What is Asia's Risk Management Number?

Nicholas de Boursac, CEO of the Asia Securities Industry & Financial Markets Association (ASIFMA) feels the FSB and G20 will advise members to implement a universal Legal Entity Identifier by end 2012.

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In the wake of the global financial crisis, key international regulatory bodies, such as the FSB, the G20 and IOSCO, have recognized the need for a global approach in compiling data to identify counterparties to transactions and allow for more comprehensive monitoring of such transactions and entities. Many if not all jurisdictions assign a reference number or code to legal entities upon registration, but currently no standardized international code exists that consistently identifies an entity, regardless of jurisdiction. Without such a standard, regulators cannot efficiently and swiftly communicate among themselves regarding issues related to the monitoring or aggregation of activities or exposures across jurisdictions.

Good data leads to good analysis, which is the lifeblood of effective surveillance. Market participants also stand to benefit from a universal Legal Entity Identifier (LEI) system, since it will improve reference data quality and significantly enhance operational efficiencies around legal entity data management, such as aggregation of counterparty data, risk modeling, and hierarchy management. In addition, this will allow firms to offer improved customer service through enhanced customer on-boarding and more efficient corporate action management, among other practices. Over time, use of global LEIs will no doubt also improve the straight-through processing of transactions.

To address the need for enhanced monitoring, a group of international financial industry associations, with input from regulators, developed a coordinated approach to counterparty identification based on a unique 20-digit code that would be assigned to all entities through the application of specifically developed ISO standard for LEIs, namely ISO 17442 (to be released early in 2012). This effort, commonly referred to as the LEI solution, is gaining momentum rapidly. In addition to a unique code for each legal entity, a limited amount of data attributes would be collected and stored, including the entity's legal name and address. The LEI database would make only the public data attributes available to market participants and would not collect any transaction or position information. Transaction and position information would be gathered and managed separately by relevant regulators under current standards of confidentiality. One obvious benefit of this approach is that it would allow the global regulatory community to monitor systemic risk and cross-border transactions quickly and efficiently, while at the same time enhancing cross-border communications among regulators.

The LEI solution currently under consideration is based on six principles;

- measure and monitor global systemic risk
- promote regulatory coordination
- design a pragmatic, adaptable solution
- encourage participation
- make data freely available
- promote non-profit governance.

It's obvious that the current multiplicity of identifiers inhibits cross-border communications among regulators, since incompatible identifier numbers cannot be imported into existing databases; and this also inhibits the effectiveness of risk monitoring for market participants. Universal adoption of global LEIs will fill this information gap. Currently, the political will to establish such a solution appears to exist, creating an opportunity to move forward that should be seized with both hands.

The Hong Kong Monetary Authority (HKMA) seems to have taken an early step in Asia, recommending the adoption of LEIs in a recent trade repository related rule making. Canadian Securities Administrators also have recognized the value of LEIs, and other financial regulators, like the US Commodity Futures Trading Commission and Australian Securities Investments Commission, have indicated the intention to apply a global LEI regime as well.

While momentum is gaining for the broad adoption and implementation of LEI standard by global regulators, challenges remain. Jurisdictions in Asia and across the globe will need to address perception issues surrounding privacy and find ways to create incentives or draft rules to encourage or require LEI registration for entities trading in their respective markets. Additionally, certain smaller Asian markets may consider the cost of implementation high relative to the nominal size of their current cross-border transactions. The success of the LEI solution will rely not only on global implementation of a uniform approach to gathering and maintaining LEIs, and broad cross-border coordination among regulators and market participants, but also the establishment of an inclusive and appropriately structured governance model for the proposed LEI utility, which is still being finalized.

We believe the FSB and the G20 will advise members to implement a universal LEI by the end of 2012. Endorsement at such a high level will provide the necessary regulatory mandate and momentum for jurisdictions to write the LEI approach into rulemakings, first for OTC derivatives and later for other financial transactions.

With all of the benefits of a global LEI solution in mind, we think the time for action has come and applaud early adopters for providing leadership in this important endeavor. We anticipate that within a few years regulators and market participants both in Asia and around the world will wonder why on earth they didn't agree to implement the LEI approach sooner.