to the truth of the allegations concerning the components of the alleged purchase by Hartford from Reliance Group Holdings ("Reliance") and the alleged payment by Hartford to Reliance.

35. Deny knowledge or information sufficient to form a belief as to the truth of the allegations contained in Paragraph 35 of the Complaint, except admit, upon information and belief, that Hartford, at some time, hired McElroy.

36. Deny knowledge or information sufficient to form a belief as to the truth of the allegations contained in Paragraph 36 of the Complaint, except admit, upon information and belief, that Hartford, at some time, hired Rafferty and Price.

37. Deny each and every allegation contained in Paragraph 37 of the Complaint, except deny knowledge or information sufficient to form a belief as to the truth of the allegations concerning the positions of, and particular information allegedly known or disclosed to, McElroy, Rafferty and Price (together, the "Individuals") during their employment at HFP.

38. Deny knowledge or information sufficient to form a belief as to the truth of the allegations contained in Paragraph 38 of the Complaint.

39. Deny knowledge or information sufficient to form a belief as to the truth of the allegations contained in Paragraph 39 of the Complaint.

40. Deny each and every allegation contained in Paragraph 40 of the Complaint, except deny knowledge or information sufficient to form a belief as to the truth of the allegations concerning the HFP staff during the Individuals' employment at HFP.

41. Deny knowledge or information sufficient to form a belief as to the truth of the allegations contained in Paragraph 41 of the Complaint.

42. Deny knowledge or information sufficient to form a belief as to the truth of the allegations contained in Paragraph 42 of the Complaint.

43. Deny knowledge or information sufficient to form a belief as to the truth of the allegations contained in Paragraph 43 of the Complaint.

44. Deny knowledge or information sufficient to form a belief as to the truth of the allegations contained in Paragraph 44 of the Complaint.

45. Deny knowledge or information sufficient to form a belief as to the truth of the allegations contained in Paragraph 45 of the Complaint.

46. Deny knowledge or information sufficient to form a belief as to the truth of the allegations contained in Paragraph 46 of the Complaint.

47. Deny knowledge or information sufficient to form a belief as to the truth of the allegations contained in Paragraph 47 of the Complaint.

48. Deny knowledge or information sufficient to form a belief as to the truth of the allegations contained in Paragraph 48 of the Complaint.

49. Deny knowledge or information sufficient to form a belief as to the truth of the allegations contained in Paragraph 49 of the Complaint.

50. Deny each and every allegation contained in Paragraph 50 of the Complaint.

51. Deny each and every allegation contained in Paragraph 51 of the Complaint, except deny knowledge or information sufficient to form a belief as to the truth of the allegations concerning what McElroy might have said at a different time in a different context concerning HFP.

52. Deny each and every allegation contained in Paragraph 52 of the Complaint.

53. Deny each and every allegation contained in Paragraph 53 of the Complaint.

54. Deny each and every allegation contained in Paragraph 54 of the Complaint, except admit that AIGI hired McElroy, in connection with which it agreed to compensate him in return for his performance of duties as set forth in his agreement of employment.

55. Deny each and every allegation contained in Paragraph 55 of the Complaint.

56. Deny knowledge or information sufficient to form a belief as to the truth of the allegations contained in Paragraph 56 of the Complaint, except admit, upon information and belief, that McElroy retired from his position at HFP prior to June 8, 2009.

57. Deny knowledge or information sufficient to form a belief as to the truth of the allegations contained in Paragraph 57 of the Complaint, except admit, upon information and belief, that McElroy's retirement entitled him to receive certain compensation.

58. Deny each and every allegation contained in Paragraph 58 of the Complaint.

59. With respect to the allegations contained in Paragraph 59 of the Complaint, admit, upon information and belief, that McElroy retired from his position at HFP prior to June 8, 2009, and admit that McElroy commenced his employment at AIGI on Monday, June 8, 2009.

60. Deny knowledge or information sufficient to form a belief as to the truth of the allegations contained in Paragraph 60 of the Complaint, except admit, upon information and belief, that Rafferty and Price are no longer employed at HFP.

61. Deny each and every allegation contained in Paragraph 61 of the Complaint, except deny knowledge or information sufficient to form a belief as to the truth of the allegations

concerning Rafferty's role at Hartford, admit that, on June 15, 2009, AIGI made a public announcement, and refer to that press release for the full contents thereof, and admit that Rafferty is the head of the Executive Assurance division of the Financial & Professional Liability Group at AIGI.

62. Deny each and every allegation contained in Paragraph 62 of the Complaint, except admit that subsequent to the employment of the Individuals by AIGI, certain other HFP employees contacted AIGI in search of employment, and that certain of those individuals were employed by AIGI.

63. Deny each and every allegation contained in Paragraph 63 of the Complaint.

64. Deny each and every allegation contained in Paragraph 64 of the Complaint, except deny knowledge or information sufficient to form a belief as to the truth of the allegation that Arch employees may have communicated with employees of HFP concerning the possibility of their employment at AIGI and their employment prospects.

65. Deny each and every allegation contained in Paragraph 65 of the Complaint, except deny knowledge or information sufficient to form a belief as to the truth of the allegation that Arch employees may have communicated with employees of HFP concerning the possibility of their employment at AIGI, their employment prospects and the status and stability of HFP.

66. Deny each and every allegation contained in Paragraph 66 of the Complaint.

67. Deny each and every allegation contained in Paragraph 67 of the Complaint.

68. Deny each and every allegation contained in Paragraph 68 of the Complaint, except admit, upon information and belief, that since June 8, 2009, more than 60 former employees of Hartford have chosen to leave Hartford and to accept offers of employment from AIGI, that Hartford has not been damaged by the alleged conduct of which it complains in the Complaint, and that even if it had been damaged, it had overcome these alleged losses by the date of the Complaint.

69. Deny each and every allegation contained in Paragraph 69 of the Complaint, except deny knowledge or information sufficient to form a belief as to the truth of the allegation that Arch employees may have communicated with any insurance broker or Arch client concerning the business, status and stability of HFP.

70. Deny each and every allegation contained in Paragraph 70 of the Complaint, except deny knowledge or information sufficient to form a belief as to the truth of the allegations that reinsurance is an integral part of HFP's underwriting operations, and make no answer to the allegation that "None of the Defendants stands to gain anything from undermining HFP's ability to reinsure its commitments" on the grounds that it is improperly argumentative and dependent on a false assumption.

71. As to the allegations contained in Paragraph 71 of the Complaint, make no response to the allegations of Count One of the Complaint because Count One of the Complaint is not alleged against Arch.

72. As to the allegations contained in Paragraph 72 of the Complaint, make no response to the allegations of Count One of the Complaint because Count One of the Complaint is not alleged against Arch.

73. As to the allegations contained in Paragraph 73 of the Complaint, make no response to the allegations of Count One of the Complaint because Count One of the Complaint is not alleged against Arch.

74. As to the allegations contained in Paragraph 74 of the Complaint, make no response to the allegations of Count One of the Complaint because Count One of the Complaint is not alleged against Arch.

75. As to the allegations contained in Paragraph 75 of the Complaint, make no response to the allegations of Count One of the Complaint because Count One of the Complaint is not alleged against Arch.

76. As to the allegations contained in Paragraph 76 of the Complaint:

(a) repeat each and every response made herein to Paragraphs 1 through 70, inclusive, of the Complaint with the same force and effect as if set forth at length hereat;

(b) as to the allegations contained in Paragraph 71 of the Complaint, repeat each and every response made herein to Paragraphs 1 through 70, inclusive, of the Complaint with the same force and effect as if set forth at length hereat;

(c) deny each and every allegation contained in Paragraph 72 of the Complaint, except deny knowledge or information sufficient to form a belief as to the truth of the allegations concerning Hartford's relationship with the Individuals, and admit, upon information and belief, that the Individuals were senior employees at HFP prior to their employment at AIGI;

(d) deny knowledge or information sufficient to form a belief as to the truth of the allegations contained in Paragraph 73 of the Complaint, except make no response to the allegations to the extent that they state legal conclusions;

(e) deny each and every allegation contained in Paragraph 74 of the Complaint; and

(f) deny each and every allegation contained in Paragraph 75 of the Complaint.

77. Deny each and every allegation contained in Paragraph 77 of the Complaint, except deny knowledge or information sufficient to form a belief as to the truth of the allegations concerning Hartford's relationship with the Individuals and make no response to those allegations to the extent that they state legal conclusions.

78. Deny each and every allegation contained in Paragraph 78 of the Complaint.

79. Deny each and every allegation contained in Paragraph 79 of the Complaint.

80. Deny each and every allegation contained in Paragraph 80 of the Complaint.

81. Deny each and every allegation contained in Paragraph 81 of the Complaint.

82. As to the allegations contained in Paragraph 82 of the Complaint, make no response to the allegations of Count Three of the Complaint because Count Three of the Complaint is not alleged against Arch.

83. As to the allegations contained in Paragraph 83 of the Complaint, make no response to the allegations of Count Three of the Complaint because Count Three of the Complaint is not alleged against Arch.

84. As to the allegations contained in Paragraph 84 of the Complaint, make no response to the allegations of Count Three of the Complaint because Count Three of the Complaint is not alleged against Arch.

85. As to the allegations contained in Paragraph 85 of the Complaint, make no response to the allegations of Count Three of the Complaint because Count Three of the Complaint is not alleged against Arch.

86. As to the allegations contained in Paragraph 86 of the Complaint, make no response to the allegations of Count Three of the Complaint because Count Three of the Complaint is not alleged against Arch.

87. As to the allegations contained in Paragraph 87 of the Complaint, make no response to the allegations of Count Three of the Complaint because Count Three of the Complaint is not alleged against Arch.

88. As to the allegations contained in Paragraph 88 of the Complaint, make no response to the allegations of Count Three of the Complaint because Count Three of the Complaint is not alleged against Arch.

89. As to the allegations contained in Paragraph 89 of the Complaint, make no response to the allegations of Count Three of the Complaint because Count Three of the Complaint is not alleged against Arch.

90. As to the allegations contained in Paragraph 90 of the Complaint, make no response to the allegations of Count Four of the Complaint because Count Four of the Complaint is not alleged against Arch.

91. As to the allegations contained in Paragraph 91 of the Complaint, make no response to the allegations of Count Four of the Complaint because Count Four of the Complaint is not alleged against Arch.

92. As to the allegations contained in Paragraph 92 of the Complaint, make no response to the allegations of Count Four of the Complaint because Count Four of the Complaint is not alleged against Arch.

93. As to the allegations contained in Paragraph 93 of the Complaint, make no response to the allegations of Count Four of the Complaint because Count Four of the Complaint is not alleged against Arch.

94. As to the allegations contained in Paragraph 94 of the Complaint, make no response to the allegations of Count Four of the Complaint because Count Four of the Complaint is not alleged against Arch.

95. As to the allegations contained in Paragraph 95 of the Complaint, make no response to the allegations of Count Four of the Complaint because Count Four of the Complaint is not alleged against Arch.

96. As to the allegations contained in Paragraph 96 of the Complaint, make no response to the allegations of Count Four of the Complaint because Count Four of the Complaint is not alleged against Arch.

97. As to the allegations contained in Paragraph 97 of the Complaint:

(a) repeat each and every response made herein to Paragraphs 1 through 81, inclusive, of the Complaint with the same force and effect as if set forth at length hereat;

(b) as to the allegations contained in Paragraph 82 of the Complaint, repeat each and every response made herein to Paragraphs 1 through 81, inclusive, of the Complaint with the same force and effect as if set forth at length hereat;

(c) deny knowledge or information sufficient to form a belief as to the truth of the allegations contained in Paragraph 83 of the Complaint, except make no response to the allegations to the extent that they state legal conclusions;

(d) deny knowledge or information sufficient to form a belief as to the truth of the allegations contained in Paragraph 84 of the Complaint;

(e) deny knowledge or information sufficient to form a belief as to the truth of the allegations contained in Paragraph 85 of the Complaint;

(f) deny knowledge or information sufficient to form a belief as to the truth of the allegations contained in Paragraph 86 of the Complaint, except make no response to the allegations to the extent that they state legal conclusions;

(g) deny each and every allegation contained in Paragraph 87 of the Complaint;

(h) deny each and every allegation contained in Paragraph 88 of the Complaint;

(i) deny each and every allegation contained in Paragraph 89 of the Complaint;

(j) as to the allegations contained in Paragraph 90 of the Complaint, repeat each and every response made herein to Paragraphs 1 through 89, inclusive, of the Complaint with the same force and effect as if set forth at length hereat;

(k) deny each and every allegation contained in Paragraph 91 of the Complaint;

(l) deny knowledge or information sufficient to form a belief as to the truth of the allegations contained in Paragraph 92 of the Complaint;

(m) deny each and every allegation contained in Paragraph 93 of the Complaint;

(n) deny each and every allegation contained in Paragraph 94 of the Complaint;

(o) deny each and every allegation contained in Paragraph 95 of the Complaint; and

(p) deny each and every allegation contained in Paragraph 96 of the Complaint.

98. Deny knowledge or information sufficient to form a belief as to the truth of the allegations contained in Paragraph 98 of the Complaint, except make no response to the allegations to the extent that they state legal conclusions.

99. Deny each and every allegation contained in Paragraph 99 of the Complaint.

100. Deny each and every allegation contained in Paragraph 100 of the Complaint.

101. Deny each and every allegation contained in Paragraph 101 of the Complaint.

102. Deny each and every allegation contained in Paragraph 102 of the Complaint.

103. Deny each and every allegation contained in Paragraph 103 of the Complaint.

104. As to the allegations contained in Paragraph 104 of the Complaint, repeat each and every response made herein to Paragraphs 1 through 103, inclusive, of the Complaint with the same force and effect as if set forth at length hereat.

105. Deny each and every allegation contained in Paragraph 105 of the Complaint, except admit, upon information and belief, that the Individuals had certain knowledge concerning HFP's relationships with its clients.

106. Deny each and every allegation contained in Paragraph 106 of the Complaint.

107. Deny each and every allegation contained in Paragraph 107 of the Complaint.

108. Deny each and every allegation contained in Paragraph 108 of the Complaint.

109. Deny each and every allegation contained in Paragraph 109 of the Complaint.

110. As to the allegations contained in Paragraph 111 of the Complaint, repeat each and every response made herein to Paragraphs 1 through 109, inclusive, of the Complaint with the same force and effect as if set forth at length hereat.

111. Deny each and every allegation contained in Paragraph 110 of the Complaint.

112. Deny each and every allegation contained in Paragraph 112 of the Complaint.

113. Deny each and every allegation contained in Paragraph 113 of the Complaint.

114. Deny each and every allegation contained in Paragraph 114 of the Complaint.

115. Deny each and every allegation contained in Paragraph 115 of the Complaint.

116. As to the allegations contained in Paragraph 116 of the Complaint, repeat each and every response made herein to Paragraphs 1 through 115, inclusive, of the Complaint with the same force and effect as if set forth at length hereat.

117. Deny each and every allegation contained in Paragraph 117 of the Complaint.

118. Deny each and every allegation contained in Paragraph 118 of the Complaint.

119. Deny each and every allegation contained in Paragraph 119 of the Complaint.

120. As to the allegations contained in Paragraph 120 of the Complaint, repeat each and every response made herein to Paragraphs 1 through 119, inclusive, of the Complaint with the same force and effect as if set forth at length hereat.

121. Deny each and every allegation contained in Paragraph 121 of the Complaint.

122. Deny each and every allegation contained in Paragraph 122 of the Complaint.

123. Deny each and every allegation contained in Paragraph 123 of the Complaint.

FOR A FIRST DEFENSE
TO THE SECOND AND FIFTH THROUGH
NINTH, INCLUSIVE, COUNTS OF THE COMPLAINT

124. The Complaint, and each purported Count alleged therein against Arch, fails to state a claim against Arch upon which relief can be granted.

FOR A SECOND DEFENSE
TO THE SECOND AND FIFTH THROUGH
NINTH, INCLUSIVE, COUNTS OF THE COMPLAINT

125. The Individuals worked at HFP at will; they had no employment contracts with Hartford; they had not been asked by Hartford to sign covenants not to compete; and they had not been asked by Hartford to sign agreements not to solicit their customers or employees, or any other restrictive covenants.

126. The Individuals did not bring to Arch, and have not attempted to use at Arch, any confidential information, proprietary information, or purported trade secrets, of Hartford.

127. Nonetheless, Hartford, through this litigation, attempts to handicap Arch's ability to conduct a business competitive with HFP's business.

128. The Complaint, and each purported Count alleged therein against Arch, violates public policy by attempting to impose an impermissible restraint on competition.

FOR A THIRD DEFENSE
TO THE SECOND AND FIFTH THROUGH
NINTH, INCLUSIVE, COUNTS OF THE COMPLAINT

129. Arch repeats and realleges each and every allegation contained in Paragraphs 125 through 127, inclusive, hereof, with the same force and effect as if set forth at length hereat.

130. At all relevant times, Hartford has been aware of all of the facts alleged in Paragraph 125 hereof.

131. Upon information and belief, at all relevant times, Hartford has had no reason to believe that the facts alleged in Paragraph 126 hereof are not true.

132. The Complaint, and each purported Count alleged therein against Arch, is barred by Hartford' unclean hands.

FOR A FOURTH DEFENSE
TO THE SECOND AND FIFTH THROUGH
NINTH, INCLUSIVE, COUNTS OF THE COMPLAINT

133. To the extent that there has been a decline of the business, status, value and stability of HFP, that decline has resulted from (among other factors unrelated to Arch or the Individuals) the general deterioration of Hartford's financial strength, ratings, status and stability since in or about mid-2008.

134. Any damage suffered by Hartford in connection with the decline of HFP resulted not from any actions of Arch or the Individuals, but from other factors unrelated to and not caused by either Arch or the Individuals.

FOR A FIFTH DEFENSE
TO THE SECOND AND FIFTH THROUGH
NINTH, INCLUSIVE, COUNTS OF THE COMPLAINT

135. If, *arguendo*, Hartford has been damaged, it has adequate remedies at law.

COUNTERCLAIMS

Arch, by its attorneys, for its Counterclaims against Hartford, alleges as follows:

FIRST COUNT:
INDEMNIFICATION
ON ACCOUNT OF WRONGFUL REFUSAL TO PAY UNDER THE HFP PLANS

136. Upon information and belief, Hartford provided that certain of its employees, including without limitation the Individuals and Catherine Kelly, were entitled to, in addition to their cash salaries, certain deferred compensation to be paid under programs and plans that were in place during the time that the Individuals were employed at Hartford, including without limitation the 2007 HFP Annual Incentive & Profit Contribution Plan (the "2007 Plan") and the predecessor HFP Annual Cash Incentive & Profit Contribution Plan (the "2000 Plan," together with the 2007 Plan, the "HFP Plans").

137. Upon information and belief, each of the Individuals and Kelly earned, and is entitled to, cash payments from Hartford under the HFP Plans for accident years 2000 through 2009, which amounts remain, in substantial part, unpaid.

138. Upon information and belief, under Hartford's long-time policy, practice, and application of the HFP Plans, Hartford would pay to McElroy the as-yet-unpaid deferred compensation due to him in accordance with the HFP Plans, in light of his retirement; and would pay to Rafferty, Price and Kelly the as-yet-unpaid deferred compensation due to them in accordance with the HFP Plans, in light of the fact that, in connection with Hartford's acceptance of funding from the federal government's Troubled Assets Relief Program, they would have faced a material reduction in compensation that was not due to poor performance had they remained in Hartford's employ.

139. The Individuals have requested that Hartford make payment to them under the HFP Plans.

140. Hartford has notified the Individuals that it will not make any payment to them under the HFP Plans and, upon information and belief, Hartford will not make any payment to Kelly under the HFP Plans.

141. Hartford's notifications and determinations of nonpayment to the Individuals and to Kelly under the HFP Plans are in violation of the express terms of, and the covenants of good faith and fair dealing implied into, the HFP Plans, and were unfairly, arbitrarily, and discriminatorily made, and wrongfully made in retaliation against the Individuals and Kelly for their having left HFP's employ and accepted employment at AIGI.

142. Each of the Individuals and Kelly is now employed by AIGI pursuant to an employment agreement (together, the "Employment Agreements").

143. Pursuant to each of the Employment Agreements, and subject to certain terms and conditions, AIGI agreed that each of the Individuals and Kelly will be entitled to cash payments from AIGI equal to the amounts, if any, he or she would have received from Hartford under the HFP Plans, to the extent that such payments are not made by Hartford.

144. By reason of Hartford's wrongful determinations of nonpayment to the Individuals and to Kelly under the HFP Plans, AIGI will be required to reimburse the Individuals and Kelly in the amounts, if any, that they should have been paid, but have not been and will not be paid, by Hartford.

145. Accordingly, Hartford is obligated to indemnify AIGI in the amounts that AIGI is or will be required to pay to the Individuals under the HFP Plans.

SECOND COUNT:
INDEMNIFICATION
ON ACCOUNT OF WRONGFUL REFUSAL TO PAY UNDER THE BY-LAWS

146. Upon information and belief, and as alleged in the Complaint by Hartford, the Individuals are former officers of, and former employees who held management positions with, HFP, a division of plaintiff The Hartford Financial Services Group, Inc. ("Hartford Financial"), and the Individuals served as such at the request of Hartford Financial.

147. Upon information and belief, and as alleged in the Complaint by Hartford, McElroy is a former officer of plaintiffs Twin City Fire Insurance Company, Hartford Insurance Company of Illinois, Hartford Insurance Company of the Midwest, Hartford Insurance Company of the Southeast, Nutmeg Insurance Company and Hartford Casualty Insurance Company, all direct or indirect subsidiaries of Hartford Financial, and McElroy served as such at the request of Hartford Financial.

148. Upon information and belief, and as alleged in the Complaint by Hartford, Rafferty is a former officer of plaintiffs Twin City Fire Insurance Company and Nutmeg Insurance

Hartford seeks from the Individuals, among other things, the return of all compensation earned during the period of their alleged disloyalty to Hartford, compensatory damages "in no event less than many millions of dollars," and punitive damages.

151. Pursuant to Sections 4.1(a) and 4.6 of the Amended and Restated By-Laws of Hartford Financial (the "Hartford Financial By-Laws"), Hartford Financial is obligated (among other things) to indemnify, to the fullest extent permitted by law, each of its former officers, employees and agents who is involved in any litigation by reason of the fact that he was an officer, employee or agent of Hartford Financial, against all expenses, including attorneys' fees, actually and reasonably incurred by such person in connection with such a litigation.

152. Pursuant to Sections 4.1(a), 4.5(d)(ii), and 4.6 of the Hartford Financial By-Laws, Hartford Financial is obligated (among other things) to indemnify, to the fullest extent permitted by law, each of its former officers, employees and agents who is involved in any litigation by reason of the fact that he was serving as an officer, employee, fiduciary or agent of any "Covered Entity" (defined as any entity other than Hartford Financial in respect of which the person to be indemnified was serving as a director, officer, employee, fiduciary or agent at the request of Hartford

Financial) against all expenses, including attorneys' fees, actually and reasonably incurred by such person in connection with such a litigation.

153. Pursuant to Sections 4.4 and 4.6 of the Hartford Financial By-Laws, each person to be indemnified under the By-Laws is entitled to receive, from time to time, advance payment of any indemnifiable expenses.

154. Accordingly, under the Hartford Financial By-Laws, Hartford is obligated to indemnify the Individuals by paying their costs and expenses incurred in connection with this litigation.

155. The Individuals have requested that Hartford make payment to them under

[redacted]

159. Accordingly, upon information and belief, under the Subsidiary By-Laws, Hartford is obligated to indemnify the Individuals by paying their costs and expenses incurred in connection with this litigation.

160. Upon information and belief, Hartford has determined that it will not make any payment to the Individuals under the Subsidiary By-Laws.

161. Hartford's notifications and determinations of nonpayment to the Individuals under the Hartford Financial By-Laws and the Subsidiary By-Laws (together, the "By-Laws") are in violation of the express terms of, and the covenants of good faith and fair dealing implied into, the By-Laws, and were unfairly and arbitrarily made, and wrongfully made in retaliation against the Individuals for their having left HFP's employ and accepted employment at AIGI.

162. Pursuant to each of the Employment Agreements, and subject to certain terms and conditions, AIGI agreed to indemnify the Individuals for, and to hold them harmless against, any liability, including reasonable attorneys' fees, incurred by them as a result of a claim by Hartford arising out of their conduct or actions taken in connection with their commencement of employment with AIGI.

163. By reason of Hartford's commencement of this litigation, and Hartford's wrongful determinations of nonpayment to the Individuals under the By-Laws, AIGI has been and will be required to pay on the Individuals' behalves costs and expenses, including attorneys' fees, incurred in connection with this litigation, which amounts should be paid, but have not been and will not be paid, by Hartford.

164. Accordingly, Hartford is obligated to indemnify AIGI in the amounts that AIGI has been and will be required to pay for the Individuals' costs and expenses, including attorneys' fees, incurred in connection with this litigation.

THIRD COUNT:
INDEMNIFICATION
ON ACCOUNT OF UNJUST ENRICHMENT

165. Arch repeats each and every allegation contained in Paragraphs 136 through 164, inclusive, hereof, with the same force and effect as if set forth at length hereat.

166. Hartford's failure to honor its obligations to the Individuals and to Kelly under the HFP Plans, and to the Individuals under the By-Laws, has resulted, and will result, in the unjust enrichment of Hartford at the expense of AIGI.

167. Accordingly, Hartford is obligated to indemnify AIGI in the amounts that AIGI is, has been, or will be required to pay (a) to the Individuals and to Kelly under the HFP Plans, and (b) for the Individuals' costs and expenses, including attorneys' fees, incurred in connection with this litigation.

WHEREFORE, Arch seeks the following:

a. Entry of judgment dismissing the Complaint, and each purported Count alleged therein against Arch, with prejudice, and denying all relief therein sought;

b. Entry of judgment against Hartford on the First Count of the Counterclaim, awarding AIGI the amounts that it is or will be required to pay to the Individuals and to Kelly under the HFP Plans;

c. Entry of judgment against Hartford on the Second Count of the Counterclaim, awarding AIGI the amounts that it has been or will be required to pay for the Individuals' costs and expenses, including attorneys' fees, incurred in connection with this litigation;

d. Entry of judgment against Hartford on the Third Count of the Counterclaim, awarding AIGI the amounts (i) that it is or will be required to pay to the Individuals and to Kelly under the HFP Plans, and (ii) that it has been or will be required to pay for the Individuals' costs and expenses, including attorneys' fees, incurred in connection with this litigation; and

e. Entry of an order awarding Arch its costs and disbursements herein, including attorneys' fees, together with such other and further relief as this Court may deem just and proper.

DATED: New York, New York
July 16, 2010

FOLEY & LARDNER LLP

By: Susan J. Schwartz

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*Attorneys for Defendants*
*Arch Insurance Group Inc.*
*and Arch Capital Group Ltd.*

SUPREME COURT OF THE STATE OF NEW YORK
COUNTY OF NEW YORK

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|---|---|
| TWIN CITY FIRE INSURANCE COMPANY, HARTFORD INSURANCE COMPANY OF ILLINOIS, HARTFORD INSURANCE COMPANY OF THE MIDWEST, TRUMBULL INSURANCE COMPANY, HARTFORD INSURANCE COMPANY OF THE SOUTHEAST, NUTMEG INSURANCE COMPANY, PROPERTY AND CASUALTY INSURANCE COMPANY OF HARTFORD, HARTFORD FIRE INSURANCE COMPANY, HARTFORD CASUALTY INSURANCE COMPANY, HARTFORD ACCIDENT AND INDEMNITY INSURANCE COMPANY, HARTFORD UNDERWRITER INSURANCE COMPANY, PACIFIC INSURANCE COMPANY, LIMITED and THE HARTFORD FINANCIAL SERVICES GROUP, INC.,<br><br>Plaintiffs,<br><br>-against-<br><br>ARCH INSURANCE GROUP, INC., ARCH CAPITAL GROUP LTD., DAVID McELROY, JOHN RAFFERTY and MICHAEL PRICE,<br><br>Defendants. | Index No. 09/602062<br><br>**AMENDED ANSWER AND COUNTERCLAIMS OF DAVID McELROY, JOHN RAFFERTY AND MICHAEL PRICE** |

Defendants David McElroy, John Rafferty, and Michael Price (the "Individuals"), by their attorneys Friedman Kaplan Seiler & Adelman LLP, answer the complaint of plaintiffs (referred to herein, individually and collectively, as "Hartford") as follows:

1. Deny the allegations of paragraph 1.

2. Deny the allegations of paragraph 2, except state that on May 21, 2009, Mr. McElroy gave notice of his retirement to a representative of Hartford, and that pursuant thereto, his last day at the Hartford Financial Products ("HFP") division of Hartford was June 5, 2009.

3. Deny the allegations of paragraph 3, except state that Arch Insurance Group Inc. ("Arch") (misidentified as Arch Insurance Group, Inc.) issued press releases dated June 8, 2009 and June 15, 2009, and respectfully refer to the those press releases for the contents thereof.

4. Deny the allegations of paragraph 4, except admit, on information and belief, Hartford's allegation that it has overcome the effects of any alleged misconduct by defendants.

5. Deny the allegations of paragraph 5, except admit that since June 8, 2009, more than 60 persons, whose immediate prior employment was at Hartford, including certain senior executives at HFP, have begun employment at Arch.

6. Deny the allegations of paragraph 6 as to themselves, and deny knowledge or information sufficient to form a belief as to the truth of the allegation that persons (not including the Individuals) have sent such emails, made such telephone calls, or sent such text messages.

7. Deny the allegations of paragraph 7.

8. Deny the allegations of paragraph 8.

9. Deny the allegations of paragraph 9, except deny knowledge or information sufficient to form a belief as to the truth of the allegation that reinsurance of HFP's insurance obligations is an integral component of HFP's underwriting operations.

10. Deny the allegations of paragraph 10, except state that there is publicly available an Arch Capital Group Ltd. and Subsidiaries Code of Business Conduct, and respectfully refer to it for the contents thereof.

11. Deny knowledge or information sufficient to form a belief as to the truth of the allegations of paragraph 11.

12. Deny the allegations of paragraph 12, except admit, on information and belief, Hartford's allegation that it has effectively managed and contained any damage from defendants' alleged conduct.

13. Deny knowledge or information sufficient to form a belief as to the truth of the allegations of paragraph 13, except state that Hartford's principal place of business is at One Hartford Plaza, Hartford, Connecticut, and that numerous companies operate collectively under the trade name "The Hartford" and are engaged in the business of selling investment and/or insurance products.

14. Deny knowledge or information sufficient to form a belief as to the truth of the allegations of paragraph 14.

15. Deny knowledge or information sufficient to form a belief as to the truth of the allegations of paragraph 15.

16. Deny knowledge or information sufficient to form a belief as to the truth of the allegations of paragraph 16.

17. Deny knowledge or information sufficient to form a belief as to the truth of the allegations of paragraph 17.

18. Deny knowledge or information sufficient to form a belief as to the truth of the allegations of paragraph 18.

19. Deny knowledge or information sufficient to form a belief as to the truth of the allegations of paragraph 19.

20. Deny knowledge or information sufficient to form a belief as to the truth of the allegations of paragraph 20.

21. Deny knowledge or information sufficient to form a belief as to the truth of the allegations of paragraph 21.

22. Deny knowledge or information sufficient to form a belief as to the truth of the allegations of paragraph 22.

23. Deny knowledge or information sufficient to form a belief as to the truth of the allegations of paragraph 23.

24. Deny knowledge or information sufficient to form a belief as to the truth of the allegations of paragraph 24.

25. Deny knowledge or information sufficient to form a belief as to the truth of the allegations of paragraph 25.

26. Admit the allegations of paragraph 26, except state that Arch Capital Group Ltd. is misidentified as Arch Capital Group, Ltd.

27. Admit the allegations of paragraph 27, except deny that Arch writes insurance or reinsurance.

28. Deny the allegations of paragraph 28, except state that Mr. McElroy is a resident of the State of Connecticut, that he was employed from some time after September 2000 until his retirement on June 5, 2009 as a Senior Vice President of Hartford, and at all times from September 2000 through June 5, 2009 as the head of Hartford's HFP division, and that during this period, Mr. McElroy had offices at 2 Park Avenue, New York, New York (and before that at 7 World Trade Center, New York, New York) and at Hartford's facility in Hartford, Connecticut.

29. Deny the allegations of paragraph 29, except state that Mr. Rafferty is a resident of the State of Illinois, that he was a Vice President at HFP until June 9, 2009, and that in this capacity he traveled frequently to 2 Park Avenue, New York, New York, where he had an office

(and before that to 7 World Trade Center, New York, New York), and deny knowledge or information sufficient to form a belief as to the truth of the allegation that he was an officer of Nutmeg Insurance Company or Twin City Fire Insurance Company.

30. Deny the allegations of paragraph 30, except state that Mr. Price is a resident of the State of New Jersey, that he was a Vice President of HFP until June 10, 2009, and that he had an office at 2 Park Avenue, New York, New York (and before that at 7 World Trade Center, New York, New York).

31. Paragraph 31 states legal conclusions to which no response is required.

32. Deny the allegations of paragraph 32, except state that HFP was a substantial provider in the United States of Directors and Officers, Employment Practices, Liability, Errors and Omissions, and crime insurance.

33. Deny the allegations of paragraph 33, except state that, as Hartford publicly announced on June 19, 2000, it agreed to acquire the in-force, new and renewal business of Reliance Group Holdings, Inc.'s ("Reliance") financial products business, as well as the majority of Reliance's excess and surplus ("E&S") line, as a result of which Hartford's specialty operation expected to write approximately $250 million in additional annual gross premium, and moreover, Reliance's financial products and E&S staff of more than 100 employees would join Hartford's subsidiary, Hartford Specialty Company, and remain in New York to manage the business being assumed in this transaction (the "Transaction").

34. Deny knowledge or information sufficient to form a belief as to the truth of the allegations of paragraph 34, except deny that anything Hartford or a Hartford affiliate acquired in the Transaction comprised a trade secret.

35. Deny the allegations of paragraph 35, except state that in connection with the Transaction, Mr. McElroy was hired as a Vice President by Hartford, which later named him a

Senior Vice President of Hartford, and that between September 2000 and June 5, 2009, he was also, by Hartford's appointment, the head of HFP.

36. Deny the allegations of paragraph 36, except state that in 2000, in connection with the Transaction, Mr. Rafferty was hired by Hartford (which at a certain point named Mr. Rafferty a Vice President at HFP) and Mr. Price was also hired by Hartford, which named him an Assistant Vice President at HFP (and later promoted Mr. Price to a Vice President at HFP).

37. Deny the allegations of paragraph 37, including the allegation that any of the identified information to which the Individuals were allegedly privy comprised a trade secret belonging to Hartford, and state that they had access to certain information by virtue of their positions at HFP, including contact information for certain brokers and clients, certain strategy materials, and renewal schedules and other data for certain HFP clients.

38. Deny the allegations of paragraph 38, except state HFP paid the Individuals certain monetary compensation, reimbursed certain travel and entertainment expenses of the Individuals associated with business development, and expended certain resources in furtherance of the development of clients that the Individuals serviced and the development of products that the Individuals sold.

39. Deny the allegations of paragraph 39, except state that HFP reimbursed tuition paid by Mr. Price for a limited number of classes at New York University's Stern School of Business, and that HFP provided the Individuals with certain benefits, resources, and support during their employment.

40. Deny the allegations of paragraph 40, except state that the Individuals, with the assistance of others, helped build HFP's business, and that as of June 1, 2008, the vast majority of employees at HFP were not individuals who had joined Hartford or HFP directly from Reliance.

41. Deny the allegations of paragraph 41, except state that the Individuals, with the assistance of others, helped develop new clients and client contacts at HFP, helped develop several new insurance products at HFP, and helped substantially rewrite and re-file with the relevant state authorities all of HFP's products, in connection with all of which certain resources of HFP were employed.

42. Deny the allegations of paragraph 42, and state that Hartford purports to have found an account of a 2001 interview of Mr. McElroy, and respectfully refer to that account for the contents thereof.

43. Deny knowledge or information sufficient to form a belief as to the truth of the allegations of paragraph 43.

44. Deny knowledge or information sufficient to form a belief as to the truth of the allegations of paragraph 44.

45. Deny knowledge or information sufficient to form a belief as to the truth of the allegations of paragraph 45.

46. Deny knowledge or information sufficient to form a belief as to the truth of the allegations of paragraph 46.

47. Deny knowledge or information sufficient to form a belief as to the truth of the allegations of paragraph 47.

48. Deny knowledge or information sufficient to form a belief as to the truth of the allegations of paragraph 48.

49. Deny knowledge or information sufficient to form a belief as to the truth of the allegations of paragraph 49.

50. Deny the allegations of paragraph 50, and state that, as Mr. McElroy told Ramani Ayer, Chairman and Chief Executive Officer of Hartford, in March 2009, representatives of certain insurers, including Arch, had made overtures to Mr. McElroy about acquiring HFP.

51. Deny the allegations of paragraph 51, and respectfully refer to the text which Hartford purports (in the last line of paragraph 51) to have found, quoting Mr. McElroy, for the contents thereof.

52. Deny the allegations of paragraph 52.

53. Deny the allegations of paragraph 53.

54. Deny the allegations of paragraph 54.

55. Deny the allegations of paragraph 55.

56. Deny the allegations of paragraph 56, except state that on May 21, 2009, Mr. McElroy gave notice of his retirement to a representative of Hartford, and that Mr. McElroy's last day at HFP was June 5, 2009.

57. Deny the allegations of paragraph 57, except state that Mr. McElroy is entitled to collect certain sums from Hartford, including in March 2010, but that he received no compensation in any form from Hartford or HFP on or about June 5, 2009, his date of retirement, in respect of his retirement.

58. Deny the allegations of paragraph 58.

59. Deny the allegations of paragraph 59, except state that Mr. McElroy's first day of employment at Arch was June 8, 2009.

60. Deny the allegations of paragraph 60, except state that Mr. Rafferty resigned at HFP on June 9, 2009, and that Hartford constructively terminated Mr. Price at HFP on June 10, 2009.

61. Deny the allegations of paragraph 61, except state that Arch issued press releases dated June 8, 2009 and June 15, 2009, and respectfully refer to the those press releases for the contents thereof.

62. Deny the allegations of paragraph 62, except state that on or after June 8, 2009, certain persons applied to Arch for employment whose then-current or immediate prior employment was at HFP, and that Arch made offers of employment to certain of these persons, and that certain of these persons to whom Arch made offers accepted them.

63. Deny the allegations of paragraph 63 as to themselves, and deny knowledge or information sufficient to form a belief as to the truth of the allegation that persons (not including the Individuals) have engaged in such conduct.

64. Deny the allegations of paragraph 64 as to themselves, and deny knowledge or information sufficient to form a belief as to the truth of the allegation that persons (not including the Individuals) have engaged in such conduct or made such statements.

65. Deny the allegations of paragraph 65 as to themselves, and deny knowledge or information sufficient to form a belief as to the truth of the allegation that persons (not including the Individuals) have made such telephone calls or sent such text messages.

66. Deny the allegations of paragraph 66.

67. Deny the allegations of paragraph 67 as to themselves, and deny knowledge or information sufficient to form a belief as to the truth of the allegation that persons (not including the Individuals) have engaged in such conduct.

68. Deny the allegations of the first sentence of paragraph 68, except admit that since June 8, 2009, more than 60 persons, whose immediate prior employment was at Hartford, including certain senior employees at HFP, have begun employment at Arch. Deny the allegations

of the second sentence of paragraph 68, except admit, on information and belief, Hartford's allegation that it has overcome any losses due to the departure of persons from HFP and their subsequent employment by Arch.

69. Deny the allegations of paragraph 69 as to themselves, and deny knowledge or information sufficient to form a belief as to the truth of the allegation that persons (not including the Individuals) had such conversations.

70. Deny the allegations of the first sentence of paragraph 70, deny knowledge or information sufficient to form a belief as to the truth of the allegations of the second sentence of paragraph 70, and the third sentence of paragraph 70 is an argument rather than an allegation of fact as to which no response is required.

71. Repeat and re-allege their answers to paragraphs 1-70.

72. Deny the allegations of paragraph 72, except state that the Individuals held the positions at HFP described in paragraphs 28-30 of this Answer, and that they were trusted employees.

73. Paragraph 73 states legal conclusions to which no response is required.

74. Paragraph 74 states legal conclusions to which no response is required.

75. Deny the allegations of paragraph 75.

76. Repeat and re-allege their answers to paragraphs 1-75.

77. Paragraph 77 purports to state a claim against "Arch," to which no response from the Individuals is required.

78. Paragraph 78 purports to state a claim against "Arch," to which no response from the Individuals is required.

79. Paragraph 79 purports to state a claim against "Arch," to which no response from the Individuals is required.

80. Paragraph 80 purports to state a claim against "Arch," to which no response from the Individuals is required.

81. Paragraph 81 purports to state a claim against "Arch," to which no response from the Individuals is required.

82. Repeat and re-allege their answers to paragraphs 1-81.

83. Paragraph 83 states legal conclusions to which no response is required.

84. Deny knowledge or information sufficient to form a belief as to the truth of the allegations of paragraph 84.

85. Deny knowledge or information sufficient to form a belief as to the truth of the allegations of paragraph 85.

86. Paragraph 86 states legal conclusions to which no response is required.

87. Deny the allegations of paragraph 87.

88. Paragraph 88 states legal conclusions to which no response is required.

89. Deny the allegations of paragraph 89.

90. Repeat and re-allege their answers to paragraphs 1-89.

91. Deny the allegations of paragraph 91.

92. Deny knowledge or information sufficient to form a belief as to the truth of the allegations of paragraph 92.

93. Deny the allegations of paragraph 93.

94. Deny the allegations of paragraph 94.

95. Paragraph 95 states legal conclusions to which no response is required.

96. Deny the allegations of paragraph 96.

97. Repeat and re-allege their answers to paragraphs 1-96.

98. Paragraph 98 purports to state a claim against "Arch," to which no response from the Individuals is required.

99. Paragraph 99 purports to state a claim against "Arch," to which no response from the Individuals is required.

100. Paragraph 100 purports to state a claim against "Arch," to which no response from the Individuals is required.

101. Paragraph 101 purports to state a claim against "Arch," to which no response from the Individuals is required.

102. Paragraph 102 purports to state a claim against "Arch," to which no response from the Individuals is required.

103. Paragraph 103 purports to state a claim against "Arch," to which no response from the Individuals is required.

104. Repeat and re-allege their answers to paragraphs 1-103.

105. Deny the allegations of paragraph 105, except state that the Individuals had certain knowledge as to HFP's relationships with certain of its clients.

106. Paragraph 106 states legal conclusions to which no response is required.

107. Paragraph 107 states legal conclusions to which no response is required.

108. Deny the allegations of paragraph 108.

109. Deny the allegations of paragraph 109.

110. Repeat and re-allege their answers to paragraphs 1-110.

111. Paragraph 111 purports to state a claim against "Arch," to which no response from the Individuals is required.

112. Paragraph 112 purports to state a claim against "Arch," to which no response from the Individuals is required.

113. Paragraph 113 purports to state a claim against "Arch," to which no response from the Individuals is required.

114. Paragraph 114 purports to state a claim against "Arch," to which no response from the Individuals is required.

115. Paragraph 115 purports to state a claim against "Arch," to which no response from the Individuals is required.

116. Repeat and re-allege their answers to paragraphs 1-115.

117. Paragraph 117 purports to state a claim against "Arch," to which no response from the Individuals is required.

118. Paragraph 118 purports to state a claim against "Arch," to which no response from the Individuals is required.

119. Paragraph 119 purports to state a claim against "Arch," to which no response from the Individuals is required.

120. Repeat and re-allege their answers to paragraphs 1-119.

121. Deny the allegations of paragraph 121.

122. Deny the allegations of paragraph 122.

123. Deny the allegations of paragraph 123.

## FIRST AFFIRMATIVE DEFENSE

The complaint should be dismissed, in whole or in part, because it fails to state any claim upon which relief may be granted.

## SECOND AFFIRMATIVE DEFENSE

Hartford's claims are barred, in whole or in part, by the statute of frauds.

## THIRD AFFIRMATIVE DEFENSE

Hartford's claims are barred, in whole or in part, by its inequitable conduct and/or by the doctrines of estoppel, waiver, *in pari delicto*, and/or unclean hands.

## FOURTH AFFIRMATIVE DEFENSE

Hartford has failed to protect its alleged confidential or proprietary information or its alleged trade secrets.

## FIFTH AFFIRMATIVE DEFENSE

The Individuals did not bring to Arch, and have not used or attempted to use at Arch, any confidential or proprietary information or trade secrets of Hartford.

## SIXTH AFFIRMATIVE DEFENSE

The Individuals' conduct has been consistent with any of their legal obligations to Hartford.

## SEVENTH AFFIRMATIVE DEFENSE

As Hartford is aware, it employed the Individuals at will, and they were not (and are not) subject to restrictive covenants. The complaint violates public policy by attempting to restrain freedom of employment and competition.

## EIGHTH AFFIRMATIVE DEFENSE

Hartford's claims are barred, in whole or in part, because the Individuals acted in good faith and/or without the requisite wrongful intent.

## NINTH AFFIRMATIVE DEFENSE

The complaint should be dismissed, in whole or in part, because Hartford has not sustained any legally cognizable injuries or damages by reason of any of the acts of the Individuals alleged in the complaint, but rather from factors unrelated to and not caused by the Individuals.

## TENTH AFFIRMATIVE DEFENSE

The complaint should be dismissed, in whole or in part, because any damages that Hartford allegedly suffered are not attributable to the Individuals, but rather, are the result of, among other things, Hartford's own actions, misconduct, culpable conduct, negligence, or contributory negligence. To the extent that Hartford has sustained injuries, they are not attributable to the Individuals, but rather, they are due to, among other things, declines in Hartford's ratings; its tenuous financial condition; the performance of its investment portfolio, which relative to its peers was disproportionately poor; and the failings in various of its businesses and products, such as variable annuities linked to the equity markets and bearing guaranteed returns.

## ELEVENTH AFFIRMATIVE DEFENSE

Hartford's damages, if any, should be reduced by the amount of compensation that it has withheld or will withhold, in either event wrongfully, from the Individuals, including (without limitation) amounts that it owes or shall owe to any of the Individuals pursuant to the Hartford Financial Products Annual Cash Incentive & Profit Contribution Plan, the 2007 Hartford Financial Products Annual Cash Incentive & Profit Contribution Plan, The Hartford Performance Unit Plan, and The Hartford 2005 Incentive Stock Plan.

## TWELFTH AFFIRMATIVE DEFENSE

Hartford has failed to mitigate its damages, if any.

## THIRTEENTH AFFIRMATIVE DEFENSE

If Hartford has been damaged, then it has adequate remedies at law.

## FOURTEENTH AFFIRMATIVE DEFENSE

The complaint should be dismissed, in whole or in part, because Hartford has not sustained any legally cognizable injuries or damages. Hartford foresees the same earnings for 2009 as it foresaw before the Individuals left Hartford.

## FIFTEENTH AFFIRMATIVE DEFENSE

The Individuals hereby give notice that they intend to rely upon such further defenses as may become available or apparent during proceedings in this action, and the Individuals hereby reserve the right to assert such additional defenses, and further reserve their right to amend this answer as necessary to assert such additional defenses.

## COUNTERCLAIMS

The Individuals, by their attorneys Friedman Kaplan Seiler & Adelman LLP, for their counterclaims against Hartford, allege as follows:

## BACKGROUND

1. These counterclaims seek relief for Hartford's improper (a) failure and refusal to pay to the Individuals compensation that they have earned and to which they are entitled, as well as (b) failure and refusal to indemnify, and repudiation of its obligation to indemnify, the Individuals for expenses, including attorneys' fees, incurred in connection with this litigation.

2. The Individuals are former officers of Hartford. Among other things, they are former officers of plaintiff The Hartford Financial Services Group, Inc. ("Hartford Financial"), and at Hartford Financial's HFP division; in particular, Mr. McElroy is the former president, and Messrs. Rafferty and Price are former vice presidents, at HFP. In addition, Mr. McElroy served as an officer of Hartford subsidiaries -- plaintiffs Hartford Casualty Insurance Company, Hartford Insurance Company of Illinois, Hartford Insurance Company of the Midwest, Hartford Insurance Company of the Southeast, Nutmeg Insurance Company, and Twin City Fire Insurance Company

(collectively, the "Hartford Subsidiaries"); Mr. Rafferty served as an officer of Nutmeg Insurance Company and Twin City Fire Insurance Company. The Individuals were also agents of Hartford Financial and its affiliates.

3. At Hartford's request, in connection with the Individuals' decision to commence employment at Hartford in 2000, the Individuals agreed to accept below-market cash salaries while employed at Hartford, in consideration for Hartford's agreement to pay to them, in addition to those salaries, certain deferred compensation.

4. This deferred compensation was to be distributed to the Individuals under various corporate benefit plans, including the Hartford Financial Products Annual Cash Incentive & Profit Contribution Plan (the "Old Plan"), the 2007 Hartford Financial Products Annual Cash Incentive & Profit Contribution Plan (the "New Plan"), The Hartford Performance Unit Plan, and The Hartford 2005 Incentive Stock Plan (collectively, the "Deferred Compensation Plans").

5. Pursuant to the Old Plan and the New Plan, a certain percentage of the profits from business written at HFP during any given year was to be set aside and placed in an annual profit pool. A portion of this annual profit pool was to be used to fund deferred compensation awards to certain employees, including the Individuals, through the issuance of "profit contribution units." Participants were to receive cash payouts in regular installments based on the number of profit contribution units they had earned.

6. Pursuant to The Hartford Performance Unit Plan, certain Hartford employees, including the Individuals, were to receive "performance units." After a vesting period, performance units were to result in cash payments based on a per unit monetary valuation.

7. Pursuant to The Hartford 2005 Incentive Stock Plan, certain Hartford employees, including the Individuals, were to receive "restricted stock" of Hartford Financial, which could be exchanged for common stock of Hartford Financial after a designated period, as well as

"restricted stock units," each of which constituted the contractual right to receive common stock of Hartford Financial after a designated period.

8. The Deferred Compensation Plans constitute valid and binding agreements pursuant to which Hartford is obligated to pay deferred compensation to participants, including the Individuals, and to act in good faith and to deal fairly in connection with such payments.

9. For the period of 2000 through 2009, Hartford granted to each of the Individuals deferred compensation under each of the Deferred Compensation Plans, in the form of profit contribution units, performance units, restricted stock, and restricted stock units. This deferred compensation represented a significant portion of the compensation that each of the Individuals earned while employed at Hartford.

10. A portion of the deferred compensation earned by each of the Individuals was paid to him while he was employed by Hartford, in accordance with the terms of the Deferred Compensation Plans.

11. It has been, and upon information and belief continues to be for Hartford employees other than the Individuals, Hartford's long-time policy, practice, and application of the Deferred Compensation Plans that when an employee (including specifically an employee of HFP) found him/herself facing a potential material reduction in compensation – as a consequence of any factor other than poor performance – that employee is given the option, if he/she chooses not to accept such reduction, of resigning from employment with fully vested deferred compensation under the Deferred Compensation Plans, to be paid together with a severance payment.

## FIRST CAUSE OF ACTION

## BREACH OF CONTRACT - DEFERRED COMPENSATION PLANS (ON BEHALF OF DAVID McELROY)

12. Mr. McElroy repeats and re-alleges the allegations in paragraphs 1 through 11 of the counterclaims as if fully set forth herein.

13. On May 21, 2009, Mr. McElroy gave notice of his retirement to a representative of Hartford, and pursuant thereto, his last day at Hartford was June 5, 2009.

14. Pursuant to the Deferred Compensation Plans, Mr. McElroy earned, and was owed by Hartford:

(A) awards under the Old Plan;

(B) awards under the New Plan;

(C) performance units;

(D) restricted stock; and

(E) restricted stock units.

15. Pursuant to the Deferred Compensation Plans, Mr. McElroy is entitled to receive his as-yet-unpaid deferred compensation.

16. Mr. McElroy has requested that Hartford pay to him the compensation he earned and is still owed under the Deferred Compensation Plans.

17. Mr. McElroy has performed fully his obligations under these agreements.

18. Since the retirement of Mr. McElroy from Hartford, and contrary to the understandings and agreements of the parties, Hartford has failed and refused to make payment to Mr. McElroy under the Deferred Compensation Plans, which failure and refusal is in bad faith, without justification, unfair, arbitrary, discriminatory, and, upon information and belief, in retaliation for his having accepted employment at Arch.

19. Hartford's failure and refusal to make payment to Mr. McElroy under the Deferred Compensation Plans constitutes a breach of the express terms of, and the covenant of good faith and fair dealing implied into, its agreements with Mr. McElroy.

20. As a natural, direct, and proximate result of Hartford's breach of the Deferred Compensation Plans, Mr. McElroy has suffered substantial money damages in an amount to be determined. To the extent Mr. McElroy has been or will be paid a portion of this amount by Arch, he will remit to Arch an amount equivalent to that paid in damages to him by Hartford.

## SECOND CAUSE OF ACTION

## BREACH OF DUTY OF GOOD FAITH AND FAIR DEALING - DEFERRED COMPENSATION PLANS (ON BEHALF OF JOHN RAFFERTY AND MICHAEL PRICE)

21. Messrs. Rafferty and Price repeat and re-allege the allegations in paragraphs 1 through 11 of the counterclaims as if fully set forth herein.

22. Hartford applied for funding from the U.S. Treasury Department's Capital Purchase Program, part of the federal government's Troubled Assets Relief Program ("TARP"). On May 14, 2009, Hartford announced that the government preliminarily had approved Hartford's receipt of $3.4 billion in TARP monies. Final approval ultimately was granted, and TARP monies were paid to Hartford.

23. On June 2 and June 3, 2009, Hartford stated to each of Messrs. Rafferty and Price that, in order for him to remain in Hartford's employ, he was required to sign a waiver and release of all rights and claims he had against Hartford with respect to any prospective changes to his compensation or benefits that might result from Hartford's receipt of TARP monies – which changes might include prohibitions and/or further deferrals of his entitlements under the Deferred Compensation Plans. Hartford stated to each of Messrs. Rafferty and Price that he had one week,

until noon on June 10, 2009, to sign the Hartford-provided waiver or to resign, and that if he did neither, he would be terminated for cause.

24. In these circumstances, and without waiving any rights, Messrs. Rafferty and Price's last days at Hartford were June 9 and June 10, 2009, respectively.

25. Pursuant to the Deferred Compensation Plans, Mr. Rafferty earned, and was owed by Hartford:

(A) awards under the Old Plan;

(B) profit contribution units for 2007 under the New Plan;

(C) profit contribution units for 2008 under the New Plan;

(D) performance units;

(E) restricted stock; and

(F) restricted stock units.

26. Pursuant to the Deferred Compensation Plans, Mr. Price earned, and was owed by Hartford:

(A) awards under the Old Plan;

(B) profit contribution units for 2007 under the New Plan;

(C) profit contribution units for 2008 under the New Plan;

(D) performance units;

(E) restricted stock; and

(F) restricted stock units.

27. Pursuant to the Deferred Compensation Plans, Messrs. Rafferty and Price are entitled to receive their as-yet-unpaid deferred compensation.

28. Messrs. Rafferty and Price have requested that Hartford pay to them the compensation they earned and are still owed under the Deferred Compensation Plans.

29. Messrs. Rafferty and Price have performed fully their obligations under these agreements.

30. Since the departure of Messrs. Rafferty and Price from Hartford, and contrary to the understandings and agreements of the parties, and to Hartford's longstanding policy, practice, and application of the Deferred Compensation Plans, Hartford has failed and refused to make any payment to either Mr. Rafferty or Mr. Price under the Deferred Compensation Plans, which failure and refusal is in bad faith, without justification, unfair, arbitrary, discriminatory, and, upon information and belief, in retaliation for their having accepted employment at Arch.

31. Hartford's failure and refusal to make payment to Messrs. Rafferty and Price under the Deferred Compensation Plans constitutes a breach of the covenant of good faith and fair dealing implied into its agreements with Messrs. Rafferty and Price.

32. As a natural, direct, and proximate result of Hartford's breach, Messrs. Rafferty and Price have suffered substantial money damages in an amount to be determined. To the extent Messrs. Rafferty and Price have been or will be paid portions of these amounts by Arch, they will remit to Arch an amount equivalent to that paid in damages to them by Hartford.

## THIRD CAUSE OF ACTION

## BREACH OF CONTRACT – BY-LAWS (ON BEHALF OF DAVID McELROY, JOHN RAFFERTY, AND MICHAEL PRICE)

33. The Individuals repeat and re-allege the allegations in paragraphs 1 through 11 of the counterclaims as if fully set forth herein.

34. Pursuant to Sections 4.1(a) and 4.6 of the Amended and Restated By-Laws of Hartford Financial (the "By-Laws"), Hartford Financial is obligated, among other things, to indemnify, to the fullest extent permitted by law, each of its former officers, employees, or agents involved in any litigation by reason of the fact that he or she was an officer, employee, or agent of

Hartford Financial. The indemnification covers all expenses, including attorneys' fees, actually and reasonably incurred in connection with litigation.

35. Pursuant to Sections 4.1(a), 4.5(d)(ii), and 4.6 of the By-Laws, Hartford Financial is obligated, among other things, to indemnify, to the fullest extent permitted by law, each of its former officers, employees, or agents involved in any litigation by reason of the fact that he or she was an officer, employee, or agent of a "Covered Entity." A "Covered Entity" is defined in the By-Laws as any entity (other than Hartford Financial) of which each such person was serving as an officer, employee, agent, director, or fiduciary at the request of Hartford Financial. The indemnification covers all expenses, including attorneys' fees, actually and reasonably incurred in connection with litigation.

36. The Hartford Subsidiaries are Covered Entities, within the meaning of the By-Laws.

37. Pursuant to Sections 4.4 and 4.6 of the By-Laws, each person to be indemnified thereunder is entitled to receive, from time to time, advance payment of any indemnifiable expenses.

38. Upon information and belief, each Hartford Subsidiary is governed by by-laws containing provisions substantially similar or identical to Article 4 of the By-Laws, including Sections 4.1(a), 4.4, 4.5(d)(ii) and 4.6, thereof.

39. The Individuals served as officers of HFP and of the Hartford Subsidiaries, and as agents of Hartford Financial and its affiliates, at the request of Hartford Financial.

40. Hartford alleges that by reason of the Individuals' former relationships with Hartford, they owed fiduciary and other duties to Hartford; that they breached those duties in connection with their commencement of employment with Arch; and that those purported breaches damaged Hartford. In connection with those allegations, Hartford seeks from the Individuals the

return of all compensation earned during the period of their alleged disloyalty to Hartford, as well as many millions of dollars in compensatory damages, and punitive damages.

41. Under the By-Laws, and upon information and belief under the by-laws governing the Hartford Subsidiaries, Hartford is obligated to indemnify the Individuals by paying their costs and expenses incurred in connection with this litigation, and to act in good faith and to deal fairly in connection with such indemnification.

42. The Individuals have requested that Hartford so indemnify them, and each of the Individuals has provided to Hartford an undertaking in which he commits to repay the amounts so advanced by Hartford, if it should ultimately be determined that he is not entitled to payments.

43. Contrary to the understandings and agreements of the parties, Hartford has failed and refused to indemnify, and has repudiated its obligation to indemnify, the Individuals, which failure, refusal, and repudiation is in bad faith, without justification, unfair, arbitrary, and, upon information and belief, in retaliation for the Individuals having accepted employment at Arch.

44. Hartford's failure and refusal to indemnify, and repudiation of its obligation to indemnify, the Individuals constitutes a breach of the express terms of, and the covenant of good faith and fair dealing implied into, the By-Laws, and, upon information and belief, the by-laws that govern the Hartford Subsidiaries.

45. As a natural, direct, and proximate result of Hartford's breach of the By-Laws and, upon information and belief, of the by-laws that govern the Hartford Subsidiaries, the Individuals have suffered substantial money damages in an amount to be determined.

## FOURTH CAUSE OF ACTION

## UNJUST ENRICHMENT
## (ON BEHALF OF DAVID McELROY, JOHN RAFFERTY, AND MICHAEL PRICE)

46. The Individuals repeat and re-allege the allegations in paragraphs 1 through 45 of the counterclaims as if fully set forth herein.

47. Hartford's failure to honor its obligations to the Individuals under the Deferred Compensation Plans, the By-Laws, and upon information and belief, under the by-laws governing the Hartford Subsidiaries, has resulted, and will result, in the unjust enrichment of Hartford at the expense of the Individuals.

48. The circumstances are such that in equity and good conscience, Hartford should be required to pay the Individuals all deferred compensation owed to them, and to indemnify them.

## PRAYER FOR RELIEF

WHEREFORE, the Individuals pray that judgment be awarded in their favor and against Hartford as follows:

(A) Dismissing the complaint in its entirety as against the Individuals, with prejudice, and denying all relief therein sought;

(B) Awarding the Individuals compensatory damages and indemnification on the counterclaims in an amount to be proven;

(C) Awarding the Individuals attorneys' fees, costs and disbursements incurred in the defense of this action and the prosecution of the counterclaims; and

(D) Such other and further relief as the Court may deem just and proper.

Dated: New York, New York
July 16, 2010

FRIEDMAN KAPLAN SEILER & ADELMAN LLP

By: _____

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*Attorneys for David McElroy, John Rafferty, and Michael Price*

SUPREME COURT OF THE STATE OF NEW YORK
COUNTY OF NEW YORK

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| TWIN CITY FIRE INSURANCE COMPANY, HARTFORD INSURANCE COMPANY OF ILLINOIS, HARTFORD INSURANCE COMPANY OF THE MIDWEST, TRUMBULL INSURANCE COMPANY, HARTFORD INSURANCE COMPANY OF THE SOUTHEAST, NUTMEG INSURANCE COMPANY, PROPERTY AND CASUALTY INSURANCE COMPANY OF HARTFORD, HARTFORD FIRE INSURANCE COMPANY, HARTFORD CASUALTY INSURANCE COMPANY, HARTFORD ACCIDENT AND INDEMNITY INSURANCE COMPANY, HARTFORD UNDERWRITERS INSURANCE COMPANY, PACIFIC INSURANCE COMPANY, LIMITED, and THE HARTFORD FINANCIAL SERVICES GROUP, INC.<br><br>Plaintiffs,<br><br>-against-<br><br>ARCH INSURANCE GROUP, INC., ARCH CAPITAL GROUP LTD., DAVID McELROY, JOHN RAFFERTY and MICHAEL PRICE,<br><br>Defendants. | Index No. 602062/09<br><br>Lowe, J.S.C<br><br>Motion Seq. No. 003<br>Document Number 38 |

**MEMORANDUM OF LAW IN SUPPORT OF PLAINTIFFS' MOTION TO DISMISS THE INDIVIDUAL DEFENDANTS' FIRST, SECOND AND FOURTH COUNTERCLAIMS AND TO DISMISS IN THEIR ENTIRETY ARCH'S COUNTERCLAIMS**

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Plaintiffs respectfully submit this memorandum of law in support of their motion, pursuant to CPLR §§ 3211(a)(1) and (7), to dismiss in part the counterclaims of David McElroy, John Rafferty, and Michael Price and in their entirety the counterclaims of Defendants Arch Capital Group, Inc. and Arch Capital Group Ltd. against them.

## Preliminary Statement

In early 2009, Defendant David McElroy was the head of Hartford Financial Products ("HFP"), a division of The Hartford Financial Services Group Inc.'s family of companies and affiliates ("The Hartford"). HFP was a very profitable division and McElroy was among the most highly compensated individuals in Plaintiffs' entire management structure, earning millions of dollars a year. Apparently unhappy with his multi-million dollar compensation package, however, McElroy began looking for a new home—not just for himself, but for Plaintiffs' entire HFP division and the hundreds of millions of dollars in premiums it represented. Internal emails reveal that McElroy, while still employed by Plaintiffs, was secretly meeting with the senior management of Arch and other competitors and conducting a private auction for The Hartford's HFP business. In these discussions he was quite explicit that he intended to bring his entire senior management team and as much of the business as possible with him.

Thus, on June 5, 2009, McElroy "retired" as President of HFP and three days later he was named President of the newly-formed "Financial and Professional Liability Group" at Arch Insurance Group, Inc., a subsidiary of Arch Capital Group, Ltd. (collectively, "Arch"). What followed was one of the largest raids in corporate history: within weeks of McElroy's "retirement", 64 employees—more than 25 percent of HFP's workforce and virtually all of HFP's senior management—had left HFP. During that period, HFP employees were bombarded with direct solicitations from Arch; HFP clients and prospects were shamelessly misappropriated

(after being told that HFP "would not exist" in the future); and a significant amount of HFP's intellectual capital—including contacts, customer information, pricing, renewal dates, policy innovations and business plans—was simply transferred wholesale, for no consideration, to Arch. McElroy and Arch attacked all levels of HFP, and also timed the raid to coincide with the renegotiation of HFP's vital reinsurance treaties—contracts essential to HFP's ability to place and retain business.

Shortly after the raid, The Hartford and several of its underwriting affiliates sued Arch, McElroy and two of his co-conspirators, John Rafferty and Michael Price (collectively, the "Individual Defendants"). Arch and the Individual Defendants filed answers without counterclaims and did not move to dismiss.

Now, however, Arch and the Individual Defendants have amended their answers to assert certain alleged counterclaims. Incredibly, the thrust of their claims is that, notwithstanding their efforts to cripple The Hartford, the Individual Defendants would like to collect their bonuses. These claims fail for multiple independent reasons.

*First,* the operative plans specifically state that awards of incentive compensation are discretionary, and McElroy himself repeatedly confirmed, in writing, that no employee had any right to any bonus compensation until such compensation was actually paid. Given the astonishing breaches of fiduciary duty and other malfeasance of the Individual Defendants, it is hardly surprising that The Hartford exercised its discretion not to award them post-employment incentive compensation.

*Second,* payment under the operative plans is tied to continued employment. Because Individual Defendants Rafferty and Price *resigned*, they were not eligible to receive bonus compensation in the first place, even leaving aside the issue of discretion. Rafferty and Price

suggest that they were "forced out" of HFP because—being among the 25 most highly compensated individuals in The Hartford's entire 30,000 employee workforce—The Hartford required that they execute certain federally mandated documentation relating to the Trouble Asset Relief Program ("TARP")—documentation that all other highly compensated employees were required to sign. In any event, for whatever reason, Defendants Rafferty and Price resigned. Having done so, they gave up their (non-existent) right to any bonus.

*Third*, at least according to Arch, the Individual Defendants have not suffered any damage, as they have been made whole for any lost incentive compensation as a part of their compensation from Arch in connection with the raid. *See JP Morgan Chase v. J.H. Elec. of N.Y., Inc.*, 69 A.D.3d 802, 803, 893 N.Y.S.2d 237, 239 (2d Dep't 2010) (damages are a necessary element of an action for breach of contract).

*Fourth*, to the extent that *Arch* attempts to make out a claim for some kind of payment under the bonus plans, such a claim is not cognizable. Arch's argument appears to be, in various guises, that it has been forced to make the Individual Defendants whole for their lost Hartford incentive compensation. Leaving aside the fact that Arch could have avoided this problem by not engineering a massive and improper raid in the first place or committing to an employment package that would reward the Individual Defendants in the likely event they did not receive their discretionary compensation from the employer they had just attempted to undermine, Arch asserts no relationship between it and The Hartford that would make The Hartford liable for Arch's compensation decisions regarding its employees. *See Board of Educ. v. Sargent, Webster, Crenshaw & Folley*, 71 N.Y.2d 21, 29, 523 N.Y.S.2d 475, 479 (1987) (no claim for indemnification absent allegation that claimant "was unfairly required to discharge a duty that should have been discharged by another"). Arch's claim that The Hartford is somehow

responsible for whatever "make whole" provisions it negotiated with its inside men at The Hartford is entirely without legal basis. It and the other counterclaims relating to incentive compensation should be dismissed.

## Background

### A. The HFP Business and the Individual Defendants' Employment at The Hartford

The Hartford Financial Products business was purchased for a substantial premium by The Hartford in 2000 from Reliance Group Holdings, where the business at the time of The Hartford's purchase had approximately $295 million in premiums in force. (Kramarsky Aff. Ex. A ¶ 33). The senior leadership team at Reliance—including all of the Individual Defendants—joined The Hartford. McElroy was hired to lead the HFP division[1] (*Id.* ¶ 35), and Rafferty and Price became senior managers at HFP. (*Id.* ¶ 36). Throughout their tenure at HFP, the Individual Defendants received substantial compensation. (*Id.* ¶ 38). For example, McElroy's 2008 compensation was millions of dollars and each of the Individual Defendants was among the 25 most highly compensated of The Hartford's 30,000 employees. From 2000 to 2009 HFP's business more than doubled, with approximately $720 million in premiums in force. (*Id.* ¶ 33). During that time, many new clients and client contacts were developed; new and innovative insurance products and policies were developed; and HFP ultimately became an extremely important and profitable division of The Hartford. (*Id.* ¶ 41).[2]

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[1] HFP is the trade name of the underwriting unit of the Property & Casualty companies of The Hartford that provide management and professional liability coverage. HFP is not an independent legal entity, and thus any "title" assigned to the Individual Defendants in connection with HFP does not reflect a corporate officer position.

[2] The recent severe downturn in the financial markets negatively affected diversified insurance companies, such as The Hartford, beginning primarily in late 2008. In 2009, The Hartford applied for assistance under the federal government's Troubled Asset Relief Program ("TARP") and received approval for a $3.4 billion TARP loan. The Hartford has now repaid that loan in full.

### B. Arch and the Individual Defendants Conspire to Raid HFP

On June 5, 2009, Defendant David McElroy announced his "retirement" as President of HFP. (*Id.* ¶ 56). Yet, on June 8, 2009—the first business day following his so-called retirement—he was named President of the newly formed Financial and Professional Liability Group at Arch. (*Id.* ¶ 60). McElroy had been in contact with Arch executives for some time about leaving The Hartford and taking the entire HFP business with him. (*Id.* ¶ 50). Indeed, on June 3, 2009—before McElroy had even left HFP—Arch announced internally that McElroy would be joining Arch. (*Id.* ¶ 58). Defendants John Rafferty and Michael Price resigned from HFP within days of McElroy and followed him to Arch. (*Id.* ¶ 60). The weeks that followed saw a raid of HFP's workforce—over 60 employees left to join Arch, more than 25 percent of HFP workforce and virtually all of HFP's senior management.

During this time, the Individual Defendants and others brazenly solicited HFP employees to join Arch. (*Id.* ¶¶ 62-63). These solicitations—often made by the Individual Defendants personally—quickly degenerated into threats, conveyed orally and by text and email that, in sum, HFP would soon cease to exist. (*Id.* ¶¶ 64-65). HFP employees were also told that if they did not move to Arch immediately, the job offer would no longer be available. (*Id.* ¶ 64). To facilitate the raid, the Arch Human Resources Department phone number was circulated at HFP; "leavers" told other HFP employees what to tell Arch Human Resources; and offers of employment at Arch—usually and notably on the same terms and conditions as the employee had at HFP, down to the number of vacation days—promptly followed.

Arch and McElroy also agreed that in order to successfully develop the specialty business at Arch—a business Arch wanted, but was unwilling to pay for—the *entire* business would need to be moved from The Hartford (*id.* Ex. A ¶¶ 51-52), and they would need to cripple HFP by

stripping it of its personnel, taking its clients, damaging its reputation in the industry and attempting to undermine its critical reinsurance contracts. (*Id.* ¶ 53). For example, several banks and/or brokers were told that The Hartford would not be able to service its business so the client should transition to Arch. (*Id.*). In at least one case, Arch actually paid the client directly to transition its business to Arch. In addition, the Individual Defendants have systematically misused The Hartford's confidential information that they took when they resigned to solicit clients and personnel of The Hartford and develop their new group at Arch. (*Id.* ¶ 54).

**C. Litigation Ensues**

***1. The Complaint***

On July 2, 2009, Plaintiffs filed suit against Arch and the Individual Defendants seeking injunctive relief and damages arising out of Defendants' misuse of confidential information, raid of HFP employees and interference with client relationships, as well as the Individual Defendants' breaches of their fiduciary duties and Plaintiffs' Confidentiality Agreements and Code of Ethics. Defendants answered the Complaint on August 14, 2009.

***2. Plaintiffs Determine Not to Issue Discretionary Bonus Compensation to the Individual Defendants***

In March 2010, Plaintiffs distributed annual discretionary bonus compensation and stock incentives pursuant to the HFP bonus program ("Bonus Plan"), The Hartford Incentive Stock Plan ("Stock Plan") and The Hartford Performance Unit Plan ("PU Plan") (collectively, the "Plans"). Pursuant to the terms of the Plans, no discretionary payments were made to the Individual Defendants.

***3. The Answers and Counterclaims***

On July 16, 2010, the Individual Defendants filed counterclaims seeking discretionary bonus compensation and indemnification and advancement of legal fees. (Kramarsky Aff. Ex.

B). Arch filed its answer the same day and counterclaimed for the same damages sought by the Individual Defendants—namely, anticipated payments under the Plans and legal fees—under theories of indemnification and unjust enrichment. (*Id.* Ex. C). Arch alleges that the Individual Defendants' employment agreements with Arch provide for cash payments equal to the amounts they anticipated under the Plans in the event that no compensation is actually paid by Plaintiffs. (*Id.* Counterclaims ¶ 143). Arch further alleges that it is advancing the Individual Defendants' legal expenses in this litigation. (*Id.* ¶ 163). Arch seeks to recover from Plaintiffs the amounts it has elected to pay to the Individual Defendants.[3]

## Argument

### I. STANDARD FOR MOTION TO DISMISS UNDER CPLR §§ 3211(a)(1) and (7)

CPLR § 3211(a)(1) permits "[a] party [to] move for judgment dismissing one or more causes of action asserted against him on the ground that a defense is founded upon documentary evidence". *Id.*; *Gephardt v. Morgan Guar. Trust Co.*, 191 A.D.2d 229, 229, 594 N.Y.S.2d 248, 249 (1st Dep't 1993) ("It is well settled that a defense based on documentary evidence can succeed if the documents submitted resolve all of the factual issues as a matter of law."). Similarly, pursuant to CPLR § 3211(a)(7), a party may move to dismiss "one or more causes of action asserted against him on the ground that the pleading fails to state a cause of action". *Id.*; *see also Beattie v. Brown & Wood*, 243 A.D.2d 395, 395, 663 N.Y.S.2d 199, 199 (1st Dep't 1997) (affirming dismissal where factual claims were "flatly contradicted by documentary evidence"). In deciding a motion to dismiss, "bare legal conclusions and factual claims, which are either inherently incredible or flatly contradicted by documentary evidence" are not

[3] The present motion is directed at all of Arch's counterclaims and the Individual Defendants' claims for incentive compensation. The Individual Defendants' indemnification and advancement claims are also entirely without merit and Plaintiffs will address them at an appropriate time.

presumed to be true or accorded every favorable inference. *O'Donnell, Fox & Gartner, P.C. v. R-2000 Corp.*, 198 A.D.2d 154, 154, 604 N.Y.S.2d 67, 68 (1st Dep't 1993).

Here the plain language of the relevant Plans and the applicable law mandate that the Individual Defendants' counterclaims under the Plans and all of Arch's counterclaims must be dismissed. The Individual Defendants' claims to further compensation under the Plans are flatly contradicted by the Plans themselves, whose language explicitly vests discretion regarding payments in Plaintiffs' board and management. Arch's claims for indemnification from Plaintiffs are without a factual, legal or commonsense basis and must also be dismissed.

## II. THE INDIVIDUAL DEFENDANTS HAVE NO RIGHTS TO AWARDS UNDER THE PLANS

In their first, second and fourth counterclaims, McElroy, Rafferty and Price seek further compensation from Plaintiffs under three types of unambiguously discretionary bonus compensation plans: the Bonus Plan, Stock Plan and PU Plan. Specifically, McElroy alleges breach of the terms of these Plans and breach of the implied covenant of good faith and fair dealing (Kramarsky Aff. Ex. B Counterclaims ¶ 19), and Rafferty and Price allege breach of the implied covenant of good faith and fair dealing with respect to the Plans (*id.* ¶¶ 25, 26). But the plain language of each of the Plans precludes recovery: New York law is clear that employees have no claim to payment under a bonus or discretionary compensation plan. The Individual Defendants' first and second counterclaims must be dismissed.

### A. Interpretation of the Plans Is Appropriate on a Motion to Dismiss

It is well settled that the interpretation of a contract is a question of law that the Court may determine on a motion to dismiss. *See 805 Third Ave. Co. v. M. W. Realty Assocs.*, 58 N.Y.2d 447, 451, 461 N.Y.S.2d 778, 780 (1983) ("Interpretation of the contract is a legal matter for the court") (citations omitted). This is equally true when the contracts at issue are bonus or

discretionary compensation plans. "An employee's entitlement to a bonus is governed by the terms of the employer's bonus plan." *Hall v. United Parcel Serv. of Am.*, 76 N.Y.2d 27, 36, 556 N.Y.S.2d 21, 27 (1990). Accordingly, where "bonus compensation" sought is "purely discretionary", courts decide such questions as a matter of law. *Kaplan v. Capital Co. of Am. LLC*, 298 A.D.2d 110, 111, 747 N.Y.S.2d 504, 505 (1st Dep't 2002).

**B. The Plans Are Fully Discretionary**

"The rule with respect to bonuses is that an employee's entitlement to a bonus is governed by the terms of the employer's bonus plan." *Brennan v. J.P. Morgan Sec., Inc.*, 7 Misc. 3d 1013(A), 801 N.Y.S.2d 230, 2004 WL 3314910, at *2 (Sup. Ct. N.Y. Co. Aug. 31, 2004) (Lowe, J.) (*citing, inter alia, Hall*, 76 N.Y.2d at 36, 556 N.Y.S.2d at 27). Thus, "where the employee has already earned compensation under the terms of his employment contract, his termination does not affect his rights to that compensation, but where the employer retains discretion to award a bonus (or other compensation), no forfeiture of earned wages occurs if the bonus is not paid." *Vetromile v. JPI Partners, LLC*, --- F. Supp. 2d ---, 2010 WL 1529246, at *4 (S.D.N.Y. Mar. 30, 2010) (citations omitted); *see also Aquavella v. Viola*, No. 2002/06929, 13 Misc. 3d 1234(A), 831 N.Y.S.2d 353, 2006 WL 3232167, at *7 (Sup. Ct. Monroe Co. Sept. 25, 2006) (distinguishing between "a discretionary bonus or [compensation] otherwise payable at the discretion of the employer" and "earned wages or salary subject to the long standing policy against the forfeitures of normal wages") (internal quotation marks omitted)), *aff'd as modified*, 39 A.D.3d 1191, 834 N.Y.S.2d 808 (4th Dep't 2007). Each of the Plans is a bonus or discretionary compensation plan and contains explicit and unequivocal language to that effect.

### *1. The Bonus Plan*

The Bonus Plan is, by its terms, the epitome of a discretionary compensation plan. (*See* Kramarsky Aff. Ex. D).[4] The Plan establishes a "bonus pool" tied to HFP's revenues from which managers could authorize bonus compensation to eligible and meritorious employees employed at the time of distribution. (*Id.* Ex. D at 6-10; Ex. E at 2-3; Ex. F at 4). Each iteration of the Bonus Plan has explicitly and repeatedly emphasized that payments under the Bonus Plan are entirely discretionary. In the initial Bonus Plan, which is peppered with unequivocal language establishing HFP's discretion (*see, e.g.*, Kramarsky Aff. Ex. D at 4 ("Some percentage of employees will receive zero awards"); *id.* at *2 ("The Incentive Programs reviewed in this presentation are discretionary incentive plans. . . . These plans may be modified or cancelled at anytime [*sic*] without prior notice.")),[5] HFP explicitly reserved the rights to deny any eligible employee payment under the Plan and to eliminate the Plan entirely:

> Hartford management retains full control over decisions regarding interpretation of formulas, results and eligibility under this program. Although employees are eligible for periodic updates, *no one is entitled to any payment.*
>
> The Hartford retains full control to change, amend, alter or terminate this bonus program at any time. This may apply to all participants or a subset as defined by management.

(*Id.* at 18 (emphasis added)). The 2007 iteration of the Bonus Plan contains similar language:

> Participation in the HFP Plan neither constitutes a guarantee of employment nor a guarantee of award for the entire Plan year or any specific time period. The Company reserves the right to revise or terminate the HFP Plan at any time, with or without advance notice.

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[4] Exhibit D is comprised of two series of numbered pages. Pages from the latter series will be cited: *[page number].

[5] (*See also* Kramarsky Aff. Ex. D at 2 ("Individual bonus awards will be based on your manager's assessment of your performance"); *id.* at *11 ("Actual ratio of units to dollars earned in annual incentive plan at management discretion"); *id.* at *15 ("issuance of units [in annual profit pool] . . . are at management discretion and contingent on satisfactory performance")).

[redacted]

Plan); *id.* at 4 ("management discretion may be applied in establishing the pool"); *id.* ("Actual awards from the annual incentive plan may range from zero to two (2) times the participant's annual target award dollars."); *id.* at 5 ("The decision relative to the actual ratio of units issued to dollars earned under the annual cash incentive plan is at management discretion."); *id.* at 7 ("there is no implied or specific guarantee of future value of each unit at the time of issuance"); *id.* at 9 ("All incentive awards under this program are entirely discretionary.")).

> Awards under the Profit Contribution component of the HFP plan ***are not earned*** at the time the units are initially distributed. Rather, to encourage employee retention **and** to ensure that the distributed annual profit pool most accurately reflects the real performance of the business, awards under the Profit Contribution Plan are not earned until payout is made.

(*Id.* at 7 (emphasis in original)).

### 2. *The Stock Plan*

The Stock Plan was established in 2005 "to motivate and reward superior performance on the part of Key Employees" of The Hartford. (*Id.* Ex. G at 1). To that end, the Stock Plan invests the Compensation and Personnel Committee of the Board (the "Committee") with the authority to provide "incentive awards" in the form of options, stock appreciation rights, performance shares, restricted stock, restricted units, or any combination of these—"as the Committee may determine" (*id.* at 1)—to Key Employees, defined as "Eligible Employee[s] . . . whose responsibilities and decisions, in the judgment of the Committee, directly affect the performance of the Company and its subsidiaries." (*Id.* at 3). The Stock Plan's terms reinforce throughout the Committee's absolute authority to determine the recipients, the make-up and the terms of any award that is granted. (*See, e.g.*, *id.* at 1 ("Awards will be made, in the discretion of the Committee"); *id.* at 3, 5 (definitions of "Fair Market Value", "Key Employee", "Restricted Stock", "Restricted Unit", "Restriction Period" and "Total Disability" subject to Committee's judgment); *id.* at 7 (Committee shall designate employees to whom awards will be granted, determine the form(s) of award to be granted, determine the number of shares of stock subject to each award and determine the terms and conditions of each award); *id.* at 22 ("All decisions, determinations or actions of the Committee made or taken pursuant to grants of authority under the Plan shall be made or taken in the sole discretion of the Committee and shall be final,

conclusive and binding on all persons for all purposes.")). A revised Stock Plan, effective January 1, 2009, retains this language. (*See id.* Ex. H).

### 3. *The PU Plan*

Finally, the PU Plan provides the same Committee absolute discretion "to motivate and reward superior performance on the part of Key Employees" by awarding performance units payable in cash. (*Id.* Ex. I at 2). The language of the PU Plan tracks closely that of the Stock Plan, leaving no doubt that awards, if made, will be granted at the Committee's sole discretion. (*See, e.g., id.* at 3 ("Eligible Employee" defined as holding a position "at a level determined by the Committee"); *id.* at 5 ("Key Employee" defined as "Eligible Employee . . . whose responsibilities and decisions, in the judgment of the Committee, directly affect the performance of the Company and its subsidiaries"); *id.* at 13 ("The Committee shall have full power, discretion and authority to interpret, construe and administer the Plan and any part thereof in any manner deemed appropriate in its sole discretion, and its interpretations, constructions, and other determinations and actions taken hereunder shall be, except as otherwise determined by the Board, final, conclusive and binding on all persons for all purposes.")).

Thus, Plaintiffs' management retained complete discretion with respect to the Plans. The Plans provide for awards the issuance of and amounts of which are entirely discretionary and tied to both the performance of the company and assessment of the performance of the employee. This language is functionally identical to that at issue in *Namad v. Salomon Inc.*, the seminal Court of Appeals case concerning the interpretation of incentive compensation clauses, which held that, where such a clause provides that "[t]he amounts of other compensation entitlements, if any, including regular bonuses, special bonuses and stock awards, shall be at the discretion of management", the clause "unambiguously vests discretion regarding the amount of bonus

compensation to be awarded in defendants' management." 74 N.Y.2d 751, 752-53, 545 N.Y.S.2d 79, 80 (1989). Indeed, *Namad* makes it clear that courts require far less emphatic language than that present in the Plans to establish management's complete discretion over a bonus or discretionary compensation plan. *See also Miller v. Hekimian Laboratories, Inc.*, 257 F. Supp. 2d 506, 510, 514 (N.D.N.Y. 2003) (clause providing that "[t]he Employee's participation in other benefits or incentive payments shall be at the discretion of the Board of Directors or the President of the Corporation or his designee" "unambiguously vest[ed] discretion" regarding incentive payments in company's management); *Sathe v. Bank of New York*, No. 89 Civ. 6810 (LBS), 1990 WL 58862, at *1, 3 (S.D.N.Y. May 2, 1990) (plan providing that "Nothing in this Plan shall give rise to any special compensation or other sum under the Plan unless and until any such amount shall have been paid to such individual, and prior to such payment the Chairman shall have the power to revoke and nullify any and all steps previously taken towards making any award to any person" "contain[ed] clear language as to the discretionary nature of the bonus award").

### C. New York Law Is Clear That an Employee Has No Enforceable Right to Compensation Under a Discretionary Compensation or Bonus Plan

Given the explicit and unequivocal language in each of the Plans giving Plaintiffs complete discretion, the Individual Defendants' claims for compensation under the Plans must fail. It is well settled that "[a]n employee has no enforceable right to compensation under a discretionary compensation or bonus plan" *Nikitovich v. O'Neal*, 40 A.D.3d 300, 300-01, 836 N.Y.S. 2d 34, 34-35 (1st Dep't 2007); *see also Truelove v. Northeast Capital & Advisory, Inc.*, 95 N.Y.2d 220, 225, 715 N.Y.S.2d 366, 369 (2000) (employee has no vested right to discretionary bonus compensation); *Rutkowski v. Hill, Betts & Nash*, 206 A.D.2d 258, 258, 613 N.Y.S.2d 874, 875 (1st Dep't 1994); *Brennan*, 2004 WL 3314910, at *2.

This is true whether the discretionary bonus compensation at issue takes the form of cash payments (*e.g.*, *Brennan*, 2004 WL 3314910, at *3); performance units (*e.g.*, *Markby v. PaineWebber Inc.*, 169 Misc. 2d 173, 180, 650 N.Y.S.2d 950, 954 (Sup.Ct. N.Y. Co. 1996)); or restricted stock or options to purchase restricted stock. *See, e.g.*, *id.*, 650 N.Y.S.2d at 954; *Welland v. Citigroup, Inc.*, No. 00 Civ. 738 (NRB), 2003 WL 22973574, at *12 (S.D.N.Y. Dec. 17, 2003) (former employee had no right to restricted stock where agreements provided employer full discretion to determine whether stocks would be forfeited upon employee's termination). This Court's decision in *Brennan* is particularly on point. As here, Brennan sought to recover bonus compensation from his former employer under, *inter alia*, contract and quasi-contract theories. *Brennan*, 2004 WL 3314910, at *1. Like Plaintiffs' Plans, the incentive compensation plan at issue in *Brennan* explicitly provided that awards would be based on the performance of both the employee and his team and distributed from a bonus pool at the discretion of the employer. *Id.* at *3. Also like Plaintiffs' Plans, the *Brennan* plan warned that an employee had no rights under the bonus plan. *Id.* This Court held that the plan "unambiguously provides that the employer has the discretionary authority to decide if and how much the employee is to be paid" and accordingly dismissed Brennan's claims and denied his cross-motion to amend the complaint. *Id.* at *3, 4.

Thus, McElroy cannot claim that The Hartford's decision, within its discretion, not to issue to him any additional compensation under the Plans constitutes a breach of contract. *See Kaplan v. Capital Co. of Am. LLC*, 298 A.D.2d 110, 111, 747 N.Y.S.2d 504, 505 (1st Dep't 2002) ("The court properly dismissed plaintiff's breach of contract claims since he had no contractual right to bonuses" "clearly stated in the company handbook to be purely discretionary"); *Arrouet v. Brown Bros. Harriman & Co.*, No. 02 Civ. 9061 (TPG), 2005 WL

646111, at *4 (S.D.N.Y. Mar. 18, 2005) ("An employee cannot establish that an employer breached a contract to pay a particular amount of bonus compensation where the employer retains discretion regarding the amount of bonus compensation to be awarded.") (citations omitted); *Welland*, 2003 WL 22973574, at *12; *see also Miller*, 257 F. Supp. 2d at 514 (where provision of employment agreement "unambiguously vests discretion" regarding incentive payments in company's management, the court cannot amend the employment agreement in such a way as to deny management that discretion).

Nor can McElroy dress up the same claim as one for breach of the implied covenant of good faith and fair dealing. (Kramarsky Aff. Ex. B Counterclaims ¶ 19). Such a claim fails for all the reasons set forth above, and also must be dismissed as it is duplicative of the claim for breach of contract. *See Amcan Holdings, Inc. v. Canadian Imperial Bank of Commerce*, 70 A.D.3d 423, 426, 894 N.Y.S.2d 47, 49-50 (1st Dep't 2010) ("The claim that defendants breached the implied covenant of good faith and fair dealing was properly dismissed as duplicative of the breach-of-contract claim, as both claims arise from the same facts and seek the identical damages for each alleged breach.").

Notably, Defendants Rafferty and Price do not even *attempt* to assert a breach of contract claim because the Plans unambiguously cut off any right to bonus compensation for employees who voluntarily resign, which they are forced to admit they did. (Kramarsky Aff. Ex. B Counterclaims ¶¶ 23-24, Answer ¶ 60). Instead they attempt to make out a claim for breach of the implied covenant of good faith and fair dealing, apparently under some theory of constructive termination. (*Id.* Counterclaims ¶ 19, Answer ¶ 60). Under New York law, such a claim requires that Rafferty and Price assert that The Hartford, by requiring its top 25 mostly highly compensated employees to sign TARP waivers, "intentionally create[d] a work atmosphere so

intolerable" that no reasonable person could remain employed there under those conditions. *Nugent v. St. Lukes-Roosevelt Hosp. Ctr.*, 303 Fed. Appx. 943, 945 (2d Cir. 2008). Leaving aside the absurdity of this assertion as a matter of fact, such a claim simply fails as a matter of law. "An employee has no enforceable right to compensation under a discretionary compensation or bonus plan and, accordingly, a forfeiture of such compensation does not occasion a cause of action for breach of the implied covenant of good faith and fair dealing." *Nikitovich*, 40 A.D.3d at 300-01, 836 N.Y.S.2d at 34-35; *see also Kaplan*, 298 A.D.2d at 111, 747 N.Y.S.2d at 506 (where plaintiff had "no contractual right to a bonus", he could not recover in quantum meruit or under other enumerated theories); *Sathe*, 1990 WL 58862, at *4 (finding no good faith requirement where employer possessed the discretion to give no bonus at all). Indeed, this is self-evident given that the Plans do not support a breach of contract claim. *Nikitovich*, 40 A.D.3d at 300-01, 836 N.Y.S. 2d at 35 ("A claim for breach of the implied covenant of fair dealing cannot substitute for an unsustainable breach of contract claim.").

### D. The Individual Defendants Have Alleged No Damages in Support of Their Claims Concerning the Plans

The Answers of both the Individual Defendants and Arch admit that Arch has committed in its employment agreements with the Individual Defendants to pay them "cash payments" "equal to the amounts, if any, he or she would have received" from Plaintiffs under the Plans. (Kramarsky Aff. Ex. B Counterclaims ¶ 143). As a result, none of the Individual Defendants will suffer any damages as a result of Plaintiffs' determination not to award them discretionary incentive compensation. Because an allegation of damages is a necessary element of both a breach of contract claim and a claim for breach of the implied covenant of good faith and fair dealing (*see JP Morgan Chase v. J.H. Elec. of N.Y., Inc.*, 69 A.D.3d 802, 803, 893 N.Y.S.2d 237, 239 (2d Dep't 2010) ("essential elements" of a breach of contract claim include "the existence

of a contract, the [claimant's] performance under the contract, the defendant's breach of that contract, and resulting damages"), the Individual Defendants' inability to allege damages provides an independent basis for dismissal. *See Wilmington Trust Co. v. Metropolitan Life Ins. Co.*, 2008 N.Y. Slip Op. 32239(U), at *10, 2008 WL 3819698 (Sup. Ct. N.Y. Co. Aug. 4, 2008) (Lowe, J.) (dismissing breach of contract claim where claimant "failed to allege any credible theory of damages").

## III. THE INDIVIDUAL DEFENDANTS' CLAIM FOR UNJUST ENRICHMENT IS PRECLUDED BY THE EXISTENCE OF A VALID CONTRACT

The Individual Defendants' claims grounded in unjust enrichment are duplicative of their claims under the Plans and the Plaintiffs' by-laws and must therefore be dismissed. "The existence of a valid and enforceable written contract governing a particular subject matter precludes recovery in quasi-contract or unjust enrichment for occurrences or transactions arising out of the same matter." *Eagle Comtronics, Inc. v. Pico Prods., Inc.*, 256 A.D.2d 1202, 1202-03, 682 N.Y.S.2d 505, 506 (4th Dep't 1998) (*citing Clark-Fitzpatrick, Inc. v. Long Is. R. R. Co.*, 70 N.Y.2d 382, 388-89, 521 N.Y.S.2d 653, 656 (1987)); *see also Johnson v. Stanfield Capital Partners, LLC*, 68 A.D.3d 628, 629, 891 N.Y.S.2d 383, 385 (1st Dep't 2009) ("[a]s the parties' relationship is governed by a contract, plaintiff may not recover [bonus compensation] under quasi-contractual theories") (citation omitted). There is no dispute that the Plans and the Plaintiffs' by-laws are enforceable; the parties simply disagree as to Plaintiffs' obligations thereunder. Accordingly, the Individual Defendants' fourth counterclaim fails.

Moreover, given that the Individual Defendants have no right to discretionary bonus compensation under the Plans as a matter of law, they cannot assert a viable claim for such compensation under *quantum meruit*. *See Kaplan*, 298 A.D.2d at 111, 747 N.Y.S.2d at 506.

## IV. ARCH'S COUNTERCLAIMS ARE BASELESS AND SHOULD BE DISMISSED

In its counterclaims, Arch seeks indemnification from Plaintiffs for payments it claims it is obligated to make to Individual Defendants (and Catherine Kelly[8]) purportedly due to Plaintiffs' decision not to make such payments (Kramarsky Aff. Ex. C Counterclaims ¶¶ 143-44), payment of the Individual Defendants' legal fees (*id.* ¶ 163), and, presumably in the alternative, Plaintiffs' alleged unjust enrichment as a result (*id.* ¶¶ 166, 167). But Arch's claims defy both relevant law and common sense.

### A. Arch Fails to Adequately Allege Claims for Indemnification

A claim for indemnification (in the absence of a contract, which Arch does not claim) requires a particular relationship between the claimant and the would-be indemnitor. That is, absent an express right to indemnification, an implied right to indemnification can only be found given: (1) "the special nature of a contractual relationship between parties" or (2) "a great disparity in the fault of two tortfeasors, [where] one of the tortfeasors has paid for a loss that was primarily the responsibility of the other". *Peoples' Democratic Republic of Yemen v. Goodpasture, Inc.*, 782 F.2d 346, 351 (2d Cir. 1986) (citations omitted); *see also Linwen Indus., Inc. v. Ross*, 2009 N.Y. Slip Op. 30497(U), at *5, 2009 WL 720972 (Sup. Ct. N.Y. Co. Mar. 3, 2009) (same). Neither exists here.

Arch and Plaintiffs are not linked by a special contractual relationship—or any contractual relationship at all. To the contrary, they are determined competitors. Therefore, there is no quasi-contractual basis for Arch's indemnification claims. *Compare, e.g., Linwen*, 2009 WL 720972, at *5 ("Nothing in the evidence before the court suggests the existence of a special

[8] Arch's claims with respect to Catherine Kelly—who is not a defendant in this action and asserts no claims for compensation under the Plans—are patently inappropriate.

relationship between [the parties] or the existence of a nondelegable duty, which is central to the theory of implied contractual indemnity.").

Nor has Arch asserted any grounds for an implied right to indemnification arising out of tort. There are no tort allegations in Defendants' counterclaims, nor is there any basis for a tort allegation against Plaintiffs. The counterclaims asserted by the Individual Defendants—upon which Arch's indemnification claims piggyback—are purely contractual, arising out of the Plans and the By-Laws (and are, as shown above, groundless, given the language of those agreements).[9] In any event, contract claims alone will not support a claim for indemnification. *See Lawrence Dev. Corp. v. Jobin Waterproofing, Inc.*, 186 A.D.2d 634, 636, 588 N.Y.S.2d 422, 424 (2d Dep't 1992) ("It is well settled that [indemnification and contribution] are not available in actions seeking recovery for purely economic loss resulting from the breach of contractual obligations."); *Briar Contracting Corp. v. New York*, 156 A.D.2d 628, 629, 550 N.Y.S.2d 717, 718 (2d Dep't 1989) ("absent a violation of a legal duty independent of the contract, a plaintiff is limited to his contractual remedies").

Further, Arch can allege no link between itself and Plaintiffs to support an implied right to indemnification. "[T]he key element of a common law cause of action for indemnification is not a duty running from the indemnitor to the injured party, but rather is a separate duty owed the indemnitee by the indemnitor." *Pimentel v. DeJesus*, 53 A.D.3d 401, 401, 861 N.Y.S.2d 332, 332-33 (1st Dep't 2008); *see also Kahn v. Gates Constr. Corp.*, 133 A.D.2d 141, 144, 518 N.Y.S.2d 815, 818 (2d Dep't 1987) (where "there is no duty as between the joint tort-feasors to prevent injury to the victim, there can be no right of indemnity to one from the other"); *Garrett v. Holiday Inns, Inc.*, 86 A.D.2d 469, 471, 450 N.Y.S.2d 619, 621 (4th Dep't 1982) ("an indemnity

[9] Nor can Hartford's suit to enforce its rights vis-à-vis Defendants be construed as a wrong against them—although Arch absurdly implies as much. (*See* Kramarsky Aff. Ex. C ¶ 163 (Arch "required" to pay litigation costs "[b]y reason of Hartford's commencement of this litigation")).

cause of action can be sustained only if the third-party plaintiff and the third-party defendant have breached a duty to plaintiff and also if some duty to indemnify exists between them").

Indeed, the payments of which Arch complains simply are not embraced by the law of indemnification. Whereas "[c]ommon-law indemnification . . . permits one held vicariously liable who has been compelled to pay for the wrong of another to shift the entire burden of the loss to the actual wrongdoer", Arch seeks reimbursement for payments it was not "compelled" to make at all—let alone compelled to make due to another's wrongdoing. *See The Mountbatten Surety Co. v. Oriska Ins. Co.*, 2008 N.Y. Slip. Op. 32627(U), at *6, 2008 WL 4461447 (Sup. Ct. N.Y. Co. Sept. 30, 2008) (Lowe, J.). Arch independently committed itself to make payments in order to induce the Individual Defendants to move to Arch. Arch cannot recover from Plaintiffs for a contractual provision with parties other than Plaintiffs—a contractual provision, moreover, in furtherance of its scheme to steal Plaintiff's business (*see, e.g., Texaco, Inc. v. A. A. Gold, Inc.*, 78 Misc. 2d 1050, 1054, 357 N.Y.S.2d 951, 956 (Sup. Ct. Kings Co. 1974) ("It is not [the court's] function to guarantee every businessman's success in his enterprise, or to protect him from entering into improvident or ill-advised contracts, or to relieve him from contracts freely negotiated, that prove to be onerous."))—and certainly not under a theory of indemnification. *See Board of Educ. v. Sargent, Webster, Crenshaw & Folley*, 71 N.Y.2d 21, 29, 523 N.Y.S.2d 475, 479 (1987) (dismissing indemnification claim where, "[a]s originally pleaded, the third-party complaint does not allege facts showing that [claimant] was unfairly required to discharge a duty that should have been discharged by another, such that a contract to indemnify should be implied by law"); *Saraco Glass Corp. v. Yeled V'Yalda Early Childhood Ctr., Inc.*, 11 Misc. 3d 1071(A), 816 N.Y.S.2d 700, 2006 WL 782430, at *5 (Sup. Ct. Kings Co. Mar. 28, 2006) (holding that

parties "are *per-se* not entitled to any indemnification" where their liability arose from their own acts) (citations omitted)). Arch's first and second counterclaims must therefore be dismissed.

Finally, Arch's claim for indemnification of payments under the Plans must fail because Arch has made no such payments. *See, e.g., Travelers Indem. Co. v. LLJV Dev. Corp.*, 227 A.D.2d 151, 154, 643 N.Y.S.2d 520, 523 (1st Dep't 1996) ("it is well settled that a cause of action based upon a contract of indemnification does not arise until liability is incurred by way of actual payment"); *Aldrich v. Marsh & McLennan Co.*, 25 Misc. 3d 1207(A), 901 N.Y.S.2d 897, 2009 WL 3152794, at *8 (Sup. Ct. N.Y. Co. Sept. 29, 2009) ("Payment is an element of the claim."). Arch's first counterclaim makes it clear that the company has not yet made any payments to the Individual Defendants under the Plans. (Kramarsky Aff. Ex. C Counterclaims ¶ 144 (Arch "will be required" to make payments to the Individual Defendants under the Plans)). The failure to allege payment is thus an independent ground for dismissal of Arch's first counterclaim.

**B. Arch's Unjust Enrichment Claim Also Fails**

Arch also asserts an indemnification claim to recover any payments to the Individual Defendants and Kelly—either to replace discretionary bonus compensation under the HFP Plans or to provide for the Individual Defendants' litigation costs—under a theory of unjust enrichment. This claim is incredible for the same reason that Arch's indemnification claims are incredible, and it fails for the same reason: namely, there is no basis to hold Plaintiffs liable for Arch's independent decision to provide bonus compensation and legal fees to the Individual Defendants (and Kelly) under their employment agreements as an inducement to Plaintiffs' then employees to harm The Hartford.

"It is well settled that '[t]he essential inquiry in any action for unjust enrichment or restitution is whether it is against equity and good conscience to permit the defendant to retain what is sought to be recovered.'" *Sperry v. Crompton Corp.*, 8 N.Y.3d 204, 215, 831 N.Y.S.2d 760, 766 (2007). In making that determination, courts look to the thing that is to be recovered: the benefit conferred upon the party allegedly unjustly enriched. *See Paramount Film Distrib. Corp. v. State*, 30 N.Y.2d 415, 421, 334 N.Y.S.2d 388, 393 (1972) ("Generally, courts will look to see if a benefit has been conferred on the defendant under mistake of fact or law, if the benefit still remains with the defendant, if there has been otherwise a change of position by the defendant").

*First*, the argument can hardly be made that Plaintiffs have received a benefit. Rather, Plaintiffs determined not to reward disloyal former employees with entirely discretionary bonus compensation payments after those employees joined with a competitor to raid a highly profitable business unit and steal clients worth millions of dollars in premiums. *Compare id.* at 422, 334 N.Y.S.2d at 393 (finding it "difficult to say that the State has received any benefit, let alone unjust enrichment" from the collection of fees that "defrayed the cost of the licensing program"). *Second*, even assuming arguendo that Plaintiffs have been enriched—which they have not—they certainly have not been enriched unjustly. *See Dobroshi v. Bank of Am., N.A.*, 65 A.D.3d 882, 885, 886 N.Y.S.2d 106, 109 (1st Dep't 2009) ("It is not sufficient that a defendant is enriched; rather, the enrichment must be unjust.") (*citing McGrath v. Hilding*, 41 N.Y.2d 625, 629, 394 N.Y.S.2d 603, 606 (1977)).

*Third*, Arch can allege no basis to hold Plaintiffs liable for payments that Arch freely committed to make. *Compare Sperry*, 8 N.Y.3d at 215-16, 831 N.Y.S.2d at 766 (claim for unjust enrichment did not lie between purchaser of faulty tires and producer of chemicals used in the

rubber-making process because connection between the two "is simply too attenuated to support such a claim"). Arch's claim for unjust enrichment must therefore be dismissed.

## Conclusion

For all of the foregoing reasons, the first, second and fourth counterclaims of the Individual Defendants and the entirety of Arch's counterclaims should be dismissed with prejudice.

Dated: New York, New York
September 3, 2010

DEWEY PEGNO & KRAMARSKY LLP

By: _____

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SUPREME COURT OF THE STATE OF NEW YORK
COUNTY OF NEW YORK

TWIN CITY FIRE INSURANCE COMPANY, HARTFORD INSURANCE COMPANY OF ILLINOIS, HARTFORD INSURANCE COMPANY OF THE MIDWEST, TRUMBULL INSURANCE COMPANY, HARTFORD INSURANCE COMPANY OF THE SOUTHEAST, NUTMEG INSURANCE COMPANY, PROPERTY AND CASUALTY INSURANCE COMPANY OF HARTFORD, HARTFORD FIRE INSURANCE COMPANY, HARTFORD CASUALTY INSURANCE COMPANY, HARTFORD ACCIDENT AND INDEMNITY INSURANCE COMPANY, HARTFORD UNDERWRITERS INSURANCE COMPANY, PACIFIC INSURANCE COMPANY, LIMITED, and THE HARTFORD FINANCIAL SERVICES GROUP, INC.

Plaintiffs,

-against-

ARCH INSURANCE GROUP, INC., ARCH CAPITAL GROUP LTD., DAVID McELROY, JOHN RAFFERTY and MICHAEL PRICE,

Defendants.

Index No. 602062/09

**PLAINTIFFS' ANSWER TO THE COUNTERCLAIMS OF DAVID MCELROY, JOHN RAFFERTY, AND MICHAEL PRICE**

Plaintiffs Hartford Insurance Company of Illinois, Hartford Insurance Company of the Midwest, Trumbull Insurance Company, Hartford Insurance Company of the Southeast, Nutmeg Insurance Company, Property and Casualty Insurance Company of Hartford, Hartford Fire Insurance Company, Hartford Casualty Insurance Company, Hartford Accident and Indemnity Company, Hartford Underwriters Insurance Company, Twin City Fire Insurance Company, and Pacific Insurance Company, Limited, and The Hartford Financial Services Group, Inc. (collectively "The Hartford" or "Plaintiffs"), by their undersigned attorneys, as and for their

Answer to the Counterclaims asserted by Defendants David McElroy, John Rafferty, and Michael Price (collectively "Individual Defendants"), allege as follows, with knowledge as to their own actions, and otherwise on information and belief:

## ANSWER TO COUNTERCLAIMS

1. Plaintiffs state that the allegations in paragraph 1 are legal conclusions as to which no response is required.

2. Plaintiffs deny in part the allegations in paragraph 2 but admit that David McElroy was an officer for the following entities: (i) Hartford Insurance Company of the Southeast, (ii) Nutmeg Insurance Company, (iii) Hartford Fire Insurance Company, (iv) Hartford Casualty Insurance Company, (v) Hartford Accident and Indemnity Company, (vi) Hartford Underwriters Insurance Company, and (vii) Twin City Fire Insurance Company; John Rafferty was an officer of Nutmeg Insurance Company and Twin City Fire Insurance Company; David McElroy held the title of Senior Vice President of HFP and used and was authorized to use the title President of HFP; John Rafferty held the title of Vice President of HFP; Michael Price held the title of Vice President of HFP.

3. Plaintiffs deny the allegations in paragraph 3.

4. Plaintiffs deny the allegations in paragraph 4 but admit that there existed a 2000 HFP Annual Cash Incentive & Profit Contribution Plan ("Old Plan"), a 2007 HFP Annual Cash Incentive & Profit Contribution Plan ("New Plan"), The Hartford Incentive Stock Plan in 2005, and The Hartford Performance Unit Plan.

5. Plaintiffs deny the allegations in paragraph 5.

6. Plaintiffs deny the allegations in paragraph 6.

7. Plaintiffs deny the allegations in paragraph 7.

8. Plaintiffs state that the allegations in paragraph 8 are legal conclusions as to which no response is required, but to the extent a response is required Plaintiffs deny the allegations in paragraph 8.

9. Plaintiffs deny the allegations in paragraph 9.

10. Plaintiffs deny the allegations in paragraph 10.

11. Plaintiffs state that the allegations in paragraph 11 are legal conclusions as to which no response is required, but to the extent a response is required Plaintiffs deny the allegations in paragraph 11.

**First Cause of Action**
**Breach of Contract (On Behalf of David McElroy)**

12. Plaintiffs' responses to paragraphs 1 through 11 of the Counterclaims are incorporated herein by reference as though set forth in full.

13. Plaintiffs admit that McElroy sent written notice to Juan Andrade on May 21, 2009 announcing that he was retiring and that his last day at The Hartford was June 5, 2009.

14. Plaintiffs state that the allegations in paragraph 14 are legal conclusions as to which no response is required, but to the extent a response is required Plaintiffs deny the allegations in paragraph 14.

15. Plaintiffs state that the allegations in paragraph 15 are legal conclusions as to which no response is required, but to the extent a response is required Plaintiffs deny the allegations in paragraph 15.

16. Plaintiffs state that the allegations in paragraph 16 are legal conclusions as to which no response is required, but to the extent a response is required Plaintiffs deny the allegations in paragraph 16.

17. Plaintiffs state that the allegations in paragraph 17 are legal conclusions as to which no response is required, but to the extent a response is required Plaintiffs deny the allegations in paragraph 17.

18. Plaintiffs state that the allegations in paragraph 18 are legal conclusions as to which no response is required, but to the extent a response is required Plaintiffs deny the allegations in paragraph 18.

19. Plaintiffs state that the allegations in paragraph 19 are legal conclusions as to which no response is required, but to the extent a response is required Plaintiffs deny the allegations in paragraph 19.

20. Plaintiffs state that the allegations in paragraph 20 are legal conclusions as to which no response is required, but to the extent a response is required Plaintiffs deny the allegations in paragraph 20.

**Second Cause of Action**

Plaintiffs need not respond to the Second Cause of Action as it has been dismissed.

**Third Cause of Action**
**Breach of Contract (On Behalf of David McElroy, John Rafferty, and Michael Price)**

33. Plaintiffs' responses to paragraphs 1 through 20 of the Counterclaims are incorporated herein by reference as though set forth in full.

34. Plaintiffs state that the allegations in paragraph 34 are legal conclusions as to which no response is required, but to the extent a response is required Plaintiffs deny the allegations in paragraph 34.

35. Plaintiffs state that the allegations in paragraph 35 are legal conclusions as to which no response is required, but to the extent a response is required Plaintiffs deny the allegations in paragraph 35.

36. Plaintiffs state that the allegations in paragraph 36 are legal conclusions as to which no response is required, but to the extent a response is required Plaintiffs deny the allegations in paragraph 36.

37. Plaintiffs state that the allegations in paragraph 37 are legal conclusions as to which no response is required, but to the extent a response is required Plaintiffs deny the allegations in paragraph 37.

38. Plaintiffs state that the allegations in paragraph 38 are legal conclusions as to which no response is required, but to the extent a response is required Plaintiffs deny the allegations in paragraph 38.

39. Plaintiffs state that the allegations in paragraph 39 are legal conclusions as to which no response is required, but to the extent a response is required Plaintiffs deny the allegations in paragraph 39 and refer to the response to paragraph 2.

40. Plaintiffs state that the allegations in paragraph 40 are legal conclusions as to which no response is required, but to the extent a response is required Plaintiffs deny the allegations in paragraph 40.

41. Plaintiffs state that the allegations in paragraph 41 are legal conclusions as to which no response is required, but to the extent a response is required Plaintiffs deny the allegations in paragraph 41.

42. Plaintiffs state that McElroy, Rafferty, and Price have requested indemnification and have signed an undertaking.

43. Plaintiffs state that the allegations in paragraph 43 are legal conclusions as to which no response is required, but to the extent a response is required Plaintiffs deny the allegations in paragraph 43.

44. Plaintiffs state that the allegations in paragraph 44 are legal conclusions as to which no response is required, but to the extent a response is required Plaintiffs deny the allegations in paragraph 44.

45. Plaintiffs state that the allegations in paragraph 45 are legal conclusions as to which no response is required, but to the extent a response is required Plaintiffs deny the allegations in paragraph 45.

**Fourth Cause of Action**

Plaintiffs need not respond to the Fourth Cause of Action as it has been dismissed.

Plaintiffs deny any and all allegations not specifically admitted herein.

**FIRST AFFIRMATIVE DEFENSE**

The Individual Defendants' counterclaims fail, either in whole or in part, to state a claim upon which relief may be granted.

**SECOND AFFIRMATIVE DEFENSE**

The Individual Defendants' counterclaims are barred in whole or in part by the doctrine of unclean hands, waiver, and/or estoppel.

**THIRD AFFIRMATIVE DEFENSE**

The Individual Defendants' counterclaims are barred by the doctrine of laches.

**FOURTH AFFIRMATIVE DEFENSE**

The Individual Defendants have suffered no damages, and thus are not entitled to recovery.

**FIFTH AFFIRMATIVE DEFENSE**

Plaintiffs were not the proximate cause of any potential injury to the Individual Defendants.

**SIXTH AFFIRMATIVE DEFENSE**

The Individual Defendants' counterclaims are barred in whole or in part by the doctrines precluding double recovery or windfall.

**SEVENTH AFFIRMATIVE DEFENSE**

To the extent that the Individual Defendants prevail on and are awarded damages for any of their claims, their recovery should be offset by the damages to which Plaintiffs are entitled.

**EIGHTH AFFIRMATIVE DEFENSE**

The Individual Defendants' counterclaims are barred in whole or in part due to their bad acts or wrongdoing in general and as employees of Plaintiffs.

Dated: New York, New York
August 2, 2011

DEWEY PEGNO & KRAMARSKY LLP

By:_____

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*Attorneys for Plaintiffs*

SUPREME COURT OF THE STATE OF NEW YORK
COUNTY OF NEW YORK

TWIN CITY FIRE INSURANCE COMPANY, et al.

Plaintiffs,

-against-

ARCH INSURANCE GROUP, INC., et al.

Defendants.

Index No. 602062/09

Motion Seq. Nos. 003 and 004

**NOTICE OF ENTRY**

PLEASE TAKE NOTICE that the within are 1) a true and correct copy of an Order entered in the Office of the Clerk of the Supreme Court, New York County, on July 13, 2011 and 2) a true and correct copy of an Order entered into the Office of the Clerk of Supreme Court, New York County, on September 13, 2011, correcting scrivener's error in the July 13, 2011 Order.

Dated: September 27, 2011
New York, New York

DEWEY PEGNO & KRAMARSKY LLP

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*David McElroy, John Rafferty and*
*Michael Price*

## AFFIDAVIT OF SERVICE

KAMANI SINGH affirms under penalty of perjury that:

1. I am over the age of eighteen years, not a party to this action, and an employee of the firm of Dewey Pegno & Kramarsky LLP, attorneys for Plaintiffs in this matter.

2. On the 27th day of September 2011, I caused a copy of the foregoing: **Notice of Entry** to be served on:

**BY U.S. MAIL**

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Dated: New York, New York
September 27, 2011

Kamani Singh

Sworn to before me this
27th day of September, 2011

Notary Public

ANN MARIE CORRADINI
Notary Public - State of New York
NO. 01CO6139166
Qualified in Queens County
My Commission Expires 10.3.2014

FILED: NEW YORK COUNTY CLERK 09/13/2011 INDEX NO. 602062/2009
NYSCEF DOC. NO. 63 RECEIVED NYSCEF: 09/13/2011

# SUPREME COURT OF THE STATE OF NEW YORK
# NEW YORK COUNTY

PRESENT: JUSTICE SHIRLEY WERNER KORNREICH PART 54
*Justice*

Index Number : 602062/2009
TWIN CITY FIRE INSURANCE
vs.
ARCH INSURANCE GROUP
SEQUENCE NUMBER : 004
OTHER RELIEFS

INDEX NO. _____
MOTION DATE 08/24/11
MOTION SEQ. NO. _____

The following papers, numbered 1 to _____, were read on this motion to/~~for~~ correct scrivener's errors

Notice of Motion/Order to Show Cause — Affidavits — Exhibits _____ | No(s). 58-62

Answering Affidavits — Exhibits _____ | No(s). _____

Replying Affidavits _____ | No(s). _____

Upon the foregoing papers, it is ordered that this motion is

**MOTION IS DECIDED IN ACCORDANCE WITH ACCOMPANYING MEMORANDUM DECISION AND ORDER.**

MOTION/CASE IS RESPECTFULLY REFERRED TO JUSTICE FOR THE FOLLOWING REASON(S):

Dated: 9/9/11

JUSTICE SHIRLEY WERNER KORNREICH, J.S.C.

1. CHECK ONE: ..... ☐ CASE DISPOSED ☒ NON-FINAL DISPOSITION
2. CHECK AS APPROPRIATE: .....MOTION IS: ☒ GRANTED ☐ DENIED ☐ GRANTED IN PART ☐ OTHER
3. CHECK IF APPROPRIATE: ..... ☐ SETTLE ORDER ☐ SUBMIT ORDER
☐ DO NOT POST ☐ FIDUCIARY APPOINTMENT ☐ REFERENCE

SUPREME COURT OF THE STATE OF NEW YOR
COUNTY OF NEW YORK: IAS PART 54

----------x

TWIN CITY FIRE INSURANCE COMPANY, HARTFORD INSURANCE COMPANY OF ILLINOIS, HARTFORD INSURANCE COMPANY OF THE MIDWEST, TRUMBULL INSURANCE COMPANY, HARTFORD INSURANCE COMPANY OF THE SOUTHEAST, NUTMEG INSURANCE COMPANY, PROPERTY AND CASUALTY INSURANCE COMPANY OF HARTFORD, HARTFORD FIRE INSURANCE COMPANY, HARTFORD CASUALTY INSURANCE COMPANY, HARTFORD ACCIDENT AND INDEMNITY INSURANCE COMPANY, HARTFORD UNDERWRITERS INSURANCE COMPANY, PACIFIC INSURANCE COMPANY, LIMITED, and THE HARTFORD FINANCIAL SERVICES GROUP, INC.,

Plaintiffs,

-against-

ARCH INSURANCE GROUP, INC., ARCH CAPITAL GROUP LTD., DAVID McELROY, JOHN RAFFERTY and MICHAEL PRICE,

Defendants.

----------x

Index No.: 602062/09

**DECISION & ORDER**

HON. SHIRLEY WERNER KORNREICH, J.:

Plaintiffs move for an order correcting two scrivener's errors in this court's decision and order dated July 12, 2011. Defendants do not oppose plaintiffs' proposed amendments. The court has examined the proposed corrections and finds them to be appropriate. Accordingly, it is hereby

ORDERED that this Court's Decision and Order dated July 12, 2011 is modified and amended as follows, and in all other respects remains in full force and effect: (1) the second decretal paragraph is deleted in its entirety and replaced with the following: "ORDERED that

plaintiffs' motion to dismiss the first counterclaim of defendant David McElroy for breach of contract is denied; and it is further"; and (2) the third decretal paragraph is deleted in its entirety and replaced with the following: "ORDERED that plaintiffs' motion to dismiss the second counterclaim for breach of the covenant of good faith and fair dealing of defendants John Rafferty and Michael Price is granted; and it is further".

Dated: 9/9/11

Enter:

J.S.C.

FILED: NEW YORK COUNTY CLERK 07/13/2011 INDEX NO. 602062/2009
NYSCEF DOC. NO. 56 RECEIVED NYSCEF: 07/13/2011

SUPREME COURT OF THE STATE OF NEW YORK — NEW YORK COUNTY

PRESENT: KORNREICH PART 54

JUSTICE SHIRLEY WERNER KORNREICH Justice

TWIN CITY et al

- v -

Rock Drum et al

INDEX NO. 602062/09

MOTION DATE

MOTION SEQ. NO. 003

MOTION CAL. NO.

The following papers, numbered 1 to _____ were read on this motion to/for _____

| | PAPERS NUMBERED |
|---|---|
| Notice of Motion/ Order to Show Cause — Affidavits — Exhibits ... | 36, 37, 38, 39 |
| Answering Affidavits — Exhibits | 43, 44, 45 |
| Replying Affidavits | 46, 47 |

Cross-Motion: ☐ Yes ☒ No

Upon the foregoing papers, it is ordered that this motion is decided in accordance with the annexed opinion.

MOTION/CASE IS RESPECTFULLY REFERRED TO JUSTICE FOR THE FOLLOWING REASON(S):

Dated: 7/12/11

JUSTICE SHIRLEY WERNER KORNREICH J.S.C.

Check one: ☐ FINAL DISPOSITION ☒ NON-FINAL DISPOSITION

Check if appropriate: ☐ DO NOT POST ☐ REFERENCE

☐ SUBMIT ORDER/ JUDG. ☐ SETTLE ORDER/ JUDG.

SUPREME COURT OF THE STATE OF NEW YOR
COUNTY OF NEW YORK: IAS PART 54

----------x

TWIN CITY FIRE INSURANCE COMPANY, HARTFORD INSURANCE COMPANY OF ILLINOIS, HARTFORD INSURANCE COMPANY OF THE MIDWEST, TRUMBULL INSURANCE COMPANY, HARTFORD INSURANCE COMPANY OF THE SOUTHEAST, NUTMEG INSURANCE COMPANY, PROPERTY AND CASUALTY INSURANCE COMPANY OF HARTFORD, HARTFORD FIRE INSURANCE COMPANY, HARTFORD CASUALTY INSURANCE COMPANY, HARTFORD ACCIDENT AND INDEMNITY INSURANCE COMPANY, HARTFORD UNDERWRITERS INSURANCE COMPANY, PACIFIC INSURANCE COMPANY, LIMITED, and THE HARTFORD FINANCIAL SERVICES GROUP, INC.,

Plaintiffs,

-against-

ARCH INSURANCE GROUP, INC., ARCH CAPITAL GROUP LTD., DAVID McELROY, JOHN RAFFERTY and MICHAEL PRICE,

Defendants.

----------x

Index No.: 602062/09
DECISION & ORDER

KORNREICH, J.:

Plaintiffs (collectively, Hartford) bring this action against defendants Arch Insurance Group., Inc. and Arch Capital Group Ltd. (collectively, Arch), a competitor, and defendants David McElroy, John Rafferty and Michael Price, former senior executives of Hartford's Financial Products division (HFP) and present employees of Arch. Plaintiffs, now, move, pursuant to CPLR 3211(a) (1) and (7), for an order dismissing, in part, the counterclaims of defendants McElroy, Rafferty and Price (collectively, the Individual Defendants), and dismissing, in their entirety, the counterclaims of defendants Arch.

*I. Facts:*

*A. Complaint*

The following facts are taken from the complaint, unless otherwise stated.

McElroy retired, effective June 5, 2009, from his position as a senior vice president of Hartford and president of HFP. On June 8, 2009, Arch announced that McElroy would head its newly-formed Financial and Professional Liability Group. Hartford contends that a large corporate raid on and disparagement of Hartford ensued, resulting in HFP's loss of 60 employees comprising more than 25% of HFP's workforce and virtually all of its senior management. Additionally, it asserts that Rafferty and Price, then vice presidents of HFP, resigned from HFP within days of McElroy's retirement and followed him to Arch. Hartford alleges that, subsequently, HFP employees were directly solicited by Arch, HFP clients and prospects were misappropriated, and a significant amount of HFP's intellectual capital was transferred, for no consideration, to Arch. Hartford seeks to enjoin Arch's alleged improper conduct and recover damages caused thereby.

*B. Counterclaims*

In their four counterclaims, the Individual Defendants "seek relief for Hartford's improper (a) failure and refusal to pay to [them] compensation that they have earned and to which they are entitled, as well as (b) failure and refusal to indemnify, and repudiation of its obligation to indemnify, [them] for expenses, including attorneys' fees, incurred in connection with this litigation." Individual Defendants' Counterclaims, ¶1. The following facts are taken from the Individual Defendants' counterclaims, unless otherwise stated, and presumed true for the purposes of this motion.

The Individual Defendants admit they are former officers of HFP and that McElroy also served as an officer of other Hartford subsidiaries. They claim that when they, former employees of Reliance Insurance, commenced employment at Hartford in 2000, they accepted below-market salaries in consideration for Hartford's agreement to pay additional salary in the form of deferred compensation. The Individual Defendants describe these deferred plans as including the Hartford Financial Products Annual Cash Incentive & Profit Contribution Plan (the Old Plan), the 2007 Hartford Performance Annual Cash Incentive & Profit Contribution Plan (the New Plan), The Hartford Performance Unit Plan ( the PU Plan) and The Hartford 2005 Incentive Stock Plan (the 2005 Stock Plan) (collectively, the Deferred Compensation Plans). According to the Individual Defendants, they received compensation under the Plans from 2000 to 2009.

McElroy gave notice of his retirement on May 1, 2009 and retired on June 5, 2009. He contends he has not received any deferred compensation since.

The Individual Defendants further contend that Hartford applied to the federal government's Troubled Assets Relief Program (TARP) and received preliminary approval on or about May 14, 2009. As a result, on June 2 or 3, Hartford told Rafferty and Price that they were required "to sign a waiver and release of all rights and claims [they] had against Hartford with respect to any prospective changes to [their] compensation or benefits that might result from Hartford's receipt of TARP monies – which changes might include prohibitions and/or further deferrals of their entitlements under the Deferred Compensation Plans." Ans., para. 23. They were given until June 10, 2009 to sign the waivers. Rafferty resigned on June 9, and Price resigned on June 10. They contend that they have received no deferred compensation since.

The counterclaims describe the Plans:

5. Pursuant to the Old Plan and the New Plan, a certain percentage of the profits from business written at HFP during any given year was to be set aside and placed in an annual profit pool. A portion of this annual profit pool was to be used to fund deferred compensation awards to certain employees, including the Individuals, through the issuance of "profit contribution units." Participants were to receive cash payouts in regular installments based on the number of profit contribution units they had earned.

6. Pursuant to The Hartford Performance Unit Plan, certain Hartford employees, including the Individuals, were to receive "Performance Units." After a vesting period, performance units were to result in cash payments based on a per unit monetary valuation.

7. Pursuant to The Hartford 2005 Incentive Stock Plan, certain Hartford employees, including the Individuals, were to receive "restricted stock" of Hartford Financial, which could be exchanged for common stock of Hartford Financial after a designated period, as well as "restricted stock units," each of which constituted the contractual rights to receive common stock of Hartford Financial after a designated period.

The Individual Defendants also claim that Sections 4.1(a) and 4.6 of Hartford Financial's Amended and Restated By-Laws obligate it to indemnify its former officers and employees for litigation "by reason of the fact that he or she was an officer, employee or agent of Hartford Financial." Ans., para. 34. Moreover, they claim that the By-Laws entitle former officers and employees to be indemnified for all lawyer and litigation expenses and entitle them to advance payments as the litigation proceeds.

The Individual Defendants allege causes of action for breach of contract under the Deferred Compensation Plan on behalf of McElroy (First Cause of Action), breach of duty of good faith and fair dealing on behalf of Rafferty and Price in regard to the Compensation Plans (Second Cause of Action), breach of contract under the By-Laws on behalf of the Individual Defendants (Third Cause of Action) and unjust enrichment on behalf of the Individual Defendants as to the monies not paid them pursuant to the Deferred Compensation and as to indemnification for the litigation fees (Fourth Cause of Action).

Arch's three counterclaims sound in: (1) indemnification for Hartford's refusal to pay and Arch's payment of the Individual Defendants' and Catherine Kelly's (another former HFP and current Arch employee) compensation allegedly owed to them under the Old Plan and the New Plan; (2) indemnification for Hartford's refusal to pay and Arch's payment of the Individual Defendants' costs and expenses, including attorneys' fees, incurred in connection with the instant action; and (3) indemnification for Hartford's unjust enrichment. Arch's claims are based on certain terms of its employment agreements with the Individual Defendants and Kelly, in which Arch agreed (a) to pay the Individual Defendants and Kelly the amounts, if any, they would have received from Hartford under the Old and New Plans, to the extent that Hartford does not make such payments; and (b) to indemnify the Individual Defendants and hold them harmless against any liability, including reasonable attorneys' fees, incurred by them as a result of a claim by Hartford arising out of their commencement of employment with Arch.

C. *Documentary Evidence Submitted by Plaintiff*

*July 2003 (Old Plan)*

The parties stated at oral argument that no formal document existed outlining the Old Plan. Rather, a powerpoint presentation and informal letters describing the plan were submitted by plaintiffs.

*Powerpoint*

Plaintiffs submit a July 2003 Powerpoint entitled "Hartford Financial Products Bonus Program" (Powerpoint). The Powerpoint describes the program as providing "Individual bonus awards" based "on your manager's assessment of your performance" ( Powerpoint, p. 2), which would reflect "individual performance and contribution to HFP's profit results." *Id.* at 3, 17. It warns that some employees will "receive zero awards" and that the award would reflect results

achieved by the employee, the difficulty and the employees contribution to HFP. *Id.* at 4. Moreover, the Powerpoint states that the bonuses in each pool of insurance would be calculated over seven years to reflect the results of the insurance pools, with different percentages of the pool paid out each year. *Id.* at 6-16.

The Powerpoint explains that payments are made on an annual basis, usually by March 31 of the following year, and describes those eligible as employees having "satisfactory performance." *Id.* at 18. Also,

> "[i]ndividuals transferred to HFP will be eligible for a full payment under the HFP pool calculation. Those individuals hired during the first quarter are eligible for full payment; those hired during 2nd quarter are eligible for pro-rata payment; and those hired after October 1 (4th quarter) are not eligible. Active employees must have worked a continuous six months to be eligible for payment. Individuals on leave at time of payment will be eligible to receive payment upon return to work. Individuals who resign during the year are ineligible for payments; those who resign after December 31 (during the first quarter of the following year) are eligible for payments. Individuals who terminate due to job elimination or retirement (after July 1) *may* be eligible for a prorated payment. [emphasis added]

*Id.* Again, the Powerpoint emphasizes that "no one is entitled to any payment," that Hartford Management retains full control over decisions regarding payment and eligibility of "this bonus program," and that Hartford could change the program at any time. *Id.*

*McElroy Letters*

Plaintiffs submit two 2007, two 2008 and three 2009 letters written by plaintiff McElroy to defendant Price, defendant Rafferty and a Bryan Berkman, describing the Old and New Plans. In his February 16, 2009 letter to Bryan Berkman describing the Old and New Plans, McElroy wrote:

> ...you must remain an active employee of HFP and/or The Hartford organization at large at the time of actual payment to receive any awards. Please understand any provision of the *Old Plan and New Plan* or your eligibility for an award does not constitute a guarantee of employment in any fashion or for any fixed period

of time, nor does it modify the at-will status of any employee. In the event of a dispute regarding the rationale, calculation and/or payment of any amounts under the *Old Plan or New Plan.* The Hartford retains full control over decisions regarding the interpretation of the formulae, eligibility, payments and administration related to participation. Furthermore, no one is contractually entitled to any payment and The Hartford reserves the right to amend or terminate the *Old Plan or New Plan* at any time. Once again, thank you for your contribution to the success of HFP and for allowing me this opportunity to provide you an update to your *Old Plan and New Plan* award picture.

McElroy wrote three letters to Rafferty, describing the Old and New Plans, in 2007, 2008 and 2009. In a May 24, 2007 letter, he explained that the Old Plan had been replaced with the New Plan in 2007. He wrote:

> ...This New Plan will provide all regular, active HFP employees the opportunity to earn an annual incentive award (first payable in March 2008), and for qualifying HFP employees, profit contribution units (first awarded in March 2008 with first potential payable in March 2010). New Plan information is available under separate cover.
> In addition to any New Plan awards you may earn, the sunset of the Old Plan leaves you eligible for trailing awards based upon your contributions to the establishment, success and profitability of HFP from its formation through 2006 performance year. Please understand that due to plan design the longer-term nature of ultimate profitability calculations, the remaining, unpaid award pool from the Old Plan is not fully quantifiable at this time....
> * * * *
> ...You must remain an active employee of HFP and/or The Hartford organization at large at the time of actual payment to receive any award(s). Please understand any provision of the sunset of the Old Plan or the entitlement to an award does not constitute a guarantee or contract of employment in any fashion or for any fixed period of time, nor does it modify the at-will status of any employee. In the event of a dispute regarding the rationale, calculation and/or payment of any amounts under the Old Plan, The Hartford retains full control over decisions regarding the interpretation of the formulae, eligibility, payments and administration related to participation. Furthermore, no one is contractually entitled to any payment and The Hartford reserves the right to amend or terminate the Old Plan at any time. Thank you for your contributions to the success of HFP to date and for allowing me the opportunity to provide some clarity to your Old Plan incentive award picture.

In the 2008 and 2009 letters to Rafferty, McElroy repeats the paragraph beginning with "Please," in which he admonishes that entitlement to an award is not a guarantee of employment

and that payment calculations under the Old Plan are at Hartford's discretion and could be terminated. The last paragraph describing the Old Plan as an "incentive plan" is also repeated. The same three letters were sent by McElroy to Price.

*2007 Powerpoint*

This Powerpoint has a page marked "Disclaimer," in which it states that the "incentive plans" are discretionary and for eligible HFP employees. *Id.* at 2. The Powerpoint asserts that "[n]othing in the incentive plans described herein constitute a guarantee of employment for any specific duration or period of time," that employment is terminable at will and that the "plans may be modified or cancelled at anytime without prior notice." *Id.* The Powerpoint states that awards depend on business results, individual performance, eligibility and the success of Hartford. *Id.* at 3. Reviewing the key components of the "2007 HFP Incentive Plan," the Powerpoint first addresses "Annual Incentives." *Id.* at 4. It enumerates those: actual awards are determined by individual accomplishments annually and HFP's annual performance; payouts during the first quarter following the performance year; and eligibility. *Id.* Referring to the "Multi-year Profit Contribution" Plan, it states that this plan "[p]rovides opportunity for select HFP employees to receive units in an annual profit pool tied to the long-term development of the book business." *Id*

Addressing the Annual Incentive plan, the Powerpoint explains that awards are discretionary and contingent on satisfactory performance. *Id.* at 8. As to eligibility, a table is provided which, *inter alia*, states that an individual who voluntarily resigns before the payout date is not eligible but that one who retires is eligible "prorated based on number of months eligible." *Id.*

In regard to the "Multi-Year Profit Contribution Plan" (New Plan), the Powerpoint specifies the "[a]nnual issuance of 'units' based on individual contributions and subsequent payout of units over time [which] establishes visible value – encouraging retention of critical talent." *Id.* at 10. Eligible participants are defined as "[a]ll regular, active employees" in specific tiers, and the units received depend on "acceptable or better performance." *Id.* at 11. Receipt of units are contingent upon receiving an award from the HFP annual plan and are at management's discretion. *Id.* at 15. " Payments...are considered to be a long-term deferred award and thereby do not count toward earnings under the company's Retirement Plan(s) or the 401(k) savings & Investment Plan." *Id.* Those who voluntarily terminate their employment "forfeit all units and future interest in the annual profit pool." *Id.* Involuntary termination retains eligibility for 12 months, and retirees vest. *Id.* The 2007 Powerpoint addresses the transition from the Old Plan to the New Plan, setting forth what would be paid through 2011 under the Old Plan. *Id.* at 17.

*New Plan*

*2007 Writing*

A 2007 writing setting forth the plan, is submitted. It reflects what was presented in the 2007 Powerpoint. It explicitly states that the plan "is intended to engage participants to actively drive growth and retention of profitable business, while fostering the retention of key employees..." 2007 Written Plan, p. 1; *see id.* also at 1 ("intended to reward participants for the successful stewardship of the business, support retention of key employees..."), 7 ("to encourage employee retention"). It repeatedly notes that awards are at managements' discretion (*id.* at 1, 3, 5, 6), refers to the awards as incentive payments (*id.* at 1, 2, 3, 5, 6, 9), and provides for discretionary revision or termination of the award. *Id.* at 3, 5, 9. The Plan provides that if an

employee is terminated for cause or resigns, "all units and future interest in the annual pool(s) will be forfeited." *Id.* at 8. "If the termination of employment is due to retirement ..., the participant ... shall fully and immediately vest at the next immediate scheduled payment date based on the calculated unit value of the pool at that time." *Id.* at 8. The table provided in the written plan describes a retiree as "[e]ligible" and his award as "[p]rorated based on number of months eligible." *Id.* at 4.

*January 2009 Restatement of New Plan*

The 2009 Restatement of the New Plan is similar to the power point and 2007 writing. The Plan is described as comprised of two components – (1) an annual cash incentive; and (2) the profit contribution which "may provide additional future compensation to certain eligible roles" based on business during the calendar year. 2009 Restatement, p. 1. Payments are to be made over a five year period following the year the insurance was written (*id.* at 6) and awards are not earned at the time distributed but distributed from an annual profit pool with 50% paid out following the third year, 75% following the fourth year, and 100% following the fifth year. *Id.* at 7. Again, the description states that those who voluntarily resign are not eligible for the yearly distribution and retirees are eligible for a "[p]ro-rated" amount. *Id.* at 8.

*Stock Plan*

Two documents are submitted regarding the Stock Plan. The purpose of the plan is described as motivating and rewarding key employees at the discretion of the Committee. A key employee is defined in the documents as an Eligible Employee, including an officer, whose responsibilities and decisions directly affect the performance of the Company. Section 6(f) of the documents provides:

If a Key Employee terminates service ...during a Performance Period or any

applicable Restriction Period...(iii)solely in the case of a Key Employee with an original hire date before January 1, 2002, because of his or her voluntary termination of employment due to Retirement, ..., that Key Employee may, as determined by the Committee, be entitled to payment.... If a Key Employee terminates service with all Participating Companies during a Performance Period or any applicable Restriction Period for any other reason, then such Key Employee shall not be entitled to any Award with respect to the Performance Period and shall forfeit any shares of Stock subject to the Restriction Period unless the Committee shall otherwise determine.

*PU Plan*

The document submitted for the PU Plan contains the same language as cited above in regard to the Stock Plan.

*D. Argument*

*Hartford*

Hartford contends that the Individual Defendants' counterclaims fail for several reasons. First, according to Hartford, the incentive compensation awards under the Plans are discretionary. Hartford maintains that, given the Individual Defendants' breaches of fiduciary duty and other malfeasance, it is not surprising that, in March 2010, when Hartford distributed annual discretionary bonus compensation and stock incentives under the Plans, it chose not to award the Individual Defendants any post-employment incentive compensation.

Second, according to Hartford, payment under the Plans is tied to continued employment at Hartford. Hartford contends that the language of the Plans and the applicable law mandate that the Individual Defendants' counterclaims under the Plans must be dismissed. It asserts that the Individual Defendants' claims to further compensation under the Plans are contradicted by the explicit language of the Plans, which grants Hartford's board and management discretion regarding payments thereunder. Moreover, Hartford points out that McElroy, while president of HFP, repeatedly confirmed in writing that no employee had a right to any bonus compensation

until such compensation was actually paid. Hartford asserts that, because Rafferty and Price resigned, they were not eligible to receive bonus compensation, even aside from the issue of discretion. Further, Hartford refutes Rafferty's and Price's claim that they were forced to resign – constructively terminated. According to Hartford, it needed the funds from TARP to continue to operate. To obtain such funding, the 25 most highly compensated individuals in Hartford's 30,000-employee workforce, were required to execute federally mandated documentation which would have resulted in pay cuts. Rafferty and Price chose to resign rather than sign the TARP documents.

Finally, Hartford asserts that the Individual Defendants have not suffered any damage, as they have been made whole for any lost incentive compensation as a part of their compensation from Arch. However, as noted below at II(A) and in oral argument, if the Individual Defendants earned the money they are claiming as wages, the money cannot be forfeited. *See Ryan v Kellogg Partners Institutional Servs.*, 79 AD2d 447, 448 (1st Dept 2010). On the other hand, if the money was a discretionary bonus, they will not be entitled to it. *See Gruber v J.W.E. Silk, Inc.*, 52 AD3d 339, 340 (1st Dept. 2008). The compensation the Individual Defendants obtained from Arch is immaterial. This argument, thus, is without merit.

In sum, Hartford contends that all of the Individual Defendants' claims that relate to incentive compensation - the first and second counterclaims, and the fourth counterclaim, to the extent it refers to the first two counterclaim - should be dismissed. It argues that the third counterclaim, and that part of the fourth counterclaim relating to the third counterclaim, which seek indemnification and advancement of legal fees, also are meritless and will be addressed at another time.

*Individual Defendants*

The Individual Defendants explain that they joined HFP in 2000, when Hartford purchased Reliance Group Holdings, an insurance company that went into liquidation and became HFP. They contend that, at Hartford's request, they agreed to accept below-market cash salaries from Hartford in consideration for its agreement to pay them, in addition to their salaries, certain deferred compensation based on the profitability of their endeavors. Defendants maintain that the deferred compensation was to be paid pursuant to what evolved into the Plans. The Individual Defendants state that the compensation was, in part, paid and distributed to them while they were at HFP. They maintain that, at the time they left HFP, they had earned, and were owed by Hartford, substantial additional payments and distributions under the Plans.

Defendants explain that, under the Old Plan, pools were created as to the book of business HFP wrote each year from 2000 onward, and each such pool for each such year was paid out over the course of seven years, based on set formulas applied to the pre-tax profitability of each year's book of business as the seven-year period unfolded. They assert that each participating HFP employee's awards under the Old Plan reflected his or her individual performance and contribution to HFP's results. The Old Plan applied to, and remains in place with respect to, years 2000 through 2006. In 2007, Hartford replaced the Old Plan with the New Plan, under which HFP employees continued to share in HFP's profitability, but on a post-tax basis, with payouts as to the profitability of each business year made only in the third through fifth years, after the conclusion of that year.

Defendants note that, when the New Plan was put into effect, the Old Plan was adjusted to conclude by March 2011, and Hartford allocated to each participant in the Old Plan a set percentage of the pools yet to be paid out thereunder. They contend that, after the set

percentages were allocated to the employees, all payouts under the Old Plan were to be made strictly pursuant to such percentages.

Defendants point out that neither the Old Plan nor the New Plan was reduced to one comprehensive writing. They state that some of the plans' terms were explained in summary documents shown and/or distributed to employees, while other terms were a matter of understandings between Hartford management and HFP employees. According to defendants, under both the Old and New Plans, the awards of employees who retire or who are terminated without cause are immediately and fully vested.

Defendants explain that the PU Plan and the 2005 Stock Plan provide additional compensation to HFP senior management. They state that, under those plans, interests awarded vest 100% at the end of a three-year period, and a retiring employee or an employee terminated without cause is entitled to receive a pro-rated award for the portion of the three-year period during which he or she was actively employed.

The Individual Defendants argue that the awards made to them under the Plans cannot be taken away in Hartford's discretion. They assert that Hartford's position that it is entitled to withhold such awards is contrary to the terms of the Plans, to the interpretation and practice of Hartford when administering those plans, and to Hartford's promise that their deferred compensation awards over time would make up for their sacrifice of immediate cash compensation.

*II. Discussion*

*A. Arch's Counterclaims*

Hartford argues that Arch's counterclaims should be dismissed in their entirety because they fail to state a cognizable claim. Hartford specifically notes that Arch *chose* to enter into

employment packages that would reward the Individual Defendants in the event that they did not receive compensation from Hartford under the Old and New Plans. In any case, according to Hartford, it has no relationship with Arch that would make it liable for Arch's compensation decision and Arch owed no duty to pay the employees. Hartford, therefore, argues that all of Arch's counterclaims should be dismissed.

Indemnification occurs where the liability of one party shifts to another. *Mas v Two Bridges Assocs.*, 75 NY2d 680, 690 (1990). The shift of liability arises from a duty owed to the indemnitee by the indemnitor, either through an express contract or due to vicarious liability of the indemnitee due to the conduct of the indemnitor. *Id.*, 689-90; *see Equitable Life Assurance Society of the U.S. v Werner*, 286 AD2d 632 (1st 2001) ("The key element of a common-law cause of action for indemnification is not a duty running from the indemnitor to the injured party, but rather is 'a separate duty owed the indemnitee by the indemnitor.'" [citation omitted]).

Here, Hartford owed no duty to Arch either by contract or by implied or common law indemnification. Indeed, at oral argument on February 24, 2011, Arch admitted as much. The terms of the Individual Defendants' employment agreements with Arch and the wages paid them by Arch were separate agreements, negotiated by them. Hartford was not privy to them and owed no duty under them. Similarly, Arch was not privy to the agreements between the Individual Defendants and Hartford.

At oral argument, however, Arch explained that it brought the indemnification counterclaims to prevent Hartford from arguing that the Individual Defendants suffered no damages due to Hartford's failure to pay compensation under the Old and New Plans since they received these amounts from Arch. This argument is to no avail, because either the Individual Defendants are owed earned compensation under the terms of the Hartford Plans or they are not.

The compensation they received from Arch is irrelevant. Consequently, Arch's counterclaims are dismissed in their entirety.

*B. Individual Defendants' Counterclaims*

"On a motion to dismiss pursuant to CPLR 3211 (a) (1), the [movant] has the burden of showing that the relied-upon documentary evidence 'resolves all factual issues as a matter of law, and conclusively disposes of the ... claim'" *Fortis Fin. Servs. v Fimat Futures USA*, 290 AD2d 383, 383 (1st Dept 2002), quoting *Scadura v Robillard*, 256 AD2d 567, 567 (2d Dept 1998). Moreover, in assessing the adequacy of pleadings on a motion to dismiss pursuant to CPLR 3211 (a) (7), the court must construe the allegations therein liberally, giving the pleading party the benefit of all favorable inferences. *Leon v Martinez*, 84 NY2d 83 (1994). Allegations that consist of bare legal conclusions, and claims that are contradicted by documentary evidence, however, are not entitled to such a presumption. *Caniglia v Chicago Tribune-N.Y. News Syndicate*, 204 AD2d 233, 233-34 (1st Dept 1994).

*First & Second Causes of Action*

Hartford moves to dismiss the first and second counterclaims. The Individual Defendants' first counterclaim, brought by McElroy, alleges breach of contract, based on Hartford's failure to live up to its commitments to him under the Plans. The second counterclaim, brought by Rafferty and Price, alleges that Hartford breached the implied covenant of good faith and fair dealing in the Plans. They allege no breach of contract claim. The fourth counterclaim alleges that Hartford was unjustly enriched at the Individual Defendants' expense, by the breaches set forth in their first three counterclaims. Hartford moves to dismiss the fourth count to the extent that it relates to the breaches alleged in the first and second counterclaims, but not to the extent it relates to the third counterclaim.

McElroy voluntarily retired from HFP, while Rafferty and Price resigned. Rafferty and Price argue that their resignations were not voluntary. They assert that Hartford wrongfully forced their involuntary resignations, thereby, in effect, terminating them without cause, by offering them an impossible choice under TARP between (a) signing a waiver by which they would agree to slashed compensation; (b) resigning; or (c) being terminated "for cause." According to Rafferty and Price, Hartford, in bad faith, attempted to parlay their contrived resignations into a license to breach its obligations by denying them their entitlements under the Plans. This court finds that the claims of McElroy, who retired, and those of Rafferty and Price, who resigned, must be examined separately.

*Rafferty and Price*

> In general, and like other contractual entitlements, entitlement to a bonus only exists where the terms of the relevant contract require it. "However, this rule is limited by the 'long standing policy against the forfeiture of earned wages.'" Consistent with this rule (and its limitation), where the employee has already earned compensation under the terms of his employment contract, his termination does not affect his rights to that compensation, but where the employer retains discretion to award a bonus (or other compensation), no forfeiture of earned wages occurs if the bonus is not paid. [citations omitted]

*Vetromile v JPI Partners, LLC*, 706 F.Supp2d 442, 448 (SDNY 2010).

Additionally, "[a]n employee's entitlement to a bonus is governed by the terms of the employer's bonus plan." *Hall v UPS of Amer., Inc.*, 76 NY2d 27, 36 (1990); *accord Truelove v Northeast Capital & Advisory, Inc.*, 95 NY2d 220, 225 (2000); *Smalley v The Dreyfus Corp.*, 40 AD3d 99 (1st Dept 2007). Where a bonus plan is reasonably susceptible to one interpretation, extrinsic evidence is inadmissible to vary its language. *Namad v Salomon, Inc.*, 74 NY2d 751, 753 (1989).

It is clear that, if Rafferty and Price had resigned under normal circumstances, their

counterclaims would be dismissed. While there is no single document encompassing the terms of the Old Plan or the New Plan, those documents that have been submitted explicitly provide that an employee who voluntarily resigns is not entitled to any post-resignation payments under the Old and New Plans. This is reinforced in letters McElroy wrote to employees, including Rafferty and Price, describing the transition from the Old Plan to the New Plan and stating that you "must remain an active employee of HFP and/or The Hartford organization at large at the time of actual payment to receive any award[s]." *See Truelove*, *supra* (employee not entitled to bonus where plan explicitly predicated payment upon continuation of employment). The PU Plan and the 2005 Stock Plan also note that employees who resign are not entitled to future benefits, in the form of either compensation or stock incentives. All the plans repeatedly refer to Hartford's discretion in awarding the plans' compensation (*see Namad*, *supra*), the payments as contingent on annual performance [*see Johnson v Stanfield Capital Partners, LLC*, 68 AD3d 628, 385 (1st Dept 2009)], and the ability of Hartford to modify or annul the plans (*see Smalley*, *supra*). Rafferty and Price, thus, attempt to distinguish the TARP-related circumstances under which they resigned from a more typical resignation scenario and attempt to re-categorize their departures as constructive terminations.

This court finds, however, that Rafferty's and Price's resignations were, despite the unusual circumstances, voluntary resignations and were not terminations without cause. The terms of the TARP program were set forth by the federal government. As two of the 25 most highly compensated employees at Hartford, they, like the other 23 most highly compensated employees, had the option to agree to the TARP terms, to resign, or to be terminated for cause from Hartford. They chose to resign. Their attempt to re-characterize what happened, by stating that Hartford wrongfully forced their involuntary resignations, is not persuasive.

Rafferty and Price do not allege breach of contract. Instead, they allege breach of the implied covenant of good faith and fair dealing. An implied obligation of good faith and fair dealing "is in aid and furtherance of other terms of the agreement of the parties. No obligation can be implied, however, which would be inconsistent with other terms of the contractual relationship." *Murphy v American Home Prods. Corp.*, 58 NY2d 293, 304 (1983). Hartford acted in compliance with the terms of the Plans in denying Rafferty and Price further compensation or payments thereunder after they resigned. As a result, their claim for breach of implied covenant of good faith and fair dealing, is dismissed.

*McElroy*

To begin, plaintiffs conceded during oral argument that McElroy, as a retiree, is entitled to payment under the 2005 Stock Plan and the PU Plan. Plaintiffs stated that McElroy has been paid under these plans and will continue to be paid under them. Hence, the only issues before this court on this motion is McElroy's entitlement to payment under the Old and New Plans.

The Plans treat one whose employment with HFP ends by retirement, differently from how they treat an employee who voluntarily resigns or is terminated for cause. However, where the New Plan directly and explicitly explains the rights of a retiree, the Old Plan, in the Powerpoint presented, states that a retire "may" be eligible to payment pursuant thereto, at Hartford's discretion. McElroy's own letters, on the other hand, specifically warn that payments under the plans are discretionary, confined to active employees and may be terminated or amended at any time. Therefore, the Old Plan is ambiguous as to whether McElroy is entitled to payment.

The documentary evidence submitted in regard to the New Plan explicitly states that a retiree vests in the Plan upon retirement. The New Plan speaks to pro-rata payments. Certain benefits

under the Plan, thus, continue after employment ends in the case of a retiring employee. Consequently, this court finds that McElroy's first counterclaim, sounding in breach of contract, survives the instant motion.

*Unjust Enrichment*

The unjust enrichment cause of action, to the extent it relates to the first and second causes of action, is dismissed as to the Individual Defendants, because the terms of the Plans deal with the same subject matter as the unjust enrichment claim. *See Johnson*, 68 AD3d 629 (party may not recover under quasi-contractual theory where relationship is governed by contract); *Goldstein v CIBC World Mkts. Corp.*, 6 AD3d 295, 296 (1st Dept 2004) (unjust enrichment claim dismissed where contract covering same subject matter exists between parties).

*Request To Replead*

Defendants requested that, if the court were to dismiss the counterclaims, they be granted leave to replead, a request opposed by Hartford. Hartford notes that its motion to dismiss is based, in part, on documentary evidence that firmly contradicts the counterclaims and maintains that these documents will not change, such that any repleaded counterclaims again would be deficient.

Presumably Arch will not seek to replead its counterclaims, based on its contentions at oral argument. The Individual Defendants have not submitted their proposed counterclaims. Given that the second counterclaim is dismissed on the basis of documentary evidence, and given that the fourth counterclaim is dismissed to the extent it refers to the first and second counterclaims, this court does not, at this time, foresee repleaded counterclaims that could remedy the shortcomings of the dismissed counterclaims. If, however, the Individual Defendants believe they can overcome the weaknesses in their current counterclaims, they may

move for leave to replead, and submit such proposed repleaded counterclaims to this court, which will then determine their adequacy. While leave to amend or replead is generally freely granted, a court should deny leave when the proposed amendment or repleading "is devoid of merit or palpably insufficient." *Janssen v Incorporated Vil. of Rockville Ctr.*, 59 AD3d 15, 27 (2d Dept 2008); *Mehlman v Gold*, 183 AD2d 634 (1st Dept 1992). Accordingly, it is

ORDERED that plaintiffs' motion to dismiss the counterclaims of defendants Arch Insurance Group., Inc and Arch Capital Group Ltd is granted; and it is further

ORDERED that plaintiffs' motion to dismiss the first counterclaim of defendants David McElroy, John Rafferty and Michael Price for breach of contract, is denied; and it is further

ORDERED that plaintiffs' motion to dismiss the second counterclaim for breach of the covenant of good faith and fair dealing of defendants David McElroy, John Rafferty and Michael Price is granted; and it is further

ORDERED that plaintiffs' motion to dismiss the fourth counterclaim of unjust enrichment of defendants David McElroy, John Rafferty and Michael Price, is dismissed to the extent said counterclaim relates to their first and second counterclaims; and it is further

ORDERED that plaintiffs are directed to serve a reply to the remaining counterclaims within 20 days after entry of this order upon the efiling system.

Dated: July 12, 2011

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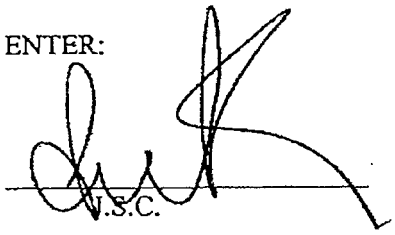

J.S.C.