

Exhibit ___ (KLE-10)
Docket U-072375
Witness: Kenneth L. Elgin

BEFORE THE WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION

In the Matter of the Joint Application of

DOCKET U-072375

**PUGET HOLDINGS LLC AND PUGET
SOUND ENERGY, INC.,**

**For an Order Authorizing Proposed
Transaction**

EXHIBIT TO TESTIMONY OF

Kenneth L. Elgin

**STAFF OF
WASHINGTON UTILITIES AND
TRANSPORTATION COMMISSION**

*Standard & Poors Ratings Direct
Summary: Puget Sound Energy
September 17, 2008*

June 18, 2008

September 17, 2007

Summary:

Puget Sound Energy Inc.

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Summary:

Puget Sound Energy Inc.

Credit Rating: BBB-/Stable/A-3

Rationale

The 'BBB-' corporate credit rating on Puget Energy Inc. (Puget) and Puget Sound Energy Inc. (PSE) reflect the strong business profile of PSE, a regulated, vertically integrated electric and gas utility, and the consolidated financial risk profile of Puget.

As of Jun. 30, 2007, Bellevue, Wash.-based Puget had about \$2.7 billion in total debt, including \$250 million in hybrid securities.

PSE's strong business risk profile ('4' on a 10-point scale, with '1' being 'excellent') reflects its combined electric and gas utility business, which is subject to regulation by the Washington Utilities and Transportation Commission (WUTC).

Ratemaking by the WUTC is a key driver of credit quality, especially in light of PSE's high capital needs and commodity price exposure. On Jan. 5, 2007, the WUTC published its final rate order on the company's 2006 general rate case, granting PSE a 10.4% ROE on a hypothetical 44% equity layer as well as permission to recover costs for recent plant additions and for short-term financing needs related to power supply hedging. The commission did not approve the company's requests for a gas "decoupling" mechanism, a depreciation tracker, and a modification to its power cost adjustment (PCA) mechanism.

PSE's service territory in western Washington is large and diverse, with low industrial and commercial customer concentration. Competition is limited, given the absence of mandatory retail choice for electricity users and residential gas users, which make up most of PSE's retail base. Electric and gas rates are competitive for the region.

The company's primary operational challenge is the management of market and fuel price risk, which is considerably higher for electric utility operations than gas operations due to the gas system's strong fuel cost passthrough mechanism. The PCA mechanism requires the company to bear the risk and rewards of the first \$20 million of power cost variance in any given year and then divides the next \$20 million between company and ratepayers, which assume 90% or more of any additional variance thereafter. Electric utility operations are exposed to market prices and hydrology risk as a result of its dependence on market purchases and a primarily hydro, gas and wind-based generating fleet.

Capital requirements are very high, with capital expenditures of about \$2.1 billion at PSE budgeted for 2007 and 2009 due to system upgrade needs, customer growth, and further resource additions. PSE expects to pursue up to seven projects, together totaling 1,100 MW or about 25% of peak load requirements, as part of its ongoing resource acquisition goal of procuring an average 1,500 MW of additional energy supply. On Feb. 21, 2007, PSE finalized its \$120 million purchase of the 277 MW combined-cycle Goldendale Energy Center. The company is also participating in the \$44 million expansion of the Jackson Prairie Storage Project, owned jointly with Northwest Natural Gas Corp. and Avista Corp., to 1,150 million cubic feet per day (mmcf/day) maximum firm deliverability by 2008 from 850 mmcf/day at present.

Financial measures are adequate for the rating, although cash flow coverage metrics are somewhat weak. Excluding the effects of a one-time \$89 million payment to low-cost supplier Chelan County Public Utility District, adjusted funds from operations (FFO) to interest coverage was approximately 3.3x while FFO to average total debt was at about 15.9% for the 12 months ended Jun. 30, 2007. Including debt adjustments for operating leases, purchased power, and hybrid securities, adjusted debt leverage was approximately 60.9%, as of Jun. 30, 2007 following the issuance of a \$250 million subordinated note in the 2nd quarter 2007. Puget expects to internally fund about 50% of capital expenditures.

Short-term credit factors

PSE's short-term rating is 'A-3'. Overall liquidity at PSE was adequate, with approximately \$252 million in undrawn capacity as of Jun. 30, 2007 under its \$500 million committed unsecured bank credit agreement at PSE that expires April 15, 2012. In March 2007, the company entered into a \$350 million credit agreement with a group of 5 banks to support hedging activities. The facility was fully available as of Jun. 30, 2007. Secondary liquidity resources at PSE include a \$200 million receivables securitization facility and a \$30 million revolving credit facility with Puget Energy in form of a promissory note. As of Jun. 30, 2007, \$150 million and \$5.5 million were respectively available under these facilities.

Parent Puget Energy no longer maintains a separate credit facility at the parent level, having paid down and closed its \$5 million committed credit agreement in September 2005.

Liquidity requirements will remain high at PSE in 2007 and 2008 due to about \$ 1.3 billion in planned capital spending and potential collateral requirements related to the company's electric and gas supply arrangements. Debt maturities are manageable, with about \$179 million due in 2008 and \$158 million due in 2009.

Outlook

The stable outlook reflects our expectation of reasonable rate relief for PSE, consistent with the WUTC's latest general rate case decision, and a favorable revision to PSE's power cost adjustment mechanism. Credit stability will also depend not only on the approval of resource additions and sufficiency of rate relief, but also on maintaining a sufficient amount of equity to support capital investment needs and PSE's authorized 44% equity ratio.

Consideration of a positive rating outlook will depend on more favorable rate relief in future years, consistently strong cash flow coverage metrics, and Puget's ability to improve its equity capitalization. An improved mechanism for commodity cost recovery could also provide support for a positive outlook.

Alternatively, if weak cash flow metrics persist and are deemed likely to continue in the absence of adequate rate relief, a negative outlook would likely result. Factors that could lead to a negative outlook include additional commodity cost disallowances, the excessive accumulation of power cost deferrals, inadequate regulatory treatment of capital additions, a disproportionate reliance on debt financing to meet its capital needs, or significant power cost deficits beginning in 2007.