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**

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

REDACTED VERSION

OCTOBER 23, 2008

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I. INTRODUCTION

1. The Joint Applicants, Puget Holdings LLC ("Puget Holdings") and Puget Sound Energy, Inc. ("PSE"), submit this Reply Brief in response to the Opening Brief filed by the Public Counsel Section of the Washington State Attorney General's Office ("Public Counsel"). In this Reply Brief, the Joint Applicants address the following flaws in Public Counsel's Opening Brief:

- Public Counsel ignores the substantial access to capital provided by the Proposed Transaction;
- Public Counsel incorrectly asserts that the Proposed Transaction increases risks for PSE and its customers;
- Public Counsel improperly minimizes the transaction commitments; and
- Public Counsel's claims of bias are without merit.

The evidence in this proceeding refutes each of Public Counsel's arguments and proves that the Proposed Transaction creates no harm to the public interest.

2. In essence, Public Counsel assumes that any deviation from the way PSE operated in the past equates to harm; but "change" is not necessarily "harm". In judging whether "change" is "harm", the Commission must weigh the Proposed Transaction in the context of future challenges to PSE. Commission precedent suggests a forward-looking test that requires approval if the Proposed Transaction creates no harm as "*compared with what could reasonably*

be expected to have occurred in the absence of the transaction."[1] Public Counsel erroneously uses a backwards-looking test and measures the Proposed Transaction against the past, rather than measuring the Proposed Transaction against what PSE is likely to face going forward as a stand-alone company. Given the volatile stock markets, tight credit market, and PSE's significant capital expenditure needs, the landscape PSE faces going forward as a stand-alone company is quite different from what it has experienced over the past six years.

3. Public Counsel ignores evidence in the record demonstrating that the multi-billion dollar commitments of the members of Puget Holdings will provide a more secure source of capital for PSE than is currently available through the public equity and debt markets. Public Counsel also ignores substantial evidence in the record that the Proposed Transaction will benefit customers, including likely improvements in credit quality, rate credits, dedicated capital expenditure facilities, and the agreed ring fencing provisions that do not currently exist. Post-closing, PSE will have a stronger balance sheet and ring fencing provisions that will serve to insulate customers from financing activities of Puget Energy or other affiliates. Even Public Counsel has acknowledged the adequacy of this ring fencing.[2]

4. Public Counsel is the only party who opposes the Proposed Transaction. All other parties to this proceeding recognize the benefit of the Proposed Transaction and have either (i) joined in the Multiparty Settlement Stipulation and concurred that the Proposed Transaction is in the public interest, or (ii) not opposed the Multiparty Settlement Stipulation. The Commission

[1] *In re Puget Sound Power & Light Co. & Wash. Natural Gas Co.*, UE-951270 & UG-960195, Fourteenth Supp. Order at 40-41 (Feb. 5, 1997) (emphasis added).

[2] At hearing, Public Counsel witness, Mr. Hill, failed to identify a single ring-fencing provision that Public Counsel deemed inadequate when specifically requested to do so. (*See* Hill, TR. 1036:9 – 1039:24.) Indeed, Mr. Hill cited to the ring-fencing provisions approved by this Commission in prior proceedings—and adopted by the Joint Applicants in this proceeding—as "the best I had seen." (Hill, TR. 1036:20-23.)

should reject Public Counsel's claims of harm because they do not withstand scrutiny, and the Commission should approve the Proposed Transaction.

II. PUBLIC COUNSEL APPLIES THE WRONG LEGAL STANDARD

A. Public Counsel Erroneously Asserts That the Joint Applicants Must Demonstrate an Operational or Financial Justification for the Proposed Transaction

5. Public Counsel acknowledges that the standard for approving a change of control transaction is a "no harm" standard[3] but proceeds to ignore this standard in analyzing the Proposed Transaction. For example, Public Counsel states the following:

> The Joint Applicants' chief, indeed the only real, rationale offered to justify the transaction is improved access to capital. There is no claim of operational necessity or efficiency.[4]

While the Joint Applicants have demonstrated on the record that there are significant benefits from the Proposed Transaction, they are not required to demonstrate an "operational or financial justification" for the Proposed Transaction. The Commission has recognized that WAC 480-143-170 does not require a showing that customers or the public will be better off if the Commission approves the Proposed Transaction. Rather, the Commission must approve the Proposed Transaction if (i) the Joint Applicants demonstrate that there will be no harm to the public interest, and (ii) the Joint Applicants are qualified to take over ownership of PSE.[5] The Joint Applicants have satisfied this standard[6], and the Commission should approve the Proposed Transaction.

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[3] *See* Public Counsel Opening Br. at ¶¶ 3, 5.

[4] *Id*. at ¶ 9.

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

[6] *See, e.g.,* Brief of the Industrial Customers of Northwest Utilities at ¶ 17; Initial Brief of NW Energy Coalition at ¶¶ 5, 7; and Brief of Commission Staff at ¶ 13.

B. Public Counsel Improperly Focuses On Pre-Settlement Positions of Settling Parties

6. The Commission's focus should be on the end results of the Multiparty Settlement Stipulation. Throughout its brief, Public Counsel improperly cites the pre-settlement testimony of Commission Staff witnesses and erroneously argues that Commission Staff agrees with Public Counsel's opposition to the Proposed Transaction.[7] The Commission has rejected similar attempts to go beyond the terms of a settlement among parties to a pending case, noting that the Commission's "overarching concern . . . is with the end results produced under the settlement."[8] Although Commission Staff initially filed testimony opposing the transaction as originally proposed, the Joint Applicants subsequently offered several additional commitments in conjunction with their rebuttal testimony filed on July 2, 2008.[9] Further, during two weeks of settlement negotiations the Joint Applicants' agreed to several new commitments. With these additional commitments, Commission Staff was satisfied that its concerns had been adequately addressed and resolved.[10] Commission Staff and the other signatories to the Multiparty Settlement Stipulation agreed that the Proposed Transaction is consistent with the public interest and filed the Multiparty Settlement Stipulation on July 23, 2008.[11] The Multiparty Settlement Stipulation and testimony in support thereof are the "end results produced under the settlement" on which the Commission should focus.

[7] *See, e.g.,* Public Counsel Opening Br. at ¶¶ 6, 10, 14, 19, 23, 36, 44, 46, 55, 73, and 99-103.

[8] *WUTC. v. PacifiCorp, d/b/a Pac. Power & Light Co.,* Docket No. UE-032065, Order No. 6 at ¶¶ 53-54 (Oct. 27, 2004).

[9] *See* Reynolds, Exh. No. 134.

[10] *See* Early, *et al.*, Exh. No. 302 at 37:17 – 43:1.

[11] *See* Multiparty Settlement, Exh. No. 301 at ¶ 11.

III. PUBLIC COUNSEL IGNORES THE SUBSTANTIAL ACCESS TO CAPITAL PROVIDED BY THE PROPOSED TRANSACTION

7. The Joint Applicants have testified that PSE needs to fund $5.7 billion in capital expenditures through 2013, and Public Counsel does not dispute this need. Public Counsel argues, however, that the public financial markets are a more reliable and less risky source of funding for these needs as compared to the committed funding provided by the Proposed Transaction. As set forth below, Public Counsel's position does not withstand scrutiny.

A. Public Counsel's Recitation of the Turmoil in the Public Markets Highlights the Benefits of the Proposed Transaction In Terms Of Access to Capital

8. Public Counsel has documented in the record the dire state of the public equity markets and the tightening of credit markets.[12] Public Counsel fails to acknowledge, however, that these are the very same financial markets on which PSE currently relies to fund a significant portion of its capital expenditures as a stand-alone company, and which Public Counsel views to be the only reliable source to fund PSE's significant capital expenditure needs.[13]

9. The ongoing financial market turmoil highlights the benefits of the Proposed Transaction to PSE and its customers. In spite of the tightening credit markets, Puget Holdings has successfully arranged financing for the Proposed Transaction and raised over $2.15 billion to support PSE's future operations, including $1.4 billion for PSE's capital expenditure needs.[14]

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[12] *See* Exh. Nos. 195 – 200, Exh. Nos. 235 – 237, and Exh. Nos. 500 – 12.

[13] Public Counsel apparently now recognizes the challenges that PSE can expect to face if it remains dependent on public markets to fund its billions of dollars of capital expenditure needs. Public Counsel states that "[i]n the recent past, markets have been valuing the utility industry strongly and capital has been available on reasonable terms *at least up to 2007* when the transaction was announced." Public Counsel Opening Br. at ¶ 15 (emphasis added). As stated previously, the relevant period analysis of the Proposed Transaction is not the period "up to 2007 when the transaction was announced." The Commission must compare the Proposed Transaction to what "*could reasonably be expected to have occurred in the absence of the transaction*." *In re Puget Sound Power & Light Co. & Wash. Natural Gas Co.,* UE-951270 & UG-960195, Fourteenth Supp. Order at 40-41 (Feb. 5, 1997) (emphasis added).

[14] The $2.15 billion raised by Puget Holdings to support PSE's future operations consists of (i) a $1 billion capital expenditure facility at PSE's parent company, Puget Energy, Inc. ("Puget Energy"); (ii) a $400 million capital

Also, the members of Puget Holdings have already invested $296 million of equity into Puget Energy.[15] The Proposed Transaction will provide PSE with a dedicated source of funding for PSE's capital expenditure needs for the next five years. The benefit of the committed lines of credit raised by Puget Holdings is evident now more than ever.

B. Public Counsel Ignores the Evidence Regarding the Difficulties Puget Energy Faces as a Serial Issuer of Stock in the Public Market

10. Public Counsel discounts the substantial evidence regarding the challenges PSE and its parent company, Puget Energy, have faced, and will continue to face over the next five years, as a serial issuer of common stock in the public markets for equity capital.[16] Steve Reynolds, Chief Executive Officer of PSE and Chairman of the Board of PSE and Puget Energy, testified about the difficulties Puget Energy experienced with its recent equity issuance. According to Mr. Reynolds, in 2005 "we were issuing too many shares at a point in time when the market was saturated with Puget stock."[17] Mr. Reynolds further testified that it has become increasingly difficult over the past six years to sell equity on reasonable terms because the "low hanging fruit with regard to additional equity . . . is pretty well gone,"[18] and the dilution caused by these serial issuances of equity means that Puget is not viewed as an attractive party from an equity standpoint.[19]

11. Justin Pettit provided compelling evidence, at hearing and in rebuttal testimony, that Puget Energy faces external equity financing requirements that are among the largest in the

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expenditure facility at PSE; (iii) a $350 million hedging facility at PSE; and (iv) a $400 million liquidity facility for working capital at PSE. *See* Markell, Exh. No. 71T at 22:7-17; *see also* Joint Applicants' Response to Bench Request No. 024, Exh. No. 424.

[15] *See* Markell, Exh. No. 71T at 11:8 – 14:8.

[16] *See, e.g.*, Public Counsel Opening Br. at ¶ 10.

[17] Reynolds, TR. 605:7-16.

[18] *Id*. at 607:10-12.

[19] *See id.* at 607:23 – 608:3.

utility industry in relation to its equity market capitalization and daily trading volume.[20] Mr. Pettit further testified to PSE's likely difficulties in the upcoming years:

> [T]he sector is facing a major capital spending cycle over the next several years. PSE will need to compete for capital with much larger companies, all of whom are investing to meet the needs of their customers. PSE's equity story will need a more compelling vision for the use of proceeds than investors' next best choice, or PSE will face a flight of capital. Ultimately, it is the pricing, terms and timing of the equity issuance that suffers the most.[21]

12. In the face of this compelling evidence, Public Counsel argues that raising $900 million in equity over a five-year period would not present a significant challenge for Puget Energy.[22] Public Counsel, however, reaches this conclusion by manipulating data and using the data in a manner inconsistent with the industry standard.[23] For example, when equity and "equity like" issuances are included, the capital that must be raised is $1.4 billion rather than $900 million.[24] Also, Mr. Pettit rejected Public Counsel's use of fifteen years of historical data to determine the average equity issuance as a percent of market capitalization; he testified that the industry looks at very recent data, not lengthy historical data, to determine the market's ability to absorb new stock issuances. Mr. Pettit described his analysis, which goes back ten

[20] *See* Pettit, Exh. No. 111CT at 10:11 – 11:9.
[21] *Id.* at 18:12 – 19:5.
[22] *See* Public Counsel Opening Br. at ¶ 15.
[23] The Public Counsel Opening Brief is replete with improper manipulation of data and false inferences. A prime example of this is Public Counsel's claim that the Proposed Transaction is similar to Babcock & Brown's application to acquire Northwestern Corporation in Montana, and Texas Pacific Group's proposal to purchase Portland General Electric in Oregon. *See* Public Counsel Opening Br. at ¶ 8. Public Counsel makes no substantive comparison of these two cases with the Proposed Transaction. Indeed, Public Counsel admits that the Proposed Transaction includes "a lower percentage debt and a higher percentage of equity involved in this initial part of the transaction than, for example, the recent Kohlberg, Kravis, Roberts and Co. (KKR) purchase of TXU . . . ." Hill, Exh. No. 251HCT at 14:14-16.
[24] *See* Pettit, Exh. No. 111CT at 7:10-12.

years, as conservative compared to the industry practice of looking at only the most current year of data.[25]

13. Public Counsel's argument that Mr. Pettit should not have included the hybrid securities in his analysis is also without merit.[26] The testimony of Puget Energy Treasurer Donald Gaines, relied on by Public Counsel,[27] is consistent with Mr. Pettit's testimony. Both agree that these "hybrid" securities have characteristics of both debt and equity and they receive 50% equity credit from the ratings agencies.[28] Mr. Pettit makes clear that his analysis appropriately includes the equity and equity-like issuances that Puget intends to make through 2013.[29] He testified that to exclude Puget Energy's equity-like securities from the analysis would result in comparing "apples to oranges" because the comparator group likewise includes more than common equity.[30] Although Public Counsel argues there are differences between Mr. Markell's and Mr. Pettit's testimony on the inclusion of hybrids, there is actually no disagreement on this point.[31]

14. Moreover, it is misleading to characterize the amount of equity Puget Energy was able to raise in the public markets over the past six years as $800 million,[32] given that only $500 million has been raised in public offerings in the six-year period since 2002. The most

[25] *See* Pettit, TR. 656:12-24.
[26] *See id*. at 636:5 – 642:16.
[27] *See* Public Counsel Opening Br. at ¶ 37, n.69.
[28] *Compare* Pettit, TR. 637:1-23 to Gaines, Exh. No. 231 at 1-3 note (c) (noting that hybrids are included as long-term debt in the table but ratings agencies give 50% equity credit); *see also* Kupchak, Exh. No. 26 at 4-5.
[29] *See* Pettit, TR. 636:5 – 642:16.
[30] *See id*. at 639:13 – 642:13.
[31] Mr. Markell testified that in terms of Wall Street's digestibility, "anyone putting capital in a firm, whether it's preferred, common, or hybrid, considers the total cash requirements of the company and whether or not all aspects of those cash requirements can be raised timely to meet the needs of the company." Markell, TR at 674:19-23. The fact that Mr. Pettit based his analysis on market capitalization and Mr. Markell used book value of stock in his testimony demonstrates that, under either analysis, Puget Energy's equity needs over the next five years are daunting. *See id.* at TR. 677:14-21.
[32] *See* Public Counsel Opening Br. at ¶¶ 15-16, n.25.

recent $296 million in equity, raised in December 2007, was a private placement with the members of Puget Holdings.[33] Puget Energy's ability to raise equity through this private placement would have been unlikely but for the Proposed Transaction. Thus, a more accurate comparison is the $500 million in equity Puget Energy raised in the public markets prior to 2007, compared to the $1.2 billion needed to be raised from 2007 through 2013.[34]

C. Public Counsel Erroneously Suggests That Funds Will Not Be Available to PSE to Meet Its Significant Capital Expenditure Needs

1. Public Counsel Ignores the Projected Capital Expenditures of $5.95 Billion in the Puget Holdings Model

15. Public Counsel suggests that because there is no express commitment by Puget Holdings to fund $5.7 billion for capital expenditures over the next five years, the funds will not be available and PSE will not meet its capital expenditure needs.[35] Public Counsel ignores the fact that the $5.7 billion in PSE's multiyear business plan is only a high-level projection of PSE's capital expenditure needs through 2013.[36] The consolidated cash flow projections in the financial model developed independently by Puget Holdings actually demonstrate an estimated $5.95 billion of capital expenditure investments over the 2008-2013 period:[37]

Year	2008	2009	2010	2011	2012	2013	TOTAL
Total Capex (millions)	$[redacted]	$[redacted]	$[redacted]	$[redacted]	$[redacted]	$[redacted]	$5,954

Of course, the actual amount of capital expenditures over this period may be higher or lower than the $5.7 billion projected by PSE's model and the $5.95 billion projected by Puget Holdings' model.

[33] *See* Markell, Exh. No. 71T at 11:8 – 14:8.
[34] *See* Joint Applicants Opening Br. at ¶ 27.
[35] *See, e.g.,* Public Counsel Opening Br. at ¶ 2.
[36] *See* Markell, Exh. No. 76C.
[37] Leslie, Exh. No. 52HC at 6 (sum of Total Non-Discretionary CapEx and Discretionary CapEx).

16. The Joint Applicants do not have perfect knowledge of the capital expenditure amounts that will be necessary through 2013. Therefore, the Joint Applicants cannot make a firm regulatory commitment to fund $5.7 billion in capital expenditures through 2013. Had the Joint Applicants made a firm regulatory commitment to fund $5.7 billion in capital expenditures through 2013, PSE could face arguments about the prudence of such committed funds and allegations that PSE was "gold-plating" its system by firmly committing to spend billions in capital expenditures before specific capital expenditure needs are known. Instead, Puget Holdings has confirmed its intention to fund necessary capital expenditures and arranged for credit facilities of $1.4 billion[38] that, in combination with PSE's retained earnings and long-term debt issuance, will be available to fund PSE's capital expenditures projected at $5.7 billion in PSE's multi-year business plan[39] and projected at $5.95 billion in Puget Holdings' financial model.[40] Moreover, the investors in Puget Holdings testified to their ability to contribute additional equity into PSE as required.[41]

2. Public Counsel Misleadingly Suggests that the Coverage Ratio Designations Affect PSE's Ability to Meet Its Public Service Obligations

17. Public Counsel misleadingly suggests that the coverage ratio designations in the credit facilities affect PSE's ability to spend funds to meet its public service obligations.[42] As discussed in testimony and in the Joint Applicants' Opening Brief, Public Counsel continues to

[38] The credit facilities are revolving in nature; PSE can draw down as needed, repay with the proceeds of long-term debt issuance or additional equity, and draw down again. *See generally* Joint Applicants' Response to Bench Request No. 24, Exh. No. 424.

[39] *See* footnote 36, *supra.*

[40] *See* footnote 37, *supra*. Public Counsel also argues that the capital expenditure facilities might not actually be available to PSE because they are not yet drawn. *See* Public Counsel Opening Br. at ¶ 28 (noting that the $1.0 billion capital expenditure facility and $750 million accordion feature are undrawn at closing). Puget Energy and PSE will only draw down on these facilities as PSE's capital expenditure needs arise.

[41] *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.

[42] *See, e.g.,* Public Counsel Opening Br. at ¶ 31.

ascribe meanings to these terms that are not consistent with the terms of the credit agreements.[43] PSE may use the capital expenditure credit facilities to fund Utility Capital Expenditures incurred in the acquisition, renewal and replacement of Public Service Property in accordance with Good Utility Practice.[44]

D. Public Counsel Wrongly Concludes That the "Record Does Not Establish That the Transaction Will Offer Access to 'Patient' Capital"

18. Public Counsel wrongly concludes that the "record does not establish that the transaction will offer access to 'patient' capital."[45] In fact, there is extensive testimony from the members of Puget Holdings that, consistent with infrastructure investment, they intend to hold PSE as a long-term investment.[46] For the members of Puget Holdings, the focus is on the fundamentals of the business, measured over the long term.[47] Moreover, in addition to providing credit facilities of over $2.15 billion to support PSE's future operations,[48] the members of Puget Holdings have testified that they are looking for additional opportunities to invest capital in investments, such as PSE, should additional capital expenditure needs arise that are not covered by the existing financing.[49]

19. Public Counsel's assertion that Macquarie Capital Funds has "only been engaged in infrastructure investing since 1996"[50] is irrelevant. Public Counsel has not offered evidence

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[43] *See* Joint Applicants Opening Br. at ¶¶ 88-89; s*ee also* Exh. No. 424, Att. A at 17, 32, Schedule 1.01.B; Att. B at 25, 31, Schedule 1.01B

[44] *See* Exh. No. 424, Att. A at 74, 35, 16, 61-62,; Att. B at 78, 33, 4, 15, 30, 33.

[45] Public Counsel Opening Br. at ¶ 34.

[46] *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.

[47] *See* Leslie, 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.

[48] *See* footnote 14, *supra*.

[49] *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.

[50] Public Counsel Opening Br. at ¶ 34.

that any member of Puget Holdings has engaged in short-term acquisition and divestiture of infrastructure assets. In fact, the evidence shows, quite to the contrary, that very few assets have been sold.[51] Moreover, the [redacted] investor forecasts[52] and the long-term liability profile for the pension plans[53] attest to the investors' plan to hold PSE for the long term. The Proposed Transaction provides welcome relief from the public market's short-term performance demands.

20. Public Counsel confuses the evidence in the record in order to reach the erroneous conclusion that the Puget Holdings investment in PSE has a finite, ten-year term.[54] But the language on which Public Counsel relies does not apply to Puget Holdings.[55] Several members of Puget Holdings testified that they do not have a defined exit strategy or finite term for their investment in PSE, and they consider themselves long-term investors.[56]

21. Public Counsel also erroneously asserts that Puget Holdings' commitment to provide capital is limited by [redacted].[57] Again, the language Public Counsel cites does not apply to Puget Holdings' investment in PSE—or even in MIP's commitment to Puget Holdings.[58] Mr. Leslie testified that there is no

[51] Leslie, Exh. No. 031T at 11:7-17.

[52] Leslie TR. 767:4 – 768:18.

[53] *See* McKenzie, Exh. No. 091T at 5:11-15, Webb, Exh. No. 141T at 6:13 – 7:2; Webb, Exh. No. 143 at 8; Wiseman, Exh. No. 151T at 11:19 – 12:5.

[54] *See, e.g.,* Public Counsel Opening Br. at ¶ 34.

[55] Public Counsel cites to Leslie, Exh. No. 50, which is the Private Placement Memorandum for Macquarie Infrastructure Partners ("MIP"). Leslie, Exh. No. 50 and the language Public Counsel cites from that exhibit do not apply to Puget Holdings' investment in PSE, as Public Counsel alleges. Throughout this case, Public Counsel has repeatedly confused MIP with Puget Holdings and has repeatedly misread the MIP Private Placement Memorandum as defining Puget Holdings' investment in PSE. *See, e.g.,* Hill, Exh. No. 251 HCT at 13:1-3 (misstating the structure of Puget Holdings as "Macquarie is the general or lead partner and the members of the Investor Consortium are the limited partners). Moreover, it should be noted that although MIP was created as a [redacted] investment fund, there are opportunities for extension of the fund, as acknowledged by Public Counsel. *See* Leslie, Exh. No. 50 at 11.

[56] *See generally* Leslie, Exh. No. 31T at 6:16 – 7:20; 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.

[57] *See* Public Counsel Opening Br. at ¶ 33.

[58] Public Counsel references Leslie, Exh. No. 50, which is the MIP Private Placement Memorandum. Its terms apply to investments in the MIP fund, not to Puget Holdings investment in PSE. *See* Leslie, Exh. No. 50 at 10.

[redacted].[59] Public Counsel's mistaken belief that [redacted] is in no way relevant to this proceeding.

IV. PUBLIC COUNSEL INCORRECTLY ASSERTS THAT THE PROPOSED TRANSACTION INCREASES RISK FOR PSE AND ITS CUSTOMERS

A. Public Counsel Fails to Recognize That the Proposed Transaction Improves PSE's Balance Sheet

22. Public Counsel erroneously asserts that the Proposed Transaction "reverses [PSE's] corporate direction of lowering financial risk."[60] It is undisputed that the Proposed Transaction *improves* PSE's balance sheet. In that regard, PSE will continue in the direction it has established over the past six years by decreasing its debt ratio and increasing its equity ratio.

1. Public Counsel Ignores the Improvement in PSE's Equity Ratio

23. Public Counsel does not dispute that the Proposed Transaction will increase PSE's equity ratio but improperly focuses on the consolidated equity ratio of Puget Energy and PSE and ignores the effects of the commitments made as part of the Multiparty Settlement Stipulation.[61] The Joint Applicants have committed to (i) increase PSE's equity ratio to 50 percent within 60 days of the closing of the Proposed Transaction, (ii) maintain the PSE equity level at or above 44 percent thereafter, unless a lower equity level is set for ratemaking

[59] *See* Leslie, TR. 751:20-24.
[60] Public Counsel Opening Br. at ¶ 41.
[61] *See, e.g., id*. at ¶ 43.

purposes by the Commission;[62] and (iii) implement state of the art ring fencing to insulate PSE from financing activities at Puget Energy or other affiliates.[63] Public Counsel's focus on Puget Energy's increased debt is in error and deviates from Commission precedent. The Commission has previously rejected similar attempts to consolidate debt ratios of an operating company and its holding company where, as here, state of the art ring fencing provisions serve to protect customers from risks at the holding company level.[64]

2. Public Counsel Ignores the Credit Improvement and Ratings Separation Expected to be Achieved by the Proposed Transaction

24. Public Counsel falsely states that the Proposed Transaction jeopardizes PSE's "[c]urrently healthy credit ratings."[65] [redacted].[66]

25. Public Counsel's arguments that the Proposed Transaction jeopardizes PSE's credit ratings are patently false. The Proposed Transaction will likely lower the risk, as measured by credit profile, of PSE. Moreover, Public Counsel's argument that "full ratings delinking" is needed, rather than "ratings separation"[67] is not supported by any evidence in the record.

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[62] *See* Multiparty Settlement, Exh. No. 301, Appx. A, Commitment No. 35; *see also* Early, *et al.*, Exh. No. 302T at 15:3-14.

[63] *See* Multiparty Settlement, Exh. No. 301, Appx. A, Commitment Nos. 8, 9, 10, 16, 25; *see also* Early, *et al.*, Exh. No. 302T at 18:18 – 24:1.

[64] *See, e.g., WUTC v. PacifiCorp d/b/a Pac. Power & Light Co.*, Docket No. UE-050684, Order 04 at ¶ 285 (Apr. 17, 2006) (stating that "[i]f the risks and costs of activities at the parent-level are born exclusively by shareholders—because customers are insulated from them by the ring fence—then it is fair and appropriate for the shareholders, and not the customers, to receive the benefits that result from those activities.")

[65] Public Counsel Opening Br. at ¶ 2.

[66] *See* Horton, *et al.*, Exh. No. 305C at 2; *see also* Horton, *et al.*, Exh. No. 304CT at 6:6 – 7:5.

[67] *See* Public Counsel Opening Br. at ¶ 64. Public Counsel has cited to no authority that advocates for, or

3. Public Counsel Erroneously Suggests that Goodwill at Puget Energy Will Affect PSE Customers

26. Public Counsel's concern about the goodwill asset is unfounded.[68] The goodwill will be placed on the books at Puget Energy, not PSE. The ring fencing protects PSE's customers from any risk associated with possible goodwill impairment and renders Public Counsel's argument irrelevant.[69]

4. Public Counsel Confuses Dividend Projections with Promises

27. Public Counsel cites projections contained in various presentations to investors regarding the internal rate of return and PSE dividends to support the erroneous claim that the members of Puget Holdings expect excessive returns on their investment in PSE.[70] The plain language of the documents on which Public Counsel relies is clear that such numbers are not an "annual return promised by Macquarie to the investors"[71] but merely projections:

> Any financial projections have been prepared and set out for illustrative purposes only and do not in any manner constitute a forecast. They may be affected by changes in economic and other circumstances that cannot be foreseen and it must be recognized that the reliance to be placed on them is a matter of commercial judgment.[72]

The members of Puget Holdings bear the risk if these projections are not accurate. [redacted]

[redacted]

even defines, "full ratings delinking," and Public Counsel's witness Mr. Hill did not testify as to the need for further ratings separation or "full ratings delinking" when questioned by the Commission about the adequacy of the ring fencing. *See* Hill, TR. 1036:20-23.

[68] *See* Public Counsel Opening Br. at ¶¶ 44-46.

[69] Moreover, Public Counsel incorrectly calculates the incremental debt by failing to subtract the $393 million reduction in debt at PSE that results from the Proposed Transaction. *See* Public Counsel Opening Br. at ¶ 46; Markell, Exh. No. 071T at 29:19 – 30:20 (discussing post-closing debt redemptions by PSE).

[70] *See* Public Counsel Opening Br. at ¶¶ 47, 78.

[71] *Id*. at ¶ 75.

[72] Leslie, Exh. No. 49HC at 6.

[redacted].[73]

B. Public Counsel Improperly Disregards Puget Holdings' Intent to Refinance the Credit Facilities

28. Public Counsel criticizes the length of the five-year term of the credit facilities but then dismisses the intention of Puget Holdings to refinance the term loan of Puget Energy using medium-term and/or long-term financing.[74] Mr. Kupchak testified that this has always been the investors' intent and their practice in previous transactions and that Puget Holdings has already received proposals for refinancing.[75] It is simply not possible for the Joint Applicants to obtain longer-term financing until the Commission has approved the Proposed Transaction.

C. Public Counsel Wrongly Asserts that the Assets of PSE Serve as Collateral for the Proposed Transaction

29. Public Counsel erroneously suggests that the assets of PSE are the collateral for the credit facilities.[76] Puget Energy's equity interest in PSE—not the assets of PSE—serve as the collateral for the facilities.[77] Thus, even in the highly unlikely event that a default were to occur, the consortium of banks that hold the Puget Energy debt have no claim to the operating assets of PSE. At most, the consortium of banks could seek Commission approval to take over ownership of Puget Energy, pursuant to Chapter 80.12 RCW. Through such approval process,

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[73] Moreover, Public Counsel's assertion that the members of Puget Holdings will receive the equivalent of [redacted] is based on flawed logic. *See* Public Counsel Opening Br. at ¶ 47. Mr. Leslie explained the problems with Public Counsel's computation of yield during cross-examination. Puget Holdings will make considerable investments in PSE, consistent with PSE's planning processes, which will cause the productive value of the rate base to grow significantly, which likewise allows for a larger yield as compared to the status quo. *See* Leslie, TR. 774:3-22.

[74] *See* Public Counsel Opening Br. at ¶¶ 52 – 54.

[75] *See* Kupchak, TR. 553:21 – 555:7; *see also* Multiparty Settlement Stipulation, Exh. No. 301, Appx. A, Commitment No. 57; *see also* Early, *et al.*, Exh. No. 302T at 13:5-11.

[76] *See* Public Counsel Opening Br. at ¶ 56.

[77] *See* Joint Applicants' Response to Bench Request No. 024, Exh. No. 424 at 179 – 236 (Exhibit C-1 (Form of Security Agreement) and Exhibit C-2 (Form of Pledge Agreement) to Credit Agreement).

the Commission can, and likely would, require ring-fencing provisions to govern the new owners. Public Counsel's concern that the current ring-fencing provisions may not apply to a future transaction is misplaced because the Commission would set the terms for any subsequent change of control.

D. Public Counsel Wrongly Suggests That the Proposed Transaction Will Increase the Cost of Capital

30. In Commitment No. 24, the Joint Applicants committed that they would not advocate for a higher cost of debt or equity capital as compared to what PSE's cost of debt or equity capital would have been absent Puget Holdings' ownership.[78] Thus, Public Counsel's assertion that the Proposed Transaction will increase capital costs[79] is a moot point. To the extent capital costs increase as a result of the Proposed Transaction, in comparison to where such costs would be absent the Proposed Transaction, PSE's customers will be insulated from those higher capital costs.

31. In any event, the Joint Applicants disagree with Public Counsel's statement that the cost of capital will be higher as a result of the Proposed Transaction.[80] PSE's [redacted] as a result of the Proposed Transaction because of the higher equity ratio and because of the ring fencing provisions and dividend restrictions separating PSE from its parent companies.[81] Further, the Joint Applicants have committed to provide $88 million in non-offsetable rate credits, which equate to a reduction in the return on equity they will be able to achieve. [redacted], debt capital costs could decrease, and equity capital costs will be lower as a result of the rate credits.

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

[79] *See* Public Counsel Opening Br., Section V.

[80] *See id.* at ¶ 70.

[81] *See* Horton, *et al.*, Exh. No. 305C at 6-7.

E. Public Counsel Misunderstands the Purpose of the Financial Model and Misrepresents Key Assumptions

32. Public Counsel misunderstands the purpose of the financial model and overstates its importance. The assumptions in the financial model do not dictate the financial performance of PSE or cause harm to customers. The purpose of the financial model contained in Exhibit No. 52HC is to project base case financial scenarios for potential investors and lenders. As Mr. Leslie testified:

> The model is but one case, is a base case, if you like, based on all the assumptions what we expect to be a likely outcome. But we weigh that, also, against a whole variety of sensitivities in terms of risks and opportunities that are presented, giving us a range of possible outcomes. And then we make judgments as to whether the base case outcome is reasonable in the context of the whole thing.[82]

Mr. Leslie further testified that this financial model, as with similar models, contains some level of unpredictability, particularly as one moves out farther in time from the date of the investment, and that although the investors assess the assumptions for integrity and internal consistency, at the end of the day it a commercial judgment on the assumptions.[83] Public Counsel quotes disclaimer language from the financial model making clear that the model is a projection only—not a guarantee of performance.[84]

33. Moreover, the commitments made by the Joint Applicants and the fact that the Commission retains full regulatory jurisdiction over PSE will serve to protect PSE and its customers from the hypothetical allegation that someone might use the financial model as a business plan.

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[82] *See* Leslie, TR. 805:10-18.
[83] Leslie, TR. 804:12 – 805:9.
[84] *See* Public Counsel Opening Br. at ¶ 81 (quoting Leslie, Exh. No. 52HC at 2).

34. Public Counsel's assertion that the financial model assumptions are unrealistic is also wrong.[85] [redacted].[86] [redacted].[87] [redacted].[88] [redacted].[89] [redacted],[90] [redacted].

35. Furthermore, Public Counsel disregards clear testimony on the record dispelling the notion that PSE will [redacted].[91] [redacted].[92] [redacted].

36. Despite extensive testimony in the record, Public Counsel fails to understand the treatment of commodity costs in the financial model and in the debt covenants. As Mr. Kupchak testified, [redacted]

[85] *See id.* at ¶¶ 79 – 95.
[86] *See* Kupchak, TR. 889:25 – 890:12.
[87] *See* Kupchak, Exh. No. 11HCT at 19:2-8.
[88] *Compare* Leslie, TR. 810:15-19 to Markell, Exh. No. 76C at 6.
[89] *See* Kupchak, Exh. No. 11HCT at 18:16 – 19:1.
[90] Public Counsel erroneously suggests that a return on projected capital expenditure cannot exceed depreciation. *See* Public Counsel Opening Br. at ¶ 88.
[91] *See* Public Counsel Opening Br. at ¶ 86.
[92] Leslie, TR. 810:20 – 811:21.

[redacted].[93] [redacted]

[redacted].[94] PSE's hedging program further limits PSE's exposure to power cost run-ups.[95] Indeed, the Joint Applicants demonstrate that default on debt is unlikely and would require extreme situations for a number of years.[96] Such extreme and prolonged situations would cause extreme financial hardship for PSE, regardless of whether the Proposed Transaction is approved.

37. [redacted].[97] [redacted].[98] In fact, the financial model has endured extensive scrutiny from potential investors, lenders, and from KPMG, which audited the model.[99] [redacted].[100]

[93] *See* Kupchak, TR. 927:21 – 928:1.
[94] *See id.* at 928:8 – 928:15.
[95] *See id.* at 928:21 – 929:13.
[96] *See* Leslie, Exh. No. 66HC.
[97] *See* Public Counsel Opening Br. at ¶¶ 90 – 95.
[98] *See* Kupchak, TR. 1057:2-3, 1058:4-9.
[99] *See id.* at 890:9-20.
[100] *See* Kupchak, Exh. No. 23HC (demonstrating that the Puget Holdings model projected Puget Energy dividends in 2008 that were approximately $5 million less than the actual Puget Energy dividends in 2007).

F. Public Counsel's Focus on the Macquarie Model Ignores the Diverse Members of Puget Holdings

38. Public Counsel's suggestion that Macquarie's involvement in the Proposed Transaction creates additional financial risk for PSE[101] is unfounded. Despite challenges faced by certain financial institutions in the current markets, Macquarie remains profitable, well capitalized and well funded with a solid regulatory capital position. Macquarie's strong capital position is demonstrated by the fact that there have been no downgrades of Macquarie Group Ltd.'s credit ratings by Standard and Poor's or Moody's.[102] The rating agency reports distinguish Macquarie from the victims of the current credit crisis.[103] Despite the difficult markets, Macquarie continues to attract significant capital to invest.[104]

39. Additionally, Public Counsel fails to acknowledge the fact that the Proposed Transaction involves ownership by Puget Holdings, a diverse consortium of well-funded investors looking to invest their considerable capital over the long term. Public Counsel ignores the presence of, and significant investments being made in PSE by, the Canada Pension Plan Investment Board, British Columbia Investment Management Corporation and Alberta Investment Management Corporation. In the long term, PSE and its customers can expect to benefit from ownership by a consortium of experienced investors with nearly half a trillion dollars in assets under management.[105]

40. It is also important to note that Macquarie Infrastructure Partners and Macquarie-FSS Infrastructure Trust, which together own more than one third of Puget Holdings, are owned

[101] *See* Public Counsel Opening Br. at ¶ 99.
[102] *See* Exh. Nos. 513 – 516.
[103] *See, e.g.,* Exh. No. 514 (Moody's Investor Services Report, dated September 18, 2008) and Exh. No. 515 (Standard & Poor's Report, dated September 17, 2008).
[104] *See, e.g.,* Exh. No. 516.
[105] *See* Leslie, Exh. No. 38HCT at 8:3-15.

by the underlying investors in the funds, and these underlying investors are the source of capital from those funds for the Proposed Transaction.[106]

G. PSE's Governance Structure Does Not Create Risks for Customers

41. The Proposed Transaction involves the purchase of Puget Energy's publicly traded shares by the investors and the delisting of Puget Energy from the New York Stock Exchange ("NYSE"). Because Puget Energy will no longer be a publicly traded company, it will not be possible for Puget Energy to abide by every NYSE rule that applies to publicly traded companies.[107] This does not suggest, however, that a privately held company is inherently more risky than a publicly traded company, as Public Counsel posits.[108]

42. Public Counsel seems to argue that customers will be harmed because, after Puget Holdings purchases PSE, it will, as the owner of PSE, exercise some level of control over PSE by appointing its representatives to serve on PSE's board of directors.[109] Public Counsel ignores the fundamental premise of corporate ownership that the owners elect or appoint directors or managers of the corporate entity (or other business organization). It is an undisputed fact that, today, Puget Energy is controlled by a board of directors elected by its current owners, and that Puget Energy elects the PSE board.

43. However, notwithstanding their right under laws applicable to business organizations to appoint whomever they please to manage their investment, the members of Puget Holdings have committed to a board structure that includes some independent directors/managers, and a governance structure that requires the vote of an independent

[106] *See* Leslie, TR. 465:5-13.
[107] *See* Joint Applicants' Response to Bench Request No. 22, Exh. No. 422.
[108] *See* Public Counsel Opening Br. at ¶¶ 113 – 124.
[109] *See id.* at ¶¶ 114 – 118.

director/manager for decisions on the business plan and other supermajority issues.[110] Additionally, the Joint Applicants have agreed to abide by many of the NYSE,[111] SEC,[112] and Sarbanes-Oxley requirements,[113] even though as a privately held company they are no longer required to meet these requirements. Moreover, the Commission will continue to regulate PSE, which will be subject to the Commission's audit powers and the Commission's review of executive compensation, among other things.[114] In short, the Company's operations will continue to be transparent and closely scrutinized.

44. Public Counsel argues that the Proposed Transaction creates risks because there will be fewer "local" directors than under the current status quo.[115] However, currently there is no obligation for directors to be "local," and the Commission has no jurisdiction to determine who sits on the board of PSE or Puget Energy. Although there currently are "local" directors on the Puget Energy board, there is no guarantee this will always be true in the future. Further, there are differing views as to whether it is preferable to use directors with local connections or directors with specific recognized areas of expertise.[116] The bottom line is that there will continue to be local directors on the boards of PSE and Puget Energy.

45. Public Counsel's argument for local control also ignores the fact that Puget Energy equity is currently listed on a stock exchange in New York, and is owned by investors around the world. Under the status quo, Puget Energy is not locally owned.

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[110] *See* Joint Applicants' Response to Bench Request 8, Exh. No. 408; Multiparty Settlement, Exh. No. 310, Appx. A, Commitment No. 41.

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

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

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

[114] *See* RCW 80.04.080.

[115] *See* Public Counsel Opening Br. at ¶ 119.

[116] *See* Reynolds, TR. 598:1 – 599:6.

H. Public Counsel Erroneously Suggests That the Proposed Transaction Harms Customers by Impairing the Commission's Ability to Regulate PSE

46. Public Counsel erroneously suggests that the Proposed Transaction impairs the Commission's ability to regulate PSE.[117] Contrary to such suggestion, PSE will continue to be a public service company subject to Title 80 RCW. Many of the commitments that Public Counsel dissects and criticizes are the same or substantially the same as commitments in prior transactions that Public Counsel endorsed, including Commitment Nos. 26(b) and 27(b).[118] These two commitments, as well as Commitment No. 28(c), affirm the Joint Applicants' understanding that the Commission will continue to have the same jurisdiction over PSE as a public service company that the Commission exercises today.

47. Public Counsel argues that the Commission should have access to all books and records of, and assert control over, Puget Holdings, even beyond matters that relate to PSE.[119] No legal basis justifies the Commission's exercise of such control over an entity that is not a public service company. The Commission does not currently have such authority over Puget Energy, nor does it exercise such authority over the parent companies of other regulated utilities in Washington, such as Berkshire Hathaway.

48. Moreover, the investors have testified at hearing that they will make themselves available to the Commission in Washington.[120] As noted by Mr. Wiseman, it would be folly to do otherwise.[121] The Commission has authority to penalize PSE and Puget Holdings under

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[117] *See* Public Counsel Opening Br. at ¶¶ 125 – 142.

[118] *See In re MDU Res. Group, Inc. & Cascade Natural Gas Corp.*, Docket No. UG-061721, Order 06, Settlement Stipulation, Commitment Nos. 3 & 8 (June 27, 2007); *In re MidAmerican Energy Holdings Co. & PacifiCorp, d/b/a Pac. Power & Light Co.*, Docket No. UE-051090, Order 07, Appx., Commitment Nos. 3, 4, and 12 (Feb. 22, 2006).

[119] *See* Public Counsel Opening Br. at ¶ 131.

[120] *See* Wiseman, TR. 569:3-18.

[121] *See id.*

Chap. 80.04 RCW, in addition to its general authority to regulate PSE and set its rates. A failure by the members of Puget Holdings to appear in Washington to respond to Commission questions about PSE could result in penalties and would likely adversely affect their investment in PSE.

V. PUBLIC COUNSEL IMPROPERLY MINIMIZES THE TRANSACTION COMMITMENTS

A. Public Counsel Improperly Dismisses the $200 Million Equity Infusion

49. Public Counsel minimizes the significance of the additional $200 million in equity that Puget Holdings agreed to invest in Puget Energy during the settlement negotiations.[122] This additional equity infusion demonstrates the ability of the members of Puget Holdings to raise equity in a very compressed timeframe, even in difficult financial times. The additional $200 million equity commitment significantly increases the amount at risk for the members of Puget Holdings to $3.4 billion and provides added assurances that they will not walk away from this investment (and the significant funds they have invested) during difficult times.

50. More to the point, Public Counsel's demand that the Commission require an additional infusion of $500 million equity at Puget Energy (above the ring-fenced utility)[123] is inconsistent with Commission precedent. The Commission has consistently declined to impute the debt of a parent to its subsidiary utility's capital structure when the financial circumstances of the utility are separated from the parent through state of the art ring fencing.[124] There is no basis for the Commission to require an additional equity infusion at Puget Energy.

[122] *See* Public Counsel Opening Br. at ¶ 59.
[123] *See id.*
[124] *See* footnote 64, *supra*.

B. Public Counsel Admits that the Proposed Dividend Restrictions Provide Positive Benefits to Customers But Erroneously Dismisses Them as "Limited"

51. Public Counsel admits that the dividend restrictions in Commitment No. 40 provide positive benefits to customers.[125] Although Public Counsel characterizes these positive benefits as "limited," they are, in fact, substantial. Commitment No. 40 provides assurance that PSE will retain cash, and not pay dividends, if certain financial metrics are not met. Most importantly, the dividend restrictions in Commitment No. 40 (and in Commitment Nos. 36 and 37) create protections that do not exist under the status quo. Currently there is no mechanism in place that prescribes when dividends can be paid or how much of a dividend can be paid.

C. Public Counsel Criticizes a Non-Consolidation Opinion Commitment that Public Counsel has Supported in Two Precedent Transactions

52. Public Counsel criticizes Commitment Nos. 8 and 25 that require the Joint Applicants to obtain a non-consolidation opinion within 90 days of closing.[126] This commitment is substantially the same as the commitments included in the PacifiCorp and Cascade Natural Gas mergers, which Public Counsel endorsed.[127] When given the opportunity to critique the ring fencing provisions at hearing, Public Counsel witness Mr. Hill offered no criticism or suggestion for alternative language.[128]

53. Public Counsel now seems to argue that these commitments do not offer absolute protection from bankruptcy, but PSE does not currently have similar guarantees that it will not

[125] *See* Public Counsel Opening Br. at ¶ 62.

[126] *See* Public Counsel Opening Br. at ¶¶ 67 – 69.

[127] *See In re MDU Res. Group, Inc. & Cascade Natural Gas Corp.*, Docket No. UG-061721, Order 06, Settlement Stipulation, Commitment No. 30 (June 27, 2007); *In re MidAmerican Energy Holdings Co. & PacifiCorp, d/b/a Pac. Power & Light Co.*, Docket No. UE-051090, Order 07, Appx., Commitment No. Wa 8 (Feb. 22, 2006). In the Settlement Stipulations (to which Public Counsel was a party) in each of those proceedings, the Settlement Stipulations allowed the applicants three months from the closing of the transaction to obtain non-consolidation opinions, and if they were unsuccessful in obtaining such opinions, they must notify the Commission and propose additional ring-fencing provisions.

[128] *See* Hill, TR. 1036:9 – 1039:24 (describing the Commission's ring-fencing as "the best I had seen.").

be drawn into a Puget Energy bankruptcy. Although there currently is no debt at Puget Energy, there is nothing prohibiting the placement of debt at Puget Energy in the future. Commitment Nos. 8 and 25 are consistent with Commission precedent and require the Joint Applicants to provide assurance to the Commission that there is sufficient separation between PSE and Puget Energy so that a bankruptcy court would not order substantive consolidation of the two entities, should Puget Energy file for bankruptcy.[129] The Commission should reject Public Counsel's belated and unsubstantiated critique of these commitments.

D. Public Counsel Ignores the Significance of Other Commitments

54. Public Counsel ignores the significance of several other commitments made by the Joint Applicants. Commitment No. 35 sets forth an alternative means by which equity can be infused into PSE, in the unlikely scenario where Puget Energy or Puget Holdings are in financial distress.[130] This was an important feature for Commission Staff in the settlement discussions and it provides extra "belt and suspenders" protections to ensure back-up sources of equity are available to PSE from sources other than Puget Energy or Puget Holdings.[131]

55. Public Counsel also ignores the significant benefit provided by the Joint Applicants' commitments to maintain a 44% equity level (unless a lower ratio is used to set rates).[132] As discussed significantly in the record and in the Joint Applicants' Opening Brief, this is a commitment that did not exist previously, and that could have benefited PSE's customers during the Western Energy Crisis.[133] Public Counsel discounts this commitment and improperly focuses on the consolidated equity ratio at Puget Energy.

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[129] *See* Multiparty Settlement Stipulation, Exh. No. 301, Appx. A, Commitment Nos. 8 and 25.
[130] *See id.* at Commitment No. 35.
[131] *See* Early, *et al.*, Exh. No. 302T at 38:11-19.
[132] *See* Public Counsel Opening Br. at ¶ 65.
[133] *See* Joint Applicants Opening Br. at ¶¶ 46 – 48; *see also* Horton, *et al.*, Exh. No. 304CT at 13:1 – 14:13.

56. Public Counsel's also ignores the significant community benefits provided by the Proposed Transaction. Public Counsel casually dismisses the $100 million provided by the Proposed Transaction.[134] Such a casual disregard of a commitment to provide $100 million in rate credits is difficult to understand. These credits are significantly larger than credits included in other merger transactions approved by the Commission.[135] Finally, Public Counsel also ignores the commitments to (i) increase funding for low income customers;[136] (ii) support PSE's existing PSE energy conservation and renewable energy initiatives;[137] and (iii) contribute $5 million to the Puget Sound Energy Foundation, which, among other things, provides benefits and services to the economically disadvantaged in PSE's service territory.[138]

VI. PUBLIC COUNSEL'S CLAIMS OF BIAS ARE WITHOUT MERIT

57. Public Counsel incorrectly states that the Proposed Transaction is not consistent with the public interest and claims that the Commission should disregard the testimony of PSE senior management and Macquarie witnesses because of bias.[139] There are several problems with Public Counsel's argument. First, the Puget Energy board put specific safeguards in place to avoid conflicts of interest on the part of senior management when evaluating the Proposed Transaction.[140] Second, the non-Macquarie members of Puget Holdings view the fees Macquarie receives as reasonable and consistent with fees charged in the industry.[141] These

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[134] *See* Public Counsel Opening Br. at ¶ 145.

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

[136] *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.

[137] *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.

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

[139] *See* Public Counsel Opening Br. at ¶ 144.

[140] *See, e.g.,* Campbell, Exh. No. 1CT at 4:10 – 6:13.

[141] *See, e.g.,* McKenzie, Exh. No. 91T at 11:1-14.

disinterested investors, who do not benefit from the Macquarie fees cited by Public Counsel, have testified to their long-term commitment to PSE and the benefits the Proposed Transaction provides to PSE's customers.[142] Most importantly, Public Counsel ignores the nearly unanimous support for the Proposed Transaction; each of the eight parties that signed the Multiparty Settlement Stipulation agreed that the Proposed Transaction is consistent with the public interest.[143]

VII. CONCLUSION

58. The members of Puget Holdings have demonstrated a long-term commitment to PSE and its customers. They have already contributed nearly $300 million in equity to PSE, and have arranged $1.4 billion in committed credit for future capital expenditures.

59. Puget Holdings' commitment to PSE goes beyond financial support. Puget Holdings has recognized and embraced the other important facets of PSE's business model that make PSE a valued community citizen and leader, as is evidenced by the 63 commitments offered in the Multiparty Settlement Stipulation. Puget Holdings has worked closely with other stakeholders in this process and has earned the support of almost all parties to this proceeding. Only Public Counsel fails to recognize the benefits of the Proposed Transaction. The supporting parties have divergent interests and goals, yet they have acknowledged that the Proposed Transaction is in the public interest, and they have supported the Multiparty Settlement Stipulation. This support results from the Joint Applicants' continued commitment to PSE's core goals including low-income assistance, energy conservation, and responsiveness to the PSE's commercial and industrial customers and its customers and service territory in general.

[142] *See id.*
[143] *See* Multiparty Settlement Stipulation, Exh. No. 301 at ¶ 11.

60. For these reasons, the Joint Applicants respectfully request that the Commission approve the Proposed Transaction.

DATED this 23rd day of October, 2008.

Respectfully submitted

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