

**EXHIBIT NO. ___(EMM-11)
DOCKET NO. UE-07___/UG-07___
2007 PSE GENERAL RATE CASE
WITNESS: ERIC M. MARKELL**

**BEFORE THE
WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION**

**WASHINGTON UTILITIES AND
TRANSPORTATION COMMISSION,**

Complainant,

v.

PUGET SOUND ENERGY, INC.,

Respondent.

**Docket No. UE-07___
Docket No. UG-07___**

**TENTH EXHIBIT (NONCONFIDENTIAL) TO THE
PREFILED DIRECT TESTIMONY OF
ERIC M. MARKELL
ON BEHALF OF PUGET SOUND ENERGY, INC.**

DECEMBER 3, 2007

Puget Energy

Rate Case Decision Essentially in Line with Expectations; Adjusting Estimates

The WUTC awarded PSE electric and gas rate increases essentially in line with our expectations. We view the WUTC ruling favorably given PSE's history of somewhat challenging regulatory outcomes.

- **Rate increases and capital structure seem reasonable.** The WUTC issued a final order in the PSE rate cases, granting a \$17.2 million electric base rate increase and a \$31.3 million gas base rate increase. PSE was awarded a 10.4% ROE and a 44% equity component. New rates will be effective mid January, once power costs have been updated.
- **Could see reduction to baseline power costs.** The WUTC instructed PSE to update its baseline power costs, and we believe it is possible that the new power costs estimates could result in a *net reduction* to rates given declining natural gas prices.
- **Depreciation lag assessment more constructive than expected.** The WUTC's assessment of depreciation lag, including its consideration of remedies like out-of-period adjustments, was much more constructive than we anticipated.
- **Updating estimates.** We are increasing our 2006E EPS to \$1.45, reducing our 2007E EPS to \$1.60 and introducing a 2008E EPS of \$1.75.
- **Discount valuation warranted.** PSD shares trade at 15.4x our 2007E EPS, a discount to the utility group multiple of 16.3x. We believe the discount is warranted given Puget's challenging regulatory environment but would expect PSD's dividend yield to support the shares.

Puget Energy (PSD;PSD US)

	2005A	2006E (Old)	2006E (New)	2007E (Old)	2007E (New)
EPS (\$)					
Q1 (Mar)	0.70	0.63A	0.63A		
Q2 (Jun)	0.15	0.26A	0.26A		
Q3 (Sep)	0.06	0.14A	0.14A		
Q4 (Dec)	0.52		0.40		
FY	1.42	1.40	1.45	1.65	1.60
P/E FY	17.3	17.6	17.0	14.9	15.4

Source: Company data, Reuters, JPMorgan estimates. Note: Official estimates are rounded to the nearest \$0.05 per share.

Neutral

\$24.62

05 January 2007

Electric Utilities

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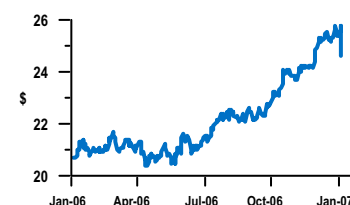
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Price Performance



	YTD	-1M	-3M	-12M
Absolute	-2.9%	-2.6%	5.9%	19.2%

Source: RIMES, Reuters.

Company Data

Price (\$)	24.62
Date Of Price	05 Jan 07
52-week Range (\$)	25.91 - 20.28
Mkt Cap (\$ mn)	2,853.24
Fiscal Year End	Dec
Shares O/S (mn)	116
Div. Yield	

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See page 5 for analyst certification and important disclosures, including investment banking relationships.

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Rate Case Outcome Reasonable; Base Rates and Capital Structure in Line

On Friday afternoon, the Washington Utilities and Transportation Commission (WUTC) issued a final order in the Puget Sound Energy (PSE) electric (Docket # UE-060266) and gas (Docket # UG-060267) rate cases filed in February 2006. Electric base rates were increased \$17.2 million and gas base rates were increased \$31.3 million, essentially in line with our expectations. The utility was awarded a 10.4% return on equity and a 44% equity component. New rates will be effective mid-January, once power costs have been updated. We view the WUTC ruling favorably given PSE's history of somewhat challenging regulatory outcomes. Although proposed rate structures like the depreciation tracker and natural gas decoupling were denied, PSE was awarded a return on equity and capital structure comparable to our projections. Also, we were encouraged by the Commission's tone regarding several issues likely to be re-evaluated in future proceedings, most notably "out-of-period adjustments" to depreciation expense/rate base investment – a potential vehicle to mitigate depreciation lag.

Table 1: Puget Sound Energy Rate Case Outcome versus Request/Projections

\$ in millions

	WUTC Order	PSE Request*	JPM Estimate**
Electric Revenue Requirement	17.2	33.5	25.0
Gas Revenue Requirement	31.3	38.9	30.0
Return on Equity	10.40%	11.25%	10.50%
Equity Component	44.00%	45.00%	44.00%

Source: WUTC, company reports and JPMorgan estimates.

*PSE request excludes power costs and reflects adjustments agreed to by PSE and intervenors.

**JPM estimate excludes power costs.

Still Some Rate Uncertainty; Could See Reduction to Baseline Power Costs

As part of the final order, the WUTC instructed PSE to update the inputs to its baseline power cost projection model, AURORA. Specifically, the utility is required to rerun AURORA using gas prices based on forward prices for the three months ended November 30, 2006. We expect PSE to file an updated baseline power cost tariff with the WUTC within the week. We believe it is possible that the new baseline power cost could result in a *net reduction* to rates for customers. As a point of reference, PSE's original rate case filing included a baseline power cost of \$59.21 per MWh. In August, power costs were revised down to \$58.93 per MWh, to reflect lower natural gas prices. Any potential rate decrease would reflect power costs only and not impact our gross margin assumptions.

Depreciation Lag Assessment More Constructive Than Expected

The Commission's assessment of depreciation lag, including its consideration of remedies like out-of-period adjustments, was much more constructive than we anticipated. Although such remedies were not approved in this rate case, the WUTC provided clarity regarding the specificity they would need to consider out-of-period adjustments and left the door open for future requests, in our view. Specifically, the order stated:

...there is nothing that precludes PSE from seeking additions to rate base between rate cases so long as the amounts are not so large as to trigger a general rate proceeding under our rules. If the investments are shown to be prudent, the amounts are reasonable, and the plant is demonstrated to be

used and useful, the Commission may exercise its discretion to allow recovery in rates. (WUTC Order 08, January 5, 2007, pg. 19)

We believe the Commission's willingness to explore pro forma adjustments to test-year depreciation expense and/or rate base is significant because it could provide a mechanism to update incremental transmission and distribution investment that is put into service after the end of the test year, which may help to reduce regulatory lag.

Expect Update on Next Regulatory Steps on Earnings Conference Call

We expect Puget Energy management to provide investors an update on the utility's next regulatory steps on the fourth quarter earnings conference call in early February. PSE could file a PCORC (versus a general rate case) to have the Goldendale plant incorporated into rate base after the acquisition closes sometime toward the end of the first quarter. If PSE were to file a general rate case to update costs and revisit issues denied in the 2006 GRC, it would also have to address several other issues identified by the WUTC including executive compensation recovery in rates and forward market prices in power cost calculations.

Adjusting 2006E and 2007E EPS and Introducing 2008 Estimates

We are increasing our 2006 EPS estimate to \$1.45 from \$1.40 to reflect a number of adjustments to our earnings model, including reductions to interest expense and taxes. While we expect a year-over-year increase in O&M expense in the fourth quarter associated with storm recovery costs, we are uncertain of the magnitude of these costs and the extent to which other factors may partially offset these expenses. We are also reducing our 2007 EPS estimate to \$1.60 from \$1.65, primarily reflecting the results of the rate case. Additionally, we are introducing a 2008 EPS estimate of \$1.75. Our 2008 estimate assumes partial year benefit from either a generation-related PCORC or a general rate case.

Discount Valuation Continues to Be Warranted

Puget Energy shares trade at 15.4x our revised 2007 earnings estimate, a discount to the utility group average P/E multiple of 16.3x. Although the results of PSE's rate case were essentially in line with our expectations, we continue to believe the discount multiple is warranted given our belief that the regulatory environment in Washington will remain challenging. That said, we would expect Puget's above-average 4.1% dividend yield to support the shares.

Investment Risks

The *positive* risks to our Neutral rating on PSD depend, in large part, on the utility's ability to remedy its regulatory lag. The 2006 general rate case unsuccessfully sought to address a portion of the lag through a depreciation tracker. The filing included no mechanisms to rectify historical test years which contribute to the systemic under-recovery of O&M expense. The introduction of a rate structure that would lead to a more timely recovery of operating expenses would likely result in PSD shares outperforming.

The biggest *negative* risk to our Neutral rating on PSD is an unfavorable regulatory ruling in the future that could contribute to Puget Sound Energy under-earning its allowed ROE. If Puget experiences additional under-earning pressure or is unable to

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add its planned utility investment to rate base, we would expect EPS, and thus the share price, to come under pressure.

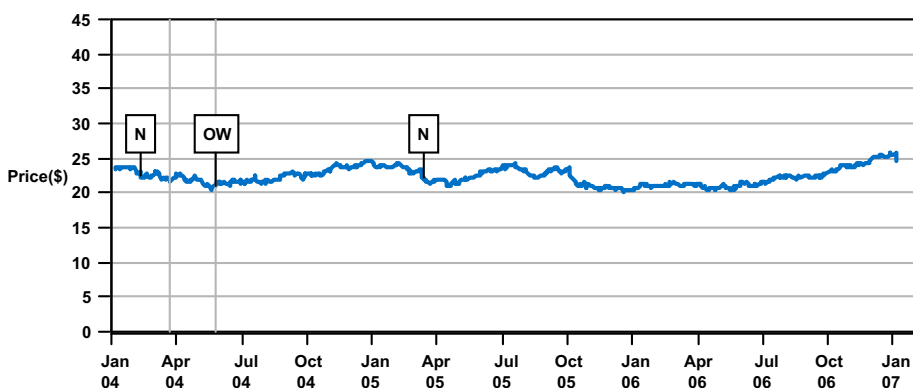
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Puget Energy (PSD) Price Chart



Date	Rating	Share Price (\$)	Price Target (\$)
12-Feb-04	N	22.51	-
25-May-04	OW	20.90	-
14-Mar-05	N	22.15	-

Source: Reuters and JPMorgan; price data adjusted for stock splits and dividends.
Break in coverage Mar 23, 2004 - May 25, 2004. This chart shows JPMorgan’s continuing coverage of this stock; the current analyst may or may not have covered it over the entire period. As of Aug. 30, 2002, the firm discontinued price targets in all markets where they were used. They were reinstated at JPMSI as of May 19th, 2003, for Focus List (FL) and selected Latin stocks. For non-JPMSI covered stocks, price targets are required for regional FL stocks and may be set for other stocks at analysts’ discretion.
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