

# Investment Adviser Newsletter

## DIGITAL ASSETS—ARE THEY RIGHT FOR YOUR CLIENTS?

Investment advisers have mentioned to Division of Securities (Division) staff that clients are asking about digital assets and their role in investment portfolios. While digital assets may or may not be securities, they are becoming increasingly popular with retail clients. The Division is providing the following thoughts for investment advisers to consider as they are contemplating the viability of recommending digital assets to clients.

In keeping with your fiduciary duty, any recommendations of digital assets should be in the best interest of your client. This duty requires that the investment adviser know the client, after obtaining and documenting suitability information such as the client's net worth, annual income and other financial information, investment objectives, risk tolerance and experience.

For any investment advisers recommending digital assets, the firm should undertake formidable due diligence efforts, including whether the adviser understands digital assets, digital wallets, and any networks or applications used in connection with digital assets. The due diligence should cover the liquidity and volatility of the digital asset and focus on risks related to the trading venues, trade execution, and settlement.



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## DIGITAL ASSETS CONTINUED...

Digital assets may have unique risks that should be disclosed to clients. Disclosure should include any conflicts of interest that may occur. Risk disclosures for digital assets could include cybersecurity and custody risks. Disclosure could also include price volatility, illiquidity, and valuation methodologies.

Digital assets pose other compliance-related questions for investment advisers. Does executing transactions in digital assets create a custody issue for the investment adviser? How does the investment adviser maintain proper books and records of these transactions? How does digital assets factor into the firm's calculation of regulatory assets under management?

Bottom line - be careful if you decide to give advice on digital assets.

## REGISTRATION RENEWALS FOR 2022

The start of the 4<sup>th</sup> Quarter reminds us that renewal season is approaching. Soon it will be time to renew your firm and individual registrations through IARD (Investment Adviser Registration Depository). Your renewal statement will be available on IARD beginning November 8<sup>th</sup>. Renewal payments for 2022 are due no later than December 13<sup>th</sup> for firm, individual, and branch registrations. Be sure to submit your timely renewal payment to avoid a lapse in your firm's ability to conduct business.

If you are based in Wisconsin and your future plans do not include

renewing for 2022, please take a minute to send an email to [deborah.fabritz@dfi.wisconsin.gov](mailto:deborah.fabritz@dfi.wisconsin.gov) to confirm that you will not be renewing for next year. You should also file an ADV-W regarding your firm's planned withdrawal. Beginning November 1<sup>st</sup>, you may submit ADV-W forms that are post-dated for 12/31/21.

Click [here](#) for the 2022 Renewal Program Calendar. For questions regarding the renewal process or your firm's status, you may contact either the IARD Call Center at (240) 386-4848 or our Examiner of the Day at (608) 266-2139.

## NASAA REPORTS ON 2021 EXAM DEFICIENCIES

The North American Securities Administrators Association (NASAA) conducted a coordinated sweep of examinations of state-registered investment advisers. The full article can be viewed [here](#). A presentation of the data can be found [here](#).

The sweep consisted of 1,206 examinations across 42 US jurisdictions, conducted from January 1<sup>st</sup> to July 7<sup>th</sup> of 2021. The top categories of deficiencies are in registration (e.g., Form ADV and Form U-4 inaccuracies), books & records, and contracts respectively. The Division conducted its own exam sweep of Wisconsin registered investment advisers for exams conducted in the year of 2019. The results of that study can be found in the [2020 Spring newsletter](#). The major deficiencies noted in NASAA's exam sweep and Wisconsin's study are similar, with the exception that our state had a larger share of issues related to invoicing (itemization & delivery) which falls under the "custody" section of the Wisconsin securities rule book.

*"The top categories of deficiencies are in registration, books & records, and contracts respectively"*

This list of best practices recommended by NASAA can be helpful in addressing common compliance issues that face many advisers. It would be a good idea to take some time to review this list and compare it to your firm's own policies & procedures, and make any applicable changes and/or updates. A link to the Wisconsin-specific applicable rule can be found next to the best practice where applicable.

NASAA's Best Practices for Investment Advisers (with rule links).

- Review and revise Form ADV and disclosure brochure annually to reflect current and accurate information. [DFI-Sec 5.04\(3\)\(a\) & 5.04\(3\)\(b\)](#)
- Review and update all contracts. [DFI-Sec 5.05\(2\)](#).

## EXAM DEFICIENCIES CONTINUED...

- Prepare and maintain all required records, including financial records. Back-up electronic data and protect records. Document checks forwarded. [DFI-Sec 5.03\(1\)](#) and [DFI-Sec 5.035\(3\)\(a\)](#).
- Prepare and maintain client profiles or other client suitability information. Maintain due diligence file for recommended products or strategy. [DFI-Sec 5.03\(2\)\(c\)](#).
- Prepare a written compliance and supervisory procedures manual relevant to the type of business to include business continuity plan and information security policies/procedures. [DFI-Sec 5.05\(1\)](#).
- Prepare and distribute a privacy policy initially and annually. Be aware of confidential information transmitted via unsecure means. [NASAA model rule](#).
- Keep accurate and current financials. File timely with the jurisdiction. Maintain surety bond if required. [DFI-Sec 5.03\(1\)](#) and [DFI-Sec 5.02](#).
- Calculate and document fees correctly in accordance with contracts and ADV. [DFI-Sec 5.035\(1\)\(f\)2b](#).
- Review all advertisements, including website and social media for accuracy. [DFI-Sec 5.06\(19\)](#).
- Implement appropriate custody safeguards, especially for direct fee deduction. Prepare and send appropriate fee invoices to clients. [DFI-Sec.5.05\(13\)](#) and [DFI-Sec 5.035\(1\)\(f\)2b](#).
- Add policies/procedures for seniors/vulnerable persons to include training of personnel. [NASAA model rule](#).

If you're uncertain if a best practice or rule would apply to your firm, you can always reach out to the Division of Securities with your questions via telephone at 608-266-2139.

## FEE DISCLOSURES SHOULD BE CLEAR TO YOUR CLIENTS

As a fiduciary, advisers must make certain disclosures to clients, including the fee charged for each investment or financial service. The SEC requires a fee schedule to be disclosed in Item 5 of the ADV Part 2 (brochure), and Wisconsin DFI-Sec 5.05(2)(b) requires the fee and the formula for the fee to be disclosed in the advisory contract. In addition, providing a clear and detailed fee schedule can help prospective clients easily understand and compare costs and services between advisers.

Are your fees clearly disclosed on your ADV Part 2 and advisory contract? To ensure a prospective client can easily understand what services are covered under each fee, make sure your ADV Part 2, Item 5, addresses the following:

- Fee schedules. Describe how you are compensated for your advisory services and provide a fee schedule for each service offered. Disclose whether the fees are negotiable.
- Additional fees. Describe any other types of fees or expenses clients may pay in connection with your advisory services, including fees paid directly to you (administrative or platform fees) or fees clients pay to a third party (custodian fees or mutual fund expenses).
- Complimentary/combined services. Be clear as to whether a paid service includes additional complimentary services, such as asset management clients receiving optional ongoing financial planning at no additional charge.
- AUM tiered schedules. Specify whether your service fees are charged at one tier, or whether a portion of assets under management will be charged across several tiers (weighted).
- Complex fee structures. For services that have complex or tiered fee structures, consider providing sample fee calculations to demonstrate what an actual client might pay for services.

## FEE DISCLOSURES CONTINUED...

- Solicitors/subadvisers. If you are a solicitor or manage assets for other advisers, include a breakdown of what fee or percentage gets paid to each party, and what the client will pay in total.
- Periodic financial planning. For monthly or annual financial planning or consulting fees, indicate in the ADV Part 2 or in the contract whether the contract is ongoing, or if it will need to be renewed at the end of the period.

Make sure your advisory contract addresses the following:

- Fees and formula. List both the fee charged for your advisory service and the formula used (if applicable) to compute that fee.
- Negotiated fees. Be sure any negotiated fees or special agreements are clearly defined in the client's contract.
- Uniformity. Do the fees and services listed in your advisory contract match what is in your brochure, and vice versa? If your fees or offered services have changed, be sure both the contract and the ADV Part 2 have been updated.





## DO YOU HAVE SENIOR FINANCIAL EXPLOITATION POLICIES AND PROCEDURES?

Last month at its annual conference, the North American Securities Administrators Association (NASAA) reported the results of state-registered investment adviser examination data. Every two years, NASAA collects exam data from state securities examiners. This year, the data was voluntarily reported by 42 U.S. jurisdictions (including Wisconsin) between January and July 2021.

The exam results show that nearly 59% of the state-registered investment advisers from the 1,206 advisor exams conducted across the country don't have policies or procedures in place to address financial exploitation of seniors or vulnerable persons.

Protecting senior investors continues to be a priority for NASAA and state regulators. Through its state members, NASAA has done extensive work on issues relating to senior and vulnerable adult financial exploitation. In 2016, NASAA members voted to approve the [NASAA Model Act to Protect Vulnerable Adults from Financial Exploitation](#). As of July 14, 2021, the Act has been adopted, in whole or in part, by thirty-two states. Wisconsin currently has proposed legislation that includes provisions similar to the Model Act pending in the legislature.

*“Investment advisers may be one of the first to notice changes in behavior or signs of unusual financial activities of a client.”*

Investment advisers may be one of the first to notice changes in behavior or signs of unusual financial activities of a client. Early detection of these issues may prevent a client from becoming a victim of financial exploitation. Firms should have up-to-date policies and practices in place that address potential cases of diminished capacity or financial exploitation and will better equip financial services professionals to:

- 1) recognize diminished capacity and financial exploitation;
- 2) understand when and how to escalate reporting of such issues within a firm; and

## POLICY AND PROCEDURES CONTINUED...

3) direct reports to governmental agencies that can conduct additional investigations and provide needed services.

NASAA established a [guide](#) to assist investment advisers in developing practices and procedures for protecting senior investors and vulnerable adults from financial exploitation. NASAA prepared this document to provide investment advisers with information for detecting, reporting, and mitigating senior financial exploitation. Included are suggested practices firms may implement that are designed to detect and address instances of diminished capacity in senior and other clients.

In addition, it is important that employees of the firm are [trained](#) to identify the signs that indicate the possibility of financial exploitation. The signs and red flags that a senior client could be the victim of financial exploitation include:

- Uncharacteristic and repeated cash withdrawals or wire transfers.
- Appearing with new and unknown associates, friends or relatives.
- Uncharacteristic nervousness or anxiety when visiting the office or conducting telephonic transactions
- Lacking knowledge about his or her financial status.
- Having difficulty speaking directly with the client or customer without interference by others.
- Unexplained or unusual excitement about an unexplained or unusual windfall: reluctance to discuss details.
- Sudden changes to financial documents such as powers of attorney, account beneficiaries, wills or trusts.
- Large, atypical withdrawals or closing of accounts without regard to penalties.

Don't wait to develop policies and procedures to address the issues and events associated with elder financial exploitation. Given the often urgent nature of the problems arising from exploitation, having these procedures in place could significantly help to protect your clients.



## A TRUSTED CONTACT MAY HELP YOU HELP YOUR CLIENT

NASAA, the SEC, and FINRA have recently implemented a new campaign to help encourage retail investors to provide their financial professionals with the name of a trusted contact person. While [FINRA rule 4512](#) requires broker dealer firms to ask clients to identify a trusted contact, no such requirement currently exists for state registered investment advisory firms. However, state IAs would be well served to ask for this information which could facilitate communications with or about a client.



A trusted contact form authorizes the firm to contact a person trusted by the client to disclose information under limited circumstances. It's important for clients and their advisers to understand that a trusted contact:

- Is not authorized to make trades in the investor's account.
- Can't unilaterally make decisions about the investor's account; and
- Does not become a power of attorney, legal guardian, trustee or executor by virtue of being identified as a trusted contact.

It is not uncommon for investment advisers to have relationships with clients that span generations and provide a

## TRUSTED CONTACT CONTINUED...

comprehensive view into the clients' financial lives. An investment adviser may be the first to observe that clients aren't acting like themselves financially or notice unusual or suspicious withdrawals from client accounts. Having a trusted contact in place can help advisers reach out to someone previously identified by the client.

There are various situations where a trusted contact could be helpful. Perhaps clients are traveling and cannot be reached. Or more serious circumstances – if a client is having a health issue or the adviser has concerns about potential fraud in the account. A trusted contact is ideally an extra layer of protection on a client's account and can put a financial firm in a better position to act in a client's best interests.

For these reasons and more, the Division suggests having a conversation with clients about selecting a trusted contact person. For more information, visit [NASAA's website](#) on establishing a trusted contact.

## NEW YORK ADOPTS INVESTMENT ADVISER REPRESENTATIVE REGISTRATION AND EXAM REQUIREMENTS

On February 1, 2021, new regulations took effect requiring individuals associated with New York registered investment advisers and certain SEC registered advisers to register and to meet examination requirements (or qualify for exemptions). Prior to the new regulations taking effect, New York was the only state that did not require the registration of IARs.

If your firm is registered or notice filed in New York, you should review your advisory business and

consider whether New York requires registration of your investment adviser representatives under the new regulations. More information can be found here: <https://ag.ny.gov/investor-protection/investment-advisers>. Also, New York issued the following guidance: <https://ag.ny.gov/sites/default/files/part11-iar-registration-guidance.pdf>

## CONTINUING EDUCATION ON THE HORIZON FOR INVESTMENT ADVISER REPRESENTATIVES

Wisconsin is currently on track to adopt new continuing education requirements for investment adviser representatives (IARs). The proposed rules in Wisconsin will create DFI-Sec 11 of the administrative code, specifically relating to the new continuing education (CE) requirements for IARs. The scope statement for the new rules was approved by Governor Evers on February 19, 2021, and published in Administrative Register No. 783A1 on March 1, 2021. The current legislative materials, including the proposed rule text, can be found on the [Wisconsin State Legislature website](#).

The proposed rules were approved by the Governor on October 7th to be submitted to the legislature. If the rules are adopted prior to the end of this year, the anticipated effectiveness date is January 1, 2022. If adopted in 2022, compliance with the rules will begin in January 2023 (so there is always a full calendar year for compliance).

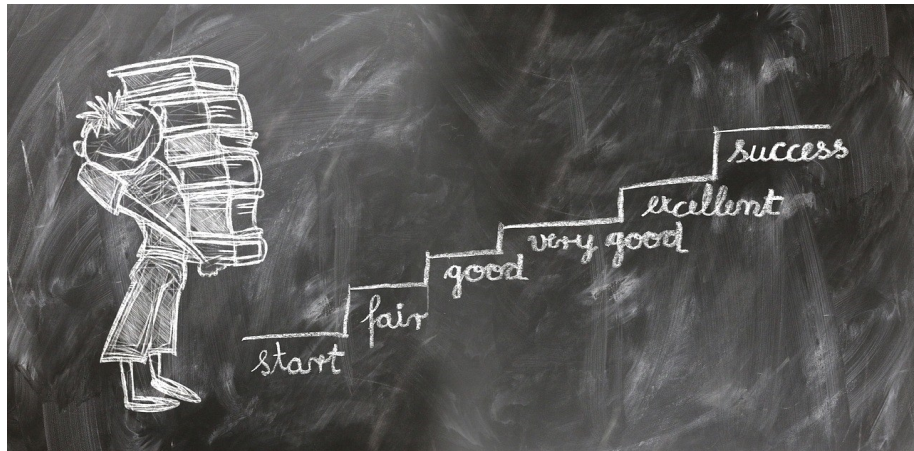
Consistent with the NASAA CE model rule (as referenced in last Spring's newsletter), Wisconsin's proposed CE rules require a total of 12 credits per year, including 6 credits received from courses about products and practices, and 6 credits for courses covering ethics and professional responsibility. The Products and Practices component is designed to ensure ongoing knowledge and competency related to investment products, strategies, standards, and compliance practices relevant to the investment advisory industry. The Ethics and Professional Responsibility component will provide knowledge and competency related to an IAR's duties and obligations to his or her clients including but not limited to the fiduciary duty owed to clients.

*“IARs are free to select approved courses that appeal to their interests”*

Since this is a national program, and many IARs are registered in multiple states, credits will be reported to and tracked by FINRA as NASAA's CE reporting database. This will enable Wisconsin and the securities regulators of other states, as well as the IARs themselves, to easily monitor CE compliance.

## CONTINUING EDUCATION CONTINUED...

IARs who are dually registered as broker-dealer agents who complete their FINRA regulatory element CE may receive credit for the Products and Practices component and then will be in compliance with the IAR CE program by obtaining 6 credits of Ethics and Professional Responsibility. IARs with professional designations are expected to use credits from courses taken to maintain their professional designations to also meet the IAR CE requirements, so long as the course is approved for purposes of IAR continuing education.



Anyone, including investment advisers, can offer and provide continuing education for IARs so long as they are approved as a CE provider and the course is approved for the CE program. IARs are free to select approved courses that appeal to their interests. The CE providers will report the CE credits and roster of all IARs who completed a course to the CE reporting database.

Prometric serves as the course management vendor for the IAR CE program and is currently accepting applications from CE providers. A [Program Handbook](#) was developed and recently updated to help potential providers understand and meet the requirements for acceptable IAR CE course material. The [NASAA website](#) has additional information including course provider application materials, a list of approved CE providers, and FAQs regarding the CE program. If you are interested in becoming a CE provider, please explore the information

## CONTINUING EDUCATION CONTINUED...

and materials on the website.

Please also feel free to direct any questions regarding the future IAR continuing education program to Deb Fabritz at [deborah.fabritz@dfi.wisconsin.gov](mailto:deborah.fabritz@dfi.wisconsin.gov)

## MICHAEL SHILLIN ENFORCEMENT UPDATE

In an update to the Enforcement News article in the Division's [2021 Spring Newsletter](#) regarding Michael Shillin, the Securities and Exchange Commission (SEC) filed a civil action on September 23, 2021, charging Shillin with defrauding at least 100 investment advisory clients.

The [SEC complaint](#) alleges Shillin 1) misrepresented to certain clients that they had successfully subscribed for IPO or pre-IPO shares in high-profile companies when they had not, and lied to clients about the true value of their investment portfolios; 2) provided certain clients with fabricated account statements; 3) encouraged several advisory clients to roll over their existing life insurance policies into new policies that were non-existent or had fewer benefits than Shillin claimed, and 4) received hundreds of thousands of dollars in ill-gotten gains (commissions and advisory fees) as a result of his fraudulent conduct.

The SEC is seeking injunctive relief, disgorgement with prejudgment interest, a civil penalty, and a bar against Shillin serving as an officer or director of a public company. The entire complaint can be reviewed [here](#). Shillin was previously barred by the WI Division of Securities from future registration.



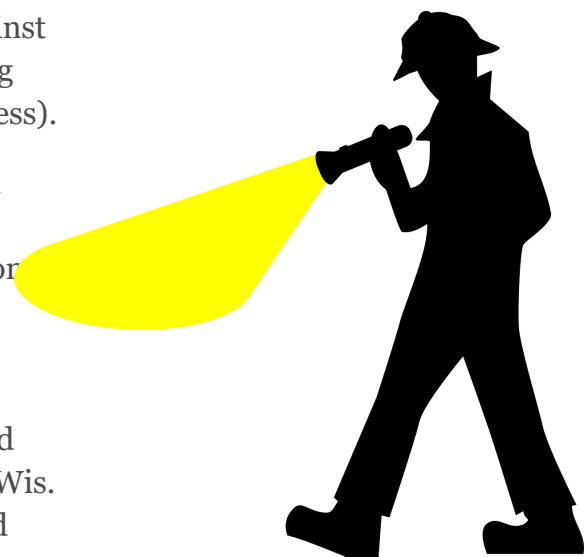
## ENFORCEMENT NEWS

The Wisconsin Division of Securities is responsible for administering and enforcing the state's securities laws. To read our latest enforcement actions, please visit our [website](#). Below are some highlights from recent enforcement orders:

On September 1, 2021, DFI issued a Summary Order to Cease and Desist and Imposing Restitution and Civil Penalties against **Randy L. Mayer** (DFI Case No. S-242139 (EX)). The Order found that Mayer transacted business as an unregistered investment adviser in violation of Wis. Stat. § 551.403(1); Mayer employed a device, scheme, or artifice to defraud, and engaged in an act, practice, or course of business that operates or would operate as a fraud or deceit upon a Wisconsin investor in violation of Wis. Stat. § 551.502 by using a Wisconsin investor's money in a manner contrary to what Mayer had represented, and for Mayer's personal benefit; failing to disclose his prior criminal history of dishonesty; and providing a Wisconsin investor with ongoing fake investment account statements.

On August 31, 2021, DFI issued a Summary Order to Cease and Desist against **Matthew J. Wetzel** (DFI Case No. S-242295 (EX)). The Order found that Wetzel violated Wis. Stat. § 551.301 when he offered securities which were not registered or exempted from registration under Ch. 551, and omitted material facts, including but not limited to the numerous judgments, lawsuits, and tax warrants against him and his business, Laughing Grass (a purported CBD business).

On July 28, 2021, DFI issued a Summary Order to Cease and Desist and Imposing Restitution and Civil Penalties against **Charles Winn, LLC and Charlie Jake Smith** (DFI S-242235 (EX)). The Order found that Winn and Smith violated Wis. Stat. 551.301 when they offered and sold securities in Wisconsin





## ENFORCEMENT NEWS CONTINUED...

which were not registered or exempted from registration under Ch. 551; Winn and Smith violated Wis. Stat. 551.403 when they transacted business in Wisconsin as an investment adviser without being registered or exempted from registration; Winn and Smith violated Wis. Stat. 551.501(2) when they omitted to state a material fact necessary in order to make statements made, in light of the circumstances under which they were made, not misleading, including but not limited to the regulatory orders issued against Winn in Texas, Washington, Illinois, and Michigan for their unlawful conduct in offering and selling securities; and when they made misrepresentations in connection with the offer and sale of a security, including but not limited to the misstatement that they were established in 2006.

On July 14, 2021, DFI issued a Summary Order to Cease and Desist against **Ronald R. Shepard** (DFI Case No. S-243881 (EX)). The Order found that Shepard violated Wis. Stat. § 551.301(1) when he offered securities which were not registered or exempted from registration under Ch. 551, and that Shepard violated Wis. Stat. § 551.501(2) when he offered securities while omitting material facts, including but not limited to his previous felony convictions for fraud and theft.

On June 15, 2021, DFI issued a Summary Order to Cease and Desist and Imposing Restitution and Civil Penalties against **BoomFX Trades.Online and Alfred Brent**. The Order found that BoomFX and Brent violated Wis. Stat. § 551.401(1) when they transacted business in Wisconsin as a broker-dealer without being registered under Ch. 551 or exempted from registration under Wis. Stat. § 551.401(2); BoomFX and Brent violated Wis. Stat. § 551.301(1) when they offered securities that were not registered or exempted from registration under Ch. 551; and that Brent violated Wis. Stat. § 551.501(2) when he made an untrue statement of a material fact by telling an investor that he was licensed as a Customs Broker License with the Financial Services Commission of Mauritius, when in fact no such license or registration exists with that agency.

On June 11, 2021, DFI entered into a Final Order by Consent to Cease & Desist was issued against **John M. Stevens & Service Financial, LLC** (DFI Case No. S-240800 (EX)). The Order found that Stevens and Service Financial violated Wis. Stat. § 551.402(1) when they transacted business in



## More Ways to Connect with DFI

The Wisconsin Department of Financial Institutions (DFI) Facebook page provides information on DFI activities, financial literacy, investor education, scam warnings, and other timely news to help protect investors.

Please check out DFI's [Facebook](#) page and share any content that you find useful. Feel free to "like" our page so that you receive future posts in your Facebook newsfeed.

In addition, to keep up with the latest from DFI, follow us on [Twitter](#) and [LinkedIn](#).

## ENFORCEMENT NEWS CONTINUED...

Wisconsin as an investment adviser without being registered or exempted from registration under Ch. 551; they violated Wis. Stat. § 551.402(4) when they associated with or employed an unregistered person to solicit clients; they violated numerous provisions of Wis. Stat. §§ 551.501 and 551.502 when they employed a device, scheme, or artifice to defraud an investor, including but not limited to holding themselves out as being registered investment advisers when they were not registered, sending false and deceptive account statements to induce the liquidation of pre-existing securities to invest the proceeds with Stevens and Service Financial, and failing to disclose the numerous civil suits, judgments, and foreclosures against Stevens.

On May 26, 2021, DFI issued a Consent Order to Cease and Desist against **John L. Adkins** (DFI Case No. S-243667 (EX)). The Consent Order found that Adkins violated Wis. Stat. § 551.301(1) when he offered securities which were not federally covered, registered, or exempted from registration in Wisconsin; that Adkins violated Wis. Stat. § 551.402 when he transacted business as an agent in Wisconsin without being registered or exempted from registration under Ch. 551; and that Adkins violated Wis. Stat. § 551.501(3) when he engaged in an act, practice, or course of business that operates or would operate as a fraud or deceit upon another person by directing a Wisconsin resident to utilize a VPN to illegally invest in EndoTech.

