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UNITED STATES DISTRICT COURT

DISTRICT OF NEVADA

SECURITIES AND EXCHANGE COMMISSION,

Plaintiff,

vs.

PROFIT CONNECT WEALTH SERVICES, INC., JOY I. KOVAR, and BRENT CARSON KOVAR,

Defendants.

Case No.

PLAINTIFF SECURITIES AND EXCHANGE COMMISSION'S MEMORANDUM OF POINTS AND AUTHORITIES IN SUPPORT OF ITS *EX PARTE* APPLICATION FOR ENTRY OF TEMPORARY RESTRAINING ORDER AND ORDERS: (1) FREEZING ASSETS; (2) REQUIRING ACCOUNTINGS; (3) PROHIBITING THE DESTRUCTION OF DOCUMENTS; (4) GRANTING EXPEDITED DISCOVERY; AND (5) APPOINTING A TEMPORARY REEIVER; AND ORDER TO SHOW CAUSE RE PRELIMINARY INJUNCTION AND APPOINTMENT OF A PERMANENT RECEIVER

(Filed Under Seal)

I. INTRODUCTION

Plaintiff Securities and Exchange Commission ("SEC") brings this emergency action to stop an ongoing investment fraud being perpetrated by Defendant Joy Irene Carson Kovar ("J. Kovar") and her recidivist son, Defendant Brent C. Kovar ("B. Kovar"), through their entity, Defendant Profit Connect Wealth Services, Inc. ("Profit Connect") (collectively "Defendants"). Over 277 investors have invested more than $12 million with Profit Connect since at least May 2018, on promises of guaranteed 20% to 30% in annual returns from a pooled investor fund. Profit Connect claims to use a proprietary Artificial Intelligence "supercomputer" to determine where to allocate investor funds in order to generate consistently high returns with no market volatility. In reality, none of the money has been invested. Instead, Defendants have used investor funds for J. Kovar's personal expenses, to pay commissions to promoters who hype Profit Connect on various social media platforms, and to pay other investors in a Ponzi-like fashion. Profit Connect further advertises that investor funds are safe and guaranteed, and that Profit Connect has financial reserves significantly higher than all money raised. This is false. As of March 2021, Profit Connect had less than 20% of the total investor funds raised in its accounts.

The Profit Connect scheme is not only ongoing, it is gaining in momentum. In May 2021 alone, Profit Connect raised over $2.2 million from investors. Yet in the last two months (April 21, 2021 through June 9, 2021) J. Kovar has made ten transfers of at least $120,000 each from the Profit Connect account to her personal account, totaling more than $1.2 million in misappropriated investor funds. This leaves only $3,504,541.38 in the Profit Connect accounts as of May 31, 2021.

The SEC seeks emergency relief to stop this ongoing fraud and protect investors' assets and funds. Without the intervention of the Court, there will be nothing to stop Defendants' egregious securities laws violations from continuing to further harm investors.

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II. STATEMENT OF FACTS

A. The Defendants and Their Entity

Profit Connect's principal place of business is in Las Vegas, NV. Declaration of Teri Melson ("Melson Decl.") at ¶ 9, Ex. 4 at pp. 19-20. J. Kovar, age 86, formed Profit Connect on May 2, 2018, listing herself as the company's president, secretary, treasurer and sole director. Melson Decl. at ¶ 5, Ex. 1. In April 2019, J. Kovar named B. Kovar as the director of Profit Connect in her place, and added another individual as the secretary of Profit Connect. *Id.* at ¶ 6, Ex. 2. J. Kovar remained the president and treasurer of Profit Connect, positions she holds today. *Id.* B. Kovar has been identified on social media platforms as the company's CEO. Declaration of Elizabeth Blaylock ("Blaylock Decl.") at ¶ 7, Ex. 1. Profit Connect admits on its website that neither it nor its securities offerings are registered with the Commission. Melson Decl. at ¶ 9, Ex. 4 at p. 12. Neither J. Kovar or B. Kovar are registered in any fashion with the SEC. Melson Decl. at ¶ 7.

J. Kovar and B. Kovar control Profit Connect's bank accounts. J. Kovar has opened at least eight bank accounts in the name of Profit Connect at three different banks. Declaration of Dora Zaldivar ("Zaldivar Decl.") at ¶ 8. J. Kovar was the sole signatory on six of the Profit Connect bank accounts, including the primary account that received investor funds, until May 21, 2021, when she added B. Kovar as a signatory to two existing Profit Connect bank accounts, and to two new bank accounts in the name of Profit Connect. *Id.* at ¶ 8(j), Ex. 2. B. Kovar identified himself as "president" of Profit Connect in these new bank opening documents, and J. Kovar was identified as the CEO of Profit Connect. *Id*. at ¶ 8(i), Ex. 2. Investor funds transferred to J. Kovar's personal bank account have been earmarked for B. Kovar and some investors have referenced "Brent" when wiring money to Profit Connect. *Id.* at ¶ 9(d) and 9(h)(ii). In total, B. Kovar has received almost $353,000 of Profit Connect investor funds through his use of a Profit Connect credit card. Zaldivar Decl. at ¶ 22.

Profit Connect is not the Kovars' first business enterprise. In 2010, the SEC sued B. Kovar for fraud in connection with another entity, Sky Way Global, LLC (dba Sky Way Global, Inc.), a pump and dump scheme. *SEC v. Sky Way Global LLC, et al.*, Civ. No. 09-CV-455 (M.D. Fla. Mar. 13, 2009). Melson Decl. at ¶ 8, Ex. 3. B. Kovar, while neither admitting nor denying the charges, was permanently enjoined from future violations of the securities laws, banned from participating in penny stock offerings, and barred from serving as an officer or a director of a public company. *Id.*

B. The Profit Connect Offering

Since May 2018, Defendants have raised at least $12 million from at least 277 investors residing in numerous states. Zaldivar Decl. at ¶¶ 9(d) and 9(e). Defendants solicit through Profit Connect's website, social media, and by word of mouth.

On its website, Profit Connect represents that investors who open an account are purchasing a Wealth Builder supercomputer "seat" which purportedly represents "cycle time on our supercomputer system." Melson Decl. at ¶ 9, Ex. 4 at page 12. The website states that after opening a wealth builder account, a representative will call the investor to answer any questions and to provide a "custom wealth builder spreadsheet" that is updated monthly. *Id*. at page 12. Funds are purportedly invested in sectors chosen by the Profit Connect "supercomputer" and the profits are then "deposit[ed] into [a] FDIC-NCUA Insured Profit Connect Cumulative Business Account" at Bank of America, Chase, Wells Fargo and/or Navy Federal Credit Union." *Id.* at page 14. The website also includes the official logos for each of these banks in an attempt to portray Profit Connect as having a business relationship or partnership with these financial institutions, which Profit Connect refers to as "our banking association," and Profit Connect heavily promotes to investors that because their profits are deposited into these accounts their money is insured and safe. *Id.* at page 14. Profit Connect also provides step by step instructions on its website showing investors how to open a self-directed IRA so that they can invest their retirement funds with Profit Connect. *Id.* at page 14.

Profit Connect's growing popularity appears to be in part due to a multi-level-marketing operation that promotes Profit Connect through various social media platforms. Profit Connect has a separate website devoted to the purported 1000+ "successful worldwide agents and affiliates[.]" *Id.* at ¶ 15, Ex. 10. In addition, a number of individuals promote Profit Connect on YouTube, Facebook, Instagram and LinkedIn. *Id.* at ¶ 16. These promoters often post on their social media a screenshot of the Profit Connect website showing 20%-30% guaranteed returns. *Id.*

Promoters are well-compensated for their efforts. The Profit Connect website for agents and affiliates indicates that they are paid up to 20% for referrals and can receive additional bonuses based on factors such as the number of referrals and monthly sales volume. *Id*. at ¶ 15, Ex.10. Bank records indicate that at least 26% of investor funds were used to pay commissions and bonuses to those who promoted Profit Connect. Zaldivar Decl. at ¶ 9(h)(i).

C. Defendants' Material Misrepresentations and Omissions

Defendants solicit investors to Profit Connect with false promises of lucrative, guaranteed returns. Profit Connect's website tells investors that they have the opportunity to invest by opening a "Wealth Builder Supercomputer Seat APR account." Melson Decl. at ¶ 9, Ex. 4 at p. 13. The website further claims that the company uses "proprietary A[rtificial] intelligence" and a "supercomputer" in order to obtain "a higher return APR." *Id.* ¶ 9, Ex. 4 at p. 12. The website further represents that Wealth Builder accounts are "not the same as money market funds or a savings account, the APR is not affected by the stock market, foreign exchange currency market or the asset market." *Id.* ¶ 9, Ex. 4 at p. 13. Profit Connect claims that it has four "Wealth Services income streams" including a Block-Chain Ai Prediction Algorithm, Forex & Asset Trading, Stock Trading, and Venture Capital Services. *Id.* ¶ 9, Ex. 4 at p. 16; ¶ 11, Ex. 6.

The Profit Connect website guarantees investors that they will receive fixed annual returns of 20% to 30%, depending on the amount invested. *Id.* ¶ 9, Ex. 4 at p.

13. Profit Connect also advertises on its website that it has a "monthly subscription" option in which an investor deposits a set amount each month, ranging from $50 to $1,000, with guaranteed returns of 15% to 20% per year. *Id.* On its website Profit Connect actively encourages the investment of funds from investors IRAs. *Id.* ¶ 9, Ex. 4 at p. 14. The website then promises that "all of its Seat purchasers' deposits are secure at all times. Profit Connect's financial reserves are significantly higher than all of its Seat purchasers' deposits combined." *Id.*

In addition to Profit Connect's website, B. Kovar personally solicits investors with similar false claims. In a 2019 YouTube video, still accessible to the public, B. Kovar states that Profit Connect Wealth Builder "uses AI for trading on the Forex exchange, as well as the crypto currency exchanges, and now we are just bringing online the AI being used on the New York Stock Exchange." *Id.* at ¶ 10, Ex. 5. B. Kovar goes on to explain that "there are no fees for this[.]" *Id.* He also states that because Profit Connect uses artificial intelligence to leverage investments, the investor "does not have to do anything … but enjoy life." *Id.* He repeatedly tells potential investors that Profit Connect does not charge any fees (unlike mutual funds or hedge funds) and investors can opt out of the investment and receive a return of their principal and interest at any time. *Id.* According to B. Kovar, Profit Connect makes returns similar to a bank, but instead of keeping all of the profits for itself, Profit Connect shares more of the high returns with investors because Profit Connect sees itself as a "disrupter" that plans to change the banking industry. *Id.*

D. Defendants' Misappropriation of Funds

Rather than invest the funds as promised, Defendants misused investor funds for their own personal use, to pay the promoters who lure investors to Profit Connect using social media platforms, and to repay investors in Ponzi-like payments. None of the money raised from investors has been used to invest in any securities, to engage in any forex, to conduct trading, or for any other investment purpose as represented by the Defendants. Zaldivar Decl. at ¶ 9(h), Ex. 10.

Upon investment, investors' funds are pooled together primarily in a single bank account. Zaldivar Decl. at ¶ 9(e), Ex. 8. Investor funds were then used as follows:

- Over $3 million of investor funds was used to make payments to various promoters who solicited investors in Profit Connect using their social media platforms. *Id.* at ¶ 9(h)(i), Ex. 10.
- Approximately $1 million went to other individuals associated with Profit Connect, including individuals who have been issued credit cards in the name of Profit Connect. *Id.* at ¶ 9(h)(ii), Ex. 10.
- As of April 12, 2021, J. Kovar had used at least $1.679 million of investor funds for her own use, including for credit card purchases, in-person cash withdrawals, and an automobile. *Id.* at ¶ 9(h)(iii), Ex. 10.
- Over $250,000 went to charges for photography, apparel and a charity related to B. Kovar. *Id.* at ¶ 9(h)(viii), Ex. 10.
- At least $440,000 was used to purchase and make improvements on a residential home in January 2021 which B. Kovar facilitated by signing the grant deed to purchase the home. *Id.* at ¶ 9(h)(vii), Exs. 9 and 10.
- At least $629,000 was used to repay previous investors. *Id.* at ¶ 9(h)(v), Ex. 10. For example, on July 15, 2018 a payment was made to an investor in the amount of $86,760. *Id.* at ¶ 9(h)(vi). At this time, the only source of funds available in the Profit Connect bank account were investor funds. *Id.* Similarly, in June 2019, Profit Connect received two wire transfers totaling $433,800, both of which referred to the purchase of a super computer seat. *Id.* at ¶ 9(j). Immediately after the receipt of these presumed investor funds, there were numerous transfers out of the Profit Connect bank account, including payments to individuals presumed to be investors. *Id.* At the time of these payments, the only source of cash in the Profit Connect bank account was investor funds.

Id.

- $1.6 million of investor funds went to make payments on a number of different credit cards, including a credit card in the name of Profit Connect, for which both J. Kovar and B. Kovar were authorized users. *Id.* at ¶ 9(h)(iv), Ex. 10. These credit card charges included almost $353,000 charged on the Profit Connect credit card assigned to B. Kovar for expenses related to restaurants, grocery stores, Amazon and Costco between June 9, 2020 and April 8, 2021. *Id.* at ¶ 22. On April 2, 2021 alone, for example, B. Kovar charged over $23,500 at Costco. *Id.* at ¶ 22.

E. Defendants' Fraud Is Ongoing

Defendants are both raising and dissipating investor assets very quickly and on an ongoing basis. For example, from April through May 31, 2021, Profit Connect raised at least $3,382,305. *Id.* at ¶ 10(a). From April 21, 2021 through June 9, 2021, J. Kovar has made ten transfers of at least $120,000 each from the Profit Connect bank account to her own personal bank account – for a total of more than $1.2 million in less than two months. *Id.* at ¶ 10(e)(iii). As of March 2021, Profit Connect had less than 20% of the total investor funds raised in its bank accounts and could not possibly return all investor funds. *Id.* at ¶ 9(g).

III. ARGUMENT

A. The SEC Is Seeking Emergency Relief in the Public Interest

Section 20(b) of the Securities Act and Section 21(d) of the Exchange Act authorize the SEC to obtain a preliminary injunction or restraining order without a bond. *See* 15 U.S.C. §§ 77t(b) & 78u(d). In the Ninth Circuit, preliminary injunctive relief is warranted if there is "either (1) a combination of probable success on the merits and the possibility of irreparable injury or (2) that serious questions are raised and the balance of hardships tips in the applicant's favor." *United States v. Nutri-Cology, Inc.*, 982 F.2d 394, 397 (9th Cir. 1992) (quotations and citations omitted).

District courts in the Ninth Circuit have interpreted the preliminary injunctive relief standard in SEC emergency actions to require that the SEC make only make a two-prong showing: (1) a prima facie case that the defendants have violated the federal securities laws, and (2) a reasonable likelihood that the defendants will repeat their violations. *See, e.g., SEC v. Blockvest, LLC*, No. 18CV2287-GPB(BLM), 2019 WL 625163, at *4 (S.D. Cal. Feb. 14, 2019); *SEC v. Sripetch*, No. 20-CV-01864-H-AGS, 2020 WL 6396927, at *3 (S.D. Cal. Nov. 2, 2020); *SEC v. Schooler*, 902 F. Supp. 2d 1341, 1345 (S.D. Cal. 2012); *SEC v. Eadgear, Inc.*, No. 3:14-CV-04294-RS, 2014 WL 6900938, at *1 (N.D. Cal. Dec. 8, 2014); *SEC v. Homestead Props., L.P.*, No. SACV09-01331-CJC (MLGx), 2009 WL 5173685, at *2 (C.D. Cal. Dec. 18, 2009); *SEC v. Trabulse*, 526 F. Supp. 2d 1008, 1012 (N.D. Cal. 2007); *SEC v. Cap. Cove Bancorp LLC*, No. SACV15980JLSJCX, 2015 WL 9704076, at *6 (C.D. Cal. Sept. 1, 2015).

The SEC appears before the Court "not as an ordinary litigant, but as a statutory guardian charged with safeguarding the public interest in enforcing the securities laws." *SEC v. Management Dynamics, Inc.*, 515 F.2d 801, 808 (2d Cir. 1975). Because this enforcement action is brought in the public interest, the Court's "equitable powers assume an even broader and more flexible character than when only a private controversy is at stake." *FSLIC v. Sahni*, 868 F.2d 1096, 1097 (9th Cir. 1989) (quoting *FTC v. H.N. Singer, Inc.*, 668 F.2d 1107, 1112 (9th Cir. 1982)); *SEC v. United Financial Group, Inc.*, 474 F.2d 354, 358 (9th Cir. 1973) (in SEC enforcement action, "[a] prima facie case of the probable existence of fraud … is sufficient to call into play the equitable powers of the court").

B. The SEC Has Made a *Prima Facie* Showing That Defendants Are Violating the Federal Securities Laws

1. Defendants are violating the antifraud provisions of Section 17(a), Section 10(b) and Rule 10b-5

J. Kovar, B. Kovar, and Profit Connect are violating the antifraud provisions of

the Securities Act and the Exchange Act.

Securities Act Section 17(a) makes it unlawful for any person, in the offer or sale of a security, directly or indirectly, (1) to employ any device, scheme, or artifice to defraud, (2) to obtain money or property by means of any false or misleading statement of material fact, or (3) to engage in any transaction, practice, or course of business which operates or would operate as a fraud or deceit upon the purchaser. Similarly, Exchange Act Section 10(b) and Rule 10b-5(a) makes it unlawful for any person, directly or indirectly, in connection with the purchase or sale of any security (1) to employ any device, scheme, or artifice to defraud, (2) to make any false or misleading statement of material fact, or (3) to engage in any act, practice, or course of business that operates or would operate as a fraud or deceit upon any person. Those who knowingly disseminate false statements can also be held liable under Exchange Act Rules 10b-5(a) and (c) and Securities Act Section 17(a)(1). *See Lorenzo v. SEC*, 139 S. Ct. 1094, 1100-1101 (2019). Defendants have violated both antifraud provisions.

a. Investments in the Profit Connect Wealth Builder accounts are securities

The Defendants are selling securities in the form of Profit Connect Wealth Builder accounts, which are securities under the federal securities laws.

Securities Act Section 2(a)(1) and Exchange Act Section 3(a)(10) of the Exchange Act define the term "security" to include "investment contracts." An investment contract involves (1) an investment of money, (2) in a common enterprise, (3) with an expectation of profits derived from the efforts of others. *SEC v. W.J. Howey Co*., 328 U.S. 293, 298-299 (1946). "This definition 'embodies a flexible rather than a static principle, one that is capable of adaptation to meet the countless and variable schemes devised by those who seek the use of the money of others on the promise of profits.'" *SEC v. Edwards*, 540 U.S. 389, 393 (2004) (quoting *Howey*, 328 U.S. at 299).

The Profit Connect Wealth Builder accounts offered by Profit Connect satisfy all three elements of the *Howey* test and, therefore, are "securities" under the Securities Act and the Exchange Act. First, investors deposited their money with Profit Connect. Second, the Profit Connect Wealth Builder accounts are a common enterprise. In the Ninth Circuit, the common enterprise element is satisfied by the existence of either horizontal commonality (a pooling of investor funds and interests) or strict vertical commonality (the fortunes of the investor are linked with those of the promoter). *SEC v. R.G. Reynolds Enter., Inc.*, 952 F.2d 1125, 1130 (9th Cir. 1991). Here, there is a common enterprise because both investors and Profit Connect were to make money through Profit Connect's investments (strict vertical commonality), Profit Connect pooled all investor funds, and Profit Connect used some of those funds to make payments to investors (horizontal commonality). Third, Profit Connect investors reasonably expected their profits to come from the Profit Connect supercomputer and AI software, because they were passive investors who relied entirely on Profit Connect and its proprietary and "disruptive technology" to generate returns on their money. Thus, the Profit Connect Wealth Builder accounts are securities under the federal securities laws.

2. Defendants engaged in a scheme to defraud

Defendants have engaged, and are continuing to engage, in a scheme to defraud Profit Connect's investors. Sections 17(a)(1) and 17(a)(3) of the Securities Act prohibit any person, "in the offer or sale of any securities," from employing "any device, scheme, or artifice to defraud," 15 U.S.C. § 77q(a)(1), or from engaging in "any transaction, practice, or course of business which operates, or would operate, as a fraud or deceit upon the purchaser." 15 U.S.C. § 77q(a)(3). Likewise, Section 10(b) of the Exchange Act and Rules 10b5(a) and (c) thereunder make it unlawful for any person, "in connection with the purchase or sale of any security," "[t]o employ any device, scheme or artifice to defraud," or "[t]o engage in any act, practice, or course of business which operates or would operate as a fraud or deceit upon any

person." 15 U.S.C. § 78j(b); 17 C.F.R. §§ 240.10b-5(a), (c). To be liable for a scheme to defraud, a defendant "must have engaged in conduct that had the principal purpose and effect of creating a false appearance of fact in furtherance of the scheme." *Simpson v. AOL Time Warner, Inc.*, 452 F.3d 1040, 1048 (9th Cir. 2006), vacated on other grounds sub nom., *Avis Budget Group Inc. v. Cal. State Teachers' Ret. System*, 552 U.S. 1162 (2008); *see also SEC v. Sells*, No. C-11-4941, 2012 WL 3242551, at *7 (N.D. Cal. Aug. 10, 2012).

Defendants are engaged in a course of business designed to defraud investors. From May 2018 onward, Defendants collected over $12 million from investors but did not use the proceeds to invest in any securities or investments as they represented. Instead, Defendants engaged in deceptive acts to convince investors that their funds were safe by falsely claiming that profits were deposited into a Profit Connect business account insured by the FDIC and NCUA and used the official logos of major banks, including Wells Fargo Bank, N.A. and Navy Federal Credit Union, to convince investors that Profit Connect had banking relationships with them. In reality, J. Kovar and Profit Connect never deposited money into any Wells Fargo accounts, because no such accounts existed, and the Navy Federal Credit Union account only ever had the initial $250 opening deposit. Zaldivar Decl. at ¶ 20.

Profit Connect's investment offerings also encouraged investors to keep their money with Profit Connect for long periods of time (*i.e.*, up to 18 years) and Profit Connect told investors on its website that it would provide them with monthly spreadsheets showing their profits. This conduct furthered the scheme and helped the Defendants avoid detection by encouraging investors to keep their money invested with Profit Connect for as long as possible and to invest additional funds. *SEC v. Wang*, 2015 U.S. Dist. LEXIS 192319, *48 (C.D. Cal., Aug. 18, 2015) (citing *United States v. Brown*, 578 F.2d 1280, 1285 (9th Cir. 1978) (finding that "activities tending to lull investors, either to prevent discovery of fraud or to permit further fraudulent activities to progress unhindered have been held to constitute a part of the execution

of the fraudulent scheme and to be integral to the offense rather than incidental to it.")

In addition, Profit Connect occasionally made payments to those few investors who sought a return of their funds, which created the false impression among investors that Profit Connect's purported investment profits were real. *See SEC v. Scoville*, 913 F.3d 1204, 1224 (10th Cir. 2019) ("[O]perating a Ponzi scheme…is 'inherently deceptive.'"); *Donell v. Kowell*, 533 F.3d 762, 777 (9th Cir. 2009) (Ponzi payments are deceptive acts made to create the appearance of a profitable business and to raise money from new investors). In reality, the Defendants were using these investor funds for their own personal use, to pay those promoters bringing in more investor funds, and to repay investors. *SEC v. Private Equity Management Group*, No. CV 09-2901 PSG, 2009 WL 2019788, *14 (C.D. Cal. Jul. 2, 2009) (misappropriation of investor money is a scheme to defraud).

3. Defendants' materially false statements and omissions

To establish a *prima facie* case that a person made false or misleading statements in connection with the offer, purchase, or sale of securities under Section 17(a) of the Securities Act, Section 10(b) of the Exchange Act, and Exchange Act Rule 10b-5, the SEC must prove by a preponderance of the evidence four basic elements: (1) a material misrepresentation or omission; (2) in connection with the offer, purchase, or sale of a security; (3) with scienter; and (4) in interstate commerce. *SEC v. Platforms Wireless*, 617 F.3d 1072, 1092 (9th Cir. 2010); *see also SEC v. Rana Research, Inc.*, 8 F.3d 1358, 1364 (9th Cir. 1993).

Violations of the antifraud provisions require that the misstatements and omissions concern material facts. *Basic Inc. v. Levinson*, 485 U.S. 224, 231-32 (1988); *TSC Indus., Inc. v. Northway, Inc.*, 426 U.S. 438, 449 (1976). A fact is material if there is a substantial likelihood that a reasonable investor would consider it important in making an investment decision. *See TSC Indus.*, 426 U.S. at 449; *Platforms Wireless*, 617 F.2d at 1092. Liability arises not only from affirmative representations but also from failures to disclose material information. *SEC v. Dain*

Rauscher, Inc., 254 F.3d at 855-56. The antifraud provisions impose "'a duty to disclose material facts that are necessary to make disclosed statements, whether mandatory or volunteered, not misleading.'" *SEC v. Fehn*, 97 F.3d 1276, 1290 n.12 (9th Cir. 1996) (*quoting Hanon v. Dataproducts Corp.*, 976 F.2d 497, 504 (9th Cir. 1992)). *See also SEC v. Murphy*, 626 F.2d at 653 (profitability of an issuer was material to investors).

The misstatements and omissions were material to investors in Profit Connect because they go to the heart of the investment – how the funds are used, whether the funds really are secure and whether the purported guaranteed profits really exist. Any reasonable investor would consider it important to know that his or her money was not used as represented, but instead used to pay other investors and the personal expenses of J. Kovar and her son, recidivist B. Kovar. *See SEC v. Chemical Trust*, 2000 U.S. Dist. Lexis 19786 (S.D. Fla. 2000) (use or misuse of investor proceeds is material).

These misstatements were "in the offer or sale" of securities under Section 17(a)(2) of the Securities Act and "in connection with" the purchase and sale of securities under Section 10(b) and Rule l0b-5 thereunder. Defendants' misstatements and omissions were made to investors at the time Profit Connect was offering and selling its Wealth Builder accounts and when investors were deciding whether to invest with Profit Connect.

4. Defendants are the makers of the false statements

Defendants are "makers" of these false and misleading statements under Exchange Act Rule 10b-5(b). *See Janus Capital Group, Inc. v. First Derivative Traders*, 564 U.S. 135, 142 (2011) ("the maker of a statement is the person or entity with ultimate authority over the statement, including its content and whether and how to communicate it"). B. Kovar made multiple misstatements in promoting Profit Connect on a YouTube video in early 2019 that is currently still accessible to the public. The false and misleading statements are on Profit Connect's website. *See*

Blank v. Tripoint Global Equities, LLC, 338 F. Supp. 3d 194, 213 (S.D.N.Y. 2018) ("TriPoint Capital and TriPoint Global clearly can be liable for statements 'made' on their own corporate websites."). J. Kovar is also a maker of the statements because, as Profit Connect's founder, president and treasurer and as someone who controls its bank accounts, she has ultimate authority over the substance of the representations and how they are communicated. *Janus*, 564 U.S. at 144.

5. Defendants obtained money

For purposes of Securities Act Section 17(a)(2), Defendants obtained money by means of the fraudulent statements because investors paid money for the Profit Connect Wealth Builder accounts into an account held by Profit Connect, to which J. Kovar and B. Kovar were signatories, and which J. Kovar controlled. J. Kovar and B. Kovar also "obtained" these funds by misappropriating money received from investors and using them to pay personal expenses.

6. Defendants are acting with scienter

Exchange Act Section 10(b) and Securities Act Section 17(a)(1) require a showing of scienter, while claims under Securities Act Sections 17(a)(2) and 17(a)(3) only require a showing of negligence. *Aaron v. SEC*, 446 U.S. 680, 701-02 (1980). Scienter is a "mental state embracing intent to deceive, manipulate, or defraud." *Ernst & Ernst v. Hochfelder*, 425 U.S. 185, 193 n.12 (1976). Scienter can be established by showing "knowing or reckless conduct." *Vernazza v. SEC*, 327 F.3d 851, 860 (9th Cir. 2003). As for negligence, it may be proven by showing that a defendant failed to conform to the standard of care that would be exercised by a reasonable person. *See SEC v. Dain Rauscher, Inc.*, 254 F.3d 852, 856 (9th Cir. 2001).

Defendants acted with a high degree of scienter. As the only person with signatory authority over the Profit Connect bank accounts until very recently and control over investor funds, J. Kovar knew, or was reckless in not knowing, that investor funds were being used to pay for her own personal expenses and not in accordance with the representations made to investors on the Profit Connect website.

See, e.g., Lowry v. SEC, 340 F.3d 501, 505 (8th Cir. 2003) (the fact that a principal spends investor funds on personal expenses establishes the requisite state of mind for committing securities fraud). Additionally, J. Kovar regularly signed withdrawal slips in order to withdraw cash at the bank from the Profit Connect bank accounts. B. Kovar claimed to investors that their funds would be used for various investments, would generate guaranteed returns of up to 20% and could be withdrawn at any time. As the sole director of Profit Connect, son of J. Kovar, and someone who promoted the company to investors on social media, B. Kovar knew, or was reckless in not knowing, that all of these representations were false. Despite knowing that investor funds had not been used to conduct trading or for venture capital projects and knowing that Profit Connect had not earned any profits, Profit Connect nevertheless continued to solicit and accept new investments and repaid investors using other money from investors. The scienter of J. Kovar and B. Kovar is imputed to Profit Connect because the scienter of an entity's management can be imputed to the entity. *See ChinaCast Educ. Corp. Sec. Litig.*, 809 F.3d 471, 477 (9th Cir. 2015); *SEC v. Manor Nursing Ctrs., Inc.*, 458 F.2d 1082, 1089 n.3 (2d Cir. 1972).

7. Defendants are also negligent

To establish negligence, the SEC must show that the defendants failed to conform to the standard of care that would be exercised by a reasonable person. *See Dain Rauscher*, 254 F.3d at 856; *SEC v. Hughes Capital Corp.*, 124 F.3d 449, 453-54 (3d Cir.1997) (defining negligence in the securities context as the failure to exercise reasonable care or competence). Here, Defendants' raising money by lying about how the funds would be used, fabricating relationships with banks, and making Ponzi payments, falls below the standard of care of any reasonable person in the securities industry.

8. Defendants engaged in fraud in connection with the purchase and sale and in the offer and sale of securities

Defendants' activities were clearly "in the offer or sale," and "in connection

with the purchase or sale" of securities and in interstate commerce. *See SEC v. Zandford*, 535 U.S. 813, 822 (2002) (fraud that "coincide[s]" with the securities transactions satisfies the "in connection with" requirement); *United States v. Naftalin*, 441 U.S. 768, 777-78 (1979) ("in the offer or sale" is broad enough to cover the entire selling process). The phrase "in connection with the purchase or sale" of a security is met when the fraud alleged "coincides with a securities transaction." *Merrill Lynch, Pierce, Fenner & Smith Inc., v. Dabit*, 547 U.S. 71, 85 (2006). Moreover, "in connection with" requires only that there be "deceptive practices touching" the purchase or sale of securities. *See Superintendent of Ins. v. Bankers Life & Casualty Co*., 404 U.S. 6, 12-13 (1971); *see also SEC v. Zandford*, 535 U.S. 813, 819 (2002). Here, Defendants made false statements and engaged in deceptive conduct to induce investors to deposit their money into a Profit Connect Wealth Builder account to be invested. The fraud therefore coincides with, and took place in, the offer and sale, and in connection with the purchase and sale, of securities. *See Lorenzo*, 139 S. Ct. at 1101-02 (knowing dissemination of misrepresentations with an intent to deceive violates Rules 10b-5(a) and (c) and Section 17(a)(1)); *see also Malouf*, 933 F.3d at 1260 (applying *Lorenzo* to Section 17(a)(3) because it "is virtually identical to Rule 10b-5(c)").

9. Defendants are using interstate commerce

Defendants' activities clearly occurred in interstate commerce, by soliciting via a website and through B. Kovar's YouTube videos among other social media methods of solicitation. *United States v. Hornaday*, 392 F.3d 1306, 1311 (11th Cir. 2004) (The internet is an instrumentality of interstate commerce, as is the telephone); *see also Utah Lighthouse Ministry v. Foundation for Apologetic Info. & Research*, 527 F.3d 1045, 1054 (10th Cir. 2008) ("We agree that the Internet is generally an instrumentality of interstate commerce.")

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C. J. Kovar Is Liable in the Alternative for Violations of the Exchange Act as a Control Person

In addition, J. Kovar is also liable for violations of the Exchange Act as a control person of Profit Connect. Under Exchange Act Section 20(a), a person may be held liable for another person's violation of the Exchange Act as a control person. To state a prima facie case of control person liability, the Commission must establish: "(1) a primary violation of the securities laws and (2) 'control' over the primary violator by the alleged controlling person." *Adams v. Kinder-Morgan, Inc.*, 340 F.3d 1083, 1107 (10th Cir. 2003); *see also SEC v. Todd*, 642 F.3d 1207, 1223 (9th Cir. 2011). Exchange Act Rule 12b-2 defines "control" as "the possession, direct or indirect, of the power to direct or cause the direction of the management and policies of a person, whether through the ownership of voting securities, by contract, or otherwise." If a plaintiff satisfies the prima facie burden, the burden shifts to the defendant to show that he or she "acted in good faith and did not directly or indirectly induce the act or acts constituting the violation or cause of action." 15 U.S.C. § 78t(a).

J. Kovar holds herself out as the founder, president and treasurer of Profit Connect and has sole signatory authority over its bank accounts. As such, J. Kovar controlled the actions of Profit Connect since its inception. *See, e.g., New Jersey v. Sprint Corp.*, 314 F. Supp. 2d 1119, 1143 (D. Kan. 2006) ("Clearly, [a CEO] would not be entitled to dismissal of the control person liability claims."). Therefore, in the alternative, Kovar is liable as a control person for Profit Connect's violations of Section 10(b) of the Exchange Act and Rule 10b-5 thereunder.

D. The SEC Has Shown the Violations Are Likely to Be Repeated

In addition to making a *prima facie* showing of Defendants' securities laws violations, the SEC has demonstrated a likelihood that Defendants' violations will be repeated. Whether a likelihood of future violations exists depends upon the totality of the circumstances. *See SEC v. Murphy*, 626 F.2d 633, 655 (9th Cir. 1980); *Fehn*, 97 F.3d at 1295-96. The existence of past violations may give rise to an inference

that there will be future violations. *See Murphy*, 626 F.2d at 655; *SEC v. United Financial Group, Inc.*, 474 F.2d 354, 358-59 (9th Cir. 1973); *see also Odessa Union Warehouse Co-Op*, 833 F.2d at 176. Courts also consider factors such as the degree of scienter involved, the isolated or recurrent nature of the violative conduct, the defendant's recognition of the wrongful nature of the conduct, the likelihood that, because of the defendant's occupation, future violations may occur, and the sincerity of a defendant's assurances (if any) against future violations. *See Murph*y, 626 F.2d at 655.

Here, Defendants' fraud is ongoing since May 2018, with funds being raised and misappropriated through at least the end of May 2021. B. Kovar is a securities fraud recidivist, having been charged by the SEC in 2009 in a pump and dump penny stock scheme. Nonetheless, B. Kovar has continued to publicly solicit investors in Profit Connect. Thus, there can be no question that a temporary restraining order is necessary to protect investors from Defendants' fraudulent conduct.

E. The Other Relief Sought by the SEC Is Needed

In addition to a restraining order, the SEC also seeks an asset freeze over Defendants' assets, an accounting, appointment of a temporary receiver, and expedited discovery. Federal courts have "inherent equitable power to issue provisional remedies ancillary to its authority to provide final equitable relief." *Reebok Int'l, Ltd v. Marnatech Enterprises, Inc.*, 970 F.2d 552, 559 (9th Cir. 1992); SEC v. Wencke, 622 F.2d 1363, 1369 (9th Cir. 1980). "[O]nce the equity jurisdiction of the district court properly has been invoked, the court has power to order all equitable relief necessary under the circumstances." *SEC v. Materia*, 745 F.2d 197, 200 (2d Cir. 1984).

1. The Court should freeze the Defendants' assets

The Court's equitable powers include the authority to freeze assets of both parties and nonparties. *See SEC v. Hickey*, 322 F.3d 1123, 1131 (9th Cir. 2003); *SEC v. Int'l Swiss Invest. Corp.*, 895 F.2d 1272, 1276 (9th Cir. 1990). The purpose of a

freeze order is to prevent the dissipation of assets so that they may be available to be paid as disgorgement for the benefit of victims of the fraud. *See*, *e.g.*, *Hickey*, 322 F.3d at 1132 (affirming asset freeze over nonparty brokerage firm controlled by defendant to effectuate disgorgement order against defendant); *SEC v. Manor Nursing Ctrs., Inc.*, 458 F.2d 1082, 1105-06 (2d Cir. 1972). The Ninth Circuit has found that "the public interest in preserving the illicit proceeds [of a defendant's fraud] for restitution to the victims is great." *FTC v. Affordable Media, LLC*, 179 F.3d 1228, 1236 (9th Cir. 1999). Courts have recognized that a disgorgement order will often be rendered meaningless unless an asset freeze is imposed prior to the entry of final judgment. *See SEC v. Unifund SAL*, 910 F.2d 1028, 1041 (2d Cir. 1990).

"A party seeking an asset freeze must show a likelihood of dissipation of the claimed assets, or other inability to recover monetary damages if relief is not granted." *Johnson v. Couturier*, 572 F.3d 1067, 1085 (9th Cir. 2009). Courts consider a defendant's prior unlawful acts and the location of the assets in considering whether an asset freeze is warranted. *See*, *e.g.*, *id*. at 1085; *Affordable Media*, 179 F.3d at 1236 ("district court's finding regarding the likelihood of dissipation is far from clearly erroneous" where defendant had a "history of spiriting their commissions away to a Cook Islands trust"); *Manor Nursing*, 458 F.2d at 1106 ("uncertainty existed with respect to the total amount of proceeds received and their location," thus asset freeze was warranted).

Here, Defendants have raised over $12 million, but only have $3,504,541.38 in in the Profit Connect accounts at Bank of America as of May 31, 2021. Zaldivar Decl. at ¶¶ 10(d), 11(c), 12(d), 14, 16. An asset freeze is necessary to preserve any remaining assets. Moreover, because of the emergency nature of this action, the SEC has not located the all of the possible assets and accounts under Defendants' control. A freeze over all of Defendants' accounts is necessary to prevent them from further dissipating the investor funds.

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2. The Court should order accountings, document preservation and expedited discovery

The Court's broad equitable powers in SEC enforcement actions include the ability to order ancillary relief to require an accounting and prohibit document destruction. *See Wencke*, 622 F.2d at 1369. The Court should enter an order prohibiting the destruction of documents to prevent Defendants from destroying evidence of their violations and ongoing fraud. The Court should also allow the SEC to obtain discovery on an expedited basis. Expedited discovery is authorized by Rules 30 and 34 of the Federal Rules of Civil Procedure and a court's broad equitable powers in SEC enforcement actions to order all necessary ancillary relief. *See Wencke*, 622 F.2d at 1369. The Court should also require Defendants to prepare accountings, so the SEC can identify all available assets to help ensure that funds and assets are frozen properly and available to satisfy any future order of disgorgement or civil penalties against them. *See Int'l Swiss Invs. Corp*., 895 F.2d at 1276.

3. A receiver is necessary to protect the assets

The SEC seeks the appointment of a temporary receiver over Profit Connect. The Court has broad discretion to appoint an equity receiver in SEC enforcement actions. *See Wencke*, 622 F.2d at 1365. The breadth of this discretion "arises out of the fact that most receiverships involve multiple parties and complex transactions." *SEC v. Capital Consultants, LLC*, 397 F.3d 733, 738 (9th Cir. 2005) (quotation omitted). A receiver plays a crucial role in preventing further dissipation and misappropriation of investors' assets. *Wencke*, 783 F.2d at 836-37 n.9. Factors such as the integrity of management and the likelihood of future misuse of assets are critical in determining whether a receiver should be appointed. *See SEC v. Fifth Ave. Coach Lines, Inc.*, 289 F. Supp. 3, 42 (S.D.N.Y. 1968), *aff'd*, 435 F.2d 510 (2d Cir. 1970).

This case involves a classic offering fraud being perpetrated, at least in part, by an individual with a recidivist history. Defendant B. Kovar has a demonstrated lack of any integrity and should not be trusted with investor funds or assets. A receiver

can rationalize the investors' interests, manage a claims process, and assist the Court to make sure assets are distributed fairly to legitimate claimants, under the supervision and direction of the Court. The SEC also requests that the receiver be excused from posting a bond. *See SEC v. Universal Financial*, 760 F.2d 1034, 1039 (9th Cir. 1985).

IV. CONCLUSION

For the foregoing reasons, the SEC respectfully asks the Court to grant the SEC's Motion and enter the proposed Temporary Restraining Order and other requested relief.

Dated: July 8, 2021

/s/ Kathryn C. Wanner

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