In the Kalamazoo County Circuit Court For the State of Michigan

SCOTTSDALE CAPITAL ADVISORS CORPORATION,

Plaintiff,

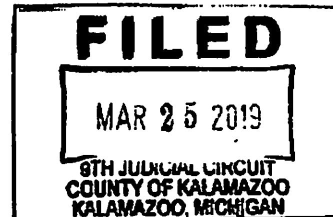
v.

MORNINGLIGHTMOUNTAIN, LLC, MICHAEL GOODE, and DOES 1-10,

Defendants.

Civil No. 18-0153-CZ

HON. ALEXANDER C. LIPSEY



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DEFENDANTS' REPLY IN SUPPORT OF MOTION FOR SUMMARY DISPOSITION OF THIRD AMENDED COMPLAINT

I. SPECIAL STANDARD OF REVIEW: Scottsdale ignores the new points raised in Defendants' opening brief that the special standard applies in private-figure cases.

Although the Court previously ruled that the special standard of review in defamation cases is limited to cases involving public officials and public figures, (Op. 4 (Oct. 4, 2018)), Defendants have offered caselaw proving that the special standard also applies in private-figure cases. (Br. 6–8 (citing *Rouch II*, *Trost*, and *Royal Palace Homes*).) Scottsdale offered no critique of these cases when opposing the last motion for summary disposition, and it has failed to do so again. The Court should treat this as a concession that Defendants' analysis is correct.

II. THE STATEMENT: Scottsdale has not addressed Defendants' core arguments.

A. *Hyperbole.* As noted in Defendants' opening brief, a challenged statement is not actionable unless it is *provably* false. (Br. 8.) In opposition, Scottsdale simply says the facts of this case are different than the *Komorov* example cited in the opening brief. (Opp'n 6–7.) (Notably, Scottsdale ignores *Hogan*, *Fasi*, *Haberstroh*, or *Springett*. (Br. 9, n. 24.)) Of course, the factual differences are irrelevant; the legal principle is the same. Statements of the "everyone knows" variety are not *provably* false. Scottsdale cannot "poll" the community for its proofs. (Br. 9.) Scottsdale does not dispute this; it offers not a single case where "polling the community" was recognized as a viable means of proving an "everybody knows" statement. (*See* Opp'n 6–7.) Indeed, Scottsdale just ignores the impossibility of its proofs altogether.

B. *Substantial Truth.* Scottsdale does not dispute that the actual words of the challenged statement are true. The Court has already agreed with Defendants that the statements are true, too. (Op. 7.)

Instead, Scottsdale argues that the statement falsely implies that FINRA fined it $1.5 million for its involvement in a penny stock pump-and-dump scheme, which it says is an "inference of criminal conduct." (Opp'n 7, Part C.1.) This is unpersuasive for three reasons.

First, FINRA is a *civil* regulatory authority that would have no authority to punish Scottsdale for *criminal* conduct. Keeping in mind that *Air Wisconsin* requires the Court to assess

the challenged statement from the perspective of the reasonable audience—here, sophisticated consumers of news concerning the penny-stock market—the implication Scottsdale wishes to read into the statement is not reasonable. The reasonable audience for the Article would understand that FINRA fines are civil in nature.

Second, even if the reasonable audience made that unreasonable inference, Scottsdale refuses to acknowledge that a libel defendant "is not responsible for every defamatory implication a reader might draw from his report of true facts, absent evidence that he *intended* the defamatory implication." *Royal Palace Homes, Inc.* v. *Channel 7 of Det., Inc.*, 197 Mich. App. 48, 56 (1992) (emphasis added). Scottsdale has not pleaded any facts from which the Court could reasonably infer that Defendants *intended* the implication that Scottsdale tries to read into the statement. Tellingly, Scottsdale does not cite a single fact *pleaded in the complaint* to establish this intent element. (*See* Opp'n 7–9.)

Third, the implication of which Scottsdale complains is substantially true. "[A] statement is not considered false unless it would have a different effect on the mind of the reader from that which the pleaded truth would have produced." *Hawkins* v. *Mercy Health Servs.*, 230 Mich. App. 315, 332 n.12 (1998) (cleaned up). Here, the pleaded truth is that Scottsdale was fined for selling securities without a registration or an exemption from registration, not for engaging in pump-and-dump schemes. (Compl. ¶ 22; Opp'n 8.) Yet Scottsdale *does not dispute* Defendants' analysis of the FINRA panel's decision, which details how and why FINRA tied the fine to Scottsdale's failure to properly police transactions susceptible to pump-and-dump frauds. (Br. 11–14). FINRA held that shares sold through Scottsdale were not exempt from registration because the exemption required Scottsdale *to properly police transactions*, which it did not do. (*Id.* at 12–13.) Thus, in FINRA's estimation, Scottsdale was partly responsible for the pump-and-dump schemes. Had Scottsdale done its job properly, innocent people would not have lost money. The reasonable audience—sophisticated consumers of news concerning the penny-stock market—would detect no meaningful difference between "engaging in" behavior and

"being responsible for" that behavior. In both cases, the reasonable audience would understand Scottsdale was culpable for frauds perpetrated on the market.

C. ***Defamatory Meaning.***[1] Scottsdale argues that the FINRA report is not part of the Article that must be reviewed when assessing context. (Opp'n 8.) It cites *Nucor Corp.* and *Mandel*, cases from North Carolina and Missouri, for the proposition that defamatory meaning is judged by the content within the "four corners of the publication." (*Ibid.*) Defendants do not quarrel with that statement of the law conceptually, but the four corners of a publication includes documents attached to the publication, *Service Employees Int'l Union Local 5* v. *Professional Janitorial Serv. of Houston, Inc.*, 415 S.W.3d 387, 402–403 (Tex. App. 2013), just like attachments to a complaint are part of the complaint, *cf. Slater* v. *Ann Arbor Pub. Schs. Bd. of Educ.*, 250 Mich. App. 419, 427 (2002). Neither *Nucor Corp.* nor *Mandel* involved online publications or publications with attachments.[2] Links embedded in online articles are the functional equivalent of attachments. Scottsdale can't complain that the Article omits relevant information about the FINRA report, but then ignore that the Article links the audience to the report, making it available in 10 keystrokes and a few clicks of a mouse—the digital equivalent of turning to a motion's index of exhibits, finding the right exhibit number, and then flipping to the correct tab. *See Adelson* v. *Harris*, 973 F. Supp. 2d 467 (SDNY 2013), *affirmed* 876 F.3d 413 (CA2 2017); *Adelson* v. *Harris*, 402 P.2d 665 (Nev. 2017).

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[1] Scottsdale renews its request for sanctions, arguing the Court has already held the challenged statement to be defamatory. (Opp'n 5, n.1.) Scottsdale misinterprets the Court's statement. (*See* Part II.B, *supra.*) Otherwise, it is dictum; any ruling on the element of truth was not germane to the Court's ruling on the element of fault. Regardless, earlier rulings have no effect *for appellate purposes* because the new complaint *supersedes* the previous complaint, which is "abandoned and withdrawn." MCR 2.118(A)(4); *Grzesick* v. *Cepela*, 237 Mich. App. 554, 562 (1999). Defendants must re-raise their arguments here to preserve their challenges to any earlier rulings. *Cf. id.* at 562–563. This was explained in Defendants' reply brief in support of its last motion. Yet here Scottsdale is again asking for sanctions, recycling the same argument and caselaw, without any effort to rebut *Grzesick*.

[2] The challenged statements were in an email, *Nucor Corp.* v. *Prudential Equity Group*, 659 S.E.2d 483, 485 (N.C. App. 2008), and a letter written to members of a city council. *Mandel* v. *O'Connor*, 99 S.W.3d 33, 37 (Mo. App. 2003).

Scottsdale also renews its argument that the damage is done by the time the audience reads the FINRA report. This isn't the law. The whole article, including attachments, must be considered. (Br. 13.)

D. *Fair-Comment Privilege.* The challenged statement is privileged from liability under Michigan's fair-comment privilege. Rather than address this privilege, Scottsdale argues why the largely defunct public-interest privilege does not apply. *Rouch II*, 427 Mich. 157, 180–182 n.13 (1986) (observing that the public-interest privilege has been largely subsumed under the *New York Times* test). The fair-comment privilege remains and has more recently been called the "qualified privilege," *Dadd* v. *Mount Hope Church*, 486 Mich. 857 (2010). In that *private-figure* case, the Supreme Court held that plaintiffs must prove untruth *and* actual malice" when the privilege applies. *Id.* at 857, n.1. In a partial concurrence, Justice Markman traced the contours of the privilege. *See also*, *id.* at 860–862, 864–867 (Markman, J., dissenting in part).[3]

"The principle of 'fair comment' affords legal immunity for the honest expression of opinion on matters of legitimate public interest when based upon a true or privileged statement of fact." *Deitz* v. *Wometco West Mich. TV*, 160 Mich. App. 367, 376 (1987).[4] Here, the statement is fair comment by a media defendant about disciplinary action taken against a regulated entity whose willful nonfeasance facilitated pump-and-dump frauds, according to a trustworthy source. Scottsdale says that "criminal matters" are not always matters of public interest, (Opp'n 11), but that confuses the real issues of interest to the public in two respects. First, as noted in Part II.B, *supra*, the FINRA fine is a *civil* matter. Second, Defendants provide news to investors, including warnings about stock manipulation schemes to prevent them from being fleeced. The

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[3] Justice Markman's discussion of the qualified privilege is consistent with the majority opinion. The Court differed over whether the jury was properly instructed. The majority did not believe it reversible error for the instructions to omit a reference to "actual malice," finding the use of "reckless disregard" to be sufficient under the circumstances.

[4] *Deitz* says the fault standard is negligence, but that holding is inconsistent with *Dadd*, a subsequent Supreme Court decision that plainly holds to the contrary. *Dadd* 486 Mich. at 857 n.1.

public has an interest in understanding how pump-and-dump schemes work, how they succeed (in part through companies like Scottsdale failing to police transactions), whether a scheme has been detected or is suspected (so that investors can protect themselves), and whether they have been victimized by a scheme (so they can seek redress), among other interests. To overcome the privilege, Scottsdale must plead and prove actual malice under *Dadd*, even if it claims to be a private figure. It has not done so. (*See* Br. 14–17.)

E. ***Fault.*** Scottsdale alleges that a reasonable journalist "reads the documents he cites." (Compl. ¶ 22.) The Article in which the Statement appears quotes from the FINRA report at length. The only reasonable inference is that Mr. Goode read the report. (Br. 18.)

Scottsdale also alleges that a reasonable journalist would not report or imply that a fine for procedural noncompliance is the equivalent of a fine for intentional pump-and-dump activity. (Compl. ¶ 22.) As noted in Part II.B, the Court has already ruled that Defendants did not report this. Proceeding on a defamation-by-implication theory requires Scottsdale to plead facts from which the Court can infer that Defendants *intended* the implication. In their opening brief, and in Part II.B, *supra*, Defendants observed that Scottsdale has pleaded no such facts. (Br. 17–19.) Scottsdale does not dispute this. (Opp'n 3–4.) Instead, it merely points to its conclusory allegation that Defendants "acted negligently." (*Ibid.*) This is inadequate to state a claim upon which relief can be granted.

Respectfully submitted,

BUTZEL LONG, P.C.

Dated: MARCH 25, 2019

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