

Response of the Global Legal Entity Identifier Foundation (GLEIF) to HM Treasury on the Transposition of the Fifth Money Laundering Directive Consultation

June 2019

The Global Legal Entity Identifier Foundation (GLEIF) is pleased to provide comments to the Transposition of the Fifth Money Laundering Directive Consultation. GLEIF will focus its comments on the use of the Legal Entity Identifier (LEI) in the consultation.

First some background on the LEI.

The development of a system to uniquely identify legal entities globally had its beginnings in the 2008 financial crisis. Regulators worldwide acknowledged their inability to identify parties to transactions across markets, products, and regions for regulatory reporting and supervision. This hindered the ability to evaluate systemic and emerging risk, to identify trends, and to take corrective steps. Recognizing this gap, authorities, working with the private sector, have developed the framework of a Global LEI System (GLEIS) that will, through the issuance of unique LEIs, unambiguously identify legal entities engaged in financial transactions. Although the initial introduction of the LEI was for financial regulatory purposes, the usefulness of the LEI can be leveraged for any purpose in identity management for legal entities both by the public and private sectors spanning all industries and sectors.

The LEI initiative is driven by the Financial Stability Board (FSB) on behalf of the finance ministers and governors of central banks represented in the Group of Twenty (G20). In 2011, the G20 called on the FSB to take the lead in developing recommendations for a global LEI and a supporting governance structure. The related FSB recommendations endorsed by the G20 in 2012 led to the development of the Global LEI System that provides unique identification of legal entities participating in financial transactions across the globe and the subsequent establishment of the GLEIF by the FSB in 2014. The GLEIF is overseen by a committee of currently 71 global regulators and 18 observers, known as the LEI Regulatory Oversight Committee (LEI ROC). UK is represented by Mr. Beju Shah from Bank of England and Ms. Carmel Deenmamode from the Financial Conduct Authority in the LEI ROC.

The LEI itself is a 20-digit, alpha-numeric code based on the ISO 17442 standard developed by the International Organization for Standardization (ISO). The code connects to key reference information that enables clear and unique identification of legal entities participating in financial transactions including their ownership structure. Moreover, the LEI provides freely accessible look up (identification) of the parties to transactions. The complete database of LEIs and the associated LEI reference data is available free of any charge or barrier to anyone on the web. GLEIF operates under the Open Data Charter terms, which means the data can be used by all users without limitations.

The ability of the world's financial ecosystem to curb fraud, terrorist financing and other illicit financial activity, is hindered by its reliance on outdated processes for identity verification. While identity verification support is available through partnerships with service providers, these often face the same

fundamental challenge: low quality, non-uniform data sources are not easy to implement, prevent interoperability and promote inefficiency, which limits the capacity to add value to the surveillance process.

The changes brought by 5MLD are fundamental for improving the transparency of the financial landscape and strengthening the fight against terrorist financing.

In “*Chapter 1: New obliged entities*”, it is stated that 5MLD expands the scope of obliged entities within the property sector to include the letting agency sector for high value transactions with a monthly rent of 10,000 Euros or more. The UK government invites views on how customer due diligence (CDD) should be carried out for letting agents.

GLEIF would like to suggest that letting agents could require LEIs from their legal entity customers before establishing the business relationship for high value transactions and easily verify the identities their customers, as well as obtaining LEIs for themselves, as parties to these business transactions.

In “*Chapter 3: Electronic Money*”, it is stated that cryptoasset exchanges and wallet providers are not currently required within regulations to identify their customers, monitor transactions or report suspicious activity, making anonymous transactions possible. The UK government considers that all relevant activity involving exchange tokens, security tokens and utility tokens of crypto assets should be captured and seeks views on this approach.

GLEIF would like to propose that requiring use of LEIs as part of disclosure requirements for firms offering cryptoasset exchange services and custodian wallet service providers could contribute significantly to the transparency in this unregulated capital market. This is also consistent with the new changes 5MLD brings. 5MLD requires firms offering cryptoasset exchange services and custodian wallet services to fulfill CDD obligations and verify the identity of their customers. LEI could be used to identify legal entities on cryptoasset exchanges.

In the consultation paper, HM Treasury seeks views if new cryptoassets providers, for example Initial Coin Offerings (ICOs) issuers, should be within the scope of the regulations in addition to the 5MLD provisions.

GLEIF would like to emphasize that as underlined in the “*Cryptoassets Taskforce: final report*” published in October 2018, ICOs can be difficult for consumers to assess the risks of a particular token being issued as the documents that typically accompany ICOs are not standardized and might feature misleading information. Therefore, the information needs of investors relative to token issuers and tokens has led to the emergence of intermediaries, whose usefulness and independence from any market influence are not clear. Requiring LEI, an international standard and free of conflicts of interest, to identify token issuers could reduce the need for information intermediaries, contribute to data quality across the market and help to protect consumers against fraud.

In “*Chapter 4: Customer Due Diligence*”, it is stated that although FATF Recommendations state that relevant persons should be “required to understand the nature of their customer’s business and its ownership and control structure”, the general obligation to understand the nature of your customer’s business and its ownership and control structure is not explicitly laid out in the MRLs. 5MLD sets out the circumstances under which secure, remote or electronic identification processes may be taken into

account in undertaking CDD. Therefore, it is proposed in the consultation paper to add an explicit requirement for relevant persons to understand this information as part of their CDD obligations.

GLEIF proposes that mandating the use of LEI for relevant persons as part of CDD obligations would greatly enable the compatibility of disparate data sources that is so severely lacking in today's financial environment. Given the LEI is already mapped to other identification systems used in transaction processing such as Business Identifier Codes (BICs), the LEI system enables stakeholders to act with greater confidence that all parties involved in a transaction are unambiguously identified.

In "*Chapter 6: Enhanced Due Diligence*", it is stated that mandatory enhanced due diligence (EDD) measures in relation to designated high-risk countries is currently determined at a national level. In order to harmonize EDD in relation to high risk third countries, 5MLD sets out a series of requirements for Member States and their obliged entities. While the MLRs currently require obliged entities to examine the background and purpose of business relationships and transactions with customers established in high-risk countries, obtaining specific information, for example the customer and beneficial owner(s), is not currently required.

GLEIF would like to emphasize that, customer LEI could be required as part of EDD if the customer is a legal entity in designated high-risk countries. Currently, the Global LEI System covers more than 200 countries, which means coverage already exists for legal entities to apply for an LEI in high-risk countries and coverage in additional jurisdictions could be added.

In "*Chapter 9: Trust registration service*", it is stated that 5MLD requires the UK to collect, the legal entity's corporate name, the registered office of the legal entity and the nature of the entity's role in relation to the trust. In the consultation paper, it is confirmed that the government will publish a technical consultation for clarifying its approach on these points later in 2019.

GLEIF would like to comment that considering trusts are already eligible for obtaining LEIs and the type of new information required by 5MLD is already captured in LEI reference data, maintaining a valid LEI could be specifically required for trusts as part of as part of the 5MLD transposition. In the Global LEI System database, 38,076 trusts have LEIs in the UK, which makes 26% of all LEIs issued in the UK.

In "*Chapter 10: National register of bank account ownership*", it is stated that 5MLD requires the UK to establish a centralized automated mechanism -such as a central registry or electronic data retrieval mechanism – which allows identification of natural and legal persons, which hold or control bank accounts; payment accounts; or safe-deposits held by credit institutions within the UK. 5MLD requires the name of the customer account holder, and any person purporting to act on behalf of the customer along with a unique identification number or other information required for the purposes of CDD, to be accessible and searchable through a centralized automated mechanism.

Identification of legal entities through a valid LEI, an internationally accepted unique identifier, is also consistent with the Bank of England's ISO 20022 goals for modernizing the UK payment system and primarily use LEI as the identifier among payment institutions and then to extend LEI mandate to a wider range of parties to these transactions. LEI itself can be considered a relevant attribute in many applications where authenticated transactions are relevant.

LEI is a quality-controlled unique identifier supported by a transparent infrastructure of local identity validation and a centralized open data challenge service. LEI also acts as an identification key between databases/platforms. Use of the LEI requires no special access arrangements to use the LEI data and no concern to expose any confidential information.