

**EXHIBIT NO. ___(DEG-7)
DOCKET NO. UE-09___/UG-09___
2009 PSE GENERAL RATE CASE
WITNESS: DONALD E. GAINES**

**BEFORE THE
WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION**

**WASHINGTON UTILITIES AND
TRANSPORTATION COMMISSION,**

Complainant,

v.

PUGET SOUND ENERGY, INC.,

Respondent.

**Docket No. UE-09___
Docket No. UG-09___**

**SIXTH EXHIBIT (NONCONFIDENTIAL) TO THE
PREFILED DIRECT TESTIMONY OF
DONALD E. GAINES
ON BEHALF OF PUGET SOUND ENERGY, INC.**

MAY 8, 2009



Credit Opinion: Puget Sound Energy, Inc.

Puget Sound Energy, Inc.

Bellevue, Washington, United States

Ratings

Category	Moody's Rating
Outlook	Stable
Issuer Rating	Baa3
First Mortgage Bonds	Baa2
Senior Secured	Baa2
Sr Unsec Bank Credit Facility	Baa3
Senior Unsecured Shelf	(P)Baa3
Jr Subordinate	Ba1
Preferred Stock	Ba2
Commercial Paper	P-3
Parent: Puget Energy, Inc.	
Outlook	Stable
Issuer Rating	Ba2
Washington Natural Gas Company	
Outlook	Stable
Bkd First Mortgage Bonds	Baa2
Puget Sound Energy Capital Trust III	
Outlook	Stable
Bkd Preferred Shelf	(P)Ba1

Contacts

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Key Indicators

[1]

Puget Sound Energy, Inc.

	LTM 3Q 08	2007	2006	2005
(CFO Pre-W/C + Interest) / Interest Expense	4.2	3.5	3.4	3.0
(CFO Pre-W/C) / Debt	21%	18%	15%	14%
(CFO Pre-W/C - Dividends) / Debt	16%	14%	11%	10%
(CFO Pre-W/C - Dividends) / Capex	89%	60%	50%	49%
Debt / Book Capitalization	49%	48%	54%	50%
EBITA Margin %	14%	15%	15%	16%

[1] All ratios calculated in accordance with the Global Regulated Electric Utilities Rating Methodology using Moody's standard adjustments

Note: For definitions of Moody's most common ratio terms please see the accompanying [User's Guide](#).

Opinion

Rating Drivers

Strict focus on regulated electric and gas utility operations

Collaborative regulatory relationships and credit supportive regulatory practices

Negative free cash flow that creates external financing needs

Ring fence like mechanisms provide insulation from debt and financial risk at the parent

Corporate Profile

Puget Sound Energy, Inc. (PSE), a subsidiary of Puget Energy, Inc. (Puget), is an electric and natural gas utility serving 1.1 million electric and 720,000 natural gas customers, primarily in the Puget Sound region. PSE is regulated by the Washington Utilities and Transportation Commission (WUTC) and the Federal Energy Regulatory Commission.

Recent Developments

The impending completion of the purchase of 100% of the common stock of Puget Energy, Inc. by a consortium of infrastructure private equity investors led by Macquarie Infrastructure Partners follows receipt in January 2009 of the final required regulatory approval for the transaction from the WUTC. Financing for the transaction includes a significant \$3.4 billion equity component from the consortium, which we note has a reputation as a long-term investor. The transaction has an enterprise value of over \$7 billion, including about \$2.7 billion of PSE debt to be assumed. Closing of the transaction is expected by February 6, 2009.

SUMMARY RATING RATIONALE

PSE's Baa3 senior unsecured rating reflects its relatively low risk utility operations, collaborative regulatory relationships and credit supportive rate case outcomes, efficient handling of growing electric and gas supply needs, solid credit metrics, and access to its own committed bank credit facilities plus indirect access to a committed capital expenditure facility at the parent level to supplement internal cash flow. PSE's ratings also take into account the impending ownership change, which constrains its rating. Prospectively, PSE should be strongly positioned at Baa3, assuming continuation of credit supportive regulatory decisions in the likely annual rate case proceedings that we expect given a large multi-year capital program. Access to a mix of debt and private equity should help maintain key credit metrics at levels that might suggest a notch higher rating; however, the parent will shortly introduce a significant layer of debt above PSE and rely on the utility to service those obligations. Notwithstanding the ring fencing like mechanisms that are intended to protect PSE from undue cash demands by the parent, we believe the Baa3 rating captures the increase in financial risk at the holding company.

DETAILED RATING CONSIDERATIONS

CONSERVATIVE BACK-TO-BASICS STRATEGY

PSE accounts for all the earnings, assets and cash flow of Puget following the 2006 sale of InfrastruX, a non-regulated utility construction service company. PSE's long-term electric supply strategy focuses on increasing energy efficiency, while also adding renewable and natural gas supply sources. Specifically, PSE added over 1,600 megawatts of wind, natural gas, and solar resources during the past three years to address expected population growth and to replace some large purchased power contracts that will expire in the future. These additions also make PSE less hydro dependent, which can prove beneficial given past supply cost issues due to persistent drought conditions. They also avoid the potential pressures that loom in the medium term for predominantly coal-based utilities (which PSE is not) due to uncertainties surrounding the form and substance of future environmental legislation, the timing for implementation, and the amount of related costs to comply. PSE expects to update its integrated resource plan in 2009 to guide its future resource strategy. The initial outlay for the acquisition and construction of new generation facilities will likely be considerable; however, if PSE continues to receive supportive regulatory treatment of such investments, that scenario will result in a larger regulated rate base on which it can generate higher earnings and more robust cash flows.

COLLABORATIVE REGULATORY RELATIONSHIPS AND CREDIT SUPPORTIVE REGULATORY PRACTICES

Among the most significant risks that PSE faces are hydro-electric generation variability and the wholesale market prices of natural gas and power. PSE benefits from the increasingly collaborative regulatory environment in Washington that has been allowing more reasonable rate increases and providing risk-mitigating cost-recovery mechanisms (i.e., the power cost adjustment and purchased gas adjustment mechanisms) in some of the WUTC's more recent regulatory orders for PSE. Frequently, the decisions in PSE's power cost only rate cases (PCORC) have been in the form of settlements rather than litigated decisions. A PCORC allows PSE to revise electric rates after an expedited 5-month review of the company's power costs and new resources, instead of filing a traditional general rate case, which entails a comprehensive 11-month review of all utility costs. PSE's frequent use of the PCORC process has helped minimize regulatory lag.

SIGNIFICANT CAPITAL EXPENDITURES PLANNED OVER THE NEXT SEVERAL YEARS TO BE MET WITH CASH PLUS EXTERNAL FINANCING

PSE expects to spend about \$5 billion over the next five years to support supply and delivery infrastructure needs. Although the future amounts remain subject to review and may change based on economic, regulatory, and other factors, we still expect the trend of higher than historical average capital expenditures to continue. Accordingly, we expect frequent rate cases for PSE to minimize the effects of regulatory lag given the use of historical test years under Washington's regulatory practice. The anticipated financing for the capex program is likely to be met from a combination of internal cash flow, utility debt, and common equity infused from the new owners, while targeting a capital structure that includes common equity equal to the level that regulators use in setting rates. PSE has committed to keep a minimum common equity of 44% as calculated by the state regulators, unless the WUTC establishes some lower level as the basis for setting rates.

SOLID FINANCIAL PERFORMANCE SHOULD HELP SUSTAIN KEY FINANCIAL METRICS

Key financial metrics such as CFO Pre-W/C to interest and debt, along with adjusted debt to total capitalization have benefited from regulatory support for PSE's investments and the parent's willingness and ability to issue significant amounts of common equity. Regulatory support was apparent from the October 2008 approval by the WUTC to increase electric and gas rates by \$130.2 million (7.1%) and \$49.2 million (4.6%), respectively, using a 46% common equity ratio and an allowed return on equity of 10.15%. The latest equity infusion came in late 2007 when the Macquarie led consortium privately placed \$300 million of common equity. PSE also issued \$250 million of hybrid debt in June 2007, which we treat as 50/50 debt/equity when calculating PSE's metrics.

For the 12-months ended September 30, 2008, PSE's CFO Pre-W/C to interest and debt were 4.2x and 20.9%, respectively, reflecting improvement over the 3.5x and 17.6%, respectively, for the year ended December 31, 2007. The flexibility in PSE's balance sheet fares well versus its similarly rated peers, with adjusted debt to capitalization (i.e., including Moody's standard adjustments and deferred income taxes as part of capitalization) at 49.4% as of September 30, 2008. We expect further improvement in the balance sheet metrics as PSE debt is reduced upon completion of the change in ownership; however, PSE debt is likely to creep modestly upward in ensuing years in line with funding of the capex program. Importantly, we assume that the WUTC continues to grant supportive treatment for planned utility investments, which should help sustain the recently stronger metrics. Moreover, PSE should have ample flexibility to comply with key financial covenants in its bank revolvers and regulatory mandates that govern its dividend distributions to the parent. The regulatory protections have become an increasingly important aspect of the analysis of PSE as debt is being introduced above the operating company for the first time. Key among the ring fence like mechanisms established as a requisite of the WUTC approvals for the change in ownership are: a required "golden share" vote to address concern about potential substantive consolidation of PSE in any parent bankruptcy and any voluntary filing by PSE; minimum required levels of PSE common equity to be maintained and limits on PSE and parent distributions under certain circumstances.

Liquidity

To supplement internal cash flow upon consummation of the change in ownership, PSE will terminate all of its prior liquidity arrangements and then rely on three five-year committed credit facilities aggregating \$1.150 billion (i.e. \$400 million to backstop PSE's commercial paper program, \$350 million to support its energy hedging program, and \$400 million to provide another source of funding for utility capex). The facilities in aggregate would represent about a \$100 million increment over the aggregate of prior arrangements. As a conservative measure given the currently tight credit markets, PSE has been maintaining higher than normal unrestricted cash, including about \$158 million at September 30, 2008. Moreover, Puget Energy's \$1.0 billion committed capex facility is available to support the planned utility investments as well.

PSE also has a demand promissory note with its parent, under which it may borrow up to \$30 million. At September 30, 2008, the outstanding balance was \$24.7 million and PSE's current portion of long-term debt was \$150 million.

Although PSE's liquidity should remain sufficient to meet its short-term working capital needs and about \$150 million of long-term debt maturing in the next four quarters, liquidity could be stretched depending on access to utility debt and common equity infusion from the new owners sourced through draws under Puget Energy's capital expenditure facility to fund anticipated negative free cash flow due to the large capex program. Looking ahead, PSE also has scheduled LTD maturities of about \$230 million in 2010.

The quality of the alternate liquidity provided by PSE's new bank facilities benefits from not having any ongoing material adverse change clause or any onerous financial covenant requirements (i.e. fairly low cash flow coverage tests as defined, which replace the former maximum allowed debt covenant in the prior facilities). We expect that PSE should maintain adequate headroom against the covenants given expected financial performance and there are no rating triggers in the bank facilities that might cause acceleration or puts of obligations; however, they do contain rating sensitive pricing.

Rating Outlook

PSE's stable rating outlook reflects our view that the utility can sustain its recent financial performance under the impending new ownership, which is increasingly important given the introduction of a significant amount of structurally subordinated debt at the parent. Our expectations assume that PSE maintains conservative financing strategies and receives supportive decisions from the WUTC in future rate cases.

What Could Change the Rating - Up

PSE could be an upgrade candidate in the medium term if it achieves stronger than anticipated financial results, while coping with the challenges of executing a large capital program and helping service the parent's standalone debt. In particular, producing CFO Pre-W/C to interest and debt closer to the mid-4x and 23%, respectively, on a sustainable basis could overcome the existing constraints in the rating and provide impetus for positive rating action.

What Could Change the Rating - Down

Adding more debt above PSE than currently expected that creates undue pressure for higher dividends could lead to a downgrade, especially if there are any unexpected changes that weaken the ring-fencing like measures established by the WUTC. Moreover, shortfalls in PSE's performance that reduce CFO Pre-W/C to interest and debt below 4.0x and the mid teens, respectively, for an extended period of time, could lead to a downgrade.

Rating Factors

Puget Sound Energy, Inc.

Select Key Ratios for Global Regulated Electric Utilities

Rating	Aa	Aa	A	A	Baa	Baa	Ba	Ba
Level of Business Risk	Medium	Low	Medium	Low	Medium	Low	Medium	Low
CFO pre-W/C to Interest (x) [1]	>6	>5	3.5-6.0	3.0-5.7	2.7-5.0	2-4.0	<2.5	<2
CFO pre-W/C to Debt (%) [1]	>30	>22	22-30	12-22	13-25	5-13	<13	<5
CFO pre-W/C - Dividends to Debt (%) [1]	>25	>20	13-25	9-20	8-20	3-10	<10	<3
Total Debt to Book Capitalization (%)	<40	<50	40-60	50-75	50-70	60-75	>60	>70

[1] CFO pre-W/C, which is also referred to as FFO in the Global Regulated Electric Utilities Rating Methodology, is equal to net cash flow from operations less net changes in working capital items

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