SUPERIOR COURT OF THE VIRGIN ISLANDS

DIVISION OF ST. THOMAS AND ST. JOHN

EMPLOYEES' RETIREMENT SYSTEM OF THE GOVERNMENT OF THE VIRGIN ISLANDS, **Plaintiff,** **vs.** **BEST CONSTRUCTION, INC., EDMUND C. SCARBOROUGH a/k/a E.C. SCARBOROUGH Individual Surety and INTERNATIONAL BONDING & CONSTRUCTION SERVICES, INC. d/b/a THE IBCS GROUP, INC.,** **Defendants.**	**CASE NO. ST-08-CV-490**
EDMUND C. SCARBOROUGH a/k/a E.C. SCARBOROUGH Individual Surety, **Third Party Plaintiff,** **vs.** **UNDERWRITERS REINSURANCE, CO., LTD, THE UNDERWRITERS GROUP, INC. and FIRST MOUNTAIN BANCORP,** **Third Party Defendants.**	

MEMORANDUM OPINION

Pending before the Court are cross motions for summary judgment filed by the Employees' Retirement System of the Government of the Virgin Islands ("GERS")[1] and

[1] GERS filed its motion on May 31, 2011, and a renewed motion for summary judgment on July 13, 2011. Scarborough and IBCS filed an opposition on August 2, 2011, and GERS filed a reply on August 12, 2011.

Defendants Scarborough and IBCS Group.[2] For the following reasons, GERS' motion will be granted, thereby denying Defendants' motion.

FACTUAL AND PROCEDURAL HISTORY

On July 28, 2005, GERS and Best Construction entered into a contract concerning the construction of the GERS office building complex on St. Croix. On August 9, 2005, Edmund Scarborough, acting in the capacity of an individual surety, issued bond[3] number BESTPP080905 in the amount of Four million nine hundred sixty-two thousand four hundred eighty dollars ($4,962,480.00). Scarborough is also the chief executive officer of IBCS Group, Inc. On August 9, 2005, Scarborough signed an "affidavit of individual surety" stating that an irrevocable trust receipt issued by First Mountain Bancorp in the amount of $4,962,480.00 represented his "present assets, liabilities, and net worth and does not include any financial interest that [he has] in the assets of the principle on the attached bond." On August 11, 2005, First Mountain issued an irrevocable trust receipt that acknowledged the receipt of cash or cash equivalents totaling $4,962,480.00. The trust receipt indicates that First Mountain would hold the $4,962,480.00 in an escrow account for seventeen (17) months on behalf of GERS. On January 30, 2008, GERS submitted a letter to Best Construction and Scarborough, as individual surety and CEO of IBCS, that terminated the construction contract on the grounds that Best Construction purportedly did not comply with the terms of the agreement. On April 2, 2008, Scarborough sent GERS a letter asserting that any claim GERS had against Scarborough

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[2] Defendants served a second amended motion for summary judgment on GERS on February 22, 2011, and filed the motion on April 1, 2011. GERS filed an opposition on March 21, 2011.

[3] The bond is identified as a "payment bond" on the bond itself and as a "bid bond and/or payment & performance bond" on the affidavit of individual surety.

was denied because the bond had expired before Best Construction's default under the contract. On October 17, 2008, GERS filed a Complaint against Best Construction, Scarborough, and IBCS to recover the debt GERS had incurred to independently complete the office complex.

STANDARD OF REVIEW

Rule 56 of the Federal Rules of Civil Procedure, made applicable to the Virgin Islands Superior Court through Rule 7 of the Rules of the Superior Court, provides that summary judgment is appropriate only "if the pleadings, depositions, answers to interrogatories, and admissions on file, together with the affidavits, if any, show that there is no genuine issue as to any material fact and that the moving party is entitled to a judgment as a matter of law." In considering a motion for summary judgment, a court must "draw … all reasonable inferences from the underlying facts in the light most favorable to the non-moving party." *Battaglia v. McKendry*, 233 F.3d 720, 722 (3d Cir. 2000). An issue is "genuine" if a reasonable jury could possibly hold in the nonmovant's favor with regard to that issue. *Andersen v. Liberty Lobby, Inc.*, 477 U.S. 242, 247-48 (1986).

ANALYSIS

a) The surety bond has not expired.

Initially, Defendants assert that the bond and the irrevocable trust receipt must be read together. Parties to an agreement may incorporate contractual terms of a separate document into the agreement as long as the agreement makes clear reference to the separate document. See *Standard Bent Glass Corp. v. Glassrobots Oy*, 333 F.3d 440, 447 (3d Cir. 2003) (citing Williston on Contracts § 30.25 (4th ed. 1999)); see also *Titan Stone, Tile & Masonry, Inc. v. Hunt Const. Group, Inc.*, 394 F. App'x 862, 865 (3d Cir. 2010) (when a surety bond incorporates a subcontract by reference, "the bond and the contract must be considered as one integrated document"). Section 13 of the bond indicates that is "not valid without attached TRUST RECEIPT." (Bond number BESTPP080905, at page 4). The affidavit of individual surety also contains the same language. The trust receipt states that "payment under this TRUST RECEIPT will be made to [GERS] … conditioned by the Payment & Performance Bond criteria." (Trust receipt, at page 1). As a result, the bond and the trust receipt will be read as a single document.

Next, Defendants argue that the trust receipt had an effective period of seventeen months, after which the trust receipt expired. In addition, Defendants argue that because the bond contains language indicating that the bond is not valid without the trust receipt, the bond expired once the trust receipt expired. In support of their contentions, Defendants cite *U.S. ex rel. Hajoca Corp. v. Associated Mechanical, Inc.*, No. 2:09-cv-02087, 2011 WL 484291 (D. Nev. 2011), in which Defendant Scarborough also acted as a surety. In *Hajoca*, Amerind Builders, LLC, was the primary contractor on a construction project known as "Bldg. B718 and Bldg. B707/Contract No. FA4861-07-C-A027" located on Creech Air Force Base in Indiana Springs, Nevada. *Id.* at *1. Defendant Scarborough had issued payment and performance bonds in accordance with the terms of the contract for the project. A certificate of pledged assets was incorporated by reference into the bonds. The court determined that the certificate was dated

November 14, 2007, and was effective until the earlier of the completion of the project or twelve months. Considering that the construction project was still in operation twelve months after November 14, 2007, the court determined that the certificate and the bond, number AMERINDPP1114007, expired on November 14, 2008. Similarly, in *U.S. Government ex rel. Russel Sigler, Inc. v. Associated Mechanical, Inc.*, No. 2:09-cv-01238, 2010 WL 5100913 (D. Nev. 2010) the court considered many of the same facts as in *Hajoca* and determined that bond number AMERINDPP1114007 unambiguously terminated twelve months after its effective date due to the fact that the bond was integrated with the certificate of pledged assets, which was valid for twelve months.

Both *Hajoca* and *Sigler* rely heavily on the decision in *U.S. for Use of Modern Electric, Inc. v. Ideal Electronic Sec. Co., Inc.*, 868 F.Supp. 10 (D.D.C. 1994). In *Modern Electric*, a July 29, 1991, construction contract provided that performance and payment bonds would be issued and would "be separate for the base year and each option year. If the option is exercised, the Contractor shall be required to provide the appropriate Performance and Payment Bonds at that time." *Id.*, at 12. A surety payment bond was then issued stating it covered the July 29, 1991, contract. The Court concluded that although the bond did not specify an expiration date, the bond stated that its coverage was limited to the first year of a multi-year option contract and therefore expired on July 29, 1992. *Id.*, at 12 and 13.

The Court finds *Modern Electric, Hajoca,* and *Sigler* to be distinguishable from this case. The bond in *Modern Electric* specified a period of effectiveness, and, by extension, indicated a termination date. Moreover, the bond specifically stated that new bonds had to be issued to cover the option years of the contract if the option was exercised. In contrast, there is no such specific language delineating the effective period of the bond itself in this case. Similarly, the certificate of pledged assets in *Hajoca* and *Sigler* clearly stated that "upon completion of the Project but not to exceed twelve (12) months … this pledge agreement and all rights of any kind which Pledgee/Obligee has or may have under the pledge agreement and to the assets, shall be returned to the Pledgor and this pledge agreement shall be terminated." In contrast, the trust receipt here at issue merely states First Mountain shall hold the $4,962,480.00 in escrow for GERS for seventeen months. The trust receipt noticeably lacks clear language specifying what would happen to the funds in the escrow account on January 11, 2007, seventeen months from the date the trust receipt was issued. Based on the language of the trust receipt, it is not altogether clear whether the trust receipt expired on January 11, 2007.

Pursuant to Restatement (Second) of Contracts § 212, "the interpretation of an integrated agreement is directed to the meaning of the terms of the writing." An "unambiguous … contract must be enforced irrespective of the [contracting] parties' subjective intent." *Travelers Indem. Co. v. Bailey*, __U.S.___, 129 S.Ct. 2195, 2204 (2009) (citing Williston on Contracts § 30:4 (4th ed. 1999)). Ambiguous contract language should be construed against the drafter. *Viera v. Life Ins. Co. of North America*, 642 F.3d 407, 418 (3d Cir. 2011); see also *Fidelity Trust Co. v. American Sur. Co. of N.Y.*, 268 F.2d 805, 806 (3d Cir. 1959) (if there is doubt about the meaning of the language in a surety bond, it is not to be resolved in favor of the surety). Defendants' failure to include clear termination language in the trust receipt created an ambiguity that should be construed against Defendants.

A surety bond is "a promise to pay a certain amount, conditioned on the occurrence of certain events." *Prosser v. Prosser*, 907 F.Supp. 906, 908 (D.V.I. 1995). See also *G.D. Deal Holdings, Inc. v. Cincinnati Ins. Co.*, No. 1:05CV-3-R, 2007 WL 3306109, at *2 (W.D. Ky. 2007) "a bond is a written promise to pay money or do some act if certain circumstances occur" (citing Black's Law Dictionary 73 (2d pocket ed.1996)). Release of collateral without the substitution of collateral of equal value may discharge a surety's obligation under a bond to the extent that the collateral is impaired. Restatement (Third) of Suretyship and Guaranty § 42. Collateral may be impaired by failing to maintain perfection of the security interest in the collateral. Restatement (Third) of Suretyship and Guaranty § 42(2)(a). A security interest may be effectuated automatically upon attachment, 11A V.I.C. § 9-309; upon the filing of a financing statement, 11A V.I.C. § 9-310; by possession of an item, 11A V.I.C. § 9-313; or by control, 11A V.I.C. § 9-314. A deposit account may be perfected by control. 11A V.I.C. § 9-314.

Even if the Court were to find that the trust receipt expired on January 11, 2007, this finding would not necessarily determine the effective period of the bond. The trust receipt evidences GERS' control over the funds in the escrow account, a type of deposit account. Assuming, *arguendo*, that GERS' control over the funds may have expired on January 11, 2007, causing the security interest to be released, this fact alone has no bearing on whether the bond itself expired or whether Scarborough was discharged of his obligations under the bond. Where a secondary obligor is subrogated to the rights of an obligee, the secondary obligor may enforce the rights of the obligee against another secondary obligor, see Restatement (Third) of Suretyship and Guaranty § 28(1)(b), and against any interest in property securing the obligation of the other secondary obligor, see Restatement (Third) of Suretyship and Guaranty § 28(1)(c). There is no indication that § 28(1)(b) and § 28(1)(c) are interdependent, in which case a party's inability to enforce the obligee's rights against a secondary obligor's collateral does not necessarily preclude the party from enforcing the obligee's rights against the secondary obligor itself. Similarly, the release of GERS' security interest in the $4,962,480.00 collateral on January 11, 2007, could make it more difficult for GERS to obtain satisfaction from Scarborough in the event of a default but does not foreclose GERS' ability to obtain satisfaction from Scarborough altogether. Moreover, Defendants have provided no evidence that the $4,962,480.00 collateral was impaired on or after January 11, 2007. Accordingly, the Court is unable to find that the collateral is impaired.

Notwithstanding, Defendants contend that Scarborough's obligations under the bond were discharged because section 13 of the bond states it is "not valid without attached TRUST RECEIPT." The Court notes that the affidavit of individual surety also contains the same language. Considering that the bond was issued, and the affidavit of individual surety was formulated, on August 9, 2005, two days before the trust receipt was issued, section 13 can be reasonably construed to merely require that a trust receipt be executed and be attached to the bond in order for the bond to be valid. If Scarborough intended that the bond would be valid only as long as the trust receipt remained in full force and effect, he should have included specific language in the bond and/or the trust receipt so stating. See *Bobb v. Frank L. Talbot Theater Co.*, 221 S.W. 372, 374 (Mo. 1920) ("the measure of [a surety's] liability is fixed by the terms of the instrument which he signs, and such undertaking, when plainly expressed, cannot be enlarged or varied by judicial construction").

Finally, Defendants point out that, according to federal regulations, an individual surety "must execute the bond, and the unencumbered value of the assets (exclusive of all outstanding pledges for other bond obligations) pledged by the individual surety … must equal or exceed the penal amount of each bond." 48 CFR 28.203(b). In addition, Defendants indicate that 48 CFR 28.203(b) is relevant considering the fact that section 13 of the bond states that "by accepting this bond, the owner is exercising their home rule right to accept an 'Individual Surety' per Federal regulations." This language in the bond does not prove that the bond expired on January 11, 2007. Based on the plain language of the bond, the Court finds that the bond lacks an expiration date, in which case the bond remains in effect and Scarborough has not been discharged of his obligations under the bond.

b) Defendants are in default under the terms of the bond.

Section 14.2.1 of the construction contract indicates that the owner, GERS, may terminate the contract if Best Construction:

> persistently or repeatedly refuses or fails to supply enough properly skilled workers or proper materials; [or] fails to make payment to Subcontractors for materials or labor in accordance with the respective agreements between the contractor and the subcontractors….

GERS asserts that Best Construction was unable to make payments to subcontractors for labor and materials and that, on more than one occasion, GERS paid subcontractors directly and purchased materials in order to keep the project going. In contrast, Defendants assert that GERS failed to make timely payments under the terms of the contract, which prevented Best Construction from completing the project.

Defendants have not cited any specific provisions of the contract that GERS purportedly violated that would justify Best Construction's failure to complete the construction project. The Court is not in the position, nor does it possess the resources, to sift through the contract to discover all the contractual provisions that could support Defendants' position. See *Premier Capital Management, LLC v. Cohen*, No. 02 C 5368, 2008 WL 4378300, at *2 (N.D. Ill. 2008); see also *United States v. Dunkel*, 927 F.2d 955, 956 (7th Cir. 1991) ("[j]udges are not like pigs, hunting for truffles buried in briefs."). Notwithstanding, section 9.3.1 of the contract indicates that "[a]t least ten days before the date established for each progress payment, the Contractor shall submit to the Architect an itemized Application for Payment for operations completed in accordance with the schedule of values. Such application shall be notarized, if required, and supported by such data substantiating the Contractor's right to payment as the Owner or Architect may require." Under section 9.4.1, "the Architect will, within seven days after receipt of the Contractor's Application of Payment, either issue to the Owner a Certificate for Payment … for such amount as the Architect determines is properly due or notify the Contractor and Owner in writing of the Architect's reasons for withholding certification in whole or in part." Only after the Architect has issued the Certificate of Payment is the

Owner obligated to "make payment in the manner and within the time provided in the Contract Documents." (Construction contract, § 9.6.1). GERS submits a January 30, 2008, letter that was sent to Defendants and Best Construction entitled "notice of default and termination of contract" in which GERS stated that the "Architect has also certified that sufficient cause exist (sic) to terminate the contract." On the other hand, Defendants have not presented any evidence that would suggest that the architect issued Certificates of Payment to GERS that GERS did not honor. Mere allegations of nonpayment are insufficient. Without a showing that Best Construction properly followed the procedure for payment as set forth in the contract, Defendants have not raised a triable issue of fact surrounding the issue of Best Construction's default under the contract.

Given that the Court finds that Best Construction was in default, Defendants were obligated to complete the project under section 4 of the bond, failing which Defendants would be deemed to be in default on the bond "fifteen days after receipt of an additional written notice from the Owner to the Surety demanding that the Surety perform its obligations under this Bond." (Bond, § 5). The April 2, 2008, letter sent by Defendants to GERS, asserting that GERS' claim under the bond is denied, indicates that Defendants effectively treated GERS' January 30, 2008, letter as a written notice to the surety under section 5 of the bond. As Defendants have not submitted any evidence indicating that Scarborough completed his obligations under section 4 of the bond and completed the construction project, there is no triable issue as to whether Scarborough is in default under the terms of the bond.

Considering that Defendants have not raised any genuine issues of material fact whereby a reasonable jury could possibly hold in Defendants' favor, GERS is entitled to a judgment as a matter of law. Accordingly, GERS' motion for summary judgment will be granted and Defendants' motion for summary judgment will be denied. An Order consistent with this Opinion shall follow.

Dated: September 12, 2011

HON. MICHAEL C. DUNSTON
JUDGE OF THE SUPERIOR COURT
OF THE VIRGIN ISLANDS

ATTEST: Venetia H. Velazquez, Esq.
Clerk of Court

by: Lori B Tyson
Lori Boynes-Tyson
Court Clerk Supervisor 9/13/11

SUPERIOR COURT OF THE VIRGIN ISLANDS

DIVISION OF ST. THOMAS AND ST. JOHN

EMPLOYEES' RETIREMENT SYSTEM OF THE GOVERNMENT OF THE VIRGIN ISLANDS, **Plaintiff,** **vs.** **BEST CONSTRUCTION, INC., EDMUND C. SCARBOROUGH a/k/a E.C. SCARBOROUGH Individual Surety and INTERNATIONAL BONDING & CONSTRUCTION SERVICES, INC. d/b/a THE IBCS GROUP, INC.,** **Defendants.**	**CASE NO. ST-08-CV-490**
EDMUND C. SCARBOROUGH a/k/a E.C. SCARBOROUGH Individual Surety, **Third Party Plaintiff,** **vs.** **UNDERWRITERS REINSURANCE, CO., LTD, THE UNDERWRITERS GROUP, INC. and FIRST MOUNTAIN BANCORP,** **Third Party Defendants.**	

ORDER

Upon consideration of the premises, it is hereby

ORDERED that the Employees' Retirement System of the Government of the Virgin Islands' motion for summary judgment is GRANTED; and it is

ORDERED that Edmund C. Scarborough and IBCS Group, Inc.'s motion for summary judgment is DENIED; and it is

ORDERED that a Judgment is entered in favor of Plaintiff GERS; and it is

ORDERED that a copy of this Order shall be directed to counsel of record.

Dated: September 12, 2011

HON. MICHAEL C. DUNSTON
JUDGE OF THE SUPERIOR COURT
OF THE VIRGIN ISLANDS

ATTEST: Venetia H. Velazquez, Esq.
Clerk of Court

by:
Lori Boynes-Tyson
Court Clerk Supervisor 9/13/11