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Colorado Department of Regulatory Agencies
Office of Policy and Research

Money Order Act



October 15, 2003

STATE OF COLORADO

DEPARTMENT OF REGULATORY AGENCIES

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Bill Owens
Governor

October 15, 2003

Members of the Colorado General Assembly
c/o the Office of Legislative Legal Services
State Capitol Building
Denver, Colorado 80203

Dear Members of the General Assembly:

The Colorado Department of Regulatory Agencies has completed its evaluation of the Colorado Money Order Act. I am pleased to submit this written report, which will be the basis for my office's oral testimony before the 2004 legislative committee of reference. The report is submitted pursuant to section 24-34-104(9)(b), of the Colorado Revised Statutes (C.R.S.), which states in part:

The department of regulatory agencies shall conduct an analysis of the performance of each division, board or agency or each function scheduled for termination under this section...

The department of regulatory agencies shall submit a report and supporting materials to the office of legislative legal services no later than October 15 of the year preceding the date established for termination....

The report discusses the question of whether there is a need for the regulation provided under Article 52 of Title 12, C.R.S. The report also discusses the effectiveness of the Division of Banking in carrying out the intent of the legislation and makes recommendations for statutory changes in the event this regulatory program is continued by the General Assembly.

Sincerely,

A handwritten signature in black ink that reads "Richard F. O'Donnell".

Richard F. O'Donnell
Executive Director

2003 Sunset Review Colorado Money Order Act

Department of Regulatory
Agencies

Bill Owens
Governor

Richard F. O'Donnell
Executive Director



EXECUTIVE SUMMARY

Quick Facts

What is Regulated? Money transmission companies.

Who is Regulated?

- 30 Money transmission companies.

How is it Regulated? The Banking Board is statutorily empowered to grant or deny licenses for money transmitter applicants and to fix the required bond or securities amount between \$250,000 and \$2,000,000. It is likewise authorized to approve a licensee's request to cover outstanding payment instruments with a combination of surety bond and permissible investments, and it is vested with the statutory authority to determine the suitability of collateral other than permissible investments.

The Commissioner of Banking is responsible for the administration of the program, including examination and enforcement functions. The Commissioner is also empowered to require licensees to post additional collateral in the form of permissible investments pursuant to rules promulgated by the Banking Board.

What Does it Cost? The FY 2001-02 budget to oversee this program was \$177,803. In fiscal year 01-02 there were 2.25 FTE associated with the regulation of money transmitter companies.

What Disciplinary Activity is There? During the period FY 98/99 to FY 02/03, the Division's enforcement actions consisted of 3 Memorandums of Understanding.

Where Do I Get the Full Report? The full sunset review can be found on the internet at:
www.dora.state.co.us/opr/2003MoneyOrderAct.pdf

Key Recommendations

Continue the Money Order Act until 2013

Changes in population coupled with technological advances have contributed to strong growth in Colorado's money transmission industry. The existing regulatory scheme works to benefit Colorado consumers without being unduly burdensome to the industry. Consequently, the Money Order Act should be continued until 2013.

Eliminate the mandatory examination of licensees

The regulatory cost of examinations to both licensees and the Division of Banking itself is not justified in light of existing federal and state safeguards. More specifically, initial licensing requirements, subsequent information reporting requirements, and the surety bond licensees must post have to date proved to be adequate public protection mechanisms. Regulatory costs must also be weighed against any potential harm to consumers. For the five-year period ending December 2002, the Division received a total of eight complaints from consumers and took three enforcement actions. Consequently, the regulatory burden associated with examinations appears to be excessive in light of the potential risk to consumers.

Require licensees to post at each of their outlets public notices regarding the complaint procedures of the Division of Banking

While licensee complaint files indicate that the vast majority of issues are addressed at the institutional level, it must be recognized that for economic, cultural, educational, and linguistic reasons, many consumers would not know, or would be hesitant, to seek assistance from the Division of Banking. Consequently, it would benefit consumers greatly if licensees were required to post in a conspicuous location in their place of business a public notice informing them of their rights together with information as to how to initiate a complaint. Such posting would need to be in English and any foreign language predominantly spoken by customers at the respective locations.

...Key Recommendations Continued

Extend the time from 30 to 90 days for licensees to obtain new surety bonds

Colorado's surety bond marketplace is such that licensees are precluded from having a sufficient number of suitable providers to meet their needs. By extending the required notice period to 90 days, money transmitter licensees would have sufficient time to ensure that a new surety bond is in force prior to the existing surety company's cancellation of the bond. In addition, the Division of Banking would have extra time to verify that the licensee was able to secure a new bond, which is a requirement for licensure.

Extend the time from 120 to 150 days for licensees to file annual financial statements

Currently, every money transmitter licensee must file an annual financial statement as audited by an independent certified public accountant within 120 days following the close of each licensee's fiscal year. According to Division staff, however, external auditors have difficulty completing their audits in the required 120 days. Therefore, changing the submission date to 150 days would accommodate these professionals, and align submission requirements of money transmitters with that of other regulated financial institutions.

Increase the amount of fines for late filings

In the Division's experience, a \$25 fine does not serve its intended purpose of effectively deterring unsatisfactory reporting practices. The penalty assessment should be increased to \$250.

Require licensees to submit a copy of the engagement letter and management letter issued by an independent auditor

In addition to the submission of financial statements containing a balance sheet, a profit and loss statement, and a statement of retained earnings, each licensee should be required to submit to the Division of Banking copies of both the engagement letter and management letter issued by an independent auditor. This is similar to what is currently required of other regulated financial institutions. Submission of these two documents would enhance oversight by enabling the Division to assess the intended scope of the outside audit (engagement letter), as well as any adverse findings or recommendations by the independent auditor (management letter) following the audit, which would forewarn the Division of potential problems.

Amend the title of the Act from "Money Order Act" to "Money Transmitters Act"

The title "Money Order Act" is misleading because a money order is only one form of a money transmission instrument. It does not include, for example, traveler's checks, or wire transfers. Changing the title to "Money Transmitters Act" would more accurately reflect the content of the statute and the industry it regulates.

Major Contacts Made In Researching the 2003 Sunset Review of the Money Order Act

Non-Bank Funds Transmitters Group
First Data Corporation
Division of Banking Staff

What is a Sunset Review?

A sunset review is a periodic assessment of state boards, programs, and functions to determine whether or not they should be continued by the legislature. Sunset reviews focus on creating the least restrictive form of regulation consistent with the public interest. In formulating recommendations, sunset reviews consider the public's right to consistent, high quality professional or occupational services and the rights of businesses to exist and thrive in a highly competitive market, free from unfair, costly or unnecessary regulation.

Sunset Reviews are Prepared By:
Colorado Department of Regulatory Agencies
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1560 Broadway, Suite 1540 Denver, CO 80202
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Background

The Sunset Process

The Money Order Act, in accordance with section 12-52-117 of the Colorado Revised Statutes (C.R.S.), shall terminate on July 1, 2004 unless continued by the General Assembly. During the year prior to this date, it is the duty of the Department of Regulatory Agencies (DORA) to conduct an analysis and evaluation of this legislation pursuant to section 24-34-104(9)(b), C.R.S.

The purpose of this review is to determine whether the Money Order Act should be continued for the protection of the public and to evaluate the performance of the Banking Board and the State Bank Commissioner. During this review, the entities under review must demonstrate that there is still a need for the licensing of money transmitters, and that the regulation is the least restrictive regulation consistent with the public interest. DORA's findings and recommendations are submitted via this report to the legislative committee of reference of the Colorado General Assembly. Statutory criteria used in sunset reviews may be found in Appendix A.

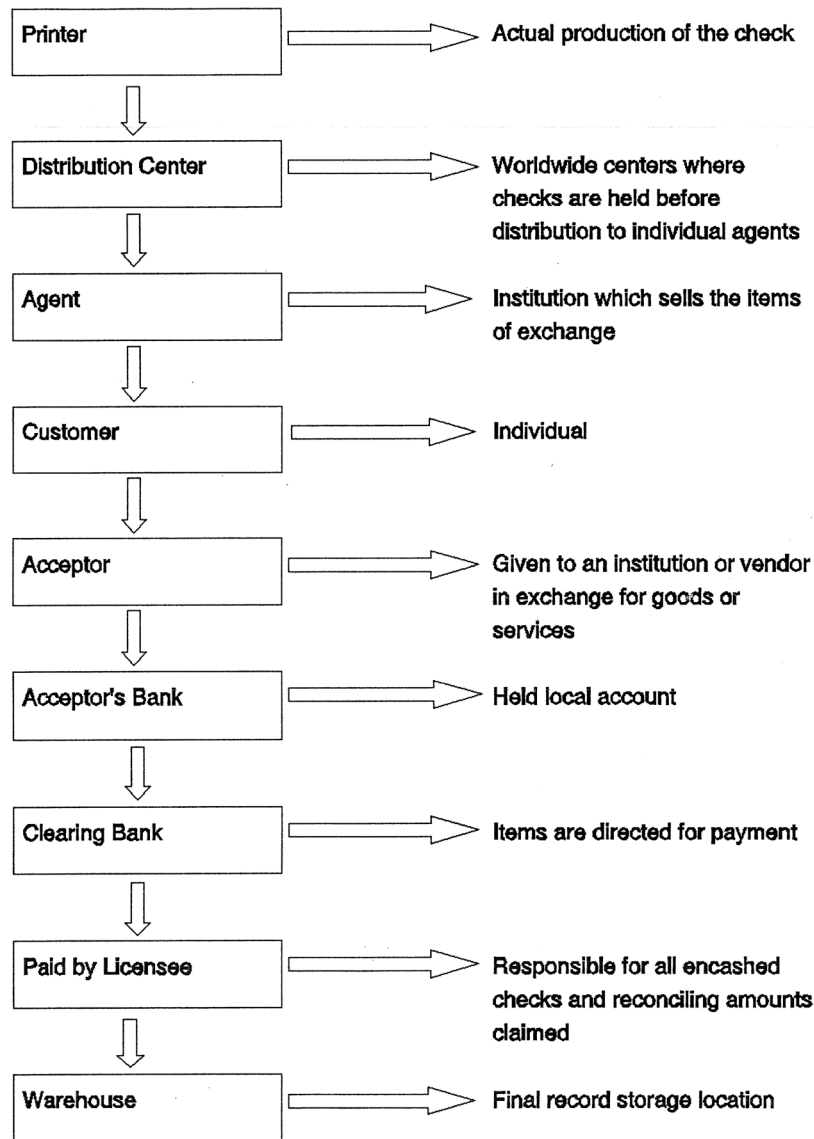
Methodology

As part of this review, we interviewed Division of Banking staff, interviewed stakeholders, reviewed Colorado statutes, and reviewed other state laws.

Profile of the Industry

A money order is a form of credit instrument calling for payment of money to a named payee and involving three parties: remitter, payee, and drawee. It may encompass non-negotiable, or negotiable instruments, and may be issued by a governmental agency, a bank, private person, or other authorized entity. The essential characteristic of a money order is that it is purchased for the purpose of paying a debt, or to transmit funds upon the credit of the issuer of the money order (Money Order Regulation, Sunset Review ,1993). In Colorado, the General Assembly has defined money orders as constituting "exchange" comprised of "any check, draft, money order, or other instrument for the transmission or payment of money or credit" (§ 12-52-103, C.R.S.). A schematic of the likely pathway that one particular type of money transmission instrument follows may be found on the following page (see also Recommendation 9 for an explanation as to why the term "money transmitters" and "money transmission," which covers travelers' checks, is more accurate than "money order companies" and similar derivations).

Life of a Travellers Check



Historically, the sale of money orders and transmission of funds (by entities other than banking organizations) was dominated by a relatively small number of large organizations with global networks. These organizations, such as *Western Union*, *Money Gram*, and *Thomas Cooke* served two primary consumer groups: “cashed-based society”, and “emergency prone households.” In recent years, the cash based or “unbanked” group has grown dramatically as result of demographic changes, increased immigration, and a higher percentage of lower-income wage earners.

Growth in the cash-based market spawned a proliferation of smaller money transmitter companies that serve specific groups and corridors. For example companies that primarily, or exclusively, transmit funds from Washington DC to Vietnam, San Francisco to China, or Denver to Mexico. These companies are generally quite small with lower levels of capital and liquidity, are not as familiar with regulatory requirements, and have less sophisticated transfer and record keeping systems. Many of these entities were small unlicensed family businesses that had essentially operated beneath the regulatory “radar screen.” Recent federal legislation that imposed substantial penalties on unlicensed money services businesses, in conjunction with tips and referrals regarding unlicensed activity, caused many of these entities to seek state licensure (unlike the banking system there is no federal regulatory body).

Internet payment providers also fall under the jurisdiction of many state money transmission statutes. Although these companies had previously argued that licensure was not required due to the lack of physical locations, the threat of penalty under federal anti-money laundering laws has caused several large internet payment providers to come forward and seek licensure. As an example, *PayPal* was licensed by the Division in the first quarter of 2002, and reported Colorado money transmission of more than \$250 million during the last three quarters of calendar 2002.

Increases in the number of institutions, wide range in size, type of activity and sophistication of institutions, in addition to language and cultural barriers, have greatly added to the difficulties of examining, licensing, and supervising money transmitter and money order companies.

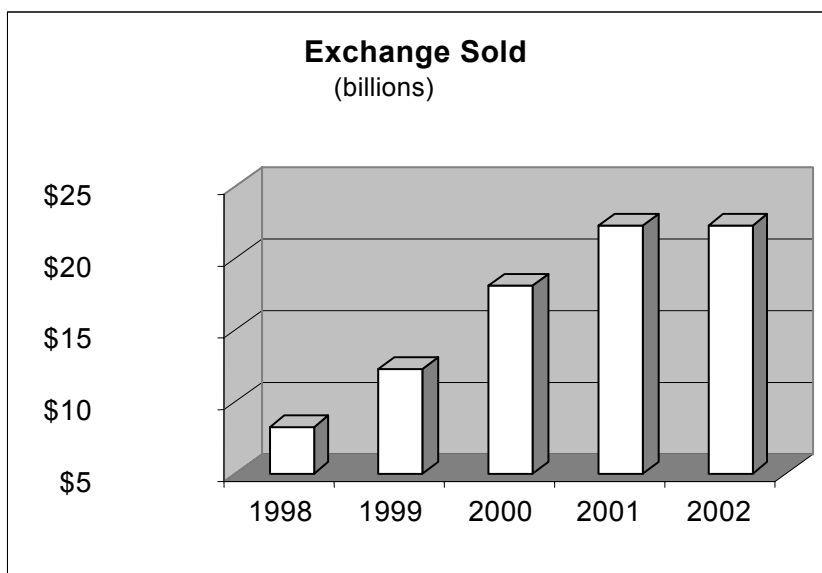
Profile of the Industry in Colorado

Colorado is the headquarters for *Western Union*, one of the largest money transmitters in the country. Colorado may be atypical in that many of its licensees are major corporations with individual assets, which customarily exceed hundreds of millions of dollars. These licensees enter into agreements with in-state agents to issue exchange for them. Agents are typically either directly affiliated with the licensee, or may be supermarkets or other outlets that contract with the licensee to offer the service as a convenience to their customers. While licensees may pay their agents a small percentage of the total amount of exchange issued, agents may also make a profit by increasing the price charged for the issuance of exchange. The fees charged to consumers, however, do not usually exceed more than a few dollars.

In the past, Colorado licensees reported that the main problem which they experience is that agents will sometimes fail to remit proceeds paid to them by consumers for the benefit of the payee, or neglect to remit such proceeds on a timely basis. Nevertheless, licensees realize substantial aggregate profits from the issuance of exchange during the “float,” the interim between the consumer’s payment of cash for the issuance of a payment instrument and the time when the licensee must pay off the instrument. This investment obviously produces a sizeable amount of interest income even if only invested for a short period of time. Some money transmitters use the income generated on the float to pay for their operating expenses.

Changes in population coupled with technological advances have contributed to strong growth in Colorado's money transmission industry. As of December 31, 2002, there were 27 organizations licensed under Colorado's Money Order Act. With the exception of governmental organizations and insured financial institutions, licensing is required of any organization selling money orders or traveler's checks or transmitting money in Colorado. The total amount of money transmitted and exchange sold or issued in Colorado during 2002 was \$22 billion, an increase of two percent over 2001. Chart 1 depicts the growth in Colorado's exchange industry over the last five calendar years.

Chart 1
Exchange Sold in Colorado, 1998-2003



While the industry continues to experience strong growth, increased competition and the added cost of complying with new anti-money laundering regulations have strained earnings. During 2002, a licensee¹ ceased operations and voluntarily surrendered its license. The company's surety bond provider was called upon to honor transactions that were outstanding as of the closure.

History of Regulation

Colorado's Money Order Act was first enacted in 1959, when House Bill 59-102 vested the Commissioner of Banking with regulatory jurisdiction over the state's money order industry. The initial legislation required all money order licensees to prove their good moral character and financial responsibility, to post a bond in the principal amount of \$10,000, and to post an additional \$10,000 "per extra issuing outlet" up to a maximum of \$50,000.

¹ Two other licensees ceased operations, but did not leave outstanding obligations.

The statutory framework for the regulation of the money order industry remained the same until 1973, when the original statute was amended to raise the bonding requirement to the principal amount of \$25,000 with an additional requirement of \$5,000 per extra issuing outlet up to a maximum of \$250,000. The statute was also revised to provide that licenses would expire automatically unless the annual renewal fee was paid by January 1, and the Division was given the authority to revoke licenses if exchange was sold or issued without receipt of payment.

This bonding requirement was considered to be adequate until the mid-1970's when a money order issuer absconded with approximately \$380,000, voiding the value of the issued exchange. Colorado purchasers of this exchange were eventually reimbursed for their loss, and the General Assembly moved to prevent a similar occurrence by enacting House Bill 77-1198. This bill increased the bonding requirement to the principal amount of \$250,000 and required an additional sum of \$10,000 per operating location up to a maximum of \$1 million. Other protective measures were incorporated into the statute, including additional application information and reporting requirements to include the submission of annual financial reports audited by an independent certified public accountant. Licensees were also required to notify the Commissioner of any new issuing outlets and of any legal action or judgment brought against the licensee within 10 days.

Several statutory modifications were effected during the next decade. Most notably, the regulatory function with respect to the money order industry was realigned in 1988 as a responsibility of the Banking Board. Moreover, the examination section of the statute was altered from the former requirement that exams be conducted annually to the existing requirement that they be conducted to the extent deemed advisable by the Banking Board. Legislation in 1990 also shifted the cost of examinations to the licensee by permitting the Banking Board to charge a reasonable amount for examinations, and it required licensees to submit at least three financial reports that specifically state their assets and liabilities.

The \$250,000 bonding requirement was satisfactory until the industry experienced significant growth in its volume of business. Licensees typically carry more than \$1 million dollars in outstanding payment instruments at any given time. For example, in 1992 one licensee had more than \$14.9 million in outstanding payment instruments, while another held \$55 million in the same period. This growth in the industry induced the General Assembly to raise the principal amount of the required bond to \$1 million. In spite of this substantial increase, the amended statute also gave the Banking Board considerable discretion to increase or decrease the bonding requirement between \$250,000 and \$2 million depending on the financial condition of the money transmitter in question. In addition to the bond requirement, the amended statute allowed the Board to require a licensee to supplement its bond with permissible investments as collateral in an amount at least equal to the amount of outstanding payment instruments issued or sold by the licensee. These changes enjoyed industry support.

Legal Framework

Federal Law

Arguably the most important federal legislation that impacts Colorado's Money Order Act is the United States Bank Secrecy Act (BSA), codified at 31 U.S.C. section 5311, *et seq.* The purpose of this 1982 law is to ensure that banks, as well other financial institutions, do not become vehicles for illicit moneys.

All money transmitters in the United States are required to file Currency Transaction Reports for all cash transactions involving an exchange of cash in excess of \$10,000. In addition, these businesses must file Suspicious Activity Reports for all transactions of \$2,000, or more, when the transmitter believes that the transaction is suspicious.

It is also important to note that federal regulations are directly enforced by the Colorado Division of Banking. More specifically, money transmitter applicants for licensure are required by the Division to certify that the company has established a written compliance program for fulfilling the requirements of the Bank Secrecy Act (BSA) that includes at least:

- a system of internal controls;
- designation of an individual to coordinate and monitor BSA compliance;
- procedures for meeting the reporting and recordkeeping requirements of the BSA;
- procedures for the detection, prevention, and reporting of suspicious transactions related to money laundering activities;
- independent testing; and,
- training of appropriate personnel.

In addition, the applicant must certify that the company has systems in place to check money transmissions against names on the Office of Foreign Assets Control's (OFAC) list of Specially Designated Nationals and Blocked Entities, and when the system identifies a designated name in a transmission, has procedures in place to comply with OFAC regulations. Finally, the applicant must certify that the company has registered with the Department of Treasury as a Money Services Business and has procedures in place to comply with section 103.41 of Title 31 of the Code of Federal Regulations.

In summary, the Colorado Banking Board itself requires compliance with federal regulations and has promulgated Rule MO6 to address this issue. This rule requires each licensee to develop a compliance plan outlining policies, procedures, and practices implemented to ensure compliance with federal laws and regulations applicable to money services businesses, including, but not limited to, federal anti-money laundering, record keeping, and registration requirements. Failure to develop such a compliance plan may be considered a basis for license revocation pursuant to section 12-52-112, C.R.S.

Colorado Law

Section 12-52-102, C.R.S., is the legislative declaration of the Money Order Act, which sets out the policy of the General Assembly as being the protection of the people of Colorado from default in the payment of checks, drafts, money orders, or other instruments used in the transmission or payment of credit or money. "Money transmission" means the sale or issuance of exchange or engaging in the business of receiving money for transmission or transmitting money within the United States or to locations abroad by any and all means including but not limited to payment instrument, wire, facsimile, or electronic transfer (§ 12-52-103(4.3), C.R.S.). In this context "exchange" means any check, draft, money order, or other instrument for the transmission or payment of money or credit. It does not mean money or currency of any nation (§ 12-52-103(2), C.R.S.).

Section 12-52-104, C.R.S., establishes that a license is required from the Banking Board in order to engage in the business of selling or issuing exchange, or for the business of money transmission. This section excludes agents, subagents, or representatives of licensees, as well as their employees. In addition, government entities and corporations organized under the general banking, savings and loan, or credit union laws of Colorado or the United States are **exempt**. Similarly, the receipt of money by an incorporated telegraph or cable company at any of their local offices for immediate transmission by telegraph or cable is permissible (§ 12-52-105, C.R.S.).

The Banking Board may make, promulgate, alter, amend, or revise reasonable rules and regulations as may be necessary for the enforcement and execution of the Money Order Act (§ 12-52-113, C.R.S.). Further, the Board is authorized to establish by rule financial standards by which to evaluate the financial condition or solvency of licensees, and for the bond amount set to be decreased to not less than \$250,000, following application by the licensee and an opportunity for hearing before the Board (§ 12-52-107(1)(b), C.R.S.). In addition to the required bond, the Banking Commissioner, pursuant to rules promulgated by the Banking Board, may require a licensee to possess investments having an aggregate market value at least equal to the amount of outstanding payment instruments issued or sold by the licensee (§ 12-52-107(3), C.R.S.).

Application requirements for a license are set out in section 12-52-106, C.R.S. Written application to the Board is required on forms of its own choosing to include identifying information and other pertinent information. Each application for a license must be accompanied by financial statements of the applicant and a bond (§ 12-52-106, C.R.S.). A corporate surety bond in the principal sum of \$1 million by a bonding company or insurance company authorized to do business in Colorado is required. The applicant must be named as obligor, and the bond run to the State of Colorado for the use and benefit of the state and of any creditor of the licensee for any liability incurred on any exchange issued by the licensee. The bond must remain in force and effect until the surety is released from liability by the Banking Board, or until the bond is cancelled by the surety, which cancellation may be had only upon 30 days' written notice to the Board (§ 12-52-107(1)(a), C.R.S.).

Upon the filing of an application, the Banking Commissioner must investigate the applicant, and if the Banking Board finds that the applicant is of good moral character and financially responsible, the Board must provide notice in writing of the approval of the applicant, who must within thirty days post the required bond and pay the required license fee, whereupon the Board issues a license to engage in the business of selling or issuing exchange (§ 12-52-108(1), C.R.S.). Licenses must be renewed annually thereafter (§ 12-52-109, C.R.S.).

Section 12-52-110(1)(a), C.R.S., empowers the Commissioner to examine the books and records of every licensee as often as deemed advisable. To the extent required by the Board, the Commissioner must produce and file a correct and detailed report disclosing the results of such examinations. In lieu of the required examination, the Commissioner may accept the audit of an independent certified public accountant or an independent registered accountant, but the cost of such audit shall be borne by the licensee (§ 12-52-110(1)(b), C.R.S.).

The Banking Board may upon 10 days notice hold a hearing for the purpose of determining whether there are grounds for license revocation. These include:

- Licensee failure to maintain the required bond;
- Licensee failure to comply with any order, decision, or finding of the Banking Board or the Commissioner;
- The existence of facts which would have warranted initial refusal to issue a license;
- The licensee is engaged in a business a substantial portion of which involves the processing, manufacture, or purchase and sale of commodities or articles of tangible personal property and such licensee has failed to maintain constantly a separate bank deposit account or accounts for the exclusive payment of exchange issued by such licensee; and,
- The licensee has sold or issued exchange without receiving payment for the face value of the exchange² prior to the time of such sale or issuance (§ 12-52-112, C.R.S.).

Licensees must also provide notice by certified mail to the Board within 10 days of any legal action brought against a licensee and of any judgment entered against a licensee relating to selling or issuing exchange or transmitting money (§ 12-52-116, C.R.S.).

Any person who violates any provision of the Money Order Act is guilty of a misdemeanor and, upon conviction, is assessed a fine of not more than ten thousand dollars. Each violation constitutes a separate offense (§ 12-52-115, C.R.S.). Any person aggrieved and directly affected by an order of the Banking Board may seek a review in the District Court of Colorado in and for the county in which the principal place of business of the licensee or applicant is located (§ 12-52-114, C.R.S.).

² “Exchange” may be thought of as money transmission.

Program Description and Administration

The mission of the Colorado Division of Banking (Division) is to serve and protect the public interest by promoting a safe and sound financial institutions industry through continuous quality regulation and supervision. More specifically, the Division is responsible for public deposit protection and the regulation of state-chartered commercial banks, industrial banks, trust companies, money transmitters, and money order companies. A more comprehensive description of the Division may be found in the companion report "Division of Banking, 2003 Sunset Review".

The Banking Board is statutorily empowered to grant or deny licenses for money transmitter applicants and to fix the required bond or securities amount between \$250,000 and \$2,000,000. It is likewise authorized to approve a licensee's request to cover outstanding payment instruments with a combination of surety bond and permissible investments, and it is vested with the statutory authority to determine the suitability of collateral other than permissible investments. The Board is also responsible for fixing the licensing and annual renewal fees for which licensees are liable, for mandating the extent and frequency of examinations, which the Commissioner must cause to conduct, and for revoking licenses under certain statutorily enumerated circumstances. Finally, it is responsible for promulgating and amending rules necessary for the enforcement and execution of the Money Order Act.

The Commissioner of Banking is responsible for the administration of the program, including examination and enforcement functions. The Commissioner is also empowered to require licensees to post additional collateral in the form of permissible investments pursuant to rules promulgated by the Banking Board.

Aggregate numbers and full-time equivalent employees (FTE) for the Division of Banking, inclusive of all programs, is presented in Table 1.

Table 1
Agency Staff and Fiscal Information, FY 97-98 to FY 01-02

	FY 97-98	FY 98-99	FY 99-00	FY 00-01	FY 01-02
Appropriations	\$3,055,955	\$3,076,895	\$3,189,026	\$3,272,446	\$3,316,101
Actual Expenditures	\$2,791,187	\$2,980,860	\$2,962,289	\$3,260,783	\$3,195,854
Authorized FTE	40.0	38.0	38.5	38.5	38.5

The remainder of this section describes the Division's functions as they relate to the regulation of money transmitters in Colorado. Table 2 shows the portion of the Division's resources that were devoted to Colorado money transmitter regulation in the period fiscal year 97-98 to fiscal year 01-02.

Table 2
Resource Allocation for Money Transmitter Regulation, FY 97-98 to FY 01-02

	FY 97-98	FY 98-99	FY 99-00	FY 00-01	FY 01-02
Allocated Expenses*	\$79,821	\$85,212	\$127,079	\$169,288	\$177,803
Allocated FTE	1.25	1.25	1.75	2.25	2.25

*Reflects salary and benefit expense of examiners and supervisor based on allocation of staff to oversee the money order/transmitter program. Increases during FY 99-00 and FY 00-01 are attributable to the assignment of an additional examiner to the program as well as additional caseload manager time in response to industry growth, complexity and exam procedures.

Program Administration

The Applications and Complaints unit of the Division of Banking is charged with the processing of license applications from prospective money transmitters. The major task assigned to the applications function of this unit is to review and analyze the complex financial, managerial, operational, and organizational information related to applications submitted to the Colorado Division of Banking for a new money order company or money transmitter license. The unit must determine if the applicant has met all of the individual application requirements, develop the agency's position regarding the applicant's request, and prepare and present written and oral recommendations (including agency justification of recommendation) to the Colorado State Banking Board within required timelines. In addition, the applications segment of this unit is responsible for the management of application processes, including reviewing the necessary scope of background investigations, updating and improving all application forms, tracking certain application processing costs, making application forms and related information available on the Division's web site, and an ongoing assessment of new interagency application forms.

Applicants seeking money transmitter licenses in Colorado must meet the *Qualification of License Applicant* criteria detailed in the State Banking Board's current rule (MO-4). Applicants may be individuals, partnerships or corporations. Complete identification of individuals, partners, directors or executive officers is required. Experience in money transmitting must be documented, as well as information concerning licensure history in other states.

Corporation applicants must provide copies of their most recent audited financial statements. The details of any petitions for bankruptcy or other relief from indebtedness in any court proceeding must be disclosed, along with any felony or misdemeanor convictions.

Only one license is issued per application. It covers a licensee's principal location and any proposed branches and agents, which are to be identified at the time the application is made.

The number of new and renewed money transmitter licenses for the period under review is depicted in Table 3. The Money Order Act (Act) provides for the Banking Board to set the fees. If adjustments are warranted, the Division would make a recommendation to the Banking Board to adjust the fee schedule. The Division's policy is to review the fee schedule on an annual basis and present recommendations to the Banking Board at its June Board meeting for the subsequent fiscal year.

Table 3
Money Transmitter Licensing Information

	Period Ending 12/31/1998	Period Ending 12/31/1999	Period Ending 12/31/2000	Period Ending 12/31/2001	Period Ending 12/31/2002	Period Ending 06/30/2003
Renewals	20	23	21	22	26	30
New Charters	4	0	2	4	7	1
Licenses Surrendered	1	2	1	0	3	2
Totals	23	21	22	26	30	29

The initial license application fee for a money transmitter is \$7,500 provided the application is made in the period January 1 to June 30 of a given year. If the application is submitted in the period from July 1 to December 31 of a given year, the fee is \$3,750. The renewal fee is \$3,000. Money transmitter licenses are renewed annually effective January 1 of each year in accordance with section 12-52-109, C.R.S.

As Table 3 shows, the number of money transmitters in Colorado has been relatively stable, with noticeable growth occurring between 2000 and 2002 in the form of nine new licensees, an increase of 36 percent.

Examinations

In accordance with the Colorado Money Order Act (Act), each licensee must be assigned a composite rating based on the examiner's evaluation of pertinent financial and operational standards, criteria, and principles. This overall rating is expressed by a numerical scale of "1" through "5" in ascending order of supervisory concern, "1" indicating the highest rating and least degree of concern, and "5" indicating the lowest rating and greatest degree of concern. To implement this rating system, the Division has divided the licensee's operations into five major areas to evaluate and consider in the assignment of the composite rating: Ownership and Management Supervision; Operations and Records; Capital Adequacy and Earnings; Bonding and Permissible Investments; and, Contingent Liabilities.

Division of Banking examinations are conducted in accordance with Banking Board Policy 80-1. This policy establishes the types and frequencies of examinations conducted by the Division based on the condition of the financial institutions under its jurisdiction, including money order companies. The type and frequency of examination is determined initially by whether it is a new licensee or an established business. The latter's examinations are based on prior composite ratings. New licensees must undergo a target on-site examination within

the first six months of operation. The examination is designed to assess whether the company has in place all the necessary operational processes and personnel to operate in a safe and sound manner. In addition, the examination introduces the company to the Division's examination and regulatory functions. Thereafter, a full scope examination occurs at 12-month intervals for the first two years of operation, unless the operation is a subsidiary of an existing Colorado licensee in good standing, in which case the examination cycle of the parent company may apply.

Money transmitter companies with a composite rating of "1" or "2" must undergo a full-scope examination at 18-month intervals on an alternating on-site, off-site basis. The examination may be performed two months prior to, or two months beyond the due date. Money transmitter companies with a composite rating of "3," "4," or "5" must undergo a full-scope examination no less than every 12 months.

The number of money transmitter examinations conducted over the last five fiscal years is depicted in Table 4

Table 4
Money Transmitter Examinations, FY 97-98 to FY 01-02

Type of Institution	FY 97-98	FY 98-99	FY 99-00	FY 00-01	FY 01-02
On Site	11	11	10	7	8
Off Site	11	13	9	19	15
Total	22	24	19	26	23

The Division of Banking conducts money transmitter examinations with the help of two full-time examiners. According to the Division, its money order and bank safety and soundness examiners have some common skills, but the money order examiners are more specialized (see the companion report "Division of Banking: 2003 Sunset Review"). The Division does not currently have any bank safety and soundness examiners that could perform money transmitter examinations. The reverse is not strictly true, however. Money order examiners have a general knowledge of bank safety and soundness examinations, and could with an investment in training, be fully competent to perform bank examinations. The Division reports that they have tried various cross-training programs in the past, but that the money transmitter exam schedule is currently too arduous to enable these examiners to assist bank examiners, who face challenges of their own. We address this set of circumstances in Recommendation 2 of this report and Recommendation 3 of the "Division of Banking: 2003 Sunset Review".

Complaints and Enforcement

The Applications and Complaints unit of the Division of Banking is charged with the processing of complaints from consumers regarding money transmitters. The major function of the complaints segment of this unit is to review and analyze written complaints against institutions regulated by the Division. This segment must determine whether there have been violations of law or rule. In addition, it acts as an arbitrator between complainants and regulated institutions when appropriate to find a resolution acceptable to both parties. The complaints segment is also responsible for the management of complaint processing, including updating and improving complaint information available on the Division's web site, as well as the revision, development, or deletion of policies related to complaint processing.

The Division did not maintain detailed consumer complaint tracking sheets until fiscal year 98-99. Prior to that time, complaints for all entities were simply tallied and reported to the Banking Board on a monthly basis. The available information is shown in Table 5.

Table 5
Complaint Information

Number of complaints	FY 97-98	FY 98-99	FY 99-00	FY 00-01	FY 01-02
Refund of Exchange	N/A	1	1	2	0
Account/Contract	N/A	1	1	1	1
Total		2	2	3	1

Consumers with complaints against institutions regulated by the Division are asked to provide the complaint in writing, with as much detail as possible. A referral letter, with a copy of the complaint, is forwarded to the institution with a requested response date. Upon receipt of a response, a Division staff member reviews the issues and responds to the complainant, with a copy to the regulated institution, explaining the findings and the resolution of the complaint. The Banking Board does not formally review complaints.

The Division has historically received very few individual consumer complaints pertaining to money order/transmitter companies. This can be explained in part by the fairly straightforward nature of money transmissions – the remitter provides cash to a licensee, or agent, at location A, and the funds are paid out to the recipient at location B. If, for some reason, the transaction is not completed, the remitter or recipient usually seeks redress from the agent or the company. Only in the event of a licensee failure or discontinuation of business (as described under the enforcement section) are the protections of the Money Order Act actively sought by consumers. While licensee complaint files indicate that the vast majority of issues are addressed at the institution level, due to economic, cultural, educational, and linguistic reasons many consumers would not know how, or would be hesitant to, seek assistance from the Division of Banking. Table 6 depicts the number and type of enforcement actions taken by the Division for the preceding five fiscal years.

Table 6
Enforcement Actions

Type of Action	FY 98-99	FY 99-00	FY 00-01	FY 01-02	FY 01-03 YTD
Memorandum of Understanding	0	1	0	0	2
Total*	0	1	0	0	2

Although various weaknesses and concerns are identified in Division examination reports, few rise to the level warranting a formal enforcement action. Section 12-52-103.5 C.R.S., grants the Banking Board and Commissioner the same enforcement authority over money order/transmitter licensees as are applicable to state banks; however, the Money Order Act, and implementing rules, do not impose the same level of operating, capital, and transactional restrictions on money order/transmitter companies. Very simply, with fewer requirements, there are fewer violations; accordingly, there are fewer enforcement actions. Nevertheless, the proliferation of new licensees, increased competition, and an economic downturn have highlighted weaknesses requiring Division action, as described in the following three actual cases:

- An El Paso, Texas company was licensed under the Colorado Money Order Act in December 1998. The company conducted Colorado operations through a limited number of agent locations. On July 25, 2002, this company abruptly discontinued all operations due to deteriorating financial conditions. Colorado agents were directed to cease accepting funds for transmission. The Division coordinated its investigation with the Texas Department of Financial Institutions. A list of outstanding transactions was developed based on agent records and reports from the El Paso office. The surety company was formally advised of potential claim and notices were sent to affected consumers. After a lengthy process, the surety company paid on all claims filed by individual consumers. However, the Division believes that an additional 25 to 30 consumers may have lost funds but cannot be located. While the surety bond has been put on notice that additional claims may be forthcoming, it is unlikely, in light of the length of time since the initial failure, that further claims will be filed. It is believed that additional claims were not filed due to the language barrier (although the Division does have a bilingual examiner) and the likely illegal immigration status of many of the consumers.
- The Division was notified during 2003 that a licensed money transmitter was discontinuing operations due to deteriorating financial conditions and voluntarily surrendered its Colorado license. Division examiners contacted the company's agent locations in Colorado to confirm that transmission activities had ceased and determine if there were any outstanding funds (i.e. funds remitted for transmission but not obtained by the intended recipient). One agent indicated that he had two uncompleted transmissions and is to provide the Division with appropriate documentation. A notice of potential claim was sent to the surety company. In addition, the chairman and principal

owner of the company in question was notified of the outstanding items and directed to reimburse the remitters. If he fails to resolve the matter in a timely manner, the Division will file claims with the surety company upon receipt of the required documentation from the agent.

- An April 2003 examination of a California company that was recently licensed to operate through agent locations in Colorado showed that the licensee was not complying with federal anti-money laundering regulations, nor was it screening recipient names and locations for federally blocked names and countries. Interestingly, the company had been recently examined by two other states and given clean examination reports. Moreover, the owner and president of this company certified in application documents that the company had systems in place to ensure compliance with applicable federal laws.

Two themes emerge from these recent cases. First, the mandatory surety bond that money transmitter companies must carry is a very important tool. It provides effective redress to aggrieved consumers in a way that few other regulatory programs do. Second, the licensing process whereby prospective licensees certify that they are in compliance with applicable federal laws should be vetted by the Division of Banking upon receipt, rather than at a future date.

Analysis and Recommendations

During the course of this sunset review, the Department of Regulatory Agencies (DORA) solicited input from a variety of sources. A number of significant issues were presented and considered including:

- Industry wishes to enter into interstate compacts concerning examinations;
- Division of Banking trends concerning examination scheduling; and,
- Federal safeguards.

Some of these issues are discussed in the recommendations that follow. Those that are not discussed were found to have fallen outside the scope of the statutory criteria that govern sunset reviews.

Recommendation 1 –Continue the Money Order Act until 2013.

Colorado has regulated money transmitters since 1959, making it one of the 45 states that do so. Alaska, Hawaii, Montana, New Hampshire, and South Carolina are the only states in the union that have no law governing money transmitters. Colorado's Money Order Act is consequently in keeping with national trends. Moreover, our regulatory scheme compliments federal policy and regulations. As noted previously, changes in population coupled with technological advances have contributed to strong growth in Colorado's money transmission industry. As of December 31, 2002, there were twenty seven organizations licensed under this Colorado law. With the exception of governmental organizations and insured financial institutions, licensing is required of any organization selling money orders or traveler's checks or transmitting money in Colorado. The total amount of money transmitted and exchange sold or issued in Colorado during 2002 was \$22 billion, an increase of two percent over 2001.

In this context, the Division of Banking has provided necessary and sufficient public protection for the period under review. At the front end, the Banking Board and the Division of Banking license money transmitters requiring them to submit detailed information about their operations. In this way, the Division can assess the initial viability of these companies, and by means of subsequent reporting requirements, the continued viability of money transmitters. At the tail end of the regulatory scheme, consumer protection is afforded primarily by providing a compensation recourse to consumers by way of filing a claim against the mandatory security bond that each licensee must post. Consequently, the existing regulatory scheme works to benefit Colorado consumers without being unduly burdensome to the industry.

In conclusion, for the reasons outlined herein, the Money Order Act and its provisions should be continued until 2013, except as otherwise noted below. As we discuss in the next recommendation, the overall number of consumer complaints and enforcement actions does not warrant far-reaching regulation, nor an accelerated review period.

Recommendation 2 – Eliminate the mandatory examination of licensees.

In the past, the General Assembly has relaxed money transmitter regulation by expressly allowing the use of examination reports by other state regulators, as well as independent accountant audits in lieu of Division of Banking examinations. This recommendation continues this trend by proposing the elimination of mandatory examinations of Colorado money transmitters.

More specifically, there are three compelling reasons to eliminate the current mandatory examination of licensees.

First, a comparison of the examination requirements of other states reveals that Colorado is one of only 15 states that require mandatory financial examinations of money transmitters. More specifically, section 12-52-110(1)(a), C.R.S., directs the Commissioner to “examine the books and records of every licensee as often as deemed advisable and to the extent required by the banking board.” The frequency of mandatory examinations is set out in Banking Board Policy 80-1 and is summarized above. As Table 7 below shows, the majority of states do not place a primary emphasis on examinations in their regulatory schemes. This appears to be the most common strategy because there are several other regulatory safeguards in place. For example, most states require each licensee to provide annual financial statements, including a balance sheet, a profit and loss statement and a statement of retained earnings related to selling or issuing exchange.

Table 7
States’ Examination Requirements

States requiring exams	15	AR, CO , FL, KS, KY, LA, MA, MN, NV, NY, ND, PA, RI, SD, WA
States that are permissive	24	AZ, CA, CT, DE, ID, IL, IN, IA, ME, MD, MI, MS, NJ, NC, OH, OK, OR, TN, TX, VT, VA, WV, WI, WY
States that do not mention exams	6	AL, GA, MO, NE, NM, UT
No state regulation	5	AK, HI, MT, NH, SC
States accepting other states’ or agencies’ exams	13	AZ, CO , CT, FL, IN, IA, LA, ME, MD, NC, TN, VT, VA

Source: Statutes of each state

Clearly, the majority of states do not regard examinations as being cost effective or necessary for public protection. In fact, five states do not regulate money transmitters at all. Indeed it is counterproductive for Colorado to be the lead state among those states that require examinations. If provisions in other states permit, the relevant states accept Colorado examinations in lieu of their own. Consequently, they may come to rely excessively and inappropriately on Colorado’s examination program. Division staff report that they do “not have the resources to consistently serve as the lead state, perform the examination, and coordinate other states requests and requirements.”

Second, the overall number of consumer complaints and enforcement actions do not warrant far-reaching regulation. For the five-year period ending December 2002, the Division of Banking received a total of eight complaints from consumers and took three enforcement actions. The Division has historically received very few individual consumer complaints pertaining to money transmitter companies. This can be explained in part by the fairly straight-forward nature of money transmissions – the remitter provides cash to a licensee, or agent, at location A, and the funds are paid out to the recipient at location B. If, for some reason, the transaction is not completed, the remitter or recipient usually seeks redress from the agent or the company.

Similarly, in the 1993 Sunset Review of Money Order Regulation we noted that

The Division has not received any complaints from the public about money order licensees, nor has the public suffered any harm as a result of the money order industry for over a decade...This remarkable record is attributable in part with the fact that Colorado's money order business is run by large, financially stable corporations which have the ability to comply with the state's historically high bonding requirement...Therefore, even though Colorado's bonding requirements pose a barrier to groups without the economic muscle to secure adequate collateral, it serves the public policy of protecting Colorado consumers by ensuring compensation for loss occasioned by the wrongdoing, negligence, or financial insolvency of money order licensees.

In short, consumer complaints in this industry are not overly worrisome either in terms of quality or quantity.

The number of enforcement actions taken by the Division of Banking is another general indication of the condition of Colorado's money transmitter industry. For the five-year period ending December 2002, the Division took three enforcement actions, all of which were in the form of a memorandum of understanding, the least stringent form of corrective action. The Division notes that "although various weaknesses and concerns are identified in Division examination reports, few rise to the level warranting a formal enforcement action." In the period 1959 to 2003, eight licensees ceased operations without exhibiting problems or adverse ratings. In the same period, three money transmitters exhibited problems or were adversely rated out of a total of 29 active licensees, while only one licensee was both adversely rated and ceased operations. Consequently, a close correlation between examinations and effective corrective action does not exist, eroding the need for the mandatory, periodic examination of licensees for this purpose.

Third, the Division of Banking faces heavy bank examination workloads. Consequently, there is an important ancillary benefit to eliminating the mandatory examination of money transmitters. Money order examiners have a general knowledge of bank safety and soundness examinations, and could with an investment in training, be fully competent to perform bank examinations. This Recommendation therefore is designed to alleviate an existing problem by making available up to 1.00 FTE to perform the primary mission of the Division of Banking, which is to ensure a safe and sound banking industry in Colorado. *It is central to our argument that this recommendation be viewed as a companion proposal to Recommendation 8 in the 2003 Sunset Review of the Division of Banking.*

In conclusion, the regulatory cost of examinations to both licensees and the Division of Banking itself is not justified in light of existing federal and state safeguards. More specifically, initial licensing requirements, subsequent information reporting requirements, and the surety bond licensees must post have to date proved to be adequate public protection mechanisms. Regulatory costs must also be weighed against any potential harm to consumers. For the five-year period ending December 2002, the Division received a total of eight complaints from consumers and took three enforcement actions. Consequently, the regulatory burden associated with examinations appears to be excessive in light of the potential risk to consumers. Mandatory examinations of Colorado money transmitters should therefore be discontinued given that the benefits of partial deregulation outweigh the costs associated with this aspect of regulation.

To effect this recommendation, section 12-52-110(1)(a), C.R.S., should be amended as follows:

The commissioner ~~shall~~ MAY examine the books and records of ~~every~~ ANY licensee ~~as often as deemed advisable~~ IN ACCORDANCE WITH RISK BASED CRITERIA AND CONSIDERING OTHER AVAILABLE REGULATORY MECHANISMS AS SPECIFIED ~~and to the extent required~~ by the banking board; shall make and file in the office of the commissioner a correct report in detail disclosing the results of such examination; and shall mail a copy of such report to the licensee examined.

Recommendation 3 – Require licensees to post at each of their outlets public notices regarding the complaint procedures of the Division of Banking.

The Division of Banking publishes on its web site the type of institutions it regulates, as well as other agency contact information so that consumers can file their complaints with the appropriate state agency. In addition, the web site outlines general complaint procedures. Although this is a good start, it also points to a fundamental problem. That is, under the existing circumstances, consumers must already be aware that the Division regulates money transmitters in order to obtain the information available to them from the Division's web site. In order to better serve the public, wider and more effective dissemination of the Division's complaint process is necessary.

The Division acknowledges that it is only in the event of a licensee failure or discontinuation of business that the protections of the Money Order Act are sought by consumers. While licensee complaint files indicate that the vast majority of issues are addressed at the institutional level, it must be recognized that for economic, cultural, educational, and linguistic reasons, many consumers would not know, or would be hesitant, to seek assistance from the Division of Banking. Consequently, it would benefit consumers greatly if licensees were required to post in a conspicuous location in their place of business a public notice informing them of their rights together with information as to how to initiate a complaint. Such posting would need to be in English and any foreign language predominantly spoken by customers at the respective locations. This recommendation would be in keeping with other similar posting requirements by government agencies. Rule 20.1 of the Colorado Civil Rights Division may serve as a model.

Recommendation 4 – Extend the time from 30 to 90 days for licensees to obtain new surety bonds.

Currently section 12-52-107(1)(a), C.R.S., holds that:

the bond shall remain in force and effect until the surety is released from liability by the banking board or until the bond is cancelled by the surety, which cancellation may be had only upon thirty days' written notice to the banking board.

Colorado's surety bond marketplace is such that licensees are precluded from having a sufficient number of suitable providers to meet their needs. In one instance, a licensee opted to surrender their license because of an inability to obtain a replacement bond. By extending the required notice period to 90 days, money transmitter licensees would have sufficient time to ensure that a new surety bond is in force prior to the existing surety company's cancellation of the bond. In addition, the Division of Banking would have extra time to verify that the licensee was able to secure a new bond, which is a requirement for licensure.

This Recommendation also makes money transmitter requirements similar to those of commercial banks, industrial banks, and trust companies, which are required to provide the Division a 90 days notice of bond cancellation.

Recommendation 5 – Extend the time from 120 to 150 days for licensees to file annual financial statements.

Currently, every money transmitter licensee must file an annual financial statement with the Commissioner, as audited by an independent certified public accountant, within 120 days following the close of each licensee's fiscal year (§ 12-52-110(2)(a), C.R.S.). According to Division staff, however, external auditors have difficulty completing their audits in the required 120 days. Therefore, changing the submission date to 150 days would accommodate these professionals, and align submission requirements of money transmitters with that of commercial banks, industrial banks, and trust companies.

Recommendation 6 – Increase the amount of fines for late filings.

Section 12-52-110(2)(c), C.R.S., provides that:

if any licensee fails to submit any statement or report to the commissioner as required by this subsection (2) such licensee shall pay to the commissioner a penalty assessment in an amount not to exceed twenty-five dollars for each additional day of delinquency as set by the banking board . . .

In the Division's experience, a \$25 fine does not serve its intended purpose of effectively deterring unsatisfactory reporting practices. The Division publishes its fee schedule on its web site, therefore licensees would not be unfairly disadvantaged in terms of adequate notice. Consequently, the penalty assessment for late filings should be increased to \$250.

Recommendation 7 – Require licensees to submit a copy of the Engagement Letter and Management Letter issued by an independent auditor.

In addition to the submission of financial statements containing a balance sheet, a profit and loss statement, and a statement of retained earnings, each licensee should be required to submit to the Division of Banking copies of both the engagement letter and management letter issued by an independent auditor. This is similar to what is currently required of commercial banks, industrial banks, and trust companies, which are also under the jurisdiction of the Division. Submission of these two documents would enhance oversight by enabling the Division to assess the intended scope of the outside audit (engagement letter), as well as any adverse findings or recommendations by the independent auditor (management letter) following the audit, which would forewarn the Division of potential problems.

Recommendation 8 - Amend the title of the Act from “Money Order Act” to “Money Transmitters Act.”

Section 12-52-102, C.R.S., is the legislative declaration of the “Money Order Act”, which sets out the policy of the General Assembly as being the protection of the people of Colorado from default in the payment of checks, drafts, money orders, or other instruments used in the transmission or payment of credit, or money. "Money transmission" means the sale or issuance of exchange or engaging in the business of receiving money for transmission or transmitting money within the United States or to locations abroad by any and all means including but not limited to payment instrument, wire, facsimile, or electronic transfer (§ 12-52-103(4.3), C.R.S.). In this context “exchange” means any check, draft, money order, or other instrument for the transmission or payment of money or credit. It does not mean money or currency of any nation (§ 12-52-103(2), C.R.S.).

The title “Money Order Act “ is misleading because a money order is only one form of a money transmission instrument. It does not include, for example, traveler's checks, or wire transfers. Changing the title to “Money Transmitters Act” would more accurately reflect the content of the statute and the industry it regulates.

Appendix A – Sunset Statutory Evaluation Criteria

- (I) Whether regulation by the agency is necessary to protect the public health, safety and welfare; whether the conditions which led to the initial regulation have changed; and whether other conditions have arisen which would warrant more, less or the same degree of regulation;
- (II) If regulation is necessary, whether the existing statutes and regulations establish the least restrictive form of regulation consistent with the public interest, considering other available regulatory mechanisms and whether agency rules enhance the public interest and are within the scope of legislative intent;
- (III) Whether the agency operates in the public interest and whether its operation is impeded or enhanced by existing statutes, rules, procedures and practices and any other circumstances, including budgetary, resource and personnel matters;
- (IV) Whether an analysis of agency operations indicates that the agency performs its statutory duties efficiently and effectively;
- (V) Whether the composition of the agency's board or commission adequately represents the public interest and whether the agency encourages public participation in its decisions rather than participation only by the people it regulates;
- (VI) The economic impact of regulation and, if national economic information is not available, whether the agency stimulates or restricts competition;
- (VII) Whether complaint, investigation and disciplinary procedures adequately protect the public and whether final dispositions of complaints are in the public interest or self-serving to the profession;
- (VIII) Whether the scope of practice of the regulated occupation contributes to the optimum utilization of personnel and whether entry requirements encourage affirmative action;
- (IX) Whether administrative and statutory changes are necessary to improve agency operations to enhance the public interest.