

1                                   BEFORE THE WASHINGTON STATE  
                                   UTILITIES AND TRANSPORTATION COMMISSION  
 2 In the Matter of the Joint        )  
 Application of                    ) DOCKET U-072375  
 3                                    )  
 PUGET HOLDINGS LLC AND         )  
 4 PUGET SOUND ENERGY, INC.     )  
                                   ) Volume VI  
 5 For an Order Authorizing        ) Pages 398 to 691  
 Proposed Transaction             )  
 6 \_\_\_\_\_)

                                  A hearing in the above matter was held on  
 7 August 25, 2008, from 9:30 a.m. to 5:30 p.m., at 1300  
 South Evergreen Park Drive Southwest, Room 206, Olympia,  
 8 Washington, before Administrative Law Judge DENNIS MOSS  
 and CHAIRMAN MARK H. SIDRAN and COMMISSIONER PATRICK J.  
 9 OSHIE and COMMISSIONER PHILIP B. JONES.

                                  The parties were present as follows:  
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24 Joan E. Kinn, CCR, RPR

25 Court Reporter

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10 WILLIAM N. HORTON  
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24           "Failing Grade" written by Jonathan R. Laing

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7 WILLIAM R. MCKENZIE

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17 116 PSE Response to Public Counsel Data Request  
18 No. 3214

19 117 PSE Response to Public Counsel Data Request  
20 No. 3216

21 118 PSE Response to Public Counsel Data Request  
22 No. 3218

23 119 PSE Response to Public Counsel Data Request  
24 No. 3219 (Confidential)

25

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1 120 PSE Response to Public Counsel Data Request

2 No. 3220

3 121 PSE Response to Public Counsel Data Request

4 No. 3223

5 122 The WACC User's Guide March 2005

6 STEPHEN P. REYNOLDS

7 131 T SPR-1T: Direct Testimony contending proposed

8 transaction is in best interest of customers,

9 employees and shareholders; providing overview

10 of PSE and its challenges; introducing other

11 witnesses

12 132 SPR-2: Witness Qualifications

13 133 T SPR-3T: Rebuttal Testimony providing overview

14 of rebuttal case; identifying 27 additional

15 commitments; offering additional testimony

16 concerning why he believes the proposed

17 transaction is in the public interest.

18 134 SPR-4: Commitments 35 - 61

19 135 SPR-5: Puget Energy News Release Describing

20 Proposed Board of Directors Membership

21 Following Closing

22 CROSS-EXAMINATION EXHIBITS

23 136 HC PSE Response to WUTC Staff Data Request

24 No. 1035 (excerpt) (Highly Confidential)

25

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1 LINCOLN WEBB

2 141T LW-1T: Rebuttal Testimony regarding  
3 transaction structure, duration and governance  
4 model; disputing concerns expressed about  
5 Macquarie

6 142 LW-2: Witness Qualifications

7 143 LW-3: bcIMC Annual Report 2006/2007

8 144 LW-4: Principles for Responsible Investment

9 (An Initiative of the UN Secretary-General  
10 implemented by UNEP Finance Initiative and the  
11 UN Global Compact)

12 CROSS-EXAMINATION EXHIBITS

13 145 PSE Response to Public Counsel Data Request  
14 No. 3238

15 146 PSE Response to Public Counsel Data Request  
16 No. 3240

17 147 PSE Response to Public Counsel Data Request  
18 No. 3242

19 148 PSE Response to Public Counsel Data Request  
20 No. 3244

21 149 PSE Response to Public Counsel Data Request  
22 No. 3246

23 MARK WISEMAN

24 151T MW-1T: Rebuttal Testimony Rebuttal Testimony  
25 regarding transaction structure, duration and

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1 governance model; disputing concerns expressed  
2 about Macquarie Model

3 152 MW-2: Witness Qualifications

4 153 MW-3: CPP Investment Board 2008 Annual Report

5 CROSS-EXAMINATION EXHIBITS

6 154 C PSE Response to Public Counsel Data Request  
7 No. 3225 (Confidential)

8 155 PSE Response to Public Counsel Data Request  
9 No. 3227

10 COMMISSION REGULATORY STAFF

11 KENNETH L. ELGIN

12 161 THC KLE-1THC: Response Testimony summarizing the  
13 proposed transaction; outlining the Joint  
14 Applicant's direct case; presenting Staff's  
15 analysis and Staff's conclusions and  
16 recommendation that the Commission not approve  
17 the sale

18 162 KLE-2: Witness Qualifications

19 163 HC KLE-3: November 2 and 12, 2007 Board of  
20 Directors Meeting "Go-Shop" Update

21 164 KLE-4: Puget Energy Proxy Statement, pp. 48-52

22 165 HC KLE-5HC: PSE Response to Staff DR 1095

23 166 KLE-6: PSE Response to Staff DR 1096

24 167 KLE-7: Macquarie Securities (USA) Inc., Annex

25 C: Group Structures



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1 168C KLE-8C: PSE Response to Staff DR 1085  
2 169 KLE-9: Standard & Poor's Issuances: Top 10  
3 U.S. Electric Utility Credit Issues for 2008  
4 and Beyond; Industry Report Card December 19,  
5 2007 (excerpted); Industry Report Card March  
6 27, 2008 (excerpted)  
7 170 KLE-10: Standard & Poor's Ratings Direct  
8 Summary: Puget Sound Energy September 17, 2007  
9 171 KLE-11: PSE Response to Staff DR 1043, ICNU DR  
10 3.56 and Public Counsel DR 3022  
11 172 KLE-12: S&P Ratings Direct Research Update on  
12 Puget Energy, October 26, 2007; and Moody's  
13 Investors Service Rating Action: PSE, October  
14 29, 2007  
15 173 HC KLE-13HC: PSE Response to Staff DR 1057  
16 174 KLE-14: S&P's Summary and Major Rating  
17 Factors, Puget Energy, March 26, 2008  
18 175 KLE-15: PSE Response to Staff DR 1053  
19 176 T KLE-16T: Cross-Answering Testimony opposing  
20 aspects of NVEC and Public Counsel's cases on  
21 low income, service quality, conservation,  
22 renewable energy and carbon  
23 WILLIAM N. HORTON  
24 181 THC WNH-1THC: Response Testimony concerning  
25 increased financial risks PSE will face as a

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1 result of the proposed transaction and the  
2 potential impact on PSE of adverse  
3 macroeconomic trends in global financial and  
4 energy markets

5 182 WNH-2: Witness Qualifications

6 RONALD H. SCHMIDT

7 191 T RHS-1T: Response Testimony discussing trends  
8 in global capital markets and energy markets  
9 and how these trends affect the utility sector

10 192 RHS-2: Witness Qualifications

11 193 RHS-3: EIA Projections for Crude Oil Price  
12 (Assuming 3% Inflation Rate)

13 194 RHS-4: The Australian, Hedge Funds Gang Up On  
14 Babcock & Brown, June 12, 2008

15 CROSS-EXAMINATION EXHIBITS

16 195 The Wall Street Journal: World Economy Shows  
17 New Strain (August 15, 2008)

18 196 The Wall Street Journal: Economists Expect  
19 2008's Second Half To Be Worse Than First  
20 (August 11, 2008)

21 197 The Wall Street Journal: Signs Say Economic  
22 Recovery Isn't Here (August 11, 2008)

23 198 IMF Survey Magazine: Year After Subprime  
24 Crash, Risks Remain Elevated, Says IMF (July  
25 28, 2008)

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1 199 The Wall Street Journal: Fannie, Freddie Drag  
2 Down Stocks (August 18, 2008)

3 200 The Economist: A series of articles on the  
4 crisis gripping the world economy and global  
5 markers starts where it all began--with  
6 America's deeply flawed system of housing  
7 finance (July 17, 2008)

8 235 The Economist: The financial crisis claims  
9 another two victims--and once again the  
10 taxpayer picks up the pieces (July 17, 2008)

11 236 The Wall Street Journal, :Mortgage-Market  
12 Trouble Reaches Big Credit Unions (August 11,  
13 2008)

14 237 The Wall Street Journal: Merrill Aims to Raise  
15 Billions More (July 29, 2008)

16 238 The Economist Newspaper and The Economist  
17 Group, Fear of failure (July 17, 2008)

18 239 The Wall Street Journal: Shaking Up the  
19 'Macquarie Model' (August 22, 2008)

20 NWECC

21 ANN ENGLISH GRAVATT

22 201 T AEG-1T: Response Testimony critiquing Joint  
23 Applicants renewable energy commitments;  
24 relating her experience with other mergers and  
25 acquisitions in the Pacific Northwest,

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1 including MEHC's acquisition of PacifiCorp;  
2 summarizing renewable energy commitments by  
3 applicants in those proceedings  
4 202 AEG-2: Witness Qualifications  
5 203 AEG-3: Texas Pacific Group's Application to  
6 Acquire Portland General Electric in Oregon  
7 PUC Docket UM 1121 (one-page excerpt)  
8 204 AEG-4: Supplemental Direct Testimony of Kelvin  
9 L. Davis on Behalf of Applicants in Oregon PUC  
10 Docket UM 1121 (two-page excerpt)  
11 205 AEG-5: Rebuttal Testimony of Kelvin L. Davis  
12 on Behalf of Applicants in Oregon PUC Docket  
13 UM 1121 (one-page excerpt)  
14 206 AEG-6: Joint Application for MidAmerican  
15 Energy Holdings Company To Acquire PacifiCorp  
16 in Oregon PUC Docket UM 1209 (two-page  
17 excerpt)  
18 207 AEG-7: Exhibit 1 of Settlement Agreement in  
19 MidAmerican Acquisition of PacifiCorp in  
20 Oregon PUC Docket UM 1209 (eight pages  
21 excerpted from various parts of exhibit)  
22 208 AEG-8: Exhibit A of Babcock &  
23 Brown/NorthWestern Energy's Restructured  
24 Proposal, Montana PSC Docket D2006.6.82  
25

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1 NANCY ELLEN HIRSH

2 211 T NEH-1T: Response Testimony concerning  
3 commitments made in the areas of energy  
4 efficiency, renewable energy resources,  
5 greenhouse gas emissions, and low-income  
6 energy services

7 212 NEH-2: Response to NWECC DR 1.04

8 213 NEH-3: Response to NWECC DR 1.02

9 214 NEH-4: Highlights of State Laws and Policies  
10 Regarding Clean and Affordable Energy Services

11 215 NEH-5: PSE Energy Efficiency Summary

12 216 NEH-6: Response to NWECC DR 1.07

13 217 NEH-7: PSE Renewable Energy Summary

14 218 NEH-8: Response to NWECC DR 1.06

15 219 NEH-9: Response to NWECC DR 1.03

16 220 NEH-10: Response to NWECC DR 2.13

17 233 NEH-11: PSE Greenhouse Gas Policy

18 234 NEH-12: Response to NWECC DR 1.08

19 MICHAEL P. GORMAN

20 221 T MPG-1T: Response Testimony critiquing the  
21 proposed transaction and opposing its  
22 approval; recommending modifications and  
23 conditions to the proposed transaction if it  
24 is approved

25 222 MPG-2: Witness Qualifications

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1 223 MPG-3: ICNU's Proposed List of Additional  
2 Conditions  
3 224 MPG-4: Response to ICNU DR 3.40  
4 225 MPG-5: S&P's Key Credit Factors, September 14,  
5 2006  
6 226 MPG-6: S&P's Corporate Ratings Criteria 2006  
7 227 MPG-7: Excerpts of Direct Testimony of Brian  
8 B. Bird In FERC Docket ER-07-46-000  
9 228 MPG-8: S&P's Ratings Direct Research Update  
10 October 26, 2007  
11 229 MPG-9: Moody's Investors Service Ratings  
12 Action: PSE, Inc. October 29, 2007  
13 230 MPG-10 Standard and Poor's Ratings Direct  
14 Research Update, May 29, 2007  
15 CROSS-EXAMINATION EXHIBITS - (not sponsored but  
16 identified as Donald E. Gaines)  
17 231 PSE Response to WUTC Staff Data Request No.  
18 189  
19 CROSS-EXAMINATION EXHIBITS - (not sponsored but  
20 identified as John H. Story)  
21 232 PSE Response to Public Counsel Data Request  
22 No. 583  
23 PUBLIC COUNSEL  
24 BARBARA R. ALEXANDER  
25 241 T BRA-1T: Response Testimony concerning

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1           addressing service quality commitments offered  
2           by Joint Applicants; risks to service quality  
3           from proposed transaction; proposed conditions  
4           for PSE service quality and customer service;  
5           proposed conditions for PSE low-income  
6           programs

7    242       BRA-2: Witness Qualifications

8    243       BRA-3: PSE--Service Quality Index Performance

9    STEPHEN G. HILL

10   251 THC    SGH-1THC: Response Testimony summarizing  
11           structure of equity buy-outs of public  
12           utilities; discussing "Macquarie Model";  
13           providing certain details of proposed  
14           transaction and underlying financial  
15           projections; discussing bond rating agencies'  
16           review and analyses of transaction;  
17           ring-fencing

18   252       SGH-2: Witness Qualifications

19   253       SGH-3: NRRI Publication by Stephen G. Hill,  
20           December 2007: Private Equity Buyouts of  
21           Public Utilities: Preparation for Regulators

22   254       SGH-4: Fortune Magazine, Would You Buy a  
23           Bridge from this Man? By Bethany McLean,  
24           October 2, 2007

25   255       SGH-5: RiskMetrics Group, April 2008,

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1                   Infrastructure Funds: Managing, Financing and  
2                   Accounting-In Whose Interests?  
3    256            SGH-6: Post-transaction Corporate Structure  
4                   (Organizational Chart)  
5    257 HC        SGH-7HC: Transaction Financing Chart  
6    258 HC        SGH-8HC: Puget Acquisition: Revenue Volatility  
7                   Graph  
8    259 HC        SGH-9HC: Puget Acquisition; Calculation of  
9                   Debt/Capital Based on Macquarie Projections  
10   260            SGH-10: Monetary Compensation Resulting from  
11                   Merger  
12   261            SGH-11THC: Response Testimony Concerning  
13                   Settlement Stipulation  
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1 P R O C E E D I N G S

2 JUDGE MOSS: Good morning everyone. My name  
3 is Dennis Moss, I am an Administrative Law Judge  
4 appointed by the Washington Utilities and Transportation  
5 Commission to preside over our hearing proceedings that  
6 are captioned In The Matter of The Joint Application of  
7 Puget Holdings LLC and Puget Sound Energy, Inc., for an  
8 Order Authorizing Proposed Transaction in Docket Number  
9 U-072375. The Commissioners are sitting in this  
10 proceeding, to my immediate right Chairman Mark Sidran,  
11 to his right Commissioner Patrick Oshie, and to his  
12 right Commissioner Philip Jones. We will shortly launch  
13 into the portion of our hearing in which we will engage  
14 counsel and various witnesses, and I will take the  
15 appearances of counsel.

16 But before we get into that, I have a few  
17 words I want to say about our process. And I'm going to  
18 say a bit more today than I typically do. Although  
19 we've had a number of proceedings such as this one over  
20 the past several years, unlike prior proceedings such as  
21 the Scottish Power acquisition of PacifiCorp in 1999 and  
22 the subsequent acquisition of PacifiCorp by the  
23 MidAmerica Energy Holdings Company and I think that was  
24 in 2006, this proceeding has attracted a tremendous  
25 amount of public attention and attention from the press.

1 Our hearing room is quite full today, and I understand  
2 there are quite a few people listening in on our  
3 teleconference bridge line. And so for those reasons,  
4 I'm going to take a little time this morning to explain  
5 how the Commission reviews an application such as this  
6 one asking for approval of the acquisition of PSE by  
7 Puget Holdings LLC.

8 By way of context, the process by which a  
9 matter such as this comes before and is considered by  
10 the Commission is dictated by various statutes and  
11 rules. Chapter 80.12 of the Revised Code of Washington  
12 is entitled Transfers of Property. It requires  
13 Commission approval in circumstances such as this where  
14 the owners of a company the Commission regulates agree  
15 to transfer ownership to new owners. In this case the  
16 owners of PSE, that is the shareholders of Puget Energy  
17 which owns PSE, have agreed to sell the Company to new  
18 owners, a group of six investment companies that formed  
19 a new company called Puget Holdings LLC expressly for  
20 the purpose of acquiring through subsidiaries 100% of  
21 the stock of Puget Energy Inc., which currently owns  
22 100% of Puget Sound Energy, the utility.

23 The Commission's rules at Chapter 480-143 of  
24 the Washington Administrative Code state the standard by  
25 which the Commission will judge the application in this

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1 way, and I quote:

2 If upon examination of any application  
3 and accompanying exhibits or upon a  
4 hearing concerning the same the  
5 Commission finds the proposed  
6 transaction is not consistent with the  
7 public interest, it shall deny the  
8 application.

9 Put another way, the Commission needs to  
10 determine whether the proposed transaction harms the  
11 public interest. If so and if conditions can not be  
12 imposed on the transaction that remove the harmful  
13 aspects of the proposal, then the Commission must deny  
14 the application. If on the other hand the Commission  
15 finds there is no harm to the public interest or that  
16 conditions can be imposed on the transaction to protect  
17 the public interest from harm, then the Commission will  
18 approve the application.

19 The manner in which the Commission makes  
20 these determinations is also spelled out in statutes and  
21 rules, specifically the Administrative Procedure Act,  
22 which is Chapter 34.05 of the Revised Code of  
23 Washington, and the Commission's own procedural rules at  
24 Chapter 480-107 of the Washington Administrative Code.  
25 In general the Commission's jurisdiction and

0441

1 decision-making process is very much like what happens  
2 in a court of law. The Commissioners who themselves sit  
3 as judges in these types of proceedings appoint an  
4 administrative law judge, in this case me, to make sure  
5 the process as spelled out by the statutes and the rules  
6 are strictly enforced. The Commission ultimately makes  
7 its decision based on a formal record of evidence, much  
8 of which has already been prefiled in this case in the  
9 form of 200 prefiled exhibits, nearly 800 pages of  
10 prefiled testimony, and more than 3,000 public comments  
11 the Commission has received in writing, and in addition  
12 many, many oral comments received in 3 public comment  
13 hearings the Commission conducted in various parts of  
14 the company's service territory.

15           Now having mentioned that extensive amount of  
16 prefiled evidence in the case, there's another topic I  
17 need to talk about because it has implications for our  
18 hearing proceedings today, and that's the subject of  
19 confidentiality. The Washington legislature recognized  
20 years ago that it's necessary for the Commission to have  
21 access to a lot of information that is sensitive in one  
22 way or another as it conducts its responsibility in  
23 terms of economic regulation of public utilities.  
24 Accordingly the legislature passed into law a statute,  
25 Revised Code of Washington 80.04.095, and I want to read

0442

1 and paraphrase a little bit that statute to you so that  
2 you understand what the legislature prescribed. And I  
3 will set the context for that by reminding everyone,  
4 you're probably familiar with, Washington does have a  
5 Public Records Act, which means that documents that are  
6 filed at the Commission in general are available to the  
7 public for review. However, records subject to the  
8 Public Records Act the legislature says, and I'm  
9 quoting:

10 Filed with the Commission or the  
11 Attorney General from any person which  
12 contain valuable commercial information  
13 including trade secrets or confidential  
14 marketing, cost, or financial  
15 information or customer specific usage  
16 and network configuration and design  
17 information shall not be subject to  
18 inspection or copying under the Public  
19 Records Act unless and until notice to  
20 the person directly affected by  
21 disclosure has been given, and if within  
22 ten days of that notice the person may  
23 obtain a superior court order that will  
24 maintain the confidentiality of the  
25 records that have been requested by a

0443

1                   member of the public.

2                   The court then determines whether the records  
3 are confidential and not subject to inspection and  
4 copying, and it does so on the basis of the question of  
5 whether the disclosure would result in private loss,  
6 including a loss of competitive advantage. When  
7 providing information to the Commission or the Attorney  
8 General, a person or a company in this instance will  
9 designate the records or portions of records that  
10 contain valuable commercial information. The final  
11 sentence of the statute is important to us this morning.

12                   Nothing in this section shall prevent  
13 the use of protective orders by the  
14 Commission governing disclosure of  
15 proprietary or confidential information  
16 in contested proceedings.

17                   The Commission does in fact routinely use  
18 protective orders, and it has entered a protective order  
19 in this case. The reason we do that is to promote the  
20 rapid and free exchange of information among all of the  
21 parties to the proceeding. By the use of a protective  
22 order, we can provide protections for documents that  
23 limit their disclosure to all of the parties in the  
24 proceeding. So they're not publicly disclosed, but all  
25 of the parties have full access to the documents. That

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1 way the Company can provide them quickly when it is  
2 requested to do so during the discovery process.

3 Now in this case, the joint applicants have  
4 been asked many questions, I don't know how many,  
5 hundreds I'm sure, and have provided a great deal of  
6 information. They have designated a fair amount of that  
7 information as confidential under the protective order  
8 and under the provisions of the statute that I read you  
9 a few minutes ago. In part because they are required to  
10 respond quickly to these requests for information and  
11 the volume of the information is very great, the joint  
12 applicants, as other parties have done in the past, have  
13 perhaps overdesignated some information as confidential  
14 in this proceeding. For example, entire documents may  
15 be designated as confidential when in fact only portions  
16 of the contents are sensitive. And so this is a problem  
17 that we face in terms of overdesignation, but it is a  
18 practical problem to which there are solutions.

19 Specifically parties to the proceedings have  
20 the right both under the statute I read you and under  
21 the terms of the protective orders in this proceeding,  
22 parties have the right to challenge the designation of a  
23 document or part of a document as confidential. The  
24 opportunity to make such challenges has been available  
25 to the parties since the outset of this proceeding. No

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1 party, however, filed a challenge to the designation of  
2 any information as confidential until last Thursday  
3 afternoon. On that date, Public Counsel filed a motion  
4 challenging confidentiality of certain materials  
5 provided in discovery by joint applicants. Now Public  
6 Counsel acknowledges in his motion that the timing is  
7 such that he is "not requesting that the motion be  
8 resolved prior to the hearings and is prepared to  
9 proceed with confidential examination on the protected  
10 material". Furthermore, Public Counsel "believes it  
11 would be appropriate for the Commission to extend the  
12 time for response to the motion until after the hearings  
13 are concluded". We agree with Public Counsel, it is not  
14 practical to try to resolve his challenge to  
15 confidentiality before or during this hearing.

16           Moreover, there's some question as to whether  
17 we have jurisdiction to resolve the matter at this time  
18 because the matter is pending with respect to the  
19 identical information before the Thurston County  
20 Superior Court pursuant to a public records action that  
21 has been filed there. It was filed there about three  
22 weeks ago at the end of July. And unless and until the  
23 Court refers the question to the Commission, the  
24 question of whether some or all of the challenged  
25 information for confidential treatment appears to rest



0446

1 with the Court.

2           In addition to the opportunity parties have  
3 to challenge a designation of information as  
4 confidential, they may also ask a party to waive its  
5 claim of confidentiality when it appears the claim is  
6 overbroad. The Commissioners can do the same thing.  
7 And, in fact, today when the Commissioners are asking  
8 their questions, there may be occasions when they will  
9 ask the parties if the information they wish to inquire  
10 about needs to maintain the cloak of confidentiality.  
11 And if not, then we'll be able to disclose that on the  
12 record. And if so, we'll handle that in a different  
13 way.

14           The parties understand that the Commission  
15 does not take the question of confidentiality lightly,  
16 respecting the need for it when it's narrowly applied,  
17 but expecting a willingness to reconsider when it is  
18 more broadly asserted to encompass for example entire  
19 documents.

20           Regardless of the outcome in the Superior  
21 Court or during this hearing when we ask for waivers of  
22 confidentiality claims, it's important for everyone to  
23 recognize that all the parties including Public Counsel  
24 have had full access to all of this information from the  
25 moment it was provided and can use it if they wish in

0447

1 their testimony, their exhibits, and their briefs.  
2 Indeed Public Counsel has done just that, and his  
3 principal witness's testimony was as a result filed on  
4 June 18, 2008, as a confidential document.

5 Now with that context hopefully in mind, and  
6 I'm going to return in a moment to why all this  
7 discussion about confidentiality was important in terms  
8 of our process today, with that context in mind let me  
9 take a few more minutes and tell you what process has  
10 occurred so far in this proceeding, what process will be  
11 conducted over the next few days in this hearing room,  
12 and what process will follow.

13 Puget Sound Energy and Puget Holdings filed  
14 their application in this proceeding on December 17th,  
15 2007. Along with that they filed direct testimony, we  
16 call it prefiled testimony, by three witnesses.  
17 Following that there was a period of what we call  
18 discovery in which all the parties are allowed to ask  
19 each other questions. Most of that is questions to the  
20 joint applicants to which they must respond within ten  
21 business days unless we shorten that period, which  
22 frankly I don't recall whether we did that at some point  
23 or not. We probably -- I'm getting different nods, but  
24 in any event ten days is pretty quick turn around. On  
25 June 18th, 2008, the various parties including the

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1 Industrial Customers of Northwest Utilities, the  
2 Northwest Energy Coalition, the Energy Project, Staff,  
3 and Public Counsel filed what we call response  
4 testimony. In this instance the response testimony was  
5 objecting to various aspects of the proposed  
6 transaction. The applicants get the last word under the  
7 Administrative Procedure Act and our rules, and so they  
8 filed rebuttal testimony which is in response to the  
9 response testimony. In other words, they got to answer  
10 what their opponents had said in the response testimony,  
11 and that was on July 2nd, 2008.

12 I mentioned before during the course of all  
13 this time we held three public comment hearings around  
14 the state in various parts of Puget Sound Energy's  
15 service territory, and the Commissioners were present  
16 for those hearings and heard a lot of comments from  
17 members of the public. We've also received many written  
18 comments from the public. Those are part of our files  
19 and will ultimately become part of the record in this  
20 proceeding when Public Counsel offers them into  
21 evidence.

22 While all of this was going on at the  
23 Commission, on the Commission side the parties  
24 themselves engaged in settlement discussions seeking to  
25 resolve some of their differences if they could do so,

0449

1 and indeed a settlement stipulation was agreed to by all  
2 of the parties that filed testimony except Public  
3 Counsel and also agreed to by two parties that did not  
4 file testimony, the Northwest Industrial Gas Users and  
5 the Kroger Company, on July 23rd, 2008. You will hear  
6 me and perhaps others refer to these parties who signed  
7 the settlement stipulation as the joint parties from  
8 time to time today.

9           Unlike what we do in some cases, we decided  
10 in this case because of its significance that we would  
11 allow three rounds of testimony in addition to those  
12 that had previously been filed by the parties. So on  
13 July 29th we had prefiled testimony by the joint parties  
14 in support of their settlement stipulation. On August  
15 5th we had prefiled response testimony by Public  
16 Counsel, who remains opposed to the settlement  
17 stipulation. And then again we allowed the joint  
18 parties to have the final word through rebuttal  
19 testimony filed on August 12th, 2008. In addition to  
20 that, the Commission itself issued what we call Bench  
21 Requests. Those are questions from the Bench that will  
22 help us understand the transaction and understand facts  
23 that are important to the Commission's determination of  
24 this matter. So we've issued 17 or 18 of those, the  
25 parties have responded to those. As I mentioned, we

0450

1 have many, many pages of exhibits, prefiled testimony,  
2 and public comments.

3 Our process starting today is our hearing  
4 process on the settlement stipulation. We're asked to  
5 consider whether the settlement stipulation establishes  
6 a set of conditions so that the acquisition of PSE by  
7 new owners who call themselves Puget Holdings LLC does  
8 not harm the public interest. That's basically the  
9 question is whether that settlement stipulation offers  
10 up sufficient conditions and protections to meet the  
11 standard that I discussed with you earlier under the  
12 Commission's rules and statutes.

13 The basis for the Commissioners' decision,  
14 for the Commission's decision, will be the record  
15 produced through this hearing. Part of that I expect  
16 will be stipulated, we'll call that the agreed record,  
17 and part of that may be disputed, there may be  
18 objections to various evidence that parties propose to  
19 present. I will rule on those objections, and the  
20 testimony or exhibit or whatever it is will either come  
21 in or it won't depending on the rules of evidence  
22 largely.

23 We will have a panel of witnesses this  
24 morning who are sponsoring the settlement stipulation,  
25 and they will be questioned by the Commissioners. After

0451

1 that, I will allow questions from others who may have  
2 follow up to responses they heard from the  
3 Commissioners' round. And then we'll have  
4 cross-examination of individual witnesses by Public  
5 Counsel. Public Counsel estimates 10 to 12 hours of  
6 total cross-examination, so we're looking at 2 to 2 1/2  
7 days of hearing to conduct that part of our process.

8           And this brings me back to the point of  
9 confidentiality. Public Counsel let me know a few days  
10 ago that he does expect to have to use confidential and  
11 highly confidential information in his examination of  
12 various witnesses. That has implications in terms of  
13 our hearing, because the only people in this hearing  
14 room who will be allowed to be in this hearing room  
15 during those portions of the testimony are those who  
16 have executed the appropriate forms that are included as  
17 part of the protective order. That means in other words  
18 we will have to have probably closed sessions for the  
19 hearing. But we have investigated the matter, because  
20 we know that only certain questions and certain answers  
21 will need to be protected from disclosure, we have  
22 investigated the capabilities of our technology, and so  
23 we have a plan that we're going to implement that we  
24 hope will allow us to keep the minimum amount of this  
25 hearing confidential.

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1                   And what we're going to do is there's another  
2 room just behind this one, Room 207, and if we have to  
3 close the hearing room, that room is connected with  
4 speakers, with a system, this PA system, and what we're  
5 going to do is we're going to ask people who are not  
6 privileged to hear the confidential and highly  
7 confidential information to go to Room 207. Sitting at  
8 the back of the hearing room is a member of our Consumer  
9 Affairs Staff, Gail Griffin-Wallace, if you will just  
10 raise your hand, Gail. She is here to assist any of you  
11 who need to remove yourselves to Room 207 where you will  
12 be able to listen to our proceedings over the PA system  
13 unless and until I get to something where we have to  
14 turn the speaker system off in that room, and I can do  
15 that from the Bench, or at least so I am informed. So  
16 that's what we're going to try. The same thing is true  
17 with respect to the conference bridge line, except there  
18 I will be cutting off everybody, whether they're  
19 privileged to hear the information or not, because I  
20 only have one switch. So I will turn that off, I will  
21 mute the send on that. So that's how we're going to try  
22 to do it. Now if that doesn't work out, if that proves  
23 to be too logistically cumbersome so that it's  
24 threatening the efficiency of our hearing and our  
25 ability to conduct it in the manner it needs to be

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1 conducted, then we will have to resort to fully closed  
2 sessions. We don't want to do that, but that may be the  
3 only option we have.

4 All right, mercifully I'm sure from your  
5 standpoint, that brings me close to the end of what I  
6 have to say. I just want to tell you there are a couple  
7 more steps after this hearing, and that is that on  
8 September 19th, 2008, the parties will have an  
9 opportunity to file briefs, that is to say written  
10 arguments concerning their respective positions that the  
11 settlement stipulation should on the one hand be  
12 accepted, adopted, and approved by the Commission, and  
13 on the other hand that it should not. And then  
14 following the receipt of briefs, the Commission will  
15 enter into its deliberations and will render a written  
16 decision in due course.

17 Now with all of that said, we will get back  
18 to the parties or for the first time get to the parties,  
19 and I will start by taking your appearances, and we'll  
20 take short form of appearances this morning since we  
21 have your appearances previously in the record, and  
22 we'll start with the joint applicants.

23 MS. CARSON: Good morning, I'm Sheree Strom  
24 Carson representing the joint applicants, PSE and Puget  
25 Holdings, and also representing is Jamie Van Nostrand.



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1                   MR. JOHNSON: David Johnson representing the  
2 Northwest Energy Coalition.

3                   MR. STOKES: Chad Stokes from the Cable  
4 Huston law firm representing Northwest Natural Gas  
5 Users.

6                   MS. DAVISON: Melinda Davison on behalf of  
7 the Industrial Customers of Northwest Utilities.

8                   JUDGE MOSS: Mr. Roseman.

9                   MR. ROSEMAN: Ronald Roseman representing the  
10 Energy Project.

11                   MR. FFITCH: Simon ffitch for Public Counsel.

12                   MR. CEDARBAUM: Robert Cedarbaum for  
13 Commission Staff. Your Honor, do you need my long form  
14 appearance since this is my first --

15                   JUDGE MOSS: No, we have previous appearance  
16 by the Attorney General's Office on behalf of the Staff,  
17 so that would be sufficient.

18                   MR. CEDARBAUM: If I may, can I ask one  
19 question about your process explanation?

20                   JUDGE MOSS: Sure.

21                   MR. CEDARBAUM: Mr. Horton, who is testifying  
22 for Commission Staff, is on the bridge line. He may be  
23 involved in discussions of confidential information.  
24 You indicated that you were going to shut the bridge  
25 line off completely --

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1                   JUDGE MOSS: I think we -- do we have that  
2 covered, Mr. ffitch, or is that just Mr. Pettit that we  
3 discussed earlier this morning?

4                   MR. FFITCH: Your Honor, we are not going to  
5 ask Mr. Horton to talk about confidential information  
6 publicly. He may be looking at a confidential exhibit,  
7 but we're going to avoid --

8                   JUDGE MOSS: All right, Mr. ffitch and I had  
9 a brief discussion off the record this morning about  
10 this problem. I was hoping that I was recalling it  
11 correctly that he's going to be able to conduct his  
12 questions in a fashion that will not require us to go  
13 into confidential session.

14                   MR. CEDARBAUM: That helps with that aspect  
15 of the concern, but my understanding is that the  
16 Commissioners have questions this morning as well, and  
17 that may lead also into confidential and highly  
18 confidential information. I don't know, but looking at  
19 the Bench Requests there's blue and yellow paper.

20                   JUDGE MOSS: The Commissioners are sensitive  
21 to the issue, and I'm sure they can ask their questions  
22 of Mr. Horton to the extent necessary in such a way as  
23 to not implicate the confidential information.

24                   MR. CEDARBAUM: Thank you.

25                   JUDGE MOSS: Thank you.

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1 All right, now are there any other counsel in  
2 the hearing room who wish to enter an appearance this  
3 morning or other representatives of parties?

4 Are there any counsel or other  
5 representatives of parties on the conference bridge line  
6 who wish to enter their appearance this morning?

7 All right, apparently not.

8 All right, we had an extensive discussion of  
9 process, probably for more extensive than anyone wanted  
10 to hear but I felt necessary. It brings me then to the  
11 question of whether there's anything preliminary from  
12 the parties, and I understand from informal discussions  
13 I had with several parties off the record this morning  
14 that there are a couple of matters concerning exhibits  
15 that we need to take up in terms of some updated  
16 information.

17 Ms. Carson, you indicated to me you had an  
18 updated response to one of our Bench Requests.

19 MS. CARSON: We do, Your Honor, we have an  
20 updated response to Bench Request 8, which is Exhibit  
21 408, that we would like to file.

22 JUDGE MOSS: All right, do you have copies  
23 for me for the Bench?

24 MS. CARSON: (Complies.)

25 JUDGE MOSS: And have these been furnished to

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1 the parties?

2 MS. CARSON: They are now being furnished to  
3 the parties.

4 JUDGE MOSS: All right, very well.

5 Do you have any others?

6 MS. CARSON: Yes, regarding Bench Request 12,  
7 Exhibit 412C, we filed a supplemental and revised  
8 response, it's not listed, and perhaps it's listed on  
9 the new exhibit list. The exhibit list we received  
10 Friday did not list it as a supplemental and revised  
11 response.

12 JUDGE MOSS: Right, I probably would not have  
13 bothered to identify it that way, but we have it.

14 MS. CARSON: All right.

15 JUDGE MOSS: Anything else?

16 MS. CARSON: There is one other exhibit,  
17 Exhibit 55, that failed to mark confidential  
18 information, and so we wanted to make sure that a  
19 correct version of that is entered into the record.

20 JUDGE MOSS: And that is an exhibit for  
21 Mr. Leslie that Public Counsel has proposed for  
22 cross-examination.

23 MS. CARSON: That's correct.

24 JUDGE MOSS: All right, the version I have is  
25 not confidential. What I have is a two-page document on

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1 white paper, it's a response to Bench Request or Data  
2 Request 3173.

3 MS. CARSON: It should be marked  
4 confidential.

5 JUDGE MOSS: It should have been marked  
6 confidential.

7 MS. CARSON: It should be marked highly  
8 confidential.

9 JUDGE MOSS: I see. For whatever reason I  
10 don't have it that way, but we will substitute this.

11 MS. CARSON: So that is a public and highly  
12 confidential version.

13 JUDGE MOSS: Okay, so you've given me both  
14 the redacted and the confidential versions.

15 MS. CARSON: Yes.

16 JUDGE MOSS: I'm distributing the highly  
17 confidential versions, and we will amend the exhibit  
18 list by including the highly confidential designation on  
19 that exhibit, and I will substitute what you have handed  
20 me for what is in my own notebook.

21 All right, anything else?

22 MS. CARSON: No, Your Honor.

23 JUDGE MOSS: All right, thank you.

24 Mr. ffitich, you indicated to me earlier that  
25 you had some I believe updated exhibit matter.

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1                   MR. FFITCH: Your Honor, we do have a list.  
2 All of these exhibits relate to later witnesses, and to  
3 avoid sort of a long walk through of these, we would be  
4 willing to wait later until a break. They are for  
5 Mr. Leslie, Mr. Pettit, Mr. Schmidt, we could take these  
6 up later, Your Honor.

7                   JUDGE MOSS: We'll take them up with the  
8 individual witnesses to avoid confusion. I will ask you  
9 during the break, however, if you can get those  
10 distributed to parties and to the Bench, then we'll get  
11 everything organized, and then we'll take up the matter  
12 on the record at the appropriate time with each witness.

13                   MR. FFITCH: All right, thank you, Your  
14 Honor.

15                   JUDGE MOSS: Let's do that.

16                   All right, anything else preliminary?

17                   All right, with that then we want to call and  
18 swear our witness panel, and I think how many witnesses  
19 do we have on the panel?

20                   MS. CARSON: Eight.

21                   JUDGE MOSS: Eight, well, then counsel are  
22 going to have to abandon their seats, because I want the  
23 panel sitting up here where they can talk directly with  
24 the Commissioners, so if you all will move back to the  
25 front row there.

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1 MS. CARSON: Your Honor, I just wanted to  
2 remind you also that there are others who are not on the  
3 panel who are in the room and available to answer  
4 questions.

5 JUDGE MOSS: That's right, I'm just about to  
6 get to that point. What I'm going to do this morning,  
7 and I can go ahead and talk about this while people are  
8 rearranging themselves, I'm going to swear the panel, at  
9 the same time I'm going to swear other witnesses in this  
10 proceeding. And the reason I'm going to do that is that  
11 the Commissioners will have a number of questions for  
12 the panel, and it may be that the panelists are the best  
13 suited to answer those questions, or it may be that  
14 there is another witness in the hearing who is better  
15 suited to answer the question or can provide some  
16 illumination that a member of the panel can not. So I  
17 will swear those witnesses, and I will rely on the  
18 panelists or the various counsel to point out those  
19 occasions if they occur when some other witness in our  
20 hearing should give us a response. And when that  
21 occurs, then we'll have that witness conveniently sworn  
22 and be able to take that testimony. This applies as  
23 well to those of you who are on the conference bridge  
24 line, those witnesses on the conference bridge line,  
25 whether or not you're on the panel, I will ask you to

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1 observe the solemnity of the oath that we take in these  
2 proceedings. Though you're not present here and though  
3 we don't have a video connection, I will nevertheless  
4 ask that you like the other witnesses in this proceeding  
5 whether sitting out there in the gallery or sitting here  
6 at the tables, I would ask you to please rise at this  
7 time and raise your right hands.

8 (Witnesses sworn.)

9 JUDGE MOSS: Thank you, you may be seated.

10 Now I've lost counsel, of course, but you're  
11 sitting right there. Let me ask, Ms. Carson, I'm going  
12 to direct things to you, other counsel of course who are  
13 sponsoring witnesses here are free to respond to me at  
14 times as well, but I will direct my questions to you  
15 since you're representing the joint applicants. Do the  
16 panelists or does counsel for the panelists wish to make  
17 any sort of an opening statement this morning?

18 MS. CARSON: Mr. Leslie is prepared to make  
19 an opening statement.

20 JUDGE MOSS: Okay.

21 MS. CARSON: And I have inquired of other  
22 counsel if their witnesses are wanting to make an  
23 opening statement, and no one else has indicated they  
24 want to.

25 JUDGE MOSS: Okay. And since you didn't have



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1 a microphone, for those on the bridge line, Ms. Carson  
2 has indicated that Mr. Leslie will make an opening  
3 statement for the panel, that others have been consulted  
4 and have declined the opportunity to do so, so we'll  
5 hear from Mr. Leslie.

6 MR. LESLIE: Thank you, Your Honor.

7 JUDGE MOSS: Go ahead.

8 MR. LESLIE: Good morning, everyone.

9 On behalf of the investors in Puget Holdings  
10 LLC, I would like to thank the Commission for this  
11 opportunity to discuss why the settlement among the  
12 Commission Staff, Puget Holdings, Puget Sound Energy,  
13 and several other interested parties in connection with  
14 the proposed acquisition of Puget Energy is in the  
15 public interest.

16 First a personal comment. All of my work is  
17 with infrastructure business, most of which are  
18 regulated in one way or another. Successful regulated  
19 businesses earn support of the parties that depend on  
20 them by listening and compromise so that business and  
21 public interests are aligned. The settlement before you  
22 is the result of listening, compromise, and alignment  
23 among your Staff, representatives of major electric and  
24 gas customers, environmental groups, and low income  
25 customers. The process undertaken with the parties to

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1 reach a settlement, as much as its specific terms, have  
2 reaffirmed my view that we want to do business here. We  
3 hope that our conduct in the settlement process has led  
4 the parties to form the same view of us.

5           So why are we here? First and foremost Puget  
6 Sound Energy needs enormous amounts of capital.  
7 Management forecasts that PSE will spend \$5.4 Billion  
8 over the next five years. As you will hear from the  
9 Company itself, that capital spending is necessary to  
10 meet population growth, which is growing faster than the  
11 U.S. as a whole, to meet job growth, again higher than  
12 the U.S. average, to replace expiring power purchase  
13 contracts with new sources, 1,600 megawatts of new  
14 capacity is needed by 2015 compared to the currently  
15 installed base of 2,116 megawatts, also to meet the  
16 statutory requirements to increase the contribution from  
17 renewable sources from 4% currently to 15% by 2020, and  
18 to upgrade its gas and electric network infrastructure  
19 to maintain or improve service reliability. These are  
20 important objectives, and capital is needed to attain  
21 them.

22           Second, to meet this enormous capital need,  
23 PSE will secure significant external financing, \$3.4  
24 Billion from 2009 to 2013, particularly in comparison to  
25 its current capitalization of \$5.2 Billion and to

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1 external financing over the last five years of \$1.9  
2 Billion. The external equity requirement over the next  
3 five years as a proportion of the current equity  
4 capitalization of the company is high relative to  
5 comparable utilities nationally, and the capital  
6 requirements are being noted by rating agency reports as  
7 heavy and very high.

8 Puget Energy's board recognized that external  
9 financing needs of this magnitude, particularly equity,  
10 pose risks to the business and its customers. Large and  
11 frequent equity offerings, adverse market conditions,  
12 and declines in earnings, even if due to short-term  
13 factors like weather, put pressure on share price,  
14 equity costs, and if things get really bad, service  
15 levels. Accordingly, the PE board decided that the  
16 Company needed to look at alternatives for a reliable  
17 source of capital, particularly equity capital, better  
18 suited to the needs of PSE than the public market.

19 As you review the settlement, it's important  
20 that you compare our proposal not to what the Company  
21 has been over the last five years, but what the Company  
22 would be over the next five years, a small to mid cap  
23 utility regularly offering equity and raising debt to  
24 fund essential capital needs.

25 The PE Board of Directors chose us to be

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1 their partner to address the Company's capital needs  
2 going forward. Why did they choose us? First, taken  
3 together our members are the most experienced investors  
4 in infrastructure and utility assets worldwide. Second,  
5 we take a long-term approach. The investors in the  
6 infrastructure funds and the Canadian partners are  
7 pension funds, endowments, and foundations who seek the  
8 long-term stable returns such as those that can be  
9 expected of a utility investment. These entities have  
10 large and growing pools of capital for which they need  
11 to find a home. This combination provides PSE with more  
12 reliable access to external capital than if PE continued  
13 as a stand-alone entity.

14 Through the transaction, Puget Holdings has  
15 obtained capital commitments sufficient, together with  
16 operating cash flow, to fund management's recommended  
17 capital program through 2013. Macquarie and its  
18 Canadian partners have about half a trillion dollars in  
19 assets under management, and that asset base is growing,  
20 so there's ample capacity to increase the investment in  
21 PE going forward. The investor consortium, the three  
22 Macquarie entities and the three Canadian partners, will  
23 invest \$3.4 Billion in equity in Puget Energy at  
24 closing, a far greater commitment to the business than  
25 any investor in the public markets today. It is

1 unthinkable that this level of investment would not  
2 attract anything but the highest level of attention in  
3 the event of unforeseen problems at PSE. Investors in  
4 the consortium have superior global relationships with  
5 lending institutions, evidenced both by an exceptional  
6 track record in raising financing even during the  
7 current financial crisis and Puget's new bank group who  
8 are financing a portion of the transaction, and that  
9 includes 18 banks new to Puget as well as a number of  
10 its existing lenders.

11           The proposed transaction strengthens the  
12 balance sheet and credit quality of the regulated  
13 utility. In our discussions with Staff and other  
14 interested parties, there was evidence that maintaining  
15 investment grade rating at PSE was important. The  
16 strength of the balance sheet and credit quality allows  
17 us to make that commitment with confidence. PSE's  
18 equity to capital ratio will increase from 43% to at  
19 least 50% at closing, and we've committed to keep that  
20 ratio at 44% or higher unless a lower ratio is used to  
21 set rates.

22           Through our experience in investing in  
23 utility assets, we have learned that utilities can only  
24 be successful by being connected to their customer needs  
25 and are best led by executives who are leaders in the

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1 community served. Accordingly, we have committed to  
2 seek to retain current management team and to keep the  
3 headquarters in the service territory. This business  
4 will be run locally by local personnel. Also we have  
5 provided for two representatives of the service area,  
6 one of whom shall be the CEO of PSE, to serve on the  
7 Holdings board of managers and for those two plus a  
8 third local representative to serve on the PSE board.  
9 One of the local representatives, Bill Ayer, a current  
10 director of PE and PSE, will be chairman of both boards.  
11 This local board presence plus retention of the current  
12 executive team will ensure that the business remains  
13 aligned with the region's needs.

14           The settlement provides substantial customer,  
15 community, and environmental benefits. Customers will  
16 receive rate credits of \$100 Million over 10 years,  
17 substantially more and longer in duration than any  
18 precedent transaction. \$12 Million in rate credits are  
19 due to reduced costs and shall be offset in future rate  
20 cases if the Company can demonstrate such costs have  
21 been eliminated from its cost of service. The remaining  
22 \$88 Million is equivalent to a .24% reduction in PSE's  
23 annual equity returns each year for 10 years.  
24 Importantly, there are no local job losses behind these  
25 \$88 Million in rate credits. They are generated solely

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1 by the consortium's willingness to invest at a lower  
2 cost of capital for 10 years. We have committed to  
3 maintain existing low income programs, to propose to  
4 increase the funding for low income customer bill  
5 assistance from \$10.25 Million to \$15 Million, and to  
6 propose increased funding for low income energy  
7 assistance programs. We have reaffirmed PSE's goal of  
8 obtaining 10% of its energy from renewable resources by  
9 2013, maintaining the Green Power and net metering  
10 programs, and implementing a voluntary carbon offset  
11 program for natural gas customers. Recognizing that PE  
12 will incur additional debt to complete the transaction,  
13 we have adopted comprehensive ring-fencing provisions  
14 consistent with Commission precedent that insulate PSE  
15 from activities of its affiliates. These ring-fencing  
16 measures such as dividend restrictions, limitations on  
17 the business activities of PE and on the use of proceeds  
18 of debt incurred by PE provide protections to PSE  
19 customers not available under the status quo.

20 Further, recognizing that your oversight  
21 requires continued access to information, we have  
22 committed to maintain our SEC registration and continue  
23 our current reporting and maintain our governance  
24 practices required by the SEC and the New York Stock  
25 Exchange even though PE's equity will no longer be

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1 publicly listed.

2           It is clear that PSE faces substantial  
3 challenges going forward. The PE board decided that we  
4 are the right owners for the business because of our  
5 access to patient investment capital, our experience in  
6 investing in businesses like PSE, and our commitment to  
7 keep the business local. We urge you to review  
8 Macquarie's record and the record of our Canadian  
9 partners in this transaction, because we are certain  
10 that you will reach the same conclusion. We are pleased  
11 to present the proposed settlement for your review today  
12 because it represents the best thinking of the parties,  
13 your Staff, the representatives of the business  
14 customers, the coalition of environmental groups, and  
15 the low income customers, as to how PSE is best managed  
16 and funded going forward.

17           Thank you very much, I will be pleased to  
18 take questions.

19           JUDGE MOSS: Thank you, Mr. Leslie.

20           I will say that Ms. Kinn is an excellent  
21 court reporter and can keep up with the pace of most  
22 speakers, including me and I get carried away from time  
23 to time. I will ask, however, that you moderate the  
24 pace of your speech in acknowledgment of the fact that  
25 she is trying to transcribe every word verbatim, so



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1 thank you for that.

2 I'm also going to make another logistical  
3 arrangement here, I'm going to ask Ms. Griffin-Wallace  
4 if she will please contact Mr. Hoonan and see if we can  
5 get a portable microphone operating in here and for the  
6 initial at least time provide that to Ms. Carson, and  
7 she may need to hand that to witnesses who are sitting  
8 behind there. So, Ms. Griffin-Wallace, if you would do  
9 that, please, Mr. Matt Hoonan would be the person to  
10 contact on our Staff, thank you.

11 Now, Mr. Leslie, we have now had you  
12 introduced to everyone in the room, but I'm going to ask  
13 that we have our other panelists introduce themselves so  
14 that everyone knows who they are, and particularly so  
15 that our court reporter will understand who is speaking any  
16 given moment in time. Go ahead.

17 MR. MARKELL: My name is Eric Markell, I am  
18 Chief Financial Officer of Puget Sound Energy.

19 MR. KUPCHAK: My name is Rob Kupchak with  
20 Macquarie Capital USA Inc.

21 MR. EBERDT: Chuck Eberdt from the Energy  
22 Project.

23 MS. HIRSH: Nancy Hirsh with the Northwest  
24 Energy Coalition.

25 MS. PYRON: Paula Pyron, Executive Director

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1 for the Northwest Industrial Gas Users.

2 MR. EARLY: Good morning, I'm Michael Early,  
3 Executive Director of the Industrial Customers of  
4 Northwest Utilities.

5 JUDGE MOSS: And we have at least one  
6 panelist on the bridge line, Mr. Horton.

7 MR. HORTON: Yes, my name is William N.  
8 Horton, I'm a principal with the Finance Scholars Group.

9 JUDGE MOSS: Okay, and I think that covers  
10 the panel. All right, very good, thank you.

11 All right, with that then I take it we are  
12 ready to begin our questioning from the Bench, and I  
13 will start with asking Chairman Sidran.

14

15 Whereupon,

16 ERIC M. MARKELL, ROBINSON K. KUPCHAK,

17 CHARLES EBERDT, CHRISTOPHER J. LESLIE,

18 NANCY E. HIRSH, PAULA E. PYRON, MICHAEL

19 B. EARLY, and WILLIAM N. HORTON,

20 having been first duly sworn, were called as witnesses

21 herein and were examined and testified as follows:

22

23 E X A M I N A T I O N

24 BY CHAIRMAN SIDRAN:

25 Q. Thank you, good morning, and let me begin by

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1 commending Mr. Leslie, your English is surprisingly  
2 good, and I'm sure the court reporter appreciates that.  
3 We'll see if your Canadian friends are your equal.

4           Let me preface this by saying that the  
5 questions that I ask will be directed to the panel, but  
6 as Ms. Carson suggested, there may be others who are  
7 more appropriate to answer a particular question. So if  
8 that's the case, I will have to depend on counsel to  
9 identify the appropriate volunteer. And hopefully by  
10 then we'll have a portable microphone so that people on  
11 the bridge line can hear the response. If we don't have  
12 that, we'll have to ask whoever the respondent is to  
13 make their way to a microphone so that they can be heard  
14 by those listening.

15           My questions are primarily going to be  
16 focusing on interpreting some of the specific terms of  
17 the settlement stipulation, and in particular I think  
18 they focus primarily on the enforceability of some of  
19 these terms, and I would like to begin with number 31 of  
20 the commitments. That commitment says in pertinent part  
21 that the joint applicants, and that term though it's not  
22 defined here in the settlement stipulation from the  
23 other -- it's not defined in the appendix which contains  
24 the settlement stipulation, but in the settlement  
25 agreement the joint applicants are defined as Puget

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1 Holdings and Puget Sound Energy, so that's my  
2 understanding. If I'm wrong, I'm sure someone will  
3 correct me. But it says that the joint applicants  
4 understand that the Commission has authority to enforce  
5 these commitments in accordance with their terms, and a  
6 variety of terms provide for access to pertinent  
7 information, documents and records and so on, that would  
8 be made available by the joint applicants and where  
9 appropriate their affiliates, and that speaks to our  
10 ability to enforce those provisions presumably by if  
11 necessary compelling the production of documents. Would  
12 our enforcement authority also extend to requiring the  
13 attendance of witnesses at hearings if those witnesses  
14 were beyond the borders of the state of Washington or  
15 outside the United States?

16 A stunned silence.

17 A. (Mr. Leslie) I might endeavor to answer. I  
18 imagine it's probably a question for our lawyers, but  
19 certainly the members of the consortium would be more  
20 than willing to come across the borders under any  
21 circumstances I'm sure. I can't speak for our Canadian  
22 partners, but the idea that we might resist traveling by  
23 reason of being in another country close by I think is  
24 something that we would not contemplate under any  
25 circumstance.

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1 Q. All right, I will take that as a qualified  
2 yes.

3 Ms. Carson, do you want to add anything?

4 JUDGE MOSS: Please will you use a  
5 microphone, Ms. Carson. We'll have a portable mike here  
6 momentarily.

7 MS. CARSON: Yes, the Commission does have  
8 the authority to request witnesses to appear for matters  
9 that relate to Puget Sound Energy. And I can't address  
10 the international law issues of that, but as Mr. Leslie  
11 has said, the investors are cooperative in that regard,  
12 they understand the Commissioners' right to question  
13 regarding matters that relate to Puget Sound Energy, and  
14 it's my understanding they will make themselves  
15 available.

16 BY CHAIRMAN SIDRAN:

17 Q. All right, thank you.

18 A. (Mr. Leslie) If I might just add one matter.

19 Q. Yes.

20 A. (Mr. Leslie) I'm actually based in New York,  
21 so there's no borders involved as far as I'm concerned.

22 Q. Well, that would depend on your view of New  
23 Yorkers, but we'll turn to the balance of number 31. It  
24 goes on to say if there is a technical violation of the  
25 terms of these commitments, then the offending party may

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1 at the discretion of the Commission have a 30 day cure  
2 period. And my question is, what does the term  
3 technical mean, can you give me an example of a  
4 technical violation of these commitments?

5 A. (Mr. Kupchak) I think I would defer to  
6 lawyers on exactly what technical means.

7 Q. And for the sake of those who are not present  
8 in the room, it would probably be helpful for those on  
9 the bridge line if you identify yourself when you're  
10 responding to a question.

11 A. (Mr. Kupchak) Sorry, this is Rob Kupchak.  
12 One technical breach that we thought of was we made a  
13 commitment to maintain board members, independent board  
14 members. If one of those members were to resign, we  
15 would have 30 days to go out and find a new one. It's  
16 that type of thing that we're looking for here. Again,  
17 I would defer to counsel on the meaning of technical,  
18 but it's that type of thing that we're looking at.

19 Q. All right, thank you.

20 Anyone else?

21 MS. CARSON: I guess I --

22 Q. You get your exercise this morning.

23 MS. CARSON: I guess I would add that if a  
24 report is due and a deadline is missed, that might be  
25 considered a technical violation.

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1 Q. All right, thank you.

2 Commitment number 33 provides in pertinent  
3 part that the commitments are binding "only" upon Puget  
4 Holdings and Puget Sound Energy and their affiliates  
5 where noted. With regard to Puget Holdings, would the  
6 commitments be binding on any successors in interest?

7 A. (Mr. Kupchak) And again I would defer to  
8 counsel to some extent, but that would be our  
9 expectation. And again that's Rob Kupchak.

10 JUDGE MOSS: Mr. Roseman, we're having to  
11 hear so frequently from Ms. Carson, I'm wondering if you  
12 would be willing to surrender your chair to her, and  
13 that way she'll have a microphone right there in front  
14 of her. We're working on a portable mike, but  
15 apparently there's some technical difficulty, so I would  
16 appreciate it if you could help us out in that way.

17 MR. ROSEMAN: Sure.

18 JUDGE MOSS: Thank you.

19 Thank you, Ms. Carson.

20 MS. CARSON: Well, for there to be a  
21 successor to Puget Holdings, it would seem to me there  
22 would be another proceeding here before the Commission  
23 that would kind of tee up all these issues again, if I'm  
24 understanding your question right. So I think until  
25 that occurs, these are binding, and then either these

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1 would continue to be binding on the successor, or there  
2 would be new commitments as part of that proceeding.

3 BY CHAIRMAN SIDRAN:

4 Q. All right, thank you. Well, I will come to  
5 that question about a subsequent proceeding in just a  
6 moment, but I appreciate that thought.

7 Commitment number 24 says in pertinent part  
8 that Puget Holdings and PSE will not advocate for a  
9 higher cost of debt or equity capital as compared to  
10 what PSE's costs of debt or equity capital would have  
11 been absent Puget Holdings' ownership. Can you give me  
12 an example of how this provision would be enforced. In  
13 other words, how would the comparator of PSE's costs  
14 without Puget Holdings' ownership be established?

15 A. (Mr. Markell) Eric Markell, Puget Sound  
16 Energy. I think the intent here is to indicate to the  
17 Commission that there is no intent to take advantage of  
18 the cost of capital rate setting process by dint of this  
19 transaction. The parties in this proceeding or the rate  
20 proceedings can make available and do make available for  
21 your consideration all the data we can gather up about  
22 what the trends are in commission setting cost of equity  
23 cost of capital throughout the nation, and we provide  
24 that data on a regular basis. And I think the intent  
25 here is to say we're not going to be using this



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1 transaction to come in and sort of add surcharges to  
2 what we know to be known and measurable cost of capital  
3 being set by commissions around the country.

4 Q. So those would be the -- the comparables  
5 would be to look at companies similarly positioned, for  
6 example Puget Sound Energy as a stand-alone?

7 A. (Mr. Markell) That's correct.

8 COMMISSIONER JONES: Mr. Chairman.

9 CHAIRMAN SIDRAN: Commissioner Jones.

10 COMMISSIONER JONES: On that point, I don't  
11 know if it's appropriate now or later, but I would like  
12 to hear from Commission Staff on that point since that  
13 was explicitly raised as something perhaps not workable  
14 in their responsive testimony.

15 CHAIRMAN SIDRAN: I think that's entirely  
16 appropriate.

17 JUDGE MOSS: That would be Mr. Horton.

18 MR. CEDARBAUM: Actually I think the best  
19 witness in the hearing room is Mr. Elgin if he could  
20 answer. But I would indicate that when the group was  
21 administered the oath, I did not kick Mr. Elgin under  
22 the table to stand up, so he needs to be sworn in.

23 JUDGE MOSS: Well, we'll swear you now,  
24 Mr. Elgin.

25 CHAIRMAN SIDRAN: You may kick him now.

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1 (Witness KENNETH L. ELGIN was sworn.)

2 JUDGE MOSS: Thank you very much, you may be  
3 seated.

4

5 Whereupon,

6 KENNETH L. ELGIN,

7 having been first duly sworn, was called as a witness  
8 herein and was examined and testified as follows:

9

10 A. (Mr. Elgin) This is Ken Elgin with  
11 Commission Staff. As Mr. Markell indicated, we would be  
12 using comparable groups. In any event, if in the  
13 unforeseen circumstance that for example there would be  
14 a downgrade, it would be incumbent upon the new owners  
15 and Puget Energy to show the Commission that its  
16 comparable group and its proposed costs are not  
17 adversely impacting the customers.

18 And the second point would be in terms of  
19 difficulty is what would be the comparable group, what  
20 would be the cause of the downgrade, and there still  
21 would be technical issues about how we would ascertain  
22 is the downgrade really from the transaction itself or  
23 some other event. But we would have to slog through  
24 that, if you will, and -- but we would make our best  
25 efforts to find a comparable group, determine what the

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1 appropriate cost of debt and preferred equity would be  
2 and then present the evidence, and the Commission would  
3 make that determination.

4 COMMISSIONER JONES: Mr. Chairman, if I could  
5 just follow up with Mr. Elgin.

6

7 E X A M I N A T I O N

8 BY COMMISSIONER JONES:

9 Q. Thank you for that explanation, but isn't it  
10 true that there are a number of factors that go into a  
11 corporate credit rating, and if S&P and Moody's were to  
12 downgrade the CCR, it would be somewhat difficult to  
13 ascertain which led to which?

14 A. (Mr. Elgin) it would be, but we would --  
15 again, the joint applicants would have to make the  
16 showing, and the parties would have an opportunity to  
17 investigate, and then we would make our own judgments  
18 and assimilate data and present the best evidence we  
19 could to try to enforce that provision.

20 Q. Have we ever done this before, has Commission  
21 Staff faced a situation like this before?

22 A. (Mr. Elgin) Not precisely this. I have read  
23 some prior cases where the Commission Staff has looked  
24 at comparable groups when there have been untoward  
25 financial circumstances with respect to our regulated

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1 companies, but this specific instance where there would  
2 be let's say hypothetically a downgrade due to the  
3 acquisition, no.

4 COMMISSIONER JONES: Thank you.

5

6 E X A M I N A T I O N

7 BY CHAIRMAN SIDRAN:

8 Q. All right, thank you, I would like to turn to  
9 commitment number 43, and that commitment says in  
10 pertinent part that Puget Sound Energy will "to the  
11 extent practical" comply with the rules applicable to a  
12 registrant under New York Stock Exchange rules. If  
13 there were a dispute about what was "practical", would  
14 that be resolved by the Commission?

15 I have the correct answer in mind,  
16 Mr. Markell.

17 A. (Mr. Markell) Indeed it would.

18 Q. Congratulations.

19 Anyone else like to respond?

20 I would like to turn to commitment number 26,  
21 and in particular commitment 26(b)(2) says in this  
22 context that Puget Holdings will notify the Commission  
23 of the change in effective control or acquisition of any  
24 "material part" of PSE by any other firm. How much of  
25 PSE would be a material part for purposes of this

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1 commitment?

2 For those on the bridge line, we're still  
3 here, we're thinking.

4 JUDGE MOSS: Ms. Carson.

5 Q. Yeah, it's not a trick question, I think  
6 material part means something less than a majority, or  
7 does it? I'm just trying to understand what material  
8 is.

9 MS. CARSON: Well, any time there's a change  
10 of control, then that is something that needs to be  
11 approved by the Commission. I'm not sure that I'm  
12 answering your question.

13 Q. Well, I guess what I'm -- all I'm trying to  
14 do is clarify the meaning of the word material, because  
15 the provision says that there will be notice. It  
16 doesn't say anything about approval by the Commission,  
17 it simply says there will be notice of the change in  
18 effective control or acquisition of any material part.  
19 And my question is, is this intended to mean material as  
20 in a controlling interest, or is it material that for  
21 example 10% or 20% or 1/3 of the Company is proposed to  
22 be transferred?

23 MS. CARSON: I'm not sure I know the answer  
24 to that. I do think that this language comes from the  
25 current holding company order that governs Puget Energy

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1 and PSE right now, and I can verify that. So I guess I  
2 can't tell you exactly what that means, but I think -- I  
3 believe it's the same language that's in force right  
4 now.

5 Q. Feel free to supplement your answer after the  
6 panel concludes.

7 MS. CARSON: I will.

8 Q. All right.

9 Anyone else?

10 All right, I would like to turn to commitment  
11 28(C). Commitment 28(c) commits PSE and Puget Holdings  
12 to comply with "all applicable" provisions of the cited  
13 statutes that pertain to transfers of property,  
14 affiliated interests, securities, and the assumptions of  
15 obligations and liabilities. Are there specific  
16 provisions of those cited statutes which the joint  
17 applicants believe would not apply to Puget Sound Energy  
18 if the transaction were approved?

19 A. (Mr. Markell) I am not aware of any.

20 Q. The same question with respect to Puget  
21 Holdings, are there specific provisions of these  
22 statutes which Puget Holdings believes would not be  
23 applicable to Puget Holdings?

24 A. (Mr. Kupchak) We are not aware of any  
25 either.

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1 Q. And again, I extend the offer to counsel to  
2 supplement that answer if subsequently you determine  
3 there are some.

4 MS. CARSON: Yes, I will.

5 JUDGE MOSS: I think in connection with these  
6 suggestions that counsel may supplement these responses,  
7 I'm going to ask you to treat these as Bench Requests, I  
8 think we're up to Numbers 19 for that question  
9 concerning material change and 20 for this most recent  
10 question, so the Company should provide a written  
11 supplemental response, if any, hopefully within the next  
12 day.

13 MS. CARSON: Okay.

14 JUDGE MOSS: Thank you.

15 CHAIRMAN SIDRAN: Thank you, Judge Moss.

16 BY CHAIRMAN SIDRAN:

17 Q. I want to stay with this commitment 28(c) for  
18 a moment, is Puget Holdings committing to comply with  
19 the transfer of property provisions of RCW 80.12 which  
20 requires Commission permission to sell all or any part  
21 of a public service company?

22 MS. CARSON: As it relates to Puget Sound  
23 Energy, yes.

24 Q. Yes, as it relates to PSE, that is my  
25 question.

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1 MS. CARSON: Yes.

2 Q. So I think you may have answered this  
3 question as well, but I want to go back to this  
4 materiality part of my question. Reading 26(b)(2) which  
5 again relates to any material part of Puget Sound Energy  
6 changing in terms of effective control or acquisition  
7 and being a notice provision, and 28(c) which has to do  
8 with compliance with our statutes, I take it that it  
9 would be correct that Puget Holdings commits to not sell  
10 any "material part" of PSE without notice to and  
11 permission from the Commission, which I believe is what  
12 you said earlier, Ms. Carson, am I right?

13 MS. CARSON: That's correct.

14 Q. All right, thank you.

15 Now I want to turn to a confidential exhibit,  
16 and bearing in mind Judge Moss's observation that the  
17 joint applicants have designated entire documents, which  
18 may or may not be compliant with our rules regarding  
19 confidentiality, I want to turn to confidential Exhibit  
20 Number 50, and I believe that I can ask this question  
21 without raising issues of confidentiality and that it  
22 can be answered without raising those issues, but if I'm  
23 wrong, please let me know. I'm not going to refer to  
24 anything specific, but I want to call your attention in  
25 particular to page 11 of confidential exhibit, I guess



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1 it's highly confidential Exhibit Number 50, and this is  
2 also by the way discussed in non-confidential terms to  
3 some degree in Mr. Leslie's rebuttal testimony which is  
4 Exhibit 38 of highly confidential testimony at pages 6  
5 and 7, and it describes the structure of Macquarie  
6 Infrastructure Partners in terms that there will come a  
7 point in time when Macquarie Infrastructure Partners  
8 investors will need to decide whether to hold on to  
9 their investment in the partnership or elect out. And  
10 my question is, when that time arrives, can you describe  
11 what happens if some or all of the investors elect out?

12 A. (Mr. Leslie) Well, I think I would start by  
13 clarifying that in many senses, you know, the manager of  
14 Macquarie Infrastructure Partners, which is Macquarie  
15 Infrastructure Partners Inc., of which I am the CEO,  
16 will have considerable influence in terms of what  
17 ultimately happens at that point. The limited partners,  
18 limited partners by nature have a relatively passive  
19 role in the management of the fund in order to preserve  
20 their limited status. However, you are correct in  
21 suggesting that at some point in the future there will  
22 need to make a decision as to what to do with the  
23 investment.

24 The options are manifold. We could for  
25 example choose to list the fund on the stock exchange.

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1 We could divest the interest subject potentially to your  
2 approval if your approval is required to make that  
3 divestment. We may transfer the investment to a  
4 follow-on fund. So for example we're presently in the  
5 process of raising Macquarie Infrastructure Partners II,  
6 and in ten years time there will be some later  
7 generation of that series of funds I imagine which will  
8 be available, so there is the potential to roll the  
9 investment over.

10                   And if you might forgive me by way of  
11 background, when we were marketing this fund  
12 particularly to U.S. investors, we marketed  
13 Infrastructure as a very long-term investment, and we  
14 continue to believe that it's a very long-term  
15 investment. However, because Infrastructure is an asset  
16 class that's relatively novel here in the United States,  
17 investors were guiding us towards a more typical private  
18 fund structure and one which is ten years long so that  
19 they could, you know, defer any consideration of fund  
20 life and focus on the nature of Infrastructure as an  
21 investment, so we were guided by our investors in  
22 setting that fund length. Our experience in other parts  
23 of the world, notably Canada, Europe, and Australia, is  
24 that as investors become familiar with the asset class  
25 that they do appreciate its long-term characteristics

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1 and that they do indeed want to hold on to investments  
2 for the long term rather than sell them.

3           And so our expectation at this point, and  
4 this is confirmed by the attitudes of our investors as  
5 we speak to them regularly, is that we will most likely  
6 roll this investment into a subsequent fund. Investors  
7 that wish to participate in that fund can do so,  
8 investors that wish to leave can do so, and new  
9 investors may be introduced at that point. But  
10 Macquarie would continue as the manager of that fund and  
11 the day-to-day active investor as it were.

12       Q.     I want to follow up on your answer. So given  
13 that there are a variety of scenarios that you've  
14 described that would potentially arise at the electing  
15 out opportunity, would some or all of those constitute a  
16 transfer or sale of a material part of Puget Sound  
17 Energy as we've previously discussed that would require  
18 permission, notice and permission from the Commission  
19 under commitments 26(b)(2) and 28(c)?

20       A.     (Mr. Leslie) I think to the extent of the  
21 existing fund, there are two extension options, we can  
22 extend by two years and a subsequent two years, although  
23 that just defers the point to which you're talking to.  
24 There is a scenario where the fund is extended in its  
25 present legal form for some further period, in which

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1 circumstances I wouldn't expect that that would  
2 represent a change of control. To the extent that we  
3 divest to a third party, I guess it would be a question  
4 along the lines of your earlier question as to what  
5 constitutes a material change in the ownership of PSE.  
6 I would note at the present time that Macquarie  
7 collectively doesn't control this business in the sense  
8 that we require the vote of at least one of our partners  
9 to make any decision concerning the business. So on one  
10 construct, even if we were to sell our entire interest  
11 under the terms of the agreement, that wouldn't  
12 necessarily constitute a change of control. But I'm not  
13 familiar with the threshold at which materiality is  
14 defined here in Washington as to what you may consider  
15 material or not material.

16 Q. Thank you.

17 I want to turn to 28(c) or go back I should  
18 say to 28(c), it goes on to say that Puget Holdings will  
19 comply with all "applicable provisions" of RCW 80.08  
20 which relates to securities, and I want to ask you about  
21 a specific provision of that statutory section or  
22 chapter, and that is RCW 80.08.020, and that provides in  
23 pertinent part, and I will just read it:

24 The power of public service companies to  
25 issue stocks or other evidence of

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1 ownership and bonds, notes, and other  
2 evidence of indebtedness is a special  
3 privilege, the right of supervision,  
4 regulation, restriction, and control of  
5 which is and shall continue to be vested  
6 in the State, and such power shall be  
7 exercised as provided by law and under  
8 such rules and regulations as the  
9 Commission may prescribe.

10 Is Puget Holdings, is this one of the  
11 applicable provisions to which Puget Holdings is  
12 subject?

13 A. (Mr. Kupchak) I believe so. There's  
14 certainly no intention to change the way that the  
15 Commission currently regulates the business.

16 Q. Thank you.

17 A. (Mr. Elgin) Chairman Sidran.

18 Q. Yes, I hear a voice, Mr. Elgin.

19 A. (Mr. Elgin) I don't know if that's entirely  
20 correct. The public service company is Puget Sound  
21 Energy, and I don't know necessarily that Puget Holdings  
22 would come under or fall under this. Again, but we  
23 might want to hear from counsel on that, but that would  
24 be how I would interpret and look at the statute.

25 Q. Thank you, I take your point, but I took the

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1 answer to be that that could be a condition of any  
2 approval of this transaction if it were approved.

3 A. (Mr. Kupchak) I guess I would have to confer  
4 with counsel, but I mean I think what I was trying to  
5 say was that we expect to continue to be regulated the  
6 way the Commission currently regulates PSE, and I'm not  
7 familiar enough with that act and I have to defer to  
8 counsel as to about exactly what it says on that regard,  
9 but our expectation is that PSE is the entity that's  
10 regulated with regards to issuing capital, and we would  
11 expect that to continue.

12 JUDGE MOSS: Ms. Carson, do you have anything  
13 to add?

14 MS. CARSON: Yes, that's correct, and  
15 currently when stock or debt is issued, notice is given  
16 to the Commission, and we would expect that to continue  
17 as to PSE. I'm not sure that that's true as it applies  
18 to Puget Holdings, which is not a public service  
19 company.

20 BY CHAIRMAN SIDRAN:

21 Q. Mr. Elgin has focused upon why I asked the  
22 question, I'm aware that Puget Holdings is not a public  
23 service company and that Puget Sound Energy is, my  
24 question is, is this statute applicable to Puget  
25 Holdings?

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1 MS. CARSON: So if it were applicable to  
2 Puget Holdings or if the joint applicants agreed to  
3 that, they would be obligated to give notice when  
4 issuing stock or additional debt, and I'm not sure that  
5 we've talked about that. I don't think that that  
6 necessarily falls under the statute, and so as you said,  
7 Chairman, I think your question is will the parties  
8 agree to that.

9 Q. Well?

10 MS. CARSON: Well, I don't think I can give  
11 that answer right now.

12 Q. All right, thank you.

13 MS. CARSON: I will be happy to get back with  
14 you.

15 Q. All right, let's move on to or I should say  
16 return to confidential Exhibit Number 50. Now this  
17 exhibit as I previously mentioned is marked in its  
18 entirety highly confidential, and I will describe the  
19 exhibit by its title, which I assume is not particularly  
20 confidential, it is the private placement memorandums  
21 issued by Macquarie Infrastructure Partners, and it's  
22 dated May 2006. And I will try to avoid any disclosures  
23 of confidential information, but I'm particularly  
24 interested in what appears at page 49 of this document,  
25 and there it among other things describes a series of

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1 financial reports that limited partners could expect to  
2 receive. Without delving into the details of the  
3 specific nature of these reports, if the Commission were  
4 to determine that some of these reports were pertinent  
5 to the execution of its responsibilities, would the  
6 kinds of reports that are described under that heading  
7 on page 49, would they be made available to the  
8 Commission on request?

9 A. (Mr. Leslie) I think to the extent that they  
10 deal with this investment, yes. I should make the  
11 Commission aware though that many of the reports are  
12 consolidated across a portfolio of 13 assets, and it's  
13 not possible to distinguish the Puget investment from  
14 the consolidation.

15 Q. I take the point. The reason for the  
16 question is that the Commission might find it useful to  
17 know what Macquarie Investment Partners is telling its  
18 limited partners about Puget Sound Energy, and some of  
19 that information presumably is going to be contained in  
20 some of these reports. And if we determined that there  
21 was a need for access to that information, would we have  
22 it?

23 A. (Mr. Leslie) Yes.

24 Q. All right, thank you.

25 Still staying with this confidential Exhibit



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1 Number 50, and here I find it necessary to actually read  
2 what this document says, and so I'm going to ask for a  
3 waiver of this assertion of confidentiality, which I  
4 think is reasonable because the language that I'm  
5 interested in does not contain any financial information  
6 at all, but rather speaks to the nature in which the  
7 investment is proposed to be managed. And so what I  
8 will do is call your attention to the specific language  
9 that I'm interested in, and then you can determine  
10 whether you are willing to waive confidentiality. I'm  
11 interested in page 11 under the heading investment  
12 objective, and I'm interested in the second full  
13 sentence, the one that appears in the middle of that  
14 paragraph. Are you willing to waive confidentiality  
15 with respect to that sentence?

16 A. (Mr. Leslie) Yes.

17 Q. Thank you. So I will read it to you, or  
18 perhaps more accurately to those who don't have it in  
19 front of them. This says under the heading investment  
20 objective, again this is referring to the private  
21 placement memorandum dated May 2006, it says:

22 Where practicable, MIP intends to seek  
23 significant influence over the  
24 management operations and strategic  
25 direction of its portfolio investments.

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1 I would like you to describe the  
2 applicability of this statement to Puget Sound Energy.

3 A. (Mr. Leslie) Okay, well, the nature of  
4 Macquarie Infrastructure Partners as a fund is an  
5 infrastructure fund where we raise money from  
6 institutions and seek to invest it on their behalf, in  
7 return for which they pay us a fee. And in earning that  
8 fee, we believe investors are entitled to a degree of  
9 influence through us over the investments which we make  
10 on their behalf. So it would be unlikely for us in a  
11 broad sense to take very small minority positions in  
12 businesses where we have no influence.

13 JUDGE MOSS: Excuse me, Mr. Leslie, would you  
14 make sure your microphone is on there.

15 A. (Mr. Leslie) I'm sorry.

16 It would be unlikely for us to take very  
17 small positions in businesses where we had no ability to  
18 influence the outcome of that business, basically  
19 because simplistically why would someone pay us if we  
20 couldn't do anything about our investment I think is a  
21 generic statement. In this case, Puget Energy is a  
22 substantial business and one which is extremely well run  
23 by its existing management team. Accordingly, as we've  
24 said throughout our testimony, the business will be run  
25 locally day to day by the existing management team. We

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1 will not be for example putting any staff in the  
2 headquarters of Puget Energy to wander around and seek  
3 to influence the business real time on a daily basis.  
4 We will be having monthly calls with management. There  
5 is an asset management committee that comprises the two  
6 largest investors, we will be having a monthly call with  
7 management to understand how the business is progressing  
8 against its business plan. We will have over staff I  
9 guess an influence in the Company's construction of the  
10 business plan, but ultimately it's the Company's plan.  
11 You know, we like to interrogate management on their  
12 plan and challenge them on their assumptions, but  
13 basically management is the group that has to deliver on  
14 that. So, you know, they have to believe it first and  
15 foremost. We will try and be helpful. We think we have  
16 some expertise to add given the diversity of our  
17 businesses globally, so if we have some experience that  
18 may be relevant from utility businesses elsewhere in the  
19 States or internationally, i would hope that we might be  
20 able to bring that to bear. But by and large day to day  
21 it's the management that's running the business. So we  
22 act as an investor in a manner which seeks to protect  
23 our investment, we don't run the business on a daily  
24 basis.

25 CHAIRMAN SIDRAN: Thank you.

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1                   It's almost 11:00, and I want to ask our  
2 court reporter how she would like me to proceed, because  
3 I have two more questions, or perhaps there will be some  
4 follow-up questions, and if you would like to take a  
5 break we can do that now, or we can run through my  
6 questions and then take a break.

7                   All right, we'll take ten minutes and  
8 reconvene at 11:10.

9                   (Recess taken.)

10                  JUDGE MOSS: I want to say two quick things.  
11 One, I will caution again on the speaking pace,  
12 particularly when you're giving longer answers or  
13 answers that include terms that are perhaps specific to  
14 our industries, it's better if you can slow down a  
15 little bit for the benefit of our court reporter.

16                  Also for those of you on the bridge line, I  
17 am informed that we have had a couple of momentary  
18 interruptions, but the line has come back on. What's  
19 happening there is some technical problem that we don't  
20 know the source of, but we're monitoring that, and we  
21 will make sure we keep it going.

22                  So with that, let's resume with questions  
23 from Chairman Sidran.

24                  CHAIRMAN SIDRAN: Thank you, Judge Moss.

25 BY CHAIRMAN SIDRAN:

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1           Q.     Commitment 21 refers to transaction costs and  
2 provides that there will be no recovery of legal or  
3 advisory fees for the acquisition premium associated  
4 with this transaction in rates, but there is no specific  
5 mention of a similar bar on recovery of change of  
6 control compensation for senior executives. The record  
7 reflects that under the terms of their employment  
8 agreements, PSE's current senior executives are eligible  
9 for substantial payments upon change of control of the  
10 company and additional compensation if they are  
11 terminated in the process. Is there any reason why such  
12 payments should not also be explicitly barred from  
13 recovery in rates?

14           A.     (Mr. Markell) This is Mr. Markell,  
15 Mr. Chairman. No, there's no such reason, it is the  
16 intent that those costs be born by the shareholders.

17           Q.     Thank you.

18                     All right, I believe this will be my last  
19 question, and here I will be referring to what is Bench  
20 Exhibit 418, which is an article from Barron's, but  
21 there have been various media reports in other  
22 publications to the same effect, and these raise  
23 concerns about the credibility and performance of credit  
24 rating agencies in light of recent turmoil in the  
25 financial markets. Among other things, these articles

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1 suggest conflicts of interest arise from such practices  
2 as paying the agencies for credit rating advisory  
3 letters. Credit metrics and agency ratings are  
4 important issues in this case, and the joint applicants  
5 have submitted credit rating advisory letters. How  
6 would you respond to these concerns regarding, if you'll  
7 pardon the pun, the creditability of the credit rating  
8 agencies?

9       A.       (Mr. Leslie) The Barron's article in  
10 question I think criticizes the rating agencies on a  
11 number of levels and made suggestions as to how they  
12 might be improved. Much of the criticism is related to  
13 their performance during the recent credit crisis and in  
14 particular their ability to rate the complex structures  
15 that are part of sub prime syndication securitization  
16 programs that have gone recently. I guess my response  
17 is that those situations are inherently complex, whereas  
18 this particular situation is very straightforward, in  
19 fact almost as straightforward as it could be, the  
20 rating of the debt of a utility company. And so while  
21 Barron's may have basis for criticism in those complex  
22 situations, I think here the rating agencies are on  
23 very, very firm ground in that this is their traditional  
24 domain, and there is no complexity in this transaction.  
25 And we have been extremely transparent with them and

0500

1 fulsome in disclosing everything about this transaction  
2 to them, so I can see no reason why their ratings  
3 wouldn't be robust in this situation.

4 Q. And would you care to respond to the  
5 criticism or implication of a conflict of interest in  
6 paying for credit rating advisory letters?

7 A. (Mr. Leslie) I think there has to be  
8 potential for a conflict of interest. We believe that  
9 the rating agencies, however, act in -- without any  
10 conflict. They go to great lengths to distance  
11 themselves from the parties that are asking for the  
12 ratings and provide objective advice.

13 CHAIRMAN SIDRAN: Thank you, that's all I  
14 have at the moment.

15 JUDGE MOSS: Commissioner Oshie.

16 COMMISSIONER OSHIE: Yes, thank you, Judge  
17 Moss.

18 COMMISSIONER JONES: Mr. Chairman or Judge,  
19 Pat, before we go to that one, I have a follow up on the  
20 credit rating if I could.

21 CHAIRMAN SIDRAN: That would be fine,  
22 Commissioner Jones.

23

24

25

0501

1                                    E X A M I N A T I O N

2    BY COMMISSIONER JONES:

3            Q.    Mr. Leslie, I think the commitment to get a  
4    non-consolidation opinion applies only to Standard &  
5    Poor's; is that correct?

6            A.    (Mr. Leslie) Mr. Kupchak.

7            Q.    Mr. Kupchak.

8            A.    (Mr. Kupchak) The non-consolidation opinion  
9    is a commitment to the Commission. It's not related to  
10   one of the rating agencies. The commitment related to  
11   the rating agencies is a rating separation.

12           Q.    Excuse me, it's a separation between the  
13   respective corporate credit ratings of PE and PSE.

14           A.    (Mr. Kupchak) Right. The reason that that  
15   only relates to Standard & Poor's is that's a  
16   methodology specifically used by Standard & Poor's.  
17   Moody's does not have sort of a specific rating  
18   separation standard. They have -- they tend to have  
19   different ratings for the two entities, but they don't  
20   have a sort of a formal standard of rating separation  
21   the way S&P does, so we were referring to S&P's specific  
22   formal standard as opposed to anything else.

23           Q.    Do you pay Standard & Poor's to receive those  
24   private letters that are in the exhibits?

25           A.    (Mr. Kupchak) Yes.



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1 Q. The last Exhibit 50 I think, my question  
2 relates to Moody's, and I've read it, it's a highly  
3 confidential exhibit and I will not refer in detail to  
4 the nature of its assessment of the credit quality,  
5 either of PE and PSE, but is that the last letter for  
6 Moody's?

7 A. (Mr. Kupchak) Yes.

8 Q. So that's the only thing that the Commission  
9 has to rely upon in terms of Moody's going forward?

10 A. (Mr. Kupchak) That's correct, there is no  
11 formal -- there is no additional formal letter received  
12 from them.

13 Q. Have you had any subsequent discussions with  
14 Moody's to try to explain your position, because I think  
15 I'm fair in characterizing it as somewhat negative on  
16 the consolidated debt levels of this new entity?

17 A. (Mr. Kupchak) I'm trying to figure out how  
18 to answer this without going into confidentiality.

19 Q. Okay.

20 A. (Mr. Kupchak) I think we've provided a data  
21 request response which I think may be an exhibit, but  
22 it's a highly confidential exhibit, but we do go into it  
23 in that response. I would be happy to go into it, but  
24 mindful of the confidential nature.

25 COMMISSIONER JONES: I would defer, I have

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1

2 questions for you later, so.

3

CHAIRMAN SIDRAN: Before we turn to  
4 Commissioner Oshie, I want to just ask a follow up on  
5 Commissioner Jones' follow up.

6

7

E X A M I N A T I O N

8

BY CHAIRMAN SIDRAN:

9

Q. He was referring to commitment number 39 when  
10 he was asking about the separations and the  
11 applicability or role of Moody's in that context. The  
12 last sentence of commitment 39 states that if the joint  
13 applicants are unable to obtain or maintain ratings  
14 separation, the joint applicants will make a filing with  
15 the Commission explaining the basis for their failure to  
16 obtain or maintain such separation, and parties will  
17 have an opportunity to participate and propose  
18 additional commitments. I take it although it's  
19 implicit here, do I interpret this to mean that in the  
20 event that the joint applicants are unable to obtain  
21 separate ratings that the Commission will be able to  
22 impose, if necessary, additional commitments if for  
23 example the parties are unable to agree?

24

A. (Mr. Kupchak) Again, I'm not totally clear  
25 on what rights you do and you don't have. What we've

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1 said, what we've tried to do is if we can't get it,  
2 we'll explain to you why we can't get it. We'll make a  
3 formal filing, and then you will decide what the best  
4 course is. I don't purport to know what rights you do  
5 and you don't have, I just -- I'm not --

6 Q. We like to think we're the judge of that.

7 A. (Mr. Kupchak) Exactly.

8 Q. But, counsel, do you want to respond?

9 MS. CARSON: Yes. I think it's pretty much  
10 as it says, if they are not able to obtain the ratings  
11 separation, then we will file that information with the  
12 Commission, other parties can propose conditions, and I  
13 assume the Commission could propose conditions as well.  
14 I don't think there's any mandatory conditions set forth  
15 here.

16 JUDGE MOSS: Is there any procedural  
17 mechanism by which those commitments would be made  
18 effective that you have contemplated?

19 MS. CARSON: We haven't really contemplated  
20 it that far. This was -- there was a lot of discussion  
21 about this, and we came to this language, and it would  
22 provide interested parties, interveners in this case,  
23 the opportunity to come forward with a filing and submit  
24 what they think are adequate conditions to deal with the  
25 fact that there isn't rating separation. But there

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1 wasn't any agreement as to exactly what the nature of  
2 that filing would be or that procedure.

3 JUDGE MOSS: Mr. Early, did you have  
4 something to add?

5 A. (Mr. Early) Yeah, I wanted to comment on  
6 this. This is one of the provisions we focused on in  
7 terms of coming around to supporting the settlement. It  
8 was our language to attain and maintain, it's an ongoing  
9 obligation. And if they are unable to attain this  
10 separation from the rating agencies, then part of the  
11 protection we're relying upon is not available. So our  
12 understanding is at that point we would discuss with the  
13 applicants to see if we could come up with additional  
14 measures that provide us with the same level of comfort.  
15 If so, bring those to you. If not, then we would bring  
16 -- each of the parties would be free to bring their  
17 proposals for additional commitments that would provide  
18 us with the same degree of comfort that we would have if  
19 the separation had been obtained.

20 MR. CEDARBAUM: Your Honor, if I could just,  
21 and Mr. Elgin may want to add to this, but my  
22 understanding is that that would trigger an actual  
23 proceeding in which parties would propose additional  
24 commitments, and the Commission would make a decision on  
25 that, a formal decision. And if additional commitments

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1 were ordered, the order approving this transaction would  
2 be amended as of the next order in line. So there would  
3 be a formal process which gives the Commission ultimate  
4 authority to propose additional conditions, to amend.

5 JUDGE MOSS: And the appropriate corporate  
6 entities to the extent necessary would submit to our  
7 jurisdiction for that purpose if we did not otherwise  
8 have it?

9 MS. CARSON: Yes.

10 JUDGE MOSS: All right.

11 MR. CEDARBAUM: I think that's correct,  
12 because both Puget Sound Energy and Puget Holdings are  
13 parties to this agreement and bound by the agreement  
14 including commitment 39 and the processes that it  
15 contemplates.

16 JUDGE MOSS: Sure, thank you.

17 CHAIRMAN SIDRAN: Thank you.

18 Commissioner Oshie.

19 COMMISSIONER OSHIE: Thank you, Mr. Chairman.

20

21 E X A M I N A T I O N

22 BY COMMISSIONER OSHIE:

23 Q. I would like the parties to focus on  
24 commitment number 22. I'm mostly interested here on  
25 what the intent of the parties are when they executed

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1 this agreement. So my first question is, what is the  
2 objective of tying funding for low income energy  
3 efficiency programs to funding for energy efficiency  
4 programs for other residential customers?

5 A. (Mr. Eberdt) This is Chuck Eberdt from the  
6 Energy Project. We were encouraged by this statement in  
7 the settlement because the low income program funding  
8 has not changed in six or seven years, and there's been  
9 a huge increase in Puget's efforts in conservation and  
10 in residential in particular, and we feel that it was  
11 necessary that this is a sector that needs to walk in  
12 step with the other residential sector as well.

13 Q. When you say, Mr. Eberdt, that the program  
14 funds haven't changed over the last six years or that  
15 the -- is there a cap in place for that program?

16 A. (Mr. Eberdt) I don't think there is a cap in  
17 place, but I think that the budget that was allocated  
18 was pretty much unchanged over six years, and the way  
19 the program was handled basically took that as a cap,  
20 and that's the way the agencies responded to it.

21 Q. All right, thank you.

22 And what do the parties believe the financial  
23 impact of commitment 22 to be?

24 A. (Mr. Eberdt) Could you ask that again,  
25 please.

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1 Q. Well, maybe in plainer language, how much is  
2 this going to cost to bring the low income energy  
3 efficiency programs in step with the other programs,  
4 energy efficiency programs for residential, other  
5 residential customers, what's the dollar impact of this  
6 commitment?

7 A. (Mr. Eberdt) I would say that that's really  
8 unknown at this point. Puget has a very aggressive  
9 conservation program right now, and what we are being  
10 encouraged to do is get as much conservation as we can.  
11 But that all falls within the purview of their  
12 conservation advisory committee, and so all of that  
13 effort will be within that frame. And that I believe is  
14 also filed with the Commission, but I would have to  
15 check on that.

16 Q. Well, Mr. Eberdt, maybe I can ask the other  
17 parties to the agreement, you must have had some kind of  
18 number in mind when you agreed to this, because  
19 otherwise it would be basically an open ended order. So  
20 what did you believe that you were signing on to when  
21 you executed the agreement, what did you think the  
22 dollar impact would be? You know, give it a ball park,  
23 it doesn't have to be to the penny.

24 A. (Mr. Markell) Eric Markell for Puget Sound  
25 Energy. I think the intent here is that the low income

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1 segment of entities being helped by the energy  
2 efficiency programs have perhaps not been dealt with  
3 prorata or treated prorata over the last several years,  
4 and the intent here is to sort of catch them up and  
5 treat them equally going forward. And the process to do  
6 that is this process known as the CRAG process where the  
7 parties come together, they formulate priorities for the  
8 spending of the money, they formulate a budget, they  
9 bring it I believe to the Commission for its ultimate  
10 approval and rate setting process. So it's recognizing  
11 that there may have been one segment of the population,  
12 perhaps the most vulnerable segment, not treated as  
13 equal or equally with respect to the dispensing of  
14 energy efficiency program money.

15 Q. Thank you, Mr. Markell, but maybe,  
16 Mr. Eberdt, you can shed some light on what the parties  
17 believe the financial impact of this commitment would  
18 be. Are we talking about \$10 Million, \$20 Million, \$100  
19 Million? I mean I'm just looking for some understanding  
20 of what this commitment is going to cost. And I will  
21 follow up, maybe I will just follow up with the next  
22 question that might make it even clearer as to where I'm  
23 driving. How will the new funds for the low income  
24 energy efficiency program costs, how will those costs be  
25 recovered, no matter what they may be?



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1           A.       (Mr. Eberdt)  Again this is Chuck Eberdt, I'm  
2     trying to -- when we went into the proceeding, when we  
3     went into this intervention, one of our concerns was  
4     that the budget for the low income funding hasn't  
5     changed since 2001.  Our cost to do the work had changed  
6     considerably since 2001.  And so I did -- and I worked  
7     very closely with Puget Sound Energy over the last  
8     couple of years to get them to acknowledge and adjust  
9     what they paid us for various measures that we  
10    installed, because our costs to install those measures  
11    had gone up, and their costs had gone up considerably,  
12    and so there was quite a bit of difference between what  
13    we were being paid for measures and what the value was  
14    to Puget.  Earlier this year they filed, I might not  
15    have this technically correct in terms of what the  
16    procedure is, but the conservation filing or the -- I  
17    don't know if it was a tariff filing or not, but  
18    basically they adjusted what they pay us for measures.

19                   In order to continue to produce at the same  
20    rate we were previously producing with those new measure  
21    payment levels, we would need an additional \$1 Million  
22    in funding right there just to stay even with what we  
23    have currently been doing.  And we also want to move  
24    ahead and penetrate more into that sector, so when we  
25    came into the proceeding, we were looking for an

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1 additional \$1 1/2 Million or so funding just to try to  
2 stay even and move a step or two ahead. In the course  
3 of my conversations with the conservation department,  
4 they said, well, gee, there isn't any cap on your  
5 funding. Well, the whole thing had been budgeted in  
6 such a way that that wasn't our understanding.

7           So in terms of the magnitude of the impact,  
8 we're not talking about \$10 Million, we're not talking  
9 about anything near that. And what we would prefer to  
10 do in whatever the case is recognizing that we're  
11 talking about some infrastructure limitations anyway in  
12 terms of our ability to do the work, the availability of  
13 people out there to do the work for some of the  
14 agencies, there's got to be a ramp up to a higher number  
15 anyway, and it will be a gradual ramp up, whatever it  
16 is, and we just want to make sure that that keeps in  
17 pace with Puget's conservation efforts overall.

18       Q.     All right, thank you, Mr. Eberdt, I think you  
19 brought some level of clarity to that, to my earlier  
20 question.

21           So how will those funds be, no matter what  
22 they may be, if it's \$3 Million, \$5 Million, or more,  
23 how will they be recovered for to fund the programs that  
24 you administer?

25       A.     (Mr. Eberdt) Well, I would assume they would

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1 be recovered the way all of Puget's conservation program  
2 funding is recovered.

3 Q. So from other rate payers then?

4 A. (Mr. Eberdt) Yes.

5 Q. Was there any commitment here on the part of  
6 Puget Holdings or from Puget Sound Energy to contribute  
7 money as a result of this agreement that's not rate  
8 payer money to achieve the objective of commitment  
9 number 22?

10 A. (Mr. Eberdt) Not that I am aware of.

11 Q. All right.

12 A. (Mr. Elgin) Commissioner Oshie, this is Ken  
13 Elgin, if I could maybe try to also add, the program  
14 costs are recovered through tariff filings and the  
15 conservation tracker, so --

16 Q. That's my understanding too, Mr. Elgin.

17 A. (Mr. Elgin) And that's what I think, as I  
18 understood your question. So to the extent this 22  
19 commits the company to make the filing and to identify  
20 the programs, to bring the programs to a conservation  
21 tariff, and then the Commission would evaluate those  
22 programs and then make a determination as to what's the  
23 appropriate rate increment for the conservation tariff  
24 rider to be implemented. So in a future proceeding, you  
25 will see the budget levels, and then you will have an

0513

1 opportunity to evaluate those programs and the rates  
2 that would be necessary to recover those program costs.

3 Q. All right, thank you, Mr. Elgin.

4 JUDGE MOSS: I'm going to ask again for the  
5 witnesses to be careful and moderate the pace of their  
6 speaking, thank you.

7 Q. Before I leave this area, then perhaps, I'm  
8 not sure who will answer this but certainly open to the  
9 entire panel, as used in commitment 22, what precisely  
10 does the word commensurate mean? I mean I assume it's  
11 intended to be some measure of some kind, but what's the  
12 -- what are the -- what's the metric that the parties  
13 intend to use to determine that there's some parity  
14 between the low income energy efficiency programs and  
15 those offered by the utility to other residential  
16 customers?

17 A. (Mr. Eberdt) Again this is Chuck Eberdt from  
18 the Energy Project. That may be a level of definition  
19 that's more precise than I could actually give you.  
20 When I think of the word commensurate, I mean more or  
21 less in step with. If residential program funding was  
22 increased by 10%, I would like to see a 10% increase in  
23 the low income program funding.

24 Q. So not necessarily based on kilowatt hour  
25 usage or number of households, or perhaps it could be,

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1 but that's at least your intent, Mr. Eberdt, was looking  
2 at it as purely financial then?

3 A. (Mr. Eberdt) Yes, well, that was the way I  
4 thought about it. That doesn't necessarily mean that's  
5 the way it would ultimately be done, because I think  
6 that in the conservation advisory group that's always  
7 part of the question that comes up is what's the  
8 resource that's available and what's attainable.

9 Q. All right. And I assume that cost  
10 effectiveness through the energy efficiency programs  
11 will still be a consideration?

12 A. (Mr. Eberdt) Yes, sir.

13 COMMISSIONER OSHIE: Okay, do you have a  
14 follow up, Commissioner Jones?

15 COMMISSIONER JONES: I have a follow up on  
16 yours, Commissioner Oshie, if that's appropriate.

17 COMMISSIONER OSHIE: Sure.

18

19

20 E X A M I N A T I O N

21 BY COMMISSIONER JONES:

22 Q. This is for Mr. Markell, this is a yellow  
23 page, a confidential, it could be a yellow page question  
24 but I think can you speak generically about the business  
25 plan update presented to the Board of Macquarie Group as

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1 part of this transaction and how it treated conservation  
2 expenditures? My understanding is that there is no  
3 increase projected over time total, not just low income  
4 but total energy efficiency expenditures, so what does  
5 increase, and so if that is true, what does increase  
6 mean?

7 A. (Mr. Markell) I think you may be right that  
8 in that business plan projection we were holding it  
9 constant because we didn't have better information at  
10 the time, it was sort of a planning assumption. But as  
11 the cost of power rises, what's economic for energy  
12 efficiency and what's needed in terms of low income bill  
13 assistance changes with time, and we update that fairly  
14 regularly in the CRAG process. I think what we're  
15 trying to convey here is the Company process and the  
16 all-party process to sort out what's the right budget,  
17 what's the right criteria, and what's the right level of  
18 funding, that should go through the tariff that  
19 Mr. Elgin has just described.

20 JUDGE MOSS: I would like to interrupt here  
21 and tell the callers who are on the conference bridge  
22 line to please place their telephones on mute send,  
23 we're picking up some very lovely piano music in the  
24 hearing room, but we would just as soon not hear it.  
25 Thank you.

0516

1 BY COMMISSIONER JONES:

2 Q. Well, that's an interesting comment, but how  
3 did you, pitch is the wrong word, but how did you  
4 present the business plan update to the board and to  
5 Macquarie? Because obviously capital expenditures,  
6 which this is not, this is just recovery out of rates,  
7 and it's an expenditure, correct?

8 A. (Mr. Markell) It is.

9 Q. So how did you describe this to the board,  
10 and more importantly to --

11 A. (Mr. Markell) To be quite candid, there was  
12 not a lot of discussion around this item. It was a  
13 relatively small item and paled in comparison to the  
14 other O&M and Capex issues that we're dealing with.

15 Q. You mean compared to the \$5.6 Billion, it's  
16 small potatoes?

17 A. (Mr. Markell) Yes, sir.

18 Q. Okay, this is a question for the panelists, I  
19 think Mr. Markell --

20 JUDGE MOSS: Excuse me, Commissioner Jones, I  
21 think Commissioner Oshie has some more questions.

22 COMMISSIONER OSHIE: Go right ahead.

23 Honestly, Phil, if you would like to follow up if it's  
24 related.

25 COMMISSIONER JONES: No.

0517

1                   CHAIRMAN SIDRAN: Gentlemen, you can't fight  
2 in here, this is a hearing room.

3                   COMMISSIONER OSHIE: We'll save it for the  
4 friends and neighbors.

5

6                   E X A M I N A T I O N

7 BY COMMISSIONER OSHIE:

8           Q.       Well, let's stay on the topic of the  
9 commitments that have been made through this agreement  
10 to benefit certain classes of rate payers, and I want to  
11 explore in each one what the costs, well, what the  
12 parties believed the costs to be as they made these  
13 commitments, so let's start with commitment number 42.  
14 All right, this commitment as I understand it increases  
15 bill assistance benefits for low income customers from  
16 approximately \$10.25 Million per year to \$15 Million per  
17 year, so would you, the panel, please explain how these  
18 additional support moneys will be generated and what  
19 process will be used to accomplish this objective before  
20 the 2008/2009 heating season, if at all?

21           A.       (Mr. Markell) Eric Markell for the Company.  
22 The number frankly was arrived at by I guess they call  
23 it Western rough justice. We know that low income bill  
24 assistance --

25           Q.       As opposed to East Coast gruff justice?



0518

1           A.     (Mr. Markell) That's correct.

2                     That it's been a long time since the low  
3 income bill assistance program was increased. We have  
4 talked to the parties at participating agencies about  
5 the struggles they've had in meeting all the requests.  
6 It's very typical they go through a heating season and  
7 don't have enough money to be helpful. We have talked  
8 to our call center people who are Company employees on  
9 that very same topic. We know, as I think most of the  
10 public now knows, that there will be significant  
11 increases in the purchased gas adjustment costs for all  
12 the utilities this coming season. That ranges anywhere  
13 from 10% to I think I've heard as high as 35% or 40%.  
14 Electric increases are much less, but nevertheless  
15 they're marching along at the rates of inflation or  
16 somewhat higher, and we felt it was time that the most  
17 vulnerable group of our customers had some additional  
18 funds put out there for their benefit.

19           Q.     Okay. And how will the funds be recovered  
20 for distribution to the rate payers?

21           A.     (Mr. Markell) Through the existing processes  
22 and tariffs.

23           Q.     And Puget Holdings or Puget Sound Energy as a  
24 part of this agreement is not -- doesn't contemplate  
25 contributing its partnership dollars to this laudable

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1 goal?

2 A. (Mr. Markell) I have not talked to Puget  
3 Holdings about that, but that has not been a point of  
4 discussion as of this point in time.

5 Q. Okay. Now is this agreement to move bill  
6 assistance benefits for low income customers up by  
7 approximately \$5 Million, is that in the recently filed  
8 stipulation in the general rate case? Not to mix our  
9 docket numbers, but I would like to know.

10 A. (Mr. Markell) It is.

11 Q. It is, okay. And you assume then that the  
12 moneys, at least a portion of them, would be available  
13 for the 2008/2009 heating season, assuming the orders  
14 are approved by the Commission?

15 A. (Mr. Markell) Yes, the funds would begin to  
16 be collected.

17 Q. All right. And how will the benefits that  
18 are contemplated by commitment number 42 be distributed  
19 between electric and natural gas customers?

20 A. (Mr. Markell) We have a formula for that  
21 which we filed, and I can't recall off hand, so I would  
22 ask one of my fellow panelists to help me out on that.

23 A. (Mr. Eberdt) My recollection is that we're  
24 looking at about 75% electric and 25% gas.

25 Q. Okay, thank you, Mr. Eberdt.

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1                   There's also a provision in this commitment  
2 number 42 to include PSE's administrative costs in the  
3 program cap, so I would like the panel to explain that  
4 and also address the question of whether the inclusion  
5 of PSE's administrative costs, and I don't know what  
6 those costs may be in terms of the financial impact or  
7 what their -- this \$5 Million of additional moneys of  
8 approximate dollars will be eaten up by a material  
9 amount by the inclusion of administrative costs, but the  
10 panel can explain what is intended by this, what the  
11 financial impact may be, and whether you believe it  
12 creates any cost allocation problems in auditing and  
13 evaluating this program.

14           A.       (Mr. Markell) It is my understanding,  
15 Commissioner Oshie, that those costs were already  
16 included, but it's just not clear in how the accounting  
17 rules are defined. I don't think we expect any  
18 incremental costs to result from this rule  
19 clarification.

20           Q.       And how much, what's the financial impact --  
21 well, I guess as far as the \$5 Million, then there might  
22 be some additional costs in administering the additional  
23 dollars, but it would be immaterial in a sense or  
24 included in whatever the program costs would be?

25           A.       (Mr. Markell) I would describe it as

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1 immaterial.

2 Q. All right, thank you.

3 Please if the panel could explain the last  
4 sentence in commitment number 42, amount to be set in  
5 rates would include a gross-up over and above the  
6 program caps sufficient to cover PSE's revenue sensitive  
7 items, what does that mean, Mr. Markell?

8 A. (Mr. Markell) Commissioner Oshie, I believe  
9 it simply means it's a tax gross-up on the revenue taxes  
10 to provide a net benefit equal to the difference between  
11 \$15 Million and the \$10.25 Million currently in rates.

12 Q. All right, thank you, Mr. Markell.

13 I would like the panel to turn to commitment  
14 number 48, and this deals with the commitment to support  
15 the Northwest Energy Efficiency Alliance budget, so what  
16 is the -- what's the panel's belief here that the  
17 financial impact of this commitment is or would be?

18 Ms. Hirsh.

19 A. (Ms. Hirsh) Nancy Hirsh. Right now the  
20 Northwest Energy Efficiency Alliance's budget has been  
21 -- it's actually lower than it was ten years ago when  
22 the alliance was formed, and they have embarked on a  
23 pretty comprehensive strategic planning initiative to  
24 look at evaluating the role of market transformation.  
25 As the Bench is aware, Puget pays into and contributes

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1 to and serves on its board. In fact, a vice president  
2 of Puget chairs the strategic planning committee right  
3 now that's looking at what the role of NEEA will be.  
4 And what we were looking for in our support of this  
5 stipulation was that Puget be an advocate for looking at  
6 expanding market transformation efforts to the extent  
7 that they're cost effective. And that as part of this  
8 if they're identified within the strategic planning  
9 process that we wanted to hear that Puget Holdings would  
10 support whatever was the Puget's equal share. And I  
11 don't know at this point in time and I don't think NEEA  
12 knows what or if the budget for NEEA will go up across  
13 the board for all funding agencies or whether it will  
14 stay the same.

15 Q. And that's the intent of the language in  
16 there that it would be supported by PSE's prorata share  
17 of NEEA's budget?

18 A. (Ms. Hirsh) That's correct, so that Puget  
19 wouldn't pay any more than it currently pays now  
20 relative to the other contributors, that share would  
21 remain equal. But if the whole budget goes up and all  
22 partners agree to increase their funding, then Puget  
23 would support that increase.

24 Q. And is that considered to be I guess the term  
25 might be a hard obligation under all circumstances? In

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1 other words, for example if new members join and the  
2 budget is increased so you have more people to  
3 distribute the budget against, how would that affect  
4 this commitment, would Puget's prorata share in fact go  
5 down because it's --

6 A. (Ms. Hirsh) Yes, it could.

7 Q. All right. And how will the moneys that -- I  
8 assume that the moneys that are paid to NEEA at this  
9 time are recovered from rate payers?

10 A. (Ms. Hirsh) Yes.

11 Q. Okay, so do we have a -- so there's no --  
12 because NEEA's budget is somewhat fluid and dynamic, we  
13 really don't know what the financial impact would be of  
14 this commitment?

15 A. (Mr. Markell) I think that's correct.

16 Q. And how do moneys paid to NEEA, and this is a  
17 general question, how do moneys paid to NEEA as a result  
18 of the current practice of Puget and perhaps this  
19 commitment affect the budget for on the ground energy  
20 efficiency programs that are deployed by PSE, is there  
21 fewer dollars to make things happen within Puget's  
22 territory, or is it this is not a material amount of  
23 money that would affect the deployment of programs?

24 A. (Mr. Markell) I don't think it's a material  
25 amount of money. I believe the Commission recently

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1 approved an energy efficiency budget for Puget in the  
2 annual range of \$70 Million, and this is far less than  
3 that, so it's I would say it's immaterial relative to  
4 that commitment.

5 Q. But you don't have an exact number?

6 A. (Mr. Markell) I do not.

7 Q. Okay, thank you, Mr. Markell.

8 A. (Ms. Hirsh) I would also point out,  
9 Commissioner Oshie, that NEEA invests back in Puget  
10 service territory programs and delivers in partnership  
11 with Puget in its service territory as part of their  
12 commitment in partnership with the agency.

13 Q. All right, thank you, Ms. Hirsh.

14 I would like the panel to look at commitment  
15 number 50, and this commitment would support an  
16 objective of increasing the penetration of Puget's  
17 current Green Power program. So what was the intent of  
18 the parties or the understanding of the parties going  
19 into this commitment as to financial impact, how many --  
20 what kind of dollars are we talking about here?

21 A. (Mr. Markell) Our Green Power program  
22 participants pay a surcharge on their bill, an elective  
23 surcharge, for additional green power. So it's sort of  
24 a customer option to elect to do this. We're simply  
25 committing to try to increase the penetration rate of

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1 those who elect to participate.

2 Q. So through the Green Power program, if the  
3 Company runs advertisements on King5 to try to increase  
4 participation, those dollars that are spent to increase  
5 participation are recovered from the rate payers that  
6 join the program?

7 A. (Mr. Markell) I believe all program expenses  
8 come out from the surcharge in the Green Power program.  
9 I don't think there's anything currently in rates, but I  
10 can check that.

11 Q. All right, I would appreciate it if you  
12 would, thank you, Mr. Markell.

13 I have one more question, or actually two,  
14 and I want to sort of change horses, if you will, from  
15 the commitments that we've been talking about and  
16 financial impacts and more of a general question, so if  
17 you could turn to, please, commitment number 27. Now  
18 within the agreement, the terms Commission, Commission  
19 Staff, Public Counsel are used to identify what I will  
20 call the beneficiaries of guarantees made by PSE, Puget  
21 Energy, or Puget Holdings as to the provision of data,  
22 books, records, or other information related to the  
23 business of the regulated utility. Now are these terms  
24 because they specify Commission, Commission Staff,  
25 Public Counsel, are they intended to be limiting, do



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1 they only apply to those entities, or are they used to  
2 really affirm a general commitment that access to  
3 information by parties in the regulatory process will  
4 not be affected by the proposed commitment agreement?

5 A. (Mr. Markell) This is Mr. Markell for the  
6 Company, it's a general commitment, it's not intended to  
7 be limiting.

8 Q. Okay.

9 A. (Ms. Pyron) Commissioner Oshie, this is  
10 Paula Pyron if I may also respond to that.

11 Q. Certainly, Ms. Pyron.

12 A. (Ms. Pyron) Once a document is produced  
13 through the public records, then other interveners in  
14 the case because it becomes a public record are able to  
15 access the documents as well. So once something is  
16 auditable through the Commission's processes as well as  
17 is part of this docket, the parties who are parties to  
18 separate confidentiality agreements have access to the  
19 information.

20 Q. Thank you, and I think that really covers my  
21 next question in general. So I would assume that the  
22 parties would agree that the discovery process that we  
23 employ here at the Commission would not be affected by  
24 this agreement, and the access of the parties that  
25 participate, whether it's intervener or statutory

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1 parties, will have full access to information as they do  
2 now, at least let's use that term, that nothing would be  
3 changed by this agreement?

4 A. (Mr. Markell) That is our intent.

5 JUDGE MOSS: Mr. Cedarbaum.

6 MR. CEDARBAUM: Yes, thank you, Your Honor.

7 Just one caveat to that question, to that answer. I  
8 think the answer was correct that all the discovery  
9 processes and public records processes are not affected,  
10 but there are exemptions to public records requests, and  
11 they may or may not apply. I think we just have to take  
12 them as they come, so I didn't want to leave the  
13 implication that all these documents are always open for  
14 public inspection all the time. There may be an  
15 exemption that may apply.

16 Q. Thank you, Mr. Cedarbaum.

17 JUDGE MOSS: And as Ms. Pyron pointed out  
18 too, to the extent of confidentiality, the parties will  
19 continue to have the access they have now through the  
20 expedient of protective orders.

21 Q. Just as a follow-up question, and I would  
22 like to make sure I understand the intent of the  
23 parties, are the performance guarantees that are  
24 contained expressly in commitment 27 and which have been  
25 discussed earlier in your testimony, are they intended

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1 to recognize and ensure that the Commission will retain  
2 the right to require the production and to inspect all  
3 books, records, accounts, or other information that we  
4 believe as the Commission necessary to regulate the  
5 utility regardless of where that information, books,  
6 data, accounts are located?

7 A. (Mr. Markell) That is the intent of this  
8 commitment.

9 Q. All right, thank you, Mr. Markell.

10 I have one last question for the parties, and  
11 that is on commitment number 20. In commitment 20, PSE  
12 agrees to follow cost allocation methodology used to  
13 allocate either Puget Energy or Puget Holdings' related  
14 costs to PSE and proposed methods for standards for  
15 treatment of affiliated transactions. My question is,  
16 when will these filings be made as anticipated by the  
17 parties?

18 A. (Mr. Markell) we have not yet discussed when  
19 they ought to be made, I think as soon as we can get  
20 organized to make those filings after an order is  
21 issued.

22 Q. Mr. Markell, as you're apparently the  
23 spokesperson here, perhaps you can sort of expound a  
24 bit, what do the settling parties intend the Commission  
25 to do with the filings?

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1           A.     (Mr. Markell) Well, I think this commitment,  
2 you know, has its roots in the, you know, the generally  
3 sensitive subject in our industry about affiliate  
4 dealings and cross-subsidization between different  
5 parties. We are highly sensitive to that issue both in  
6 the state and elsewhere, and we wanted to be proactive  
7 to say we will be very forthcoming and propose ways to  
8 assure transparency and insulation of those costs if  
9 they're exchanged at all in a way that this Commission  
10 can review and approve.

11          Q.     Would you expect us to have to approve then  
12 those filings outside of a general rate case, and if so,  
13 what would be the impact then on future rate cases?

14          A.     (Mr. Markell) Quite honestly I haven't  
15 thought about the process and the issues that might give  
16 rise to a rate case. I would think that any issues of  
17 cost that would relate to recovery from our regulated  
18 rate payers would have to be dealt with in a timely  
19 manner by one of these filings or maybe as part of a  
20 general tariff filing.

21          Q.     All right, thank you, Mr. Markell.

22                 JUDGE MOSS: Ms. Carson, did you have  
23 something to add?

24                 MS. CARSON: Yes. It's my understanding that  
25 these affiliated transaction filings would occur as

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1 there are affiliated transactions to report.

2 Q. Well, the agreement requires the utility to  
3 file methodologies for us I suppose to review, I assume  
4 before there would be affiliate transactions that were  
5 actually in the queue. That's what I assume that this  
6 commitment, was the intent of the commitment, not that  
7 as transactions were actually accomplished if you will  
8 and submitted for some kind of rate treatment, that we  
9 would then know how the utility intended to deal with  
10 them procedurally.

11 MS. CARSON: And I guess at this point in  
12 time there are not specific affiliate transactions that  
13 are contemplated, and so it's been difficult to define,  
14 you know, what exactly those methodologies will be, but  
15 that's certainly something that we can look at.

16 Q. Well, it's in the commitment, I just -- I  
17 mean that's how I read the commitment, Ms. Carson. I  
18 mean it didn't say that it would be made when we filed  
19 affiliate transaction approval, if you will, for a  
20 specific transaction, it was more the methodologies and  
21 standards of treatment, but I understand your point.

22 Do the other parties agree then with  
23 Ms. Carson that as affiliate transactions would be  
24 consummated by the utility, that then it would bring  
25 those transactions forward with some methodology for us

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1 to approve? That's not how I read commitment 20, but I  
2 would like to know.

3 A. (Mr. Elgin) Commissioner Oshie, this is Ken  
4 Elgin, Commission Staff, no, that is not what we -- how  
5 we would look at 20. Once the transaction is closed,  
6 the way I read 20 and the way Staff is looking at this  
7 is they would have to file a generic methodology with  
8 the Commission for dealing with both corporate  
9 allocations and inter-company allocations to the extent  
10 they are affiliated transactions. There would be no  
11 action required by the Commission. It's the filing of  
12 the methodology so that the parties to this agreement  
13 and the Commission would know what the intent of these  
14 corporate and inter-affiliate transactions would be.  
15 Then in a subsequent rate proceeding, you would have  
16 before you the implementation of that methodology, and  
17 then you would rule on that for rate making purposes  
18 what specific costs would be included and appropriate  
19 for rates. And the presumption is that the joint  
20 applicants of Puget Energy would advocate this  
21 methodology they filed, but the parties could take  
22 objection to that and propose something else. So to  
23 answer your question, the approval would be in the rate  
24 setting process, the commitment is to file a proposed  
25 methodology that would inform the Commission and the

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1 parties as to what Puget Energy with the new owners  
2 would have in mind to deal with these costs.

3 JUDGE MOSS: Thank you.

4 Ms. Davison, something to add?

5 MS. DAVISON: Thank you, Your Honor, this is  
6 Melinda Davison for ICNU. I agree with Mr. Elgin's  
7 answer and would say that it was our interpretation that  
8 there would be a separate filing along the lines that we  
9 saw within the HC, thank you.

10 JUDGE MOSS: Thank you.

11 Mr. Markell.

12 A. (Mr. Markell) Without appearing to  
13 contradict my counsel too much, I would like to agree  
14 with Ms. Davison and Mr. Elgin. These are just very  
15 highly sensitive issues, and we would like to get a  
16 framework filed and on record that everyone can look at  
17 dealing with these sorts of issues. On a one off basis,  
18 this can lead to contentiousness and difficulties which  
19 the Company definitely does not want to engage in, so we  
20 would like to get the ground rules squared away to the  
21 extent we can.

22 Q. All right, thanks.

23 Ms. Pyron.

24 A. (Ms. Pyron) Commissioner, Paula Pyron, I  
25 just want to echo as well that we agree with the Staff's

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1 view and appreciate Mr. Markell's clarification, but I  
2 just want to point out in paragraph 28 we have further  
3 commitments that the Company has made that elaborate --

4 JUDGE MOSS: Ms. Pyron, your microphone.

5 A. (Ms. Pyron) I'm sorry, we have a touchy  
6 microphone, there we go.

7 I just wanted to point out paragraph 28 of  
8 the stipulation carries forward additional obligations  
9 to update the methodology when there are changes that  
10 impact it as well as speaks to the Company's burden of  
11 proof in a general rate case.

12 COMMISSIONER OSHIE: All right, thank you,  
13 Ms. Pyron.

14 Your Honor, that's the end of my questions  
15 for right now.

16 JUDGE MOSS: And that neatly brings us to the  
17 traditional luncheon hour or the traditional luncheon 90  
18 minutes, what would be the Commissioners' preference?

19 (Discussion on the Bench.)

20 JUDGE MOSS: All right, we'll go ahead and  
21 take our 90 minutes, recognizing that people do have to  
22 leave the building since we don't have eating facilities  
23 right here.

24 I want to say one final word while we're on  
25 the record, Mr. Horton has been waiting patiently this



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1 morning, we thought we might get to him as an individual  
2 witness for cross-examination. He is available only  
3 until 12:30, so clearly we will not be able to have him  
4 this morning. He has other obligations in New York, and  
5 as I understand it he will be available to us Wednesday  
6 morning, Mr. Cedarbaum?

7 MR. CEDARBAUM: My understanding is that he's  
8 available any time Wednesday. There is a three hour  
9 difference from where he will be calling in, so morning  
10 here would probably be best.

11 JUDGE MOSS: All right.

12 MR. HORTON: This is Bill Horton, I can  
13 accommodate the Commissioners and everyone there with  
14 respect to timing during the day, so what's best for you  
15 I can make work in my day.

16 JUDGE MOSS: Thank you, Mr. Horton. So for  
17 today at least we'll release you from contemplation of  
18 cross-examination.

19 With that, unless there's any last minute  
20 business we need to take up right now, let's be in  
21 recess until 1:30 this afternoon.

22 (Luncheon recess taken at 12:00 p.m.)

23

24 A F T E R N O O N S E S S I O N

25

(1:30 p.m.)

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1                   JUDGE MOSS: Good afternoon, everyone, we are  
2 reconvened after our luncheon recess, and I trust  
3 everyone is well energized after the break. We need to  
4 finish our questions from the Bench for the panelists,  
5 and we'll get to that in just a moment, but so it  
6 doesn't slip my mind I have had an unprecedented request  
7 to issue a Bench Request, and so I will do so to assist  
8 the Company and the parties in responding to some of the  
9 questions. Specifically the Company asked if I would  
10 designate a Bench Request so they could provide the cost  
11 information in response to Commissioner Oshie's  
12 questions concerning the low income and energy  
13 efficiency type programs, and I have agreed that I will  
14 let that be Bench Request 22, and that information will  
15 be furnished. Mr. Cedarbaum has mentioned the point  
16 that other parties might wish to respond, and that is  
17 one reason I have made these items Bench Requests is  
18 because this is our standard practice, other parties do  
19 have the right to respond to those since they will taken  
20 as evidence in the record. So I'm not going to set a  
21 definite time since I understand Mr. Trotter who is  
22 Staff's chief counsel in this case, principal counsel,  
23 had to leave town due to a family emergency, and so  
24 we'll work out a schedule later assuming it can be  
25 handled expeditiously.

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1 Mr. ffitch.

2 MR. FFITCH: Your Honor, could you please  
3 remind me what Bench Request 21 was.

4 JUDGE MOSS: Well, we had three, didn't we.  
5 You know what, I may not have identified 21, in fact I  
6 think I did not, so this will be Bench Request 21,  
7 you're right. I contemplated 21, and then I did not ask  
8 it, so the one I just mentioned will be 21.

9 All right, anything else preliminary?

10 The room is quite warm, at least I know I'm  
11 quite warm, so I want to invite those of you who are  
12 wearing jackets if you're uncomfortable to please feel  
13 free to remove your jackets while you're in the hearing  
14 room today. The thermostat may adapt to the fact that  
15 we just filled the room with warm bodies, but if not,  
16 please feel comfortable doing that.

17 All right, with that then I believe we are  
18 ready to resume our questions for the panelists, and,  
19 Commissioner Jones, your turn.

20 COMMISSIONER JONES: Thank you, Judge Moss.

21

22 E X A M I N A T I O N

23 BY COMMISSIONER JONES:

24 Q. Welcome back from lunch.

25 My first question relates to ring-fencing in

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1 general and other ring-fencing models or conditions of  
2 utilities around the country, so I would pose this to  
3 all panelists, but I will start with Mr. Markell  
4 perhaps, and others chime in. Has a ring-fence built to  
5 protect a utility, its assets, and its customers from  
6 financial distress in the holding companies ever failed?  
7 How do the ring-fencing provisions such as establishing  
8 a single purpose entity, an SPE like Equico, dividending  
9 constraints going up, utility equity requirements,  
10 separate books and records, separate CCR's, credit  
11 ratings, proposed in this case compare to such  
12 provisions contained in other ring-fences? I will start  
13 with that, and then I have a couple of follow ups,  
14 Mr. Markell.

15           Mr. Markell, I would ask you specifically in  
16 your role as CFO you had the primary responsibility to  
17 work with Morgan Stanley, I think your financial advisor  
18 on this project, and present recommendations of  
19 strategic alternatives to the board, so my question to  
20 you in particular relates to how you briefed the board  
21 on these issues of other utility M&A and other  
22 ring-fences.

23           A.     (Mr. Markell) First of all, Morgan Stanley  
24 was a direct advisor to the Board of Directors and not  
25 to the management team. I did work with them as they

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1 prepared materials for the Board of Directors, but they  
2 were not engaged by management directly.

3           The topic of ring-fencing and how we  
4 structured these commitments followed the transaction as  
5 the transaction was further developed and filed. I have  
6 no knowledge of any particular case where ring-fencing  
7 has failed. In fact, I believe it is the case that even  
8 in the cases where there's been a number of investment  
9 utilities that have filed for protection from Chapter 11  
10 and their creditors over the last two or three decades,  
11 there is no debtor that has ever gone unpaid and even  
12 has collected interest on its deferred debt. So  
13 whatever the various state systems are working in  
14 conjunction with bankruptcy law have worked to protect  
15 the debtors in full to my knowledge.

16           You had a variety of other questions, how  
17 does this compare to all other ring-fencing?

18       Q.     Yeah, and I would ask you to get specific  
19 here. I mean for example the Babcock & Brown  
20 Northwestern case, the KKRTXU case, there have been a  
21 number of M&A's after PUCA was repealed by congress in  
22 2005, correct?

23       A.     (Mr. Markell) That's correct.

24       Q.     And don't all of those M&A's have  
25 ring-fencing or many of them do --

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1           A.     (Mr. Markell)  They do, and I wouldn't  
2  purport to be an expert on each of their structures.  I  
3  do believe that some of the provisions offered up here,  
4  the commitments with respect to minimum equity ratio and  
5  dividend holdbacks or lockup provisions, if not unusual,  
6  perhaps are unique to this particular case and I think  
7  provide not only sufficient but really extraordinary  
8  protection that the current stand-alone model does not  
9  have.

10          Q.     Any of the other -- before we go to the other  
11  panelists, since you raised the point about Morgan  
12  Stanley, I guess I did and you responded, hasn't Morgan  
13  Stanley advised management before, and wasn't it an  
14  advisor to management in 2005, 6, 7 on raising equity in  
15  public markets and raising fixed income?

16          A.     (Mr. Markell)  Yeah, Morgan Stanley has  
17  worked with us with raising equity, but with respect to  
18  the merger transaction they were engaged by the Board of  
19  Directors.

20          Q.     Okay.

21                    Any of the other panelists want to comment on  
22  ring-fences, Mr. Leslie, Mr. Kupchak?

23          A.     (Mr. Kupchak)  Sure, this is Rob Kupchak  
24  again.  I think what we tried to do here was evaluate  
25  the precedent transactions in Washington state, the

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1 MidAmerican/PacifiCorp deal and the MDU/Cascade deal,  
2 and we tried to really fashion the ring-fencing measures  
3 we put into place on those transactions. We understood  
4 that they had addressed the interests of the parties in  
5 those transactions and of the Commission we believe, so  
6 we tried to mirror those wherever possible so that we  
7 could get to the same place.

8           And as far as comparing to other M&A  
9 transactions, we've done a number of other utility  
10 transactions in the U.S., and this is by far the  
11 tightest ring-fencing that we have ever employed in one  
12 of our transactions.

13           Q.     Anybody else?

14           Could the panelists refer to commitment  
15 number 35, please, I have a specific question on that.  
16 This has been referred to on numerous occasions on  
17 common equity ratio of not less than 50% at closing and  
18 then the joint parties or the investor consortium  
19 commits to a minimum of 44% except to the extent that we  
20 the Commission establish a different common equity ratio  
21 for rate making purposes. This is more of a question I  
22 think for Mr. Kupchak and Mr. Leslie. Then after that  
23 we get into the issue I think of addressing hybrid  
24 securities, and there's a provision that prohibits,  
25 well, it's written in the negative sense, it's not

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1 prohibitive from issuing new equity to third parties.  
2 And I think what you're trying to address here is the  
3 issue of hybrid securities, which I think PSE plans to  
4 issue in any case. I mean wasn't the case, Mr. Markell,  
5 that you were planning on issuing hybrid securities  
6 under the stand-alone option?

7 A. (Mr. Markell) Yes, it was.

8 Q. For the 2007 to 13 time frame?

9 A. (Mr. Markell) Yes, there's hybrid securities  
10 in that financing plan.

11 Q. So what's the purpose, Mr. Leslie or  
12 Mr. Kupchak, of the sentences here about basically it  
13 says that you -- the way I read it is that the term  
14 agreement or whatever term agreement is agreed to by the  
15 LLC's, there has to be a way of allowing the investor  
16 consortium to issue hybrid securities and then sell them  
17 to -- and these would be issued by PSE, then they could  
18 sell them to Puget Holdings, another entity, or they  
19 could, as you said this morning, go to the public  
20 markets, correct? So what's the -- and when was this  
21 inserted, what's the meaning of this and when was this  
22 inserted?

23 A. (Mr. Kupchak) And I will probably defer to  
24 Staff to some extent, because this was really, well,  
25 this was an effort to try to address specific concerns



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1 of some of the parties in settlement discussions with  
2 regards to what would happen in certain scenarios if  
3 there was an issue at Puget Energy in particular, and  
4 how would the consortium be able to get funds down into  
5 Puget Sound Energy in the case where Puget Energy for  
6 some reason wound up in bankruptcy or in default under  
7 its credit agreement. So this was really related to  
8 that specific occasion, and how would Puget Holdings get  
9 money down into Puget Sound Energy if there was a  
10 bankruptcy at that level, and that was one means of  
11 getting it down into Puget Sound Energy.

12 Q. And the settling parties felt that this was  
13 important, was this important to Staff to put in  
14 explicitly as a means of "injecting" equity into PSE,  
15 the regulated utility?

16 A. (Mr. Elgin) Yes, sir, it was, and it was  
17 specifically related to a situation as Mr. Kupchak  
18 discussed was that in the event that the Puget Energy  
19 was in financial difficulty and could not raise  
20 additional equity. It was explicit acknowledgment of  
21 the financing options that were available to protect the  
22 interests of Puget Sound Energy, the operating company,  
23 and so that what options were available in those  
24 circumstances to raise additional equity and fuse equity  
25 into the operating utility. And so that's what the

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1 intent of that is, so we have the minimum equity ratios  
2 and then the explicit acknowledgment of what options  
3 were available in a financial emergency and how they  
4 might inject equity into Puget Sound Energy.

5 Q. Okay. Related to that question, what are the  
6 enforceability provisions, Mr. Elgin, of equity  
7 injections into PSE? I'm talking about commitment  
8 number 3 where they commit to a credit facility of \$1.4  
9 Billion, but Mr. Leslie said this morning that he was  
10 fully funded or he was willing to commit to, the way I  
11 heard it, was to the \$5.6 Billion in capital that the  
12 capex plan requires. So reading commitment number 3  
13 with commitment 35, 36, and 37, how are these  
14 enforceable? For example, if the PH or the entities  
15 above PH decide not to inject new equity into the  
16 regulated entity, PSE, how is it enforced?

17 A. (Mr. Elgin) This is my reading and  
18 interpretation of the statute is under our 80.28.010,  
19 the Commission has the authority to ensure that all  
20 services are sufficient, adequate, reliable, safe, and  
21 the enforceability is for the Commission to order PSE to  
22 make certain kinds of investments. Also there's a  
23 statutory provision that would allow the Commission upon  
24 hearing to direct the operating company to make specific  
25 investments to improve quality of service. And so

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1 ultimately the orders would come and be from the  
2 Commission to the regulated utility.

3           And then the second element of that is that  
4 I've been advised by counsel that under our enforcement  
5 statutes, the Commission, by Holdings agreeing to these  
6 commitments, the Commission basically has enforcement  
7 authority over Puget Holdings to ensure that the equity  
8 would be available to carry out those orders and  
9 directions of the Commission with respect to investing  
10 in facilities necessary to carry out the public service  
11 obligation.

12           So you have kind of a two-step thing, first  
13 ordering the Company to make investments, and then the  
14 second thing is holding Puget Holdings accountable to  
15 living up to this commitment under here to provide the  
16 necessary equity capital. So that's my understanding of  
17 how these ring-fence provisions would be enforced.

18           Q.     I see. So, Mr. Elgin, just to follow up then  
19 I would like to go to Mr. Leslie. So there is no  
20 mention in the transaction commitments of the total  
21 capex needed, is there, \$5.6 Billion, of which \$3.4  
22 Billion comes from external equity?

23           A.     (Mr. Elgin) No, there is not.

24           Q.     There is not. And is the Company thereby  
25 committed to its business plan, which is confidential,

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1 we can't talk about it openly, or is it committed to the  
2 integrated resource plan that the Commission  
3 acknowledges?

4 A. (Mr. Elgin) No, what it's committing to is  
5 the financing that's in place now that they have  
6 arranged, and that's the \$1.4 Billion to fund the  
7 transaction at closing and then the \$1 Billion capex  
8 expenditure facility that's in place that's a five year  
9 term. So Mr. Markell in his prefiled direct testimony  
10 had a figure of about \$900 Million of external equity  
11 requirements.

12 Q. Yes, he did.

13 A. (Mr. Elgin) And so that \$1 Billion capex  
14 facility that's incremental to this \$1.4 Billion  
15 identified in commitment 3, that is the financing for  
16 the five year plan that's tied to the long-term business  
17 plan of Puget Sound Energy. So that's how -- the  
18 financing arrangement, and that's the committed  
19 financing they have in place now to take Puget through  
20 this five year period.

21 Q. But Puget Holdings has a term facility and a  
22 capex facility, correct, the holdco does?

23 A. (Mr. Elgin) I think they're both, yes, Puget  
24 Energy has those arrangements, yes.

25 Q. Excuse me, PE does, Puget Energy does.

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1 A. (Mr. Elgin) Yes.

2 Q. And one is -- are either of them utilized  
3 fully at closing the transaction?

4 A. (Mr. Elgin) No, just the -- my understanding  
5 is just the \$1.4 Billion will be necessary to close the  
6 transaction.

7 Q. So conceivably the 1.0 capex facility held by  
8 holdco could be drawn or could be not drawn down based  
9 on either the business plan or what you call the public  
10 service obligations and the enforceability of whatever  
11 we have as a Commission?

12 A. (Mr. Elgin) Correct.

13 Q. Service quality?

14 A. (Mr. Elgin) Correct.

15 Q. Aren't the public service obligations fairly  
16 broad?

17 A. (Mr. Elgin) Yes, they're broad, and they're  
18 not known at this time, but this is their management's  
19 best estimate of what will be necessary.

20 Q. Okay.

21 Mr. Leslie, could you address that, the  
22 enforceability of these commitments and how much is  
23 really committed to in terms of the transaction  
24 commitments in transaction commitment 3 and in 35  
25 through 37.

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1           A.     (Mr. Leslie) Just to clarify on the term  
2 loan in the capex facility at holdco, there is currently  
3 a \$1.4 Billion term loan which will be drawn to 1.2 at  
4 closing.

5           Q.     Correct.

6           A.     (Mr. Leslie) differential --

7           Q.     I understand that.

8           A.     (Mr. Leslie) -- \$200 Million.

9           Q.     I understand that.

10          A.     (Mr. Leslie) And there's a \$1 Billion capex  
11 facility that has \$750 Million accordion feature, so  
12 just to be clear because there was -- there seemed to be  
13 some confusion on that point.

14          Q.     But of course that is not drawn down at  
15 closing, is it?

16          A.     (Mr. Leslie) That's right, the capex  
17 facility is undrawn at closing, so there's \$1 Billion of  
18 committed facilities which are undrawn.

19          Q.     It's from the same two banks that committed  
20 to the overall credit facility, correct?

21          A.     (Mr. Leslie) In terms of the lead banks,  
22 yes.

23          Q.     In terms of the two lead banks?

24          A.     (Mr. Leslie) Yes.

25          Q.     And I don't know if that's confidential or

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1 not, Judge.

2 A. (Mr. Kupchak) Could I just add something?

3 Q. Yes.

4 A. (Mr. Kupchak) That facility has largely been  
5 syndicated down, so it's there were two banks initially  
6 that committed, but now there are a number of additional  
7 banks behind that, just as background.

8 Q. But, Mr. Leslie, regarding my more  
9 fundamental point about what you are committing to in  
10 these transaction commitments, you being Puget Holdings,  
11 are you going to be chairing the board of Puget Holdings  
12 or Puget Energy or PSE or all of the above?

13 A. (Mr. Leslie) There's a correction required  
14 there in that I will not be chair of any of these  
15 boards.

16 Q. You're not?

17 A. (Mr. Leslie) No.

18 Q. Oh, I thought you were chair of Puget  
19 Holdings according to the record?

20 A. (Mr. Leslie) No.

21 Q. No?

22 A. (Mr. Kupchak) I think there was an initial  
23 plan for Chris to be chairman of particular boards, but  
24 that was modified when we decided to have Bill Ayer as  
25 the chairman of those boards, so the independent

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1 director of Puget Sound Energy and Puget Holdings and I  
2 believe Puget Energy as well, so he will be the chairman  
3 of all of those.

4 A. (Mr. Leslie) I am chairman of none.

5 Q. Well, Mr. --

6 A. (Mr. Leslie) Yes, I understand the question.  
7 Well, the commitment as such comes in the form of the  
8 committed facilities and the availability of those  
9 facilities to the company and commitment in the  
10 commercial sense to allowing the Company to fulfill the  
11 present plans of management to undertake the capital  
12 expenditure plan as it's been laid out to us. So that  
13 is the nature of our commitment, it doesn't rise to the  
14 level of a regulatory commitment I believe, but it's the  
15 commercial commitment of the parties in moving into this  
16 transaction is to stand behind the funding of that  
17 capital expenditure program. So that is our intent in  
18 this transaction, and that's probably the better way to  
19 describe it, as a commercial intent as opposed to a firm  
20 commitment.

21 Q. So it's commercial intent instead of a firm  
22 commitment, and what you commit to in transaction  
23 commitment number 3 is \$1.4 Billion.

24 A. (Mr. Leslie) That's correct.

25 Q. It says secure and provide a contractually



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1 committed credit facility, and I assume by that you mean  
2 the what Mr. Kupchak just referred to, correct?

3 A. (Mr. Kupchak) Yes.

4 A. (Mr. Leslie) Yes.

5 Q. The syndicated bank?

6 A. (Mr. Leslie) Yes.

7 Q. Consolidated?

8 A. (Mr. Leslie) We are committing to secure and  
9 provide the facility.

10 Q. Okay.

11 A. (Mr. Leslie) That is the commitment.

12 Q. And is that -- so that's debt, what is that  
13 debt rated at presently, is that BB+, is that below  
14 investment grade?

15 A. (Mr. Kupchak) Well, they're current list  
16 facilities currently, I mean they won't be fully in  
17 place until the transaction closes.

18 Q. But S&P has rendered an opinion on --

19 A. (Mr. Kupchak) They've rendered an opinion --

20 Q. -- on that term facility, correct?

21 A. (Mr. Kupchak) That's correct.

22 Q. And again what is it rated at?

23 A. (Mr. Kupchak) That's a confidential  
24 document.

25 Q. That's confidential?

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1           A.     (Mr. Kupchak) Yes, the existence of that is  
2 confidential.

3           Q.     Okay, I will hold that question until  
4 individual questioning then.

5                     Moving right along --

6           CHAIRMAN SIDRAN: Excuse me, Commissioner  
7 Jones, if you don't mind I just want to ask a follow-up  
8 question so this point is clear in my mind.

9

10                               E X A M I N A T I O N

11 BY CHAIRMAN SIDRAN:

12           Q.     I'm trying to understand the difference  
13 between a commercial commitment and a regulatory  
14 commitment. So do I understand the joint applicants'  
15 position to be that the \$1.4 Billion is a regulatory  
16 commitment so to speak, because it's embedded in the  
17 terms here of the commitment, but the additional \$1  
18 Billion capital facility is a commercial commitment  
19 which might or might not after closing be a binding  
20 commitment?

21           A.     (Mr. Kupchak) No, sorry, just to be precise  
22 the \$1.4 Billion that's mentioned in the commitment is  
23 for the capital expenditure facility, so there's \$1  
24 Billion that PE -- capital expenditure facility.  
25 There's also \$400 Million at PSE. So the \$1.4 Billion

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1 refers solely to the capital expenditure facility. It  
2 does not refer to the term facilities that are necessary  
3 to fund the transaction. So this is just capex, the  
4 1.4, and that is the regulatory commitment.

5 CHAIRMAN SIDRAN: All right, thank you.

6

7 E X A M I N A T I O N

8 BY COMMISSIONER JONES:

9 Q. So what you're saying, Mr. Kupchak, is the  
10 Commission needs to look at the \$400 Million opco capex  
11 facility together with the \$1 Billion holdco capex  
12 facility together?

13 A. (Mr. Kupchak) That's correct.

14 Q. And neither are drawn at closing, correct?

15 A. (Mr. Kupchak) That's correct.

16 JUDGE MOSS: Just for the clarity of those  
17 listening, when Commissioner Jones refers to the opco I  
18 believe he is referring to PSE, and when he refers to  
19 the holdco I believe he is referring to PE, am I  
20 correct?

21 COMMISSIONER JONES: Yes, excuse me, Judge  
22 I'm referring to -- there's so many terms in this  
23 transaction, that is correct.

24 JUDGE MOSS: Thank you.

25 BY COMMISSIONER JONES:

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1 Q. If you could turn to commitment 38, please.  
2 This regards Equico, this new special purpose entity.  
3 Commitment 38 provides for a new entity, Equico, to  
4 exist in the corporate structure between Puget  
5 Intermediate and Puget Energy for the single purpose of  
6 holding all of Puget Energy's equity or stock. Will  
7 Equico have an independent director as described in  
8 commitment number 16 for PSE? And again, Mr. Leslie, I  
9 guess you are not a director of anything any more, so.

10 A. (Mr. Leslie) That's not true.

11 Q. But my question here more is on the  
12 independent director.

13 A. (Mr. Leslie) Well, I'm not sure whether  
14 we've resolved that at this point. Mr. Kupchak might be  
15 able to enlighten us.

16 A. (Mr. Kupchak) Yeah, I think that's the  
17 intention in order to make it bankruptcy remote as per  
18 the commitment that there would need to be an  
19 independent director at that level that would hold the  
20 bankruptcy.

21 Q. Okay.

22 And could you turn to commitment, turn your  
23 pages up a bit, turn to commitment number 57, please.  
24 This is one where I wanted to shy away from confidential  
25 information that is either in your exhibits,

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1 Mr. Kupchak, or in another part of the record. So with  
2 regard to commitment 57, the joint applicants commit to  
3 refinance the term loan using medium term or long term  
4 financing, i.e., you're agreeing to explore I think,  
5 develop, plan, and explore the idea of longer term  
6 financing. Does this commitment address only the term  
7 loan, or does it also apply to the capex facility?

8 A. (Mr. Kupchak) Well, I will have to read the  
9 specific language, but the intention is to make -- is  
10 that we wanted to make it clear to people that we did  
11 not like refinancing risk, and having a lot of debt  
12 coming on at one point in time would create a larger  
13 refinancing risk than we were comfortable with. We  
14 wanted to memorialize the intension to stagger the  
15 maturity profiles of the debt, including what you had in  
16 a term facility as well as what you would eventually  
17 have in a capex facility, to stagger the debt maturity  
18 profile over a longer period of time. So what we're  
19 committing to here is to memorialize that, that that's  
20 our plan is to stagger that maturity profile and push  
21 out some of it for a longer term. And we think it's a  
22 prudent thing to do, we wanted to memorialize that  
23 because the parties had addressed some concern over  
24 that. So it would refer to I mean both the term  
25 facility and the capex facility.

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1 Q. Have you already received a proposal, several  
2 proposals to refinance this term facility into a longer  
3 term bond?

4 A. (Mr. Kupchak) We have had a number of  
5 discussions with various banks and/or credit facilities  
6 that have been interested in helping us with that  
7 refinancing.

8 Q. Okay.

9 My last question for the panel is for  
10 Mr. Leslie, and you opened the door for me a little bit  
11 today with your written opening remarks. You said that  
12 "Puget Sound Energy requires an enormous amount of  
13 capital". You're an experienced investor, you're  
14 looking at utility needs in this sector right now, why  
15 do you say they're enormous, and on what basis do you  
16 make that assertion? For example, current utility needs  
17 with debt equity and project financing I think are in  
18 the range of what, last year \$120, \$130 Billion, that's  
19 just one year, so aren't all utilities and specifically  
20 those utilities with a BBB, an investment grade rating,  
21 facing similar issues as Puget does?

22 A. (Mr. Leslie) Yes, I think generally that's a  
23 fair statement. There are a number of pressures bearing  
24 on the industry in terms of modernizing the fleet, moves  
25 to renewable energy, integrating transmission grids and

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1 so forth, so it's correct to say that there is a very  
2 large burden upon the industry as a whole as far as  
3 capital expenditure goes. I think the point of my  
4 statement this morning though was that \$5.4 Billion  
5 relative to the size of Puget as it stands today where  
6 it is a relatively small player in the national industry  
7 is a disproportionately large burden.

8 Q. Disproportionate to what, its market cap or  
9 its sales?

10 A. (Mr. Leslie) To Puget's present size.

11 Q. Size meaning what?

12 A. (Mr. Leslie) The rate base of its existing  
13 assets.

14 Q. Rate base?

15 A. (Mr. Leslie) Its market cap, yes.

16 JUDGE MOSS: Let's please be careful not to  
17 overtalk one another, take pauses, thank you.

18 Q. Are you aware that Puget has raised \$800  
19 Million in equity over the past six years?

20 A. (Mr. Leslie) Yes.

21 Q. And the equity needs of this company over the  
22 next six years are about the same, aren't they?

23 A. (Mr. Leslie) The reinvestment of dividends  
24 in this company, Mr. Kupchak, if you could assist in  
25 terms of -- we meet the capital needs of the company

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1 over the next five years through the debt facilities and  
2 reinvestment, so that would amount to what sort of  
3 level?

4 A. (Mr. Kupchak) Well, I think that they are  
5 larger than \$600 Million in my recollection, but I think  
6 Mr. Markell would be better.

7 A. (Mr. Markell) Commissioner, again, the five  
8 year plan would provide \$900 Million of new equity in  
9 addition to retained earnings, so it's in aggregate  
10 perhaps \$1 Million to \$1.3 Million over the period we're  
11 talking about.

12 Q. I'm referring, Mr. Markell, only to the  
13 external equity required.

14 A. (Mr. Markell) About \$900 Million.

15 Q. Thank you.

16 Mr. Leslie, you also said you were, quote, an  
17 experienced investor in U.S. utility markets, and you  
18 talked about your management style, so two questions.  
19 How long have you been in U.S. utility markets, hasn't  
20 it been two years or three years? Now by utility I mean  
21 combined gas and electric utilities, I'm not referring  
22 to Macquarie and the water utility in Connecticut.

23 A. (Mr. Leslie) Okay, well, I arrived in the  
24 United States in November 1999, so I'm coming up for  
25 nine years in the U.S. And one of the first areas that



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1 we examined for potential investment in infrastructure  
2 as the Macquarie Group was electricity transmission  
3 throughout the United States, particularly in response  
4 to FERC Order 2000 dealing with original transmission  
5 organization. So as part of that endeavor, I guess the  
6 first actual investment in which I was involved was  
7 Altlink, the creation of Altlink in the province of  
8 Alberta, taking TransAlta's grid and spinning it out  
9 from the integrated utility and thereafter in Michigan  
10 Electric Transmission Company. These were transactions  
11 in which I was part of the investment banking, if you  
12 like, the advisory part of our business where  
13 Mr. Kupchak presently sits. I changed roles to take my  
14 present role approximately three years ago, whereupon  
15 the first transaction in which we invested was to  
16 Canlight, so I think technically I could agree with you  
17 that it's been two years in terms of my role as an  
18 investor directly, although the functions of our  
19 investment banking business and our funds management  
20 business are quite closely aligned, and so the  
21 investment experience extends back almost to the time I  
22 moved to the States back in '99, early 2000.

23 Q. In your opening remarks you talked about that  
24 you would exert "significant influence" over the  
25 management decisions of the regulated utility in spite

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1 of the fact it's well run but just your fiduciary  
2 responsibility as manager of MIP, it sounds like MIP II  
3 is on its way, M-I-P that is, so I would ask you to  
4 expound on that somewhat, because I do believe the  
5 investment banking experience is different than the  
6 infrastructure class experience that is before us today;  
7 is that a fair statement?

8 A. (Mr. Leslie) It's absolutely correct, I  
9 think the role of an investment banker in drawing  
10 transactions together is quite different to the  
11 fiduciary responsibilities of my present role in terms  
12 of managing a fund on behalf of our investors. There is  
13 a clear distinction between the two.

14 Q. So I guess my question, and I will have  
15 further questions depending on where Mr. ffitch goes  
16 this afternoon, but my broad kind of high level question  
17 is how active of a management style do you intend to be,  
18 and how active have you been with the Canlight for  
19 example? Do you have regular board meetings monthly, do  
20 you look at everything the company does in terms of  
21 strategic reviews, capex budgets, everything, or just  
22 explain to me your frequency of meetings, frequency of  
23 time that you devote to it?

24 A. (Mr. Leslie) Okay, the broad framework I  
25 think can be defined in three elements principally

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1 revolving around the business plan, the development of  
2 the business plan for the company. That's something  
3 that management undertakes in detail. In fact, we're  
4 about to embark on a business planning cycle for next  
5 year for most of our portfolio companies, sort of come  
6 back from summer and get the management teams, you know,  
7 working on the business plan process. That's an  
8 interactive process, they do the first couple of drafts,  
9 they will share with us their thoughts, and we'll have  
10 input and questions during that process. The second  
11 element is really risk management. We review the  
12 Company's risk management frameworks, we offer  
13 suggestions, we occasionally change policies to the  
14 extent that they're not aligned with our own policies.  
15 And then the third element of the process is performance  
16 reporting, so we look on a monthly, quarterly, and  
17 annual basis to examine the performance reports of the  
18 business, and we line those up against the business  
19 plan. That obviously provides a framework to consider  
20 the performance of the business, see whether there's  
21 anything we might do to improve the performance of the  
22 business obviously, and it also goes to the remuneration  
23 of the executives in terms of their performance against  
24 the plan. We meet quarterly for board meetings as a  
25 general rule and monthly for asset management meetings,

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1 so there is a formal asset management group that meets  
2 and considers management accounts on a monthly basis.  
3 That's typically done by way of conference call where  
4 management sends the reports, usually with far less on  
5 than we would like but promptly before the call, and we  
6 go through the metrics of the past month. That enables  
7 that subgroup of the board really to see if there are  
8 any emerging trends in the business that then go to  
9 obviously inform the more formal board meetings where  
10 strategic decisions may be taken.

11 COMMISSIONER JONES: Thank you, that's all I  
12 have. I'll have some more questions I think later, but  
13 that's it for the panel, thank you.

14 JUDGE MOSS: Okay, if there's nothing further  
15 from the Bench, and there does not appear to be at this  
16 time, we offer the opportunity to counsel for the other  
17 parties, I guess specifically in this case we're looking  
18 at you, Mr. ffitch, since you're the opponent here, if  
19 you have follow-up questions to what we heard this  
20 morning. Now, of course, as you and I have discussed  
21 and I have copied all parties on the E-mail exchanges  
22 and phone conversations that we've had and so forth,  
23 this is not the time for cross-examining the individual  
24 witnesses that you've identified, you will hold that  
25 until later. But in terms of things you heard this

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1 morning and early this afternoon from the Bench, I want  
2 to give you the opportunity if you have any follow up.  
3 If not, we'll move on to the individual witnesses.

4 MR. FFITCH: Thank you, Your Honor.

5 JUDGE MOSS: Mr. ffitich, excuse me, I'm going  
6 to have to interrupt you. Chairman Sidran has -- that's  
7 all right, go ahead then.

8 MR. FFITCH: I don't have any extensive  
9 follow up. I'm prepared to go ahead with the  
10 individualized cross-examination. Obviously there are  
11 some of these areas we'll come back to in different  
12 ways.

13 JUDGE MOSS: Sure.

14 MR. FFITCH: But I did have one clarification  
15 point on a matter of confidentiality. Mr. Leslie named  
16 a figure with respect to accordion financing, and I  
17 wanted the joint applicants or counsel for joint  
18 applicants to clarify whether that is intentionally now  
19 no longer confidential.

20 MS. CARSON: That has been confidential  
21 information, is that something that you want to waive?

22 MR. KUPCHAK: Do we have a choice?

23 JUDGE MOSS: To the extent that it's been  
24 publicly disclosed here today, I think the waiver has  
25 been effected.

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1           MR. FFITCH: I just wanted to clarify that  
2 for the record, thank you, Your Honor.

3           JUDGE MOSS: You're welcome.

4

5                           E X A M I N A T I O N

6 BY CHAIRMAN SIDRAN:

7           Q. I just have one clarifying question I would  
8 like to ask about the meaning of the word region in the  
9 commitment. This is number 41 that refers to board  
10 members, a certain number of the board of directors will  
11 be from the region, which is different I take it from  
12 the service territory because that is used in another  
13 place in the commitments with regard to the location of  
14 the corporate headquarters. I have my own sense of what  
15 the region encompasses, and sometimes that includes  
16 British Columbia and sometimes it doesn't. What does  
17 the region mean?

18           A. (Mr. Leslie) It generically has to mean the  
19 Pacific Northwest. We also have Bill Ayer who has of  
20 course affiliations with Alaska and Hope Simon who is  
21 local Seattle region and obviously Steve Reynolds who is  
22 the present CEO. So they all qualify, and we would  
23 expect that people from the Pacific Northwest  
24 generically. I don't think we put a hard boundary on  
25 it, but in a conceptual sense it has to be somebody who

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1 has close association with the Seattle region and  
2 understands the issues which may be important to the  
3 local constituents.

4 Q. Well, of course the local constituents would  
5 not want themselves perhaps associated with the Seattle  
6 region, but that's another matter. So you take the  
7 region to mean, the parties take the region to mean the  
8 Pacific Northwest, not for example Puget Sound?

9 A. (Mr. Markell) that's correct. I guess  
10 there's actually a legal geographic definition for the  
11 Bonneville Power area that involves several parts or  
12 most of the Pacific Northwest as generally understood  
13 what that means. That's as good a definition as I could  
14 offer about the region.

15 CHAIRMAN SIDRAN: Thank you.

16 MR. FFITCH: Your Honor, I do have a follow  
17 up, Chairman Sidran anticipated one of my later  
18 questions.

19

20 E X A M I N A T I O N

21 BY MR. FFITCH:

22 Q. Since we're on the topic, I guess I can just  
23 follow up first with Mr. Markell, but that region under  
24 the Bonneville definition includes portions of Canadian  
25 provinces, does it not?

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1 A. (Mr. Markell) I believe it does.

2 Q. British Columbia?

3 A. (Mr. Markell) It's the drainage basin for  
4 the Columbia River I believe how the geographers define  
5 that, I guess that would pick up part of British  
6 Columbia.

7 Q. And does it also include portions of Alberta?

8 A. (Mr. Markell) It probably does. I can --  
9 just to be clear, we have not had a geographic  
10 definition around what the region meant, whether it's --

11 A. (Mr. Leslie) If you would prefer, we'll  
12 constrain to the American portions of the Pacific  
13 Northwest, I'm sure that's something we would consider.

14 CHAIRMAN SIDRAN: I don't want to appear  
15 provincial, I'm just trying to establish if there's a  
16 meaning that the parties intended with respect to the  
17 word.

18 MS. CARSON: Chairman, I'm being told that it  
19 is the BPA Columbia Basin area, it only includes the  
20 U.S. portion, so it does not include British Columbia or  
21 Alberta.

22 CHAIRMAN SIDRAN: Okay.

23 MS. CARSON: So if we're using the BPA  
24 definition, it's just the U.S.

25 CHAIRMAN SIDRAN: Thank you.





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1 MS. CARSON: Excuse me, Judge Moss, we did  
2 have one follow-up area that we would like to pursue if  
3 we could.

4 JUDGE MOSS: Tell me what that is.

5 MS. CARSON: It relates to the question this  
6 morning about whether or not the investors would make  
7 themselves available here, and it was left that  
8 Mr. Leslie is in New York but --

9 JUDGE MOSS: So this would just be by way of  
10 supplementing your response to a previous question?

11 MS. CARSON: Right.

12 JUDGE MOSS: Okay, I will allow that.

13 MS. CARSON: Specifically I would like one or  
14 all of the Canadian investors to speak to that, if  
15 that's acceptable.

16 JUDGE MOSS: Well, let's try to keep it to  
17 one.

18 MS. CARSON: Okay.

19 CHAIRMAN SIDRAN: Would that be in English or  
20 in French?

21 MS. CARSON: Actually in English, he is from  
22 Toronto, Mr. Mark Wiseman.

23 MR. WISEMAN: (French)

24 JUDGE MOSS: We won't expect that to be  
25 transcribed.

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1                   Please introduce yourself.

2                   MR. WISEMAN: Thank you, it's Mark Wiseman,  
3 I'm the Senior Vice President of Private Investments at  
4 the Canada Pension Plan Investment Board.

5                   JUDGE MOSS: And were you here earlier to be  
6 sworn?

7                   MR. WISEMAN: I was indeed.

8                   JUDGE MOSS: Thank you.

9

10 Whereupon,

11   MARK WISEMAN,  
12 having been first duly sworn, was called as a witness  
13 herein and was examined and testified as follows:

14

15                   MR. WISEMAN: One thing I just wanted to say,  
16 and I will speak on behalf of the Canada Pension Plan  
17 Investment Board but also on behalf of my colleagues at  
18 the British Columbia Investment Commission  
19 Corporation --

20                   MR. FITCH: Your Honor, if I can interject,  
21 I'm not sure where Mr. Wiseman is going, but he's not in  
22 our view permitted at this point to provide additional  
23 direct testimony on general topics. I believe he's been  
24 called up to address one specific question from the  
25 Bench.

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1                   JUDGE MOSS: One specific question, that's  
2 right.

3                   MR. WISEMAN: And I will keep my response to  
4 that and also my colleagues from Aimco who are here, but  
5 just that we -- this is a very important investment to  
6 us. It's obviously a very large investment amounting to  
7 hundreds of millions of dollars, and it would be our  
8 intention to make ourselves available as required by the  
9 regulator. We are a long-term investor, and the return  
10 on our investment in the long term is dependent on us  
11 having a good relationship with this regulator and any  
12 other regulator that we would have dealings with. And  
13 therefore although we may not have a legal incumbency to  
14 make ourselves available, it would be folly for us not  
15 to do so. And I think it was important that the  
16 Commission hear that and understand that, and we  
17 certainly are very committed to the investment and to  
18 making ourselves available, as we have today.

19                   JUDGE MOSS: Okay, I think we take the point,  
20 thank you very much.

21                   MR. WISEMAN: Thank you.

22                   JUDGE MOSS: All right, now we're going to  
23 release the panel, I want to move on. All right,  
24 panelists, you may please step down.

25                   Since we are not able to have Mr. Horton as

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1 we previously discussed, Mr. Reynolds I believe is the  
2 first witness indicated in our order of witnesses.

3 I believe you were here to be sworn  
4 previously, were you not?

5 MR. REYNOLDS: Yes.

6 JUDGE MOSS: You may proceed, Mr. ffitch.

7 MR. FFITCH: Thank you, Your Honor.

8 JUDGE MOSS: I'm sorry, Mr. ffitch, let me  
9 interrupt because there is a matter of business we need  
10 to take care of with respect to Mr. Reynolds, and indeed  
11 with respect to the witnesses who will follow, and that  
12 is that while we had our panelists this morning and we  
13 have certain exhibits that pertain to those panelists, I  
14 don't think there's going to be any controversy with  
15 respect to the admission of the exhibits identified on  
16 our exhibit list 301 through 307, which is all the  
17 various testimonies and so forth that relate  
18 specifically to the multi-party settlement agreement.  
19 And so absent objection, I will make those Exhibits 301  
20 through 307 as previously identified part of our record,  
21 and I will furnish a copy of the exhibit list to our  
22 court reporter at the end of the day.

23 In addition to that, I will go ahead and  
24 identify the Bench Exhibits so far, 401 through 418, and  
25 then we've had some other Bench Requests today. It's my

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1 intention to make the responses to the Bench Requests  
2 exhibits in the proceeding, is there any objection?

3 Hearing no objection, those will be admitted  
4 as marked, and then we'll supplement to the extent other  
5 parties wish to respond within the next couple days or  
6 to the extent we have additional responses.

7 Now with respect to the remaining prefiled  
8 testimony and exhibits, I will turn to you first,  
9 Ms. Carson, and ask was it the joint applicants'  
10 intention to seek the admission of all of the joint  
11 applicant's and the Company's and for that matter the  
12 other joint parties' witnesses' prefiled testimony and  
13 exhibits?

14 MS. CARSON: Yes, that's correct.

15 JUDGE MOSS: And, Mr. Ffitch, do you have  
16 objection to any of that?

17 MR. FFITCH: We do not, Your Honor, with the  
18 understanding that we can conduct the cross-examination  
19 that we've outlined with the exhibits that we have.

20 JUDGE MOSS: Well, of course we have allowed  
21 for you to conduct the cross-examination of the  
22 witnesses you've identified. Now of course your  
23 cross-examination remains subject to any objection that  
24 someone might raise.

25 MR. FFITCH: Certainly.

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1                   JUDGE MOSS:  And if there's any guidance from  
2 the Bench that that might affect that.  Okay then, it's  
3 my understanding then that we can admit the prefiled  
4 testimonies and exhibits of the various witnesses  
5 including Mr. Reynolds, which is why I took this pause  
6 at the time I did, and those will be made part of the  
7 record as they have been previously identified and  
8 marked.

9                   Now we also have I will call it a significant  
10 volume, if you will, of presubmitted prefiled proposed  
11 cross-examination exhibits, have the parties had an  
12 opportunity to consider those as between themselves and  
13 whether there are some as to which we may stipulate or  
14 all as to we may stipulate, is there objections to some,  
15 have you all worked all that out?

16                   MS. CARSON:  We have worked much of it out, I  
17 think there are still a few that Mr. ffitch and I need  
18 to discuss, some that need to be supplemented perhaps,  
19 I'm not sure if Mr. ffitch has done that.  Certainly as  
20 to Mr. Reynolds there are no objections as to his  
21 cross-examination exhibits.

22                   JUDGE MOSS:  All right, then what I'm going  
23 to do is I'm going to admit all of the prefiled  
24 testimonies and exhibits as I previously indicated, and  
25 for present purposes I will also admit, Mr. ffitch, I

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1 show just one proposed cross-examination exhibit for  
2 Mr. Reynolds, and that's marked 136HC.

3 MR. FFITCH: Actually, Your Honor, I think we  
4 can withdraw that because it's the subject of a Bench  
5 Request.

6 JUDGE MOSS: All right, very good, then we  
7 don't have anything we need to worry about.

8 All right, at this time it would be  
9 reasonable to go ahead with your cross-examination, I  
10 apologize for interrupting you in that way.

11 MR. FFITCH: Your Honor, the only other  
12 matter in that vein is Mr. Hill's testimony and  
13 Ms. Alexander's testimony for Public Counsel, did you  
14 want to address those?

15 JUDGE MOSS: Do the parties intend to  
16 stipulate those testimonies and exhibits into the record  
17 as well, is there no objection?

18 MS. CARSON: No.

19 JUDGE MOSS: Hearing no objections,  
20 Mr. Hill's and Ms. Alexander's testimonies and exhibits  
21 as prefiled and as marked in our exhibit list will be  
22 admitted.

23 MR. FFITCH: Thank you, Your Honor.

24 JUDGE MOSS: You're welcome.

25 Now you may proceed with your questions,



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1 thank you.

2 MR. FFITCH: Thank you.

3 Whereupon,

4 STEPHEN P. REYNOLDS,

5 having been first duly sworn, was called as a witness

6 herein and was examined and testified as follows:

7

8 C R O S S - E X A M I N A T I O N

9 BY MR. FFITCH:

10 Q. Good afternoon, Mr. Reynolds.

11 A. Good afternoon, Mr. ffitch.

12 Q. I want to start out by asking you to look at  
13 the chart which is sitting next to you, do you recognize  
14 this as an enlargement of the Appendix B of the  
15 multi-party settlement, which I think is Exhibit 301?

16 A. Yes, I do.

17 MR. FFITCH: And, Your Honor, can I approach  
18 the witness?

19 JUDGE MOSS: Yes, you may, but not too  
20 closely, Mr. ffitch.

21 BY MR. FFITCH:

22 Q. Mr. Reynolds, can I ask you to a draw a box  
23 around Puget Energy as it currently exists and Puget  
24 Sound Energy.

25 JUDGE MOSS: And I'm going to interrupt again

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1 and ask if Mr. ffitch can be handed the portable  
2 microphone which we have in the room. Mr. Parvinen is  
3 bringing that up now, Mr. ffitch. It is particularly  
4 important for those on the conference room line who  
5 otherwise would not be able to hear you.

6 MR. FFITCH: Thank you, Your Honor. I'm told  
7 it's already on.

8 JUDGE MOSS: Well, we'll have to hope for the  
9 best, I can't tell.

10 BY MR. FFITCH:

11 Q. I'll just repeat my question then,  
12 Mr. Reynolds, could you draw a box around Puget as it  
13 currently exists with the magic marker.

14 A. I would be glad to. I will note it's a green  
15 magic marker.

16 Q. And just --

17 CHAIRMAN SIDRAN: Mr. ffitch, I just want to  
18 interrupt with all due respect to Judge Moss, could I  
19 ask that Staff confirm whether people on the bridge line  
20 can hear Mr. ffitch through this microphone in some way,  
21 because it is not audibly on in this hearing room, and I  
22 know that there are people who would like to follow this  
23 proceeding. If they can't hear his questions, that will  
24 be difficult. So is there some way that we can confirm  
25 that this is actually functional? Otherwise, perhaps,

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1 Mr. ffitch, you can use Mr. Van Nostrand's microphone  
2 which is conveniently located there.

3 MR. FFITCH: Actually, Your Honor, I was  
4 pretty much done with this portion.

5 JUDGE MOSS: So you can resume your seat.

6 MR. FFITCH: Yeah.

7 JUDGE MOSS: Great, solves the problem.

8 We apologize to those on the bridge line, but  
9 we've had some technical difficulties with our portable  
10 microphone system today. Mr. ffitch is going to resume  
11 his seat. And just for the purposes of those of you who  
12 did not understand the engagement we just had with  
13 Mr. Reynolds, Mr. ffitch asked him to circle on Appendix  
14 B to the multi-party settlement stipulation that portion  
15 of the post acquisition organizational chart that  
16 exhibits the current Puget Energy Inc. and Puget Sound  
17 Energy Inc., and he circled the bottom two boxes with a  
18 green magic marker.

19 Go ahead, Mr. ffitch.

20 MR. FFITCH: Thank you, Your Honor.

21 BY MR. FFITCH:

22 Q. That's the status quo right now, isn't it,  
23 Mr. Reynolds?

24 A. That's our current Puget Energy structure,  
25 that's correct.

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1 Q. And you are currently President and CEO of  
2 both of those entities, both Puget Energy and PSE,  
3 correct?

4 A. I am Chairman, President, and CEO of both  
5 entities, that's correct.

6 Q. All right.

7 A. As amended.

8 Q. So you are Chairman of the Board of both of  
9 those as well as being President and CEO?

10 A. Correct.

11 Q. And in your testimony initially, your direct  
12 testimony, you state you will continue as President and  
13 CEO of Puget Sound Energy; is that still correct?

14 A. That's correct.

15 Q. And are you also going to continue as  
16 President and CEO for Puget Energy?

17 A. I will be a board member, I'm not sure that  
18 we've determined whether or not there will be officers  
19 for Puget Energy, but I will be a board member of Puget  
20 Holdings and --

21 Q. I'm asking if you are going to be the  
22 President and CEO of Puget Energy?

23 A. Why not, let's assume that I will be.

24 Q. Do you not know the answer to that question?

25 A. There are a number of organizational issues

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1 that have been -- that it's been a bit premature to make  
2 final determinations about, but I believe that the  
3 intention we've discussed would be for me to be the CEO  
4 at any of the different organizational levels.

5 Q. All right. Now post closing you state, your  
6 testimony contains an exhibit that states that you will  
7 be on the board of managers of Puget Holdings; is that  
8 right?

9 A. That's correct.

10 Q. And that's covered in the press release  
11 that's attached to your testimony, you don't really need  
12 to go look at it, but your Exhibit SPR-5 is a press  
13 release that explains that, correct?

14 A. That's correct.

15 JUDGE MOSS: And for the record, that will be  
16 Exhibit 35.

17 MR. FFITCH: Thank you, Your Honor.

18 BY MR. FFITCH:

19 Q. Mr. Reynolds, why are you not continuing as  
20 Chairman of the Board of Puget Sound Energy or Puget  
21 Energy?

22 A. Why am I not? Primarily because I'm not  
23 convinced that it's good corporate governance for the  
24 CEO to be both the Chairman as well as the CEO, and this  
25 is an opportunity in light of the willingness of Bill

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1 Ayer to step up and be the non-executive chairman. I  
2 think its an absolutely extraordinary improvement in  
3 overall corporate governance, and I think that it's  
4 something that in discussions with the investor  
5 community they are very supportive of as well.

6 Q. But you have held all those positions,  
7 President, CEO, and Chairman of the Board with Puget  
8 Sound Energy and Puget Energy for a period of several  
9 years, have you not?

10 A. I've been Chairman about the last two and a  
11 half years. Prior to that I was President and CEO. So  
12 I'm very comfortable with having a non-executive  
13 chairman.

14 Q. Were there governance issues during the  
15 period of time that you held all those positions,  
16 governance problems?

17 A. No, but it's a matter of business focus in  
18 corporate -- in an evolving area of corporate governance  
19 where I'm very supportive of a separation between a  
20 non-executive chair and an executive internal CEO  
21 manager makes a lot of business sense to me.

22 Q. How many people are on the Puget Sound  
23 Energy/Puget Energy Board right now?

24 A. I believe there are nine.

25 Q. I have a printout from the Puget Sound Energy

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1 web site if you need some assistance with my next few  
2 questions. I count ten on this list I believe.

3 A. It would be 10 including myself, correct.

4 Q. Yeah, all right, we're on the same page then.

5 Could you go through the members of the current board of  
6 directors and tell me what their or whether they have a  
7 Washington or regional residence or affiliation, just  
8 name each one of them and a brief description of their  
9 residence or affiliation.

10 A. Sure. Our lead director who you'll have the  
11 pleasure of meeting maybe tomorrow, Phyllis Campbell, is  
12 local, President CEO of the Seattle Foundation. Another  
13 local director is Tomio Moriguchi, a CEO of Uwajimaya.  
14 Third director is Sally Narodick, the CEO of Apex  
15 Learning, and also is local in the Puget Sound area.  
16 Fourth is Herb Simon, who will also be a new director  
17 within the new consortium, who is also from the state of  
18 Washington out of Tacoma. Fifth is Bill Ayer, who is  
19 the Chairman and CEO of Alaska Airlines, and who also  
20 does reside within the state of Washington although his  
21 business profile is from Alaska to Hawaii to Mexico.  
22 Sixth is Ken Mortimer, retired President of the  
23 University of Hawaii, retired President of Western  
24 Washington University, and whose residence alternates  
25 from East Coast to the state of Washington. We also

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1 have another Washington resident, Craig Cole, the  
2 Chairman of Brown & Cole grocery stores, who resides in  
3 Bellingham. Then we have Steve Frank, the retired  
4 President and CEO of Southern California Edison utility  
5 company, who lives in Reno, Nevada. And George  
6 Watson --

7 Q. So, I'm sorry, just to interject, you  
8 wouldn't classify Mr. Frank as a local or a resident for  
9 the purposes of this --

10 A. He would not be classified as a resident, and  
11 hence as we looked at director candidates going forward,  
12 we did not look at Steve Frank.

13 Q. All right.

14 A. Though other enterprises in this state have  
15 seen fit to put him into positions of responsibility.

16 The last board member, unless I've forgotten  
17 somebody, is George Watson, who is a retired President  
18 and CEO of TransCanada and who resides in Alberta.

19 Q. And then there's yourself?

20 A. And then there's myself.

21 Q. And are you local?

22 A. You know, I reside in our gas service  
23 territory, correct.

24 Q. All right. So if I'm looking at these  
25 numbers correctly, out of 10 I count 7 local resident



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1 members of the current Board of Directors plus  
2 Dr. Mortimer would make it 7 1/2 perhaps since he shares  
3 his time; do I have that right?

4 A. That's approximately correct. I would  
5 augment maybe it would be useful, Mr. ffitch, to at  
6 least describe a little bit what happens with regard to  
7 governance in today's world with regard to board  
8 members.

9 MR. FFITCH: Well, Your Honor, I'm not asking  
10 that question. If counsel for Company wants to explore  
11 that later.

12 JUDGE MOSS: All right, fine, you can have  
13 that question on redirect.

14 In the meantime, I want to remind parties who  
15 have called in on the conference bridge line to please  
16 put their phones on mute caller. We're getting  
17 interference in the hearing room from the last caller to  
18 join us, so please do that.

19 Thank you.

20 All right, Mr. ffitch, go ahead with your  
21 questions.

22 MR. FFITCH: It may be my cross-examination  
23 is already going down the drain.

24 JUDGE MOSS: I won't remark on that,  
25 Mr. ffitch.

0583

1 BY MR. FFITCH:

2 Q. Now as you note, Mr. Reynolds, the joint  
3 applicants have committed to include Mr. Ayer on the  
4 Boards of Puget Energy and PSE, correct?

5 A. Mr. Ayer, correct, along with myself and  
6 along with Herb Simon.

7 Q. And, well, just follow me here because I'm  
8 trying to be specific, with respect to Mr. Simon, the  
9 commitment is to have Mr. Simon on the Board of Puget  
10 Sound Energy, correct?

11 A. That's correct.

12 Q. But not Puget Energy?

13 A. He would serve as the special unique director  
14 at the Puget Holding company level.

15 Q. But not Puget Energy?

16 A. You know, I'm going to basically say at this  
17 point in time I don't know. I think the commitment is  
18 that he would be -- the intention and I could -- would  
19 be that these meetings would be simultaneous, and for  
20 all intents and purposes they would meet concurrently  
21 just as the Board of Puget Sound Energy and Puget Energy  
22 does today, but there may be certain voting authorities  
23 he would not have in certain circumstances.

24 Q. Is it your testimony that the meetings of  
25 Puget Sound Energy Board of Directors and Puget Holdings

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1 Board of Directors would be simultaneous?

2 A. That's what they have been during my tenure.

3 Q. Well, Puget Holdings hasn't existed during  
4 your tenure, has it?

5 A. Excuse me, I meant Puget Energy.

6 Q. All right, so my question is, are you  
7 testifying that the meetings of Puget Holdings and Puget  
8 Sound Energy are going to be simultaneous in the future?

9 A. That is my expectation. There are a number  
10 of logistical issues to work out, but the current plan  
11 as alluded to by Mr. Leslie and others would be meetings  
12 concurrent basically scheduled much like we have had in  
13 the past, but for special reasons to convene a  
14 stand-alone meeting with either the Board of Puget Sound  
15 Energy or Puget Holdings, that they would be concurrent  
16 meetings.

17 Q. All right.

18 I want to ask you a question or two about  
19 commitment 41, I don't know if you have those. Do you  
20 have those there with you at the witness table?

21 Do you have that?

22 A. Yes, I do.

23 Q. All right. And under commitment 41, the  
24 joint applicants commit that Puget Sound Energy will  
25 have at least three directors who are residents of the

0585

1 region, one of whom would be the CEO, currently  
2 yourself, correct?

3 A. Correct.

4 Q. And it goes on to commit that Puget Energy  
5 will have at least two regional residents, one of whom  
6 is the CEO, correct?

7 A. Correct.

8 Q. So that's fewer than Puget Sound Energy by  
9 one, correct?

10 A. That's correct.

11 Q. Simple mathematics. In commitment 41, there  
12 is no commitment to any regional residents on the boards  
13 of Puget Holdings, Puget Intermediate Holdings, or  
14 Equico; is that correct?

15 A. That's correct.

16 Q. And we've already discussed this question  
17 before, but I will ask you, what is your definition of  
18 regional?

19 A. My definition of regional is the state of  
20 Washington.

21 Q. Turning to another area, Mr. Reynolds, in  
22 Bench Request Number 4, the joint applicants or Puget  
23 was asked to produce information related to your  
24 employment contract; do you recall that?

25 A. Certainly do.

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1 Q. And you produced the 2002 employment  
2 agreement and amendments related to the pending  
3 transaction, right?

4 A. I do not believe that there were any  
5 amendments relating to the pending transaction.

6 Q. Well, let's just address briefly the original  
7 agreement in 2002. The 2002 agreement is for a three  
8 year term to 2005, correct?

9 A. That was correct.

10 Q. And after that it provided for automatic  
11 renewal for one year terms, correct?

12 A. That's correct.

13 Q. With a right of termination on each side with  
14 180 days notice; am I reading that right?

15 A. You know, I'm going to assume you're correct,  
16 I don't have it in front of me.

17 Q. Is that the provision that governs your  
18 current status with Puget Sound Energy?

19 A. There was one amendment to the original  
20 contract that was made through -- that carried through  
21 2008 and some modifications in relationship to some  
22 interpretations related to how to handle certain FASB  
23 requirements.

24 MS. CARSON: Mr. Reynolds, would it be  
25 helpful for you to have Bench Request 4 in front of you?

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1 THE WITNESS: That would be great.

2 MR. FFITCH: That's fine, Your Honor, I don't  
3 have a lot more detailed questions, but I'm happy to  
4 have him look at it.

5 THE WITNESS: Dangerous chairs.

6 JUDGE MOSS: Is it all right, is it stable?  
7 We can replace it.

8 THE WITNESS: File an OSHA complaint.

9 JUDGE MOSS: You're not our employee,  
10 Mr. Reynolds.

11 THE WITNESS: No comment. I think we all  
12 work for you guys.

13 BY MR. FFITCH:

14 Q. Actually my question, maybe we can go there  
15 in a minute, my question was more to the point of your  
16 term of employment being still on an annual automatic  
17 renewal basis with 180 days notice; is that still the  
18 situation?

19 A. That's correct.

20 Q. Now you did mention that there were some  
21 amendments, one of the amendments related to the change  
22 in control provisions, correct?

23 A. That's correct.

24 Q. And do you recall when you began discussions  
25 with Macquarie regarding the potential acquisition of

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1 Puget Sound Energy?

2 A. The detailed discussions with Macquarie as  
3 reflected in the proxy that's been filed really began  
4 seriously about August and September last year.

5 Q. They didn't begin in 2005?

6 A. Not with regard to any specific transaction  
7 of the sort that's contemplated in the discussions  
8 today.

9 Q. Were there some conversations of any type  
10 with Macquarie starting in 2005?

11 A. Again as referenced in the proxy statement,  
12 we became acquainted in 2005 while they were actively  
13 engaged in watching and trying to decide whether or not  
14 to participate in the Cascade Natural Gas transaction.

15 Q. All right. And then early 2006, as Bench  
16 Request 4 indicates, there were some amendments related  
17 to change in control provisions in your contract,  
18 correct?

19 A. There were some amendments made in  
20 relationship to just I would call them clarifying  
21 language related to all of the officers' change of  
22 control agreements.

23 Q. All right.

24 I would like to now ask you about another  
25 Bench Request, and that's Bench Request 12, that's the

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1 one relating to compensation matters. Just give me a  
2 moment, I'll get my copy.

3 MR. FFITCH: Your Honor, I believe that Puget  
4 this morning distributed a new copy of that response.

5 JUDGE MOSS: Did that replace the previously  
6 submitted?

7 MS. CARSON: No, we did not submit a new copy  
8 of Bench Request 12 today, that was Bench Request 8.

9 MR. FFITCH: Well, I have a -- all right, I  
10 thought I was given a copy of Bench Request 12 today.

11 MS. CARSON: Well, we may have provided it,  
12 we filed it last week, and we may have provided it to  
13 counsel today.

14 JUDGE MOSS: Just to be sure that we're all  
15 on the right copy, what I have in my notebook is  
16 submission dated August 19th; is that the correct one?

17 MS. CARSON: I believe that is correct.

18 MR. FFITCH: Your Honor, the copy --

19 JUDGE MOSS: And it's partially confidential?

20 MS. CARSON: It is the first revised and  
21 supplemented response.

22 JUDGE MOSS: Yes, first supplemental and  
23 revised response was submitted on August 19th,  
24 Mr. ffitich.

25 MR. FFITCH: Well, maybe this is unnecessary



0590

1 confusion, the document that I was handed this morning  
2 by counsel says at the bottom, date of response August  
3 18th, 2008.

4 JUDGE MOSS: Well, that would be the day  
5 before it was filed.

6 MR. FFITCH: All right.

7 MS. CARSON: If I could clarify, I think the  
8 reason we provided that today was because the exhibit  
9 list did not reflect that it was a supplemental revised  
10 version, so we wanted to make sure that it was, but it  
11 is the same response that we filed last week.

12 JUDGE MOSS: Yes, that's correct.

13 MR. FFITCH: Sorry, I didn't mean to cause  
14 confusion, I just wanted to make sure that we were all  
15 looking at the same document.

16 BY MR. FFITCH:

17 Q. Okay, Mr. Reynolds, I'm going to take you to  
18 the third yellow page, first page of Attachment A, I'm  
19 sorry, it's not yellow, first page of Attachment A is  
20 not yellow, has your name at the top, do you have that?

21 A. I do.

22 Q. And this page of the exhibit provides the  
23 amount that you and the other or the top five officers  
24 of Puget will receive upon a change of control of the  
25 company or change of control with termination, correct?

0591

1 A. That is correct.

2 Q. And what is the amount there shown as the  
3 amount that you will receive upon change of control, in  
4 other words if this transaction is approved?

5 A. The number is \$9.626 Million.

6 Q. Does the fact that you will receive this  
7 amount affect your opinion about whether this  
8 acquisition should be approved?

9 A. As I have said very clearly in my rebuttal  
10 testimony, absolutely not.

11 Q. Do you know if this number includes all of  
12 the proceeds from the sale of all of your Puget Energy  
13 stock?

14 A. I do not believe that it includes proceeds  
15 from the sale of Puget Energy stock.

16 Q. Do you know how much additional proceeds  
17 would result from that sale?

18 A. I do not know specifically. I do have and  
19 own some stock, I'm a significant shareholder, I'm also  
20 -- I have some stock options that I'm entitled to.

21 Q. Do you have a ball park idea of what you  
22 would receive from the sale of those stock holdings?

23 A. I don't have it off the top of my head, but  
24 it's very thoroughly laid out in the proxy.

25 Q. All right.

0592

1           A.     And has been rigorously explored by you and  
2 others in the recent rate case.

3           Q.     Is there any reason why that information is  
4 not shown in response to this exhibit?

5           A.     I think that this --

6           Q.     Or Bench Request, sorry?

7           A.     I'm of the opinion that this basically tries  
8 to address the question framed in the Bench Request.

9           MR. FFITCH: Well, Your Honor, I guess I  
10 would like to make either a record requisition for the  
11 additional proceeds that would result from the sale of  
12 the stock of the top five officers shown on this page or  
13 in the alternative request that there be a supplement to  
14 the Bench Request if that is the Bench's preference.

15           JUDGE MOSS: Well, the Bench Request asked  
16 what it asked and got what it asked for. As far as the  
17 information is understood, what Mr. Reynolds just said,  
18 this information is in the proxy statement, is that  
19 right, counsel, can you confirm that?

20           MS. CARSON: I believe that's correct.

21           JUDGE MOSS: All right, well, you check  
22 during the break, and if that information is already in  
23 the record, there's no reason to ask him to supply it  
24 again.

25           MR. FFITCH: All right, thank you, Your

0593

1 Honor.

2 Those are all the questions that I have for  
3 Mr. Reynolds, thank you.

4 JUDGE MOSS: All right, questions from the  
5 Bench before we have any redirect?

6 CHAIRMAN SIDRAN: Yes.

7

8 E X A M I N A T I O N

9 BY CHAIRMAN SIDRAN:

10 Q. This is Mark Sidran. I did not understand  
11 the numbers in that last colloquy, so maybe you can  
12 explain them to me. You cited a number that was  
13 something in the range of 9.6 if I heard you correctly;  
14 is that right?

15 A. Yes, Mr. Chairman.

16 Q. So I'm looking at your name in the column  
17 upon changing control, and there are a series of numbers  
18 there and a total of \$14,568,835, what is the 9.6, how  
19 did you arrive at that number?

20 MS. CARSON: Mr. Chairman, you are looking at  
21 the original response that we filed last week. We, as I  
22 said, filed a supplemental and revised version after our  
23 HR director came back from vacation and was able to more  
24 accurately respond to this Bench Request.

25 CHAIRMAN SIDRAN: All right, bear with me one

0594

1 minute.

2 MR. VAN NOSTRAND: I have some more copies,  
3 Your Honor.

4 CHAIRMAN SIDRAN: We do not have that in our  
5 Bench book, we have the original.

6 JUDGE MOSS: We're going to get that.

7 CHAIRMAN SIDRAN: Thank you.

8 Well, while we're at it, then perhaps you can  
9 explain and simply clarify what happened requiring the  
10 clarification, what's the source of the clarification?

11 MS. CARSON: Well, I want to say we also have  
12 Mr. Tom Hunt, who is a Director of HR, who is here to  
13 explain it because it is somewhat of a detailed  
14 explanation. But as I understand it, there is a  
15 difference in either the SERP or the LTIP in terms of  
16 what Mr. Reynolds otherwise is entitled to. A portion  
17 of it he was entitled to absent the merger, and that was  
18 not accurately reflected in the first response. But if  
19 you have detailed questions, we did make sure we had  
20 Mr. Hunt available here to answer questions.

21 CHAIRMAN SIDRAN: Refresh my memory about  
22 what LTIP is.

23 MS. CARSON: It's the Long-Term Incentive  
24 Program.

25 CHAIRMAN SIDRAN: So that appears to be the

0595

1 major change just eyeballing the difference here?

2 MS. CARSON: (Nodding head.)

3 CHAIRMAN SIDRAN: All right, thank you.

4 COMMISSIONER JONES: Ms. Carson, on that  
5 point, this is Commissioner Jones, is there -- I'm  
6 getting quite confused as well, and I haven't read  
7 Mr. Hunt's explanation, but is there a line item for  
8 what is commonly referred to as a change of control  
9 payment?

10 MS. CARSON: I don't --

11 COMMISSIONER JONES: There isn't, there  
12 doesn't appear to be.

13 MS. CARSON: No, I think these --

14 COMMISSIONER JONES: This is just the  
15 long-term incentive plan, the acceleration of stock  
16 vesting options, the estimated excise tax gross-up, a  
17 cash severance.

18 A. If I might, Commissioner Jones, I believe  
19 that if you looked at the cash severance, that basically  
20 would constitute the change of control for base pay,  
21 which under our change of control agreements for all of  
22 our officers is about, you know, three times base pay.

23

24 E X A M I N A T I O N

25 BY COMMISSIONER JONES:

0596

1 Q. But is it base pay plus the targeted bonus?

2 A. Plus the targeted bonus, yes.

3 Q. Is that true for the other officers or just  
4 for you?

5 A. The only difference between myself as laid  
6 out in my employment agreement is I do have what's call  
7 a double trigger. In other words, mine goes regardless.  
8 With the rest of the officers, there's no severance  
9 paid, only if their job is eliminated as a result of the  
10 change.

11 Q. But you -- so they have a single trigger and  
12 you have a double trigger?

13 A. And I have a double trigger.

14 Q. In your employment contract?

15 A. And that goes back to the history of the  
16 employment agreement in 2002.

17 MS. CARSON: If I could clarify, I think he's  
18 reversed those, that you have a single trigger and --

19 A. Correct, I'm sorry.

20 COMMISSIONER JONES: Okay.

21 JUDGE MOSS: I think the record is clear.

22 COMMISSIONER JONES: I'm sorry, single  
23 trigger versus double trigger.

24 JUDGE MOSS: I think we probably got our  
25 clarification.

0597

1                   Let me ask if there is any redirect?

2                   MS. CARSON: There is.

3                   JUDGE MOSS: Go ahead.

4

5                   R E D I R E C T   E X A M I N A T I O N

6 BY MS. CARSON:

7           Q.     Mr. Reynolds, Mr. ffitch asked you about the  
8 directors and which ones currently are local directors,  
9 can you speak to the planned composition of the  
10 directors on the boards after the merger is complete,  
11 and tell me if you think the local interests are  
12 adequately protected by the directors that have been  
13 designated?

14          A.     Absolutely, that's been one of the key issues  
15 that we have worked on both with the current directors,  
16 it's been a high priority with our current directors,  
17 and with the prospective new owners, and the set of  
18 governance principles is starting to evolve that will  
19 give an extraordinary deference to the positions taken  
20 by the current what I would call local directors. And  
21 by local, I define that as the state of Washington.

22          Q.     And Mr. ffitch was talking with you again  
23 about the local directors, and you were elaborating on  
24 board governance issues, and you were cut off, can you  
25 go ahead and finish your thought there?



0598

1           A.     One of the trends that we have worked very  
2 diligently at at Puget Energy today, and we would  
3 continue assuming we would be stand-alone, is to  
4 continue to broaden and diversify our director base.  If  
5 you look at the most recent set of directors we've  
6 added, they have brought special expertise in some  
7 particularly important element of our business to our  
8 board, regardless of where they come from, adding  
9 somebody whose specialization is natural gas or someone  
10 who has actually worked in the energy sector or has a  
11 special skill set in finance.  And that to us, and I  
12 think it's reflected in the skill set that we will see  
13 going forward, is what we were trying to accomplish with  
14 which directors would carry forward.  Someone like Bill  
15 Ayer who's an active CEO of a current regional business,  
16 who has to deal with all of the broad based business  
17 governance issues that one has to deal with.  Someone  
18 who's active in the business community and an investor  
19 and prominent in the region like Herb Simon who's  
20 actually a University of Washington Regent as well as a  
21 very skilled real estate investor in this region.  So  
22 that would be what I would characterize as good  
23 governance on a go forward bases for Puget Energy or  
24 with the Puget Holdings director on a go forward bases.  
25 I think we've got an extraordinary set of directors.  We

0599

1 will have retirees in the next few years. In fact, we  
2 have one board member carried over by virtue of this  
3 transaction as part of looking forward to what we would  
4 add, it's the same debate we're having here, which is  
5 what additional skills would complement what already  
6 exists on the board regardless of where they're from.

7 Q. I wanted to clarify the role of Mr. Simon on  
8 the board. I think you testified that he would be on  
9 boards other than PSE's board, and I just wanted to  
10 clarify is Mr. Simon the independent director?

11 A. He will be the -- I mean again I have to  
12 admit that I'm not the detailed expert on this, maybe I  
13 should respond to that more directly, but I believe he's  
14 a PSE board member.

15 Q. Correct. And do you have an understanding of  
16 why he is on PSE's board and not on Puget Energy's  
17 board?

18 A. From a standpoint of providing some of the  
19 structural protections I think that all the settlement  
20 parties wanted and whichever one I think who's been  
21 concerned with the transaction wants, he would serve as  
22 an independent director at Puget Sound Energy and  
23 provide bankruptcy protection.

24 Q. Mr. ffitch's questions left the impression  
25 that the change of control provision in your employment

0600

1 agreement was because of this transaction; is that  
2 correct?

3 A. He sure seemed to want to imply that, didn't  
4 he, yes. The change of control adjustments that were  
5 made in all of the change of control agreements were  
6 tied to I believe it's 409(a) changes required for the  
7 deferred compensation plans, standardized across all  
8 business today, and had absolutely nothing to do with  
9 anything other than being in conformity with the new set  
10 of rules from the SEC.

11 Q. Now regarding the sale of your Puget Energy  
12 stock that you currently hold, that's, just to clarify,  
13 is that something that you're able to do because of this  
14 transaction, or would you otherwise be able to gain from  
15 the sale of that stock?

16 A. As I said, I'm a fairly significant  
17 shareholder, I've taken a large amount of compensation  
18 in stock, that's, you know, I would always have that,  
19 because I basically bought it and pay taxes on it.

20 Q. And just to clarify, the compensation that  
21 you receive if there is a change of control and  
22 specifically the compensation and the \$9 Million that's  
23 laid out in the Bench request, are customers paying for  
24 that?

25 A. As Mr. Markell indicated today, there's no

0601

1 intention whatsoever to have customers pay for any  
2 portion of any of these change of control agreements.  
3 And in addition, as I have testified in my rebuttal  
4 testimony, a significant portion of anything that I get  
5 I intend to contribute on behalf of -- to the Puget  
6 Sound Energy Foundation on behalf of the customers and  
7 communities that we serve in this particular state.

8 Q. Were there procedures that were put in place  
9 when the board was considering this transaction to make  
10 sure there was no conflict of interest in terms of pay  
11 that you or others would get on the change of control?

12 A. Yes, there was our compensation committee  
13 independently reviewed whether or not there was any  
14 conflict associated with my own position and separately  
15 any of the officers' position with regard to  
16 consideration of this. They identified it, they went  
17 through the same discussion we're having here but with  
18 far more rigor, and were acutely concerned about that.  
19 They as well as with regard to any perception of their  
20 own compensation clearly separated that from the issue  
21 of whether or not they would recommend this particular  
22 transaction to shareholders. It was something that they  
23 were acutely aware of, and in particular, as Mr. Markell  
24 said earlier today, we walled off all management from  
25 deliberations, and final deliberations at the full board

0602

1 were done without me, so.

2 MS. CARSON: Thank you, I have nothing  
3 further.

4 JUDGE MOSS: Okay.  
5 Commissioner Jones.

6

7 E X A M I N A T I O N

8 BY COMMISSIONER JONES:

9 Q. I'm moving away from your employment  
10 agreement.

11 A. Thank you.

12 Q. Not to say that it's not important.

13 A. I understand.

14 Q. I'm going to go back to your rebuttal  
15 testimony and get into the larger issue of raising  
16 capital on "reasonable" terms, and I specifically refer  
17 you to page 10 or page 12 if you have that in front of  
18 you.

19 JUDGE MOSS: What's the exhibit number,  
20 Commissioner Jones?

21 COMMISSIONER JONES: Oh, I'm sorry, rebuttal  
22 is 133.

23 JUDGE MOSS: Thank you. And your page?

24 COMMISSIONER JONES: Page 12.

25 JUDGE MOSS: Thank you.

0603

1 BY COMMISSIONER JONES:

2 Q. Tell me when you're there, Mr. Reynolds.

3 A. I'm there.

4 Q. Okay. You've been in the utility business  
5 for a long time, haven't you, how long?

6 A. Do I have to answer that?

7 Q. Yes, you do.

8 A. 40 years.

9 Q. Hasn't the raising of external capital,  
10 whether it be equity primarily because of the dilutive  
11 effect of that on earnings or fixed income, hasn't it  
12 always been challenging, and wasn't it very challenging  
13 during the last capex cycle, capital expenditure cycle,  
14 in the 1970's?

15 A. Yes, it was tough during the mid '70's, high  
16 inflation, a tough market to raise equity, yes.

17 Q. You also state on lines 5 and 6 that you have  
18 raised \$800 Million of capital through four equity  
19 issuances totalling 37 million common shares?

20 A. That's correct.

21 Q. So could you just summarize for us, summarize  
22 for me at least, the equity issuances during your tenure  
23 as Chairman and CEO, and approximately how large, and do  
24 you recall who the underwriter is?

25 A. Yes, we -- and I would just say we have spent

0604

1 an inordinate amount of time and energy in financial  
2 markets since 2002 trying to improve our balance sheet,  
3 and we've made remarkable progress, and that's reflected  
4 by about 6 million shares in 2002, which was largely  
5 done as a bought deal with J.P. Morgan.

6 Q. That was 2002, and what was the net issuance  
7 amount of that?

8 A. About 115, we issued 5.75 million shares, I  
9 think proceeds were about \$115 Million.

10 Q. What percent of market cap was that at the  
11 time?

12 A. I don't have my calculator with me, but the  
13 market cap was probably about \$2.3 Billion at the time,  
14 so it would be \$115 Million divided by 2.3.

15 Q. So about 4%, 5%, something like that. Wasn't  
16 there an issue, Mr. Reynolds, before your time in 2001,  
17 are you aware of that one?

18 A. No.

19 Q. Of 370 million or above 350 million?

20 A. I'm unaware of that, I'm not familiar with  
21 that, that's not my recollection of our corporate  
22 history.

23 Q. Okay.

24 A. We did another in November of 2003, another  
25 100 million shares, that was a bought deal with Franklin

0605

1 Advisors, one major investor stepped up and bought that  
2 whole transaction.

3 Q. And how much was that?

4 A. About 100 million.

5 Q. Okay, keep going, I would like to get to 800  
6 million.

7 A. We did a very large deal in November 2005, 15  
8 million shares, \$310 Million raised. Lehman Brothers  
9 took that again on a bought deal and then marketed it.  
10 And I think as I mentioned in my testimony, and it was a  
11 very, very difficult transaction to accomplish by the  
12 time -- but for the approach that was taken, the type of  
13 transaction that we did. They suffered. We did fine,  
14 we got out with our money, but it was very clear that we  
15 were issuing too many shares at a point in time that the  
16 market was saturated with Puget stock. That was a very  
17 large offering for us, and we learned a lot of lessons  
18 associated with that one, as I say in my testimony.

19 Q. But from a Puget perspective, was there any  
20 concern about the discounts or the terms offered or the  
21 execution of the issuance, was there any major problem  
22 with that issuance?

23 A. We were -- and I would compliment our  
24 management team, I think that from a Puget standpoint we  
25 fixed a good price, and the business risk was



0606

1 transferred to Lehman Brothers to a large degree.

2 Q. Okay.

3 A. And then the last issuance was the issuance  
4 in November of last year that was done by the  
5 consortium, 12 1/2 million shares was picked up for  
6 again almost \$300 Million prebought as part of our  
7 transaction here and which has really boosted us up from  
8 an equity standpoint to pretty close to 47% equity right  
9 now, which is one we -- skeptical that in this market we  
10 could have done anywhere near what we were able to do  
11 with that particular equity offered.

12 Q. So the market cap, go back to 2005 for a  
13 minute, the market cap at that point was maybe 2.3  
14 billion or so, so that \$310 Million equity issuance was  
15 significantly larger as a percentage of your market  
16 capitalization, correct?

17 A. Though our market capitalization went up  
18 considerably after the announcement of this transaction,  
19 so.

20 Q. So the issue, Mr. Reynolds, is, I think  
21 Public Counsel has issued a data request on this and I  
22 think you mentioned it in your rebuttal testimony, the  
23 issue is not the access to capital, Puget has adequate  
24 access to capital, correct?

25 A. As --

0607

1 Q. Excuse me, it's the terms on which that you  
2 can raise the capital, is that the primary point that  
3 led to this transaction?

4 A. As we've said numerous times in our written  
5 testimony, rebuttal testimony, we have now seen what we  
6 can do raising capital as a small to mid cap player.  
7 And as we look forward, as Mr. Leslie and Mr. Markell  
8 said earlier, as we look forward the next five years,  
9 becoming a serial issuer of equity is going to be very,  
10 very difficult for us. The low hanging fruit with  
11 regard to additional equity we think is pretty well  
12 gone.

13 Q. What do you mean by serial, that is a  
14 pejorative term, is it not?

15 A. It means we will be in the equity markets  
16 very regularly. If we're looking at upwards to \$5  
17 Billion worth of capital in the next five years, that  
18 means that about once a year on average you're going to  
19 be out looking at upwards to 200 plus million dollars  
20 worth of equity, again on average.

21 Q. But haven't you been in the equity and debt  
22 markets constantly for the past eight to ten years?

23 A. We have been for the last six to seven years.  
24 And as I said earlier, each time we've been there it's  
25 become increasingly difficult to sell equity. It's been

0608

1 dilutive, it's continued to drive down stock price,  
2 we're not necessarily viewed as an attractive party from  
3 an equity standpoint.

4 Q. But isn't that true for many BBB rated  
5 utilities across the country, whether mid cap, small  
6 cap, large cap, they all face significant external  
7 capital requirements?

8 A. I think that our relative appetite for  
9 capital by being -- by virtue of having historically  
10 been generation short, we didn't own a lot of  
11 generation, we've adopted state energy policy to move  
12 directly in that direction, the level of capital that we  
13 need to go and acquire, as has been pointed out by  
14 others, is disproportionate to our own market size.  
15 Therefore it makes it more and more difficult, and  
16 that's what we're confronting. That's what's nice about  
17 having a set of investors here who are patient  
18 investors, whose sense with regard to the timing isn't  
19 tied to how close to a rate case decision are we going  
20 to issue equity, how close to when are we going to be  
21 out dealing with giving earnings guidance, all of which  
22 tend to make it very, very difficult with regard to when  
23 you're able to sell and how satisfactorily you will be  
24 able to sell more equity. And again, I think it's been  
25 our board's conclusion that a sustainable set of owners

0609

1 on behalf of providing access to capital on a future  
2 bases, that allows us to do what we can do best, which  
3 is go out and provide good service to customers to  
4 address the energy issues of the future, is an  
5 extraordinarily high priority for us, not trying to, you  
6 know, run around Wall Street continuously trying to  
7 argue for why we need more capital and why people should  
8 invest in us.

9 Q. And do you believe that private equity is,  
10 either private equity or infrastructure asset funds of  
11 the Macquarie type, I don't know what to call them  
12 exactly, but do you think that they're not oriented  
13 towards performance? Didn't Mr. Leslie say today that  
14 they have very strong monthly meetings, and one of their  
15 key criteria is performance? Performance means to me  
16 short term as well as medium term, what does it mean to  
17 you?

18 A. What it means to me, and again I think you  
19 would find our entire management team perfectly  
20 comfortable with performance, we want to be held  
21 accountable, and we believe we can deliver on that, but  
22 we also want the ability to have people who are there  
23 for the long run, that understand and will be  
24 appreciative of whether it's storms or whether it's what  
25 happened with a regulatory disallowance or things of

0610

1 that sort that impact our forward looking earnings, that  
2 they will stay with us. And what we have here is a very  
3 diversified consortium, a very different set of players,  
4 that bring that patient capital to us. And I look  
5 forward to those performance discussions with them. I  
6 think that they can be of some help to us, and first and  
7 foremost they will be in a position to provide the  
8 capital that we believe our customers and the  
9 communities we serve need.

10 Q. What specific assurances are there in the  
11 transaction commitments that they are actually going to  
12 supply that capital, Mr. Reynolds?

13 A. I feel very, very comfortable with regard to  
14 the commitments that are there in the short run for the  
15 first five years, and I feel very, very comfortable with  
16 regard to it, and I would challenge you to ask the  
17 settlement parties that question themselves.

18 Q. I will, but I'm asking you now.

19 A. I feel very, very comfortable based on the  
20 due diligence we've done, the detailed discussions that  
21 we've done, not only myself, our management team, but  
22 more importantly our Board of Directors in agreeing and  
23 supporting something like this. I don't think it's  
24 often really understood, boards of directors don't go  
25 about supporting things like this unanimously without a

0611

1 lot of agony and the sense that this is the right thing  
2 for them to do.

3 Q. Shifting a bit, you mentioned due diligence,  
4 how much due diligence did you actually apply to the  
5 "option" called execution of business plan, the  
6 stand-alone option? My understanding is that there were  
7 several alternatives presented, and you have to clarify  
8 for me here because you're Chair, President, and CEO,  
9 you're being advised by Morgan Stanley as Chair of the  
10 Board or as CEO, because you fulfill both boards, but  
11 Morgan Stanley provided several strategic alternatives  
12 to the Company's Board throughout 2006, 2007, correct?

13 A. During 2006 we engaged Morgan Stanley  
14 primarily because we had not used Morgan Stanley for  
15 anything else. As you went through the list of who  
16 worked with us from an equity and a debt standpoint, we  
17 had not used Morgan Stanley, and in early 2006 we  
18 engaged them to advise the Board with regard to what was  
19 happening in the industry at large.

20 Q. So just, excuse me just for a minute, the  
21 Board engaged Morgan Stanley in 2006, because the  
22 definitive agreement according to the proxy statement  
23 was not signed until October of 2007?

24 A. That's correct. Morgan Stanley participated  
25 in a series of Board discussions starting in 2006 by --

0612

1 brought to -- management basically asked them to come,  
2 we did not pay anything, for their basically basic  
3 background work with regard to what was going on in the  
4 industry. We had done the same thing the prior year  
5 with a different investment banking firm. Part of what  
6 a board does, it's not dissimilar from what Mr. Leslie  
7 said takes place with some of his portfolios companies,  
8 is every year you stop and take a snapshot of where is  
9 your business today, and what are the current issues,  
10 and where could it and should it be going on a forward  
11 looking bases. And particularly at a point in time when  
12 boards are continuously reminded of their fiduciary  
13 responsibility as board members to loyalty, duties,  
14 things along those lines, and so getting a third  
15 parties' view of what's happening in the industry is  
16 very instructive. Morgan Stanley did that for us in New  
17 York in April of 2006 and followed up with a more robust  
18 presentation of what was happening in the industry and  
19 some options later on in 2006. And you're absolutely  
20 right, we did not finally engage Morgan Stanley, the  
21 Board did not get involved in the transaction until we  
22 felt we were comfortable that we wanted to consider a  
23 transaction, and that was really mid 2007.

24 Q. But isn't it fair to say that of the six or  
25 seven strategic options that were outlined by Morgan

0613

1 Stanley, that the execution of the business plan was the  
2 default option or it was the option default because that  
3 was what management, and you're the head of management,  
4 right, CEO, Mr. Markell reports to you, right, so the  
5 business update in the capex plan was being updated per  
6 management as well?

7 A. Correct.

8 Q. So the point I'm driving at is how much due  
9 diligence, once you employed or had Morgan Stanley  
10 provide you with financial advisory services, how much  
11 time did you actually spend on the other options, and  
12 specifically the stand-alone option? It appears to me  
13 that you were quite preoccupied with M&A activity.

14 A. Commissioner, with all due respect, I would  
15 disagree with that, we were not preoccupied with M&A  
16 activity. We have been preoccupied since 2002 with  
17 rebuilding the financial health of the utility, with  
18 trying to determine what can and should be done with  
19 regard to improving in that direction. We have spent an  
20 inordinate amount of time issuing equity, disposing of  
21 unregulated affiliates, and again taking the proceeds of  
22 say our sale of our infrastructure subsidiary and  
23 plowing it back into the utility. We have continued to  
24 look at better ways, and I think a number of different  
25 concepts have been brought forward in front of this



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1 Commission numerous times to try to see what could be  
2 done in order to improve the financial attractiveness of  
3 the stand-alone utility with the purposes of trying to  
4 make ourselves look more -- perform better in the public  
5 marketplace. So we have been absolutely dedicated to  
6 the stand-alone, and in fact we still are. I think the  
7 only thing that's different here is we found a different  
8 source of capital which we think will allow us to  
9 execute our stand-alone business plan better.

10 JUDGE MOSS: Commissioner Jones, let me  
11 interrupt and ask how much more you have for this  
12 witness, we've been going nearly two hours, I want to  
13 give the court reporter a break.

14 COMMISSIONER JONES: I have two or three more  
15 questions, so maybe we could --

16 JUDGE MOSS: A few more minutes, do you want  
17 to continue?

18 COMMISSIONER JONES: I would prefer to take a  
19 break.

20 JUDGE MOSS: All right, let's go ahead and  
21 take our break now for the afternoon break, let's be  
22 back at 3:35, please.

23 (Recess taken.)

24 JUDGE MOSS: We will continue our questions  
25 from the Bench. Commissioner Jones, did you have

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1 anything further?

2 COMMISSIONER JONES: Yes, I had one last  
3 question.

4 BY COMMISSIONER JONES:

5 Q. Mr. Reynolds, you mentioned that in, what was  
6 it, 2002, 2003, that you had a bought placement with  
7 Franklin Mutual Fund Company, Franklin Investors?

8 A. Franklin Advisors, correct.

9 Q. Franklin Advisors. How has that investment  
10 worked out for them, and what kinds of things are you  
11 hearing from them about your stock in terms of the  
12 dividend, the business case that you presented to them?

13 A. Franklin Advisors is one of our single  
14 largest, if not the single largest, shareholder prior to  
15 the investment by the consortium. They have actually  
16 met with our Board to talk about what their view of  
17 investment in the utilities sector is. You may recall  
18 that Franklin Advisors was one of those entities who  
19 opposed the TXU deal publicly for an inadequate price.  
20 I have had conversations with Franklin Advisors, and I  
21 would say Franklin Advisors is strongly supportive of  
22 this transaction, they voted their entire shares in  
23 support of it, thought that this was an extremely  
24 appropriate transaction to propose based on price and  
25 based on the long-term prospects for their investment.

0616

1 Q. And have you met with your other current  
2 institutional investors as well frequently over the last  
3 year or two while this transaction has been taking  
4 place?

5 A. During the pendency of the shareholder vote,  
6 couldn't meet, sort of like can't talk with you guys.  
7 But once the shareholder vote was concluded, we had  
8 several discussions with the major investors, and again  
9 they're very complimentary of this particular  
10 transaction.

11 Q. I'm going to ask a couple of questions, I  
12 would appreciate a yes or no response. Isn't it true  
13 that you pay an above average dividend yield compared to  
14 other utilities, isn't that in the record?

15 A. I'm trying to determine how to answer that  
16 yes or no.

17 JUDGE MOSS: If you can't answer it yes or  
18 no, you may say so, Mr. Reynolds.

19 A. No, because current stock price -- our  
20 dividend yield is, which is fairly high for us, is not  
21 that high.

22 Q. Mr. Reynolds, I'm not talking about at the  
23 current stock price, I'm talking about prior to the  
24 transaction was announced in the markets.

25 A. At \$20 a share, our \$1 dividend yielded about

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1 5%, and that was very --

2 Q. Is that above market or not?

3 A. That would be above market at \$20 a share.

4 Q. What about your dividend payout ratio, is it  
5 above market or below market?

6 A. Our dividend payout ratio, our dividend  
7 payout is targeted to be about 60% of earnings, and we  
8 have continued as we've tried to grow earnings to reach  
9 the point where we could look at whether or not we would  
10 be able to pay out more from a dividend standpoint, but  
11 we have not gotten there.

12 Q. I thought it was higher, in the 65% to 70%  
13 range at times?

14 A. No.

15 Q. Depending on earnings of course. No?

16 A. (Shaking head.)

17 Q. Could you turn to page 13 of your testimony,  
18 my last question.

19 JUDGE MOSS: Is this the rebuttal or --

20 COMMISSIONER JONES: This is the rebuttal,  
21 Judge, this is Exhibit 133.

22 JUDGE MOSS: Thank you.

23 BY COMMISSIONER JONES:

24 Q. Page 13, lines 16 through 20, tell me when  
25 you're there, Mr. Reynolds.

0618

1 A. Page 13?

2 Q. 13, it's on this question of higher risk  
3 premium for utilities that have frequent rate cases.

4 A. Yes, I'm there.

5 Q. I guess my fundamental question here, is this  
6 really true when at least around the country I think all  
7 utilities or the majority of BBB rated utilities are  
8 filing frequent rate cases, so why, what sort of  
9 documentation do you have for this assertion that  
10 there's a higher risk premium for the uncertainty during  
11 the review process, isn't that true for all utilities  
12 with major capital expenditure programs?

13 A. I would say yes, but with a qualifier if you  
14 don't mind. And that is we are literally a 100%  
15 regulated utility today. A number of the utilities in  
16 our business base are a mixture of unregulated and  
17 regulated businesses, and in some cases those  
18 businesses, partly perhaps by virtue of the performance  
19 of their unregulated sector, are not necessarily  
20 frequent rate case filers on the regulated side of the  
21 business. We are for all intents and purposes fully a  
22 regulated utility today.

23 COMMISSIONER JONES: Thank you very much,  
24 that's the end of my questions.

25 JUDGE MOSS: Anything else from the Bench?

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1 All right, do we have anything further for  
2 Mr. Reynolds, or may we excuse him?

3 MS. CARSON: I have some follow-up questions.

4 JUDGE MOSS: All right, go ahead.

5

6 R E D I R E C T E X A M I N A T I O N

7 BY MS. CARSON:

8 Q. Mr. Reynolds, I just wanted to clarify the  
9 equity issuances that have been discussed here, both the  
10 ones leading up to today and then going forward. The  
11 800 million of equity sales by PE that's been referenced  
12 here, does that include the 300 million that was sold to  
13 the investor consortium in December of 2007?

14 A. Yes, it does.

15 Q. So if we take that out, the amount actually  
16 raised over the time period 2002 to the present is 500  
17 million; is that right?

18 A. That's correct.

19 Q. And the amount that you have to raise going  
20 forward according to your business plan is how much?

21 A. We're, as Mr. Markell said earlier, it's over  
22 the next five years it's close to 900 million plus.

23 Q. So that's approximately two times more than  
24 what you've raised over the past few years?

25 A. If you subtract out the investment from the

0620

1 new consortium, that's correct, yes.

2 MS. CARSON: I have nothing further.

3 JUDGE MOSS: Thank you.

4 Anything else?

5 All right, Mr. Reynolds, we thank you for  
6 your testimony, and with that I'm sure you will be  
7 relieved that you can step down.

8 THE WITNESS: Thank you, Your Honor.

9 JUDGE MOSS: Next we'll have Mr. Markell.

10 MR. FFITCH: Your Honor, if I may be heard  
11 for a moment, we conferred with Ms. Carson about  
12 Mr. Pettit, because of his special situation we're  
13 willing to, and because he's I think pretty much only  
14 available this afternoon, we're willing to take him out  
15 of order if he's available.

16 JUDGE MOSS: And he's appearing by telephone,  
17 is that right?

18 MR. FFITCH: Yes.

19 JUDGE MOSS: And as I recall for those in the  
20 court who don't know, Mr. Pettit had a matter in the  
21 nature of a family health matter I shall say that  
22 required him to be out of the hearing room today, but he  
23 did arrange to make himself available to us  
24 telephonically.

25 Mr. Pettit, are you there?

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1 MR. PETTIT: Yes, I am.

2 JUDGE MOSS: And were you previously sworn?

3 MR. PETTIT: Yes, I was.

4 JUDGE MOSS: All right, then Mr. ffitch will  
5 have some questions for you.

6 Mr. ffitch, how long did you estimate for  
7 Mr. Pettit?

8 MR. FFITCH: I believe one hour, Your Honor.

9 JUDGE MOSS: One hour, all right.

10 So, Mr. Pettit, it looks like you better have  
11 a comfortable chair.

12 MR. PETTIT: Not a problem, thanks.

13 JUDGE MOSS: All right, hang on a secretary,  
14 Mr. ffitch.

15 (Discussion on the Bench.)

16 JUDGE MOSS: We're going to take just a pause  
17 here for a second, Mr. ffitch, we've been discussing our  
18 scheduling here, and Mr. Reynolds was on the stand  
19 perhaps a bit longer than I had anticipated in planning  
20 our hearing management. We're going to go until 5:30  
21 this afternoon to extend our hearing day just a little  
22 bit and perhaps accomplish some more that way. Tomorrow  
23 we will begin at 9:00, and we will go until noon, and we  
24 will take a break of just over an hour and come back at  
25 1:15, and we will plan again to go until 5:30 in the



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1 evening. And then depending on where we stand then, we  
2 may start at some truly onerous hour of the day on  
3 Wednesday, so keep that in mind as you sharpen your  
4 questions today.

5 With that, Mr. ffitch, please go ahead and  
6 ask your questions of Mr. Pettit.

7 MR. FFITCH: Thank you, Your Honor.

8

9 Whereupon,

10 JUSTIN PETTIT,

11 having been first duly sworn, was called as a witness  
12 herein and was examined and testified as follows:

13

14 C R O S S - E X A M I N A T I O N

15 BY MR. FFITCH:

16 Q. Good afternoon, Mr. Pettit.

17 A. Good afternoon.

18 Q. My name is Simon ffitch, and I'm the attorney  
19 for the Public Counsel Office here in Washington, and I  
20 understand you're dealing with important family matters,  
21 thank you for being available. Hopefully we won't  
22 extend beyond our predicted time.

23 We had told your counsel the documents that  
24 we probably would be asking about, so hopefully you have  
25 those with you available. If not, let me know, and

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1 we'll figure out what to do at that point. Ms. Carson  
2 is looking at me a little quizzically but --

3 MS. CARSON: Do we need to stipulate those  
4 into the record?

5 JUDGE MOSS: The cross-exhibits?

6 MS. CARSON: Yes.

7 JUDGE MOSS: Yes, what about that?

8 MS. CARSON: We can stipulate those.

9 JUDGE MOSS: All right, well, Mr. ffitch's  
10 exhibits for Mr. Pettit as previously identified on the  
11 exhibit list will be admitted as marked.

12 MR. FFITCH: And there is one substitution,  
13 Your Honor, Exhibit 118, and I have provided copies for  
14 the Bench.

15 JUDGE MOSS: All right.

16 MR. FFITCH: It's the response to Data  
17 Request Number 3218. I have also distributed those to  
18 counsel. The only difference is page 3, this is a  
19 printout of an electronic file, and we had inadvertently  
20 not printed out all the tabs, we left page 3 out in the  
21 predistributed exhibit, so.

22 JUDGE MOSS: And what you have handed out is  
23 a complete substitute?

24 MR. FFITCH: This is a complete substitute.

25 JUDGE MOSS: All right, thank you.

0624

1 MR. FFITCH: And I believe that's been  
2 E-mailed to Mr. Pettit.

3 JUDGE MOSS: All right.

4 BY MR. FFITCH:

5 Q. Now, Mr. Pettit, you're Vice President of  
6 Booz & Company formerly known as Booz & Allen, correct?

7 A. Correct.

8 Q. Prior to that, according to your exhibits you  
9 were Head of Strategic Advisory for USB Investment Bank  
10 Global Merger and Acquisition Practice, right?

11 A. UBS Investment Bank.

12 Q. UBS Investment Bank?

13 A. Correct.

14 Q. All right. And you indicate you are also a  
15 frequent lecturer for advanced corporate finance classes  
16 at universities in the New York area, correct?

17 A. Yes, that's right.

18 Q. And you also noted in your testimony that you  
19 had published many articles; is that right?

20 A. Yes, that's right.

21 Q. And we asked you in Public Counsel Data  
22 Request 3212 that's been marked as Exhibit 114 to  
23 provide copies of those, and you provided a list of  
24 about 20 publications going back to 1998, correct?

25 A. Yes, that's right.

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1 Q. One item that you did not list or one  
2 document that you did not list in response to Exhibit  
3 114 was entitled, the WACC User's Guide, and that's now  
4 been marked as Exhibit 122; do you have that?

5 A. Yes, I do, thanks.

6 Q. Do you recall that paper, that was published  
7 in March 2005?

8 A. Yes, it has since been superseded by the  
9 first chapter of my book.

10 Q. All right. First of all, what does WACC  
11 stand for, W-A-C-C?

12 A. Weighted average cost of capital.

13 Q. Well, you've indicated this has been  
14 superseded by a subsequent publication, but just bear  
15 with me, let's take a look at what this Exhibit 122  
16 says. In the paper, you provide an estimate of the cost  
17 of equity capital for electric utility operations,  
18 correct?

19 A. Yes, that's right.

20 Q. And could you please turn to page 20 of  
21 Exhibit 122.

22 A. Appendix A?

23 Q. Appendix A, correct.

24 A. Yes.

25 Q. It says cost of capital by industry and

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1 subindustry.

2 A. Yes, this would be the expected return on the  
3 market value of capital.

4 Q. All right. And if we look down a little past  
5 halfway down on the left column, we see power, correct?

6 A. Yes.

7 Q. And it shows electric utilities and gas  
8 utilities, and if you go across to the third column  
9 under cost of equity, you've estimated the cost of  
10 equity capital for electric utility operations at 7.4%,  
11 correct?

12 A. Investors would expect return on the market  
13 value of total capital of roughly 7.4%, that's correct.

14 Q. All right. And for gas utility operations  
15 7.3%, correct?

16 A. On the market value of capital, correct.

17 Q. All right.

18 JUDGE MOSS: Let me interrupt just a second.  
19 Counsel, those of you who have your microphones on, if  
20 you could please turn them off, that would probably  
21 reduce the feedback problem, thank you.

22 Go ahead.

23 MS. CARSON: I just want to object to the  
24 extent Mr. ffitich's questioning goes beyond the scope of  
25 Mr. Pettit's rebuttal testimony, his very narrow scope

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1 of his testimony. He has published this article, but  
2 the fact that he's published this article does not in  
3 and of itself make it relevant to the testimony, and the  
4 cross-examination is on Mr. Pettit's testimony.

5 JUDGE MOSS: Okay, Mr. Ffitch, how does this  
6 tie to Mr. Pettit's testimony?

7 MR. FFITCH: Well, first of all, Your Honor,  
8 I have one more question to this line of questioning,  
9 and then I'm going to move on. But Mr. Pettit's  
10 testimony goes to the needs of investors in this  
11 transaction, the equity markets, the cost of capital in  
12 the equity markets generally, and the need for Puget  
13 Sound Energy to look at a range of sources of equity  
14 investment, so we think this is relevant to that.

15 JUDGE MOSS: All right, go ahead with your  
16 last question on this subject.

17 BY MR. FFITCH:

18 Q. Let's assume for a moment, Mr. Pettit, that  
19 the cost of equity capital to a publicly traded electric  
20 utility is currently 7.4% as you say in this paper, why  
21 would an investor need to be offered a 12 1/2% return on  
22 equity in order to provide incentive to invest in a  
23 privately held electric utility?

24 MS. CARSON: Same objection, goes beyond the  
25 scope of Mr. Pettit's testimony.

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1                   JUDGE MOSS: Mr. ffitch, beyond the scope,  
2 does Mr. Pettit testify as you just said?

3                   MR. FFITCH: This is a --

4                   JUDGE MOSS: 12.5% return on equity is  
5 required to attract investments, that's your question,  
6 isn't it?

7                   MR. FFITCH: Yes, we're still questioning on  
8 this same exhibit, Your Honor.

9                   JUDGE MOSS: I understand, but the objection  
10 is that it doesn't relate in any way to Mr. Pettit's  
11 testimony, which of course your cross-examination is  
12 limited to that, so I'm trying to ascertain in what way  
13 it ties back to his testimony. If he's not testifying  
14 on the amount of equity capital that is required to  
15 attract investors, then I don't see the relationship.  
16 I'm just trying to explore that with you, Mr. ffitch.

17                   MR. FFITCH: Well, I'm exploring a risk issue  
18 here, Your Honor, and Mr. Pettit's testimony does go to  
19 Puget's capital needs and how it attracts investment to  
20 meet those capital needs, so we think it's connected.

21                   JUDGE MOSS: All right, Mr. ffitch, I'm going  
22 to give you a little bit of latitude here, but let's be  
23 careful to confine the cross-examination to the  
24 testimony, or we're going to be here for a very long  
25 time, go ahead.

0629

1 BY MR. FFITCH:

2 Q. Do you want me to repeat the question,  
3 Mr. Pettit?

4 A. Yeah, I didn't understand where 12 1/2 came  
5 from, is that my words?

6 Q. It's a hypothetical.

7 A. I don't think I would assert 12 1/2 is what's  
8 expected.

9 Q. Well, let me restate the question. Let's  
10 assume for a moment that the cost of equity capital to a  
11 publicly traded electric utility is currently 7.4% as  
12 you say in your published paper, why would an investor  
13 need to be offered a 12 1/2% return on equity in order  
14 to provide an incentive to invest in a privately held  
15 electric utility?

16 MS. CARSON: Same objection.

17 A. I think we're comparing apples and oranges in  
18 different time periods, different situations. I didn't  
19 publish anything about 12 1/2.

20 Q. This is a hypothetical, Mr. Pettit, and  
21 assume that the equity or the investment opportunities  
22 are occurring in the same time frame in the same market.

23 A. But the 7.4 isn't in the same time frame,  
24 correct?

25 Q. In the hypothetical it's in the same time



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1 frame, an investor could be offered 7.4% as a reasonable  
2 rate of return as indicated in your testimony for a  
3 electric utility or alternatively --

4 A. My document is several years old that you're  
5 referencing.

6 Q. Do you have a different number in mind now  
7 for what is a reasonable --

8 A. I have not been called to weigh in on  
9 regulated rates of return in a rate case, but if I were,  
10 I would certainly go through that exercise.

11 Q. Well, the question --

12 JUDGE MOSS: Okay, Mr. ffitch, I think we've  
13 gone as far down this line as we can go based on what  
14 I'm hearing from the witness, so I'm going to ask you to  
15 move on.

16 MR. FFITCH: All right, thank you, Your  
17 Honor.

18 BY MR. FFITCH:

19 Q. Let's turn to page 9 of your rebuttal, that's  
20 Exhibit 111. And this is confidential, and, Mr. Pettit,  
21 we're being careful here not to actually discuss  
22 confidential information, so I may ask you to look at  
23 confidential information that's on a page but not to  
24 state that information. Right now we're in an open  
25 hearing room, so we need to, you know, observe the

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1 designations.

2 A. Okay, thanks.

3 Q. I'm looking at your testimony at lines 8  
4 through 10, and actually I don't know that that is  
5 confidential per se.

6 MR. FFITCH: Let me ask counsel for the  
7 Company, this is on yellow paper but not shaded, are  
8 lines 8 through 12 confidential?

9 MS. CARSON: No.

10 JUDGE MOSS: And I will just say in general,  
11 where we have shaded, that is consistent with our rules  
12 and our requirements. The shaded information will be  
13 treated as confidential. If it's not shaded on a page  
14 like this, then you are free to ask about it,  
15 Mr. ffitch, without concern.

16 MR. FFITCH: Thank you.

17 BY MR. FFITCH:

18 Q. Here, Mr. Pettit, you take issue with Staff's  
19 comparison of Puget's external capital needs with the  
20 Company's book value, indicating that book equity  
21 numbers tend to be distorted by accounting conventions,  
22 isn't that right, and some other factors?

23 A. That's right.

24 Q. And one of the book value problems you point  
25 to is good will; do you recall that testimony?

0632

1 A. Yes, I do.

2 Q. And could you turn to Exhibit 117, please,  
3 that's Data Request 3216.

4 A. Yes.

5 Q. Would you please read the second paragraph,  
6 well, first of all that data request asks you to explain  
7 why good will would be considered a distortion of value,  
8 correct, in part B?

9 A. Yes.

10 Q. Could you please read the second paragraph of  
11 your response.

12 A. Starting with good will?

13 Q. Correct.

14 A. (Reading)

15 Good will is a distortion because it has  
16 no value. It can not be bought or sold.

17 Lenders do not afford benefit to it,

18 value can not be associated with

19 anything specific in particular. In a

20 merger, good will appears on the balance

21 sheet in the amount by which the

22 purchase price based on enterprise value

23 exceeds net tangible assets of the

24 merged company.

25 Q. Thank you.

0633

1                   Can you please turn to page 7 of your  
2    rebuttal, and here I'm going to be asking you some  
3    questions about Exhibit 76C, which is confidential, that  
4    is the exhibit that you have referred to here in your  
5    testimony of Mr. Markell, I'm going to get my own copy  
6    here.

7                   JUDGE MOSS:   And, Mr. Pettit, while  
8    Mr. Ffitch is looking there, in your testimony this is  
9    referred to as Exhibit EMM-6C so you can see the point  
10   there where he's looking.

11                  THE WITNESS:   Thank you.

12                  JUDGE MOSS:   You're welcome.

13   BY MR. FFITCH:

14           Q.     And this has been referred to a couple times  
15   before, this is the business plan update and review,  
16   correct, dated October 19, 2007?

17           A.     Right.

18           Q.     And here I'm going to ask you about some  
19   general projections of capital needs, and I think most  
20   of these numbers are actually public, there's been a lot  
21   of discussion of these so far, but they're -- so I want  
22   to tread carefully here.

23                  JUDGE MOSS:   Well, let's just stop and ask  
24   then, how about the numbers in that second full  
25   paragraph there on page 7, are those remaining

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1 confidential, do those remain confidential or not?

2 MS. CARSON: I believe they are.

3 JUDGE MOSS: All right, then you'll have to  
4 proceed accordingly, Mr. ffitch.

5 MR. FFITCH: All right.

6 BY MR. FFITCH:

7 Q. Well, let's look at line 7, Puget management  
8 estimates that approximately that number of capital  
9 needs would be required through internally generated  
10 funds, correct?

11 A. Yes.

12 Q. And the remaining amount which is shown in  
13 shading would be funded by a combination of the next  
14 number shown in shading of debt issued by Puget plus,  
15 quoting your testimony, a shaded number that will be  
16 financed with primarily equity and equity-like  
17 securities, correct; have I read that right?

18 A. Correct.

19 Q. First of all, the capital expenditures here  
20 that you refer to, and I'm talking about the total  
21 number of 5.7 billion that's not shaded at line 5,  
22 that's from 2007 through 2013, isn't that right, not  
23 2008 as you state in your testimony at line 5?

24 A. Would you like me to get a calculator out and  
25 add it up?

0635

1 Q. Well, I'm just asking you about the years  
2 that are involved in that projection. You've stated  
3 that they're 2008 through 2013, they're actually 2007  
4 through 2013, correct? You can look at page 3 of  
5 Mr. Markell's exhibit, the business plan, Exhibit 76.

6 A. Okay, so would you like me to get a  
7 calculator out and add these numbers up?

8 Q. Well, I'm just asking you about the years.  
9 Let's turn to page 3 of Mr. Markell's Exhibit 76C.

10 A. Right.

11 Q. And doesn't that show the projected  
12 expenditures from 2007 through 2013, not 2008 through  
13 2013?

14 A. It shows 2007 through 2013, yes, it does, and  
15 then there's a total on the far right that says 2008  
16 through 2013.

17 Q. Okay, you've moved over to page 4 of the  
18 exhibit.

19 A. Page 3 in the text, oh, yes, this number is  
20 on page 3 as well as page 4, sorry.

21 JUDGE MOSS: Yes, it's page 4 of the exhibit.

22 A. Yes, page 4 of the exhibit, the last column  
23 adds them up for you from 2008 through 2013, which is  
24 5.652, which rounds roughly to the 5.7 in line 5 of the  
25 testimony.

0636

1 Q. All right.

2 MR. FFITCH: May I have a moment, Your Honor?

3 JUDGE MOSS: Yes, you may.

4 BY MR. FFITCH:

5 Q. Let's stay on page 4 of the exhibit, on that  
6 same page. Are you with me, Mr. Pettit?

7 A. Yes.

8 Q. And you will see that there's a line under  
9 sources, right above total sources for new equity,  
10 correct?

11 A. Yes.

12 Q. And that shows that Mr. Markell projects a  
13 figure, and if we look all the way over to the far right  
14 under the total for 2008 through 2013, we see the  
15 figure, total figure that he projects, correct?

16 A. Yes.

17 Q. Now that is a number that is significantly  
18 lower than your analysis, the number that you use in  
19 your analysis of Puget's ability to issue common equity,  
20 right?

21 MS. CARSON: What are you referring to,  
22 Mr. ffitich?

23 Q. I believe it's the number on line 11.

24 A. Right.

25 Q. Of your rebuttal testimony.

0637

1           A.     Right.  If you read the footnote on the  
2     exhibit, there's a discussion around a hybrid which gets  
3     equity credit, so I'm actually putting common plus  
4     preferred all together.

5           Q.     All right.

6           A.     The hybrid preferred.

7           Q.     Are you familiar with the type of hybrid  
8     securities recently issued by the Company that get 50%  
9     equity credit by the rating agencies, Mr. Pettit?

10          A.     Yes.

11          Q.     And the hybrid securities that Puget issued  
12     are 250 million of junior subordinated notes; isn't that  
13     right?

14          A.     Correct.

15          Q.     And Company Treasurer Donald Gaines testified  
16     in the rate case that these hybrid securities are a form  
17     of debt, correct?

18          A.     They're actually a hybrid, which is part  
19     equity and part debt.

20          Q.     So you would not agree with Mr. Gaines that  
21     the hybrid securities are a form of debt?

22          A.     I would prefer to call them a hybrid  
23     security.

24          Q.     Do Puget's hybrid securities --

25                 MR. FFITCH:  I'm sorry, Your Honor, just to



0638

1 back up, the testimony of Mr. Gaines that I referred to  
2 has been provided for this record in Exhibit 26, it's  
3 marked for Mr. Kupchak by the Company in response to a  
4 data request.

5 JUDGE MOSS: All right, thank you.

6 BY MR. FFITCH:

7 Q. Do Puget's hybrid securities create any tax  
8 responsibility for the Company, Mr. Pettit?

9 A. I have not studied the tax situation of the  
10 structured products issued by Puget.

11 Q. So you don't know?

12 A. No.

13 Q. Let's assume that instead, now you have this  
14 number in mind from line 11 in your testimony of the  
15 remaining amount that needs to be financed?

16 A. Through SBN equity-like securities, correct.

17 Q. Right, that's the shaded number in line 11 of  
18 your rebuttal?

19 A. Yes.

20 Q. Let's assume that instead of intending to  
21 issue that amount of common equity, Puget intended to  
22 issue about 900 million of common equity, that's the  
23 number that we've heard in the hearing room today.

24 A. Right, I didn't specify common equity, I just  
25 said total equity and equity-like.

0639

1 Q. Well, this is I'm asking you to make an  
2 assumption for purposes of my question, do you  
3 understand that?

4 A. Okay, so we set aside some of the funding in  
5 the hybrid, and then we're left with roughly 900 or  
6 something in common is what you're saying, right?

7 Q. Well, let me just ask the question again and  
8 just follow me. The hypothetical is assume that instead  
9 of intending to issue your shaded number of common  
10 equity, Puget intended to issue about 900 million, are  
11 you with me?

12 A. Yes.

13 Q. Do you agree that it would be less  
14 problematical for Puget Sound Energy or Puget Energy to  
15 issue 900 million of common equity over the 2007 to 2013  
16 period than it would be to issue your number?

17 A. No, I do not, because that was my assumption  
18 all along roughly, some of the equity would be common  
19 and some would be through a hybrid.

20 Q. But under the hypothetical, do you agree that  
21 it would be less problematical to issue the 900 million  
22 rather than your number?

23 A. No, because that's what my number was based  
24 on, we're on the same page.

25 Q. Would you turn to your rebuttal, page 10, and

0640

1 at line 19 you estimate that Puget's equity issuances  
2 from 2009 through 2013 are or will be that shaded  
3 number, correct?

4 Are you with me, this is page --

5 A. Page 9?

6 Q. Page 10.

7 A. Page 10, okay.

8 Q. Line 19.

9 A. Right.

10 Q. Okay, and that is a statement of estimated  
11 equity issuances for Puget for the years 2009 through  
12 2013 on an annual basis per year, right?

13 A. Correct.

14 Q. Now if we turn the page to page 11 of your  
15 rebuttal and we look at that table, if hypothetically  
16 the cumulative equity issuance percentage were lower,  
17 that would bring Puget down from what you have estimated  
18 to be the 99th percentile to somewhere lower on that  
19 chart, correct?

20 MS. CARSON: Object to the form of the  
21 question.

22 A. No, it's actually not correct anyway. The  
23 comparator is common plus preferred, so I think what  
24 you're suggesting is to exclude preferred, but then I  
25 would need to do the same on the comparator data to

0641

1 compare apples and apples.

2 Q. I'm not suggesting that.

3 JUDGE MOSS: Frankly, Mr. ffitch, I didn't  
4 understand the question, and the objection was to the  
5 form of the question. If you want to try again, perhaps  
6 we can get at it.

7 MR. FFITCH: We'll try again, Your Honor.

8 BY MR. FFITCH:

9 Q. I think the question is a little more  
10 straightforward, Mr. Pettit, if the amount of equity to  
11 be issued is less than you assume, would the number on  
12 that graph be lower?

13 A. I think you still don't understand my graph.

14 Q. Well, I would just like an answer to the  
15 question.

16 A. No, because you're not comparing apples and  
17 apples. If I take out the preferred, then I need to  
18 also take the preferred out of the benchmark data.

19 Q. My question didn't say anything about  
20 preferred, you're adding facts to the hypothetical.

21 MR. FFITCH: And I would ask that the witness  
22 be directed to answer the hypothetical, which is --

23 JUDGE MOSS: Mr. ffitch, I think the witness  
24 is doing the best possible job to answer your question  
25 as it's been posed. He's trying to tell you that the

0642

1 question you're asking is assuming something about this  
2 table that isn't true, so there's no way he can answer  
3 the question. Now if you assume the table is as he  
4 presented it and you can change his assumptions in the  
5 table, if we can understand what they are which at this  
6 point I don't, and then ask your question that way. But  
7 right now he's telling you no, he can't give you  
8 anything but a negative answer to your question because  
9 it to him doesn't make sense in terms of what table he's  
10 presented here. That's how I understand the state of  
11 the testimony right now, and I'm not cutting you off  
12 from trying again, but that's just how I understand it  
13 right now.

14 MR. FFITCH: I think we'll just leave it  
15 there, Your Honor.

16 JUDGE MOSS: Thank you, Mr. ffitch.

17 MR. FFITCH: It's a little bit hard to do  
18 this --

19 JUDGE MOSS: It's a little bit hard with the  
20 abstractions, I understand.

21 MR. FFITCH: -- with the confidential  
22 numbers.

23 BY MR. FFITCH:

24 Q. Let's turn to your calculation of the average  
25 equity issuance as a percentage of market

0643

1 capitalization, Mr. Pettit, and I'm looking at page 10,  
2 line 14, and there you say in your testimony that the  
3 average equity issuance is about 4% of market  
4 capitalization based on 10 years of data, correct?

5 A. I'm sorry, you cut out with a beep.

6 Q. All right, I'm looking at --

7 JUDGE MOSS: We'll try to pause when those  
8 interruptions come, Mr. Pettit, that's just a function  
9 of the technology we're using here, sorry.

10 Q. I'm looking at page 10 of your rebuttal  
11 testimony, line 14.

12 A. Okay.

13 Q. Where you say that the average equity  
14 issuance is about 4% of market capitalization based on  
15 10 years of data, right?

16 A. Right, over the last ten years roughly 4%,  
17 more recently it's dropped to about 2%.

18 Q. And from that 4%, you get your 20% five year  
19 cumulative percent that we've just been talking about,  
20 right?

21 A. Correct.

22 Q. Because 20% is five times 4%, right?

23 A. Yes.

24 Q. Now I'm going to ask you to take a look at  
25 this exhibit that we just substituted, it's Exhibit 118,

0644

1 do you have that with the new page 3? Hopefully they  
2 were able to get that to you.

3 A. 3218?

4 Q. It's 3218, and it's the printout that's  
5 attached, the page 3 of the exhibit is what I'm looking  
6 at. It's the --

7 A. Yes.

8 Q. All right. And the heading is  
9 issuance/market cap on the left side of the page.

10 A. Yes.

11 Q. And where this came from is in that data  
12 request we asked you to provide the data on which your  
13 averages were based, and you provided those data in  
14 spreadsheet form, and this is a copy of the output sheet  
15 of that analysis; is that right?

16 A. Yes.

17 Q. And if we look at the column on the left of  
18 this, and again we're on page 3 of the exhibit, we see a  
19 column that -- we see a line that says average for 10  
20 years, and that says 4%, right?

21 A. Yes.

22 Q. Now if we average the last 15 years, which is  
23 all of the data in your analysis, the average equity  
24 issuance as a percent of market capitalization would be  
25 according to our calculations 6.55%; would you accept

0645

1 that subject to check?

2 A. I'm sorry, what was the question?

3 Q. If we're going to average the last 15 years.

4 A. So you go back further in time?

5 Q. Correct.

6 A. Okay.

7 Q. That's all of the data in the analysis that  
8 you provided to us.

9 A. So that's trending down.

10 Q. Well, I'm just asking you to confirm subject  
11 to check that the average is 6.55%.

12 A. It makes sense because it's trending down, so  
13 you've got a higher number by adding older history,  
14 right.

15 Q. All right, you're agreeing that that sounds  
16 like the right number subject to check?

17 A. I'm not going to go check it, but it sounds  
18 reasonable.

19 Q. All right.

20 JUDGE MOSS: I think we can all do the math,  
21 Mr. ffitich, why don't you go ahead and ask your next  
22 question.

23 Q. And five times that 6.55% overall average  
24 would indicate an average cumulative five year equity  
25 issuance of 32.75% of total capital, correct?



0646

1 A. Yes.

2 MR. FFITCH: May I have one more moment, Your  
3 Honor, I'm getting to the end.

4 JUDGE MOSS: Okay, thank you.

5 BY MR. FFITCH:

6 Q. Just one or two more questions about this  
7 same page 3, Exhibit 118, Mr. Pettit, there's a line  
8 that says Puget, what does that number represent or that  
9 line represent?

10 A. Those would be Puget's equity issuance.

11 Q. As a percentage of market capitalization,  
12 right?

13 A. Common plus preferred.

14 Q. Now there's a line above it that says  
15 average, am I correct that that represents the industry  
16 average?

17 A. Yes.

18 Q. And if you look at the years 1999 through the  
19 year 2002, you see that Puget's numbers are  
20 significantly higher than the industry average, correct?

21 A. Yes.

22 MR. FFITCH: That's all the questions I have,  
23 Your Honor.

24 Thank you, Mr. Pettit.

25 JUDGE MOSS: Thank you, Mr. ffitch.

0647

1 Do you have any redirect?

2 MS. CARSON: No, Your Honor.

3 JUDGE MOSS: Okay, do we have any questions  
4 for Mr. Pettit from the Bench.

5 COMMISSIONER JONES: Yes, Judge Moss.

6 JUDGE MOSS: Commissioner Jones.

7

8 E X A M I N A T I O N

9 BY COMMISSIONER JONES:

10 Q. Good evening, it's 7:20 back there,  
11 Mr. Pettit, I won't take -- I have several questions,  
12 fairly straightforward, so I hope this won't take too  
13 long.

14 A. Not a problem, please go ahead.

15 Q. What's the basis of the data support that was  
16 just referenced by Public Counsel ffitch, what's the  
17 source of data, is this your data or EEI data or what is  
18 it?

19 A. All of the data is pulled from Capital IQ,  
20 which is a Thompson Reuters product.

21 Q. Thank you.

22 Can you turn to page 4 and 6 of your  
23 testimony, please, where you talk about trends in  
24 utility capital requirements generally.

25 JUDGE MOSS: And that's Exhibit Number 111CT.

0648

1 Q. Excuse me, Exhibit 111, the rebuttal  
2 testimony of Mr. Pettit. Are you there, Mr. Pettit?

3 A. Pages what?

4 Q. It's section 2, so pages 4 through 6.

5 A. Okay, got it.

6 Q. This is more of a general question, and you  
7 may have heard my question to Mr. Reynolds before, but  
8 there's very little in this analysis about the type of  
9 capital requirements by credit quality, by BBB or  
10 whatever utility is out there, it's just very large  
11 gross amounts of utility sector investment, and so my  
12 question to you is did you do any analysis of capital  
13 requirements by type of utility, specifically by credit  
14 quality, and in this instance Puget being a BBB company?

15 A. Yes, the analysis that we just spent some  
16 time going through was investment grade only, and so we  
17 excluded all of the non-investment grade credits from  
18 the data.

19 Q. Would you agree, Mr. Pettit, with the general  
20 proposition or the general statement that the capex  
21 cycle that you refer to on pages 4 through 6 is  
22 fundamentally different today than the one in the 1970's  
23 because of the generally lower credit quality compared  
24 to the capex cycle in the 1970's?

25 A. I think there are a number of differences,

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1 and certainly that would be among them.

2 Q. Turning to page 7 of your testimony, this  
3 relates -- I think it's 7. And my question, I think  
4 Mr. Fitch covered this but it's still a little bit  
5 confusing to me, two questions on the hybrids. Based on  
6 your experience in the utility industry, how has the  
7 rating agency treated the equity and debt components of  
8 hybrids?

9 A. It has tended to be on a very  
10 product-specific basis, and so whenever we would  
11 innovate a new product, we would need to go out to the  
12 agencies, hear their opinion on how to treat that  
13 product, so there's really a spectrum of what's  
14 available. The one contemplated here gets C bucket  
15 treatment, and it's junior long dated subordinated note  
16 with some deferral language around the dividends to  
17 enable a 50% equity, 50% debt treatment.

18 Q. Turn to page 9, please, of your testimony,  
19 and at the bottom of that page, this is more of a  
20 general question about capital investment and the risk  
21 and benefits associated with that. As a general  
22 proposition, do you believe that capital budget growth  
23 can be a positive thing for shareholders if the risks  
24 and benefits are appropriately compensated, in other  
25 words capital budget growth can be used to serve more

0650

1 electric load, increasing rate base, and if the  
2 incremental ROE, the return on equity, is greater than  
3 the incremental cost of the new resource, that can be  
4 accretive to earnings?

5 A. Yes, I think ideally it should be value  
6 creating, and the biggest concern in our sector is the  
7 regulatory lag.

8 Q. Did you do any such analysis for PSE as part  
9 of this project as a stand-alone entity based on the  
10 capital budget or the business plan given to you by  
11 management?

12 A. An analysis of the value creation, no.

13 Q. Okay.

14 Next question is on page 10 of your  
15 testimony, Mr. Ffitch referred to this a bit, page 10,  
16 lines 12 through 17, if we could go back to that.

17 A. Yes.

18 Q. A general question first on what you  
19 described as patient money of the infrastructure funds,  
20 how can you describe the infrastructure funds as being  
21 patient money in the U.S. utility market since they're  
22 so new? I mean patient to me would mean you would need  
23 at least 10, 15 years to see if the money is patient or  
24 not. Most private equity funds in this infrastructure  
25 or the infrastructure funds have been purchasing assets

0651

1 in this market since what, 2005 or 6?

2 A. Right, I think it comes back to perspective.  
3 In the public market, many people feel that the  
4 investment horizon is quarter to quarter, and certainly  
5 we've got lots of folks who turn their portfolio several  
6 times over per year. Private equity tends to invest 5  
7 years and more, and so 5 years is 20 times longer than a  
8 quarter.

9 Q. Understand.

10 Did you have a chance, did you hear  
11 Mr. Reynolds speak this morning about the equity  
12 issuances over the past six years?

13 A. Yes, I have been dialed in all day.

14 Q. Was there anything in his statements or his  
15 analysis that would cause you to change your analysis in  
16 lines 11 through 17?

17 A. No.

18 Q. Okay.

19 In terms of this same section, section 4 of  
20 your testimony, did you have a chance to examine a  
21 comparable group of companies, specific companies that  
22 would be in the comparable group of Puget Sound Energy?  
23 For example, I think you're familiar with Morgan  
24 Stanley's group of comparable companies listed on pages  
25 43 and 44 of the proxy statement.

0652

1 A. Yes.

2 Q. There are six companies there. Did you have  
3 a chance to look at the market size, the credit quality,  
4 and the capital expenditures and equity issuances of  
5 those six companies?

6 A. We looked at them, I don't think we did a  
7 study per se. Did look at them, but more ad hoc.

8 Q. Are you aware, for example, that Avista in  
9 this state, a regulated utility in Oregon, Washington  
10 and Idaho, just had an equity issuance recently, and did  
11 you have a chance to look at both the percent of market  
12 cap, the trading volume, and the impact on the share of  
13 currently traded prices?

14 A. No, didn't study that.

15 Q. Could you turn to page 15 of your testimony,  
16 please. I think Counsel ffitch was referring to these  
17 where you have two footnoted journal studies, one is by  
18 Rene Stulz and the other I guess is by the World  
19 Economic Forum; is that correct?

20 A. Yes.

21 Q. Now these are academic studies, are they not?

22 A. Yes.

23 Q. One was done in the fall of '95, correct?

24 A. Yes.

25 Q. The private equity and infrastructure funds

0653

1 started investing in this country in 2006, correct?

2 A. Yes.

3 Q. So how relevant and what is the proper  
4 evidentiary basis for some of your statements here that  
5 private equity money or non-public sources of capital  
6 are more patient than public markets?

7 A. The footnote number 3 is the one that  
8 references that. Footnote number 2 is a different  
9 issue.

10 Q. I see.

11 A. But footnote number 3 is the most  
12 comprehensive study that has ever been done on private  
13 equity looking at the last 30 years of investment  
14 globally and thousands of transactions, and it was  
15 published also in a peer reviewed journal.

16 Q. And is it based on actual, I haven't had a  
17 chance to read it yet, but is it actually based on data  
18 just in the United States utility market or Canada,  
19 Australia, and other markets as well?

20 A. It is not utility specific, nor is it U.S.A.  
21 specific. It's a global view of all deals, all sectors,  
22 so a very broad study.

23 Q. Mr. Pettit, I understand you've worked in the  
24 telecom sector within a leveraged buyout when you were  
25 with UBS; is that correct?



0654

1           A.     That would have been more recently with Booz  
2     & Company.

3           Q.     Booz & Company?

4           A.     Yeah.

5           Q.     Are you aware of the recent purchase of  
6     Alltel by a private equity firm and its subsequent sale  
7     to Verizon?

8           A.     No.

9           Q.     I think it had a period of gestation with a  
10    private equity company of one year, I thought you might  
11    be familiar with that.

12                    COMMISSIONER JONES:  That's the end of my  
13    questions, Judge Moss.

14                    JUDGE MOSS:  Thank you, Commissioner Jones.

15                    Anything further from the Bench?

16                    Apparently not.

17                    Any follow up to the Commission's questions  
18    and Mr. Pettit's answers to them?

19                    MR. FFITCH:  Your Honor, I had one question  
20    if I may.

21                    JUDGE MOSS:  You may.

22

23                    C R O S S - E X A M I N A T I O N

24    BY MR. FFITCH:

25           Q.     You were asked, Mr. Pettit, about the

0655

1 cyclical nature of capital expenditures I believe by  
2 Commissioner Jones. What was the last major  
3 construction cycle in the electric utility industry, the  
4 1980's, early 1990's sound familiar, would that be  
5 correct?

6 A. Sure.

7 Q. Do you have an opinion as to why from 1993  
8 through '96 the annual average equity issuance by  
9 electric utilities was, and I'm just, you know, done  
10 this math from Exhibit 118, it's 11 1/2%, which is more  
11 than 5 times higher than the average amount issued last  
12 year?

13 A. There was a lot of repair of balance sheets  
14 going on.

15 Q. Did you say repair of balance sheets?

16 A. Correct.

17 Q. Was that left over from the construction  
18 cycles in the '80's and early '90's?

19 A. And the early '90's recession, yes.

20 MR. FFITCH: All right, thank you, those are  
21 my only questions.

22 JUDGE MOSS: Okay, thank you.

23 If there's nothing further for Mr. Pettit,  
24 Ms. Carson.

25 MS. CARSON: I believe we have one redirect.

0656

1 R E D I R E C T E X A M I N A T I O N

2 BY MS. CARSON:

3 Q. Mr. Pettit, in your chart, Exhibit I believe  
4 it's 118, 3218 is the data request, page 3.

5 JUDGE MOSS: Do you have an exhibit number  
6 for us?

7 Q. I believe it's 118.

8 A. 118, yes.

9 JUDGE MOSS: Okay, Exhibit 118.

10 Q. Just wondering why you use an average of 10  
11 years but you show 15 years on the chart?

12 A. Sure. Typically in equity capital markets as  
13 a banker we would size up markets for digestibility, and  
14 we would typically only use very current data, the last  
15 few months' worth. In some cases where there's not a  
16 lot of data you might look at everything that's been  
17 done that year. And had I done that, I would have  
18 actually come up with a much smaller number. I was  
19 trying to be as conservative as possible and use as much  
20 data as possible, and so I went for the whole decade, a  
21 ten year piece of data if you will, to prove statistical  
22 stability of the results. But the practice in banking  
23 would actually be to err on fewer years, not more, and  
24 probably just to use the most current year of data.

25 MS. CARSON: No further questions.

0657

1 JUDGE MOSS: All right, thank you.

2 All right, apparently there's nothing further  
3 for Mr. Pettit then.

4 MR. FFITCH: Correct, Your Honor.

5 JUDGE MOSS: All right, Mr. Pettit, we thank  
6 you for staying on the phone for so long with us today  
7 and for being patient while we conducted this  
8 examination, and with that I believe we can release you  
9 to go about your affairs there on the East Coast, thank  
10 you.

11 MR. PETTIT: All right, thanks very much.

12 JUDGE MOSS: All right, now should we go back  
13 then to Mr. Markell, is that the plan?

14 MR. FFITCH: Yes, Your Honor.

15 JUDGE MOSS: All right. And I will say in  
16 that regard it's now 4:35, so how much do you have for  
17 Mr. Markell?

18 MR. FFITCH: We should be able to finish  
19 close to 5:00 or certainly by 5:30.

20 JUDGE MOSS: And you also indicated, part of  
21 our discussion off the record concerning our hearing  
22 management has been to the effect that you would group  
23 your cross-examination so as to have a period at least  
24 when you have Mr. Leslie when you would not need to --  
25 we would not need to be concerned about highly

0658

1 confidential or confidential, so that would be a half an  
2 hour or so, is that right?

3 MR. FFITCH: Approximately, maybe 45 minutes.

4 JUDGE MOSS: Fine, I'm just thinking if we  
5 can start him today without having to close the hearing  
6 room, which I don't want to do. All right, thanks,  
7 tells me what I need to know for now.

8 Mr. Markell, since we had you on the panel  
9 for quite a while, I know you were previously sworn, and  
10 with that I believe we can go ahead and begin.

11 MS. CARSON: We are willing to stipulate  
12 cross-examination exhibits.

13 JUDGE MOSS: All right, we're going to  
14 stipulate Mr. Markell's exhibits, the exhibits that  
15 Public Counsel has designated for potential  
16 cross-examination for Mr. Markell will be stipulated  
17 into the record as previously marked on the exhibit  
18 list.

19 So, Mr. ffitch, you may proceed.

20 MR. FFITCH: Thank you, Your Honor.

21

22 Whereupon,

23

ERIC M. MARKELL,  
24 having been first duly sworn, was called as a witness  
25 herein and was examined and testified as follows:

0659

1 C R O S S - E X A M I N A T I O N

2 BY MR. FFITCH:

3 Q. Good afternoon, Mr. Markell.

4 A. Good afternoon.

5 Q. First I would like to look at, well, I don't  
6 know if you have to look at it, but under commitment 16  
7 of the settlement there's a commitment that PSE will  
8 have at least one independent director, correct?

9 I'm happy for you to look at it.

10 A. Yes.

11 Q. And this sort of elaborates, this commitment  
12 elaborates on that by saying that the independent member  
13 would be not a member, shareholder, director, officer,  
14 or employee of Puget Holdings, correct?

15 A. Correct.

16 Q. Or its affiliates. And can you look at  
17 commitment 43, please, and there the joint applicants  
18 state that PSE will, to the extent practical, comply  
19 with the rules applicable to a registrant under the New  
20 York Stock Exchange Rules, correct?

21 A. Correct.

22 Q. And then there's a reference to your Exhibit  
23 11, which has been marked as Exhibit 81 in this hearing,  
24 can we go to your Exhibit 81, Exhibit 11. Do you have  
25 that?

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1 A. I do.

2 Q. Okay, let's go to page 1 of the exhibit, and  
3 that is where you lay out in table form the New York  
4 Stock Exchange corporate government standards current  
5 requirement, the post closing requirement on the new  
6 Puget, and then the post closing commitment, right?

7 A. Correct.

8 Q. Now let's go down to the bottom half of the  
9 page next to section 303.A, and that relates to  
10 independent directors there in the first description  
11 column, and it's correct, is it not, that the NYSE  
12 requirement is that there must be a majority of  
13 independent directors on the board?

14 JUDGE MOSS: Let me caution people who are on  
15 the conference bridge line to please put their phones on  
16 mute caller.

17 A. Correct.

18 Q. All right. So I guess I'm not sure if that  
19 question got completely transcribed, but the question  
20 was under current NYSE rules, Puget must have a majority  
21 of independent directors on its Board of Directors,  
22 correct?

23 A. Correct.

24 Q. And then in the next column we see that after  
25 the transaction is closed, that will not be required,

0661

1 that's what your chart shows, right?

2 A. Correct.

3 Q. And then in the far right you're indicating  
4 that PSE will include at least two independent directors  
5 and one who is unaffiliated with the Macquarie  
6 Consortium, right, that's what you say there?

7 A. Yes.

8 Q. So that means that you will have at least two  
9 independent directors, one of those independent  
10 directors would be an independent director who would be  
11 or could be affiliated with the Macquarie Consortium,  
12 correct; am I reading that right?

13 A. Yes.

14 Q. So that's a change from the status quo,  
15 correct?

16 A. Yes.

17 Q. Please turn to the next page, and again a  
18 little over halfway down under the description column we  
19 see the current rules for the nominating and governance  
20 committee, and it states there that that committee has  
21 to be composed of independent directors, correct?

22 A. Correct.

23 Q. And if we look over to the right-hand column,  
24 the joint applicants' commitment is stated there, and  
25 the statement is it will not be composed entirely of



0662

1 independent directors, correct?

2 A. Correct.

3 Q. And that is a change from the status quo, is  
4 it not?

5 A. It is.

6 Q. If we go to the next box, we see again this  
7 is the compensation committee, the requirement currently  
8 is that it be composed of independent directors, right?

9 A. Correct.

10 Q. Post closing commitment is that it will not  
11 be composed entirely of independent directors, correct?

12 A. Correct.

13 Q. And that is a change from the status quo, is  
14 it not?

15 A. It is.

16 Q. If we go to the next page, page 3 of your  
17 exhibit, under the audit committee description at the  
18 top of the page, again the audit committee must be  
19 composed of independent directors, correct?

20 A. Correct.

21 Q. And that is the status quo with Puget right  
22 now, correct?

23 A. It is.

24 Q. The post closing commitment is that the  
25 committee will not be composed entirely of independent

0663

1 directors, correct?

2 A. Correct.

3 JUDGE MOSS: Mr. ffitch, are there any more  
4 of these that you want to go through, because what I'm  
5 going to suggest is if there are, instead of going  
6 through each one this way, let's just identify the ones  
7 that there's a change from the present to the post, and  
8 then we can read it, it's all right here.

9 MR. FFITCH: I've only got a couple more.

10 JUDGE MOSS: All right, a couple more is  
11 fine.

12 BY MR. FFITCH:

13 Q. The next page, page 4 of your exhibit, I want  
14 you to take a look at the section under corporate  
15 governance guidelines; do you see that?

16 A. I do.

17 Q. And you indicate that those are no longer  
18 required, but the commitment is that Puget will maintain  
19 these guidelines but will revise them as necessary to  
20 reflect the post closing governance structure, correct?

21 A. Correct.

22 Q. Who will make those revisions?

23 A. I assume that the new boards will make those  
24 revisions in consultation with their corporate secretary  
25 and counsel at the time.

0664

1 Q. That would be the board of Puget Holdings?

2 A. Puget Holdings, PSE, and PE.

3 Q. And will the board of Puget Intermediate  
4 Holdings or Equico participate in that decisionmaking?

5 A. I don't know.

6 Q. Who will ultimately approve the revision  
7 that's referenced there on the exhibit?

8 A. I assume the boards of directors of those  
9 individual entities.

10 Q. Now you also addressed future compliance with  
11 Sarbanes-Oxley requirements, did you not, in this  
12 exhibit if we go ahead to page 8?

13 A. That's correct.

14 Q. The bottom of page 8, bottom part of the  
15 table refers, if you look at the third box over, that  
16 refers to the audit committee, right?

17 A. Yes.

18 Q. And this is a Sarbanes-Oxley requirement  
19 that, just sort of summarizing what we see here, there's  
20 a requirement that the audit committee consist entirely  
21 of independent members, correct?

22 A. Correct.

23 Q. And then in the far right-hand box under the  
24 post closing commitment, you've referenced back to the  
25 NYSE commitment that the joint applicants made above

0665

1 with respect to this audit committee, right?

2 A. Correct.

3 Q. And that commitment is that the committee  
4 will not be composed entirely of independent directors;  
5 is that correct?

6 A. I think we say we will maintain the  
7 committee, I don't know whether or not it will be  
8 entirely independent directors or not at this point.

9 Q. Well, the exhibit speaks for itself.

10 A. It does.

11 Q. We can go back to it if you want, but.

12 Just one other area, Mr. Markell. If you  
13 take a look at what's been marked as Exhibit 90, this is  
14 one of the cross-examination exhibits that's the  
15 response to Data Request 3089.

16 A. I don't have 90 available I don't think.

17 JUDGE MOSS: If that could be furnished to  
18 the witness, please.

19 All right, Mr. Markell now has the exhibit.

20 Q. Mr. Markell, in Exhibit 90 we asked for a  
21 statement of the costs or fees, consulting fees,  
22 associated with this transaction, correct?

23 A. That's correct.

24 Q. And this exhibit shows that the total  
25 transaction costs for the acquisition are \$148.9

0666

1 Million, correct?

2 A. Correct.

3 Q. And of that, \$77 Million, if we see in the  
4 breakout above, \$77.1 Million goes to Puget Holdings?

5 A. That's correct.

6 Q. And the legal fees to Perkins Coie are \$3.2  
7 Million; is that right?

8 A. In combination with that of Dewey & LeBuff.

9 Q. Yes, I see, and Dewey & LeBuff. Does that  
10 include the legal fees for this contested proceeding?

11 A. I would have to go back and look at work  
12 papers to see all that that included.

13 Q. Are any of these amounts, including the legal  
14 fees, going to be recovered from rate payers?

15 A. No.

16 Q. There's going to be no request to recover any  
17 of these amounts from rate payers?

18 A. We have so stated in our testimony.

19 Q. Who is going to pay the \$148 Million?

20 A. It comes out of shareholder funds.

21 Q. The shareholders of Puget Sound Energy?

22 A. Well, of Puget Energy.

23 Q. The new investors, the new owners?

24 A. In effect it will be out of the new owners,  
25 that's correct.

0667

1 Q. So is this being essentially paid for from  
2 the debt amounts that are being issued in connection  
3 with this transaction?

4 A. Debt and equity.

5 Q. Can you state the total amount of Puget's  
6 2007 annual dividend to shareholders?

7 A. It was \$1 a share, and the weighted average  
8 shares outstanding was probably maybe 117 million  
9 shares, so approximately \$117 Million.

10 MR. FFITCH: All right, thank you, those are  
11 all the questions I have for Mr. Markell.

12 JUDGE MOSS: All right, thank you,  
13 Mr. ffitch.

14 Any redirect?

15 MS. CARSON: Yes.

16

17 R E D I R E C T E X A M I N A T I O N

18 BY MS. CARSON:

19 Q. Mr. Markell, is it true that under the New  
20 York Stock Exchange rules when reference is made to  
21 independent directors that is interpreted to mean  
22 independent of management?

23 A. Yes.

24 MS. CARSON: I have no further questions.

25 JUDGE MOSS: Thank you.

0668

1                   We have some questions from the Bench,  
2 Chairman Sidran.

3

4                   E X A M I N A T I O N

5 BY CHAIRMAN SIDRAN:

6           Q.     Well, counsel, you may have clarified this  
7 for me because I was going to ask in commitment 45 it  
8 refers to compliance with New York Stock Exchange  
9 registrant requirements to the extent they are  
10 "practical", I'm sorry, it's 43, refers to the extent  
11 practical, and I was going to ask what is it that's  
12 impractical with respect to compliance with the  
13 independent directors? I guess perhaps there's a  
14 difference between independent directors, as counsel  
15 suggests, so could you clarify for me what it is we're  
16 talking about here?

17           A.     Well, the caveat to the extent practical is  
18 probably unfortunate wording. I mean the intent of  
19 laying out all these commitments is to try to provide  
20 the Commission and others a clear road map of what's  
21 required today, what will or will not be required for  
22 each entity post closing, and to the extent there's a  
23 gap, our best efforts under the going forward commitment  
24 to continue to be transparent and open with all of these  
25 reporting requirements and ongoing corporate governance

0669

1 as much as we can replicate it today to do that in the  
2 future.

3 Q. So when it comes to the list that Public  
4 Counsel just went through of independent directors that  
5 are required under the New York Stock Exchange rules and  
6 the notations that that will not be required apparently  
7 under this stipulation, am I interpreting that  
8 correctly?

9 A. Well, I think as counsel clarified, the  
10 independent standard is that of non-management  
11 directors. Going forward, you know, Mr. Reynolds and  
12 Mr. Leslie today described to the extent that they were  
13 able to who the new directors will be at each level, and  
14 that's a bit of a work in progress.

15 Q. All right, thank you.

16 I also would appreciate some clarification  
17 here with respect to commitment 45, which relates to  
18 Sarbanes-Oxley. And there it says joint applicants  
19 commit to the following post closing commitments with  
20 respect to Sarbanes-Oxley for both Puget Sound Energy  
21 and Puget Energy, and then at F in that list it says  
22 Section 301 requirements with respect to the audit  
23 committee, but I thought when Public Counsel just went  
24 through that chart the chart says something to the  
25 contrary, or perhaps I misunderstand this.



0670

1           A.     I think I would say it is the intent to have  
2     an audit committee, to continue the current practices of  
3     the present audit committee as required by SEC and NYSE  
4     standards. That audit committee has not yet been  
5     organized or populated with directors. I'm not sure how  
6     much more clear I can be about that.

7           Q.     Well, okay. Turn to page 8 of Exhibit 81,  
8     this is the chart that Public Counsel walked you  
9     through. So I'm looking at this chart, and at the top  
10    it says Sarbanes-Oxley reporting and governance  
11    obligations, and in the bottom box of the chart it says  
12    with respect to Section 301 public company audit  
13    committees, and then in the next box it says committee  
14    to consist entirely of independent members, and then  
15    over in the far box it refers backs to the New York  
16    Stock Exchange commitments.

17          A.     Right.

18          Q.     So I'm just confused about trying to square  
19    up what commitment 45 says, which says there will be  
20    compliance with 301, in the chart I just referred to it  
21    refers back to the New York Stock Exchange commitments  
22    where it says that will not be complied with, but again  
23    maybe I'm confused about --

24          A.     I would turn your attention back to page 3 of  
25    11 where we described the NYSE audit standards

0671

1 requirements. The reference is back to them, and I  
2 think what we're trying to say here is that we will  
3 maintain an audit committee, but it may not be composed  
4 entirely of independent directors. It will have the  
5 same sort of charter as today, except that any changes  
6 to that charter that may have to be adopted to reflect  
7 the post closing governance requirements of that entity.

8 Q. All right, I will try this once more, I just  
9 want -- and I'm not trying to be difficult, I just want  
10 to be clear that when commitment 45 says that the joint  
11 applicants will commit to complying with Section 301 of  
12 Sarbanes-Oxley, this chart says they will not comply  
13 with Section 301 except to the extent that that  
14 coincides with the New York Stock Exchange requirement?

15 A. I think that's an appropriate qualification.

16 Q. So this is -- then it seems to me we should  
17 probably, if we were to approve this, we should probably  
18 clarify this, because what this says is not what appears  
19 to be at least the intent of the joint applicants. I  
20 don't know what the intent is of the joint parties to  
21 the settlement, but I can't square these two documents.

22 A. I think that clarification is in order.

23 Q. I haven't gone through this whole table, are  
24 there other things in here that introduce similar  
25 confusion between Sarbanes-Oxley and New York Stock

0672

1 Exchange requirements?

2 A. I hope not.

3 Q. All right, well, consider this a Bench  
4 Request, if you find any, would you tell us?

5 A. We will come running.

6 CHAIRMAN SIDRAN: Thank you, that's all I  
7 had.

8 MR. FFITCH: Can I just follow up if there  
9 are no -- I don't want to interrupt Bench questions.

10 JUDGE MOSS: That will be Bench Request 22.

11 Anything else?

12 Commissioner Jones has some questions or a  
13 question.

14

15 E X A M I N A T I O N

16 BY COMMISSIONER JONES:

17 Q. Mr. Markell, could you turn to page 10 of  
18 your rebuttal testimony, lines 6 through 13.

19 Are you there? The second sentence where you  
20 say -- you're talking about the interest of  
21 shareholders, at some point the impact grows to a level  
22 that imperils the ability of the utility to access  
23 capital and thereby imposes great risk to customers as  
24 well. Are you seriously implying in this sentence that  
25 based on all the discussion we've had on the panel and

0673

1 today that PSE and PE as a stand-alone entity can not  
2 access capital, or is it that it can not access on terms  
3 reasonable, what you and the board judge to be  
4 reasonable?

5 A. I think my testimony both in direct and here  
6 is access on reasonable terms.

7 Q. So this sentence is really not helpful or not  
8 accurate. And then what do you mean when you say great  
9 risk to customers, what great risks are you talking  
10 about?

11 A. I think it's --

12 Q. Excuse me, the public service obligation in  
13 general on the reliability and safety of the system?

14 A. At some point when capital becomes  
15 constrained over time, capital expenditures and budgets  
16 get constrained, and over time that gets to be an  
17 accretive problem for all utilities. We've seen it for  
18 example with Consolidated Edison where they have not  
19 invested properly in their distribution system, and now  
20 they've undertaken a multi-hundred million dollar  
21 catch-up program.

22 Q. I'm not talking about Consolidated Edison,  
23 I'm talking about Puget Sound Energy.

24 A. It would certainly not be our intent,  
25 Commissioner, to constrain capital in a way that it

0674

1 would be adverse. This is a general statement about it  
2 can happen over time.

3 Q. Let's go back to the discussion, I can't  
4 reference the page now, on the 900 million, it's this  
5 issue, there appears to be a discrepancy between the  
6 stated testimony numbers of yours and Mr. Pettit's on  
7 the need for external equity. Yours is 900 million and  
8 his appears to be 1.4 billion. Is this primarily  
9 related to the issuance of hybrids?

10 A. It is.

11 Q. In your experience with Wall Street, does  
12 Wall Street consider the variance, the new variance of  
13 structured products, including hybrids and the  
14 digestibility of such variance, what kind of -- I guess  
15 my question is, does Wall Street consider the hybrids  
16 equally digestible as common equity?

17 A. Well, there's two different markets for these  
18 products, common equity and so-called hybrids. I  
19 suspect that anyone putting capital in a firm, whether  
20 it's preferred, common, or hybrid, considers the total  
21 cash requirements of the company and whether or not all  
22 aspects of those cash requirements can be raised timely  
23 to meet the needs of the company. I don't know if I can  
24 say that they specifically look at equity or hybrids,  
25 but they certainly look at the total ability to raise

0675

1 capital and what those needs are.

2 Q. When did you become CFO?

3 A. Early May of 2007.

4 Q. So were you responsible for the business plan  
5 and the business plan update prepared for 2007?

6 A. I was.

7 Q. Who was your financial advisor working with  
8 management, not the board, from what I understand it was  
9 Morgan Stanley, but did you have a financial advisor  
10 hired to work with management to look at your equity  
11 funding requirements?

12 A. With respect to the preparation of the  
13 business plan update, no.

14 Q. No. Who made the decision to hire Morgan  
15 Stanley, you as the CFO or Mr. Reynolds as CEO?

16 A. The Board of Directors.

17 Q. So you were divorced from that decision?

18 A. I was.

19 Q. Let's turn to page 9. Much of this is  
20 confidential. According to that business plan --

21 A. Excuse me, rebuttal testimony?

22 Q. Rebuttal, that's Exhibit --

23 JUDGE MOSS: 75.

24 Q. -- 75. Here you are talking about the  
25 valuation metrics and the inability, I guess your

0676

1 conclusion is it's either too expensive or you're not  
2 able to issue new common equity on reasonable terms, and  
3 you list some numbers in there related to earnings, and  
4 I think the proxy statement also deals with the  
5 earnings, the net income and the EBITDA in terms of the  
6 information you provided to Morgan Stanley, the number  
7 that you use on line 6, isn't that a selective number,  
8 meaning that's just one year in the seven year plan?

9 A. It is one year in a seven year plan, and it's  
10 used here in the context of --

11 Q. Well, I know the context.

12 A. Yes, it is a single year.

13 Q. So why didn't you use more of an average or  
14 perhaps the out years, because I think the -- there are  
15 different numbers, in fact the net income increases in  
16 the out years, meaning 2009 through 2013, according to  
17 the proxy statement, correct?

18 A. That's correct.

19 Q. So if the earnings number changes, doesn't  
20 that have a direct and tangible impact on the valuation  
21 metrics used?

22 A. It can if those numbers are disclosed and  
23 people apply their various valuation models to what  
24 those expected growth rates are, it could impact the  
25 valuation. These data that you see here in confidential

0677

1 form have been more or less independently confirmed in  
2 recent analyst reports that have been provided to us, so  
3 they're looking at share valuation very much the way  
4 it's presented here.

5 Q. On line 13 you talk about book value per  
6 share, but in Mr. Pettit's testimony he disparages the  
7 notion of book equity, so I am somewhat confused as to  
8 why you reference this number and your capital expert  
9 witness prefers not to use that as a metric.

10 A. Well, I think you would have to ask  
11 Mr. Pettit why he chooses another metric. We're  
12 obviously concerned with the preservation of the market  
13 cap of the company, and relevance to book value is  
14 that's the earning base of the company. I think both  
15 Mr. Pettit and I have expressed our views that so-called  
16 serial issuance of equity when it's large relative to  
17 the earnings base of the company creates downward price  
18 pressure. And what we're attempting to describe here is  
19 some range of where we think those prices may ultimately  
20 go with a stand-alone model given the current business  
21 plan.

22 Q. I understand what you're trying to do, but  
23 what I'm pointing out is perhaps it's inaccurate or  
24 misleading.

25 A. Well, I can only say, and we can provide you



0678

1 additional exhibit on this, that this approach and these  
2 evaluations are -- they've recently been independently  
3 arrived at by other analyst firms.

4 Q. What price per share was the private  
5 placement arranged with, with the 4% discount to the  
6 investor consortium?

7 A. Roughly \$23.67.

8 Q. Roughly, that's pretty to the penny.

9 A. It was a difficult negotiation.

10 Q. Is that above book value?

11 A. It is.

12 COMMISSIONER JONES: That's all I have.

13 JUDGE MOSS: Anything further from the Bench?

14 Apparently not.

15 Anything further for this witness?

16 MR. FFITCH: Yes, Your Honor.

17

18 R E C R O S S - E X A M I N A T I O N

19 BY MR. FFITCH:

20 Q. I want to go back, if I could, Mr. Markell,  
21 again to the New York Stock Exchange requirements that  
22 Chairman Sidran talked about, and I guess now I am  
23 confused. Let's take a look at page 3 with reference to  
24 the audit committee.

25 A. Okay.

0679

1 Q. There's no argument that you're going to have  
2 an audit committee or that Puget Holdings or actually  
3 Puget Energy, PSE, will maintain an audit committee,  
4 that's the commitment, right?

5 A. Correct.

6 Q. And you said it's going to have the same or  
7 similar practices, that's the second bullet point,  
8 that's the charter, correct?

9 A. Correct.

10 Q. But this commitment here which is essentially  
11 verbatim with some of the others I walked through says  
12 that it will not be composed entirely of independent  
13 directors. That is the case, is it not, there is no  
14 commitment that Puget Energy or PSE will have an audit  
15 committee composed entirely of independent directors, is  
16 there?

17 A. That is what we state here.

18 Q. Okay, and you're not changing that commitment  
19 in this hearing, that position in this hearing, correct?

20 A. Correct.

21 Q. And there's no qualification in this table  
22 about different definitions of different types of  
23 independent directors, is there?

24 A. No, we have not taken that step. Again, the  
25 intent of this table is to the best we can indicate a

0680

1 continuation of the current practices that we have  
2 required by Sarbanes-Oxley, NYSE, SEC, that apply to the  
3 currently registered entity, Puget Energy Inc. Since we  
4 know that that will not be a public entity going  
5 forward, we're trying to transform or transfer all of  
6 those obligations from the current practice to the  
7 future practice as best we can. It is quite possible,  
8 Mr. Ffitch, that someplace along the line in that  
9 translation there's some gap that we missed here, but I  
10 can assure you it's not intentional. We're trying to  
11 maintain all the reporting, all the transparency, and  
12 all the high quality corporate governance we have today.

13 Q. But there is no commitment today in this  
14 hearing in the written commitments that are being  
15 proposed to this transaction to have an audit committee  
16 or any of the other committees here that consist  
17 entirely of independent directors, is there?

18 A. There is not.

19 Q. And there is no commitment that the boards of  
20 Puget Energy and Puget Sound Energy will have a majority  
21 of independent directors, is there?

22 A. No.

23 MR. FFITCH: Those are all my questions,  
24 thank you, Your Honor.

25 JUDGE MOSS: Thank you.

0681

1 Anything further for this witness?

2 MS. CARSON: Yes, Your Honor, some redirect.

3

4 R E D I R E C T E X A M I N A T I O N

5 BY MS. CARSON:

6 Q. To your knowledge, Mr. Markell, has it been  
7 established who all is on the audit committee?

8 A. It has not been formed nor has it been  
9 populated.

10 Q. Assuming that the definition of independent  
11 director is a director who is independent of management  
12 and assuming the audit committee is made up of investors  
13 from the investor consortium, would it then be -- would  
14 they then consist of all independent directors?

15 A. They would all be independent.

16 Q. And are the current directors on the audit  
17 committee independent of management?

18 MR. FFITCH: Excuse me, Your Honor, I'm  
19 having difficulty hearing counsel's questions.

20 JUDGE MOSS: Pull the microphone a little  
21 closer if you would.

22 Q. Are the current members of the audit  
23 committee independent of management?

24 A. They are, and I believe Mr. Reynolds is sort  
25 of ex officio member, but the basic audit committee

0682

1 members are all independent.

2 MS. CARSON: That's all I have, thanks.

3 JUDGE MOSS: Thank you.

4 All right, it appears that that completes our  
5 examination of Mr. Markell, we thank you for being on  
6 the stand this afternoon again, and you may step down.

7 (Discussion on the Bench.)

8 JUDGE MOSS: All right, given that our next  
9 witness is Mr. Leslie and the indicated  
10 cross-examination time for him is quite considerable, I  
11 think we will forgo the last 20 minutes today. I do  
12 have some business matters to take up with the counsel,  
13 and the Commissioners don't need to be here for that, so  
14 they can go back and conduct some other business in the  
15 remaining hours of the day, and I will take this up with  
16 you all.

17 Is there something, Ms. Carson, before they  
18 leave?

19 MS. CARSON: Yes, before the Commissioners  
20 leave, I just wanted to confirm that they have no more  
21 questions for the Canadian witnesses, many of whom are  
22 planning to leave tonight unless there are other  
23 questions.

24 JUDGE MOSS: That will be Mr. Webb,  
25 Mr. Wiseman, and Mr. McKenzie, does the Bench have

0683

1 questions for these witnesses? No, none that can't be  
2 handled by telephone.

3 CHAIRMAN SIDRAN: I don't have any questions,  
4 but based on the panel's representations, I assume that  
5 if I did have a question they would come back.

6 MS. CARSON: They would.

7 MR. STOKES: Your Honor, I've got the same  
8 question for Paula Pyron, whether she can be excused  
9 from the panel at this time for the rest of the hearing.

10 JUDGE MOSS: I think we can release  
11 Ms. Pyron, yes.

12 MR. STOKES: Thank you.

13 JUDGE MOSS: All right, very good.

14 All right, I think perhaps the only matter I  
15 need to take up with you as a point of business, I  
16 mentioned in my opening remarks today the motion that  
17 you filed, Mr. ffitich, concerning confidentiality, and I  
18 checked the RMS during the noon hour, that's our record  
19 management system, and see that you have not yet or at  
20 least as of noon have not yet been able to file what has  
21 been indicated or identified as Appendix A to that  
22 motion, which will lay out the specific information to  
23 which you are raising your challenge, which of course is  
24 a necessary part of our in camera review and any  
25 response and so on and so forth, so my first question to

0684

1 you is when do you anticipate you will be able to file  
2 that Appendix A?

3 MR. FFITCH: We anticipate filing that  
4 tomorrow, Your Honor. We have other staff working on  
5 that, and we had agreed with Ms. Carson to show her the  
6 appendix before we filed it to make sure that we weren't  
7 making a mistake, and we may, there may be a  
8 modification I will talk to her about based on testimony  
9 today, changes in designations, but we should be able to  
10 file that tomorrow, Your Honor.

11 JUDGE MOSS: Okay, so that will be tomorrow  
12 is the 26th, right?

13 MR. FFITCH: Yes, Your Honor.

14 JUDGE MOSS: Okay. Then really as a  
15 practical matter then I will have to say that the  
16 responding parties have not really had an opportunity to  
17 work on any sort of response at this juncture. I'm  
18 trying to figure out the timing here for a response  
19 date. Have you all talked about that? Because what I  
20 have in mind is that the parties typically are allowed  
21 five business days to respond to a motion. I'm  
22 hesitating only slightly because I don't know how much  
23 detail is involved, I haven't gone systematically back  
24 to the testimony to see how much volume we're talking  
25 about here. I would say tomorrow probably we shouldn't

0685

1 count nor perhaps Wednesday since we'll probably still  
2 be in hearing, so that will be Thursday and Friday of  
3 this week would count as business days for this purpose,  
4 and then I would also be inclined to discount the 3rd of  
5 next week since we'll be in hearing again many of us in  
6 the general rate case. So I'm thinking perhaps either  
7 the 5th or the 8th as a reasonable date for the Company  
8 or let me just say for the joint applicants I guess or  
9 the joint parties, whoever it may be who's responding to  
10 this, I guess it will be the joint applicants actually  
11 because it's all their data, the 5th or 8th, will that  
12 work?

13 MS. CARSON: The 8th will be very workable.

14 JUDGE MOSS: Preferable?

15 MS. CARSON: Yes.

16 JUDGE MOSS: All right, so we'll have that  
17 response and I'll ask for that response on the 8th, and  
18 that can be an electronic submission date, so the  
19 official filing date will actually be the 9th. I'm not  
20 going to issue a notice on this, so everybody take  
21 notes.

22 All right, and then after that there will  
23 have to be some opportunity of course for the Commission  
24 to review, and I'm not sure exactly how that will play  
25 out, but in any event we will have that response on the



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1 8th, and the Commission will take the matter under  
2 advisement.

3                   And I guess I have to ask one more question,  
4 I'm not sure, Mr. Cedarbaum, whether this puts you in a  
5 difficult spot since you're not the principal counsel  
6 here. I noted earlier, Mr. Ffitch, perhaps you can  
7 respond to this, the very same information that is the  
8 subject of your motion in this proceeding challenging  
9 the designation of this material as confidential under  
10 the protective order I take it is the subject of the  
11 pending action in the Thurston County Superior Court.  
12 Now my initial thought on that without having researched  
13 it carefully is that that would create a jurisdictional  
14 conflict of sorts as a practical matter even though  
15 we're actually talking on the one hand about the Public  
16 Records Act and on the other hand about the protective  
17 order, so I wonder if you can, you or perhaps  
18 Mr. Cedarbaum or other counsel, can shed some light on  
19 what I see as a potential jurisdictional conflict in  
20 terms of the Commission actually resolving this even  
21 when it has your paper. I will take whoever wants to  
22 respond.

23                   MR. CEDARBAUM: Your Honor, I can try to  
24 contribute something here. My understanding is that a  
25 TRO has issued in the Superior Court with respect to the

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1 court case against disclosure of the information and  
2 that on September 5th the court will hear motions for  
3 preliminary injunction. So it seems like setting the  
4 schedule for replies on Public Counsel's motion for the  
5 8th is probably a reasonable thing to do since the court  
6 may act on the 5th as to whether or not it will decide  
7 the issue or kick it back to the Commission to decide  
8 the issue.

9 JUDGE MOSS: I assume somebody is going to  
10 raise the question of referring this matter back to the  
11 Commission since we have such expertise on these things.

12 MR. CEDARBAUM: That's an argument that could  
13 be made. I don't know, Mr. Trautman is representing the  
14 Commission in that court case, I just -- I guess what  
15 I'm saying is that at this point in time and with the  
16 schedule that you've just stated, I think that the  
17 jurisdictional issue could be avoided, and it seems to  
18 make sense to just go ahead and keep that September 8th  
19 reply date set. And then if the court -- if we need to  
20 change that because of what the court does on the 5th,  
21 that could be done.

22 JUDGE MOSS: Okay, I think that's a fair  
23 assessment of the situation, and I don't really need to  
24 hear any more about it. We'll see what the court does.  
25 If the court refers it back, of course then that will

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1 make our jurisdiction clear enough. If the court does  
2 some other action, perhaps that will also make our  
3 jurisdiction or lack thereof clear enough, so we don't  
4 need to have any further discussion about that today.  
5 We will expect those responses then or that response.

6 MR. CEDARBAUM: One quick additional point.

7 JUDGE MOSS: Yes.

8 MR. CEDARBAUM: It may be that if the  
9 Commission is to decide that issue through responses on  
10 the 8th that Staff will want to weigh in on the issue,  
11 and you had indicated that just the joint applicants  
12 might be responding. I don't know that Staff will or  
13 will not be taking a position, but it's a possibility.

14 JUDGE MOSS: And I didn't mean to suggest  
15 that others might not wish to respond. I think other  
16 parties if they feel it appropriate to do so certainly  
17 we have a motion pending, and counsel have not proven  
18 loathe in the past to file something when they have  
19 something to say, so I would expect them to do that in  
20 this instance as well, so that would be just fine if  
21 Staff wants to weigh in. And, of course, as in all  
22 instances, circumstances may change, and parties can  
23 always bring the matter back to me if we need to have  
24 some adjustment or further process or what have you.

25 Okay, do you all have anything for me in the

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1 way of housekeeping matters before we go off the record  
2 for today?

3 Go ahead, Mr. Stokes.

4 MR. STOKES: I was going to ask if there's  
5 any objection to excusing me from the rest of the  
6 hearing at this point.

7 JUDGE MOSS: I have no problem with that, I  
8 can't imagine other counsel would object to that anyway,  
9 so you may be released.

10 MR. STOKES: Thank you.

11 JUDGE MOSS: Thank you for asking.

12 MR. CEDARBAUM: Just looking ahead --

13 JUDGE MOSS: No, Mr. Cedarbaum, you have to  
14 remain.

15 MR. CEDARBAUM: I have had some E-mail  
16 discussion with Mr. Horton about the timing for his  
17 testimony on Wednesday, and at least tentatively he and  
18 I have discussed first thing our time Wednesday morning.  
19 I can confirm that with him if that's acceptable to the  
20 Bench.

21 JUDGE MOSS: Okay, that's fine, and I think  
22 to the extent we run into Wednesday, we probably will  
23 start at 9:00, that will be noon his time.

24 Okay, any other business we need to take up  
25 before we go off the record for the day?

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1                   MR. FFITCH: Your Honor, there were a few  
2 exhibit matters, I guess two of them relate to  
3 Mr. Leslie's cross exhibits, they're both corrections,  
4 and so they're supplementing existing exhibits, so I  
5 could get into that now if you would like, I have copies  
6 here and so on.

7                   JUDGE MOSS: Yes, if we can get copies of  
8 anything that we're going to use tomorrow now, then I  
9 can get those to the Commissioners' support staff and we  
10 can get our notebooks updated so we don't have the  
11 situation we had today where they had an out of date  
12 exhibit.

13                   MR. FFITCH: Your Honor, one is Exhibit 49,  
14 which is a response to Data Request 3008, and that is in  
15 this instance, Your Honor, we have not -- this is a very  
16 large exhibit, we discovered there was inadvertently a  
17 blank page copied into it, so we have provided just the  
18 substitute page for that exhibit.

19                   JUDGE MOSS: That's fine.

20                   MR. FFITCH: So I can pass that out.

21                   JUDGE MOSS: Yes, appreciate you saving our  
22 trees.

23                   MR. FFITCH: How many copies for the Bench,  
24 Your Honor?

25                   JUDGE MOSS: Six for the Bench.

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1                   MR. FFITCH: And then we have Exhibit 65.  
2 This is a substitute exhibit. Exhibit 65 is marked for  
3 Mr. Leslie, these are Puget Sound Energy statements of  
4 income for the five year period, and we're substituting  
5 this because we inadvertently put in a statement for  
6 Puget Energy instead of Puget Sound Energy, so we've  
7 just put together a corrected exhibit for that.

8                   JUDGE MOSS: Okay, this will be a complete  
9 substitution then?

10                  MR. FFITCH: Yes.

11                  JUDGE MOSS: All right.

12                  MS. CARSON: What's the number on that?

13                  MR. FFITCH: 65. This is not a response to  
14 data request.

15                  JUDGE MOSS: Actually, let's go off the  
16 record for the rest of this.

17                  (Discussion off the record.)

18                  JUDGE MOSS: All right, we've taken care of  
19 some exhibit housekeeping matters with Mr. ffitch, there  
20 apparently are no other similar matters, is there any  
21 other business today?

22                  Apparently not, we will be in recess until  
23 9:00 tomorrow morning.

24                  (Hearing adjourned at 5:30 p.m.)

25