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CLYDE&CO

LIBOR bulletin

LIBOR manipulation press coverage

Investigations and regulator action

In the February Bulletin we referred to the investigations by Germany's banking supervisor, BaFin, into possible EURIBOR manipulation by at least three banks. BaFin's preliminary findings have been summarised in an internal report, however this has not been made public. Investigations are continuing. The person in charge of the investigation, Raimund Roeseler, is quoted as saying that, so far, there has been no evidence of systematic crime involving management board members.

Deutsche Bank confirmed it was cooperating with regulatory authorities in Europe, North America and Asia Pacific after receiving subpoenas and requests for information from various law and regulatory enforcement agencies probing their role in the rates-manipulation scandal.

The Canadian Competition Bureau has indicated that the Canadian affiliate of RBS has abandoned its challenge to an order of the Ontario Superior Court of Justice compelling it to produce certain records located outside of Canada to the Commission. The Commission has indicated that this will allow it to move forward with its investigation in relation to the setting of Yen LIBOR rates. It is reported that the bank has said that it is cooperating fully with the investigation, and only challenged the method of obtaining the information due to confidentiality concerns.

The International Organisation of Securities Commissions (IOSCO), which sets standards for the regulation of securities markets around the world, prepared a Consultation Report on 'Principles for Financial Benchmarks'. This closed on 16 May 2013. The principles are intended to be used as guidelines by benchmark administrators, national regulators and other relevant bodies. They set out the roles and responsibilities of administrators and contributors, accountability mechanisms and complaints procedures. They also include guidelines on establishing benchmarking quality, including design, input and periodic review processes. The way the principles are applied should be proportional to the size and risks posed by each benchmark setting process, which may or may not include regulatory action. The Report also discusses the feedback from the Consultation Report on Financial Benchmarks published by IOSCO on 11 January 2013 (see more below).

Global regulators have said that the only way to repair and maintain public confidence in the financial industry is to urgently overhaul the rules for interbank lending rates and other benchmark rates.

A roundup of the views of the various regulators is noted in the table below:

Regulator	Rules for internet lending rates
The Financial Stability Board (FSB) (a group of finance ministers, central bankers and regulators from G-20 countries)	Mark Carney, in his role as Chairman of the FSB, is of the opinion that whilst policymakers can set the standard of good conduct, it is ultimately up to the private sector to decide how to achieve that standard, including whether or not to change the way benchmark rates are set. Carney also stated that regulators internationally should ensure that the setting of benchmark rates globally meet a global standard of "transparency and good governance"
The Financial Stability and Oversight Council (FSOC), a panel of US regulators	FSOC think interest-rate benchmarks must be tied to market transactions, instead of estimates, in order to adequately protect the financial system across the world. They also think that prompt action needs to be taken to find an alternative system as concerns about LIBOR manipulation is damaging market integrity
Financial Conduct Authority (FCA)	Martin Wheatley, Head of the FCA, states that the approach should not be to "throw something away before you have an alternative." He suggests a 'dual track' with the current rate-setting process, which relies on input from a panel of banks, running alongside a transaction based rate – at least until the LIBOR system can be fully overhauled. He gave warning about the difficulties of suddenly replacing LIBOR because many long-term contracts are linked to LIBOR -- an estimate of USD 350 trillion worth of contracts worldwide.
The International Organisation of Securities Commissions (IOSCO), which sets standards for the regulation of securities markets around the world	The IOSCO thinks that global benchmark interest rates should be based on actual transactions rather than estimates. Gary Gensler, who is Chairman of the US's CTFC but also co-chairman of the IOSCO's Benchmark Taskforce (with Martin Wheatley), has said that: "*to promote market integrity, it is critical that benchmark interest rates be anchored in observable transactions and supported by appropriate governance structures […] I support that international regulators and market participants have begun to discuss appropriate alternatives and possible approaches to a smooth and orderly transition from LIBOR, Euribor and similar rates*." IOSCO has also demanded a more effective mechanism for whistle-blowers, and codes of conduct for those involved in the rate-setting.

Other financial benchmark rates investigations

The US's Commodity Futures Trading Commission (CTFC) is now investigating potential rate-manipulation of other benchmark rates, known as ISDAfix, for interest-based swaps. ISDAfix is used as a benchmark for credit default swap contracts, an instrument designed to protect banks and their customers from swings in interest rates.

The European Commission confirmed it carried out unannounced inspections at the premises of several companies active in and providing services to crude oil, refined oil products and bio fuels sectors. The EC has "concerns that the companies may have colluded in reporting distorted prices to a Price Reporting Agency to manipulate the published prices for a number of oil and bio fuel products". The prices assessed and published by Price Reporting Agencies serve as benchmarks for trade in the physical and financial derivative markets for a number of commodity products in Europe and globally.

Industry response

The public's response to the IOSCO's Consultation Report on Financial Benchmarks can be located on the IOSCO's website. More than 50 responses were received. The Consultation Report discusses concerns regarding the potential inaccuracy or manipulation of Benchmarks and identifies Benchmark related policy issues across securities and derivatives and other financial sectors.

The Salz Review ("the Review") of Barclays' Business Practices delivered its report to the Board of Barclays PLC. The full report, which has been published at Barclays' request, is available at the Review website www.salzreview.co.uk. The Review was commissioned by the Board of Barclays in July 2012 as an independent external Review of Barclays' business practices to be led by Anthony Salz. The Review's mandate was to determine how Barclays can rebuild trust and develop business practices which make it a leader, not only among its business peers, but also among multinational corporates more generally. The Review was not mandated to determine the truth or otherwise of allegations surrounding past events, or to pass judgment on the shape of the business or strategic decisions previously taken. The two conclusions at the heart of the Salz Review were:

- that 'pay contributed significantly to a sense among a few that they were somehow unaffected by the ordinary rules' and
- Barclays' willingness to push the rules and let an adversarial relationship with regulators develop….. The institutional cleverness….stretched relationships with regulators and resulted in them and the market questioning some of Barclays' financial information. Barclay was sometimes perceived as being within the letter of the law but not within the spirit'.

Litigation

In both the US and UK, claimants bringing private law actions for damages against LIBOR banks, arising out of the regulatory investigations into LIBOR manipulation, are not having an easy time of it.

USA

Re LIBOR based financial instruments anti-trust litigation – these are the consolidated cases being heard in the federal court. The plaintiffs include various municipalities, commodities traders, investors, bond holders and Charles Schwab against the global banks. In April US District Judge Buchwald's dismissed individual claims by Charles Schwab and two class actions (one by owners of LIBOR pegged securities and the other by derivatives traders) that raised anti-trust and racketeering allegations (see April Bulletin for her reasoning). She then granted leave to the Plaintiffs to file a motion to amend their complaints 'given the obvious magnitude of this litigation', but she went on to express scepticism that the pleadings could be amended sufficiently to address the concerns that led her to grant the motion to dismiss. She will also review the amended complaint prior to requiring the defendants to respond to any motion for leave to amend in light of her concerns, the 'comprehensive manner' of her prior order and the 'tremendous amount of resources already expended by the defendants'.

Gusinsky v Barclays – this is the Barclays shareholders securities class action lawsuit in the Southern District of New York. The suit was filed on behalf of class of persons who purchased Barclays ADRs between 10 July 2007 and 27 June 2012. It alleges that the defendants participated in an illegal scheme to manipulate the LIBOR rates and '*made material misstatements to the company's shareholders about the company's purported compliance with their principles and operational risk management processes and repeatedly told shareholders that Barclays was a model corporate citizen even though at all relevant times it was flouting the law*'. Judge Scheindlin has granted Barclays and two of its former executives (former CEO, Robert Diamond and former Chairman, Marcus Agius), motion to dismiss. Judge Scheindlin found that many of the statements concerning Barclay's business practices, particularly general statements about its high standards constituted 'mere puffery'. She also noted that even if certain statements relating to LIBOR practices were arguably not puffery, the plaintiff's allegations failed to connect the statements to the company's LIBOR practices – 'finding such statements actionable on these facts would render every financial institution liable to every investor for every act that broke the law or harmed reputation'. Plaintiffs have been denied leave to amend.

Charles Schwab Corporation - meanwhile one of the plaintiffs from the consolidated LIBOR litigation filed an action in San Francisco County Superior Court asserting a variety of common and statutory law claims as well as claims under the Securities Act 1933. The action pleads multiple separate causes of action including fraud, deceit and concealment, breach of contract and unjust enrichment; violation of the California Corporate Code and federal Securities Act 1933. It also alleges that LIBOR banks conspired to suppress the benchmark borrowing rate and this artificial suppression permitted the banks to pay unduly low interest rates on both floating-rate securities fixed to LIBOR and short-term fixed-rate notes with returns based on LIBOR rates.

Salix Capital v [a dozen LIBOR banks] – the Plaintiff owns claims belonging to several shuttered hedge funds that once operated under the FrontPoint umbrella. It has filed a complaint in the New York State Supreme Court in which it alleges that in 2007 and 2008 the FrontPoint funds engaged in Libor-pegged interest rate swaps with LIBOR panel banks as part of complex, multi-security deals known as corporate bond basis packages. The swaps were supposed to be a hedge against the global banking crises since LIBOR should have increased as it became more expensive for banks to borrow from one another. Instead the panel banks artificially suppressed LIBOR, undermining the trading strategy of FrontPoint funds'. It blames the LIBOR manipulation for FrontPoint funds' big losses in 2008 and demise in 2009 and claims USD 250 million in damages from, amongst other reasons listed, inflated payments to the defendants. Common law fraud and breach of contract is asserted against the banks.

UK

Graiseley Properties Ltd (and Guardian Care Homes) v Barclays Bank - this is the test case being brought against Barclay's for damages arising from mis-selling of interest rate swap products which used LIBOR as a benchmark. In October 2012 the High Court gave Graiseley permission to amend its claim to plead fraudulent misrepresentation based on certain implied representations as to the integrity of LIBOR. The application by Graiseley followed publication of the FSA's final notice against Barclays in June 2012. Barclays have been granted permission to appeal this decision and the appeal is listed between September 2013 and January 2014.

Deutsche Bank & Others v Unitech Ltd & Others. Unitech is appealing the decision to refuse it permission to amend its counterclaim to include a claim for misrepresentations based on alleged manipulation of LIBOR. The court denied permission on the basis that:

- some of the implied representations alleged by Unitech were too wide and uncertain to arise, as they placed in the mouth of one bank a statement about overall integrity of the system and the parts played by every bank in it
- there was a difference between an implied term of a contract that a party will not manipulate the specific LIBOR rate referred to in it, and a separate non-contractual representation that nothing has been done or is now being done to impact on any of the many LIBOR rates claimed

The details of the court's decision are looked at more thoroughly in the April Bulletin. The decision has been appealed and is listed for hearing between July and December 2013.

It is possible that both appeals will be heard together.

Comment

A number of Regulators offer views on how best to regulate interbank lending rates and other benchmark rates. IOSCO's Consultation Report on the Principles for Financial Benchmarks follows on from its Consultation Report on Financial Benchmarks earlier this year. The Consultation closed on 16 May 2013. The Salz Review into Barclays delivers its report and recommendations to Barclays. Barclays Chairman, Sir David Walker, says it made 'uncomfortable reading'. The eye of the Regulators moves from LIBOR to other financial benchmark rates. CTFC starts probing ISDAfix for interest based swaps. The EC also looks at published prices for a number of oil and bio fuel products. On the litigation front a number of US class actions are dismissed whilst new individual actions are brought pleading 'tight targeted fraud claims'. Meanwhile in the UK it is possible that both the Graiseley Properties Ltd (test case) and Deutsche Bank v Unitech appeals will be heard together sometime between July 2013 and January 2014.

Further information

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