

NOTICE TO SUBMIT COMMENTS: *Anyone may file a statement in support of or in opposition to this proposed amendment with the Department of Insurance, Financial Institutions and Professional Registration, Attention: Tamara W. Kopp, Receivership Counsel, Director's Office, PO Box 690, Jefferson City, MO 65102. To be considered, comments must be received within thirty (30) days after publication of this notice in the Missouri Register. No public hearing is scheduled.*

**Title 20—DEPARTMENT OF INSURANCE,
FINANCIAL INSTITUTIONS AND PROFESSIONAL
REGISTRATION
Division 700—Insurance Licensing
Chapter 1—Insurance Producers**

PROPOSED AMENDMENT

20 CSR 700-1.147 Reasonable Supervision in Variable Life [and Variable Annuity] Sales. The department is amending the title, purpose, and sections (1) and (3).

PURPOSE: *This amendment makes this rule only applicable to the offer, sale, or exchange of variable life products. This rule implements the requirements of sections 375.141.1(8) and 375.143, RSMo, with respect to the demonstration of incompetence, untrustworthiness, or financial irresponsibility by producers in the offer, sale, or exchange of variable life products. The department is amending this rule by removing all language that relates to annuity recommendations. The department's proposed rule, 20 CSR 400-5.900 Suitability in Annuity Transactions, is replacing the language contained in this rule.*

PURPOSE: *This rule [implements the requirements] effectuates and aids in the interpretation of section[s] 375.141.1(8) [and 375.143], RSMo, with respect to the demonstration of incompetence, untrustworthiness, or financial irresponsibility by producers in the offer, sale, or exchange of variable life [and variable annuity] products.*

(1) Grounds for the discipline or disqualification of producers shall include, in addition to other grounds specified in section 375.141, RSMo, failure to comply with or violation of the following professional standards of conduct:

(A) Individual Producers. Each individual producer licensed to sell variable life [and variable annuity] products shall be supervised by a member of the Financial Industry Regulatory Authority (FINRA), which member shall also be licensed as a business entity producer with the director (supervising member)./;

(B) Supervising Members.

1. Supervisory system.

A. Each supervising member shall establish and maintain a system to supervise the activities of each individual producer that is reasonably designed to achieve compliance with applicable state insurance laws and regulations, federal securities laws and regulations, and with applicable FINRA rules. Final responsibility for proper supervision shall rest with the supervising member. A supervising member's supervisory system shall provide, at a minimum, for the following:

(I) The establishment and maintenance of written procedures as required by paragraphs (1)(B)2. and 3. of this rule;

(II) The designation, where applicable, of an appropriately qualified and registered FINRA principal(s) with authority to carry out the supervisory responsibilities of the supervising member for variable life [and variable annuity products] producers;

(III) The designation of an office of supervisory jurisdiction (OSJ) of each location that meets the definition contained in FINRA Rule [3010(g)(2), effective January 31, 2005] 3110(f),

effective July 31, 2015. The supervising member shall also designate such other OSJs as it determines to be necessary in order to supervise its producers and employees in accordance with the standards set forth in this rule, taking into consideration the following factors:

(a) Whether the individual producers or employees engage in retail sales or other activities involving regular conduct with public customers;

(b) Whether a substantial number of individual producers conduct sales activities at, or are otherwise supervised from, such location;

(c) Whether the location is geographically distant from another OSJ of the supervising member;

(d) Whether the individual producers are geographically dispersed; and

(e) Whether the investment or insurance activities at such location are diverse and/or complex;

(IV) The designation of one (1) or more appropriately qualified and registered FINRA principal(s) in each OSJ, including the main office, and one (1) or more appropriately FINRA qualified and licensed producers in each non-OSJ branch office (as defined in FINRA Rule [3010(g)(1), effective January 31, 2005] 3110(f), effective July 31, 2015) with authority to carry out the supervisory responsibilities assigned to that office by the supervising member;

(V) The assignment of each individual producer to an appropriately FINRA qualified and licensed producer who shall be responsible for supervising that person's activities;

(VI) Reasonable efforts to determine that all supervisory personnel are qualified by virtue of experience or training to carry out their assigned responsibilities;

(VII) The participation of each producer, either individually or collectively, no less than annually, in an interview or meeting conducted by persons designated by the supervising member at which compliance matters relevant to the activities of the individual producer(s) are discussed. Such interview or meeting may occur in conjunction with the discussion of other matters and may be conducted at a central or regional location or at the individual producer's place of business.

2. Written procedures.

A. Each supervising member shall establish, maintain, and enforce written procedures to supervise the variable life [and variable annuity] business in which it engages and to supervise the activities of individual producers that are reasonably designed to achieve compliance with applicable state insurance laws and regulations, federal securities laws and regulations, and with applicable FINRA rules.

B. The supervising member's written supervisory procedures shall set forth the supervisory system established by the supervising member pursuant to subparagraph (1)(B)1.A. above, and shall include the titles, registration/licensure status and locations of the required supervisory personnel and the responsibilities of each supervisory person as these relate to the types of business engaged in, applicable insurance laws and regulations, applicable federal securities laws and regulations, and applicable FINRA rules. The supervising member shall maintain on an internal record the names of all persons who are designated as supervisory personnel and the dates for which such designation is or was effective. Such record shall be preserved by the supervising member for a period of not less than three (3) years, the first two (2) years in an easily accessible place.

C. A copy of a supervising member's written supervisory procedures, or the relevant portions thereof, shall be kept and maintained in each OSJ and at each location where supervisory activities are conducted on behalf of the supervising member. Each supervising member shall amend its written supervisory procedures as appropriate within a reasonable time after changes occur in applicable state insurance laws and regulations, applicable federal securities laws and regulations, and applicable FINRA rules, and as changes

occur in its supervisory system, and each supervising member shall be responsible for communicating amendments to the individual producers it supervises.

3. Internal inspections.

A. Each supervising member shall conduct a review, at least annually, of the businesses in which it engages, which review shall be reasonably designed to assist in detecting and preventing violations of, and achieving compliance with, applicable state insurance laws, applicable federal securities laws and regulations, and with applicable FINRA rules. Each supervising member shall review the activities of each office, which shall include the periodic examination of customer accounts, to detect and prevent irregularities or abuses.

(I) Each supervising member shall inspect at least annually every office of supervisory jurisdiction and any branch office that supervises one (1) or more non-branch locations.

(II) Each supervising member shall inspect at least every three (3) years every branch office that does not supervise one (1) or more non-branch locations. In establishing how often to inspect each non-supervisory branch office, the firm shall consider whether the nature and complexity of the variable life *[and variable annuity]* sales activities for which the location is responsible, the volume of business done, and the number of individual producers assigned to the location require the non-supervisory branch office to be inspected more frequently than every three (3) years. If a supervising member establishes a more frequent inspection cycle, the supervising member must ensure that at least every three (3) years, the inspection requirements enumerated in subparagraph (1)(B)3.B. have been met. The non-supervisory branch office examination cycle, an explanation of the factors the supervising member used in determining the frequency of the examinations in the cycle, and the manner in which a supervising member will comply with subparagraph (1)(B)3.B. if using more frequent inspections than every three (3) years, shall be set forth in the supervising member's written supervisory and inspection procedures.

(III) Each supervising member shall inspect on a regular periodic schedule every non-branch location. In establishing such schedule, the firm shall consider the nature and complexity of the variable life *[and variable annuities]* activities for which the location is responsible and the nature and extent of contact with customers. The schedule and an explanation regarding how the supervising member determined the frequency of the examination schedule shall be set forth in the supervising member's written supervisory and inspection procedures.

(IV) Each supervising member shall retain a written record of the dates upon which each review and inspection is conducted.

B. An office inspection and review by a supervising member pursuant to subparagraph (1)(B)3.A. must be reduced to a written report and kept on file by the supervising member for a minimum of three (3) years, unless the inspection is being conducted pursuant to part (1)(B)3.A.(III) and the regular periodic schedule is longer than a three- (3-)/-/ year cycle, in which case the report must be kept on file at least until the next inspection report has been written. The written inspection report must also include, without limitation, the testing and verification of the supervising member's policies and procedures, including supervisory policies and procedures in the following areas:

- (I) Safeguarding of customer funds *[and annuities]*;
- (II) Maintaining of books and records;
- (III) Supervision of customer accounts serviced by branch office managers;
- (IV) Transmittal of funds between customers and individual producers;
- (V) Validation of customer address changes; and
- (VI) Validation of changes in customer account information.

If a supervising member does not engage in all of the activities enumerated above, the supervising member must identify those activities

in which it does not engage in the written inspection report and document in the report that supervisory policies and procedures for such activities must be in place before the supervising member can engage in them.

C. An office inspection by a supervising member pursuant to subparagraph (1)(B)3.A. may not be conducted by the branch office manager or any person within that office who has supervisory responsibilities or by any individual who is supervised by such person(s). However, if a supervising member is so limited in size and resources that it cannot comply with this limitation (e.g., a supervising member with only one (1) office or a supervising member has a business model where small or single-person offices report directly to an office of supervisory jurisdiction manager who is also considered the office's branch office manager), the supervising member may have a principal who has the requisite knowledge to conduct an office inspection perform the inspections. The supervising member, however, must document in the office inspection reports the factors it has relied upon in determining that it is so limited in size and resources that it has no other alternative than to comply in this manner. A supervising member must have in place procedures that are reasonably designed to provide heightened office inspections if the person conducting the inspection reports to the branch office manager's supervisor or works in an office supervised by the branch manager's supervisor and the branch office manager generates twenty percent (20%) or more of the revenue of the business units supervised by the branch office manager's supervisor. For the purposes of this paragraph only, the term "heightened inspection" shall mean those inspection procedures that are designed to avoid conflicts of interest that serve to undermine complete and effective inspection because of the economic, commercial, or financial interests that the branch manager's supervisor holds in the associated persons and businesses being inspected. In addition, for the purpose of this paragraph only, when calculating the twenty percent (20%) threshold, all of the revenue generated by or credited to the branch office or branch office manager shall be attributed as revenue generated by the business units supervised by the branch office manager's supervisor irrespective of a supervising member's internal allocation of such revenue. A supervising member must calculate the twenty percent (20%) threshold on a rolling, twelve- (12-)/-/ month basis.

4. Review of transactions and correspondence.

A. Supervision of individual producers. Each supervising member shall establish procedures for the review and endorsement by a FINRA qualified principal in writing, on an internal record, of all transactions and for the review by a registered principal of incoming and outgoing written and electronic correspondence of its individual producers with the public relating to the variable life *[or variable annuities]* business of such supervising member. Such procedures should be in writing and be designed to reasonably supervise each individual producer. Evidence that these supervisory procedures have been implemented and carried out must be maintained and made available to the director upon request.

B. Review of correspondence. Each supervising member shall develop written procedures that are appropriate to its business, size, structure, and customers for the review of incoming and outgoing written (i.e., non-electronic) and electronic correspondence with the public relating to its variable life *[or variable annuities]* business, including procedures to review incoming, written correspondence directed to individual producers and related to the supervising member's variable life *[or variable annuities]* business to properly identify and handle customer complaints and to ensure that customer funds and variable life *[and variable annuities]* business are handled in accordance with supervising member's procedures. Where such procedures for the review of correspondence do not require review of all correspondence prior to use or distribution, they must include provision for the education and training of associated persons as to the supervising member's procedures governing correspondence, documentation of such education and training, and surveillance and follow-up to ensure that such procedures are implemented

and adhered to.

C. Each supervising member shall retain correspondence of producers relating to its variable life *[and variable annuity]* business in accordance with Rules 17a-3 and 17a-4 under the Securities and Exchange Act of 1934. The names of the persons who prepared outgoing correspondence and who reviewed the correspondence shall be ascertainable from the retained records and the retained records shall be readily available to the director, upon request.

5. Qualifications investigated.

A. Each supervising member shall have the responsibility and duty to ascertain by investigation the good character, business repute, qualifications, and experience of any individual producer prior to assisting in the application of such person for a variable life *[or variable annuity]* line with the department.

B. Where an applicant for license has previously been licensed with the department, the supervising member shall review a copy of the Uniform Termination Notice of Securities Industry Registration (Form U-5) filed with the FINRA by such person's most recent previous FINRA member employer, together with any amendments thereto that may have been filed pursuant to Article V, Section 3 of the FINRA's By-Laws. The supervising member shall review the Form U-5 as required by this rule no later than sixty (60) days following the filing of the application for license or demonstrate to the department that it has made reasonable efforts to comply with the requirement. In conducting its review of the Form U-5 and any amendments thereto, a supervising member shall take such action as may be deemed appropriate.

6. Supervisory control system.

A. General requirements.

(I) Each supervising member shall designate and specifically identify one (1) or more principals who shall establish, maintain, and enforce a system of supervisory control policies and procedures that:—

(a) Test and verify that the supervising member's supervisory procedures are reasonably designed with respect to its activities and the activities of its employees, to achieve compliance with applicable state insurance laws and regulations, applicable federal securities laws and regulations, and with applicable FINRA rules; and

(b) Create additional or amend supervisory procedures where the need is identified by such testing and verification.

(II) The designated principal or principals must submit to the supervising member's senior management no less than annually, a report detailing each supervising member's system of supervisory controls, the summary of the test results and significant identified exceptions, and any additional or amended supervisory procedures created in response to the test results.

(III) The establishment, maintenance, and enforcement of written supervisory control policies and procedures pursuant to part (1)(B)6.A.(I) shall include:

(a) Procedures that are reasonably designed to review and supervise the customer account activity conducted by the supervising member's branch office managers, sales managers, regional or district sales managers, or any person performing a similar supervisory function.

I. A person who is either senior to, or otherwise independent of, the producing manager must perform such supervisory reviews. For purposes of this rule, an "otherwise independent" person: may not report either directly or indirectly to the producing manager under review; must be situated in an office other than the office of the producing manager; must not otherwise have supervisory responsibility over the activity being reviewed (including not being directly compensated based in whole or in part on the revenues accruing for those activities); and must alternate such review responsibility with another qualified person every two (2) years or less.

II. If a supervising member is so limited in size and resources that there is no qualified person senior to, or otherwise independent of, the producing manager to conduct the reviews pur-

suant to item (1)(B)6.A.(II)(a)I. above (e.g., a supervising member has only one (1) office or an insufficient number of qualified personnel who can conduct reviews on a two- (2-)/- year rotation), the reviews may be conducted by a principal who is sufficiently knowledgeable of the supervising member's supervisory control procedures, provided that the reviews are in compliance with item (1)(B)6.A.(II)(a)I. to the extent practicable.

III. A supervising member relying on item (1)(B)6.A.(II)(a)II. above must document in its supervisory control procedures the factors used to determine that complete compliance with all of the provisions of item (1)(B)6.A.(II)(a)I. is not possible and that the required supervisory systems and procedures in place with respect to any producing manager comply with the provisions of item (1)(B)6.A.(II)(a)I. above to the extent practicable./;;

(b) Procedures that are reasonably designed to review and monitor the following activities:

I. All transmittals of funds (e.g., wires or checks, etc.) from customers to third party accounts (i.e., a transmittal that would result in a change of beneficial ownership); from customer accounts to outside entities (e.g., banks, investment companies, etc.); from customer accounts to locations other than a customer's primary residence (e.g., post office box, "in care of" accounts, alternate address, etc.); and between customers and registered representatives, including the hand-delivery of checks;

II. Customer changes of address and the validation of such changes of address; and

III. Customer changes of investment objectives and the validation of such changes of investment objectives./;;

(c) The policies and procedures established pursuant to subpart (1)(B)6.A.(II)(b) must include a means or method of customer confirmation, notification, or follow-up that can be documented. If a supervising member does not engage in all of the activities enumerated above, the supervising member must identify those activities in which it does not engage in its written supervisory control policies and procedures and document in those policies and procedures that additional supervisory policies and procedures for such activities must be in place before the supervising member can engage in them; and

(d) Procedures that are reasonably designed to provide heightened supervision over the activities of each producing manager who is responsible for generating twenty percent (20%) or more of the revenue of the business units supervised by the producing manager's supervisor. For the purposes of this part only, the term "heightened supervision" shall mean those supervisory procedures that evidence supervisory activities that are designed to avoid conflicts of interest that serve to undermine complete and effective supervision because of the economic, commercial, or financial interests that the supervisor holds in the associated persons and businesses being supervised. In addition, for the purpose of this part only, when calculating the twenty percent (20%) threshold, all of the revenue generated by or credited to the producing manager or the producing manager's office shall be attributed as revenue generated by the business units supervised by the producing manager's supervisor irrespective of a supervising member's internal allocation of such revenue. A supervising member must calculate the twenty percent (20%) threshold on a rolling, twelve- (12-)/- month basis.

(3) Interpretation of this rule shall be guided by judicial and administrative opinions and decisions construing substantially similar requirements of the FINRA or its predecessor or successor organizations. Any person in compliance with substantially similar requirements of the FINRA shall be deemed to be in compliance with the provisions of this rule.

AUTHORITY: [sections 374.040, 374.045, and 375.013, RSMo 2000 and sections 375.143 and 376.309.6, RSMo Supp. 2007] sections 374.045, 375.141, and 375.143, RSMo Supp. 2013, and section 375.013, RSMo 2000. Original rule filed

July 5, 2005, effective Jan. 30, 2006. Amended: Filed Nov. 30, 2007, effective July 30, 2008. Amended: Filed Sept. 30, 2016.

PUBLIC COST: *The proposed amendment will not cost state agencies or political subdivisions more than five hundred dollars (\$500) in the aggregate.*

PRIVATE COST: *The proposed amendment will not cost private entities more than five hundred dollars (\$500) in the aggregate.*

NOTICE TO SUBMIT COMMENTS: *Anyone may file a statement in support of or in opposition to this proposed amendment with the Department of Insurance, Financial Institutions and Professional Registration, Attention: Tamara W. Kopp, Receivership Counsel, Director's Office, PO Box 690, Jefferson City, MO 65102. To be considered, comments must be received within thirty (30) days after publication of this notice in the Missouri Register. No public hearing is scheduled.*

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Chapter 1—Insurance Producers**

PROPOSED RESCISSION

20 CSR 700-1.148 Reasonable Supervision in Indexed and Fixed Annuity Sales. This rule aided in the interpretation of section 375.141.1(8), RSMo, with respect to the demonstration of incompetence, untrustworthiness, or financial irresponsibility by producers in the offer, sale, or exchange of indexed or fixed annuity products.

PURPOSE: *This rule is being rescinded because proposed rule 20 CSR 400-5.900 Suitability in Annuity Transactions, is replacing the language contained in this rule.*

AUTHORITY: *section 374.045, RSMo 2000 and sections 375.141 and 375.143, RSMo Supp. 2007. Original rule filed April 30, 2008, effective Dec. 30, 2008. Rescinded: Filed Sept. 30, 2016.*

PUBLIC COST: *The proposed rescission will not cost state agencies or political subdivisions more than five hundred dollars (\$500) in the aggregate.*

PRIVATE COST: *The proposed rescission will not cost private entities more than five hundred dollars (\$500) in the aggregate.*

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