



## **LIBOR Governance and Scrutiny**

*- Proposals agreed by the FX & MM Committee, 17th November 2008.*

FX & MM Committee Secretariat  
C/O BBA  
105 – 108 Old Broad St.  
London EC2N 1EX

## **Contents**

### **1. Introduction.**

### **2. Governance**

- Proposed Governance Structures
- Proposed disciplinary procedures
- Expansion of the FX & MM Committee, and status of members
- Status of “Observers”
- Future of the LIBOR Steering Group

### **3. Scrutiny**

- Data to be collected
- Analysis of data
- Presentation of data to Committees.

## ***Appendices***

- I Draft FX & MM Committee Terms of Reference
- II Draft Terms of Reference for Contributors
- III Proposed Committee structure Diagram.

## 1 Introduction

- 1.1. This paper presents the proposed methodology for how enhanced LIBOR governance and scrutiny will operate in future. It is intended that the FX & MM Committee should discuss this paper and once agreed, with alterations as necessary, it will be submitted to the BBA's auditors, the Financial Reporting Council and Clifford Chance for their approval. It will also be given to the FSA and interested central banks for information purposes.
- 1.2. It builds on the recent LIBOR consultation paper, the comments we received in response to the paper, and discussions since then with the Bank of England. This paper also reports on discussions with third parties who are helping with this process:
- 1.3. **Thomson Reuters** ("TR") act as the "designated distributor" of BBA LIBOR rates. All contributions to the LIBOR rate-setting process are collected by Thomson Reuters, who currently perform checking procedures, supervised by the LIBOR manager, on all the submissions before running the calculation and distributing the fixes. Thomson Reuters also perform a similar function for other market rates such as SONIA and EURIBOR. We are exploring how Thomson Reuters might expand this role to collect and collate some of the data required to scrutinise LIBOR contributor submissions in line with the proposals in the recent Feedback Statement. Thomson Reuters currently have analysts working on this and are regularly updating the LIBOR manager on progress.
- 1.4. **Clifford Chance** ("CC") Their role is to provide advice to ensure that all of the structures and processes necessary to oversee LIBOR reflect best practice. They are working with the BBA to ensure that all personal and corporate liability for contributors and committee members is eliminated as far as possible, and that these proposals do not have implications with regard to competition or other law. They will also advise on what levels of transparency are appropriate.
- 1.5. The bodies and individuals involved in the governance of LIBOR are:
- 1.6. **Foreign Exchange and Money Markets Committee** ("FX & MM Committee") This independent body has the overarching responsibility for the operation and development of BBA LIBOR. The construction, constitution and objectives of the group are detailed in section 2, below.
- 1.7. **LIBOR Manager** The BBA employs a full time manager to supervise on a day-to-day basis all aspects of LIBOR calculation and dissemination to the marketplace. The LIBOR manager works with a team of professionals both in-house and externally to ensure all processes operate to the highest standards. The LIBOR manager also acts as secretariat to the FX & MM Committee and is responsible for ensuring they are fully informed about all issues pertaining to LIBOR, and that their decisions are communicated to the market and acted upon. The LIBOR Manager is appointed for a two year term by the FX & MM Committee, upon recommendations from the BBA. Within this period the FX & MM Committee may at any time review this appointment. The LIBOR manager may stand for re-appointment without restriction.
- 1.8. Other regulators, statutory institutions and public bodies are also consulted in the governance of LIBOR.

## Governance

- 1.9. This section of the paper describes the oversight of LIBOR. As part of the strengthened governance, LIBOR contributors will be reviewed twice annually, typically in June and December.

### Proposed Governance Structures

- 1.10. The FX & MM Committee will continue to have the sole responsibility for all aspects of the functioning and development of BBA LIBOR. The Committee will typically meet bi-monthly but at times of market stress or when other conditions demand it will meet more frequently as required. This will also allow members to consider and if necessary expand and refine the new reports from the BBA, as described in 3.23 below.
- 1.11. The Committee will comprise of highly respected practitioners from a representative sample of contributing banks, some non-contributing banks and rate users – see 2.10, below, for details. It will be chaired by a representative from a contributing bank, and have two deputy chairmen, also from contributing banks. The deputy chairmen will also act as chairs of the subcommittees described below.
- 1.12. All Committee members shall have a vote, apart from the secretary. The Committee secretary will be the LIBOR manager at the BBA, who will also act as secretary to the sub-committees described in section 2.5, below. Proposed new terms of reference for this committee are included as Appendix I. Each member will have the option to allow a named alternate of suitable standing to attend meetings if they are not able to and this alternate will act in place of the member.
- 1.13. The Committee will form two sub-committees: A Fixings Sub-committee and an Oversight Sub-committee. These will be chaired by the deputy chairs of the main committee. Membership will be taken from the members of the main committee.

#### ❖ Fixings Subcommittee

This Sub-committee scrutinises the fixing process. Should an issue arise that has not been resolved by Thomson Reuters, it is referred to the LIBOR manager who initiates an investigation and reports in full to the Fixings Sub-committee. The outcome of the deliberations and any recommendations of the Fixings Sub-committee are referred to the FX & MM Committee for final decision.

Issues raised from sources other than Thomson Reuters will be investigated if appropriate by the LIBOR manager and the same reporting structure will be followed. The Fixings Sub-committee may instruct the LIBOR manager to visit contributor banks to discuss their quoting behaviour in confidence and provide a written report of this.

The Fixings Sub-committee shall also conduct the review of the contributors to the LIBOR panels – see 2.16, below.

Meetings of this body will be as required.

❖ Oversight Sub-committee.

Should the FX & MM Committee decide that an issue has not been satisfactorily resolved in conjunction with the contributor, then action will be initiated via the Oversight sub-committee. Tools at their disposal are detailed in 2.8 below and will include but are not limited to: issuing written guidance, to include a re-statement of contributor protocols; requiring an up-to-date audit of a panel bank's contribution processes; plus other measures as appropriate (in extremis, a recommendation that a contributor be removed from the relevant panel at the next review). In the latter case this must be approved by a special meeting of the FX & MM Committee.

- 1.14. All contributors must sign the required procedures for contributors attached as Appendix II. The signatory shall be the individual with the responsibility of submitting LIBOR rates each day. In the case of banks on multiple panels, each individual submitting rates must sign.
- 1.15. These required procedures oblige contributors to ensure that their adherence to the procedures is reviewed at least annually, by a formal internal audit and that a statement of confirmation is forwarded to the FX & MM Committee accordingly.

Proposed Disciplinary Procedures

- 1.16. Discipline of contributors may take three forms:

❖ **Written guidance.** On the instructions of the Oversight Sub-committee the FX & MM Committee secretary will write to the contributor in confidence detailing the reasons the contributor is believed not to be acting in accordance with the LIBOR definition or terms of reference for contributors and ask them to justify or remedy their actions. A full record of all correspondence will be kept and presented to the next meeting of the FX & MM Committee. However this will not be made public.

If a contributor receives guidance, the Sub-committee will set a date to re-convene and review the actions of the contributor since the original guidance was issued. At this point the issue will either be closed or disciplinary action will escalate.

❖ **Requirement for a Re-Audit.** The sub-committee may issue a recommendation that a contributor is required to re-audit its internal rate submitting processes. This could happen when it is considered that the contributor is not reliably complying with the written guidance or if there are concerns with the existing audit process.

❖ **Recommendation for next review** The sub-committee may issue a recommendation that a contributor is removed at the following review of LIBOR contributors. This will happen either when it is considered that the contributor has not complied with written guidance, or if the group believes the bank is unquestionably in breach of the LIBOR definition or terms of reference for contributors. The group may ask for external input from legal counsel to ensure that decisions do not raise competition law issues or implicitly favour one bank over another. In either case the secretary will retain records which will be made

available to observers and the BBA auditors. This will ensure that any enforcement action can be demonstrated to be fair.

The makeup of contributor panels is often changed at reviews, and in the past no commentary has accompanied the announcements, which are made by the BBA on behalf of the FX & MM Committee. It is intended that this will continue to be the case. A bank that has been replaced however may choose to comment.

### Expansion of the FX & MM Committee and status of its members

- 1.17. Currently Committee members sit in their own right as individuals, and membership is not publicly disclosed. However there is justifiable interest from the market in the make-up of the Committee, as they wish to see that the body is independent and appropriately constituted.
- 1.18. In future, therefore, committee members will sit as individuals representing their firms, and will be expected to act in the best interests of the LIBOR benchmark and the markets it serves. The committee will be expanded to include:
- ❖ A representative of a (currently) non-contributing US bank that is active in the money markets
  - ❖ A representative of a (currently) non-contributing European bank that is active in the money markets
  - ❖ One representative from Liffe and one from the Chicago Mercantile Exchange (CME)
  - ❖ Two “rate takers”: one from the fund management industry and one from the Association of Corporate Treasurers.
- 1.19. The BBA will contact the above and present a list of names and titles for consideration by the Committee.
- 1.20. Once the Committee has reached its complement, the names of all firms represented will be released, but not names of the individual members. This will be accompanied by a statement which describes the capacity in which members serve.
- 1.21. The BBA is subject to a regular independent audit of practices and processes and in future the FX & MM Committee and LIBOR processes will be included in this audit.

### Status of Observers

- 1.22. Certain public bodies in the UK, Europe, USA, and Asia have expressed an interest in engaging more closely with the BBA and the LIBOR governance process.
- 1.23. The LIBOR manager will invite any interested public body to discuss the ongoing operation and development of LIBOR at their convenience.

### Future of the LIBOR Steering Group

- 1.24. The LIBOR Steering Group currently meets only once a year with the sole purpose of considering the LIBOR Review and providing a recommendation to the FX & MM Committee. There is a wide overlap in membership between the LIBOR Steering Group and the FX & MM Committee. Historically it is rare for the FX & MM Committee to take a different view on membership of the contributor panels than that recommended by the LIBOR Steering Group. It is therefore proposed that this Steering Group is wound up and its duty assumed by the Fixings Sub-committee.

## 2. Scrutiny

- 2.1. This section of the paper details the data that will be used to check LIBOR contributions and how this will work in practice.
- 2.2. As far as is possible, for each data point or series, there is a proposal for acceptable tolerances (see below). It is envisaged that if these tolerances are exceeded, the contributor will be queried by the fixings team at Thomson Reuters or the FX & MM secretary, and if there is not a satisfactory explanation, this will be brought to the attention of the FX & MM Committee in the manner described in section 2, above. Queries will be by telephone to the individual in each bank responsible for setting the rate.

### Data to be collected

#### **l) Consistency**

- 2.3. It is recognised that, subject to their best efforts and time constraints, Thomson Reuters will undertake both pre- and post-publication analysis of rates submitted by panel banks. Thomson Reuters are currently building the infrastructure to provide all the data below.
- 2.4. Thomson Reuters will undertake the following checks prior to publication:
  - ❖ Missing contributions (commencing at 11.10am).
  - ❖ Spread filters for each currency: moveable band, set per currency, outside which the contributor will automatically be contacted by Thomson Reuters.
  - ❖ The data are to five decimal places or less.
  - ❖ The data are numeric.
  - ❖ Spread between top and bottom quotes for each maturity. Outliers may be contacted.
  - ❖ Contributors' rate is checked against the (as yet) unpublished potential LIBOR rate, for greater than 0.04 variance from average, subject to changing market conditions, after which the contributor may be contacted.
- 2.5. Post-publication checks will be undertaken by the LIBOR manager based on data supplied by Thomson Reuters who will endeavour to provide the LIBOR Manager with the following data: initial data to be covered USD, GBP, JPY, CHF and EUR for ON, 1, 3, 6 & 12 month tenors. BBA to specify required checks and times e.g. as those listed in section 3.4 with the following questions answered:
  - ❖ unexplained submissions more than two standard deviations from the previous fix for that maturity.
  - ❖ submissions that move the contributor from materially above to materially below the fix, or vice versa.
  - ❖ submissions that are more than approximately 5bp higher or lower than the previous submission, unless the majority of the rest of the panel have also moved the same amount in the same direction. In this latter case, Thomson Reuters will provide the data and the LIBOR manager will investigate the nature of such a market-moving event and discuss with the FX & MM Committee.

- 2.6. A call to a contributor to check a rate is in no way an accusation of inaccuracy or manipulation, it is a request for confirmation and as such does not in any way stigmatise that contributor.
- 2.7. If there are factors that will affect a contributor's rates in the medium to long term, once these have been made clear to the LIBOR manager, the LIBOR manager may take these into account and elect not to contact the contributor each day if a quote falls outside of the parameters laid out above, and the reasons previously given by the bank are consistent with the observed quoting pattern.

### **LIBOR vs. dealt rates**

- 2.8. It has been suggested that LIBOR contributions could be compared with the indicative rates from brokers shown on Thomson Reuters and Bloomberg screens. However, this is unlikely to provide any useful insights as it is a comparison of a bank's perceived cost of funding against a broker's perception of where a bank could access funds, and neither of these needs to be tied to an actual dealt rate.
- 2.9. The BBA is in discussion with the Wholesale Market Brokers Association (WMBA) and its members with a view to providing a Volume Weighted Average Price for all cash transacted between banks via brokers in the London market. This initiative is fully supported by the panel banks.
- 2.10. It is not possible to receive the details of individual dealt rates as the confidentiality agreements between brokers and their clients preclude these from being disclosed.
- 2.11. It is intended that this rate will be used as one of many sources of market data for scrutinising BBA LIBOR contributions.

### **II) Audit**

- 2.12. Contributors undertake to have their internal processes for submitting rates audited as part of their firm's annual compliance procedures and provide written confirmation to the FX & MM Committee that this audit has been completed.

### Analysis of data

- 2.13. Day-to-day monitoring of internal consistency of submissions as laid out will be carried out by the fixings team at Thomson Reuters and analysts at the BBA. The fixings team at Thomson Reuters has many years of experience in setting the rates. They are currently working closely with the BBA to programme these checks into their existing automated verification systems, and will be able to continue to refine and add additional analysis to the fixing process. The scope of the analysis will be widened as an ongoing project to continually refine and evolve the scrutiny of data.
- 2.14. If a submitted rate triggers a query, Thomson Reuters will immediately contact the bank in question and ask it to confirm its rate. Contributions that do not conform to the expected norms are usually a result of an error that is quickly rectified. This is an extension of current practice. If a bank confirms that it intends to submit a rate that would still trigger an alert, Thomson Reuters will contact the LIBOR manager who will ask the bank its reasoning for the submission. Each time this occurs, the LIBOR manager will log the circumstances and include full details in the regular report to the FX & MM Committee as described in 3.23, below. Discussion of this

report will be a standing agenda item at Committee meetings. Details of the report and discussions thereof will be confidential, and members may not disclose any information outside the committee meetings.

- 2.15. If, in the view of the LIBOR manager, a bank's submitted rate is aberrant or the bank's explanation for its submission is unsatisfactory, the LIBOR manager will inform the Fixings Sub-committee who will meet to consider the issue.
- 2.16. As part of the required procedures for contributors, as detailed in Appendix II, all contributors agree that:
  - (i) The LIBOR manager will visit all contributors regularly, at minimum once a year, in order to discuss the LIBOR process and get the contributor's views on market conditions and any areas of concern. These comments will be fed back to the FX & MM Committee.
  - (ii) The LIBOR manager may visit a contributor's office on an ad hoc basis to discuss its rate submissions, if these are queried by the FX & MM committee or subcommittees thereof. These discussions may involve a request for the bank to provide evidence to support its quotes. Any such evidence which includes sensitive information will be held in absolute confidence by the LIBOR manager: specifics of actual transactions or positions will not be shared with FX & MM Committee members.
  - (iii) Brokers can discuss contributors' trading behaviour with the LIBOR manager in absolute confidence.

#### Input from market

- 2.17. As LIBOR is used by participants from a wide cross-section of the market, it is proper that all participants should be allowed to comment on LIBOR rates. The BBA will therefore set up a secure page on the BBA LIBOR website which will enable interested parties to comment on rates. The address for this page will be included in future statements regarding governance and scrutiny of LIBOR.
- 2.18. This secure page will consist of a form which will require any parties to fill in details in a specified manner, listing the date, currency and tenor of the fixings they believe to be inaccurate, the reason why they believe this is the case and contact details. When complete, these will be forwarded to an email inbox accessible only to the LIBOR manager (or a colleague, in the event the manager is not available). It will be clearly stated that anonymous information will not be forwarded.
- 2.19. The LIBOR manager will investigate all emails received via this inbox and provide a full report plus initial commentary in the monthly report to the FX & MM Committee described in 3.23 below.
- 2.20. All submissions to this process will receive an automated reply thanking them for their comments, which will also commit the LIBOR manager to replying more substantially after initial examination and discussion by the FX & MM Committee.
- 2.21. Clifford Chance will provide an analysis of any legal implications of this process to the next meeting of the FX & MM Committee.

Presentation of data to Committees.

2.22. Each month the LIBOR manager will compile a report to be sent to the FX & MM Committee detailing the behaviour of contributors and comparing LIBOR rates with relevant market indicators. This will also contain full details surrounding any queried contributions.

2.23. The format of the report will be as follows:

<b>Heading</b>	<b>Description</b>
Queries	Report on any contributions that have triggered a query from Thomson Reuters or the BBA, with details, context and any comments or explanation from the contributors themselves.
Queries from sources other than Thomson Reuters	Report on any external queries and what action if any was taken.
Contributions	Detailed statistics on outlying and late contributors.
Governance and Scrutiny	Update from BBA on progress on implementing the new governance and scrutiny framework, discussions with potential contributors, central banks, regulators and other market participants.
Media	Round-up of media coverage of BBA LIBOR with links to original sources.
Public bodies	Schedule for secretary's regular meetings with public bodies interested in LIBOR. Reports on any such meetings since the last update.
Market feedback & development of LIBOR	Information on any new initiatives proposed by the BBA or requested by market participants. Brief update on the commercial status of LIBOR and relations with partners such as exchanges and major data vendors

## **Appendix I**

### **Draft terms of reference for the Foreign Exchange and Money Market Committee**

The Foreign Exchange and Money Market Committee ('the Committee') is the entity responsible for the governance of LIBOR.

1. The Committee is independent of the BBA and any other organisation.
2. The composition of the Committee is:-
  - a. At least one member from a panel bank for each of the 10 LIBOR rates.<sup>1</sup>
  - b. At least three members from financial entities other than banks that use LIBOR. Typically one from the fund management industry, one from corporate treasurers and one from major exchanges trading LIBOR products<sup>2</sup>
3. The Panel is to have a Chairman and typically two Deputy Chairmen. The Chairman to be drawn from a bank that is on the Panel for at least three LIBOR currencies including US dollar and sterling.
 

Where possible one deputy to be drawn from a non UK incorporated European bank and one from a US-incorporated bank.
4. The LIBOR manager is the secretary to the Committee and is non-voting.
5. All representatives on the Panel will be senior and practitioners with the relevant experience.
6. The Committee will meet regularly, typically bi-monthly.
7. The Committee will have two sub-committees. The Fixings Sub-committee will consider any relevant information in respect of concern about a rate or about a fix generally. The Oversight Sub-committee will decide what action needs to be taken in respect of a particular contributing bank referred to them by the Fix Committee. Each sub-committee is to be chaired by a Deputy Chairman of the Committee.
8. In discharging its responsibilities, the Committee is required to have policies and processes for checking the appropriateness of the contributions made to the relevant currencies by the contributing banks. These policies will be transparent and available on the LIBOR website.

---

<sup>1</sup> Although it may be that one contributing bank member can fulfil the necessary criteria for a multiple number of currencies, a broad spread of banks must be maintained on the Committee at all times.

<sup>2</sup> The total of members of the Committee from contributing banks must at all times be greater than the total of those from all other categories of membership.

9. The Committee will have arrangements in place for liaison with statutory authorities, particularly central banks.
10. All members of the Committee will serve as individuals representing their firms and will be expected to act in the best interests of the LIBOR benchmark and the markets it serves.
11. The Committee will publish its review of panel banks which in turn actively seeks additional potential contributors for consideration.
12. The FX & MM Committee secretary, on behalf of the Committee will produce a LIBOR annual report to include assurances from the contributing banks of their adherence to the standards for submitting their rate.
13. The Committee will be subject to the annual independent audit of LIBOR practices and processes which will form part of the BBA's regular audit.

## Appendix II

### **DRAFT Required Procedures for LIBOR contributors**

1. Each contributor bank must provide the Designated Distributor by 11.10 each London Business day **the rate at which an individual Contributor Panel bank could borrow funds, were it to do so by asking for and then accepting inter-bank offers in reasonable market size, just prior to 11.00 London time.** The definition of “funds” is: unsecured interbank cash or cash raised through primary issuance of interbank Certificates of Deposit.
2. The rate at which each contributor submits must be formed from that bank’s perception of its cost of funds in the interbank market. The area of the contributing bank that has the primary responsibility for managing that bank’s cash will be solely responsible for the calculation and accuracy of the rate submitted
3. The submitted cost of funds must be for funds:
  - I) at 11.00 London time
  - II) In the London market
  - III) In reasonable size
  - IV) Which are unsecured
4. Each contributor bank must supply the Designated Distributor and the BBA with the name, job title, telephone number, email and mobile telephone number of the appropriate person(s) to contribute rates (see 2, above), and provide the same details for an alternate. Should the contributing individual change roles so that they are no longer the appropriate person to contribute, the contributing bank must supply details of their replacement to the BBA and Designated Distributor.
5. For those banks that contribute to more than one LIBOR currency or have more than one individual responsible for setting BBA LIBOR rates, up to date details of all contributors as described above must be sent to the BBA and Designated Distributor.
6. Contributor banks must undertake to provide rates on every London business day. The exception to this shall be for BBA Euro LIBOR contributors, who must undertake to provide rates on every TARGET business day, including those that fall on London bank holidays.
7. Rates shall be submitted to five decimal places.
8. In the event that a contributed rate is queried by the BBA or FX & MM Committee, the contributor bank agrees to provide its rationale for that contributed rate in an informal or formal manner, as appropriate.
9. Contributor banks understand and accept that membership of each BBA LIBOR currency panel is at the sole discretion of the FX & MM Committee. By signing this document, each contributor bank agrees that should it be deselected from a panel, the FX & MM Committee decision is final and neither the bank nor its agents shall attempt any action, legal or otherwise, to influence or overturn that decision. By signing this document, the individuals so doing assert their ability to commit their institutions in this manner.

10. Contributors undertake to have their internal processes for submitting rates audited as part of their firm's annual compliance procedures and provide written confirmation to the FX & MM Committee that this audit has been completed.

11. The LIBOR manager will visit all contributors regularly, at least once a year, in order to discuss the LIBOR process and get the contributor's views on market conditions and any areas of concern. These comments will be fed back to the FX & MM Committee.

12. Contributors agree that the LIBOR manager may visit their office on an ad hoc basis to discuss a bank's rate submissions with individual contributors, if these are queried by the FX & MM Committee or subcommittees thereof. These discussions may involve a request for the bank to provide evidence to support its quotes. Any such evidence which includes sensitive information will be held in absolute confidence by the LIBOR manager.

13. The FX & MM Committee gathers data from a wide range of sources in order to ensure LIBOR remains an accurate benchmark. This includes input from brokers and the Wholesale Market Brokers Association. By signing this document, contributors agree that they are willing for brokers to discuss their trading behaviour with the LIBOR manager in absolute confidence.

Name of Bank \_\_\_\_\_

Name of signatory \_\_\_\_\_

Position \_\_\_\_\_

Signature \_\_\_\_\_

Date. \_\_\_\_\_