Delek US Holdings, Inc.
7102 Commerce Way
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February 20, 2017

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

Via Electronic Submission

Re: Comment to Notice of Proposed Rulemaking – Regulations Q and Y; Risk-Based Capital and Other Regulatory Requirements for Activities of Financial Holding Companies Related to Physical Commodities and Risk-Based Capital Requirements for Merchant Banking Investments [Docket No. R-1547; RIN7100 AE58]

Dear Mr. Frierson,

On behalf of Delek US Holdings, Inc. ("Delek"), we appreciate the opportunity to submit this letter in response to the Board of Governors of the Federal Reserve System's (the "Board") Notice of Proposed Rulemaking (the "Proposed Rule") regarding the physical commodities activities conducted by financial holding companies ("FHCs").[1] We are submitting this comment because our business both relies on FHC market making functions and regularly transacts with FHC counterparties in physically settled commodity transactions to support our operations. As noted in our previous comment to the 2014 Advanced Notice of Proposed Rulemaking,[2] we would like to take this opportunity to note our belief that the Proposed Rule's punitive requirements on FHCs engaged in commodities activities would directly burden commodities-based US businesses. Delek, in particular, would likely face increased market risks, costs, and greater instability in light of restrictive capital requirements to counterparties in which we rely upon to effectively manage our business needs. Because of the importance of sustainable growth within our industry, we respectfully request that the Board reconsider

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[1] Notice of Proposed Rulemaking, Regulations Q and Y; Risk-Based Capital and Other Regulatory Requirements for Activities of Financial Holding Companies Related to Physical Commodities and Risk-Based Capital Requirements for Merchant Banking Investments, 81 Fed. Reg. 67220 (Sept. 30, 2016) [hereinafter the "Proposed Rule"].

[2] See Delek US Holdings, Inc. comments to the Advance Notice of Proposed Rulemaking, Complementary Activities, Merchant Banking Activities, and Other Activities of Financial Holding Companies related to Physical Commodities (Docket No. 1479 and RIN 7100 AE-10) (submitted Apr. 16, 2014), available at https://www.federalreserve.gov/SECRS/2014/May/20140509/R-1479/R-1479_041614_124570_481900486198_1.pdf.

the downstream effects and costs the Proposed Rule may have on market participants and revise the Proposed Rule accordingly.

I. Who Are We?

Delek is a diversified downstream energy company with operations in two primary business segments: petroleum refining and logistics. We are headquartered in Brentwood, Tennessee and employ more than 1,300 people across three states.

- Our refining segment operates 155,000 barrels per day in combined production capacity at refineries in Tyler, Texas, and El Dorado, Arkansas.
- Our logistics segment gathers, transports, and stores crude oil, as well as markets, distributes, transports and stores refined production in the southeast US and west Texas. These operations support our refining segment and third parties.

In order to serve its customers and to help manage its complex business, Delek depends upon the physical commodity and commodity derivatives markets to help manage its business in meeting the needs of its customers. These markets not only play a critical role in assisting Delek with conducting its day-to-day business, but also serve to as effective mechanisms in which we manage market and commercial risks.

II. How We Rely on FHCs to Grow Our Business and Mitigate Risk, An Example

Under a current arrangement at our El Dorado refinery, FHCs assist in sourcing certain of the crude oil to be delivered to the refinery, purchase all of the crude oil either from the source or from Delek and hold title to such crude oil until its arrival at the refinery. Following our refining of the crude oil, FHCs then repurchase the refined products and deliver them using our logistics assets to the point of sale, where we then sell the refined products to our and FHC customers.

This arrangement is advantageous to Delek for a number of reasons. First, this arrangement obviates the need for us to arrange for separate financing of our inventory of both crude oil and refined products at the El Dorado refinery. Because FHCs hold title to the crude oil on its way to the refinery and to the refined products on their way from the refinery to the point of final sale, the only inventory required to be financed by Delek is the linefill within the refinery itself. Absent these arrangements with FHCs, we would be forced to finance approximately $150-250 million in working capital through an asset-based loan or other type of traditional financing, with the inventory of crude oil and refined products almost certainly required to serve as collateral. Such financing customarily involves a syndicate of multiple lenders and includes restrictive covenants and other provisions with respect to available borrowing base and other financial requirements, all of which would likely restrict our flexibility to acquire feedstocks, manage inventory or to make acquisitions and other capital investments in growing our business in comparison to our current arrangement with FHCs.

Second, because we only hold title to crude oil and finished product inventory during the limited time such inventory is being processed at the refinery, this arrangement lessens the need for us to hedge our exposure to price fluctuations that affect the spread between prices at which we purchase crude oil inputs and sell refined product outputs. Without this arrangement, whereby FHCs hold title to both crude oil prior to entering the refinery and refined products after leaving the processing units, the period of time for which a very large portion of our El Dorado inventory would be exposed to commodity price risk would be much longer, necessitating more expensive hedging instruments against the greater risk.

III. We Are Concerned With the Punitive Nature of the Proposed Rule

Our commercial needs are best addressed by deep, competitively priced markets. We are concerned that the Proposed Rule would decrease overall market depth in a sector that has already retracted due to increased legislative and regulatory scrutiny. Compounding burdens on the activities of FHC counterparties will serve to only further reduce the number of banks willing to transact in physical commodities. As the Board has already admitted,[3] and based on our business interactions, there has been a retraction in the markets since the Financial Crisis. The Proposed Rule would negatively impact markets by increasing risk weighting and capital requirements for FHCs relying on Section 4(o) and Section 4(k) authority.

Failure to consider the practical implications of the Proposed Rule and the real possibility of a market with limited to no FHC activity has the potential to adversely affect Delek by increasing prices and reducing the number of sophisticated parties in which we rely on to efficiently hedge, finance and otherwise transact within the commodities market.

IV. We Require Sophisticated Counterparties

While we acknowledge that we likely would be able to engage in certain financing and hedging transactions with other intermediaries, we think it would be highly unlikely that any single intermediary could or would be willing to offer us the combination of strong knowledge of the commodities markets themselves with the financial resources and credibility that FHCs alone offer together. Moreover, we do not believe that the remaining intermediaries that exist in or could be expected to enter the market would be

[3] The Advanced Notice of Proposed Rulemaking notes that 14 FHCs are currently authorized to engage in physical commodities activities, either under Section 4(k) or Section 4(o) of the BHCA. See Advance Notice of Proposed Rulemaking, Complementary Activities, Merchant Banking Activities, and Other Activities of Financial Holding Companies related to Physical Commodities, 79 Fed. Reg. 3329 (Jan. 21, 2014).

able to service our physical commodity and commodity derivatives needs as well as FHCs currently do because of FHCs' unique combination of favorable characteristics:

- FHCs are sophisticated market participants that are in the business of making markets in physical commodities and related derivatives products.

- FHCs have the extensive market presence and knowledge to allow them to purchase and store crude oil and refined products in ways that are advantageous to end-users like Delek, obviating our need for alternative financing and risk mitigation with respect to those materials.

- FHCs are knowledgeable, sophisticated and active market participants that are able to customize creative solutions for our business's specific needs and to suggest transactions proactively that are beneficial and in which, otherwise, we would not have engaged.

The flexibility and other benefits provided by FHCs' participation in the physical commodity markets, including unique financing arrangements that meet our needs and that also reduce our exposure to risk and the benefits provided by partnering with a knowledgeable, sophisticated and active market participant, would likely not otherwise be available to smaller market participants such as Delek from other potential traditional trading counterparties in the market.

In particular, we would note that many non-bank institutions, when compared to FHCs, lack the capital necessary to engage in large trades; do not provide the economies of scale and cost-savings; tend to focus on niche areas of the commodities market (e.g., dealing only in certain commodities); cannot provide a one-stop financing and hedging solution; are relatively less sophisticated; and most importantly, will likely only engage in this space to meet their discrete needs. In contrast, FHCs' economies of scale provide flexibility to Delek by having the resources to fund the purchase of crude oil opportunistically at times when cost-advantaged refinery feedstocks are available and then store such feedstocks until Delek is able to process it—a benefit that we would not be able to realize without the support of an FHC. For example, during a periodic maintenance turnaround at our El Dorado refinery, FHCs continued purchasing crude oil for eventual processing at the refinery under Delek's current arrangement at lower local prices available at that time and then, using their and Delek's relationships, stored that crude oil for later use by the refinery following resumption of processing after the turnaround was complete. The FHCs' ability to continue purchasing at advantageous prices and store the crude oil until Delek's refinery was able to take delivery in effect preserved Delek's access to such favorably priced crude oil immediately upon refinery restart and for the long term. Without the participation of FHCs in the market and the flexibility provided thereby, Delek could otherwise have been forced out of the purchasing market while the refinery was in turnaround and could in consequence have lost its access to this favorably priced, locally sourced crude oil.

FHCs are large enough to operate across the market, provide depth and transparency to less opaque commodities (e.g., asphalt), are better equipped to tailor products to individual companies, provide financing solutions for commodity rich businesses, and provide an economical venue in which to hedge commodities risks.

V. We Require Liquid Markets

As a market participant in physical commodities and commodity-based derivatives, we wish to emphasize that efficient markets require depth, competence and narrow pricing spreads. We are concerned that, especially in the markets for highly-customized commodity products, a retreat by FHC affiliates will lead to greater market illiquidity and greater price variation.

We believe the current participation of FHCs and their affiliates as market-makers in physical commodities increases the liquidity of the market, reduces bid and ask pricing spreads, increases the overall volume of commodities products, and reduces price volatility. By facilitating the exchange of physical commodities, FHCs help to stabilize commercial growth by providing a mechanism in which businesses, particularly smaller independent refiners like Delek, can manage their short- and long-term inventory needs.

It would therefore be presumably more difficult and expensive for companies like Delek in a relatively illiquid marketplace to access the physical commodity markets as efficiently as we do with FHCs, and we would likely not be able to obtain the customized solutions that FHCs currently provide us. Fewer market participants and reduced liquidity likely would increase our costs of participating in these markets, and we believe these increased costs would have an anticompetitive impact by exerting a disproportionately negative effect on smaller market participants like Delek than some of our larger competitors that could absorb these costs as a result of their scale and/or vertical integration.

In addition to market access, a reduction in market liquidity could increase price differentiation between the physical and related financial assets. Unlike other financial products, commodity instruments are directly related to the physical product itself. Under the current regulatory authority of Section 4(o) and Section 4(k), the volume of commodities-based transactions by FHCs help to reduce any inefficiency in the market by better converging prices of the financial instrument and the correlating physical commodity. The Proposed Rule, however, ignores this critical function and would likely subject us to increased risks due to price differences and market arbitrage.

The Proposed Rule would drastically reduce an FHC's ability to provide such services by increasing funding costs and limiting their reliance on Section 4(k). As FHC affiliates are frequently the most knowledgeable, most willing and most equipped participants to address our market-necessary customized trades, we will likely experience a reduction in the volume and variety of commodities-based products.

As market participants and operators of physical commodity refineries, we rely on accurate and efficient pricing of physical commodities.

VI. We Prefer to Transact with Financially Sound and Well-Regulated Counterparties

Our business is already wrought with numerous risks – market solutions and corresponding regulation should serve to reduce such risks, not increase them. Stability and credibility in our counterparties is an important characteristic in which we have come to rely upon. We view FHCs as a strong counterparty to our commodities transactions because they are well regulated by various agencies, including the Board, the Securities and Exchange Commission, the Commodity Futures Trading Commission and the Federal Energy Regulatory Commission. In addition, smaller market participants like Delek are often able to leverage the widely recognized credibility of FHC intermediaries as transaction partners to obtain more favorable transaction terms from other market participants than would be made available to market participants that are less well known, less regulated, and less stable. Unlike FHCs, however, these entities are unlikely to provide the same credibility benefits, as they almost certainly would not be subject to the same extensive regulation covering FHCs, nor would they be likely to have the same recognition and credibility with all participants across the marketplace. As such, transacting with such entities could pose additional risks to our business, such as counterparty risk, that we do not currently regard as significant. The Proposed Rule threatens to destabilize the current regulatory framework, a regime that gives both us and our business partners confidence when transacting with and through the intermediation of FHCs, and the entities that might take their place may not engender the same confidence or, therefore, deliver the same benefits.

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For the foregoing reasons, we believe that the Board should reconsider the Proposed Rule's additional restrictions on FHCs that engage in physical commodities and commodity-related derivatives activities. As currently contemplated, we believe the Proposed Rule would have the effect of harming end-users, especially smaller and/or regional market participants such as Delek. We again appreciate the opportunity to comment and are happy to answer any questions the Board may have as it continues to analyze these issues.

Very Truly Yours,

Delek US Holdings, Inc.

Assaf Ginzburg
Executive Vice President and Chief Financial Officer