



LIBOR: FREQUENTLY ASKED QUESTIONS

1. What is ICE LIBOR and how is it calculated?

What is ICE LIBOR?

ICE LIBOR is designed to reflect the short term funding costs of major banks active in London, the world's most important wholesale financial market.

Like many other financial benchmarks, ICE LIBOR¹ (formerly known as BBA LIBOR) is a 'polled' rate. This means that a panel of representative banks submits rates which are then combined to give the ICE LIBOR rate. Panel banks are required to submit a rate in answer to the ICE LIBOR question:

"At what rate could you borrow funds, were you to do so by asking for and then accepting inter-bank offers in a reasonable market size just prior to 11 am?"

Although banks now use transaction data to anchor their submissions, having a polled rate is crucial to ensure the continuous publication of such a systemic benchmark, even in times when liquidity is low and there are few transactions on which to base the rate.

Currently only banks with a significant London presence are on the ICE LIBOR panels, yet transactions with other – non-bank – financial institutions can often inform panel banks' submissions.

'Reasonable market size' is intentionally unquantified. The definition of an appropriate market size depends on the currency and tenor in question, as well as supply and demand. The current wording therefore avoids the need for frequent and confusing adjustments.

11 am was chosen because it falls in the most active part of the London business day. It is also sufficiently early in the day to allow the users of ICE LIBOR to use each day's rates for valuation processes, which may take place in the afternoon.

All ICE LIBOR rates are quoted as an annualised interest rate. This is a market convention. For example, if an overnight Pound Sterling rate from a contributor bank is given as 0.5000%, this does not indicate that a contributing bank would expect to pay 0.5% interest on the value of an overnight loan. Instead, it means that it would expect to pay 0.5% divided by 365².

¹ Referred to here as 'ICE LIBOR' or 'LIBOR'

² The day count follows normal market convention: 365 days for GBP, 360 days for the other currencies

How is ICE LIBOR calculated?

ICE LIBOR is the ‘trimmed arithmetic mean’ of all of the panel banks’ submissions. This means that the highest and lowest 25%³ are removed and the rest is averaged (the actual number of banks removed depends on the number of submitters for each currency). The resulting rate is then published to the market at approximately 11.55 am London time⁴.

In order to help ensure the integrity of the rate, individual submissions are not published until three months after the submission date. This helps in two ways: firstly, it makes it harder for banks to set their submissions purely in line with other panel banks rather than at their own perceived funding costs; and secondly, it also protects banks from the negative signalling effects that their submissions might have on market perceptions of a bank’s financial viability. This credit-signalling or ‘stigma-effect’ was one of the conflicts of interest which led to attempted manipulation of the rate.

2. What is ICE LIBOR used for?

ICE LIBOR is an essential cog in the financial system. Its importance to the global financial industry and other non-financial companies arises from most corporate debt and interest-rate thinking being “ibor”-based. It is used as the floating rate for many financial contracts, from interest rate swaps to student loans, mortgages and corporate funding instruments. In total, hundreds of trillions of dollars’ worth of interest rate exposure is tied to ICE LIBOR. Given its role as a global funding benchmark, ICE LIBOR is also frequently used for valuing existing positions.

ICE LIBOR determines the settlement prices for some of the most important exchange-traded short-term interest rate futures contracts. These contracts help companies around the world hedge their interest rate exposure. They also provide private sector economists and central bankers with insights into market expectations of economic performance and interest rate developments.

ICE LIBOR is also an important indicator used by some central banks when determining their official interest rate target.

3. Why did a new administrator take over LIBOR and why did ICE Benchmark Administration (IBA) take on this responsibility?

In 2012, the Chancellor of the Exchequer commissioned Martin Wheatley (then managing director of the FSA and Chief Executive-designate of the Financial Conduct Authority (FCA)) to review the framework for setting LIBOR. The Wheatley Review into LIBOR concluded that the existing governance and surveillance frameworks were inadequate to safeguard the integrity of LIBOR. One of the key recommendations of the Wheatley Review was that LIBOR needed to be administered by an independent entity. The Hogg Committee selected IBA to take over (via a competitive tender process), and the FCA gave its authorisation from the 1st February 2014.

³ Indicative – please see ICE LIBOR explained for details

⁴ ICE LIBOR is expected to be published at 11.55 am London time as of 27 March 2017

As a leading provider of financial markets infrastructure globally, ICE was well placed to help restore credibility, trust and integrity to LIBOR. Specifically, its deep regulatory experience in many jurisdictions as both a front line regulator and a regulated entity, its technology skills and assets, and its long track record of managing other benchmarks, uniquely positioned ICE to restore market confidence in this crucial global benchmark.

4. “Administered by IBA, regulated by the FCA” – what does that mean?

Restoring the integrity of such an important and widely used benchmark as ICE LIBOR requires a combined effort from many organisations, including: the panel banks, the independent administrator (IBA), the regulator and other stakeholders. The FCA now has extensive new powers to supervise panel banks and to take individuals to court for benchmark-related misconduct. This increased regulatory oversight is a welcome development and is mirrored at both the European and the Global levels where the European Commission and the International Organisation of Securities Commissions (IOSCO) have published suggestions for strengthening benchmark governance. Banks have already committed significant resources and capital to improve their LIBOR processes and their internal governance, in line with new regulatory requirements.

As the new, independent administrator, IBA has introduced new surveillance systems and statistical analysis techniques which subject the submissions to much closer scrutiny. These compare the data provided by the panel banks with related markets, their own submission history and that of other panel banks. These tighter checks and controls will enable us to identify potential errors, manipulation and collusion, which will be escalated to the FCA.

We have also instituted an oversight and governance structure that emphasises independence, accountability and transparency for benchmark submitters and the administrator alike. We established an independent Board composed of experienced professionals and experts from the fields of financial markets, financial law and regulation. The Oversight Committee, which brings together key ICE LIBOR stakeholders from users, benchmark submitters and independent industry experts will regularly review the Code of Conduct. The Code has been approved by the FCA as industry guidance for the market, and will continue to evolve in order to reflect changes in the market and best practices.

5. ICE LIBOR Continuity

ICE LIBOR is a continuation of what was previously known as BBA LIBOR and there are no changes in how the rate is calculated or how the submissions are collected at present.

On 23 January 2014, the Loan Markets Association published two guidance notes discussing the impact of the administration of LIBOR moving to ICE. These are available for their members on their website: <http://www.lma.eu.com/documents.aspx>

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