



December 29, 2005

U.S. Department of Energy
Office of Fossil Energy (FE-30)
ATTN: Trudy Transtrum
1000 Independence Avenue, SW
Washington, DC 20585

Re: Request for Comments on the Outlook for Natural Gas Supply and Demand

Direct Energy Services, LLC ("Direct Energy") appreciates the opportunity to submit these comments on the outlook for natural gas supply and demand in the United States.

Direct Energy strongly believes that the Department of Energy (the "Department") should use this process to begin to collaborate with government at all levels to further strengthen and expand retail and wholesale natural gas markets so that all consumers can get the best possible service at the best possible price. While increased conservation and increased supply are critical to respond to the current price environment, Direct Energy believes that too often well-functioning markets are not seen as a key part of the solution. In fact, Direct Energy argues that Department should use its resources to help educate consumers that have a choice of natural gas suppliers and a choice of pricing arrangements to make affirmative decisions about their natural gas needs. Moreover, Direct Energy believes that the Department should work to expand retail and wholesale competition

wherever possible. Finally, Direct Energy believes that the Department should work to inform policymakers to consider very skeptically calls for price controls or cost deferrals; this is the wrong solution to restore a more balanced supply and demand situation. In fact, now is the time to strengthen and expand retail and wholesale natural gas markets, not to move backward from whence we came.

I. BACKGROUND

Direct Energy is a subsidiary of Centrica, a global energy company with upstream natural gas production and storage assets, electric generation, retail natural gas and power customers, and a growing presence in the LNG marketplace. Centrica has annual revenues of \$33 billion, \$17 billion in market capitalization, 38,000 employees, and over 25 million customer relationships. For more information on Centrica, please visit our website at www.centrica.com.

Direct Energy has over 5 million customer relationships in North America. In the United States, Direct Energy provides natural gas, electricity and energy-related services to customers in Texas, Ohio, Michigan, Pennsylvania, Illinois, New Jersey, Maryland, Rhode Island, Connecticut, Maine and Massachusetts. Importantly, Direct Energy is one of a small number of competitive energy retailers that offers its services to both business customers and to households. Specific to this discussion, Direct Energy is proud of the fact that we recently won the business of our 200,000th customer in the Ohio natural gas markets. We are strongly committed to our customers and to making energy markets function well for all consumers.

II. COMMENTS

In order to ensure reliable and affordable energy for American consumers, economic growth and prosperity in the United States, and a healthier environment, it is critical that competitive natural gas markets be strongly encouraged and vigorously promoted at both the retail and wholesale levels. Markets are the best solution for balancing supply and demand in the short term *and* in the long term. Markets most efficiently and effectively allocate resources and infrastructure by sending proper signals to producers and consumers. Markets also allow individual consumers to make individual decisions that are appropriate for their specific needs.

A. Benefits of Competitive Natural Gas Markets

Ohio provides a very good example of how competitive natural gas markets benefit consumers, and ultimately the overall economy. During the 1970s, Ohio faced a huge problem – natural gas regulation had not provided sufficient incentives to maintain a reasonable and reliable supply of natural gas. Curtailments and fears of curtailments were a significant topic of discussion.¹ Jump forward to today. Given pro-market policy changes at both the federal and state level, natural gas supply reliability is no longer an issue in Ohio.

But the benefits of competitive natural gas markets are not limited solely to reliability. Competitive markets also allow consumers to make important choices about service, terms and prices. In Ohio, many businesses and households (over 1 million in total) make an individual decision about how to manage their needs.² For Direct Energy's

¹ US Congress Office of Technology Assessment 'An Analysis of the Impacts of the Projected Natural Gas Curtailments for the Winter 1975-1976' November 1975.

² Nearly 60% of the 1.2 million customers of Dominion East Ohio Gas have switched to a competitive supplier, with around 30% switching in the Columbia Gas of Ohio and Vectren Energy Delivery of Ohio

customers in Ohio, there are many that signed up on a price protection program before the recent supply disruptions caused by Hurricane Katrina and Hurricane Rita. In signing up for a price protection program, these families and businesses made an affirmative decision to take market risk out of their pocketbooks. These customers were not necessarily looking for the lowest possible price; they were looking to manage the uncertainty related to future natural gas costs. Given the current situation, our Ohio customers have already saved millions of dollars this winter heating season versus what they would have paid by remaining as a sales customer of their Local Distribution Company. None of these benefits could have occurred without functioning retail and wholesale natural gas markets.

But retail competition has another benefit. Given the nature of risk management, when companies like Direct Energy help our customers manage their market risk, we will contract with producers or marketers to guarantee either price and/or delivery. This process provides a real price signal to natural gas producers that allow them to make investment decisions. Hence, the action of individual households and businesses to manage their specific needs works through the market to ultimately provide producers with proper price signals.³

B. Regulatory Intervention Must Not Simply Defer the Problem

Direct Energy fully appreciates the difficulty the current price environment causes many consumers. We strongly suggest, however, that policymakers avoid attempts to “move” the problem to another timeframe. Specifically, Direct Energy believes that price

markets. This competitive activity is a testament to the Public Utility Commission of Ohio focusing on implementing workable natural gas markets, including recent decisions establishing monthly Gas Cost Recovery mechanisms based largely on NYMEX prices.

³ Our policy position, in which each consumer is allowed to express his or her own preference and risk tolerance, is vastly different than the policy recommendation that would have a Local Distribution Company make a “one size fits all” forward contracting decision on behalf of their ratepayers.

controls or deferral mechanisms, while well intentioned, are not the right answer for consumers and will only further compound our current problem. Under these solutions, consumers do not see real price signals and are therefore unable to adjust their usage to the current price environment. This creates problems in both the short-term (where price will signal consumers to use less this Winter) and in the long-term (where price will inform consumers to make more efficient decisions on new equipment). In addition, under deferral programs, consumers will still have to pay for the natural gas they consume (in many cases also paying interest). Any policy that sets up a false notion that “cheap” natural gas is available both today and into the future is the wrong approach .

C. Actions to Support Competitive Natural Gas Markets

Given the benefits of retail and wholesale natural gas markets, Direct Energy believes that the Department should work throughout the natural gas industry to promote and further encourage competition. For instance, the Department could expand this request for comments to include a discussion of barriers to effective retail and wholesale natural gas markets. Included with this discussion should be an analysis of how market rules vary by state (and often by Local Distribution Company within a state) and the impact of this lack of standardization on competitive markets and consumers.⁴

The Department should also use its resources to help educate consumers on their options; consumers in competitive markets should be sent a strong message that they have the right and ability to take market risk out of their pocketbooks. The Department should help customers understand that they have options.

⁴ Retail natural gas markets are at various stages of advancement across the United States. Nearly all states allow large consumers to choose their retail natural gas supplier, but this is not true for medium and small natural gas customers. In states that have allowed retail natural gas competition, there are significant rule and operational differences. This failure to establish a consistent framework across multiple states increases the cost of entry, which leads to less competitors and ultimately to a less optimal market.

Finally, the Department could provide additional information to both consumers and the industry. For instance, the Department should seek to provide better retail market information, including customer-switching statistics, to the public. The Department should also consider undertaking a study on how competitive natural gas markets have impacted the overall natural gas industry – this study should seek to quantify the overall benefits and costs from restructuring from retail and wholesale competition.

III. CONCLUSION

Direct Energy believes that sound energy policy must include a strong commitment and support for workable retail and wholesale natural gas markets. The Department should encourage natural gas markets by working with all levels of government to ensure that barriers to effective natural gas markets are removed in a timely manner. Advancing market solutions is the best way to provide natural gas at affordable rates now and in the future.

Respectfully submitted,

James Steffes
Direct Energy Services, LLC

Direct Energy
12 Greenway Plaza, Suite 600
Houston, TX 77046
713-877-3818
james.steffes@directenergy.com