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Colorado Department of Regulatory Agencies  
Office of Policy, Research and Regulatory Reform

# The Functions of the Division of Insurance Related to the Issuance of Certificates of Authority for Health and Life Insurance



October 14, 2005

# STATE OF COLORADO

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Bill Owens  
Governor

October 14, 2005

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 the evaluation of the functions of the Colorado Division of Insurance (DOI) related to the issuance of certificates of authority for health and life insurance. I am pleased to submit this written report, which will be the basis for my office's oral testimony before the 2006 legislative committee of reference. The report is submitted pursuant to section 24-34-104(8)(a), 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 3 of Title 10, C.R.S. The report also discusses the effectiveness of the DOI and staff in carrying out the intent of the statutes and makes recommendations for statutory changes in the event this regulatory program is continued by the General Assembly.

Sincerely,



Tambor Williams  
Executive Director

## 2005 Sunset Review

# The Functions of the Division of Insurance Related to the Issuance of Certificates of Authority for Health and Life Insurance

Department of Regulatory  
Agencies

Bill Owens  
Governor

Tambor Williams  
Executive Director



## Executive Summary

### Quick Facts

#### **What is Regulated?**

Certificates of authority are required by Colorado law in order to conduct business as a health or life insurance provider in this state. In addition to the initial certificate of authority, similar authorization is required prior to expansion of the original certificate of authority or to amend any aspect of the corporate charter.

#### **Who is Regulated?**

Certificates of authority are required of all health and life insurance providers in Colorado. Presently, 10 domestic and 6,526 foreign insurance providers are authorized to conduct life and health insurance business in this state.

#### **How is it Regulated?**

Colorado law requires that companies demonstrate a sound business plan and adequate capital (statutory minimum capital requirements are \$1.5 million for life and health insurance companies), favorable liquidity, adequate re-insurance, sound management and stable revenue.

#### **What Does it Cost?**

The initial certificate of authority application fee is \$500. Subsequent to the granting of authority to conduct business in Colorado, annual fees are graduated based on the previous year's premium collections. Annual fees range from \$670 to \$3,345.

**Where Do I Get the Full Report?** The full sunset review can be found on the internet at:

<http://www.dora.state.co.us/opr/oprpublications.htm>.

### Key Recommendations

**Continue the Division of Insurance's function of the issuance of certificates of authority of health and life insurance companies doing business in Colorado.**

Colorado Division of Insurance ensures that insurance companies meet all statutory and financial criteria prior to issuing a certificate of authority. The Division of Insurance also determines whether an applicant possesses the necessary experience, expertise, and management skills to conduct the type of business that was requested in the certificate of authority application. Without this function, insurance companies would be able to conduct business in Colorado without demonstrating that they meet the minimum standards necessary to protect the welfare of Colorado citizens.

**Amend scope of future Division of Insurance sunset reviews.**

Legislative oversight of the regulatory functions of the DOI would be improved by establishing a broader scope of sunset reviews in the future.

**Track data regarding the Uniform Certificate of Authority Application process.**

The DOI could benefit from more information and data relating to the Colorado Division of Insurance's adherence to established deadlines for evaluating, approving, and denying applications. This information would be important in light of the possible SMART Act legislation and monitoring compliance with National Association of Insurance Commissioners standards.

**Major Contacts Made in Researching the 2005 Sunset Review of the Functions of the Division of Insurance Related to the Issuance of Certificates of Authority for Health and Life Insurance**

National Association of Insurance Commissioners  
Insurance Officials in Other States  
Representatives of Colorado's Insurance Industry  
Colorado Division of Insurance

**What is a Sunset Review?**

A sunset review is a periodic assessment of state boards, programs, and functions to determine whether 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:  
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## **Background**

### *The Sunset Process*

The functions of the Division of Insurance (DOI) related to the issuance of Certificates of Authority (COA) for health and life insurance, in accordance with Article 3 of Title 10, Colorado Revised Statutes (C.R.S.), shall terminate on July 1, 2006, 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 the functions of the DOI related to the issuance of COA for health and life insurance pursuant to section 24-34-104, C.R.S.

The purpose of this review is to determine whether the function should be continued for the protection of the public and to evaluate the performance of the DOI in relation to the issuance of COA to life/health insurers. During this review, the DOI must demonstrate that there is still a need for the function and that the function 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 on page 31.

### *Methodology*

As part of this review, DORA staff attended meetings with DOI officials; interviewed DOI staff; reviewed DOI records, including complaint and disciplinary actions; interviewed officials with state and national professional associations; reviewed Colorado statutes and DOI rules; and reviewed other states' laws.

### *Profile of the Industry*

Insurance plays an important role in our society. The use of insurance dates back to antiquity. Put simply, it provides a financial safety net for unanticipated consequences. A buyer will enter into a contract with an insurer whereby the buyer pays a premium to the insurer that is equal to a small amount of the insured item. This ensures that if the item is damaged or lost, its value is replaced.

Today, the role of insurance has grown considerably worldwide, and insurance has become one of the largest industries in Colorado. It permeates every facet of our society and lives. In many cases, insurance is statutorily required. Various professions require an individual to hold a form of errors and omissions insurance, and owners of automobiles must obtain liability insurance prior to vehicle registration. The free market has evolved to the point where in order to participate in various business and commercial transactions insurance is mandatory. For example, most individuals may not obtain a mortgage for a home without having insurance, even when using a private lender.

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The Colorado General Assembly has determined that market forces alone do not protect the public from potential insurance misuse and fraud. The complexity of the insurance market makes it difficult for the public to adequately protect itself without government regulations. Consequently, the DOI was formed to regulate the insurance industry. Its task is to provide oversight that protects the public from unstable insurance companies and illegitimate or questionable insurance products, with minimum interference to the insurance market. Overregulation will make it infeasible for insurance companies to operate in the state, and underregulation will leave consumers vulnerable to abuse. As a result of this dichotomy, regulation of the industry must maintain a delicate balance between encouraging competition and protecting the public.

The legislative declaration to the Colorado Insurance Code (§ 10-1-101, C.R.S.) acknowledges this theme by stating:

The General Assembly finds and declares that the purpose of this title is to promote the public welfare by regulating insurance to the end that insurance rates shall not be excessive, inadequate, or unfairly discriminatory, to give consumers thereof the greatest choice of policies at the most reasonable cost possible, to permit and encourage open competition between insurers on a sound financial basis, and to avoid regulation of insurance rates except under circumstances specifically authorized under the provisions of this title. Such policy requires that all persons having to do with insurance services to the public be at all times actuated by good faith in everything pertaining thereto, abstain from deceptive or misleading practices, and keep, observe, and practice the principles of law and equity in all matters pertaining to such business.

Under this declaration, the DOI is charged with “encourage(ing) open competition between insurers” while at the same time seeking to regulate in such a manner that insurance rates are not “excessive, inadequate, or unfairly discriminatory.” The bifurcated regulatory charge of the DOI creates a difficult balance to maintain. There is an inherent conflict between the roles of insurance consumer advocate and guarantor of insurance industry solvency.<sup>1</sup> DOI staff must balance the interests of the consumer and the industry, which at times can be difficult.

Under section 10-1-103(1), C.R.S., the DOI is charged with “the execution of the laws relating to insurance, and has a supervisory authority over the business of insurance in this state.”

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<sup>1</sup> Colorado State Auditor’s Office, Performance Audit of the Division of Insurance, 1989.

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Section 10-1-102(12), C.R.S., defines insurance as:

a contract whereby one, for consideration, undertakes to indemnify another or to pay a specified or ascertainable amount or benefit upon determinable risk contingencies, and includes annuities.

The DOI complies with its statutory duties through an elaborate regulatory process that provides oversight of the insurance industry through varying levels of monitoring. This monitoring helps ensure the dual role of responsibilities of the DOI to protect the public welfare and encourage open competition within the insurance industry.

The DOI is an agency within DORA. The Governor, with Senate confirmation, appoints the Commissioner of Insurance (Commissioner) to oversee the operations of the DOI. In 11 of the 55 states and territories, insurance commissioners are elected to their positions by the vote of the general public.<sup>2</sup> The Commissioner has broad responsibility and authority to enforce the insurance laws of Colorado.

In July 2001, the Commissioner established a 12-member advisory council, known as the Consumer Insurance Council (Council), as a forum to obtain consumer feedback on regulations and initiatives developed by the DOI. The Council discusses issues affecting consumers in Colorado related to health and life insurance. Meetings are held quarterly in the Denver-metro area.

To fulfill its stated mission of protecting the state's insurance customers, the DOI licenses and oversees the activities of Colorado's 66 domestic and 1,405 foreign insurance companies.<sup>3</sup> A foreign insurance company is one whose state of domicile is other than the state in which it does business.

The Commissioner has broad responsibility to enforce the insurance laws in Colorado. The Commissioner must maintain permanent records of administrative and rule-making proceedings and keep open records concerning the financial condition of regulated insurance companies; examine all requests and applications for licenses; and refuse to issue any license until the Commissioner is satisfied with the qualifications of the applicant.

The duty of the Commissioner is best summarized by section 10-1-108 (7), C.R.S., which states:

It is the duty and responsibility of the Commissioner to supervise the business of insurance in the state to assure that it is conducted in accordance with the laws of this state and in such a manner as to protect policyholders and the general public.

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<sup>2</sup> National Association of Insurance Commissioners, *2003 Insurance Department Resources Report*, p.2.

<sup>3</sup> National Association of Insurance Commissioners, *2004 Insurance Department Resources Report Questionnaire*, Part III, pgs. 2-4.

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The DOI indicates that it serves the public interest through the following areas of responsibilities:

- Provide a prompt and effective complaint resolution process for Colorado consumers.
- Provide prompt and effective service and education to Colorado consumers, the public, and regulated entities.
- Promote and preserve a sound, competitive insurance marketplace through effective state regulation.
- Promote access to affordable insurance that allows for adequate consumer choice.
- Promote and develop more streamlined, uniform, and efficient regulatory processes.
- Ensure that management systems are in place to operate the DOI efficiently and effectively.
- Provide resources, training, and support for DOI staff to promote and maintain a knowledgeable, dedicated, and productive workforce.

The DOI lists its basic program functions as follows:

- Consumer Affairs, which includes Life/Health Consumer Affairs, Property/Casualty Consumer Affairs, and Senior Consumer Services;
- Market Regulation, which includes Rates and Forms, Producer Licensing, Market Conduct, Market Analysis, and Investigations;
- Finance and Administration, which includes Financial Examinations, Financial Affairs, Corporate Affairs, Premium Tax Collection, Budget Services, and Actuarial; and
- Compliance.

### **National Association of Insurance Commissioners**

The National Association of Insurance Commissioners (NAIC) is an organization of insurance regulators from the 50 states, the District of Columbia, and the four U.S. territories. The NAIC provides a forum for the development of uniform policies and procedures when uniformity is considered necessary and appropriate.

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The stated mission of the NAIC is to assist state insurance regulators, individually and collectively, in serving the public interest and achieving the following fundamental insurance regulatory goals in a responsive, efficient and cost effective manner, consistent with the wishes of its members:

- Protect the public interest;
- Promote competitive markets;
- Facilitate the fair and equitable treatment of insurance institutions; and
- Support and improve state regulation of insurance

Under the McCarran-Ferguson Act of 1945, the authority of the federal government to regulate insurance was delegated to the states. The act provides that the federal government will not regulate the insurance industry if states choose to do it instead. Today, the states provide the primary regulation of the insurance industry. Consequently, most insurance companies must be licensed and are regulated by every state in which they do business, although primary financial oversight and examination responsibilities rest with the insurance commission of the state where the company is domiciled. The absence of federal oversight coupled with regulatory responsibility by the states created a need for a national presence to assist in coordinating state regulations and to promote communication among states to provide regulatory guidance to the insurance community. The NAIC is that national presence. Composed of state insurance regulators, this voluntary association helps coordinate regulatory activities and assists state officials in performing their tasks. Membership to the NAIC is automatic for all states, and every state actively participates.

In response to the insurance insolvency crisis in the late 1980s and a subsequent Congressional investigation, the NAIC developed national accreditation standards for state regulatory programs. A team of NAIC auditors reviews state programs to determine if the state meets the standards for accreditation. The NAIC accredits states that meet statutory and regulatory criteria and that maintain resources to enforce them. Colorado was one of the first states accredited when the program began in the early 1990s.

Colorado has a very strong presence in the NAIC. The Commissioner is a member of many committees and task forces including Examination Oversight, Consumer Participation Board of Trustees, Accident Health Insurance Committee, and the State and Federal Health Insurance Task Force. Additionally, other agency personnel within the DOI sit on various NAIC task forces and working groups that develop new guidelines for enforcement and regulatory oversight.

The DOI complies with its statutory duties through an elaborate regulatory process that provides oversight of the insurance industry through varying levels of monitoring. This monitoring helps ensure the dual role of responsibilities of the DOI to protect the public welfare and encourage open competition within the insurance industry.

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The DOI relies on NAIC tools to assist in its regulatory oversight of insurance companies. When applicable (i.e., not statutorily prohibited or not as strong as state requirements), the DOI adopts NAIC-proposed guidelines in an effort to maintain a high regulatory presence. Additionally, the NAIC provides various national databases that allow the DOI to monitor financial status and trends as well as complaints and enforcement actions against insurers.

The NAIC provides a number of on-line databases to assist states in identifying and communicating with other states about their regulatory actions and complaints against insurance companies and producers. State insurance regulators may use these databases to assist in claims handling, advertising and marketing, producer and company licensing, company management, and consumer information. For example, state regulators may prevent violators from obtaining licenses in multiple states by searching the databases prior to granting a license. Other databases report on complaints and activities of market conduct concerns. The following are a few of the databases provided to the states by the NAIC:

- Regulatory Information Retrieval System - contains the names of producers and companies that have been subject to formal regulatory or disciplinary action.
- Special Activities Database - contains firms and individuals that have had charges brought against them, have been the object of specific investigation, or have been reported to be involved in fraudulent, unlicensed, or unauthorized activity.
- Complaint Database System - consists of aggregated consumer complaint data from insurance departments.
- Producer Database - tracks information on all producers involved in the business of insurance.

Additionally, the NAIC provides financial monitoring assistance such as the Financial Analysis Workboards and the Examination Jumpstart program. In summary, NAIC provides valuable tools to help state regulators enforce insurance statutes. Ultimately, the health of the insurance industry and the effects on consumers lies squarely on the shoulders of the states. The NAIC has no direct regulatory authority over insurance companies. However, it disseminates information and provides support to states' regulatory programs. Due to each state's reliance upon the other to regulate the insurance industry, constant communication with each other is the only way that a program of this nature can be effective.

### **Key Regulatory Function - Inspections**

Insurance regulators are responsible for monitoring the solvency of all insurers doing business in their respective states. However, with the increasing number of companies licensed to do business in each state and the multistate nature of many insurance enterprises, it is efficient for regulators to focus primarily on those insurance companies domiciled in their respective states.

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Pursuant to NAIC directives, the primary responsibility for monitoring non-domiciliary companies (foreign and alien companies) is generally delegated to the domiciliary state's insurance regulators. The members of the NAIC have instituted an accreditation program to ensure that minimum standards of conduct are being followed by each state. In fact, more than 98 percent of financial examinations nationwide in 2003 were conducted by individual states on their own domestic insurers. The ability to rely on their counterparts across the country allows state regulators to more efficiently use their limited resources to protect insurance consumers. This also saves money for insurers because they are being subject to redundant examinations.

To monitor solvency and evaluate market conduct, state insurance departments examine insurance companies. Generally, companies are examined every three to five years. Special circumstances might warrant more frequent examinations of a specific company.

Desk audits and solvency monitoring aid regulators in targeting companies for special attention.

Company examinations are either single-state or multi-state in nature. Single state examinations are conducted by, and reports are filed with, one particular state or territory. Multi-state examinations are generally performed on companies doing a significant amount of business in more than one state. These examinations are called by the company's domiciliary state and the other states are given the opportunity to participate. Examination reports resulting from such an examination are filed and may be accepted by each participating state. More than one-half of the company examinations conducted each year are multi-state examinations.

Financial examinations investigate a company's accounting methods, procedures and financial statement presentations. These examinations verify and validate what is presented in the annual statement to ascertain whether the company is in good financial standing. The main thrust of these financial examinations is the verification of the company's general financial condition and solvency, and whether the company has complied with state laws and regulations. Improvements have been made in the examination process through increased examiner training, the use of specialized computer audit software, and enhancements to the NAIC's Examiner Handbook.

Statutory financial and market conduct examinations occur on a scheduled basis and cover every aspect related to the financial status or market conduct of the company.

Discretionary examinations are conducted when deemed necessary by the DOI. The examination may focus only on a specific area of concern, such as a company's investment portfolio or reinsurance agreements, or could be a complete financial or market conduct examination.

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## History of Regulation

Insurance regulation has been a matter of state concern since the U.S. Supreme Court decision Paul v. Virginia, 8 Wall. 168 (1869). The Supreme Court held that transactions in commerce did not include the issuance of insurance policies. Therefore, transactions in insurance would not fall under the Interstate Commerce Clause of the United States Constitution. As a result, insurance regulation became the responsibility of the states. Reacting to the Paul decision, several states, led by New York and Maryland, formalized insurance regulation by creating state regulatory agencies.

In 1944, the U.S. Supreme Court reversed Paul in U.S. v. South-Eastern Underwriters Association, 322 U.S. 533 (1944). The decision that insurance was commerce and therefore subject to interstate regulation by the federal government raised concerns in the insurance industry of a new federal bureaucracy. Congress responded to these concerns with the passage of the McCarran - Ferguson Act in 1945. This act acknowledged the authority of Congress to regulate insurance as interstate commerce. However, it recognized that each state already regulated insurance and that the exercise of federal power in this area was unnecessary. Under the McCarran - Ferguson Act, the federal government's authority to regulate insurance is held in abeyance as long as the states effectively regulate the industry.

Colorado began to regulate insurance through the State Auditor's Office in 1883. The Colorado Department of Insurance was formed in 1913, in response to widespread growth in the industry. In the mid-1960s, the Insurance Department became part of the Colorado Department of Regulatory Agencies (DORA) as the Division of Insurance (DOI). The head of the DOI is the Commissioner of Insurance, appointed by the Governor and confirmed by the Colorado Senate.

In 1999, the U.S. Congress enacted the Gramm-Leach-Bliley Act (GLBA) that repealed Depression-era restrictions against affiliations between banks, insurance companies and securities firms, while affirming the functional regulation of insurance by the states. The GLBA also contained provisions requiring the states to achieve reciprocity or uniformity as it relates to insurance producer licensing by November 12, 2002, or face the pre-emption of non-resident licensing by the National Association of Registered Agents and Brokers (NARAB). Since the passage of GLBA, the NAIC has focused on responding to the call for increased uniformity as it relates to the regulation of insurance by the states and in assisting states in meeting the deadlines established in GLBA as they relate to producer licensing and in creating the standards for uniformity in company and producer licensing.

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## **Legal Framework**

State statutes and Division of Insurance (DOI) regulations control the issuance of Certificates of Authority (COAs) to life/health companies in Colorado. Specifically, Title 10, Colorado Revised Statutes (C.R.S.), contains the statutory directives for the insurance industry in Colorado. Section 10-3-105, C.R.S., prohibits any foreign or domestic life or health insurance company from transacting business in Colorado unless the company first procures a COA from the Commissioner of Insurance (Commissioner) authorizing the company to do business in this state.

Section 10-1-108(1)(b), C.R.S., authorizes the Commissioner to issue COA to any insurance company that fully complies with the laws of Colorado. Pursuant to section 10-1-108(8), C.R.S., the Commissioner must examine all requests and applications from insurers for COA, and the Commissioner is authorized to refuse to issue any such COA until the Commissioner is reasonably satisfied as to the qualifications and general fitness of the insurer to comply with the provisions of Title 10, C.R.S.

The provisions of Title 10, Article 1, Part 2, C.R.S., are intended to enable the Commissioner to adopt a flexible system of examinations of insurance companies that utilizes DOI resources as may be deemed appropriate and necessary for the administration of the insurance laws of Colorado. An examination in this context, means a formal financial examination or market conduct examination, as well as an informal investigation performed by the Commissioner for the purpose of determining compliance with the law. Section 10-1-203, C.R.S., sets forth the scope and timing of said investigations, and section 10-1-204, C.R.S., delineates the guidelines and procedures to be followed by the DOI's examiners and the individual insurance companies at these examinations.

Article 3 of Title 10, C.R.S., controls the regulation of the Colorado insurance industry. This article sets forth criteria for the formation of insurance companies, general requirements for a COA, as well as delineating policies and procedures in dealing with insurance companies that may be financially unstable. Section 10-3-125, C.R.S., contains provisions authorizing the redomestication of foreign companies to Colorado, and section 10-3-126, C.R.S., allows alien companies to acquire a certificate to transact business in Colorado.

The grounds and procedure for the suspension or revocation of a COA can be found in section 10-1-110, C.R.S. Specifically, the COA may be suspended or revoked by the Commissioner for reasons that include, but are not limited to:

- (a) Insolvency or impairment, as defined in section 10-3-212, C.R.S.;
- (b) Failure to meet the requirements of section 10-3-201, C.R.S.;
- (c) Refusal or failure to submit an annual report, as required by section 10-3-109, C.R.S., or any other report required by law or by lawful order of the Commissioner;
- (d) Doing an unauthorized insurance business in another state, as set forth in section 10-1-117, C.R.S.;

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- (e) Failure to comply with the provisions of its own charter or bylaws, if such failure renders its operation hazardous to the public or to its policyholders;
  - (f) Failure to submit to examination or any legal obligation relative thereto;
  - (g) Refusal to pay the cost of examination, as authorized by law;
  - (h) Use of methods that, although not otherwise specifically proscribed by law, nevertheless render its operation hazardous, or its condition unsound, to the public or to its policyholders;
  - (i) Failure to otherwise comply with the law of this state, if such failure renders its operation hazardous to the public or to its policyholders;
  - (j) Use of practices or existence of conditions that render its financial position unsound to the public or its policyholders.

The Commissioner, pursuant to section 10-1-109, C.R.S., has the authority to establish or amend rules that are reasonably necessary to enable the DOI to effectuate the Commissioner's duties under the laws of Colorado. To this end, the DOI has promulgated numerous rules and regulations relating to the criteria for the issuance, denial, operation, suspension and revocation of COA for life and health insurance providers.

DOI Amended Regulation 2-1-7 is the DOI's primary regulation relating to the issuance of a COA. The purpose of this regulation is to delineate the standards for issuing COAs to transact insurance business in Colorado. This regulation can be found in its entirety in Appendix B on page 32. A summary of DOI Amended Regulation 2-1-7 is as follows:

- Applications for formation of domestic insurers, applications for entry into Colorado for foreign insurers, and applications for changes to existing authority must be submitted in a form prescribed by the Commissioner.
- Requires a sound business plan and adequate capital to support said plan, and adequate access to additional capital for all companies requesting a COA to transact business in Colorado. In addition, the applicant must demonstrate favorable liquidity, adequate reinsurance from companies authorized in Colorado, sound management, and stable revenue, earnings and surplus trends. Foreign companies seeking to transact business in Colorado must also demonstrate at least three years of favorable operating results.
- Sets forth the general financial standards for insurers at initial licensure and on an on-going basis. After a review of the applicant's company type and requested lines of business, the DOI determines the amount of capital and surplus necessary to conduct business in Colorado. An amount in excess of the statutory minimum capital and surplus is necessary at the time of licensure to ensure that the company has a sufficient cushion to absorb any surplus strain. Requires a company to maintain a surplus either at the amount required by statute or three times the authorized control level, based on the most recent annual risk based capital calculation, whichever is greater.

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- When the Commissioner has reason to question the adequacy of the available surplus of an applicant, the Commissioner may require an actuarial opinion and a surplus sufficiency report prior to licensure.
  - When reviewing requests to amend a COA, the Commissioner has the authority to determine whether the applicant has the necessary expertise, experience, and financial ability for continued licensure after the proposed modification or change.

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## **Program Description and Administration**

### **Certificates of Authority**

To ensure that only responsible and financially viable companies provide insurance to consumers, Colorado statutes require all entities providing insurance in Colorado become licensed through the acquisition of a state issued Certificate of Authority (COA). An insurance provider interested in offering its products in Colorado must apply to the Division of Insurance (DOI) for a license. The DOI, Corporate Affairs Section, reviews the application and conducts an extensive examination to verify and analyze the financial data submitted by the applicant. Due to the complexity of many applicants' financial condition, Corporate Affairs can enlist the services of other sections of the DOI, such as the Actuarial and Financial Affairs Sections to help determine whether an applicant meets the financial criteria for licensure. As a result of the submitted information and subsequent review by the Corporate Affairs Section, the DOI can approve or disapprove said application,

When the DOI approves an application, the insurance company is considered licensed and the DOI issues a COA. The issuance of a COA is the point at which the company is identified as falling under the regulatory authority of the Colorado DOI. Pursuant to statute, such companies are subject to taxes, fees, and financial and market conduct examinations.

To receive a COA, an insurance company must meet the capital and surplus requirements contained in the statute for the line(s) of business for which the company is seeking authorization, as well as the risk-based capital standards developed by the DOI in conformance with National Association of Insurance Commissioners- (NAIC) parameters. The application fee for all COA applicants is \$500 and is non-refundable. After licensure is granted, fees for health and life insurance companies are graduated based on the previous year's premium collections. Table 1 identifies the fees a life/health insurer holding a COA in Colorado would be required to pay to transact that identifiable volume of business pursuant to section 10-3-207(1), Colorado Revised Statutes (C.R.S.)

**Table 1**

#### **Annual Fees**

Prior year's direct written premiums in Colorado not exceeding \$1 million	\$670
Prior year's direct written premiums in Colorado in excess of \$1 million but not exceeding \$10 million	\$2,010
Prior year's direct written premiums in Colorado In excess of \$10 million	\$3,345

Source: Section 10-3-207, C.R.S.

In addition, insurance companies may be required to maintain deposits or surpluses with the Commissioner of Insurance (Commissioner) dependent upon the types of business they conduct. The Commissioner bases surplus requirements on formulas developed by the NAIC. Table 2 shows the minimum amounts of surpluses for various lines of business pursuant to section 10-3-201, C.R.S. However, pursuant to DOI Amended Regulation 2-1-7, an applicant may be required to maintain a surplus amount required by statute (Table 2), or three times the authorized control level based on the most recent annual risk based capital calculation, whichever is greater. Consequently, some companies may be required to maintain an amount in excess of the statutory level.

**Table 2**

**Capital/Guaranty Fund Plus Surplus Requirements**

Type of Company	Capital/Guaranty Fund Plus Surplus
Life/Health	\$1.5 million
Fire	\$1.5 million
Casualty	\$1.5 million
Multiple Line	\$2 million
Title	\$750,000

Source: Section 10-3-201(1)(a)(V), C.R.S.

Table 3 sets forth the statutory minimum capital and surplus requirements in Colorado and nine other states. As noted above, the risk based capital computation is generally higher than the statutory minimum amount, and consequently affords the public enhanced protection from possible financial problems or deficiencies.

**Table 3**

**Comparative States' Statutory Minimum Capital and Surplus Requirements**

State	Statutory Minimum Capital and Surplus Requirements
California	\$2.5 million
Colorado	\$1.5 million or Risk Based Capital Computation
Georgia	\$3 million
Iowa	\$5 million or Risk Based Capital Computation
Michigan	\$7.5 million
Montana	Life - \$600,000 Multiple Lines - \$1 million
Nevada	\$500,000 capital and \$1 million surplus
Ohio	\$2.5 million
Oregon	\$2.5 million capital or surplus
Texas	\$700,000 capital stock and \$700,000 surplus

Source: Compiled by the Office of Policy, Research and Regulatory Reform (OPRRR) from NAIC Data

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The DOI monitors insurance companies through periodic on-site examinations and off-site reviews of annual financial statements. Examinations determine whether insurance companies are financially sound and able to meet their financial obligations. In general, an examination involves reviewing the insurance company's financial records and operations, and summarizing this review in an examination report.

Nationally, the regulation of insurance companies is the responsibility of the individual states. As a result, each state has enacted laws to ensure the detection and prevention of insurance company solvency. For example, all states have laws that require minimum capital and surplus amounts. Using their respective statutory requirements, insurance departments in the various states conduct examinations to assess the companies' financial strength.

In addition to the surplus requirements set forth in Table 2 above, the DOI promulgated Amended Regulation 2-1-7 under the authority of section 10-1-109, C.R.S. This regulation pertains to the issuance of a COA to an insurance company and contains a provision granting the Commissioner authority to establish standards that require an insurer to maintain a surplus greater than the minimum statutory level. Pursuant to DOI Amended Regulation 2-1-7, an applicant may be required to maintain a surplus amount required by statute (Table 2), or three times the authorized control level based on the most recent annual risk based capital calculation, whichever is greater. Consequently, based on the amount and nature of the anticipated business transactions, some companies may be required to maintain an amount in excess of the minimum statutory level.

Section 5E of DOI Amended Regulation 2-1-7 also refers to an actuarial opinion, which provides an expert financial analysis, and is referred to by the DOI as a surplus sufficiency report. This review considers, among other things, whether a company has access to additional capital in the event that operations during the first year fail to meet expectations or result in a net loss. Sections 5B and 5D of DOI Amended Regulation 2-1-7 both make reference to the need for a Colorado domestic insurer having initial funding in excess of the statutory minimum, and having access to additional capital.

The Commissioner can assign examination staff or an individual supervisor to work with financially troubled companies. These individuals become responsible for the management and direct supervision of the financial activity of the company. Persons acting in this capacity oversee all management activity of the company.

One of the primary methods by which the DOI oversees the financial condition of insurance companies is through regular on-site examinations. Through this process, the DOI provides assurance to the public that funds set aside for the future will be available when needed.

Table 4 sets forth the number of domestic and foreign insurers in Colorado and nine other states, in the areas of health and life insurance. Colorado has a total of 19 health/life insurers domiciled in the state.

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**Table 4**

**Comparative States – Number of Domestic and Foreign Insurers**

State	Number of Domestic Insurers		Number of Foreign Insurers	
	Life/Health	Health	Life/Health	Health
California	28	-	469	-
Colorado	10	19	526	0
Georgia	20	11	526	0
Iowa	26	6	472	9
Michigan	19	44	456	0
Montana	3	5	526	0
Nevada	3	9	539	4
Ohio	41	134	527	3
Oregon	3	14	550	0
Texas	165	238	546	2

Source: Compiled by OPRRR from NAIC Data

**Uniform Certificate of Authority Application**

The Uniform Certificate of Authority Application (UCAA) process is designed to allow insurers to file copies of the same application for admission in all states. Every state now accepts the UCAA and consequently all states are designated as uniform states. While each uniform state still performs its own independent review of each application, the need to file different applications, in different formats, has been eliminated since all states now accept uniform applications.

The UCAA includes three applications, which have been drafted and endorsed by the NAIC. The Primary Application is for use by a newly formed company seeking a COA in its domicile state and by a company wishing to redomesticate to a uniform state. The Expansion Application is for use by a company in good standing in its state of domicile that wishes to expand its business into a uniform state. The Corporate Amendments Application is for use by an existing insurer for requesting amendments to its COA.

**Primary Applications**

The Primary Application to the UCAA is designed for use in the formation of a new insurer, or by an existing insurer that is making application to redomesticate to another state. Uniform states are committed to using the UCAA review process for company licensing and admissions. Primary Applications are also required for alien insurers who have not previously acquired a COA from another state. Alien insurers are insurers formed under the laws of a country other than the United States, (§ 10-3-301(1), C.R.S.) The DOI conducts an extensive financial review of all companies submitting a Primary Application.

As part of the Primary Application process, the DOI reviews the corporate applicant's bylaws, articles of incorporation, proposed plan of operation, in addition to a biographical and background check of all officers and board members of the applicants.

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## **Forms required for Primary Certificate of Authority Applications**

1. Application Form and Attachments
2. Filing Fee
3. Minimum Capital and Surplus Requirements
4. Statutory Deposit Requirements
5. Name Approval
6. Plan of Operation
7. Holding Company Form "B" Registration Statement
8. Statutory Membership(s)
9. U.S. Securities and Exchange Commission Filings or Consolidated Financial Statement that complies with Generally Accepted Accounting Principles
10. Debt-to-Equity Ratio Statement
11. Custody Agreements
12. Public Records Package
13. NAIC Biographical Affidavits
14. State-Specific Information

## **Expansion Application**

The Expansion Application is generally used by an insurer who wishes to offer insurance in a state other than its state of domicile. State-specific regulations in Colorado require that foreign applicants seeking to redomesticate in Colorado must demonstrate favorable liquidity, adequate reinsurance from companies authorized in this state, sound management, at least three years of favorable operating results, and stable revenue, earnings and surplus trends.

The Expansion Application must show that the applicant meets the state's statutory minimum capital and surplus requirements, and the applicant must submit an explanation of the applicant's compliance with the capital and surplus. In Colorado and most states, the minimum capital and surplus requirements are determined by the classes of insurance that the applicant is requesting authority to transact, and the classes of insurance the applicant is authorized to transact in all other jurisdictions. Each individual state determines the level of capital and surplus required to issue a COA after considering, among other items, the applicant's product line, operating record and financial condition. Therefore, compliance with the statutorily prescribed minimum surplus requirement may not be sufficient for all applicants.

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The Expansion Application to the UCAA is for use by an insurer who wishes to expand into one or more states. Expansion Applications may be filed simultaneously in as many states as desired. This process is relatively uniform as all states are committed to using the UCAA review process for company admissions.

The Expansion Application is an abbreviated version of the Primary Application and is designed to allow solidly performing companies that are in good standing in all admitted states to quickly and easily gain admission into new states. Pursuant to NAIC directives, it is the goal of all states to complete their reviews of Expansion Applications within 60 calendar days of receipt. The 60-day review process includes two weeks to determine if the application is complete and acceptable. During the remaining 45-60 day time-span, the application should receive a financial and operational review. The 60-day processing goal may not be achieved in instances where substantial follow-up is required, in states with limited resources, or in instances when applications are filed during peak business periods such as year-end and annual statement filing periods.

Based on the circumstances of a particular application, it may be necessary for the reviewing state to request additional information.

### **Corporate Amendments Application**

The UCAA Corporate Amendments Application is designed for use by an existing insurer for requesting amendments to its COA. This category of insurer has previously received a COA, and must utilize this application to notify and acquire approval for any change or modification to the underlying information that was submitted in the original Primary or Expansion Applications. This modification or change may be of minor importance, such as a change of street address, or of major importance, such as a merger or modification of the company's by-laws.

The UCAA Corporate Amendments Application can be used to file more than one change in the same submission.

Each state's review process may follow slightly different time lines to complete a comprehensive and detailed operational and financial review of the applicant's modification. As with the Expansion Application, it is the goal of all states to complete their reviews of Corporate Amendments Applications within 60 calendar days of receipt. The 60-day review process includes two weeks to determine if the application is complete and acceptable for filing. During the remaining time-span, the application will receive a financial and operational review. The 60-day processing goal may not be achieved in instances where substantial follow-up is required, in states with limited resources, or in instances when applications are filed during peak business periods such as year-end and annual statement filing periods.

Based on the circumstances of a particular application, it may be necessary for the reviewing state to request additional information. Typically, any additional information that is needed will be requested within 30 days after the application is accepted.

Table 5 sets forth the number of applications for COA from health and life insurers received by the DOI, Corporate Affairs Section. Table 5 contains separate sections for each of the three NAIC applications, Primary, Expansion, and Corporate Amendments.

The figures indicate that although little activity has occurred in the area of Primary Applications, 19 life insurance companies expanded their insurance businesses into Colorado during the five-year period ending in 2004. Table 5 shows the activity surrounding the applications for COAs for calendar years 2000 through 2004. See Appendix C on page 36 for a listing of specific COA applications received but not approved between the years 2000 through 2004

**Table 5**

**DOI Certificate of Authority Activity**  
1/1/2000 - 12/31/2004

<b>PRIMARY APPLICATIONS</b>					
(Domestic companies initial application for Certificate of Authority)					
	<b>2000</b>	<b>2001</b>	<b>2002</b>	<b>2003</b>	<b>2004</b>
<b>Approved</b>					
Life	0	0	0	0	0
Health	0	0	0	0	0
<b>Withdrawn/Denied/Incomplete</b>					
Life	0	0	0	0	1
Health	0	0	0	0	0
<b>EXPANSION APPLICATIONS</b>					
(Foreign companies initial application for Certificate of Authority)					
	<b>2000</b>	<b>2001</b>	<b>2002</b>	<b>2003</b>	<b>2004</b>
<b>Approved</b>					
Life	2	5	4	2	6
Health	2	0	0	0	0
<b>Withdrawn/Denied/Incomplete</b>					
Life	2	4	2	4	1
Health	0	0	0	0	0
<b>CORPORATE AMENDMENTS</b>					
(Changes to Certificates of Authority for domestic and foreign companies)					
	<b>2000</b>	<b>2001</b>	<b>2002</b>	<b>2003</b>	<b>2004</b>
<b>Approved</b>					
Life	57	138	23	23	53
Health	0	0	0	0	0
<b>Withdrawn/Denied/Incomplete</b>					
Life	2	3	1	0	0
Health	0	0	0	0	0

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## **Operations Related to Certificates of Authority**

Since 1990, the DOI has been organized according to three key functions: Administration, Consumer Affairs, and Financial Regulation. The overall day-to-day supervision of the DOI is the responsibility of the Deputy Commissioner. Two Assistant Commissioners supervise the financial and consumer areas, which are further subdivided into sections. The major organizational units that comprise the Finance and Administration subdivision include financial affairs, financial examination, corporate affairs, actuarial, and premium tax collection. These sections of the DOI are mostly responsible for the granting, denial, monitoring, supervision, suspension, revocation or other discipline or oversight of companies holding a Colorado-issued COA. The Market Conduct section also contributes to the monitoring of health/life insurance companies after they acquire a COA.

### **Corporate Affairs Section**

The Corporate Affairs Section is responsible for performing pre-licensure reviews of the financial viability and statutory compliance of all new domestic and foreign entities regulated by DOI. Specifically, Corporate Affairs staff determines whether insurance companies meet the statutory and financial criteria to operate in Colorado. This process includes an actuarial review to determine if the company complies with the financial requirements outlined in the statutes and DOI regulations to conduct business in Colorado. A distinction is made between domestic and foreign applications, with a more thorough review performed on domestic companies. However, foreign companies generally have to provide additional experience documentation indicating at least three years of favorable operating results in the states in which they operate.

The Corporate Affairs Section recently assumed the responsibility of monitoring foreign insurers' financial solvency. These reviews are performed on a priority basis for those companies determined to have high-risk financial profiles.

Statutory financial criteria and capital surplus requirements vary based on the lines of insurance requested, and the amount and character of the intended scope of business. The Corporate Affairs Section reviews risk-based capital requirements with life and health insurance company applicants when determining whether they have met financial thresholds to operate in Colorado. Risk based capital (RBC) is an extensive review and analysis of the minimum capital and surplus amounts required to be maintained by licensed insurers in Colorado. RBC standards provide for the early detection of a potentially hazardous or otherwise dangerous condition of a life/health insurer or health organization in order to protect its insured, enrollees, members, and the general public. RBC directives are codified in DOI Regulation 3-1-11, which additionally provides for reporting, corrective measures, and enforcement actions.

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Corporate Affairs also reviews corporate changes, such as management changes, and corporate activities such as mergers and acquisitions. The intent of these reviews is to ensure that the company is still able to meet Colorado's requirements after the corporate modification. Additionally, Corporate Affairs evaluates reinsurance arrangements between companies licensed in Colorado. Generally, reinsurance is an activity whereby an insurance company transfers or assigns risk to another company. This frees up company reserves and allows the company to sell more insurance. Insurance regulation requires strict standards for reinsurance to reduce the possibility that a reinsurance company does not have the financial ability to pay the assumed claims.

Corporate Affairs reviews encompass the traditional life and health insurance companies as well as non-traditional insurance entities. This section reviews all non-traditional entities annually to assure that each meets minimum financial solvency and compliance requirements. Non-traditional entities include government pools, captive insurers, preneed funeral sellers, motor vehicle self-insurance plans, medical malpractice coverage plans, and managed care entities (such as limited service licensed provider networks, and prepaid dental plans).

The Corporate Affairs Section also reviews annual applications for regional home office eligibility and the financial solvency and compliance of approved surplus line carriers, non-admitted reinsurers, and alien (non U.S.) insurers. In addition, the section also maintains the ongoing accuracy of the DOI's company Fines, Regulatory Actions, Etc. Database (FRED). This includes daily maintenance for corporate changes such as name changes, foreign insurer redomestications, mergers, changes of control for licensed insurers, and address changes of all companies. This section also registers risk retention groups and purchasing groups, and monitors liquidations and transfers of business between insurers.

Companies may also sell insurance in Colorado as authorized but unlicensed companies. This usually occurs with a company that sells only surplus line insurance or a single specialty insurance product, such as environmental liability, or professional malpractice insurance not available through a licensed company. Authorized but unlicensed companies are subject to a thorough financial review and these entities are required to maintain a significantly higher amount of capital surplus than required of licensed companies.

### **Financial Affairs Section**

The essential function of the Financial Affairs Section is to preserve a safe and sound insurance marketplace for Colorado policyholders through review and analysis of financial statements and other required filings made with the DOI pursuant to the requirements of sections 10-3-201, *et seq.* and 10-3-801, *et seq.* C.R.S. More specifically, the Financial Affairs Section has the overall responsibility for monitoring, through the Financial Analysis System, the financial solvency of the 51 Colorado domiciled companies. The Financial Analysis System is designed to monitor a variety of licensed entities including life, accident and health, multiple-line, casualty, county mutual, fraternal, health maintenance organization, non-profit hospital, medical-surgical, and health service corporations, title, and quasi-state agencies such as the CoverColorado and Pinnacol Assurance Company (formerly the Colorado Compensation Insurance Authority).

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A key objective of the Financial Affairs Section is to detect errors in financial reporting, solvency concerns, or negative financial trends affecting domestic insurers. Once errors or solvency issues are identified, the Financial Affairs Section addresses the issues with the company, obtain a corrective plan, assesses the feasibility of the plan, monitors the company's compliance with the corrective plan, and recommends appropriate regulatory action to the Commissioner.

The Financial Affairs Section utilizes automated programs developed by the NAIC to monitor the financial condition of its domestic companies. These programs include trending and other analytical documents compiled by the NAIC, as well as audit programs that are utilized as part of the analysis of the financial filings reviewed by the Financial Affairs Section.

The NAIC establishes standards that the Financial Affairs Section must follow in fulfilling its financial solvency monitoring duties for the State of Colorado. The NAIC sets forth these standards as part of determining if a state will be considered an accredited state. The accreditation program was established to ensure uniformity of laws and solvency monitoring techniques between all the states. To be an accredited state, the state must meet the minimum requirements that cover the area of model laws, the Financial Examination Section and the Financial Affairs Section. To remain an accredited state, each state must annually complete a self-audit, answering a series of questions that demonstrate that the state continues to meet the minimum qualifications for NAIC-accreditation. Every five years, the NAIC sends a team of accreditation auditors to review the state's laws and examination and analysis oversight functions. If a state passes this audit, it is re-accredited for another five-year period.

### **Financial Examinations Section**

The Financial Examinations Section is responsible for conducting financial condition examinations (audits) of Colorado domestic insurers. Financial condition examinations are conducted to protect the public interest by:

- Detecting, as early as possible, those insurers with potential financial troubles;
- Assessing the financial condition and operating practices of insurers to determine compliance with applicable statutes, regulations and statutory accounting principles;
- Compiling information/documentation needed for timely, appropriate regulatory action; and
- Monitoring regulatory actions against insurers that are financially troubled or otherwise hazardous to the public.

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Once a company receives approval from the Corporate Affairs Section and begins to operate in the state, the Financial Examinations Section will perform periodic examinations to determine compliance with state statutes. There are 11 FTE within the Financial Examinations Section: one chief examiner, nine financial examiners, and one information systems (IS) auditor. Most of the examiners are Colorado certified public accountants or have earned the designation of Accredited Financial Examiner or Certified Financial Examiner through the National Society of Financial Examiners. The fluctuation in number of examinations per year is related to the size of the companies being examined. The DOI provides companies notice prior to an examination. This notice is followed by a request for documents from the examiner in charge.

An examination consists of an audit of the insurance company's operations and financial records. DOI personnel will review financial statements, transactional information, management information, and claims information, as well as corporate charters and bylaws to ensure that the company is in compliance with all statutory requirements and fiduciary duties. Additionally, the examination will look at other factors in order to identify potential solvency problems such as whether the company is paying its claims. The examination is also important because it checks the accuracy of the annual statement that is relied upon by the DOI to provide yearly monitoring of the insurance company. DOI conducts financial examinations using procedures in the Colorado Examiners Handbook, which include all NAIC guidelines for conducting an examination.

Depending upon statutory requirements and assessed risk, the Financial Examinations Section conducts financial condition examinations of commercial life and health insurers; usually once every three to five years; however, examinations may be conducted on a more frequent basis. The focus of the unit is primarily on domestic insurance companies, as foreign companies are required to be examined by their respective states of domicile. Reports of examination, including those produced by the DOI, are shared between the various state regulators and used for regulatory purposes.

The DOI has the authority to take regulatory action against insurers based upon the findings of the financial condition examinations. Examples of regulatory actions, which may be taken by the DOI include:

- Assess penalties relating to the examination findings – section 10-1-205, C.R.S.
- Require corrective action plans (e.g., Plan of Abatement or Risk Based Capital Plan) – section 10-1-205, C.R.S., DOI Regulations 3-1-7 and 3-1-11.
- Place a company under supervision – section 10-3-405, C.R.S.
- Place a company under receivership/conservatorship – section 10-3-512, C.R.S.
- Place a company under liquidation – section 10-3-516, C.R.S.

Examination procedures, guidelines and practices are prescribed by the NAIC and are contained in the NAIC Examiners' Handbook and NAIC Accreditation Program. All financial examination reports are public documents, accessible through the DOI's website. Tables 6 and 7 indicate the number of examinations conducted by the Financial Affairs Section, as well as the number of annual statements received and analyzed by the DOI.

**Table 6**

**Financial Examinations**

<b>Financial Examinations</b>	<b>Actual FY 03-04</b>	<b>Actual FY 04-05</b>
Financial Examinations Conducted		
Target	13	10
Actual	12	8

**Table 7**

**Financial Monitoring**

<b>Financial and Corporate Affairs</b>	<b>Actual FY 03-04</b>	<b>Actual FY 04-05</b>
Annual Financial Statements Received		
Target	1,450	1,450
Actual	1,443	1,455
Domestic Annual Financial Statements Analyzed		
Target	57	51
Actual	51*	51
Troubled Company Monitoring, Foreign		
Target	100	100
Actual	90	66

\*Six companies redomesticated, ceased operations or were merged out during FY 03-04.

**Actuarial Section**

The Actuarial Section is involved in the regulation of life and health insurers, as well as health maintenance organizations, pools, captives, and limited service licensed provider networks. The DOI's actuaries provide a broad range of services, which generally mirror those found in the insurance industry. This section serves as a DOI resource when it comes to numerical and financial analyses. The unit supports the DOI objective of assuring the adequacy of licensee reserves and appropriateness of rates. In addition, the Actuarial Section evaluates innovations in product design and corporate actuarial systems. The unit promotes uniformity of actuarial standards and regulation, unless uniformity is contrary to the interests of Colorado policyholders.

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The Actuarial Section provides review and analysis of targeted rate and other filings; participates in financial and market conduct examinations and/or arranges for and supervises the actuarial consultants on those examinations; regulates the actuarial requirements of insurers and non-traditional insurers; provides development or analysis of current and proposed regulations, legislation and NAIC models; provides analysis and review of filings and issues related to medical financial responsibility, reinsurance, corporate changes (including licensure), multiple employer welfare associations and other financial and corporate issues; provides review of referred consumer complaints; provides actuarial support to other sections of the DOI; addresses actuarial or statistical questions and concerns from the general public, industry, other regulators or national organizations; provides support and training for, and enhancements to, the DOI's integrated data base; and coordinates and monitors data transmissions.

The Actuarial Section's primary customers are internal to DOI. Major tasks performed for other DOI sections include review of rate filings for the Rates and Forms Section, participation or coordination in domestic financial examinations for the Financial Examinations Section, report and actuarial review for the Financial Affairs Section, actuarial aspects of admissions/expansions and reinsurance for the Corporate Affairs Section, participation in examinations for the Market Conduct Section, and analysis of complaints for the Consumer Affairs Section.

Outside stakeholders may include domestic and foreign insurers, consulting actuaries, and the general public. The Actuarial Section also participates in surveys and studies, and NAIC actuarial issue identification and problem solving.

### **Market Conduct Section**

The Market Conduct Section assists DOI in its oversight of Colorado's insurance industry. This is accomplished by means of market conduct examinations of insurance carriers. The overall purpose of market conduct examinations is to ensure that insurance carriers are operating within the parameters of Colorado law to ensure consumers and providers receive equitable treatment, services, and benefits from insurance carriers.

Market conduct examinations are periodic reviews of an insurance company's operational procedures, claims and underwriting practices, conducted either by DOI staff or contract employees. Examinations are conducted in accordance with procedures developed by DOI, based on model procedures developed by the NAIC. Examinations typically include on-site visits, and may involve considerable periods of time. An examination may involve a review of management and administrative controls, the COA, board of directors meeting minutes, internal/external auditing functions, record retention, and provider contracts. The conclusions and findings of examinations are public records.

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## **Rates and Forms Section**

The Rates and Forms Section has the primary responsibility for processing and maintaining policy form and rate filings as required by statute. The section reviews such filings in depth for compliance prior to issuance. For most lines of insurance subject to “file and use” or “certification” requirements under the statute, the section is responsible for receiving filings or certifications and performing targeted reviews (or desk audits) to verify that policy forms issued by the company comply with statute. Another primary duty of the section is to process and maintain rate filings and to perform reviews as necessary. This oversight function is important to consumers, since most rates are “file and use” (companies may simultaneously use the rates, when they have been filed with the DOI). Rate filings with significant consumer impact are selected for review upon receipt. The section also performs targeted desk audits of rate filings for selected product lines, domestic companies and companies with significant market share in the state. A database is maintained to track all rate and policy form filings received and to ensure compliance with statutory and regulatory timeliness standards.

## **Selection of Companies for Examination**

Each year the DOI identifies and selects a number of domestic companies to be examined, based on established factors.<sup>4</sup>

The DOI documents the rationale used to select insurance companies identified for financial examinations. For example, the DOI may not select a company identified by the NAIC as being a high priority for examination because that company is already operating under a state-appointed outside supervisor who monitors the company’s financial status on a continual basis. In another situation, the DOI may not select a certain company but prefer to wait and conduct simultaneous examinations with other companies that offer the same line of insurance with similarly identified concerns about reserves, unearned premium, and premium accounting. This simultaneous examination facilitates the identification and consistent treatment of issues unique to these companies.

Costs of the examination for domestic companies headquartered in the state are covered by the premium tax imposed on all insurance companies licensed in the state. If the domestic insurance company is not headquartered in the state or does not pay premium taxes, the insurance company must reimburse DOI for the financial examination. There are approximately 20 companies domiciled in Colorado but not headquartered in the state. When DOI participates in the financial examination of a foreign insurer operating in the state of Colorado, the company must reimburse DOI for the cost of the examination.

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<sup>4</sup> For example, the DOI uses the following factors:

- A. Any company identified by the DOI as high-priority. Companies identified by the NAIC early warning system and the NAIC Examiner Team as needing immediate regulatory attention and concurred with by the DOI.
- B. Companies selected based on negative reports from the Financial Examinations and Actuarial Sections as well as consideration of each entity’s financial condition, risk-based capital, and surplus, results from prior examinations, and changes in operations and/or management.
- C. Examinations required by statute.

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The financial examination team identifies operational and financial issues in a report. The DOI issues a draft of the report to the insurance company to allow the company to make written comments with respect to any issues identified in the report. After reviewing written comments and reviewing the report, the Commissioner issues an order which:

- Adopts the report as filed or with specific modifications. If the report identifies statutory noncompliance, the company is ordered to take corrective action to cure the violation;
- Rejects the report and directs the examiners to reopen the examination for the purpose of obtaining additional information and refile the report; or
- Calls for an investigatory hearing for purposes of obtaining additional data or information.

Commissioner orders are considered final agency decisions and are served upon the company along with the final report. A review of the decision may be sought by the company in Denver District Court. The reports become public records 30 days after the issuance of the Commissioner's order. Within 60 days after the issuance of the order, the company's directors are required to file affidavits stating they have received a copy of the adopted report and related order.

The DOI has no punitive authority to fine a company that has been in violation of a statute, nor may it formally require that corrective action be taken by a specific date. The DOI's leverage lies with its ability to issue an order placing the company under supervision or receivership, depending on the severity of noncompliance.

### **Corrective Actions**

Once a company has been identified as a "troubled company," the DOI may take a number of actions to protect the public. Regulatory actions taken against insurers by the DOI vary depending upon severity of the problem and whether the company is domestic or foreign. All remedies under law apply to all insurers doing business in Colorado.

Regulatory actions taken upon domestic insurers generally constitute special monitoring activities, prohibiting a domestic insurer from selling new business, placing the insurer under a DOI order of supervision, or placing the insurer into receivership through court proceedings for rehabilitation or liquidation.

Regulatory actions taken upon foreign insurers constitute special monitoring activities, prohibiting the insurer from selling new business through an informal "no sales" agreement, or an order of suspension. When a foreign insurer is placed into receivership by the domiciliary state, the DOI will issue an order of suspension upon the insurer.

Other actions are designed to rehabilitate the company. Some rehabilitation activities closely monitor the insurance company, and the DOI may require special reporting requirements. The Financial Affairs Section monitors all reports to ensure that the insurance company does not become incapable of meeting its financial obligations. Other rehabilitative actions may require supervision of the company by an outside person until it becomes financially sound. If the company is severely financially handicapped, the DOI may place the insurance company into receivership. Should this action occur, the DOI takes control of the company in an attempt to rehabilitate the company. If the company cannot be rehabilitated, the company's books of business may be sold or its assets may be liquidated.

If the examination reveals a financial condition that could jeopardize policyholders, the Commissioner has several regulatory options. The Commissioner may order closer monitoring of the company, including increasing the frequency of either financial reports or examinations. The Commissioner could also place the company under supervision, in which case the Commissioner would select an outside insurance or financial executive to serve as the chief executive officer under a supervision order. In extreme situations, the Commissioner can place the company into receivership until it either recovers or is liquidated. In each of these situations, oversight for the company is the responsibility of the Financial Affairs Section. Table 8 delineates the number of serious actions taken against COAs by different states in 2003. A company that is suspended will sometimes be unable to resolve its financial woes and consequently loses its COA by revocation.

**Table 8**

**Actions Taken Against Certificates of Authority - 2003**

State	Actions Taken Against Certificates of Authority	
	Suspended	Revoked
California	0	0
Colorado	6	0
Georgia	5	0
Iowa	4	0
Michigan	0	8
Montana	12	0
Nevada	8	14
Ohio	20	18
Oregon	9	0
Texas	1	1

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## **Analysis and Recommendations**

*Recommendation 1 – Continue the Division of Insurance’s function of the issuance, monitoring, oversight, and discipline of the Certificates of Authority of health and life insurance companies doing business in Colorado.*

The primary sunset analysis examines whether regulation (in this case the functions of issuing certificates of authority (COAs) to insurance companies) is necessary to protect the public. As this review has demonstrated, the issuance of a COA to conduct business in Colorado revolves around the ability of the applicant insurance company to demonstrate compliance with Colorado’s financial criteria (such as risk based capital requirements). Other requirements, such as the requirement for a sound business plan, further protect the public beyond the financial requirements.

One need simply analyze at the margin the removal of this state oversight function to conclude the necessity for continuation. In a market with no regulated point of entry, insurance companies would be free to commence business with no ability to pay claims. Insureds, then, could be left with legal action as the only option to receive payment for claims.

The next level of analysis required by the sunset criteria examines changes to the conditions which led to regulation and, given current conditions, asks should state regulation be more, less, or the same as the initial regulation.

This review points out that insurance regulation in Colorado dates back to 1883. There can be no serious argument that the conditions that led to regulation have changed somewhat. Although the essential role of government regulation of the insurance industry then and now is strikingly similar, it is much greater in scope in 2005.

This sunset review finds no compelling evidence supporting any significant change in the level of regulation related to the function of the issuance of COAs. This review has pointed out that the Colorado Division of Insurance’s (DOI’s) issuance of a COA is based upon compliance with statutory standards, as well as in conformance with certain parameters of the National Association of Insurance Commissioners (NAIC).

Nationwide, there has been some criticism of state insurance regulation and a move by the insurance industry to create a dual regulatory system similar to the current banking regulation scheme. One of the major complaints of the industry is the red tape and time delay in getting new products approved by regulators. In terms of this sunset review, which essentially examines the process of company licensing, proponents of federal regulation concede that the NAIC model is efficient and effective if states agree to use that model.

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The DOI does employ the NAIC model and DOI staff contributed to the development of the model. One can reasonably conclude from the DOI's adherence to the NAIC model, touted as the necessary reform to the company licensing question, that the agency meets its sunset burden of proof vis-à-vis statutory criteria examining agency efficiency and effectiveness.

To further that conclusion, representatives of the insurance industry interviewed in the conduct of this review reported general satisfaction with Colorado's COA process.

Although many aspects of this function are guided or delineated by the NAIC, some important issues relating to COAs are within Colorado's discretion. The process of deciding whether to issue a COA to an insurer is one of the most compelling responsibilities of the DOI.

Colorado has the duty to ensure that new insurance companies meet or exceed the criteria for the issuance of a COA. The DOI must ensure that insurance companies have and maintain sufficient capital and surplus to conduct business, and be financially prepared in the event that the expected or anticipated business venture fails to meet projections.

Colorado's DOI must ensure that applicant insurance companies meet all statutory and financial criteria, including risk-based capital requirements and financial reviews, in dealing in the oversight of merger or acquisition situations. Corporate changes require a careful and thorough review to ensure that the applicant is able to meet Colorado's statutory requirements after the corporate modifications. Pursuant to this function, the DOI is responsible for the determination of whether an applicant possesses the necessary experience, expertise, and management skills to conduct the nature and quantity of business that was requested in the COA application.

In conclusion, the DOI's issuance of COAs function meets the statutory burden of proof for sunset review.

*Recommendation 2 – Amend scope of future Division of Insurance sunset reviews.*

This review is the first of a series of reviews of the DOI by function, rather than a review of the DOI as a whole. The purpose of the bifurcation was to focus the reviews and generate a more useful product to inform legislative oversight.

Unfortunately, the opposite has occurred. In the instant case, references to COAs appear in almost 90 statutory provisions, and, while the administration of the function is fairly well contained within one section of the DOI, the administration of the activity is so restricted and so tied to NAIC standards as to render a sunset review too narrow to be of use in the legislative oversight process.

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In order to effectuate an improved cycle of DOI reviews, the following amendments to section 24-34-104, Colorado Revised Statutes (C.R.S.), should be made:

2007 - Add sunset review of the regulation of life insurance by the Colorado Division of Insurance;

2010 - Amend section 24-34-104(41)(n), C.R.S., to include sunset review of the regulation of property and casualty insurance (Strike existing language); and

2012 - Add sunset review of the regulation of health care coverage by the Division of Insurance.

*Recommendation 3 – Track data regarding the Uniform Certificate of Authority Application process.*

Table 5 on page 18 shows basic activity of the DOI around issuance of COAs as regards Primary Applications, Expansion Applications and Corporate Amendments Applications.

Because Colorado participates in the Uniform Certificate of Authority Application process, it is valuable to know if the DOI is complying with the terms of the uniform process. This uniform process is partially a response to the complaints of insurance companies nationwide for more streamlined, reciprocal regulatory processes. One of the primary metrics of the uniform process is adherence to established deadlines for evaluating, approving, and denying applications.

The DOI's compliance with the Uniform Certificate of Authority Application process is also important in relation to possible legislation, known as the State Modernization and Regulatory Transparency Act (SMART Act). The SMART Act would preempt state regulatory authority over insurance. Therefore, policymakers may find it beneficial to have information to determine if preemption is appropriate.

The DOI does not track this information although it can be retrieved from files on a company-by-company basis. The DOI regulatory process could be improved by accurately tracking all aspects of the COA application process. This data could effectively be used to monitor compliance with NAIC standards as well as for comparison with other states relating to areas for improvement.

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## **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.

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## **Appendix B – DOI Amended Regulation 2-1-7**

### **Amended Regulation 2-1-7**

#### **CONCERNING ISSUANCE OF A CERTIFICATE OF AUTHORITY**

Section 1	Authority
Section 2	Background And Purpose
Section 3	Scope
Section 4	Application By Foreign Insurers
Section 5	Formation Of A Colorado Domestic Insurer
Section 6	Change To Existing Authority
Section 7	Reinstatement Of Suspended Authority
Section 8	Confidentiality
Section 9	Severability
Section 10	Effective Date
Section 11	History

#### **Section 1 Authority**

This regulation is promulgated under the authority of §§10-1-109 and 10-14-505, C.R.S.

#### **Section 2 Background And Purpose**

The purpose of this regulation is to clarify the standards for issuing certificates of authority to transact insurance business in Colorado to insurers, fraternal benefit societies and interinsurance exchanges.

#### **Section 3 Scope**

This regulation applies to any company seeking a Certificate of Authority as a property, casualty, multiple line, life or title insurer, fraternal benefit society or interinsurance exchange, or any such company seeking to add lines to its current certificate of authority, redomesticate, change its name or otherwise amend its Certificate of Authority.

#### **Section 4 Application By Foreign Insurers**

A. Any foreign company seeking a Certificate of Authority in Colorado as an insurer, fraternal benefit society, or interinsurance exchange shall submit an application, in a form prescribed by the Commissioner.

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B. An applicant's capital and surplus must meet or exceed the minimum required by Colorado statute. Section 10-3-201, C.R.S. establishes the minimum amount of capital and surplus for each company type. The Division will review both the applicant's company type as determined by its state of domicile and the lines of business that it currently writes. The Division will determine the minimum required under each of these scenarios and apply the greater of the two amounts. For example, an insurer licensed as a multiple line carrier by its state of domicile, which currently only writes casualty lines of business as defined by a Colorado certificate of authority, would be considered a multiple line carrier in Colorado. As such the company would need to meet the capital and surplus requirement for a multiple line company.

C. If the company's operation is predominately that of a reinsurer, such as where 50% or more of its operation measured by premium, underwriting or reserves is reinsurance, the surplus requirements of a reinsurer pursuant to § 10-3-118, C.R.S. must be met.

D. The applicant must demonstrate the ability to maintain the minimum level at the time of initial licensure and on an on-going basis. This includes the ability to fund for product development and for other causes of surplus strain resulting from increasing business writings or new business ventures. An amount in excess of the statutory minimum capital and surplus is necessary at the time of licensure to ensure that the company has a sufficient cushion to absorb any surplus strain. Generally, the applicant should have three (3) times the authorized control level based on the most recent annual risk based capital calculation.

E. The applicant must have a sound business plan, sufficient capital to support the plan, and adequate access to additional capital. In addition, the applicant must also demonstrate favorable liquidity, adequate reinsurance from companies authorized in this state, sound management, at least three years of favorable operating results, and stable revenue, earnings and surplus trends.

F. The commissioner may, at his or her discretion, require an actuarial opinion and a surplus sufficiency report prior to licensure or at any time after licensure when the commissioner believes that there is a need to review the adequacy of the available surplus with respect to the types of assets and writings of the company.

G. A company seeking licensure must be authorized by its domiciliary state to write the lines of insurance being requested and demonstrate that it possesses the expertise necessary to write and service such insurance. An applicant who is increasing its market to include new products is also required to demonstrate the necessary expertise. The commissioner may waive this requirement if the company is affiliated with a company licensed in Colorado that writes the same type of insurance being requested. An applicant may be required to provide a guaranty on a form prescribed by the commissioner, to maintain surplus either at the amount required by statute or three (3) times the authorized control level based on the most recent annual risk based capital calculation, whichever is greater.

H. The commissioner may require any applicant, or affiliated company of the applicant to remedy any hazardous financial condition as outlined in Regulation 3-1-7 prior to licensure.

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I. Substantial errors, fraudulent statements contained in an application or incomplete applications constitute sufficient grounds for denial of the application.

J. The most recent financial examination of the applicant must have a date of account no later than five years from the date of the application for licensure.

**Section 5 Formation Of A Colorado Domestic Insurer**

A. An application for the formation of a Colorado domestic insurance company as an insurer, fraternal benefit society, or interinsurance exchange must be in a form prescribed by the Commissioner.

B. The applicant must demonstrate the ability to maintain the minimum level at the time of initial licensure and on an on-going basis. This includes the ability to fund for product development and for other causes of surplus strain resulting from increasing business writings or new business ventures. An amount in excess of the statutory minimum capital and surplus is necessary at the time of licensure to ensure that the company has a sufficient cushion to absorb any surplus strain. Generally, the applicant should have three (3) times the authorized control level based on the most recent annual risk based capital calculation.

C. If the company's operation is predominately that of a reinsurer, such as where 50% or more of its operation measured by premium, underwriting or reserves is reinsurance, the surplus requirements of a reinsurer pursuant to § 10-3-118, C.R.S. must be met.

D. The applicant must have a sound business plan, sufficient capital to support the plan, and adequate access to additional capital. In addition, the applicant must also demonstrate favorable liquidity, adequate reinsurance from companies authorized in this state, sound management, and stable revenue, earnings and surplus trends.

E. The commissioner may, at his or her discretion, require an actuarial opinion and report of the company's surplus adequacy prior to licensure or at any time during which the company is licensed when it is believed that there is a need to review the adequacy of the available surplus with respect to the types of assets and writings of the company.

F. Substantial errors, fraudulent statements contained in an application or incomplete applications constitute sufficient grounds for denial of the application.

**Section 6 Change To Existing Authority**

A. A company may apply to add or delete lines of authority, redomesticate, change its name or otherwise amend its Certificate of Authority. Applications must be on a form prescribed by the Commissioner.

B. The Commissioner will determine whether the company has the necessary expertise, experience and financial ability for continued licensure in Colorado after the proposed change.

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**Section 7 Reinstatement Of Suspended Authority**

Any suspended foreign or domestic insurer, fraternal benefit society or interinsurance exchange may have its certificate of authority reinstated by demonstrating that it meets all the conditions and standards for licensure. Applications must be on a form prescribed by the Commissioner.

**Section 8 Confidentiality**

A. Documents submitted in compliance with this regulation, shall generally be considered public records under the public records act, § 24-72-201, C.R.S., et seq.

B. If an applicant considers a document to be confidential, the applicant must submit the document under separate cover clearly labeled "CONFIDENTIAL" with an explanation of why the applicant believes the documents are confidential.

C. Documentation found to be confidential by the Division will be maintained in a separate, confidential file and will not be released to the general public for inspection or copying except upon court order or agreement of the applicant.

**Section 9 Severability**

If any provision of this regulation or the application thereof to any person or circumstance is for any reason held to be invalid, the remainder of this regulation shall not be affected thereby.

**Section 10 Effective Date**

This amended regulation shall be effective September 1, 2002.

**Section 11 History**

Originally adopted November 1, 1990.

Amended September 1, 1992.

Amended March 1, 1994.

Amended November 1, 1999.

Amended September 1, 2002.

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## **Appendix C – Specific Certificate of Authority Applications Received but Not Approved - 2000-2004**

The following list consists of specific insurance companies whose Certificate of Authority applications were received but not approved (mostly non-Colorado domiciled companies), between 1/1/2000 and 12/31/2004.

**Sterling Life Insurance Company:** The company initially applied on 7/27/00, and that application was withdrawn 9/26/00 because the filing was incomplete. The company re-applied on 11/17/00, and that application was approved 1/18/01.

**First America Life Corporation:** The company initially applied on 9/12/00, and that application was withdrawn on 9/15/00 because the filing was incomplete. The company re-applied on 2/16/01, and the company withdrew that application on 4/6/01 due to a change in its marketing strategy.

**William Penn Life Insurance Company of New York:** The company applied on 7/27/01, and the application was withdrawn on 9/18/01 because the filing was incomplete.

**Unified Life Insurance Company:** The company initially applied on 9/18/01, and that application was withdrawn due to the potentially hazardous financial condition of an affiliate company. The company re-applied on 4/5/02, and that application was approved on 5/23/02.

**Educators Mutual Life Insurance Company:** The company initially applied on 10/4/01, and that application was withdrawn because the filing was incomplete. The company re-applied on 8/23/02, and that application was withdrawn because the filing was incomplete. The company applied a third time on 9/21/04, and that application was approved on 11/3/04.

**Unimerica Insurance Company:** The company initially applied on 6/13/02, and that application was withdrawn on 8/16/02 because the filing was incomplete. The company re-applied on 2/9/04, and that application was approved on 4/26/04.

**Mid-Continent Preferred Life Insurance Company:** The company initially applied on 11/21/02, and that application was withdrawn on 12/31/02 because the filing was incomplete. The company re-applied on 11/17/03, and that application was closed (not approved) on 12/8/04 because the filing was incomplete.

**Southland National Insurance Corporation:** The company initially applied on 5/19/03 and that application was withdrawn on 6/25/03 because the filing was incomplete. The company re-applied on 10/20/03, and that application was approved on 1/27/04.

**American Medical and Life Insurance Company:** The company applied on 7/29/03, and withdrew its application on 10/6/03 because financial results did not meet the qualification criteria for approval.

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**Westward Life Insurance Company:** The company applied on 9/15/03 and withdrew its application on 12/11/03 because the financial results did not meet the qualification criteria for approval.

**Life of Colorado Insurance Company:** The company applied on 3/31/04, and the application was denied on 0/30/04 because the company did not have the financial resources required for approval. This company was based in Colorado Springs and would have been domiciled in Colorado.