# Libor: a question of ethics

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"It's getting so a businessman can't expect no return from a fixed fight," mused a mobster in *Miller's Crossing*. "Now, if you can't trust a fix, what can you trust?"

That's a very good question for the British Bankers' Association, guardian of the 150 varieties of the London Interbank Offered Rate, which attempt to measure banks' cost of funding. Those rates, which underpin the prices of trillions of dollars of loans and derivatives around the world, have always been a fabrication. No bank actually borrows at the three-month sterling Libor rate, for example; that rate is a trimmed average of the price of hypothetical transactions between hypothetical parties. Markets rely on that number, though, because they have faith in the BBA's ability to root out quotes from contributing banks that deviate too far from actual deals. The integrity of the "fix" is everything.

It is vital, therefore, that the BBA puts up a robust defence of its procedures during the regulatory investigations that have ensnared at least four banks. The BBA's basic method – gathering quotes on a voluntary basis, then stripping out top and bottom quartiles – has been copied around the world. But the subpoenas change the picture. Now that contributors are directly exposed to reputational damage, the BBA may have to pay them to remain on the panel.


It should also weigh the merits of a shake-up similar to New Zealand, which used to have a BBA-like system. Now, the rate is set based on a weighted average price of the volume of paper traded during a daily, two-minute window. New Zealand's benchmark used to be assumed to be an accurate barometer of the cost of funding; now it manifestly is. For the BBA, after 25 years of dealing in hypotheticals, it could be time to get real.

*E-mail the Lex team in confidence*