



# The Global LEI Initiative

LEI issuance, lapsed LEIs and parent registration all inch up.

## A Research Note by Financial InterGroup

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### Inside this report:

#### **LEI ISSUANCE**

New highs reached for LEI issuance as well as total lapsed LEIs

#### **RELATIONSHIP DATA COLLECTION**

LEIs for parent relationships inch up

#### **COMMENTARY**

Maintaining the LEI

LEI Hierarchies Intended for Risk Analysis

Keeping the Cost Savings and Risk Mitigation Objectives in Site

Unifying an Alphabet Soup of Identifiers

The Illusive Golden Copy

Resolving Remaining Issues

Sustaining Yesterday's Interoperability Model vs. Tomorrow's Distributed Technologies



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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 May, 2018 month-end and year-to-date reporting of LEI Issuance<sup>1</sup>, the progress on Relationship Data collection, and our comments.**

## LEI ISSUANCE

This month saw a slight uptick of issued LEIs after a progressive decline over the last four months of 2018. This decline preceded the run-up in LEI registrations precipitated by year-end 2017 MiFid II LEI “No LEI No Trade” requirements. The current decline is probably being impacted by the EU’s six month moratorium on the requirement to obtain a LEI, originally set for year-end 2017, now reset to month-end June, 2018.

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 May, 2018 now stands at 1,195,780. In the twelve months since LEIs were required to register LEIs for MiFid II trade reporting and register their parent LEIs, 689,324 LEIs have been registered (month-end April 30, 2017 506,456 – April 30, 2018 1,195,780), representing 58% of total LEIs issued.

This is occurring while the ratio of issued vs. lapsed LEIs at year-end 2016 of 29% has declined significantly to 15.5%, although the total lapsed LEIs are on a steady yet small monthly uptick to another all-time high at 186,021. Beginning May 1, 2018 GLEIF has 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 those LEIs registered in the last quarter of 2017 when the monthly average of registered LEIs leapt from 7,476 from the prior three quarters of 2017 to 127,281 in the last quarter.

	2016 Year-end	2017 Year-end	Jan. 2018 Month-end YTD	Feb. 2018 Month-end YTD	Mar. 2018 Month-end YTD	Apr. 2018 Month-end YTD	May 2018 Month-end YTD
	2016 Monthly Avg.	2017 Monthly Avg.	Jan. 2018 Month-end	Feb. 2018 Month-end	Mar. 2018 Month-end	Apr. 2018 Month-end	May 2018 Month-end
Newly Issued	5,334	40,237*	92,029	39,760	33,120	22,882	23,412
Lapsed	6,300	7,134	7,494	8,296	8,904	7,529	6,409
Net Increase/decrease	-996	33,103	84,535	31,464	24,216	15,353	17,003
Lapsed rate	29.0% (Year-end %)	17.4% (Year-end %)	16.0%	15.8%	15.7%	15.7%	15.5%
Total Lapsed (Year & month-end Totals)	139,461	169,778	171,472	175,540	179,803	183,466	186,021

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

<sup>1</sup> GLEIF Data Quality Report – May 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-may-2018#>, June 4, 2018

## RELATIONSHIP DATA COLLECTION

May 2018 represented the first month of data collection after a full year of GLEIF’s relationship data (Level 2 data) initiative or what is referred to as ‘who owns whom’ data – registering and collecting the immediate parent and ultimate parent of each LEI. In their data quality reporting the GLEIF reports statistics on “LEIs with Parent Relationships” (79,270, up 3.9% from last month’s 76,268 which was up 4.5% from the prior month’s 72,953). This statistic is the sum of unique LEIs for registration entities reporting both an immediate and ultimate parent. This compares to the 134,141 statistic (shown in chart below) at month-end May 2018 which includes 54,871 LEIs (134,141 – 79,270) that have either an immediate or ultimate parent (international branches, stand-alone entities) but not both.

As can also be seen from the Month-to-Month Change column in the chart below the monthly reporting of the number of registered LEIs with parent relationships has begun to decline after increasing for the first time last month after steadily declining since such data has been reported by the GLEIF.

<b>Level 2 Relationship Data</b>	<b>Number of Immediate &amp; Ultimate LEI Parent Records</b>	<b>Month-to-Month Change</b>
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
Month-end April 2018	129,128	6,322
Month-end May 2018	134,141	5,013

Also the GLEIF’s statistics shows a steady rise in “LEIs with Complete Parent Information” (963,991 up 5.9% from last month’s 909,859 which was up 9.05% from the prior month’s 834,384). 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 recording these relationship records in the Reporting Exceptions file there are currently 1,814,341 records as of month-end May vs 1,067,968 at year-end 2017.

<b>Level 2 Reporting Exceptions</b>	<b>Number of Immediate &amp; Ultimate LEI Parent Exception Records</b>	<b>Month-to-Month Change</b>
Year-end 2017	1,067,968	-
Month-end January 2018	1,309,801	241,833
Month-end February 2018	1,435,891	126,090
Month-end March 2018	1,560,558	124,667
Month-end April 2018	1,700,551	139,993
Month-end May 2018	1,814,341	113,790

Also, as of year-end 2017, legal entities with LEIs have identified that they have parents, but those parents do not have LEIs. There are 72,000 direct parents and 69,000 ultimate parents in this category. They have been separately recorded by the GLEIF, given a code different than an LEI and the associated reference data kept in a private database until the ROC decides what to do

next. These 141,000 entities, when compared to the year-end 88,198 that have complete parent information, suggests a large gap in the collection process. This could lead to the inability to use the LEI for aggregating financial transaction data for risk analysis. As of this time only 39% of known legal entities with parents potentially at risk are included in the database.

A more detailed explanation of those categories used by registered legal entities to explain their reason for not supplying LEI parent data is available – see FIG’s February’s LEI Research Note, [The Global LEI Initiative: Starting the Second Million New Year - Progress and Pitfalls](#)) at pages 3-4.

## COMMENTARY

### **Maintaining the LEI**

Maintaining updates to the LEI code itself is critical to correctly recording all entities and most importantly the controlling entities at risk in financial transactions. Maintaining the quality of associated LEI reference data, measured by both the lapsed rate and by challenge metrics, are important indicators of a maintenance discipline as they act as a proxy for data quality. Also, using the LEI as the prefix for the Unique Transaction Identifier (UTI) places additional burdens on timely and correct changes to LEI data.

The importance of finalizing the way timely updates to the identifier itself is resolved is critical to data quality and the usefulness of the LEI system for risk analysis. For example many unresolved issues exist: establishing one of two existing LEIs when mergers or acquisitions occur; new assignments of LEIs to replace multiple existing merged entities; resolving which entity would be responsible for decommissioning existing LEIs when companies go bankrupt or informally close down operations; resolving whether a new LEI is to be issued for spin-offs and under what circumstances; how to define parentage for special purpose entities (SPEs); whether or not to record a new LEI when a change of control takes place due to capital restructuring/share ownership changes; what change, if any, should occur to the ultimate parent LEI if the ultimate parent moves from its original headquartered risk reporting regime to another.

Thereafter, and most importantly, will be how updating the ultimate and immediate parents’ LEI reference data occurs due to corporate reorganizations and changes in control that update the underlying LEIs. This is particularly complex because both updates and searches must be propagated throughout the globally disbursed databases of each LOU that may contain component LEIs of the entire hierarchy of all LEIs making up the ultimate parent.

Notwithstanding the above remaining issues, use of the LEI for precise identification of a financial market participant is probably the most successful aspect of the LEI initiative to date although timing issues in updating the LEI database and global adoption is still a concern. Regulatory compulsion, expected to overcome the financial industry’s failure to solve their collective action problem has now reemerged as regulators collective action problem. For example only recently did the Bank of England mandate the use of the LEI in payment processing systems.<sup>2</sup>

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<sup>2</sup> Bank of England, ISO 20022 consultation paper: a global standard to modernise UK payments, <https://www.bankofengland.co.uk/-/media/boe/files/payments/iso-20022-consultation-paper.pdf>, June 2018

### **LEI Hierarchies Intended for Risk Analysis**

Different configurations of LEI hierarchies will be critical to meet industry and regulatory objectives for aggregating data to accommodate common risk mitigation methods: systemic risk management; enterprise risk management; counterparty risk management; credit limit setting, trading limit setting; concentration risk; and other yet to be determined needed LEI hierarchies. The singular accounting hierarchy currently being accommodated in the ongoing relationship data collection effort relies on account consolidation rules used in financial reporting. It is a way of starting on this data collection journey, not the end of the journey.

Whether these reconfigurations of the hierarchies is to be left to each individual sovereign regulator and/or individual financial enterprise remains to be decided. However, without a standard for such other hierarchies the usefulness of the new data standards regime for systemic risk analysis will be put at risk. This later point is tied to the still unmet need of applying standard measures of risk to the data that is aggregated. This is distinct from aggregating transactional data as each risk reporting regime may be different. It may require incorporating further details of each LEI's risk regime into the reference data of the Global LEI System (GLEIS). Here maintaining a proxy for each risk regime such as a code for each financial market regulator that oversees the legal entity could follow the same GLEIF process for maintaining the '[Entity Legal Forms \(ELF\) Code List](#)'.

### **Keeping the Cost Savings and Risk Mitigation Objectives in Site**

Entire hierarchies of LEIs was always expected to be the defining and ultimate objective for the success of the global LEI data initiative. The declaration by the ROC and the GLEIF that the LEI initiative is fully implemented under the G20 framework and the Financial Stability Board (FSB) framework confers a sense of finality to the GLEIS as a 'system'. This begs the question of whether industry members and the large set of sovereign regulators, along with the set of global standards entities, would confer such finality to this effort when the objectives of risk aggregation and significant cost savings has not been achieved.

Fulfilling these dual objectives requires that not only must the LEI effort be concluded, but the Unique Product Identifier (UPI), UTI and CDE (Common Data Element) standards as well. To be fully operational the GLEIS must be timely updated and work in an integrated way with the other standards.

### **Unifying an Alphabet Soup of Identifiers**

Further complicating these efforts is the competing interests of International Securities Identification Standards (ISIN) issuance organizations with those of global derivatives interests and US regulators in supporting different standards for the EU, for the US and for the derivatives industry. ISINs for derivatives are being issued by ANNA's Derivatives Service Bureau (DSB) and used in transaction reporting, generated in real-time without validation of data elements at its source. Also conceptual design problems have arisen, most notably around different ISINs assigned at different trading venues for the same Swap product and issuance of multiple ISINs for each maturity date of a swap.

It should also be noted that neither the governance nor technical definition of the system of the UPI<sup>3</sup>, nor the set of CDE's<sup>4</sup>, are finalized. In regard to the UPI the GLEIF has proposed to conduct the governance function for it, which would go far in providing an integrated framework for these two critical pillars of financial transactions. Even more than a framework, taken together with the already recommended use of the LEI for the UTI, it shows promises for an integrated data identification scheme that was originally anticipated by the US Treasury's OFR, the SEC and CFTC when such an identification scheme was first proposed by regulators back in 2010.

### **The Illusive Golden Copy**

The Global LEI System has as its objective to maintain the highest quality data base worthy of a golden copy designation for reference data associated with every financial market participant globally. This is similar to the objective of the Financial Instrument Reference Data System (FIRDS), a European Securities and Markets Authority's data base of reference data associated with every financial instrument and contract trading on EU trading venues.

Both databases are intended to be queried by financial enterprises to update internal records of trades with standard identifiers and common data elements. Those trades then flow to one of 25 trade repositories established in multiple sovereign countries and regional territories. Trades are accumulated for regulators' use in data aggregation at each trade repository and, for systemic risk purposes, across all of them although this capability has not yet been demonstrated.

Let us be reminded that this golden copy journey of identity standards and common reference data was begun three decades ago at the time of the market crash of 1987. Industry members still struggle to comply with all the new data standards and data reporting rules while encountering a plethora of issues. In the case of FIRDS some fundamental systems design issues have arisen with untimely setup of new instrument data at the source end of FIRDS, where trading venues update FIRDS. The GLEIS issues have been identified previously in this Research Note.

Both data bases suffer from the age old "garbage in garbage out" phenomenon where manual activities at source introduce human error. It would seem that a solution to this problem could be found in using pre-defined input taxonomies (like XBRL for financial statement reporting) that is designed for gathering input directly from the word processed source documents where all of this input is originated from. Overseeing the preparation of these documents by a second source (perhaps by an auditor-provided assurance service) could go a long way in improving data quality.

### **Resolving Remaining Issues**

Caution is also warranted in the face of billions of financial transactions containing data sourced from the GLEIS and FIRDS sitting in trade repositories, unable yet to aggregate this data. With so

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<sup>3</sup> FSB, Public responses to the second consultation on Governance arrangements for the unique product identifier (UPI), <http://www.fsb.org/2018/06/public-responses-to-the-second-consultation-on-governance-arrangements-for-the-unique-product-identifier-upi/>, June 4, 2018

<sup>4</sup> BIS, Harmonisation of critical OTC derivatives data elements (other than UTI and UPI) – third batch, <https://www.bis.org/cpmi/publ/d160.pdf>, June 2017

much yet to be done, and recognizing it would be hard to slow down regulatory momentum, it still may be wise to do so. The FSB might want to address these remaining issues quickly, not as individual issues but collectively as part of their data aggregation consultation. The FSB's data aggregation consultation embodied the end objective for all data standards initiatives, that of data aggregation for risk analysis. That consultation had been left in a 'framework state'. Now a more granular and detailed follow-up should be called for.

Leaving all these FSB inspired initiatives to be implemented piecemeal and in silos, and postponing the tough issues to the end, leaves regulators and the industry on a path to a fragmented, incremental and costly solution. What is needed, and what was expected was a common data structure, integrated identification scheme and a forward looking technology platform for the global financial industry's 21<sup>st</sup> century digital future not one based on legacy mindsets of best practices of the past.

### **Sustaining Yesterday's Interoperability Model vs. Tomorrow's Distributed Technologies**

It is important to evaluate all these initiatives together, especially at this time, to make sure there are no conceptual design flaws that have already been exposed. Fixing each problem as they are encountered may again breed a patchwork of workarounds - much like how the existing data management infrastructure evolved, requiring mappings and interoperability handoffs, manual reconciliations, text and fax communication, and a myriad of costly data and infrastructure intermediaries to move data along the financial industry's supply chain.

Already the new set of regulations promulgated since the financial crisis has spawned another permanent set of post trade financial infrastructure intermediaries. Multiple entities: Trade Repositories; Local Operating Units; OTC Central Counterparties (CCPs), Collateral depots and Clearing houses; and Approved Publication Arrangement (APA) services providers; and singular entities: FIRDS, DSB and GLEIF. Soon to come are the UPIs new infrastructure entities, potentially multiple UPI Service Providers 's and Reference Data Library (RDL) operators – the number yet to be determined. Truly a new Rube Goldberg or Heath Robinson complex construction sitting atop vintage financial infrastructure of similar construction.

Fixing this plumbing issue is a timely endeavor given the ongoing interest in distributed ledger technology (DLT) for supporting post-trade processes. Maintaining a database of standardized identifiers and reference data is probably one of the simplest applications for current DLT capabilities, whether of the Blockchain design or earlier distributed technology techniques.<sup>5</sup> It is also fundamental to fixing the infrastructure plumbing of the global financial system. It would also ease many of the remaining issues identified above, whose solutions were the subject of last month's FIG Research Note<sup>6</sup>.

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<sup>5</sup> Grody A.D., Hughes P., Reinger D., Final Report on Global Identification Standards for Counterparties and Other Financial Market Participants, Journal of Risk Management in Financial Institutions, [https://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=2016874](https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2016874), at page 39-42, March 10, 2015

<sup>6</sup> Financial InterGroup Research Note, The Global LEI Initiative - LEI Issuance and parent registration slowing, FIG comments on where to go next, <http://www.financialintergroup.com/cmsAdmin/uploads/downloads/FIG-Research-Note-The-Global-LEI-Initiative-Apr-2018-Report-Mar-2018-data.pdf>, pages 5-7, May, 2018

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