

**EXHIBIT NO. \_\_\_(SPR-1T)**  
**DOCKET NO. UE-07\_\_\_/UG-07\_\_\_**  
**2007 MERGER PROCEEDING**  
**WITNESS: STEPHEN P. REYNOLDS**

**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. UE-07\_\_\_**  
**Docket No. UG-07\_\_\_**

**PREFILED DIRECT TESTIMONY (NONCONFIDENTIAL) OF**  
**STEPHEN P. REYNOLDS**  
**ON BEHALF OF PUGET SOUND ENERGY, INC.**

**DECEMBER 17, 2007**

**PUGET SOUND ENERGY, INC.**

**PREFILED DIRECT TESTIMONY (NONCONFIDENTIAL) OF  
STEPHEN P. REYNOLDS**

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1 **PUGET SOUND ENERGY, INC.**

2 **PREFILED DIRECT TESTIMONY (NONCONFIDENTIAL) OF**  
3 **STEPHEN P. REYNOLDS**

4 **I. INTRODUCTION**

5 **Q. Will you please state your name, business address, and position with Puget**  
6 **Sound Energy, Inc.?**

7 A. My name is Stephen P. Reynolds. My business address is 10885 N.E. Fourth St.,  
8 Suite 1200, Bellevue, Washington 98004. I am employed by Puget Sound  
9 Energy, Inc. (“PSE” or the “Company”) as President and Chief Executive Officer.  
10 I also serve as Chairman of the Board of Directors for both PSE and Puget  
11 Energy, Inc. (“Puget Energy”).

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. \_\_\_(SPR-2).

15 **Q. What are your responsibilities as Chairman, President and Chief Executive**  
16 **Officer of PSE?**

17 A. I have overall management responsibility for PSE and Puget Energy, as well as  
18 their respective Boards of Directors. In consultation with our executive team and

1 Board of Directors, I set the Company's strategic business goals and direct our  
2 efforts to achieve those goals.

3 **Q. Have you previously testified or sponsored testimony before the Commission**  
4 **and other utility commissions?**

5 A. Yes. I testified in the Company's 2004 general rate proceeding, Docket Nos. UE-  
6 040640, *et al.*

7 **Q. What is the purpose of your testimony in this proceeding?**

8 A. The purpose of my testimony is to describe why the acquisition of control of PSE  
9 by Puget Holdings LLC ("Puget Holdings") (the "Proposed Transaction") is in  
10 the best interests of PSE's customers, employees and shareholders. My testimony  
11 identifies the other witnesses testifying on behalf of Puget Holdings and PSE (the  
12 "Joint Applicants"). I also provide an overview of PSE, discuss some of the  
13 current and future challenges that the Company faces, and address the primary  
14 factors driving PSE's decision to enter into the Agreement and Plan of Merger,  
15 dated as of October 25, 2007 ("Merger Agreement"), by and among PSE's Parent,  
16 Puget Energy, and Puget Holdings and its direct and indirect subsidiaries, Puget  
17 Intermediate Holdings Inc. and Puget Merger Sub Inc. ("Merger Sub").

18 **Q. Who are the other witnesses testifying on behalf of the Joint Applicants?**

19 A. The following additional witnesses are testifying on behalf of the Joint  
20 Applicants:

- Christopher J. Leslie, Chief Executive Officer of Macquarie Infrastructure Partners and a manager of Puget Holdings.
- Eric J. Markell, Executive Vice President and Chief Financial Officer of Puget Energy and its wholly owned subsidiary, PSE.

**Q. What position will you hold with PSE after the proposed transaction is closed?**

A. I will continue as the President and Chief Executive Officer of PSE and will continue my service on the Board of Directors of PSE. Additionally, I will serve on the Board of Managers of Puget Holdings.

## **II. OVERVIEW OF PUGET ENERGY AND PSE**

**Q. Please describe Puget Energy.**

A. Puget Energy is an energy services holding company incorporated in the State of Washington. All of its operations are conducted through its subsidiary, PSE.

**Q. Please describe PSE.**

A. PSE is the sole subsidiary of Puget Energy and is the oldest and largest electric and gas utility in the State of Washington. With a 6,000 square-mile service territory stretching across 11 counties principally in the Puget Sound region, PSE serves more than 1 million electric customers and 725,000 natural gas customers.

**Q. Please describe PSE's current business focus.**

A. PSE meets the energy needs of its growing customer base, primarily in Western

1 Washington, through incremental, cost-effective energy conservation,  
2 procurement of sustainable energy resources and far-sighted investment in  
3 energy-delivery infrastructure. PSE employees are dedicated to providing great  
4 customer service to deliver energy that is safe, reliable, reasonably priced and  
5 environmentally responsible.

6 **Q. What are the current challenges facing PSE?**

7 A. As discussed in more detail in Mr. Markell's direct testimony, Exhibit  
8 No. \_\_\_(EMM-1T), PSE faces significant challenges in its efforts to access  
9 capital at a reasonable cost in order to meet the growing energy needs of our  
10 customers, while continuing to provide safe and reliable service to this dynamic  
11 region. Customer growth, the need to expand and replace the Company's aging  
12 power generating and delivery infrastructure, and the need to acquire more  
13 "green" energy, all contribute to the Company's increasing capital needs. Despite  
14 considerable improvement in PSE's financial position since I arrived in 2002, the  
15 Company still has considerable ongoing need to strengthen its balance sheet and  
16 credit metrics to provide the level of service its customers will require in future  
17 years.

18 **III. THE PROPOSED TRANSACTION**

19 **Q. Why did PSE decide to explore opportunities for a merger?**

20 A. As discussed in Mr. Markell's testimony, PSE will need to raise external  
21 financing of \$3.4 billion over the next five years, which will be a substantial

1 challenge in relation to PSE's current book equity, as of September 30, 2007, of  
2 \$2.1 billion. The magnitude of this financing requirement relative to its current  
3 capital base puts the Company and the region at risk.

4 In order to address the significant capital needs the Company faces over the next  
5 several years as discussed above and in Mr. Markell's direct testimony, Puget  
6 Energy and PSE determined that partnering with parties that have access to  
7 significant investment capital and that are focused on long-term investment in the  
8 utility business was the best means to balance the interests of customers,  
9 shareholders and employees.

10 **Q. What process did PSE follow in evaluating opportunities for a business**  
11 **combination?**

12 A. The process followed by PSE in evaluating opportunities for a business  
13 combination is described in the Proxy Statement, which will be filed with the  
14 Securities and Exchange Commission in January 2008.

15 **Q. Why did PSE decide to enter into the Proposed Transaction?**

16 A. The long-term investment goals of the Investor Consortium<sup>1</sup> members who make  
17 up Puget Holdings fit well with the Company's need for significant capital  
18 investment over the foreseeable future. Mr. Leslie's direct testimony, Exhibit  
19 No. \_\_\_(CJL-1T), describes the investment goals of the Investor Consortium in

1 more detail. The Proposed Transaction will support the Company's expected  
2 need to invest nearly \$6 billion over the next six years, helping to insulate the  
3 Company and its customers from volatility in the public equity markets.

4 Partnering with the Investor Consortium, which comprises committed and  
5 experienced long-term infrastructure investors, will provide the best end result for  
6 our customers, our employees and the communities we serve in Western  
7 Washington.

8 Additionally, the members of the Investor Consortium share PSE's vision of a  
9 greener future and will help make it a reality. The Proposed Transaction will  
10 enable PSE to maintain its position as an environmental steward and a long-time  
11 employer and corporate citizen in Washington. This partnership also allows our  
12 customers to continue receiving exceptional service from the same team of high-  
13 quality local PSE employees.

14 **Q. Could PSE continue to access the capital markets as a publicly-traded**  
15 **company as it has in the past?**

16 A. Yes, in its current structure, PSE can obtain capital through the public markets.  
17 But, as described in more detail by Mr. Markell, PSE needs significant amounts  
18 of additional capital over the next several years in order to fulfill its obligation to  
19 customers and to the region.

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<sup>1</sup> Macquarie Infrastructure Partners, Macquarie Capital Group Ltd., Macquarie-FSS Infrastructure Trust, Canada Pension Plan Investment Board, British Columbia Investment Management Corporation and Alberta Investment Management are referred to collectively as the "Investor Consortium."



1 PSE needs to replace and upgrade its aging infrastructure, satisfy customer  
2 reliability requirements, and address increasing regulatory compliance  
3 requirements for reliability, security and other matters. PSE's growing power  
4 supply requirements and renewable energy mandates require PSE to have reliable  
5 access to capital not just for the next couple of years but over the long-term.

6 Timely funding of PSE's capital plan is also critical to serving PSE's customers  
7 safely and reliably. As a publicly-traded entity, the Company is exposed to the  
8 risks and uncertainties of the public equity markets. Additionally, PSE's capital  
9 need is exceptionally large relative to its size. Therefore, the financial  
10 implications on the Company's future earnings and the value of its common stock  
11 will likely make it very difficult to raise equity in the public markets at reasonable  
12 terms because the Company would be competing with other firms for the same  
13 capital.

14 **Q. Did Puget Energy determine whether the marketplace would offer any**  
15 **acquisition proposals more favorable to Puget Energy's shareholders than**  
16 **the Merger Agreement?**

17 A. Yes. Puget Energy made this determination by conducting a "go shop"  
18 solicitation, pursuant to the terms and conditions of the Merger Agreement. Puget  
19 Energy conducted that solicitation during the period from the date of execution of  
20 the Merger Agreement through December 10, 2007.

1 IV. CORPORATE APPROVALS

2 **Q. Have the Boards of the members of the Investor Consortium approved the**  
3 **Proposed Transaction?**

4 A. Yes. The Proposed Transaction has been approved by the Boards of the Investor  
5 Consortium members.

6 **Q. Has Puget Energy's Board of Directors recommended to Puget Energy's**  
7 **shareholders that they approve the Merger Agreement?**

8 A. Yes. Puget Energy's Board of Directors unanimously has determined that the  
9 Proposed Transaction is in the best interests of Puget Energy and has directed that  
10 the Merger Agreement be submitted to Puget Energy's shareholders for approval.

11 **Q. When will Puget Energy's shareholders vote on the Merger Agreement?**

12 A. As will be described in the Proxy that will be filed with the Securities Exchange  
13 Commission in January 2008, a special meeting of Puget Energy's shareholders  
14 will be scheduled for the first quarter of 2008. At that special meeting, Puget  
15 Energy's shareholders will consider and vote upon a proposal to approve the  
16 Proposed Transaction

17 **Q. What percentage of Puget Energy's shareholders must vote to approve the**  
18 **Merger Agreement in order for the Proposed Transaction to be**  
19 **consummated?**

20 A. An affirmative vote of the holders of two-thirds of the outstanding shares of the

1 common stock of Puget Energy is needed to approve the Merger Agreement.

2 **V. THE PROPOSED TRANSACTION BENEFITS**  
3 **CUSTOMERS, EMPLOYEES AND THE PUBLIC**

4 **Q. Will the Proposed Transaction serve the interests of PSE's customers?**

5 A. Yes. As discussed above and in the prefiled direct testimonies of Mr. Markell and  
6 Mr. Leslie, the proposed transaction serves the interests of PSE's customers  
7 because it allows the Company improved access to capital so that the Company  
8 can replace aging energy delivery system infrastructure in order to maintain  
9 reliable electric and gas distribution systems and acquire new electric generating  
10 resources needed to meet the growth in the region.

11 Additionally, the Investor Consortium and PSE are dedicated to continually  
12 improving the quality of service to PSE's residential and business customers. In  
13 this regard, the Investor Consortium has agreed to continue the Service Quality  
14 measures currently in place for PSE that would otherwise expire. Following the  
15 merger, customers can expect that the high level of service and dependability for  
16 which PSE is known will continue.

17 **Q. Does the Proposed Transaction provide any other benefits to PSE's**  
18 **customers?**

19 A. Yes, the Proposed Transaction will help continue to free PSE from its dependence  
20 on the short-term energy market by enabling PSE to finance more of its own  
21 energy resources. Customers will benefit from a more secure energy future that

1 in turn permits a more integrated and state-of-the-art utility system.

2 **Q. Does the Proposed Transaction harm PSE’s customers or the public**  
3 **generally?**

4 A. No, to the contrary, the Proposed Transaction provides significant benefits to  
5 customers, as discussed above. Additionally, the Joint Applicants have made  
6 certain commitments that insulate PSE and its customers from the financial  
7 activities of its affiliates. These commitments are discussed in more detail in the  
8 direct testimonies of Mr. Markell and Mr. Leslie.

9 **Q. Will the Proposed Transaction have an adverse effect on the management**  
10 **and employees of PSE?**

11 A. No. Under the terms of the Merger Agreement, PSE’s headquarters will remain  
12 in Bellevue, and PSE’s current management team will remain in place. The  
13 Investor Consortium has also committed to honor the current collective  
14 bargaining agreements in place for PSE’s represented employees with the  
15 International Brotherhood of Electric Workers, Local 77, and United Association  
16 of Journeymen and Apprentices of the Plumbing and Pipefitting Industry of the  
17 United States and Canada, Local 26 and Local 32. Additionally, the Investor  
18 Consortium has committed to maintain staffing and presence in the communities  
19 in which PSE operates at levels sufficient to maintain the provision of safe and  
20 reliable service and cost-effective operations. The retention of management and  
21 employees is key in the success of the partnership, and the Investor Consortium is

1 committed to PSE's workforce. This continuity in management and staffing will  
2 also benefit customers. This is *not* a merger of two companies in which the  
3 acquiring company seeks to impose its business practices and management style  
4 on the acquired company. As mentioned by Mr. Leslie, PSE is a well managed  
5 and respected energy company. This is why the Consortium approached PSE and  
6 why it does not want to see changes in the way PSE does business in its  
7 communities.

## 8 VI. CONCLUSION

9 **Q. Do you recommend that the Commission approve the Proposed Transaction?**

10 A. Yes. For the reasons stated in my testimony and in the direct testimony of  
11 Mr. Markell and Mr. Leslie, the Proposed Transaction is consistent with the  
12 public interest. I therefore recommend that the Commission approve the  
13 Proposed Transaction.

14 **Q. Does this conclude your direct testimony?**

15 A. Yes, it does.