U.S. Securities and Exchange Commission

U.S. SECURITIES AND EXCHANGE COMMISSION

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Accounting and Auditing Enforcement Release No. 2550 / February 6, 2007

SEC v. RenaissanceRe Holdings Ltd., 07 CV 865 (S.D.N.Y.)

Reinsurer Settles Accounting Fraud Case Involving Sham Reinsurance Transaction

Washington, D.C., February 6, 2007 - The Securities and Exchange Commission filed settled securities fraud charges in the United States District Court for the Southern District of New York against RenaissanceRe Holdings Ltd. (RenRe), a property catastrophe reinsurance company. In its complaint, the Commission alleges that RenRe created a sham reinsurance transaction that had no economic substance and no purpose other than to smooth and defer over $26 million of its earnings from 2001 to 2002 and 2003. In effect, the transaction enabled RenRe to create a "cookie jar" into which it put excess revenue in one good year, to be pulled out in a future year to increase income.

In settling the Commission's charges, RenRe agreed to an injunction, to retain an independent consultant, and to pay a $15 million civil penalty, among other things.

In September 2006, the Commission charged RenRe's former chairman and chief executive officer, James N. Stanard, RenRe's former controller, Martin J. Merritt, and a former senior vice president of RenRe's principal reinsurance subsidiary, Michael W. Cash. Those charges remain pending in federal court in Manhattan.

According to the Commission's complaint, RenRe concocted a sham transaction to smooth its earnings. RenRe used two seemingly unrelated contracts that were, in fact, intertwined to conceal what was in reality simply a round trip of cash. In the first contract, RenRe purported to assign $50 million of receivables at a discount to Inter-Ocean Reinsurance Company, Ltd. in exchange for $30 million in cash, for a net transfer to Inter-Ocean of $20 million. RenRe recorded income of $30 million upon executing the assignment agreement. The remaining $20 million of its $50 million assignment became part of a "bank" or "cookie jar" that RenRe used in later periods to bolster income.

The second contract was a purported reinsurance agreement with Inter-Ocean that was, in fact, a vehicle to refund to RenRe the $20 million transferred under the assignment agreement plus the purported insurance premium paid under the reinsurance agreement. This reinsurance agreement was also a sham. Not only was RenRe certain to meet the conditions for coverage; it also would receive back all of the money paid to Inter-Ocean under the agreements plus investment income earned on the money in the interim, less transactional fees and costs.

RenRe accounted for the sham transaction as if it involved a real reinsurance contract that transferred risk from RenRe to Inter-Ocean when in fact, the complaint alleges, certain of RenRe's senior officers knew that this was not true. RenRe's former controller and former chief executive officer also misrepresented or omitted certain key facts about the transaction to RenRe's auditors. As a result of RenRe's accounting treatment for this transaction, RenRe materially understated income in 2001 and materially overstated income in 2002, at which time it made a "claim" under the "reinsurance" agreement. It then received as apparent reinsurance proceeds the funds it had paid to Inter-Ocean and that Inter-Ocean had held in a trust for RenRe's benefit.

In a Feb. 22, 2005 press release, RenRe announced that it would restate its financial statements for the years ended Dec. 31, 2001, 2002 and 2003. On March 31, 2005, RenRe filed its Form 10-K for the year ended Dec. 31, 2004, which contained restated financial statements for those years. RenRe's former chief executive officer signed and certified the 2004 Form 10-K. However, both the press release and the Form 10-K attributed the restatement of the Inter-Ocean transaction to accounting "errors" due to "the timing of the recognition of Inter-Ocean reinsurance recoverables." These statements were misleading. In fact, the transaction contained no real reinsurance and the company's restated financial statements accounted for the transaction as if it had never occurred. In short, the entire transaction was a sham, and the company both failed to disclose that fact and misrepresented the reasons for the restatement.

The Commission's complaint charges RenRe with securities fraud in violation of Section 17(a) of the Securities Act of 1933 and Section 10(b) and Rule 10b-5(a), (b), and (c) of the Securities Exchange Act of 1934, and with violating the reporting, books-and-records, and internal controls provisions of Exchange Act Sections 13(a) and 13(b)(2) and Rules 12b-20, 13a-1, 13a-13, and 13b2-1. Without admitting or denying the allegations in the Commission's complaint, RenRe has consented to a judgment requiring it to pay a civil penalty of $15 million and nominal disgorgement of $1 and permanently enjoining it from future violations of the federal securities laws. RenRe has also consented to undertakings that, among other things, require it to retain an independent consultant to review the design and implementation of the prior review conducted by independent counsel and the additional procedures performed by the company's auditors and make recommendations concerning the adequacy of RenRe's internal controls, audit department, and compliance function.

The corporate penalty in this case was negotiated before the Commission issued its statement Concerning Financial Penalties (http://www.sec.gov/news/press/2006-4.htm). The Commission has therefore elected not to apply that Statement to this corporate penalty.

SEC Complaint in this matter

http://www.sec.gov/litigation/litreleases/2007/lr19989.htm

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