

CR 10-062**ORDER OF THE STATE OF WISCONSIN,
DEPARTMENT OF FINANCIAL INSTITUTIONS, DIVISION OF SECURITIES
ADOPTING RULES**

1 The Wisconsin Department of Financial Institutions, Division of Securities adopts the following
2 order to repeal and recreate s. DFI-Sec 1.02(7), create s. DFI-Sec 1.02(8), amend s. DFI-Sec
3 1.02(14) (intro) and (c), amend s. DFI-Sec 2.02(5)(d)1., amend s. DFI-Sec 2.02(9)(c), amend
4 DFI-Sec 2.028 (intro), repeal s. DFI-Sec 4.01(4)(g), create s. DFI-Sec 4.04(7)(d), create s. DFI-
5 Sec 5.01(2)(f)3., repeal and recreate s. DFI-Sec 5.01(4)(a), create s. DFI-Sec 5.04(5)(d), amend
6 s. DFI-Sec 5.04(6)(b), repeal s. DFI-Sec 5.05(8)(i), create s. DFI-Sec 5.06(25), repeal and
7 recreate s. DFI-Sec 5.10, repeal and recreate s. DFI-Sec 5.13(2), amend s. DFI-Sec 7.01(3)(a),
8 repeal s. DFI-Sec 8.03 (note), and amend s. DFI-Sec 32.07(1), relating to minor revisions to
9 securities law and franchise law administrative code sections.

Analysis Prepared by the Department of Financial Institutions, Division of Securities

Statute(s) interpreted: s. 551.615, Stats.

Statutory authority: ss. 551.406(5), 551.412(5), 551.605(1), 553.31(1), 553.58(1) and 227.11(2), Stats.

Related statute or rule: none.

Explanation of agency authority: Pursuant to chs. 551 and 553, Stats., the division regulates securities and franchise investment.

10 Summary of proposed rule: The objective of the rule is to repeal and recreate s. DFI-Sec 1.02(7),
11 create s. DFI-Sec 1.02(8), amend s. DFI-Sec 1.02(14) (intro) and (c), amend s. DFI-Sec
12 2.02(5)(d)1., amend s. DFI-Sec 2.02(9)(c), amend DFI-Sec 2.028 (intro), repeal s. DFI-Sec
13 4.01(4)(g), create s. DFI-Sec 4.04(7)(d), create s. DFI-Sec 5.01(2)(f)3., repeal and recreate s.
14 DFI-Sec 5.01(4)(a), create s. DFI-Sec 5.04(5)(d), amend s. DFI-Sec 5.04(6)(b), repeal s. DFI-Sec
15 5.05(8)(i), create s. DFI-Sec 5.06(25), repeal and recreate s. DFI-Sec 5.10, repeal and recreate s.
16 DFI-Sec 5.13(2), amend s. DFI-Sec 7.01(3)(a), repeal s. DFI-Sec 8.03 (note), and amend s. DFI-
17 Sec 32.07(1), relating to minor revisions to securities law and franchise law administrative code
18 sections. The purpose of the rule is as follows:

19 Section 1: The branch office definition for broker-dealers has been harmonized with
20 FINRA and other state regulators for many years. However, with the change in the Uniform
21 Securities Act in 2009, the branch office definition in the rule was changed to refer to a slightly

22 different statutory definition of “place of business.” The statutory definition works for
23 investment advisers but not broker-dealers, hence the change in this rule.

24 Section 2: This is a new definition to accompany the solicitor rules proposed for s. DFI-
25 Sec 5.06(25) based on language developed by the NASAA IA Regulatory Policy and Review
26 Project Group.

27 Section 3: These changes clarify that the definition applies to investment advisers as well
28 as investment adviser representatives and the nature of the solicitations made by third party
29 solicitors.

30 Section 4: This amendment changes the terminology used in the current rule (which
31 limits applicability of its coverage solely to limited partnerships) by substituting the term
32 “entity” to thereby have the rule apply to any type of business organization.

33 Section 5: Incident to the Division’s 2008 rules revision to coordinate with the adoption
34 of the new Wisconsin Securities Law effective January 1, 2009, current rule DFI-Sec 2.02(9)(c)
35 inadvertently cross-referenced statute section 551.102(11) rather than the proper corresponding
36 statute in sec. 551.202(13) [which specifically refers to “accredited investors,” whereas sec.
37 551.102(11) does not]. This amendment corrects that cross-referencing error.

38 Section 6: This amendment would limit use of this registration exemption to sales of
39 equity securities by Wisconsin-based entities meeting the exemption’s requirements. This
40 exemption provision was originally created in 1986 for use by early-stage Wisconsin businesses
41 to raise risk capital for its operations. As such, the exemption’s original language was
42 specifically limited to sales of common stock of the business (which don’t obligate a business to
43 redeem/payback the invested funds). Debt securities -- which require payback to investors --
44 could not be sold under the original language of this exemption. The original language of the
45 exemption restricting its use to sales of common stock was changed in 1991 to read “securities,”
46 thus enabling the exemption to be used for sales of debt as well as equity securities
47 Subsequently, some filings have been made by Wisconsin businesses for the purpose of selling
48 their debt securities, including sales by a Wisconsin finance company of several million dollars
49 of its Notes that currently are in default, and the company is in bankruptcy. To restore the
50 exemption’s use back to its original purpose of enabling Wisconsin businesses to raise risk
51 capital -- not capital from debt securities requiring repayment -- the language of the preamble
52 is changed to permit only sales of equity securities.

53 Section 7: In a FINRA rule change comment published as Notice 09-70, FINRA
54 recommended the repeal of the S47 Japan Module of the General Securities Representative
55 examination. However, FINRA indicated that the examination was never actually implemented
56 and therefore is not an available examination anyone can take in lieu of the Series 7 exam.

57 Section 8: This new section clarifies that a notice of the opening of a branch office is not
58 complete and therefore, not deemed “filed” until all fees, including any applicable late filing
59 fees, are received. This parallels the fee payment component in the broker-dealer application
60 rule in s. DFI-Sec 4.01(2)(b) and the agent rule in s. DFI-Sec 4.01(2)(c).

61 Section 9: S. DFI-Sec 4.01(6) currently provides the same review authority as s. DFI-Sec
62 5.01(2)(f) except for the ability to perform a pre-registration examination of the adviser’s records.
63 This provision was inadvertently left out of the investment adviser rules.

64 Section 10: This amendment clarifies that the Series 65 and 66 exams referred to are the
65 post-1999 version as specified in subd. 2. It also adds clarification that if the applicant was
66 registered as an agent of a broker-dealer within two years of the application and the approval of

67 that registration was based on passage of the Series 7 and 66 exams, those exams would still be
68 considered active for purposes of meeting the exam requirement in subd. 3.

69 Section 11: This new section clarifies that a notice of the opening of a branch office is not
70 complete and therefore, not deemed “filed” until all fees, including any applicable late filing
71 fees, are received. This parallels the fee payment component in the investment adviser
72 application rule in s. DFI-Sec 5.01(2)(a) and the investment adviser representative rule in s. DFI-
73 Sec 5.01(2)(b).

74 Section 12: Because applications are effective 30 days after filing, a renewal for January
75 1 effectiveness must be filed by December 1st. The date of November 30th is incorrect.

76 Section 13: This provision was instituted to require all investment advisers to deliver
77 updated disclosure documents to clients by January 1, 2002 to comply with changes to the law at
78 that time. This subsection has met its sunset date and is no long applicable.

79 Section 14: This section specifies what activity constitutes solicitation on behalf of an
80 investment adviser and parallels the disclosure and agreement requirements found in U.S.
81 Securities & Exchange Commission rule 206(4)-3 under the Investment Advisers Act of 1940
82 but with much more clarity and is based on language developed by the NASAA IA Regulatory
83 Policy and Review Project Group.

84 Section 15: The Division currently requires only the ADV Part 1 to be filed
85 electronically. This rule change will require advisers to file their initial and updated Form ADV
86 Part 2 electronically via the Investment Adviser Registration Depository rather than in paper.
87 Subsection 1 is the general requirement to file both parts of the form via the Investment Adviser
88 Registration Depository and sub. (3) mandates existing registrants to have their Part 2 filed
89 electronically by July 1, 2011. The software is available for free to convert their Part 2 disclosure
90 document for electronic filing. Because this is the public disclosure portion of the application, it
91 is in the interest of investors in Wisconsin to be able to review this document via the Investment
92 Adviser Public Disclosure website. Requiring all advisers to make such filings will
93 automatically add them to the public disclosure website. It will also relieve Division staff from
94 processing paper applications, especially since all application materials are now retained by the
95 Division in electronic format only.

96 Section 16: This rule changes the exemption provision for investment adviser solicitors
97 following an exemption developed by the NASAA IA Regulatory Policy and Review Project
98 Group. This exemption is based on “impersonal investment advice” and eliminates the de
99 minimis exemption that was unique to Wisconsin and in effect permitted an unlimited total
100 number of solicitations so long as no more than 9 per year were for any one adviser.

101 Section 17: Corrects a statutory citation.

102 Section 18: This amendment deletes the Note at the end of rule DFI-Sec 8.03 (which
103 deals with appearances and defaults before the Division of Securities) because the 2003
104 *Krahenbuhl* case cited in the Note has been superseded by Supreme Court Rule 40.05 (effective
105 January 1, 2009) which establishes new criteria/requirements regarding the ability of non-
106 Wisconsin attorneys to represent clients in contested case proceedings before Wisconsin state
107 agencies.

108 Section 19: This rule contains the following amendments: (1) specifies that the
109 application to amend should use the Uniform Franchise Registration Application Form (Form
110 A); and (2) changes the franchise statute cross-referenced in the rule to be s. 553.31(1), Stats.,
111 which is the statute specifically dealing with amendments.

Summary of and preliminary comparison with existing or proposed federal regulation: There are no newly-developed or proposed federal regulations addressed by this rule. However, Wisconsin Securities Law and rules are generally coordinated with corresponding federal requirements, pursuant to s. 551.615, Stats.

Comparison with rules in adjacent states: These rule chapters reflect the 2002 Uniform Securities Act which Iowa and Minnesota have adopted and written rules; Illinois and Michigan have not.

Summary of factual data and analytical methodologies: The division applied its own experience in its regulation of securities generally for the minor clarifications, corrections, revisions and other matters addressed by the rule.

Analysis and supporting documentation used to determine effect on small business: The rule makes minor clarifications, corrections and revisions for conformity with existing statutes; imposes no additional substantive requirements; and reduces the same.

Summary of Final Regulatory Flexibility Analysis: This proposed rule will have no adverse impact on small businesses.

Summary of Comments received by Legislative Review Committees: No comments were received.

Agency Contact Persons

To obtain a copy of the rule or fiscal estimate at no charge or for questions regarding the agency's internal processing of the rule, contact Mark Schlei, Deputy General Counsel, Department of Financial Institutions, Office of the Secretary, P.O. Box 8861, Madison, WI 53708-8861, tel. (608) 267-1705, e-mail mark.schlei@wisconsin.gov. A copy of the rule may also be obtained and reviewed at the Department of Financial Institution's website, www.wdfi.org.

For substantive questions on the rule, contact Randall Schumann, Attorney, Department of Financial Institutions, Division of Securities, P.O. Box 1768, Madison, WI 53701-1768, tel. (608) 266-3414, e-mail randall.schumann@wisconsin.gov.

Pursuant to the statutory authority referenced above, the Department of Financial Institutions, Division of Securities adopts the following:

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- 112 SECTION 1. DFI-Sec 1.02(7) is repealed and recreated to read:
- 113 **DFI-Sec 1.02(7)** (a) For purposes of ch. DFI-Sec 4, "branch office" has the same meaning as
- 114 rule 3010(g)(2) of the Financial Industry Regulatory Authority.

115 (b) For purposes of ch. DFI-Sec 5, "branch office" has the same meaning as "place of business"
116 in s. 551.102 (21), Stats.

117 SECTION 2. DFI-Sec 1.02(8) is created to read:

118 **DFI-Sec 1.02(8)** "Solicitor" means any individual, person, or entity who, directly or indirectly,
119 receives a cash fee or any other economic benefit for soliciting, referring, offering or otherwise
120 negotiating for the sale or selling of investment advisory services to clients, including
121 prospective clients, on behalf of an investment adviser.

122 SECTION 3. DFI-Sec 1.02(14) (intro) and (c) are amended to read:

123 **DFI-Sec 1.02(14)(intro)** The following defined terms apply for purposes of the definition of
124 "investment adviser" in s. 551.102(15), Stats., and "investment adviser representative" in s.
125 551.102 (16), Stats.:

126 (c) "Third party solicitor" means a person soliciting others to become clients on behalf of a
127 registered investment adviser or a federal covered investment adviser who is neither a partner,
128 officer, director, or employee of the adviser, nor a supervised person of that adviser.

129 SECTION 4. DFI-Sec 2.02(5)(d)1. is amended to read:

130 **DFI-Sec 2.02(5)(d)1.** Except as provided in this subdivision, any offer or sale of interests in a
131 ~~limited partnership~~ an entity that is or will be primarily engaged in oil, gas or mining activities,
132 any investment contract irrespective of the kind of assets held or business engaged in by the
133 enterprise, or any certificate of interest or participation in an oil, gas or mining title or lease, or in
134 payments out of production under the title or lease, if the aggregate offering price or face
135 amount, whichever is greater, of all securities to be offered by or on behalf of the issuer, together
136 with the value of any securities sold to persons in this state by or on behalf of the issuer during
137 the prior 12 months, exceeds \$100,000, unless prior to the offering the issuer files a notice of the

138 proposed offer or sale with the division, including any prospectus, circular or other material to be
139 delivered to offerees, and other information as the division may require, and the division does
140 not by order withdraw, deny or revoke the exemption within 10 days. This paragraph is not
141 applicable to any offer or sale made by a broker-dealer registered in Wisconsin if the broker-
142 dealer is not affiliated with either the issuer or sponsor of the issuer by means of direct or
143 indirect common control;

144 SECTION 5. DFI-Sec 2.02(9)(c) is amended to read:

145 **DFI-Sec 2.02(9)(c)** Any transaction pursuant to an offer to existing security holders of the issuer,
146 and to not more than 25 other persons in this state less the number of persons in this state with
147 whom the issuer has effected any transactions during the period of 12 months preceding the offer
148 pursuant to s. 551.202 (14) and (24), Stats., excluding persons listed in s. ~~551.102–(11)~~
149 551.202(13) , Stats., and rules there under, if no commission or other remuneration other than a
150 standby commission is paid or given directly or indirectly for soliciting any security holder in
151 this state; and if the issuer files with the division prior to the offering a notice specifying the
152 terms of the offer, including any prospectus, circular or other material to be delivered to offerees
153 in connection with the transaction and such other information as the division may require, and
154 the division does not by order disallow the exemption within 10 days.

155 SECTION 6. DFI-Sec 2.028 (intro) is amended to read:

156 **DFI-Sec 2.028 (intro) Wisconsin issuer registration exemption by filing.** If all of the
157 following conditions are met, other than any condition or conditions waived by the division upon
158 a showing of good cause, a transaction registration exemption is available under s. 551.203,
159 Stats., for any offer or sale for cash of the equity securities of an issuer having, both before and

160 upon completion of the offering, its principal office and a majority of the full-time employees
161 located in this state:

162 SECTION 7. DFI-Sec 4.01(4)(g) is repealed.

163 SECTION 8. DFI-Sec 4.04(7)(d) is created to read:

164 **DFI-Sec 4.04(7)(d)** The notice filed for a branch opening pursuant to par. (a) is deemed filed in
165 accordance with par. (c) upon receipt by the division of the appropriate filing fee and any late
166 filing fee due pursuant to s. DFI-Sec 7.01(6)(d).

167 SECTION 9. DFI-Sec 5.01(2)(f)3. is created to read:

168 **DFI-Sec 5.01(2)(f)3.** Before action on an application, the division may designate an employee to
169 make an examination of the books, records and affairs of the applicant at the applicant's expense.

170 SECTION 10. DFI-Sec 5.01(4)(a) is repealed and recreated to read:

171 **DFI-Sec 5.01(4)(a)1.** The applicant has taken and passed either the post-1999 version of the
172 Series 65 Uniform Investment Adviser State Law Examination, or both the post-1999 version of
173 the Series 66 Uniform Combined State Law Examination and the Series 7 General Securities
174 Representative Examination within 2 years prior to the date the application is filed with the
175 division; or

176 2. The applicant has been registered as an agent of a broker-dealer within two years prior to the
177 date the application is filed, based on having passed the post-1999 version of the Series 66
178 examination and the Series 7 examination.

179 SECTION 11. DFI-Sec 5.04(5)(d) is created to read:

180 **DFI-Sec 5.04(5)(d)** The notice filed for a branch opening pursuant to sub. (a) is deemed filed in
181 accordance with sub. (c) upon receipt by the division of the appropriate filing fee and any late
182 filing fee due pursuant to s. DFI-Sec 7.01(6)(d).

183 SECTION 12. DFI-Sec 5.04(6)(b) is amended to read:

184 **DFI-Sec 5.04(6)(b)** Directly with the division for federal covered investment advisers, not later
185 than ~~November 30~~ December 1.

186 SECTION 13. DFI-Sec 5.05(8)(i) is repealed.

187 SECTION 14. DFI-Sec 5.06(25)(intro)(a) – (e) is created to read:

188 **DFI-Sec 5.06(25)** Paying a cash fee or any other economic benefit, directly or indirectly, in
189 connection with solicitation activities unless the requirements of pars. (a) through (d) are met.

190 (a) The solicitor is registered as an investment adviser or investment adviser representative or is
191 exempt from registration as provided for in s. DFI-Sec 5.13(2).

192 (b) The cash fee or any other economic benefit is paid by the investment adviser with respect to
193 solicitation activities that are impersonal in nature in that they are provided solely by means of:

194 1. Written material or oral statements which do not purport to meet the objectives or needs of
195 the specific client; or

196 2. Statistical information containing no expressions of opinions as to the merits of particular
197 securities or investment advisers; or

198 3. Any combination of the foregoing services.

199 (c) The cash fee or any other economic benefit is paid pursuant to a written agreement to which
200 the investment adviser is a party and all of the following conditions are met:

201 1. The written agreement;

202 a. Describes the solicitation or referral activities to be engaged in by the solicitor on behalf of
203 the investment adviser and the cash fee or any other economic benefit to be received for such

204 activities; and

205 b. Contains an undertaking by the solicitor to perform its duties under the agreement in a
206 manner consistent with the instructions of the investment adviser and the provisions of ch. 551,
207 Stats., and rules there under; and

208 c. Requires that the solicitor, at the time of any solicitation or referral activities for which a cash
209 fee or any other economic benefit is paid or to be paid by the investment adviser, provide the
210 client with a current copy of the investment adviser's disclosure document required under s. DFI-
211 Sec 5.05(8) and a separate disclosure statement as described in subsection (d) of this rule, either
212 in paper or electronic format; and

213 2. The investment adviser receives from the client, prior to or at the time of entering into any
214 written investment advisory contract, a signed and dated acknowledgement of receipt of the
215 investment adviser's written disclosure statement and the solicitor's written disclosure
216 document; and

217 3. The investment adviser makes a bona fide effort and has a reasonable basis for believing that
218 the solicitor has complied with the agreement; and

219 4. The requirements in subd. 1., 2. and 3. shall not apply if the solicitor is any of the following:

220 a. A partner, officer, director or employee of such investment adviser; or

221 b. A partner, officer, director or employee of a person that controls, is controlled by, or is under
222 common control with such investment adviser, provided the status of the solicitor is disclosed to
223 the client at the time of the solicitation or referral.

224 (d) The separate written disclosure document required to be furnished by the solicitor to the
225 client pursuant to par. (c)1.c. shall contain the following information:

226 1. The name of the solicitor;

227 2. The name of the investment adviser;

- 228 3. The nature of the relationship, including any affiliation, between the solicitor and the
229 investment adviser;
- 230 4. A statement that the solicitor will be compensated for solicitation or referral services by the
231 investment adviser;
- 232 5. The terms of the compensation arrangement including a description of the cash fee or any
233 other economic benefit paid or to be paid to the solicitor; and
- 234 6. The amount of compensation the client will pay, if any, in addition to the advisory fees, and
235 whether the cash fee or any other economic benefit paid to the solicitor will be added to the
236 advisory fee, creating a differential with respect to the amount charged to other advisory clients
237 who are not subject to the solicitor compensation arrangement.

238 (e) Nothing in this subsection shall be deemed to relieve any person of any fiduciary or other
239 obligation to which such person may be subject under any law.

240 SECTION 15. DFI-Sec 5.10 is repealed and recreated to read:

241 **DFI-Sec 5.10 Electronic filing.** (1) Each investment adviser shall file a copy of its current form
242 ADV Parts 1 and II electronically with the Investment Adviser Registration Depository.

243 (2) Any documents or fees required to be filed with the division that are not permitted to be filed
244 with, or cannot be accepted by, the investment adviser registration depository or the central
245 registration depository shall be filed directly with the division.

246 (3) Each investment adviser that is registered in this state on January 1, 2011 shall file a copy of
247 its current form ADV Part 2 electronically with the Investment Adviser Registration Depository
248 by no later than July 1, 2011.

249 SECTION 16. DFI-Sec 5.13(2) is repealed and recreated to read:

250 **DFI-Sec 5.13(2)** A solicitor is not required to be registered as an investment adviser or as an
251 investment adviser representative if the solicitor is in compliance with all requirements of s. DFI-
252 Sec 5.06(25), and the solicitor satisfies par. (a) or (b).

253 (a) Provides solicitation activities that are impersonal in nature as set forth in s. DFI-Sec
254 5.06(25)(b) and the solicitor to whom a cash fee or any other economic benefit is paid for such
255 referral does not trigger any of the following as being a person:

256 1. Subject to an order of the U.S. Securities & Exchange Commission issued under section
257 203(f) of the Investment Advisers Act of 1940;

258 2. Subject to an order of the administrator, the securities administrator of any other state, the U.S.
259 Securities and Exchange Commission, or any self regulatory organization denying, suspending,
260 or revoking registration as a broker-dealer, agent, investment adviser, or investment adviser
261 representative or barring the person from the securities or advisory industry or associating or
262 affiliating with the securities or advisory industry, entered after notice and opportunity for
263 hearing;

264 3. Convicted within the previous ten years of any felony, or any misdemeanor involving conduct
265 described in section 203(e)(2)(A) through (D) of the Investment Advisers Act of 1940;

266 4. Convicted within the previous ten years of any felony, or any misdemeanor involving conduct
267 described in s. 551.412(4)(c) Stats.;

268 5. Found by the U.S. Securities & Exchange Commission to have engaged, or has been convicted
269 of engaging in, any of the conduct specified in sections 203(e)(1), (5) or (6) of the Investment
270 Advisers Act of 1940;

271 6. Found by the administrator to have engaged, or has been convicted of engaging in, any of the
272 conduct specified in ss. 551.412(4)(a), (b) or (f) Stats.;

273 7. Subject to an order, judgment or decree described in section 203(e)(4) of the Investment
274 Advisers Act of 1940;

275 8. Subject to an order, judgment or decree described in s. 551.412(4)(d) Stats.

276 (b) Receives an order of the administrator waiving the registration requirement.

277 SECTION 17. DFI-Sec 7.01(3)(a) is amended to read:

278 **DFI-Sec 7.01(3)(a)** Application for an initial registration of a broker-dealer or investment
279 adviser or a successor under s. 551.401, 551.403, or ~~551.411(4)~~ 551.407, Stats.,\$200.

280 SECTION 18. DFI-Sec 8.03 (note) is repealed and recreated to read:

281 See Supreme Court Rule 40.05 (effective January 1, 2009) which establishes requirements to be
282 met to enable non-Wisconsin attorneys to represent clients in contested case proceedings before
283 Wisconsin state agencies.

284 SECTION 19. DFI-Sec 32.07(1) is amended to read:

285 **DFI-Sec 32.07(1)** An application to amend the registration statement shall be filed using the
286 ~~cover page~~ Uniform Franchise Application Form (Form A) of the 2008 Franchise Registration
287 and Disclosure Guidelines adopted on June 6, 2008 by the North American Securities
288 Administrators Association) , and containing the information ~~and accompanied by the fee~~
289 required in s.~~553.26 (1)~~ 553.31(1), Stats. ~~, and~~ The application shall be accompanied by a
290 copy of the amended disclosure document prepared in conformance with those Disclosure
291 Guidelines, ~~and~~ together with the \$200 filing fee prescribed in s. DFI-Sec 35.01.

292 **Effective date.** This rule shall take effect on the first day of the month following
293 publication in the *Wisconsin Administrative Register* as provided in s. 227.22 (2) (intro.), Stats.

Dated: _____ Agency: _____
Patricia Struck, Administrator