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Hearings Unit, OIC
Patricia D. Petersen
Chief Hearing Officer

**BEFORE THE STATE OF WASHINGTON
OFFICE OF INSURANCE COMMISSIONER**

In the Matter of

**EDMUND C. SCARBOROUGH and
WALTER W. WOLF,**

Respondents.

Docket No. 13-0084

**OIC'S OPPOSITION TO
SCARBOROUGH'S MOTION
FOR SUMMARY JUDGMENT
AND CROSS-MOTION FOR
SUMMARY JUDGMENT**

I. INTRODUCTION

After Respondent Edmund C. Scarborough and Respondent Walter W. Wolf ("Respondents") transacted certain of Mr. Scarborough's surety bonds in Washington, copies of these bonds were given to the Washington State Office of the Insurance Commissioner ("OIC") with a complaint. Although these are surety bonds, are Mr. Scarborough's bonds, and they do unequivocally indicate that Mr. Scarborough purports to be the surety who issued them, Mr. Scarborough contends that he enjoys a special and different status, "individual surety." He theorizes that once he has given himself this status, he can transact surety insurance free from the requirements of the Washington Insurance Code ("Insurance Code" or "Code"). He claims that his theorem rings especially true for the surety bonds he has issued for federal projects/contracts. Mr. Scarborough is wrong, his motion for summary judgment should be denied, and OIC's cross motion on all issues in its favor should be granted.

II. BACKGROUND

A. *Overview of Surety Bonds.*

A surety bond is a contract involving three parties in which a surety assumes the responsibility for the debt or default of obligations owed by a principal to an obligee.

Although used in a variety of circumstances, surety bonds are common in the construction business. Construction projects routinely involve three types of surety bonds: (i) bid bonds, which guarantee that a principal can perform the work promised in its bid if it is awarded a contract; (ii) performance bonds, which guarantee that a principal will perform work under the contract; and (iii) payment bonds, which guarantee that a principal will pay for labor and supplies required to complete the work. In short, these surety bonds ensure against financial loss by the obligee in the event that a principal cannot meet its obligations on a construction project.

For construction projects, the principal (usually a general contractor or subcontractor) obtains a surety to provide surety bonds for the benefit of the obligee (usually the governmental or private entity requesting the work, or the general contractor on the project). If the principal fails to perform or make payment as required, the obligee may call the bond and demand payment from the surety. As such, the surety's financial stability and assets available to cover potential losses are essential to ensure payment in the event of loss or default by the principal.

B. *Overview of Corporate Sureties and Individual Sureties.*

Corporate sureties are incorporated entities subject to licensure and oversight by the OIC and other state insurance regulators in those states in which they are domiciled and/or

1 transact business. In Washington, as detailed in the Insurance Code, corporate sureties must
2 be authorized and qualified to do business, satisfy capital requirements, file reports, and
3 comply with other laws relating to their financial condition. *See, e.g.,* RCW 48.05 *et seq;*
4 RCW 48.12 *et seq;* RCW 48.13 *et seq;* etc. Under the Code's requirements, corporate sureties
5 must have sufficient assets to cover bonds that they issue, follow statutes regarding quality
6 and types of assets held for potential claims, and meet other requirements. Corporate sureties
7 are recognized and regulated by all fifty states.

8 Federal law also recognizes corporate sureties while providing separate procedures for
9 qualifying and approving them for federal public works projects. Pursuant to the Miller Act,
10 the United States requires contract surety bonds on federal construction projects. *See* 40
11 U.S.C. §§ 3131 to 3134. Specifically, Section 3131 of the Miller Act requires performance
12 and payment bonds for contracts of more than \$100,000 awarded for the construction,
13 alteration, or repair of any public building or public work of the Federal Government. These
14 surety bonds are required to protect the United States Government and its contractors from
15 losses in the event of default or non-payment.¹ Contracting officers for the Federal
16 Government review the qualifications of sureties and approve their use independent of any
17 involvement by state regulators.

18 Corporate sureties issuing bonds for projects under the Miller Act must be listed as a
19 qualified surety on the Treasury List, which identifies sureties who have applied for
20 recognition as qualified sureties and demonstrated that they are financially sound. Such
21 corporate sureties are supposed to be incorporated under the laws of the United States, the
22
23

1 States or territories, and “that may under those laws guarantee (A) the fidelity of persons
2 holding positions of trust; and (B) bonds and undertakings in judicial proceedings.” 31
3 U.S.C. § 9304(a).

4 Individual sureties are fundamentally different from corporate sureties, as explained
5 below, but individual sureties may provide surety bonds for federal contracts under the Miller
6 Act provided they follow certain prescribed procedures. Part 28.2 of the Federal Acquisition
7 Regulations (“FAR”) “prescribes procedures for the use of sureties to protect the Government
8 from financial losses.”² FAR 28.200. These procedures include the requirements that an
9 individual surety place cash or cash equivalents equal to the amount of the bonds in escrow
10 with a federally insured financial institution, or provide the Federal Government with a deed
11 of trust on real property with sufficient equity to secure the bond. *See* FAR 28.203-2 and
12 28.203-3. Additionally, Section 28.203(b) requires individual sureties to complete Standard
13 Form 28 – which is an “Affidavit of Individual Surety” that must describe the pledged assets.

14 Prior to 1990, the Federal Government had less stringent procedures for individual
15 sureties on federal projects. At that time, individual sureties only needed to provide a sworn
16 statement that their net worth exceeded the bond obligation. *See* FAR 28.202-2(a) (48 C.F.R.
17 § 28-202 (1988)). Following numerous abuses and fraud, the FAR was amended in 1990 to
18 require individual sureties to pledge cash or cash equivalents. *See* FAR; Individual Sureties,
19 53 Fed. Reg. 44,564 (Nov. 3, 1988). Problems regarding verification of individual surety
20 assets, however, have required continued vigilance in view of concerns that such assets may
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23 ¹ The Miller Act, however, neither applies to nor protects all persons in the contract chain for federal projects. For example, subcontractors may not be able to make claims under the Miller Act and the subcontractors' surety bonds are not governed by the requirements of the Miller Act.

1 not be appropriate, may not be readily available, or may not even exist in the event of a loss.³
2 See *Tip Top Constr., Inc. v. United States*, 563 F.3d 1338, 1343-44 (Fed. Cir. 2008) (holding
3 that individual surety may not pledge mined coal as an acceptable asset under FAR 28.203
4 because of difficulty in evaluating its value and liquidity).

5 Various state insurance regulators have taken action to enjoin the activities of
6 individuals who have claimed to be “individual sureties” but who were actually transacting
7 surety insurance business in their states. Two illustrative examples are Robert Joe Hanson
8 and Lawrence (“Larry”) Wright. Mr. Hanson, like Mr. Scarborough, individually and through
9 several companies, engaged in a business of providing surety bonds for state and local
10 construction projects across the country. Numerous state regulators, however, discovered that
11 Hanson was not licensed, his companies were not qualified to do business, and that he had
12 misrepresented the nature and ownership of the assets allegedly backing his surety bonds.
13 Virginia was among the states that pursued Hanson to stop him from acting as an individual
14 surety. See *Commonwealth ex rel. State Corp. Comm'n v. Global Bonding, Inc.*, Case No.
15 INS-2007-00155 (filed July 20, 2007) (enjoining Hanson from transacting surety insurance in
16 Virginia). Virginia, however, was not alone in taking action against Hanson’s individual
17 surety business. See, e.g., *In the Matter of Individual Sur., Ltd.*, Case No. 2004-19 (Mt. Dep’t
18 Ins., filed Feb. 22, 2007) (ordering Hanson to cease and desist from operating as an illegal
19 surety in Montana and imposing penalties); Official Order of the Comm’r of Ins. of the State
20 of Tex. (filed Mar. 3, 2005) (ordering Hanson to cease and desist from providing surety
21

22 ² FAR is codified in 48 C.F.R. pt. 1 to 51. The portion of FAR addressing sureties is located at 48 C.F.R. pt. 28.

23 ³ Scarborough was the individual surety who attempted to pledge the coal assets that were the subject of the Federal Circuit’s decision in *Tip Top Construction*.

1 insurance in Texas); *In the Matter of Individual Sur., Ltd.*, No. D04-189 (OIC, filed Aug. 27,
2 2004) (ordering Hanson to cease and desist from providing surety insurance in Washington);
3 *In the Matter of Global Bonding*, Cause No. 03.757 (Nev. Div. of Ins., filed Mar. 9, 2004)
4 (ordering Hanson to cease and desist from providing surety insurance in Nevada and noting
5 prior violations of cease and desist orders); *In the Matter of Global Bonding, Inc.*, Docket No.
6 MC 04-39 (Conn. Ins. Dep't, filed Apr. 1, 2004) (ordering Hanson to cease and desist from
7 providing surety insurance in Connecticut); *In the Matter of Global Bonding*, Case No.
8 72037-03-CO (Fla. Off. of Ins. Reg., filed Dec. 23, 2003) (ordering Hanson to cease and
9 desist from providing surety insurance in Florida); and *In the Matter of Global Bonding*, Case
10 No. EF-2003-023 (Ga. Office of Comm'r of Ins., filed Dec. 9, 2003) (ordering Hanson to
11 cease and desist unauthorized surety business in Georgia).⁴

12 Mr. Scarborough's former business partner, Larry Wright, also has been the subject of
13 state regulatory action for his engagement in the business of transacting surety insurance
14 while pretending to be an "individual surety." Mr. Wright, individually and through his
15 "Underwriters Reinsurance Co. Ltd.," provided surety bonds, even though they were not
16 licensed to provide insurance and were found financially untrustworthy. *See Oklahoma ex*
17 *rel. Holland v. Underwriter Reins. Co. Ltd.*, Case No. 08-0420-UNI (Ok. Ins. Comm'r, filed
18 Aug 6, 2008) (ordering Wright and Underwriters Reinsurance to cease and desist from
19 providing insurance in Oklahoma). *See Decl. Singer Exh. A.*

20 Mr. Scarborough has also been the subject of similar regulatory actions in Iowa,
21 Virginia, and Idaho. Each of these states has determined him to be in violation of state
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23 ⁴ Copies of these actions are attached to the declaration accompanying this motion. *See Decl. Singer Exh. A.*

1 insurance regulatory laws. *See* Decl. Singer Exhs. A and B. He, too, claims to be an
2 “individual surety,” but is not.

3
4 **III. FACTS**

5 OIC has been denied reasonable discovery answers and responses, and so is limited in
6 its present ability to present evidence concerning how Mr. Scarborough sells bonds. For
7 example, when asked in discovery (e.g., interrogatory number 3) how Mr. Scarborough
8 markets his bonds, he refused to answer the question and merely listed objections to the
9 question. OIC asked for a stipulation of facts for purposes of this motion, but received none.
10 OIC has been given no opportunity to cross-examine Mr. Scarborough as to the statements he
11 has asserted in his various declarations submitted to date, and OIC has not received full and
12 complete answers and responses to discovery propounded to him. Accordingly, OIC disputes
13 many assertions in his declaration supporting his motion for summary judgment, specifically
14 including his assertion that his bonds are supposedly “fully collateralized” (as this appears at
15 odds with the fact that Mr. Scarborough and his wife and business partner, Yvonne, filed for
16 Chapter 13 bankruptcy protection in federal court, and that in discovery Mr. Scarborough has
17 refused to provide any statement of his net worth and solvency and other relevant
18 information), and his declaration paragraphs number 3, 6, the first two sentences of 7, 8, and
19 all but the first and last sentences of 9, as these set forth inadmissible conclusory statements,
20 legal conclusions, and opinions; such statements are inadmissible, should be stricken, and
21 should not be considered on summary judgment.⁵

22
23 For purposes of this motion, the following facts, gleaned from other sources in the
face of Mr. Scarborough’s refusal to provide discovery, are reflected in documents setting
forth those facts. Those documents are attached and incorporated into the Declaration of Alan

⁵ Legal conclusions are improper, inadmissible, and must be disregarded for purposes of a summary judgment motion. *Orion v. State*, 103 Wn.2d 441, 462, 693 P.2d 1369 (1985).

1 Michael Singer Opposing Edmund Scarborough's Motion for Summary Judgment ("Del.
2 Singer") filed herewith. Those documents reveal the following facts:

3 Mr. Scarborough sells surety bonds on construction projects. He sells them in all
4 states and in Puerto Rico. Since 2004 he has sold 7,000 such bonds. In 2006 alone, Mr.
5 Scarborough's business collected nearly \$6 million in "premium income." Mr. Scarborough
6 has issued bonds on at least 22 projects in Washington, supposedly backed by his own assets,⁶
and has shared copies. See Decl. Singer Exh. E.

7 As part of his bond business, Mr. Scarborough maintains a number of websites which
8 advertise his business activities to persons in all states, including Washington. On his
9 advertisements to the public in his scarboroughbonds.com website, for example, he equates
10 his bonds to those of a surety company or a corporate firm. Mr. Scarborough advertises his
11 bonds for sale to the public and his website references at least five other different websites
12 apparently connected to him. On at least one such website, Mr. Scarborough argues that
13 corporate surety bonds have "inherent weaknesses" and he encourages the public to purchase
his bonds instead.

14 Mr. Scarborough has worked with and still may work with brokers and insurance
15 producers to help himself secure new bond business. He modifies bond forms as he wishes to
16 include language favorable to only himself. He protects his interests in the bonds he issues
17 using indemnity agreements. He implements "funds control" if he receives claims under his
18 bonds.

19 Mr. Scarborough collects "premiums" for the bonds he issues; he also calls these
20 monies "fees." His premium rates are "considerably higher" than those charged by authorized
21 surety insurance companies he competes with; he apparently charges a flat rate of \$35 per
thousand dollars. He has refused to disclose the total amount of premium collected on his

22 ⁶ For purposes of summary judgment, OIC does not dispute that Mr. Scarborough has made statements regarding
23 alleged collateral for bonds. But OIC does not concede that the value of any such collateral equals or exceeds
the value of contracts guaranteed by Mr. Scarborough.

1 Washington bonds, but if he charges \$35 per thousand dollars, and has issued 7,000 bonds,
2 then his business is a multi-million dollar business.

3 Mr. Scarborough has an application for those interested in purchasing his bonds, with
4 a non-refundable underwriting fee of \$750. Mr. Scarborough engages in underwriting efforts
5 before issuing his bonds. (However, the details of this underwriting have not been disclosed
6 to OIC, because Mr. Scarborough has refused to provide reasonable answers and responses to
7 OIC's discovery that asked about this.) Mr. Scarborough also reviews for approval contracts
8 and projects prior to issuing his bonds. He issues bonds in coordination with corporations,
9 some of which appear also connected to him,⁷ to help perform project estimates, underwriting
functions, claims analysis, and risk assessment.

10 Although Mr. Scarborough characterizes himself as an "individual surety," he operates
11 a corporation called "Scarborough Bond and Guarantee Program," a company which appears
12 to consist of or be related with or connected to several other companies which assist him with
13 services related to his bond business. Mr. Scarborough's "Scarborough Bond and Guarantee
14 Program" is a facility through which his surety bonds are issued. Mr. Scarborough's "IBCS
15 Group" is another related corporation which is the authorized risk and claims manager of the
16 "Scarborough Bond Guarantee Program," and Mr. Scarborough is or has been a "paid officer"
17 at his IBCS corporation. IBCS Group has an exclusive relationship with the Scarborough
18 Bond and Guarantee Program. Another connected corporation, "IBCS Fidelity," does
19 underwriting for his bonds. Another connected corporation, "IBCS Mining," is the owner of
20 Mr. Scarborough's indentured trust agreement with the nationally recognized bank, Wells
21 Fargo. Before "using" Wells Fargo, Mr. Scarborough claims he secured reinsurance and
22 contracted with reinsurers for his bonds. He claims he has had and has used a "reinsurance
23 treaty" to help sell his bonds. Before starting what he calls his "coal operation," Mr.
Scarborough issued bonds "backed by Underwriters Reinsurance," Mr. Wright's company.

⁷ Again, Mr. Scarborough has refused to disclose details about these companies in discovery.

1 Mr. Scarborough didn't know what the asset was – his position was that Underwriters
2 Reinsurance reinsured his bond program, they supplied the asset, and Mr. Scarborough paid
3 them for the use of their asset; he utilized their financial wherewithal to support his position.

4 When some number of Mr. Scarborough's bonds were rejected, Mr. Scarborough still
5 kept the premium he collected. He believes there are standards for trade and claims
6 administration and practices for "insurance," "but not related to suretyship."

7 Mr. Scarborough maintains no insurance license, and he has no Certificate of
8 Authority or other license as an insurer or as a surety. He has testified that he believes he has
9 the legal authority to act as an individual surety because his "bonds are basically the direction
10 of acceptance from the department or any governmental agency, their insurance is a diverse
11 risk management, risk associated loss ratio business that is regulated, the assets of which can
12 be placed into a loss ratio type occurrence." He moved for summary judgment on this issue in
13 Idaho before that state's insurance regulator, and his motion was denied. *See Decl. Singer*
14 Exh. B. Each state insurance regulator that considered Mr. Scarborough's activities has taken
15 action against him as an unauthorized or unlicensed insurer.

14 IV. RELIEF REQUESTED

15 OIC respectfully requests an order denying Mr. Scarborough's motion for summary
16 judgment, and granting OIC's cross-motion for summary judgment on all issues presented.

17 V. STATEMENT OF THE ISSUES

18 1. Were Respondents required to obtain authorization as an insurance company from the
19 Washington State Insurance Commissioner prior to conducting the activities at issue herein? What
20 is the answer to this question when the bond is issued relative to a federal project/contract? What
21 is the answer to this question when the bond is issued relative to a non-federal project/contract?

22 2. Were Respondents required to obtain licenses as insurance producers in Washington prior
23 to conducting the activities at issue herein? What is the answer to this question when the bond is

1 issued relative to a federal project/contract? What is the answer to this question when the bond is
2 issued relative to a non-federal project/contract?

3 3. Is the OIC authorized to impose a fine on Respondents based upon the activities at issue
4 herein? If so, can the fine be calculated as a per violation amount, e.g., if there are 22 bonds then
5 is the fine a monetary amount times 22? Or, must the fine be calculated as a total amount
6 considering all of the bonds essentially as one violation? What is the answer to this question when
7 the bond is issued relative to a federal project/contract? What is the answer to this question when
8 the bond is issued relative to a non-federal project/contract? If those bonds which were issued
9 relative to a federal project/contract are outside the OIC's jurisdiction, can the fine be
10 calculated only as to those non-federal related projects/contracts if those non-federal
11 projects/contracts are determined to be within the OIC's jurisdiction?

11 VI. LEGAL AUTHORITY AND ARGUMENT

12 A. Summary Judgment standard.

13 CR 56 provides that a motion for summary judgment may be granted "if the pleadings,
14 depositions, answers to interrogatories, and admissions on file, together with the affidavits, if
15 any, show that there is no genuine issue of material fact and that the moving party is entitled
16 to judgment as a matter of law." CR 56(c).

17 B. The Insurance Code governs Respondents' activities.

18 Respondent Scarborough moves for summary judgment on the grounds that he feels
19 the Washington State Insurance Commissioner ("Commissioner" or "OIC") may not enforce
20 provisions of the Code against him. He provides three reasons in support of this argument.
21 First, he claims that because he calls himself an "individual surety," he believes the
22 Commissioner has no authority over him. Second, he argues that his bonds really are not
23 "insurance," so the Commissioner has no authority over him. Third, he argues that, as for
federal projects/contracts otherwise within the scope of the Code under RCW 48.01.020,
federal law preempts the Insurance Code. For the reasons that follow, Respondent

1 Scarborough's analysis and arguments are incorrect, and his activities are governed by the
2 Insurance Code. Since summary judgment should lie in OIC's and not Respondent's favor,
3 OIC herein cross-moves for summary judgment on all issues at hand.

4 **1. Respondents were required to obtain authorization as an insurance company
prior to selling Mr. Scarborough's construction bonds.**

5 **a. Respondent Scarborough's bonds are "insurance."**

6 Respondent Scarborough wrongly contends that "bonds issued by individual sureties
7 are not 'surety insurance.'" See Respondent Scarborough's Motion for Summary Judgment
8 ("Scarborough MSJ") at p. 4, l. 17-18. Although there are differences between surety
9 insurance and classic indemnity coverage,⁸ different provisions in the Insurance Code and
10 Washington Supreme Court precedent provide that surety insurance and bonds like Mr.
11 Scarborough's are "insurance" and fall within the Insurance Code. His contentions should be
rejected, and OIC herein cross-moves for an order that his bonds are "insurance."

12 First, Mr. Scarborough's bonds meet the definition of "insurance" set forth in
13 Washington's Insurance Code:

14 Insurance is a contract whereby one undertakes to indemnify another or pay a
specified amount upon determinable contingencies.

15 RCW 48.01.040. Each of Mr. Scarborough's Washington bonds makes the same basic
16 promise. They promise that a contractor's failure to perform under a construction contract is
17 a determinable contingency triggering the duty resting in the principal and the surety – Mr.
18 Scarborough – jointly and severally to make payment to others in the amount specified in the

19 _____
20 ⁸ According to Couch on Insurance 3d, §1:18-

21 The essential distinction between an indemnity contract and a contract of guaranty or suretyship is that
22 the promisor in an indemnity contract undertakes to protect his or her promisee against loss or damage
23 through a liability on the part of the latter to a third person, while the undertaking of a guarantor or
surety is to protect the promisee against loss or damage through the failure of a third person to carry out
his or her obligations to the promisee.

1 bond. Since Mr. Scarborough, as the surety on his bonds, undertakes to pay a specified
2 amount upon determinable contingencies, such bonds constitute "insurance" under Insurance
3 Code section RCW 48.01.040.

4 But even beside RCW 48.01.040, Respondent Scarborough's bonds are also
5 "insurance" under other parts of the Code. For example, the Code recognizes several lines or
6 types of insurance, and makes clear that one such line, surety insurance, specifically includes
7 "bonds." That provision states that "surety insurance" specifically includes "guaranteeing the
8 performance of contracts, [...] and guaranteeing and executing bonds, undertakings, and
9 contracts of suretyship." RCW 48.11.080(4). Moreover, the Legislature seems to have been
10 repeatedly clear about its intent that surety bonds are surety insurance.⁹ Here, Mr.
11 Scarborough's contracts meet RCW 48.11.080(4)'s definition.¹⁰ His bonds not only
12 guarantee the performance of construction contracts, they are actually solicited as "bonds,"
13 and they expressly present Mr. Scarborough as a surety who becomes bound to pay the penal
14 sum in the event of a failure by the principal to carry out the subject construction contract.
15 But while both RCW 48.11.080(4) and RCW 48.01.040 each independently establish that Mr.
16 Scarborough's bonds are "insurance," still other binding legal authority also supports this
17 conclusion.

18 ⁹ In fact, RCW 19.27.107(1) also indicates that a "surety bond" means and includes "any form of surety
19 insurance as defined in RCW 48.11.080." This statute, too, emphasizes that the Legislature intended that "surety
20 bonds" are without question a kind of "surety insurance" under RCW 48.11.080.

21 ¹⁰ In addition, these definitions do not appear inconsistent with the undefined term, "surety." According to
22 Black's Law Dictionary, a "surety" is defined as:

23 One who undertakes to pay money or to do any other act in event that his principal fails therein.
One bound with his principal for the payment of a sum of money or for the performance of some
duty or promise and who is entitled to be indemnified by some one who ought to have paid or
performed if payment or performance be enforced against him. Everyone who incurs a liability in
person or estate, for the benefit of another, without sharing in the consideration, stands in the
position of a "surety," whatever may be the form of his obligation.

Black's Law Dictionary 1293 (5th ed. 1979).

1 The Washington Supreme Court has also repeatedly recognized that construction
2 bonds such as Mr. Scarborough's performance and other bonds are properly considered
3 "surety insurance." For example, in *Ritter v. Shotwell*, 63 Wn.2d 601, 603, 388 P.2d 527
4 (1964) the Court noted that "[a] performance bond is presently defined as 'surety insurance.'" *Ritter*,
5 63 Wn.2d at 603 (citing RCW 48.11.080.) Similarly, in *Seattle-First Nat'l Bank v.*
6 *Wash. Ins. Guar. Ass'n*, 116 Wn.2d 398, 804 P.2d 1263 (1991), the Court indicated that
7 "[s]uretyship is a contractual relation whereby one person, called the surety, agrees to be
8 answerable for the debt or default of another, called the principal. Hence, surety insurance is
9 commonly defined as insurance against defaults on the part of persons who have undertaken
10 contract obligations." (Cites omitted.) *Seattle-First Nat'l Bank v. Wash. Ins. Guar. Ass'n*, 116
11 Wn.2d 398, 406, 804 P.2d 1263 (1991). Surety insurance tends to insure against contractual
12 default and establishes a surety/principal relationship. *Id.*

13 Again more recently, in *Colorado Structures, Inc., v. Ins. Co. of the West et al*, 161
14 Wn.2d 577, 167 P.3d 1125 (2007), the Court provided a more detailed explanation of its
15 conclusion that surety bonds of compensated sureties are contracts of insurance. "The
16 undertakings of compensated sureties are regarded as 'in the nature' of insurance contracts."
17 (Cites omitted.) *Colorado Structures*, 161 Wn.2d at 586. "A bond is a contract that governs
18 the surety's liability to the obligee." *Id.* at 588. In its analysis of precisely the same surety
19 performance bonds issued by Mr. Scarborough, the Court found them to be no different than
20 any other insurance contracts:

21 The process for purchasing surety performance bonds is much like the process for
22 purchasing insurance contracts. A contractor seeking a bond contacts an agent whose
23 "job is to help convince a surety company to issue the bond." *In re Tech. for Energy Corp.*,
140 B.R. 214, 215-16 (E.D. Tenn. 1992) (reporting on the "basic rules and practices in the surety business").
The bond application is then reviewed by underwriters for the surety company who decide if the surety will or will not issue the bond. *Id.* The bonds are purchased with the payment of a premium, after which a surety requires no further performance by the obligee or the principal: the surety upon receipt of the premium has all it will ever get from the contract. [...] The surety's position is like an insurance company--it calculates premiums based on the risk that it

1 ... may have to make a payment. [...] It is, like an insurance company, in a surety's
2 financial interest to withhold payment. Ideally, a surety collects premiums and never
pays claims. [...].

3 When an event occurs that arguably triggers the surety or insurance company's duty to
4 make payments, the parties may dispute whether payment is in fact owed. The
5 disparity of power, at this point in the relationship, is compelling. Sureties may be
6 tempted to withhold payment in every case, gambling that the transaction costs of
7 litigation will dissuade even a percentage of their obligees from asserting their right to
payment. If the maximum risk to the surety is the penal amount of its bond, a surety
has nothing to lose. The obligee has no leverage over the surety to compel payment,
except litigation. If the transaction costs of litigation are too high relative to the bond,
obligees will simply cut their losses.

8 This unfortunate reality hits the smallest construction companies hardest, as their
9 projects are less expensive and thus so are their bonds. A construction company
10 facing a surety refusing to pay several thousand dollars on a bond, after consulting an
11 attorney, will likely decide that the transaction costs are too great to move forward
with litigation. The surety, risking only the value of the bond, may be motivated to
withhold payment. [...] The disparity of power between surety and obligee is, with
respect to compulsion of performance, identical to the disparity between insurers and
the insured.

12 (Cites omitted.) *Id.* at 601-03. In conclusion, the Court observed that “[t]here is little to
13 distinguish construction performance bonds from other forms of insurance.” *Id.* at 605.¹¹

14 At pages 6 through 9 of his summary judgment motion, Mr. Scarborough argues that
15 his bonds are not “insurance.” But none of the authorities he cites undermines the foregoing
16 analysis and conclusions, and the reasons he provides to support his arguments should be
17 rejected as irrelevant or faulty. For example, at page 7 of his motion he points to the Code's
18 definition of “insurance” and emphasizes that his bonds are not contracts of indemnity as they
19 do not undertake to indemnify others, as liability insurance does. But the idea of insurance as
20 just “a two-party and two-interest contract” is a restricted and outdated view. “The notion of

21 ¹¹ The Court's conclusion that surety bonds are insurance is in no way inconsistent with what others have long
22 observed. “As a practical matter, the corporate surety conducts its business along the same lines as does the
23 insurance company. [...] The surety, like the insurance company, spreads the risk among the many principals
covered, for it is ultimately by the premiums collected that a fund is established to provide for administrative
costs and probable matured risks.” *The Contract of the Corporate Surety*, 5 *Fordham L. Rev.* 473, 480 (1936),
available at <http://ir.lawnet.fordham.edu/flr/vol5/iss3/8>.

1 insurance as a device merely to “indemnify” has also been considerably attenuated.”
2 Denenberg, *The Legal Definition of Insurance*, 30 J. Ins. 319, 323 (1963). Moreover, it is a
3 view that ignores what RCW 48.01.040 says. It broadly defines insurance as a contractual
4 promise to indemnify, “or” to “pay.” RCW 48.01.040’s language is “broad enough to sweep
5 in both indemnity and non-indemnity contracts. That is, it includes not only those contracts
6 which promise indemnity in the strict sense, but also those which pay a “specified amount
7 upon determinable contingencies.” *Id.* at 328. Mr. Scarborough’s bonds, like all bonds, meet
8 this definition because they promise “to pay” in the event of contractor default.

9 Mr. Scarborough also contends his bonds are not “insurance” because his bonds
10 include the statement, “[t]his Bond is a guarantee, it is not an insurance policy.” See
11 Scarborough MSJ at p. 8, l. 12-18. Even if his bonds include this statement, an insurance
12 contract cannot disclaim being “insurance” merely by including those words in an insurance
13 contract:

14 It is suggested in brief for appellee that the contract shows, on its face, and so states,
15 that it is not an insurance policy. But that is wholly beside the question. No one can
16 change the nature of insurance business by declaring in the contract that it is not
17 insurance. As was said in the case of *State v. Beardsley*, 88 Minn. 20, 92 N. W. 472,
18 474: 'The real character of this promise, or of the act to be performed, cannot be
19 concealed or changed by the use or absence of words in the contract itself; and it is
20 wholly immaterial that on its face this contract does not expressly purport to be one of
21 insurance, and that this word nowhere appears in it. Its nature is to be determined by
22 an examination of its contents, and not by the terms used.'

23 *McCarty v. King County Medical Serv. Corp.*, 26 Wn.2d 660, 684, 175 P.2d 653 (1946),
citing *Allin v. Motorists' Alliance*, 234 Ky. 714, 29 S. W. (2d) 19, 71 A. L. R. 688 and *State v.*
Beardsley, 88 Minn. 20, 92 N. W. 472, 474.

For all the foregoing reasons, Mr. Scarborough’s bonds are “insurance.” OIC cross-
moves for summary judgment on this point.

1 **b. Respondent Scarborough's Washington bonds are governed by the Code.**

2 Respondent Scarborough does not argue that his Washington bonds somehow fall
3 outside the scope of the Insurance Code, perhaps because he agrees they do not. RCW
4 48.01.020 defines the "scope of [the] code" as follows: "All insurance and insurance
5 transactions in this state, or affecting subjects located wholly or in part or to be performed
6 within this state, and all persons having to do therewith are governed by this code." Here,
7 each of his bonds involves Washington contractors, Washington projects, Washington project
8 owners, or persons having to do therewith. Mr. Scarborough's Washington bonds do fall
9 within RCW 48.01.020's scope and thus are "governed by" the Insurance Code. OIC cross-
moves for summary judgment on this point.

10 **c. Respondent Scarborough is and has acted as an "insurer."**

11 Respondent Scarborough's Washington insurance activities render him an "insurer"
12 requiring a Certificate of Authority. Under RCW 48.01.050, an "insurer" includes "every
13 person engaged in the business of making contracts of insurance..."¹² (Emphasis added.)
14 "Persons and entities that are so engaged are subject to regulation by the Washington State
15 insurance commissioner." *Bordeaux, Inc. v. Am. Safety Ins. Co.*, 145 Wn. App. 687, 695, 186
P.3d 1188 (2009).

16 While the Code does not define the word "business," dictionaries relied on by
17 Washington courts do.¹³ Black's Law Dictionary defines "business" as "[a] commercial

18 _____
19 ¹² "Person" is defined under the Code as "any individual, company, insurer, association, organization, reciprocal
or interinsurance exchange, partnership, business trust, or corporation." RCW 48.01.070.

20 ¹³ When a word is not defined in a contract or a statute, Washington courts have looked to a limited number of
21 dictionaries for definitions. Such dictionaries have included Black's Law Dictionary and Webster's Third New
22 International Dictionary. See *Ryan v. Harrison*, 40 Wn. App. 395, 397, 699 P.2d 230 (1985) (standing for the
23 principle that an undefined word "must be given its usual and ordinary meaning." In *Ryan*, like other
Washington cases, the court looked to both Black's and Webster's.) See also *Burgeson v. Columbia Producers*,
60 Wn. App. 363, 367, 803 P.2d 838 (1991) and *Ueland v. Reynolds Metals Co.*, 103 Wn.2d 131, fn 1, 691 P.2d
190 (1984) (each citing Black's.) This applies whether a word is undefined in a contract or in a statute. See *Am.*
Legion Post No. 149 v. Dep't of Health, 164 Wn.2d 570, 592 fn. 17, 192 P.3d 306 (2008) (also looking to Webster's
where word is undefined in the statute at issue.)

1 enterprise carried on for profit; a particular occupation or employment habitually engaged in
2 for livelihood or gain.” Black’s Law Dictionary 226 (9th ed. 2009). “Business” is defined in
3 Webster’s Third New International Dictionary (unabridged) (1964, G & C Merriam Co.
4 Publishers) at page 302 as, among other things, “a usu[al] commercial or mercantile activity
5 customarily engaged in as a means of livelihood and typically involving some independence
6 of judgment and power of decision,” “an activity engaged in toward an immediate specific
7 end and usu[ally] extending limited period of time,” and “a commercial or industrial
8 enterprise.” Similarly, the same dictionary defines “enterprise” as: “a unit of economic
9 organization or activity.” *Id.* at 757.

10 Under any of the foregoing definitions, Respondent Scarborough has issued his
11 Washington bonds in the course of a “business” of making such insurance contracts.¹⁴ His
12 bonds are designed to last for a set duration, they involve reinsurance, they utilize complex
13 agreements with Wells Fargo, and he exercises independent judgment and power of decision
14 in crafting and issuing his bonds.¹⁵ His operation is commercially provided, sophisticated,
15 and he does so in his capacity as the principal of the “Scarborough Bond & Guarantee
16 Program.” Respondent Scarborough holds himself and his business out and open to the
17 public, competing with all of the authorized insurance companies for the same surety
18 construction bond business. *See, e.g.,* Decl. Singer Exh. F (screenshot of Scarborough
19 program webpage, comparing his bonds with “corporate” bonds.) He markets himself as an
20 alternative to his authorized surety insurance company competitors, presenting himself to
21 contractors seeking bonds but who have been turned away by these corporate surety insurance

21 ¹⁴ While Mr. Scarborough has refused to provide OIC answers and responses to its discovery seeking the details
22 of the business he engages in, he has at least testified before courts in the past that, indeed, he is “in the business
of acting as an individual surety and is the owner of IBCS. He provides payment and performance bonds to
general contractors and subcontractors.” *Persaud Cos. v. IBCS Group, Inc.*, 2010 U.S. Dist. LEXIS 34183.

23 ¹⁵ Although he uses underwriting for his bond business, Mr. Scarborough has refused to disclose details when
asked in discovery.

1 company-goliaths.¹⁶ No evidence shows his bond sales have ever occurred *gratis*; instead, he
2 issues bonds for money, expressly characterizing it as “bond premium” on at least some
3 number of his bonds. One such Washington bond he disclosed to OIC revealed a “bond
4 premium” “rate” of \$35.00 for every thousand dollars of the bond’s penal sum – a substantial
5 amount of money,¹⁷ and a rate apparently exceeding what his competitors charge.¹⁸ *See*
6 Decl. Singer. Moreover, he has issued thousands of these bonds, generating a multi-million
7 dollar business. Since Mr. Scarborough undisputedly engaged in this “business,” under RCW
8 48.01.050 he is an “insurer.” OIC cross-moves for summary judgment on this point.

9 **d. Respondent Scarborough’s activities required a Certificate of Authority.**

10 Since Respondent Scarborough acted as an “insurer” by being in the business of
11 making and otherwise “transacting”¹⁹ Washington insurance contracts, he violated RCW
12 48.05.030(1):

13 No person shall act as an insurer and no insurer shall transact insurance in this state
14 other than as authorized by a certificate of authority issued to it by the commissioner
15 and then in force, except, as to such transactions as are expressly otherwise provided
16 for in this code.

17 Similarly, he also violated RCW 48.15.020(1):

18 ¹⁶ As indicated in the article available online concerning Mr. Scarborough’s bond activity,
19 http://enr.construction.com/business_management/ethics_corruption/2013/0225-A-Bold-Individual-Surety-Claims-His-Coal-Backed-Bonds-are-Rock-Solid.asp?page=1, Mr. Scarborough’s website proclaims “If you or
20 your clients have been told NO by traditional sureties, try one of our many services.” The article suggests Mr.
21 Scarborough stands as an alternative to “corporate sureties” who would apparently like to see laws passed “at the
22 expense of the overwhelming majority of small, up-and-coming or independent contractors, who would no
23 longer exist.” Of Mr. Scarborough, the author wrote “[he] has a gift for hitting the corporate surety world,
deploying a narrative in which he plays a noble, unbending David struggling valiantly against corporate surety’s
imposing Goliath—all for the benefit of small and minority contractors.”

¹⁷ For example, in just one case, Mr. Scarborough issued a bond or bonds after receiving a “bond premium of
\$121,557.” *Persaud Cos. v. IBCS Group, Inc.*, 2010 U.S. Dist. LEXIS 34183.

¹⁸ In fact, in the hearing officer’s order denying Mr. Scarborough’s motion for summary judgment before the
Idaho insurance regulator, the hearing officer wrote that Mr. Scarborough’s bond business “typically charges a
higher servicing fee than premiums charged by corporate sureties.” *See* Decl. Singer.

¹⁹ The “transaction” of insurance is defined at RCW 48.01.060.

1 An insurer that is not authorized by the commissioner may not solicit insurance
2 business in this state or transact insurance business in this state, except as provided in
3 this chapter.

4 Mr. Scarborough's business *is* the transaction of insurance business in this state. That activity
5 requires, at minimum, a properly issued Certificate of Authority if it is to happen at all.

6 Mr. Scarborough's insurance business is to be contrasted with other individuals who
7 choose to act as individual sureties without requiring authority from OIC as an insurer. For
8 example, when a friend, relative, or other individual gratuitously posts a bond, even as an
9 "individual surety," they are not engaged in the course of work, occupation or trade of
10 insurance. They do not engage "in the business of making contracts of insurance" and thus do
11 not meet the "insurer" definition in RCW 48.01.050. Unlike Respondent Scarborough, such a
12 person may so act without a Certificate of Authority or other OIC approval, and without
13 violating RCW 48.15.020(1)'s prohibition against the unauthorized transaction of "insurance
14 business." While an individual may act as an individual surety, they may not act as an insurer
15 because a Certificate of Authority is required to act as a surety insurer or any other kind of
16 insurer in Washington.

17 Moreover, individuals cannot act as an insurer in Washington because only
18 corporations may be insurers. Pursuant to RCW 48.05.040(1), with an exception not relevant
19 here, only stock, mutual or reciprocal insurers of the same general type as may be formed as a
20 domestic insurer under RCW 48.06 may apply for a Certificate of Authority. The Insurance
21 Code does not grant the "individual surety" any exception. This remains true whether they
22 hold an insurance producer license or not. But individual sureties who do not engage in "the
23 business of insurance" or "insurance business" certainly do not require a Certificate of
24 Authority.

25 Mr. Scarborough is no exception to any of the foregoing laws and reasoning. His
26 transaction of Washington insurance without a Certificate of Authority violated RCW
27

1 48.15.020(1) and RCW 48.05.030(1), and on summary judgment, OIC herein cross-moves for
2 an order to enter to this effect.

3 **e. Mr. Scarborough's "individual surety" arguments should be rejected.**

4 Mr. Scarborough makes several arguments as to why he feels his declaring himself to
5 be an "individual surety" essentially abrogates the Insurance Code with respect to its
6 application to him and his bond-issuing activities. Each of his arguments lacks merit and
7 should be rejected.

8 Mr. Scarborough argues that "bonds issued by individual sureties are not 'surety
9 insurance'" and that "only corporate sureties and not individual sureties are subject to the
10 commissioner's authority." See Scarborough MSJ at p. 4, l. 14-18. But it doesn't matter who
11 issues the bonds – it's the contracts themselves which determine whether they are "insurance"
12 or not, and it's the conduct of the person that determines whether the person is an "insurer."
13 Whether Mr. Scarborough has decided to call himself an "individual surety" makes no
14 difference. Just as one cannot magically turn a contract of insurance into something else
15 simply by including the words, "this is not insurance," Mr. Scarborough cannot change into
16 something other than an insurer simply by declaring "I am not an insurer." "It is elementary
17 that the law looks at substance instead of form, and is not deceived by the gloss of words."
18 *Wheeler v. Ben Hur Life Ass'n*, 264 S.W.2d 289, 291 (Ky. 1953). Moreover, as already
19 explained above, both the Insurance Code and the decisions of the Washington Supreme
20 Court establish that the bonds Mr. Scarborough issued and issues *are* contracts of "insurance,"
21 and that all "insurers" *are* subject to the commissioner's authority. The undisputed evidence
22 shows that Mr. Scarborough has issued contracts of insurance and is an "insurer" under RCW
23 48.01.050.

Respondent Scarborough also raises several arguments based on RCW 19.72 *et seq*
("the Chapter"). He argues that the existence of these statutes, which acknowledges the
existence of individual sureties, should essentially abrogate the Insurance Code with respect

1 to its application to him and his bond-issuing activities. Each of Mr. Scarborough's
2 contentions should be rejected.

3 As a preliminary matter, however, Mr. Scarborough isn't a resident of this state and
4 RCW 19.72.020 plainly requires any individual surety to be a resident of this state. Since Mr.
5 Scarborough fails to qualify as an "individual surety" under the very Chapter of Washington
6 law he seeks to invoke, this prevents him from claiming the Chapter has any application to
7 him. For this reason alone, all of Mr. Scarborough's arguments about RCW 19.72 *et seq*
8 should be rejected. But there are also other reasons why RCW 19.72 *et seq* does not abrogate
the Insurance Code in whole or in part.

9 Nowhere does Chapter 72 of Title 19 RCW discuss authorizing individuals to engage
10 in the business of insurance or act as an insurer, nor does it discuss usurping or abrogating the
11 Insurance Commissioner's authority under the Insurance Code. No provision in that chapter
12 makes even a suggestion that the Insurance Code is superseded or annulled by dint of its mere
13 existence. No Washington court has ever ruled that the Chapter's purpose is to abrogate the
Insurance Code.

14 In fact, the Chapter's only purpose is to protect individual sureties. While very few
15 Washington courts have ever even mentioned the Chapter, one that did only indicated that
16 RCW 19.72 *et seq* sets forth laws "which provide[] protections for sureties who post bonds."
17 *In re Marriage of Bralley*, 70 Wn. App. 646, 654 fn. 4, 855 P.2d 1174 (1993). The apparent
18 intent of the Legislature was to provide protections to people who serve as sureties, not to
19 declare that such people could engage in the business of insurance without being subject to
the Insurance Code.

20 Moreover, the Chapter isn't concerned with Mr. Scarborough's bonds. The title of
21 RCW Title 19 is "BUSINESS REGULATIONS — MISCELLANEOUS," which reflects that
22 the chapters set forth "miscellaneous" business regulations, ones which might only
23 occasionally arise. Consistent with this, the Chapter only provides limited guidance as to how

1 sureties will be treated in certain situations, and those situations in particular only involve
2 bonds that are of a type different from the ones being sold by Mr. Scarborough. The Chapter
3 is only concerned with bonds used during miscellaneous business transactions like court
4 proceedings (RCW 19.72.040), delivery and replevin (RCW 19.72.070), public officials'
5 bonds, taxing districts' bonds, guardians' bonds, executors' bonds, and so forth. RCW
6 19.72.109(1)). In sum, the Chapter simply does not govern Mr. Scarborough's conduct.

7 Respondent Scarborough further contends that "the suretyship statute [RCW 19.72 *et*
8 *seq*] distinguishes between individual surety bonds and 'surety insurance.'" See Scarborough
9 MSJ at p. 4, l. 20-21. But the Chapter actually states the opposite – that the bonds and surety
10 bonds it references are *the same* as "insurance" under the Insurance Code: "surety bond
11 means any form of surety insurance as defined in RCW 48.11.080." RCW 19.72.107(1).

12 Mr. Scarborough also contends that RCW 19.72 *et seq* "reserves to the insurance code
13 only matters relating to 'surety insurance,' providing in RCW 19.72.060: 'Corporate surety:
14 See surety insurance: Chapter 48.28 RCW.'" (Emphasis added.) See Scarborough MSJ at p.
15 4, l. 21-23. But a careful review of RCW 19.72 *et seq* reveals that it simply doesn't make any
16 such 'reservation,' nor does it indicate that the Insurance Code "only" governs what Mr.
17 Scarborough incorrectly claims it governs. As to RCW 19.72.060, Mr. Scarborough reads
18 into that section a meaning that isn't there. RCW 19.72.060 simply provides a cross-reference
19 to Chapter 28 of the Insurance Code, which merely provides some regulations concerning
20 corporate sureties' bonds in transactions such as the ones discussed in RCW 19.72 *et seq*. For
21 example, Code Chapter 28 clarifies that when corporate sureties issue bonds like the ones
22 discussed in RCW 19.72 *et seq*, such bonds are to be deemed sufficient. RCW 48.28.010. It
23 also sets forth clarifications about some details in transactions involving fiduciary bonds,
judicial bonds, and official bonds. RCW 48.28.020-040. But nowhere does Chapter 28 of the
Code declare that it is limited in the way Mr. Scarborough contends. And in fact, as

1 indicated, RCW 19.72.107(1) even makes explicit that the chapter's references to bonds or
2 surety bonds means the same thing as "surety insurance."

3 Pointing to RCW 48.28.050, Mr. Scarborough next contends that "individuals may be
4 sureties and [RCW 48.28.050 "plainly recognizes"] that they are governed by a different law
5 than surety insurers." See Scarborough MSJ at p. 5, l. 7-8. But here, too, Mr. Scarborough
6 reads into a law a meaning which simply is not there. RCW 48.28.050 merely states that a
7 "surety insurer may be released from its liability on the same terms and conditions as are
8 provided by law for the release of individuals as sureties." This in no way addresses or even
9 alludes to what laws govern the sureties or their bonds.

10 Mr. Scarborough also contends that "[t]he 'surety insurance' governed by chapter
11 48.28 includes transactions by corporate sureties but not the issuance of bonds by individual
12 sureties." See Scarborough MSJ at p. 4, l. 23-25. But the Insurance Code draws no such
13 distinction. As already indicated, the Code governs the issuance of bonds as "insurance" and
14 those who act as "insurers," regardless of what the person selling bonds or acting as an insurer
15 calls himself.

16 Mr. Scarborough also contends that "[c]onstruing the insurance code and its
17 requirement of a certificate of authority as applying them to individual sureties would
18 effectively prohibit them, nullifying the provisions in chapter 19.72 RCW that expressly
19 authorize them." See Scarborough MSJ at p. 6, l. 5-7. But this is not correct, both as to the
20 Code's requirements for licenses, and its requirement for a Certificate of Authority.

21 As for licenses, the Insurance Code requires a license for those who sell, solicit, or
22 negotiate insurance. RCW 48.17.060. It also requires a license for "surplus lines" brokers
23 who help others procure unauthorized insurance. RCW 48.15.040. But a true individual
surety does not sell, solicit, or negotiate insurance, and does not serve as a surplus lines
broker, so RCW 48.17.060 and RCW 48.15.040 will not require any such license. The
Insurance Code doesn't "nullify" any part of RCW 19.72 *et seq* in this or any other regard,

1 nor does Mr. Scarborough cite a specific section in RCW 19.27 *et seq* which he believes
2 would specifically be 'nullified' by the Code's license requirements.

3 Likewise, as for the Code's Certificate of Authority requirement, RCW 48.05.030(1)
4 requires that anyone acting as an "insurer" or transacting insurance as an "insurer" must
5 obtain such a certificate from the Commissioner. But again, since a true individual surety
6 does not perform such acts, they need no Certificate of Authority. While true individual
7 sureties do not engage in the business of insurance, and thus do not cross the line between
8 being an individual surety and being an insurer, Mr. Scarborough has crossed that line. He
9 wishes to compete, and does compete, with corporate sureties by acting as an insurer and
10 engaging in a business of transacting surety insurance. He is quite distinguishable from the
11 traditional individual sureties contemplated under RCW 19.27 *et seq*.

12 Ultimately, Respondent Scarborough's arguments demonstrate that he fundamentally
13 misapprehends what an "individual surety" really is. While some have called themselves an
14 "individual surety" as a pretext, engaging in the business of surety insurance even with
15 fraudulent construction bonds,²⁰ real individual sureties are quite unlike what Mr.
16 Scarborough is doing. Individual sureties have, historically, usually been a friend or a relative
17 of the principal, had confidence in the principal, and volunteered to assume the obligation of
18 answering for the principal's performance of a duty. Mr. Scarborough, on the other hand, is
19 in the business of bond selling. His business is huge and complex, involving numerous
20 corporation entities with reinsurance, indemnity agreements, underwriting, risk assessment,
21 and other functions. While Mr. Scarborough is functionally indistinguishable from the
22 corporate surety insurance companies he expressly competes with for bond premiums, true
23 individual sureties serve without charging or collecting any premium. Working for free, they
do not engage in any business of making bonds, they do not engage in underwriting, and they
do not compete with corporate surety insurers for the bond-issuing business.

²⁰ See examples included at Decl. Singer Exh. A.

1 The function of the individual surety was that of an accommodation party. In the eyes
2 of the law, if not always in fact, he received nothing for his undertaking which was
3 presumably based on friendship or family tie. He made little effort to protect his
4 interests. He did not prepare the contract; often he did not even read it; rarely did he
5 understand its full scope and legal significance.

6 *The Contract of the Corporate Surety*, 5 Fordham L. Rev. 473, 474-75 (1936), available at
7 <http://ir.lawnet.fordham.edu/flr/vol5/iss3/8>. The individual surety's voluntary and gratuitous
8 undertaking was conducted in a "casual and irregular" fashion, out of "friendly courtesy or
9 family conscience." *Id.* at 477-78. It

10 arose incidentally rather than systematically and as a part of a business enterprise.
11 Parties were not solicited; the element of engaging in an organized business was
12 entirely absent from the transaction.

13 *Id.* at 474, fn 6, and 477. The undertaking of the individual surety was "vast[ly] dissimilar] in
14 purpose and incentive" to the "corporate surety," or insurance companies. *Id.* at 477. While
15 friendly courtesy or family conscience drive individual sureties to act, profit and business
16 drive corporate sureties/insurance companies. Corporate insurers issue bonds in exchange for
17 "a stipulated premium." *Id.* at 478. Corporate insurers issued bonds "enveloped in an
18 atmosphere of detail, system and efficiency" and held themselves out "to the business world
19 as an agency for the accomplishment of a needed service." *Id.* at 477. Corporate sureties
20 "usually require[] an application in which both the principal and oblige join in representations
21 which are made conditions of the bond." *Id.* at 477, fn 20. These differing characteristics
22 between individual sureties and corporate sureties led the "[t]he courts [to] presume that the
23 contract of the individual surety is gratuitous and motivated by friendship," and to understand
the individual surety as someone who "is or may be to a certain extent, powerless to protect
himself." *Id.* at 474-75, fn. 7 and 9.²¹

²¹ By the 1930s, the individual surety was seen as a "rapidly disappearing competitor" to surety insurance companies and it all but disappeared. *Id.* at 476.

One fact cannot be disputed: the self-protective and precise method of corporate surety is rapidly displacing the informal procedure characteristic of the individual or accommodation surety. [...]

1 While today's court decisions rarely mention the almost extinct individual surety, in
2 the late 1800s and early 1900s, when corporate surety insurance companies were busy
3 replacing individual sureties, courts from that era mentioned them. Some of those earlier
4 court cases described the characteristics of individual sureties and noted the differences
5 between them and the surety insurance companies that were rapidly displacing them. Some of
6 those decisions described the nonprofit and noble motives of the individual surety and
7 contrasted them against corporation insurers' business savvy, sophistication, and profit
8 motives:

8 [A]n individual surety [...] is a mere volunteer. Surety companies are not to be
9 so described; they are insurers, paid for their services, bound by contracts
10 which are usually carefully drawn by themselves, and, as a general rule,
11 satisfactorily secured by counter indemnity. They perform a most useful, and
12 indeed, according to modern custom, an indispensable, function in the business
13 and legal world; but they differ so much from an individual surety of the
14 ordinary type as to render inapplicable some of the reasons that have led the
15 courts to guard the rights of the individual surety with jealous care.

16 (Cite omitted.) *U.S. Fid. & Guar. Co. v. United States*, 178 F. 692, 694-95 (3rd Cir C.A.
17 1910).

18 The individual surety as formerly known was usually a relative or friend who
19 had confidence in the principal, and voluntarily assumed the obligation of
20 answering for the latter's faithful performance of duty. I need not speak of the
21 individual who became surety for pay, for the very name of 'professional bail
22 goer' is a reproach to every branch of the administration of justice which he
23 was allowed to contaminate with his presence. But the voluntary surety,
24 however honest and well qualified at the time of his approval by the court, is
25 liable to the contingencies of business, the changes of value in property, and
26 the inexorable chance of death which brings his estate into the administration
27 of the law under wholly changed circumstances. [...] On the other hand, the
28 surety company [...] must have a capital, the amount, nature of investment,
29 and management of which, are known and within constant sight of the court
30 and the parties interested. It is obliged to make reports of its condition to the

31 Because of the nature of the corporate surety's business which holds itself out publicly to those in need
32 of its services the idea quickly took root and the surety company has to a large measure almost wholly
33 displaced the individual surety.

Id. at 474 and fn 6.

1 courts and to the commonwealth, and is at all times subject to the visitorial
2 power of the latter, and finally it has the sharp incentive of prevention of loss
3 by looking closely after the administration of his trust by its principal for
4 whom it has become responsible, not from friendly personal confidence, but as
5 a strict business venture. [...] 'Corporation suretyship is another product of
6 modern thought and ingenuity, and may be said to possess many advantages
7 over individual bail or security. * * * Our daily experience has proved that
8 corporate security and the oversight and management by expert officers of the
9 trust and security companies are highly advantageous not only to the fiduciary,
10 but to all the parties interested, whether creditors, legatees or distributees.'

11 (Cites omitted.) *The Bencliff*, 158 F. 377, 378 (E.D. Pa. 1908). Similarly, this court
12 compared corporate surety insurers with individual sureties, and noted the former's "superior
13 means and facilities" to the latter:

14 The very reason for the existence of this kind of corporations [sic], and the
15 strongest argument put forward by them for patronage, is that the
16 embarrassment and hardship growing out of individual suretyship that give
17 application for this rule is by them taken away; that it is their business to take
18 risks and expect losses.

19 *Atlantic Trust & Deposit Co. v. Laurinburg*, 163 F. 690, 695-96 (C.A. 4th Cir. 1908). Again,
20 while the corporate sureties' takeover of the bond market has rendered true individual sureties
21 quite rare, and modern courts seldom mention them, when they do, they still see individual
22 sureties the same way courts did over a century ago.²²

23 Viewed through this historically accurate lens, Mr. Scarborough is not a true
"individual surety" and Chapter 72 of Title 19 RCW has no impact on the Insurance Code.
Whereas true individual sureties "volunteer" to gratuitously help someone out, Mr.
Scarborough is the opposite. He an insurance entrepreneur, a businessman, operating a
complex and sophisticated operation. He underwrites. He collects premium. He uses
complex reinsurance, "indentured trust agreements," and "irrevocable trust receipts" from
Wells Fargo. He advertises and holds himself out and open to the public to conduct business.

²² "Although the bond system is primarily aimed at serving society's interest in securing the appearance of criminal suspects, the justice system should ensure at least minimal fairness to individual sureties, who are frequently family members or friends and may undertake heavy financial responsibility without sufficient understanding." *U.S. v. Figuerola*, 58 F.3d 502, 504 (C. A. 9th Cir. 1995).

1 He has sold thousands of very lucrative construction bonds in competition against authorized
2 United States surety insurance companies, seeking the same bond market they do, all for a
3 profit. By contrast, an individual surety is and always has been historically someone like a
4 friend, family member, or employer simply trying to help someone out – without charging
5 premiums, without taking insurance applications, without reinsurance treaties, and without
6 any underwriting. Mr. Scarborough is not a true “individual surety.” In his business, Mr.
7 Scarborough undoubtedly acts as an insurer, not truly as an “individual surety,” so RCW
8 19.72 *et seq* has no application to him or to his activities.

9 And contrary to Respondent Scarborough’s argument that OIC’s position is
10 inconsistent with RCW 19.72 *et seq*, true individual sureties *can* function as a traditional,
11 individual surety without falling under RCW 48.01.050’s definition of “insurer.” As
12 indicated, the Insurance Code is concerned with insurers transacting insurance. A true
13 individual surety, by contrast, traditionally just occasionally provides a bond as an
14 accommodation party, gratuitously, motivated solely by friendship. A true traditional
15 individual surety serves the noble goal of fulfilling friendly courtesy or family conscience, but
16 is not engaged in any business of selling insurance. So while Mr. Scarborough contends there
17 is a conflict between RCW 18.27 *et seq* and the Insurance Code, he is wrong. The Insurance
18 Code comes into play when a person “engages in the business of making contracts of
19 insurance.” RCW 48.01.050. If an individual surety acts the way individual sureties have
20 traditionally acted, they will not meet the Code’s definition of “insurer.” Nothing in the
21 Insurance Code obstructs, nullifies, undermines, or conflicts with RCW 19.72 *et seq*, and
22 nothing requires Mr. Scarborough be treated differently.

23 Nor is there any good reason why Mr. Scarborough *should* be treated differently from
every authorized surety insurer against whom he competes for construction surety bond
business. The business of insurance is one affected by the public interest, and it is incumbent
on the Commissioner to preserve inviolate its integrity. RCW 48.01.030. It would undermine

1 this fundamentally crucial ideal to subject only authorized insurance companies regulatory
2 requirements designed to ensure fair claims rules, solvency rules, consumer protection rules
3 for transacting insurance, and other Code requirements, but turn a blind regulatory eye to
4 unauthorized insurers who could pose great risk to the public with promises that could be
5 fraudulent, simply because they have decided to anoint themselves the nomenclature of
6 “individual surety.”

7 Here, the bonds Mr. Scarborough sells are the same products consumers and
8 governmental units require during large construction projects, and the Washington Supreme
9 Court has explained why such bonds’ promises are of such great importance from a public
10 policy and “social good” perspective:

11 In such a contract, whether or not titled “insurance policy,” certainty is
12 of the essence from the obligee-insured’s point of view. The developer
13 seeks a bond in order to be certain of timely, dependable performance of
14 the construction contract. [...] The financial viability of the entire project
15 may depend upon the surety’s good faith performance of these duties.

16 As with any other form of insurance, the surety bond system allows one
17 party to shift to another a contingent risk that the first party, the developer-
18 obligee, cannot itself bear. The social good served by such contracts is the
19 same served by other classes of insurance: greater freedom of activity by
20 more participants than would be possible if each had to bear all the risks of
21 its own enterprise.

22 Certainty of performance being the essential value of performance
23 bonds, their worth is deeply undermined if sureties can regularly choose to
ignore their obligations, having nothing to fear but contract damages that
will approximate what they would pay in performance.

Colorado Structures, 161 Wn.2d at 601, citing *Cates Constr. Inc. v. Talbot Partners*, 21 Cal.
4th 28, 65-66, 980 P.2d 407, 86 Cal. Rptr. 2d 855 (1999) (Mosk, J., dissenting).

Finally, while Mr. Scarborough’s motion fails to disclose this, Washington is not the
first state and not the first insurance regulator to take the foregoing positions. The States of
Virginia, Iowa, and Idaho have not only each taken regulatory action against Mr.
Scarborough, Idaho even heard his similar motion for summary judgment there and denied it.
(The Idaho regulator later settled with Mr. Scarborough for payment of a fine, although it is

1 unknown whether that fine has yet been paid.) See Decl. Singer Exhs. A and B. In fact, OIC
2 staff is unaware of any state that has reached different conclusions.

3 Mr. Scarborough has acted as an insurer, not the "individual surety" he calls himself.
4 His contentions to the contrary are meritless. His transaction of Washington surety insurance
5 without a Certificate of Authority violated RCW 48.15.020(1) and RCW 48.05.030(1), and on
6 summary judgment, OIC herein cross-moves for an order to enter to this effect.

7 **2. Respondents were also required to obtain insurance producer licenses prior
8 to selling construction bonds.**

9 As indicated above, Mr. Scarborough and his agents also required licenses. RCW
10 48.17.060(1) provides:

11 A person shall not sell, solicit, or negotiate insurance in this state for any line or lines
12 of insurance unless the person is licensed for that line of authority in accordance with
13 this chapter.

14 Here, Mr. Scarborough or his agents sold Washington bonds, and those bonds are insurance.
15 This selling, soliciting and negotiation activity required a license under RCW 48.17.060(1).
16 Similarly, since none of the Respondents holds a Certificate of Authority and they are
17 unauthorized insurers, the sale of their unauthorized insurance may only happen pursuant to
18 RCW 48.15.040, if at all. RCW 48.15.020(2)(a) prohibits a person from representing an
19 unauthorized insurer without a license to conduct the business of surplus lines insurance. On
20 summary judgment, OIC herein also cross-moves for an order to enter to this effect.

21 **3. It makes no difference whether Mr. Scarborough's bonds are for state or
22 federal projects/contracts – there is no federal preemption of the Code.**

23 Mr. Scarborough's bonds fit into one of two categories: (1) bonds that have been
issued relative to non-federal projects/contracts, and (2) bonds that have been issued relative
to federal projects/contracts. OIC takes the position that all such bonds are subject to the
Insurance Code's requirements, as set forth above, and herein cross-moves for summary
judgment accordingly. However, as to the second category of bonds, Mr. Scarborough also
argues that the Insurance Code is federally preempted by two sources of federal laws – the

1 Miller Act and the Federal Acquisition Regulation or Regulations (“FAR”). For the reasons
2 that follow, Mr. Scarborough’s preemption argument should be rejected, and OIC cross moves
3 for summary judgment on this issue as well.

4 “The [United States] Supreme Court has outlined three ways in which a federal law
5 may preempt state law: the federal law may do so expressly; it may reflect a Congressional
6 intent to occupy the entire legal field in the area; or the state law may conflict with the federal
7 law, either directly in that it is not possible to comply with both, or indirectly in that the state
8 law is an obstacle to the accomplishment of the federal objective.” (Citations omitted.) *K-W
Industries v. National Surety Corp.*, 855 F.2d 640, 642, fn. 3 (C.A. 9th Cir. 1988).

9 Our United States Supreme Court justices start with the assumption that there is no
10 federal preemption of an area traditionally occupied by the states absent clear and manifest
11 support. “[B]ecause the States are independent sovereigns in our federal system, we have
12 long presumed that Congress does not cavalierly pre-empt state-law [...]. In all pre-emption
13 cases, and particularly in those in which Congress has “legislated . . . in a field which the
14 States have traditionally occupied,” [...], we “start with the assumption that the historic police
15 powers of the States were not to be superseded by the Federal Act unless that was the clear
16 and manifest purpose of Congress.” (Cites omitted.) *Medtronic v. Lohr*, 518 U.S. 470, 485,
17 116 S. Ct. 2240, 135 L. Ed. 2d 700 (1996). This presumption against preemption can only be
18 overcome by evidence of a “clear and manifest” intent of Congress to preempt state law.
19 *Wisconsin Public Intervenor v. Mortier*, 501 U.S. 597, 610, 111 S. Ct. 2476, 115 L. Ed. 2d
532 (1991).

20 Given that the Court has indicated that the foregoing principles ring particularly true in
21 areas historically occupied by the states, it should be noted that the regulation of insurance by
22 the states is one such area. There is a history of Supreme Court cases and Congressional
23

1 action whereby the Court acknowledged this. Before considering further the Miller Act, the
2 FAR, or any of the principles of federal preemption, this history should be recounted.

3 During the last third of the 19th century, the Court was called upon to answer the
4 question of whether insurance – then subject to state regulation – was within the scope of the
5 United States Constitution’s Commerce Clause. In its 1868 decision in *Paul v. Virginia*, the
6 Court answered this question in the negative. The Court held that “[i]ssuing a policy of
7 insurance is not a transaction of commerce.” *Paul v. Virginia*, 75 US 168, 183 (1868). At the
8 time, the *Paul* Court saw issuing insurance policies as “local transactions.” *Id.* Consequently,
9 the Court felt that issuing insurance policies was not a transaction in interstate commerce, and
therefore was not subject to federal regulation.

10 But after *Paul*, the Supreme Court expanded the scope of federal regulation over
11 interstate commerce until in 1944 it essentially reversed *Paul*’s course. In *United States v*
12 *South-Eastern Underwriters Association*, the Court held that “no commercial enterprise of
13 any kind which conducts its activities across state lines has been held to be wholly beyond the
14 regulatory power of Congress under the Commerce Clause. We cannot make an exception of
15 the business of insurance.” *United States v South-Eastern Underwriters Association*, 322 US
16 533, 553 (1944). “Although Justice Black’s majority opinion emphasized that the decision
17 did not alter existing state authority to regulate insurance, the insurance industry feared
18 Congress would soon attempt to use *South-Eastern Underwriters* to fashion federal
19 regulation.” *COMMENT: After Fabe: Applying the Pireno Definition of "Business of*
20 *Insurance" in First-Clause McCarran-Ferguson Act Cases*, 2000 U Chi Legal F 447, 451
(2000). Later that same year, before the industry’s fears grew real, Congress acted.

21 Within one year of the Court’s *South-Eastern Underwriters* decision, Congress
22 responded to it by passing legislation which essentially reversed *South-Eastern Underwriters*
23 and even established a reverse preemption of state insurance regulatory law over federal law.

1 The McCarran-Ferguson Act ("the Act"), Pub L No 79-15, 59 Stat 33 (1945), codified at 15
2 USC § § 1011-15 (1994), not only prohibits Congress from enacting federal insurance
3 regulation to preempt state insurance regulatory laws, such as incidental taxes or antitrust
4 laws, it establishes that these state laws actually preempt any such federal laws:

5 No Act of Congress shall be construed to invalidate, impair, or supersede any law enacted
6 by any State for the purpose of regulating the business of insurance, or which imposes a
7 fee or tax upon such business, unless such Act specifically relates to the business of
8 insurance [...].

9 15 USC § 1012(b) (1994). Of this Act, the Court observed that when Congress enacted it,

10 Congress must have had full knowledge of the nation-wide existence of state
11 systems of regulation and taxation; of the fact that they differ greatly in the
12 scope and character of the regulations imposed and of the taxes exacted; and of
13 the further fact that many, if not all, include features which, to some extent,
14 have not been applied generally to other interstate business. Congress could
15 not have been unacquainted with these facts and its purpose was evidently to
16 throw the whole weight of its power behind the state systems, notwithstanding
17 these variations.

18 *Prudential Ins. Co. v. Benjamin*, 328 U.S. 408, 430 (1946). By creating the Act, which
19 remains the law still to this day, Congress "remov[ed] obstacles to state action" arising from
20 Congressional laws. *Id.* at 430-31.

21 Since the passage of the McCarran-Ferguson Act, the United States Supreme Court
22 has continued to recognize that it will exercise reluctance when it is asked to disturb the
23 states' insurance regulatory schemes, noting that the regulation of insurance is one particular
area that has long been occupied by the states. The Court has indicated it will proceed "with a
reluctance to disturb the state regulatory schemes that are in actual effect, either by displacing
them or by superimposing federal requirements on transactions that are tailored to meet state
requirements. When the States speak in the field of "insurance," they speak with the authority
of a long tradition. For the regulation of "insurance," though within the ambit of federal
power (*United States v. Underwriters Association*, 322 US 533), has traditionally been under
the control of the States." *SEC v. Variable Annuity Life Ins. Co of America et al*, 359 U.S. 65,

1 68-69 (1959). This historical backdrop disfavors Mr. Scarborough's argument that the Miller
2 Act or the FAR or both preempt the Insurance Code.

3 As a preliminary matter, Respondent Scarborough's motion does not point to or allege
4 any language in either the Miller Act or the FAR that expressly preempts the Insurance Code.
5 Nor does Respondent Scarborough's motion point to or allege any language in either the
6 Miller Act or the FAR that reflects a Congressional intent to occupy the entire legal field in
7 the area of the regulation of insurance. Accordingly, these first two of three possible grounds
8 for federal preemption are not alleged by Respondent Scarborough, nor do they appear to
9 apply here. The only recognized ground upon which he appears argues that preemption
10 should lie is the third ground – that he believes the Insurance Code conflicts with the Miller
11 Act and/or FAR, either directly, in that it is not possible to comply with both, or indirectly in
12 that the Insurance Code is an obstacle to the accomplishment of the federal objective
13 supposedly reflected in the Miller Act and/or FAR. For several reasons, the Miller Act and
14 the FAR do not preempt the Insurance Code.

15 First, Mr. Scarborough points to no directly controlling language, authority, or legal
16 precedent which supports his preemption argument. His motion fails to identify any court
17 decision holding that the Miller Act or the FAR preempts state insurance regulators from
18 regulating the business of insurance. Nor could OIC staff locate any court case in any United
19 States court of law which has ever held that the Miller Act or the FAR preempts state
20 insurance regulators from regulating the business of insurance.²³

21 Mr. Scarborough only supports his argument that the Miller Act supposedly preempts
22 the Insurance Code by citing just one provision in the Miller Act – former 40 U.S.C. §
23 270a(a). *See* Scarborough MSJ at p. 11, l. 12-13. But this provision contains no “clear and

²³ Nor does Mr. Scarborough argue that federal contracts/projects are not within the scope of the Code under RCW 48.01.020; he merely argues that federal preemption should lie with respect to those projects/contracts.

1 manifest” intent of Congress to preempt the Insurance Code, it does not show that Congress’
2 [purpose was to displace state insurance regulations, and no courts have ever concluded that
3 this was its intention or purpose. To the contrary, courts have held that “[t]he purpose of the
4 Miller Act ‘is to protect persons supplying materials and labor for federal projects.’” *K-W*
5 *Industries, supra*, at 642-43. “The [Miller] Act simply requires the posting of a payment bond
6 of a specified amount; it neither regulates the conduct of sureties nor ensures that such
7 conduct remains unregulated.” *Id.* at 642, fn. 3. “The Miller Act requires a contractor for a
8 federal construction project to furnish a payment bond of a statutorily specified amount to
9 secure payment for all suppliers of labor and material.” *Id.*

10 Nor does the Insurance Code conflict with former 40 U.S.C §270a(a) either directly, in
11 that it is not possible to comply with both, or indirectly in that the Insurance Code is an
12 obstacle to the accomplishment of the federal objective. As already explained, a true
13 individual surety may serve as such under the Miller Act or elsewhere since they do not
14 engage in the business of insurance and thus do not act as an insurer, so there is no conflict.

15 Respondent Scarborough’s motion for summary judgment points to several FAR
16 provisions²⁴ he feels present grounds for preemption, but again, none of the rules he cites
17 demonstrates sufficient grounds to conclude that any of the FAR preempts the Code. His
18 motion points to FAR provisions discussing adequacy of assets (48 C.F.R. §28.203-1, 48
19 C.F.R. §28.203-2, 48 C.F.R. §28.203(f) and 48 C.F.R. §28.203(b)) and a FAR provision
20 listing certain circumstances when an individual may be excluded from acting as a surety on
21 bonds submitted by offerors on procurement by the executive branch of the Federal
22 Government (48 C.F.R. §28.203-7). But none of these provisions shows an intent to occupy
23 or displace the Insurance Code. These provisions are consistent with the Miller Act’s purpose
of protecting the Federal Government and other parties to federal contracts/projects, but none

²⁴ Respondent Scarborough’s motion repeatedly erroneously references the FAR provisions as residing in 28 C.F.R.; actually, the FAR reside in 48 C.F.R.

1 demonstrates Congress's intent to occupy the traditionally long held field of state insurance
2 regulation. None of these provisions demonstrate that the Insurance Code conflicts with them
3 either directly, in that it is impossible to comply with both, either. As indicated, there is no
4 conflict. Nor does Mr. Scarborough argue that the Insurance Code's requirements serve as an
5 obstacle to the accomplishment of a federal objective contained in the provisions he cites. In
6 fact, in the instant case, not only is there no conflict between the Insurance Code and the
7 Miller Act or the FAR, but a key common purpose is shared between them: they all intend to
8 protect parties to insurance contracts, including governmental entities and subcontractors that
9 have fully performed.

10 While no state or federal court has squarely ruled that the Insurance Code is not
11 preempted by either the Miller Act or the FAR, courts *have* ruled that the Miller Act does *not*
12 preempt other state laws. *See Scandale Associated Builders & Engineers, Ltd. v. Bell Justice*
13 *Facilities Corp.*, 455 F. Supp. 2d 271 (M.D. Pa. 2006) and *K-W Industries, supra*. In both
14 *Scandale* and *K-W Industries*, federal courts concluded that the Miller Act did not preempt
15 state laws to prevent Miller Act sureties from being held civilly liable.

16 While no court decision appears to have ever addressed the specific question of
17 whether the Miller Act or FAR preempts any state's insurance regulatory requirements as to
18 Miller Act sureties, one state insurance regulator has relied upon the Ninth Circuit's decision
19 in *K-W Industries, supra*, to conclude that state insurance laws are *not* preempted by the
20 Miller Act or the FAR. In a 2007 order in the matter of "Individual Surety, Ltd.," "Individual
21 Surety," "Shonto Surety, Inc.," and Robert Joe Hanson, case number 2004-19, the Montana
22 State Auditor and Commissioner of Insurance held, relying on *K-W Industries*, that "the
23 Miller Act was not intended to occupy the entire legal field of regulating sureties on federal
construction projects and Montana law is not an obstacle to the objective of the Miller Act,"
and "the [Miller] Act requires the posting of a bond, [but] does not regulate the conduct of
sureties and does not provide that such sureties are unregulated by state law." *See Decl.*

1 Singer Exh. A. The Montana insurance regulator concluded that the purported individual
2 surety was violating insurance laws by selling construction bonds without an insurer's license
3 or authority.

4 Respondent Scarborough does cite three court decisions in support of his contention
5 that federal law preempts the Insurance Code. But each of these cases is distinguishable and
6 should be rejected.

7 In *Sperry v. State of Florida ex. Rel. Florida Bar*, 373 U.S. 379 (1963), the United
8 States Supreme Court rejected state attorney licensing requirements for attorneys to practice
9 before the United States Patent Office ("USPO"). In that case, an attorney had not been
10 licensed by the Florida state bar, but was licensed before the USPO. The attorney was
11 enjoined by the state from appearing before the USPO because he had no Florida law license.
12 The attorney wished to engage in the practice of law without a Florida license, but only before
13 the USPO, where he was licensed, and which expressly permitted persons such as him to
14 practice before the USPO, even if they did not possess a corresponding state law license as
15 well. Here, however, Mr. Scarborough actually engaged in the business of insurance on
16 federal contracts/projects within the scope of RCW 48.01.020, and he never truly acted as an
17 individual surety under the Miller Act or the FAR. Moreover, in *Sperry*, the federal statutes
18 and their legislative history showed a manifest, clear and express intention to allow attorneys
19 lacking a state law license to appear before the USPO – unlike here, where the Miller Act and
20 FAR manifest no hint of expression or intent to abrogate the Code, let alone the kind of clear
21 and manifest expression to overcome the Court's "reluctance to disturb the state regulatory
22 schemes that are in actual effect." See *SEC, supra*.

23 Respondent also relies on *Leslie Miller, Inc. v. Arkansas*, 352 U.S. 187 (1956), and the
related California case *Gartrell Constr. v. Aubry*, 940 F.2d 437 (C.A. 9th Cir. 1991), which
relied on and simply applied *Leslie Miller*. In *Leslie Miller*, an Arkansas contractor submitted
a bid, signed a contract, and did work on the contract, all without a state contractor's license.

1 He later got into trouble with the state of Arkansas over the lack of a state license. But the
2 Court found that a conflict existed between the state license requirements and the federal ones
3 (which were provided under the federal Armed Services Procurement Act) because both sets
4 of requirements were essentially the same. Consequently, the Court correctly determined that
5 the Arkansas laws allowing the state to review the same issues and same requirements the
6 federal government would review would improperly give the state a virtual power of review
7 over the federal government's decision. (*Gartrell* merely reached the same conclusion, but
8 involving California licensing laws similar to Arkansas' laws; the *Gartrell* court followed and
9 applied the *Leslie Miller* case holding as *stare decisis*.) But here, in Mr. Scarborough's case,
10 no such parallel licensing or qualification system exists as existed in *Leslie Miler* and
11 *Gartrell*. Neither the Miller Act nor the FAR includes any consideration of whether someone
12 is truly an "individual surety" or is an "insurer." Only state insurance regulations like those
13 under the Code look at this issue. Unlike *Leslie Miller* and *Gartrell*, state insurance regulators
14 and OIC are not second-guessing any federal determination made about whether a person is
15 truly an individual surety or an insurer – because no such federal determination on this point
16 is ever made. This is a concern that has traditionally long been held and considered by the
17 states, and the FAR and the Miller Act do not concern themselves with this issue. Moreover,
18 as indicated, nothing prevents individuals from serving as true individual sureties under the
19 Miller Act and FAR.

20 Moreover, the FAR should not be found to preempt the Code simply because its
21 poorly written language does not clearly and manifestly show intent to preempt. In fact, in
22 Judge Lynn J. Bush's August 1, 2008 order in the *Tip Top* matter (a copy of which may be
23 viewed at the link located at
<http://caselaw.lp.findlaw.com/data2/circs/fedclaim/2008/08352cp.pdf>), the judge emphasized
how exactly unclear the FAR's language really is:

- 1 • At page 25, she observed “the convoluted manner” in which the
2 disputed FAR provisions were drafted.
- 3 • At page 30, she observed “[t]he court acknowledges that the various
4 related sections of these particular provisions of the FAR are
5 convoluted and not easily followed. The manner in which these
6 provisions have been worded has brought about a lengthy debate [...]”
7 She noted that “ambiguities” were “created by the [FAR’s] imprecise
8 language.”
- 9 • At page 31, she observed that some FAR language’s “unfortunate
10 wording” was “so ambiguous” that it would be a “daunting endeavor”
11 to attempt to divine how it should be construed or what it intended.
- 12 • At pages 33 and 34, she again observed that the FASR included
13 provisions “written in a convoluted manner” that led to a “high”
14 susceptibility that the language could be seen as having “more than one
15 interpretation.” She expressed that the parties had differing arguments
16 about the FAR provisions’ meaning due primarily “to the confounding
17 manner in which the disputed FAR provisions were written.”

18 The FAR’s “confounding,” “convoluted,” “ambiguous,” and “unfortunate” wording, taken
19 with the Court’s “reluctance” to find preemption absent a “clear and manifest” intent of
20 Congress to preempt state law, leads to the conclusion that the Miller Act and the FAR do not
21 preempt the Code.

22 The Miller Act and the FAR do not show a “clear and manifest” intent of Congress to
23 preempt state law, and do not preempt the Insurance Code here. Mr. Scarborough presents no
reasons or legal authority to persuade to the contrary. For the foregoing reasons,
Respondent’s motion should be denied, and OIC’s cross-motion on this and all other issues
should be granted.

24 **C. The Commissioner is authorized to impose a \$25,000 fine for each violation.**

25 Respondent’s last arguments contend (1) that the Commissioner lacks the authority to
26 fine him for failing to obtain a Certificate of Authority, and (2) the Commissioner lacks the
27 authority to fine him for each violation – such as, for example, for each bond issued. Both
28 arguments should be rejected, and OIC cross-moves for summary judgment that the

1 Commissioner *does* have, in both respects, the authority Mr. Scarborough erroneously claims.
2 the Commissioner does not have.

3 Mr. Scarborough's first argument simply misstates the issue. He seems to contend
4 that the Commissioner's sole authority to act against unauthorized insurers is confined to
5 RCW 48.02.080, and apparently, RCW 48.05.185. See Scarborough MSJ at p. 13-14. Such a
6 contention is incorrect. Here, in both in the Notice of Request for Hearing for Imposition of
7 Fines, and in OIC staff's November 1, 2013 letter,²⁵ Mr. Scarborough was informed that at
8 hearing fines of \$25,000 will be sought for each violation, such as for each bond sold,
9 because, in part, Mr. Scarborough's transaction of insurance as an unauthorized insurer
10 violated RCW 48.15.020.²⁶ In turn, RCW 48.15.023(5)(a) expressly authorizes the
11 Commissioner to take all the remedies under RCW 48.02.080, and to also impose a \$25,000
12 fine "for each violation, after providing notice and an opportunity for a hearing in accordance
13 with chapters 34.05 and 48.04 RCW." Thus, RCW 48.15.023(5)(a) not only expressly
14 authorizes the Commissioner to seek the fines sought here, it expressly authorizes such fines
15 "for each violation."

16 Without mentioning RCW 48.15.020 or RCW 48.15.023, Respondent contends the
17 Commissioner may not impose a fine under a different Code section entirely – RCW
18 48.05.185. But the Commissioner is plainly authorized under RCW 48.15.023(5)(a) to
19 impose a fine of \$25,000 per violation – such as per bond, sold, per solicitation of insurance
20 business in this state, or per transaction of insurance business in this state. The
21 Commissioner, already being authorized to enforce the entire Code, RCW 48.02.060(2), and
22 having authority both express and reasonably implied, RCW 48.02.060(1), has the authority

23 _____
²⁵ A copy of this letter was submitted in support of OIC's motion to compel, and was attached and incorporated
in the OIC staff declaration that was submitted in support of that motion.

²⁶ RCW 48.15.020(1) provides that "[a]n insurer that is not authorized by the commissioner may not solicit
insurance business in this state or transact insurance business in this state, except as provided in this chapter."

1 to enforce RCW 48.15.020 and RCW 48.15.023. Any suggestion to the contrary should be
2 rejected, and OIC moves for summary judgment on this point.

3 Last, citing numerous Code provisions (except, it is worth noting, RCW 48.15.023),
4 cases, and legislative history, Mr. Scarborough also argues that the Commissioner cannot
5 impose more than a single \$10,000 fine under RCW 48.05.185. But as indicated, RCW
6 48.15.023 plainly and expressly authorizes a \$25,000 fine for every violation, or incident
7 involving a solicitation or a transaction of insurance business in this state. Mirroring RCW
8 48.01.020, the scope of such a violation occurring in this state under RCW 48.15.020 includes
9 an act "committed, in whole or in part, in the state of Washington, or affects persons or
10 property within the state and relates to or involves an insurance contract." RCW
11 48.15.023(2). This means that the Insurance Commissioner is free to impose a fine in an
12 appropriate amount, up to and including \$25,000 per violation pursuant to RCW 48.15.023.
13 Accordingly, OIC requests that Respondent's argument be rejected, and OIC requests that it
14 be granted summary judgment in its favor on this issue.

13 VII. CONCLUSION

14 Based on the foregoing, OIC respectfully requests that Respondent's motion for
15 summary judgment be denied, and that OIC's cross-motion on all issues be granted.

16 DATED this 3rd day of February, 2014.

17 OFFICE OF INSURANCE COMMISSIONER

18
19
20 By: 

21 Alan Michael Singer
22 Staff Attorney
23 Legal Affairs Division

1
2 **CERTIFICATE OF SERVICE**

3 The undersigned certifies under the penalty of perjury under the laws of the State of
4 Washington that I am now and at all times herein mentioned, a citizen of the United States, a
5 resident of the State of Washington, over the age of eighteen years, not a party to or interested
6 in the above-entitled action, and competent to be a witness herein.

7 On the date given below I caused to be served the foregoing and the subjoined
8 declaration of Alan Michael Singer Opposing Edmund Scarborough's Motion for Summary
9 Judgment, with attached exhibits, on the following individuals in the manner indicated:

10
11 Timothy Parker
12 Jason Anderson
13 Carney Badley Spellman
14 701 Fifth Ave. # 3600
15 Scattle, Washington 98104-7010
16 (XXX) Via U.S. Mail
17 (XXX) Via E-Mail

18
19 Hon. Patricia Petersen
20 5000 Capitol Blvd
21 Tumwater, Washington
22 (XXX) Via hand-delivery (c/o Kelly Cairns inbox)
23 (XXX) Via E-Mail (c/o Kelly Cairns)

SIGNED this 3rd day of February, 2014, at Tumwater, Washington.

20 
21 _____
22 Renee Molnes
23

FILED

FEB 3, 2014

Hearings Unit, OIC
Patricia D. Petersen
Chief Hearing Officer

In re the Matter of:

**EDMUND C. SCARBOROUGH and
WALTER W. WOLF,**

Respondents.

) Docket No. 13-0084
)
) **DECLARATION OF**
) **ALAN MICHAEL SINGER**
) **OPPOSING EDMUND**
) **SCARBOROUGH'S MOTION**
) **FOR SUMMARY JUDGMENT**
)

I, Alan Michael Singer, state and declare as follows:

1. My name is Alan Michael Singer. I make this Declaration on the basis of first hand personal knowledge. I am over the age of eighteen (18) years. I am competent and authorized to testify to the matters set forth herein.
2. I am employed by the Washington State Office of the Insurance Commissioner (OIC). My title is Staff Attorney within the Legal Affairs Division.
3. Attached and incorporated herein collectively as **Exhibit A** are true and correct copies of the following orders of the below-indicated state insurance regulators:
 - *Commonwealth ex rel. State Corp. Comm'n v. Global Bonding, Inc.*, Case No. INS-2007-00155 (filed July 20, 2007) (Virginia)
 - *In the Matter of Individual Sur., Ltd.*, Case No. 2004-19 (Mt. Dep't. Ins., filed Feb. 22, 2007) (Montana)
 - Official Order of the Comm'r of Ins. of the State of Tex. (filed Mar. 3, 2005) (Texas)
 - *In the Matter of Individual Sur., Ltd.*, No. D04-189 (OIC, filed Aug. 27, 2004) (Washington)
 - *In the Matter of Global Bonding*, Cause No. 03.757 (Nev. Div. of Ins., filed Mar. 9,

2004) (Nevada)

- *In the Matter of Global Bonding, Inc.*, Docket No. MC 04-39 (Conn. Ins. Dep't, filed Apr. 1, 2004) (Connecticut)
- *In the Matter of Global Bonding*, Case No. 72037-03-CO (Fla. Off. of Ins. Reg., filed Dec. 23, 2003) (Florida)
- *In the Matter of Global Bonding*, Case No. EF-2003-023 (Ga. Office of Comm'r of Ins., filed Dec. 9, 2003) (Georgia)
- *Oklahoma ex rel. Holland v. Underwriter Reins. Co. Ltd.*, Case No. 08-0420-UNI (Ok. Ins. Comm'r, filed Aug 6, 2008) (Oklahoma)
- Orders from Idaho, Virginia, and Iowa regarding Respondent Edmund Scarborough

4. In Idaho, Mr. Scarborough (and his colleague, Steve Golia) moved for summary judgment, raising many of the same issues raised in his January 21, 2014 filed with OIC. On May 28, 2013, an order entered denying his motion. A true and correct copy of this order is attached hereto and incorporated herein as **Exhibit B**.

5. A true and correct copy of Respondent Scarborough's objections, answers, and responses to OIC's discovery is attached hereto and incorporated herein as **Exhibit C**.

6. Attached hereto and incorporated herein as **Exhibit D** are true and correct copies of pages of transcribed deposition testimony in several lawsuits involving Mr. Scarborough. The deponent and the lawsuit captions are included in the first page preceding the copied pages of testimony from each deposition transcript.

7. Through his attorneys, apparently, Respondent Scarborough has shared with OIC staff copies of certain bond documents which his attorneys claim show Washington bonds Mr. Scarborough has issued. True and correct copies of these bond documents is attached hereto and incorporated herein as **Exhibit E**.

8. Attached hereto and incorporated herein as **Exhibit F** are true and correct copies of some of Mr. Scarborough's webpages and the article, "A Bold Individual Surety Claims his Coal-Backed Bonds are Rock Solid," available at the following website link as of today:

http://enr.construction.com/business_management/ethics_corruption/2013/0225-a-bold-individual-surety-claims-his-coal-backed-bonds-are-rock-solid.asp.

I declare under penalty of perjury under the laws of the State of Washington that the foregoing is true and correct.

EXECUTED this 3rd day of February, 2014 at Tumwater, Washington.



Alan Michael Singer