

**BEFORE THE
WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION**

In the Matter of the Joint Application of

PUGET HOLDINGS LLC

And

PUGET SOUND ENERGY, INC.

For an Order Authorizing Proposed Transaction

Docket No. U-072375

**BRIEF (CONFIDENTIAL) OF
PUGET HOLDINGS LLC AND
PUGET SOUND ENERGY, INC.
IN SUPPORT OF THE PROPOSED TRANSACTION**

**REDACTED
VERSION**

SEPTEMBER 24, 2008

**BRIEF (CONFIDENTIAL) OF PUGET HOLDINGS LLC AND
PUGET SOUND ENERGY, INC. IN SUPPORT OF
THE PROPOSED TRANSACTION**

TABLE OF CONTENTS

I.	INTRODUCTION	1
II.	LEGAL STANDARDS	7
	A. The Proposed Transaction Satisfies the Commission’s Standard for Approval of a Settlement.....	7
	B. The Proposed Transaction Satisfies the Commission’s Standard for Approval of a Change of Control of a Public Service Company	8
	C. Public Counsel’s Opposition to the Proposed Transaction Is Based on an Application of Incorrect Standards	9
III.	THE PROPOSED TRANSACTION IS IN THE PUBLIC INTEREST AND SHOULD BE ACCEPTED.....	11
	A. The Proposed Transaction Provides PSE Access to Capital to Allow PSE to Meet Its Capital Expenditure Needs by Matching PSE with Experienced, Well-Funded Infrastructure Investors.....	11
	1. PSE Faces Significant Challenges In Funding Its Capital Expenditure Needs Over the Next Several Years	11
	2. Puget Holdings Has Arranged Committed Financing for PSE’s Capital Needs and Has the Financial Capabilities to Meet Those Needs for the Long-Term	15
	3. The Proposed Transaction Provides Further Protection to PSE Through Express Commitments that Ensure that PSE Can Access Capital Should Puget Energy or Puget Holdings Face Financial Distress	21

TABLE OF CONTENTS (contd.)

B. The Proposed Transaction Makes PSE a Stronger Utility23

1. The Proposed Transaction Strengthens PSE’s Capital Structure.....23

2. The Joint Applicants Expect that the Proposed Transaction Will Improve PSE’s Credit Quality26

3. The Proposed Transaction Provides Extensive Ring Fencing Provisions and Regulatory Commitments that Strengthen PSE and Protect PSE’s Customers From Business Risks of Unregulated Affiliates28

C. The Commitments Provide Additional Benefits and Assurances to PSE’s Customers and the Community PSE Serves32

1. Rate Credits of \$100 Million Benefit PSE’s Customers and the Economy of the Puget Sound Region32

2. The Proposed Transaction Provide Assurances that PSE Will Continue to Have a Strong Local Presence and to Pursue its Key Objectives33

3. The Joint Applicants’ Commitment Regarding Access to Books and Records Exceeds PSE’s Current Obligations to Make Such Records Available35

D. The Proposed Transaction Provides For Representation by Local Directors, Transparency, and Balance Among the Members of Puget Holdings36

1. The Proposed Transaction Provides For Local Representation36

2. The Proposed Transaction Provides For Transparency37

3. The Proposed Transaction Provides For Balance Among the Members of Puget Holdings37

IV. PUBLIC COUNSEL’S ARGUMENTS OPPOSING THE PROPOSED TRANSACTION ARE NOT SUPPORTED BY THE EVIDENCE OR THE LAW.....38

TABLE OF CONTENTS (contd.)

1. Ring Fencing Protects PSE Customers from Debt at Puget Energy, and There Is No Justification for Public Counsel’s Argument That Additional Equity Is Needed38

2. Public Counsel’s Concerns Regarding Risks to PSE Customers Due to Goodwill Impairment Are Unfounded.....41

B. The Insertion of Equico between Puget Intermediate and Puget Energy Protects Puget Energy and PSE from Financing Risks of the Parent Companies above Puget Energy43

C. The Proposed Transaction Will Improve PSE’s Balance Sheet44

D. Capital For Infrastructure Will Be More Available Under the Proposed Transaction.....44

1. The Proposed Transaction Ensures that PSE Will Have Access to Equity Capital As Necessary to Fund Its Infrastructure Needs.....44

2. Credit Facilities for PSE Capital Expenditures in the Amount of \$1.4 Billion Have Been Secured and Will Be Available to Be Drawn on Post-Closing45

3. The Capital Expenditure Facilities Support PSE’s Ability to Fund Capital Expenditures to Meet Its Public Service Obligations.....46

E. Public Counsel’s Assertion that the Proposed Transaction Is Not Necessary Is Incorrect and Also Is Irrelevant To the Legal Standard To Be Applied by the Commission47

F. The Challenges in Today’s Credit Market Exist and Confront PSE Whether PSE Is a Stand Alone Publicly Traded Company or Acquired by Puget Holdings49

G. Public Counsel’s Assertion that the Benefits and Risks of the Proposed Transaction Weigh in Favor of Shareholders Is Incorrect and Also Is Irrelevant To the Legal Standard to Be Applied by the Commission.....52

V. CONCLUSION.....54

**BRIEF (CONFIDENTIAL) OF PUGET HOLDINGS LLC AND
PUGET SOUND ENERGY, INC. IN SUPPORT OF
THE PROPOSED TRANSACTION**

TABLE OF AUTHORITIES

Statutes

Chapter 80.12 RCW 8

RCW 34.05.455 1

Rules and Regulations

WAC 480-07-740 7

WAC 480-07-750 7

WAC 480-143-170 8

Cases

*In re Avista Corporation d/b/a Avista Utilities, Docket No. U-060273,
Order 03 (Feb. 28, 2007)* 28

*In re MDU Resources Group, Inc. and Cascade Natural Gas Corporation,
Docket No. UG-061721, Order 06 (June 27, 2007)* 28

*In re MidAmerican Energy Holdings Company and PacifiCorp d/b/a Pacific
Power & Light Company, Docket No. UE-051090, Order 07
(Feb. 22, 2006)* 28

*In re PacifiCorp and Scottish Power plc, Docket No. UE-981627,
Third Supplemental Order at 3 (Apr. 2, 1999)* 8, 9, 10

*Washington Utilities and Transportation Commission v. PacifiCorp
d/b/a Pacific Power & Light Company, Docket No. UE-032065, Order 06
(Oct. 27, 2004)* 7

*Washington Utilities and Transportation Commission v. PacifiCorp
d/b/a Pacific Power & Light Company, Docket No. UE-050684, Order 04
(Apr. 17, 2006)* 29, 39, 40

TABLE OF AUTHORITIES (contd.)

Cases (contd.)

*Washington Utilities and Transportation Commission v. PacifiCorp
d/b/a Pacific Power & Light Company, Docket No. UE-061546, Order 08
(June 21, 2007)*40

Treatises

Black’s Law Dictionary 695 (6th ed. 1990).....41

Financial Accounting Standards Board Statement No. 14141

1 **BRIEF (CONFIDENTIAL) OF PUGET HOLDINGS LLC AND**
2 **PUGET SOUND ENERGY, INC. IN SUPPORT OF**
3 **THE PROPOSED TRANSACTION**

4 **I. INTRODUCTION**

5 1. Puget Holdings LLC (“Puget Holdings”) and Puget Sound Energy, Inc. (“PSE”),
6 the Joint Applicants in this proceeding, respectfully request that the Commission approve the
7 merger transaction as set forth in the Joint Application¹ filed with the Commission on December
8 17, 2007, as modified by the Multiparty Settlement Stipulation² (the “Multiparty Settlement”).
9 Such merger transaction, as modified by the Multiparty Settlement, is referred to in this brief as
10 the “Proposed Transaction.” Six parties have joined with the Joint Applicants to support the
11 Proposed Transaction: Staff of the Washington Utilities and Transportation Commission
12 (“Commission Staff”),³ the Industrial Customers of Northwest Utilities, the NW Energy
13 Coalition, The Energy Project, the Northwest Industrial Gas Users, and The Kroger Company,
14 on behalf of its Fred Meyer Stores and Quality Food Centers divisions. These parties have
15 agreed that the Proposed Transaction, which provides PSE with access to committed capital
16 required to support growth in the Puget Sound region, strengthens PSE’s capital structure and
17 provides additional benefits to customers and the community, is consistent with the public
18 interest and should be approved. Only one party—the Public Counsel Section of the Washington

¹ Joint Application for an Order Authorizing Proposed Transaction, Docket No. U-072375 (Dec. 17, 2007).

² Multiparty Settlement Stipulation, Docket No. U-072375 (July 22, 2008).

³ In formal proceedings such as this, Commission Staff functions as an independent party with the same rights, privileges, and responsibilities as other parties to the proceeding. There is an “ex parte wall” separating the Commissioners, the presiding Administrative Law Judge, and the Commissioners’ policy and accounting advisors from all parties, including Commission Staff. *See* RCW 34.05.455. The three-member panel of Commissioners is not a party to the Multiparty Settlement. The Commissioners must review, consider, and decide whether the Multiparty Settlement should be adopted by the Commission.

1 State Attorney General’s Office (“Public Counsel”)—opposes the Proposed Transaction. As
2 discussed in more detail below, Public Counsel’s objections to the Proposed Transaction are
3 based on the application of incorrect legal standards and a misunderstanding of the facts.

4 2. The Proposed Transaction meets the Commission’s standard for approval of a
5 settlement; it is not contrary to law or public policy, and the evidence in the record supports the
6 Proposed Transaction. Additionally, the Proposed Transaction is consistent with, and does not
7 harm, the public interest. Thus, the Proposed Transaction meets the Commission’s standard for
8 approval of a change of control of PSE.

9 3. The Joint Applicants and the settling parties have presented a compelling case for
10 approval of the Proposed Transaction. First and foremost, PSE needs enormous amounts of
11 capital. Management forecasts that PSE will spend \$5.7 billion over the next five years⁴ to meet
12 gas and electricity demand due to customer growth, “green” PSE’s energy supply as required by
13 law, and replace expiring power purchase agreements and aging generation and delivery
14 infrastructure. Second, to meet this enormous capital need, PSE must secure significant external
15 financing (\$3.4 billion from 2009-2013).⁵ The board of Puget Energy Inc. (“Puget Energy”)
16 recognized that external financing of this magnitude poses risks to the business and its
17 customers.⁶ After thorough consideration of the options, the Puget Energy board chose Puget
18 Holdings as the partner that would provide PSE with the financial backing it needs.⁷

19 4. Puget Holdings was chosen because, together, the members of Puget Holdings are
20 among the most experienced investors in infrastructure and utility assets in the United States and

⁴ See Pettit, Exh. No. 111CT at 7:4-6; see also Markell, Exh. No. 76C.

⁵ See Pettit, Exh. No. 111CT at 7:7-10; see also Markell, Exh. No. 76C.

⁶ See Campbell, Exh. No. 1CT at 5:1 – 8:2.

⁷ See Campbell, Exh. No. 1CT at 8:3 – 10:19.

1 worldwide. The members of Puget Holdings target stable, long-term investments and, together,
2 have assets under management totaling nearly half a trillion dollars from pension plans,
3 endowment funds and other similar long-term funds, among others.⁸ These members of Puget
4 Holdings, and their respective ownership interests, are as follows:⁹

- 5 (i) Macquarie Infrastructure Partners I¹⁰ (31.8% ownership interest);
- 6 (ii) Macquarie Capital Group Ltd.¹¹ (15.9% ownership interest);
- 7 (iii) Macquarie-FSS Infrastructure Trust (3.7% ownership interest)¹²
- 8 (iv) Canada Pension Plan Investment Board (28.1% ownership interest);
- 9 (v) British Columbia Investment Management Corporation (14.1% ownership
10 interest); and
- 11 (vi) Alberta Investment Management (6.3%).¹³

12 The members bring diversity and balance to the Proposed Transaction. No one investor or group
13 of affiliated investors holds a controlling stake in Puget Holdings.¹⁴

⁸ See Leslie, Exh. No. 38HCT at 8:3-15.

⁹ Please note that the ownership interests add to 99.9% due to rounding.

¹⁰ Macquarie Infrastructure Partners consists of three limited partnerships that will invest indirectly in Puget Holdings: Macquarie Infrastructure Partners A, L.P., Macquarie Infrastructure Partners International, L.P., and Macquarie Infrastructure Partners Canada, L.P. See Leslie, Exh. No. 31T at 5 n.6.

¹¹ Macquarie Capital Group Ltd. is a wholly owned subsidiary of the Australian-listed Macquarie Group Limited and the operating company for Macquarie Group Limited's non banking operations. Macquarie Capital Group Ltd. often invests alongside Macquarie Group managed funds in investments of this kind in an underwriting capacity. This is the case for Puget Holdings, and Macquarie Capital Group Ltd. expects to sell down its minority position to other Macquarie Group-managed funds prior to financial close or shortly thereafter. See Leslie, Exh. No. 31T at 8:26 – 9:2; Leslie, TR. 721:14-21.

¹² Macquarie Infrastructure Partners, Macquarie Capital Group Ltd. and Macquarie-FSS Infrastructure Trust are all members of the Macquarie Group. See Leslie, Exh. No. 31T at 5:17 –6: 8. For purposes of this proceeding, the Macquarie Group refers to Macquarie Group Limited with its subsidiaries, affiliates, and the vehicles they manage. Macquarie Group comprises two separate sub groups, a Banking Group (including Macquarie Bank Limited) and a Non-Banking Group, known as Macquarie Capital, which undertakes principal investment activity and provides a full range of investment services including financial advisory and funds management. See Leslie, Exh. No. 31T at 1 n.1.

¹³ See Leslie, Exh. No. 31T at 5:17 – 6:6.

¹⁴ See Wiseman, Exh. No. 151T at 10:1-5; Leslie, TR. 719:14-22.

1 5. These members of Puget Holdings (the “Investor Consortium”) have already
2 infused \$296 million of equity into PSE as part of a private placement of Puget Energy shares in
3 December 2007,¹⁵ undertaken in conjunction with the signing of the merger agreement, and have
4 committed to invest an additional \$3.1 billion into Puget Energy at closing.¹⁶ Additionally, the
5 Investor Consortium has put into place \$1.4 billion of committed credit facilities that PSE may
6 draw on after closing to fund capital expenditure.¹⁷ At the same time the Joint Applicants have
7 sought to strengthen the balance sheet and credit quality of PSE with additional equity and
8 commitments to maintain an investment grade rating and a capital ratio of not less than 44%
9 (unless a lower ratio is used to set rates).¹⁸ Further, the Proposed Transaction includes new
10 dividend restrictions, ring fencing mechanisms, and restrictions on the business purpose of Puget
11 Energy that together provide protections not currently available to PSE’s customers.¹⁹

12 6. The members of Puget Holdings are engaged and responsible owners of utility
13 assets and will remain independent of PSE management. In response to concerns of parties to
14 this proceeding (and in keeping with the experiences of the members of the Investor Consortium
15 that utility ownership requires sensitivity and awareness to local needs and concerns), the
16 investors have committed to a local presence on the boards of Puget Holdings and PSE.²⁰ The
17 chief executive officer of PSE and one local director will serve on the board of Puget Holdings.

¹⁵ See generally Markell, Exh. No. 71T at 11:6 – 14:8.

¹⁶ See generally Multiparty Settlement, Exh. No. 301 at ¶ 9.

¹⁷ See Multiparty Settlement, Exh. No. 301, Appx. A, Commitment No. 3; see also Early, *et al.*, Exh. No. 302T at 12:3-5.

¹⁸ See Multiparty Settlement, Exh. No. 301, Appx. A, Commitment No. 35; see also Early, *et al.*, Exh. No. 302T at 15:7-10.

¹⁹ See Multiparty Settlement, Exh. No. 301, Appx. A, Commitment Nos. 8, 9, 10, 16, 19, 20, 25, 26, 27, 28, 35, 36, 37, 38, 39, 40, 56, and 59; see also Early, *et al.*, Exh. No. 302T at 14:1 –24:1.

²⁰ See Early, *et al.*, Exh. No. 302T at 26:3-12.

1 These two individuals and one additional local director will serve on the board of PSE.²¹ One of
2 these local directors will serve as chairman of the board of PSE and Puget Holdings.²² In
3 addition, PSE will continue to be locally managed, be headquartered in PSE’s service territory²³
4 and will seek to retain existing senior management.²⁴ In response to concerns that private
5 ownership could lead to less transparency in management, the Joint Applicants have committed
6 that Puget Energy and PSE will continue to abide by many of the requirements of the Securities
7 and Exchange Commission (“SEC”),²⁵ the New York Stock Exchange (“NYSE”),²⁶ and
8 Sarbanes-Oxley,²⁷ which apply to publicly trade companies, although Puget Energy will no
9 longer be a publicly traded company.

10 7. In addition, the commitments made by the Joint Applicants provide benefits to
11 customers that do not currently exist. Most notably, the \$100 million in rate credits that the Joint
12 Applicants have agreed to provide over the next ten years is more sizeable than rate credits
13 offered in any previous utility change of control transactions in Washington and will provide a
14 significant investment in the Puget Sound economy.²⁸

²¹ See Multiparty Settlement, Exh. No. 301, Appx. A, Commitment No. 41; *see also* Early, *et al.*, Exh. No. 302T at 26:4-9.

²² See Reynolds, Exh. No. 135 at 1.

²³ See Multiparty Settlement, Exh. No. 301, Appx. A, Commitment No. 41; *see also* Early, *et al.*, Exh. No. 302T at 26:4-9.

²⁴ See Multiparty Settlement, Exh. No. 301, Appx. A, Commitment No. 17; *see also* Early, *et al.*, Exh. No. 302T at 26:3-4.

²⁵ See Multiparty Settlement, Exh. No. 301, Appx. A, Commitment No. 44; *see also* Early, *et al.*, Exh. No. 302T at 25:12-17.

²⁶ See Multiparty Settlement, Exh. No. 301, Appx. A, Commitment No. 43; *see also* Early, *et al.*, Exh. No. 302T at 25:10-12.

²⁷ See Multiparty Settlement, Exh. No. 301, Appx. A, Commitment No. 45; *see also* Early, *et al.*, Exh. No. 302T at 25:17-19.

²⁸ See Multiparty Settlement, Exh. No. 301, Appx. A, Commitment No. 34; *see also* Early, *et al.*, Exh. No. 302T at 27:13 – 29:3.

1 8. Throughout these proceedings, in the Joint Applicants’ direct testimony, rebuttal
2 testimony and in the settlement process, the Joint Applicants have demonstrated their
3 commitment to work with parties to this case, stakeholders in the community, and the
4 Commission, to forge a positive working relationship and to be transparent in governance and
5 management issues. The Joint Applicants have made 63 commitments addressing a wide range
6 of topics including:

- 7 • Capital Requirement and Access to Capital Commitments;
- 8 • Financial Integrity Commitments;
- 9 • Regulatory and Ring Fencing Commitments;
- 10 • Staffing, Management, and Governance Commitments;
- 11 • Local Presence Commitments;
- 12 • Rate Commitments;
- 13 • Quality of Service Commitments;
- 14 • Low-Income Assistance Commitments; and
- 15 • Environmental, Renewable Energy, and Energy Efficiency
16 Commitments.²⁹

17 9. The comprehensive commitments offered as part of the Proposed Transaction
18 strengthen PSE financially by increasing the equity and decreasing the debt at PSE, which is
19 consistent with the direction PSE has been moving over the past six years. Mechanisms such as
20 dividend restrictions, which do not currently exist, have been put into place through these
21 commitments to ensure that PSE remains financially strong. The commitments also protect
22 PSE’s customers from risks associated with business activities of non-regulated affiliates.

²⁹ See Multiparty Settlement, Exh. No. 301, Appx. A; *see also* Early, *et al.*, Exh. No. 302T at 10:13 – 33:7.

1 13. The Proposed Transaction meets the Commission standard for approval. As
2 discussed below, the Proposed Transaction provides additional benefits and protections to
3 customers, in addition to the benefits and protections that the Joint Applicants offered in their
4 direct and rebuttal filings. The Proposed Transaction is not contrary to law, nor does it offend
5 public policy, and the evidence supports approval of the Proposed Transaction.

6 **B. The Proposed Transaction Satisfies the Commission’s Standard for**
7 **Approval of a Change of Control of a Public Service Company**

8 14. WAC 480-143-170 establishes the standard by which the Commission reviews an
9 application for a change of control of a public service company through transfer of the public
10 service company’s stock, filed pursuant to Chapter 80.12 RCW. The rule states that:

11 If, upon examination of any application and accompanying exhibits, or
12 upon a hearing concerning the same, the commission finds that the
13 proposed transaction is not consistent with the public interest, it shall deny
14 the application.³³

15 The Commission has found that this standard does not require a showing of positive benefits to
16 the public in order to approve a change of control:

17 The standard in our rule does not require the Applicants to show that
18 customers, or the public generally, will be made better off if the
19 transaction is approved and goes forward. In our view, Applicants’ initial
20 burden is satisfied if they at least demonstrate no harm to the public
21 interest.

22 ...

³³ WAC 480-143-170; see also *In re PacifiCorp and Scottish Power PLC*, Docket No. UE-981627, Third Supplemental Order at 3 (Apr. 2, 1999) (articulating a standard of “no harm” to the public interest).

1 Generally, then, we need consider only whether Applicants are qualified
2 to take over management of a jurisdictional public utility in Washington.³⁴

3 15. As discussed in more detail below, approval of the Proposed Transaction will not
4 cause harm, and in fact provides significant benefits, to PSE's customers and the public interest.
5 Customers will receive \$100 million in rate credits over ten years. PSE's capital structure and
6 balance sheet will improve. PSE will have a dedicated source of funding to meet its extensive
7 capital expenditure needs. Protections have been put in place to isolate PSE's customers from
8 any risks from unregulated affiliates. PSE will continue to be regulated by the Commission,
9 locally managed and will have local directors on its board.

10 **C. Public Counsel's Opposition to the Proposed Transaction Is Based on an**
11 **Application of Incorrect Standards**

12 16. Public Counsel's opposition to the Proposed Transaction is based on the
13 application of several incorrect legal standards. For example, Public Counsel focuses on
14 whether the Joint Applicants have shown a need for the Proposed Transaction:

15 This transaction is not necessitated by the public interest generally or the
16 interests of Puget's customers . . . The Joint Applicants have shown
17 neither a financial nor an operational need for this acquisition. There is no
18 demonstration that Puget is unable to raise the capital necessary to fulfill
19 its public service obligations.³⁵

20 17. Although the Joint Applicants believe that such a need has been demonstrated—
21 given PSE's significant capital expenditure requirements over the next several years—such a
22 showing of need is not the standard by which the Commission must weigh the Proposed
23 Transaction. Nor is it required that the Joint Applicants demonstrate that the Proposed

³⁴ *In re PacifiCorp and Scottish Power plc*, Docket No. UE-981627, Third Supplemental Order at 3 (Apr. 2, 1999).

³⁵ Hill, Exh. No. 261HCT at 2:11-17.

1 Transaction is superior to any other hypothetical proposed transaction or to the status quo.
2 Absent a showing that the Proposed Transaction harms the public interest or that the Joint
3 Applicants are not qualified to manage PSE, the Commission must approve the Proposed
4 Transaction.³⁶

5 18. Public Counsel also incorrectly evaluates the Proposed Transaction by comparing
6 the benefits to shareholders against the benefits to customers. This is an irrelevant analysis,
7 given the “no harm” standard discussed above. Further, as discussed in more detail below,
8 customers will benefit significantly from the Proposed Transaction including by way of their
9 receipt of \$100 million in rate credits—most of which are not offsettable and none of which are
10 associated with any loss of jobs. These rate credits exceed—by a wide margin—any rate credit
11 provided in previous transactions in Washington, and they provide not only a benefit to
12 individual customers but also a significant investment in the Puget Sound region. Moreover, the
13 ring fencing and regulatory commitments provided in the Proposed Transaction provide
14 protections that PSE customers currently do not have. Commitments setting a minimum equity
15 level and prohibiting dividend payments to PSE’s parent if financial metrics are not met ensure
16 that PSE can maintain an appropriate equity layer even in times of financial distress.

17 19. In sum, Joint Applicants and the other settling parties have satisfied the legal
18 standards, and the Commission should approve the Proposed Transaction.

³⁶ See *In re PacifiCorp and Scottish Power plc*, Docket No. UE-981627, Third Supplemental Order at 3 (Apr. 2, 1999).

1 **III. THE PROPOSED TRANSACTION IS IN THE PUBLIC INTEREST**
2 **AND SHOULD BE ACCEPTED**

3 **A. The Proposed Transaction Provides PSE Access to Capital to Allow PSE to**
4 **Meet Its Capital Expenditure Needs by Matching PSE with Experienced,**
5 **Well-Funded Infrastructure Investors**

6 20. A key component of the Proposed Transaction is the superior access to capital
7 brought by Puget Holdings to support PSE’s significant capital expenditure. Public Counsel has
8 not disputed PSE’s significant capital needs over the next five years, and the evidence
9 demonstrates PSE has faced, and expects to face, increasing difficulty financing its capital needs
10 through equity issuances in the public market.³⁷ As part of the Proposed Transaction, the
11 members of Puget Holdings have (i) contributed a much needed \$296 million in equity in
12 advance of the Proposed Transaction, demonstrating their willingness to invest equity in PSE;³⁸
13 (ii) committed to an additional \$3.1 billion investment at close of the Proposed Transaction;³⁹
14 and (iii) secured credit facilities of sufficient size, together with substantial reinvestment of cash
15 flow, to fund PSE’s projected capital infrastructure needs.⁴⁰

16 **1. PSE Faces Significant Challenges In Funding Its Capital Expenditure**
17 **Needs Over the Next Several Years**

18 21. The Joint Applicants have provided evidence of PSE’s significant capital
19 expenditure needs through 2013 and beyond. Customer growth, the need to expand and replace

³⁷ See generally Campbell, Exh. No. 1CT at 6:14 – 8:2; Markell, Exh. No. 75CT at 3:2 – 15:10; Pettit, Exh. No. 111CT at 7:1 – 19:5.

³⁸ See generally Markell, Exh. No. 71T at 11:6 – 14:8.

³⁹ See Early, *et al.*, Exh. No. 302T at 33:20-21.

⁴⁰ See Early, *et al.*, Exh. No. 302T at 33:21 – 34:2.

1 PSE’s aging power generating and delivery infrastructure, and the need to acquire more “green”
 2 energy, all contribute to PSE’s increasing capital needs.⁴¹ Public Counsel has not disputed
 3 PSE’s need for substantial capital.

4 22. PSE faces significant challenges in its efforts to access capital at a reasonable cost
 5 in order to meet the growing energy needs of its customers, while continuing to provide safe and
 6 reliable service to this dynamic region.⁴² PSE has prepared a business plan that includes
 7 management’s estimates of the capital expenditures required to execute this plan.⁴³ Management
 8 has estimated that \$5.7 billion of capital expenditures are required between 2008 and 2013 to
 9 continue to meet the needs of PSE’s customers.⁴⁴

10 23. PSE management estimates that approximately \$2.3 billion of this capital
 11 requirement can be provided through internally generated funds, resulting in a requirement to
 12 access the capital markets for the remaining \$3.4 billion of capital required.⁴⁵ PSE forecasts that
 13 \$2 billion of this will be financed with debt, leaving \$1.4 billion that will need to be financed
 14 with primarily equity and equity-like securities.⁴⁶

15 24. Puget Energy’s estimated equity issuances per its business plan average
 16 approximately [REDACTED] from 2009 through 2013, which is well above the industry
 17 average equity issuance.⁴⁷ Assuming [REDACTED], PSE’s equity needs represent a
 18 99th percentile transaction in terms of relative size among regulated power companies.⁴⁸ In

⁴¹ See Reynolds, Exh. No. 131T at 4:7-13.

⁴² See generally Campbell, Exh. No. 1CT at 6:14 – 8:2; Markell, Exh. No. 75CT at 3:2 – 15:10; Pettit, Exh. No. 111CT at 7:1 – 19:5.

⁴³ See Markell, Exh. No. 76C.

⁴⁴ See Pettit, Exh. No. 111CT at 7:4-6; see also Markell, Exh. No. 76C.

⁴⁵ See Pettit, Exh. No. 111CT at 7:7-10; see also Markell, Exh. No. 76C.

⁴⁶ See Pettit, Exh. No. 111CT at 7:10-12; see also Markell, Exh. No. 76C.

⁴⁷ See Pettit, Exh. No. 111CT at 10:18-20; see also Markell, Exh. No. 76C.

⁴⁸ See Pettit, Exh. No. 111CT at 10:20 – 11:1.

1 other words, 99% of all equity offerings in the sector would be smaller than what PSE needs to
 2 raise, in relative terms. Practically speaking, the PSE equity financing would be executed in a
 3 series of tranches over time, to enable the market to digest this level of issuance. However, even
 4 on a cumulative 5-year basis, the PSE needs represent 90th percentile equity needs, excluding
 5 equity issue for balance sheet repair by severely overleveraged power companies.⁴⁹

6 25. The Board of Puget Energy was concerned that (i) this long-term business plan
 7 required raising significant equity and debt capital relative to both internally generated funds and
 8 to the capital base of Puget Energy and (ii) these external financing requirements could place
 9 pressure on share price and credit ratings.⁵⁰ Smaller and mid-size utilities that need to fund large
 10 projected capital spending programs, such as PSE, are often unfavorably viewed by the public
 11 markets as “serial” issuers of equity. When combined with significant regulatory lag, the
 12 perceived risk profile can increase.⁵¹

13 26. Even if Puget Energy and PSE were to execute on all elements of their business
 14 plans perfectly, Puget Energy’s medium-term earnings per share outlook [REDACTED]
 15 [REDACTED]⁵² Because
 16 equity investors look for consistent and rising earnings per share to support rising dividends, the
 17 Board of Puget Energy was very concerned that regular and large equity offerings in the face of
 18 their forecast earnings per share outlook would adversely affect the share price, cause dilution of
 19 current shareholders, and ultimately make it difficult for PSE to obtain the necessary capital for
 20 capital expenditures.⁵³ The analysis of Morgan Stanley, independent financial advisor to the

⁴⁹ See Pettit, Exh. No. 111CT at 11:5-8.

⁵⁰ See Campbell, Exh. No. 1CT at 6:16-20.

⁵¹ See Reynolds, Exh. No. 133T at 14:7-11; *see generally* Pettit, Exh. No. 111CT.

⁵² See Campbell, Exh. No. 1CT at 7:10-12.

⁵³ See Campbell, Exh. No. 1CT at 7:13-17.

1 Board of Puget Energy, supported this forecast of essentially flat earnings and the need for
2 significant amounts of capital relative to Puget Energy's and PSE's earnings power.⁵⁴

3 27. Although Puget Energy has raised over \$800 million of capital over the past six
4 years through four equity issuances, totaling approximately 37 million common shares,⁵⁵
5 approximately 37.5% of the capital raised by Puget Energy over the past six years
6 (approximately \$296 million of the \$800 million) was provided by members of Puget Holdings
7 pursuant to a private placement undertaken in conjunction with the Proposed Transaction.⁵⁶ This
8 investment was made at the end of 2007, in preparation for 2008 capital requirements.⁵⁷ When
9 the private placement is removed from the historical analysis, Puget Energy's future external
10 equity requirement (including hybrid equity) is even more daunting. Puget Energy raised only
11 \$500 million over the past six years up to the date of execution of the Merger Agreement⁵⁸ and
12 required an additional \$1.2 billion to fund PSE's projected capital needs from through 2013.

13 28. Moreover, Puget Energy found each public issuance to be increasingly
14 challenging.⁵⁹ Indeed, Puget Energy's last public offering proved to be a very difficult
15 transaction—one that illustrated the difficulties of serial equity issuances to the Board of Puget
16 Energy.⁶⁰

⁵⁴ See Campbell, Exh. No. 1CT at 7:20 – 8:2.

⁵⁵ See Reynolds, Exh. No. 133T at 12:4-6.

⁵⁶ See generally Markell, Exh. No. 71T at 11:6 – 14:8.

⁵⁷ See generally Markell, Exh. No. 71T at 11:6 – 14:8.

⁵⁸ Over the past six years, Puget Energy has raised over \$800 million of capital through four equity issuances. See Reynolds, Exh. No. 133T at 12:4-6. As discussed above, the members of Puget Holdings provided \$296 million of the \$800 million pursuant to the private placement in December of 2007. Therefore, Puget Energy, raised \$504 million in the public markets since 2002.

⁵⁹ See Reynolds, Exh. No. 133T at 12:6-7; Campbell, TR. 991:12-22.

⁶⁰ See Reynolds, TR. 605:7 – 608:3.

1 **2. Puget Holdings Has Arranged Committed Financing for PSE’s**
2 **Capital Needs and Has the Financial Capabilities to Meet Those**
3 **Needs for the Long-Term**

4 29. The members of Puget Holdings understand PSE’s capital needs and the
5 importance of meeting those needs to the Puget Sound region. They also have the financial
6 credentials to fulfill this need. As discussed above, in December 2007, the members of Puget
7 Holdings contributed to PSE, through a private placement undertaken in conjunction with the
8 signing of the merger agreement, nearly \$296 million in equity.⁶¹ At closing Puget Holdings
9 will contribute an additional \$3.1 billion in capital to Puget Energy.⁶² In addition, despite the
10 existing turmoil in the credit market, the Investor Consortium has arranged \$1.4 billion in
11 committed credit facilities on which PSE may draw to meet its capital expenditure needs after
12 closing.⁶³ These capital expenditure credit facilities will by their terms limit the use of such
13 funds only for financing PSE capital expenditures.⁶⁴ Other un-drawn facilities are similarly
14 reserved for working capital needs and hedging collateral.⁶⁵ With an aggregate of \$499 billion in
15 assets under management, the Investor Consortium is also capable of investing additional capital
16 to benefit PSE and its customers.⁶⁶

17 **a. The Members of Puget Holdings Have Billions of Dollars in**
18 **Capital to Invest**

19 30. The investors in Puget Holdings are investment funds and specialized
20 infrastructure investors with “large and growing pools of capital for which they need to find a

⁶¹ See generally Markell, Exh. No. 71T at 11:6 – 14:8.

⁶² See generally Multiparty Settlement, Exh. No. 301 at ¶ 9.

⁶³ See Multiparty Settlement, Exh. No. 301, Appx. A, Commitment No. 3; see also Early, *et al.*, Exh. No. 302T at 12:1-5.

⁶⁴ See Multiparty Settlement, Exh. No. 301, Appx. A, Commitment No. 58; see also Early, *et al.*, Exh. No. 302T at 13:12-17.

⁶⁵ See Markell, Exh. No. 71T at 28:6 – 29:4.

⁶⁶ See Early, *et al.*, Exh. No. 302T at 34:2-4.

1 home.”⁶⁷ The investors in these funds generally include entities such as pension funds,
2 foundations and endowments with long-term investment horizons.⁶⁸ Accordingly, these funds
3 generally seek out investments that produce steady, predictable, long-term cash flow streams
4 from high quality assets, and they do not require a sale or defined exit strategy to achieve their
5 investment goals.⁶⁹ These types of investments effectively match the long-term liabilities of
6 public sector and corporate pension plans such as Canada Pension Plan Investment Board,
7 British Columbia Investment Management Corporation, Alberta Investment Management, and
8 the investors in Macquarie Group’s managed infrastructure funds.⁷⁰

9 31. As discussed in the Joint Application and at hearing, the Macquarie Capital
10 Group, Ltd. is underwriting the commitment to invest in Puget Holdings with the expectation
11 that it will transfer its interest prior to or shortly after closing to a Macquarie-managed fund.⁷¹ It
12 is currently expected that Macquarie Capital Group, Ltd. will transfer this interest in Puget
13 Holdings to Macquarie Infrastructure Partners II.⁷² Macquarie Infrastructure Partners II is a
14 “sister fund” to Macquarie Infrastructure Partners I, and Macquarie Infrastructure Partners, Inc.
15 manages and controls each of Macquarie Infrastructure Partners I and Macquarie Infrastructure
16 Partners II.⁷³ The Joint Applicants will provide the Commission with fourteen days advance
17 notice of such a transfer in accordance with Commitment No. 26.⁷⁴

⁶⁷ See Leslie, TR. 465:10-11.

⁶⁸ See Leslie, TR. 465:6-8.

⁶⁹ See Markell, Exh. No. 31T at 6:16 – 7:20; McKenzie, Exh. No. 91T at 2:4 – 6:4; Webb, Exh. No. 141T at 2:6 – 7:2; Wiseman, Exh. No. 151T at 2:5 – 7:14.

⁷⁰ See generally Leslie, Exh. No. 31T at 6:18-21; Joint Applicants’ Response to Bench Request No. 13, Exh. No. 413; McKenzie, Exh. No. 91T at 2:4 – 6:4; Webb, Exh. No. 141T at 2:6 – 7:2; Wiseman, Exh. No. 151T at 2:5 – 7:14.

⁷¹ See Leslie, Exh. No. 31T at 8:26 – 9:2.

⁷² See Leslie, TR. 721:14-21.

⁷³ See Leslie, TR. 721:14-21.

⁷⁴ See Joint Applicants’ Response to Bench Request No. 19, Exh. No. 419.

32. In many respects, the members of Puget Holdings are not significantly different from some of the current large institutional investors in Puget Energy.⁷⁵ However, the opportunity to invest directly in PSE, rather than investing through the public markets, benefits both PSE and the members of the Investor Consortium. Direct investment frees PSE from the public market's demands for short-term returns and quarterly earnings per share performance,⁷⁶ shields the utility and the investors from the volatility in the listed equity market, and provides the members of the Investor Consortium with the opportunity to provide more direct support of the management and oversight of their investment.⁷⁷

33. It is undisputed that the members of Puget Holdings have significant assets under management, are experienced and responsible utility investors, and are looking for relatively stable investments in which to invest their capital. The table below shows the significant assets under management for the members of Puget Holdings.⁷⁸

Assets Under Management	Alberta Investment Management Corporation	British Columbia Investment Management Corporation	Canada Pension Plan Investment Board	Macquarie Group, Ltd.	Total
(\$ billions) as of Mar. 31, 2008	\$73.5 ⁷⁹	\$83.3 ⁸⁰	\$120.5 ⁸¹	\$222.0 ⁸²	\$499.3⁸³

⁷⁵ See Joint Applicants' Response to Bench Request No. 6, Exh. No. 406.

⁷⁶ See, e.g., Reynolds, TR. 608:16 – 609:8

⁷⁷ See, e.g., Wiseman, Exh. No. 151T at 8:19-21, 10:9-11:8.

⁷⁸ Canadian and Australian Dollars converted to USD at 1.02 and 1.045 / 1, respectively. See Leslie, Exh. No. 38HCT at 8:n.1.

⁷⁹ See McKenzie, Exh. No. 91T at 4.

⁸⁰ See Webb, Exh. No. 141T at 3.

⁸¹ See Wiseman, Exh. No. 151T at 4.

⁸² See Leslie, Exh. No. 38HCT at 8.

⁸³ See Leslie, Exh. No. 38HCT at 8:13-15.

1 34. The Canada Plan Pension Investment Board (“CPP Investment Board”) provides
2 a good example of the stability and financial growth of these investors. CPP Investment Board’s
3 long-term goal is to contribute to the financial strength of the Canada Pension Plan (“CPP”) and
4 help sustain the pensions of 17 million CPP contributors and beneficiaries by investing CPP
5 assets (i.e., the funds not needed by the CPP to pay current benefits) and to maximize returns
6 without undue risk of loss.⁸⁴ Contributions to the CPP are expected to exceed annual benefits
7 paid through to the end of 2019, providing a 12-year period before any portion of the investment
8 income is needed to help pay pensions. The Chief Actuary of Canada has projected that CPP
9 assets will grow to approximately C\$250 billion by 2016.⁸⁵

10 **b. The Members of Puget Holdings are Experienced**
11 **Infrastructure Investors that Hold Direct Ownership Interests**
12 **in Other Regulated Utilities**

13 35. Not only do the members of Puget Holdings have significant assets under
14 management, they are among the most experienced infrastructure investors in regulated utilities
15 in the United States and globally. They have successfully gained regulatory approval of their
16 ownership of several utilities globally over the past decade by being responsive to local concerns
17 and the responsibilities that come with ownership of important community assets.

⁸⁴ See Wiseman, Exh. No. 151T at 2:9-14.

⁸⁵ See Wiseman, Exh. No. 151T at 2:15-20.

1 **Direct Regulated Utility Investments by At Least One Investor Consortium Member⁸⁶**

Asset	Location	Type of Service
AltaLink	Canada	Electric Trans.
United Energy Distribution	Australia	Electric T&D
Multinet Gas	Australia	Gas T&D
Alinta Gas Networks	Australia	Gas T&D
Dampier to Bunbury Pipeline	Australia	Gas Trans.
Wales & West Utilities	UK	Gas T&D
AWG (Anglian Water Services)	UK	Water
Sutton & East Surrey Water	UK	Water
The Gas Company	USA	Gas T&D
Corix	USA, Canada	Water
Transelec	Chile	Electric T&D
Thames Water	UK	Water
Aquarion Water	USA	Water
Duquesne Light	USA	Electric T&D

2 36. Three members of Puget Holdings are members of the Macquarie Group—
3 Macquarie Infrastructure Partners I, Macquarie-FSS Infrastructure Trust, and Macquarie Capital
4 Group Ltd (in an underwriting capacity for a fund expected to be Macquarie Infrastructure
5 Partners II). The Macquarie Group is one of the world’s largest owners and managers of
6 infrastructure assets. Through its investments, the Macquarie Group is responsible for providing
7 utility service to over 13.7 million households.⁸⁷ Macquarie Infrastructure Partners currently has
8 twelve infrastructure investments in the utility, toll road, ports and communications sectors.⁸⁸
9 Macquarie-FSS Infrastructure Trust currently holds interests in five assets across sectors

⁸⁶ Please see Joint Applicants’ Response to Public Counsel Data Request No. 3020, Exh. No. 51HC, for more information regarding the direct regulated utility investments.

⁸⁷ See Leslie, Exh. No. 31T at 9:13-21.

⁸⁸ See Leslie, Exh. No. 31T at 8:7-15; Leslie, TR. 709:1-5.

1 including communications infrastructure, vehicle inspection, utilities, and water infrastructure in
2 three countries: the USA, Spain, and the U.K.⁸⁹

3 37. The CPP Investment Board has direct private investments in infrastructure,
4 including a regulated water company, wireless communication towers, electrical transmission
5 company, and regulated gas distribution business.⁹⁰ The CPP Investment Board also invests in
6 infrastructure funds.⁹¹

7 38. bcIMC's Strategic Investment and Infrastructure Program was established in 2002
8 to offer clients the ability to gain investment exposure to long-term interests in tangible assets
9 traditionally associated with the core infrastructure of modern economies.⁹² The program has
10 holdings in North America, Europe and Latin America. Major direct investments have been
11 made in water utilities (Corix, Thames Water, and Aquarion Company) and energy and power
12 companies (Transelec SA and InterGen NV).⁹³

13 39. AIMCo invests client funds across a wide range of asset classes, such as equities,
14 bonds, and alternative investments. Alternative investments include infrastructure, private
15 equity, real estate, and timberland.⁹⁴ AIMCo has been investing in infrastructure for more than
16 five years and has an investment team dedicated to making and actively managing infrastructure
17 investments. AIMCo has made eight direct equity investments and has invested in twelve
18 infrastructure funds.⁹⁵

⁸⁹ See Leslie, Exh. No. 31T at 8:16-25.

⁹⁰ See Wiseman, Exh. No. 151T at 6:6-20.

⁹¹ See Wiseman, Exh. No. 151T at 6:21-28.

⁹² See Webb, Exh. No. 141T at 4:18-21.

⁹³ See Webb, Exh. No. 141 T at 5:2-7.

⁹⁴ See McKenzie, Exh. No. 91T at 2:17-19.

⁹⁵ See McKenzie, Exh. No. 91T at 4:12-15.

1 40. Notwithstanding their investment experience in infrastructure assets and regulated
2 utilities, the members of Puget Holdings have made clear that they do not consider themselves to
3 be managers or operators of utilities.⁹⁶ The investors view themselves as engaged owners and
4 informed board members who believe that an effective long-term investment involves supporting
5 strong management teams, such as the PSE management team currently in place. Puget
6 Holdings intends to provide an environment where local management and local employees have
7 the strategic support to do their jobs with a view to long-term success.⁹⁷ Toward this end, Puget
8 Holdings has committed to seek to retain the current management and employees of PSE, and
9 has made several commitments indicating its intent for PSE to continue pursuing the same
10 objectives PSE has been pursuing over the past six years including service quality, renewable
11 resource acquisition, energy conservation, and support of low-income programs.

12 **3. The Proposed Transaction Provides Further Protection to PSE**
13 **Through Express Commitments that Ensure that PSE Can Access**
14 **Capital Should Puget Energy or Puget Holdings Face Financial**
15 **Distress**

16 41. Notwithstanding the financial capabilities of the members of Puget Holdings,
17 prior to settlement some parties expressed concern that de-listing Puget Energy might cause
18 harm by limiting PSE's ability to access the public markets. The investors firmly believe that
19 un-listed capital is a more secure and stable form of equity financing for PSE than the public
20 markets. Recent equity market turbulence only supports this belief. Nevertheless, in response to
21 these concerns, the Joint Applicants agreed to a commitment that would ensure that Puget

⁹⁶ See Leslie, Exh. No. 31T at 20:14 – 23:12; Leslie, Exh. No. 36; McKenzie, Exh. No. 91T at 7:4-11; Webb, Exh. No. 141T at 9:3-7; Wiseman, Exh. No. 151T at 10:19 – 11:8.

⁹⁷ See Leslie, Exh. No. 31T at 20:14 – 23:12; Leslie, Exh. No. 36; McKenzie, Exh. No. 91T at 7:4-11; Webb, Exh. No. 141T at 9:3-7; Wiseman, Exh. No. 151T at 10:19 – 11:8.

1 Holdings can access the public market to raise equity on behalf of PSE, and that PSE has means
2 to access capital even if Puget Energy or Puget Holdings experience financial distress.

3 42. Commitment No. 35 states that Puget Holdings will not be prohibited from
4 issuing new equity to third parties (including public markets).⁹⁸ Additionally, in Commitment
5 No. 35, the Joint Applicants commit that the transaction documents permit PSE to issue certain
6 hybrid securities to third parties (including public markets) and to Puget Holdings.⁹⁹ If Puget
7 Holdings makes a new equity issuance for the purpose of (i) contributing the proceeds thereof
8 (through its relevant subsidiaries) to Puget Energy or PSE, or (ii) applying the proceeds thereof
9 toward the purchase from PSE of hybrid securities that are permitted to be issued under the
10 transaction documents,¹⁰⁰ Commitment No. 35 mandates that the proceeds of any such new
11 equity issuances by Puget Holdings shall be used for such purpose.¹⁰¹ Thus, PSE has options
12 available to raise additional capital and for equity to be infused into the operating utility in the
13 event Puget Energy or Puget Holdings is in financial difficulty.¹⁰² The Joint Applicants commit
14 in Commitment No. 35 to provide an annual certificate of an officer of Puget Holdings certifying
15 that neither Puget Holdings nor PSE is prohibited from undertaking the transactions described in
16 such Commitment No. 35.¹⁰³

⁹⁸ See Multiparty Settlement, Exh. No. 301, Appx. A, Commitment No. 35; *see also* Early, *et al.*, Exh. No. 302T at 12:10-13.

⁹⁹ See Multiparty Settlement, Exh. No. 301, Appx. A, Commitment No. 35; *see also* Early, *et al.*, Exh. No. 302T at 12:14-16.

¹⁰⁰ See Multiparty Settlement, Exh. No. 301, Appx. A, Commitment No. 35; *see also* Early, *et al.*, Exh. No. 302T at 12:16-21.

¹⁰¹ See Multiparty Settlement, Exh. No. 301, Appx. A, Commitment No. 35; *see also* Early, *et al.*, Exh. No. 302T at 12:16-21.

¹⁰² See Markell, Tr, 541:11 – 543:4.

¹⁰³ See Multiparty Settlement, Exh. No. 301, Appx. A, Commitment No. 34; *see also* Early, *et al.*, Exh. No. 302T at 13:1-4.

B. The Proposed Transaction Makes PSE a Stronger Utility

43. The Proposed Transaction will strengthen PSE by increasing the Company’s equity ratio and establishing a number of ring fencing measures and dividend restrictions tied to equity level, credit ratings and other financial metrics that will separate PSE from entities above it in the corporate structure.

[REDACTED]

[REDACTED]

1. The Proposed Transaction Strengthens PSE’s Capital Structure

44. The Proposed Transaction reduces the debt capital of PSE and reduces PSE’s financial risk, contrary to assertions of Public Counsel that the Proposed Transaction adds “substantial amounts of debt capital [that] would increase Puget’s financial risk.”¹⁰⁴ Indeed, as shown below, the Proposed Transaction is projected to strengthen the capital structure of PSE.¹⁰⁶

	Actual (Sept. 30, 2007)	Forecast Assuming No Consummation of the Proposed Transaction (at Sept. 30, 2008)	Forecast Assuming Consummation of the Proposed Transaction (at Sept. 30, 2008)
Debt including Short-term & Current Maturities	60.4%	56.3%	49.6%
Preferred Stock	0.0%	0.0%	0.0%
Common Equity	39.6%	43.7%	50.4%
Total	100.0%	100.0%	100.0%

¹⁰⁴ See Horton *et al.*, Exh. No. 304CT at 6:4 – 7:4; Horton *et al.*, Exh. No. 305C at 6-7.

¹⁰⁵ Hill, Exh. No. 261HCT at 4:5-6.

¹⁰⁶ See Horton, *et al.*, Exh. No. 306 at 1.

1 45. Although it is true that, under the Proposed Transaction, Puget Energy will have
2 debt, as discussed below, significant ring fencing provisions have been put into place, which
3 protect PSE’s customers from any potential risks associated with the debt at Puget Energy.
4 Moreover, although Public Counsel has focused on the fact that Puget Energy currently has no
5 debt, there is nothing today that prevents the issuance of debt by Puget Energy. For example, if
6 the Commission were not to approve the Proposed Transaction, debt could be placed at Puget
7 Energy to fund PSE’s significant capital expenditure needs or even to make acquisitions of
8 unregulated businesses. Without the Proposed Transaction, the extensive ring fencing provisions
9 provided for in the Proposed Transaction would not exist (e.g., dividend restrictions, limitations
10 on ownership of entities other than PSE). Accordingly, if Puget Energy were to issue debt or
11 acquire unregulated businesses, customers would face risks that they do not face under the
12 Proposed Transaction.

13 46. A number of commitments made by the Joint Applicants in the Proposed
14 Transaction serve to strengthen PSE’s capital structure. In Commitment No. 35, the Joint
15 Applicants have committed that (i) PSE will have a common equity ratio of not less than
16 50 percent as of the closing of the Proposed Transaction (or within sixty days thereof); and (ii) at
17 all times thereafter, PSE will have a common equity ratio of not less than 44 percent, except to
18 the extent a lower equity ratio is established for ratemaking purposes by the Commission.¹⁰⁷

19 47. Furthermore, Commitment No. 36 would prohibit PSE from declaring or making
20 any PSE distribution unless, on the date of such PSE distribution, the PSE common equity ratio
21 after giving effect to such PSE distribution is not less than 44%, except to the extent a lower

¹⁰⁷ See Multiparty Settlement, Exh. No. 301, Appx. A, Commitment No. 35; see also Early, *et al.*, Exh. No. 302T at 15:5-10.

1 equity ratio is established for ratemaking purposes by the Commission.¹⁰⁸ Contrary to the
2 assertion of Public Counsel that this Commitment No. 36 does not “help to protect the public
3 interest in this transaction”,¹⁰⁹ Commitment No. 36 provides direct benefits to PSE and its
4 customers because it assures that PSE will be capitalized with an appropriate level of equity over
5 the long term. Indeed, this Commitment No. 36 provides a significant improvement to the
6 “status quo,” where no such minimum equity level or related dividend restriction currently
7 exists. Under the “status quo,” external events can rapidly erode PSE’s equity ratio to the
8 detriment of PSE and its customers,¹¹⁰ and PSE is currently under no obligation to maintain such
9 a minimum equity level or to restrict its dividend payments if the minimum equity level is not
10 met. In their settlement rebuttal testimony, Commission Staff and the Joint Applicants discussed
11 how such a minimum equity level could have prevented the financial deterioration that PSE
12 experienced during the Western Energy Crisis in 2001. Commitment No. 36 would have
13 protected PSE by requiring that PSE maintain, at a minimum, a 44 percent equity ratio, except to
14 the extent a lower equity ratio is established for ratemaking purposes by the Commission. If
15 PSE’s equity ratio deteriorated below the minimum, the Investor Consortium could satisfy
16 Commitment No. 36 by limiting dividends from PSE or by providing additional equity infusions,
17 or a combination of the two.¹¹¹

18 48. Moreover, Public Counsel errs in suggesting that the Proposed Transaction will
19 cause PSE’s financial health to stop improving as a result of the use of “substantial amounts of
20 debt capital [that] would increase Puget’s financial risk.”¹¹² PSE’s financial health will be better

¹⁰⁸ See Horton, *et al.*, Exh. No. 304CT at 8:16 – 9:10.

¹⁰⁹ Hill, Exh. No. 261HCT at 10:18 – 11:5.

¹¹⁰ See Horton, *et al.*, Exh. No. 304CT at 12:8-17.

¹¹¹ See Horton, *et al.*, Exh. No. 304CT at 13:1 – 14:13.

¹¹² Hill, Exh. No. 261HCT at 4:5-6.

1 than recent historical levels, given the Commitment to have at least a 44% equity ratio, except to
2 the extent a lower equity ratio is established for ratemaking purposes by the Commission
3 (Commitment Nos. 35 and 36). Dividends from Puget Energy to Equico are further restricted by
4 Commitments Nos. 37 and 40, and, as stated in testimony, there is no intention to issue any third-
5 party debt at a corporate level above Puget Energy, reinforced by Commitment No. 38, which
6 prohibits Equico from issuing any debt whatsoever.¹¹³ All of the dividend restrictions serve to
7 strengthen PSE's equity ratio.

8 49. Public Counsel ignores the substantial upfront investment by the Investor
9 Consortium in PSE and the substantial reinvestment of PSE cash flow. [REDACTED]

10 [REDACTED]

11 [REDACTED]

12 [REDACTED].¹¹⁴ Finally, [REDACTED]

13 [REDACTED], as discussed below.

14 **2. The Joint Applicants Expect that the Proposed Transaction Will**
15 **Improve PSE's Credit Quality**

16 50. The Joint Applicants expect that the Proposed Transaction will *improve* the credit
17 quality of PSE (and thus lower PSE's ongoing debt costs paid by PSE customers) by:

- 18 1. increasing the equity ratio of PSE from 43.7% to 50.4%;
- 19 2. enforcing a minimum 44% equity ratio at PSE, unless a lower ratio
20 is approved by the Commission for ratemaking;
- 21 3. establishing a number of ring fencing measures and dividend
22 restrictions, including dividend restrictions directly tied to credit
23 ratings; and

¹¹³ See Horton, *et al.*, Exh. No. 304CT at 10:6-20.

¹¹⁴ See Horton, *et al.*, Exh. No. 304CT at 9:15 – 10:5.

1
2
3
4
5
6
7
8
9
10
11
12
13
14
15
16
17
18
19
20

4. [REDACTED]

¹¹⁵

51. [REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

¹¹⁶ [REDACTED]

[REDACTED]

[REDACTED] ¹¹⁷ [REDACTED]

[REDACTED]

52. [REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED] ¹¹⁸

¹¹⁵ See Horton, et al., Exh. No. 304CT at 5:10-22.
¹¹⁶ See Horton, et al., Exh. No. 304CT at 6:6-14; see also Horton, et al., Exh. No. 305C.
¹¹⁷ See Horton, et al., Exh. No. 304CT at 6:15-17.
¹¹⁸ See Horton, et al., Exh. No. 304CT at 6:20 – 7:5; see also Horton, et al., Exh. No. 305C.

1 **3. The Proposed Transaction Provides Extensive Ring Fencing**
2 **Provisions and Regulatory Commitments that Strengthen PSE and**
3 **Protect PSE’s Customers From Business Risks of Unregulated**
4 **Affiliates**

5 53. Ring fencing provisions and regulatory commitments are key components of the
6 Proposed Transaction. The Commission has recognized the importance of ring fencing in
7 previous transactions.¹¹⁹ Specifically, the Commission recognized that ring fencing provisions
8 serve to (i) protect utility customers from potential adverse impacts associated with a holding
9 company structure, (ii) protect customers from future financial risk, including the risk of
10 bankruptcy of parents and affiliates of the utility, (iii) protect customers from the effects of
11 affiliated interest transactions, (iv) require the utility and its parents and affiliates to keep
12 separate books, records, and assets, and (v) require that the utility and its parents and affiliates
13 provide the Commission and Staff with access to financial records relevant to the utility so the
14 Commission can continue to regulate the utility effectively.¹²⁰ The ring fencing commitments in
15 the Proposed Transaction are more comprehensive than the ring fencing provisions in other
16 transactions approved by this Commission. Tellingly, Public Counsel witness Stephen Hill
17 offered no additional ring fencing measures when questioned by the Commission but instead
18 criticized the amount of debt that lies outside of the ring fencing protections.¹²¹ As discussed
19 below, Public Counsel’s argument violates Commission precedent adopting the benefit/burden

¹¹⁹ See, e.g., *In re MDU Resources Group, Inc. & Cascade Natural Gas Corp.*, Docket No. UG-061721, Order 06 at ¶ 17 (June 27, 2007); *In re Avista Corp. d/b/a Avista Utils.*, Docket No. U-060273, Order 03 at ¶¶ 21-25 (Feb. 28, 2007); and *In re MidAmerican Energy Holdings Co. & PacifiCorp d/b/a Pac. Power & Light Co.*, Docket No. UE-051090, Order 07 at ¶ 16 (Feb. 22, 2006).

¹²⁰ See *In re MDU Resources Group, Inc. & Cascade Natural Gas Corp.*, Docket No. UG-061721, Order 06 at ¶ 17 (June 27, 2007).

¹²¹ See Hill, TR. 1025:17 – 1040:4.

1 principle that customers are only entitled to benefits from an action if they have borne the cost or
2 risks of that action.¹²²

3 54. The Joint Applicants have made numerous commitments that would hold PSE
4 customers harmless from Puget Energy, Puget Holdings and its other affiliates. Pursuant to
5 Commitment No. 9, the Joint Applicants commit to (i) maintain separate books and records;
6 (ii) agree to prohibitions against loans or pledges of utility assets to Puget Energy or Puget
7 Holdings without Commission approval; and (iii) generally hold PSE customers harmless from
8 any business and financial risk exposures associated with Puget Energy, Puget Holdings and its
9 other affiliates.¹²³ In Commitment No. 20, the Joint Applicants commit that (i) PSE will file cost
10 allocation methodologies used to allocate Puget Energy or Puget Holdings-related costs to PSE;
11 (ii) PSE will propose methods and standards for treatment of affiliate transactions; and (iii) there
12 will be no cross-subsidization by PSE customers of unregulated activities.¹²⁴

13 55. The Joint Applicants further commit that PSE's customers will be held harmless
14 from the liabilities of any non-regulated activity of PSE or Puget Holdings. In any proceeding
15 before the Commission involving rates of PSE, the fair rate of return for PSE will be determined
16 without regard to any adverse consequences that are demonstrated to be attributable to the non-
17 regulated activities. Any new non-regulated subsidiary will be established as a subsidiary of
18 either Puget Holdings or Puget Intermediate Holdings Inc., rather than as a subsidiary of PSE or

¹²² See *Wash. Utils. & Transp. Comm'n v. PacifiCorp d/b/a Pac. Power & Light Co.*, Docket No. UE-050684, Order 04 at ¶ 285 (Apr. 17, 2006).

¹²³ See Multiparty Settlement, Exh. No. 301, Appx. A, Commitment No. 9; see also *Early, et al.*, Exh. No. 302T at 22:4-11.

¹²⁴ See Multiparty Settlement, Exh. No. 301, Appx. A, Commitment No. 20; see also *Early, et al.*, Exh. No. 302T at 22:11-15.

1 Puget Energy. Measures providing for separate financial and accounting treatment will be
2 established for each non-regulated activity.¹²⁵

3 56. Puget Holdings and PSE commit to notify the Commission subsequent to Puget
4 Holdings' board approval and as soon as practicable following any public announcement of:
5 (1) any acquisition of a regulated or unregulated business representing five percent or more of
6 the capitalization of Puget Holdings; or (2) the change in effective control or acquisition of any
7 material part of PSE by any other firm, whether by merger, combination, transfer of stock or
8 assets.¹²⁶ In implementing Commitment No. 26(b)(2), the Joint Applicants will provide not less
9 than fourteen days' written notice to the Commission prior to any sale or transfer of stock
10 representing ten percent or more of the equity ownership of Puget Holdings or PSE. With
11 respect to whether Commission approval of any sale or transfer of stock is required, it is not
12 Joint Applicants' intent to change the existing law or precedent regarding change of effective
13 control triggering the need for Commission approval; provided, however, that PSE and Puget
14 Holdings will seek approval if a sale or transfer of Puget Holdings stock will give a new or
15 existing holder effective control of Puget Holdings under the then-applicable LLC Agreement.¹²⁷

16 57. If and when any subsidiary of PSE becomes a subsidiary of Puget Holdings,
17 Puget Intermediate Holdings Inc., or Puget Energy, PSE will so advise the Commission within
18 thirty (30) days and will submit to the Commission a written document setting forth PSE's
19 proposed corporate and affiliate cost allocation methodologies.¹²⁸ PSE will notify the

¹²⁵ See Multiparty Settlement, Exh. No. 301, Appx. A, Commitment No. 26(a); *see also* Early, *et al.*, Exh. No. 302T at 22:16 – 23:3.

¹²⁶ See Multiparty Settlement, Exh. No. 301, Appx. A, Commitment No. 26(b); *see also* Early, *et al.*, Exh. No. 302T at 23:6-12.

¹²⁷ See Joint Applicants' Response to Bench Request No. 19, Exh. No. 419 at 1.

¹²⁸ See Multiparty Settlement, Exh. No. 301, Appx. A, Commitment No. 28(a); *see also* Early, *et al.*, Exh. No. 302T at 23:15-19.

1 Commission of any change in corporate structure that affects PSE's corporate and affiliate cost
2 allocation methodologies. PSE will propose revisions to such cost allocation methodologies to
3 accommodate such changes.¹²⁹

4 58. Pursuant to Commitment No. 10, PSE will maintain separate debt and preferred
5 stock, if any. PSE will maintain its own corporate and debt credit rating, as well as ratings for
6 long-term debt and preferred stock.¹³⁰

7 59. A key ring fencing provision is the inclusion of an Independent Director who can
8 prevent the parent company from voluntarily bringing the utility into a bankruptcy proceeding.
9 The commitments in the Proposed Transaction provide for such an independent director at PSE.
10 Specifically, in Commitment No. 16, the Joint Applicants commit that at least one director of
11 PSE will be an Independent Director who is not a member, stockholder, director (except as such
12 Independent Director of PSE), officer, or employee of Puget Holdings or its affiliates. The
13 organizational documents for PSE will not permit PSE, without the unanimous consent of all its
14 directors, including the Independent Director, to consent to the institution of bankruptcy
15 proceedings or the inclusion of PSE in bankruptcy proceedings of its upstream affiliates.¹³¹

16 60. Another standard ring fencing provision that is contained in the Settlement
17 Stipulation is the inclusion of a non-consolidation opinion. Within ninety days of closing of the
18 Proposed Transaction, PSE and Puget Holdings will file a non-consolidation opinion with the
19 Commission which concludes, subject to customary assumptions and exceptions, that the ring

¹²⁹ See Multiparty Settlement, Exh. No. 301, Appx. A, Commitment No. 28(b); *see also* Early, *et al.*, Exh. No. 302T at 23:19 – 24:1.

¹³⁰ See Multiparty Settlement, Exh. No. 301, Appx. A, Commitment No. 10; *see also* Early, *et al.*, Exh. No. 302T at 19:5-8.

¹³¹ See Multiparty Settlement, Exh. No. 301, Appx. A, Commitment No. 16; *see also* Early, *et al.*, Exh. No. 302T at 19:9-15.

1 fencing provisions are sufficient that a bankruptcy court would not order the substantive
2 consolidation of the assets and liabilities of PSE with those of Puget Energy or its affiliates or
3 subsidiaries.¹³² If the ring fencing provisions are insufficient to obtain a non-consolidation
4 opinion, Puget Holdings and PSE commit to promptly:

- 5 (i) notify the Commission of this inability to obtain a non-
6 consolidation opinion.
- 7 (ii) propose and implement, upon Commission approval, such
8 additional ring fencing provisions around PSE as are sufficient to
9 obtain a non-consolidation opinion subject to customary
10 assumptions and exceptions.¹³³

11 **C. The Commitments Provide Additional Benefits and Assurances to PSE’s**
12 **Customers and the Community PSE Serves**

13 **1. Rate Credits of \$100 Million Benefit PSE’s Customers and the**
14 **Economy of the Puget Sound Region**

15 61. The Joint Applicants commit, in Commitment No. 34, to provide rate credits of
16 \$100 million (\$10 million per year for a 10-year period) commencing at the closing of the
17 Proposed Transaction.¹³⁴ These rate credits are far more than a “modest proposal,”¹³⁵ as
18 suggested by Public Counsel. The rate credits offered in Commitment No. 34 exceed, in both
19 quantity and duration, any rate credits previously offered in any precedent transaction before this
20 Commission involving an electric or natural gas utility. These rate credits will provide the

¹³² See Multiparty Settlement, Exh. No. 301, Appx. A, Commitment No. 8; see also Early, *et al.*, Exh. No. 302T at 19:16-21.

¹³³ See Multiparty Settlement, Exh. No. 301, Appx. A, Commitment No. 25; see also Early, *et al.*, Exh. No. 302T at 19:21 – 20:7.

¹³⁴ See Multiparty Settlement, Exh. No. 301, Appx. A, Commitment No. 34; see also Early, *et al.*, Exh. No. 302T at 27:13 – 29:3.

¹³⁵ Hill, Exh. No. 261HCT at 6:16.

1 economy of the Puget Sound region with a sizable economic stimulus over the course of the next
2 decade and demonstrate the long-term commitment of the Investor Consortium to the region.¹³⁶

3 62. Unlike virtually every other transaction approved by the Commission, the vast
4 majority—\$88 million of the \$100 million—of rate credits offered are not offsettable by any cost
5 savings, and none of the rate credits are achieved through a reduction in jobs, and instead
6 effectively equate to a stimulus to the region.¹³⁷ These credits are the result of a reduction in the
7 return on equity that PSE will be able to achieve for the decade following closing of the
8 Proposed Transaction, which in turn will help to mitigate the impact on PSE’s customers of the
9 significant investment required to upgrade PSE’s utility infrastructure over that period¹³⁸—an
10 investment that is necessary regardless of whether or not the Proposed Transaction is
11 consummated.

12 **2. The Proposed Transaction Provide Assurances that PSE Will**
13 **Continue to Have a Strong Local Presence and to Pursue its Key**
14 **Objectives**

15 63. The Proposed Transaction contains several commitments that provide assurances
16 to PSE’s customers, employees, community, and the Commission, that PSE will continue to have
17 a strong local presence and to pursue the goals it has set over the past several years. For
18 example, Commitment No. 15 states that Puget Holdings will seek to retain all current senior
19 management of PSE.¹³⁹ Puget Holdings believes PSE is a well-managed utility with a track
20 record of providing excellent electricity and natural gas service throughout the region,¹⁴⁰ and

¹³⁶ See Horton, *et al.*, Exh. No. 304CT at 18:11-15.

¹³⁷ See Leslie, TR. 467:14 – 468:2.

¹³⁸ See Horton, *et al.*, Exh. No. 304CT at 18:19 – 19:6.

¹³⁹ See Multiparty Settlement, Exh. No. 301, Appx. A, Commitment No. 15; *see also* Early, *et al.*, Exh. No. 302T at 24:13-17.

¹⁴⁰ See Leslie, Exh. No. 31T at 4:4-5.

1 Puget Holdings' efforts to retain senior management will allow PSE to continue to be a well-
2 managed utility. Additionally, the Joint Applicants have committed to maintain PSE's corporate
3 headquarters in PSE's service territory.¹⁴¹

4 64. In Commitment No. 1, Puget Holdings and PSE commit to continue the Service
5 Quality measures currently in place, or as they may be modified. Thus, the Joint Applicants will
6 support the revised service quality measures that are proposed in the settlement of PSE's
7 ongoing general rate case.¹⁴²

8 65. In addition to maintaining its existing level of corporate contributions and
9 community support in the State of Washington for a period of at least five years after closing,
10 Puget Holdings has committed to make a one-time contribution of \$5 million to the Puget Sound
11 Energy Foundation.¹⁴³

12 66. PSE has long been a supporter of energy conservation and renewable energy
13 initiatives. The Proposed Transaction contains several commitments that demonstrate that PSE
14 will continue to be a leader in this area. Specifically, Commitment Nos. 47 through 55 make
15 clear that PSE will continue to pursue its existing renewable resource acquisition schedule, seek
16 to increase penetration of the Green Power Program, continue to produce an annual greenhouse
17 gas emissions inventory report, and continue to support energy conservation measures and
18 funding, among other commitments.¹⁴⁴

¹⁴¹ See Multiparty Settlement, Exh. No. 301, Appx. A, Commitment No. 17; *see also* Early, *et al.*, Exh. No. 302T at 26:3-4.

¹⁴² See Multiparty Settlement, Exh. No. 301, Appx. A, Commitment No. 1; *see also* Early, *et al.*, Exh. No. 302T at 30:7-11.

¹⁴³ See Multiparty Settlement, Exh. No. 301, Appx. A, Commitment No. 18; *see also* Early, *et al.*, Exh. No. 302T at 26:13-22.

¹⁴⁴ See Multiparty Settlement, Exh. No. 301, Appx. A, Commitment Nos. 47 – 55; *see also* Early, *et al.*, Exh. No. 302T at 31:19 – 33:7.

1 67. The Joint Applicants recognize PSE’s history of working with low income
2 agencies to address issues of low-income customers, and the Joint Applicants have committed to
3 continue such work and to support increased budgeted funding of low-income energy efficiency
4 programs at a level commensurate with increases in funding for energy efficiency programs for
5 other residential customers.¹⁴⁵

6 68. It is important to note that the inclusion of these commitments in the Proposed
7 Transaction does not relieve PSE of obligations to demonstrate the prudence or just and
8 reasonable character of any investments, expenditures or actions undertaken to pursue the above-
9 referenced goals or any of the activities referenced in the Commitments.¹⁴⁶

10 **3. The Joint Applicants’ Commitment Regarding Access to Books and**
11 **Records Exceeds PSE’s Current Obligations to Make Such Records**
12 **Available**

13 69. Public Counsel erroneously asserts that Commitment No. 27, which addresses
14 access to the books and records of Puget Holdings and other affiliates, is a “step backward from
15 the ‘status quo.’”¹⁴⁷ In fact, Commitment No. 27 represents a “step forward” from current
16 requirements. For example, Commitment No. 27(a) requires the Joint Applicants to maintain an
17 audit trail for all corporate, affiliate or subsidiary transactions with PSE, or that result in costs
18 allocable to PSE. Commitment No. 27(b) assures that the corporate structure will not be used as
19 a basis to oppose access to books and records. Commitment No. 27(c) ensures that the Proposed
20 Transaction will not limit the Commission’s access to records under RCW 80.04.070 (general) or
21 RCW 80.16.030 (affiliated interests). Finally, Commitment No. 27(d) provides that Puget

¹⁴⁵ See Multiparty Settlement, Exh. No. 301, Appx. A, Commitment Nos. 22, 23, and 42; *see also* Early, *et al.*, Exh. No. 302T at 30:13 – 31:16.

¹⁴⁶ See Multiparty Settlement, Exh. No. 301, Appx. A, Commitment No. 33.

¹⁴⁷ Hill, Exh. No. 261HCT at 13:1; *see also id.* at 12:11 – 13:2.

1 Holdings and PSE will each agree to provide information provided by and to credit rating
2 agencies. In sum, subparts (a) through (c) of Commitment No. 27 confirm the “status quo” with
3 respect to transparency, and subpart (d) of Commitment No. 27 provides a new requirement with
4 respect to transparency.¹⁴⁸

5 **D. The Proposed Transaction Provides For Representation by Local Directors,**
6 **Transparency, and Balance Among the Members of Puget Holdings**

7 **1. The Proposed Transaction Provides For Local Representation**

8 70. The board of directors of PSE will include at least three directors who are
9 residents of the region, one of whom shall be the chief executive officer of PSE, and the boards
10 of directors of Puget Energy and Puget Holdings will include at least two directors who are
11 residents of the region, one of whom shall be the chief executive officer of PSE.¹⁴⁹ William
12 Ayer, who currently serves on the board of directors of Puget Energy, will serve as the initial
13 chairman of the board at both PSE and Puget Holdings, and Herb Simon, who currently serves
14 on the board of directors of Puget Energy and PSE, will serve as the third local director at
15 PSE.¹⁵⁰ Additionally, certain significant corporate decisions relating to the operation and
16 business strategy of Puget Holdings will require the vote of either the PSE chief executive
17 officer or the other local manager.¹⁵¹ These local directors and managers provide additional
18 assurance to the community and PSE’s customers that local concerns will be considered at both
19 the PSE and Puget Holdings board level.

¹⁴⁸ See Multiparty Settlement, Exh. No. 301, Appx. A, Commitment No. 27; Horton, *et al.*, Exh. No. 304CT at 22:4-16.

¹⁴⁹ See Multiparty Settlement, Exh. No. 301, Appx. A, Commitment No. 41; Early, *et al.*, Exh. No. 302T at 25:2-6.

¹⁵⁰ See Reynolds, Exh. No. 135 at 1-2.

¹⁵¹ See Joint Applicants’ Response to Bench Request No. 8, Exh. No. 408 at 1.

1 **2. The Proposed Transaction Provides For Transparency**

2 71. The governance of Puget Energy and PSE will remain open and transparent.

3 Although Puget Energy will no longer be a publicly traded company, the Joint Applicants have
4 agreed to comply with many of the reporting requirements and provisions of the SEC, the NYSE
5 and Sarbanes-Oxley, with which they otherwise would not be required to comply.¹⁵² For
6 example, Puget Energy/PSE will continue to comply with the disclosure requirements of Section
7 13(a) and 15(d) of the Exchange Act to the same extent it complied as a publicly traded
8 company. It will continue to file 10-K, 10-Q and 8-K reports.¹⁵³ Additionally, Puget
9 Energy/PSE will continue to maintain an internal audit function in compliance with section
10 303A.07 of NYSE Corporate Governance Standards and will continue to engage an independent
11 auditor in compliance with Section 201 of Sarbanes-Oxley.¹⁵⁴ Puget Energy/PSE will continue
12 to maintain an audit committee and a compensation committee. The directors on these
13 committees will be independent of PSE management, although not necessarily “independent”
14 directors as defined under NYSE standards.

15 **3. The Proposed Transaction Provides For Balance Among the**
16 **Members of Puget Holdings**

17 72. Additionally, Puget Holdings has a balanced structure, which brings strength and
18 diversity to the Proposed Transaction. Public Counsel focuses much attention on Macquarie
19 while disregarding the strengths and diversity that the other members of the Investor Consortium
20 bring to the Proposed Transaction. No one investor or group of affiliated investors holds a
21 controlling stake in Puget Holdings. Even if the ownership interests of all the Macquarie entities

¹⁵² See generally Markell, Exh. No. 81; Joint Applicants’ Response to Bench Request No. 22, Exh. No. 422.

¹⁵³ See Joint Applicants’ Response to Bench Request No. 22, Exh. No. 422, Att. A at 6.

¹⁵⁴ See Joint Applicants’ Response to Bench Request No. 22, Exh. No. 422, Att. A at 8.

1 in the Investor Consortium are aggregated, the sum creates a 51.5% ownership interest, less than
2 the 55% threshold required for “simple majority” rights.¹⁵⁵

3 **IV. PUBLIC COUNSEL’S ARGUMENTS OPPOSING**
4 **THE PROPOSED TRANSACTION ARE NOT**
5 **SUPPORTED BY THE EVIDENCE OR THE LAW**

6 **A. The Ring Fenced Debt at Puget Energy Does Not Create a Risk to PSE’s**
7 **Customers**

8 73. As discussed above, the significant ring fencing between PSE and Puget Energy
9 protects PSE’s customers from risk associated with the debt at Puget Energy. Nevertheless,
10 Public Counsel ignores this ring fencing and incorrectly argues that more equity at Puget Energy
11 is required to protect PSE’s customers. Neither previous Commission orders nor the facts in the
12 record support Public Counsel’s arguments, and the Commission should reject these arguments.

13 **1. Ring Fencing Protects PSE Customers from Debt at Puget Energy,**
14 **and There Is No Justification for Public Counsel’s Argument That**
15 **Additional Equity Is Needed**

16 74. The Joint Applicants have instituted state of the art ring fencing provisions
17 consistent with previous Commission orders that protect PSE’s customers from any risks that
18 might result from the debt located at Puget Energy.¹⁵⁶ Such ring fencing provisions include
19 maintenance of separate books and records, prohibitions against loans or pledges of utility assets,
20 commitment to hold PSE customers harmless from any business and financial risk exposures
21 associated with unregulated affiliates, various dividend restrictions, and prohibitions against
22 cross-subsidization by PSE customers of unregulated activities. Given the separation of PSE

¹⁵⁵ See Wiseman, Exh. No. 151T at 10:1-5; Leslie, TR. 719:14-22.¹⁵⁶ See, e.g., Multiparty Settlement, Exh. No. 301, Appx. A, Commitment Nos. 8, 9, 10, 16, 19, 20, 25, 26, 27, 28, 35, 36, 37, 38, 39, 40, 56, and 59; see also Early, *et al.*, Exh. No. 302T at 14:1 –24:1.

1 from Puget Energy through ring fencing commitments, there is no basis for Public Counsel’s
2 claim that the debt at Puget Energy creates risks for PSE customers.

3 75. At hearing, Public Counsel asserted a new argument that suggests that the
4 Proposed Transaction would be acceptable to Public Counsel if the members of Puget Holdings
5 contribute an additional \$500 million of equity to Puget Energy and reduce the debt at Puget
6 Energy by an equal amount:

7 I think the key element would be more equity, less debt. And in
8 discussing this with my counsel, trying to figure out a place where we
9 could land in all of this, I would prefer that the investor consortium start
10 off the consolidated capital structure of PE with a 40 percent equity ratio.
11 And that would mean a contribution of about \$500 million of equity and a
12 reduction of that much debt.¹⁵⁷

13 In essence, Public Counsel argues that the Proposed Transaction should be rejected because
14 Public Counsel would “prefer” that an affiliate outside the ring fence have a different capital
15 structure and not because of any demonstrable “harm” that will befall PSE.

16 76. Public Counsel’s argument violates Commission precedent adopting the
17 benefit/burden principle that customers are only entitled to benefits from an action if they have
18 borne the cost or risks of that action. In *Washington Utilities and Transportation Commission v.*
19 *PacifiCorp d/b/a Pacific Power & Light Company*,¹⁵⁸ the Commission rejected arguments that
20 “double leverage” adjustments be applied to PacifiCorp’s capital structure and cost rates to
21 reflect debt in the capital structure of its parent company. In that

¹⁵⁷ Hill, TR. 1037:4-12. It should be noted that Public Counsel’s recommended equity investment is designed to achieve a consolidated capital structure with a 40% equity ratio at Puget Energy. At or shortly after closing of the Proposed Transaction, the Joint Applicants project that the consolidated capital structure of Puget Energy will have an equity ratio of 44.3%--in excess of the 40% equity ratio that Public Counsel purports that its recommended equity investment is intended to achieve. See Early, *et al.*, Exh. No. 306 at 2.

¹⁵⁸ *Wash. Utils. & Transportation Comm’n, v. PacifiCorp d/b/a Pac. Power & Light Co.*, Docket No. UE-050684, Order 04 (Apr. 17, 2006).

1 order, the Commission states as follows with respect to the benefit/burden principle:

2 Nonetheless, after having insulated PacifiCorp and its customers from the
3 risks of leveraged financing at the parent, Staff and Public Counsel seek to
4 secure for customers the cost and tax benefits of that financing. The
5 Company’s expert witness argues this may violate the familiar principle in
6 utility law that financial benefits should follow burden of risks. We agree.

7 If the risks and costs of activities at the parent-level are born exclusively
8 by shareholders—because customers are insulated from them by the ring
9 fence—then it is fair and appropriate for the shareholders, and not the
10 customers, to receive the benefits that result from those activities.¹⁵⁹

11 In a subsequent rate PacifiCorp rate case, the Commission reiterated its support for the
12 benefit/burden principle in rejecting an argument to allocate to PacifiCorp’s customers the tax
13 value of imputed interest on debt at PacifiCorp’s parent company even though the interest costs
14 of PacifiCorp’s parent company produced the benefit:

15 The second key problem is the care taken to separate the financial
16 circumstances of PacifiCorp from the other affiliates, including MEHC,
17 through “state of the art” ring fencing approved by the Commission in the
18 acquisition proceeding. In this context, it would be very difficult to justify
19 joining the financial circumstances of MEHC and PacifiCorp by imputing
20 MEHC debt costs into PacifiCorp’s capital structure. As the Company
21 and Staff argue, this smacks of the very sort of thing we squarely rejected
22 in the Company’s most recent prior general rate proceeding when
23 presented as a “double leverage” adjustment.¹⁶⁰

24 77. In both decisions, the Commission has been clear that adequate ring fencing
25 negates the need for the Commission to join the financial circumstances of a utility and its parent
26 or affiliate entities. Yet that is precisely what Public Counsel asks the Commission to do.
27 Rather than consider the debt and equity of PSE as a ring-fenced utility, Public Counsel seeks to

¹⁵⁹ See *Wash. Utils. & Transportation Comm’n, v. PacifiCorp d/b/a Pac. Power & Light Co.*, Docket No. UE-050684, Order 04 at ¶ 285 (Apr. 17, 2006).

¹⁶⁰ *Wash. Utils. & Transp. Comm’n, v. PacifiCorp d/b/a Pac. Power & Light Co.*, Docket No. UE-061546, Order 08 at ¶ 151 (June 21, 2007).

1 consolidate the debt of Puget Energy and PSE. Public Counsel makes this argument despite the
2 fact that no party—not even Public Counsel—has argued that the ring fencing provisions are
3 inadequate.

4 78. With this ring fencing in place, and at the closing of the Proposed Transaction,
5 PSE is forecast to have a very healthy capital structure of 50 percent debt and 50 percent equity.
6 This is an improvement from PSE’s current equity level. In light of the uncontested ring fencing
7 between PSE and Puget Holdings and PSE’s improved debt to equity ratio, there is no basis for
8 consolidating the debt of Puget Energy and PSE or requiring an additional \$500 million equity to
9 be contributed to Puget Energy.

10 79. Public Counsel’s position turns the Commission’s benefit/burden principle on its
11 head. In effect, Public Counsel argues that if customers are prevented from enjoying the benefits
12 of activities outside the ring fence when they are protected from the risks, the members of Puget
13 Holdings should also be prevented from enjoying any such benefits. The Commission should
14 uphold its commitment to the benefit/burden principle, recognize the sufficiency of the extensive
15 ring fencing provisions offered in the Proposed Transaction and reject Public Counsel’s new
16 argument that would require an additional investment of \$500 million.

17 **2. Public Counsel’s Concerns Regarding Risks to PSE Customers Due to**
18 **Goodwill Impairment Are Unfounded**

19 80. In the acquisition of a business, goodwill “generally is the difference between the
20 purchase price and the value of the assets acquired.”¹⁶¹ Public Counsel suggests that the

¹⁶¹ Black’s Law Dictionary 695 (6th ed. 1990); *see also* Financial Accounting Standards Board Statement No. 141 (defining “goodwill” as the “excess of the cost of an acquired entity over the net of the amounts assigned to assets acquired and liabilities assumed).

1 commitments contained in the Proposed Transaction will not protect PSE and its customers in
 2 the event the goodwill is impaired.¹⁶² However, Puget Energy—not PSE—will book the
 3 goodwill associated with the Proposed Transaction; therefore, if there is any impairment of the
 4 goodwill, it will occur at Puget Energy—not PSE. Even if such a write-down of Puget Energy’s
 5 goodwill were to occur and result in PSE’s corporate credit rating falling below investment grade
 6 [REDACTED], Commitment No. 24
 7 would protect PSE and its customers from any cost of capital increase to PSE that resulted from
 8 a write-down related to the Proposed Transaction, and Commitment No. 40 would restrict
 9 dividends from PSE to Puget Energy. This Commitment No. 40 also bars Puget Energy from
 10 making any dividends whatsoever to the Investor Consortium, via Equico, without Commission
 11 permission, in the scenario where PSE falls below investment grade corporate credit ratings—
 12 even if PSE still meets the financial ratio in subparagraph (a) of Commitment No. 40. If PSE
 13 also fails that financial ratio, PSE pays no dividends whatsoever.¹⁶³

14 81. There are two effects from the above-described commitments. First, the
 15 commitments provide a strong incentive for the Investor Consortium to resolve any potential
 16 financial problem at Puget Energy. Second, the commitments allow each of Puget Energy’s and
 17 PSE’s financial ratios to improve during the period in which the level of dividends to the
 18 Investor Consortium is restricted. Finally, Commitment No. 36 assures the Commission that
 19 PSE will have at least a 44 percent equity ratio, except to the extent a lower equity ratio is
 20 established for ratemaking purposes by the Commission.¹⁶⁴

¹⁶² See Hill, Exh. No. 261HCT at 14:19 –15:5.

¹⁶³ See Horton, *et al.*, Exh. No. 304CT at 15:7 – 16:8.

¹⁶⁴ See Horton, *et al.*, Exh. No. 304CT at 16:9-15.

1 **B. The Insertion of Equico between Puget Intermediate and Puget Energy**
2 **Protects Puget Energy and PSE from Financing Risks of the Parent**
3 **Companies above Puget Energy**

4 82. Public Counsel’s argument that the holding system structure of Puget Holdings is
5 too complex¹⁶⁵ fails to recognize the additional ring fencing protections provided by such a
6 structure. For example, the insertion of Equico between Puget Intermediate and Puget Energy
7 provides additional ring fencing protection from financial risks of parent company above Equico.
8 As explained in Commitment No. 38, Equico will be a special purpose entity holding all the
9 common stock of Puget Energy and no debt.¹⁶⁶ The Joint Applicants offered to insert Equico
10 between Puget Intermediate and Puget Energy to satisfy a ring-fencing recommendation of
11 ICNU.¹⁶⁷ ICNU proposed that any entity owning Puget Energy stock should be capitalized with
12 100 percent equity and should not be able to issue any debt.¹⁶⁸ Because Equico will hold no
13 securities other than Puget Energy common stock and have no binding financial obligations, it is
14 expected to be “bankruptcy remote.”¹⁶⁹

15 83. The insertion of Equico between Puget Intermediate and Puget Energy further
16 protects PSE and its customers because it provides structural separation between (i) Puget
17 Energy and PSE and (ii) Puget Holdings, Puget Intermediate, or any member of the Investor
18 Consortium.¹⁷⁰ This structural separation protects Puget Energy and PSE from financing risks of
19 the parent companies above Puget Energy.¹⁷¹

¹⁶⁵ See, e.g., Hill, Exh. No. 261HCT at 11:10-12.

¹⁶⁶ See Multiparty Settlement, Exh. No. 301, Appx. A, Commitment No. 38; see also Horton, et al., Exh. No. 304CT at 11:11-12.

¹⁶⁷ See Leslie, Exh. No. 38HCT at 28:11-24.

¹⁶⁸ See Gorman, Exh. No. 221T at 25:20-23.

¹⁶⁹ See Horton, et al., Exh. No. 304CT at 11:17-18.

¹⁷⁰ See Horton, et al., Exh. No. 304CT at 12:2-5.

¹⁷¹ See Horton, et al., Exh. No. 304CT at 12:5-7.

1 84. Moreover, Public Counsel’s focus on the alleged “complexity” of the structure is
2 irrelevant given the state of the art ring fencing that protects PSE from financial risks upstream.

3 **C. The Proposed Transaction Will Improve PSE’s Balance Sheet**

4 85. As discussed above, the Proposed Transaction will improve PSE’s balance sheet.
5 The Joint Applicants have committed to (i) increase PSE’s equity to 50 percent at the close of
6 the Proposed Transaction, and (ii) maintain the PSE equity level at or above 44 percent
7 thereafter, unless a lower equity level is set for ratemaking purposes by the Commission.¹⁷²
8 Thus, Public Counsel is incorrect that the Proposed Transaction will reverse the progress made
9 on improving PSE’s balance sheet. In fact, the Proposed Transaction actually furthers the
10 improvement of PSE’s balance sheet by raising PSE’s equity ratio to a point not achieved since
11 the 1990s. Furthermore, as a result of the Proposed Transaction, the [REDACTED]

12 [REDACTED]
13 [REDACTED]
14 [REDACTED].
15 **D. Capital For Infrastructure Will Be More Available Under the Proposed**
16 **Transaction**

17 **1. The Proposed Transaction Ensures that PSE Will Have Access to**
18 **Equity Capital As Necessary to Fund Its Infrastructure Needs**

19 86. The investors in Puget Holdings have access to large pools of committed equity
20 capital. The members of Puget Holdings have stated that they would be willing to make further
21 investments in PSE if there were an opportunity to deploy capital in a value-accretive and

¹⁷² See Multiparty Settlement, Exh. No. 301, Appx. A, Commitment No. 35.

1 prudent manner.¹⁷³ Indeed, PSE is ideally suited to the desire of the investors in Puget Holdings
2 to invest additional funds in attractive infrastructure assets. These investors are pension fund
3 and endowment investors, and they are constantly seeking opportunities to invest in such stable
4 cash flow streams to match their long-dated obligations.¹⁷⁴ These characteristics, along with
5 their \$3.4 billion initial investment of capital, ensure that PSE will have access to equity capital
6 as necessary to fund its infrastructure needs.

7 **2. Credit Facilities for PSE Capital Expenditures in the Amount of**
8 **\$1.4 Billion Have Been Secured and Will Be Available to Be Drawn on**
9 **Post-Closing**

10 87. Puget Holdings has already put in place \$1.4 billion in credit facilities solely for
11 the purpose of funding PSE's capital needs—including power plants to generate electricity, new
12 substations and distribution facilities to provide power and natural gas to PSE's increasing
13 customer base. These credit facilities are available to be drawn on by PSE after the closing of
14 the Proposed Transaction.¹⁷⁵ Given the availability of these credit facilities and the investors'
15 deep pockets already demonstrated by the \$296 million equity contribution in December 2007,¹⁷⁶
16 Public Counsel's argument that there is no assurance that capital for infrastructure will be any
17 more available with the Proposed Transaction¹⁷⁷ is unfounded. Moreover, as to the affordability
18 of the capital for infrastructure under the Proposed Transaction, Commitment No. 24 provides

¹⁷³ See, e.g., McKenzie, Exh. No. 91T at 9:12-14; Webb, Exh. No. 141T at 12:5-7; Wiseman, Exh. No. 151T at 13:13-16.

¹⁷⁴ See Leslie, Exh. No. 38HCT at 8:3-15.

¹⁷⁵ See Multiparty Settlement, Exh. No. 301, Appx. A, Commitment No. 3; see also Early, *et al.*, Exh. No. 302T at 12:3-5.

¹⁷⁶ See generally Markell, Exh. No. 71T at 11:6 – 14:8.

¹⁷⁷ See, e.g., Hill, Exh. No. 261HCT at 14: 7-15

1 that PSE will not advocate for a higher cost of debt or equity capital as compared to what PSE’s
2 cost of debt or equity capital would have been absent Puget Holdings’ ownership.¹⁷⁸

3 **3. The Capital Expenditure Facilities Support PSE’s Ability to Fund**
4 **Capital Expenditures to Meet Its Public Service Obligations**

5 88. The capital expenditure credit facilities support PSE’s ability to fund capital
6 expenditures to meet its public service obligations, notwithstanding Public Counsel’s argument
7 to the contrary.¹⁷⁹ In prefiled testimony and at the hearing, Mr. Kupchak and Mr. Leslie
8 corrected Public Counsel’s misinterpretation of the terms “scheduled base”, “base”, and
9 “additional”, capital expenditures in the credit agreement and the erroneous assumption that
10 these terms could compromise PSE’s ability to meet its public service obligations. Mr. Leslie
11 and Mr. Kupchak explained that the term “scheduled base” (previously defined in the term
12 sheets as “non-discretionary”) was solely used to set coverage ratios in the credit agreement and
13 does not in any way limit PSE’s ability to fund capital expenditures to meet its public service
14 obligations.¹⁸⁰ The amount of “Scheduled Base CapEx” is a fixed amount, agreed upon with the
15 mandated lead arrangers of the credit facilities, and estimated by the engineering firm in the due
16 diligence process.¹⁸¹ There is no reclassification of these expenditures in the future; they were
17 simply a method for setting the coverage ratios in the financial covenants of the credit
18 agreement.¹⁸² Any actual deviation from future or past capital expenditures has no bearing on
19 the “Scheduled Base CapEx” numbers included in the calculations of the financial covenants,¹⁸³

¹⁷⁸ See Multiparty Settlement, Exh. No. 301, Appx. A, Commitment No. 24; see also Early, *et al.*, Exh. No. 302T at 27:9-12.

¹⁷⁹ See Hill Exh. No. 251HCT at 43:10 – 51:9.

¹⁸⁰ See Kupchak, Exh. No. 11HCT at 8:14 – 12:17; Leslie, TR. 817:7-818:2.

¹⁸¹ See Kupchak, Exh. No. 11HCT at 9:10-19.

¹⁸² See Kupchak, Exh. No. 11HCT at 9:10-19.

¹⁸³ See Kupchak, Exh. No. 11HCT at 9:10-19.

1 and the financial covenants in the credit agreement do not restrict PSE’s ability to carry out its
2 public service obligations.¹⁸⁴

3 89. Moreover, in the unlikely event Puget Energy were in lock up due to a failure to
4 meet its coverage ratios, PSE would have the ability to spend funds on capital expenditures
5 required to meet its public service obligations.¹⁸⁵ Furthermore, the cash flow impact of
6 movements in gas and electricity costs that flow through the Purchased Gas Adjustment (“PGA”)
7 and Power Cost Adjustment (“PCA”) mechanisms are intentionally *excluded* from the
8 calculation of the lock-up and financial covenants associated with the new debt financing
9 package.¹⁸⁶

10 **E. Public Counsel’s Assertion that the Proposed Transaction Is Not Necessary**
11 **Is Incorrect and Also Is Irrelevant To the Legal Standard To Be Applied by**
12 **the Commission**

13 90. As discussed above, the standard by which the Commission must measure the
14 Proposed Transaction is whether it will harm the public interest. Thus, Public Counsel’s
15 argument that the Joint Applicants have not shown a financial or operational need for this
16 acquisition is irrelevant. Assuming *arguendo* that Public Counsel’s legal standard were relevant,
17 which it is not, Public Counsel argument is flawed because in asserting that a financial need has
18 not been shown, Public Counsel fails to recognize the true “status quo” of PSE going forward on
19 a stand-alone basis.

¹⁸⁴ See Kupchak, Exh. No. 11HCT at 10:5-6.

¹⁸⁵ See Kupchak, Exh. No. 11HCT at 5:9-12.

¹⁸⁶ See Kupchak, Exh. No. 11HCT at 4:16 – 5:1; Kupchak, TR. 928:7 – 929:15. Moreover, Public Counsel fails to recognize the benefits of PSE’s hedging activities in the event of sudden escalations in power and gas prices. *See id*

1 91. Public Counsel’s repeated refrain is that “Puget’s customers would be better off
2 with the ‘status quo.’”¹⁸⁷ In evaluating the status quo, however, Public Counsel does not give
3 due consideration to how PSE will fare on a stand-alone basis over the next several years, given
4 PSE’s extensive capital expenditure needs and the increasing challenges it faces raising capital in
5 the public market.¹⁸⁸ Instead, Public Counsel focuses on PSE’s performance over the past six
6 years, when capital expenditure needs were less and considerably less capital was raised through
7 the public markets as compared to the amount of equity that will need to be raised over the next
8 five years.

9 92. In contrast to this historical status quo on which Public Counsel focuses, PSE
10 must assess its needs *going forward*. As a stand-alone company, PSE would face substantial
11 challenges financing its significant capital expenditures. PSE and its customers will benefit from
12 the Proposed Transaction because PSE will be backed by investors with combined assets under
13 management totaling nearly half-a trillion dollars and who are committed to the future success of
14 PSE.

15 93. As discussed above, to understand the challenge PSE faces going forward and
16 raising capital on a stand-alone basis, the Commission should compare (i) the equity raised by
17 PSE over the past six years, excluding the \$296 million raised from the Investor Consortium
18 through a private placement in conjunction with the Proposed Transaction, and (ii) the equity
19 PSE would have needed to raise through 2013. Under such an analysis, the \$500 million that

¹⁸⁷ Hill, Exh. No. 261HCT at 3:9-10.

¹⁸⁸ See generally Campbell, Exh. No. 1CT at 6:14 – 8:2; Markell, Exh. No. 75CT at 3:2 – 15:10; Pettit, Exh. No. 111CT at 7:1 – 19:5; *In re Puget Sound Power & Light Co. and Wash. Natural Gas Co.*, Dockets UE-951270 and UE-960195, Fourteenth Supp. Order (Feb. 5, 1997)(“The transaction should not harm customers by causing risks or rates to increase . . . compared to what could reasonably be expected to have occurred in the absence of the transaction.”)

1 PSE raised over the past six years pales in comparison to the \$1.2 billion that PSE would need to
2 raise in the public markets. Raising this additional capital would be a daunting task. As Mr.
3 Reynolds and Ms. Campbell testified, raising equity has become increasingly difficult.¹⁸⁹
4 Further, Mr. Pettit testified to the continued and exacerbating challenges Puget Energy would
5 face as a serial issuer of equity through 2013.¹⁹⁰ In contrast to this very difficult standalone
6 scenario, the investors (i) have provided \$296 million in equity through a private placement,¹⁹¹
7 (ii) have secured credit facilities in the amount of \$1.4 billion to fund PSE’s capital expenditure
8 needs,¹⁹² (iii) have committed to provide an additional \$3.1 billion at closing,¹⁹³ and (iv) are
9 capable of investing additional capital to benefit PSE and its customers.¹⁹⁴

10 **F. The Challenges in Today’s Credit Market Exist and Confront PSE Whether**
11 **PSE Is a Stand Alone Publicly Traded Company or Acquired by Puget**
12 **Holdings**

13 94. The turmoil in the public markets over the past year underscores the risks inherent
14 in relying solely on listed equity markets for raising equity capital. Public Counsel’s stated
15 position in this proceeding is that PSE’s “customers would be better off with the ‘status quo’—a
16 publicly-traded investment-grade utility”¹⁹⁵ This position is flawed. In fact, PSE, as a
17 publicly-traded utility, is far more vulnerable to the turmoil of the financial markets than it
18 would be under the ownership of Puget Holdings because PSE currently raises equity capital—
19 through Puget Energy—on the New York Stock Exchange.

¹⁸⁹ See generally Campbell, Exh. No. 1CT at 6:14 – 8:2; Markell, Exh. No. 75CT at 3:2 – 15:10.

¹⁹⁰ See generally Pettit, Exh. No. 111CT at 7:1 – 19:5.

¹⁹¹ See generally Markell, Exh. No. 71T at 11:6 – 14:8.

¹⁹² See Multiparty Settlement, Exh. No. 301, Appx. A, Commitment No. 3; see also Early, et al., Exh. No. 12:3-5.

¹⁹³ See generally Multiparty Settlement, Exh. No. 301 at ¶ 9.

¹⁹⁴ See Early, et al., Exh. No. 302T at 34:2-4.

¹⁹⁵ Hill, Exh. No. 261HCT at 3:9-10.

1 95. As a publicly-traded utility, PSE must rely on the very institutions that are
2 currently failing for lack of capital. Neither domestic nor international financial markets are
3 immune to the liquidity crisis created by problems in the U.S. real estate market and associated
4 complex financial securities. Indeed, two of the largest underwriters of investment-grade utility
5 debt in the U.S.¹⁹⁶ effectively disappeared on September 15, 2007. The separate announcements
6 that (i) Merrill Lynch & Co. was to be sold to Bank of America Corp. and (ii) Lehman Brothers
7 Holding Inc. had filed a petition for protection under Chapter 11 of the U.S. Bankruptcy Code
8 with the U.S. Bankruptcy Court for the Southern District of New York created serious and
9 negative concerns worldwide.¹⁹⁷ It should be noted that Lehman Brothers was the underwriter of
10 Puget Energy's last public offering of 15 million shares in November 2005.¹⁹⁸

11 96. The domestic and international financial market, the difficulties faced by major
12 firms in these financial markets, and the resultant consolidation in the domestic and international
13 financial services industry will likely present obstacles to PSE in obtaining capital on reasonable
14 terms absent the Proposed Transaction. Indeed, many publicly-listed utilities face increasing
15 share price volatility and uncertainty in their ability to raise equity capital in the listed markets.

16 97. The Joint Applicants do not dispute Public Counsel's assertions that these are
17 challenging times, particularly for a public-listed company facing a large capital shortfall in an

¹⁹⁶ See Joint Applicants' Response to Public Counsel Data Request No. 3202, Exh. No. 19HC at 32 (listing the largest underwriters of investment-grade utility debt in the U.S.).

¹⁹⁷ See Carrick Mollenkamp *et al.*, *Crisis on Wall Street as Lehman Totters, Merrill is Sold, AIG Seeks to Raise Cash*, The Wall Street Journal, Sept. 15, 2008, Exh. No. 500; Susanne Craig *et al.*, *AIG, Lehman Shock Hits World Markets*, The Wall Street Journal, Sept. 16, 2008, Exh. No. 501; Press Release, Lehman Brothers Holdings Inc., As Previously Announced, Lehman Brothers Holdings Inc. Filed Chapter 11; No Other U.S. Subsidiary or Affiliate, Including Its Broker-Dealer and Investment Management Subsidiaries, Was Included in the Filing (Sept. 15, 2008), Exh. No. 502; Lynn Thomasson, *U.S. Stocks Decline as Lehman Bankruptcy Deepens Market Turmoil*, Bloomberg, Sept. 15, 2008, Exh. No. 503; Matthew Karnitschnig *et al.*, *Bank of America to Buy Merrill*, The Wall Street Journal, Sept. 15, 2008, Exh. No. 504.

¹⁹⁸ See Joint Applicants' Response to Bench Request No. 2, Exh. No. 402HC at 337; Reynolds, TR. 605:7-18.

1 uncertain environment. Indeed, Mr. Markell, Ms. Campbell, and Mr. Pettit have each supplied
2 extensive testimony on the challenges PSE would face in this environment as a stand-alone
3 entity.¹⁹⁹

4 98. In contrast to the potential perils of relying solely on the public markets, the
5 Proposed Transaction would provide a new source of equity capital for PSE—deep-pocketed
6 unlisted funds of infrastructure capital. The Proposed Transaction significantly decreases the
7 potential effect of market volatility on PSE, while not preventing PSE from accessing listed
8 markets if needed. The Investor Consortium has demonstrated a track record of success in
9 securing financing even during the current financial crisis--with Macquarie alone raising
10 \$71 billion of debt financing since July 2007.²⁰⁰ Additionally, the Investor Consortium (i) has
11 already invested \$296 million of equity in PSE, (ii) has committed to invest \$3.4 billion in the
12 Proposed Transaction, and (iii) has raised \$3.6 billion of committed debt facilities to fund the
13 Proposed Transaction and PSE's ongoing capital expenditure and working capital needs for the
14 next five years. Every dollar of this capital was committed after the onset of the current credit
15 crisis, with the most recent addition being a commitment by the Investor Consortium in July
16 2008 to invest another \$200 million of equity into Puget Energy in response to concerns raised in
17 this proceeding.²⁰¹

18 99. In short, the Proposed Transaction will provide PSE with the real benefit of more
19 options in a time of crisis. The greater access to diverse global markets provided by the Investor
20 Consortium's size, scale, and relationship base are significant and important benefits of the

¹⁹⁹ See, e.g., Campbell, 1CT; Markell, Exh. No. 71T; Markell, Exh. No. 75CT; Pettit, Exh. No. 111CT.

²⁰⁰ See Horton, *et al.*, Exh. No. 304CT at 20:3-8.

²⁰¹ See Horton, *et al.*, Exh. No. 304CT at 20:9-17.

1 Proposed Transaction.

2 **G. Public Counsel’s Assertion that the Benefits and Risks of the Proposed**
3 **Transaction Weigh in Favor of Shareholders Is Incorrect and Also Is**
4 **Irrelevant To the Legal Standard to Be Applied by the Commission**

5 100. As discussed above, there is no legal basis for Public Counsel’s attempt to
6 evaluate the Proposed Transaction on the basis of weighing the benefits to customers against the
7 benefits to Puget Energy’s shareholders and PSE’s officers.²⁰² However, the benefits that PSE’s
8 customers and the Puget Sound region stand to gain from the Proposed Transaction are
9 significant. Most notable are the \$100 million of rate credits that Puget Holdings has agreed to
10 provide. The rate credits provide rate relief to PSE’s customers and also provide a significant
11 infusion of capital into the economy of the Puget Sound region.²⁰³ It is difficult to understand
12 how Public Counsel can dismiss \$100 million in rate credits as insubstantial.²⁰⁴ As discussed
13 above, these rate credits exceed, in both quantity and duration, any rate credits previously
14 offered in any precedent transaction before this Commission involving an electric or natural gas
15 utility.²⁰⁵ From the perspective of the members of the Investor Consortium, these rate credits
16 represent an effective decrease in PSE’s authorized return on equity of 24 basis points for the 10-

²⁰² The Joint Applicants have committed that the shareholders of Puget Energy will bear the costs of any costs of executive compensation triggered by the Proposed Transaction and that such costs would not be passed on to PSE customers. *See* Joint Applicants’ Response to Bench Request No. 12, Exh. No. 412. Moreover, Stephen Reynolds testified that his decision to support and approve the Proposed Transaction as a member of the Board of Puget Energy was independent from any personal benefit he would receive as part of the Proposed Transaction. *See* Reynolds, Exh. No. 133T at 15:16-20. Finally, each member of the Board of Puget Energy acted within his or her fiduciary responsibility, discharged the duties as a director in good faith with the care an ordinarily prudent person in a like position would exercise under similar circumstances, and in a manner the director reasonably believed to be in the best interests of Puget Energy. *See generally* Campbell, Exh. No. 1T at 9:1 – 10:19.

²⁰³ *See* Multiparty Settlement, Exh. No. 301, Appx. A, Commitment No. 34; *see also* Early, *et al.*, Exh. No. 302T at 27:13 – 29:3.

²⁰⁴ *See, e.g.*, Hill, Exh. No. 261HCT at 5:10-13 (describing \$100 million of rate credits as “a very small commitment on the part of the Investor Consortium . . .”).

²⁰⁵ *See* Horton, *et al.*, Exh. No. 304CT at 18:11-15.

1 year period.²⁰⁶

2 101. Public Counsel wrongly infers that these rate credits are swallowed up by rate
3 increases that Puget Holdings plans and that would otherwise not occur, but there is no evidence
4 supporting Public Counsel's assertion.²⁰⁷ Public Counsel ignores the fact that, regardless of the
5 Proposed Transaction, PSE plans to pursue a general rate case or a power cost only rate case on
6 an annual basis, at least through 2013, and that rates are expected to increase over this time
7 frame, because of its need to bring in significant new electric resources to meet PSE's growing
8 load, and to replace aging transmission and distribution infrastructure in order to continue
9 providing high quality service.²⁰⁸

10 102. Another clear benefit of the Proposed Transaction is the superior access to capital
11 the investors in Puget Holdings bring for PSE's significant capital expenditure needs. PSE can
12 move forward with its business plan and acquire the power plants, wind farms, and transmission
13 and distribution facilities it requires to provide high quality service, knowing that a source of
14 patient capital is able to fund this necessary infrastructure. This will provide comfort to PSE's
15 customers and the region that high quality service will continue, PSE will be able to provide
16 power to meet the growth of the region, and PSE can pursue renewable resources and other
17 resources as opportunities arise.

18 103. Additionally, the ring fencing structure as set forth in the Proposed Transaction
19 Stipulation provides additional protections to customers that they do not have under the current

²⁰⁶ See Leslie, Exh. No. 38HCT at 25:17-23.

²⁰⁷ See Hill, Exh. No. 261HCT at 6:3-17.

²⁰⁸ Public Counsel uses numbers and assumptions from the investors' financial model out of context to argue that customer rates will be higher with the Proposed Transaction. In so doing, Public Counsel has misinterpreted or misunderstood the meaning of these numbers and assumptions from the financial model. See, e.g., Leslie, TR. 811:2-21 (regarding rate case recovery assumptions), Kupchak, TR. 1065:14 – 1073:17 (regarding depiction of commodity and non-commodity in the financial model as related to potential rates).

1 structure where PSE is a subsidiary of the unregulated Puget Energy. For example, the dividend
2 restrictions that set limits on when dividends may be paid to PSE's parent based on financial
3 metrics and credit ratings provides a benefit that does not currently exist and thus allows PSE to
4 be a stronger utility. Also, the commitment to maintain a minimum equity level of 44%, unless a
5 lower equity level is set by the Commission for ratemaking purposes, provides a benefit that
6 does not currently exist and that can provide protections to customers in the event of turmoil in
7 the power market, as was the case in the 2001 Western Energy Crisis. Also, the higher equity
8 and lower debt level at PSE should allow PSE to access capital on more favorable terms.

9 *104.* In short, Public Counsel's pessimistic view of the Proposed Transaction is at odds
10 with the evidence in this case. The benefits to PSE's customers from the Proposed Transaction
11 are significant, and PSE's customers are protected from risk by state of the art ring fencing
12 provisions.

13 **V. CONCLUSION**

14 *105.* The Commission should approve the Proposed Transaction because the Proposed
15 Transaction does not harm the public interest, and, in fact, provides significant and substantial
16 benefits to customers and the Puget Sound region. PSE will no longer be reliant on the turbulent
17 public market to finance its significant capital expenditure needs. Instead, it will be owned by an
18 Investor Consortium with deep pockets that has committed to invest \$3.4 billion and put in place
19 \$1.4 billion of credit facilities to fund PSE's capital expenditure needs. Additionally, the
20 Proposed Transaction reduces financial risk by implementing dividend restrictions and minimum
21 equity ratio requirements that are not currently in place, and it provides substantial quantitative
22 and qualitative benefits to the customer base and the region.

