What's a financial scandal?

Thomas Angeletti argues that financial scandals are social phenomena with shared characteristics

What happens when a financial scandal occurs – as in the case of the LIBOR (London Interbank Offered Rate) scandal which is the focus here? In recent years, the number of newspaper headlines decrying financial scandals has increased significantly as has public interest. The manipulation of the LIBOR rate by major banks in 2012, the foreign exchange market manipulation in 2013, and the Swiss Leaks' scandal on tax avoidance and money laundering schemes at HSBC revealed in 2015, are significant examples of this growing concern. These scandals occurred in a time of financial crisis. What social phenomena are involved during such events? Financial scandals consist of situations where central conflicts in society are being tackled, where the authority of institutions is under question, and, finally, where there is debate about responsibilities involved – three points that I consider in more detail below.

Firstly, financial scandals occur when central societal conflicts are at stake, such as antagonism between social classes and, more broadly, inequalities. This is especially the case in finance, given that this sector has mainly contributed to rising inequalities in the last decades, especially in France (Godechot 2012) and the UK (Bell and Van Reenen 2010), as the research programme on the consequences of financialization has shown. These sources of inequalities have raised concern and public outrage. In 2011, the Occupy movement identified financial elites and financial places as sources of rising inequality. Debates of financial scandals regularly focus on the means available for elites to get rich – to express it in a trivial way – and the legitimate or illegitimate character of these means.

Secondly, scandals are specific situations where the authority of financial and regulatory institutions is questioned and put under the spotlight; their role is interrogated and this can lead to public controversies. For example, the scandal surrounding the LIBOR manipulation generated growing concerns about the definition and calculation of LIBOR, two processes supposed to be safeguarded by financial and regulatory institutions such as the British Bankers' Association. The LIBOR – as its name shows – is an interbank interest rate used in the financial markets and estimated on a daily basis in London. It was calculated for 10 different currencies (Euros, Dollars, Pounds, Yen, etc.) and for 15 different maturities (from one day to one year) at the time of the scandal. Considering the decisive role that LIBOR played in the financial markets, it is important to understand precisely how it is calculated. It is an estimated rate, not measured on past transactions, but made every day by several banks. The banks selected to present their evaluations are assumed to be 'major banks' in the currencies they are submitting. These banks send, daily, their estimation of the rate to the institution in charge of collecting them, Thompson-Reuters, which acts on behalf of the British Bankers' Association. In order to give their estimate, every submitter in the banks needs to answer the following 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?*. Take the example of the Yen rate. Every three months, a panel of 16 banks submitted their own estimated rate. Thompson-Reuters received the respective rates and made a daily calculation, discarding the top four submitted rates as well as the bottom four. A simple average is calculated on the eight remaining rates. That calculation method would not be so important if LIBOR had not been a key benchmark in the financial markets. The Wheatley Report estimated in 2012 that the total value of contracts using LIBOR as a benchmark amounted to US$300 trillion. This sum includes syndicated loans, floating rate notes, interest swap rates, exchange-traded interest rate futures and options, and forward rate agreements. In that way, LIBOR is linked to both commercial and personal consum-

er loans, including home mortgages and student loans. When a manipulation of a rate of such significance occurs or is being suspected, it is likely that there will be a decline in confidence in the ability of those institutions tasked with guaranteeing the functioning of financial markets.

Thirdly, there is a tension between an individualization and collectivization of responsibilities. The recent trial of Thomas Hayes, a trader convicted in the UK for his role in the manipulation of LIBOR, made this paradox explicit. Charged with eight counts of conspiracy to defraud, this trader was jailed for 14 years in August 2015. Through his particular case – it was the first case connected to the LIBOR manipulations that occurred in the UK – the financial system as a whole was questioned. Representatives of the British Bankers' Association as well as financial experts were called as witnesses to explain the regular functioning of financial markets. Over the course of the 11-week long hearings, the trial exposed different interpretations of this trader's actions by the prosecutor, the defence lawyers, the judge, several witnesses and the trader himself. In particular, there was a variety of views as to who was responsible for the LIBOR manipulation. On one hand, there were those that attributed responsibility to a single individual, the trader. The trader was seen as a lone individual and as the 'epicentre' of the LIBOR manipulation. The actions that led to the scandal were described in such a way that they could be attributed to this single person.

On the other hand, there were those that suggested that responsibility is collectively distributed and can be ascribed in that regard to much larger entities than individuals: a social group (the traders), a common culture (sustained by the regular contacts between the submitters of LIBOR and the traders), a bank (UBS, Citigroup), or even the financial system in itself. Such tensions between an individualization and collectivization of responsibilities can be observed in several court cases involving traders in the recent years – such as the affair of Jérôme Kerviel and Société Générale in France in 2008. This tension between individual and collective responsibility is even more significant if we consider that this trial took place after several banks had already paid fines, including the employer of this condemned trader. Of course, in the logic of criminal law, individual responsibility is the primary dimension to focus on, and all the references that are being made to another level must be formally discarded. But if we consider traders as individuals in positions that can lead to collective risk-taking, the division between criminal condemnation of mid-level traders and the payment of fines by banks appears especially inadequate.

These three distinct dimensions – conflicts in society, challenges to the authority of institutions, and conflict over the allocation of responsibilities – are not always combined in the same way in different financial scandals. It is only by studying these scandals and the interplay of these different dimensions that we can gain a better understanding of the place of finance in contemporary societies, as well as the expectations and critiques of citizens among elites.

References

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Thomas Angeletti is a sociologist and postdoctoral researcher at the Max Planck Institute for the Study of Societies in Cologne. He visited **carr** in July and August 2015.