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**Report From Agency****PROPOSED ORDER OF THE STATE OF WISCONSIN,  
DEPARTMENT OF FINANCIAL INSTITUTIONS, DIVISION OF SECURITIES  
ADOPTING RULES**

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

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**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.

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

20 Section 1: The branch office definition for broker-dealers has been harmonized with  
21 FINRA and other state regulators for many years. However, with the change in the Uniform  
22 Securities Act in 2009, the branch office definition in the rule was changed to refer to a slightly  
23 different statutory definition of “place of business.” The statutory definition works for  
24 investment advisers but not broker-dealers, hence the change in this rule.

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

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

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

34 Section 5: Incident to the Division’s 2008 rules revision to coordinate with the adoption  
35 of the new Wisconsin Securities Law effective January 1, 2009, current rule DFI-Sec 2.02(9)(c)  
36 inadvertently cross-referenced statute section 551.102(11) rather than the proper corresponding  
37 statute in sec. 551.202(13) [which specifically refers to “accredited investors,” whereas sec.  
38 551.102(11) does not]. This amendment corrects that cross-referencing error.

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

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

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

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

65 Section 10: This amendment clarifies that the Series 65 and 66 exams referred to are the  
66 post-1999 version as specified in subd. 2. It also adds clarification that if the applicant was  
67 registered as an agent of a broker-dealer within two years of the application and the approval of  
68 that registration was based on passage of the Series 7 and 66 exams, those exams would still be  
69 considered active for purposes of meeting the exam requirement in subd. 3.

70 Section 11: This new section clarifies that a notice of the opening of a branch office is not  
71 complete and therefore, not deemed “filed” until all fees, including any applicable late filing  
72 fees, are received. This parallels the fee payment component in the investment adviser

73 application rule in s. DFI-Sec 5.01(2)(a) and the investment adviser representative rule in s. DFI-  
74 Sec 5.01(2)(b).

75 Section 12: Because applications are effective 30 days after filing, a renewal for January  
76 1 effectiveness must be filed by December 1<sup>st</sup>. The date of November 30<sup>th</sup> is incorrect.

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

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

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

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

102 Section 17: Corrects a statutory citation.

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

109 Section 19: This rule contains the following amendments: (1) specifies that the  
110 application to amend should use the Uniform Franchise Registration Application Form (Form  
111 A); and (2) changes the franchise statute cross-referenced in the rule to be s. 553.31(1), Stats.,  
112 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.

### **Agency Contact Persons**

To obtain a copy of the proposed rule or fiscal estimate at no charge, to submit written comments regarding the proposed rule, or for questions regarding the agency's internal processing of the proposed 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 proposed rule may also be obtained and reviewed at the Department of Financial Institution's website, www.wdfi.org. Written comments must be received by the conclusion of the department's hearing regarding the proposed rule.

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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- 113           SECTION 1. DFI-Sec 1.02(7) is repealed and recreated to read:
- 114   **DFI-Sec 1.02(7)** (a) For purposes of ch. DFI-Sec 4, "branch office" has the same meaning as
- 115 rule 3010(g)(2) of the Financial Industry Regulatory Authority.
- 116 (b) For purposes of ch. DFI-Sec 5, "branch office" has the same meaning as "place of business"
- 117 in s. 551.102 (21), Stats.
- 118           SECTION 2. DFI-Sec 1.02(8) is created to read:

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

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

124 **DFI-Sec 1.02(14)(intro)** The following defined terms apply for purposes of the definition of  
125 "investment adviser" in s. 551.102(15), Stats., and "investment adviser representative" in s.  
126 551.102 (16), Stats.:

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

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

131 **DFI-Sec 2.02(5)(d)1.** Except as provided in this subdivision, any offer or sale of interests in a  
132 ~~limited partnership~~ an entity that is or will be primarily engaged in oil, gas or mining activities,  
133 any investment contract irrespective of the kind of assets held or business engaged in by the  
134 enterprise, or any certificate of interest or participation in an oil, gas or mining title or lease, or in  
135 payments out of production under the title or lease, if the aggregate offering price or face  
136 amount, whichever is greater, of all securities to be offered by or on behalf of the issuer, together  
137 with the value of any securities sold to persons in this state by or on behalf of the issuer during  
138 the prior 12 months, exceeds \$100,000, unless prior to the offering the issuer files a notice of the  
139 proposed offer or sale with the division, including any prospectus, circular or other material to be  
140 delivered to offerees, and other information as the division may require, and the division does  
141 not by order withdraw, deny or revoke the exemption within 10 days. This paragraph is not

142 applicable to any offer or sale made by a broker-dealer registered in Wisconsin if the broker-  
143 dealer is not affiliated with either the issuer or sponsor of the issuer by means of direct or indirect  
144 common control;

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

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

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

157 **DFI-Sec 2.028 (intro) Wisconsin issuer registration exemption by filing.** If all of the  
158 following conditions are met, other than any condition or conditions waived by the division upon  
159 a showing of good cause, a transaction registration exemption is available under s. 551.203,  
160 Stats., for any offer or sale for cash of the equity securities of an issuer having, both before and  
161 upon completion of the offering, its principal office and a majority of the full-time employees  
162 located in this state:

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

199 3. Any combination of the foregoing services.

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

202 1. The written agreement;

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

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

209 c. Requires that the solicitor, at the time of any solicitation or referral activities for which a cash  
210 fee or any other economic benefit is paid or to be paid by the investment adviser, provide the

211 client with a current copy of the investment adviser's disclosure document required under s. DFI-  
212 Sec 5.05(8) and a separate disclosure statement as described in subsection (d) of this rule, either  
213 in paper or electronic format; and

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

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

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

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

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

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

227 1. The name of the solicitor;

228 2. The name of the investment adviser;

229 3. The nature of the relationship, including any affiliation, between the solicitor and the  
230 investment adviser;

231 4. A statement that the solicitor will be compensated for solicitation or referral services by the  
232 investment adviser;

233 5. The terms of the compensation arrangement including a description of the cash fee or any  
234 other economic benefit paid or to be paid to the solicitor; and  
235 6. The amount of compensation the client will pay, if any, in addition to the advisory fees, and  
236 whether the cash fee or any other economic benefit paid to the solicitor will be added to the  
237 advisory fee, creating a differential with respect to the amount charged to other advisory clients  
238 who are not subject to the solicitor compensation arrangement.

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

