Response of the Global Legal Entity Identifier Foundation (GLEIF) to the European Banking Authority's call for input on 'de-risking' and its impact on access to financial services
September 2020

The Global Legal Entity Identifier Foundation (GLEIF) is pleased to provide comments to the European Banking Authority call for input on 'de-risking' and its impact on access to financial and banking services.

GLEIF will focus its comments on the use of the Legal Entity Identifier (LEI) in countering de-risking and its impact on access to financial and banking services.

According to the most recently published data by the Committee on Payments and Market Infrastructures (CPMI), the number of correspondent banking relationships has shrunk by 20% over the past seven years. The continuing decline in the number of correspondent banking relationships in many countries around the world remains a source of concern. De-risking causes the loss of significant numbers of clients, especially corporate companies and exporters.

Despite different interpretations of the cause behind this trend, there is general agreement that global financial institutions follow a rather conservative approach in their anti-money laundering (AML)/counter terrorist financing (CTF) risk perception. This conservative approach is linked with increasing costs due to (i) penalties for non-compliance with AML, Know your Customer (KYC), and sanctions regulations and (ii) client identification. According to Fenergo's most recent mid-year report, by the end of July 2020 global financial institution fines have totaled $5.6 billion. Other research conducted by Fenergo showed that the fragmented nature of the onboarding process might cost up to 22,000 Euros per institutional client for financial institutions.

Additionally, a research report produced by Loudhouse on behalf of GLEIF found that financial institutions use on average 4 different identifiers for identifying a legal entity client. Using multiple identifiers leads to inconsistent information, a drain on resources as reconciliation of different identifiers requires manual intervention, and lack of transparency due to reliance on proprietary identification systems. Identifiers of legal entities are easily obtained from a host of different issuers but are not kept up-to-date in a systematic way.

Therefore, as the current financial system, even in low-risk jurisdictions, is already costly due to existing inefficiencies in client identification processes, reliance on respondent banks' client identification and KYC processes becomes more costly and risky for many financial institutions.

GLEIF suggests that improved and standardized legal entity identification using the Legal Entity Identifier (LEI) can reverse this trend and help to create an efficient, secure and transparent financial ecosystem for all. The EBA could consider encouraging a collaborative Customer Due Diligence (CDD) approach, where the LEI is obtained as part of the client identification and the very first fundamental step performed. GLEIF would like to elaborate further on how such an approach would work in practical terms, would serve to counter de-risking and would improve client identification capabilities on a global scale.

For a correspondent bank, establishing the identity of the respondent bank is a fundamental area of due diligence. Therefore, the EBA could consider requiring correspondent banks to consistently leverage the LEI for respondent bank identification to enhance their CDD and AML/CFT capacities.

Additionally, correspondent banks should require respondent banks to identify all legal entity clients with an LEI. This could be completed at the time of onboarding or during ongoing customer lifecycle management. As suggested in the report of the International Finance Corporation (IFC) of the World Bank, encouraging emerging market banking customers to obtain LEIs would further support banks' capacity for CDD and AML/CFT. The LEI, a globally recognized standard for entity identification, can help to overcome the informality gap in some developing countries, where local systems for entity identification are not easily accessible, may not be transparent, and sometimes lack quality standards. Equipping the entities in these countries with the LEI could help them to access cross border payments, credit facilities, and supply chains without identity restrictions. It would also enable clear communication and information sharing between all involved parties – respondent banks, correspondent banks, and supervisory authorities. Therefore, contributing to a secure financial ecosystem where all involved parties are clearly identified and verified.

When the correspondent banks and respondent banks speak the same language in entity identification, risk assessment and associated costs should be lower for all involved parties. Financial Institutions can easily connect to the Global LEI Repository via the GLEIF Look-up Application Programming Interface (API), which allows developers to access the complete LEI data pool in real-time directly and perform on-demand checks for changes to specific LEI records in a convenient and easy-to-read format. The application, developed by the GLEIF, responds to the market needs of multiple LEI stakeholders, including financial institutions, regulators, fintech companies, third party payment providers and analysts seeking to include LEI data in their machine-readable and automated processes. The GLEIF API can easily be integrated into internal systems based on the widely supported JSON data format. The use of the API is free of charge and does not require registration.

Under the "Validation Agent" framework, GLEIF pilots with financial institutions leveraging their know-your-customer (KYC), anti-money laundering (AML) and other regulated 'business-as-usual' onboarding processes, to enable clients to obtain an LEI during initial onboarding or standard client refresh cycles. Optimizing the quality, reliability and usability of LEI data empowers market participants to benefit from the wealth of information available with the LEI population and is at the core of GLEIF's mission. This mission would be particularly transformative for legal entities with limited data footprint. GLEIF is currently engaging in several pilot projects with financial institutions to evaluate jointly the operational, legal, and technical adjustments required to make this model a success.

Lastly, as rightly put by the FATF's current President Dr. Marcus Pleyer, all financial market participants and policy makers should avoid discouraging legitimate economic activity in the financial ecosystem. A trusted identity is the first step to financial inclusion for micro, small and medium enterprises and is a foundational in the journey to ensure access to finance and to prevent entities from migrating to unregulated areas due to de-risking.