The Global LEI Initiative

LEI issuance stabilizes, lapsed LEIs still rising, parent registration stalls

A Research Note by Financial InterGroup

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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 July, 2018 month-end and year-to-date reporting of LEI Issuance [1]; on the progress of Relationship Data collection and the reporting of GLEIF's Quarterly Business Reports as of Q2 2018 and from inception [2]; and our Commentary.

LEI ISSUANCE

This is the first month of a slight decrease of issued LEIs after a progressive, yet slight increase over the previous three months of 2018. This decline follows the run-up in LEI registrations precipitated by the EU's year-end 2017 MiFid II LEI "No LEI No Trade" requirements. The current down tick is probably being impacted by the end of the EU's six month moratorium on the requirement to obtain a LEI, originally set for year-end 2017, extended and now ended at month-end June, 2018. It either indicates all registrants needing to register a LEI have been exhausted or that potential registrants have found alternatives via allowed exceptions. However, most likely it is that expected compelling legislation has not materialized in all jurisdictions.

LEI Issuance and Lapsed LEIs – see Note below	**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**	**June 2018 Month-end YTD**	**July 2018 Month-end YTD**
	481,522	975,741	1,071,693	1,113,339	1,148,170	1,172,295	1,195,780	1,221,330	1,242,095
	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**	**June 2018 Month-end**	**July 2018 Month-end**
Newly Issued	5,334	40,237*	92,029	39,760	33,120	22,882	23,412	23,801	19,951
Lapsed	6,300	7,134	7,494	8,296	8,904	7,529	6,409	7,166	7,278
Net Increase/decrease	-996	33,103	84,535	31,464	24,216	15,353	17,003	16,635	12,673
Lapsed rate	29.0% (Year-end %)	17.4% (Year-end %)	16.0%	15.8%	15.7%	15.7%	15.5%	15.5%	15.6%
Total Lapsed (Year & month-end Totals)	139,461	169,778	171,472	175,540	179,803	183,466	186,021	189,712	193,657

Note: In the second quarter of 2018 the largest LEI issuer, Business Entity Data B.V, (known in the US as the GMEI Utility) adjusted the status of a significant number of historic LEIs under its management from 'fully corroborated' to 'entity supplied only'. This resulted in a decrease of fully corroborated Level 1 reference data to 76.1% vs. first quarter's 84.6%. GLEIF is investigating the matter.[3]

*We will continue to monitor lapsed rates and particularly of those LEIs registered in the last quarter of 2017 which leapt to 127,281 from the 7,476 monthly average from the prior three quarters of 2017 and which is coming due for annual renewal in the last quarter of 2018.

[1] GLEIF Data Quality Report – July 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-july-2018#, Aug. 3 , 2018
[2] Global LEI System Business Report Q2 2018., https://www.gleif.org/en/lei-data/global-lei-index/download-global-lei-system-business-reports# August 8, 2019
[3] ibid, at page 2

This leveling off of LEI issuance is occurring while the ratio of issued vs. lapsed LEIs at year-end 2016 of 29% has declined significantly to 15.6%, although the total lapsed LEIs are on a steady yet small monthly uptick to another all-time high of 193,657.

RELATIONSHIP DATA COLLECTION

July 2018 was the third month of data collection after a full year of the GLEIF calling for the registration and collection of the immediate parent and ultimate parent of each LEI (Level 2 Relationship Data). GLEIF reports statistics on how many immediate and ultimate parent records were reported (see the first numeric column in the chart below) and of these, how many of each unique LEI registrant reported both a parent and immediate parent (see the third column in the chart below).

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 leveled off over the last five months, averaging about 4,000 per month from the first two months average of about 15,000. A similar pattern has emerged for the number of LEIs reporting both parents (column 3), with the % increase also showing a slowing trend in these same two periods.

Level 2 Relationship Data	Number of Immediate & Ultimate LEI Parent Records	Month-to-Month Change	Number of Unique LEIs Reporting both Parent Relationships	% Month-to-Month Change
Year-end 2017	88,198	-	51,944	-
Month-end Jan 2018	109,057	20,859	63,237	21.7%
Month-end Feb 2018	119,438	10,381	70,584	3.7%
Month-end Mar 2018	122,806	3,368	72,953	3.4%
Month-end Apr 2018	129,128	6,322	76,268	4.5%
Month-end May 2018	134,141	5,013	79,270	3.9%
Month-end Jun 2018	136,403	2,262	80,718	1.8%
Month-end Jul 2018	139,127	2,724	82,487	2.6%

The GLEIF also reports on reasons why LEI registrants failed to provide either an ultimate parent LEI and/or an immediate parent LEI (see the first numeric column in the chart on the following page). This metric nearly doubled, from year-end 2017 at 1,067,968 to Month-end June 2018 at 2,099,985. Also, GLEIF reports on how many of each unique LEI registrant reported either a parent and/or immediate parent or provided an exception reason for not providing either or both (see the third column in the same chart on the following page).

In the chart on the following page, month–end figures for June 2018 and comparisons between months was distorted due to a change in reporting by one LEI Issuer, Business Entity Data B.V. (known in the US as the GMEI Utility). According to the GLEIF this change in reporting is erroneous and is expected to be remediated during the third quarter of 2018.[4]

[4] Ibid, 2, at page 2

Level 2 Reporting Exceptions	Number of Immediate & Ultimate LEI Parent Exception Records	Month-to-Month Change	Number of LEIs with Complete Parent Information	% Month-to-Month Change
Year-end 2017	1,067,968	-	572,818	-
Month-end Jan 2018	1,309,801	241,833	702,154	22.6%
Month-end Feb 2018	1,435,891	126,090	770,652	9.8%
Month-end Mar 2018	1,560,558	124,667	834,384	8.3%
Month-end Apr 2018	1,700,551	139,993	909,859	9.0%
Month-end May 2018	1,814,341	113,790	963,991	5.9%
Month-end Jun 2018 -see Note	2,099, 985*	285,644	1,115,160**	15.7%
Adj.Month-end Jun 2018	1,899,368	85,027	914,543***	-5.1%
Month-end Jul 2018	1,952,927	53,559	1,043,199	14.1%

Note:
*GMEI Utility reported an abnormal jump in parent exception records between June 25ths 512,238 to June 26ths 714,753 (difference + 200,617) which was subsequently rescinded between July 16ths 720,096 to July 17ths 519,479 (difference -200,617).
**GMEI also reported LEIs with Complete parent Information at 385,647 (+42.05 %) from its earlier Month end May, 2018 report of 271,485.

***This figure was decreased by 200,617, assuming the GMEI error also affected this statistic

GLEIF's issuance of its Quarterly Business Reports summarizes data on both Level 1 (business card data on each LEI) and the Level 2 data collection effort (parent relationships). In these reports, first issued in Q2 of 2017, we can see from the chart below that data on ultimate and immediate parents entered into the GLEIS was entered unverified (not "Fully Corroborated"). This corroboration is supposed to be done by each managing LOU.

% of Parent LEIs Reported by Registrant Only / % Fully Corroborated

Business Report	Immediate Parent	Ultimate Parent
Q2 2017	76/24	76/24
Q3 2017	52/46	51/47
Q4 2017	70/28	69/28
Q1 2018	69/28	63/33
Q2 2018	70/27	64/33

Also, in the Q2 2018 Business Report, GLEIF reports on information of legal entities reporting either one or both parents with a LEI or those with allowed exceptions. In this regard in the Q2 2018 Business report 93% of the LEI registrants reported information on direct and ultimate parents vs. the previous quarters 75%. However, the percent of legal entities citing legal obstacles preventing them from providing or publishing parent information increased fivefold, from 4% to 19%. This dramatic change in reporting is attributed by the GLEIF to one LEI Issuer, Business Entity Data B.V. The GLEIF states that this change in reporting is erroneous and is expected to be remediated during the third quarter of 2018.

COMMENTARY

Expanding the Role of the Registration Agent to Solve Verification Issues

The concept of a Certifying Agent interacting with a Registration Authority was described in FIGs original proposal to the FSB (see Final Report on Global Identification Standards for Counterparties). The concept was later implemented by GLEIF as a Registration Agent to help legal entities interact with a network of LEI issuing organizations known as Local Operating Units (LOUs) - Registration Authorities in our proposal. The LOU was to verify (corroborate) the registration data.

An important incentive left out of the Registration Agent function as implemented by GLEIF was that of validating the registration data at source, thus enabling the Registration Agent to become the notary, or "Certifying Agent" as described in our proposal.

As can be seen by the low rate of LOU corroboration of LEIs issued for parent relationships as described in the earlier chart on the previous page, this Certifying Agent recommendation, if followed, should solve the validation issue for parent relationship data. This issue and most other data quality issues, and still outstanding ROC consultations (corporate actions and fund hierarchies) can also be resolved through such an at-source professional certification service.

Such services, known as Assurance Services are offered by all the Big 4 and many other major auditing and consulting firms. It should be noted that the Big 4, at the time of our proposal referenced above, had been collaborating on maintaining an identification system and global data base of their collective public clients for conflict of interest issues.

One of the GLEIF Registration Agents, a Big 4, Deloitte AG, has been approved to register LEIs on behalf of the Swiss markets while Deloitte Managed Services operates the Swiss Legal Entity Identifier Service (LOU). A further role for Deloitte and the other Big 4 audit, accounting and professional service firms could be to assure that the correct hierarchies of LEIs are entered into the GLEIS following the required financial statement account consolidation reporting rules.

In Germany all financial market participants that use derivatives require external auditors to validate procedures of newly enacted derivatives regulations and for clients to pay for the service. All financial market participants that act as counterparties in derivatives trades, and therefore require a LEI, are subject to the new audits. Importantly this includes non-financial companies exceeding a notional outstandings or number of contracts threshold.

Expanding the use of such a globally situated trusted professional organization, for example in a collaboration of the Big 4 - to validate official source documents, provide timely awareness of corporate reorganizations and monitor renewals, would be a major step in assuring high quality, timely updated data. The $100 per renewal (currently $120 million) spent on LOU services by LEI registrants annually could substituted for such a service. LOUs now spend their time and money buying secondary sources of entity data to validate registrants' existence and reference data.

Finally, the Big 4 can maintain LEI registrants' privacy, as may be required by each sovereign regulator, through technical means. Such technical means could be as the keeper of private keys for authentication through hashing, for assurances of approved redactions through encryption, and as auditors of distributed ledgers, the latter already offered as a service by Big 4 PwC.

All of the above was first proposed by FIG in their proposals to the FSB (see FinancialInterGroup Response to Financial Stability Board's Consultative Paper: Feasibility Study on Approaches to Aggregate OTC Derivatives Trade Repository Data).

A Second Phase Needed for Furthering the Global LEI Initiative

The Global LEI initiative has accomplished its first objective, assigning unique codes and gathering a minimum amount of reference data for each. It has done this through organizing a federated group of local operating units (LOUs) and, of late, Registration Agents. 1.2 million LEIs have been assigned. European markets are further along, given their need for such a singular code for financial market participants to unify EU reporting under the single market reporting concept.

The ability to press further into assigning and recording hierarchies of LEIs for transaction aggregation and, ultimately, systemic risk analysis is not yet clear, although that was the precipitating objective for the LEI initiative agreed to by the G20. This objective is being thwarted by high rates of permitted LEI parent registration 'opt outs' (exceptions) and failure of the ROC to yet publish conclusions of their consultation paper on Fund hierarchies.

Growing lapsed (non-renewed) LEIs are also of concern owing to their ability to thwart proper funding of the LEI initiative and the potential to dilute the quality of reference data. The ROC's failure to yet publish conclusions of their consultation paper on corporate reorganizations also has an impact on the quality of the accumulated data stored in the LEI database.

Most importantly, changes in control and ownership implemented through corporate reorganizations has a significant impact on changing risk parameters of any affected entity undergoing a merger, acquisition, spin-off or other corporate restructuring. Synchronization of updating of internal financial institutions' data bases in this regard with the external GLEIF data base is crucial lest the purpose of a 'golden copy' of both LEIs and their hierarchies maintained by GLEIF be negated.

Finally, as with any major systems effort, it is usual to test systems and implementation procedures; to take data from older legacy systems and convert them into the new system; and to make sure required adjustments identified can be implemented. Then and only then is the go-no-go decision taken. Unfortunately, in the heat of the financial crisis the political class dominated the decision to proceed. We now have a global initiative, a framework given to us by legislators and regulators that should have been more thoroughly thought through first at the detail level, especially in such a first ever globally synchronized data initiative as is the global LEI initiative.

GLEIF has recognized the crossroad they are now at. This was clear when they convened a private conference in May, 2018 inviting the most knowledgeable and expert individuals to provide them with input and to hold discussion with regulators.

A lot of new understanding about this global data initiative has been gained. Further dialogue is needed of what is possible currently or what new agreements are needed at the G20, at the FSB or at the local sovereign country level to move forward.

New technologies are now available to ease implementation of distributed systems. Regulators in sovereign jurisdictions and in collaboration with other regulators are already seeing themselves as nodes on a distributed ledger system and are actively encouraging and funding systems toward this objective.

LOUs, likewise, should be encouraged to see themselves transformed from physically maintaining data bases into overseeing distributed nodes storing registered LEIs, their reference data and their parent LEI hierarchies. LEIs placed into the network by registrants through at-source trusted validators, as described earlier, would facilitate the transformation of LOUs from their physical batch-oriented organizationally federated form into highly automated straight-through-processing nodes on a distributed network. Costs for sourcing untimely and second level data feeds for validating LEI data would be eliminated.

A second phase of the Global LEI system to remedy observed weaknesses and support our future needs should be contemplated. Consideration should be given to transforming the current expedient approach of reusing costly, error prone and high risk legacy concepts and systems that failed us in the past. Automated systems are fragile, those built in haste in incremental fashion are even more so.

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