# My thwarted attempt to tell of Libor shenanigans

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In 1991, I began trading for Morgan Stanley, the investment bank, in London. I was trading bonds, derivatives and related securities. One of those securities was based on the three-month Libor rate: the interest rate at which banks can borrow money for three months from each other. Morgan Stanley does not trade on the interbank market so I could not directly borrow or loan money at Libor rates. What I could do, however, was trade a futures contract on the three-month Libor rate.

As an example of how a futures contract works, consider the following. Suppose that we are concerned about three-month Libor rates increasing in the future; in particular, we are concerned about what the three-month rate will be in September. If that rate is, say, 1 per cent, we can agree today to effectively lock it in. If, come September, the actual three-month rate is 2 per cent, then our contract will ensure we can still borrow at 1 per cent. Futures contracts on three-month Libor were – and are – traded on the London International Financial Futures Exchange (Liffe, now part of NYSE Euronext). There was a standard contract for the month of September. That contract had its rate settled on the third Wednesday of the month, at 11am.

In 1991, I had live trading screens that showed the Libor rates. In September of that year, on the third Wednesday, at 11am, I watched those screens to see where the futures contract *should* settle. Shortly afterwards, Liffe announced the contract settlement rate. Its rate was different from what had been shown on my screens, by a few hundredths of a per cent.

As a result, I lost money. The amount was insignificant for me, but I believed that I had been defrauded and I complained to Liffe. Liffe explained that the settlement rate was not determined by what rates were actually in the market. Instead, the British Banker's Association polled some banks, asking them what the rates were. The highest and lowest reported rates were discarded and the rest averaged, giving the settlement rate. Liffe explained that, in doing this, they were adhering to the terms of the contract.

I talked to some of my more experienced colleagues about this. They told me banks misreported the Libor rates in a way that would generally bring them profits. I had been unaware of that, as I was relatively new to financial trading. My naivety seemed to be humorous to my colleagues.

Simply put, then, it seems the misreporting of Libor rates may have been common practice since at least 1991. Although the difference between the reported rate and the actual rate might seem small, the total amount of money involved is material, given that Libor rates affect contracts worth hundreds of trillions. Also important is what such misreporting says about the culture.

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During 1991, at the London office of Morgan Stanley, the head of interest rate trading was a person who has been at the centre of the current scandal: Bob Diamond. I do not recall discussing Libor misreporting with Mr Diamond but since the misreporting was common knowledge among traders, I presume he was aware. (That, however, is not a criticism of Mr Diamond: what could he have done about this?)

There have been two distinct motivations for banks to misreport Libor rates. One motivation is discussed above: to directly increase profits. The other motivation arose during the 2008 financial crisis: to mask liquidity problems.

Libor misreporting has been going on for decades. Why have investigations only recently begun? It seems highly implausible that all the investigating agencies could have been unaware for decades. Indeed, those agencies have a reputation among traders of being like Potemkin villages. I suspect what has happened is that, after the financial crises of 2008, the agencies decided they ought to perform more of their stated duties. That would also explain why the investigations appear to be ignoring any misreporting in years before 2005: to cover up the illusoriness of their earlier work.

One of the investigations is being undertaken by the House of Commons Treasury committee. I telephoned the committee on July 3 and spoke with a committee specialist. I told the specialist about the foregoing and said that I was willing to testify under oath. The specialist seemed extremely interested. They said they were to have a meeting about the Libor scandal and would call me back afterwards. I did not hear back, however, so I phoned to ask what was happening. My testimony was not wanted, the specialist told me, because it "contradicts the narrative".

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