CR 92-135

CERTIFICATE

STATE OF WISCONSIN)
OFFICE OF THE) ss.
COMMISSIONER OF SECURITIES)

TO ALL TO WHOM THESE PRESENTS SHALL COME, GREETINGS:

I, Wesley L. Ringo, Commissioner of the State of Wisconsin Office of the Commissioner of Securities, as custodian of the official records of said agency, do hereby certify that the annexed rules relating to the operation of Ch. 551, Wis. Stats., the Wisconsin Uniform Securities Law, and Ch. 553, Wis. Stats., the Wisconsin Franchise Investment Law, relating to: securities and franchise registration exemptions, securities registration and disclosure standards and requirements, securities broker-dealer, securities agent and securities investment adviser licensing requirements and procedures; and certain fee-related provisions under the securities law, were duly approved and adopted by this agency on November 16, 1992.

I further certify that said copy has been compared by me with the original on file in this agency and that the same is a true copy thereof, and of the whole of such original.

IN TESTIMONY WHEREOF, I have hereunto set my hand and affixed the official seal of the Office of the Commissioner of Securities in the City of Madison, this 16th day of November, 1992.

[SEAL]

Wesley L. Ringo
Commissioner of Securities
State of Wisconsin

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Revisor of Statutes
Bureau

1-1-93

FINAL ORDER OF THE
OFFICE OF THE COMMISSIONER OF SECURITIES
STATE OF WISCONSIN
ADOPTING, AMENDING AND REPEALING RULES

To renumber SEC 2.02(4)(e) and 5.03(6); to amend SEC 2.02(4)(d)4, 2.02(6), 3.01(1), 3.01(3), 3.16, 3.17, 3.23(2)(h), 4.01(4)(b), 4.01(5)(intro.), 4.03(1)(intro.), 4.03(1)(r)2, 4.03(2), 4.03(3)(e), 4.05(6), 4.06(2)(e), 4.11(1)(c), 5.01(3), 5.03(1)(intro.), 5.05(7), 7.01(5)(d), 7.02(1)(b) and 32.05(1)(c)5; to repeal and recreate SEC 3.03, 3.07 and 5.01(4); and to create SEC 2.02(4)(e), 3.045, 3.06(5)(d), 4.01(10), 5.02(3) and 5.03(6) relating to: securities and franchise registration exemptions, securities registration and disclosure standards and requirements, securities broker-dealer, securities agent and securities investment adviser licensing requirements and procedures; and certain fee related provisions under the securities law.

Pursuant to sections 551.63(1) and (2), 551.23(8)(f), 551.27(4), (7) and (10), 551.28(1)(e) and (f), 551.32(1)(a) and (b), (4), (5), (6) and (7), 551.33(1), (2) and (6), and 553.25 and 553.58, Wis. Stats., the Office of the Commissioner of Securities repeals, amends and adopts rules interpreting those sections as follows:

FINAL FORM OF
AMENDMENTS TO RULES OF THE
WISCONSIN COMMISSIONER OF SECURITIES

SECTION 1. SEC 2.02(4)(d)4 is amended to read:

SEC 2.02(4)(d)4. Any organization described in section 501(c)(3) of the internal revenue code, or any corporation (other than a bank as defined in section 3(a)(2) of the securities act of 1933 or a savings and loan association or other institution referenced in section 3(a)(5)(A) of the securities act of 1933 or a foreign bank or savings and loan association or equivalent institution).

ANALYSIS: This amendment adds minor clarification language to the rule to make it more readable. The rule, which is one of the listing of additional "institutional investors" for purposes of the registration exemption of sec. 551.23(8), was adopted last year verbatim from the listing of "Qualified Institutional Buyers" designated in federal Rule 230.144A(a)(1)(i)(G) under the Securities Act of 1933.

SECTION 2. SEC 2.02(4)(e) is renumbered SEC 2.02(4)(f).

ANALYSIS: This renumbering is for the purpose of making room for a new paragraph in the following SECTION that, in the numbering sequence of SEC 2.02(4), belongs before the "catch-all" provision in current sub. (4)(e) (which allows the Commissioner to designate persons or entities as "institutional investors" by rule or order).

SECTION 3. SEC 2.02(4)(e) is created to read:

SEC 2.02(4)(e) Any entity, all of the equity owners of which are persons designated in s. 551.23(8) or rules thereunder, acting for its own account or the accounts solely of other persons designated in s. 551.23(8) or rules thereunder.

ANALYSIS: This rule adopts the equivalent "Qualified Institutional Buyer" classification specified in U.S. Securities and Exchange Commission rule 230.144A(a)(1)(v) under the Securities Act of 1933. It adds to the other categories of "Qualified Institutional Buyers" designated under federal Rule 144A that this agency adopted as part of

its 1991 rule revision process and set forth in secs. SEC 2.02(4)(d)1 to 4.

SECTION 4. SEC 2.02(6) is amended to read:

SEC 2.02(6)"Class vote" within the meaning of s. 551.23(13), Stats., includes any vote pursuant to the articles of incorporation or the applicable corporation statute, of the stockholders of a corporation voting as one class, and any vote of stockholders of any class taken in accordance with the provisions of s. ~~180.52~~ 180.1004, Stats., or comparable provisions of the articles of incorporation or of an applicable corporation statute of another state.

ANALYSIS: This amendment changes the numbering of the Wisconsin Business Corporation Law provision cross-referenced in this rule to reflect a recent recodification and renumbering of the entirety of the Wisconsin Business Corporation Law.

SECTION 5. SEC 3.01(1) is amended to read:

SEC 3.01(1) SELLING EXPENSES. (1) Except for offerings by issuers specified in subs. (2) and (3), the aggregate amount of selling expenses in an offering may be deemed unfair and inequitable to purchasers unless the offering complies with the provisions of the North American Securities Administrators Association Statement of Policy Regarding Selling Expenses and Selling Security Holders, as adopted effective September 14, 1989, and amended effective October 24, 1991.

Note: The Statement of Policy is published in the CCH NASAA Reports published by Commerce Clearing House and is on file at the offices of the Wisconsin secretary of state and the revisor of statutes. Copies of the Statement of Policy are available from the commissioner's office for a prepaid fee of $4.

ANALYSIS: This SECTION adopts the amendments to the subject NASAA Statement of Policy that were adopted at the NASAA

1991 Fall Conference by vote of member jurisdictions, including Wisconsin.

SECTION 6. SEC 3.01(3) is amended to read:

SEC 3.01(3) With respect to investment company shares or face amount certificates sold pursuant to a contractual plan or program payable in installments, unless the offering complies with the provisions of the North American Securities Administrators Association Guidelines For Registration of Periodic Payment Plans, as adopted March 29, 1992, the selling commission may be deemed unreasonable if more than a pro rata portion of the total selling commission payable over the period of the contract is payable in connection with any installment payment, or if any charge or penalty is assessed for failure to make any installment payment.

Note: The Guidelines are published in the CCH NASAA Reports published by Commerce Clearing House and are on file at the offices of the Wisconsin secretary of state and the revisor of statutes. Copies of the Statement of Policy are available from the commissioner's office for a prepaid fee of $4.

ANALYSIS: This SECTION adopts the subject NASAA policy that was adopted at the NASAA 1992 Spring Conference by vote of member jurisdictions, including Wisconsin.

SECTION 7. SEC 3.03 is repealed and recreated to read:

SEC 3.03 OPTIONS AND WARRANTS. (1) Except as provided in sub. (2), the amounts and kinds of options and warrants to purchase securities issued or sold, other than ratably to purchasers, in connection with a proposed offering of equity securities or securities convertible into equity securities, as well as the amounts and kinds of options and warrants issued or reserved for issuance at the date of the public offering may be deemed unfair and inequitable unless the

offering complies with the provisions of the North American Securities Administrators Association Statement of Policy Regarding Options and Warrants, as adopted effective October 24, 1992.

Note: The Statement of Policy is published in the CCH NASAA Reports published by Commerce Clearing House and is on file at the offices of the Wisconsin secretary of state and the revisor of statutes. Copies of the Statement of Policy are available from the commissioner's office for a prepaid fee of $4.

(2) The total amount of options and warrants issued or reserved for issuance at the date of the public offering by a Wisconsin corporation having its principal office in Wisconsin, excluding options and warrants issued to financing institutions, other than underwriters, and excluding those issued to an entity being acquired, does not exceed 20% of the shares to be outstanding upon completion of the offering, with options and warrants not to exceed 10% for any one person, or 20% of the shares outstanding during the period the registration statement is effective. The number of options and warrants reserved for issuance may be disregarded if the issuer states in the prospectus that the amount of outstanding options and warrants does not exceed either of the amounts in this subsection during the period the registration statement is effective.

ANALYSIS: This SECTION does the following: (a) Adopts the subject NASAA policy on options and warrants that was adopted at the NASAA 1991 Fall Conference by vote of member jurisdictions, including Wisconsin; (2) Retains the alternative test for the total amount of options and warrants by a Wisconsin corporation with its principal office in Wisconsin that is currently set forth in SEC 3.03(4)(b).

SECTION 8. SEC 3.045 is created to read:

SEC 3.045 IMPOUNDMENT OF PROCEEDS. In any offering that the

commissioner determines impoundment of offering proceeds is required as a condition of registration, the commissioner may require that the terms and conditions of the impoundment comply with the provisions of the North American Securities Administrators Association Statement of Policy regarding the Impoundment of Proceeds, as adopted effective October 24, 1991.

Note: The Statement of Policy is published in the CCH NASAA Reports published by Commerce Clearing House and is on file at the offices of the Wisconsin secretary of state and the revisor of statutes. Copies of the Statement of Policy are available from the commissioner's office for a prepaid fee of $4.

ANALYSIS: This SECTION adopts the subject NASAA policy that was adopted at the NASAA 1991 Fall Conference by vote of member jurisdictions, including Wisconsin.

SECTION 9. SEC 3.06(5)(d) is created to read:

SEC 3.06(5)(d) Preferred stock of an issuer that is senior to, or of substantially equal rank with, other securities of the same issuer which are listed, designated, or approved for listing or designation on the exchanges or trading markets specified in s. 551.22(7), Stats., or rules promulgated thereunder.

ANALYSIS: This new rule adds to the list of types of securities that are not subject to the earnings requirements in SEC 3.06 for preferred stock and debt securities offerings that are the subject of a registration application under the Wisconsin Uniform Securities Law. The added category of securities that are excluded from the earnings requirement in the rule is the preferred stock of NYSE, AMEX or NASDAQ/National Market System issuers which have securities listed or designated on such trading exchanges/markets that are junior to, or of substantially equal rank with, the preferred stock being offered. The earnings requirements of SEC 3.06 remain applicable to the debt securities of such issuers because, in contrast to preferred stock--which is of an equity nature and has no stated maturity date such that there is no obligation on the issuer to redeem at a particular time--debt securities, by definition, are required to be paid in full at their

maturity date.

SECTION 10. SEC 3.07 is repealed and recreated to read:

SEC 3.07 VOTING RIGHTS. If the issuer is a corporation or business trust having more than one class of equity securities authorized or outstanding, the offer or sale may be deemed unfair and inequitable to purchasers unless the offering complies with the provisions of the North American Securities Administrators Association Statement of Policy Regarding Unequal Voting Rights, as adopted October 24, 1991.

Note: The Statement of Policy is published in the CCH NASAA Reports published by Commerce Clearing House and is on file at the offices of the Wisconsin secretary of state and the revisor of statutes. Copies of the Statement of Policy are available from the commissioner's office for a prepaid fee of $4.

ANALYSIS: This SECTION adopts the subject NASAA policy relating to voting rights for corporations or business trusts that was adopted at the NASAA 1991 Fall Conference by vote of member jurisdictions, including Wisconsin. Subsection (2) of the current voting rights rule (which relates to limited partnerships) is not retained in this rule in its recreated form. Retaining current sub. (2) would be duplicative and unnecessary because the various NASAA Statements of Policy incorporated by reference in Chapter SEC 3 relating to the different types of activity that limited partnerships can engage in (real estate, oil and gas drilling, cattle feeding, commodity pools, etc.) each have requirements regarding voting rights.

SECTION 11. SEC 3.16 and 3.17 are amended to read:

SEC 3.16 TRANSACTIONS WITH AFFILIATES. The offer or sale of securities by an issuer that has engaged or has a policy to engage in transactions with affiliates, may be deemed to be unfair and inequitable to purchasers unless the terms of the transactions comply with the provisions of the North American Securities Administrators Association Statement of Policy Regarding Affiliated Transactions, as

adopted effective September 14, 1989, and amended effective October 24, 1991.

Note: The Statement Policy is published in the CCH NASAA Reports published by Commerce Clearing House and is on file at the offices of the Wisconsin secretary of state and the revisor of statutes. Copies of the Statement of Policy are available from the commissioner's office for a prepaid fee of $4.

SEC 3.17 REAL ESTATE INVESTMENT TRUSTS. The offer or sale of securities of a corporation, trust or association, other than a real estate syndication, engaged primarily in investing in equity interests in real estate, including fee ownership and leasehold interests, or in loans secured by real estate, or both, may be deemed unfair and inequitable to purchasers unless the offering complies with the provisions of the North American Securities Administrators Association Statement of Policy on Real Estate Investment Trusts, as adopted April 28, 1981, and amended effective January 1, 1986, and October 24, 1991.

Note: The Statement Policy is published in the CCH NASAA Reports published by Commerce Clearing House and is on file at the offices of the Wisconsin secretary of state and the revisor of statutes. Copies of the Statement of Policy are available from the commissioner's office for a prepaid fee of $4.

ANALYSIS: This SECTION adopts the amendments to the two subject NASAA Statements of Policy that were adopted at the NASAA 1991 Fall Conference by vote of member jurisdictions, including Wisconsin.

SECTION 12. SEC 3.23(2)(h) is amended to read:

SEC 3.23(2)(h) If the offering is exempt under ~~either~~ section 3(a)(2), 3(a)(11) or ~~section~~ 4(2) of the securities act of 1933, and a filing is required to be made under ch. 551, Stats., or rules

promulgated thereunder, each of the following two statements in bold-face type, as applicable to the offering:

IN MAKING AN INVESTMENT DECISION, INVESTORS MUST RELY ON THEIR OWN EXAMINATION OF THE ISSUER AND THE TERMS OF THE OFFERING, INCLUDING THE MERITS AND RISKS INVOLVED. THESE SECURITIES HAVE NOT BEEN RECOMMENDED BY ANY FEDERAL OR STATE SECURITIES COMMISSION OR REGULATORY AUTHORITY. FURTHERMORE, THE FOREGOING AUTHORITIES HAVE NOT CONFIRMED THE ACCURACY OR DETERMINED THE ADEQUACY OF THIS DOCUMENT. ANY REPRESENTATION TO THE CONTRARY IS A CRIMINAL OFFENSE.

THESE SECURITIES ARE SUBJECT TO RESTRICTIONS ON TRANSFERABILITY AND RESALE AND MAY NOT BE TRANSFERRED OR RESOLD EXCEPT AS PERMITTED UNDER THE SECURITIES ACT OF 1933, AS AMENDED, AND THE APPLICABLE STATE SECURITIES LAWS, PURSUANT TO REGISTRATION OR EXEMPTION THEREFROM. INVESTORS SHOULD BE AWARE THAT THEY MAY BE REQUIRED TO BEAR THE FINANCIAL RISKS OF THIS INVESTMENT FOR AN INDEFINITE PERIOD OF TIME.

ANALYSIS: These amendments do the following: (1) Add a cross-reference to the "governmental security" exemption under the federal Securities Act of 1933 to specify that the prospectus disclosures required under the rule apply also to filings that are required to be made under SEC 2.01(1)(a)3 to claim the Wisconsin "governmental security" exemption in sec. 551.22(1), Wis. Stats.; and (2) Add language to clarify that the bold-face prospectus disclosures required under the rule apply only to offerings where a filing is required to be made with this Office to obtain a registration or to claim registration exemption status such that the prospectus disclosure requirement of SEC 3.23 becomes applicable.

In a modification made to this rule as a result of a comment letter received, the language "as applicable to the offering" is added at the end of the preamble to provide that the general requirement under the rule to include both bold-face statements is subject to an applicability test which would take into account the specific facts of a particular offering. For instance, as was pointed out in the comment letter, the second of the 2 bold-face paragraph statements (the one regarding restrictions on

transferability) generally need not be (and should not be) contained in a prospectus for an offering exempt under section 3(a)(2) of the federal Securities Act of 1933 because such securities are not restricted in their transferability for federal or state securities law purposes.

SECTION 13. SEC 4.01(4)(b) is amended to read:

SEC 4.01(4)(b) The applicant has been licensed~~,~~ ~~within~~ for at least 2 years ~~prior to~~ immediately preceding the date the application for license is filed in this state, as an agent or as a broker-dealer under the securities law of any other state that ~~requires~~ has required the passing of the uniform securities agent state law examination during that two year period and, in the case of examinations required by sub. (3)(a) to (e) has been registered with the national association of securities dealers, inc., to engage in the type of business for which the applicant is applying for license within two years prior to the date of filing the application for license ~~is filed to engage in the type of business for which the applicant is applying for license~~.

ANALYSIS: These amendments restrict the portion of this rule providing a "reciprocity" waiver from the agent examination/testing requirement rule for an agent applicant that has been previously licensed in another state. The amendments are necessary because several states over the past few years have adopted the NASD Series 63 Examination as an examination-passage requirement for agent licensure in those states. The rationale and basis of the reciprocity waiver under the rule is that an agent has demonstrated his/her ability to conduct business in a state requiring the Series 63 without actual passage of the exam. The amendment requires for purposes of the waiver that a securities agent applicant must have been licensed in a state requiring passage of the NASD Series 63 exam for at least 2 years immediately preceding the filing of a license application in Wisconsin. The time-licensed-in-another-state requirement establishes the agent's ability to function under, and in compliance with, the laws and rules addressed by the exam. The last phrase in the current rule is moved to a different part of the sentence to make it more readable.

SECTION 14. SEC 4.01(5)(intro.) is amended to read:

SEC 4.01(5) Prior to issuance of an initial license as a broker-dealer, at least one employe ~~located at the~~ its principal office ~~of the broker-dealer~~ or designated office of supervision in accordance with s. SEC 4.03(1), shall be designated in the license application to act in a supervisory capacity and be licensed as an agent for the broker-dealer. Each designated supervisor shall meet the examination requirement in sub. (3) and shall pass with a grade of at least 70% the examination in par. (a), unless the broker-dealer's proposed securities activities will be restricted, in which case the designated supervisor is required to pass each examination in pars. (b) to (d) that relates to the broker-dealer's securities activities, unless the examination is waived under sub. (4):

ANALYSIS: The amendments to this broker-dealer licensing procedure rule relating to designated supervisors is necessary to reflect the amendment to SEC 4.03(1) permitting the Commissioner to allow a broker-dealer to retain its books and records at a designated location other than its "principal office."

The amendment language has been modified from its comment draft form as a result of public comment letters received and also reflects the modifications made to rule SEC 4.03(1) which is cross-referenced in this rule to clarify that a broker-dealer is in compliance with this rule when it chooses to identify/specify someone either from its principal office, or from a designated office other than the principal office, as the designated supervisor. Thus, any broker-dealer firm which might have records retained in several regional storage locations need not have examination-qualified supervisory personnel at each separate location.

SECTION 15. SEC 4.01(10) is created to read:

SEC 4.01(10) An agent seeking to provide investment advisory services as part of the business of the employing broker-dealer either must pass the examination prescribed in s. SEC 5.01(3), or satisfy a basis for waiver of the examination under SEC 5.01(4).

ANALYSIS: This new subsection under the broker-dealer licensing provision of SEC 4.01 is needed to clarify (by cross-referencing to the examination requirement of SEC 5.01(3) and its related examination waiver provision in SEC 5.01(4)) examination requirements for those agents employed by a broker-dealer whose activities include providing investment advisory services on behalf of the firm to customers. The current rules under SEC 4.01 do not provide an examination category for securities agents whose activities with customers of the firm include providing investment advisory services.

Modifications to this proposed rule were made as a result of public comment letters and hearing testimony received to clarify that securities agents of broker-dealers generally will not be impacted by this rule and will not need to take the Series 65 examination prescribed in SEC 5.01(3) which is cross-referenced in this rule. In particular, language was added to specifically cross-reference rule section SEC 5.01(4) which provides several different bases for waiver from the need to take the Series 65 examination prescribed in SEC 5.01(3). Of principal note is the examination waiver provision of SEC 5.01(4)(a) that applies to any person who has passed (or received a waiver from the need to pass) either the NASD Series 2, 7 or 24 examination, and in addition has passed the NASAA Series 63 examination. Because virtually all agents of broker-dealers already will have passed one of the listed NASD examinations, as well as the NASAA Series 63 examination to be able to conduct business as a securities agent on behalf of their broker-dealer employer, they will automatically qualify for a waiver (under SEC 5.01(4)(a)) from the need to pass the Series 65 examination referred to in this rule.

As additional clarification of the scope of this rule, it is to be noted that broker-dealers and their agents whose performance of investment advisory services is solely incidental to the conduct of their brokerage business and who receive no special compensation for providing advisory services do not fall within the definition of "investment adviser" to begin with, such that this rule (regarding investment adviser examinations and waivers) is not even applicable.

SECTION 16. SEC 4.03(1)(intro.) is amended to read:

SEC 4.03(1) Every licensed broker-dealer shall prepare and keep current at its principal office, at a designated office located in the United States specified in writing to, and permitted by, the commissioner, 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 amendment (to the broker-dealer licensing rule requirement relating to where a firm's books and records must be kept) is necessary to provide flexibility to cover the following two types of situations: (1) Where a broker-dealer's principal office is not physically located in the U.S., a U.S. office location must be designated to facilitate regulatory access to the firm's books and records; (2) Where a U.S. broker-dealer elects to maintain its books and records at an "operations center" or other location separate from its "principal" or headquarters office, any such alternative location for retention of a firm's books and records must be permitted by the Commissioner.

Modifications to this proposed rule were made as a result of public comment letters and hearing testimony received. Specifically, the identical language "or at an office under the direct supervision and control of the principal or designated office" found in SEC 4.03(2) was added to this rule to clarify--not only for purposes of this rule, but also for purposes of the designated supervisor provisions in SEC 4.01(5) and SEC 4.05(6)--that any broker-dealer firm which might have records in several regional storage locations need not have examination-qualified supervisory personnel at each separate location where records might be located/kept. Rather, by means of the language added to this rule, together with the identical language already in SEC 4.03(2), such a broker-dealer is in compliance when it chooses to identify someone either from the principal office, or from a designated office other than the principal office, as the designated supervisor for any or all such records.

SECTION 17. SEC 4.03(1)(r)2. is amended to read:

SEC 4.03(1)(r)2. As to offerings made under s. 551.23(10) and (19), Stats., or made pursuant to an order of exemption issued under s. 551.23(18), Stats., that limits sales, the name and address of each purchaser,other than an "accredited investor" as defined in Rules 501 and 506 of Regulation D of the securities act of 1933, the date the sale was made, the control number on any offering circular or other advertising material given to the purchaser and the names of all persons making the sale.

ANALYSIS: Recently, the staff has had difficulty in determining compliance with limited offering requirements

when examining a broker-dealer's Offeree Sales Register form required by this rule. Because an unlimited number of "accredited investors" are allowed in federal Regulation D offerings made in Wisconsin pursuant to sec. 551.23(19), Wis. Stats., this change clarifies that the Register Form need only include information concerning persons other than accredited investors.

SECTION 18. SEC 4.03(2) is amended to read:

SEC 4.03(2) Every licensed broker-dealer shall preserve at its principal office, at a designated office permitted by the commissioner under s. SEC 4.03(1), or at an office under the direct supervision and control of the principal or designated office, for at least 6 years, the first 2 years in an easily accessible place, all records required under sub. (1) and under s. SEC 4.035(2), except that records required under sub. (1)(k), (l), and (m) shall be preserved by the broker-dealer for at least 6 years after the closing of the account; and records. Records required under sub. (1)(o) shall be preserved by the broker-dealer for at least 6 years after withdrawal or expiration of its license in this state. The record may be retained by computer if a printed copy of the record can be prepared immediately upon request. In the event a record has been preserved for one year as required under this subsection, a microfilm copy may be substituted for the remainder of the required period. Compliance with the requirements of the U.S. securities and exchange commission concerning preservation and microfilming of records, or other means of retention of records, is deemed compliance with this subsection.

ANALYSIS: These amendments to the broker-dealer recordkeeping rule specifying the retention period for books and records are necessary to reflect the amendment to SEC 4.03(1) permitting the Commissioner to allow a broker-dealer to retain its books and records at a location other than its "principal office."

In a modification to this rule made as a result of a comment

letter received, the language "or other means of retention of records" is added to the last sentence in the rule. The language is added to specifically provide that in the event the U.S. Securities and Exchange Commission grants approval to the securities industry's pending proposal to allow retention of records by Optical Disk Storage Technology (which is more advanced than microfilm storage), broker-dealer firms choosing to use such new technology for federal record retention purposes also will be in compliance with this Office's record retention rule.

SECTION 19. SEC 4.03(3)(e) is amended to read:

SEC 4.03(3)(e) ~~Branch offices of broker-dealers~~ Each branch office of a broker-dealer engaged solely in the offer and sale of either securities issued by open-end investment companies, face amount certificate companies or unit investment trusts registered under the investment company act of 1940, or the securities of direct participation program issuers, or both, shall prepare and keep current copies of those records described in subs. (1)(f), (i), (j), (k), and (3)(c) and (d). Additionally, each such branch office shall prepare and keep current records described in sub. (1)(p), but only of advertising materials either generated from the branch office or mailed by or placed in media by the branch office.

ANALYSIS: These amendments add two categories of records (an advertising file per SEC 4.03(1)(p) and copies of customer monthly or periodic statements per SEC 4.03(3)(d)) to those records required to be kept in branch offices of broker-dealers whose activities are restricted to mutual fund or direct participation program securities. The customer statement category of records is important to enable agents to review and monitor their customer's securities holdings, and to enable the Commissioner's staff when conducting branch office examinations to review customer activity and timeliness of order execution. The advertising file is necessary to enable the Commissioner's staff to review during branch office examinations, advertising placed by the branch office in local media or otherwise published or circulated relating to the conduct of the broker-dealer's business at the branch office. Branch offices of full-service broker-dealers are required to prepare and keep those two categories of records, and the agency does not see any justifiable basis why branch offices of mutual fund or DPP broker-dealers should not have to

also.

As a result of public comment letters and hearing testimony received, modifications were made to both the language in, and the ANALYSIS for, this rule to clarify the intended scope and coverage of the amendments in the rule. With respect to the amendment cross-referencing sub. (1)(p) (which refers to an advertising file), a separate sentence is added specifying that the advertising materials to be prepared and kept current in such file at each branch office of a mutual fund or DPP broker-dealer are advertising materials either generated from such branch office or mailed by or placed in media by the branch office. Thus each branch office would not have to maintain hard copies of advertising materials generated by, and mailed/distributed from, the principal/national office.

Additionally, with respect to the amendment language in the rule cross-referencing SEC 4.03(3)(d) (relating to customer monthly statement records), language is added herein to the ANALYSIS noting that the cross-reference to sub. (3)(d) must be read in conjunction with current sub. 4.03(4). Subsection 4.03(4) provides that the record retention requirement for <u>any</u> type of record listed under sub. (3) (thus including customer monthly statements) may be satisfied by computer retention so long as a printed copy of the record can be prepared immediately upon request.

SECTION 20. SEC 4.05(6) is amended to read:

SEC 4.05(6) Every licensed broker-dealer shall employ at its principal office <u>or designated office of supervision in accordance with s. SEC 4.03(1),</u> at least one person designated in writing to the commissioner to act in a supervisory capacity who is licensed as a securities agent in this state and has satisfied the supervisory examination requirement in s. SEC 4.01(5), ~~provided that if~~ <u>. I</u>f a licensed broker-dealer is not in compliance with the requirements of this paragraph, it has 45 days from the first date of non-compliance to meet the requirements of this paragraph.

<u>ANALYSIS</u>: This amendment to the broker-dealer rule of conduct provision relating to designated supervisors is necessary as a result of the amendment to SEC 4.03(1) in an earlier SECTION.

The amendment language has been modified from its comment draft form as a result of public comment letters received

and also reflects the modifications made to rule SEC 4.03(1) (which is cross-referenced in this rule) to clarify that a broker-dealer is in compliance under the rule when it chooses to identify/specify someone either from its principal office, or from a designated office other than the principal office, as the designated supervisor. Thus, any broker-dealer firm which might have records retained in several regional storage locations need not have examination-qualified supervisory personnel at each separate location.

SECTION 21. SEC 4.06(2)(a) is amended to read:

SEC 4.06(2)(a) Borrowing money or securities from, or lending money or securities to, a customer of the agent or the broker-dealer that employs the agent unless that customer is a financial institution or institutional investor designated in s. 551.23(8), Stats., or s. SEC 2.02(4);

ANALYSIS: This amendment to a prohibited business practice rule applicable to securities agents clarifies that the rule's prohibition extends to any securities customer of the agent or the broker-dealer firm. The amendment is necessary to remedy an ambiguity in the current form of the rule that was raised in the context of an enforcement inquiry by the Commissioner's staff. The issue in that situation became whether the prohibition was triggered when an agent borrowed funds from a person who was a customer of the broker-dealer firm, but where the customer did all his securities transactions with a different agent of the firm than the agent who actually borrowed the funds. This amendment would remedy that ambiguity and would preclude any situation where two agents could work in collusion to seek to avoid triggering the prohibition. Language is included in the amendment to provide that the restrictions under the rule do not extend to borrowing/lending transactions by an agent with 551.23(8) financial institutions (such as incident to obtaining a real estate mortgage or car loan from a bank) to cover situations where such financial institution might be a "customer" of the broker-dealer firm in some context.

SECTION 22. SEC 4.11(1)(c) is amended to read:

SEC 4.11(1)(c) Disclose, in conjunction with any reference to either the absence of a penalty for early withdrawal or to a secondary resale market for the certificates of deposit, that the resale price in a transaction in the secondary market may be less than the face

value of the certificate.

ANALYSIS: These amendments to sub. (1)(c) of SEC 4.11 (which deals with brokered certificates of deposit) makes the disclosure requirement of the rule applicable also when brokered CD advertising materials make reference to the absence of a penalty for early withdrawal. The required disclosure to a customer under the rule relating to the risk of principal loss should be triggered in any situation involving early liquidation in a secondary market transaction of a brokered CD.

SECTION 23. SEC 5.01(3) is amended to read:

SEC 5.01(3)(a) Unless waived under sub. (4)-~~(a)~~, each applicant for an initial license as an investment adviser or for qualification as an investment adviser representative after January 1,-~~1984~~-1993, and each applicant whose application has not become effective by January 1,-~~1984~~-1993, is required to pass ~~Part-I-of-the-Wisconsin Investment-Adviser-Representative~~-the North American Securities Administrators Association Series 65 Uniform Investment Adviser Law Examination with a grade of at least ~~75~~-70%.

ANALYSIS: These amendments to the Wisconsin rule containing the investment adviser examination testing requirement, substitute passage of the recently developed NASAA Series 65 Investment Adviser Examination for the current Wisconsin examination.

SECTION 24. SEC 5.01(4) is repealed and recreated to read:

SEC 5.01(4) The examination requirement in sub. (3) shall be waived for any applicant who meets any of the following criteria:

(a) The applicant has passed, or has received a waiver from the need to pass, the National Association of Securities Dealers, Inc. Series 2, 7 or 24 examination, or predecessor examination, and in addition has passed the North American Securities Administrators Association Series 63 Examination.

(b) The applicant has been licensed as an investment adviser or qualified as an investment adviser representative under ch. 551. Stats., within 2 years prior to the date the application is filed.

(c) The applicant has received an order of the commissioner, issued under such conditions as the commissioner may prescribe, waiving the requirement to take and pass the examination in sub. (3).

ANALYSIS: This SECTION revises SEC 5.01(4) which lists the various bases upon which a waiver is available from the need to pass the investment adviser examination testing requirement in SEC 5.01(3). The changes from the current rule are as follows: (1) Repealed are the bases for waiver under current sub. (4)(a)2 (meeting the exam requirement within the prior 2 years), sub. (4)(a)3 (licensed within the prior 2 years by another state requiring an equivalent exam), and sub. (4)(a)4 (waiver by the commissioner on an individual case basis). (2) Added to the list of alternative securities examinations in current SEC 5.01(4)(a)1 whose passage can be considered for purposes of a waiver thereunder, is the NASD Series 24 examination (or its predecessor), as well as the predecessors to the NASD's Series 2 or Series 7 Examinations. (3) Deleted is the entirety of current SEC 5.01(4)(b) because the existing Wisconsin Investment Adviser Representative Examination is being abolished and will be replaced by the NASAA Series 65 Examination. Retained without change as pars. (b) and (c) are the waivers specified in current rules SEC 5.01(4)(a)5 (licensure within the prior 2 years) and (4)(a)6 (waiver by order of the commissioner).

SECTION 25. SEC 5.02(3) is created to read:

SEC 5.02(3) The commissioner may by order exempt any investment adviser 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 commissioner determines that compliance with the provisions is not necessary in the public interest or for the protection of investors.

ANALYSIS: This new subsection to the investment adviser net capital requirement adds waiver language (paralleling language in sub. (4) of the broker-dealer net capital requirement of SEC 4.02) permitting the Commissioner to

exempt by order an investment adviser from the net capital requirement upon a proper showing.

SECTION 26. SEC 5.03(1) (intro.) is amended to read:

SEC 5.03 INVESTMENT ADVISERS' RECORDS (1) Every licensed investment adviser shall ~~maintain~~ prepare and keep current at its principal office, at a designated office located in the United States as specified in writing to, and permitted by, the commissioner, 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 amendment to the investment adviser licensing rule requirement relating to where a firm's books and records must be kept, parallels an identical amendment to the equivalent broker-dealer requirement in SEC 4.03(1)(intro.).

Additionally, identical modifications to this proposed rule were made as were made to SEC 4.03(1) as a result of public comment letters and hearing testimony received. Specifically, the identical language "or at an office under the direct supervision and control of the principal or designated office" found in SEC 4.03(2) was added to this rule to clarify--not only for purposes of this rule, but also for purposes of the designated supervisor requirements in SEC 5.05(7)--that any investment adviser firm which might have records in several regional storage locations need not have examination-qualified supervisory personnel at each separate location where records might be located/kept. Rather, by means of the language added to this rule, such an investment adviser is in compliance when it chooses to identify someone either from the principal office, or from a designated office other than the principal office, as the designated superisor for any or all such records.

SECTION 27. SEC 5.03(6) is renumbered SEC 5.03(7)

ANALYSIS: This renumbering is for the purpose of making room for a new paragraph in the following SECTION that, in the numbering sequence of SEC 5.03 belongs before current sub. (6) (which gives general authority to the Commissioner to exempt an investment adviser from all or part of the recordkeeping requirements listed in SEC 5.03).

SECTION 28. SEC 5.03(6) is created to read:

SEC 5.03(6) An investment adviser whose office location where its books and records are prepared and kept pursuant to SEC 5.03(1) is outside the United States, shall enter into a memorandum of understanding acceptable to the commissioner describing how the adviser's records will be accessible for examination by the commissioner, and establishing a surety bonding requirement to provide for payment of expenses incurred by the commissioner's staff in conducting an examination of the adviser's activities or books and records in a foreign country.

ANALYSIS: This new subsection of the investment adviser books and records requirement is necessary to deal with licensing application situations now being encountered by the agency involving investment advisers that have their principal office located outside the United States. This situation poses a difficult obstacle to the agency's staff with regard to conducting field office examinations of the firm's books and records. The costs of travel to foreign countries, particularly Europe, while arguably chargeable to the licensee or applicant under SEC 7.01(3)(e), would generally be substantially higher than for such examinations within the continental U.S. The new rule requires investment advisers whose principal office, or designated office for retention of books and records, is outside the U.S. to make provision for these regulatory concerns through the mechanism of entering into a Memorandum of Understanding with the Commissioner--which is how the U.S. Securities and Exchange Commission deals with non-U.S. investment advisers. The provisions of the MOU under this rule would do the following: (1) Detail how the firm's books and records will be accessible for examination by the agency's staff; and (2) Establish a surety bonding requirement to provide for payment of expenses incurred by the agency's staff in conducting an examination of the adviser's activities or books and records in a foreign country.

SECTION 29. SEC 5.05(7) is amended to read:

SEC 5.05(7) Every licensed investment adviser shall employ at its principal office or designated office of supervision in accordance with s. SEC 5.03(1), at least one person designated in writing to the commissioner to act in a supervisory capacity who is qualified as an

investment adviser representative in this state and has satisfied the supervisory examination requirement in s. SEC 5.01(5)~~;-provided-that if~~ .If a licensed investment adviser is not in compliance with the requirements of this paragraph, it has 45 days from the first date of noncompliance to meet the requirements of this paragraph.

ANALYSIS: This amendment to the investment adviser rule of conduct provision relating to designated supervisors is necessary as a result of the amendment to SEC 5.03(1) in an earlier SECTION and parallels an identical amendment to the equivalent broker-dealer requirement in SEC 4.05(6).

As a result of comment letters received, the amendment language has been modified from its comment draft form (in identical fashion to modifications made to the equivalent broker-dealer rule in SEC 4.05(6)) to clarify that an investment adviser is in compliance with the rule when it chooses to identify/specify someone either from its principal office, or from a designated office other than the principal office, as the designated supervisor. Thus any investment adviser that might have records retained in several regional storage locations need not have examination-qualifed supervisory personnel at each seaprate location.

SECTION 30. SEC 7.01(5)(d) is amended to read:

SEC 7.01(5)(d) ~~Copy-of-small-~~Small corporate offering registration and prospectus disclosure form on printed Form U-7 or on 3-1/2" computer diskette, IBM compatible, running "Word Perfect" 5.0 software with a minimum of 720K of capacity $5

ANALYSIS: This amendment provides that the Form U-7 Small Corporate Offering Registration and Prospectus Disclosure Form will be available in a computer diskette format, as well as in printed form, for the same $5 cost.

SECTION 31. SEC 7.02(1)(b) is amended to read:

SEC 7.02(1)(b). Advertising published or circulated relating to a security exempted under s. 551.22, Stats., except under s. SEC 2.01 ~~(3)~~(4)(a); or relating to a transaction exempted under s. 551.23(4), (5), (6), (7) or (8), Stats.; or relating to a transaction exempted under s. 551.23(12), (13) or (14), Stats., if the issuer has

any securities registered under section 12 of the securities exchange act of 1934 or exempted from registration by section 12(g)(2)(G) thereof or is an investment company registered under the investment company act of 1940; or relating to a transaction exempt from registration under s. SEC 2.027 where the advertising has been filed with the commissioner under s. SEC 2.027(7); or relating to a transaction subject to the filing requirements of section 14(d) of the securities exchange act of 1934; provided the transaction is not subject to the filing requirements of s. SEC 6.05(1).

ANALYSIS: This amendment corrects a cross-reference in the rule to reflect a previous renumbering of SEC 2.01(3)(a) that occurred in the 1990 agency rule revision process.

SECTION 32. SEC 32.05(1)(c)5 is amended to read:

SEC 32.05(1)(c)5. There is filed by or on behalf of the franchisor, at least 10 business days prior to the offer of a franchise in this state, a notice of the proposed offer or sale, including any prospectus, circular or other material to be delivered to prospective franchisees and other information the commissioner may require, together with a consent to service of process as specified in s. 553.27(10), Stats., and the commissioner does not by order withdraw, deny or revoke the exemption within 10 business days. The commissioner may, within 10 days after the filing date of the notice or other information, require that additional information reasonably related to the offering be filed . If the commissioner requires additional information, the date by which the commissioner may withdraw, deny or revoke the exemption is 10 days after the date of filing that information.

ANALYSIS: This amendment adds to the subdivision containing the notice filing requirement for purposes of claiming the franchise registration exemption of SEC 32.05(1)(c),

language based on sec. 553.24(6) and 551.24(6). The amendment is necessary to clarify an ambiguity under the language of sec. 553.24(6) which provides that it applies to "applications" filed under sec. 553.25, Wis. Stats., and rules thereunder, whereas the filing made under this rule is technically regarded as a 10-day "notice"-type filing.

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

DATED this 16th day of November, 1992.

(SEAL)

WESLEY L. RINGO
Commissioner of Securities