Deutsche Bank Pays $2.5 Billion Fine for Interest Rate Rigging

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Deutsche Bank headquarters. Photo: gravitat-OFF. Used under Creative Commons license

Deutsche Bank has agreed to pay out a record $2.5 billion fine to settle U.K. and U.S. government investigations into allegations of fixing global interest rates, just months after six other banks paid out $4.3 billion on similar charges. Activists say that the banks should have faced criminal charges.

"The question remains: does the punishment fit the crime?" writes Angela McClellan of Transparency International. "We think not: why allow a company to settle when they fail to cooperate with the investigation? Also, given the gravity of the situation a big fine won't do, criminal charges should be considered as well."

The banks have been accused of manipulating the global system of interest rates for $360 trillion in financial contracts, notably the London Inter Bank Offer Rate (LIBOR). LIBOR is set by the British Bankers Association which publishes an average of rates reported to them verbally by participating bankers. Such rates exist for as many as 150 different kinds of loans – mostly for overnight transfers between banks although they ultimately also affect the price of consumer loans like mortgages, car loans and credit card loans.

Since LIBOR rates are set based on private conversations held between a small group of individuals that are not subject to verification, the banks have allegedly been fixing the rates illegally for over 30 years to increase profits, according to whistleblowers.

Government investigators have published transcripts of instant messages between traders to prove that they were knowingly rigging the interest rates.

For example, on August 20, 2007, Mark Wong of Deutsche Bank was quoted saying: "It's just amazing how Libor fixing can make you that much money or lose if opposite. It's a cartel now in London."

Two days later, Jezri Mohideen, head of yen products for Royal Bank of Scotland in Singapore, asking other traders to help him rig LIBOR rates.

Mohideen: "What's the call on the Libor?"
Trader 2: "Where would you like it, Libor that is?"
Trader 3: "Mixed feelings, but mostly I'd like it all lower so the world starts to make a little sense."
Trader 4: "The whole HF [hedge fund] world will be kissing you instead of calling me if Libor move lower."

Trader 2: “OK, I will move the curve down 1 basis point, maybe more if I can.”

Under the terms of the new settlement, Deutsche Bank has agreed to pay the regulators substantial fines to drop the investigation. The U.S. Commodity Futures Trading Commission (CFTC) was paid $800 million, the U.S. Department of Justice received $775 million in criminal fines, the New York state’s Department of Financial Services got $600 million in regulatory fines and the UK’s Financial Conduct Authority (FCA) was paid $344 million in regulatory fines.

Last November, Bank of America, Citibank, JP Morgan, HSBC, Royal Bank of Scotland and UBS also agreed to pay multiple regulators in return for dropping the investigations. Citibank and JP Morgan each paid out a total of $1 billion – $350 million to the CFTC and $310 million each to the U.S. Office of the Comptroller of the Currency. UBS, a Swiss bank, paid the FCA $371 million and a Swiss Franc 134 million ($138 million) fine to Finma, Switzerland’s financial regulator.

Regulators say that the public interest has been served because the banks have admitted that their staff were engaged in fraud.

“We must remember that markets do not just manipulate themselves: It takes deliberate wrongdoing by individuals,” Benjamin Lawsky, the superintendent of financial services for New York state said in a press release. “Deutsche Bank employees engaged in a widespread effort to manipulate benchmark interest rates for financial gain.”

“One division at Deutsche Bank had a culture of generating profits without proper regard to the integrity of the market,” Georgina Philippou, acting director of enforcement at the FCA said in a press statement. “This wasn’t limited to a few individuals but, on certain desks, it appeared deeply ingrained.”

Observers say that knowledge of the practice was likely to have extended beyond just one division. “It seems hard to imagine a situation today where such wide scale misconduct could be carried out without the executive management knowing or at least turning a blind eye,” Tony Brown, managing director of Bivonas Law, told the Financial Times.

Indeed the FCA noted that Deutsche Bank falsely claimed to have created controls over LIBOR traders, accidentally destroyed evidence; and took two years to provide other information requested by investigators.

Given these circumstances, McClellan says that the fines amount to no more than a slap on the wrist for the senior executives.

“Although the amount of the fine seems exorbitantly high, the deterrent effect of fines is questionable in this case too. The expected impact on Deutsche Bank’s earnings will be small,” she wrote. “The most effective deterrent for unethical behaviour are sanctions on individuals. There is still a possibility that criminal charges will be pursued. If these are senior enough people and the criminal investigation proceeds, this would send a strong signal to the banking community that bad behaviour results in personal punishment.”

Others agreed. “If senior executives like board members were not directly involved but responsible, they should go to jail,” David Pereiz, partner with the New York law firm Reisman, Peirez, Reisman and Capobianco, told the Wall Street Journal. Otherwise the misconduct is “never going to stop.”

The interest rate scandal is only one of several scandals surrounding the big global banks. Fifteen major banks are currently being for investigated for rigging the $5.3 trillion global foreign exchange market. The final tally of fines in the foreign exchange scandal has been projected to be as high as $41 billion.

Not surprisingly, the banks being investigated are the very same as those implicated in the interest rate scandal. Indeed just four major banks together control over half the foreign-exchange market, according to Euromoney, an industry publication. Barclays of the UK has 10.2 percent of the market, Citigroup in the U.S. has 14.9 percent, Deutsche Bank from Germany has a 15.2 percent share while UBS of Switzerland has 10.1 percent.

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