UK's FSA says failed to act fast enough on Libor

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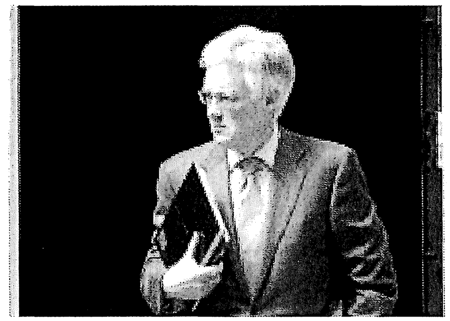
By Huw Jones



LONDON (Reuters) - Britain's financial watchdog said it should have been faster in spotting how banks "lowballed" Libor benchmark interest rates but stopped short of admitting to major regulatory failure.

After pressure from UK lawmakers in a scandal that has seen top bankers depart and banks fined billions of pounds, the FSA published a 103-page internal report into when it first knew about manipulation of the London Interbank Offered Rate (Libor).

Regulators around the world are still probing banks, traders and brokers who help set a rate which is used to price trillions of dollars of products from credit cards to home loans.

FSA Chairman Adair Turner said that at the time the watchdog had no direct oversight of Libor, and therefore "did not respond rapidly to clues that lowballing might be occurring", referring to banks submitting artificially low quotes to Libor compilation to give the impression they were having no difficulty borrowing money at the height of the 2007-09 financial crisis.

"The report also reveals that while some information was available relating to lowballing, there is, for the period covered, no evidence of any information, direct or indirect, available to the FSA which indicated that traders were manipulating Libor for profit," Turner said.

The FSA conceded it was too narrowly focused in its handling of Libor-related information, should have considered that it was likely Libor was being lowballed given cumulative information and should have better managed the information it did receive.

Two UK banks, RBS (RBS.L: Quote, Profile, Research, Stock Buzz), Barclays (BARC.L: Quote, Profile, Research, Stock Buzz), and Swiss UBS (UBSN.VX: Quote, Profile, Research, Stock Buzz) have been fined for rigging Libor and other benchmark rates, with others expected to settle similar charges soon.

The benchmark is compiled from banks submitting quotes for interest rates at which they say they could borrow.

The Bank of England, which also came under fire from UK lawmakers, said in a statement on Tuesday it was widely known that the Libor market had effectively closed as the 2007-09 financial crisis unfolded.

"This report shows that, where the Bank was aware of market rumors about the process for setting Libor, it passed them promptly to the regulator - the FSA," the central bank said.

DIRECT REFERENCES

The three banks were fined for manipulating Libor to make money on their derivatives contracts, or for low-balling.

The probe, which cost 600,000 pounds, covered January 2007 to May 2009 when markets were in turmoil and regulators were focusing on the "very viability" of lenders.

It searched 17 million records, reviewed 97,000 documents and interviewed 20 FSA staff or former staff.

It found 26 direct references to potential or actual lowballing, including two telephone calls from Barclays in March and April 2008, described as "the clearest contacts that indicated an individual bank was lowballing".

The FSA, which will be scrapped on March 31 and its bank supervisory tasks handed to the Bank of England, with a new standalone Financial Conduct Authority to handle enforcement, also published a 25-page management response to its report

The response said that the FSA's Martin Wheatley, who will head the new FCA, and the Bank of England's top banking supervisor Andrew Bailey accepted the main report's findings.

The management response said articles published by the Bank for International Settlements and the International Monetary Fund had argued that Libor was not being manipulated.

Neither the U.S. Commodity Futures Trading Commission nor the FSA were aware of Libor manipulation by traders until 2008 when evidence emerged while looking into lowballing, it added.

"The British Bankers' Association did not raise concerns over the conduct of market participants with the FSA," the FSA management response said, referring to the industry association which governs Libor.

Identifying trader manipulation in real time would have required "very large and perhaps disproportionate" staffing when direct supervision was not a legal requirement.

The report makes several recommendations to the Bank of England and the FCA, such as making sure staff circulate information internally better and are more inquiring.

Wheatley has already proposed reforming how Libor is set by stripping the BBA of its Libor governance role, introducing direct supervision, and criminal punishment for gaming rates.