A New Future for Legal Entity Identification

Financial services businesses are investing valuable time and resource on client identification. Is a standardized approach the way forward?

LEI
GLOBAL LEGAL ENTITY IDENTIFIER FOUNDATION

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Executive Summary

It was the financial crisis of 2008 that laid bare the need for a universal system of identifying legal entities, and despite the subsequent development of the global Legal Entity Identifier (LEI), the process continues to be notoriously complex for many businesses, especially in a global marketplace. To investigate this issue, and to reveal the extent of that complexity, the Global Legal Entity Identifier Foundation (GLEIF) has worked with the London-based research agency Loudhouse to gather the data contained in this report.

Key findings include:

- Businesses use an average of **4 identifiers**
- Onboarding takes an average of **6–7 weeks**
- **57%** agree that reliability of reference data is a challenge
- **55%** agree that the resourcing of onboarding is a challenge
- **55%** agree lengthy processes mean risk of business loss
- **61%** agree that digital technology will further complicate the process

The need for greater adoption of a publicly available, global directory of legal entities is clear. Financial services businesses are investing significant amounts of time, money and resource into the basic task of identifying legal entities as they onboard new client organizations. It also has to be kept in mind that entity verification processes do not stop with the conclusion of the onboarding process. The client data must be maintained up-to-date throughout the business relationship, which includes regularly verifying business card information and changes to the ownership structure.

And as long as businesses are not using a standardized, widespread approach, it will continue to be a long and laborious process, liable to taking experts away from servicing and sales, and demanding too much focus on administration.

Adoption of the LEI would deliver quantifiable value for these businesses. The days of gathering information from multiple sources just to establish basic entity and ownership data, that's often hard to trace and link, would be over. Transactional and operational friction would be reduced and important information would be more accessible and traceable. Collectively, that reduces time and improves reliability.

The Global LEI Index is the only global online source that provides open, standardized and high quality legal entity reference data. Each LEI contains information about an entity's ownership structure and thus answers the questions of 'who is who' and 'who owns whom' among market participants.

In the pages that follow, we detail the inefficiencies of today's onboarding processes, looking at how they can be a drain on time and resource for financial services businesses. We go on to explain how the issues surrounding the inefficient identification of legal entities can have real business consequences. Finally, our report explores the impact of rising digital technologies and the potential capabilities and benefits afforded by adopting a standardized method for identifying legal entities.

Replacing disjointed information with a globally accepted approach takes the complexity out of business transactions and delivers real results. Time savings, greater transparency and more streamlined working processes are all up for grabs for the businesses that introduce the use of LEIs.

This report is a collaborative effort between GLEIF and the London-based research agency Loudhouse. The research presented within it was conducted among 102 senior salespeople in the banking sector, with a regional split as follows: 35 US, 34 UK and 33 German businesses. The organizations surveyed ranged evenly from having under 50 employees to over 1,000 employees. The detailed results are available for download on the GLEIF website.

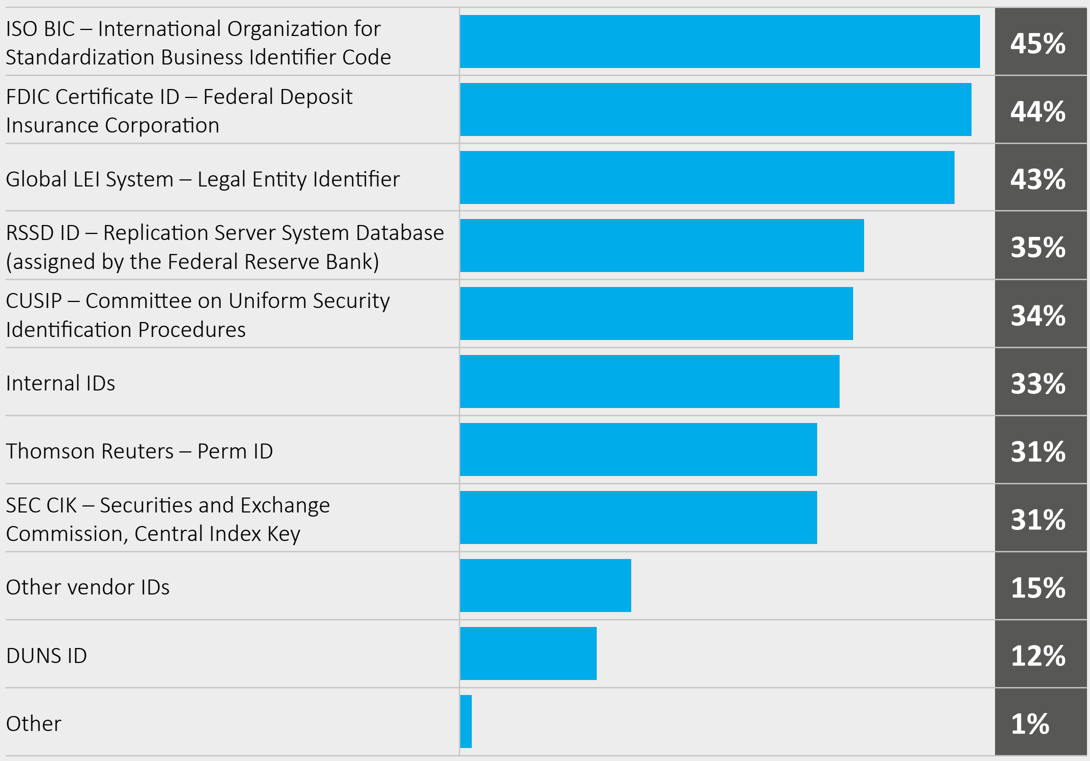
Onboarding Inefficiencies

It will come as little surprise to businesses in the financial services sector that, in the majority of cases, the process used for the onboarding of new legal entities is convoluted and inefficient. In this first section of our report, our respondents – all senior salespeople in the banking sector – reveal the true extent of the issue as they uncover what's really going on each time a new legal entity is onboarded for a business transaction.

The proliferation of identifiers

Perhaps the key finding in our research, from which all other lines can be drawn, is the simple fact that financial institutions are using an average of **four identifiers** to accurately identify and crosscheck new legal entities throughout the client relationship. And approximately one-third of respondents reveal that they're actually using a combination of **five or more identifiers**. As Fig. 1 makes abundantly clear, there's to date no standard identifier for the industry – no single identifier that has gained global acceptance, as a substantial proportion of organizations continue to use a wide range of different identifiers.

Fig. 1
Identifiers used



With such a multitude in use, it's little wonder that over half (**54%**) of respondents agree that the use of different identifiers for the same legal entity leads to inconsistency of information. But that's not the only problem with the proliferation of identifiers. There's also the logistical fact that it makes onboarding a hugely burdensome, time-consuming process for sales teams.

As we see in Fig. 2, it takes an average of **six to seven weeks** to onboard a new legal entity, with **six in ten senior salespeople** spending more than **1.5 days per week** on tasks related to onboarding. It's worth noting, too, that an average of **25%** of the onboarding process involves manual tasks, often being undertaken by senior members of the team.

The use of multiple identifiers in new business onboarding and maintaining the accuracy of the data later on is undoubtedly a time-consuming burden. Moreover, there seems to be a lack of resounding consensus among surveyed businesses over what it is that's taking up the most time – 18% say it's compliance with Know Your Customer (KYC) regulations; 16% say it's documentation management; 15% say it's identification of the legal entity; and so the list goes on, doing little to deny the inconsistent nature of the process as it is today.

Almost half (**49%**) agree middle- and back-office activities related to onboarding are a **major burden**. A similar number (**48%**) agree the exact cost of onboarding is **extremely difficult to quantify**.

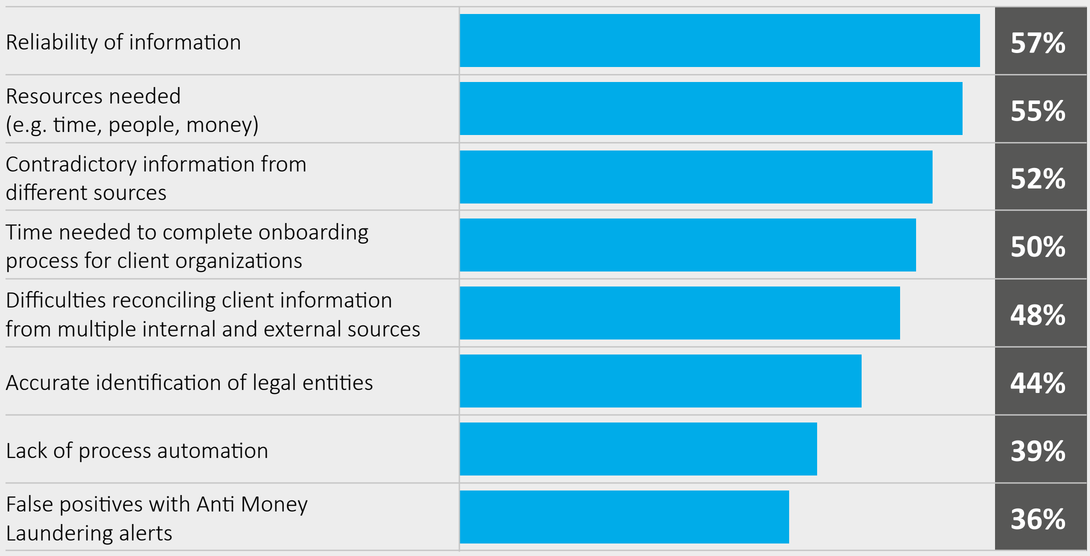
Fig. 2

		Number of identifiers used	
	Total	**1–3**	**4+**
Time to onboard a new client organization (weeks)	**6**	**6**	**7**
Spend more than 1.5 days a week doing onboarding-related activities	**57%**	**53%**	**61%**

The pitfalls of onboarding

There is greater consensus, on the other hand, around the kind of challenges businesses are facing when it comes to the quality of the identifiers they're using. We see in Fig. 3 that the same themes crop up again and again. Mainly concerning the reliability and accuracy of the information being gleaned from the diverse range of identifiers used each time, as detailed earlier in Fig. 1, along with an array of logistical challenges relating to the drain of onboarding on time and resource.

Fig. 3
Top 5 Challenges of onboarding



The need for transparency

Legal entity identification is complex indeed – but multiple identifiers and highly convoluted processes don't just mean inconsistent information and a drain on resource. They also mean a distinct lack of transparency, which doesn't bode well when it comes to meeting compliance regulations in financial transactions. This has a knock-on effect for both individual businesses and the financial services industry.

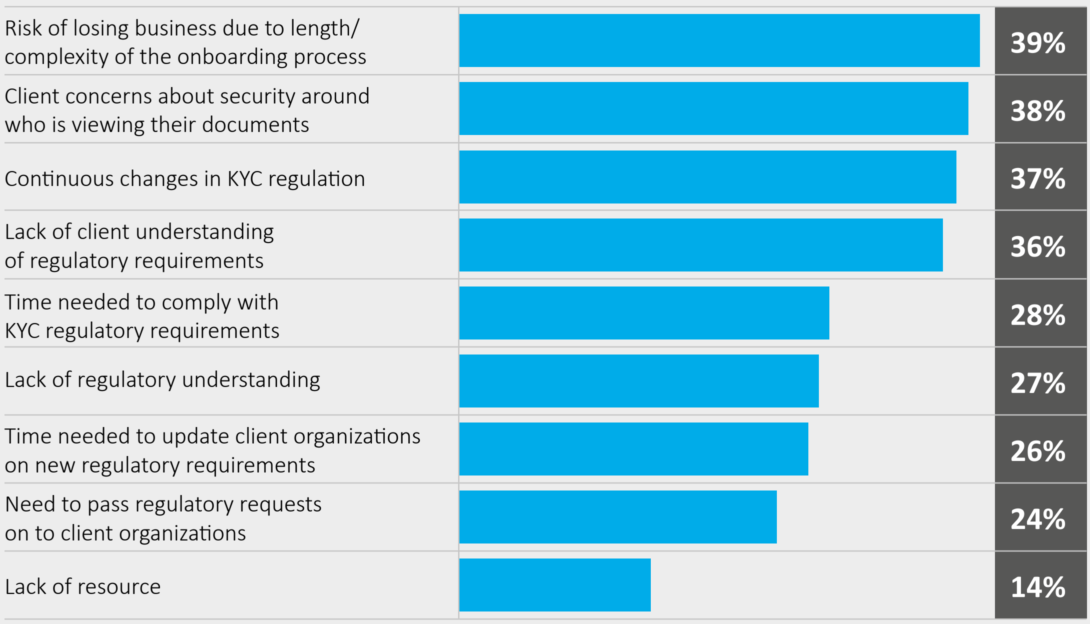
For businesses, muddied waters make it difficult to evaluate risks properly. Onboarding and transacting decisions can't be made with confidence, visibility or control. Most financial businesses turn to KYC providers to aid the onboarding process, but even then, transparency remains an issue. As many as **46%** of respondents acknowledge that it's a non-transparent way of identifying and reporting corporate structure – along with the **47%** who say the information is usually out-of-date (or **59%** for those using 4+ identifiers) and the **46%** who admit the service itself is expensive.

In finance, a lack of transparency means being more prone to fraud and market abuse. Suffice to say, transparency is better for everyone.

Identification Issues are Business Issues

Using multiple identifiers eats up time and hinders transparency – that much is clear. But there's an even bigger business issue at stake when it comes to onboarding new legal entities. Because the reality is that client organizations aren't always sympathetic to the demands placed on financial services businesses by compliance regulations. With exactly half of our respondents agreeing that it's becoming more and more difficult to comply with KYC regulations, Fig. 4 details exactly why:

Fig. 4
Top 3 KYC challenges



The risk of business loss is real

55% agree that prospects might turn to competitors if their onboarding process takes too long – and they're right to be concerned.

As we see from the estimations in Fig. 5, lost business is thought to be a very real consequence of the current identification process, either through inability to glean adequate information or simply lack of patience on the part of the new legal entity. The irony being, of course, that the legal entity might not find the process to be any quicker if and when they do take their business elsewhere – after all, our research shows that the majority of financial institutions are all using 4+ identifiers to onboard new entities, and are therefore liable to the same inefficiencies.

Fig. 5	Proportion of business estimated to be lost
14%	**Transaction is rejected** because not enough information is known about the legal identity of the counterpart
15%	**Legal entity leaves** because onboarding process is too difficult/takes too long

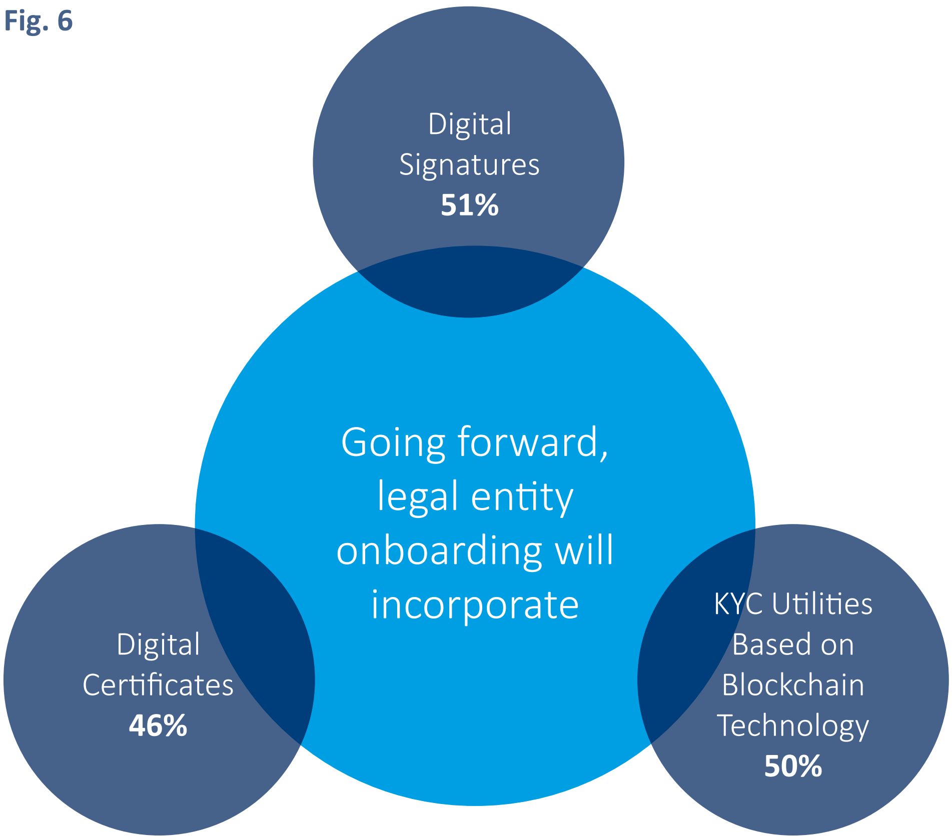
Improving Identification

One thing's for sure: a robust, simplified, improved identification process is long overdue, particularly as **52%** of our respondents think that onboarding time is only going to rise thanks to a combination of increased fraud, tighter regulations and growth in today's business landscape.

The rise of digital technology

Businesses need a system that keeps them on the right side of both regulators and clients, while making them more efficient overall. And they're aware that new technologies are increasingly likely to play a part in that. Fig. 6 highlights the predicted rise of technologies, but there's a caveat to go along with that: **61%** of our respondents believe that the growth of digital solutions will actually make identity verification more difficult, simply because it'll mean a rise in the number of legal entities transacted with.

Fig. 6



What LEI means for identification

Identifying legal entities at a global level has long been a complex, multifaceted undertaking, so could LEIs be just the tonic?

The Global LEI Index is the only global online source that provides open, standardized and high quality legal entity reference data. Each LEI contains information about an entity's ownership structure and thus answers the questions of 'who is who' and 'who owns whom' among market participants.

LEI codes offer businesses a standardized, one-stop approach to identifying legal entities, which has the potential to take the complexity out of business transactions. With LEIs, key reference information is connected by a 20-digit alphanumeric code, enabling quick, consistent, accurate identification of the legal entities taking part in financial transactions, and making time-consuming, inconsistent identification processes a thing of the past. The problems associated with using multiple identifiers, outlined earlier in this report, along with the concern that introducing digital technologies won't necessarily make life easier, are both taken care of.

The rollout of LEIs could also increase the stability of international financial markets and support higher quality and accuracy of financial data overall – but businesses could reap individual benefits too. Like slicker onboarding of new legal entities, reduced inconsistency and reduced risk of business-loss, as well as more efficient use of valuable (and often senior) resource. Like being able to make smarter, more informed and reliable decisions about who to do business with, based on up-to-date, transparent and accurate data.

It's estimated that the use of LEIs in capital markets could lead to a 3.5% reduction in the overall capital markets operations costs. For the global investment banking industry alone, this could result in over $150 million in annual savings[1]. But that's just a fraction of the potential wider savings, because any process that requires identification or verification of legal entities has the chance of being made more efficient and reliable through the use of LEIs. Not least because access to the LEI data pool is, and always will be, free of charge for all.

1 McKinsey & Company and GLEIF White Paper: The Legal Entity Identifier: The Value of the Unique Counterparty ID.

Better Knowledge, Better Business

The findings in this report speak volumes about the need for an accurate and transparent source for legal entity identification. Too many businesses, especially in the financial services industry, are losing vast amounts of time and money each time they make a business transaction as a result of a range of inefficient processes – and it's that inefficiency that means they run the risk of losing the business anyway. Not to mention encountering compliance and security issues because of poor identification.

Adoption of LEIs promises to deliver real business capabilities, benefits and quantifiable value for those businesses that make the switch[2]. Not only will it reduce operational friction, but it also makes information more accessible and reliable. This opportunity to cut costs and get more efficient and accurate in their operations, all whilst gaining deeper insights into the global marketplace, should appeal to all businesses. But then so should the fact that a global standard for legal entity identification, with open access to transparent and high quality reference data for all, would be a force for good in the financial industry as a whole.

Want to learn more about the LEI? Visit us online **www.gleif.org**

2 See also, for example: Basel Committee on Banking Supervision: Guidelines – Sound Management of Risks Related to Money Laundering and Financing of Terrorism; the Wolfsberg Group: Correspondent Banking Due Diligence Questionnaire.

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