



The Global LEI Initiative

LEI Issuance and parent registration slowing, FIG comments on where to go next

A Research Note by Financial InterGroup

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Inside this report:

LEI ISSUANCE

- Total LEI Issuance at all time high 1,148,170. How many more to go no one knows
- LEI Issuance trending lower in 2018: Jan - 92,029, Feb – 39,760, Mar – 33,120
- Total lapsed LEIs still increasing in 2018: Jan 171,142, Feb 175,540, Mar 179,803

RELATIONSHIP DATA COLLECTION

- Full parent Relationship Data Collection reaches 122,806 but 1,560,558 have no parents or chose an opt out exception
- Full parent Relationship Data Collection slowing in 2018: Jan 20,859, Feb 10,381, Mar 3,368
- The majority of parent/ultimate parent data that is ‘entity supplied only’ is 69-70% vs. being completely or partially validated by the LOU (30-31%) as required.

FIG COMMENTS – Beyond the LEI Issuance and Relationship Data Collection phase

- Facilitating risk data aggregation and risk reporting
- Maintaining data quality
- Following accountants’ consolidation rules and beyond
- Potential for direct input from original sources
- The encrypted LEI



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The Global Legal Entity Identification Foundation (GLEIF) has been reporting statistics on Legal Entity Identifier (LEI) data since January, 2016. We are pleased to bring you this Research Note on the GLEIF’s March 2018 reporting of LEI Issuance¹, the progress on Relationship Data collection, and our comments.

LEI ISSUANCE

This month again saw the momentum of LEIs being issued declining. Whether the year-end rush to register LEIs due to the European Union’s (EU’s) MiFid II ‘No LEI No Trade’ rule exhausted most of the eligible registrant’s or was impacted temporarily by the EU’s six month moratorium remains to be seen.

After crossing into a first ever record of over one million LEIs issued through January, 2018 the number of LEIs issued as of month-end March, 2018 now stands at 1,148,170. In the eleven months since LEIs were required to register LEIs for MiFid II trade reporting and register their parent LEIs, 641,714 LEIs have been registered (month-end April 30, 2017 506,456 – March 31, 2018 1,148,170), representing 56% of total LEIs issued.

This is occurring at the same time that the 29% ratio of issued vs. lapsed LEIs at year-end 2016 has declined significantly to 15.7%, although the total lapsed LEIs at 179,803 are now at an all-time high.

	2016 Year-end	2017 Year-end	Jan. 2018 Month-end YTD	Feb. 2018 Month-end YTD	Mar. 2018 Month-end YTD
	2016 Monthly Avg.	2017 Monthly Avg.	Jan. 2018 Month-end	Feb. 2018 Month-end	Mar. 2018 Month-end
Newly Issued	5,334	40,237*	92,029	39,760	33,120
Lapsed	6,300	7,134	7,494	8,296	8,904
Net Increase/decrease	-996	33,103	84,535	31,464	24,216
Lapsed rate	29.0% (Year-end %)	17.4% (Year-end %)	16.0%	15.8%	15.7%
Total Lapsed (Year & month-end Totals)	139,461	169,778	171,472	175,540	179,803

* Monthly average Jan. - Sept. 7,476 vs. monthly average Oct. – Dec. 127,281

The Regulatory Oversight Committee (ROC) expects that the ‘Lapsed issue’ will be dealt with through the ROC’s corporate action consultation, having conjectured that this problem may be caused by ‘non-operational’ LEIs. A follow up Webinar is scheduled for April 18, 2018 when the

¹ GLEIF Data Quality Report – March 2018 <https://www.gleif.org/en/lei-data/gleif-data-quality-management/about-the-data-quality-reports/download-data-quality-reports/download-global-lei-data-quality-report-march-2018#>, Apr. 6, 2018

ROC’s recommendations on this consultation are expected to be discussed as well as the data history and funds relationship hierarchies’ consultation.

The ROC has stated its position that Lapsed LEIs should not be permitted to be used in transaction reporting while the EU has done the opposite, confirming Lapsed LEIs are permitted in their reporting regimes for counterparties and clients of investment firms.

As annual renewals progress we will be monitoring the lapsed rate as a means to observe the influence the ROC has to enforce their renewal mandate vs. EU regulators’ allowing lapsed LEIs. Also it is not yet apparent as to the effort the ROC has ahead of it to obtain a complete set of LEIs for all required financial market participants. The total LEIs required have yet to be accurately estimated. Also, there is no regulatory compulsion to reject LEI registrations if they have not filed their relationship data. The ROC has no regulatory authority to compel compliance. They rely on sovereign regulators to promulgate the necessary rules to compel compliance.

RELATIONSHIP DATA COLLECTION

March, 2018 was the eleventh month for GLEIF’s collection of relationship data (Level 2 data) or what is referred to as ‘who owns whom’ data – the immediate parent and ultimate parent of each LEI. After next month’s Level 2 data collection (May, 2018) GLEIF will have entered the annual renewal cycle for the new LEIs registered with reference to their immediate and ultimate parent LEIs. We will continue to monitor lapsed rates and particularly of these LEIs registered after May 1, 2017.

Level 2 Relationship Data	Number of Immediate & Ultimate LEI Parent Records	Month-to-Month Change
Year-end 2017	88,198	-
Month-end January 2018	109,057	20,859
Month-end February 2018	119,438	10,381
Month-end March 2018	122,806	3,368

In their data quality reporting the GLEIF has begun to report statistics on “LEIs with Parent Relationships” (72,953, up 2.87% from last month’s 70,564). This statistic is the sum of unique LEIs for registration entities reporting both an immediate and ultimate parent. This compares to the 122,806 statistic (shown in chart above) at month-end March 2018 which includes 49,853 LEIs that have either an immediate or ultimate parent (international branches, stand-alone entities) but not both (122,806 – 72,953). As can also be seen from the Month-to-Month Change column in the above chart the monthly reporting of the number of registered LEIs with parent relationships has been steadily declining since such data has been reported by the GLEIF.

Also the GLEIF has begun to report statistics on “LEIs with Complete Parent Information” (834,384, up 8.26% from last month’s 770,652). This figure is comprised of the earlier parent relationship figure plus the legal entities that reported reasons why they were not providing either an ultimate parent LEI and/or an immediate parent LEI.

In the recording of these relationship records, the descriptions in the table below are those used by GLEIF to instruct registrants and LOUs on their submission of data for the Reporting Exceptions file, currently containing 1,560,558 records vs. last month's 1,435,891 and the prior month's 1,309,801.

The bulk of the exception records in the eight months reported to GLEIF in 2017 (1,113,932 records) at the start of collecting relationship data were recorded by the registering legal entities themselves, 76%, in Q2, 51-52% in Q3 and 69-70% in Q4. The latest GLEIF business report (Q4 2017) presents the percent of parent and ultimate parent 'entity supplied only' data (69-70%) as opposed to this data being completely or partially validated (30-31%) by the LOU. LOUs are expected to do this validation. ²

The number per Exception Reason for Each Direct Accounting Consolidation Parent and each Ultimate Accounting Consolidation Parent follows (A more detailed explanation of what each category in the below chart includes is available in FIG's February's LEI Research Note, [The Global LEI Initiative: Starting the Second Million New Year - Progress and Pitfalls](#)):

EXCEPTION REASON	All LEIs	Newly Registered LEIs 01May2017**– 31Mar2018
NON_CONSOLIDATING	516,175	383,143
NO_KNOWN_PERSON	427,734	304,770
NATURAL_PERSONS	365,066	300,424
NO_LEI	189,161	92,135
CONSENT_NOT_OBTAINED	43,345	23,115
BINDING_LEGAL_COMMITMENTS	5,971	3,082
LEGAL_OBSACLES	6,271	3,757
DISCLOSURE_DETRIMENTAL	3,755	1,746
DETRIMENT_NOT_EXCLUDED	3,062	1,760
Total Exception Records	1,560,540***	1,113,932

** May 1, 2017 is the date GLEIF began accepting Level 2 data from prior and newly registered LEIs.

*** The GLEIF reports 1,560,558 Exceptions, the difference of 18 records attributed to timing differences in receipt and processing of the files.

Note: the above data was supplied in collaboration with **pTools (www.ptools.com)** a Dublin, Ireland and UK domiciled technology company driving digital transformation in finance.

The required number of parent relationships still has to be determined. Out of 1,148,170 issued LEIs, just 72,953 have reported with complete parent data, another 49,853 with either one or the other parent and the balance either not reporting at all or reporting the reasons why they could not do so – see chart above for exception reasons.

² GLEIF, Global LEI System Business Report, <https://www.gleif.org/content/4-lei-data/2-global-lei-index/2-download-global-lei-system-business-reports/20180214-download-global-lei-system-business-report-q4-2017/2017-12-31-quarterly-business-report.pdf>, at page 9, Feb. 14, 2018

Parent information is essential to aggregating transaction data for monitoring systemic risk, the reason regulators had first embarked on this data standardization initiative. Accurate parent information is essential. If relationship data continues to be supplied by the registrant without validation by the LOU, then a longer term validation solution will be required. We address this in our FIG Comments section below.

FIG COMMENTS – Beyond the LEI Issuance and Relationship Data Collection phase

Facilitating risk data aggregation and risk reporting

The collection of a first generation of GLEIF data files is well underway and the initial set of known issues are, with all good intention soon to be resolved. We now need to focus on the quality of the data and if LEI data can be used for its intended purpose, risk data aggregation both within companies (enterprise risk) and across companies (systemic risk). Specifically to this later point, in its 2017 progress report on the 30 Globally Systemically Important Financial Institutions (G-SIFI's), the evaluating supervisors expressed their belief that the LEI has an important role to play in the implementation of their 'Principles for effective risk data aggregation and risk reporting' (known as BCBS 239).

“LEI availability could enhance banks’ management of information across legal entities, facilitate a comprehensive assessment of risk exposures at the global consolidated level and improve the speed at which information is available internally and to supervisors, especially after a merger and acquisition.”³

Maintaining data quality

Maintaining the quality of the LEI's reference data and relationship data in the GLEIS is now accomplished through a two tiered process, a first tier validation at the LOU level based on accessing authoritative sources and a secondary 'crowdsourcing' challenge mechanism. The validation of reference data by LOUs has been recorded by the GLEIF since Q1 2016, starting at 75% and reaching as high as 89%. It has settled at 85% in Q4 2017.⁴ Relationship data has been reported on by the GLEIF through the first nine months of the Level 2 data collection process (Q2-Q4, 2017). LOU validation rate has gone from a low of 24%, to 51-52% in Q2, and, in the last quarter to 30-31%.

In addition each financial institution, regulator, data vendor, financial analysis company, et al relies on a myriad of commercial companies, governmental data sources and trading venues to supply registration and ownership information. The sources for this data is selected by each organization, based on their own history of quality and costs, and the degree of difficulty in accepting additional sources into their technology and operational environment. Costs limit the number of commercial sources that can be used. It is hoped that the GLEIS data is to become

³ Bank for International Settlements (BIS), Basel Committee on Banking Supervision (BCBS), Progress in adopting the Principles for effective risk data aggregation and risk reporting, <https://www.bis.org/bcbs/publ/d399.pdf>, page 20, Footnote 8, March, 2017

⁴ See footnote 2 at page 4

another source, a free source for this data, and eventually becoming the best quality golden source of this data.

Going forward, the challenges remaining beyond the quality of the data will be twofold. First, as stated earlier, can the hierarchical information supplied by GLEIF be used for risk data aggregation as anticipated? Secondly, can the GLEIS reduce costs for the industry overall, as was the original business justification that enabled the industry to support the LEI initiative and champion regulatory compulsion to overcome the industry's collection action problem.

Following accountants' consolidation rules and beyond

It has been our long-standing advice to engage with accountants to assure the completeness and quality of GLEIS data. This was first proposed to the SEC and CFTC as they became champions for the LEI initiative for US markets, then to the Financial Stability Board as they took on the LEI initiative globally, and finally to the GLEIF. Long before, we engaged with Big 4 accounting firm Chairman to assure their interest and that of the accounting profession. At that time they had been collaborating on their own global legal entity database for determining partner conflicts of interest in ownership of public companies.

In addition, accountants have had a need on behalf of their clients to validate each legal entity for its materiality (exposure to misstatements in financial reports) as they consolidate these entities' financial information up to the reporting parent. This accounting consolidation process and accountants professional judgments applied to this process is the method of organizing Level 2 data the ROC adopted for determining the hierarchical relationships of LEIs for the GLEIS.

An accounting firm not being aware of a legal entity that is part of an organizations' hierarchical structure can lead it to material misstate financial results in the consolidated financial statements. This is why the auditors need to know each new, acquired, merged, sold or retired entity within an organizations' relationship hierarchy. They also use their professional judgment to determine which entities should be consolidated when globally accepted accounting consolidation rules require such judgement.

The above activity carried out by accountants are the same processes that is supposed to be captured in the GLEIS and validated by LOUs. However, while the accountants along with their clients are considered the authoritative source of this data, the authoritative source for the GLEIS are sources that, at best, are one step behind those of the registrants. This delay will become more evident and more problematic when the GLEIS moves from its current data conversion mode of taking in existing LEI and relationship data and cleaning it up, to that of knowing when changes to that collected data takes place and maintaining timely and accurate updates as it occurs.

Potential for direct input from original sources

Finally, misinterpretations of manual sources of data that are entered into the many currently identified 'authoritative sources' will over time corrupt the accuracy of the data. GLEIF and XBRL International are collaborating on this problem. As an example of a starting point is the US's requirement for every reporting company to provide a schedule of its legal entities, signed off by their auditors in their formal filings to the SEC.

Hopefully they will take up our long-standing recommendation to obtain at-source data for directly placing it into the GLEIS. This should start with US legal entities overseen by their auditors adding the LEI for each entity to the already required SEC 10k Exhibit 21 schedule and reporting the hierarchy in XBRL format. XBRL is the way in which computer readable financial reports are reported for the main financial statement. Making this reporting process timely, with changes required on an immediate basis, will solve the looming maintenance problem. It will also be the route to assuring the highest quality data. That bodes well for the GLEIS to become the singular authoritative source for timely, accurate and comprehensive financial market participant data, leading to meeting objectives for data aggregation and cost savings, the reason both industry and government started on this path.

The encrypted LEI

A final thought. As more interest appears around cybersecurity and secure identity management, the opportunity of legal entities themselves owning and securing their digital identities becomes more relevant. To this end obtaining and validating a secure encrypted code through the legal entity Identification system could become the definitive way to assure legitimate and secure entry into global financial transaction systems. Obtaining such a key, the LEI, is currently the responsibility of the codes registrant, the legal entity itself. However, with proper electronic notarization, complemented by a private code known only to its auditor, that code can become encrypted and anonymous.

An encrypted code would assure its protection as both a transparent identity for regulators on a need to know basis, and, on a redacted basis for order placement, trading and securing financial transactions. This also sets up a trusted source at the transactions source level allowing this duopoly of the client and its auditor to give assurances of a trusted transaction directly with its counterparty over any future Blockchain application. Already the Big 4 provide all manner of assurance services to its clients and one of the Big 4, PwC has launched an audit service for Blockchains⁵. In fact the most meaningful application for a secure legal entity key would be a Blockchain application of the GLEIS itself with notarized and secured direct input from the registrants themselves.

⁵ WSJ, PwC Has an Answer for the Blockchain: Audit It, <https://www.wsj.com/articles/pwc-has-an-answer-for-the-blockchain-audit-it-1521194401>, March 16, 2018

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