

**EXHIBIT NO. ___(PJC-1CT)
DOCKET NO. U-072375
2007 MERGER PROCEEDING
WITNESS: PHYLLIS J. CAMPBELL**

**BEFORE THE
WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION**

**In the Matter of the Joint Application of
PUGET HOLDINGS LLC
And
PUGET SOUND ENERGY, INC.
For an Order Authorizing Proposed Transaction**

Docket No. U-072375

**PREFILED REBUTTAL TESTIMONY (CONFIDENTIAL) OF
PHYLLIS J. CAMPBELL
ON BEHALF OF PUGET SOUND ENERGY, INC.**

**REDACTED
VERSION**

JULY 2, 2008

PUGET SOUND ENERGY, INC.

**PREFILED REBUTTAL TESTIMONY (CONFIDENTIAL) OF
PHYLLIS J. CAMPBELL**

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1 **PUGET SOUND ENERGY, INC.**

2 **PREFILED REBUTTAL TESTIMONY (CONFIDENTIAL) OF**
3 **PHYLLIS J. CAMPBELL**

4 **I. INTRODUCTION**

5 **Q. Will you please state your name and business address?**

6 A. My name is Phyllis J. Campbell. My business address is 1200 Fifth Avenue,
7 Suite 1300, Seattle, WA 98101-3151.

8 **Q. By whom are you employed and in what capacity?**

9 A. Since 2003 I have been the President and CEO of The Seattle Foundation, the
10 largest community foundation in the State of Washington. Previously I held
11 various positions, including President, with U.S. Bank, Washington.

12 **Q. Have you prepared an exhibit describing your education, relevant**
13 **employment experience, and other professional qualifications?**

14 A. Yes, I have. It is Exhibit No. ___(PJC-2).

15 **Q. Are you a director of Puget Energy and PSE?**

16 A. Yes.

1 **Q. If the Proposed Transaction as contemplated by the Merger Agreement is**
2 **completed, will you have a role with the surviving entity?**

3 A. No.

4 **Q. If the Proposed Transaction is completed, will you receive a “change of**
5 **control” or other payment?**

6 A. No. The shares I own, however, would be exchanged for the same \$30 per share
7 payment made to all other shareholders.

8 **Q. Please summarize the purpose of your rebuttal testimony.**

9 A. This rebuttal testimony responds to arguments raised by Commission Staff and
10 Public Counsel that the Joint Applicants have failed to provide support for their
11 conclusion that the Proposed Transaction offers better access to capital compared
12 to PSE (as a subsidiary of Puget Energy) continuing as a stand-alone business.

13 **II. THE BOARD AND ITS ROLE IN SETTING STRATEGY**

14 **A. Experience and Positions on the Puget Energy Board**

15 **Q. What is your role on the boards of Puget Energy and PSE?**

16 A. I am the Lead Independent Director of the Boards of Puget Energy and of Puget
17 Sound Energy. I have been on the Board of PSE since 1993.

1 **Q. Are you on any Puget Energy or PSE Board committees?**

2 A. Yes. I am the Chair of the Boards' Securities Pricing Committees, a member of
3 Puget Energy's Strategic Review Committee, and a member of the Boards'
4 Governance and Public Affairs Committees.

5 **Q. Do you serve as a director on the boards of other companies or entities?**

6 A. Yes. I am on the boards of Alaska Air Group, of Joshua Green Corporation, and
7 of Nordstrom Inc.

8 **Q. Please summarize your duties as the Lead Independent Director.**

9 A. These duties are set forth in the Company's Corporate Governance Guidelines
10 and in its Bylaws. Briefly, among other things, I am to stay informed as to
11 strategy and critical issues facing the Company and its performance, to help set
12 the meeting agendas, to lead executive sessions of Board meetings without
13 management present, and to be the primary shareholder contact for the Board.

14 **Q. What is the purpose of the Securities Pricing Committee?**

15 A. The Securities Pricing Committee enables the Company to execute equity and
16 debt financings more quickly than it could if it had to secure approval of the full
17 Board. Its members gain knowledge of the marketing, pricing and terms of Puget
18 Energy's and PSE's equity and debt offerings, and of the objectives of investors
19 considering the Company's offerings.

1 **Q. What is the Strategic Review Committee?**

2 A. The Board established the Strategic Review Committee to consider various
3 alternatives affecting the direction of the overall business, including acquisitions,
4 divestitures, combinations or other transactions.

5 **Q. In what capacity have you been involved in the consideration of the Merger**
6 **Agreement with the Investor Consortium?**

7 A. As Lead Independent Director, member of the Strategic Review Committee, and
8 as a Director, I was involved in substantially all of the board-level discussions
9 regarding the Merger Agreement with the Investor Consortium.

10 **B. The Board's Role in the Strategic Review of this Transaction**

11 **Q. Does the Board determine the Company's strategy?**

12 A. Yes, in working with the Company's senior management, the Board develops
13 strategic plans and reviews, debates and approves any given strategy.

14 **Q. How frequently does the Board consider major changes in strategy?**

15 A. The Board is available to consider proposals to change corporate strategy at any
16 time. Absent a specific proposal, however, the Board conducts a significant
17 strategic review of the Company's long-term business plan at least annually.

1 **Q. Prior to the initiation of discussions with the Investor Consortium about a**
2 **transaction involving some or all of the Company, what concerns did the**
3 **Board have with respect to the Company's strategy?**

4 A. The Board has been concerned for some time about the Company's growing need
5 to raise equity and debt capital externally to fund the Company's capital
6 programs. As background, the Company's capital expenditure or capital
7 expenditure budgets, which we approve, has exceeded the prior year's capital
8 expenditure budget every year for the past five years. This trend will continue.

9 **Q. What is driving this need for capital?**

10 A. Among the factors driving the need for capital are the following: (1) much of
11 PSE's existing infrastructure has aged to the point that replacement and upgrading
12 is now required; (2) many long-term wholesale power contracts will soon expire,
13 and so will have to be replaced at higher cost; (3) growth in this region continues
14 to outpace national averages, requiring substantial new infrastructure; and
15 (4) legislative and regulatory mandates impose additional costs on the utility.

16 **Q. Why did the Board create the Strategic Review Committee?**

17 A. Following some preliminary discussions by management with Macquarie
18 Securities (USA) Inc. about our gas distribution business, the Board determined
19 that a more complete review of strategic alternatives facing the Company was
20 prudent and should be conducted by a special committee. As discussions with

1 third parties unfolded during 2006 and 2007, the Committee met to consider the
2 options available to the Company. The Proxy Statement describes this process in
3 detail.

4 **Q. What strategic alternatives did the Strategic Review Committee and the full**
5 **Board consider?**

6 A. The Strategic Review Committee and the full Board considered a sale or strategic
7 combination of the gas distribution business, the sale of the entire Company to
8 buyers including the Investor Consortium, and remaining an independent
9 company.

10 **Q. Did the Board seek outside advice in the course of its evaluation of the**
11 **various strategic alternatives?**

12 A. Yes. The Board, independent from management, sought and received input from
13 Morgan Stanley and from Dewey & LeBoeuf LLP.

14 **Q. When considering a continuation of PSE as an independent utility, what**
15 **issues were of concern to the Board?**

16 A. The Board was concerned that the Company's long-term business plan required
17 raising significant equity and debt capital relative to both internally generated
18 funds and to the capital base of the company. We were also aware of the pressure
19 these external financing requirements could put on the Company's share price and
20 credit ratings. In order to run and maintain the utility prudently, this need for

1 capital was unavoidable. We understood the risks inherent in a strategic plan that
2 called for repeated equity sales and debt issuances.

3 **Q. Please describe the risks that concerned you.**

4 A. First, capital markets are neither static nor predictable. Once a company starts a
5 capital program requiring external funding, the flexibility in the timing and
6 amount of offerings is limited. However, the price of capital (as measured by
7 utility stock indices and interest rates) and investor interest in various forms of
8 securities is constantly changing. The larger the external funding need, the more
9 significant the consequence of higher pricing or declines in investor demand.

10 [REDACTED]

11 [REDACTED]

12 [REDACTED]

13 [REDACTED]

14 [REDACTED]

15 [REDACTED]

16 [REDACTED]

17 [REDACTED]

18 **Q. Did materials from outside experts corroborate the challenges of this**
19 **alternative?**

20 A. Yes. In addition to internal financial projections, Morgan Stanley's independent

1 financial analysis supported this forecast of essentially flat earnings, and the need
2 for significant amounts of capital relative to our earnings power.

3 **Q. Were there elements of the Proposed Transaction proposed by the Investor**
4 **Consortium that addressed your concerns regarding the challenges the**
5 **Company faced on a stand-alone basis with a flat earnings forecast and the**
6 **need for significant amounts of capital relative to earning power?**

7 A. Yes. Among the important elements of the Proposed Transaction was the fact
8 that the Investor Consortium was committing to provide five years' of the
9 Company's capital needs. Also, the price offered by the Investor Consortium was
10 at a significant premium to the then-current stock price, and appeared to be a
11 significant premium to likely future stock prices, given the likely effect of
12 repeated future sales of equity on the price of the Company's common stock.

13 **Q. Did you seek any particular commitments from the Investor Consortium in**
14 **connection with your consideration of the Proposed Transaction?**

15 A. Yes. The Board was explicit that a transaction must include commitments from
16 the buyers to, among other things, maintain existing personnel levels, keep the
17 headquarters local, and commit to existing strategies regarding environmental
18 matters and philanthropic involvement. The Board also sought and received
19 assurances that some current Board members would continue as "hold-over"
20 directors on the new Board and current management would remain in place.

1 **Q. What is your understanding of your obligations as a Board member**
2 **contemplating a combination or similar strategic transaction?**

3 A. It is my understanding that directors have certain fiduciary duties to the company
4 they serve and to shareholders. A director must discharge his or her duties as a
5 director in good faith with the care an ordinarily prudent person in a like position
6 would exercise under similar circumstances, and in a manner the director
7 reasonably believes to be in the best interests of the corporation. In addition, in a
8 merger or acquisition transaction like this one, directors also have a duty to make
9 reasonable efforts to optimize shareholder value.

10 **Q. Were there other interests you considered?**

11 A. Because gas and electric utilities serve a special role in society, we believe that as
12 directors of a utility we must consider a complex set of interests in any
13 deliberation. The interests of customers, employees, owners, regulators, the
14 region served, and even the environment itself, must be balanced by a thoughtful
15 Board.

16 **Q. Do you think PSE's customers are well-served by the Proposed Transaction?**

17 A. Yes. Committed capital, during a time of turbulent markets and quickly
18 escalating costs, provides security that works to the benefit of customers. The
19 Investor Consortium is comprised of patient investors, not short-term speculators,
20 who view this asset as a long-term core holding. Also, the Proposed Transaction

1 is different from strategic combinations that often lead to significant cut-backs in
2 local employment, philanthropy or other local involvement. These buyers are
3 experienced financial investors who fully support the Company's existing
4 commitments.

5 **Q. Does the Proposed Transaction expose PSE's customers to new and**
6 **unaccustomed risks?**

7 A. No. It is essential to remember that the Company has tremendous capital needs
8 regardless of its owners. Aging infrastructure must be replaced, expiring
9 wholesale power contracts must be renegotiated, and a high-growth region must
10 be served. The stand-alone or status quo case, in light of these massive needs for
11 capital, poses its own significant challenges. Turning to the capital markets
12 repeatedly, while continuing on the status quo route, would expose the
13 Company's continued financial well-being to very real risks. And a financially
14 weak utility is not to the customer's benefit.

15 **Q. Did the independent members of the Board consider the Merger Agreement**
16 **and deliberate separate and apart from management?**

17 A. Yes.

18 **Q. What was the decision?**

19 A. We voted unanimously in favor of the Proposed Transaction.

III. CONCLUSION

1

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Q. Does that conclude your prefiled rebuttal testimony?

3

A. Yes.