

1 **STATE OF WASHINGTON**
2 **DEPARTMENT OF FINANCIAL INSTITUTIONS**
3 **SECURITIES DIVISION**

4 IN THE MATTER OF DETERMINING
5 Whether there has been a violation of the
6 Securities Act of Washington by:

7 Kenyon Capital Investment Holdings LLC;
8 Shaun Brog;
9 Ryan Brog;

Respondents.

Order No.: S-17-2137-18-SC01

STATEMENT OF CHARGES AND NOTICE OF
INTENT TO ENTER ORDER TO CEASE AND
DESIST, TO DENY FUTURE REGISTRATIONS, TO
IMPOSE FINES, AND TO CHARGE COSTS

10 THE STATE OF WASHINGTON TO:

Kenyon Capital Investment Holdings LLC
Shaun Brog (CRD #5000205)
Ryan Brog (CRD #5798126)

11 **STATEMENT OF CHARGES**

12 Please take notice that the Securities Administrator of the State of Washington has reason to believe
13 that Respondents Kenyon Capital Investment Holdings LLC, Shaun Brog, and Ryan Brog have each violated
14 the Securities Act of Washington. The Securities Administrator believes those violations justify the entry of
15 an order against the Respondents to cease and desist from such violations and to charge costs pursuant to
16 RCW 21.20.390, to impose fines under RCW 21.20.395 and RCW 21.20.110, and to deny future registrations
17 under RCW 21.20.110. The Securities Administrator finds as follows:

18 **TENTATIVE FINDINGS OF FACT**

19 **Respondents**

20 1. Kenyon Capital Investment Holdings LLC (“Kenyon Capital”) is a Washington entity formed
21 on October 27, 2014, with its principal place of business in Richland, Washington. Kenyon Capital operated
22 as a pooled investment vehicle, primarily seeking to invest in alternative assets.

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1 appropriately. These duties include, but are not necessarily limited to: (a) engaging a qualified custodian to
2 send account statements to investors or an independent CPA to examine and verify the fund's assets; (b)
3 providing clients with itemized invoices when deducting fees; and (c) engaging an independent party to
4 authorize fee withdrawals or providing investors with yearly audited financial statements. The Brogs did not
5 engage a qualified custodian to send account statements to investors or an independent CPA to verify the
6 fund's assets, did not provide clients with itemized invoices when taking fees, did not engage an independent
7 party to authorize their fee withdrawals, and never provided investors with audited financial statements. The
8 Respondents also have not provided investors with quarterly account statements for either the first or second
9 quarter of 2018. Kenyon Capital, and Shaun and Ryan Brog, failed to disclose to investors that the fund had
10 no established policies or procedures to verify that they were charging appropriate fees, or to guard against
11 potential misuse of investor funds.

12 8. As a result of their failures to comply with Washington's custody requirements, the Brogs were
13 able to determine their own compensation because they valued the fund's assets and evaluated their own
14 performance with no independent oversight. The Brogs continued to ignore Washington's custody
15 requirements even after receiving a warning from the Division in April 2017 that the fund could be a pooled
16 investment vehicle which would need to comply with such requirements. The Brogs' failure to comply with
17 custody requirements also enabled them to use Kenyon Capital's fund accounts for personal expenses, write
18 checks to themselves, and make regular cash withdrawals as purported "fees," without notifying investors of
19 such uses.

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1 **Use of Investor Funds**

2 9. Rather than withdrawing their performance fees or salary on a lump-sum basis, Shaun and
3 Ryan Brog regularly used the fund’s account to directly pay personal expenses as needed, commingling both
4 Kenyon Capital’s business expenses and their own personal expenses within the fund account. Throughout
5 2016 and 2017, the Brogs made both business and personal expenditures with Kenyon Capital’s money which
6 significantly exceeded the fees they would have been allowed to charge by the fund’s operating agreement
7 and Washington law.

8 10. From at least December 2015 to February 2017, Kenyon Capital’s contract with most investors
9 provided that the fund’s managers would receive the following fees:

- 10 a. An annual maintenance fee of 2% of fund assets for the business expenses of Kenyon
11 Capital (not as personal compensation for the Brogs);
- 12 b. A management fee of 0.75% of fund assets; and
- 13 c. A performance fee of 15% or 20% of the fund’s gains “on a bi-annual basis,” depending on
14 whether the fund’s performance exceeded, respectively, the Barclays Aggregate Bond
15 Index or the S&P 500 Benchmark Index.²

16 11. For the 2% annual maintenance fee, the Brogs maintained an American Express card, which
17 they represented to the Division was used for all of Kenyon Capital’s business expenses. As described further
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19 ² For five of the investors who rolled over their investments from Kenyon Capital NY, the contract provided that Shaun and Ryan
20 Brog, through Kenyon Capital, would charge the same maintenance fee capped at 2% of assets, but a management fee of 0.5% of
21 assets and a performance fee of 15% of gains “on a twice yearly basis only if said returns are realized by the closure of trades,
distribution of cash from partnership and LLC interests or otherwise tangibly acquired by the company.” Kenyon Capital’s
performance appears to have come primarily from unrealized gains based on the Brogs’ own asset valuations, rather than realized
gains, but the Brogs do not appear to have made this distinction when calculating performance fees.

1 below, Kenyon Capital's operating agreement with investors allows for a maintenance fee of 2% of fund
2 assets to be used for business expenses (not for personal use by the Brogs). Based on the purported size of
3 Kenyon Capital's asset base at the end of 2016 and 2017 (approximately \$1.11 million and \$1.46 million
4 respectively), the Division estimates that this fee would total no more than \$50,000 for both years combined.
5 Kenyon Capital paid \$144,902.91, nearly triple that amount, to American Express.³

6 12. In addition to the American Express payments, Shaun and Ryan Brog both regularly withdrew
7 money from Kenyon Capital's account at ATMs, took advances on the Visa card connected to Kenyon
8 Capital's account, and wrote checks to themselves from Kenyon Capital's account. These expenditures totaled
9 \$148,874.26, specifically including:

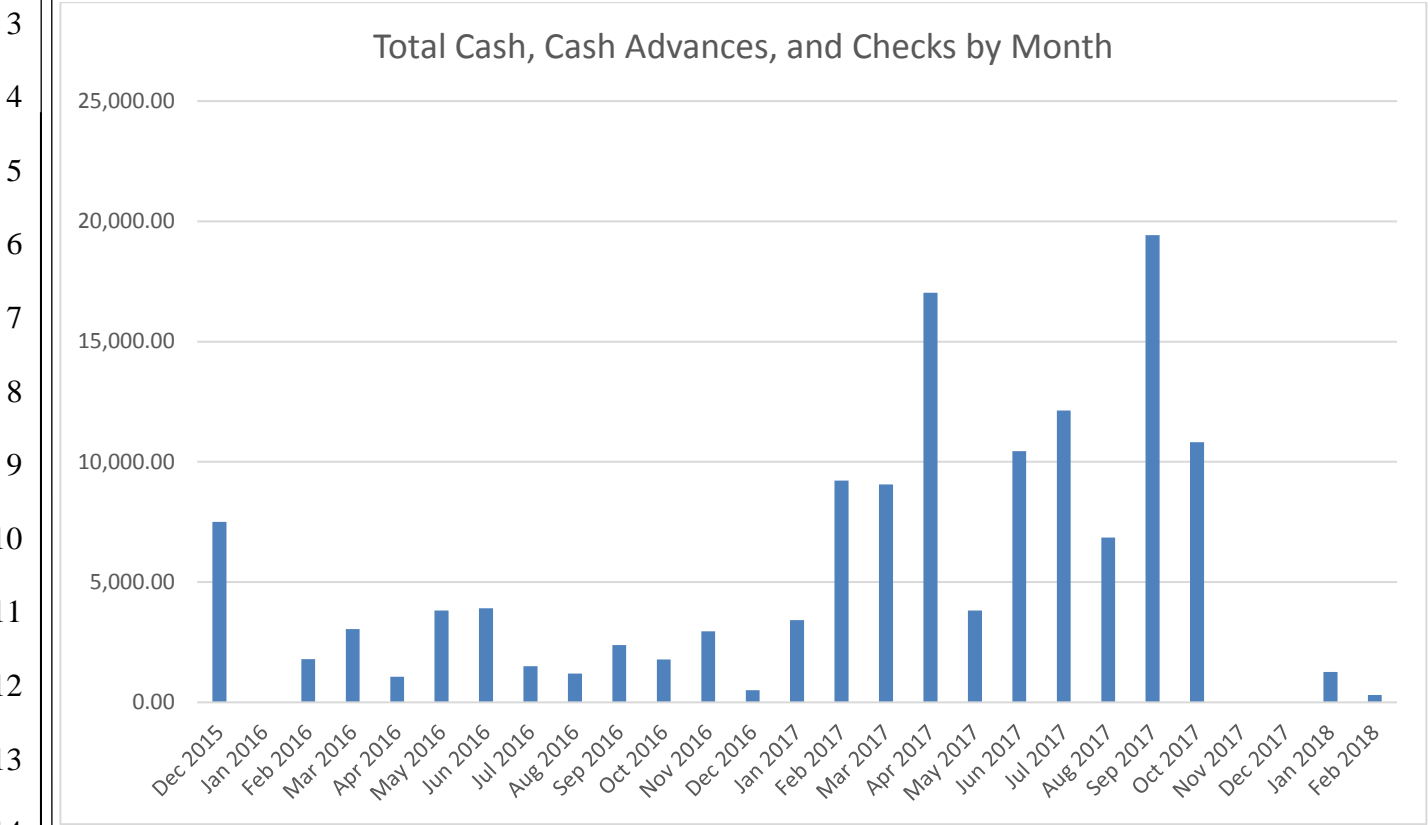
- 10 a. \$72,419.26 in ATM withdrawals by Shaun Brog;
- 11 b. \$27,135.00 in ATM withdrawals by Ryan Brog;
- 12 c. \$7,950 in checks to Shaun Brog;
- 13 d. \$32,620.00 in checks to Ryan Brog;⁴
- 14 e. \$3,000 in Visa cash advances to Shaun Brog;
- 15 f. \$5,750.00 in Visa cash advances to Ryan Brog;

16 The Brogs often made multiple ATM withdrawals in the same day for hundreds of dollars, particularly in the
17 latter part of 2017. These withdrawals substantially increased in early 2017, shortly after the Brogs received
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19 ³ It is likely that some of this amount represents investments by the fund, rather than general business expenses. The Brogs
20 represented to the Division that \$9,800 was spent on wine investments in 2016 out of \$51,693.77 in total spending on the American
Express card.

21 ⁴ Ryan Brog wrote a total of \$5,225 in checks to Kenyon Capital during the relevant period, for a net amount of \$27,395.

1 an inquiry from the Securities and Exchange Commission about the fund. The chart below shows the
2 combined monthly amounts withdrawn by the Brogs from December 2015 to February 2018.



13. In addition to the cash, cash advances, and checks, the Brogs also spent other money directly
15 from Kenyon Capital’s account on what appear to be personal uses. These expenditures, totaling \$48,166.38,
16 include but are not necessarily limited to:

- 18 a. A net total of \$27,438.14 in transfers to a Scottrade account in Ryan Brog’s name (\$60,360
19 from Kenyon Capital to the Scottrade account and \$32,921.82 in transfers from the
20 Scottrade account to Kenyon Capital)
- 21 b. \$11,037.50 in apartment rent; and

1 c. \$9,690.74 on retail and services.

2 14. The Brogs first overdrew Kenyon Capital's Merrill Lynch account in July 2017, and repeatedly
3 overdrew the account on at least five separate occasions during the remainder of 2017. The Brogs generally
4 repaid overdrafts within a day or two. However, in late October 2017, the Brogs overdrew Kenyon Capital's
5 account by \$1,268.53, and did not fully repay the overdraft until approximately two months later. The Brogs
6 also incurred approximately 102 separate returned-check fees, totaling over \$2,000, between July 2017 and
7 January 2018.

8 15. As of the end of February 2018, Kenyon Capital's Merrill Lynch account was overdrawn by
9 \$100. An existing investor in the fund invested an additional \$15,000 approximately two weeks later. The
10 Respondents failed to disclose the fund's financial status and low levels of working capital to that investor
11 before the March 2018 investment.

12 Kenyon Capital's Improper Fees and Salary Payments

13 16. As described above, Kenyon Capital's operating agreement provided that the fund would
14 charge investors three different types of fees: a maintenance fee for the fund's business expenses, a
15 management fee of 0.75% of fund assets, and a performance fee of 15-20% of the fund's annual gains.
16 Additionally, the Respondents represented to the Division that Ryan Brog was paid a "salary" of \$1,000 per
17 month for 2016.

18 17. The Respondents represented to the Division that Shaun and Ryan Brog were collectively paid
19 \$16,935 in performance fees for 2015, and \$46,144 in performance fees for 2016.⁵ However, the numbers

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21 ⁵ It is unclear when Kenyon Capital and the Brogs calculated these fees or authorized Ryan Brog's salary because the documents
provided to the Division are undated and Shaun Brog failed to appear for testimony.

1 which the Respondents provided for their performance fees and for Ryan Brog's salary bear no relation to
2 their actual withdrawals from the fund's accounts. Rather than withdrawing management and performance
3 fees in a lump sum at the end of the quarter or year, as is standard industry practice, the Brogs simply made
4 personal expenditures, wrote themselves checks, and withdrew cash directly from Kenyon Capital's Merrill
5 Lynch account at their discretion, without notifying investors that they were taking fees. To the extent that
6 the Brogs' expenditures and withdrawals from the fund accounts can be attributed to performance fees or
7 Ryan Brog's salary, these forms of compensation violated either Washington law or Kenyon Capital's
8 operating agreement with investors.

9 18. First, the Respondents entered into contracts with investors which contained performance fees
10 prohibited by Washington law. Investment advisers may charge fees based on a percentage of assets under
11 management, but may not enter into a contract to charge the client a percentage of the gains received unless
12 the client meets the definition of a "qualified client" as provided in WAC 460-24A-150. For example, if an
13 adviser's client had a portfolio of \$500,000, the adviser could charge the client a fee of 1% of the assets under
14 management, i.e. \$5,000. However, if the portfolio gained in value by \$50,000 for the year, the adviser could
15 not charge the client a fee based directly on those gains, unless they were a qualified client.⁶ As a result,
16 private funds are often open only to qualified clients, so that the fund adviser can charge both performance
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20 ⁶ To be a qualified client, an investor generally must have at least one million dollars managed by the adviser, or have a total net
21 worth of at least \$2.1 million excluding their primary residence. A high-level director or manager of the investment adviser, or a
lower-level employee of the adviser who participates in the investment activities of the fund, can also be a qualified client.

1 fees and assets under management fees without the additional administrative issues of determining which fees
2 can be charged to which investors.⁷

3 19. Although the Respondents asked investors whether they were “accredited investors,” they did
4 not inquire whether Kenyon Capital’s investors were qualified clients. The net worth threshold for qualified
5 clients is currently \$2.1 million not including the investor’s primary residence, double the \$1 million threshold
6 for accredited investors.⁸ Thus, an investor can be an accredited investor without being a qualified client if
7 their net worth falls between \$1 million and \$2.1 million. Of the fund’s 22 investors, at least 14 were neither
8 accredited investors nor qualified clients; it is unknown whether the remainder (who were accredited
9 investors) were also qualified clients. Despite Kenyon Capital and the Brogs’ lack of information about
10 whether their investors were qualified clients, all of the fund’s contracts with investors included the
11 performance-based fees described above.

12 20. In April 2017, after examining Kenyon Capital’s fee structure, the Division sent a warning
13 letter to Kenyon Capital and the Brogs, cautioning them (among other things) that their performance fees
14 likely violated Washington law. Rather than reducing their ATM withdrawals and personal expenditures from
15 the fund account, the Brogs significantly increased them. As detailed above, over half of the cash, cash
16 advances and check withdrawals by the Brogs were made between April 2017 and October 2017.

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⁷ For instance, in a “2-and-20” structure, the adviser charges a management fee of 2% of assets under management, and a
20 performance fee of 20% of the gains over a certain period, as defined in their contract with investors. The specific numbers vary
depending on the fund.

21 ⁸ The threshold was increased from \$2 million on August 15, 2016.

1 convertible notes in early-stage small businesses, wine, silver, and personal loans. The Respondents marketed
2 this strategy to investors as offering low correlation with financial markets and the potential for better returns.
3 In their marketing materials, they claimed to have achieved a 34% return over the S&P 500 from 2012 to
4 2015.¹⁰

5 23. Because most of Kenyon Capital's assets are not regularly traded in financial markets, they are
6 generally more difficult to value than more traditional assets such as stocks or bonds which can easily be
7 valued by reference to their recent trading prices. Shaun and Ryan Brog considered having an auditor examine
8 the fund, but found that due to the nature of the fund's assets, the auditors' fees would range from \$25,000 to
9 \$40,000, which they considered prohibitively expensive given the size of the fund. As a result, for most of
10 Kenyon Capital's holdings, both the fund and its investors relied on Shaun and Ryan Brog to value the assets
11 using their own financial models. Because Shaun and Ryan Brog's compensation depended on the asset value
12 of the fund and on the fund's gains, this reliance created a substantial conflict of interest. The Respondents
13 failed to disclose this conflict of interest to investors. The Respondents also failed to disclose to at least one
14 investor that the historical return figures they presented had not been audited like most private funds would
15 have been, and that an audit to independently verify the fund's purported asset values would likely be
16 prohibitively expensive for the foreseeable future.¹¹

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19 ¹⁰ These claims were tied to the performance of the predecessor fund, Kenyon Capital NY, not to the Washington entity which is a
respondent in this matter.

20 ¹¹ Although the fund purportedly established a "Valuation Oversight Committee" in early 2017 to verify asset values, the
21 committee consisted entirely of investors in the fund, who also had a conflict of interest because they could have incentives to push
for different valuations depending on their personal interests.

1 to postpone the testimony to the following week and attempted to confirm a new date, but Shaun Brog again
2 requested a postponement the day before the rescheduled testimony, claiming that the Division's confirmation
3 emails had gone into his spam folder.¹² The Division attempted to reschedule the testimony for February 2018,
4 but Shaun Brog failed to reply to followup attempts, by email, phone, and letter, to arrange a new testimony
5 date. During the time the Division was attempting to schedule Shaun Brog's testimony, Kenyon Capital's
6 account balance was consistently overdrawn or near zero. As a result of Shaun Brog's failure to appear for
7 testimony, the Division was unable to clarify remaining issues relating to the Respondents' fees, their use of
8 funds, their valuation models, and the disclosures they made to investors.

9 Based upon the above Tentative Findings of Fact, the following Conclusions of Law are made:

10 **CONCLUSIONS OF LAW**

- 11 1. The offer and sale of the LLC interests in Kenyon Capital, as described above, constituted the
12 offer and sale of securities as defined in RCW 21.20.005(14) and (17).
- 13 2. Shaun Brog and Ryan Brog, as described above, engaged in the business of advising Kenyon
14 Capital as to the value of securities and the advisability of investing in, purchasing, or selling securities, and
15 are therefore investment advisers as defined in RCW 21.20.005(8).
- 16 3. Kenyon Capital, Shaun Brog, and Ryan Brog violated RCW 21.20.010(2), because, as set forth
17 in the Tentative Findings of Fact, in connection with the offer and sale of LLC interests in Kenyon Capital,
18 they made untrue statements of material fact or omitted to state material facts necessary to make the statements
19 made, in light of the circumstances in which they were made, not misleading.

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21 ¹² It is unclear why these emails would have been filtered as spam, given that the Division was replying to an email from two days
earlier, in the same email chain, and had previously exchanged a substantial volume of email correspondence with Shaun Brog.

1 4. Kenyon Capital, Shaun Brog, and Ryan Brog violated RCW 21.20.010(3), because, as set forth
2 in the Tentative Findings of Fact, in connection with the offer and sale of LLC interests in Kenyon Capital,
3 they engaged in an act, practice, or course of business which operated as a fraud on Kenyon Capital’s investors
4 by using Kenyon Capital’s funds for personal purposes, making business expenditures which substantially
5 exceeded the amounts allowed by the operating agreement with investors, and repeatedly overdrafting the
6 fund’s account as a result.

7 5. Shaun and Ryan Brog violated RCW 21.20.020 by engaging in an act, practice, or course of
8 business which operated as a fraud on their investors by failing to comply with the requirements of:

- 9 a. WAC 460-24A-105, by failing to engage either a qualified custodian to send account
10 statements to clients or an independent CPA to verify client funds and securities;
- 11 b. WAC 460-24A-106, by failing to provide itemized invoices to clients or provide notice to
12 the qualified custodian of any fee deductions;
- 13 c. WAC 460-24A-107, by failing either to engage an independent party to authorize
14 withdrawals from Kenyon Capital’s pooled account, or to provide audited financial
15 statements for the fund to all investors.

16 6. Shaun and Ryan Brog violated RCW 21.20.030 by entering into investment advisory contracts
17 which failed to provide in writing that they would not be compensated on the basis of a share of capital gains
18 upon or capital appreciation of client funds for non-qualified clients.

19 7. Shaun and Ryan Brog violated RCW 21.20.040 by acting as investment advisers to Kenyon
20 Capital while unregistered to do so in the state of Washington, and by acting as securities salespersons for
21 interests in Kenyon Capital while unregistered as such in the state of Washington.

1 8. Kenyon Capital, and Shaun and Ryan Brog, violated RCW 21.20.140, because, as set forth in
2 the Tentative Findings of Fact, they offered and sold securities for which no registration is on file with the
3 Securities Administrator.

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5 **NOTICE OF INTENT TO ORDER THE RESPONDENTS TO CEASE AND DESIST**

6 Based upon the above Tentative Findings of Fact and Conclusions of Law, the Securities
7 Administrator intends to order, pursuant to RCW 21.20.390(1), that Respondents Kenyon Capital Investment
8 Holdings LLC, Shaun and Ryan Brog, and their agents and employees, each shall cease and desist from
9 violations of RCW 21.20.010 and RCW 21.20.140, and that Respondents Shaun and Ryan Brog, and their
10 agents and employees, each shall cease and desist from violations of RCW 21.20.040, RCW 21.20.030, and
11 RCW 21.20.020.

12 **NOTICE OF INTENT TO IMPOSE FINES**

13 Pursuant to RCW 21.20.395, and based upon the Tentative Findings of Fact and Conclusions of Law,
14 the Securities Administrator intends to order that Respondents Kenyon Capital Investment Holdings LLC,
15 Shaun Brog, and Ryan Brog shall be jointly and severally liable for and shall pay a fine of \$200,000.

16 **NOTICE OF INTENT TO CHARGE COSTS**

17 Pursuant to RCW 21.20.390, and based upon the Tentative Findings of Fact and Conclusions of Law,
18 the Securities Administrator intends to order that Respondents Kenyon Capital Investment Holdings LLC,
19 Shaun Brog, and Ryan Brog shall be jointly liable for and shall pay the costs, fees, and other expenses incurred
20 in the administrative investigation and hearing of this matter, in an amount not less than \$20,000.

21 **NOTICE OF INTENT TO DENY FUTURE REGISTRATION**

1 Pursuant to RCW 21.20.110(1), and based upon the above Tentative Findings of Fact and Conclusions
2 of Law, the Securities Administrator intends to order that any future application for securities salesperson,
3 broker-dealer, investment adviser, or investment adviser representation registration of Respondents Kenyon
4 Capital Investment Holdings LLC, Shaun Brog, or Ryan Brog, shall be denied.

5 **AUTHORITY AND PROCEDURE**

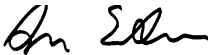
6 This Statement of Charges is entered pursuant to the provisions of Chapter 21.20 RCW and is subject
7 to the provisions of Chapter 34.05 RCW. The Respondents, Kenyon Capital Investment Holdings LLC, Shaun
8 Brog, and Ryan Brog may each make a written request for a hearing as set forth in the NOTICE OF
9 OPPORTUNITY TO DEFEND AND OPPORTUNITY FOR HEARING accompanying this Order. If a
10 Respondent does not make a hearing request in the time allowed, the Securities Administrator intends to adopt
11 the above Tentative Findings of Fact and Conclusions of Law as final and to enter a permanent order to cease
12 and desist as to that Respondent, to impose any fines sought against that respondent, and to charge any costs
13 sought against that Respondent.

14 Signed and Entered this 3rd day of August, 2018.

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18 William M. Beatty
Securities Administrator

19 Approved by:

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Presented by:

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Suzanne Sarason
Chief of Enforcement

Adam N. Yeaton
Financial Legal Examiner

Reviewed by:



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Financial Legal Examiner Supervisor