

BEFORE THE SECURITIES COMMISSIONER
STATE OF COLORADO

Case No. 2024-CDS-006

CONSENT ORDER

IN THE MATTER OF VAILSHIRE CAPITAL MANAGEMENT, LLC. AND JEFFREY
ROSS,

Respondents.

THIS MATTER is before Tung Chan, Securities Commissioner for the State of Colorado ("Commissioner"), on the Stipulation for Consent Order ("Stipulation") between the Staff of the Colorado Division of Securities (the division, "Division" and the staff, "Staff") and Vailshire Capital Management, LLC (IARD #169132) and Jeffrey Ross (CRD #6249794) (collectively, "Respondents"). After reviewing the Stipulation and grounds therein, the Commissioner makes the following Findings and enters the order as follows:

FINDINGS

1. The Commissioner has jurisdiction over the Respondents and this matter pursuant to the provisions of the Colorado Securities Act, §§ 11-51-101 through 803, C.R.S.
2. By entering into the Stipulation, Respondents waive the following rights: (1) to have a formal hearing pursuant to §§ 11-51-606(1), 24-4-104 and 24-4-105, C.R.S.; (2) to be represented by counsel in that action; (3) to present a defense through oral or documentary evidence; (4) to cross-examine witnesses at such hearing; and (5) to seek judicial review of the Consent Order as provided in §§ 11-51-607 and 24-4-106, C.R.S.
3. Respondents further waive the findings required by § 11-51-410(1), C.R.S. and do not contest that pursuant to § 11-51-704(2), C.R.S. entry of this Consent Order is necessary and appropriate in the public interest and is consistent with the purposes of the Colorado Securities Act.

ORDER

NOW, THEREFORE, based on the foregoing, it is ORDERED as follows:

1. The terms of the attached Stipulation are incorporated and made a part of this Consent Order.
2. Respondents shall comply with all agreements, undertakings, and directives contained in the Stipulation, to the extent any such agreements, undertakings, or directives remain unsatisfied on the date of this Consent Order.
3. Respondents Vailshire Capital Management, LLC. and Jeffrey Ross will voluntarily withdraw their respective registrations as investment adviser and investment adviser representative with the State of Colorado within ninety (90) days of the execution of the Consent Order. Respondents will also complete additional required compliance action items and provide required Reports to the Division as described in the Stipulation.
4. The Commissioner shall retain jurisdiction over this action to ensure Respondents' compliance with this Consent Order and reserves the power to enter additional orders as needed to ensure the compliance by the Respondents with this Consent Order.
5. In the event Respondents fail to comply with any of the terms or conditions set forth in this Stipulation or the Consent Order, the Commissioner or the Staff, in their sole discretion, may initiate formal enforcement proceedings against Respondents for such noncompliance. The Stipulation and this Consent Order shall be admissible as evidence in any such proceeding.
6. This Consent Order, and the terms and conditions herein, shall be binding on all successors and assigns.

DATE: May 28, 2024



Tung Chan
Securities Commissioner

BEFORE THE SECURITIES COMMISSIONER
STATE OF COLORADO

Case No. 2024-CDS-006

STIPULATION FOR CONSENT ORDER

IN THE MATTER OF VAILSHIRE CAPITAL MANAGEMENT, LLC. AND JEFFREY
ROSS,

Respondents.

The Staff of the Colorado Division of Securities (the staff, “Staff” and the division, the “Division”) and Respondents Vailshire Capital Management, LLC and Jeffrey Ross (collectively, “Respondents”) hereby enter into this Stipulation for Consent Order (the “Stipulation”) in this matter as follows:

I. Background

1. The Staff conducted an examination of Respondents pursuant to § 11-51- 409, C.R.S.
2. As a result of its examination, the Staff alleges that Respondents engaged in the following conduct:
 - a. Vailshire Capital Management, LLC. (IARD #169132) (“Vailshire” or the “Firm”), is a Colorado limited liability company with its principal place of business located at 3835 Edgecliff Court, Colorado Springs, CO 80904.
 - b. Vailshire Capital Management, LLC., has been licensed in Colorado as an investment adviser since at least January 02, 2014. The Firm manages approximately \$31,000,000 of clients’ assets on a discretionary basis as of February 2024.
 - c. Jeffrey Ross (“Ross”) (CRD #6249794) has been licensed in Colorado as an investment adviser representative with Vailshire, since at least January

- d. 02, 2014, and is currently the managing director and chief compliance officer of Vailshire.
- e. Vailshire and Ross manage a pooled investment vehicle, the Vailshire Partners, LP (the "Fund"), and also provide asset management to clients with separately managed accounts ("SMA"), serving approximately 140 individual clients. The Firm utilizes Interactive Brokers ("IB") as the custodian for clients' funds and securities.
- f. Before starting an advisory relationship, Vailshire and Ross did not provide SMA clients a written disclosure brochure, the Form ADV Part 2, ("brochure") or provide, on an annual basis, a summary of material changes and offer to provide an updated copy of the brochure as required by § 11-51-409.5 and Rule 51-4.7.
- g. Vailshire and Ross entered an Investment Management Agreement ("IMA") with clients. The IMA included an Exhibit A document titled, "Investment Objective," and an Exhibit A-1 document titled "Client Suitability Questionnaire."
- h. The IMA Investment Objective was provided to all clients and stated "...The Adviser seeks to create growing, long-term value by acquiring a diversified core of under-appreciated assets while simultaneously selling safe options to reduce risk and profit from volatility. Under appreciated assets may include U.S. and international equities, bonds, ETFs, other funds, REITs, and MLPs. A core of market-dominating, stable, "blue chip" or similar stocks will be used for the frequent selling of puts and calls to benefit from market volatility by collecting current income. Leverage will generally be avoided." The Firm's filed brochure stated substantially the same investment strategy.
- i. The Staff requested the IMA Client Suitability Questionnaires for 19 specific clients. The Firm was unable to produce questionnaires for 8 of the 19 clients and several of the questionnaires were missing essential information such as "risk tolerance" or indicated a net worth of only "\$10,000," though the account size was substantially larger.
- j. Firm clients also had to complete a custodian application with Interactive Brokers ("IB"). The IB application included a risk profile form. In

establishing clients' custodian accounts, Ross pre-filled the form with his trading experience and, in some cases, directed clients on the selections to fill in. Ross, in response to one client who was not granted the trading permission for complex and leveraged exchange traded products, directed the client to "...adjust your income/net worth higher and (importantly) DO NOT select "Preservation of Capital" as one of the investment objectives."

- k. Vailshire and Ross directed SMA clients to adjust their income and net worth responses higher, avoid selecting "preservation of capital" or "income generation" as the investment objective, and to answer the suitability questionnaire based on the Firm's trading experience, instead of the clients' risk tolerance, in order to allow the Firm to recommend higher risk products including inverse and leveraged ETFs and cryptocurrency proxies. In the Firm's January 2023 update, sent to SMA clients, it stated that with the "trading and investing limitations of our Conservative accounts, I am not able to actively hedge these portfolios." But "those 'Conservative' clients who wish to be more aggressively hedged against anticipated declines in the equities markets, you will need to log into your Vailshire account(s) at Interactive Brokers and apply for trading privileges in 'leveraged or complex exchange traded products.'"
- l. The Staff found that Vailshire and Ross provided recommendations to some clients to purchase, sell, or exchange a security based on inaccurate suitability information provided to IB and the permissions approved by the client instead of suitability information furnished by the client after a reasonable inquiry concerning the client's investment objectives, financial situation and needs in violation of Rule 51- 4.8(IA)(A).
- m. Vailshire and Ross's actual strategy included recommendations for most SMA clients to purchase a high concentration of high risk and complex products including cryptocurrency focused investments such as cryptocurrency proxies (Bitcoin and Ether trusts) and crypto mining companies as well as Inverse/Leveraged ETFs ("Firm Strategy").
- n. The Firm began to trade cryptocurrency proxies as early as Q4 2019 on behalf of the Fund and SMA clients. The proxies included Bitcoin and Ether trusts ("cryptocurrency trusts") and other investments with a high sector allocation in blockchain and cryptocurrencies. The Firm sent an email update to clients in late 2019 about Bitcoin, which email discussed the benefits of holding some Bitcoin investments. The notice did not

discuss corresponding risks or include any disclaimers about suitability (other than Bitcoin is “highly volatile”) and it did not address cryptocurrency trusts. In emails with clients the Firm represented that the trusts were the equivalent of holding cryptocurrencies “direct.” Digital asset-related trades were not discussed in any Firm brochures (filed, but not provided to SMA clients) until the Firm’s March 2023 annual updates or in any email communications reviewed by Staff.

- o. Cryptocurrency trusts generally allow investors to trade shares in trusts holding large pools of cryptocurrencies. Cryptocurrency trusts involve significant and unusual risks, including but not limited to, significant volatility based on the underlying asset; the price of trust shares (NAV) can trade at a discount or premium to the price of the cryptocurrency, only roughly tracking the price; and trusts are traded within limited hours and the stated object is to reflect value at a specific time of the day.
- p. Similarly, the Firm in 2020 and 2021 for the Fund and in 2022 for both SMAs and the Fund, purchased Inverse/Leveraged ETFs. The Firm purchased sixteen different Inverse/Leveraged ETFs, such as ProShares Short Bitcoin Strategy ETF (BITI), ProShares Ultra QQQ (QLD), ProShares UltraPro QQQ (TQQQ), ProShares UltraPro Short QQQ ETF (SQQQ), or Tuttle Capital Short Innovation Daily ETF (SARK) (collectively, the “Inverse/Leveraged ETFs”). All of the Inverse/Leveraged ETFs recommended were designed to achieve their stated objective on a daily basis. In many cases, the products were held for up to 3.5 months. Inverse/Leveraged ETFs were not discussed in any Firm brochures (filed, but not provided to SMA clients) and in email communications to clients. Vailshire and Ross explained to clients that the Firm’s use of inverse and/or leveraged ETFs was to act as a “hedge” without discussing the corresponding risks.
- q. Inverse and/or leveraged ETFs are complex investment products of which the risks are not properly understood by non- institutional investors. Some ETFs are designed to invest as if the investor is using borrowed funds (known as “leveraged ETFs”) which deliver multiples of the daily performance of the index or benchmark that it tracks. Most leveraged ETFs reset each day, which means they are designed to achieve their stated objective on a daily basis.

- r. One of the risks associated with leveraged ETFs is the compounding over time of the daily returns that ETFs are designed to achieve (“compounding risk”), which can create unpredictable returns even when they successfully achieve their stated daily objective day after day. When held for periods longer than one day, volatility present in the index the leveraged ETF tracks skews the overall returns, when the index or sector moves in the general direction the purchaser predicted or expected. The greater the volatility in the market during the time of holding the fund, the more likely the leveraged ETF will produce an extreme or unpredictable result.
- s. The Securities and Exchange Commission and FINRA have released numerous investor alerts that explain the risks associated with longer holding periods including that the performance over longer periods may differ significantly from the performance of the underlying benchmark during the same time period. (See <https://www.sec.gov/investor/pubs/leveragedetfs-alert>).
- t. The Staffs’ review showed that the Firm’s strategy, specifically at the end of July 2022, included a significant number of clients holding only Inverse/Leveraged ETFs in their accounts, in some cases for as long as 2-3 months with an average holding period of approximately three weeks. The holdings in client accounts included a combination of ProShares Short Bitcoin Strategy ETF (BITI) and ProShares UltraPro Short QQQ ETF (SQQQ). ProShares states in their investment objective that “...the Fund does not seek to achieve its stated investment objective over a period of time greater than a single day.” For the clients holding Inverse/Leveraged ETFs only, the holdings made up around 18% of their account value, the rest was cash. The stated objective of the BITI ETF is to seek daily investment results that correspond to the inverse (-1x) of the daily performance of a Bitcoin Index on a daily basis. The stated purpose of the SQQQ is to seek daily investment results that correspond to three times the inverse of the daily performance of the NASDAQ-100. Other clients were holding only one cryptocurrency focused stock (MicroStrategy Incorporated (MSTR) in their accounts. For clients with MSTR holdings, they made up close to 95% of the account. Some of these accounts were traditional/rollover IRA and Roth IRA accounts.
- u. This Firm Strategy and its associated risks were very different than that disclosed to clients and potential clients in the Firm’s brochure and IMA Investment Objective, which stated that the Firm would acquire a

“diversified core of under-appreciated assets while simultaneously selling safe options to reduce risk and profit from volatility, ” and that “... leverage will generally be avoided” and in client communications where the Firm stated it would use Inverse/Leveraged ETFs as a “hedge” without disclosing any risks. The Firm failed to disclose or made inaccurate disclosure in several material areas including:

- i. The Firm’s method of analysis and investment strategies included recommending cryptocurrency focused investments as well as Inverse/Leveraged ETFs that were held substantially longer than one day.
- ii. That the Firm did not always use a “diversified core” or assets, but sometimes put clients in highly concentrated positions that included only a few Inverse/Leveraged ETFs or a single cryptocurrency sector stock.
- iii. That the Firm did not use safe options to reduce risk, but instead relied on Inverse/Leveraged ETFs as a “hedge.”
- iv. That the Firm’s use of Inverse/Leveraged ETFs was not in fact a hedge when the only other holdings in the account were cash and an (-1x) inverse bitcoin ETF and (-3x) inverse stock market index. The Firm’s strategy was to short the market.
- v. That the cryptocurrency and ETF products that the Firm recommended involved substantial and unusual risks.
- vi. Vailshire and Ross in disclosing the Firm’s investment strategy and associated risks did not meet their affirmative obligation to employ reasonable care to avoid misleading and provide full and fair disclosure of all material facts in violation of Rule 51- 4.8(IA)(A).

Based on this alleged conduct, the Staff alleges that Respondents have willfully violated or willfully failed to comply with provisions of the Colorado Securities Act and rules thereunder, and pursuant to § 11-51-410(1)(b), C.R.S., an appropriate sanction is warranted.

II. Stipulation

The Staff and Respondents, in order to resolve this matter without formal hearing, hereby enter into this Stipulation for Consent Order in this matter and Respondents and the Staff hereby stipulate as follows:

1. The Securities Commissioner for the State of Colorado has jurisdiction over the Respondents and the subject matter of this action.
2. Respondents agree to the entry of a Consent Order in the form attached (the "Consent Order") and incorporated herein by reference.
3. Following entry of this Consent Order, Respondents will voluntarily withdraw their respective registrations as investment adviser and investment adviser representative with the State of Colorado within ninety (90) days of the execution of the Consent Order. Following such withdrawal, Vailshire shall act as an exempt reporting adviser and manage only the Fund (and may manage other private funds in the future), pursuant to Rule 704-1-51-4.11(IA),
4. The Staff agrees that the Respondents' withdrawal of their respective registrations is wholly voluntary and nothing in this Consent Order shall be viewed as a denial, suspension, revocation, restriction, or bar from licensure with the State of the Colorado, and that Respondents may apply for registration with the State of Colorado at any point in the future.
5. Respondents agree to the following:
 - a. Respondents agree to fully comply with all Fund-related items applicable to an exempt reporting adviser in the Division deficiency letter dated April 19, 2024 ("deficiency letter").
 - b. Respondents shall submit a written report to the Division detailing all actions taken to comply with this Stipulation and Consent Order within sixty (60) days of execution of the Order ("Report"). Respondents agree to reconcile contributions to the Fund's Interactive Brokers ("IB") account as identified in the deficiency letter. Respondents shall review the Fund's equity holdings and identify the origin and nature of the differences highlighted in the deficiency letter. The Firm's assessment, as well as supporting documentation, shall be delivered to the Division as part of the required Report.

- c. Respondents agree to update Ross' Form U-4 as required by the Division deficiency letter and update the Firm's Form ADV and Ross's Form U-4 to disclose this Order before filing to withdraw their respective licenses. Detail the filings made in the required Report.
- d. Respondents agree to determine whether each beneficial owner/investor of the fund was a qualified client at the time of purchase. The review shall include all beneficial owners/investors that have made a purchase from inception of the fund. If a beneficial owner/investor was not a qualified client at the time of purchase, the Respondents agree to return to the beneficial owner/investor the total value of the beneficial owner's original investment plus any gains. The required Report shall include documentation verifying the qualified client status or non-qualified client status of each beneficial owner/investor and documentation that evidences return of an initial investment plus any gains to a beneficial owner/investor that was not a qualified client at the time of purchase.
- e. Respondents agree to provide written notification to all Firm clients that they will no longer be providing investment advisory services or investment advice because Respondents will be withdrawing their Colorado investment adviser representative and investment adviser licenses. The firm shall maintain documentation the written notification was sent to each client and the written notification was received by each client. The written notification should explain the reason(s) for the withdrawals, give all clients updated account information, provide the current custodian's contact information, and instruct the clients on who to contact regarding their accounts prior to and after the Respondents withdraw their licenses. The written notification shall be sent, along with a copy of this Stipulation and Consent Order, to all clients within forty-five (45) days of the execution of the Consent Order. Respondents will maintain documentation of timely delivery and provide copies of the documentation with the required Report to the Division.
- f. Respondents agree to comply with the Consent Order 2024-CDS-006, and develop all required policies and procedures to ensure compliance with the Colorado Securities Act and rules thereunder that are applicable to an exempt reporting adviser.

- g. Respondents will give the Division written notice they are filing their Form ADV-W and Form U-5 at least seven (7) business days prior to making the filing.
 - h. Respondents agree to provide the Division with a second written report ("Second Report") within one (1) year of withdrawal of the licenses, describing how management of the Fund or other private funds complies with all sections of Rule 704-1-51-4.11(IA) (the "rule"). If the Respondents have not complied with specific sections of the rule, the Second Report shall describe the reason(s) why the Respondents have not complied with those rule sections. The Second Report shall be accompanied by documentation that demonstrates compliance with the rule and shall include, copies of all required filings for the fund or other private funds, copies of all disclosures provided to beneficial owners of the fund or other private funds, a copy of the most recent annual audited financial statements for each fund or other private funds, and documentation that verifies each beneficial owner was a qualified client at the time of purchase.
6. Respondents understand that they have the following rights: (1) to have a formal hearing pursuant to § 11-51-606(1), C.R.S.; (2) to be represented by counsel in that action; (3) to present a defense through oral or documentary evidence; (4) to cross-examine witnesses at such hearing; and (5) to seek judicial review of the Consent Order as provided in §§ 11-51-607 and 24-4-106, C.R.S. By entering into this Stipulation, Respondents expressly waive the rights set forth in this paragraph.
7. Respondents acknowledge that they have entered into this Stipulation voluntarily, after the opportunity to consult with counsel, and with the understanding of the legal consequences of this Stipulation and Consent Order.
8. Respondents hereby waive the findings required by § 11-51-410(1), C.R.S.; and pursuant to § 11-51-704(2), C.R.S., Respondents do not contest that the entry of a Consent Order is necessary and appropriate in the public interest and is consistent with the purposes and provisions of the Colorado Securities Act.
9. Respondents agree that the entry of the Consent Order is a disciplinary event that is material to a client's or prospective client's evaluation of their advisory business or the integrity of its management and must disclose the event in required filings and disclosure documents.

10. By consenting to the entry of the Consent Order, Respondents agree not to take any action or to make, or permit to be made, any public statement denying, directly or indirectly, any Finding or Conclusion in the Consent Order or creating the impression that said Consent Order lacks a factual basis
11. Respondents further acknowledge that any violation of the Consent Order, when issued, may constitute grounds for further sanctions and formal proceedings against them for such violations.
12. This Stipulation is subject to approval by the Securities Commissioner and shall become binding upon the parties hereto upon such approval.

BY RESPONDENTS:

Jeffrey Ross:

Jeff Ross

Individually

Vailshire Capital Management, LLC.:

BY Jeff Ross:
Jeffrey Ross, Managing Director and Chief Compliance Officer

BY THE STAFF OF THE DIVISION OF SECURITIES:

Jeffrey S. Eaby

Jeffrey S. Eaby
Deputy Commissioner

May 28, 2024

Date