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DFI 2,55 - INVESTMENT
ADVISOR - REQUIREMENT 98-114



State of Wisconsin
Department of Financial Institutions

Tommy G. Thompson, Governor

Richard L. Dean, Secretary

July 7, 1998

Joint Committee for Review
of Administrative Rules
✓ c/o Senate Co-Chair Robert Welch
1 East Main St. Room 201
Madison WI 53702
c/o Assembly Co-Chair Glenn Grothman
125 West Capitol
Madison WI 53702

JUL 07

Re: Filing of Copy of Order Adopting Emergency Rules/
DFI-Sec Rules of the Division of Securities

Dear JCRAR Co-Chairs:

Pursuant to the statutory requirements in Chapter 227, Wis. Stats., for adopting emergency rules, a copy is herewith filed with the Co-Chairs of the JCRAR of an Order Adopting Emergency Rules issued by this Division as published in the official state newspaper on this date, July 7, 1998, for subsequent effectiveness on July 9, 1998. Certified copies are being concurrently filed with the Secretary of State and the Revisor of Statutes, and copies are also being filed with the Chief Clerk of each house of the legislature. Additionally, the Senate Sergeant-at-Arms and the Assembly Sergeant-at-Arms have been provided with sufficient copies of the Order, together with a cover memo and fiscal estimate, to make the required distribution under sec. 227.24(3), Wis Stats., of the materials to all members of the legislature.

If you have any comments or questions, please call me at 266-3414.

Very truly yours,


Randall E. Schumann
Legal Counsel for the Division

RES
enclosure
cc: Patricia D. Struck, Division Administrator



ORDER OF THE
DEPARTMENT OF FINANCIAL INSTITUTIONS
DIVISION OF SECURITIES
STATE OF WISCONSIN
ADOPTING EMERGENCY RULES

To repeal 2.01(3)(a) to (d), 2.02(9)(a) and (L), 3.01(2); to renumber 5.02(2) and (3), 5.03(2) to (7); to amend 1.02(2)(b), 1.02(5)(c)2(intro.) and 2a., 1.02(7)(b), Chapter DFI-Sec 2 (title), 2.01(1)(a)2, 2.01(9) and (10)(a), 3.01(1)(a), 3.02(1)(h) and (m), 3.03(3), 3.07(1) and (2), 5.01(1) and (3), 5.02(1), 5.03(1), (5) and (6), 5.04(1), 5.05(11)(d) 3 and (12), 5.06(intro.) and (7), 5.07(title), (1) and (2), 5.08(2), 5.09, 7.07(1)(a), (d) and (f), 9.01(1)(b) 12 and 13; to repeal and recreate Chapter DFI-Sec 5 (title), 5.03(7); and to create 1.02(5)(c) 2d, 1.02(14) to (18), 2.04(1) to (4), 5.02(2), (4) and (5), 5.03(2), 5.04(7) and (8), 5.06(12), 5.07(3) and (4), 9.01(1)(b) 20 and 21, and (d); relating to federal covered securities, federal covered advisers and investment adviser representatives.

Statutory Authority: 551.63(1) and (2); 551.02(7m)(a) and (b); 551.29(1) to (4); 551.31(4)(c); 551.32(1)(a) and (b), (1m)(a), (4), (5), (6), (8)(a) 3 and (9)(a); 551.33(1), (2) and (8); 551.52(1)(b)1 and 2.

Statutes Interpreted: 551.02(7m)(a) and (b), 551.29(1) to (4), 551.31(4)(c), 551.32(1)(a) and (b), (1m)(a), (4), (5), (6), (8)(a)3 and (9)(a); 551.33(1), (2) and (8); 551.52(1)(b)1 and 2.

FINDING OF EMERGENCY

The Department of Financial Institutions, Division of Securities, finds that an emergency exists and that the attached rules are necessary for the immediate preservation of the public peace, health, safety or welfare. A statement of the facts constituting the emergency follows.

Recently enacted legislation in 1997 Wisconsin Act 316 that is scheduled for publication on July 8, 1998 to become effective the following day on July 9, 1998 made a number of changes to the Wisconsin Uniform Securities Law, principally to conform to changes required under federal legislation in the National Securities Markets Improvement Act of 1996 ("NSMIA").

NSMIA preempted state securities law regulation in two principal areas: (1) prohibiting state securities registration and exemption requirements from being applicable to categories of so-called "federal covered securities," but permitting states to establish certain notice filing requirements (including fees) for such "federal covered securities;" and (2) prohibiting state securities licensing requirements from being applicable to certain investment advisers meeting criteria to qualify as a "federal covered adviser," but

permitting states to establish certain notice filing requirements (including fees) for those federal covered advisers that have a place of business in Wisconsin and more than 5 Wisconsin clients.

The legislation in 1997 Wisconsin Act 316 established notice filing requirements for "federal covered securities" and "federal covered advisers," and in addition, established statutory requirements for the licensing of "investment adviser representatives" (who previously were subject only to a qualification" process in Wisconsin). Comprehensive administrative rules are needed immediately to implement the statutory changes contained in 1997 Wisconsin Act 316, particularly relating to the filing requirements for federal covered securities, federal covered advisers and investment adviser representatives. In order to have such rules in place contemporaneously with the effectiveness of 1997 Wisconsin Act 316, these emergency rules are adopted on an interim basis until identical permanent rules can be promulgated using the standard rule-making procedures.

Pursuant to the statutory authority referenced above, the Department of Financial Institutions, Division of Securities, adopts emergency rules interpreting the statutes referenced above as follows:

SECTION 1. DFI-Sec 1.02(2)(b) is amended to read:

DFI-Sec 1.02(2)(b) A licensed investment adviser or federal covered adviser when placing orders for the accounts of its clients in accordance with rules prescribed by the division, provided that no commission or other remuneration is received by the investment adviser solely for placing the orders.

ANALYSIS: The amendment to this rule (which currently provides an exclusion from the definition of broker-dealer for licensed investment advisers) extends the exclusion to also cover “federal covered advisers.” Federal covered advisers are a new category of investment advisers designated by statute in 1997 Wisconsin Act 316, corresponding to federal legislation impacting state securities laws under the National Securities Markets Improvement Act (“NSMIA”).

SECTION 2. DFI-Sec 1.02(5) (c)2. (intro.) and 2.a. are amended to read:

DFI-Sec 1.02(5)(c)2. Any person who complies with Rule 206(4)-3. of the investment advisers act of 1940 and meets any of the following conditions is not considered to be “soliciting” for purposes of ~~s. 551.31(3), Stats.~~ subd. (c)1 and the definition of “transact business” in sub. (5):

2.a. The person is licensed in this state as an investment adviser or ~~is qualified as an investment adviser representative of an investment adviser licensed in this state;~~ or

ANALYSIS: These amendments do the following: (1) In (c)2. (intro.), correct the cross-reference used in the rule to reflect the proper administrative rule provisions that are applicable; and (2) in (c)2.a., deletes the term “qualified” as it applies to investment adviser representatives because 1997 Wisconsin Act 316 replaced the prior

“qualification” requirement with a licensing requirement.

SECTION 3. DFI-Sec 1.02(5) (c)2.d. is created to read:

DFI-Sec 1.02(5)(c)2.d. The person is a federal covered adviser.

ANALYSIS: This amendment adds the category of “federal covered adviser,” as created under 1997 Wisconsin Act 316, to the list of persons who can qualify for an exclusion from the definition of “soliciting” if the person complies with the requirements of Rule 206(4)-3 of the federal Investment Advisers Act of 1940.

SECTION 4. DFI-Sec 1.02(7)(b) is amended to read:

DFI-Sec 1.02(7)(b) "Branch office" for purposes of the investment adviser provisions of ch. 551, Stats., and chs. DFI-Sec 1 to 9 means any office in this state of an investment adviser or federal covered adviser that is held out to the public by any means as a business location of the investment adviser.

ANALYSIS: The amendment is needed to make this rule (defining “branch office” for purposes of the investment adviser provisions of the Wisconsin Securities Law and rules) apply also to federal covered advisers, as created in 1997 Wisconsin Act 316.

SECTION 5. DFI-Sec 1.02(14) is created to read:

DFI-Sec 1.02(14) The following defined terms apply for purposes of the definition of “investment adviser representative” in s. 551.02(7m)(a), Stats.

(a) A “supervised person” means any of the following:

1. Any partner, officer or director of, or other person occupying a similar status or performing similar functions for, an investment adviser or federal covered adviser.
 2. Any employee of an investment adviser or federal covered adviser, except for clerical or ministerial employees.
 3. Any other person who provides investment advice on behalf of an investment adviser and is subject to the supervision and control of the investment adviser or federal covered adviser.
- (b) A “client” has the same definition as that set forth in rule 275.203(b)(3)-1 under section 203 of the investment advisers act of 1940, except that supervised persons need not count clients that are not residents of the United States.
- (c) An “excepted person” means any of the following:
1. A natural person who, immediately after entering into an investment advisory contract with an investment adviser, has at least \$500,000 under management with the investment adviser.
 2. A natural person who the investment adviser reasonably believes, immediately prior to entering into an advisory contract, has a net worth (together with assets held jointly with a spouse) at the time the contract is entered into of more than \$1,000,000.
- (d) “Impersonal investment advice” means investment advisory services provided by means of written material or oral statements that do not purport to meet the objectives or needs of specific individuals or accounts.

- (e) "Third party solicitor" means a person soliciting clients on behalf of a licensed investment adviser or a federal covered adviser who is neither a partner, officer, director, or employee of the adviser, nor a supervised person of that adviser.

ANALYSIS: The rules in paras. (14)(a) to (e) of this SECTION define all of the substantive terms contained in the definition of "investment adviser representative" created in 551.02(7m)(a) by the 1997 Wisconsin Act 316, with language corresponding to federal statutes and rules defining those same terms. In particular: (1) "supervised person" in para. (a) corresponds with language in section 202(a)(25) of the Investment Advisers Act of 1940 as created in Title III of NSMIA, except for references to "federal covered adviser" added at the end of subd. (a)1, 2 and 3, and an exclusion for "clerical or ministerial employees" in subd. (a)2 based on language contained in the definition of "investment adviser representative" in section 401(g) of the Uniform Securities Act of 1956; (2) "client" in para. (b) corresponds with the federal rule definition cited, including that non-U.S. residents need not be counted; (3) "excepted person" and "impersonal investment advice" in paras. (c) and (d) correspond with the federal rule definitions in 203A-3(a)3(i) and 3(ii) under the Investment Advisers Act of 1940; (4) "third party solicitor" in para. (e) is based on the U.S. Securities and Exchange Commission's commentary to its investment adviser rulemaking relating to the cash solicitation rule in 2.06(4)-3 under the Investment Advisers Act of 1940.

SECTION 6. DFI-Sec 1.02(15) is created to read:

DFI-Sec 1.02(15) "Place of business" for purposes of the investment adviser provisions of ch. 551, Stats., and chs. DFI-Sec 1 to 9 means any location held out to the public by any means

at which an investment adviser or an investment adviser representative regularly provides investment advisory services, or solicits, meets with, or otherwise communicates with clients or prospective clients.

ANALYSIS: This rule defines the term “place of business” for purposes of the investment adviser licensing statutes and rules based on subsection (b)(1) of the federal definition of “place of business” in rule 203A-3 [as amended effective July 8, 1997] under the Investment Advisers Act of 1940.

SECTION 7. DFI-Sec 1.02(16) is created to read:

DFI-Sec 1.02(16) For purposes of s. 551.02(7m)(a)1.a., Stats., the specified percentage of clients of the supervised person who are natural persons that are not excepted persons shall be 10%.

ANALYSIS: This rule establishes for purposes of the definition of “investment adviser representative” in s. 551.02(7m)(a)1.a., Stats., the percentage of clients of a supervised person “who are natural persons that are not excepted persons.” The 10% number established in this rule is the same percentage used in federal rule 203A-3(a)(1) [as amended effective July 8, 1997] under the Investment Advisers Act of 1940.

SECTION 8. DFI-Sec 1.02(17) and (18) are created to read:

DFI-Sec 1.02(17) “Principal office” for purposes of the licensing provisions of ch. 551, Stats., and related rules in chs. DFI-Sec 1 to 9, means the office from which the officers, partners, or managers of a broker-dealer or an investment adviser direct, control, and coordinate the activities of the broker-dealer or investment adviser.

(18) "Custody" for purposes of the licensing provisions of ch. 551, Stats., and related rules in chs. DFI-Sec 1 to 9, includes having possession of customer funds or securities or the power to access or control the disposition of such assets to third parties.

ANALYSIS: These new definitional rules do the following: (1) define "principal office" for purposes of the securities licensing statutes and related rules, using identical language from rule 203A-3(c) [as amended effective July 8, 1997] under the Investment Advisers Act of 1940; and (2) define "custody" for purposes of the Wisconsin securities licensing statutes and related rules using language derived from the U.S. Securities and Exchange Commission's staff interpretations of what activities or practices constitute "custody" under rule 206(4)-2 of the Investment Advisers Act of 1940.

SECTION 9. Chapter DFI-Sec 2 (Title) is amended to read:

Chapter DFI-Sec 2

REGISTRATION EXEMPTIONS AND FEDERAL

COVERED SECURITY NOTICE FILINGS

ANALYSIS: This SECTION amends the Title to Chapter 2 of the Division's rules to reflect that the administrative rules relating to making notice filings for various categories of federal covered securities provided for in s. 551.29(1) to (3), Stats., (as created in 1997 Wisconsin Act 316) are being placed in Chapter 2.

SECTION 10. DFI-Sec 2.01(1)(a)2 is amended to read:

DFI-Sec 2.01(1)(a)2. Any securities of the enterprise, or any securities of an unconditional guarantor of all payments under the lease, sale or loan arrangement, are covered

securities under section 18(b)(1) of the securities act of 1993 or are exempt under s. 551.22(7),
Stats.

ANALYSIS: This amendment adds a cross-reference to the section of NSMIA that now designates as “covered securities” securities listed on various securities exchanges that (pre-NSMIA) had been designated for purposes of the “exchange listing” registration exemption in s. 551.22(7), Wis. Stats. Because NSMIA’s designation of qualifying exchanges in Section 18(b)(1) preempts s. 551.22(7), Wis. Stats., a cross-reference to that NSMIA section is necessary to give effect to the rule.

SECTION 11. DFI-Sec 2.01(3)(a) to (d) are repealed.

ANALYSIS: This SECTION deletes the rule subsections in 2.01(3)(a) to (d) which designate for purposes of the “exchange-listing” registration exemption in s. 551.22(7), Stats., the following exchanges: (1) the National Market System of NASDAQ [in sub (a)]; (2) the Chicago Board Options Exchange [in sub (b)]; (3) Tier 1 of the Pacific Stock Exchange [in sub (c)]; and (4) Tier 1 of the Philadelphia Stock Exchange [in sub (d)]. The deletions are warranted because those Wisconsin registration exemption designations are preempted and superseded by the designation in Section 18 (b)(1) of NSMIA of the National Market System of NASDAQ as a “covered security,” and by adoption on January 14, 1998, of Rule 146(b) under the Securities Act of 1993 by the U.S. Securities and Exchange Commission designating securities listed on the Chicago Board Options Exchange, Tier 1 of the Pacific Stock Exchange, and Tier 1 of the Philadelphia Stock Exchange as “covered securities” for purposes of Section 18 of the Securities Act of 1933.

SECTION 12. DFI-Sec 2.01(9) and (10)(a) are amended to read:

DFI-Sec 2.01(9) Any ~~government~~ security, other than a revenue obligation ~~and other than a security issued or guaranteed by the United States or an agency or corporate instrumentality of the United States,~~ issued by the state of Wisconsin or any political subdivision or agency or corporate or other instrumentality of the state of Wisconsin. is exempted under s. 551.22(17), Stats., if it is a security which matures within 16 months of date of issue and the issuer has levied a direct annual irrevocable tax under article XI, section 3, Wis. Const. or otherwise pledged levied taxes sufficient in amount to pay the interest on the securities as it falls due and also to pay and discharge the principal on the securities at maturity.

(10) (a) Any ~~government~~ security, other than a revenue obligation ~~and other than a security issued or guaranteed by the United States or an agency or corporate instrumentality of the United States,~~ issued by the state of Wisconsin or any political subdivision or agency or corporate or other instrumentality of the state of Wisconsin. is exempted under s. 551.22(17), Stats., if a notice of the proposed offering containing the information in par. (b) is filed with the division prior to the offering and the division does not by order deny the exemption within 10 days of the date the notice is filed.

ANALYSIS: The amendments to each of these registration exemption rules under 551.22(17), Stats., do the following: (1) delete the rule language referring to U.S. government securities because such securities are designated in NSMIA as “covered securities” under Section 18(b)(4)(C) of the Securities Act of 1933, thus preempting all state securities registration and exemption requirements; and (2) substitute language making each exemption rule applicable only to the securities (other than revenue

obligations) issued by the State of Wisconsin or its political subdivisions, agencies or instrumentalities, because NSMIA does permit a state's securities registration exemption provisions to apply when the governmental issuer of the securities is located in such (home) state. Accordingly, applicability of these exemption rules are limited to Wisconsin governmental issuers.

SECTION 13. DFI-Sec 2.02(9)(a) is repealed.

ANALYSIS: The repeal of this registration exemption rule under s. 551.23(18), Wis. Stats., (which applies to certain isolated sales of the securities of an investment company) is warranted because all investment company securities are designated in NSMIA as "covered securities" under Section 18(b)(2) of the Securities Act of 1933, thus preempting all state securities registration and exemption requirements.

SECTION 14. DFI-Sec 2.02(9)(L) is repealed.

ANALYSIS: The repeal of this registration exemption rule under s. 551.23(18), Wis. Stats., (which applies to securities of a unit investment trust, a type of investment company under the Investment Company Act of 1940) is warranted because all investment company securities are designated in NSMIA as "covered securities" under Section 18(b)(2) of the Securities Act of 1933, thus preempting all state securities registration and exemption requirements.

SECTION 15. DFI-Sec 2.04(1) to (4) are created to read:

DFI-Sec 2.04 FEDERAL COVERED SECURITY NOTICE FILINGS. (1)(a) With respect to a federal covered security referred to in s. 551.29(1)(a), Stats., there shall be filed with the division not later than the initial offer of the security in this state, a consent to service of process signed by the issuer and the notice filing fee prescribed under s. 551.52(1)(a), Stats. Additionally, if a completed Form NF as prescribed in DFI-Sec 9.01(1)(d) is included with the consent to service of process and the notice filing fee, the issuer need not also include with the filing copies of any documents that are part of the registration statement filed under the securities act of 1933, although the division may at a later time require the filing of a copy of any document that is part of the registration statement filed under the securities act of 1933.

(b) After the initial offer in this state of a federal covered security referenced in s. 551.29(1)(a), Stats., if the issuer files an amendment to its registration statement with the securities and exchange commission under the securities act of 1933 that relates either to a name change of the issuer, or to a change in the designation of the federal covered security, there shall be filed with the division concurrent with the federal filing, a fee of \$200, which shall be accompanied by a copy of each amendment-related document filed with the securities and exchange commission unless the issuer files with the division a completed Form NF as prescribed in DFI-Sec 9.01(1)(d). The division may at a later time require the filing of a copy of any document relating to the amendment filed under the securities act of 1933.

(2) With respect to a federal covered security referred to in s. 551.29(2), Stats., there shall be filed with the division not later than 15 days after the first sale of the security in this state, a notice consisting of a completed Form D as prescribed by rule 503 of regulation D under the securities act of 1933, signed by the issuer, together with a \$200 fee.

(3) With respect to a federal covered security referred to in s. 551.29(3), Stats., that is a revenue obligation issued by a non-Wisconsin governmental issuer which, prior to the National Securities Market Improvement Act of 1996 would have required a filing with the division under s. 551.22(1)(b), Stats., there shall be filed with the division not later than the earlier of the first offer or sale in this state, a notice consisting of a \$200 fee and which, in order to provide information about the offering for the division's database, may at the option of the issuer include a letter identifying the securities being offered, the aggregate dollar amount of the offering, the name of the governmental issuer, and the name and address of the non-governmental industrial or commercial enterprise providing payment of the principal and interest on the security.

(4) With respect to a federal covered security referred to in s. 551.29(3), Stats., that is being exchanged by the issuer with its existing securityholders and which, prior to the National Securities Market Improvement Act of 1996 would have required a filing with the division under s. 551.23(12), Stats., there shall be filed with the division not later than the earlier of the first offer or sale in this state, a notice consisting of a \$200 fee and a copy of each document relating to the offering filed under the securities act of 1933. If the issuer is not required to file documents relating to the offering under the securities act of 1933, in order to provide information about the offering and the issuer for inclusion in the division's database, the issuer at its option may include with the notice a letter identifying the issuer and its address, the securities being offered and the aggregate dollar amount of the offering.

ANALYSIS: This SECTION creates a new section of the securities rules (DFI-Sec 2.04) dealing specifically with the categories of "federal covered securities" created federally in NSMIA that are also dealt with for state securities law purposes in s. 551.29, Stats., in 1997 Wisconsin Act 316. Each subsection of 551.29, Stats., grants rulemaking authority

to the Division to adopt rules regarding filing requirements relating to the categories of federal covered securities dealt with in the particular subsection.

The rules in DFI-Sec 2.04(1)(a) and (b) parallel the statutory notice filing provisions for investment company federal covered securities contained in ss. 551.29(1)(a), Stats., (for initial offerings) and (1)(b) (for amendment filings) which set forth the prescribed materials to be filed and fees. Each of the rule subsections particularizes an option available to the issuer (referred to in each statutory section) which provides that copies of federally-filed documents need not be included with the filing with the Division if a completed Form NF [as prescribed in DFI-Sec 9.01(1)(d)] accompanies the filing with the Division. The rule also provides, however, that the Division may at a later time following such filing, require that copies of federally-filed documents be provided to the Division.

The rule in DFI-Sec 2.04(2) parallels the statutory notice filing provisions for Regulation D-Rule 506 federal covered security offerings contained in s. 551.29(2), Stats., with respect to the materials required to be filed, the fee, and the prescribed filing deadline.

The rule in DFI-Sec 2.04(3) is adopted under the rule-making authority granted to the Division under s. 551.29(3), Stats., to establish notice filing requirements – including a fee and any federally-filed documents – for categories of federal covered securities created under NSMIA as specified in section 18(b)(3) or (4) of the federal Securities Act of 1933. This rule applies solely to certain types of state/municipal governmental securities [which are included under Section 18(b)(4) as an exempt security in Section

3(a)(2) of the Securities Act of 1933]; namely, revenue obligations issued by a non-Wisconsin governmental issuer which, prior to NSMIA would have required a filing with the Division under s. 551.22(1)(b), Stats. The rule prescribes a required \$200 notice filing fee and, because such governmental securities offerings do not have to file any documents federally, the rule also states that in order to provide basic information about the offering and the issuer for inclusion in the Division's database, the issuer has the option of including with the notice a letter identifying the securities offered, the aggregate dollar amount of the offering, the name of the governmental issuer, and the name and address of the non-governmental industrial or commercial enterprise providing payment of the principal and interest on the security.

The rule in DFI-Sec 2.04(4) is adopted under the rule-making authority granted to the Division under s. 551.29(3), Stats., to establish notice filing requirements – including a fee and any federally-filed documents – for categories of federal covered securities created under NSMIA as specified in section 18(b)(3) or (4) of the federal Securities Act of 1933. This rule applies solely to exchange offers by securities issuers with their existing securityholders (which are included under Section 18(b)(4) as an exempt security in Section 3(a)(12) of the Securities Act of 1933). The rule prescribes a required \$200 notice filing fee and a copy of each document relating to the offering filed under the Securities Act of 1933. Also, similar to rule DFI-Sec 2.04(3) above, the rule states that if the issuer does not have to file any documents relating to the offering under the Securities Act of 1933, in order to provide the Division with basic information about the offering and the issuer for inclusion in the Division's database, the issuer has the option of

including with the notice a letter identifying the issuer and its address, the securities being offered and the aggregate dollar amount of the offering.

SECTION 16. DFI-Sec 3.01(1)(a) is amended to read:

DFI-Sec 3.01(1)(a) Copies of the articles of incorporation and by-laws or equivalents currently in effect, any agreements with or among underwriters, any instrument governing the issuance of the security to be registered, a specimen of the security and, if the security to be registered is a note, bond, debenture or other evidence of indebtedness, a trust indenture meeting the requirements of s. DFI-Sec 3.04, ~~unless the security is a face amount certificate registered under the investment company act of 1940 or~~ unless the requirement to furnish a trust indenture relating to the securities is waived by the division for good cause shown; and

ANALYSIS: The amendment to this rule (which lists certain information to be included with a filing for registration by coordination under s. 551.25, Stats.) repeals the reference to securities of a face amount certificate company (a type of investment company under the Investment Company Act of 1940) because under NSMIA, all investment company securities are designated as “covered securities” under Section 18(b)(2) of the Securities Act of 1933, thus preempting state securities statute and rule registration provisions.

SECTION 17. DFI-Sec 3.01(2) is repealed.

ANALYSIS: The repeal of this procedural rule under the securities registration by coordination section (which rule relates to registration of an indefinite amount of securities for certain categories of investment companies) is warranted for the following reasons: (1) Under NSMIA, all investment company securities are designated as

“covered securities,” thus preempting state securities statute and rule registration provisions (although registration or exemption can be required for non-payment of notice filing fees); (2) If the securities of an investment company are subject to registration in Wisconsin by application of s. 551.29(4), Stats., (in 1997 Wisconsin Act 316), as a result of non-payment of fees, the existing statutory provisions of s. 552.52(1)(b)1, Stats., (as amended by 1997 Wisconsin Act 316) serve to provide for an indefinite amount of securities to be registered.

SECTION 18. DFI-Sec 3.02(1)(h) is amended to read:

DFI-Sec 3.02(1)(h) The kind of securities and the amount to be offered (~~which, in the case of redeemable securities of an open-end management company, unit investment trust and face amount certificate company, as defined in the investment company act of 1940, shall be indefinite~~); the proposed offering price or the method by which it is to be computed; and variation therefrom at which any proportion of the offering is to be made to any person or class of persons other than the underwriters, with a specification of any such person or class; the basis upon which the offering is to be made if otherwise than for cash; the estimated aggregate underwriting and selling discounts or commissions and finders' fees (including separately cash, securities, contracts, or anything else of value to accrue to the underwriters or finders in connection with the offering) or, if the selling discounts or commissions are variable, the basis of determining them and their maximum and minimum amounts; the estimated amounts of other selling expenses, including legal, engineering, and accounting charges; the name and address of every underwriter and every recipient of a finder's fee; a copy of any underwriting or selling group agreement pursuant to which the distribution is to be made, or the proposed form of any

such agreement whose terms have not yet been determined; and a description of the plan of distribution of any securities which are to be offered otherwise than through an underwriter;

ANALYSIS: This amendment deletes the references in the rule to several categories of investment companies because under NSMIA, all investment company securities are designated as “covered securities” under Section 18(b)(2) of the Securities Act of 1933, thus preempting state securities statute and rule regulation provisions.

SECTION 19. DFI-Sec 3.02(1)(m) is amended to read:

DFI-Sec 3.02(1)(m) A specimen or copy of the security being registered; a copy of the issuer’s articles of incorporation and bylaws, or equivalents, as currently in effect; and if the security to be registered is a note, bond, debenture or other evidence of indebtedness, a trust indenture meeting the requirements of s. DFI-Sec 3.04, ~~unless the security is a face amount certificate registered under the investment company act of 1940 or unless the requirement to~~ furnish a trust indenture relating to the securities is waived by the division for good cause shown;

ANALYSIS: See ANALYSIS to DFI-Sec 3.01(1)(a).

SECTION 20. DFI-Sec 3.03(3) is amended to read:

DFI-Sec 3.03(3) The prospectus shall contain a full disclosure of all material facts relating to the issuer and the offering and sale of the registered securities. A prospectus meeting the requirements under the securities act of 1933 that receives full review by the U.S. securities and exchange commission, shall not be subject to disclosure adequacy review or comment by the division. ~~A prospectus meeting the requirements of form N-1A or form S-6 and subsequent post effective amendments as filed under the securities act of 1933, or the investment company act of~~

~~1940, or both, by a registration applicant or an existing registrant shall not be subject to disclosure adequacy review or comment by the division.~~ If the offering is being made pursuant to use of either Rule 504 of Regulation D under the securities act of 1933 or rule 147 under section 3(a)(11) of the securities act of 1933, the form U-7 disclosure document as adopted by the North American Securities Administrators Association, Inc. may be used.

ANALYSIS: The amendment to this rule (relating to staff review of the disclosure adequacy of prospectuses contained in registration filings) deletes reference to prospectuses for investment company securities because under NSMIA, state securities administrators may not impose merit requirements or conduct a disclosure adequacy review of prospectuses for investment company securities.

SECTION 21. DFI-Sec 3.07(1) and (2) are amended to read:

DFI-Sec 3.07 EXTENSION OF REGISTRATION STATEMENTS. (1) Application for an extension of the offering period of a registration statement, except one relating to ~~redeemable securities issued by an open end management company or a face amount certificate company as defined in the investment company act of 1940,~~ or securities of a finance company licensed under s. 138.09, Stats., shall be filed in the form prescribed by the division not less than 30 days prior to the end of one year from the effective date of the registration statement or an extended period of effectiveness for the registration statement, whichever is most recent. The application shall be accompanied by a prospectus updated in accordance with s. DFI-Sec 3.03(6), a balance sheet of the issuer as of the end of its most recent fiscal year, and a comparative statement of income and changes in financial position and analysis of surplus for each of the 3 most recent fiscal years (or for the period of the issuer's and any predecessor's existence if less

than 3 years), all meeting the requirements of s. DFI-Sec 7.06, provided that if the date of any of the above financial statements is more than 120 days (180 days with respect to a corporation organized and operated not for private profit but exclusively for religious, educational, benevolent or charitable purposes) prior to the date of the extension of the registration statement, the statements shall be updated (which may be done without audit) to within the 120-day or 180-day requirement above. If no order specifying a different effectiveness period is in effect, renewal of the registration statement becomes effective on the day on which the prior registration statement expires or at such earlier time as the division determines.

(2) A registration statement relating to ~~redeemable securities issued by an open end management company or a face amount certificate company as defined in the investment company act of 1940, or securities of a finance company licensed under s. 138.09, Stats.,~~ is deemed to include an application for the continuous offering of the securities. The offering period of the registration statement is automatically extended until it is permitted to be withdrawn or the division issues a stop order suspending or revoking its effectiveness pursuant to s. 551.28, Stats., if the issuer ~~complies with s. 551.52(1)(b), Stats., which may involve the filing of form RS-IC as referred to in s. DFI-Sec 9.01,~~ and if the issuer files with the division not less than annually during the offering period, within 120 days of the end of its fiscal year, a prospectus updated in accordance with s. DFI-Sec 3.03(6), a balance sheet of the issuer as of the end of the fiscal year, and a statement of income and change in financial position and analysis of surplus of the issuer for the fiscal year meeting the requirements of s. DFI-Sec 7.06.

ANALYSIS: The amendments to these registration exemption rules (relating to extensions) do the following: (1) Delete the references at the beginning of subs. (1) and (2) to certain categories of investment companies because under NSMIA, all investment

company securities are designated as “covered securities” under Section 18(b)(2) of the Securities Act of 1933, thus preempting state securities statute and rule registration provisions. (2) The second deletion in sub. (2) is necessary because as a result of the deletion in the first part of the subsection, the subsection relates only to the securities of finance company issuers.

SECTION 22. In the following rules, each reference therein to “qualified” is amended to read “licensed”: DFI-Sec 5.01(4)(b), 5.01(5) and (7), 5.05(7) and (10).

ANALYSIS: The legislation in 1997 Wisconsin Act 316 contained a specific licensing requirement (in s. 551.31(3), Stats.) for representatives of investment advisers, replacing a “qualification” provision that had previously existed. This SECTION makes the appropriate amendment (changing the terminology from “qualified” to “licensed”) in those rule provisions specified in Chapter DFI-Sec 5 where that is the only amendment necessary.

SECTION 23. Chapter DFI-Sec 5 (title) is repealed and recreated to read:

CHAPTER DFI-SEC 5

**LICENSING AND NOTICE FILING PROCEDURES FOR
INVESTMENT ADVISERS, FEDERAL COVERED ADVISERS, AND
INVESTMENT ADVISER REPRESENTATIVES**

ANALYSIS: This SECTION amends the Title of Chapter DFI-Sec 5 of the rules to reflect that its scope has been expanded as a result of enactment of 1997 Wisconsin Act 316 which provides authority to now regulate investment adviser representatives as

licensees and establish notice filing and related procedures for certain federal covered advisers.

SECTION 24. DFI-Sec 5.01(1) is amended to read:

DFI-Sec 5.01 LICENSING PROCEDURE. (1) Applications for initial and renewal licenses ~~and qualifications~~ of investment advisers and their investment adviser representatives shall be filed on forms prescribed by the division in s. DFI-Sec 9.01 (1).

ANALYSIS: These technical amendments delete the reference in the rule to “qualification,” and add language to have the rule apply to “investment adviser representatives” which is now a defined term as created in 1997 Wisconsin Act 316.

SECTION 25. DFI-Sec 5.01(3) is amended to read:

DFI-Sec 5.01(3) Unless waived under sub. (4), each applicant for an initial license as an investment adviser or ~~for qualification~~ as an investment adviser representative after ~~January 1, 1996~~ July 9, 1998, and each applicant whose application has not become effective by ~~January 1, 1996~~ July 9, 1998, is required to pass either of the following examinations with a grade of at least 70%:

ANALYSIS: These technical amendments delete the reference in the rule to “qualification” and substitute for the January 1, 1996 date therein, the effective date of 1997 Wisconsin Act 316 that contains amendments to the investment adviser and investment adviser representative licensing requirement.

SECTION 26. DFI-Sec 5.02(1) is amended to read:

DFI-Sec 5.02 NET CAPITAL REQUIREMENT. (1) ~~Every~~ Except as required under sub. (2), investment adviser whose principal office is in this state that collects advisory fees 6 months or more in advance or collects more than \$2,000 in advance fees for preparing a financial plan shall maintain net capital of not less than \$5,000, which shall be in the form of cash or securities or other liquid assets as determined by the division.

ANALYSIS: Under NSMIA, no state can impose regulations establishing net capital, bonding, or books and records requirements on an investment adviser beyond those required under the laws of the state in which the investment adviser maintains its principal place of business. Accordingly, this existing net capital rule subsection is amended to provide that it is applicable only to investment advisers having a principal office in Wisconsin. The new, separate, net capital rule created below in DFI-Sec 5.02(2) for investment advisers having custody of client funds or securities similarly is made applicable only to investment advisers having a principal office in Wisconsin. The net capital requirement of \$35,000 or 1% of assets under management is taken from a proposed Model Rule on this subject [§ 202(d)-1(a)(1)] developed by a North American Securities Administrators Association Working Group on investment adviser capital and bonding requirements..

SECTION 27. DFI-Sec 5.02(2) is renumbered 5.02(3)

ANALYSIS: This SECTION moves existing rule 5.02(2) to become sub. (3) to make room for a newly-created separate net capital rule that needs to follow existing sub. (1) in sequence.

SECTION 28. DFI-Sec 5.02(2) is created to read:

DFI-Sec 5.02(2) Every investment adviser whose principal office is in this state that has custody of client funds or securities shall maintain a minimum net capital of \$35,000 or 1% of the adviser's assets under management, whichever is greater.

ANALYSIS: See the ANALYSIS to SECTION 26.

SECTION 29. DFI-Sec 5.02(3) is renumbered 5.02(6) and as renumbered is amended to read:

DFI-Sec 5.02(6) The division may by order exempt any investment adviser whose principal office is in this state from the provisions of this section, either unconditionally or upon specified conditions, if by reason of the special nature of its business or the particular facts and circumstances of the application, the division determines that compliance with the provisions is not necessary in the public interest or for the protection of investors.

ANALYSIS: Another amendment adding NSMIA-required language to provide that the substantive regulatory provisions in this existing rule relating to investment adviser net capital requirements (this rule grants exemption/waiver authority to the Division) can only be imposed by a state on those investment advisers whose principal office is in that particular state.

SECTION 30. DFI-Sec 5.02(4) and (5) are created to read:

DFI-Sec 5.02(4) Every investment adviser that has its principal office in a state other than this state shall maintain only the minimum capital as required by the state in which the

investment adviser maintains its principal office, provided that the investment adviser is licensed in such state and is in compliance with such state's minimum net capital requirements.

(5) For purposes of this section, the term "net capital" means an excess of assets over liabilities, as determined by generally accepted accounting principles, but shall not include as assets any of the following:

- (a) Prepaid expenses, deferred charges, goodwill, franchise rights, organizational expenses, patents, copyrights, marketing rights, unamortized debt discount and expense, and all other assets of an intangible nature.
- (b) Home, home furnishings, automobiles and any other personal items not readily marketable, if the investment adviser is an individual.
- (c) Advances or loans to stockholders and officers, if the investment adviser is a corporation.
- (d) Advances or loans to partners, if the investment adviser is a partnership.

ANALYSIS: These two new rules relating to investment adviser net capital requirements do the following: (1) in sub. (4), adopt language contained in NSMIA which provides that for investment advisers having a principal office outside Wisconsin, they need maintain only such minimum net capital as required by the state in which the investment adviser maintains its principal office (provided that the adviser is licensed in such state and is in compliance with that state's minimum net capital requirements); (2) in sub. (5), adopt a definition of "net capital" taken from a proposed NASAA Model Rule [§202(d) - 1(c)] developed by a North American Securities Administrators Association Working Group on investment adviser capital and bonding requirements.

SECTION 31. DFI-Sec 5.03(1) is amended to read:

DFI-Sec 5.03(1) Every licensed investment adviser whose principal office is in this state shall prepare and keep current at ~~its principal~~ that office, or at a designated office located in the ~~United States~~ this state, as specified in writing to, and permitted by, the division, or at an office under the direct supervision and control of the principal or designated office, the following books and records relating to its business:

ANALYSIS: This SECTION adds NSMIA-required language to provide that substantive state regulatory provisions relating to investment adviser books and records requirements can only be imposed by a state on those investment advisers whose principal office is in that particular state.

SECTION 32. DFI-Sec 5.03(2), (3), (4), (5) and (7) are renumbered 5.03(3), (4), (5), (6) and (8), respectively, and DFI-Sec 5.03(5) and (6) as renumbered, are amended to read:

DFI-Sec 5.03(5) Every branch office as defined in s. DFI-Sec 1.02 (7) (b), of a licensed investment adviser whose principal office is in this state, shall prepare and keep current the records described in subs. (1) (c), (f), (g), (h), (k) and (L) and (2) (a) and (b).

(6) The records required in sub. (4) (5) shall be preserved at the branch office for a period of not less than 3 years, the first 2 years in an easily accessible place. Upon closing of the branch office, the records shall be transferred to the home office for the duration of the required retention period. The record may be retained by computer if a printed copy of the record can be prepared immediately upon request. If a record has been preserved for the first year of the 3-year

period required in this subsection, a microfilm copy may be substituted for the remainder of the required retention period.

ANALYSIS: This SECTION does the following: (1) amends sub. (5) by adding NSMIA-required language to provide that substantive regulatory provisions in the existing rule relating to investment adviser books and records requirements (this rule requires branch offices of licensed broker-dealers to prepare and keep current certain records) can only be imposed by a state on those investment advisers whose principal office is in that particular state; (2) amends sub. (6) by renumbering the rule cross-referenced in line 1 to reflect its renumbering [from sub. (4) to sub. (5)] in the title of this SECTION.

SECTION 33. DFI-Sec 5.03(2) is created to read:

DFI-Sec 5.03(2) Each licensed investment adviser whose principal office is in this state who has custody or possession of securities or funds of any client shall maintain and keep current the following books and records in addition to those required under sub. (1):

- (a) A journal or other record showing all purchases, sales, receipts and deliveries of securities, including certificate numbers, for all accounts and all other debits and credits to the accounts.
- (b) A separate ledger for each client showing all purchases, sales, receipts and deliveries of securities, the date and price of each purchase and sale, and all debits and credits.
- (c) Copies of confirmations of all transactions effected by or for the account of any client.

(d) A record for each security in which any client has a position, which record shall show the name of each client having any interest in each security, the amount or interest of each client, and the location of each security.

ANALYSIS: This new rule establishes an additional books and records requirement for those investment advisers whose principal office is in Wisconsin and who also have custody or possession of securities or funds of any client. Prior to enactment of 1997 Wisconsin Act 316, Wisconsin had prohibited (under sec. 551.44, Wis. Stats.) investment advisers from having custody of any client funds or securities. However, because the federal securities laws do not prohibit investment advisers from having custody of clients funds or securities, and Section 222(a) of NSMIA provides that state's investment adviser requirements cannot conflict with federal provisions, the prohibition formerly in sec. 551.44, Wis. Stats., was repealed in 1997 Wisconsin Act 316. The new rule specifies the kinds of records that licensed investment advisers having custody of customer funds and securities must maintain – which listing of records corresponds to the records specified in a proposed Model Rule on this subject [§ 202(d)-1(b)] developed by a North American Securities Administrators Association Working Group on investment adviser capital and bonding requirements.

SECTION 34. DFI-Sec 5.03(6) is renumbered 5.03(7), and as renumbered, is repealed and recreated to read:

DFI-Sec 5.03(7) Every investment adviser that has its principal office in a state other than this state shall maintain only such books and records as are required by the state in which the

investment adviser maintains its principal office, provided that the investment adviser is licensed in such state and is in compliance with such state's books and records requirements.

ANALYSIS: This SECTION adds NSMIA-required language [similar to that contained in the net capital rule in DFI-Sec 5.02(4) above] to provide that for investment advisers having a principal office outside Wisconsin, they need maintain only such books and records as required by the state in which the investment adviser maintains its principal office (provided that the adviser is licensed in such state and is in compliance with that state's books and records requirements).

SECTION 35. DFI-Sec 5.04(1) is amended to read:

DFI-Sec 5.04 REPORTING REQUIREMENTS. (1) Every investment adviser shall file with the division immediate notice via facsimile whenever the net capital of the investment adviser is less than is required under s. DFI-Sec 5.02(1) or (2), specifying the amount of net capital on the date of the notice and the steps the investment adviser has taken or will take to come into compliance.

ANALYSIS: The amendment to this reporting rule (regarding net capital deficiencies) adds a cross-reference to new rule DFI-Sec 5.02(2) created above which adds an alternative net capital requirement for any investment adviser with its principal office in Wisconsin that has custody of client funds or securities.

SECTION 36. DFI-Sec 5.04(7) and (8) are created to read:

DFI-Sec 5.04(7) Each investment adviser shall file annually with the division incident to its license renewal application, a copy of Schedule I to Form ADV confirming its regulatory

status with the U.S. securities and exchange commission and the dollar amount, if any, of assets under management.

(8) Each federal covered adviser that has filed a notice with the division under s. 551.32(1m)(a), Stats., shall file a copy of its Schedule I to Form ADV contemporaneously with its filing of that schedule with the U.S. securities & exchange commission.

ANALYSIS: This SECTION creates two reporting rules relating to the following: (1) a requirement in sub. (7) that each investment adviser file annually with the Division incident to its license renewal application, a copy of Schedule I to Form ADV confirming its regulatory status with the U.S. Securities and Exchange Commission and the dollar amount, if any, of assets under management. Such annual information is necessary because, under NSMIA, if an investment adviser has more than \$25 million of assets under management, it becomes subject to federal regulation and triggers the definition of “federal covered adviser” in s. 551.02(4)(g), Stats., in 1997 Wisconsin Act 316 with the result that the investment adviser no longer would be subject to the Wisconsin investment adviser licensing requirements. (2) a requirement in sub. (8) that each “federal covered adviser” (as defined in s. 551.02(4)(g), Stats., in 1997 Wisconsin Act 316) required to file a notice under s. 551.32(1m)(a), Stats., must file with the Division a copy of the Schedule I to Form ADV contemporaneously with the adviser’s filing of that schedule with the U.S. Securities and Exchange Commission. Such annual information is necessary to enable the Division to verify that the federal covered adviser continues to be subject to federal regulation and not subject to state licensure under the Wisconsin Uniform Securities Law. The time for making the filing is contemporaneous with the adviser’s

filing the Schedule I with the U.S. Securities and Exchange Commission (rather than incident to the adviser making its annual renewal notice filing under s. 551.32(1m)(b), Stats., which is on a different annual date than its federal filing) so that the adviser will not have to keep track of a separate reporting date for the Wisconsin filing.

SECTION 37. DFI-Sec 5.05(11)(d)3. is amended to read:

DFI-Sec 5.05(11)(d)3. Establishment of a system that ensures that all books and records required by rule or order under ch. 551, Stats., are properly maintained, ~~and that precludes the investment adviser from taking or having custody of customer funds or securities as prohibited under s. 551.44, Stats.~~

ANALYSIS: The amendment to this Rule of Conduct provision deletes language relating to the statutory prohibition formerly contained in s. 551.44, Stats., (precluding investment advisers from having custody of client funds or securities) because that statutory prohibition was repealed in 1997 Wisconsin Act 316.

SECTION 38. DFI-Sec 5.05(12)(intro.) is amended to read:

DFI-Sec 5.05(12)(intro.) No investment adviser or investment adviser representative, in connection with a telephone or electronic solicitation, shall:

ANALYSIS: The amendment to this Rule of Conduct provision (relating to telephone or electronic solicitation of persons to become clients) adds language making the rule applicable to investment adviser representatives (as well as investment advisers) because 1997 Wisconsin Act 316 makes investment adviser representatives "licensees" that are subject to applicable licensing provisions of Chapter DFI-Sec 5.

SECTION 39. DFI-Sec 5.06 (intro.) is amended to read:

DFI-Sec 5.06 PROHIBITED BUSINESS PRACTICES. The following are deemed "dishonest or unethical business practices" or "taking unfair advantage of a customer" by an investment adviser or an investment adviser representative under s. 551.34 (1) (g), Stats., without limiting those terms to the practices specified in this section:

ANALYSIS: In similar fashion to the previous SECTION, the amendment to the introductory portion of the Prohibited Business Practices section of rules adds language making the section applicable to investment adviser representatives (as well as investment advisers) because 1997 Wisconsin Act 316 makes investment adviser representatives "licensees" that are subject to applicable licensing provisions of Chapter DFI-Sec 5.

SECTION 40. DFI-Sec 5.06(7) is amended to read:

DFI-Sec 5.06(7) ~~Representing itself as a~~ Using the title financial or investment planner, consultant, or adviser, when the representation does not accurately describe the nature of the services offered, the qualifications of the person offering the services, and the method of compensation for the services;

ANALYSIS: This amendment makes a technical language change for the reason that because investment adviser representatives are now licensees subject to the Prohibited Business Practices section, the term "itself" currently contained in the rule is no longer appropriate as applied to individual persons subject to the rule.

SECTION 41. DFI-Sec 5.06(12) is created to read:

DFI-Sec 5.06(12) Taking or having custody of client funds or securities without being in compliance with rule 206(4)-2 of the investment advisers act of 1940 and the net capital requirement in s. DFI-Sec 5.02(2).

ANALYSIS: As a result of the amendment to s. 551.44, Stats., in 1997 Wisconsin Act 316 (which removed language that previously had prohibited investment advisers from having custody of client funds or securities), this rule creates as a Prohibited Business Practice, the failure by an investment adviser having custody of client funds or securities to comply with either the federal rule requirements regarding such activity or with the Wisconsin net capital rule relating to such activity.

SECTION 42. DFI-Sec 5.07 (title), (1) and (2) are amended to read:

DFI-Sec 5.07 LICENSE AND NOTICE FILING PERIOD. (1) The license of an investment adviser expires April 30 of each year. Each licensed investment adviser seeking renewal of its license shall file with the division an application for renewal not later than March 31 prior to the expiration of its license. ~~The qualification of an investment adviser representative expires on the same day as that of the investment adviser which the person represents. The division may by order limit the period of, or specify an earlier expiration date for, any license.~~

(2) ~~The qualification~~ license of an investment adviser representative expires on the same day as that of the investment adviser which the person represents. The license of an investment adviser representative is not effective during any period when the investment adviser which that person represents is not licensed or during any period when the representative is not employed

either by a specified investment adviser licensed under ch. 551, Stats., or a federal covered adviser that has filed a notice with the division under s. 551.32.(1m)(a). Stats:

ANALYSIS: These amendments do the following: (1) add “notice filing” to the title of the section to reflect the creation in 1997 Wisconsin Act 316 of notice filing procedures for certain federal covered advisers; (2) delete the last sentence in sub. (1) relating to the expiration date for the “qualification” of an investment adviser representative because 1997 Wisconsin Act 316 provides for licensure of investment adviser representatives such that the subject matter of that last sentence in (1) can be transferred to sub. (2); and (3) add language in sub. (2) that (i) reflects the “licensure” of investment adviser representatives, (ii) transfers the “expiration date” provision from the last sentence of sub. (1) to sub. (2), and (iii) adds a reference at the end of the subsection to federal covered advisers that have filed a notice with the Division under s. 551.32(1m)(a), Stats., because investment adviser representatives can be licensed in Wisconsin to represent such federal covered advisers.

SECTION 43. DFI-Sec 5.07(3) and (4) are created to read:

DFI-Sec 5.07(3) The division may by order limit the period of, or specify an earlier expiration date for, any license.

(4) The notice filing of a federal covered adviser that has filed a notice with the division under s. 551.32.(1m)(a), Stats., expires April 30 of each year. Each federal covered adviser seeking renewal of its notice filing shall file with the division the form prescribed in s. DFI-Sec 9.01(1)(b)20 not later than March 31 prior to the expiration of its notice filing.

ANALYSIS: This SECTION does the following: (1) creates in sub. (3) a separate rule taken from the last sentence of current rule DFI-Sec 5.07(1) providing authority for the Division to limit the period of, or specify an earlier expiration date for, any license; (2) creates in sub. (4) a rule prescribing a uniform expiration date for notices filed with the Division by federal covered advisers, as well as a uniform renewal filing deadline date.

SECTION 44. DFI-Sec 5.08(2) is amended to read:

DFI-Sec 5.08(2) An application for withdrawal from the status of a qualified licensed investment adviser representative shall be filed ~~by the investment adviser which the person represents~~ pursuant to s. 551.31(4)(c), Stats., within 15 days of the termination of the representative's employment on Form U-5 prescribed by the division.

ANALYSIS: This SECTION does the following: (1) substitutes "licensed" for "qualified" in line (1); and (2) substitutes a cross-reference to s. 551.31(4)(c), Stats., created in 1997 Wisconsin Act 316, because the two subsections in (4)(c) differ in prescribing who is responsible for filing termination/withdrawal notices for investment adviser representatives with the Division.

SECTION 45. DFI-Sec 5.09 is amended to read:

DFI-Sec 5.09 DENIAL, SUSPENSION, REVOCATION AND CENSURE. Any order denying, suspending or revoking the license of an investment adviser or an investment adviser representative or censuring a licensee may include such other sanctions as the division finds appropriate.

ANALYSIS: In similar fashion to amendments in SECTION 39 to DFI-Sec 5.06 Prohibited Business Practices, this amendment adds language making the Denial, Suspension and Revocation section (DFI-Sec 5.09) applicable to investment adviser representatives (as well as investment advisers) because 1997 Wisconsin Act 316 makes investment adviser representatives “licensees” that are subject to applicable licensing provisions of Chapter DFI-Sec 5.

SECTION 46. DFI-Sec 7.01(7)(a) is amended to read:

DFI-Sec 7.01(7)(a) Delinquent filing of broker-dealer or investment adviser license renewal application or federal covered adviser renewal notice filing.....\$100.

ANALYSIS: The amendment extends applicability of this rule (prescribing a \$100 delinquency fee for broker-dealers or investment advisers that are not timely in filing license renewals with the Division) to federal covered advisers that are not timely in filing their renewal notice required under s. 551.32(1m)(b), Stats., as created in 1997 Wisconsin Act 316. Under Section 307(b) of NSMIA, state filing-related fees applicable to investment advisers that were in effect prior to enactment of NSMIA are preserved.

SECTION 47. DFI-Sec 7.01(7)(d) is amended to read:

DFI-Sec 7.01(7)(d) Delinquent filing of notice of broker-dealer, ~~or~~ investment adviser or federal covered adviser branch office registration, renewal, relocation or closing.....\$100.

ANALYSIS: The amendment extends applicability of this rule (prescribing a \$100 delinquency fee for broker-dealers and investment advisers that are not timely in

providing notice of branch office openings, closings or relocations) to federal covered advisers. Under Section 307(b) of NSMIA, state filing-related fees applicable to investment advisers that were in effect prior to enactment of NSMIA are preserved.

SECTION 48. DFI-Sec 7.01(7)(f) is amended to read:

DFI-Sec 7.01(7)(f) Delinquent filing of broker-dealer agent, or agent for issuer license renewal, or of investment adviser representative license renewal.....\$100.

ANALYSIS: The amendment to this delinquent filing fee rule (which includes applicability to investment adviser representatives) adds language to reflect that as a result of 1997 Wisconsin Act 316, investment adviser representatives are now “licensed.”

SECTION 49. DFI-Sec 9.01(1)(b)12. and 13. are amended to read:

DFI-Sec 9.01(1)(b)12. ADV. Uniform application for investment adviser registration license.

13. IAR(WI). Application for renewal of investment adviser license and qualification of and investment adviser representatives representative license.

ANALYSIS: The amendments to these two licensing-related Forms rules do the following: (1) correct the terminology used in subd. (1)(b) 12 by changing the current language investment adviser “registration” (federal terminology) to read investment adviser “license” and thereby reflect the Wisconsin state licensing status for investment advisers; and (2) substitute in subd. (1)(b) 13 the terminology “licensed” for “qualified” reflecting the licensing requirement for investment adviser representatives created under 1997 Wisconsin Act 316.

SECTION 50. DFI-Sec 9.01(1)(b)20. and 21. are created to read:

DFI-Sec 9.01(1)(b)20. IAN(WI) Federal covered adviser initial and renewal notice filing form.

21. ADV-W. Application for withdrawal of investment adviser license.

ANALYSIS: These new licensing-related Forms rules do the following: (1) create in subd. (1)(b)20 a specific form for use by federal covered advisers in making their initial or renewal notice filings under ss. 551.32(1m)(a) and (b), Stats.; and (2) designate Form ADV-W as the form to be used by investment advisers when withdrawing their license in Wisconsin.

SECTION 51. DFI-Sec 9.01(1)(d) is created to read:

DFI-Sec 9.01(1)(d). NF. Uniform investment company notice filing.

ANALYSIS: This SECTION lists newly-created Form NF as the designated form for use by an investment company when making a notice filing as provided for in s. 551.29(1)(a), Stats. (created in 1997 Wisconsin Act 316) and rule DFI-Sec 2.04(1)(a) to offer its securities in Wisconsin, or to make a filing relating to an amendment under s. 551.29(1)(b) and rule DFI-Sec 2.04(1)(b).

* * * *

EFFECTIVE DATE

The emergency rules adopted by this Order shall take effect at 12:01 A.M., on July 9, 1998, which is subsequent to publication of the rules in the official state newspaper pursuant to the provisions of s. 227.24(1)(c), Stats.

DATED at Madison, Wisconsin, this 3d day of July, 1998.

[SEAL]



PATRICIA D. STRUCK
Administrator
Division of Securities

END



END

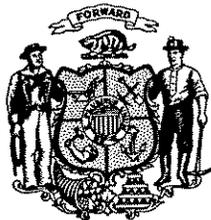
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FORM 2

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CLEARINGHOUSE REPORT TO AGENCY

[THIS REPORT HAS BEEN PREPARED PURSUANT TO S. 227.15, STATS. THIS IS A REPORT ON A RULE AS ORIGINALLY PROPOSED BY THE AGENCY; THE REPORT MAY NOT REFLECT THE FINAL CONTENT OF THE RULE IN FINAL DRAFT FORM AS IT WILL BE SUBMITTED TO THE LEGISLATURE. THIS REPORT CONSTITUTES A REVIEW OF, BUT NOT APPROVAL OR DISAPPROVAL OF, THE SUBSTANTIVE CONTENT AND TECHNICAL ACCURACY OF THE RULE.]

CLEARINGHOUSE RULE 98-114

AN ORDER to repeal DFI-Sec 2.01 (3) (a) to (d), 2.02 (9) (a) and (L) and 3.01 (2); to renumber DFI-Sec 5.02 (2) and (3) and 5.03 (2) to (7); to amend DFI-Sec 1.02 (2) (b), (5) (c) 2. (intro.) and 2a. and (7) (b), chapter DFI-Sec 2 (title), 2.01 (1) (a) 2., 2.01 (9) and (10) (a), 3.01 (1) (a), 3.02 (1) (h) and (m), 3.03 (3), 3.07 (1) and (2), 5.01 (1) and (3), 5.02 (1), 5.03 (1), (5) and (6), 5.04 (1), 5.05 (11) (d) 3. and (12), 5.06 (intro.) and (7), 5.07 (title), (1) and (2), 5.08 (2), 5.09, 7.07 (1) (a), (d) and (f) and 9.01 (1) (b) 12. and 13.; to repeal and recreate chapter DFI-Sec 5 (title) and 5.03 (7); and to create DFI-Sec 1.02 (5) (c) 2d. and (14) to (18), 2.04 (1) to (4), 5.02 (2), (4) and (5), 5.03 (2), 5.04 (7) and (8), 5.06 (12), 5.07 (3) and (4) and 9.01 (1) (b) 20. and 21. and (d), relating to federal covered securities, federal covered advisers and investment adviser representatives.

Submitted by **DEPARTMENT OF FINANCIAL INSTITUTIONS**

08-13-98 RECEIVED BY LEGISLATIVE COUNCIL.
09-11-98 REPORT SENT TO AGENCY.

RNS:DLS:kjf;jt

LEGISLATIVE COUNCIL RULES CLEARINGHOUSE REPORT

This rule has been reviewed by the Rules Clearinghouse. Based on that review, comments are reported as noted below:

1. STATUTORY AUTHORITY [s. 227.15 (2) (a)]

Comment Attached YES NO

2. FORM, STYLE AND PLACEMENT IN ADMINISTRATIVE CODE [s. 227.15 (2) (c)]

Comment Attached YES NO

3. CONFLICT WITH OR DUPLICATION OF EXISTING RULES [s. 227.15 (2) (d)]

Comment Attached YES NO

4. ADEQUACY OF REFERENCES TO RELATED STATUTES, RULES AND FORMS
[s. 227.15 (2) (e)]

Comment Attached YES NO

5. CLARITY, GRAMMAR, PUNCTUATION AND USE OF PLAIN LANGUAGE [s. 227.15 (2) (f)]

Comment Attached YES NO

6. POTENTIAL CONFLICTS WITH, AND COMPARABILITY TO, RELATED FEDERAL
REGULATIONS [s. 227.15 (2) (g)]

Comment Attached YES NO

7. COMPLIANCE WITH PERMIT ACTION DEADLINE REQUIREMENTS [s. 227.15 (2) (h)]

Comment Attached YES NO

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CLEARINGHOUSE RULE 98-114

Comments

[NOTE: All citations to "Manual" in the comments below are to the Administrative Rules Procedures Manual, prepared by the Revisor of Statutes Bureau and the Legislative Council Staff, dated September 1998.]

2. Form, Style and Placement in Administrative Code

a. In s. DFI-Sec 1.02 (5) (c) 2. (intro.), the added language should be replaced by "subd. 1.".

b. In s. DFI-Sec 1.02 (14) (intro.), a colon should be inserted after "Stats." The definitions following the (intro.) should be put in alphabetical order, beginning with "'Client" has the meaning given in . . ."; that is, the "A" or "An" at the beginning of defined terms should be deleted. In addition, all of the definitions in s. DFI-Sec 1.02, including the new definitions, should be alphabetized.

In par. (a) 2., "employee" should be "employe" and "employees" should be "employes." The entire rule should be reviewed for this change.

In par. (b), the "except that" clause needs to be redrafted to fit more clearly into the definition. It appears to say "except that "client" does not include a person who is not a resident of the United States if the supervised person decides not to count that client as a client." This is not suggested language, just a reiteration of what the language appears to say. The clause should be redrafted beginning with "except that "client" . . .".

In par. (c) 2., the parentheses should be replaced by commas.

c. In s. DFI-Sec 1.02 (15), a comma should be inserted after "1 to 9".

d. The material in s. DFI-Sec 1.02 (16) is not a definition and should therefore be placed in a different section.

e. In s. DFI-Sec 1.02 (17) and (18), "for purposes of the licensing provisions of ch. 551, Stats., and related rules in chs. DFI-Sec 1 to 9," is not needed and should be deleted. Current s. DFI-Sec 1.02 (intro.) states the applicability of all terms that are defined in that section.

f. In s. DFI-Sec.1.02 (18), "such assets" should be replaced by "customer funds or securities."

g. The treatment clause for SECTION 15 should state: "SECTION 15. DFI-Sec 2.04 is created to read:". Also, in s. DFI-Sec 2.04 (1) (a) and (2), "there shall be filed" should be replaced by "the issuer shall file." In the second sentence of par. (1) (a), "Additionally" should be deleted.

Subsections (2), (3) and (4) specify that a "notice" has to be filed but does not specify what it is notice of (i.e., "notice of . . ."); these provisions should be clarified.

h. In SECTION 23, the title does not have to be underlined since it is being repealed and recreated. [See s. 1.06 (5), Manual.]

i. In SECTION 26, "an" should be inserted after "sub (2).".

j. In several treatment clauses that involve renumbering a rule, the prefix "DFI-Sec" should be inserted before the number of the renumbered rule. For example, in the treatment clause for SECTION 27, "DFI-Sec" should be inserted before "5.02 (3)." Also, a period is needed at the end of SECTION 27.

k. In s. DFI-Sec 5.02 (4), "such" should be replaced by "that" in two places. The same comment applies to s. DFI-Sec 5.03 (7).

l. In s. DFI-Sec 5.04 (7), "at the same time it files" should replace "incident to." In sub. (8), "with the division at the same time it files" should replace "contemporaneously with its filing."

4. Adequacy of References to Related Statutes, Rules and Forms

a. Section DFI-Sec 1.02 (5) (c) 2. refers to "Rule 206 (4)-3. of the investment advisers act of 1940." The U.S. Code cite to this provision should be included. [See s. 1.07 (3), Manual.]

b. In s. DFI-Sec 5.07 (2), "s. 551.32. (1m) (a)" should be "s. 551.32 (1m) (a)" (i.e., delete the period after "551.32"). The same comment applies to the reference to that provision in sub. (4) of that section. Also in sub. (4), second sentence, the citation should read "9.01 (1) (b) 20." (i.e., insert a period after the subdivision number).

c. Although s. DFI-Sec 9.01 (1) (intro.) states that the forms listed in that subsection may be obtained from the division of securities in Madison, the division should consider listing

its address and telephone number in a note. Since some of these forms are available on the Internet, the division should consider listing its web site in the note. [See s. 1.09 (2), Manual.]

8/7/98

DEPARTMENT OF FINANCIAL INSTITUTIONS
DIVISION OF SECURITIES

Proposed Permanent Rules to Implement 1997 Wisconsin Act 316 Relating to Federal Covered Securities, Federal Covered Advisers and Investment Adviser Representatives

SECTION 1. DFI-Sec 1.02(2)(b) is amended to read:

DFI-Sec 1.02(2)(b) A licensed investment adviser or federal covered adviser when placing orders for the accounts of its clients in accordance with rules prescribed by the division, provided that no commission or other remuneration is received by the investment adviser solely for placing the orders.

ANALYSIS: The amendment to this rule (which currently provides an exclusion from the definition of broker-dealer for licensed investment advisers) extends the exclusion to also cover "federal covered advisers." Federal covered advisers are a new category of investment advisers designated by statute in 1997 Wisconsin Act 316, corresponding to federal legislation impacting state securities laws under the National Securities Markets Improvement Act ("NSMIA").

SECTION 2. DFI-Sec 1.02(5) (c)2. (intro.) and 2.a. are amended to read:

DFI-Sec 1.02(5)(c)2. Any person who complies with Rule 206(4)-3. of the investment advisers act of 1940 and meets any of the following conditions is not considered to be

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“soliciting” for purposes of ~~s. 551.31(3), Stats. subd. (c)1~~, and the definition of “transact business” in sub. (5):

2.a. The person is licensed in this state as an investment adviser or ~~is qualified as an investment adviser representative of an investment adviser licensed in this state; or~~

ANALYSIS: These amendments do the following: (1) In (c)2. (intro.), correct the cross-reference used in the rule to reflect the proper administrative rule provisions that are applicable; and (2) in (c)2.a., deletes the term “qualified” as it applies to investment adviser representatives because 1997 Wisconsin Act 316 replaced the prior “qualification” requirement with a licensing requirement.

SECTION 3. DFI-Sec 1.02(5) (c)2.d. is created to read:

DFI-Sec 1.02(5)(c)2.d. The person is a federal covered adviser.

ANALYSIS: This amendment adds the category of “federal covered adviser,” as created under 1997 Wisconsin Act 316, to the list of persons who can qualify for an exclusion from the definition of “soliciting” if the person complies with the requirements of Rule 206(4)-3 of the federal Investment Advisers Act of 1940.

SECTION 4. DFI-Sec 1.02(7)(b) is amended to read:

DFI-Sec 1.02(7)(b) “Branch office” for purposes of the investment adviser provisions of ch. 551, Stats., and chs. DFI-Sec 1 to 9 means any office in this state of an investment adviser or federal covered adviser that is held out to the public by any means as a business location of the investment adviser.

ANALYSIS: The amendment is needed to make this rule (defining "branch office" for purposes of the investment adviser provisions of the Wisconsin Securities Law and rules) apply also to federal covered advisers, as created in 1997 Wisconsin Act 316.

SECTION 5. DFI-Sec 1.02(14) is created to read:

DFI-Sec 1.02(14) The following defined terms apply for purposes of the definition of "investment adviser representative" in s. 551.02(7m)(a), Stats. °

(a) A "supervised person" means any of the following:

1. Any partner, officer or director of, or other person occupying a similar status or performing similar functions for, an investment adviser or federal covered adviser.
2. Any employee of an investment adviser or federal covered adviser, except for a clerical or ministerial employees.
3. Any other person who provides investment advice on behalf of an investment adviser and is subject to the supervision and control of the investment adviser or federal covered adviser.

(b) A "client" has the same definition as that set forth in rule 275.203(b)(3)-1 under section 203 of the investment advisers act of 1940, (except that supervised persons need not count clients that are not residents of the United States.)

(c) An "excepted person" means any of the following:

1. A natural person who, immediately after entering into an investment advisory contract with an investment adviser, has at least \$500,000 under management with the investment adviser.

2. A natural person who the investment adviser reasonably believes, immediately prior to entering into an advisory contract, has a net worth ^(together with assets held jointly with a spouse) at the time the contract is entered into of more than \$1,000,000, ^{and one's net worth of spouse}
- (d) "Impersonal investment advice" means investment advisory services provided by means of written material or oral statements that do not purport to meet the objectives or needs of specific individuals or accounts.
- (e) "Third party solicitor" means a person soliciting clients on behalf of a licensed investment adviser or a federal covered adviser who is neither a partner, officer, director, ^{or} or employee of the adviser, nor a supervised person of that adviser.

ANALYSIS: The rules in paras. (14)(a) to (e) of this SECTION define all of the substantive terms contained in the definition of "investment adviser representative" created in 551.02(7m)(a) ^{Stats.} by the 1997 Wisconsin Act 316, with language corresponding to federal statutes and rules defining those same terms. In particular: (1) "supervised person" in para. (a) corresponds with language in section 202(a)(25) of the Investment Advisers Act of 1940 as created in Title III of NSMIA, except for references to "federal covered adviser" added at the end of subd. (a)1, 2 and 3, and an exclusion for "clerical or ministerial employees" in subd. (a)2 based on language contained in the definition of "investment adviser representative" in section 401(g) of the Uniform Securities Act of 1956; (2) "client" in para. (b) corresponds with the federal rule definition cited, including that non-U.S. residents need not be counted; (3) "excepted person" and "impersonal investment advice" in paras. (c) and (d) correspond with the federal rule definitions in 203A-3(a)3(i) and 3(ii) under the Investment Advisers Act of 1940; (4) "third party

solicitor” in para. (e) is based on the U.S. Securities and Exchange Commission’s commentary to its investment adviser rulemaking relating to the cash solicitation rule in 2.06(4)-3 under the Investment Advisers Act of 1940.

SECTION 6. DFI-Sec 1.02(15) is created to read:

DFI-Sec 1.02(15) “Place of business” for purposes of the investment adviser provisions of ch. 551, Stats., and chs. DFI-Sec 1 to 9, means any location held out to the public by any means at which an investment adviser or an investment adviser representative regularly provides investment advisory services, or solicits, meets with, or otherwise communicates with clients or prospective clients.

ANALYSIS: This rule defines the term “place of business” for purposes of the investment adviser licensing statutes and rules based on subsection (b)(1) of the federal definition of “place of business” in rule 203A-3 [as amended effective July 8, 1997] under the Investment Advisers Act of 1940.

SECTION 7. DFI-Sec 1.02(16) is created to read:

not a def. → **DFI-Sec 1.02(16)** For purposes of s. 551.02(7m)(a)1.a., Stats., the specified percentage of clients of the supervised person who are natural persons that are not excepted persons shall be 10%. 7

ANALYSIS: This rule establishes for purposes of the definition of “investment adviser representative” in s. 551.02(7m)(a)1.a., Stats., the percentage of clients of a supervised person “who are natural persons that are not excepted persons.” The 10% number

established in this rule is the same percentage used in federal rule 203A-3(a)(1) [as amended effective July 8, 1997] under the Investment Advisers Act of 1940.

SECTION 8. DFI-Sec 1.02(17) and (18) are created to read:

alpha → **DFI-Sec 1.02(17)** “Principal office” for purposes of the licensing provisions of ch. 551, Stats., and related rules in chs. DFI-Sec 1 to 9, means the office from which the officers, partners, or managers of a broker-dealer or an investment adviser direct, control, and coordinate the activities of the broker-dealer or investment adviser. *Sec 1.02 (intro.)*

(18) “Custody” for purposes of the licensing provisions of ch. 551, Stats., and related rules in chs. DFI-Sec 1 to 9, includes having possession of customer funds or securities or the power to access or control the disposition of *cust funds or securities* such assets to third parties.

ANALYSIS: These new definitional rules do the following: (1) define “principal office” for purposes of the securities licensing statutes and related rules, using identical language from rule 203A-3(c) [as amended effective July 8, 1997] under the Investment Advisers Act of 1940; and (2) define “custody” for purposes of the Wisconsin securities licensing statutes and related rules using language derived from the U.S. Securities and Exchange Commission’s staff interpretations of what activities or practices constitute “custody” under rule 206(4)-2 of the Investment Advisers Act of 1940.

SECTION 9. Chapter DFI-Sec 2 (Title) is amended to read:

Chapter DFI-Sec 2

REGISTRATION EXEMPTIONS AND FEDERAL
COVERED SECURITY NOTICE FILINGS

ANALYSIS: This SECTION amends the Title to Chapter 2 of the Division's rules to reflect that the administrative rules relating to making notice filings for various categories of federal covered securities provided for in s. 551.29(1) to (3), Stats., (as created in 1997 Wisconsin Act 316) are being placed in Chapter 2.

SECTION 10. DFI-Sec 2.01(1)(a)2 is amended to read:

DFI-Sec 2.01(1)(a)2. Any securities of the enterprise, or any securities of an unconditional guarantor of all payments under the lease, sale or loan arrangement, are covered securities under section 18(b)(1) of the securities act of 1993 or are exempt under s. 551.22(7), Stats.

ANALYSIS: This amendment adds a cross-reference to the section of NSMIA that now designates as "covered securities" securities listed on various securities exchanges that (pre-NSMIA) had been designated for purposes of the "exchange listing" registration exemption in s. 551.22(7), Wis. Stats. Because NSMIA's designation of qualifying exchanges in Section 18(b)(1) preempts s. 551.22(7), Wis. Stats., a cross-reference to that NSMIA section is necessary to give effect to the rule.

SECTION 11. DFI-Sec 2.01(3)(a) to (d) are repealed.

ANALYSIS: This SECTION deletes the rule subsections in 2.01(3)(a) to (d) which designate for purposes of the "exchange-listing" registration exemption in s. 551.22(7), Stats., the following exchanges: (1) the National Market System of NASDAQ [in sub (a)]; (2) the Chicago Board Options Exchange [in sub (b)]; (3) Tier 1 of the Pacific Stock Exchange [in sub (c)]; and (4) Tier 1 of the Philadelphia Stock Exchange [in sub (d)].

The deletions are warranted because those Wisconsin registration exemption designations are preempted and superseded by the designation in Section 18 (b)(1) of NSMIA of the National Market System of NASDAQ as a "covered security," and by adoption on January 14, 1998, of Rule 146(b) under the Securities Act of 1993 by the U.S. Securities and Exchange Commission designating securities listed on the Chicago Board Options Exchange, Tier 1 of the Pacific Stock Exchange, and Tier 1 of the Philadelphia Stock Exchange as "covered securities" for purposes of Section 18 of the Securities Act of 1933.

SECTION 12. DFI-Sec 2.01(9) and (10)(a) are amended to read:

DFI-Sec 2.01(9) Any government security, other than a revenue obligation and other than a security issued or guaranteed by the United States or an agency or corporate instrumentality of the United States, issued by the state of Wisconsin or any political subdivision or agency or corporate or other instrumentality of the state of Wisconsin, is exempted under s. 551.22(17), Stats., if it is a security which matures within 16 months of date of issue and the issuer has levied a direct annual irrevocable tax under article XI, section 3, Wis. Const. or otherwise pledged levied taxes sufficient in amount to pay the interest on the securities as it falls due and also to pay and discharge the principal on the securities at maturity.

(10) (a) Any government security, other than a revenue obligation and other than a security issued or guaranteed by the United States or an agency or corporate instrumentality of the United States, issued by the state of Wisconsin or any political subdivision or agency or corporate or other instrumentality of the state of Wisconsin, is exempted under s. 551.22(17), Stats., if a notice of the proposed offering containing the information in par. (b) is filed with the

division prior to the offering and the division does not by order deny the exemption within 10 days of the date the notice is filed.

ANALYSIS: The amendments to each of these registration exemption rules under 551.22(17), Stats., do the following: (1) delete the rule language referring to U.S. government securities because such securities are designated in NSMIA as “covered securities” under Section 18(b)(4)(C) of the Securities Act of 1933, thus preempting all state securities registration and exemption requirements; and (2) substitute language making each exemption rule applicable only to the securities (other than revenue obligations) issued by the State of Wisconsin or its political subdivisions, agencies or instrumentalities, because NSMIA does permit a state’s securities registration exemption provisions to apply when the governmental issuer of the securities is located in such (home) state. Accordingly, applicability of these exemption rules are limited to Wisconsin governmental issuers.

SECTION 13. DFI-Sec 2.02(9)(a) is repealed.

ANALYSIS: The repeal of this registration exemption rule under s. 551.23(18), Wis. Stats., (which applies to certain isolated sales of the securities of an investment company) is warranted because all investment company securities are designated in NSMIA as “covered securities” under Section 18(b)(2) of the Securities Act of 1933, thus preempting all state securities registration and exemption requirements.

SECTION 14. DFI-Sec 2.02(9)(L) is repealed.

ANALYSIS: The repeal of this registration exemption rule under s. 551.23(18), Wis. Stats., (which applies to securities of a unit investment trust, a type of investment company under the Investment Company Act of 1940) is warranted because all investment company securities are designated in NSMIA as "covered securities" under Section 18(b)(2) of the Securities Act of 1933, thus preempting all state securities registration and exemption requirements.

Perk
SECTION 15. DFI-Sec 2.04(1) to (4) are created to read:

DFI-Sec 2.04 FEDERAL COVERED SECURITY NOTICE FILINGS. (1)(a) With respect to a federal covered security referred to in s. 551.29(1)(a), Stats., there shall be filed with the division not later than the initial offer of the security in this state, a consent to service of process signed by the issuer and the notice filing fee prescribed under s. 551.52(1)(a), Stats.

~~Additionally,~~ if a completed Form NF as prescribed in DFI-Sec 9.01(1)(d) is included with the consent to service of process and the notice filing fee, the issuer *is not required to* ~~need not also~~ include with the filing copies of any documents that are part of the registration statement filed under the securities act of 1933, *except that* although the division may at a later time require the filing of a copy of any *of these* documents that is part of the registration statement filed under the securities act of 1933.

(b) After the initial offer in this state of a federal covered security referenced in s. 551.29(1)(a), Stats., if the issuer files an amendment to its registration statement with the securities and exchange commission under the securities act of 1933 that relates either to a name change of the issuer, or to a change in the designation of the federal covered security, there shall be filed with the division concurrent with the federal filing, a fee of \$200, which shall be accompanied by a copy of each amendment-related document filed with the securities and

exchange commission unless the issuer files with the division a completed Form NF as prescribed in DFI-Sec 9.01(1)(d). The division may at a later time require the filing of a copy of any document relating to the amendment filed under the securities act of 1933.

(2) With respect to a federal covered security referred to in s. 551.29(2), Stats., there shall be filed with the division not later than 15 days after the first sale of the security in this state, a notice ^{of what?} consisting of a completed Form D as prescribed by rule 503 of regulation D under the securities act of 1933, signed by the issuer, together with a \$200 fee.

(3) With respect to a federal covered security referred to in s. 551.29(3), Stats., that is a revenue obligation issued by a non-Wisconsin governmental issuer which, prior to the National Securities Market Improvement Act of 1996 would have required a filing with the division under s. 551.22(1)(b), Stats., there shall be filed with the division not later than the earlier of the first offer or sale in this state, ^{of what?} a notice consisting of a \$200 fee and which, in order to provide information about the offering for the division's database, may at the option of the issuer include a letter identifying the securities being offered, the aggregate dollar amount of the offering, the name of the governmental issuer, and the name and address of the non-governmental industrial or commercial enterprise providing payment of the principal and interest on the security.

(4) With respect to a federal covered security referred to in s. 551.29(3), Stats., that is being exchanged by the issuer with its existing securityholders and which, prior to the National Securities Market Improvement Act of 1996 would have required a filing with the division under s. 551.23(12), Stats., there shall be filed with the division not later than the earlier of the first offer or sale in this state, ^{of what?} a notice consisting of a \$200 fee and a copy of each document relating to the offering filed under the securities act of 1933. If the issuer is not required to file documents relating to the offering under the securities act of 1933, in order to provide

information about the offering and the issuer for inclusion in the division's database, the issuer at its option) may include with the notice a letter identifying the issuer and its address, the securities being offered and the aggregate dollar amount of the offering.

ANALYSIS: This SECTION creates a new section of the securities rules (DFI-Sec 2.04) dealing specifically with the categories of "federal covered securities" created federally in NSMIA that are also dealt with for state securities law purposes in s. 551.29, Stats., in 1997 Wisconsin Act 316. Each subsection of 551.29, Stats., grants rulemaking authority to the Division to adopt rules regarding filing requirements relating to the categories of federal covered securities dealt with in the particular subsection.

The rules in DFI-Sec 2.04(1)(a) and (b) parallel the statutory notice filing provisions for investment company federal covered securities contained in ss. 551.29(1)(a), Stats., (for initial offerings) and (1)(b) (for amendment filings) which set forth the prescribed materials to be filed and fees. Each of the rule subsections particularizes an option available to the issuer (referred to in each statutory section) which provides that copies of federally-filed documents need not be included with the filing with the Division if a completed Form NF [as prescribed in DFI-Sec 9.01(1)(d)] accompanies the filing with the Division. The rule also provides, however, that the Division may at a later time following such filing, require that copies of federally-filed documents be provided to the Division.

The rule in DFI-Sec 2.04(2) parallels the statutory notice filing provisions for Regulation D-Rule 506 federal covered security offerings contained in s. 551.29(2), Stats., with respect to the materials required to be filed, the fee, and the prescribed filing deadline.

The rule in DFI-Sec 2.04(3) is adopted under the rule-making authority granted to the Division under s. 551.29(3), Stats., to establish notice filing requirements – including a fee and any federally-filed documents – for categories of federal covered securities created under NSMIA as specified in section 18(b)(3) or (4) of the federal Securities Act of 1933. This rule applies solely to certain types of state/municipal governmental securities [which are included under Section 18(b)(4) as an exempt security in Section 3(a)(2) of the Securities Act of 1933]; namely, revenue obligations issued by a non-Wisconsin governmental issuer which, prior to NSMIA would have required a filing with the Division under s. 551.22(1)(b), Stats. The rule prescribes a required \$200 notice filing fee and, because such governmental securities offerings do not have to file any documents federally, the rule also states that in order to provide basic information about the offering and the issuer for inclusion in the Division's database, the issuer has the option of including with the notice a letter identifying the securities offered, the aggregate dollar amount of the offering, the name of the governmental issuer, and the name and address of the non-governmental industrial or commercial enterprise providing payment of the principal and interest on the security.

The rule in DFI-Sec 2.04(4) is adopted under the rule-making authority granted to the Division under s. 551.29(3), Stats., to establish notice filing requirements – including a fee and any federally-filed documents – for categories of federal covered securities created under NSMIA as specified in section 18(b)(3) or (4) of the federal Securities Act of 1933. This rule applies solely to exchange offers by securities issuers with their

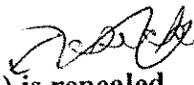
existing securityholders (which are included under Section 18(b)(4) as an exempt security in Section 3(a)(12) of the Securities Act of 1933). The rule prescribes a required \$200 notice filing fee and a copy of each document relating to the offering filed under the Securities Act of 1933. Also, similar to rule DFI-Sec 2.04(3) above, the rule states that if the issuer does not have to file any documents relating to the offering under the Securities Act of 1933, in order to provide the Division with basic information about the offering and the issuer for inclusion in the Division's database, the issuer has the option of including with the notice a letter identifying the issuer and its address, the securities being offered and the aggregate dollar amount of the offering.

SECTION 16. DFI-Sec 3.01(1)(a) is amended to read:

DFI-Sec 3.01(1)(a) Copies of the articles of incorporation and by-laws or equivalents currently in effect, any agreements with or among underwriters, any instrument governing the issuance of the security to be registered, a specimen of the security and, if the security to be registered is a note, bond, debenture or other evidence of indebtedness, a trust indenture meeting the requirements of s. DFI-Sec 3.04, ~~unless the security is a face amount certificate registered under the investment company act of 1940 or unless the requirement to furnish a trust indenture relating to the securities is waived by the division for good cause shown; and~~

ANALYSIS: The amendment to this rule (which lists certain information to be included with a filing for registration by coordination under s. 551.25, Stats.) repeals the reference to securities of a face amount certificate company (a type of investment company under the Investment Company Act of 1940) because under NSMIA, all investment company

securities are designated as "covered securities" under Section 18(b)(2) of the Securities Act of 1933, thus preempting state securities statute and rule registration provisions.


SECTION 17. DFI-Sec 3.01(2) is repealed.

ANALYSIS: The repeal of this procedural rule under the securities registration by coordination section (which rule relates to registration of an indefinite amount of securities for certain categories of investment companies) is warranted for the following reasons: (1) Under NSMIA, all investment company securities are designated as "covered securities," thus preempting state securities statute and rule registration provisions (although registration or exemption can be required for non-payment of notice filing fees); (2) If the securities of an investment company are subject to registration in Wisconsin by application of s. 551.29(4), Stats., (in 1997 Wisconsin Act 316), as a result of non-payment of fees, the existing statutory provisions of s. 552.52(1)(b)1, Stats., (as amended by 1997 Wisconsin Act 316) serve to provide for an indefinite amount of securities to be registered.

SECTION 18. DFI-Sec 3.02(1)(h) is amended to read:

DFI-Sec 3.02(1)(h) The kind of securities and the amount to be offered (~~which, in the case of redeemable securities of an open-end management company, unit investment trust and face amount certificate company, as defined in the investment company act of 1940, shall be indefinite~~); the proposed offering price or the method by which it is to be computed; and variation therefrom at which any proportion of the offering is to be made to any person or class of persons other than the underwriters, with a specification of any such person or class; the basis

upon which the offering is to be made if otherwise than for cash; the estimated aggregate underwriting and selling discounts or commissions and finders' fees (including separately cash, securities, contracts, or anything else of value to accrue to the underwriters or finders in connection with the offering) or, if the selling discounts or commissions are variable, the basis of determining them and their maximum and minimum amounts; the estimated amounts of other selling expenses, including legal, engineering, and accounting charges; the name and address of every underwriter and every recipient of a finder's fee; a copy of any underwriting or selling group agreement pursuant to which the distribution is to be made, or the proposed form of any such agreement whose terms have not yet been determined; and a description of the plan of distribution of any securities which are to be offered otherwise than through an underwriter;

ANALYSIS: This amendment deletes the references in the rule to several categories of investment companies because under NSMIA, all investment company securities are designated as "covered securities" under Section 18(b)(2) of the Securities Act of 1933, thus preempting state securities statute and rule regulation provisions.

SECTION 19. DFI-Sec 3.02(1)(m) is amended to read:

DFI-Sec 3.02(1)(m) A specimen or copy of the security being registered; a copy of the issuer's articles of incorporation and bylaws, or equivalents, as currently in effect; and if the security to be registered is a note, bond, debenture or other evidence of indebtedness, a trust indenture meeting the requirements of s. DFI-Sec 3.04, ~~unless the security is a face amount certificate registered under the investment company act of 1940 or unless the requirement to~~ furnish a trust indenture relating to the securities is waived by the division for good cause shown;

ANALYSIS: See ANALYSIS to DFI-Sec 3.01(1)(a).

SECTION 20. DFI-Sec 3.03(3) is amended to read:

DFI-Sec 3.03(3) The prospectus shall contain a full disclosure of all material facts relating to the issuer and the offering and sale of the registered securities. A prospectus meeting the requirements under the securities act of 1933 that receives full review by the U.S. securities and exchange commission, shall not be subject to disclosure adequacy review or comment by the division. ~~A prospectus meeting the requirements of form N-1A or form S-6 and subsequent post effective amendments as filed under the securities act of 1933, or the investment company act of 1940, or both, by a registration applicant or an existing registrant shall not be subject to disclosure adequacy review or comment by the division.~~ If the offering is being made pursuant to use of either Rule 504 of Regulation D under the securities act of 1933 or rule 147 under section 3(a)(11) of the securities act of 1933, the form U-7 disclosure document as adopted by the North American Securities Administrators Association, Inc. may be used.

ANALYSIS: The amendment to this rule (relating to staff review of the disclosure adequacy of prospectuses contained in registration filings) deletes reference to prospectuses for investment company securities because under NSMIA, state securities administrators may not impose merit requirements or conduct a disclosure adequacy review of prospectuses for investment company securities.

SECTION 21. DFI-Sec 3.07(1) and (2) are amended to read:

DFI-Sec 3.07 EXTENSION OF REGISTRATION STATEMENTS. (1) Application for an extension of the offering period of a registration statement, except one relating to ~~redeemable securities issued by an open end management company or a face amount certificate~~

~~company as defined in the investment company act of 1940, or securities of a finance company~~ licensed under s. 138.09, Stats., shall be filed in the form prescribed by the division not less than 30 days prior to the end of one year from the effective date of the registration statement or an extended period of effectiveness for the registration statement, whichever is most recent. The application shall be accompanied by a prospectus updated in accordance with s. DFI-Sec 3.03(6), a balance sheet of the issuer as of the end of its most recent fiscal year, and a comparative statement of income and changes in financial position and analysis of surplus for each of the 3 most recent fiscal years (or for the period of the issuer's and any predecessor's existence if less than 3 years), all meeting the requirements of s. DFI-Sec 7.06, provided that if the date of any of the above financial statements is more than 120 days (180 days with respect to a corporation organized and operated not for private profit but exclusively for religious, educational, benevolent or charitable purposes) prior to the date of the extension of the registration statement, the statements shall be updated (which may be done without audit) to within the 120-day or 180-day requirement above. If no order specifying a different effectiveness period is in effect, renewal of the registration statement becomes effective on the day on which the prior registration statement expires or at such earlier time as the division determines.

(2) A registration statement relating to ~~redeemable securities issued by an open end management company or a face amount certificate company as defined in the investment company act of 1940, or securities of a finance company~~ licensed under s. 138.09, Stats., is deemed to include an application for the continuous offering of the securities. The offering period of the registration statement is automatically extended until it is permitted to be withdrawn or the division issues a stop order suspending or revoking its effectiveness pursuant to s. 551.28, Stats., if the issuer ~~complies with s. 551.52(1)(b), Stats., which may involve the filing~~

of form RS-IC as referred to in s. DFI-Sec 9.01, and if the issuer files with the division not less than annually during the offering period, within 120 days of the end of its fiscal year, a prospectus updated in accordance with s. DFI-Sec 3.03(6), a balance sheet of the issuer as of the end of the fiscal year, and a statement of income and change in financial position and analysis of surplus of the issuer for the fiscal year meeting the requirements of s. DFI-Sec 7.06.

ANALYSIS: The amendments to these registration exemption rules (relating to extensions) do the following: (1) Delete the references at the beginning of subs. (1) and (2) to certain categories of investment companies because under NSMIA, all investment company securities are designated as "covered securities" under Section 18(b)(2) of the Securities Act of 1933, thus preempting state securities statute and rule registration provisions. (2) The second deletion in sub. (2) is necessary because as a result of the deletion in the first part of the subsection, the subsection relates only to the securities of finance company issuers.

SECTION 22. In the following rules, each reference therein to "qualified" is amended to read "licensed": DFI-Sec 5.01(4)(b), 5.01(5) and (7), 5.05(7) and (10).

ANALYSIS: The legislation in 1997 Wisconsin Act 316 contained a specific licensing requirement (in s. 551.31(3), Stats.) for representatives of investment advisers, replacing a "qualification" provision that had previously existed. This SECTION makes the appropriate amendment (changing the terminology from "qualified" to "licensed") in those rule provisions specified in Chapter DFI-Sec 5 where that is the only amendment necessary.

Should actually change each of these in RULES
OK

SECTION 23. Chapter DFI-Sec 5 (title) is repealed and recreated to read:

CHAPTER DFI-SEC 5

LICENSING AND NOTICE FILING PROCEDURES FOR
INVESTMENT ADVISERS, FEDERAL COVERED ADVISERS, AND
INVESTMENT ADVISER REPRESENTATIVES

NO
underline
1.1.1.1

ANALYSIS: This SECTION amends the Title of Chapter DFI-Sec 5 of the rules to reflect that its scope has been expanded as a result of enactment of 1997 Wisconsin Act 316 which provides authority to now regulate investment adviser representatives as licensees and establish notice filing and related procedures for certain federal covered advisers.

SECTION 24. DFI-Sec 5.01(1) is amended to read:

DFI-Sec 5.01 LICENSING PROCEDURE. (1) Applications for initial and renewal licenses and qualifications of investment advisers and their investment adviser representatives shall be filed on forms prescribed by the division in s. DFI-Sec 9.01 (1).

ANALYSIS: These technical amendments delete the reference in the rule to “qualification,” and add language to have the rule apply to “investment adviser representatives” which is now a defined term as created in 1997 Wisconsin Act 316.

SECTION 25. DFI-Sec 5.01(3) is amended to read:

DFI-Sec 5.01(3) Unless waived under sub. (4), each applicant for an initial license as an investment adviser or for qualification as an investment adviser representative after January 1, 1996 July 9, 1998, and each applicant whose application has not become effective by January 1,

1996 July 9, 1998, is required to pass either of the following examinations with a grade of at least 70%:

ANALYSIS: These technical amendments delete the reference in the rule to “qualification” and substitute for the January 1, 1996 date therein, the effective date of 1997 Wisconsin Act 316 that contains amendments to the investment adviser and investment adviser representative licensing requirement.

SECTION 26. DFI-Sec 5.02(1) is amended to read:

DFI-Sec 5.02 NET CAPITAL REQUIREMENT. (1) ~~Every~~ Except as required under sub. (2), ^{every an} investment adviser whose principal office is in this state that collects advisory fees 6 months or more in advance or collects more than \$2,000 in advance fees for preparing a financial plan shall maintain net capital of not less than \$5,000, which shall be in the form of cash or securities or other liquid assets as determined by the division.

ANALYSIS: Under NSMIA, no state can impose regulations establishing net capital, bonding, or books and records requirements on an investment adviser beyond those required under the laws of the state in which the investment adviser maintains its principal place of business. Accordingly, this existing net capital rule subsection is amended to provide that it is applicable only to investment advisers having a principal office in Wisconsin. The new, separate, net capital rule created below in DFI-Sec 5.02(2) for investment advisers having custody of client funds or securities similarly is made applicable only to investment advisers having a principal office in Wisconsin. The net capital requirement of \$35,000 or 1% of assets under management is taken from a proposed Model Rule on this subject [§ 202(d)-1(a)(1)] developed by a North American

Securities Administrators Association Working Group on investment adviser capital and bonding requirements..

578-sec

SECTION 27. DFI-Sec 5.02(2) is renumbered 5.02(3)

ANALYSIS: This SECTION moves existing rule 5.02(2) to become sub. (3) to make room for a newly-created separate net capital rule that needs to follow existing sub. (1) in sequence.

SECTION 28. DFI-Sec 5.02(2) is created to read:

DFI-Sec 5.02(2) Every investment adviser whose principal office is in this state that has custody of client funds or securities shall maintain a minimum net capital of \$35,000 or 1% of the adviser's assets under management, whichever is greater.

ANALYSIS: See the ANALYSIS to SECTION 26.

SECTION 29. DFI-Sec 5.02(3) is renumbered 5.02(6) and as renumbered is amended to read:

DFI-Sec 5.02(6) The division may by order exempt any investment adviser whose principal office is in this state from the provisions of this section, either unconditionally or upon specified conditions, if by reason of the special nature of its business or the particular facts and circumstances of the application, the division determines that compliance with the provisions is not necessary in the public interest or for the protection of investors.

ANALYSIS: Another amendment adding NSMIA-required language to provide that the substantive regulatory provisions in this existing rule relating to investment adviser net

capital requirements (this rule grants exemption/waiver authority to the Division) can only be imposed by a state on those investment advisers whose principal office is in that particular state.

SECTION 30. DFI-Sec 5.02(4) and (5) are created to read:

DFI-Sec 5.02(4) Every investment adviser that has its principal office in a state other than this state shall maintain only the minimum capital as required by the state in which the investment adviser maintains its principal office, provided that the investment adviser is licensed ^{that} in such state and is in compliance with such state's ^{net} minimum net capital requirements.

(5) For purposes of this section, the term "net capital" means an excess of assets over liabilities, as determined by generally accepted accounting principles, but shall not include as assets any of the following:

- (a) Prepaid expenses, deferred charges, goodwill, franchise rights, organizational expenses, patents, copyrights, marketing rights, unamortized debt discount and expense, and all other assets of an intangible nature.
- (b) Home, home furnishings, automobiles and any other personal items not readily marketable, if the investment adviser is an individual.
- (c) Advances or loans to stockholders and officers, if the investment adviser is a corporation.
- (d) Advances or loans to partners, if the investment adviser is a partnership.

ANALYSIS: These two new rules relating to investment adviser net capital requirements do the following: (1) in sub. (4), adopt language contained in NSMIA which provides that for investment advisers having a principal office outside Wisconsin, they need

maintain only such minimum net capital as required by the state in which the investment adviser maintains its principal office (provided that the adviser is licensed in such state and is in compliance with that state's minimum net capital requirements); (2) in sub. (5), adopt a definition of "net capital" taken from a proposed NASAA Model Rule [§202(d) - 1(c)] developed by a North American Securities Administrators Association Working Group on investment adviser capital and bonding requirements.

SECTION 31. DFI-Sec 5.03(1) is amended to read:

DFI-Sec 5.03(1) Every licensed investment adviser whose principal office is in this state shall prepare and keep current at ~~its principal~~ that office, or at a designated office located in the ~~United States~~ this state, as specified in writing to, and permitted by, the division, or at an office under the direct supervision and control of the principal or designated office, the following books and records relating to its business:

ANALYSIS: This SECTION adds NSMIA-required language to provide that substantive state regulatory provisions relating to investment adviser books and records requirements can only be imposed by a state on those investment advisers whose principal office is in that particular state.

SECTION 32. DFI-Sec 5.03(2), (3), (4), (5) and (7) are renumbered 5.03(3), (4), (5), (6) and (8), respectively, and DFI-Sec 5.03(5) and (6) as renumbered, are amended to read:

DFI-Sec 5.03(5) Every branch office as defined in s. DFI-Sec 1.02 (7) (b), of a licensed investment adviser whose principal office is in this state, shall prepare and keep current the records described in subs. (1) (c), (f), (g), (h), (k) and (L) and (2) (a) and (b).

(6) The records required in sub. (4) (5) shall be preserved at the branch office for a period of not less than 3 years, the first 2 years in an easily accessible place. Upon closing of the branch office, the records shall be transferred to the home office for the duration of the required retention period. The record may be retained by computer if a printed copy of the record can be prepared immediately upon request. If a record has been preserved for the first year of the 3-year period required in this subsection, a microfilm copy may be substituted for the remainder of the required retention period.

ANALYSIS: This SECTION does the following: (1) amends sub. (5) by adding NSMIA-required language to provide that substantive regulatory provisions in the existing rule relating to investment adviser books and records requirements (this rule requires branch offices of licensed broker-dealers to prepare and keep current certain records) can only be imposed by a state on those investment advisers whose principal office is in that particular state; (2) amends sub. (6) by renumbering the rule cross-referenced in line 1 to reflect its renumbering [from sub. (4) to sub. (5)] in the title of this SECTION.

SECTION 33. DFI-Sec 5.03(2) is created to read:

DFI-Sec 5.03(2) Each licensed investment adviser whose principal office is in this state who has custody or possession of securities or funds of any client shall maintain and keep current the following books and records in addition to those required under sub. (1):

- (a) A journal or other record showing all purchases, sales, receipts and deliveries of securities, including certificate numbers, for all accounts and all other debits and credits to the accounts.
- (b) A separate ledger for each client showing all purchases, sales, receipts and deliveries of securities, the date and price of each purchase and sale, and all debits and credits.
- (c) Copies of confirmations of all transactions effected by or for the account of any client.
- (d) A record for each security in which any client has a position, which record shall show the name of each client having any interest in each security, the amount or interest of each client, and the location of each security.

ANALYSIS: This new rule establishes an additional books and records requirement for those investment advisers whose principal office is in Wisconsin and who also have custody or possession of securities or funds of any client. Prior to enactment of 1997 Wisconsin Act 316, Wisconsin had prohibited (under sec. 551.44, Wis. Stats.) investment advisers from having custody of any client funds or securities. However, because the federal securities laws do not prohibit investment advisers from having custody of clients funds or securities, and Section 222(a) of NSMIA provides that state's investment adviser requirements cannot conflict with federal provisions, the prohibition formerly in sec. 551.44, Wis. Stats., was repealed in 1997 Wisconsin Act 316. The new rule specifies the kinds of records that licensed investment advisers having custody of customer funds and securities must maintain – which listing of records corresponds to the records specified in a proposed Model Rule on this subject [§ 202(d)-1(b)] developed by a North American Securities Administrators Association Working Group on investment adviser capital and bonding requirements.

SECTION 34. DFI-Sec 5.03(6) is renumbered 5.03(7), and as renumbered, is repealed and recreated to read:

DFI-Sec 5.03(7) Every investment adviser that has its principal office in a state other than this state shall maintain only such books and records as are required by the state in which the investment adviser maintains its principal office, provided that the investment adviser is licensed ⁱⁿ such state and is in compliance with ^{that} such state's books and records requirements.

ANALYSIS: This SECTION adds NSMIA-required language [similar to that contained in the net capital rule in DFI-Sec 5.02(4) above] to provide that for investment advisers having a principal office outside Wisconsin, they need maintain only such books and records as required by the state in which the investment adviser maintains its principal office (provided that the adviser is licensed in such state and is in compliance with that state's books and records requirements).

SECTION 35. DFI-Sec 5.04(1) is amended to read:

DFI-Sec 5.04 REPORTING REQUIREMENTS. (1) Every investment adviser shall file with the division immediate notice ^{by} ~~via~~ facsimile, whenever the net capital of the investment adviser is less than is required under s. DFI-Sec 5.02(1) or (2), specifying the amount of net capital on the date of the notice and the steps the investment adviser has taken or will take to come into compliance.

ANALYSIS: The amendment to this reporting rule (regarding net capital deficiencies) adds a cross-reference to new rule DFI-Sec 5.02(2) created above which adds an

alternative net capital requirement for any investment adviser with its principal office in Wisconsin that has custody of client funds or securities.

SECTION 36. DFI-Sec 5.04(7) and (8) are created to read:

DFI-Sec 5.04(7) Each investment adviser shall file annually with the division incident to its license renewal application, a copy of Schedule I to Form ADV confirming its regulatory status with the U.S. securities and exchange commission and the dollar amount, if any, of assets under management.

(8) Each federal covered adviser that has filed a notice with the division under s. 551.32(1m)(a), Stats., shall file a copy of its Schedule I to Form ADV ^{at the same time it files} ~~contemporaneously with~~ ~~its filing of~~ that schedule with the U.S. securities & exchange commission.

ANALYSIS: This SECTION creates two reporting rules relating to the following: (1) a requirement in sub. (7) that each investment adviser file annually with the Division incident to its license renewal application, a copy of Schedule I to Form ADV confirming its regulatory status with the U.S. Securities and Exchange Commission and the dollar amount, if any, of assets under management. Such annual information is necessary because, under NSMIA, if an investment adviser has more than \$25 million of assets under management, it becomes subject to federal regulation and triggers the definition of "federal covered adviser" in s. 551.02(4)(g), Stats., in 1997 Wisconsin Act 316 with the result that the investment adviser no longer would be subject to the Wisconsin investment adviser licensing requirements. (2) a requirement in sub. (8) that each "federal covered adviser" (as defined in s. 551.02(4)(g), Stats., in 1997 Wisconsin Act 316) required to file

a notice under s. 551.32(1m)(a), Stats., must file with the Division a copy of the Schedule I to Form ADV contemporaneously with the adviser's filing of that schedule with the U.S. Securities and Exchange Commission. Such annual information is necessary to enable the Division to verify that the federal covered adviser continues to be subject to federal regulation and not subject to state licensure under the Wisconsin Uniform Securities Law. The time for making the filing is contemporaneous with the adviser's filing the Schedule I with the U.S. Securities and Exchange Commission (rather than incident to the adviser making its annual renewal notice filing under s. 551.32(1m)(b), Stats., which is on a different annual date than its federal filing) so that the adviser will not have to keep track of a separate reporting date for the Wisconsin filing.

SECTION 37. DFI-Sec 5.05(11) (d)3. is amended to read:

DFI-Sec 5.05(11)(d)3. Establishment of a system that ensures that all books and records required by rule or order under ch. 551, Stats., are properly maintained, ~~and that precludes the investment adviser from taking or having custody of customer funds or securities as prohibited under s. 551.44, Stats.~~

ANALYSIS: The amendment to this Rule of Conduct provision deletes language relating to the statutory prohibition formerly contained in s. 551.44, Stats., (precluding investment advisers from having custody of client funds or securities) because that statutory prohibition was repealed in 1997 Wisconsin Act 316.

SECTION 38. DFI-Sec 5.05(12)(intro.) is amended to read:

DFI-Sec 5.05(12)(intro.) No investment adviser or investment adviser representative, in connection with a telephone or electronic solicitation, shall:

ANALYSIS: The amendment to this Rule of Conduct provision (relating to telephone or electronic solicitation of persons to become clients) adds language making the rule applicable to investment adviser representatives (as well as investment advisers) because 1997 Wisconsin Act 316 makes investment adviser representatives "licensees" that are subject to applicable licensing provisions of Chapter DFI-Sec 5.

SECTION 39. DFI-Sec 5.06 (intro.) is amended to read:

DFI-Sec 5.06 PROHIBITED BUSINESS PRACTICES. The following are deemed "dishonest or unethical business practices" or "taking unfair advantage of a customer" by an investment adviser or an investment adviser representative under s. 551.34 (1) (g), Stats., without limiting those terms to the practices specified in this section:

ANALYSIS: In similar fashion to the previous SECTION, the amendment to the introductory portion of the Prohibited Business Practices section of rules adds language making the section applicable to investment adviser representatives (as well as investment advisers) because 1997 Wisconsin Act 316 makes investment adviser representatives "licensees" that are subject to applicable licensing provisions of Chapter DFI-Sec 5.

SECTION 40. DFI-Sec 5.06(7) is amended to read:

DFI-Sec 5.06(7) ~~Representing itself as a~~ Using the title financial or investment planner, consultant, or adviser, when the representation does not accurately describe the nature of the

services offered, the qualifications of the person offering the services, and the method of compensation for the services;

ANALYSIS: This amendment makes a technical language change for the reason that because investment adviser representatives are now licensees subject to the Prohibited Business Practices section, the term "itself" currently contained in the rule is no longer appropriate as applied to individual persons subject to the rule.

SECTION 41. DFI-Sec 5.06(12) is created to read:

DFI-Sec 5.06(12) Taking or having custody of client funds or securities without being in compliance with rule 206(4)-2 of the investment advisers act of 1940 and the net capital requirement in s. DFI-Sec 5.02(2).

ANALYSIS: As a result of the amendment to s. 551.44, Stats., in 1997 Wisconsin Act 316 (which removed language that previously had prohibited investment advisers from having custody of client funds or securities), this rule creates as a Prohibited Business Practice, the failure by an investment adviser having custody of client funds or securities to comply with either the federal rule requirements regarding such activity or with the Wisconsin net capital rule relating to such activity.

SECTION 42. DFI-Sec 5.07 (title), (1) and (2) are amended to read:

DFI-Sec 5.07 LICENSE AND NOTICE FILING PERIOD. (1) The license of an investment adviser expires April 30 of each year. Each licensed investment adviser seeking renewal of its license shall file with the division an application for renewal not later than March 31 prior to the expiration of its license. ~~The qualification of an investment adviser representative~~

~~expires on the same day as that of the investment adviser which the person represents. The division may by order limit the period of, or specify an earlier expiration date for, any license.~~

(2) The qualification license of an investment adviser representative expires on the same day as that of the investment adviser which the person represents. The license of an investment adviser representative is not effective during any period when the investment adviser which that person represents is not licensed or during any period when the representative is not employed either by a specified investment adviser licensed under ch. 551, Stats., or a federal covered adviser that has filed a notice with the division under s. 551.32(1m)(a), Stats.

ANALYSIS: These amendments do the following: (1) add “notice filing” to the title of the section to reflect the creation in 1997 Wisconsin Act 316 of notice filing procedures for certain federal covered advisers; (2) delete the last sentence in sub. (1) relating to the expiration date for the “qualification” of an investment adviser representative because 1997 Wisconsin Act 316 provides for licensure of investment adviser representatives such that the subject matter of that last sentence in (1) can be transferred to sub. (2); and (3) add language in sub. (2) that (i) reflects the “licensure” of investment adviser representatives, (ii) transfers the “expiration date” provision from the last sentence of sub. (1) to sub. (2), and (iii) adds a reference at the end of the subsection to federal covered advisers that have filed a notice with the Division under s. 551.32(1m)(a), Stats., because investment adviser representatives can be licensed in Wisconsin to represent such federal covered advisers.

SECTION 43. DFI-Sec 5.07(3) and (4) are created to read:

DFI-Sec 5.07(3) The division may by order limit the period of, or specify an earlier expiration date for, any license.

(4) The notice filing of a federal covered adviser that has filed a notice with the division under s. 551.32(1m)(a), Stats., expires April 30 of each year. Each federal covered adviser seeking renewal of its notice filing shall file with the division the form prescribed in s. DFI-Sec 9.01(1)(b)20, not later than March 31 prior to the expiration of its notice filing.

ANALYSIS: This SECTION does the following: (1) creates in sub. (3) a separate rule taken from the last sentence of current rule DFI-Sec 5.07(1) providing authority for the Division to limit the period of, or specify an earlier expiration date for, any license; (2) creates in sub. (4) a rule prescribing a uniform expiration date for notices filed with the Division by federal covered advisers, as well as a uniform renewal filing deadline date.

SECTION 44. DFI-Sec 5.08(2) is amended to read:

DFI-Sec 5.08(2) An application for withdrawal from the status of a qualified licensed investment adviser representative shall be filed by the investment adviser which the person represents pursuant to s. 551.31(4)(c), Stats., within 15 days of the termination of the representative's employment on Form U-5 prescribed by the division.

ANALYSIS: This SECTION does the following: (1) substitutes "licensed" for "qualified" in line (1); and (2) substitutes a cross-reference to s. 551.31(4)(c), Stats., created in 1997 Wisconsin Act 316, because the two subsections in (4)(c) differ in prescribing who is responsible for filing termination/withdrawal notices for investment adviser representatives with the Division.

SECTION 45. DFI-Sec 5.09 is amended to read:

DFI-Sec 5.09 DENIAL, SUSPENSION, REVOCATION AND CENSURE. Any order denying, suspending or revoking the license of an investment adviser or an investment adviser representative or censuring a licensee may include such other sanctions as the division finds appropriate.

ANALYSIS: In similar fashion to amendments in SECTION 39 to DFI-Sec 5.06 Prohibited Business Practices, this amendment adds language making the Denial, Suspension and Revocation section (DFI-Sec 5.09) applicable to investment adviser representatives (as well as investment advisers) because 1997 Wisconsin Act 316 makes investment adviser representatives “licensees” that are subject to applicable licensing provisions of Chapter DFI-Sec 5.

SECTION 46. DFI-Sec 7.01(7)(a) is amended to read:

DFI-Sec 7.01(7)(a) Delinquent filing of broker-dealer or investment adviser license renewal application or federal covered adviser renewal notice filing.....\$100.

ANALYSIS: The amendment extends applicability of this rule (prescribing a \$100 delinquency fee for broker-dealers or investment advisers that are not timely in filing license renewals with the Division) to federal covered advisers that are not timely in filing their renewal notice required under s. 551.32(1m)(b), Stats., as created in 1997 Wisconsin Act 316. Under Section 307(b) of NSMIA, state filing-related fees applicable to investment advisers that were in effect prior to enactment of NSMIA are preserved.

SECTION 47. DFI-Sec 7.01(7)(d) is amended to read:

DFI-Sec 7.01(7)(d) Delinquent filing of notice of broker-dealer, ~~or investment adviser or~~
federal covered adviser branch office registration, renewal, relocation or
closing.....\$100.

ANALYSIS: The amendment extends applicability of this rule (prescribing a \$100 delinquency fee for broker-dealers and investment advisers that are not timely in providing notice of branch office openings, closings or relocations) to federal covered advisers. Under Section 307(b) of NSMIA, state filing-related fees applicable to investment advisers that were in effect prior to enactment of NSMIA are preserved.

SECTION 48. DFI-Sec 7.01(7)(f) is amended to read:

DFI-Sec 7.01(7)(f) Delinquent filing of broker-dealer agent, ~~or agent for issuer license renewal, or of investment adviser representative~~ license renewal.....\$100.

ANALYSIS: The amendment to this delinquent filing fee rule (which includes applicability to investment adviser representatives) adds language to reflect that as a result of 1997 Wisconsin Act 316, investment adviser representatives are now “licensed.”

SECTION 49. DFI-Sec 9.01(1)(b)12. and 13. are amended to read:

DFI-Sec 9.01(1)(b)12. ADV. Uniform application for investment adviser registration license.

13. IAR(WI). Application for renewal of investment adviser ~~license and qualification of~~
and investment adviser representatives representative license.

ANALYSIS: The amendments to these two licensing-related Forms rules do the following: (1) correct the terminology used in subd. (1)(b) 12 by changing the current

language investment adviser “registration” (federal terminology) to read investment adviser “license” and thereby reflect the Wisconsin state licensing status for investment advisers; and (2) substitute in subd. (1)(b) 13, the terminology “licensed” for “qualified” reflecting the licensing requirement for investment adviser representatives created under 1997 Wisconsin Act 316.

SECTION 50. DFI-Sec 9.01(1)(b)20. and 21. are created to read:

DFI-Sec 9.01(1)(b)20. IAN(WI) Federal covered adviser initial and renewal notice filing form.

21. ADV-W. Application for withdrawal of investment adviser license.

ANALYSIS: These new licensing-related Forms rules do the following: (1) create in subd. (1)(b)20 a specific form for use by federal covered advisers in making their initial or renewal notice filings under ss. 551.32(1m)(a) and (b), Stats.; and (2) designate Form ADV-W as the form to be used by investment advisers when withdrawing their license in Wisconsin.

SECTION 51. DFI-Sec 9.01(1)(d) is created to read:

DFI-Sec 9.01(1)(d). ~~NF~~ Uniform investment company notice filing.

ANALYSIS: This SECTION lists newly-created Form NF as the designated form for use by an investment company when making a notice filing as provided for in s. 551.29(1)(a), Stats. (created in 1997 Wisconsin Act 316) and rule DFI-Sec 2.04(1)(a) to offer its securities in Wisconsin, or to make a filing relating to an amendment under s. 551.29(1)(b) and rule DFI-Sec 2.04(1)(b).

The rules and amendments contained in this Order shall take effect as provided in s. 227.22(2)(intro.), Stats., on the first day of the month following the date of publication in the Wisconsin Administrative Register.

DATED this _____ day of _____, 1998.

[SEAL]

PATRICIA D. STRUCK
Administrator
Division of Securities