

**EXHIBIT NO. ___(CJL-8HCT)
DOCKET NO. U-072375
2007 MERGER PROCEEDING
WITNESS: CHRISTOPHER J. LESLIE**

**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 (HIGHLY CONFIDENTIAL) OF
CHRISTOPHER J. LESLIE
ON BEHALF OF PUGET HOLDINGS LLC**

**REDACTED
VERSION**

JULY 2, 2008

PUGET HOLDINGS LLC

**PREFILED REBUTTAL TESTIMONY (HIGHLY CONFIDENTIAL) OF
CHRISTOPHER J. LESLIE**

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1 **PUGET HOLDINGS LLC**

2 **PREFILED REBUTTAL TESTIMONY (HIGHLY CONFIDENTIAL) OF**
3 **CHRISTOPHER J. LESLIE**

4 **I. INTRODUCTION**

5 **Q. Are you the same Christopher J. Leslie who provided prefiled direct**
6 **testimony in this proceeding on behalf of Puget Holdings LLC (“Puget**
7 **Holdings”)?**

8 A. Yes. On December 17, 2007, I filed direct testimony, Exhibit No. ___(CJL-1T),
9 and six exhibits supporting such direct testimony, Exhibit No. ___(CJL-2)
10 through Exhibit No. ___(CJL-7), in this proceeding.

11 **Q. What is the purpose of your rebuttal testimony?**

12 A. My rebuttal testimony responds to the issues raised by the Parties with regard to
13 the Proposed Transaction and seeks to clarify a number of misunderstandings that
14 the Parties appear to have with regard to our initial testimony and various
15 materials provided during the discovery process. In addition, my rebuttal
16 testimony describes additional commitments that Joint Applicants are offering to
17 address the issues raised by the Parties in their opposing testimony.

18 **Q. Please summarize your rebuttal testimony.**

19 A. As an experienced group of long-term infrastructure investors seeking to acquire

1 a business that is as important to a region as Puget Energy is to Western
2 Washington, we understand that we are facing a significant level of scrutiny from
3 a number of stakeholders. We understand that each of those stakeholders will be
4 evaluating whether or not we are a worthy owner of the business. My rebuttal
5 testimony, and that of my co-investors in Puget Holdings LLC, therefore seeks to
6 understand initial stakeholder opposition to the transaction, and to address the
7 issues that they have raised with a combination of clarifications and new
8 commitments.

9 Based on our reading, the opposition to the Proposed Transaction appears to be
10 based on (1) an undervaluation of the benefits that Macquarie and the Investor
11 Consortium are capable of bringing to Puget Sound Energy (“PSE”); (2) an
12 overstatement of the risks associated with the Proposed Transaction, particularly
13 given new commitments the Investor Consortium is prepared to offer; and (3) an
14 apparent misunderstanding of certain aspects of the Proposed Transaction,
15 including associating with the Proposed Transaction information that has no
16 bearing on it. My rebuttal testimony therefore will make the following points:

- 17 • The Parties in their opposing testimony overlook or
18 undervalue the benefits of the Proposed Transaction. As
19 experienced long-term infrastructure investors, the Investor
20 Consortium brings improved access to both equity and debt
21 capital that will provide benefits to PSE to finance its large
22 capital expenditure requirement. My rebuttal testimony
23 describes these benefits, and corrects any misstatements.
- 24 • The Parties in their opposing testimony overstate the risks
25 associated with the Proposed Transaction. Part of this is
26 clearly linked to certain misunderstandings regarding the
27 terms of the Credit Agreement and the financial

1 projections. My rebuttal testimony corrects these
2 misstatements, and provides an accurate portrayal of the
3 credit arrangements.

- 4 • Joint Applicants are offering additional commitments to
5 address the issues raised by the Parties regarding the
6 protection of PSE’s customers from perceived risks of the
7 Proposed Transaction. Specifically, Joint Applicants are
8 committing to adopt dividend restrictions at both the Puget
9 Energy (“PE” or “Puget Energy”) and PSE level to further
10 insulate PSE’s customers. In addition, Joint Applicants are
11 offering \$100 million of rate credits and merger savings
12 over the next ten years. My rebuttal testimony describes
13 these additional commitments.

- 14 • The Parties in their opposing testimony mischaracterize the
15 Proposed Transaction, such as by referring to it as a
16 “leveraged buy out” and by suggesting that investors
17 comprising the Investor Consortium are “limited partners”
18 with a requirement to return capital over a specific time
19 period. The Parties also include information that is not
20 pertinent to the Proposed Transaction, such as references to
21 the failure of Bear Stearns, the subprime mortgage
22 meltdown, collateralized debt obligations, and comparisons
23 to private equity funds. My rebuttal testimony will correct
24 these inaccuracies and misstatements, and will explain how
25 various information included in the Parties’ opposing
26 testimony is not relevant to the Proposed Transaction.

27 **II. THE INVESTOR CONSORTIUM PROVIDES PSE WITH**
28 **IMPROVED ACCESS TO CAPITAL**

29 **Q. Several intervenor witnesses challenge your assertion that the Investor**
30 **Consortium provides PSE better access to capital than it currently enjoys,**
31 **and challenge the assertion that PSE’s capital needs are large relative to both**
32 **their peers and historical standards. What is your response to these claims?**

33 A. These issues will be addressed by a number of witnesses in Joint Applicants’
34 rebuttal case, as they are clearly important points. There are two main issues that

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are critical to note:

1. There is a fundamental under-appreciation of the challenge that PSE is facing in its ability to finance the growth on a stand-alone basis; and
2. There is an apparent misunderstanding of the nature of the investors and the capital structure of the Proposed Transaction and of the corresponding benefits provided by our structure.

The first issue will be addressed by separate expert testimony provided by Mr. Justin Pettit relating to the challenges PSE faces in raising equity on a stand-alone basis; testimony from PSE Chief Financial Officer Eric Markell that articulates the relationship between access to capital on reasonable terms and customer benefits; and testimony from Phyllis Campbell on the decision-making process and analysis of the PSE Board of Directors in entering into the Proposed Transaction.

This section of my testimony will address the second issue above regarding the nature of the investors and their commitments, the transaction structure, and the improved access to capital provided by the Investor Consortium. This issue will also be addressed in rebuttal testimony provided by Mark Wiseman of Canada Pension Plan Investment Board, Lincoln Webb of British Columbia Investment Management Corporation, and William McKenzie of Alberta Investment Management Corporation.

1 **Q. Please explain the basis for your statement that the Parties in their opposing**
2 **testimony misunderstand the improved access to capital the Investor**
3 **Consortium brings to PSE.**

4 A. There are two main areas where there appears to be a misunderstanding on this
5 point. The first I associate with a lack of familiarity with the nature and goals of
6 infrastructure investors. The second is related to misunderstandings as to how the
7 committed debt financing and the access to global debt markets made available by
8 the Investor Consortium provide benefits to PSE.

9 **A. The Investor Consortium Provides PSE With Improved Access to**
10 **Equity Capital**

11 **Q. Please elaborate on the nature and structure of the transaction and the goals**
12 **of the equity investors.**

13 A. The Parties in their opposing testimony mischaracterize the Proposed Transaction
14 as a “private equity buyout” or a “leveraged buyout” or “LBO.” This is an
15 inaccurate characterization. Private equity funds, as typically defined, acquire
16 underperforming businesses, improve and streamline business operations – often
17 coupled with significant job reductions – and then sell such businesses within a
18 relatively short period of time to obtain a profit on their investment. This strategy
19 is fundamentally different from the business model of infrastructure investors, and
20 it is not consistent with past practice or the intentions of the Investor Consortium.

1 **Q. What about characterizations in the Parties’ opposing testimony of the**
2 **structure as a “limited partnership,” with the investors having a right to a**
3 **return of their capital over a specified time period?**

4 A. These statements are not correct. There is no “General Partner” of Puget
5 Holdings, and there is no agreement among investors of Puget Holdings to “return
6 capital to limited partners within a certain time period.” Exhibit No. ___(SGH-
7 1THC) at page 12, lines 17-18. The infrastructure investors in Puget Holdings
8 seek to acquire quality, well-performing businesses with strong management
9 teams that are likely to continue to perform well over the long-term. Investors in
10 Puget Holdings have not based their investment decisions on plans to “flip” such
11 a business to obtain a large profit on exit as dictated by a general partner. These
12 erroneous claims are addressed in more detail in the testimonies of Mr. Wiseman,
13 Mr. Webb and Mr. McKenzie.

14 **Q. Does the fact that one of the members of the Investor Consortium,**
15 **Macquarie Infrastructure Partners, has a [REDACTED],**
16 **mean that its investments, including in Puget Energy, must be liquidated at**
17 **the end of that period?**

18 A. Practically speaking, no. It is important to note that MIP is only one member of
19 the Consortium, comprising 31.8%, and has no unilateral ability to cause a sale of
20 the investment. The Canadian members of the Investor Consortium highlight
21 their long-term investment philosophy in their respective testimony. Further,
22 while MIP is structured as a [REDACTED] fund, it does not mean that MIP’s investors

1 will elect out of their investments at that time. Similar to the way that
2 infrastructure as an asset class has evolved elsewhere around the world, we expect
3 U.S. investors would want to hold onto these assets for the long term as they
4 become accustomed to this new asset class. However, regardless of what
5 investors decide to do at the [REDACTED] mark, there is a high likelihood that
6 Macquarie, as manager of MIP, will continue to manage the vehicle that holds
7 that portion of the PSE investment, either by transferring it into a different
8 Macquarie managed vehicle, or continuing the life of the fund through a public
9 listing or other mechanism, thereby remaining as the long-term owner.

10 **Q. Please describe the benefits of this ownership structure to PSE.**

11 A. The Investor Consortium is comprised of the Macquarie Group and three
12 Canadian pension funds, each of which has access to large amounts of equity
13 capital that are rapidly growing. Mark Wiseman, William McKenzie and Lincoln
14 Webb in their testimony each discuss their funds' access to equity capital
15 available for investment. In addition, the Macquarie Group has raised
16 approximately \$16.5 billion of equity capital since July 2007.

1 The following table shows the significant growth of the assets under management
2 of the Macquarie Group over the past four years:

	Mar. 31, 2005	Mar. 31, 2006	Mar. 31, 2007	Mar. 31, 2008
Assets Under Management	A\$97 billion	A\$140 billion	A\$197 billion	A\$232 billion

3 The Investor Consortium is comprised of long-term investors with deep pockets
4 that are actively looking for opportunities to invest for the long term. The Parties
5 have sought, in a number of places, to characterize the transaction as leaving PSE
6 with no access to capital other than debt facilities, which is not the case. The
7 Parties do not acknowledge the fact that the investors in the transaction are
8 actively seeking opportunities to invest in infrastructure businesses like PSE, and
9 have already invested nearly \$300 million of equity in PSE through a completed
10 private placement and intend to invest an additional \$2.9 billion in PE at closing.
11 To the extent that there are opportunities to invest more capital after closing than
12 is assumed in the base case financial forecast, these investors would have
13 significant funds available to do so. As an indication of the scale of capital
14 available to the Consortium for investment, they had a total of \$499 billion in
15 assets under management as of March 31, 2008.¹

16 **Q. Have the investors committed funds to invest in PSE above what has been**
17 **invested to date or the substantial amount that will be invested at closing?**

18 A. No. The Investor Consortium has arranged sufficient debt and equity financing to

¹ Canadian and Australian Dollars converted to USD at 1.02 and 1.045 / 1, respectively.

1 fund, along with the operating cash flow of the business, the currently identified
2 capital needs of PSE. However, given the amount of capital the investors have
3 and the rate at which that capital is growing, members of the Investor Consortium
4 are eager for opportunities to invest more equity capital in quality infrastructure
5 assets.

6 **Q. What criteria would the investors use to evaluate future equity investments**
7 **in PSE?**

8 A. I cannot speak for each member of the Investor Consortium in this regard.
9 However, I note that the Investor Consortium has committed \$3.2 billion to invest
10 in this transaction based on the expectation of a fair regulatory environment in the
11 state of Washington, including the rates of return on equity provided. The criteria
12 for additional investments are addressed in more detail in the testimonies of
13 Mr. Wiseman, Mr. Webb and Mr. McKenzie.

14 **Q. What other benefits are provided by this type of ownership group?**

15 A. The Investor Consortium brings to the table global expertise in the utilities sector
16 and a window into the best management practices and technological applications
17 of our portfolio companies. The Investor Consortium collectively has substantial
18 investments in electric, gas and water utilities in the U.S., Canada, South
19 America, Europe, Asia and Australia. This access to the insight of the
20 management of the businesses we own and to a network of resources that span the
21 globe can be called upon, where appropriate, to take advantage of technological

1 and operating advancements around the globe. For example, Macquarie-managed
2 funds currently have ownership interests in a number of energy and utility assets
3 around the globe, including U.S. utilities such as Duquesne Light, Aquarion
4 Company and The Gas Company. If needed, PSE would have the opportunity to
5 draw on the experience of other utilities owned by members of the Investor
6 Consortium.

7 **Q. Please illustrate how a utility has benefited from this type of access to capital**
8 **from an infrastructure investor consortium.**

9 A. One example is an investment made by Macquarie Capital, British Columbia
10 Investment Management Corporation, and Alberta Investment Management
11 Corporation (among others): Thames Water, one of the largest water utilities in
12 the world, which serves London and its surroundings. In evaluating the
13 opportunity, the acquiring consortium identified the need to inject significant
14 capital into the business in order to improve the standard of service to meet
15 regulatory-imposed operating standards. The investment was financed with that
16 in mind, and the utility was able to embark on a substantial capital expenditure
17 program upon acquisition. As a direct result of this commitment, Thames Water
18 has hit its regulator-set target for reducing leaks for the first time in seven years (a
19 12% reduction), as well as increased the security of supply (263%), reduced
20 sewer collapses (40%), and reduced main bursts (22%). In order to accomplish
21 this, annual capital expenditures nearly doubled, from approximately \$2 billion
22 prior to the acquisition to approximately \$4 billion in the 2008 business plan.

1 **Q. Please explain why, in the case of Thames Water, the investors chose to**
2 **invest so heavily in the utility.**

3 A. As in the case of PSE, the investors in Thames Water focused on returns over the
4 long term. Cost-cutting to meet short term return expectations rarely improves
5 customer service or the condition of utility infrastructure. Capital investment, on
6 the other hand, frequently achieves both aims over the long term. Infrastructure
7 investors understand that to achieve a desired long term return, they must take a
8 long term view and invest in the business. The Mayor of London recognized and
9 appreciated this relationship when he reported in July 2007: “I am glad that the
10 company has met its leakage target and feel that this is representative of the
11 positive changes achieved under new management.” Please see Exhibit
12 No. ___(CJL-9) at pages 69-70 for further information on Thames Water.

13 **Q. Why are infrastructure investors such as the Investor Consortium well-**
14 **equipped to undertake a large capital plan like that faced by Thames Water**
15 **and PSE?**

16 A. Because of the Investor Consortium’s long-term time horizon, we are able invest
17 heavily even where the benefits only accrue at some point in the future as
18 opposed to next quarter’s earnings per share or dividend.

1 **B. The Investor Consortium Provides PSE with Improved Access to Debt**
2 **Capital**

3 **Q. You also state that there appears to be some confusion related to the debt**
4 **facilities arranged for the Proposed Transaction. Can you expand on what**
5 **you mean?**

6 A. Yes. Several of the Parties suggest that the Investor Consortium's access to
7 capital is limited to the debt facilities raised for the Proposed Transaction. As
8 stated above, this is not accurate. Although the committed debt facilities in this
9 transaction do provide \$1.4 billion to fund PSE's capital expenditures, they do not
10 preclude the Investor Consortium from investing additional equity. Nor do they
11 preclude PSE from accessing the bond market.

12 **Q. Certain witnesses also imply that the Investor Consortium no longer plans to**
13 **take advantage of PSE's existing lender relationships. (Exhibit**
14 **No. ___(RHS-1T) at pages 9-10.) Is this correct?**

15 A. No. In fact, many of PSE's existing lenders are participating in the new credit
16 facilities arranged for this transaction, including key relationship lenders such as
17 [REDACTED]
18 [REDACTED]. What Macquarie and the Investor Consortium bring to PSE is
19 access to a broader lender group than PSE currently has by tapping into the global
20 and proven relationships of Macquarie and the Investor Consortium.

1 **Q. Mr. Schmidt argues that the ability of the Investor Consortium, and**
2 **particularly Macquarie, to access “global capital markets” is more risky**
3 **than the status quo of only focusing on “traditional sources of credit”.**
4 **(Exhibit No. ___(RHS-1T) at pages 10-11.) Please respond to this claim.**

5 A. Mr. Schmidt’s assertion that having access to broader sources of capital is a “bad”
6 thing is difficult to understand. As stated above, the Investor Consortium is
7 (i) maintaining PSE’s existing lender relationships and ongoing access to the
8 bond market, while adding additional committed facilities; and (ii) expanding the
9 list of options available to PSE by adding the Investor Consortium’s global debt-
10 raising expertise and relationships. Having a larger number of financing options
11 will allow PSE to pursue the lowest-cost financing available and increase access
12 to capital sources. Such capabilities are never more valuable than when credit
13 markets deteriorate; as is evident from the current credit crisis, not all markets are
14 affected equally. Rather than being a detriment – as suggested by Mr. Schmidt –
15 diversity of access to capital markets, like diversity of energy supply, provides a
16 clear benefit to ratepayers.

17 **Q. Can you provide a tangible example of the access to debt capital provided by**
18 **the Investor Consortium?**

19 A. Yes. Since the onset of the subprime mortgage crisis in August 2007, global
20 credit markets have been experiencing severe interruptions. Mergers and
21 acquisitions have declined to nearly a standstill during that time for lack of
22 financing. In contrast, the members of the Investor Consortium have been able to

1 announce and complete the financing of a number of transactions and
2 refinancings in spite of the credit crisis. For example, Macquarie in particular has
3 raised over \$71 billion of debt since July 2007.

4 **Q. Do you agree with Mr. Horton's claim that Macquarie's investments in 116**
5 **different infrastructure assets could increase the risk of a loss of reputation**
6 **and thus may restrict Puget Holdings' access to capital? (See Exhibit**
7 **No. ___(WNH-1HCT) at page 12.)**

8 A. No, I do not. Similar to the above argument on global access, this is an
9 unfounded and counterintuitive argument that scale, diversification and
10 experience are a disadvantage. The diversity of the markets in which the
11 116 assets are located, and the diversity of the sources of equity and debt capital
12 raised for these assets, actually demonstrates the opposite, *i.e.*, if there are ever
13 any problems with one of the assets in the portfolio, there would likely be a much
14 less significant impact on Macquarie than the impact of a similar event on another
15 less diversified institution. Moreover, debt associated with these 116
16 infrastructure investments is structured to be non-recourse to any other investment
17 held by Macquarie, and the overall leverage of the portfolio is relatively modest at
18 56%.

19 Notably, the same argument could be made regarding the ownership of
20 PacifiCorp by Berkshire Hathaway. Mr. Horton's argument taken to its logical
21 conclusion would have us believe that if, for example, there were a problem with
22 GEICO, that would mean that PacifiCorp's access to capital would be tarnished.

1 Is PacifiCorp disadvantaged by being a member of the Berkshire Hathaway group
2 of companies and participating in the diversity associated with a wide variety of
3 industries? In addition, Mr. Horton's claim appears to be based upon
4 inappropriate comparisons of the Macquarie Group to other institutions, such as
5 Bear Stearns. As discussed later in my testimony, the problems at Bear Stearns
6 related to assumed risks very different from Macquarie's exposure to
7 infrastructure investments that, by their very nature, tend to be stable operating
8 businesses. It should also be noted that nearly 50% of the Investor Consortium's
9 investment in this transaction is held by Canadian pension funds having their own
10 regular influx of funds, network of global relationships, and access to substantial
11 amounts of capital.

12 **Q. Are Joint Applicants willing to provide an additional commitment to**
13 **substantiate the benefits associated with greater access to capital?**

14 A. Yes. While we believe we have demonstrated that PSE's customers will benefit
15 from the new ownership structure at PSE, Joint Applicants are proposing an
16 additional commitment that provides tangible, quantifiable customer benefit
17 associated with the improved access to capital. This additional commitment is
18 discussed in Section IV of my testimony.

1 **III. THE OPPOSING TESTIMONY OVERSTATES THE**
2 **PERCEIVED RISKS OR HARMS ASSOCIATED WITH THE**
3 **PROPOSED TRANSACTION**

4 **Q. Please explain how the Parties have overstated the perceived risks or harms**
5 **associated with the Proposed Transaction.**

6 A. A good example is the fact that PSE has been placed on Negative Watch by the
7 rating agencies, which several Parties claim already equates to a negative impact
8 resulting from the Proposed Transaction.

9 **Q. Is this an accurate representation, or is it customary practice for the credit**
10 **rating agencies to place a company, especially a utility, on “negative” credit**
11 **watch pending completion of an announced transaction?**

12 A. I do not believe it is an accurate representation. It is customary for rating
13 agencies, *e.g.*, Standard & Poor’s (“S&P”), to place a company on “CreditWatch
14 Negative” pending the successful completion of the regulatory approval process
15 and subsequent financial close. The negative watch is associated with the
16 unknowns that can arise in a regulatory approval process, not the outlook
17 following the consummation of the transaction as proposed. [REDACTED]

18 [REDACTED]

19 [REDACTED]

20 [REDACTED]

21 [REDACTED]

1 **Q. Does “negative credit watch” equate to lowered credit ratings and “harm,”**
2 **as Public Counsel implies?**

3 A. No. [REDACTED]
4 [REDACTED]
5 [REDACTED]

6 **Q. Are there other examples of selective interpretation of information related to**
7 **the rating agency analysis?**

8 A. Yes. [REDACTED]
9 [REDACTED]
10 [REDACTED]
11 [REDACTED]
12 [REDACTED]
13 [REDACTED]
14 [REDACTED]
15 [REDACTED]

16 **Q. [REDACTED]**
17 **[REDACTED]**
18 **[REDACTED]**
19 **[REDACTED]**

20 A. [REDACTED]
21 [REDACTED]

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[REDACTED]

Q. A number of the Parties describe the risks they perceive to PSE associated with new debt raised by Puget Energy. Is this an accurate assessment of the impact on PSE?

A. No. We have designed a conservative and prudent capital structure for PSE, as evidenced by the maintenance of investment grade ratings at PSE. The Parties in their opposing testimony misperceive the risks associated with this structure. The Parties have misinterpreted several of the terms of the financing, which I will clarify in this section of my testimony. In addition, we have carefully examined the issues raised by the Parties that are not based on misunderstanding, and we propose to adopt certain additional measures suggested by the Parties to further insulate PSE from the leverage at Puget Energy. These additional measures are discussed in Section IV of my testimony.

Q. There appears to be confusion regarding the consolidated capitalization of Puget Energy at closing. Can you summarize the inaccuracies in the claims made by some of the intervenor witnesses?

A. Both Public Counsel witness Hill and Staff witness Elgin incorrectly state the amount of incremental debt raised to fund the acquisition – \$1.6 billion and \$1.4 billion, respectively.

1 To clarify, the debt breakdown at financial close is as follows:

	At Financial Close	➤ Incremental debt increase of \$1,050 million
PSE Debt Assumed	\$2,556 million	
PSE Debt Repaid	(\$572) million	
New PSE Debt	\$197 million	
New Puget Energy Debt	\$1,425 million	
CONSOLIDATED DEBT	\$4,177 million	

2 Where Mr. Elgin, for example, refers to the Puget Energy Term Loan of
3 \$1.4 billion, he overlooks the fact that \$375 million of existing PSE long-term
4 debt and \$197 million of short-term debt is assumed to be repaid with funds from
5 PE as part of the de-leveraging of PSE. This confusion spills over into Public
6 Counsel witness Hill's calculation of increases in PE consolidated debt as
7 approximating 50%. The actual number is a PE consolidated debt increase of
8 34%, and total debt at PSE is in fact reduced by 12%. The Joint Applicants have
9 committed to specific ring-fencing provisions that protect PSE and its customers
10 from the debt at Puget Energy.

11 **Q. Does Public Counsel witness Hill accurately represent the use of proceeds of**
12 **the new debt facilities in his statement that “[u]pon closing, the parent**
13 **company will issue at least an additional \$1.4 Billion of debt to fund capital**
14 **expenditures”?** (Exhibit No. ___(SGH-1THC) at page 14, line 20, through
15 **page 15, line 1.)**

16 A. No. PSE and PE will have \$1.4 billion of credit facilities available to support
17 PSE's ongoing capital expenditures for the next five years. As detailed in the

1 financial model, such debt will be drawn periodically as required through 2013 –
2 not immediately at closing as Public Counsel witness Hill states. Capital
3 expenditures will occur consistent with PSE’s business plan and evolving needs,
4 and will be funded with a combination of operating cash flow, equity and debt.

5 **Q. Is Public Counsel witness Hill correct when he asserts that PSE’s “ability to**
6 **safely and efficiently provide service to Washington ratepayers can be**
7 **directly affected by the debt arranged by Macquarie and incurred by Puget**
8 **Energy”?** (Exhibit No. ___(SGH-1THC) at page 51, lines 4-6.)

9 A. No. There are no restrictive covenants in the executed Credit Agreement for PSE
10 or PE which would restrict the spending of capital expenditures undertaken for
11 health and safety reasons or in accordance with common utility practice.
12 Furthermore, specific ring-fencing provisions have been committed which
13 provide additional protections to PSE and its ratepayers from the debt raised
14 above PSE.

15 **Q. Do you agree with Public Counsel witness Hill’s conclusion that the base case**
16 **projection of cash flows “are too thin to insure that they will not be violated**
17 **when compared to the level of volatility experienced in the past by Puget”?**
18 **(Exhibit No. ___(SGH-1THC) at page 55, lines 18-20.)**

19 A. No. In his analysis, Public Counsel witness Hill suggests that Funds From
20 Operations (“FFO”) less “Scheduled Base CapEx” would need to decrease by
21 \$317.9 million to reach cash lock-up and \$393.7 million to reach default. Public

1 Counsel witness Hill suggests that a decrease of that magnitude is not only
2 possible, but “not unusual.” To support this argument, Public Counsel witness
3 Hill’s analysis looks at a decrease in revenue or an increase in costs of gas and
4 electricity. Public Counsel witness Hill’s analysis is flawed in that he does not
5 recognize that costs associated with movements of gas and electricity related to
6 the Purchased Gas Adjustment (PGA) and Power Cost Adjustment (PCA)
7 mechanisms are explicitly excluded from the calculation of the lock-up ratios and
8 financial covenants. A more relevant discussion here would be an examination of
9 gross margin (which excludes movement in commodity costs captured in these
10 adjustment mechanisms). For reference, PSE has not experienced a calendar year
11 decline in gross margin since the Western Energy Crisis in 2001 when there was
12 no PCA mechanism in place, where gross margin declined by 12.4%, or
13 \$149 million, when compared to gross margin in 2000. Since 2001, PSE's gross
14 margin has increased each year at a compound annual growth rate (CAGR) of
15 5.8%.

16 **Q. What are some of the other “harms” alleged by the Parties?**

17 A. Certain Parties, and particularly Public Counsel, assert that the transaction would
18 harm ratepayers because “detailed quarterly and annual financial information [for
19 PSE] will no longer be publicly available.” Exhibit No. ___(SGH-1THC) at
20 page 7, lines 18-19. This will not be the case. Eric M. Markell describes the
21 ongoing nature of financial reporting in detail in his testimony, as well as offers
22 other commitments regarding financial reporting governance and transparency.

1 **Q. A number of Parties also raise issues with the activity of, and access to, books**
2 **and records of Puget Intermediate and Puget Holdings. How do Joint**
3 **Applicants respond to these issues?**

4 A. As described in Exhibit No. ___(CJL-6), these entities have no business
5 operations aside from their ownership in Puget Energy and PSE, and neither has
6 or intends to have any third party debt. As a result, Joint Applicants do not
7 believe any restrictions or reporting are relevant at these levels. However, to
8 alleviate these issues, Joint Applicants are willing to commit to notify the
9 Commission prior to raising any third party debt at either of these entities.

10 **Q. Are Joint Applicants offering additional commitments to address issues**
11 **about perceived “harms” associated with non-local ownership?**

12 A. Yes. In our experience, infrastructure investments require long-term
13 commitments to customer service, reliability and the communities served by the
14 infrastructure assets. Interaction with the community is essential to our
15 investment thesis, and we believe the utility must be available to hear the
16 concerns of the community. In order to achieve this, we will expand our previous
17 commitment with regard to maintaining the PSE headquarters in Bellevue, as
18 discussed further in Mr. Markell’s testimony.

19 In addition, Joint Applicants recently announced that if the Proposed Transaction
20 is approved by the Commission, the chairman of the board of directors for both
21 Puget Holdings and PSE will be William (Bill) S. Ayer, chairman and chief

1 executive of Alaska Air Group. Ayer has served on the current Puget Energy and
2 PSE boards since January 2005. Stephen P. Reynolds, who will remain on as PSE
3 president and CEO, will also continue to serve on the Puget Energy and PSE
4 boards. In addition, the PSE board will include Herbert B. Simon, who has
5 served as a director since March 2006. We believe that these additions to the
6 board of directors will provide the local understanding which is critical to the
7 business, and will ensure that we as investors are open and available to respond to
8 local concerns.

9 **Q. Do you believe that Public Counsel witness Hill's statements to the effect that**
10 **the Macquarie Group "business model" is too complex and that not enough**
11 **public information is available to explain its relationships have any basis?**

12 A. No. Public Counsel witness Hill's statements confuse the facts of this transaction
13 with various misunderstandings about the activities of the overall Macquarie
14 enterprise, and ignore the great lengths to which the Macquarie Group goes to
15 inform and educate its investors and the market. In addition to the highly detailed
16 full year's earnings presentation from May 20, 2008 as provided in Exhibit
17 No. ___(CJL-9), Macquarie also releases over 300 pages of financial information
18 and management analysis on a regular basis, a significant portion of which goes
19 beyond statutory and regulatory requirements. Additionally, the Macquarie
20 Group, as well as its various listed and unlisted vehicles, regularly updates its
21 investors and the markets through various forums such as operational briefings
22 (held twice per year), brokerage conferences, investor mailings, etc. Macquarie

1 Capital Funds have fully audited accounts, and typically provide additional
2 disclosures to assist investors and analysts.

3 **Q. Were there any other inaccurate claims made by any of the interveners**
4 **regarding the credit facilities and the financial projections in their rebuttal**
5 **testimony?**

6 A. Yes. Additional items are itemized and refuted in the rebuttal testimony of Mr.
7 Robinson Kupchak, Exhibit No. ___(RKK-1HCT).

8 **IV. JOINT APPLICANTS ARE OFFERING SIGNIFICANT NEW**
9 **COMMITMENTS TO PROVIDE QUANTIFIABLE, TANGIBLE**
10 **BENEFITS AND TO ADDRESS THE PARTIES' ISSUES REGARDING**
11 **PROTECTION OF PSE CUSTOMERS FROM RISKS**

12 **Q. You stated earlier that Joint Applicants are willing to provide an additional**
13 **commitment demonstrating the benefits associated with improved access to**
14 **capital. Please describe this additional commitment.**

15 A. While Joint Applicants believe we have demonstrated that a tangible qualitative
16 benefit related to access to capital will be provided by the new ownership of PSE,
17 we have also thoughtfully examined the issues brought forward by the Parties.
18 There seems to be a unanimous call for an additional quantifiable customer
19 benefit associated with the Proposed Transaction. In our attempt to be responsive
20 to the issues of the intervenors, we are prepared to commit to provide rate credits
21 of \$100 million (\$10 million per year for a 10-year period) commencing at the
22 closing of the Proposed Transaction. These rate credits will consist of two

1 components:

2 (i) Joint Applicants previously offered to flow through to
3 customers in future rate proceedings the \$1.2 million of
4 savings that are expected to materialize from de-listing
5 Puget Energy from the New York Stock Exchange. We
6 will commit to providing those benefits immediately,
7 through an annual rate credit of \$1.2 million. This portion
8 of the rate credit will be offsettable; to the extent PSE can
9 demonstrate in any subsequent rate proceeding that these
10 savings are reflected in the underlying cost of service, this
11 portion of the rate credit would cease to be provided
12 separately to customers.

13 (ii) Joint Applicants will provide an additional annual
14 \$8.8 million rate credit that is not offsettable, but that
15 reflects the Investor Consortium's willingness to accept
16 what, in effect, is a reduction in its returns for a limited
17 period. Based on our projections of the first ten years post-
18 closing of the Proposed Transaction, the magnitude of this
19 credit has the effect of a reduction in pre-tax return on
20 equity (ROE) of 24 basis points per year (\$8.8 million
21 divided by an average rate base of approximately \$8 billion
22 multiplied by an average equity ratio of approximately
23 47%) for the first ten years. This credit will be provided
24 regardless of the actual ROE approved by the Commission
25 during that ten-year period.

26 Together, these rate commitments provide customers with \$100 million of
27 tangible, quantifiable benefits from the Proposed Transaction. PSE's annual
28 corporate costs are committed to be \$1.2 million lower than they would have been
29 without the transaction, and Joint Applicants are committing to provide an
30 additional \$8.8 million in annual rate credits for ten years to substantiate and
31 quantify our claims regarding improved access to capital.

32 **Q. Why are Joint Applicants offering this additional rate commitment?**

33 A. The Investor Consortium is planning to invest a significant amount of capital in

1 PSE over the next 10 years, and understands that new utility investment will
2 impact ratepayers. This commitment reflects the Investor Consortium's
3 willingness to provide a discount on its invested capital for a significant period of
4 time in order to demonstrate its commitment to deliver incremental ratepayer
5 benefits as well as capital. We are therefore demonstrating the benefits to PSE's
6 customers from both improved access to capital and a reduction in the cost of
7 capital.

8 **Q. With respect to the Parties' issues regarding protection of PSE customers**
9 **from perceived risks, what ring-fencing commitments have already been**
10 **offered by Joint Applicants?**

11 A. In a joint application in this docket, Joint Applicants have committed to a number
12 of ring-fencing provisions to insulate PSE and ratepayers from risk associated
13 with the Credit Facilities secured at Puget Energy. These ring-fencing
14 commitments include, among others: the filing of a non-consolidation opinion, a
15 minimum PSE common equity ratio, and the addition of an independent "golden
16 share" director at PSE with the ability to unilaterally block a bankruptcy filing.

17 **Q. In response to the opposing testimony, what additional commitments are**
18 **Joint Applicants offering to further ring-fence PSE?**

19 A. The Investor Consortium has carefully examined the issues raised by the Parties
20 and will commit to adopt dividend restrictions at both the PSE and the PE levels.
21 Specifically, Joint Applicants propose the following additional commitments with

1 regard to PSE, which reflect precedent transactions already approved by the
2 Commission:

3 36. PSE shall not be permitted to declare or make any PSE
4 distribution, unless, on the date of such PSE distribution,
5 either:

6 (a) The ratio of PSE EBITDA to PSE interest expense
7 for the most recently ended four fiscal quarter
8 period prior to such date of any PSE distribution is
9 not less than 3.00 to 1.00; or

10 (b) PSE's corporate credit/issuer rating is at least BBB-
11 (or its then equivalent) with Standard & Poor's
12 Ratings Group and Baa3 (or its then equivalent)
13 with Moody's Investors Service, Inc.

14 37. PSE shall not be permitted to declare or make any PSE
15 distribution unless, on the date of such PSE distribution,
16 the PSE common equity ratio is not less than 44%, except
17 to the extent a lower equity ratio is established for
18 ratemaking purposes by the Commission.

19 **Q. Why are Joint Applicants proposing to offer these additional assurances?**

20 A. Joint Applicants have noted the issues raised by the Parties, including perceived
21 risks to PSE from debt leverage at Puget Energy. Several Parties, including
22 ICNU witness Gorman (page 25), Public Counsel witness Hill (page 69) suggest
23 directly or indirectly that dividend restrictions would be an effective means to
24 address this issue.

25 **Q. Are Joint Applicants willing to take additional steps to address the issues**
26 **Parties have raised regarding debt at PE?**

27 A. Yes. We firmly believe that the capital structure that we have proposed is prudent

1 and sustainable for the long term. Consequently, we are prepared to formalize
2 this belief by further committing to a dividend restriction at the Puget Energy
3 level. Such dividend restriction will mean that the Investor Consortium will not
4 be able to receive any dividends from Puget Energy if an interest coverage ratio is
5 not satisfied. The specific commitment we propose is as follows:

6 38. Puget Energy may not declare or make a PE distribution,
7 unless on the date of such PE distribution, the ratio of
8 consolidated EBITDA to consolidated interest expense for
9 the most recently ended four fiscal quarter period prior to
10 such date is equal or greater than 2.00 to 1.00.

11 **Q. Do Joint Applicants offer any changes to the proposed corporate structure to**
12 **address issues regarding perceived risks associated with increased leverage?**

13 A. Yes. ICNU proposed that any entity that owns Puget Energy's common stock
14 should "always be capitalized with 100% common equity unless the Commission
15 approves an alternative capitalization mix." Exhibit No. ___(MPG-1T) at
16 page 25, lines 2-3. In order to address ICNU's concern, Joint Applicants will
17 commit to the insertion of a special purpose entity (SPE) between Puget Energy
18 and its parent company, Puget Intermediate Holdings Inc. ("Puget Intermediate").
19 Such SPE will serve no purpose other than to own all of the common stock of
20 Puget Energy and pledge such capital stock in favor of the secured parties under
21 the Puget Energy credit facilities (and the related interest rate hedging
22 arrangements). The organizational documents of the SPE will prohibit it from
23 incurring any indebtedness or owning any securities other than the common stock
24 of Puget Energy. Please see the Exhibit No. ___(CJL-10) for a revised structure

1 diagram. The board of directors and officers of the SPE will be the same as the
2 board of directors and officers of both Puget Holdings and Puget Intermediate.

3 **V. THE OPPOSING TESTIMONY MISCHARACTERIZES THE**
4 **PROPOSED TRANSACTION AND INCLUDES INFORMATION**
5 **THAT IS NOT RELEVANT TO THE PROPOSED TRANSACTION**

6 **Q. What is the basis for your claim that the Opposing Testimony**
7 **mischaracterizes the Proposed Transaction?**

8 A. The preceding sections of my rebuttal testimony provide several examples, and
9 explain how they mischaracterize the Proposed Transaction. These include (i) the
10 reference to the transaction as a “leveraged buy-out” or a “private equity buy-
11 out”; (ii) incorrect statements regarding the role of the investors in the Investor
12 Consortium and the nature of their financial commitment (*e.g.*, suggesting that
13 they are “limited partners” and that there is a fixed date on which capital invested
14 in Puget Holdings is required to be returned); and (iii) failure to acknowledge that
15 the financial resources of Macquarie and the Investor Consortium supplement –
16 rather than replace – PSE’s existing lender relationships. Similarly, the opposing
17 testimony makes counterintuitive arguments that access to wider sources of
18 capital (*i.e.*, globally rather than nationally) and having more diversity and
19 experience in the ownership structure (*e.g.*, investment in 116 different
20 infrastructure assets) are negative or “bad” aspects of the Proposed Transaction.

1 **Q. What is the basis for your claim that the opposing testimony includes**
2 **information that is not relevant to the Proposed Transaction?**

3 A. A good example is the extensive discussion in the opposing testimony regarding
4 the current credit crisis, the collapse of Bear Stearns, the failure of the auction rate
5 securities market, the discussion of collateralized debt obligations (CDOs), and
6 the subprime mortgage crisis. Public Counsel witness Hill and Staff witnesses
7 Horton and Schmidt all raise these topics in their testimony. These recent
8 headline-grabbing events have little relevance to Macquarie's financial condition
9 and, while they provide some context for the environment in certain sectors of the
10 capital markets, they do not bear on the matters at issue in this proceeding.

11 Exhibit No. ___(CJL-11) provides a more complete rebuttal on these issues. The
12 Macquarie Group has not only survived all phases of the credit cycle, but has
13 announced record profits in each of the past 16 successive years, including
14 through the Asian Financial Crisis and the Dot-Com Crisis, and recently reported
15 a 23% increase in net profit during the current credit crisis. In particular, I would
16 draw attention to the Macquarie Group's full-year earnings announcement of
17 May 20, which highlights Macquarie's strong funding and the absence of the sort
18 of credit exposures that have plagued other institutions.

19 In fact, many of the intervenor witnesses acknowledge the strength of
20 Macquarie's reputation. Staff witness Schmidt, for example, states, "the
21 Macquarie Group has historically done well in infrastructure projects and enjoys a
22 strong reputation for selecting attractive projects. . . . There is little doubt that the

1 Macquarie Group enjoys such a reputational effect.” Exhibit No. ___(RHS-1T) at
2 page 20, lines 12-14 and at page 21, lines 3-4.

3 **Q. Is Public Counsel witness Hill’s description of the management and ancillary**
4 **fees to be earned by Macquarie as a result of the transaction accurate?**
5 **(Exhibit No. ___(SGH-1THC) at page 35, lines 14-18.)**

6 A. No. Public Counsel witness Hill fails to recognize that Macquarie (consisting of
7 Macquarie Infrastructure Partners, Macquarie Capital Group Limited, Macquarie-
8 FSS Infrastructure Trust) represents only approximately 51% of the total
9 shareholder capital contribution of the Consortium. [REDACTED]

10 [REDACTED]
11 [REDACTED]
12 [REDACTED]
13 [REDACTED]
14 [REDACTED]
15 [REDACTED]
16 [REDACTED]
17 [REDACTED]
18 [REDACTED]
19 [REDACTED]
20 [REDACTED]

1 **VI. CONCLUSION**

2 **Q. Please summarize your testimony, Mr. Leslie.**

3 A. The Proposed Transaction will produce substantial benefits for PSE and its
4 customers. Macquarie and the Investor Consortium will provide PSE with
5 improved access to both equity and debt capital, thereby enabling PSE to finance
6 its large capital expenditure requirement on reasonable terms. The Proposed
7 Transaction will also produce \$100 million in tangible, quantifiable savings over
8 ten years, in the form of reduced corporate costs (\$1.2 million annually) and non-
9 offsettable rate credits (\$8.8 million annually) that substantiate our claims
10 regarding improved and additional access to capital. In response to the issues
11 raised by the Parties with respect to the perceived risks associated with the
12 Proposed Transaction, Joint Applicants are offering additional commitments that
13 provide meaningful protection for PSE’s customers from these perceived risks,
14 including dividend restrictions at both Puget Energy and PSE. Combining these
15 commitments with the other new commitments identified by Mr. Reynolds and
16 Mr. Markell, Joint Applicants have provided a firm basis for the Commission to
17 find that approval of the Proposed Transaction would be consistent with the
18 public interest.

19 **Q. Does that conclude your prefiled rebuttal testimony?**

20 A. Yes.