



The Global LEI Initiative

A Research Note by Financial InterGroup

December 2019

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LEI ISSUANCE and NON-RENEWALS (Lapsed LEIs)

LEI registration reached another all-time high of 1,523,963 registered LEIs, up from last month's 1,504,480. While a major accomplishment in the nearly decade since US regulators first requested the LEI project, it is far from the intermediate objective of 40 million registered LEIs and even further from the 200 million needed to accomplish 'full adaption', a term used to anticipate completing the mission of a universally adopted singular legal entity identifier.

Recent monthly issued LEIs are repeatedly below monthly lapsed LEIs. Lapsed LEIs are at another all-time high of 435,134 up from last month's 415,491. Lapsed LEIs month-to-month are accelerating and now represent 28.6% of all registered LEIs vs. last month's 27.6%, a full 1% rise, following two prior months rise of .5%. Without solving this accelerating lapsed rate, the data quality of the GLEIS database will increasingly become suspect, negating the expected value of the LEI as the best-in-class source for legal entity identification.

RELATIONSHIP DATA COLLECTION

LEI registration for parent relationships (both ultimate and immediate) increased, now at 205,895 vs. last month's 203,544, representing 118,422 individual LEIs this month vs. last month's 117,124. Exceptions for not obtaining an LEI are stabilizing, although reaching another all-time high of 2,485,817 vs. last month's 2,449,422. Here, too, allowing exceptions are thwarting the ability to complete the mission of full adaption. While allowing exceptions was seen as a means to continue the momentum of the LEI registration initiative, it is now important to revisit the issue lest the regulatory objective of aggregating transaction data for risk analysis will be permanently undermined.

CLOSING COMMENT

Regulators end game for the LEI – risk analysis

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 November, 2019 month-end and year-to-date reporting of LEI issuance; on the progress of Relationship Data collection; and our Commentary.

LEI ISSUANCE

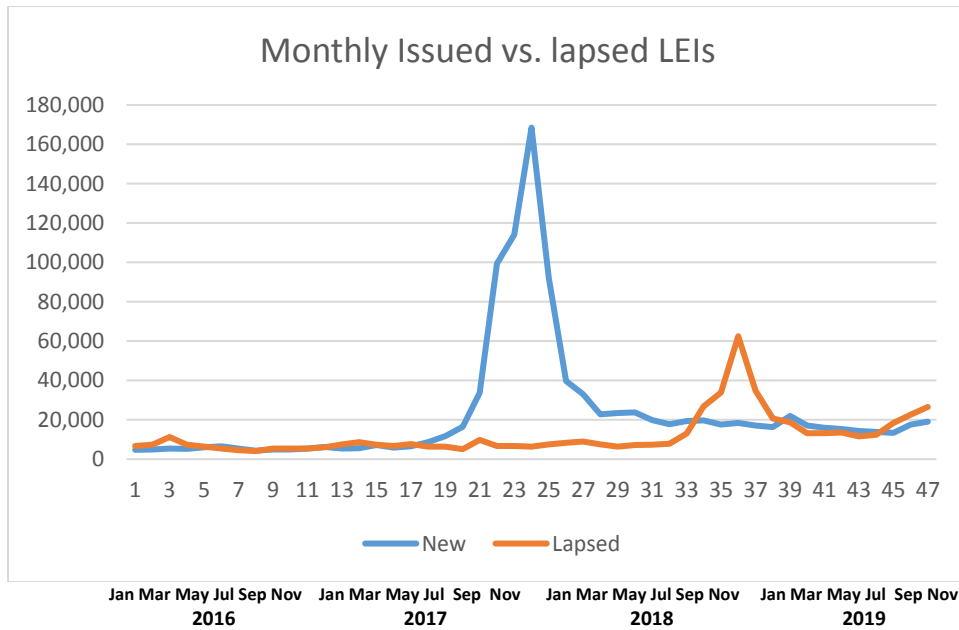
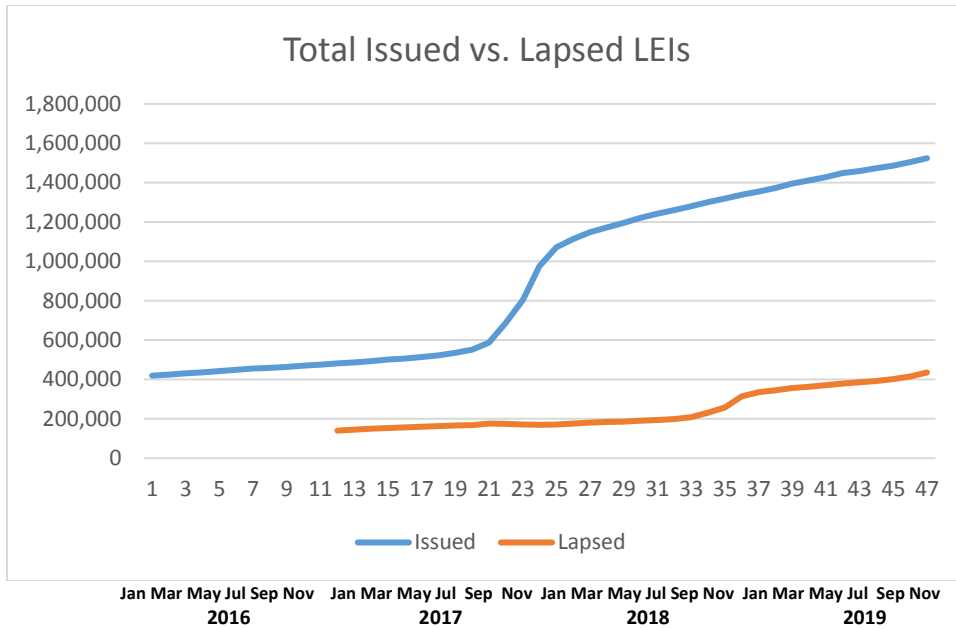
This month LEI registration reached another all-time high of 1,523,963. We continue to see a pickup of issuance of LEIs, this month's 19,106 vs. the average of 16,550 per month since the beginning of this year. In prior years the average monthly LEI issuance was 29,016 (2018) and 40,237 (2017) helped considerably by EU mandates compelling issuance. Perhaps the acceleration of LEI registrations is consistent with EU's new mandate to require LEIs for collateral posting for securities financing transactions taking effect April, 2020. This should accelerate LEI issuance as was the case when EMIR and MiFid II mandates accelerated LEI registration for trade reporting.

2016 – 2018 Year-to-Year & 2019 Month-by-Month Comparison

LEI Issuance and Lapsed LEIs – Year-to-Year & Month- by-Month Comparison	2016 Year-end	2017 Year-end	2018 Year-end	Jan 2019 Month-end & YTD	Feb 2019 Month-End & YTD	Mar. 2019 Month-end & YTD	Apr 2019 Month-end & YTD	May 2019 Month-end & YTD	Jun 2019 Month-end & YTD	Jul 2019 Month-end & YTD	Aug 2019 Month-end & YTD	Sep 2019 Month-end & YTD	Oct 2019 Month-end & YTD	Nov 2019 Month-end & YTD
Total LEIs issued at Year-end & YTD	481,522	975,741	1,337,925	1,355,375	1,372,009	1,394,469	1,412,195	1,428,403	1,443,882	1,458,621	1,472,740	1,486,441	1,504,480	1,523,963
Year-to-Year Averages/ Month-by-Month Comparisons														
Newly Issued	5,334	40,237	29,016	17,092	16,250	22,002	17,084	15,996	15,281	14,370	13,782	13,406	17,678	19,106
Lapsed	6,300	7,134	15,894	34,796	20,654	18,701	13,197	13,252	13,508	11,592	12,364	18,447	22,700	26,558
Net Increase/ decrease	-996	33,103	13,122	-17,677	-4,404	3,301	3,887	2,744	1,773	2,778	1,418	-5,041	-5,022	7,452
Lapsed rate	29.0%	17.4%	23.5%	24.7%	25.2%	25.5%	25.7%	26.0%	26.2%	26.4%	26.6%	27.1%	27.6%	28.6%
Total Lapsed LEIs	139,461	169,778	313,915	334,503	345,544	356,148	363,406	370,774	378,900	385,371	391,382	402,090	415,491	435,134

November's data saw the third month of the reversal of lapsed LEIs exceeding newly issued LEIs over the previous six months of issued LEIs exceeding lapsed LEIs. The overall rate of lapsed vs. issued LEIs is now at 28.6% vs. last year-end's 23.5% and last month's 27.6%. While the lapsed rate had continued to climb slowly, it averaged .2% month-over-month in each of the last six months, it rose a full .5% in each of the last two months and then a full 1% this past month. Lapsed LEIs are those LEIs that are not renewed at their one year anniversary of registration.

GLEIF has proffered the argument that the GLEIS database is of greater value than other similar databases regardless of falling short of solving the Lapsed LEI problem. The argument is that it is the only legal entity database that is either updated annually or can tell users if the information is not current. While exemplary, the non-current data (now nearly 1/3 of the database) is problematic. For example, when the name of an entity is not timely updated it can result in a new LEI being issued; a collection gap exists when relationship LEIs are not registered for lapsed LEIs; and when trades, permitted to contain a Lapsed LEI, are executed when the legal entity has lost its financial registration or abruptly gone out of business.

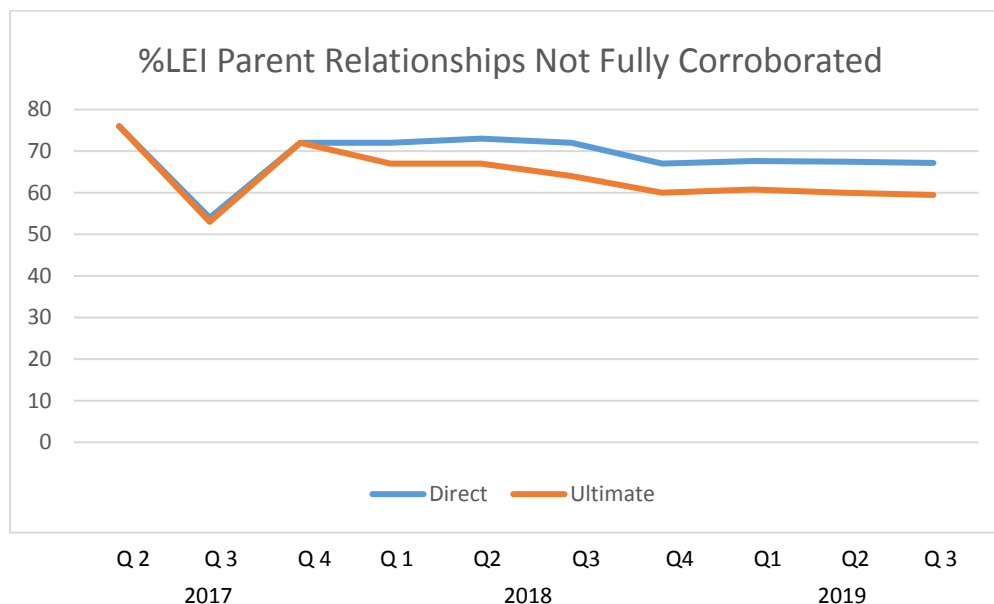


We anticipate a continuation of a rising lapsed rate (now at 28.6%) until renewing LEIs becomes more broadly required by regulation or some other means of compulsion surfaces or some other business model is agreed upon to accommodate renewals as well as to compel issuance. In this later regard a new business model is being proposed where financial institutions will issue LEIs to their clients/counterparties after they have registered them with a LOU. Financial institutions may themselves become LOUs and or Registration Agents.

RELATIONSHIP DATA COLLECTION

Relationship data collection, the recording of LEIs for parents and ultimate parents of legal entities, and the reasons for opting out in doing so, has been recorded in the global LEI database since May, 2017.

According to the **Q3 2019 GLEIS Business Report** issued Nov. 15, 2019 of the total legal entities reporting hierarchy (relationship) information, either an intermediate or ultimate parent entity (189,169), 61.9% report a LEI for an intermediate parent without Local Operating Unit (LOU) validation, while 5.3% report only partial LOU validation. For ultimate parents, 53.7% of LEIs are reported without any LOU validation while 5.8% report only partial LOU validation. These statistics seem to be stabilizing over the nearly three (3) years the GLEIF has been reporting these numbers.



This lack of validation of hierarchy information is an inhibitor to the success of the LEI initiative as the LEI is intended to be the highest quality 'go-to' data base of legal entity information. Also the use of parent LEI data for aggregating financial transaction data for risk analysis would be seriously impaired. Matthew Reed, former Chairman of the LEI's Regulatory Oversight Committee (ROC), **commented in an interview,**

"We expect that we will view the LEI file as complete only when certain corporate information is revealed with respect to hierarchy information."

The ROC has recognized that ultimate and immediate parent information falls short of complete hierarchies as requested by the FSB, which they expect to be addressed in further consultations.

According to the GLEIS Business Report, in the third quarter of 2019, approximately 1.29 million LEI registrants representing 89% of the total LEI population had reported information on direct and ultimate parents. 99.9% of LEI registrants who obtained a newly issued LEI or renewed an existing LEI in this quarter reported parent information.

The share of legal entities reporting direct parents having an LEI increased from approximately 6% at the end of 2018 to approximately 7% at the end of the third quarter of 2019. The share of legal entities reporting direct parents who do not have an LEI dropped from approximately 7% at the end of 2018 to less than 5% at the end of the third quarter of 2019. At the same time, the share of legal entities reporting ultimate parents having an LEI increased from approximately 6% at the end of 2018 to approximately 8% at the end of the third quarter of 2019. The share of legal entities reporting direct parents who do not have an LEI dropped from approximately 6% at the end of 2018 to approximately 4% at the end of the third quarter of 2019.

The number of immediate and ultimate parent records recorded in the GLEIS are seen in column 1 in the chart below. Of these, GLEIF also reports on how many of each unique LEI registrants reported both a parent and immediate parent (see column 3 in the same chart below).

Chart 1 - Level 2 Relationship Data	Number of Immediate & Ultimate LEI Parent Records (1)	Month-to-Month Change (2)	Number of Unique LEIs Reporting both Parent Relationships (3)	% Month-to-Month Change (4)
Year-end 2017	88,198	-	51,944	-
Year-end 2018	152,318	2,523	89,826	1.7%
Month-end Jan 2019	157,131	4,813	92,373	1.0%
Month-end Feb 2019	162,852	5,721	95,379	3.3%
Month-end Mar 2019	173,490	10,638	101,163	6.1%
Month-end Apr 2019	177,811	4,321	103,535	2.3%
Month-end May 2019	181,341	3,530	105,432	1.8%
Month-end Jun 2019	185,424	4,083	107,687	2.1%
Month-end Jul 2019	189,169	3,745	109,703	1.9%
Month-end Aug 2019	195,466	6,297	113,249	3.2%
Month-end Sep 2019	197,546	2,080	114,307	1.0%
Month-end Oct 2019	203,544	5,998	117,124	2.5%
Month-end Nov 2019	205,895	2,351	118,422	1.1%

As can be seen from the Month-to-Month Change Column (column 2) in the Chart 1 above, the monthly reporting of the number of registered LEIs with parent relationships has stabilized. This month's decrease to 2,351 vs. last month's 5,998 is at the low end of the average of 4,871 month-over-month for this year. It continues to show that LEI registrants are following the mandates to include parent relationship data where it is known by the registrant. Similarly, registrants report both parent relationships where they exist (column 3 in Chart 1 above). Here too the percent decrease (column 4 in Chart 1 above) of 1.1% is at the low end of the average month-to-month delta of 2.4% over the current year.

Chart 2 - Level 2 Reporting Exceptions	Number of Immediate & Ultimate LEI Parent Exception Records (1)	Month-to-Month Change (2)	Number of LEIs with Complete Parent Information (3)	% Month-to-Month Change (4)
Year-end 2017	1,067,968	-	572,818	-
Year-end 2018	2,156,909	38,952	1,146,554	1.7%
Month-end Jan 2019	2,187,337	30,428	1,163,111	1.4%
Month-end Feb 2019	2,215,647	28,310	1,179,625	1.4%
Month-end Mar 2019	2,250,448	34,801	1,201,202	1.8%
Month-end Apr 2019	2,282,691	32,243	1,218,932	1.5%
Month-end May 2019	2,312,875	30,184	1,235,212	1.3%
Month-end Jun 2019	2,342,699	29,824	1,250,360	1.2%
Month-end Jul 2019	2,368,936	26,237	1,264,688	1.1%
Month-end Aug 2019	2,394,314	25,378	1,277,504	1.0%
Month-end Sep 2019	2,418,057	23,743	1,289,519	1.0%
Month-end Oct 2019	2,449,422	31,365	1,306,391	1.3%
Month-end Nov 2019	2,485,817	36,395	1,324,469	1.4

CLOSING COMMENT

The ROC provides for existing and new LEI registrants to record legitimate (approved by the ROC) exceptions for opting out of reporting parent relationship data. The GLEIF reports on those registrants that have recorded relationship (Level 2) reporting exceptions (column 1 in Chart 2 on previous page). Also reported is how many of each unique LEI registrants reported either a parent and/or immediate parent or provided an exception reason for opting out from not providing either or both (see column 3 in Chart 2 on previous page).

Relationship data is critical if the LEI is to be used for hierarchical constructions of legal entities for risk management. Importantly, only 205,895 of the LEIs that are included in the “LEIs with complete parent relationships” category (1,324,469) report an LEI for an immediate parent and/or ultimate parent. The LEIs in the category of complete parent relationships, in the main, appears to represent those registrants that have registered an LEI; have registered one or more parent relationship LEIs; have no parents; and/or used the allowed exceptions to opt out of registering an LEI for one or both of their parents.

In cases where a registrant is reporting no ultimate parent it is being observed that some of those so identified are erroneously reporting this. This may be due to the registrant not being aware of who the immediate or ultimate parent is and/or is unaware that it already has registered a LEI. In this regard at the end of the third quarter 2019, over 21,000 legal entities had updated the information of their parents, 7,200 have provided the LEIs of their immediate parents and approximately 6,600 for their ultimate parents.

It still remains to be understood how such permitted exceptions will affect the FSB’s and the BIS’s (Bank for International Settlements) long term objective of aggregating financial transaction data for risk management at the enterprise level (the BIS’s concern) and systemic risk analysis (the FSB’s concern). Both organizations have reported on their inability to use the LEI data for such purposes. In the matter of analyzing systemic risk, a large gap in reporting via LEI was opened when the ROC declared sovereign entities would not be required to obtain a LEI.

Regulators end game for the LEI – risk analysis

Regulators main interest over the course of nearly a decade of advocating for a legal entity identifier (LEI) was, and still is, using the LEI as a means to aggregate financial transaction data. The G20-endorsed FSB report **A Global Legal Entity Identifier for Financial Markets** called for a Global LEI system (GLEIS) to include “Level 1” “business card” information on entities (e.g., official name of the legal entity, address of its headquarters, etc.), followed later by “Level 2” data on relationships among entities. Recommendation 12 of the report specifically called for the development of proposals for additional reference data on the direct and ultimate parent(s) of legal entities and relationship or ownership data.

Later the BCBS’s report **Principles for Effective Risk Data Aggregation and Risk Reporting**, determined that many banks lacked the ability to aggregate risk exposures and identify concentrations of risk quickly and accurately at the bank group level, across business lines and between legal entities and trade counterparties. The use of LEI’s for risk exposure aggregation was expected to remedy these weaknesses and their consequences for financial stability.

Both reports supported the conclusion that the LEI and its associated relationship data was essential for more granular risk aggregation beyond the balance sheet and position data that is available today. The

LEI is also necessary to assist in observing the buildup of unobserved risk across globally connected financial firms. This new category of risk called “systemic risk” surfaced as one of the reasons for the global financial credit crisis, precipitated by the bankruptcy of Lehman Brothers.

Systemic risk is created by risky behavior of financial institutions in their interactions with other financial institutions as counterparties in trades, and in the extension of trading limits and credit to common clients not observable by individual enterprises. This lack of observable risk is due to the interconnectedness of the financial system across sovereign regulatory regimes and the multitude of different computer readable identifiers representing the same entity. This lack of a transparent universally accepted unique entity identifier inhibits regulators and financial institutions from observing and aggregating transaction data for analyzing systemic risk. This was the premise for initiating the LEI initiative.

Sovereign regulatory risk regimes impose their own tools and criteria for enterprise risk management within their jurisdiction within a common framework, the Basel Capital Accords for banks and the Solvency II Directive for insurance companies. It is implemented across multiple sub-categories of financial market participants and consists of rule guidance for such risk categories as market, credit, liquidity and operational risk.

This risk guidance prescribes calibrations for capital adequacy, liquidity ratios, credit concentrations, loss reserves, margin calculations, collateral requirements, and other such key risk indicators. These calibrations are further defined for each asset and liability category and applied further against the riskiness of each financial institution, counterparty or client category. Gathering this information within and across financial enterprises can be facilitated by each financial transaction containing the exact same identifier for each enterprise and sub-entity, and each client and counterparty. This was and is the purpose of the LEI initiative.

The European Central Bank (ECB) has been concerned about this issue for some time, and although the data purity rules of BCBS 239 were designed to improve the situation, in practice they have yet to take hold in many institutions. In its May 2018 **“Report on the Thematic Review on effective risk data aggregation and risk reporting,”** the ECB stated that:

“Sound and robust risk data aggregation capabilities and risk reporting practices have become even more important since the global financial crisis. ... The outcome of the Thematic Review shows that the implementation status of the BCBS 239 principles within the sample of significant institutions is unsatisfactory, which is a source of concern.”

Further, the ECB while urging the use of the LEI fell far short of mandating the LEI, instead citing it as a “good practice”:

“Overall, the ECB observed that IT infrastructure for risk data aggregation and risk reporting sought to provide transaction-level granularity and facilitate periodic reconciliation between risk data and other credit institution data. In this respect, the use of Legal Entity Identifier codes to help aggregate exposures to counterparties would also represent a good practice.”

Marc Carney, the outgoing head of the FSB, in his **final letter to the G20** looked over the landscape of future innovations of significance to financial stability and to creating greater value for business and consumers. He concluded that alongside major technological advances one of these significant innovations was the LEI:

“More generally, the FSB and standard-setting bodies are exploring how a broad range of innovations—including distributed ledger technology, the global legal entity identifier (LEI), artificial intelligence and various payments technologies—could promote financial stability while bringing wider benefits to consumers and businesses.”

Finally, the FSB in its **Thematic Peer Review of the LEI** recommended enhancing the scope and usability of Level 2 (relationship) data by:

“considering cost-effective and reliable ways to add relationship data that would increase the value of the LEI (e.g. confidential relationships subject to access rights and appropriate controls; beneficial owners; other definition of parents);” and

“expanding the coverage of such data, for instance by conducting targeted LEI adoption campaigns for large multinational firms and by facilitating relationship reporting by parents of their group entities.”

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