



October 31, 2008

David R. Dimitriou  
Counsel to the Chairman  
Office of the Chairman  
United States Securities and Exchange Commission  
100 F Street N.E.  
Washington, D.C. 20549

Dear Mr. Dimitriou:

Re: Follow-up to Meeting of October 17, 2008

Thank you very much for taking the time to meet with me and others on October 17, 2008. As requested during our meeting, we are writing to provide additional facts concerning the experience of Fairfax Financial Holdings Limited ("Fairfax") with abusive short-sellers. Let me first say that Fairfax strongly supports the efforts of the SEC to require meaningful transparency for short positions. We continue to believe that full public disclosure of short positions together with long positions, even on a delayed basis, is necessary to provide even-handed rationality to the Commission's disclosure scheme. In addition, Fairfax applauds the Commission's new enforcement initiatives directed at curbing abusive short-selling practices and market manipulation.

Since our first comment letter on short-selling filed with the Commission on September 19, 2006, Fairfax has consistently advocated for increased market transparency. As a company that itself engages in legitimate short-selling and also has been the victim of blatantly abusive short-selling attacks, Fairfax is uniquely positioned to understand the need for transparency and robust enforcement in this area. Fairfax strongly believes that transparency with respect to short positions and more robust enforcement of abusive short-selling practices will not materially hinder legitimate short-selling and are essential to protecting the integrity of the U.S. capital markets. As Chairman Cox noted earlier this year in connection with a major enforcement action against a hedge fund trader, "[t]he Commission will vigorously investigate and prosecute those who manipulate markets with this witch's brew of damaging rumors and short sales." SEC Press Release 2008-64, "SEC Charges Wall Street Short-Seller With Spreading False Rumors," April 24, 2008 (available at <http://www.sec.gov/news/press/2008/2008-64.htm>).

First, for the same basic reasons disclosure has been required for many years for long positions, disclosure should exist equally for short positions. There is no reasoned argument for treating one kind of equity position differently from the other. Indeed, maintaining this disparity in disclosure rules substantially limits the value of even the disclosure that is currently required and in many cases results in a materially misleading picture being presented to the market. Allowing market participants to disclose only long positions in their Form 13-F filings, when they also have short positions, creates confusion in the marketplace, and also creates an opportunity for abuse by those market participants who wish to mislead others and manipulate the market in particular securities.

Moreover, disclosure of short positions is a critical requirement for effective enforcement efforts against potentially abusive short-selling practices. Rumor and fear-mongering have been widely cited as substantial contributors to the crisis of confidence that has resulted in the stunning collapse of some of America's most venerable financial institutions and in unprecedented government interventions to restore confidence in the financial services marketplace. *See, e.g.*, SEC Press Release 2008-140, "Securities Regulators to Examine Industry Controls Against Manipulation of Securities Prices Through Intentionally Spreading False Information," July 13, 2008 (available at <http://sec.gov/news/press/2008/2008-140.htm>); Securities Exchange Act of 1934 Release No. 58166, July 15, 2008;<sup>1</sup> S.E.C. Warns Wall Street: Stop Spreading the False Rumors, *New York Times*, July 14, 2008. As market rumors have since continued to stoke crises of confidence at numerous other financial and other institutions, *The New York Times* recently noted that rumors have become "one of the most dangerous weapons on Wall Street." Citadel Chief Denies Rumors of Trouble, *New York Times*, October 25, 2008.

Although the Commission and other regulators have announced their intention to increase regulation and enforcement to address these pernicious activities, identifying those responsible is substantially hampered by the complete lack of disclosure of those who have financial incentives to profit from such illegal and manipulative activities. Likewise, the lack of transparency on the short side substantially impairs the market's ability to judge the significance and potential biases of those who are disseminating information in the marketplace.

Fairfax's experience is instructive on both the need for public disclosure of short positions and more robust monitoring and enforcement of activities by short-sellers. In July 2006 -- after nearly four years of having been the target of a relentless campaign of false rumors, dirty tricks, harassment, and market manipulation by certain short-selling hedge funds and those working with them -- Fairfax had no choice but to institute a

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<sup>1</sup> As the Commission stated in its Emergency Order: "False rumors can lead to a loss of confidence in our markets. Such loss of confidence can lead to panic selling, which may be further exacerbated by 'naked' short selling. As a result, the prices of securities may artificially and unnecessarily decline well below the price level that would have resulted from the normal price discovery process. If significant financial institutions are involved, this chain of events can threaten disruption of our markets."

lawsuit to stop this illegal conduct. Fairfax Financial Holdings Limited et al. v. S.A.C. Capital Mgmt., et al., No. MRS-L-2032-06, New Jersey Superior Court, Morris County. Although many of the documents in that case remain subject to a protective order precluding disclosure, the facts in the public record concerning the short-sellers' attack on Fairfax demonstrate the need for rules and enforcement to curb these abusive practices. Moreover, these facts further make the case for increased transparency in order to deter wrongful conduct and provide market participants with the ability to evaluate and respond to these practices.

For example, almost immediately upon listing on the New York Stock Exchange in late 2002, Fairfax stock experienced unprecedented and enormous levels of short-selling immediately before the publication of a violently negative report by a research analyst from investment bank Morgan Keegan that made, among others, the unfounded claim that Fairfax was \$5 billion under-reserved for its insurance liabilities. When Fairfax questioned whether the report was issued to benefit short-sellers who were tipped off by Morgan Keegan prior to publication, Morgan Keegan denied any such collaboration or leak. It was impossible for Fairfax or other market participants -- not to mention regulators -- even to identify who had shorted the stock in the period immediately prior to the publication of the research report containing the baseless claim. Over five years later, however, it has been widely reported that based on documents produced in the Fairfax litigation, Morgan Keegan this past August fired the analyst who issued the report for, in fact, leaking his research to short-sellers prior to the report's publication. See "Morgan Keegan Fires Fairfax Analyst on Early Report Disclosure," Bloomberg News, September 10, 2008; "Analyst Fired for Fairfax Leaks," Financial Post, September 11, 2008.

Equally troubling, in 2005 and 2006, a group of some of the most prominent hedge funds, including Kynikos, Third Point, and three funds (Exis Capital, Prentice Capital, and Bridger Capital) managed by former or affiliated S.A.C. Capital Management traders (and, in at least one instance, in which S.A.C. funds were invested) were paying an individual named Spyro Contogouris -- now under indictment in the Southern District of New York for defrauding a former employer -- to write purported "research" on Fairfax and other publicly-traded companies. While being paid by these funds and working out of Exis's offices, Mr. Contogouris and a cadre of associates relentlessly prosecuted a campaign of false rumors, harassment, and dirty tricks against Fairfax designed to interfere with its business, intimidate its executives, and destroy confidence of every business constituency on which Fairfax and its subsidiaries depend, including rating agencies, auditors, customers, brokers, shareholders, analysts, employees, executives and directors. In order to mask identities and interests of those involved in such activities, these abusive tactics were frequently conducted anonymously, through aliases, and by portraying Mr. Contogouris as an objective market researcher. By way of example only, during 2005 and 2006, abusive acts against Fairfax and its officers included the following:

- The creation of an anonymous website as a vehicle to spread false rumors comparing Fairfax to Enron and Fairfax's Chief Executive Officer, Mr. Prem Watsa, to Ken Lay.
- Disseminating false rumors by sending anonymous packages and e-mail communications falsely accusing Fairfax and Mr. Watsa of various frauds to, among others, Mr. Watsa's pastor, the employees and executives with whom Mr. Watsa worked, Fairfax's auditors, securities regulators, and the exchanges on which Fairfax's shares are listed.
- Making anonymous late-night phone calls and recorded messages to Mr. Watsa at home and in the office.
- Anonymously instigating purportedly independent Internet research reports that republished false and misleading accusations of fraud by Fairfax and Mr. Watsa and comparing Fairfax to infamous corporate frauds like Enron, Refco, and Conseco.
- Disseminating and conducting numerous in-person presentations to spread the same materially false rumors and accusations in purported "research" reports and other communications to every major constituency critical to Fairfax's business, including rating agencies, research analysts, and shareholders, and using that same materially false information to instigate negative media reports.
- Illegally obtaining confidential bank, credit, investment, and other personal financial information of Fairfax employees with the objective of using that information to force those executives to assist in the effort to destroy Fairfax and its subsidiaries.

These efforts reached a crescendo in June 2006 when Fairfax suffered a coordinated short selling attack that mirrors the illegal activity that has led to recent scrutiny of rumor-mongering and abusive short-selling relating to the failure and near failure of major Wall Street institutions -- and the resulting intervention by governmental institutions. As an insurance holding company, Fairfax, like banks and other financial institutions, depends on its reputation and its ratings in order to do business. Thus, when Fairfax's reputation was attacked through the spread of false rumors, not only its short-term success, but its entire existence, was threatened.

On June 22 and 23, 2006, Fairfax received over forty telephone calls from rating agencies, broker-dealers, securities analysts and major shareholders and bondholders expressing concerns about false and defamatory rumors regarding Fairfax, including that our Chief Executive Officer, Mr. Watsa, had transferred all of his personal assets into his wife's name and fled the country with Fairfax company funds; that Canadian federal criminal investigators (the Royal Canadian Mounted Police) were raiding Fairfax's offices; and that new regulatory actions against Fairfax and its subsidiaries were

imminent. These false rumors resulted in the precipitous drop in the price of Fairfax's stock on June 23, 2006 to \$91.75 (the lowest closing price in the five-year period since 2003 and up to the present).

As the attached charts demonstrate, during June and July of the summer of 2006 these blatantly false rumors and other related activities targeting Fairfax and its shareholders, rating agencies, regulators, research analysts and broker-dealers occurred at the same time that the reported short interest in Fairfax stock rapidly increased from 3.1 million to 4.1 million shorted shares; failures-to-deliver increased approximately 1,000% from approximately 100,000 shares failing to deliver to 1 million shares failing to deliver; and the price of Fairfax's stock plummeted over 20% on a 400% increase in volume (the price of Fairfax debt similarly plummeted and the spreads on related credit default swaps widened dramatically).

In order to put all of these facts together, and to understand what was happening to its business, Fairfax was forced to expend substantial time and company resources. There was no information available to Fairfax, the investing public, or even to regulators concerning who may have had a financial interest in spreading these false rumors. Indeed, until recently, for Fairfax to even obtain, on a substantially delayed basis, the raw number of its shares that had not been delivered required a series of seriatim and cumbersome Freedom of Information Act requests. The facts surrounding the attack on our company demonstrate that robust monitoring and enforcement of laws prohibiting the spreading of false rumors and abusive short-selling practices are absolutely essential to protect the market from gross misconduct like that experienced by Fairfax. Public disclosure of short positions would greatly enhance those regulatory efforts, as well as the ability of market participants, such as shareholders and rating agencies, to better understand who is behind such conduct and generally to respond effectively to such activities.

The Commission has taken important steps in these trying times to address the acknowledged problem of market manipulation by certain short-sellers. Fairfax hopes that this will lead to implementing -- and enforcing -- a rational disclosure and enforcement system that will serve to renew the faith and trust of all market participants in our capital markets.

Thank you again for your continued time, effort and commitment to these issues.

Yours truly,

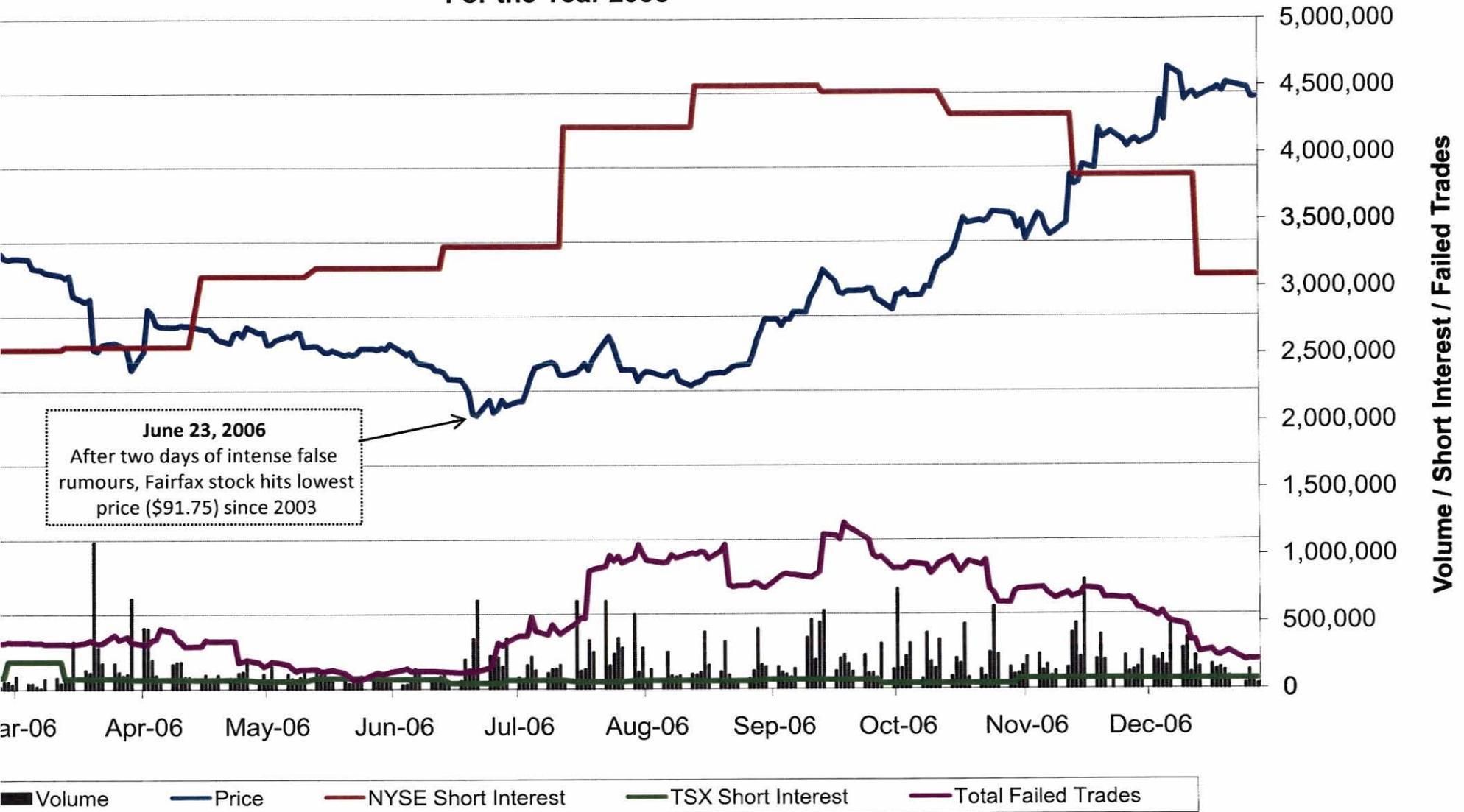
A handwritten signature in blue ink, appearing to read "Paul Rivett", is written over a large, circular blue scribble.

Paul Rivett  
Vice President and  
Chief Legal Officer

# Fairfax Financial Holdings Limited

## Price, Volume & Short Interest Analysis

### For the Year 2006



# Fairfax Financial Holdings Limited

## Price, Volume & Short Interest Analysis

### For June and July 2006

