

## Chapter SEC 5

### LICENSING OF INVESTMENT ADVISERS

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**SEC 5.01 Licensing procedure.** (1) Applications for initial and renewal licenses and qualifications of investment advisers and their representatives shall be filed on forms prescribed by the commissioner in s. SEC 9.01 (1).

(2) A licensing "application" for purposes of s. 551.32 (1) (b), Stats., means all information required by the form prescribed under sub. (1) and any additional information required by the commissioner.

(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, and each applicant whose application has not become effective by January 1, 1996, is required to pass either of the following examinations with a grade of at least 70%:

(a) The North American Securities Administrators Association Series 65 Uniform Investment Adviser Law Examination; or

(b) The North American Securities Administrators Association Series 66 Uniform Combined State Law Examination.

(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 or has received a waiver from the need to pass either the North American Securities Administrators Association Series 63 or Series 66 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).

(5) Prior to issuance of a license as an investment adviser, at least one employe located at the principal office of the investment adviser must be designated in the license application on the form prescribed in s. SEC 9.01(1)(b) and filed with the commissioner to act in a supervisory capacity and be qualified as an investment adviser representative for the investment adviser, and must satisfy the examination requirement in sub. (3) unless the examination is waived under sub. (4).

(6) Any application for license which is not completed or withdrawn within 6 months from the date it is initially received may be deemed materially incomplete under s. 551.34 (1) (a), Stats., and the commissioner may issue an order denying effectiveness to the application.

(7) Every investment adviser whose principal office is located in this state shall have at least one person qualified as an investment adviser representative employed on a full-time basis at its principal office.

**History:** Cr. Register, December, 1977, No. 264, eff. 1-1-78; am. (1), Register, December, 1979, No. 288, eff. 1-1-80; am. (1) and (6), renum. (4) (b) and (c) to be (4) (c) and (d), cr. (4) (b), r. and recr. (5), Register, December, 1980, No. 300, eff. 1-1-81; am. (3) to (5), Register, December, 1982, No. 324, eff. 1-1-83; am. (1) and (2), r. and recr. (3) and (4), Register, December, 1983, No. 336, eff. 1-1-84; am. (3),

renum. (4) (g) to be (4) (h), cr. (4) (g), Register, December, 1986, No. 372, eff. 1-1-87; renum. (3) to be (3) (a) and am., renum. (4) (b) to be (4) (c) to (i), r. (4) (intro.) and (a), cr. (3) (b), (4) (a) and (b), Register, December, 1987, No. 384, eff. 1-1-88; renum. (4) (c) to (i) to be (4) (c) 1. to 4., (4) (b) 3. and 4. and (c) 5. and; am. (3), r. and recr. (4), Register, December, 1992, No. 444, eff. 1-1-93; am. (4) (b) 3. and 4., cr. (4) (c) (intro.), Register, December, 1988, No. 396, eff. 1-1-89; renum. (4) (a), (c) 1. to 5. to be (4) (a) (intro.) and 2. to 6. and am. (intro.), cr. (4) (a) 1., am. (4) (b) (intro.), r. (4) (c) (intro.), Register, December, 1990, No. 420, eff. 1-1-91; am. (3), r. and recr. (4), Register, December, 1992, No. 444, eff. 1-1-93; renum. (3) (a) to (3), r. (3) (b), Register, December, 1994, No. 468, eff. 1-1-95; r. and recr. (3), am. (4) (a) and (5), Register, December, 1995, No. 480, eff. 1-1-96.

**SEC 5.02 Net capital requirement.** (1) Every investment adviser 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 commissioner.

(2) If an investment adviser is an individual, the person shall segregate from personal capital an amount sufficient to satisfy the net capital requirement, and the amount so segregated shall be utilized solely for the business for which the investment adviser is licensed.

(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.

**History:** Cr. Register, December, 1977, No. 264, eff. 1-1-78; cr. (3), Register, December, 1992, No. 444, eff. 1-1-93; am. (1), Register, December, 1995, No. 480, eff. 1-1-96.

**SEC 5.03 Investment advisers' records.** (1) Every licensed investment adviser shall 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:

(a) All partnership agreements, or all articles of incorporation, by-laws, minute books and stock certificate books of the investment adviser.

(b) A general ledger (or other records in the case of a sole proprietor) reflecting all asset, liability, income, expense, and capital accounts.

(c) A record showing all payments received, including date of receipt, purpose, and from whom received; and all disbursements, including date paid, purpose, and to whom made.

(d) A record showing all receivables and payables.

(e) All trial balances, financial statements, and internal audit working papers which may be prepared relating to the business of the investment adviser.

(f) A memorandum of each order given by the investment adviser for the purchase or sale of any security, of any instruction received by the investment adviser from the customer concerning the purchase, sale, receipt or delivery of a particular security, and of any modification or cancellation of any order or instruction.

The memoranda shall show the terms and conditions of the order, instruction, modification or cancellation; shall identify the person connected with the investment adviser who recommended the transaction to the customer and the person who placed the order; and shall show the account for which entered, the date of entry, and the bank, broker or dealer by or through whom executed. Orders entered pursuant to the exercise of discretionary power shall be so designated.

(g) Copies of all written communications, correspondence, confirmations, appraisals and other records relating to investment activities of customers.

(h) Copies of all complaints of customers relating to investment activities for customers, and containing evidence, including representative copies, of the responses made by the investment adviser to the complaint. In this paragraph, "complaint" means any written or oral statement of a customer or any person acting on behalf of a customer alleging a grievance involving the activities of persons under the control of the investment adviser in connection with providing investment advice or placing orders on behalf of customers.

(i) A list or other record of all accounts in which the investment adviser is vested with any discretionary power with respect to the funds, securities or transactions of any customer.

(j) A copy of all powers of attorney and other evidences of the granting of any discretionary authority by any customer to the investment adviser or to a third party.

(k) A copy of all written agreements entered into by the investment adviser with any customer, or with any other person if the agreement relates to the business of the investment adviser.

(l) A file containing any advertisement (as defined within the meaning of SEC 206 (4)-1. of the investment advisers act of 1940) used in connection with the offering of the investment advisory services in this state.

(m) A record or information demonstrating compliance with the net capital requirement in s. SEC 5.02.

(n) A record that complies with Rule 204-2 (a) (12) under section 204 of the investment advisers act of 1940 containing information for all securities transactions effected for the account of the investment adviser or any of its employees subject to that rule, including the title and amount of the security involved, the date and nature of the transaction, the execution price, and information regarding customer transactions in the same security.

(2) Each licensed investment adviser who renders investment supervisory or management service to any customer shall, with respect to the portfolio being supervised or managed and to the extent that the information is reasonably available to or obtainable by the investment adviser, maintain and keep current:

(a) Records for each customer showing the securities purchased or sold on advice of the adviser, and the date, amount, and price of each purchase and sale.

(b) Records identifying the customer and the current amount or interest owned by each customer for each security in which any customer has a current position.

(3) Every licensed investment adviser shall preserve for a period of not less than 6 years, the first 2 years in an easily accessible place, all records required under sub. (1) except that records respecting an account required under sub. (1) (i), (j) and (k) shall be preserved by the investment adviser for a period of not less than 6 years after the closing of the account and records required under sub. (1) (a) shall be preserved by the investment adviser for a period of not less than 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 2 years as required in this subsection, a microfilm copy may be substituted for the remainder of the required period.

(4) Every branch office of a licensed investment adviser, as defined in s. SEC 1.02 (7) (b), shall prepare and keep current the records described in subs. (1) (c), (f), (g), (h), (k) and (L) and (2) (a) and (b).

(5) The records required in sub. (4) 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.

(6) An investment adviser whose office location where its books and records are prepared and kept pursuant to sub. (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.

(7) The commissioner may by order exempt any investment adviser from all or part of the requirements of this section, either unconditionally or upon specified conditions, if by reason of the special nature of its business, the commissioner finds that issuance of the order is necessary or appropriate in the public interest or for the protection of investors.

**History:** Cr. Register, December, 1977, No. 264, eff. 1-1-78; r. and recr. (1), renum. (2) and (3) to be (3) and (4) and am., cr. (2), Register, December, 1980, No. 300, eff. 1-1-81; am. (3), Register, December, 1984, No. 348, eff. 1-1-85; am. (1) (b), Register, December, 1989, No. 408, eff. 1-1-90; am. (1) (intro.), renum. (4) to be (6), cr. (4) and (5), Register, December, 1991, No. 432, eff. 1-1-92; am. (1) (intro.), renum. (6) to be (7), cr. (6), Register, December, 1992, No. 444, eff. 1-1-93; am. (4), Register, December, 1994, No. 468, eff. 1-1-95; cr. (1) (m) and (n), Register, December, 1995, No. 480, eff. 1-1-96.

**SEC 5.04 Reporting requirements.** (1) Every investment adviser shall file with the commissioner immediate notice via facsimile whenever the net capital of the investment adviser is less than is required under s. SEC 5.02(1), 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.

(2) Each investment adviser shall file with the commissioner a copy of any complaint related to its business, transactions, or operations in this state, naming the investment adviser or any of its partners, officers or investment adviser representatives as defendants in any civil or criminal proceeding, or in any administrative or disciplinary proceeding by any public or private regulatory agency, within 20 days of the date the complaint is served on the investment adviser; a copy of any answer or reply to the complaint filed by the investment adviser within 10 days of the date the answer or reply is filed; and a copy of any decision, order or sanction made with respect to any such proceeding within 20 days of the date the decision, order or sanction is rendered.

(3) Except as provided in subs. (2) and (4), each investment adviser shall file with the commissioner any notice of change of control or change of name, as well as any material change in the information included in the investment adviser's most recent application for license, in an amendment to Form ADV filed with the commissioner within 30 days of the date of the change.

(4) Each investment adviser shall notify the commissioner in writing within 10 days from the first date the person who is the designated supervisor under s. SEC 5.05 (7) no longer is acting in that capacity. The notification shall either identify a substituted designated supervisor or undertake to identify to the commissioner in writing a substituted designated supervisor within the 45 day period provided under s. SEC 5.05 (7).

(5) (a) Each investment adviser shall notify the commissioner in writing at least 14 days prior to either the opening or the change of address in this state of any branch office as defined in s. SEC 1.02 (7) (b).

(b) Each investment adviser shall notify the commissioner in writing at least 14 days after the closing in this state of any branch office as defined in s. SEC 1.02 (7) (b).

(c) The notification provided to the commissioner under pars. (a) or (b) shall include the address and telephone number of the branch office, the name of the supervisor at the branch office, the number of representatives operating out of that branch office and any other information the commissioner may request.

(6) Each investment adviser shall file annually with the commissioner incident to its license renewal application, a report identifying each of its branch offices as defined by s. SEC 1.02 (7) (b) that is located in this state.

**History:** Cr. Register, December, 1977, No. 264, eff. 1-1-78; am. (2) to (4), Register, December, 1980, No. 300, eff. 1-1-81; am. (1) and cr. (1) (b), Register, December, 1982, No. 324, eff. 1-1-83; cr. (5), Register, December, 1989, No. 408, eff. 1-1-90; am. (1) (a), r. and recr. (3), r. (4), renum. (5) to be (4), Register, December, 1990, No. 420, eff. 1-1-91; am. (1) (a), cr. (5) and (6), Register, December, 1991, No. 432, eff. 1-1-91; am. (1) (a), cr. (1) (c), Register, December, 1994, No. 468, eff. 1-1-95; r. and recr. (1), Register, December, 1995, No. 480, eff. 1-1-96.

**SEC 5.05 Rules of conduct.** (1) Each investment adviser shall establish written supervisory procedures and a system for applying the procedures, which may reasonably be expected to prevent and detect any violations of ch. 551, Stats., and rules and orders thereunder. The procedures shall include the designation and qualification of a number of supervisory employees reasonable in relation to the number of its qualified investment adviser representatives, offices and activities in this state.

(2) An investment adviser shall not enter, extend, or renew any investment advisory contract if the contract:

(a) Provides for compensation to the investment adviser on the basis of a share of capital gains upon, or capital appreciation of, the funds or any portion of the funds of a client other than a person specified in s. 551.23 (8), Stats., or by rule thereunder;

(b) Fails to provide, in substance, that no assignment of the contract may be made without the consent of the customer; or

(c) Fails to provide, in substance, that the investment adviser, if a partnership, shall notify the other party to the contract of any change in the membership of the partnership within a reasonable time after such change.

(d) Fails to disclose, in substance, the term of the advisory agreement, the fee to be charged by the adviser, the formula for computing the advisory fee, the formula for computing the amount of prepaid fee to be returned in the event of contract termination or non-performance, and whether the contract grants discretionary power to the adviser.

(3) Subsection (2) (a) shall not prohibit an investment advisory contract which provides for compensation based upon the total value of a fund averaged over a definite period, or as of definite dates or taken as of a definite date. "Assignment," as used in sub. (2) (b) includes any direct or indirect transfer or hypothecation of an investment advisory contract by the assignor or of a controlling block of the assignor's outstanding voting securities by a security holder of the assignor; but, if the investment adviser is a partnership, no assignment of an investment advisory contract is considered to result from the death or withdrawal of a minority of the members of the investment adviser having only a minority interest in the business of the investment adviser, or from the admission to the investment advisor of one or more members who, after admission, will be only a minority of the members and will have only a minority interest in the business. As used in sub. (2), "investment advisory contract" means any contract or agreement whereby a person agrees to act as investment adviser or to manage any investment or trading account for a person other than persons specified under s. 551.23 (8), Stats.

(4) An investment adviser shall not enter any contract with a customer if the contract contains any condition, stipulation or provision binding the customer to waive any rights under ch. 551, Stats., or any rule or order thereunder. Any such condition, stipulation or provision is void.

(5) No licensed investment adviser may enter into, extend or renew any investment advisory contract with a customer in this state unless the contract is in writing and a copy of the contract is given to the customer within 20 days after the execution of the contract.

(6) Each investment adviser who renders account supervisory or management services shall provide at least annually to each Wisconsin customer a written summary of the customer's account which includes information setting forth the name, quantity and market value of each security under management, and the total value of cash and securities under management.

(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 on the form prescribed in s. SEC 9.01 (1) (b) and filed with 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). If a licensed investment adviser 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.

(8) Each investment adviser shall provide to each of its customers a written brochure or other document meeting the requirements of rule 204-3 under the Investment Advisers Act of 1940 relating to its business and activities.

(9) Each investment adviser that participates in a wrap fee arrangement with a broker-dealer shall disclose to each customer under the arrangement the portion of the wrap fee that is attributable to advisory services. This requirement may be satisfied if the information is contained in the brochure provided to the customer either by the investment adviser or the sponsor of the wrap fee arrangement.

**History:** Cr. December, 1977, No. 264, eff. 1-1-78; am. (1), r. (5) and (6), cr. (2) (d), (5) to (7), Register, December, 1980, No. 300, eff. 1-1-81; am. (7), Register, December, 1982, No. 324, eff. 1-1-83; cr. (8), Register, December, 1987, No. 384, eff. 1-1-88; am. (2) (a) and (7), Register, December, 1989, No. 408, eff. 1-1-90; am. (5), Register, December, 1991, No. 432, eff. 1-1-92; am. (7), Register, December, 1992, No. 444, eff. 1-1-93; cr. (9), Register, December, 1994, No. 468, eff. 1-1-95; am. (7), Register, December, 1995, No. 480, eff. 1-1-96.

**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 under s. 551.34 (1) (g), Stats., without limiting those terms to the practices specified in this section:

(1) Exercising any discretionary power in placing an order for the purchase or sale of securities for the account of a customer without first obtaining written discretionary authority from the customer unless the discretionary power relates solely to the price at which, or the time when, an order involving a definite amount of a specified security shall be executed, or both.

(2) Placing an order to purchase or sell a security for the account of a customer upon instructions of a third party without first having obtained written third party trading authorization from the customer;

(3) Inducing trading in a customer's account that is excessive in size or frequency in view of the financial resources and character of the account;

(4) Recommending to a customer the purchase, sale or exchange of any security without reasonable grounds to believe that the recommendation is suitable for the customer on the basis of information furnished by the customer after reasonable inquiry concerning the customer's investment objectives, financial situa-

tion and needs, and any other information known by the investment adviser;

(5) Placing an order to purchase or sell a security for the account of a customer without authority to do so;

(6) Borrowing money or securities from, or lending money or securities to, a customer;

(7) Representing itself as a 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;

(8) Placing an order for the purchase or sale of a security if the security is not registered or the security or transaction is not exempt from registration under ch. 551, Stats.

(9) Placing an order for a customer, or recommending that the customer place an order, to purchase or sell a security through a broker-dealer or agent not licensed under ch. 551, Stats., unless the customer is a person described in s. 551.23 (8), Stats.

(10) Recommending to a customer that the customer engage the services of a broker-dealer, agent or investment adviser not licensed under ch. 551, Stats., unless the customer is a person described in s. 551.23 (8), Stats.

(11) Failing accurately to describe or disclose in advertising or other materials used in connection with the promotion or transaction of investment advisory services in this state, the identity of the investment adviser or the nature of the investment advisory services offered or the employment relationship between the investment adviser and its representatives. For purposes of this subsection, "other materials" include, but are not limited to, business cards, business stationery and display signs.

**History:** Cr. Register, December, 1977, No. 264, eff. 1-1-78; am. (intro.) and (1), renum. (2) to be (8) and am., cr. (2) to (7), Register, December, 1980, No. 300, eff. 1-1-81; am. (9), cr. (10), Register, December, 1986, No. 372, eff. 1-1-87; cr. (11), Register, December, 1989, No. 408, eff. 1-1-90.

**SEC 5.07 License 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 commissioner 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 commissioner may by order limit the period of, or specify an earlier expiration date for, any license.

(2) The qualification 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 by a specified investment adviser licensed under ch. 551, Stats.

**History:** Cr. Register, December, 1977, No. 264, eff. 1-1-78; am. Register, December, 1980, No. 300, eff. 1-1-81; am. (1), Register, December, 1994, No. 468, eff. 1-1-95.

**SEC 5.08 Withdrawal of licenses.** (1) An application for withdrawal from the status of a licensed investment adviser under s. 551.34 (6), Stats., shall be filed by the licensee on Form ADV-W prescribed by the commissioner, and shall include a report on the status of all customer accounts of the licensee in this state and any additional information the commissioner may require.

(2) An application for withdrawal from the status of a qualified investment adviser representative shall be filed by the investment adviser which the person represents within 15 days of the termination of the representative's employment on Form U-5 prescribed by the commissioner.

**History:** Cr. Register, December, 1977, No. 264, eff. 1-1-78; am. (1) and (2), Register, December, 1979, No. 288, eff. 1-1-80; am. (2), Register, December, 1982, No. 324, eff. 1-1-83; am. Register, December, 1994, No. 468, eff. 1-1-95.

**SEC 5.09 Denial, suspension, revocation and censure.** Any order denying, suspending or revoking the license of an investment adviser or censuring a licensee may include such other sanctions as the commissioner finds appropriate.

**History:** Cr. Register, December, 1977, No. 264, eff. 1-1-78.