EP ENERGY

April 15, 2014

Mr. Robert deV. Frierson
Secretary
Board of Governors of the Federal Reserve System
20th Street and Constitution Avenue, NW
Washington, DC 20551

Re: Complementary Activities, Merchant Banking Activities, and Other Activities of Financial Holding Companies related to Physical Commodities, RIN 7100-AE-10

Dear Mr. Frierson:

EP Energy LLC ("EP Energy") would like to thank you for the opportunity to provide comments to the Board of Governors of the Federal Reserve System's ("Board") Advance Notice of Proposed Rulemaking regarding the activities of Financial Holding Companies ("FHCs") related to Physical Commodities (the "ANPRM"). We also appreciate the Board analyzing this issue for the benefit of all market participants, including end-users like us. To that end, we submit this comment letter to assist the Board and to make clear that any additional restrictions on FHCs' ability to trade in physical commodities will negatively impact energy markets by reducing liquidity, reducing the number of strong creditworthy counterparties and significantly increasing volatility for all market participants.

I. Background

EP Energy, together with its affiliates, is an independent Exploration & Production Company engaged in the acquisition and development of unconventional onshore oil and natural gas properties in the United States and in the sale of oil, natural gas and natural gas liquids produced from those properties. In the process of producing and marketing our oil and natural gas production, we transact in physical commodities and commodity derivatives. It is essential for our business to access these markets in order to sell and hedge our production against normal and expected price volatilities while maintaining stable cash flows which are critical to our operations.

As an end user, EP Energy is a price taker; therefore, we need the market to be competitive and liquid, with many strong counterparties. FHCs have been very creditworthy and critical market participants over the past decade. Even though the physical commodities marketplace contains a variety of market participants, generally the market includes a relatively small number of market-makers in each commodity sector. FHCs provide our businesses access to well-regulated counterparties/market-makers with whom we can efficiently and effectively transact at the appropriate times when such actions are needed to best manage our risk. Further, FHCs' ability to offer a suite of products in different asset classes provides us and many other end-users (e.g., airlines, chemical makers, refiners, producers, marketers, power producers, etc.) with the ability to manage our business risks conveniently and cost-effectively. FHCs have become a critical element of the physical market and have largely supplanted the oftentimes less dependable trading companies that dominated the marketplace in the early 2000's. Our fear is that once the FHCs leave the market, lightly regulated trading companies with fill the void, introducing significantly greater risk to the market.

In our experience, FHCs are highly rated credit-worthy counterparties with market experience and the ability to handle market volatility. The Board, in its ANPRM, worries about the risks arising from catastrophic environmental events, such as Deepwater Horizon and states, "The fact that a FHC has not been involved in such an event to date does not reduce the probability that such an event may occur." But this assertion is not substantiated by empirical data. Moreover, such risks attach to owner/operators of energy facilities and FHCs, in their role as market makers in physical commodity markets, are not usually involved in owning or operating energy facilities. It stands to reason that a FHC, acting as a market maker (and not, for example, as an extractor or refiner), is at extremely low risk of such an event. In fact, the market events identified by the Board in its ANPRM and that serve as a basis for the position that additional regulation may be necessary only underscore the ability of FHCs to properly manage these risks and reinforce the importance of FHCs in these markets, particularly to end-users. In our opinion, the financial crisis in 2008 was not caused by FHCs' involvement in physical commodity markets but rather their involvement in the financial derivatives market.

II. Additional Regulation of FHCs' Physical Commodities Activities Could Result In These Entities Exiting the Marketplace, Negatively Affecting End-Users

A primary reason we transact with FHCs in physical commodities and related derivatives transactions is because FHCs: 1) have strong balance sheets and are creditworthy counterparties that can soundly sustain significant and vital long-term transactions; 2) have strong compliance cultures and well-resourced support functions; 3) are supervised by regulators such as the Board; 4) possess sophisticated risk management abilities; 5) often have longstanding relationships with end users; and 6) provide real benefits to physical commodity companies by undertaking transactions that can span financial and physical activities. In addition to the counterparty benefits of FHCs, they are also important market makers in physical energy and related derivative markets and help provide market liquidity. Under the broad purview of the Federal Reserve, FHCs are subject to minimum capital requirements and safety and soundness regulations, among other statutes and regulations. In addition, FHCs are subject to regulation and oversight by the Securities & Exchange Commission ("SEC"), the Commodity Futures Trading Commission ("CFTC"), and the Federal Energy Regulatory Commission ("FERC"). As end-users, we are confident that the current regulatory framework is sufficient to protect the financial system and to properly regulate FHCs' physical commodities activities.

We fear that additional regulation of these activities, including, among other things, the imposition of increased capital requirements, will deter FHCs from participating in the physical commodities space. This fear is not without merit as some FHCs have already begun to withdraw from their physical commodities activities. It would only be reasonable to conclude that more FHCs, and their affiliates, will exit the marketplace if additional restrictions on their physical commodities activities are adopted, which will negatively impact liquidity and increase costs making it more difficult and expensive for end-users to transact in physical commodities activities necessary to run their businesses and serve their customers. These costs will be priced into end-users' products and ultimately passed to the U.S. consumer in the form of higher commodity prices.

A. The Departure of FHCs From The Physical Commodities Marketplace Could Lead to Unregulated Entities Assuming A Larger Role

If FHCs exit the physical commodities markets, end-users likely would be required to transact with an increased number of unregulated – or less regulated – entities, as was the case in the early 2000's when trading shops like Enron ruled the marketplace. Engaging in transactions with unregulated entities will create a greater risk to the physical commodities markets than the potential tail risks identified by the Board in the ANPRM. As end-users, we seek to hedge or mitigate our risks in the physical commodities markets; however, transacting with unregulated or less regulated entities unnecessarily, and significantly, increases our counterparty and market risk.

As discussed above, the current regulatory framework instills confidence in end-users that we are protected when trading with FHCs. That confidence does not exist with respect to unregulated entities. They are not subject to the same regulatory restrictions as FHCs, and it is not clear the extent to which they would have sufficient capital to take on all of the physical commodities activities currently conducted by FHCs. It certainly is the case that these entities are not subject to the same oversight by regulators such as the Federal Reserve, SEC, CFTC and the FERC. Moreover, the countries in which certain of these unregulated entities operate are not as economically stable as the United States. Although it is not our preference to transact with unregulated market participants, we fear that additional regulation could leave us with no other choice. Transacting with unregulated entities could threaten credit, safety and soundness and pose other concrete economic risks that exceed in severity the potential tail risks referenced in the ANPRM.

B. The Departure of FHCs From The Physical Commodities Marketplace Could Lead to Market Illiquidity

If FHCs depart the commodities markets due to additional regulation, end-users could suffer from reduced liquidity. This result has already begun to occur in certain physical commodity markets due to recent decisions by certain FHCs to exit such markets. The additional restrictions that the Board is contemplating would only exacerbate this exodus and result in additional market harm. Increased concentration will assuredly have the effect of increasing costs to access these services, which we, as end-users (and ultimately, our customers), will be forced to bear. It is also possible that the hedging transactions we engage in with FHCs will simply be unavailable as a result of the lack of market participants with the relevant type of expertise in the marketplace. Further, our profitability, along with many other end users, may be threatened to the extent we are unable to appropriately and efficiently manage risk.

III. Conclusion

For the foregoing reasons, we believe that the Board should not impose restrictions on FHCs that would prohibit them from engaging in meaningful future physical commodities activities. We, along with many other end-users, rely on FHCs as reliable, regulated counterparties for physical commodity activities. EP Energy believes the benefits of FCHs' participating in the physical commodity markets are significant to small, medium and large businesses because they add liquidity, provide creditworthiness & experience, increase healthy competition and are already highly regulated. We do not want to return to the early 2000's when unregulated, sometimes less-than-dependable traders, ruled the day. Accordingly, we respectfully request that the Board not proceed with any rulemaking in this area and instead that it continue its successful regulation of these entities within the current regulatory framework. We again appreciate the opportunity to comment and would be pleased to answer any questions the Federal Reserve staff may have for us as it continues to analyze these issues.

Yours sincerely,

Dennis Price
Vice President, Marketing