Paragraph 1 of Article 1 *SEG – Segregation of initial margins* under Chapter 4 – *Operational procedures* (the "**Segregation Requirement**") of the *Draft Regulatory technical standards on risk-mitigation techniques for OTC derivative contracts not cleared by a CCP under Article 11(15) of Regulation (EU) No 648/2012* dated 14 April 2014 (the "**Draft RTS**") provides that counterparties must segregate initial margin from their proprietary assets on the books and records of a third party holder, or via other legally effective arrangements made by the collecting counterparty. The use of phrase "other legally effective arrangements" would suggest that the European Supervisory Authorities ("**ESAs**") have provided market participants with the flexibility of devising any structure that achieves the goal of effective segregation so long as the structure is legally enforceable on the counterparties in the relevant jurisdiction(s).

The proposed ban on re-hypothecation set out in Article 1 *REG – Treatment of collected initial margins* under Chapter 4 – *Operational procedures* of the Draft RTS (the "**Re-Hypothecation Ban**") without a clear definition of what is meant by re-hypothecation, re-pledging or re-use of collateral has the potential consequence of creating uncertainty respecting the viability of potential legal solutions to the Segregation Requirement, especially if such solutions involve a title transfer of initial margin to a third party for the benefit of the posting counterparty.

Whilst it is assumed that the ESAs intend for the Re-Hypothecation Ban to apply to the use of posted initial margin by a collecting counterparty for its own commercial financing purposes it would be helpful if this was made clear (as has been done for example in the recently published European Commission's *Proposal for a Regulation of the European Parliament and of the Council on reporting and transparency of securities financing transactions COM (2014) 40 final – 2014/0017 (COD)*).

In addition, it is submitted that any proposed Re-Hypothecation Ban be limited only to any financing technique which would not allow a counterparty to comply with the Segregation Requirement. Stated another way, provided that a collecting counterparty engaging in normal course repo or securities lending financing receives equivalent high quality collateral (after applying any appropriate haircut valuation) in exchange for any initial margin collected from a posting counterparty and such exchanged equivalent collateral is held in a segregated manner in accordance with the Segregation Requirement and is made immediately available to the posting counterparty in the event of the default of the collecting counterparty (as supported by satisfactory legal opinion(s)) there would appear to be no policy reason to prohibit or regulate the re-use of initial margin by collecting counterparties.

Whilst not directly relevant to the proposed Re-Hypothecation Ban we also note that paragraph 3 of the Segregation Requirement is problematic. Cash, being fully fungible, is difficult if not impossible to segregate from other assets. Full title to any cash posted as initial margin is given to a collecting counterparty and a posting customer merely has a contractual claim for repayment of an equal amount of cash which in effect means that the posting member ranks as an unsecured creditor in the estate of the collecting counterparty in the event of an insolvency. It would therefore be helpful if the ESAs provided further clarity on how, in practice, the segregation of cash can be achieved.