

Emily: Welcome to a DerivSource podcast. I'm Emily Fraser Voigt, Deputy Editor of DerivSource.com.

Mifid II came into force on the 3rd of January, and firms worked hard all last year to prepare for the new transparency and reporting requirements it will bring.

One of the impacts of MiFID II is that it requires all entities involved in European trades (on both the buy and the sell side) to supply legal entity identifiers, or LEIs, in their trade reporting.

LEIs help financial firms and regulators aggregate and better understand counterparty exposures, providing enhanced market transparency and improved analysis of systemic risk.

In this podcast from May last year, we spoke with Ron Jordan, Managing Director of Data Services at the DTCC about LEI uptake, the challenges institutions might face in using them, and what impact the regulatory changes will have.

This was among our most popular pieces of content last year and we thought it was worth sharing again as the new rules go live.

Thank you Ron for joining us in this podcast.

Ron: Thank you Emily, it's my pleasure to join you.

Emily: Can you start by offering an update to our audience on the status of LEIs? How many LEIs have been issued, and across how many jurisdictions?

Ron: Sure. The LEI system really has several different components, and let me just start there. The LEI system is managed by a Global Legal Entity Identifier Foundation, called GLEIF, and that is the operating arm for the global system. Sitting underneath the GLEIF are about thirty what they call LEI operating units, or LOUs, of which DTCC is one of those thirty, and we are the operating units that issue the LEIs, validate the information and maintain the LEIs on behalf of the registrants, those in the industry, or those in the financial services world, that are required to get LEIs for regulatory reporting.

The system as it is now has been operational for several years. There are approximately 500,000 LEIs that have been issued to financial institutions and corporates across the globe, in I believe over 200 jurisdictions worldwide. The GMEI utility, which is a DTCC wholly-owned subsidiary, which you mentioned earlier, is an accredited LOU. We've issued approximately 240,000 of the 500,000 global LEIs, again in about 200 jurisdictions.

So the LEI system is maturing, and it continues to expand. I would note that beginning on May 1st, just a week away, the LEI system will be experiencing a fairly fundamental change, and rather than just requiring LEIs to be registered for core baseline information, beginning May 1st, all of the LEI operating units will start to collect information from LEI registrants for not only themselves but for their direct and their ultimate parents, and that is a requirement which is going to start May 1st, and it will be mandatory for all LEI registrants and anybody renewing an LEI. So, again, beginning May 1st, direct parent and ultimate parent information will be required to be collected upon a registration and renewal.

Emily: There have been some comments on LEIs being expensive for market participants who may not have high use for such identifiers; what would your response be to this concern?

Ron: I think there are several responses. First is that, as I mentioned, there are thirty LEI operating units and we all compete with each other, and we compete like most other companies: we compete on quality of product, user functionality, and we compete on price. So there are 30 LOUs; I think there are almost 30 different prices for registration and renewal, and there are lots of different types of services that are offered.

So my sense on the price range is that for registration, to register a corporate entity to get an LEI, the price is generally between \$150 and \$200 USD, and that is a one-time registration fee. And then there is an annual renewal requirement, and that renewal fee is generally between \$75 and \$100 Dollars per year, for each LEI. So, again, I don't believe that the pricing is too expensive. The LEI operating units take the information, we not only assign unique LEI code to the data, but we also validate the information to make sure it can be validated against publicly available sources, business registries and the like. So there is a service that is provided, the cost of which the funding covers.

Also I would say, very important that all LEIs, all 500,000 LEIs and all of the reference data associated with those LEIs, is freely available. There is no charge to receive the information. So the model here is quite different than most market data models, which require a user of the database to pay. Here, the information is in the public domain, and the way that the cost of the

validation is sustained is through these I'll call them *taxes* on the registrants, much like any new driver's license and renewing your driver's license. So every entity pays a small amount to keep the system as accurate as it can possibly be.

Again, I would argue that the prices between \$100 annual renewal and a \$200 initial registration are very reasonable, and they are subject to competition, and therefore I think the system as a whole has a very sound operating model.

Emily: What are the challenges or obstacles that impede wider adoption of LEIs?

Ron: LEIs generally are required today for certain regulatory reporting, and in the OTC derivatives markets, specifically it started with the CTFC in the United States, and then ESMA in Europe, and there have been other regulatory bodies around the globe, who've required LEIs and reporting. There is still a lack of uniform requirement of LEIs amongst global regulators, so one of the major obstacles is that unless LEIs are required, registrants are reluctant to get them, and as I mentioned they are only currently required in some derivatives asset classes in the United States and Europe, and a few other jurisdictions. So they're not widely required. That is a major obstacle right now, the lack of regulatory requirement, although that will be changing shortly with MiFID II.

The other ongoing issue is the need for compliance or making sure that the entities renew their LEIs on an annual basis. As I mentioned earlier, the renewal is important because it helps fund the system, and if a registrant gets an LEI and they fail to renew, the LEI is still valid for regulatory reporting purposes (at least now). However, it does go into a status called *lapsed*, and that lapsed status just indicates that the registrant has not come back and renewed their LEI. That's important, because without a regulatory enforcement of the annual renewal, the system funding is stretched, and that is one of the regulatory needs in the system going forward to make sure the operating model can survive.

So it's not just the rules of requiring LEIs, but it's also the rules of requiring the annual renewals of the LEIs, which become important.

Emily: Can you update our audience on the planned revision to MiFID II? What's the motivation behind this revision?

Ron: Beginning on January 1st, MiFID II will take place and will require reporting to European regulators LEIs across all asset classes, not just derivatives, for the first time. So equities, fixed income, etc, anything that's being reported

to a European regulator will have to be reported, identifying party and counterparty with an LEI. That's a fairly significant expansion of the use of LEIs for reporting purposes.

While I can't speak for the motivation of the European regulators, I can say that the use of LEIs, generally speaking by regulators, is to help regulators understand systemic risk, and risk of counterparties. So by having LEIs reported, they can uniquely and unambiguously identify parties to transactions regardless of the broker dealer, or entity that may be reporting to the regulator.

So, if firm ABC is doing a trade with three different broker dealers, firm ABC will be reported with the exact same LEI, regardless who's reporting, and that helps regulators understand better systemic risk, or whether there's any concentration risk for any entity. That is also the reason behind the reporting of direct and ultimate parent, or that's also known as Level II information, so that regulators can get an understanding not only of who is doing a trade, what entity is doing a trade, but who that entity's ultimate parent or direct parent may be, so if there's other entities, there are other children of parents transacting, the regulators can better aggregate the risk up to the parent.

So all of this has started with systemic risk analysis, and I think the LEI system continues to evolve both in Level II, you get the parent information, and now with MiFIDII coming in January, to move across derivatives into other asset classes.

Emily: Lastly, how will this revision impact market participants and LEI utilities such as GMEI?

Ron: Beginning on January 1st, or leading up to January 1st, we do expect that there will be a dramatic increase in the number of registrants for LEIs, and that volume will need to be handled on a timely basis by the LEI operating units, like DTCC GMEI Utility, as well as all of the others.

We don't know how big the rush to the door will be. We did see that when MiFID was released several years ago, where LEIs were required for derivatives reporting, there was a very large concentration of registrations just prior to the rule going into effect. We expect that to happen as well in January. As I mentioned, we don't know how big it will be; the estimates range from a 50% increase in the velocity of LEI registrants, to potentially a 500% increase.

All of the LEI operating units right now are preparing for that. We are determining how best to increase our staffing to be able to accept the registrations and turn them around in a timely manner to the issue of the

LEIs. We are looking at ways to try to incent registrants who may need LEIs for MiFID II to get those LEIs sooner than in December of 2017, not wait until the last minute. And we're working with the GLEIF as well to figure out how best to get the word out, to make sure that those people who will be affected by MiFID II understand the need for LEIs as soon as we possibly can.

So all of those things are happening. We do think it will have a volume impact on the system. We do believe that the LEI operating units will have the ability to handle that volume, although again we cannot predict right now the type of volume increase we'll see towards the end of the year.

Emily: Thank you Ron for sharing your insight with us.

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Thank you for listening, and join us next time.

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