

**Attachment A to
Settlement Stipulation**

Effective January 1, 2017

**SUMMARY OF POWER COST ADJUSTMENT (PCA) MECHANISM
SETTLEMENT TERMS**

A. OVERVIEW OF PCA

1. The PCA is a mechanism that accounts for differences in PSE's modified actual power costs relative to a power cost baseline. This mechanism provides for a sharing of costs and benefits that are graduated over three levels of power cost variances. The factors influencing the variability of power costs included in the mechanism are primarily weather or market related. PSE will be allowed to file for rate increases to implement limited power supply cost increases, discussed later.
2. **Sharing Bands:**
 - a. **Dead Band:** \$17 million (+/-) annually, 100% of costs and benefits to Company.
 - b. **First Sharing Band:** \$17-\$40 million (+/-) annually,
 - i. Costs (under-recovered) will be shared 50% to Company; 50% to Customers.
 - ii. Benefits (over-recovered) will be shared 35% to the Company; 65% to Customers
 - c. **Second Sharing Band:** Over \$40 million (+/-) annually, 10% of costs and benefits to Company; 90% of costs and benefits to Customers.
 - d. **Deferral and Interest:** The customer's share of the power cost variability will be deferred as described below, and the balance will accrue monthly interest at the interest rate calculated in accordance with WAC 480-90-233(4). Amounts will be deferred consistent with recovery under the provisions of Accounting Standards Codification 980.

3. **Timing of surcharges or credits:**

- a. The sharing amounts will be accounted for on an annual basis, with a PCA period of January 1 through December 31 for each year¹. The surcharging of deferrals can be triggered by the Company when the balance of the deferral account is approximately \$20 million. The Company shall make a filing to refund deferrals when the balance in the deferral account is a credit of \$20 million or more.
- b. To address financial needs and to provide Customers a price signal to reduce energy consumption, a surcharge can be triggered when the Company determines that, for any upcoming 12 month period, the projected increase in the deferral balance for increased power costs will exceed \$20 million. The surcharge will be implemented through a special filing subject to Commission approval detailing the events giving rise to the projected cost variance.
- c. In April of each year, the Company shall file an annual report detailing the power costs included in the deferral calculation, in a form satisfactory to the Commission, for Commission review and approval by September 30 of that year. The Commission shall have an opportunity to review the prudence of the power costs included in the deferred calculation, and costs determined to be imprudent can be disallowed at that time. Staff and other interested parties will have the opportunity to participate in the prudence review process. The Company will also provide the Commission with a quarterly report of the deferral calculation in a form satisfactory to the Commission.
- d. Unless otherwise determined by the Commission, surcharges or credits will be collected or refunded, as the case may be, over a one year period. If for any reason the PCA shall cease to exist, any balances in the deferred accounts not previously reviewed will be reviewed and set for refund or surcharge to customers at that time.

B. ELEMENTS OF PCA

4. **Power Cost Baseline Rate:** In order to focus on the component of the Company's rates to be included in a PCA, it is necessary to distinguish between power costs and all other costs in rates. Total PSE costs will be divided, or separately identified, into three categories: 1) Variable Production Costs (tracked through the PCA imbalance calculation), 2) Fixed Production Costs (that will be included in PSE's electric decoupling mechanism if the mechanism continues), and 3) Delivery Costs (currently included in PSE's decoupling plan). The Power Cost Baseline Rate is the combination

¹ PCA moved to calendar year per docket UE-050870

of Variable Production Costs and Fixed Production Costs. The following table indicates the portion of the Company's rate to be adjusted by the PCA mechanism and in the periodic "Power Cost Only Rate Case" review:

TOTAL REVENUE REQUIREMENT		
Power Cost Baseline Rate (see Exhibit A)		
Variable Production Costs²	Fixed Production Costs	Delivery Costs
<ul style="list-style-type: none"> •Fuel, FERC accounts 547 and 501; •Purchase & Interchange, FERC account 555; •Purchases/Sales of Non-Core Gas, FERC Account 456.0; •Hedging Gains or Losses on Fuel and Power Purchases and Sales and related Brokerage Fees; •Sales to Others, FERC Account 447; •Wheeling costs, FERC Account 565; •Amortization of Production regulatory assets or liabilities amortized to Accts.: 501, 547, 555 and 565. Inclusion of any other variable regulatory assets or liabilities will be decided in a future GRC or PCORC; •Acct. 408.1—Montana Electric Energy Taxes; •Commission Approved Equity Adder associated with Coal Transition PPA. 	<ul style="list-style-type: none"> •Return on Fixed Production Plant and specific Transmission³ Assets, at the current authorized net of tax rate of return; •Return on Production-related Regulatory Assets and Liabilities at the current authorized net of tax rate of return; •Depreciation expense for Production Plant and specific Transmission³ Assets; •Hydro and other Production Plant O&M (including Payroll OH/taxes); •Other Power Supply Expenses, FERC 557 (including Payroll OH/taxes); •Property Insurance associated with Production Plant; •Amortization of Regulatory Assets and Liabilities (Except amounts amortized to Accts.: 501, 547, 555 and 565); •Specific Transmission³ expense and revenues: <ol style="list-style-type: none"> 1. Transmission Expense—500 kV; 2. Acct. 456.1 - Transmission Revenue. 	<ul style="list-style-type: none"> •Transmission (other than what has been included in PCA Fixed Production Costs component) Distribution; •All other operating accounts not included in the Power Cost Baseline Rate Variable Production Costs or Fixed Production Costs; •Line of Credit costs associated with Hedging program (included as a cost of capital item in next GRC).

² Modifying the above table due to changes in account numbering by FERC or the addition of new production resources will not be subject to the 5-year moratorium. Inclusion of any other accounts will be decided in a General Rate Case, PCORC, or PCA compliance filing.

³ Specific Transmission refers to: Colstrip 1&2 line, Colstrip 3&4 line, Third AC, & Northern Intertie.

5. **New Resources:** New resources will be included in the allowable PCA costs. The prudence of new resources with a term less than or equal to two years will be determined in the Commission's review of the annual PCA report. The prudence of new resources with a term greater than two years may be reviewed in a Power Cost Only Rate Case or general rate proceeding.

6. **Power Cost Only Rate Case (PCORC)**

In addition to the yearly adjustment for power cost variances in Variable Production Costs, PSE may file a periodic proceeding that would true up *all power costs* identified in the Power Cost Baseline Rate, as well as allow new resources into the Power Cost Baseline Rate. In either case, the Company would submit a PCORC filing proposing such changes. This filing shall include testimony and exhibits that include the following:

- a. Current or updated integrated resource plan
- b. Description of the need for additional resources (as applicable)
- c. Evaluation of alternatives under various scenarios (as applicable)
- d. Adjustments to the Fixed Production Cost Component
- e. Adjustments to the Variable Production Cost Component
- f. A calculation of proforma production cost schedules that are consistent with this docket, including power supply and other adjustments impacting then current production costs.

7. If the Company shall file for a PCORC, and such filing shall result in an increase to general rates then in effect, the Company shall, within three (3) months of the effective date of any rate increase resulting from such PCORC, file a general rate case. Not more than one general rate case filing in any 12 month period shall be required to comply with this requirement. Except for requests for interim rate relief, PSE is prohibited from overlapping PCORC and general rate case filings. Additionally, PSE is limited to filing one power cost update per PCORC, with an additional update allowed as part of the compliance filing if the Commission determines the update is necessary due to increased gas costs and orders that such update be made as part of the compliance filing⁴.

⁴ See Docket UE-072300 (Order 13).

8. One objective of a new resource proceeding is to have the new Power Cost Baseline Rate in effect by the time the new resource would go into service. Upon receipt of a filing, hearings would be scheduled to review the appropriateness of adjusting the Power Cost Baseline Rate. These hearings would consider only power supply costs included within the Power Cost Baseline Rate. It is contemplated that this review would be completed within five months.⁵ Data request response time during the review period will be five days.⁶ Within 30 days following the five month review, the Commission would issue an order determining the appropriateness of all power costs included in the Power Cost Baseline Rate and the prudence of any new resource (with a term greater than two years) acquisition.

C. PCA MECHANISM (PROCEDURES)

9. Exhibit A-1 details an example of PSE's presentation of the power costs, on a test year level (as defined in the revenue requirement settlement in Docket No. UE-141141) identified in the Total Revenue Requirement Table. The purpose of this exhibit is to calculate the Power Cost Baseline Rate which is defined as the sum of both the Variable Production Costs and Fixed Production Costs, divided by the test year delivered load (MWh).
10. Exhibit B, which is based on the Company's presentation of test year costs, is an explanation and example of the calculation used to determine the amount of power cost that will be subject to the sharing mechanism. This exhibit calculates the amount subject to sharing by subtracting the Baseline Variable Production Costs from the allowed total Variable Production Costs for the PCA period. Baseline Variable Production Costs are defined as the Variable Production Cost component of the Power Cost Baseline Rate multiplied by the actual delivered load in the PCA period.
11. **Adjustments of Costs Outside of the PCA Period:** Power cost adjustments or true-ups for prior periods that fall within the PCA period are included as recoverable power costs through the Variable Production Costs component.
 - a. Adjustments for Previous PCA Periods:
 - i. Adjustments for previous PCA period(s) that are equal to or less than \$1 million (debit or credit) will flow through the current months PCA calculation.
 - ii. Adjustments or true-ups greater than \$1 million (debit or credit) that relate to prior PCA period(s) will flow through a recalculation of the previous PCA period(s) for regulatory purposes. Any changes to the customer deferrals from

⁵ See Docket UE-072300 (Order 13).

⁶ See Docket UE-072300 (Order 13).

the prior PCA period(s) will be indicated in a reconciliation schedule for deferrals by PCA period(s).

b. Exceptions to Adjustments for Previous Periods:

- i. *Company Accounting Errors:* If an error has been made in regard to accounting for power cost transactions, except for Colstrip fuel costs and to the extent that the Company should have known at the time of the transaction, the Company will reflect the appropriate adjustment to the PCA period(s) and adjust the deferral for the PCA period(s) accordingly.
- ii. *Mid-Columbia Power Costs:* Since it is difficult to determine the months impacted by any annual true-ups under PSE's Mid-Columbia contracts, any annual true-ups for PSE's costs under its Mid-Columbia contracts will be considered a Variable Production Cost and included in the same PCA period(s) for which they are booked to power costs.
- iii. *Colstrip Fuel Costs:* Any adjustments, true-ups, or corrections made for Colstrip inventory valuation for prior period will be considered a Variable Production Cost and included in the same PCA period(s) for which they are booked to power costs.

c. Adjustments for Costs Recorded after Termination of PCA Mechanism: Power cost adjustments posted in the month following the termination of the PCA Mechanism relating to the PCA period(s) will be included in power costs for the month of the final PCA calculation and the deferral will be adjusted subject to the exceptions in item B.

12. Unless otherwise ordered by the Commission, changes in rates attributable to PCA adjustments shall be charged on a cents/kWh basis, and changes in rates attributable to adjustments to the power costs as a result of a PCORC shall be charged based upon the Company's most recent approved Cost-of-Service methodology as agreed to in Docket UE-141368 or as subsequently modified pursuant to that agreement. No party is deemed to have approved or accepted these methodologies for any other purpose or precedent. Wholesale customers will be allocated power costs and power revenues at the end of a PCA year in the same relationship as done in the rate allocation from the Company's most recent approved Cost-of-Service methodology proceeding as agreed to in Docket UE-141368 or subsequently modified pursuant to that agreement.

D. DECOUPLING

13. Parties are not bound to any position with respect to the continuation of decoupling or the treatment of fixed production costs within the decoupling mechanism in PSE's next general rate case. However, if the electric decoupling mechanism continues for PSE after the review of decoupling in PSE's next general rate case, the electric

decoupling mechanism will include the Fixed Production Costs as defined in Section B above that were formerly tracked in the PCA imbalance calculation. Nothing in this agreement binds any party to any position with regard to treatment of costs in an automatic escalation factor mechanism (such as a K-factor) or in a multiyear rate plan.

E. TEMPORARY PROVISIONS

14. The parties agree to a five-year moratorium for changes to the PCA mechanism, from the implementation date of this agreement, January 1, 2017.
15. PSE's ability to file a PCORC will not change, including the continued use of the PCORC to update Fixed Production Costs referenced in Section C above. However, for the five year moratorium, PSE will agree to a limited stay-out period after the filing of any PCORC during that five-year period. Specifically, PSE agrees to not file a general rate case or a PCORC within six months of the date new rates go into effect for any PCORC filing. Additionally, the requirement to file a general rate case within 3 months of the completion of a PCORC, as outlined in Section 7 is suspended during this five-year moratorium.