MARC J. FAGEL (Cal. Bar. No. 154425)
ROBERT L. MITCHELL (Cal. Bar No. 161354)
mitchellr@sec.gov
ROBERT S. LEACH (Cal. Bar No. 196191)
leachr@sec.gov
SUSAN FLEISCHMANN (Cal. Bar No. 207194)
fleischmanns@sec.gov

Attorneys for Plaintiff
SECURITIES AND EXCHANGE COMMISSION
44 Montgomery Street, Suite 2600
San Francisco, California 94104
Telephone: (415) 705-2500
Facsimile: (415) 705-2501



BZ

**UNITED STATES DISTRICT COURT**

**NORTHERN DISTRICT OF CALIFORNIA**

**SAN FRANCISCO DIVISION**

CV 09 2302

| | |
|---|---|
| SECURITIES AND EXCHANGE COMMISSION,<br>Plaintiff,<br>vs.<br>PEGASUS WIRELESS CORPORATION, JASPER KNABB, and STEPHEN DURLAND,<br>Defendants,<br>and<br>AERO-MARINE, LLC and TAMMY KNABB,<br>Relief Defendants. | No. ________<br><br>**COMPLAINT** |

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

**SUMMARY OF THE ACTION**

1. This matter involves a securities fraud scheme by officers of Pegasus Wireless Corp., a once high-flying technology company that was based in Fremont, California.

2. After creating Pegasus from a dormant shell company, president Jasper Knabb and CFO Stephen Durland touted a series of significant acquisitions that caused Pegasus' stock price to

rise precipitously, briefly giving this once unheralded penny stock a market capitalization of more than $1.4 billion. Unbeknown to investors, however, Knabb and Durland secretly controlled hundreds of millions of Pegasus shares, which they dumped on individual investors and the open market throughout 2006 and 2008, as Pegasus' share price steadily declined to pennies. Knabb and Durland together reaped more than $30 million through their securities law violations. They used the funds to support their extravagant lifestyles, including the purchase of homes, boats, and sports cars.

3. Knabb and Durland accomplished their scheme by issuing hundreds of millions of shares to individuals and entities they controlled, including Knabb's mother-in-law, his sister-in-law, his then-mistress, and an entity ostensibly managed by Knabb's pilot. Knabb and Durland reported none of these transactions in reports with the Commission and instead falsely claimed they owned only minimal amounts of shares, including shares restricted from immediate resale, and received no compensation from Pegasus.

4. In addition, beginning in November 2006, the defendants falsely claimed in SEC filings that Pegasus had issued hundreds of millions of shares to satisfy a previously undisclosed debt. The so-called debt, however, was fabricated by Knabb and Durland, who forged and backdated promissory notes to convince others to allow the shares to be issued in a way that would permit their immediate resale. Contrary to representations in SEC filings, Pegasus issued the shares primarily to the entity ostensibly managed by Knabb's pilot, which dumped the shares and remitted millions in proceeds to Knabb's wife. The false SEC filings concealed the fact that Knabb and Durland were basically printing Pegasus shares to enrich themselves. By February 2008, Pegasus had issued more than 75% of its total outstanding shares in this fraudulent manner.

5. Along the way, the defendants also lied about how Pegasus was financed in the first place, falsely claiming in SEC filings and press releases that the key acquisitions Pegasus touted were personally financed by Knabb. In truth, the money for the acquisitions came not from Knabb's own contributions to the company, but unregistered stock sales to individual investors in violation of the federal securities laws.

6. By engaging in the acts alleged in this complaint, the defendants violated the antifraud, registration, and other provisions of the federal securities laws, and caused Pegasus to file

numerous false reports with the Commission. The Commission seeks an order enjoining the defendants from future violations of the securities laws, requiring them to disgorge ill-gotten gains with prejudgment interest and pay civil monetary penalties, and barring Knabb and Durland from serving as officers or directors of a public company, as well as other appropriate relief.

## JURISDICTION, VENUE, AND INTRADISTRICT ASSIGNMENT

7. This Court has jurisdiction over this action pursuant to Sections 20(b) and 22(a) of the Securities Act of 1933 ("Securities Act"), 15 U.S.C. §§ 77t(b) and 77v(a), and Sections 21(d), 21(e), and 27 of the Securities Exchange Act of 1934 (the "Exchange Act"), 15 U.S.C. §§ 78u(d), 78u(e), and 78aa.

8. The defendants, directly or indirectly, have made use of the means and instrumentalities of interstate commerce or of the mails in connection with the acts, transactions, practices, and courses of business alleged in this complaint.

9. Venue is proper in this District pursuant to Section 22 of the Securities Act, 15 U.S.C. § 77v, and Section 27 of the Exchange Act , 15 U.S.C. § 78aa, because acts, transactions, practices, and courses of business constituting violations alleged in this complaint occurred within the Northern District of California. Intradistrict assignment in San Francisco is appropriate because much of the misconduct occurred in Alameda County, where Pegasus was located.

## DEFENDANTS AND RELIEF DEFENDANTS

10. Defendant Pegasus Wireless Corporation ("Pegasus") is a Nevada corporation formed in 2000. After several failed enterprises, it became a shell company around 2003. In around June 2005, through a series of reverse mergers, it acquired OTC Wireless, Inc., a private company incorporated in California that designed wireless networking devices. Before the reverse mergers, OTC Wireless reported approximately $1.25 million in assets, $3 million in annual revenue, and an accumulated deficit of over $13 million. From June 2005 and through approximately January 2007, Pegasus' principal place of business was Fremont, California. It currently maintains a mailbox in Palm Beach, Florida. Since April 20, 2001, it has had a class of securities registered pursuant to Section 12 of the Exchange Act. Its shares were quoted on the OTC Bulletin Board until April 21, 2006, when they became listed on NASDAQ. Pegasus withdrew its securities from listing on

NASDAQ on October 17, 2006. After that, Pegasus shares were again quoted on the OTC Bulletin Board. Pegasus has filed no quarterly or annual report since filing a Form 10-QSB for the third quarter of 2007 on November 19, 2007. Pegasus filed for Chapter 11 bankruptcy on January 28, 2008 in the Southern District of Florida. The court dismissed the petition on October 15, 2008. Pegasus refiled on November 25, 2008. The court again dismissed the petition on April 17, 2009, and prohibited Pegasus from refilling a Chapter 11 petition for two years.

11. Defendant Jasper Knabb, age 42, resides in Anchorage, Alaska. Knabb worked briefly for OTC Wireless in 2002 and became president and a director of Pegasus as a result of the reverse mergers. He became CEO in July 2006 and, at some point, chairman. He purported to resign from his position as president and CEO on January 29, 2008.

12. Defendant Stephen Durland, age 55, resides in West Palm Beach, Florida. Durland has served as Pegasus' CFO since 2005 and also purports to be its current acting CEO. He is a certified public accountant licensed in New York. During the Commission's investigation, Durland declined to testify, asserting his Fifth Amendment privilege against self-incrimination.

13. Relief Defendant Aero-Marine, LLC ("Aero-Marine") is a Nevada limited liability company formed in February 2006 and secretly owned and controlled by Knabb. Aero-Marine's organizational documents list Knabb's personal pilot as the manager. Since at least June 2005, Aero-Marine has received at least $12.8 million in proceeds from unlawful sales of Pegasus stock. Aero-Marine has no legitimate claim to these assets. Aero Marine is named as a relief defendant in this action for the purpose of assuring complete relief.

14. Relief Defendant Tammy Knabb, 41, resides in Little River, South Carolina, and/or Anchorage, Alaska. At some point, she was married to Jasper Knabb. Tammy Knabb received money or other assets through securities law violations by the defendants and others and has no legitimate claim to them. Since at least June 2005, Aero-Marine transferred at least $7.2 million in proceeds from unlawful sales of Pegasus stock to Tammy Knabb. Tammy Knabb has no legitimate claim to these proceeds. Tammy Knabb is named as a relief defendant in this action for the purpose of assuring complete relief.

## FACTUAL ALLEGATIONS

### I. Pegasus' Rise and Fall

15. In 2004, Pegasus, then named Blue Industries, Inc., was a failed shell company with virtually no cash or assets and a reported accumulated deficit of approximately $13 million. Through a series of reverse mergers in late 2004 and early 2005, Pegasus acquired OTC Wireless, Inc., a private wireless technology company based in Fremont, California, that claimed about $3 million in annual revenue. As a result of the reverse mergers, defendant Jasper Knabb became the company's president and later its CEO and chairman. Defendant Stephen Durland became CFO.

16. In late 2005 and early 2006, Pegasus touted in SEC filings and press releases dramatic growth through a series of acquisitions, most notably the purchase of a 51% interest in two private California companies – AMAX Engineering Corporation and AMAX Information Technologies, Inc. – both controlled by the family of an OTC Wireless officer.

17. AMAX reported substantial revenue – more than $78 million in 2005 – and Pegasus claimed the acquisition would increase its engineering, production, and distribution capacity. As described in detail below, Pegasus falsely claimed the acquisitions were financed by Knabb.

18. Pegasus' stock price rose sharply after the AMAX acquisition announcement, and in April 2006 Pegasus successfully applied to have its shares listed on NASDAQ and it began trading under the symbol "PGWC." Pegasus shares reached a high of $18.69 per share in May 2006, briefly giving Pegasus a market capitalization of approximately $1.42 billion. Knabb promoted Pegasus through word of mouth, as well as unique promotional events such as an appearance at a major sporting event and a concert by a world-renowned musician.

19. The stock, however, began a steady decline after that, in apparent response to press articles questioning Pegasus' valuation and reports that Knabb and Durland had headed other micro-cap companies whose stock rose and crashed in short periods of time.

20. By September 2006, the stock traded for less than $1. Pegasus shares were delisted from NASDAQ on October 17, 2006. After that, Pegasus shares were again quoted on the OTC Bulletin Board. Today they trade for less than a penny under the symbol "PGSW."

21. In January 2007, Pegasus abruptly announced it was moving its headquarters to the Bahamas and closing the Fremont facility. By approximately July 2007, it had ceased operations and terminated most employees. Pegasus declared bankruptcy on January 28, 2008.

## II. Pegasus Raised Funds Through Unregistered Offerings

22. Between June 2005 and February 2008, Pegasus distributed hundreds of millions of its shares to the public through individuals and entities controlled by Knabb and Durland. Knabb and Durland accomplished the distribution, in part, by creating backdated promissory notes memorializing a phony debt in order to induce others to allow the shares to be issued in a way that would permit their immediate resale.

23. The nominees who received the stock sold the shares to other individual investors, and on the open market, and funneled most of the proceeds to Knabb and Durland. Knabb and Durland each reaped millions through the scheme.

24. Pegasus did not have a registration statement in effect relating to any of the securities offered and sold during the relevant period, and Knabb and Durland also failed to file reports with the SEC disclosing the acquisitions and sales by the nominees they controlled.

### A. The Initial Distribution Through Nominees

25. In June 2005, immediately after the reverse merger with OTC Wireless, Pegasus issued 11 million shares largely to friends, family, and associates of Knabb and Durland. Just before issuing the shares, Pegasus had fewer than one million shares outstanding. To control the issuance, Durland personally communicated with Pegasus' transfer agent, the entity Pegasus retained to handle the mechanics of its securities transactions. Durland directed the transfer agent to issue the shares without any restrictions limiting their resale.

26. Among the largest recipients were Nancy Speer, Knabb's mother-in-law (1 million shares); Sherri Wilson, Knabb's sister-in-law (1 million shares); and Herman Jones, a South Carolina real estate developer and restaurant owner and Knabb's close friend and business partner (784,615 shares).

27. Between July 2005 and September 2006, Speer, Wilson, and Jones frequently received additional, supposedly unrestricted Pegasus shares, either through a stock split or as a transfer from

other conduits or among themselves. Speer received approximately 4,616,740 supposedly unrestricted shares this way; Wilson received approximately 3,690,731; and Jones received approximately 4,395,732.

28. In most instances, Durland facilitated the transfers of shares to Speer, Wilson, Jones, and others between July 2005 and September 2006 by providing instructions to Pegasus' transfer agent. The instructions included Pegasus stock certificates in an individual or entity's name and a list of entities and individuals to whom the shares should be reissued. On at least dozens of occasions, Durland instructed the transfer agent to forward the reissued certificates to him.

### B. Knabb and Durland Used Backdated, Bogus Promissory Notes to Issue Hundreds of Millions of Pegasus Shares to Nominees

29. In August 2006, Pegasus began issuing massive amounts of supposedly unrestricted shares to Jones, Speer, Wilson, Aero-Marine, and others connected to Knabb and/or Durland. To convince Pegasus' transfer agent to issue the shares without restrictions on their immediate resale, Pegasus claimed it was issuing the shares to satisfy promissory notes purportedly issued by a Blue Industries, Inc. subsidiary in 2003 and 2004.

30. To support Pegasus' claim to the transfer agent, Durland presented at least 33 supposed promissory notes to the transfer agent between August 2006 and February 2008. By February 2008, Pegasus had issued nearly 479,150,000 shares – 75% of its outstanding shares – in this manner.

31. One such note, in the amount of $60,000, was purportedly issued to a former Blue Industries CEO. The note was dated August 25, 2003, and stated it was due and payable on August 24, 2005, and convertible at the former CEO's option into Pegasus stock at a price of $0.01 per share (i.e., six million shares).

32. The $60,000 note dated August 25, 2003, purportedly issued to the former Blue Industries CEO, was fabricated and backdated. Pegasus did not provide it to the former Blue Industries CEO until September 2006. The Blue Industries subsidiary did not promise in 2003 to pay the former CEO anything or agree to permit him to convert the debt into stock at a steeply discounted price.

33. Durland presented the fabricated, backdated note to Pegasus' transfer agent, requesting the agent issue six million Pegasus shares, without any restrictions on their resale, on the claim that the shares were in payment of a three-year-old debt. Durland also arranged for the notes to be presented to an outside attorney, who, based on the purported 2003 date in the note, opined that Pegasus could issue the shares without restrictions consistent with applicable rules that generally allowed certain persons to resell securities if, among other things, the securities had been held for a sufficiently long period.

34. Of the six million shares Pegasus issued based on the fabricated, backdated note, only a small number – 200,000 shares – went to the former Blue Industries CEO. Pegasus issued 5.8 million shares directly to Speer, Jones, and Aero-Marine.

35. The remaining notes, collectively purporting to evidence the Blue Industries subsidiary's promise to pay $1,401,500, were supposedly issued to an individual named Charles Adams, a close associate of Durland. The notes bore dates between June 2, 2003, and April 19, 2004, and stated they were due and payable on dates between September 2004 and April 2006 and convertible at Adams' option into Pegasus stock at a price of $0.01 per share. During the Commission's investigation, Adams declined to testify about the notes or his activities relating to Pegasus, asserting his Fifth Amendment privilege against self-incrimination.

36. The approximately $1.4 million in notes purportedly issued to Adams were likewise fabricated and backdated. The Blue Industries subsidiary did not promise in 2003 or 2004 to pay Adams anything or agree to permit him to convert the debt into stock at a steeply discounted price.

37. Durland presented the fabricated, backdated Adams notes to Pegasus' transfer agent, again requesting the agent issue Pegasus shares, without any restrictions on their resale, on the claim that the shares in payment of a debt of one or more years. Durland also arranged for the notes to be presented to the same outside attorney, who, based on the purported 2003 and 2004 dates in the note, opined that Pegasus could issue the shares without restrictions.

38. Pegasus issued at least 473,150,000 million shares based on the fabricated, backdated Adams notes, but only about 30 million shares went to Adams, the purported note holder. Pegasus issued the vast majority of the shares – 433,150,000 – directly to Speer, Wilson, Jones, and Aero-

Marine, as well as to Knabb's then-mistress, to Knabb's personal assistant, and to others tied to Knabb and/or Durland.

39. Aero-Marine, which Knabb secretly owned and controlled, was the largest recipient of shares through the bogus promissory note scheme, receiving more than 117 million shares based on the backdated, fabricated promissory notes.

40. Aero-Marine sold the shares it received through the bogus promissory note scheme (as well as additional shares it received from conduits prior September 2006) and funneled millions in proceeds to Tammy Knabb.

41. Another approximately 14.8 million shares were issued to Jones through this method. Speer received 1,030,000 shares. Wilson received 500,000.

42. Approximately 85 million Pegasus shares were issued through this method to Equity Investment Corporation to personally enrich Durland by approximately $2 million. Equity Investment is a shell company owned by a long-time business associate of Durland. In late 2005, Durland and the business associate agreed to use Equity Investment as a vehicle to fund another company, Global Event Makers, Inc., that the two owned and for which Durland served as CFO and director.

43. To accomplish their arrangement, Durland first arranged for Pegasus stock to be transferred into Equity Investment's brokerage account by the same means described above. Equity Investment then sold the shares and transferred the proceeds to a bank account in Global Event's name. As Global Event's CFO, Durland had access to its bank account, and he withdrew $2 million of these proceeds during 2006 and 2007 using the funds for personal purchases.

### C. The Nominees Sell the Shares, Provide the Proceeds to Knabb, and Are Paid for Their Assistance in the Scheme

44. Having received millions of Pegasus shares directly from Pegasus or indirectly through conduits, Speer, Wilson, Jones, and Aero-Marine proceeded to dump the shares and remit the bulk of the proceeds to Knabb. During the Commission's investigation, Speer, Wilson, Jones, and Aero-Marine's supposed manager declined to testify about the transactions or activities relating to Pegasus, asserting their Fifth Amendment privilege against self-incrimination.

45. Between June 2005 and September 2006, Jones sold at least 978,235 shares to individual investors, including unaccredited investors, in the Myrtle Beach, South Carolina area, often through face-to-face meetings. Knabb often participated in the selling efforts, accompanying Jones in the face-to-face meetings and touting Pegasus' prospects. From the proceeds of these sales directly to investors, Jones wired to Knabb at least $2.2 million between January 2005 and September 2006. Investors who acquired Jones' shares sometimes wrote checks directly to Knabb.

46. Of the 14.8 million shares Jones received through the phony promissory note scheme, Jones transferred approximately 2 million to his brokerage accounts between September 2006 and February 2008 and then sold them on the open market.

47. Knabb received millions more from stock sales through the public distribution of Speer's and Wilson's shares. Between June 2005 and 2006, Speer and Wilson transferred more than 3.8 million shares to their brokerage accounts, and from there sold the shares on the open market. They wired proceeds of approximately $5.7 million to Knabb's bank account. In addition, Knabb sold shares held in Speer's name directly to several individual investors. The remaining shares held by Speer and Wilson were sold or transferred to individual investors or transferred back to nominees. On at least one occasion, shares in Speer's name were transferred to Knabb's then-mistress.

48. Between approximately November 2006 and December 2007, relief defendant Aero-Marine sold approximately 125 million shares of Pegasus stock to the public, receiving proceeds of about $12.8 million. Aero Marine was not entitled to these assets. Aero Marine transferred approximately $7.2 million in proceeds to a bank account in relief defendant Tammy Knabb's name. Tammy Knabb was not entitled to these assets. Tammy Knabb used these funds to pay Jasper Knabb's credit card bills. Between approximately November 2006 and December 2007, Aero-Marine also sent at least $343,000 to a California law firm that had provided legal services to Jasper Knabb and to Pegasus and approximately $1 million to a law firm that performed services for Knabb and Pegasus in the Bahamas.

49. Knabb also acquired and sold Pegasus stock using an account in the name of his then-mistress. Knabb had a pecuniary interest in the account.

### D. Knabb and Durland Used the Funds from Nominee Stock Sales Partly to Fund Pegasus but Mostly to Pad Their Own Pockets

50. All told, Knabb received approximately $30 million from the sale of Pegasus shares, sold directly by him or through nominees, to the public and individual investors. Durland received at least $2 million. Knabb and Durland used most of the proceeds to purchase lavish homes, an airplane, Ferraris and other sports cars, boats and diving equipment. Knabb failed to report any of the transactions involving shares in the name of Jones, Speer, Wilson, Aero-Marine, or his former mistress, despite the fact he had a pecuniary interest in the securities. Durland likewise failed to report any of the transactions involving shares in the name of Equity Investment, despite the fact he had a pecuniary interest in the securities.

51. Durland knew or was reckless in not knowing the notes presented to Pegasus' transfer agent to justify issuing unrestricted shares were backdated and fabricated. Indeed, in May 2007, Durland told Pegasus' outside auditor that the company's obligation to repay the debt purportedly represented by the bogus promissory notes was "almost gone." At the time Durland made the statement to the auditor, Pegasus had issued about 40 million shares. Subsequent to May 2007, however, pursuant to Durland's instructions, Pegasus issued approximately 440 million additional shares to satisfy the purported debt.

52. Knabb, who was the primary beneficiary of the bogus promissory note scheme, also knew or was reckless in not knowing the notes presented to Pegasus' transfer agent to justify issuing unrestricted shares were backdated and fabricated.

## III. Knabb and Durland Made Materially False Statements About Pegasus' Financing, the Bogus Promissory Notes, and Their Compensation

### A. False Statements Regarding Knabb's Investments in Pegasus in SEC Filings

53. Beginning in around December 2005, Pegasus represented in multiple SEC filings and press releases that it had made several significant acquisitions and that Knabb personally had provided a total of $8 million to fund the acquisitions.

54. For example, Pegasus' 2005 annual report on Form 10-KSB, filed March 3, 2006, stated:

- "On December 22, 2005, the Company acquired 51% of [AMAX] . . . . The cash portion of the AMAX transaction was provided by the sale of . . . shares of restricted common stock . . . to Jasper Knabb . . . in exchange for $4,000,000 in cash."
- "On December 29, 2005, the Company acquired 51% of Cnet Technology, Inc.... The acquisition was financed by a purchase of . . . restricted shares of . . . stock by Jasper Knabb . . . in exchange for $2,000,000 in cash."
- "On January , 2006, [sic] the Company acquired 51% of SKI Technologies, Inc. . . . . The acquisition was financed by a purchase of . . . restricted shares of . . . stock by Jasper Knabb . . . in exchange for $2,000,000 in cash."

55. Pegasus made identical representations in its 2006 annual report on Form 10-KSB, filed April 2, 2007.

56. Knabb and Durland authored and signed the 2005 and 2006 annual reports. In addition, as required by the Sarbanes-Oxley Act of 2002, Durland submitted certifications representing he had read the annual reports and that they contained no untrue statements of material fact and did not omit material information. Knabb similarly certified that the 2006 annual report contained no untrue statements of material fact and did not omit material information.

57. These statements were false and misleading. Knabb did not personally invest his money in the company through the purchase of restricted stock. Rather, the money used to fund these acquisitions came from unregistered Pegasus stock sales to investors, not Knabb's independent resources.

58. Pegasus made identical representations its quarterly reports on Form 10-QSB for the first three quarters of 2006 and 2007, filed on May 8, 2006, July 25, 2006, November 22, 2006, May 21, 2007, August 14, 2007, and November 19, 2007, respectively. Durland signed the quarterly reports and submitted Sarbanes-Oxley certifications for each one. Knabb also submitted Sarbanes-Oxley certifications for all but the report for the first quarter of 2006, filed May 8, 2006.

59. Pegasus made similar representations in current reports on Form 8-K filed with the Commission, specifically:

- A current report filed December 22, 2005, attached a press release quoting Knabb and stating "[t]he cash portion [of the AMAX transaction] was partially financed by the purchase of . . . restricted shares of Pegasus Wireless Corporation's common stock by Jasper Knabb, the Company President."
- A current report filed December 23, 2005, described the AMAX acquisition and stated "[t]he cash portion of the AMAX transaction was provided by the sale of . . . shares of restricted common stock of the Company to Jasper Knabb, President of Pegasus, in exchange for $4,000,000 in cash."
- A current report filed December 29, 2005, and amended January 9, 2006, attached a press release describing the Cnet acquisition and stating "[t]he acquisition will be financed by a purchase of 222,222 restricted shares of Pegasus Wireless Corporation's common stock by Jasper Knabb, Company's President."
- A current report filed January 9, 2006, described the Cnet acquisition and stated "[t]he cash portion of the [Cnet] transaction was provided by the sale of . . . shares of restricted common stock of the Company to Jasper Knabb, President of Pegasus, in exchange for $2,000,000 in cash."
- A current report filed January 25, 2006, stated that "[t]he cash portion of the th[e] [SKI] transaction was provided by the sale of . . . shares of restricted common stock of the Company to Jasper Knabb, President of Pegasus, in exchange for $2,000,000 in cash."

60. Durland authored and signed each of the current reports. Knabb similarly drafted Pegasus' press releases included in the reports.

61. These statements were false and misleading. Knabb did not personally invest his money in the company through the purchase of restricted stock. Rather, the money used to fund these acquisitions came from unregistered Pegasus stock sales to investors, not Knabb's independent resources.

62. Knabb knew or was reckless in not knowing the money for these transactions came not from his own resources.

63. Using investor payments, and proceeds from the nominees, Knabb wired a total of $5.75 million to Pegasus during December 2005 and January 2006. Despite knowing that the money he wired fell short of the $8 million announced, Knabb falsely represented that he had invested a total amount of $8 million.

64. As Pegasus' CFO, Durland controlled the company's bank accounts and prepared its balance sheet. Durland knew or was reckless in not knowing that Knabb did not invest in Pegasus to the extent claimed in the SEC filings and press releases. He also knew or was reckless in not knowing about the nominees' stock sales and that the investment amounts came from third-party investors, not Knabb's personal assets.

65. Knabb thus failed to disclose the fact that the investment money actually came to him through third-party investors and unregistered sales of Pegasus shares by nominees he controlled and instead Knabb passed off the payments to Pegasus as his own. Pegasus' stock price rose dramatically during the first half of 2006, following these positive public statements about the acquisitions and Knabb's investments in the company. Knabb benefited from this increase in stock price as his nominees sold their Pegasus shares throughout 2006 and continued to funnel the inflated proceeds to him.

**B. False Statements About the Fictitious Debt in SEC Filings**

66. To further their scheme, Knabb and Durland also misrepresented in Pegasus' SEC filings the nature and purpose of the share issuances based on the bogus, backdated promissory notes. Beginning with the quarterly report for the third quarter of 2006, filed November 22, 2006, Pegasus falsely claimed that it had issued the shares to satisfy a previously undisclosed debt that had been concealed by management before the 2004/2005 reverse mergers.

67. In every subsequent quarterly and annual report, each authored, signed, and in certain circumstances certified by Knabb and Durland, the purported debt inexplicably increased along with the number of shares issued to satisfy it. The fraudulent statements are as follows:

- Form 10-QSB for the quarter ended September 30, 2006: "During the third quarter the Company issued 5,276,016 shares to satisfy $263,800 debt [sic] owed by the Company from prior to the change in control [in 2005]."

- Form 10-KSB for the fiscal year ended December 31, 2006: "During 2006 the Company issued 7,376,016 shares of common stock to satisfy $368,532 debt owed by the Company from prior to the change in control . . . .The Company is obligated on notes payable amounting to $145,000 remaining balance which were undisclosed when current management took control of the shell company . . . these notes . . . are convertible into common stock of the parent company at the discretion of the holder."
- Form 10-QSB for the quarter ended March 31, 2007: "In the first quarter 2007 the Company issued 13,000,000 shares of common stock to satisfy $130,000 debt [sic] owed by the Company from prior to the change in control in June 2005."
- Form 10-QSB for the quarter ended June 30, 2007: "In the first half 2007 [sic] the Company issued 20,300,000 shares of common stock to satisfy $203,000 debt [sic] owed by the Company from prior to the change in control in June 2005."
- Form 10-QSB for the quarter ended September 30, 2007: "In the first nine months 2007 [sic] the Company issued 25,300,000 shares of common stock to satisfy $253,000 debt [sic] owed by the Company from prior to the change in control in June 2005."

68. Pegasus' filings include no additional details about the provenance or reason for the supposed debt.

69. In fact, each of these representations was false and misleading. There was no discovered "undisclosed" debt from before the reverse mergers; rather, the debt was fabricated by Knabb and Durland and was an excuse to issue shares into the hands of individuals and entities they controlled.

70. In addition, the statements misleadingly stated Pegasus was obligated to issue massive amounts of shares, resulting in substantial dilution to existing shareholders, to satisfy a legitimate obligation, when, in truth, the shares were being issued to personally enrich Knabb and Durland.

71. Following the third quarter of 2007, Pegasus ceased reporting its financial results in SEC filings. However, the company continued to issue hundreds of millions of shares based on the supposed promissory notes. By February 2008, Pegasus had thus issued nearly 480 million shares,

more than 75% of its then outstanding stock, on account of the fictitious debt. No such debt was even mentioned before November 2006.

72. Durland presented each of the bogus notes to the transfer agent or opinion lawyer and knew or was reckless in not knowing they did not represent legitimate obligations. Knabb, the primary beneficiary of the bogus note scheme who also signed and certified the false SEC filings, similarly knew or was reckless in not knowing.

### C. False Statements About Knabb and Durland's Compensation

73. Pegasus' annual reports filed with the Commission on Form 10-KSB for fiscal years 2005 and 2006 stated that Knabb and Durland received no compensation as president and CFO, respectively; that Knabb beneficially owned fewer than 2 million Pegasus shares (including large amounts of restricted shares that could not be immediately resold); and that Durland beneficially owned fewer than 300,000 shares.

74. These representations were false and misleading. They falsely suggested that Knabb and Durland received no compensation when in fact they received several million dollars (and in Knabb's case tens of millions of dollars) through the issuance of stock to nominees who funneled the proceeds back to them. In addition, they understated the number of Pegasus shares they controlled.

75. Knabb and Durland knew or were reckless in not knowing the representations were false and misleading.

### D. False Statements to Pegasus' Auditor

76. In addition to making false statements in SEC filings, Durland repeatedly lied to Pegasus' outside auditor. First, as described above, Durland falsely represented in May 2007 that Pegasus was issuing shares to satisfy a debt concealed by former management, but in truth the so-called debt was fabricated as an excuse to issue shares to Knabb and Durland's nominees. Durland also lied about how many shares remained to be issued. He told the auditor the debt was "almost gone." At the time, Pegasus had issued 40 millions shares based on the so-called debt. After May 2007, however, Pegasus issued an additional 440 million shares.

77. Second, Durland provided false management representation letters to Pegasus' auditor for the quarters ended September 30, 2006, and March 31, June 30, and September 30, 2007. In each

Durland falsely stated Pegasus had made available all financial records and related data and that he knew of no fraud involving management. These were false and misleading because Knabb and Durland were engaged in a scheme to enrich themselves by issuing shares to nominees based on false documents.

## FIRST CLAIM FOR RELIEF

*Violations of Section 17(a)(1) of the Securities Act by All Defendants*

78. The Commission realleges and incorporates by reference Paragraphs 1 through 77.

79. By engaging in the conduct described above, Pegasus, Knabb, and Durland, directly or indirectly, in the offer or sale of securities, by the use of the means or instruments of transportation or communication in interstate commerce or by use of the mails, with scienter, employed devices, schemes, or artifices to defraud.

80. By reason of the foregoing, Pegasus, Knabb, and Durland have violated, and unless restrained and enjoined will continue to violate, Section 17(a)(1) of the Securities Act, 15 U.S.C. § 77q(a)(1).

## SECOND CLAIM FOR RELIEF

*Violations of Section 17(a)(2) and (a)(3) of the Securities Act by All Defendants*

81. The Commission realleges and incorporates by reference Paragraphs 1 through 77.

82. By engaging in the conduct described above, Pegasus, Knabb, and Durland, directly or indirectly, in the offer or sale of securities, by the use of the means or instruments of transportation or communication in interstate commerce or by use of the mails:

(a) obtained money or property by means of untrue statements of a material fact or omissions to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading; and

(b) engaged in transactions, practices, or courses of business which operated or would operate as a fraud or deceit upon purchasers of securities.

83. By reason of the foregoing, Pegasus, Knabb, and Durland have violated, and unless restrained and enjoined will continue to violate, Section 17(a)(2) and (a)(3) of the Securities Act, 15 U.S.C. § 77q(a)(2) and 77q(a)(3).

## THIRD CLAIM FOR RELIEF

*Violations of Section 10(b) of the Exchange Act and Rule 10b-5 Thereunder by All Defendants*

84. The Commission realleges and incorporates by reference Paragraphs 1 through 77.

85. By engaging in the conduct described above, Pegasus, Knabb, and Durland, with scienter, directly or indirectly, in connection with the purchase or sale of securities, by the use of means or instrumentalities of interstate commerce or of the mails, or of facilities of a national securities exchange:

(a) employed devices, schemes, or artifices to defraud;

(b) made untrue statements of a material fact or omitted to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading; and

(c) engaged in acts, practices, or courses of business which operated or would operate as a fraud or deceit upon other persons, including purchasers and sellers of securities.

86. By reason of the foregoing, Pegasus, Knabb, and Durland have violated, and unless restrained and enjoined will continue to violate, Section 10(b) of the Exchange Act, 15 U.S.C. § 78j(b), and Rule 10b-5, 17 C.F.R. § 240.10b-5.

## FOURTH CLAIM FOR RELIEF

*Violations of Section 5(a) and 5(c) of the Securities Act by All Defendants*

87. The Commission realleges and incorporates by reference Paragraphs 1 through 77.

88. By engaging in the acts and conduct alleged above, Pegasus, Knabb, and Durland, directly or indirectly, made use of means or instruments of transportation or communication in interstate commerce or of the mails to offer and to sell securities through the use or medium of a prospectus or otherwise when no registration statement had been filed or was in effect as to such securities and no exemption from registration was available.

89. By reason of the foregoing, Pegasus, Knabb, and Durland have violated, and unless restrained and enjoined will continue to violate, Section 5(a) and (c) of the Securities Act, 15 U.S.C. §§ 77e(a) and 77e(c).

## FIFTH CLAIM FOR RELIEF

*Violations of Section 13(b)(5) of the Exchange Act by Knabb and Durland*

90. The Commission realleges and incorporates by reference Paragraphs 1 through 77.

91. By engaging in the conduct described above, Knabb and Durland knowingly falsified books, records, or accounts of Pegasus subject to Section 13(b)(2)(A) of the Exchange Act, 15 U.S.C. § 78m(b)(2)(A).

92. By reason of the foregoing, Knabb and Durland have violated, and unless restrained and enjoined will continue to violate, Section 13(b)(5) of the Exchange Act, 15 U.S.C. § 78m(b)(5).

## SIXTH CLAIM FOR RELIEF

*Violations of Exchange Act Rule 13b2-1 by Knabb and Durland*

93. The Commission realleges and incorporates by reference Paragraphs 1 through 77.

94. By engaging in the conduct described above, Knabb and Durland, directly or indirectly, falsified or caused to be falsified, books, records, or accounts subject to Section 13(b)(2)(A) of the Exchange Act, 15 U.S.C. § 78m(b)(2)(A).

95. By reason of the foregoing, Knabb and Durland have violated, and unless restrained and enjoined will continue to violate, Exchange Act Rule 13b2-1, 17 C.F.R. § 240.13b2-1.

## SEVENTH CLAIM FOR RELIEF

*Violations of Exchange Act Rule 13b2-2 by Durland*

96. The Commission realleges and incorporates by reference Paragraphs 1 through 77.

97. Durland, while an officer and a director of Pegasus, by engaging in the conduct described above, directly or indirectly, in connection with (a) an audit, review, or examination of the financial statements of the issuer required to be made pursuant to Commission rules, or (b) the preparation or filing of any document or report required to be filed with the Commission pursuant to Commission rules: (1) made or caused to be made a materially false or misleading statement to an accountant, or (2) omitted to state, or caused another person to omit to state, a material fact necessary

in order to make the statements made, in light of the circumstances under which such statements were made, not misleading to an accountant.

98. Durland, while an officer and a director of Pegasus, by engaging in the conduct described above, directly or indirectly took actions to mislead or fraudulently influence independent public or certified public accountants engaged in the performance of an audit or review of the financial statements of Pegasus, while he knew or should have known that his actions, if successful, could result in rendering Pegasus' financial statements materially misleading.

99. By reason of the foregoing, Durland has violated, and unless restrained and enjoined will continue to violate, Exchange Act Rule 13b2-2, 17 C.F.R. § 240.13b2-2.

## **EIGHTH CLAIM FOR RELIEF**

*Violations of Section 13(a) of the Exchange Act and Rules 12b-20, 13a-1, 13a-11, and 13a-13 Thereunder by All Defendants*

100. The Commission realleges and incorporates by reference Paragraphs 1 through 77.

101. Based on the conduct alleged above, Pegasus violated Section 13(a) of the Exchange Act, 15 U.S.C. § 78m(a), and Rules 12b-20, 13a-1, 13a-11, and 13a-13, 17 C.F.R. §§ 240.12b-20, 240.13a-1, 240.13a-11, and 240.13a-13, which obligate issuers of securities registered pursuant to the Exchange Act to file with the Commission annual, quarterly, and current reports that, among other things, do not contain untrue statements of material fact or omit to state material information necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading.

102. By engaging in the conduct described above, Knabb and Durland knowingly provided substantial assistance to Pegasus' filing of materially false and misleading reports and filings with the Commission.

103. By reason of the foregoing, Pegasus has violated, and unless restrained and enjoined will continue to violate, Section 13(a) of the Exchange Act, 15 U.S.C. § 78m(a), and Rules 12b-20, 13a-1, 13a-11, and 13a-13, 17 C.F.R. §§ 240.12b-20, 240.13a-1, 240.13a-11, and 240.13a-13.

104. By reason of the foregoing, Knabb and Durland have aided and abetted Pegasus' violations, and unless restrained and enjoined will continue to aid and abet such violations, of Section

13(a) of the Exchange Act, 15 U.S.C. § 78m(a), and Rules 12b-20, 13a-1, 13a-11, and 13a-13, 17 C.F.R. §§ 240.12b-20, 240.13a-1, 240.13a-11, and 240.13a-13.

## NINTH CLAIM FOR RELIEF

*Violations of Exchange Act Rule 13a-14 by Knabb and Durland*

105. The Commission realleges and incorporates by reference Paragraphs 1 through 77.

106. Knabb and Durland signed, as Pegasus' principal executive officer and principal financial officer, respectively, false certifications pursuant to Rule 13a-14 of the Exchange Act that were included in Pegasus' 2005 and 2006 annual reports filed on Forms 10-KSB, as well as its quarterly reports filed on Forms 10-QSB. In each such certification, Knabb and Durland falsely stated, among other things, that: (a) each report did not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading; (b) each financial statement, and other financial information included in each report, fairly presented in all material respects the financial condition, results of operations, and cash flows of Pegasus as of, and for, the period presented in the report; and (c) Knabb and Durland had disclosed to Pegasus' auditors all significant deficiencies in the design or operation of Pegasus' internal controls and any fraud, whether or not material, that involved management or other employees who had a significant role in Pegasus' internal controls.

107. By reason of the foregoing, Knabb and Durland have violated, and unless restrained and enjoined will continue to violate, Exchange Act Rule 13a-14, 17 C.F.R. § 240.13a-14.

## TENTH CLAIM FOR RELIEF

*Violations of Section 16(a) of the Exchange Act and Rule 16a-3 Thereunder by Knabb and Durland*

108. The Commission realleges and incorporates by reference Paragraphs 1 through 77.

109. Based on the conduct alleged above, by failing to file accurate statements with the Commission regarding their changes in beneficial ownership of Pegasus shares, Knabb and Durland violated Section 16(a) of the Exchange Act, 15 U.S.C. § 78p(a), which obligates officers and directors of issuers registered pursuant to Section 12 of the Exchange Act, 15 U.S.C. § 78*l*, to file with the Commission statements regarding beneficial ownership of securities of the issuer.

110. By reason of the foregoing, Knabb and Durland have violated, and unless restrained and enjoined will continue to violate, Section 16(a) of the Exchange Act, 15 U.S.C. § 78p(a) and Exchange Act Rule 16a-3, 17 C.F.R. § 240.16a-3.

## PRAYER FOR RELIEF

WHEREFORE, the Commission respectfully requests that this Court:

I.

Issue an order permanently restraining and enjoining each defendant and their agents, servants, employees, attorneys, and assigns, and those persons in active concert or participation with them, from violating and/or aiding and abetting violations of the provisions of the federal securities laws each violated, including Sections 5 and 17(a)(1), (2), and (3) of the Securities Act, 15 U.S.C. §§ 77e and 77q(a); Sections 10(b), 13(a), 13(b)(5), and 16(a) of the Exchange Act, 15 U.S.C. §§ 78j(b), 78m(a), 78m(b)(5), and 78p(a); and Rules 10b-5, 12b-20, 13a-1, 13a-11, 13a-13, 13a-14, 13b2-1, 13b2-2, and 16a-3, 17 C.F.R. §§ 240.10b-5, 240.12b-20, 240.13a-1, 240.13a-11, 240.13a-13, 240.13a-14, 240.13b2-1, 240.13b2-2, and 240.16a-3.

II.

Issue an order directing defendants Knabb, Durland, and Pegasus to disgorge all wrongfully obtained benefits in an amount according to proof, plus prejudgment interest thereon.

III.

Issue an order directing all relief defendants to disgorge their ill-gotten gains in an amount according to proof, plus prejudgment interest thereon.

IV.

Issue an order directing Knabb and Durland to pay civil monetary penalties under Section 20(d) of the Securities Act, 15 U.S.C. §§ 77t(d), and Section 21(d)(3) of the Exchange Act, 15 U.S.C. §§ 78u(d)(3).

V.

Issue an order barring Knabb and Durland from serving as officers and directors of any public company, pursuant to Section 20(e) of the Securities Act, 15 U.S.C. § 77t(e), and Section 21(d)(2) of the Exchange Act, 15 U.S.C. § 78u(d)(2).

VI.

Retain 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 that may be entered, or to entertain any suitable application or motion for additional relief within the jurisdiction of this Court.

VII.

Grant such other and further relief as this Court may determine to be just and necessary.

Dated: May 26, 2009

Respectfully submitted,

Robert S. Leach
Attorney for Plaintiff
SECURITIES AND EXCHANGE COMMISSION