

UNITED STATES DISTRICT COURT  
FOR THE SOUTHERN DISTRICT OF NEW YORK

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SECURITIES AND EXCHANGE COMMISSION,

PLAINTIFF,

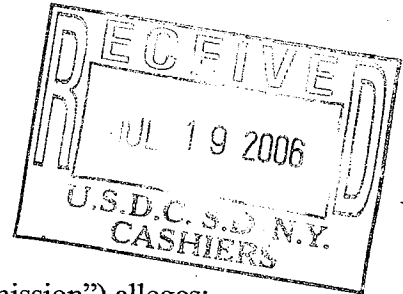
v.

STEVEN B. MISNER,

DEFENDANT.

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JUDGE KARAS  
06 CV 5465  
Civil Action No.:



COMPLAINT

Plaintiff, Securities and Exchange Commission (the "Commission") alleges:

NATURE OF THE ACTION

1. From at least July 2002 through November 2002, Defendant Steven B. Misner, the former CEO of Southwestern Water Exploration Co. ("Southwestern"), made materially false and misleading statements in two press releases, which were also posted on Southwestern's website. Southwestern's July 16, 2002 and November 4, 2002 press releases claimed that Southwestern owned rights to, and was developing, a large freshwater underground reservoir worth hundreds of millions of dollars. In fact, Misner knew, or was reckless in not knowing, that Southwestern did not own any rights to the water. Misner also knew, or was reckless in not knowing, that the press releases grossly overstated the value and amount of water in the aquifer. Furthermore, Misner knew, or was reckless in not knowing, that Southwestern had made no effort to develop the infrastructure needed to extract the water and transport it to potential end users, and Misner had no intention of developing the reservoir. By creating the false impression

that Southwestern owned water of great value, Misner engaged in a scheme to inflate Southwestern's stock price.

2. By engaging in this conduct, Misner committed securities fraud in violation of Section 10(b) of the Securities Exchange Act of 1934 (the "Exchange Act") [15 U.S.C. § 78j(b)] and Exchange Act Rule 10b-5 [17 C.F.R. § 240.10b-5].

3. Unless permanently enjoined, Misner is likely to engage in similar conduct and commit similar violations of the federal securities laws in the future.

### **JURISDICTION AND VENUE**

4. This Court possesses jurisdiction over this action pursuant to Sections 21(d) and 27 of the Exchange Act [15 U.S.C. §§ 78u(d) and 78aa].

5. Certain of the acts, practices, and courses of conduct constituting the violations of law alleged in the Complaint occurred within this judicial district. For example, Southwestern distributed the false and misleading press releases through the New York office of Business Wire. In addition, investors located in New York purchased shares of Southwestern stock in the days following the July and November 2002 press releases. Venue is thus proper under Section 27 of the Exchange Act [15 U.S.C. § 78aa].

6. Misner, directly or indirectly, has made use of the means or instrumentalities of interstate commerce, or of the mails, in connection with the acts, practices, and courses of business alleged herein.

### **DEFENDANT**

7. Steven B. Misner, age 46, is a Canadian citizen residing in Nevada. Misner founded Southwestern in 1993 with his ex-wife. Misner was Southwestern's

president from October 1993 through October 2001, and CEO from October 2001 until December 16, 2002. Misner also served as a director of Southwestern from 1993 until December 16, 2002. As of December 2002, Misner owned about 2,961,757 shares of Southwestern stock.

8. In December 2002, Misner and his ex-wife resigned as officers and directors of Southwestern after Southwestern's board learned that Misner had been criminally charged with tax evasion and his ex-wife had been criminally convicted of tax evasion in Canada as directors of American Institute of Formation Evaluation, Ltd. ("AIFE Ltd."), a Canadian corporation.

#### **RELEVANT ENTITY**

9. Southwestern, d/b/a Aqua4, Inc., a Colorado corporation, purported to engage in exploring and producing drinkable water from deep aquifers in the American Southwest. Southwestern filed for protection under Chapter 7 of the Bankruptcy Code on November 20, 2003. On May 4, 2006, the bankruptcy court authorized the bankruptcy trustee to sell all of Southwestern's assets to Paragon Water Development Corp., an entity controlled by Misner.

10. In August 2000, the appropriate regulatory authorities delisted Southwestern's stock from the OTC Bulletin Board for failing to meet the listing requirements. Southwestern filed its most recent periodic report with the Commission on November 14, 2002. It stated that Southwestern had 23,600,012 shares of common stock outstanding. From the date of the first false and misleading press release in July 2002 to the date of Misner's resignation in December 2002, Southwestern's common stock was listed for quotation in the Pink Sheets and traded between about \$0.70 and \$1.50.

Southwestern's common stock is still listed for quotation in the Pink Sheets and currently trades at about \$0.01. During all relevant times, Southwestern's stock was a "penny stock" as defined by Section 3(a)(51)(A) of the Exchange Act [15 U.S.C. § 78c(a)(51)(A)].

## **RELEVANT FACTS**

### **Background**

11. Misner founded Southwestern in 1993. He used a public shell company named Star Acquisitions Corporation to acquire American Institute of Formation Evaluation Co. ("AIFE Co.") as a wholly-owned subsidiary, and then changed the name of the public company to Southwestern. Until about 2001, Southwestern was located in Calgary, Alberta Canada and shared office space with AIFE Ltd., another entity Misner controlled.

12. From its inception, Southwestern was unprofitable, had limited operations, and funded its activities primarily by issuing stock through private placements. In March 2002, Southwestern drilled its first and only well, a monitoring hole, at an aquifer in northern Colorado. The purpose of the monitoring hole was to test the depth, quality, and other aspects of the water. According to rules of the Office of the State Engineer for Colorado, Southwestern could not convert its monitoring hole into a production well for water. Southwestern never developed any means to pump the water out of the ground or transport the water to potential end users.

13. From about 2001 until his resignation in December 2002, Misner ran Southwestern out of his home in Las Vegas, Nevada. Misner's responsibilities included raising capital for Southwestern, attending meetings with potential water brokers,

meeting with consulting engineers and the Colorado water regulatory agency, and spending time at Southwestern's one well site in Colorado. Misner also was primarily responsible for communications between the company and its investors.

14. On July 16, 2002, Southwestern issued a press release entitled, "Southwestern Water Announces Reserves of Drinking Water for Colorado Project" ("July Press Release"). Misner was primarily responsible for the content of, participated in drafting, and reviewed Southwestern's July Press Release, and his name appeared on the release as a contact for Southwestern.

15. On November 4, 2002, Southwestern issued a press release entitled, "Southwestern Water Makes Further Progress in Development of Significant Fresh Water Discovery in Colorado" ("November Press Release"). Misner was primarily responsible for the content of, participated in drafting, and reviewed Southwestern's November Press Release, and his name appeared on the release as a contact for Southwestern. Misner personally e-mailed the November Press Release to several investors.

16. The July and November Press Releases were posted on Southwestern's website until at least November 19, 2002. Misner knew that Southwestern's press releases were posted on its website.

#### **Materially False and Misleading Statements in Press Releases**

17. Misner knew, or was reckless in not knowing, that statements in the July and November Press Releases regarding Southwestern's ownership of rights to water in the aquifer, and the value and amount of water for sale in the aquifer were materially false and misleading. Misner also knew, or was reckless in not knowing, that statements

in the November Press Release that Southwestern had made progress in developing a freshwater underground reservoir in Colorado were materially false and misleading.

**Materially False and Misleading Statements Regarding Southwestern's Ownership of Rights to Water in an Underground Reservoir**

18. The July and November Press Releases contained materially false and misleading statements regarding Southwestern's ownership of rights to water in an underground reservoir.

19. The July Press Release stated: “[f]inal engineering reports state *the available water for sale* is a minimum of 129,000 acre-feet and could exceed 300,000 acre-feet” (emphasis added).

20. The November Press Release stated: “the *Southwestern Water reservoir* contains at least 300,000 acre-feet of water . . . [and] the *Southwestern Water reservoir* will last for a minimum of 100 years” (emphasis added). The November Press Release also stated that Southwestern had “retained the services of . . . water brokers *to sell the production* on an annualized basis” (emphasis added).

21. At the time Southwestern issued the press releases, Misner knew, or was reckless in not knowing, that Southwestern did not own any rights to the water or the reservoir. Thus, the reservoir was not Southwestern's and Southwestern had no water for sale. Misner knew, or was reckless in not knowing, that the water was “tributary,” which means that it was connected to a natural stream system either by surface or underground flows. Misner also knew, or was reckless in not knowing, that Southwestern had not taken effective steps to acquire rights to the water. Misner knew, for example, that Southwestern had not put the water to beneficial use and had not obtained a purchaser for the water or a decree in state water court.

**Materially False and Misleading Statements Regarding the  
Value of the Water in the Aquifer**

22. The July and November Press Releases contained materially false and misleading statements regarding the value of the water in the underground reservoir in Colorado.

23. Southwestern's July Press Release stated "recent pricing for water in the area has ranged from \$10,700 per acre-foot . . . [to] \$14,200 per acre-foot." However, the July Press Release failed to disclose that these prices were for sales of Colorado-Big Thompson ("CBT") water, not ground water like the water in Southwestern's purported aquifer, which would sell for much less than CBT water.

24. By the time of the July Press Release, Southwestern's consulting engineer had advised Misner that the water in the aquifer would sell for much less than the publicly announced prices.

25. Southwestern's November Press Release stated "[t]he price of water in this region of Colorado is currently averaging \$15,500 per acre-foot for Colorado Big Thompson (CBT) delivery."

26. By the time of the November press release, a local water broker, among others, had told Misner that the ground water in the aquifer would sell for much less than CBT water.

27. In addition, prior to issuing both press releases, Misner knew, or was reckless in not knowing, that there was no real economic value to the water because estimated development costs were so high.

**Materially False and Misleading Statements Regarding the  
Amount of Water for Sale in the Aquifer**

28. The July and November Press Releases contained materially false and misleading statements regarding the amount of water for sale in the underground reservoir in Colorado.

29. Southwestern's July Press Release stated "Final engineering reports state the available water for sale is a minimum of 129,000 acre-feet and could exceed 300,000 acre-feet dependent on which reservoir development scenario is undertaken."

30. In reality, the development scenarios in the engineering reports only allowed for the extraction of between 1,290 and 4,388 acre-feet of water in any given year, so that it would take about 30 to 100 years to extract 129,000 or more acre-feet of water from the aquifer.

31. Misner knew, or was reckless in not knowing, that the amount of water for sale was overstated in the July Press Release. For example, a few weeks before the July Press Release was issued, Southwestern's consulting engineer had cautioned Misner, "[B]e conservative about the annual water quantity you can realistically supply, say 2,900 acre-feet per year on a sustained (20- to 30-year) basis . . . Over thirty years this would be about 87,000 acre-feet."

32. Southwestern's November Press Release stated that "The reservoir can produce . . . 3,000 to 6,000 acre feet of water per year . . . . At this rate of production, the Southwestern Water reservoir will last for a minimum of 100 years." The November Press Release thereby suggested that over one hundred years, Southwestern could produce 300,000 acre-feet of water (representing 3,000 acre-feet of water per year x 100



years) to 600,000 acre-feet of water (representing 6,000 acre-feet of water per year x 100 years) from the reservoir.

33. Misner knew, or was reckless in not knowing, that the amount of water the reservoir could produce was a fraction of what was stated. For instance, by the time of the November Press Release, Southwestern's consulting engineer had informed Misner that extracting more than 129,000 acre-feet (at a rate of about 3,000 acre-feet of water per year) would damage the reservoir. Misner also had been informed that if Southwestern obtained rights to the water, for all practical purposes, it could only expect to sell the amount of water produced in one year (about 3,000 acre-feet of water), not the 300,000 to 600,000 acre-feet of water suggested by the November Press Release.

**Materially False and Misleading Statements that Southwestern Had Made Progress in Developing a Freshwater Underground Reservoir in Colorado**

34. The November Press Release contained materially false and misleading statements that Southwestern had made progress in developing a freshwater underground reservoir in Colorado.

35. The November Press Release stated "Southwestern Water Makes Further Progress in Development of Significant Fresh Water Discovery in Colorado" and Southwestern "has reached the next advanced level in bringing into service the large fresh water reservoir it discovered deep underground in Colorado." The press release also stated that "Southwestern Water, to bring this reservoir more rapidly into production, has now retained the services of independent water appraisers and water brokers . . . ."

36. As of the date of the press release, Misner knew, or was reckless in not knowing that Southwestern not only did not own any rights to the water in the aquifer, but also that Southwestern had never developed any means to pump the water out of the

ground or to transport it to potential end users. For example, Misner knew that the only well Southwestern ever drilled was a monitoring hole in March 2002, which Southwestern could not convert into a production well.

37. In fact, Misner's plan was not to develop the aquifer or bring the reservoir into production. Misner knew, among other things, that Southwestern did not have the resources to develop the aquifer.

#### **Misner Engaged in a Scheme to Mislead Investors**

38. Misner engaged in a scheme to mislead investors in order to inflate and/or maintain Southwestern's stock price.

39. Misner's false and misleading statements about Southwestern's ownership of rights to the water in the reservoir, the amount and value of the water, and Southwestern's development of the reservoir, created the illusion that Southwestern owned, and was developing, water of great value. In fact, as Misner knew or was reckless in not knowing, Southwestern had no ownership interest in the water, the water was virtually worthless, and Southwestern had not taken, and did not intend to take, any steps to develop the reservoir.

40. Misner intentionally kept the truth from investors to maximize the stock price and to encourage investment in the company. On November 1, 2002, just three days before the November Press Release, Misner sent an e-mail to two Southwestern employees. Misner wrote:

If this project blows up in our face which it may for many political and legal reasons including the tributary/non-tributary status, opposition from the public and the inability of [the water broker] to finalize a sales contract we, the company, need to ensure that we have taken every step possible to both maximize the return to the company and limit our liability. . . . [R]emember that everyone, including

[our large investor] and the majority of our shareholders, think that we have at least 100 million of water for sale which is not the case . . . .

41. Southwestern's stock price increased \$0.10 in the day following both the July and November Press Releases, an increase of 7% and 11%, respectively.

42. Misner stood to benefit from Southwestern's inflated stock price. For example, Misner owned a substantial amount of Southwestern stock. In addition, Misner received money from Southwestern, whose funding depended on Misner's effort to make private placements of its stock.

**Misner Profited from the Fraud**

43. Misner profited from his fraudulent conduct by receiving money from Southwestern from at least July 2002 through December 2002.

**FIRST CLAIM FOR RELIEF**

**Violations of Section 10(b) of the Exchange Act [15 U.S.C. § 78j(b)]  
and Exchange Act Rule 10b-5 [17 C.F.R. § 240.10b-5]**

44. The Commission realleges and incorporates by reference all preceding paragraphs.

45. From July 2002 through at least November 2002, Defendant Misner, with scienter, directly or indirectly, by use of the means or instrumentalities of interstate commerce or of the mails, in connection with the purchase or sale of securities, as described in this Complaint, has: (a) employed devices, schemes, or artifices to defraud; (b) made untrue statements of material facts or omitted to state material facts necessary in order to make the statements made, in light of the circumstances under which they were made, not misleading; or (c) engaged in acts, practices, or courses of business which operated or would operate as a fraud or deceit upon any person.

46. By reason of the activities described above, Defendant Misner violated Section 10(b) of the Exchange Act [15 U.S.C. § 78j(b)] and Exchange Act Rule 10b-5 [17 C.F.R. § 240.10b-5].

**PRAYER FOR RELIEF**

WHEREFORE, the Commission respectfully requests that this Court enter a judgment that:

- (i) Permanently enjoins Defendant Misner from violating, directly or indirectly, Section 10(b) of the Exchange Act [15 U.S.C. § 78j(b)] and Exchange Act Rule 10b-5 [17 C.F.R. § 240.10b-5];
- (ii) Orders Defendant Misner to prepare a sworn accounting of the purpose, disposition, and present location of all the money he obtained from Southwestern during the period January 1, 2002 through December 31, 2002;
- (iii) Orders Defendant Misner to disgorge all profits or proceeds that he has received as a result of his conduct as described in this Complaint, plus prejudgment interest;
- (iv) Orders Defendant Misner to pay an appropriate civil money penalty pursuant to Section 21(d)(3) of the Exchange Act [15 U.S.C. § 78u(d)(3)];
- (v) Permanently bars Defendant Misner from any future participation in the offering of any penny stock as defined by Section 3(a)(51)(A) of the Exchange Act [15 U.S.C. § 78c(a)(51)(A)], pursuant to Section 21(d)(6) of the Exchange Act [15 U.S.C. § 78u(d)(6)] and the Court's equitable powers;
- (vi) Permanently bars Defendant Misner from acting as an officer or director of any public company pursuant to Section 21(d)(2) of the Exchange Act;

(vii) Grants such other relief as this Court may deem just and appropriate; and

(viii) Retains jurisdiction of this action in accordance with the principles of equity and the Federal Rules of Civil Procedure in order to implement and carry out the terms of all orders and decrees or to entertain any suitable application or motion for additional relief within the jurisdiction of this Court.

Respectfully submitted,

By: 

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