BEFORE THE
LOUISIANA PUBLIC SERVICE COMMISSION

COMMENTS OF THE COMMISSION STAFF ON THE 2006 REQUEST FOR PROPOSALS FOR LONG-TERM RESOURCES OF ENTERGY SERVICES, INC.

MARCH 27, 2006

I. Introduction

On January 31, 2006, Entergy Services, Inc. (ESI) issued a draft Request for Proposals (RFP) for long-term resources. This submission was made to facilitate a stakeholder process in compliance with this Commission's Market-Based Mechanism (MBM) General Order (February 2004). That General Order mandates competitive procurement for jurisdictional electric utilities, subject to certain limited exceptions. The present RFP targets approximately 1,000 MW of solid fuel base load capacity (including renewable resources) plus 1,000 MW of load-following combined cycle gas turbine (CCGT) capacity. In addition, after filling those needs, if there are remaining CCGT bids that are sufficiently attractive, Entergy will consider acquiring additional capacity to replace its older inefficient gas/oil capacity not needed for reliability (RMR units).

In conducting this RFP, Entergy retained two independent monitors (IMs). Elizabeth Benson serves as the "process IM" overseeing the overall process, compliance with codes of conduct, adherence to RFP procedures and generally helping to achieve a fair and open procurement. In addition, Entergy has retained Potomac Economics to monitor the evaluation methodology both in terms of the design and application ("evaluation IM"). Both IMs have coordinated closely with the LPSC Staff.

Prior to the filing of the draft RFP on January 31, Entergy consulted extensively with the LPSC Staff and the IMs. On the basis of these informal consultations, Entergy made a number of modifications to its preliminary draft RFP. On February 23, 2006, the LPSC conducted a Technical Conference in Houston, followed by the Entergy Bidders Conference. Both ESI and the Transmission Business Unit (TBU) made presentations, and there was an extensive question and answer (and comment) session. Interested parties, including Staff, have submitted written questions concerning the RFP to Entergy. As of March 24, 2006, over 50 questions (some being multi-part) have been responded to, including 24 Staff questions.

As part of the stakeholder process, interested parties have been invited to submit written comments, and several have done so. In addition, certain comments are implied as part of the questions submitted.

Staff is submitting comments at this time for three main purposes. First, we summarize the comments submitted to Staff by interested parties. (To the extent "comments" are questions, those questions are not summarized here and instead should be responded to by Entergy.) Second, we respond briefly to these comments, indicating our concurrence or disagreement. Third, Staff provides its own comments on the RFP, including our suggestions for changes or clarifications. In some cases, we raise issues for Entergy's consideration (or assertions of Staff "reservations of rights") that do not necessarily require a change to RFP documents.

Staff supports Entergy's proposed process to acquire long-term capacity resources through an RFP, and in particular, the efforts to acquire efficient CCGT load-following capacity and solid fuel base load capacity. These resources are needed on a long-term basis both to meet capacity requirements and to reduce System energy costs. In addition, Staff supports the announced objective in the RFP to acquire additional resources to displace inefficient, existing capacity when doing so provides a net System cost savings.

Responses to several questions posted on the website indicate that ESI is willing to make certain changes to the RFP both to provide greater bidder participation flexibility and for clarification. Staff generally supports these types of changes and other discussed in these comments.

Our comments are based on presently available information, and we reserve our rights to submit additional comments during this process. We recognize that ESI has targeted April 17, 2006 to finalize the RFP documents. We request that ESI make best efforts to incorporate our suggestions and revise other issues by that date, and if necessary, amend the RFP subsequent to that date if further changes or clarifications are warranted.

II. Comments Submitted

Staff has received written comments on the draft RFP from the following parties:

(1) Louisiana Energy Users Group (LEUG);

(2) Plum Point Energy Associates;

(3) Calpine Corporation / New South Energy; and

(4) Williams Power Company.

Each of these parties has submitted comments focused on attributes of the RFP, and we believe the comments in most cases are intended to improve the proposed process. As discussed below, Staff agrees with a number of the points raised, and we disagree (or do not fully agree) with others. However, in all cases Staff appreciates both the interest and efforts of these interested parties in their attempts to improve the process.

A. Louisiana Energy Users Group (LEUG)

(1) Points Raised

The LEUG comments raise two main points. The LEUG complains that the RFP does not go far enough in addressing the retirement/replacement issue, as directed by the Commission. If we are correctly interpreting these comments, LEUG seems to suggest that a separate RFP is needed specifically to address this need. LEUG further argues that this effort should take place now, and not in a future RFP.

LEUG's second issue is the effect of complying with the Clean Air Interstate Rule (CAIR) issued by the U. S. Environmental Protection Agency (EPA) in 2005. LEUG argues that compliance costs should be factored into bid evaluations.

(2) **<u>Response</u>**

Staff agrees with LEUG that this RFP (as well as future RFPs) should address savings from the market achievable from retirements / replacements. Section 1.4 (pages 4-5) of the RFP states that ESI intends to do exactly that. The Commission accepted the Staff retirement report, including its recommendations. Staff recommended that Entergy's next RFP must first meet system capacity and energy requirements and next it should "test the market" to determine whether any remaining bids are sufficiently attractive to displace existing capacity, providing a net cost savings. While Section 1.4 may be somewhat cryptic, our discussions with Entergy indicate that ESI intends to fully comply with this directive. As discussed later, Staff agrees with LEUG that a more complete statement of intentions in the RFP is needed, including a better description of the evaluation methodology and procedures that will be used.

With respect to the CAIR issue, LEUG is correct in principle, but this issue is probably of limited practical importance at the present time. Louisiana does not yet have a defined State Implementation Plan (SIP), and to the best of our knowledge, Entergy does not have a compliance plan.

In our judgment, this is unlikely to be an important bid evaluation factor. For example, the CCGT side of the RFP will be a comparison of alternative bids that have nearly identical (and minimal) amounts of NO_x emissions and virtually no SO_2 emissions. Consequently, comparing CCGT bid "A" with CCGT bid "B" probably does not require a consideration of CAIR compliance (or at best it is a very minor factor). The same is likely to be the case for solid fuel bids, since all such bids are likely to be new projects that must comply with New Source Review (NSR) standards, which typically are more stringent than CAIR. However, it is important that all environmental compliance costs be included with bids, even if CAIR itself is not a central issue.

CAIR may be somewhat more important (though still relatively minor) in connection with retirement/replacement evaluations. We believe that Entergy has no plans to invest in control equipment for units that might be retirement candidates, and therefore those costs will not be avoided by the retirement of a candidate unit. However, Entergy's own gas/oil units will likely be required to participate in the CAIR "cap and trade" program and this should be taken into account in evaluating energy cost savings.

B. Plum Point Energy Associates (Plum Point)

(1) Points Raised

Plum Point argues for several changes to the draft RFP.

a. To maximize savings, ESI should expand the amount of baseload capacity sought in this RFP, rather than deferring acquisitions to future RFPs.

b. Debt imputation should not be used at this time absent a further investigation of the merits of this technique.

c. The fuel forecast used in the RFP should be made public, or in the alternative, validated by the IM.

d. Transmission network upgrade costs should not be included in the evaluation.

e. The due diligence information requirements are burdensome.

(2) <u>Staff Response</u>

Plum Point raises a number of useful points that warrant attention by Entergy. We believe that most of these points have merit, but in at least one case we strongly disagree.

With regard to the total amount of capacity required, Plum Point raises a theoretically valid point. Staff has queried Entergy on this issue, and Entergy has provided a thorough response (See response to LPSC-4.) Plum Point may indeed be correct that in order to minimize costs Entergy should acquire as part of this process much more than 1,000 MW of baseload capacity, but we also understand the practical limitations (technical and financial) of acquiring a large number of resources at one time. Moreover, seeking to acquire too much capacity at one time can have the unintended effect of driving up bid prices. However, in response to Plum Point's argument, we suggest that the RFP be clarified to indicate that 1,000 MW is a rough target, and Entergy may acquire more or less than that depending on the attractiveness of the bids received. If Entergy receives an abundance of bids in excess of 1,000 MW judged to provide significant system savings, then Entergy should allow itself the flexibility to acquire more than 1,000 MW as part of this RFP.

Staff shares some of the concerns expressed by Plum Point and others with regard to imputed debt and its role in bid evaluation. Entergy has made it clear that it does not intend to use imputed debt to screen out initial bids, and will apply this factor in the final evaluations in consultation with the IMs and Staff. Entergy also has committed to show the bid rankings and evaluations with and without debt imputation.

Staff, however, questions whether it is proper to justify a self-build project on the basis of debt imputation due to the extensive risks to ratepayers associated with a self-built resource. Nonetheless, there may be some merit in using debt imputation for comparisons of PPA versus asset purchases. Even in that case, it should be only one factor out of many. Staff has requested that Entergy provide further information on the debt imputation calculation, and Entergy has agreed to do so and post it on the website.

Staff disagrees with Plum Point's argument to disregard transmission upgrade costs that Entergy would incur. (We do agree that Entergy should disregard such costs if the bidder absorbs them.) Entergy has been heavily criticized in the past for not fully accounting for "delivery costs" in its RFP evaluations, and Plum Point's position would be a step backwards. Moreover, Plum Point's position is not consistent with this Commission's position on "participant funding."

Plum Point requests that fuel forecasts should be provided to bidders or validated by the IMs. In fact, the latter will occur, although it is Entergy that prepares the forecast. The fuel forecast itself may not be as critical a factor in bid evaluations as Plum Point believes. This is because baseload and CCGT resources do not compete with each other in the RFP, thus the fuel price forecast does not determine the mix of gas versus solid fuel resources resulting from the RFP.

The final point raised by Plum Point pertains to due diligence requirements. At the outset, Staff notes that the resources acquired under this RFP will involve hundreds of millions of dollars, expected to be chargeable to ratepayers. Staff expects nothing less of Entergy than a full and complete due diligence process for each resource that it acquires. That said, we are sympathetic with Plum Point's concerns. Entergy should show flexibility with regard to the response time period and should work with the counterparty to avoid requests that are redundant or unnecessarily burdensome.

C. Williams Power Company

(1) Points Raised

Williams raises points that go both to commercial practicality as well as to broad planning philosophies. With regard to the former, Williams seeks greater flexibility concerning corporate approvals, noting the difficulties in obtaining such approvals at the front end of a process that may last longer than a year. We note that Entergy has responded to this point by relaxing that requirement. In response to Bid-10, Entergy will allow the bidder to defer a corporate approval to a much later stage in the process. Williams, in general, notes the commercial problems (e.g., market movements) associated with a process that lasts up to a year. Williams argues for a much more rapid contract award as part of this RFP.

Williams' broader argument is that it would be best if the RFP took place after a comprehensive, regional transmission study is completed. Moreover, Williams argues that the RFP should be modified to allow for short to intermediate purchases.

(2) Staff Response

To a large degree, it appears that Entergy's proposed modification to bidder corporate approvals has been addressed and we support that change. However, we also believe that Williams' discussion on the length of the RFP process overstates the problem. The arguments concerning "hedging" and market movements may be valid in the context of shorter-term (e.g., one year) contracts for standard products, but it is much less valid for very long-term transactions sought in this RFP. For the very long-term resources sought in this RFP, it is understandable that the evaluation and selection process will take many months. Moreover, hedging is not needed because any CCGT contract will be indexed to the cost of gas, and hedging is not at issue at all for an asset sale.

Concerning Williams' broader argument, Staff also would like to see an effort at regional transmission planning, and this may be facilitated by the SPP ICT proposal that presently is pending. Despite the potential benefits from regional planning, Staff does not support a delay in the RFP (which might be considerable). Entergy needs the resources that will be acquired in the RFP right now, and delaying the RFP means delaying the savings. Moreover, a regional planning study is not likely to change the fact that Entergy needs to acquire additional CCGT load following and baseload capacity being sought in this RFP.

Finally, we note that Williams' comments include a large number of questions. It appears that a number of these already may have been answered on the RFP website. Entergy should endeavor to answer the others as quickly as possible.

D. Calpine / New South Energy (Calpine)

(1) Points Raised

The Calpine comments raise two very different points. The first comment addresses the existence of reliability must run (RMR) constraints and how they can be mitigated. The suggestion is made that Entergy should identify for bidders the Entergy RMR constraints and the reason for or source of each constraint. Once this is done then the technical solution to each constraint (e.g., transmission upgrade) can be identified and the mitigation savings obtained.

The second point relates to the statement made in the RFP that Qualifying Facilities (QFs) may participate but will receive no specific selection preference. The Calpine comments discuss the asserted legal rights of QFs and argue that they should receive priority. However, the nature of this priority is not defined.

(2) <u>Staff Response</u>

In general, Staff agrees that the RFP should consider the opportunity for RMR mitigation, and Entergy has now addressed this in response to LPSC-24. The purpose of the response is to recognize that in some instances (though probably not most) a bid resource can contribute to RMR mitigation. This response outlines how this benefit will be captured in the evaluations and bid ranking process, possibly with transmission upgrades. This should be incorporated into the final RFP. It also should be mentioned that the process described in the Calpine comments for identifying and costing RMR mitigating upgrades is presently being performed in the TBU's 2006 Transmission Study. It is hoped that these results will be available for at least the second phase of the bid evaluations.

The second issue concerns an alleged QF priority. Staff does not understand Calpine's position, in part because Calpine never explains how this "priority" is to be expressed in the RFP (e.g., tie breaker, preference points, etc.). Moreover, we had understood Calpine's position to be that under PURPA a QF was entitled to a long-term capacity contract <u>outside</u> of the RFP -- not from participating in the RFP. In other words, Calpine in the past has suggested that QFs are exempt from the MBM order for long-term contracting purposes.

Staff believes that the present MBM order does not provide such an exemption, nor does it provide for a "priority" for QFs within an RFP. The LPSC has not ruled otherwise. However, the ultimate determination of this issue will be in the current QF rulemaking docket which is before the LPSC (i.e., Docket No. R-28376). The present schedule calls for a Commission decision in July 2006.

III. Staff Comments

In addition to our reply to the comments submitted in response to the interested parties, Staff has several suggestions pertaining to the RFP. Some of these comments call for modifications to the draft RFP, while others are issues for Entergy to consider for future action.

(1) Solid fuel backstop pricing

Entergy's evaluation method for third-party bids should establish a ceiling price for the solid fuel resource bids. Specifically, Entergy should not accept any bid that would be more costly (i.e., less cost beneficial) than the least-cost, solid fuel unit that Entergy itself could build. There is no reason for Entergy to pay a premium over its own self-build cost. We raise this issue because the self-build proposal covers only a portion of the baseload need in this RFP. While the RFP may have intended just such a check on third-party bids, it is not entirely clear from the RFP.

We see no such need for a CCGT self-build backstop price since such bids are typically well below the full cost of a self-build CCGT.

(2) Expansion of Baseload Acquisition

As discussed in our reply to Plum Point, Entergy should allow flexibility to go beyond the identified 1,000 MW target identified in the draft RFP.

(3) Retirement/Replacement

We discussed this issue in some detail in connection with the LEUG comments. Entergy has communicated to Staff that it intends to follow a process similar to the Staff retirement study, in compliance with the LPSC's directive. The RFP should be modified and expanded to make that clear.

(4) Incorporation of RMR Benefits

It is possible that certain bid resources may be capable of providing RMR mitigation benefits. It is important that the evaluation and bid ranking method used in the RFP take any such potential savings into account, along with potential transmission upgrades that could enhance RMR mitigation. As mentioned in response to Calpine, Entergy's response to LPSC-24 addresses this issue. We recommend that ESI, in conjunction with the IMs, fully develop this procedure. It then should be described in the RFP document.

(5) Due Diligence Process

As discussed in connection with our Plum Point reply, Entergy must conduct a thorough and timely due diligence process. However, we also understand bidder concerns that they need a reasonable response time with two weeks being insufficient, and in certain instances the information list could be redundant or unnecessary. We therefore suggest flexibility on the part of ESI in working with bidders on both information needs and response timelines. However, Entergy must retain and exercise its rights for any information it reasonably needs to conduct a thorough and comprehensive due diligence.

(6) Debt Imputation

Staff's position on debt imputation is discussed in connection with the Plum Point comments. We note that Entergy's draft RFP shows considerable flexibility on this point, including its intention of consultation with the IMs. However, we would prefer that debt imputation not be used as the deciding factor in selecting a self-build project, and it must be applied in a consistent fashion to any affiliate PPA bid.

(7) Peaking Resources

The present RFP does not seek to acquire any quick start peaking resources. We agree with Entergy that load following (CCGT) and baseload should be the highest priority resources and are the proper resources in this RFP. However, Staff asks whether there is a role for quick start peaking for the Entergy System. Entergy responds to LPSC-12 that it has studied this question and does not find sufficient savings to justify acquiring peaking resources. Staff has not seen such studies, and requests that Entergy coordinate further with Staff to determine whether peaking should be solicited in a future RFP.

(8) Price Flexibility for Base Load

The Staff notes a possible area of confusion for the baseload project bids. The RFP appears to require fixed price bids, which can be reduced in the "best and finals" process. However, Appendix E-1 seems to recognize (properly in our view) that the bids for new projects may be estimates subject to change. Since the initial bids are likely to be based on estimates, it is entirely possible that they can increase over time. Indeed, that has been the experience with Cleco's Rodemacher 3 self-build project.

Entergy needs to clarify the uses of estimates in the bidding process and how this affects the "best and finals" procedures. (See Entergy's response to LPSC-14.)

(9) LOI Collateral

Entergy for the first time seeks to impose a $2 million collateral requirement for the execution of a LOI. While Staff questions whether this is a necessary component of the RFP, we defer to market participants on this issue, and no party raised this issue in comments.

In response to LPSC-17, Entergy seems to acknowledge that any forfeited collateral would be treated "above the line" for retail rate making (in some fashion). Staff agrees that forfeited collateral should be given above-the-line treatment (these are not shareholder funds), but we reserve our rights to address the regulatory treatment of such revenues in the appropriate rate proceeding, if and when a forfeiture ever occurs.

(10) EOC Allocations

In addition to the bid rankings and project selections, Staff is also interested in how the resultant resources will be allocated among the System's operating companies (except for Entergy New Orleans). The response to LPSC-18 states that the decisions will be made by the Entergy Operating Committee and that ESI will endeavor to keep Staff informed of progress on this issue.

Staff would like to emphasize the importance of this issue. We would request an opportunity for consultations on the EOC allocations decisions before decisions are made by the Operating Committee. We believe that such consultations are vital to help facilitate prompt regulatory approvals.

(11) Corporate Approvals

As noted in response to Williams, Entergy has indicated a willingness to liberalize its position on corporate approvals. Entergy needs to clarify this change in the final RFP. While we appreciate and support Entergy's added flexibility, Entergy's process should not be used as an opportunity for the gaming of bids. For example, even though the initial bids may not be legally binding, the bidder should not use this as an opportunity to "low ball" the initial (non-binding) bid to obtain short list treatment, only to raise the bid in the "best and finals." Absent a compelling justification or demonstration of changed circumstances, this behavior should not be tolerated. We would ask Entergy and the IMs to be particularly vigilant of such behavior, and the RFP should note this potential concern.

(12) Intermediate RFP

The draft RFP mentions that Entergy intends to conduct a follow-on RFP, and the Company has publicly stated that it will be filed as a draft by September 30, 2006. This commitment generally accords with the agreements reached in the collaborative in December 2005 (Docket No. U-27836, Sub Docket A). There appears to be strong interest in this follow-on RFP as well as in obtaining the savings that intermediate PPAs can provide as soon as possible.

Staff would like to discuss with Entergy the possibility of accelerating the timing of this follow-on RFP. At this point, we would suggest including language that states Entergy tentatively plans to issue the RFP by September 30, 2006 or earlier and intends to discuss the design of this RFP, including scheduling, with affected state regulators. Staff would also like to discuss the possibility of getting input from interested parties on the RFP parameters during the summer of 2006.

(13) Acceleration of Self Build

The proposed self-build repowering project at Little Gypsy has the potential to provide Entergy with substantial fuel savings. Consequently, if in the early stages of the RFP, ESI determines that this project is likely to prevail, Entergy should consider expediting project development rather than waiting for the completion of all phases of the RFP and regulatory approvals. In that case, Entergy might not begin any activities on this project until mid to late 2007. We would encourage ESI to consult with Staff on how the project can be expedited in the event there is an initial determination that it is likely to prevail in the competitive process.

(14) RFP Documentation

Page 37 of the RFP indicates that ESI intends to retain “all proposal information” through the completion of all regulatory approvals. Staff recommends that this be expanded to include all documentation pertaining to bid rankings, evaluations, due diligence and acceptance /rejection decisions.

(15) RFP Bypass

Page 37 of the RFP asserts Entergy's rights to bypass the RFP process and acquire resources outside that process. Staff recognizes the potential for exceptions, and this is explicitly recognized in the MBM General Order. We also recognize that other Entergy retail jurisdictions do not have mandatory competitive procurement rules. However, Staff generally would discourage Entergy from exercising the bypass option for resources to be acquired by EGS or ELL, absent a compelling need for an exemption. Even if Entergy exercises this exemption or bypass right, EGS and ELL capacity resources will require certification under the 1983 General Order.