UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF MARYLAND

GLOBAL DIRECT SALES, LLC, PENOBSCOT INDIAN NATION, CHRISTOPHER RUSSELL and RYAN HILL, Plaintiffs, -v- AARON KROWNE, individually and d/b/a THE MORTGAGE LENDER IMPLOD-O-METER and ML-IMPLODE.COM, KROWNE CONCEPTS, INC., IMPLODE-EXPLODE HEAVY INDUSTRIES, INC., JUSTIN OWINGS, KRISTA RAILEY, STREAMLINE MARKETING, INC. and LORENA LEGGETT, Defendants.	Case No.: 8:08-cv-02468 Assigned: Hon. Deborah K. Chasanow

DEFENDANTS' MEMORANDUM OF LAW IN OPPOSITION TO PLAINTIFFS' MOTIONS FOR A TEMPORARY RESTRAINING ORDER AND PRELIMINARY INJUNCTION

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INTRODUCTION

This case involves Plaintiffs' allegations of defamation based on an article posted on a website owned by Defendant Implode-Explode Heavy Industries, Inc. (IEHI). Plaintiffs seek to enjoin Defendants "from directly or indirectly from [sic] disseminating false or misleading statements regarding Plaintiffs, their business or their business dealings."

Plaintiffs' motions should be denied for two reasons. First, their proposed order, if adopted by the Court, would be an unconstitutional prior restraint in violation of the First Amendment. Second, Plaintiffs have not made a showing that any of the speech about which they complain is actionable under defamation law.

STATEMENT OF FACTS

The article at the center of this lawsuit concerns certain mortgage practices called seller-financed down payment assistance programs. These programs allow buyers without enough money for a down payment to buy a house nevertheless. The article focuses on FHA-insured loans, which normally require a 3% buyer down payment. In a seller-financed down payment program, the buyer receives this down payment from the seller, either directly or indirectly through a third party, typically an organization that has been structured as a non-profit. These indirect methods have been developed because direct seller grants are not allowed by the FHA. While structured as non-profits, often these organizations simply funnel funds from the seller to the buyer, taking a piece of the action in the process. The IRS has called these programs "scams." (See Declaration of Krista Railey, submitted in support of this brief ("Railey Decl."), at ¶¶ 7-9 & 11, and Exs. A, D and E.)

The Government Accountability Office ("GAO") and the Department of Housing and Urban Development ("HUD") both reported in 2005 that seller-financed down payment assistance programs lead to inflated sales prices and higher default rates. This result is not entirely surprising, since, as the GAO report explains: "A purpose of a down payment is to create 'instant equity' for the new homeowner, and our work and others have shown that loans with greater owner investment generally perform better." (Railey Decl., ¶ 10, Ex. C at introduction and page 1, and Ex. B.)

Seller-financed down payment assistance programs are a target of both regulators and the legislature. In October, 2007, HUD (the department under which FHA falls) tried to terminate such programs by regulation, but was sued successfully on the grounds that the process by which the regulation was enacted did not comply with the APA. (Railey Decl, ¶ 15 & Ex. F.) Then, On July 30, 2008, President Bush signed the Housing and Economic Recovery Act ("HERA"), Section 2113 of which eliminated direct and indirect seller-financed down payment programs as of October 1, 2008. (Railey Decl.,¶ 16.) However, the down payment assistance program industry is trying to revive such programs; H.R. 6694, currently pending in the House of Representatives, would do so. (Railey Decl., ¶ 17 & Ex. G.)

In 2006, Defendant Aaron Krowne launched a news and analysis website called the Mortgage Lender Implode-O-Meter (the "Website"). The mission of the Website is to educate about the housing finance sector, and make that sector more transparent and accountable. From its onset, the Website wrote of the extreme distortions that the mortgage industry practices were having on the U.S. economy and warned of an impending debacle. The debacle came less than a year later, with the collapse of the sub-prime mortgage market, which then led to the collapse of

Wall Street investment firms, leading to the current collapsing of the banking sector and the unavailability of credit.

In addition to its own research and tracking, the Website provides a forum for independent journalists and analysts to post articles. Defendant Krista Railey, a real estate and mortgage broker with 20 years of experience, is one of those journalists. The Website features her column, "FHA Mortgage Whistle Blower." (Railey Decl., ¶4.)

In June of this year, Ms. Railey began researching seller-financed down payment assistance programs—including that of the Plaintiffs. (Railey Decl., ¶¶ 24-25.) On September 9, 2008, she uploaded a draft of the article about the Plaintiffs to the Website for internal review and editing. (Railey Decl., ¶¶ 26-27 and Russell Certification, Ex. E.) The posting inadvertently "went live," rather than remaining accessible only internally. (Railey Decl., ¶ 28.)

Almost immediately, Plaintiff Russell commented on the Website about the article, and his comment was automatically emailed to Ms. Railey. In his comment, he called her a "hack," and threatened to sue her. Surprised to receive a personal attack on a draft article that she did not believe was publicly accessible, she contacted co-defendant Aaron Krowne and others, and the draft was permanently removed from the Website within 45 minutes. On September 15, 2008, Ms. Railey published her final draft of the article and included in it a link to Mr. Russell's comment. (Railey Decl., ¶¶ 28-30 and Exs. I and J.)

As Ms. Railey set forth in her article (and also as reported in September in Forbes magazine (*see* Railey Decl., ¶ 19 and Ex. H), Plaintiffs Russell and Hill had been players in the seller-financed down payment assistance program industry, starting a decade ago with their company AmeriDream. After the IRS stripped companies like AmeriDream of their tax-exempt status, Russell and Hill had to establish another way to provide down payment assistance

programs that would be permitted under HUD regulations for mortgages to be FHA-insured. (Railey Decl., ¶¶ 11-14.) Russell and Hill, through their company Global Direct Sales, LLC, joined forces with the Penobscot Indian Nation—a government—to establish an agency that would provide grants. Such a scheme was arguably permitted under the HUD guidelines for writing mortgages, which permit grants for buyer down-payments to come through government agencies. Working in concert, the Plaintiffs established the "Grant America Program," a seller-funded down payment assistance program under the auspices of the newly-formed PIN-FHA agency. (Railey Decl., ¶¶ 13-14.)

HUD promulgated regulations to crack down on the new industry of using sovereign Indian tribes to take advantage of the "governmental agency" loophole in HUD's mortgage writing rules. The Plaintiff Penobscot Indian Nation, sued to overturn the HUD regulations (under the APA). (Railey Decl., ¶ 15.) The court agreed that HUD had not allowed enough time for public comment and PIN and HUD entered into a settlement, leading to a Stipulation. (Railey Decl., ¶ 15 and Ex. F.)

With HUD unable to enforce its recently promulgated regulations, Congress enacted and the President signed into law the Housing and Economic Recovery Act, H.R. 3221. Section 2113 of that Act provides that any funds a buyer receives directly or indirectly from a seller may not be credited toward the minimum down-payment a buyer must make to qualify the loan for FHA insurance. (Railey Decl., ¶ 16.) However, the down-payment assistance industry is backing a new bill—H.R. 6694—which is designed to revive down payment assistance programs that Section 2113 prohibited. *See* Railey Decl., ¶ 17.

Meanwhile, if the down payment assistance industry is unsuccessful in repealing Section 2113 by statute, Russell apparently has concocted another approach which inserts another tax-

exempt organization (like a church) into the complicated scheme. One organization will give the down payment to the buyer. The other will collect repayment from the seller. In a parallel transaction, the tax-exempt organizations will switch roles. That way the down payment "donors" are not being reimbursed in the actual transaction they are funding. *See* Railey Decl., Ex. H.

Plaintiffs were enraged by Railey's article. In addition to Mr. Russell's vitriolic comment, Plaintiffs' counsel sent a letter demanding that ***all*** articles about his clients be removed from the Website. *See* Braunstein Certification, Ex. O. The very next day, Plaintiffs commenced this action.

ARGUMENT

A. PLAINTIFFS' PROPOSED INJUNCTIVE RELIEF IS A PRIOR RESTRAINT IN VIOLATION OF THE FIRST AMENDMENT

Plaintiffs' motions seek to impose impermissible prior restraints on Defendants' First Amendment rights. Temporary restraining orders and injunctions forbidding speech are classic examples of prior restraints. *Alexander v. United States,* 509 U.S. 544, 550 (1993); *Smith v. Daily Mail Publishing Co.*, 443 U.S. 97, 103 (1979). Courts presume that prior restraints are unconstitutional. *Bantam Books, Inc. v. Sullivan*, 372 U.S. 58, 70 (1963). *See also Nebraska Press Assn. v. Stuart*, 427 U.S. 539, 559 (1976) ("[P]rior restraints on speech and publication are the most serious and the least tolerable infringement on First Amendment rights."); *In re Charlotte Observer (A Div. of Knight Pub. Co. and Herald Pub. Co.)*, 921 F.2d 47, 49 (4th Cir. 1990) (same).

Prior restraints are allowed only in certain narrow circumstances constituting "exceptional cases," such as to protect military secrets in wartime or to enjoin destruction of

property rights like trademarks. *Near v. Minnesota*, 283 U.S. 697, 716 (1931); *San Francisco Arts & Athletics v. U.S.O.C.*, 483 U.S. 522, 540-541 (1987). Defamatory speech is not an exception to the general rule. *See Organization for a Better Austin v. Keefe,* 402 U.S. 415, 418-19 (1971) (internal citations omitted). *See also American Malting Co. v. Keitel,* 209 F. 351, 354 (2d Cir. 1913) ("Equity will not restrain by injunction the threatened publication of a libel, as such, however great the injury to property may be. This is the universal rule in the United States and was formerly the rule in England."); *Community for Creative Non-Violence v. Pierce*, 814 F.2d 663, (D.C. Cir. 1987) (Mikva, J.) ("The usual rule is that equity does not enjoin a libel or slander and that the only remedy for defamation is an action for damages.") (internal quotation marks and citation omitted); *Alberti v. Cruise*, 383 F.2d 268, 272 (1967) (generally, injunctions will not issue for defamation).

Maryland also has a strong public policy favoring the freedom of the press and against any prior restraints of that freedom. *See, e.g., Howard Sports Daily v. Public Service Comm.*, 179 Md. 355, 361, 18 A.2d 210, 215 (1941) (the State may not place prior restraint on printed publications or take action that might prevent discussion of public matters); *Sigma Delta Chi v. Speaker*, 270 Md. 1, 4, 310 A.2d 156, 158 (1973) ("freedom of the press … has been zealously safeguarded in Maryland."); *Telnikoff v. Matusevitch*, 347 Md. 561, 589-90, 702 A.2d 230, 244 (1997) .

The *Keefe* case is highly instructive in this instance. Keefe, a realtor, sought to enjoin a community organization from publishing and distributing leaflets critical of his business practices. The leaflets said that plaintiff was a "panic peddler" who was encouraging "blockbusting." *Keefe*, 402 U.S. at 417. The organization published the realtor's home number

in some of its leaflets, urging people to call and complain. Keefe argued that the leafleting activity harmed his right to privacy and constituted undue coercion. *Keefe*, 402 U.S. at 417-18.

The Supreme Court of the United States held:

> It is elementary, of course, that in a case of this kind the courts do not concern themselves with the truth or validity of the publication. Under *Near v. Minnesota,* the injunction, so far as it imposes prior restraint on speech and publication, constitutes an impermissible restraint on First Amendment rights .... No prior decisions support the claim that the interest of an individual in being free from public criticism of his business practices in pamphlets or leaflets warrants use of the injunctive power of a court.

See Keefe, 402 U.S. at 418-19 (internal citations omitted).

Plaintiffs have alleged that their reputations are being harmed. Like invasion of privacy, this is a harm to the person (rather than to a property right). Plaintiffs are asking the court to enjoin Defendants' publication, prior to any adjudication as to the truth or validity of Defendants' statements. Such an injunction shall not lie absent exceptional circumstances, such as an imminent threat to national security, or absent immediate harm to a property right, such as copyright or trademark. *See Near*, 283 U.S. at 716; *San Francisco Arts & Athletics,* 483 U.S. at 540-41. Plaintiffs' claims of harm do not even come close to the "exceptional circumstances" standard that they would need to show for a pre-trial injunction to issue.

Adding insult to injury is the overly broad and vague nature of the order that Plaintiffs seek. Specifically, Plaintiffs ask the Court to enjoin Defendants "from directly or indirectly from [sic] disseminating false or misleading statements regarding Plaintiffs, their business or their business dealings." Thus, if Defendants were to publish anything critical of Plaintiffs (regardless of the reasonableness of Defendants' efforts to verify the information), Plaintiffs could bring a motion for contempt because they consider the statements to be "misleading" or "false." Such a scheme would require Defendants to seek the Court's permission before publishing anything

critical about Plaintiffs, their business, or their business dealings. This is the very essence of an impermissible prior restraint.

Pre-trial injunctive relief is not available to Plaintiffs under the weight of the Supreme Court's many cases addressing this issue. The harm Plaintiffs have alleged does not rise to the level of any exceptional circumstance warranting a deviation from this long-standing jurisprudence. The Court should deny Plaintiffs' motions.

B. PLAINTIFFS HAVE NOT SHOWN ANYTHING APPROACHING A "STRONG LIKELIHOOD" OF PREVAILING ON THE MERITS

To be granted a preliminary injunction, Plaintiffs must show a strong likelihood of success on the merits where, as here, Plaintiffs cannot show that their harm is any greater than Defendants'. *Direx Israel, Ltd. v. Breakthrough Medical Corp.*, 952 F.2d 802, 812-13 (4th Cir. 1991). For Plaintiffs to prevail on their underlying claims,[1] they would have to show: (1) a false statement concerning the Plaintiffs, (2) published to a third party, (3) the requisite degree of fault, and (4) harm. *Henry v. National Ass'n of Air Traffic Specialists, Inc.*, 836 F.Supp. 1204, 1210 (D.Md. 1993). If they are public officials or public figures, Plaintiffs must show that the Defendants acted with constitutional malice—that is, with the actual knowledge of the falsity of the accused speech, or with reckless disregard for its truth. *Id.; New York Times v. Sullivan,* 376 U.S. 254, 288-91 (1964). The reckless disregard standard is purely subjective in the context of defamation claims. The standard is whether the defendant (1) published the statement with a "high degree of awareness of ... probable falsity," *Garrison v. Louisiana,* 379 U.S. 64, 74 (1964),

[1] Plaintiffs have asserted three claims: defamation, libel, and unfair competition. All three claims depend upon Plaintiffs showing that the Defendants defamed them. Thus, for purposes of this analysis, Plaintiffs must, at a minimum, show a strong likelihood of success on the merits on their defamation claim.

or (2) "in fact entertained serious doubts as to the truth of his publication." *St. Amant v. Thompson,* 390 U.S. 727, 731 (1968).

a. The constitutional malice standard applies.

As a government, the Penobscot Indian Nation is necessarily a "public official" for purposes of defamation law: no activity can be more official than the governance of a sovereign nation. As stated by the Supreme Court in *New York Times v. Sullivan*, we have a "profound national commitment to the principle that debate on public issues should be uninhibited, robust, and wide-open, and that it may well include vehement, caustic, and sometimes unpleasantly sharp attacks on government and public officials." 376 U.S. 254, 270 (1964). Indeed, as quoted by the *New York Times* Court, "[f]or good reason, 'no court of last resort in this country has ever held, or even suggested, that prosecutions for libel on government have any place in the American system of jurisprudence.'" *Id.* at 291 (citing *City of Chicago v. Tribune Co.*, 307 Ill. 595, 601, 139 N.E. 86, 88 (1923)).

GDS, Hill, and Russell are limited purpose public figures. There are two main prongs in the determination as to whether a person is a limited purpose public figure: first, whether there was a "public controversy" that gave rise to the alleged defamation and second, whether the "nature and extent of [the] individual's participation" in that controversy justifies public figure status. *See Foretich v. Capital Cities/ABC, Inc.*, 37 F.3d 1541, 1553 (4th Cir. 1994). A "'public controversy' 'is not simply a matter of interest to the public; it must be a real dispute, the outcome of which affects the general public or some segment of it in an appreciable way.'" *Foretich*, 37 F.3d at 1554 (quoting *Waldbaum v. Fairchild Publications, Inc.*, 627 F.2d 1287, 1296 (D.C. Cir.) (1980)). The Fourth Circuit has set out five requirements for a defamation

plaintiff to be considered a limited purpose public figure: (1) the plaintiff must have "access to channels of effective communication"; (2) the plaintiff must have voluntarily assumed a role of special prominence in the public controversy; (3) the plaintiff must have sought to influence the resolution or outcome of the controversy; (4) the controversy must exist before the publication of the defamatory statement; and (5) the plaintiff must have retained public-figure status at the time of the alleged defamation. *See Reuber v. Food Chemical News, Inc.*, 925 F.2d 703, 708-11 (4th Cir.) (*en banc*).

With the mortgage and housing crisis threatening to collapse the national (and global) economy, and Congress passing laws to prohibit seller-backed down-payment assistance, and now possibly reviving such assistance, it is beyond dispute that the subject of mortgage lending generally, FHA-backed mortgages, and practices impacting the ability of potential buyers to qualify for mortgages and home purchases constitute matters of public controversy.

Russell, Hill, and GDS are deeply involved in down payment assistance programs. Furthermore, they have sought voluntarily sought public attention, through their participation in and distribution of web sites and press releases. And they have received significant attention in the news media, starting well before, and continuing through, the time of the publication of Ms. Railey's article. They have also sought to impact the outcome of the dispute over seller-financed down payment assistance. *See* Railey Decl., ¶¶ 18-23. The nature and extent of the involvement by Plaintiffs Russell, Hill, and Global Direct in the down payment assistance industry, which plays a fundamental role in certain FHA-backed mortgages and home purchases, justify their being considered public figures here.

b. Plaintiffs have not shown a strong likelihood that Defendants acted with the requisite degree of fault.

Here, Plaintiffs must show a strong likelihood that they can prove that Defendants acted with constitutional malice. Further, constitutional malice must be demonstrated with "clear and convincing proof." *Gertz*, 418 U.S. at 342. Here, as shown in Ms. Railey's declaration, each of her statements were well-supported and based on thorough research. To suggest that she acted with constitutional malice is ludicrous.[2]

Plaintiffs point to no evidence of malice. Indeed, the only possible support for "malice" to which Plaintiffs even hint is the suggestion that Ms. Railey's article was in retaliation for Plaintiffs' not advertising on the Website. However, as Ms. Railey explains in her declaration, she had no knowledge that any approaches to Plaintiffs concerning advertising were rebuffed. (Railey Decl., ¶ 37) Furthermore, Ms. Railey began investigating her article due to her own interests, and not by direction of any other Defendants. Railey Decl., ¶¶ 24-25. There is no motive for any malice, and Plaintiffs can point to no evidence to the contrary.

c. The statements Plaintiffs allege to be defamatory are well-supported.

Plaintiffs point to 14 statements from Ms. Railey's draft article as the basis for their defamation claim. Plaintiffs cannot make the requisite showing of likelihood of success on the merits for any of these statements for at least two reasons.[3] First, as noted above, the Plaintiffs

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[2] Even were there some question as to whether the Plaintiffs are public figures and the applicability of the malice standard, Ms. Railey, with her exhaustive research, most of which was embedded as links in her article for the reader to evaluate for himself, was certainly reasonable in her belief in the truth of her factual statements. The negligence standard that applies to non-public figures requires no more. *Jacron Sales Co., Inc. v. Sindorf*, 276 Md. 580, 596 (1976).

[3] At this preliminary stage of the proceedings, with factual and legal analysis only beginning, it is likely Defendants will develop additional defenses in the future. For instance, it seems likely that Ms. Railey's article will be determined to be a fair comment on a matter of public interest

completely failed to prove up the requisite constitutional malice. Second, Plaintiffs have presented no real evidence of the falsity of the statements at issue.

Importantly, the **Plaintiffs** bear the burden to prove falsity in this matter of obvious public concern. *Philadelphia Newspapers, Inc. v. Hepps*, 475 U.S. 767, 775-76 (1986). Moreover, statements are non-actionable if substantially accurate, even if minor details are inaccurate. *See AIDS Counseling & Testing Ctrs. v. Group W Television, Inc.*, 903 F.2d 1000, 1004 (4th Cir. 1990). In addition, to be actionable, a statement must contain or imply a statement of **provable** false fact. *See e.g.*, *Milkovic v. Lorain Journal Co.*, 497 U.S. 1 (1990); *Chapin v. Knight-Ridder, Inc.*, 993 F.2d 1087, 1093 (4th Cir. 1993) (stating that "[t]hough opinion per se is not immune from a suit for libel, a statement is not actionable unless it asserts a provably false fact or factual connotation").

Plaintiffs have not made any showing of falsity for any of the statements they challenge. Instead, Plaintiffs simply baldly assert that the statements are false. Instead, the only evidence that goes to truth or falsity is Ms. Railey's declaration, which details the support for her article. (Railey Decl., ¶¶ 35-36 and associated exhibits.)

C. DEFENDANTS AND THE PUBLIC WILL BE IRREPARABLY HARMED BY ENTRY OF THE ORDER

Plaintiffs are engaging in mortgage practices that are, at the very least, suspect. As anyone who is aware of current events knows, the U.S. economy is facing ruin due in large part to suspicious home mortgage lending practices. Plaintiffs' business false squarely within the public spotlight.

(*Mashburn v. Collin*, 355 So. 2d 879, 882 (La. 1977)), or portions of it "imaginative expression" or "rhetorical hyperbole." *Milkovich v. Lorain Journal Co.*, 497 U.S. 1, 20 (1990).

The Website provides in-depth news coverage of the mortgage lending industry. It began warning of the impending mortgage debacle in 2006—long before it was on the radar screen of every regulator and consumer. Participants of all types in the mortgage field rely on the Website as a sentry in the industry.

Both the public and Defendants would be harmed by the proposed injunction. The public would be deprived of an important, unique and timely source of information about an issue of grave national concern. As the Supreme Court articulated in *Nebraska Press Association*:

> Prior restraints fall on speech with a brutality and a finality all their own. Even if they are ultimately lifted they cause irremediable loss: a loss in the immediacy, the impact, of speech. . . . Indeed it is the hypothesis of the First Amendment that injury is inflicted on our society when we stifle the immediacy of speech."

Nebraska Press Assoc., 427 U.S. at 609 (quoting A. Bickel, The Morality of Consent 61 (1975)). Here, the public would be impermissibly and irreparably injured in its right to be informed on a matter of vital interest.

Defendants would be irreparably harmed because their speech would be not just chilled but frozen. *See Nebraska Press Assn.*, 427 U.S. at 559 ("A prior restraint... has an immediate and irreversible sanction. If it can be said that a threat of criminal or civil sanctions after publication 'chills' speech, prior restraint 'freezes' it at least for the time."). Each passing day that an injunction were to necessitate that Defendants seek the Court's license before speaking would constitute and irreparable infringement on First Amendment values.

The harm to the First Amendment rights of the public and of Defendants far outweighs any harm to Plaintiffs' reputations, particularly when such harm, should it exist, can be remedied by an award of damages.

CONCLUSION

Plaintiffs have asked for relief that is inappropriate and unconstitutional under the circumstances. Nothing in this case justifies imposing a prior restraint on Defendants' speech. Furthermore, Plaintiffs have not met their burden of showing a "strong likelihood" of prevailing on the merits, nor could they given the facts of this case.

For these and the foregoing reasons, Defendants respectfully request that the Court deny Plaintiffs' motions for a temporary restraining order and a preliminary injunction.

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