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 U-072375**

REPLY BRIEF ON BEHALF OF COMMISSION STAFF

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ROBERT M. MCKENNA
Attorney General

DONALD T. TROTTER
Assistant Attorney General
Office of the Attorney General
Utilities & Transportation Division

1400 S Evergreen Park Drive SW
P.O. Box 40128
Olympia, WA 98504-0128
(360) 664-1189

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I. INTRODUCTION[1]

1 On October 8, 2008, the Commission issued a notice requesting the parties to provide a more direct response to the specific arguments made by each opposing party. Because Public Counsel is the only party opposing Staff's position, Staff will reply exclusively to the arguments in Public Counsel's opening brief.

II. SUMMARY

2 In Staff's opening brief, we demonstrated in detail how the Multiparty Settlement Stipulation[2] (Stipulation) satisfies the Commission's "no harm" standard. Consistent with the Commission's approach to transactions involving the sale or transfer of control of a regulated utility, Staff identified additional risk to the utility, Puget Sound Energy (PSE), because of, among other things, increased leverage at the parent, Puget Energy (PE). Then, Staff demonstrated how each ring fencing provision contained in the Stipulation protects PSE and its ratepayers from such additional risk.[3]

3 Indeed, by far, the most important issue in this case is the effectiveness of the comprehensive ring fencing provisions contained in the Stipulation. Unfortunately, the arguments advanced by Public Counsel go mostly toward identifying the potential risks caused by the transaction at the holding company level, with very little discussion about the ring fencing provisions that are designed to protect PSE, which is, after all, the public service company the Commission has jurisdiction to regulate.

4 To take a simple example, Public Counsel correctly asserts that the Stipulation does not change the new owners' general reliance on credit markets to finance the transaction and PSE's

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[1] Throughout this brief, when we cite a numbered "Commitment," we are referring to the corresponding Commitment contained in Exh. No. 301: the Multiparty Settlement Stipulation, Appendix A: "Transaction Commitments." We do not separately cite that exhibit each time we cite a Commitment.
[2] Exh. No. 301.
[3] Staff Opening Brief at 11-28, ¶¶ 30-78.

new capital needs.[4] Though Public Counsel fails to note that the Commitments do not have that purpose, the real issue under the Commission's "no harm" standard is whether such reliance creates risk, and if so, whether the ratepayers are protected from the potential harm related to that risk. As we explained in Staff's opening brief, the comprehensive ring fencing provisions contained in the Stipulation protect ratepayers in this case.[5] By contrast, Public Counsel largely ignored that issue, both at hearing and in its opening brief.[6]

5 Indeed, Staff agrees there are risks associated with this transaction.[7] Though Public Counsel overstates the evidence on the risk issue, again, the critical issue under the Commission's "no harm" standard is whether the Stipulation's ring fencing provisions protect against those risks. They do, as Staff confirms in this reply.

6 A review of Public Counsel's opening brief also reveals that Public Counsel is proposing a new "threshold" requirement, *i.e.*, that the Joint Applicants[8] must prove the need for the transaction. However, this is not part of the Commission's "no harm" standard. Consequently, Staff's reply brief will carefully analyze Public Counsel's arguments and consistently test those arguments against the applicable standard only.

7 To summarize this case, we offer three basic reasons why the Commission should approve the transaction:

8 **1. The transaction will not affect the Commission's ability to regulate PSE under applicable statutes.** The transaction does not change PSE's status: PSE will remain a regulated electric and natural gas utility subject to the same Commission orders and public

[4] Public Counsel Opening Brief at 47, ¶ 103.
[5] Staff Opening Brief at 11-28, ¶¶ 30-79.
[6] *Id.* at 35-39, ¶¶ 97-106.
[7] *Id.* at 11-12, ¶¶ 31-32 and Elgin, Exh. No. 161HCT, Schmidt, Exh. No. 191T, and Horton, Exh. 181HCT.
[8] The Joint Applicants are PSE and Puget Holdings, LLC (Puget Holdings). *Joint Application for an Order Authorizing Transaction (December 17, 2007) (Joint Application), at 1 ¶ 1.*

service laws. The transaction does not change either PSE's existing statutory obligations or the Commission's existing authority to regulate PSE as a public service company. The Commitments amply confirm this.[9] In addition, the Commitments provide substantial benefits not available under the status quo,[10] even though the Commission does not require such benefits under its "no harm" standard.[11]

9 **2. The Commission will continue to determine PSE's cost of capital for ratemaking purposes based on the risks inherent in the operation of a regulated utility company.** After the transaction is approved, the Commission will continue to determine the cost of equity for PSE based on utility-related risk only, by using the same comparable company method the Commission uses today.[12] The Commitments solidify the validity of this approach.[13] For the cost of debt, the Commission will continue to use PSE's actual cost of debt, or, if PSE's actual cost of debt is higher due to transaction-related risk, the Commission can impute a lower cost.[14] As Public Counsel agreed, the Commission has "the ability to prevent that [higher] capital cost from reaching ratepayers."[15]

10 **3. If the risks at the holding company level, such as the risks related to increased financial leverage, cause costs to increase for the new owners, the ring fencing Commitments in the Stipulation will protect PSE and its ratepayers from harm.** The new owners commit to hold PSE harmless from the financial risks of PE and Puget Holdings, and the comprehensive ring fencing provisions are adequate and enforceable to protect PSE, should PE's

[9] Staff Opening Brief at 28-33, ¶¶ 79-90 and the Commitments discussed therein.
[10] *Id.* at 25, ¶¶ 71-75.
[11] According to the Commission, under the "no harm" standard, applicants are not required "to show that customers, or the public generally, will be made better off if the transaction is approved and goes forward." *In re Application of PacifiCorp and ScottishPower PLC,* Docket UE-981627, Third Supplemental Order at 2 (April 2, 1999).
[12] Panel Testimony, TR. 477:7 - 478:7 (Markell) and TR. 479:10 - 481:3 (Elgin).
[13] Staff Opening Brief at 23-24, ¶¶ 65-67 and the Commitments discussed therein.
[14] *Id.*
[15] Hill, TR. 1028:24 - 1029:1.

increased financial risk materialize, or should the new owners run into financial difficulties for some other, unforeseen reason.[16]

III. REPLY TO PUBLIC COUNSEL

A. Public Counsel Correctly States the Legal Standard, But Incorrectly Adds a New "Threshold" Requirement and Relies on Inapposite Precedent.

Reply to Public Counsel Opening Brief Part II, Pages 2-4, ¶¶ 4-8

11 Staff agrees with Public Counsel that the Commission applies the "no harm" standard to transactions such as these.[17] However, Public Counsel urges the Commission to apply a new "threshold" requirement, *i.e.,* that the Joint Applicants must prove that the transaction is "needed."[18] According to Public Counsel, if the Commission finds that PSE can issue the necessary capital on its own, there is no reason for the transaction to move forward.[19]

12 Notably, Public Counsel cites no precedent for this new requirement, and like Public Counsel, Staff could find no precedent, either. Indeed, as the Commission has stated, under the "no harm" standard, the question is whether the transaction "[harms] customers by causing risks or rates to increase … compared to what could reasonably be expected to have occurred in the absence of the transaction."[20] There is nothing in this standard, express or implied, that justifies the new "threshold" requirement Public Counsel now seeks to apply.

13 Without analysis, Public Counsel also urges the Commission to follow the lead of the commissions in the states of Montana and Oregon, on the basis that (according to Public Counsel), that they rejected "similar" transactions in recent years.[21] In fact, those transactions are not similar to the transaction in this case.

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[16] Staff Opening Brief at 12-28, ¶¶ 33-78, and Commitments discussed therein.
[17] Public Counsel Opening Brief at 2, ¶ 5.
[18] *Id.* at 1, ¶ 2.
[19] *Id.* at 5, ¶ 11.
[20] *In re Puget Sound Power & Light Co. and Wash. Natural Gas Co.,* Dockets UE-951270 and UE-960195, Fourteenth Supplemental Order (February 5, 1997) at 19.
[21] Public Counsel Opening Brief at 4, ¶ 8.

14 For example, in the Montana case,[22] the buyer's plan was for the utility to book the $700 million acquisition premium, which then meant the utility had to "take on debt" to balance its now unbalanced capital structure.[23] Coupled with a very aggressive dividend policy, the utility's equity ratio would decline, and negatively affect the utility's bond rating, increase its borrowing costs and result in harm to ratepayers.[24] On rebuttal, the utility finally came forward with an equity ratio commitment and a loose form of dividend restriction, but it was too little, too late.[25]

15 Obviously, the Montana sale bears no resemblance to the instant transaction. First, PSE will not recognize the acquisition premium on its books. Rather, PE will recognize the acquisition premium on its books, as goodwill.[26] Moreover, the Stipulation's comprehensive ring fencing protects PSE and its ratepayers from the associated risk.[27] Indeed, the substantial restrictions on dividends, equity ratio commitments, and hold harmless provisions, *etc.*, provide far more ratepayer protections than the Montana transaction.[28]

16 The Oregon case[29] is even more dissimilar. In that case, the buyer had no experience in the utility industry,[30] plus a definite plan to resell the utility in the near future.[31] These facts led the Oregon commission to believe it was probable that the utility would make "poor spending and investment decisions" in the interim,[32] thereby harming ratepayers. In addition, the Oregon commission was concerned that the debt used to fund the transaction could adversely affect the

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[22] *In re Joint Application of NorthWestern Corp. and Babcock & Brown Infrastructure Ltd.*, 259 PUR4th 493 (Montana PSC 2007).
[23] *Id.* at 524 (Order ¶ 152).
[24] *Id.* at 525 (Order ¶ 156).
[25] *Id.* at 527-28 (Order ¶¶ 167-179). *E.g.*, "The Joint Applicants chose to submit an application that was short on substance and long on promises." *Id.* at 529 *(Order ¶ 179).*
[26] Exh. No. 74 at 2, last column, line 6 (Markell), as explained in Elgin, Exh. No. 161HCT at 15:1-11.
[27] Staff Opening Brief at 21-25, ¶¶ 59-69.
[28] *Id.* at 11-28, ¶¶ 30-78.
[29] *In re Oregon Elec. Utility Co. LLC*, 240 PUR4th 141 (Oregon PUC 2005).
[30] *Id.* at 165.
[31] *Id.* at 161-62.
[32] *Id.* at 162.

utility's credit rating, even thought the commission recognized that effect "may be small."[33] In any event, the facts in that case indicated that ratepayers would be harmed, and insufficient protections were offered to protect ratepayers from such harm.

17 By contrast, the more extensive ring fencing commitments in the Stipulation are likely to improve PSE's credit quality,[34] and otherwise protect PSE and its ratepayers from the risks of new ownership. Furthermore, the buyers in this case are long-term investors with prior experience in owning utilities, and who have no plans to sell their investment at some later time.[35] Indeed, in Commitment 2, the new owners expressly acknowledge that they understand PSE's extensive need for new equity capital, and they commit to make that a high priority. PSE's new owners have also expressed firm confidence in the current course of PSE's business, as informed by PSE's own business plan.[36] They have no plans to depart from that course.[37]

18 In sum, the Montana and Oregon cases are quite dissimilar to the PSE transaction. It would be folly for the Commission to accept Public Counsel's undefended assertion that these cases are "similar," and therefore, justify a denial of the Joint Application.

B. Public Counsel Misstates the Evidence on Access to Capital.
Reply to Public Counsel Opening Brief Part III - Pages 4-18, ¶¶ 9-39

19 As we noted above,[38] Public Counsel mistakenly applies a "threshold" requirement, *i.e.*, the Joint Applicants must prove a need for this transaction before the Commission can approve it. In doing so, Public Counsel misstates the facts on "PSE's access to capital, so we reply.

20 **PSE's access to capital under the status quo/"regulatory compact."** Public Counsel opines that PSE has always secured capital on "reasonable terms," which leads Public Counsel to

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[33] *In re Oregon Elec. Utility Co. LLC, supra,* 240 PUR 4th at 158.
[34] Exh. No. 305C.
[35] Staff Opening Brief at 8-11, ¶¶ 23-29.
[36] *E.g.,* Leslie, Exh. No. 31T at 4:4 – 5:14, and 22:8 – 23:12.
[37] *E.g.,* Leslie, Exh. No. 31T at 23:1-12: "No other changes are planned."
[38] See discussion at page 4, ¶¶ 11-12, *supra.*

predict that PSE will continue to do so, even if the Commission does not approve the transaction.[39] After all, as Public Counsel points out, PSE now has an investment grade credit rating, and Staff testified that a basic premise of regulation is for the Commission to provide rates to enable PSE to raise capital on reasonable terms.[40]

21 Of course, Public Counsel is referring here to the "regulatory compact," but that compact was never meant to be a guarantee, as Public Counsel implies. This lack of guarantee is apparent from the existence of time periods when utility stocks have consistently sold below book value,[41] thus causing dilution when the utility had to sell new shares under such conditions. Indeed, Staff would expect Public Counsel to advocate *against* any interpretation of the "regulatory compact" that would guarantee that a publicly-traded utility's equities must sell at or above book value.

22 Moreover, it is important to recognize that the "regulatory compact," including the notion that a regulated utility should be able to raise sufficient new equity on "reasonable terms," applies equally under the proposed ownership scenario as under the status quo. The point is that regulation must fairly treat the owners of PSE, whoever they are, which includes providing the utility the opportunity to earn a fair return and attract capital in order to satisfy its public service obligations.[42] It is precisely this "regulatory compact" and fair treatment by the Commission that was a major factor in the new owner's decision to purchase PE in the first place.[43]

23 **PSE's past problems raising equity capital.** Public Counsel goes on to say it "defies common sense" that PSE would have trouble raising equity capital.[44] In truth, it is Public Counsel that avoids common sense, first by brushing aside the fact that PE's last equity issuer

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[39] Public Counsel Opening Brief at 5-9, ¶¶ 12-17.
[40] *Id.* at 11, ¶ 23, quoting Elgin, Exh. No. 161 at 26:21 – 27:2.
[41] Markell, Exh. No. 78.
[42] *Fed. Power Comm'n v. Hope Natural Gas Co.*, 320 U.S. 592, 605, 64 S. Ct. 281, 88 L. Ed. 333 (1944): rates should "enable the company to operate successfully, to attract capital, and to compensate its investors for the risks assumed ..."
[43] *E.g.*, Leslie, Exh. 31T at 19:2-4.
[44] Public Counsel Opening Brief at 10, ¶ 22.

(Lehman Brothers) suffered significantly in issuing $310 million in new PSE shares in 2005, and then by assuming, without basis in fact or common sense, that the market would react only positively over the next five years, when PSE attempts to sell almost twice as much equity as it sold in the last five years.[45]

24 Indeed, Mr. Reynolds testified that in the 2005 sale of new PE stock to the public, Lehman Brothers had significant problems because too many shares were being sold.[46] Public Counsel wants to ignore those problems because they were shifted to Lehman Brothers,[47] but the next issuer certainly will not accept that; a point Public Counsel completely avoids.

25 Furthermore, given the recent events in the capital markets, it is unclear what the future may hold for PE as a publicly-traded company. However, Commitments 2 and 3 make it crystal clear that if the Commission approves the transaction, then during PSE's upcoming five-year peak in its capital spending program, PSE will have in place the necessary financing to fund all of its external equity capital requirements.

26 **PSE as an "attractive investment."** Public Counsel attempts to solidify its quickly eroding position by noting that PSE is an "attractive investment."[48] Of course, that is obvious, given the fact that PSE has attracted a buyer. However, Public Counsel fails to consider another obvious fact here: As a result of the Western Energy Crisis of 2001, PSE was not an attractive investment at all, and required a long-term "equity building" program, at a significant cost to investors and ratepayers alike.[49] For some reason, Public Counsel does not recognize that under the Commitments, the Joint Applicants will maintain a 44 percent minimum equity ratio at PSE,

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[45] In the next five years, absent the transaction, PSE would meet about $900 million of its external capital needs through new issues of common stock to the public, compared to the last five years, when PSE issued about $500 million in common stock to the public. This latter figure does not include the $300 million private equity placement in late 2007 with the Investor Consortium. *Panel Testimony, TR. 557:12-15 (Markell); Reynolds, TR. 619:8 - 620:1.*
[46] Reynolds, TR. 605:7 - 606:1.
[47] Public Counsel Opening Brief at 8, ¶ 16.
[48] *Id.* at 10, ¶ 22.
[49] See Staff Opening Brief at 26-27, ¶¶ 74-75.

thus protecting PSE and its ratepayers, should another such event threaten PSE's equity ratio due to insufficient earnings.

27 **Commitments to provide for PSE's capital needs.** Public Counsel even questions the new owners' commitment to provide for PSE's capital needs.[50] According to Public Counsel, Commitment 2 "merely states" that "Puget's" capital needs will be the board's high priority.[51] In fact, in Commitment 2,[52] the new owners also expressly acknowledge PSE's capital needs. Moreover, in Commitment 3, they commit to provide credit facilities now that are sufficient to fund 100% of PSE's external equity capital needs for the next five years, and in Commitment 4, they commit to provide all the capital PSE needs to comply with Washington's Renewable Portfolio Standard, which impacts PSE's resource acquisitions through 2020, and beyond.[53]

28 In other words, Public Counsel's cannot succeed in its persistent attempts to unfairly minimize the Commitments and the solid protections they provide PSE and its ratepayers.

29 **Discretionary/Non-discretionary analysis.** Public Counsel is equally persistent in its attempts to gain some traction with its already discredited[54] "discretionary/non-discretionary" analysis.[55] Staff looked into this issue, but when all the facts were in, there was nothing to pursue. Public Counsel also suggests the new owners do not provide "patient" capital, but even if this were true, Public Counsel fails to identify any concrete ratepayer harm from this. In any

[50] Public Counsel Opening Brief at 13-14, ¶¶ 28-33.
[51] *Id.* at 13, ¶ 28.
[52] Commitment 2 is patterned off a commitment in the Avista reorganization, which Public Counsel endorsed. The Commission favorably observed that the Stipulation in that case required that "the capital requirements of Avista will be met by AVA and such capital requirements will be given a high priority by the board of directors of AVA and Avista." *In re Application of Avista Corp.*, Docket U-060273, Order 03 (February 28, 2007) at 4, ¶ 12 (quoting Commitment 18 in that Stipulation). Public Counsel signed the Stipulation in that docket.
[53] For example, under RCW 19.285.040(2)(a)(iii), PSE must use "eligible renewable resources or acquire equivalent renewable energy credits, or a combination of both, to meet the following annual targets: … (iii) At least fifteen percent of its load by January 1, 2020, and each year thereafter."
[54] Kupchak, Exh. No. 11HCT at 8:14 – 10:18.
[55] Public Counsel Opening Brief at 14, ¶ 31.

event, the facts show that the Macquarie-led infrastructure investors are indeed committed, long-term investors.[56]

30 When all is said and done, no one knows the terms and conditions under which PSE would be able to issue new common equity in the future, absent the transaction. However, we do know that if the Commission approves the transaction, the Investor Consortium will have credit lines in place to satisfy PSE's external equity capital needs for the next several years. That is worth something. Nonetheless, we end where we started: The Commission's "no harm" standard simply does not require the Joint Applicants to satisfy Public Counsel's newly-proposed "threshold" requirement that PSE must have better access to capital under the transaction, compared to the status quo.

C. The Transaction Adds Risk, But the Ring Fencing Protects PSE and its Ratepayers From That Risk.

Reply to Public Counsel Opening Brief Part IV – Pages 18-33, ¶¶ 40-69

31 As we observed at the outset, the Commission's most critical task in this case is to identify any new risk associated with the transaction, and then evaluate whether the ring fencing and other commitments protect PSE and its ratepayers from the harm that may arise due to that risk. Public Counsel expends significant effort identifying risk, but fails to consistently and clearly identify who bears the risk: The new owners, or PSE and its customers.[57] Indeed, Public Counsel spends very little time discussing the risks specific to PSE and its customers, and only

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[56] Leslie, Exh. No. 38HCT at 6:7-7:32 and at TR. 748-18-21; Mr. Webb for bcIMC, Exh. No. 141 at 10:1 – 11:15; Mr. Wiseman for CPP, Exh. No. 151 at 11:17 – 12:16 and Mr. McKenzie for AIMCo, Exh. No. 91 at 8:6 – 9:1.

[57] In responding to Public Counsel's arguments, we are hampered by Public Counsel's ubiquitous use of the term "Puget," and its inconsistent definition of that term. In its testimony, Public Counsel defined "Puget" in the plural form: "both the parent [PE] and the subsidiary [PSE]." *Hill, Exh. 251THC at 8:21 – 9:2.* In its opening brief, Public Counsel defines "Puget" in the singular form: "the acquired company," which is literally PE, not PSE. *Public Counsel Opening Brief at 1, footnote 1; Joint Application at 11-12, ¶¶ 22-23.* In other words, Public Counsel defines "Puget" one way in its testimony, and another way in its opening brief. Public Counsel qualified both of its definitions of "Puget" with the disclaimer "unless the context requires otherwise," which leaves to the Commission and the other parties the task of trying to discern what "Puget" may mean, in light of each particular context. This is not helpful. Indeed, Public Counsel's blurring of the distinction between PSE and other entities by its ubiquitous use of the ambiguous word "Puget" handicaps the Commission and the parties. We have tried our best to respond.

considers a few of the many ring fencing provisions in this transaction. The result: Public Counsel's analysis must fail.

1. Public Counsel Overstates the Risk Presented by the Transaction.
Reply to Public Counsel Opening Brief Part IVA & B, Pages 18-27, ¶¶ 40-57

32 Staff testified that the transaction presents various risks, primarily the risk associated with additional leverage at PE, the goodwill to be recorded on PE's books, as well as refinancing risk and Macquarie's "reputational risk."[58] To the extent Public Counsel identifies these risks in its opening brief, Staff takes no particular exception. The issue is whether the Commitments protect PSE and ratepayers from these risks of PE, which they do.

33 **Proposed dividends.** However, Staff takes particular exception to Public Counsel's claim that "proposed dividends" to the new owners create a risk that will harm PSE and its ratepayers.[59] In fact, Commitments 35, 36, 37 and 40 protect ratepayers by controlling the distributions from PSE to PE and others in the ownership chain.[60]

34 **Refinancing risk.** Staff also takes exception to Public Counsel's argument that ratepayers are harmed due to refinancing risk, based on the five-year term note that is being used in part to fund the transaction.[61] Public Counsel says Commitment 57 "does nothing to remove the need to refinance" in five years, and cites Staff witness Mr. Horton's testimony to argue that the Stipulation does not adequately address refinancing risk.[62]

35 Public Counsel's arguments are misplaced. First, Public Counsel fails to emphasize that the refinancing risk related to the initial term note relates to a note to be issued by PE, not PSE. Therefore, this is not a risk directly borne by PSE or its ratepayers. Second, Public Counsel's

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[58] *E.g.*, Horton, Exh. No. 181HCT at 7:1-16:4.
[59] Public Counsel Opening Brief at 21-24, ¶¶ 47-51.
[60] Staff Opening Brief at 21-28, ¶¶ 58-78.
[61] Public Counsel Opening Brief at 24-26, ¶¶ 52-55.
[62] *Id.* at 25-26, ¶¶ 55.

analysis implicitly (and wrongly) assumes that under the status quo, PSE is insulated from refinancing risk. In fact, under the status quo, when PSE's securities are refinanced, PE and PSE are exposed to the dynamics of the capital markets, just as the new owners will be when they refinance PE securities to fulfill PSE's equity needs.

36 However, the most significant and fatal flaw in Public Counsel's argument is its exclusive use of Commitment 57 to evaluate the Stipulation on the issue of refinancing risk. While that Commitment is important (because it assures the new owners will undertake the same sort of plan to reduce refinance risk that PE would undertake absent the transaction), it is but a small part of the extensive ring fencing that protect for ratepayers from risk at the PE level and above. Indeed, by choosing to focus solely on Commitment 57 here, Public Counsel neglects several other ring fencing measures that protect PSE from risk at PE, including refinancing risk, such as Commitments 8, 9(iii), 24, 25, 26, 35, 36, 37 and 40.[63]

37 Finally, Public Counsel mischaracterizes Mr. Horton's testimony.[64] In fact, Mr. Horton testified specifically that overall, the Commitments isolate PSE from the risks of PE and other companies in the ownership chain; he did not "carve out" refinancing risk as an exception.[65] Moreover, Commitment 57 responds to Mr. Horton's specific concern that the new owners might *not* be planning to refinance the term loan with longer term securities.[66]

38 **Collateral.** The rest of Public Counsel's risk analysis is also wanting, such as Public Counsel's attempt to ascribe "risk" to the transaction because PE's lenders are using as collateral PE's equity interest in PSE.[67] Public Counsel thinks this means the lenders will own PSE's

[63] See Staff Opening Brief at 21-28, ¶¶ 58-78.
[64] Public Counsel Opening Brief at 25-26, ¶ 55.
[65] Joint Rebuttal Testimony, Exh. No. 304CT at 23:20 – 24:1 (Horton separate statement).
[66] Horton, Exh. No. 181HTC at 19:1-7; Joint Testimony, Exh. No. 302 at 13:5-11.
[67] This fact is "public" because Public Counsel's witness mentioned it on the public record at TR. 1033:19-22.

"assets" upon a default by PE,[68] but that is wrong as a matter of law. It is an elementary legal rule that holders of an equity interest in a company have no priority claim to the assets of that company; that is why stockholders are dead last in the line of claimants to a bankrupt's assets.[69]

39 More importantly, Public Counsel is wrong on the facts, because the ring fencing provisions define and govern PE's interest in PSE's equity, and this protects PSE and its ratepayers.[70] Public Counsel avoids mentioning these critical points. Of course, the mere prospect that lenders could, under whatever circumstances, acquire an interest in PSE's equity provides the new owners an overwhelming economic incentive to resolve the problem before that would ever happen, but Public Counsel fails to mention that, as well.

40 **Dr. Schmidt's analysis.** Public Counsel also wrongly suggests that the Stipulation fails to address the risks identified by Staff witness Dr. Schmidt, on the basis that Staff somehow precluded Dr. Schmidt from testifying on that issue.[71] In fact, all three of Staff's witnesses testified at the outset (and consistent with their expertise) that Dr. Schmidt's role was to identify the overall risks, and Mr. Horton's role was to analyze those risks *vis a vis* the proposed transaction.[72] Public Counsel's failure to recognize that Staff's experts maintained these roles throughout the case provides no basis for Public Counsel to discredit them now.

41 In any event, Mr. Horton, who has extensive experience analyzing mergers and similar transactions,[73] provided direct testimony that he evaluated the risks in the context of the Stipulation and concluded that "PSE's risk profile *after* consummation of the Proposed

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[68] Public Counsel Opening Brief at 26-27, ¶ 56.
[69] "Not many doctrines have passed more fully into the collective consciousness of the legal and commercial communities than the absolute priority rule, which states this prohibition: In bankruptcy, stockholders seeking to recover their investments cannot be paid before provable creditor claims have been satisfied in full." *In re Cartridge Television, Inc.*, 535 F.3d 1388, 1391 (2nd Cir. 1976)(law review quotation cite omitted).
[70] Staff Opening Brief at 38, ¶ 104 and at 21-25, ¶¶ 59-69.
[71] Public Counsel Opening Brief at 45-47, ¶¶ 99-102.
[72] Elgin, Exh. No. 161 HCT at 6:8-14; Horton, Exh. No. 181-HCT at 2:17-20; Schmidt, Exh. No. 191T at 3:4-9.
[73] Horton, Exh. No. 182 (resume); see also Staff Opening Brief at 17, ¶¶ 45-46.

Transaction is no greater than the 'status quo.'"[74] Mr. Horton's judgment is not challenged by Public Counsel's election not to cross-examine him.[75]

2. Public Counsel Provides an Inaccurate and Incomplete Ring Fencing Analysis.
Reply to Public Counsel Opening Brief Part IVC, Pages 27-33, ¶¶ 58-69

42 In its opening brief, Public Counsel devotes virtually all of its 71 pages to a discussion of risk at the PE level and above, while providing the Commission just a scant few pages discussing the ring fencing provisions contained in the Stipulation. For example, in the section Public Counsel devotes specifically to ring fencing (Part IVC), the Commission will find only 11 paragraphs (out of 153 total) devoted to a specific discussion of alleged inadequacies of the Stipulation's ring fencing provisions.[76] And, in those few paragraphs, Public Counsel mentions only six ring fencing provisions: Commitments 8, 16, 25, 35, 36[77] and 39. In this way, Public Counsel simply ignores the many other ring fencing protections that protect PSE and it customers from the risks at PE. Among the ring fencing provisions Public Counsel ignores in that section of its opening brief are:

Commitments 9:	PSE will hold customers harmless from the business and financial risks of PE and Puget Holdings, and other affiliates
Commitment 10:	PSE will maintain separate debt and preferred stock, and separate credit ratings
Commitment 20:	No cross-subsidization by PSE customers of unregulated activities
Commitment 21:	No recovery of fees and costs associated with consummating the transaction

[74] Joint Rebuttal Testimony, Exh. No. 304CT at 23:20 - 24:1 (Horton separate statement) (emphasis added).
[75] TR. 982:13-16.
[76] Public Counsel Opening Brief at 27-33, ¶ 58 and ¶¶ 60-69 (we do not count ¶ 59, because it discusses the additional $200 million equity infusion in Commitment 59, which is not a ring fencing measure).
[77] Public Counsel refers to the 44% minimum equity ratio requirement in "Commitment 36." *Public Counsel Opening Brief at 31, ¶ 65.* It is more accurate to say that this requirement is contained in Commitment 35, and it is reinforced by Commitment 36, so we treat the reference to Commitment 36 as a reference to Commitments 35 & 36.

Commitment 24:	PSE's rate of return will not reflect adverse consequences of unregulated activities; PSE will not advocate for a higher cost of debt or equity than the cost assuming the transaction had not occurred
Commitment 37:	PE will not make a distribution unless it has a 2.00 to 1.00 ratio of consolidated EBITDA to consolidated interest expense for the four prior quarters
Commitment 38:	"Equico" is created to provide further protection from business and financing risks of the parent companies above PE[78]
Commitment 40:	PSE will retain earnings under the prescribed conditions to assure its financial ratios do not deteriorate

43 It is true that Public Counsel later provides a few comments on Commitment 40, and appears to make reference to Commitments 21 and 38 (though Public Counsel neglects to identify Commitments 21 and 38 by their number).[79] However, we located no reference at all in Public Counsel's opening brief to ring fencing Commitments 8, 10, 20, 24, or 37.

44 The Commission should not allow Public Counsel's strategy to succeed, because ignoring the Stipulation's solid ring fencing commitments does not mean they do not exist. However, ignoring such ring fencing commitments serves one purpose: It proves Public Counsel's analysis is unbalanced and incomplete. But, even for the ring fencing provisions Public Counsel chose to address, Public Counsel's analysis falls short:

45 **Commitment 35 - 44 percent minimum equity ratio.** Public Counsel attempts to dismiss the significant ratepayer protections provided by this minimum equity ratio Commitment, by saying it has "little value," because PE will issue debt to fund that equity

[78] Joint Rebuttal Testimony, Exh. No. 304CT at 11:8 - 12:7.
[79] See Public Counsel Opening Brief at 33, ¶ 69 (reference to "Equico," which is the subject of Commitment 38), at 29, ¶ 61 (reference to Commitment 40), and at 67, ¶¶ 143-144 (reference to transaction costs and executive compensation payments, which are the subject of Commitment 21).

need.[80] In fact, Commitment 35 provides significant value to ratepayers because the Commission regulates PSE and sets rates based on PSE's own capital structure, and this Commitment assures that the new owners will capitalize PSE appropriately. It also protects PSE by keeping PSE credit ratings separate from PE,[81] and it protects PSE and its customers from going through the difficulties inherent in another multi-year "equity rebuilding" program, like the recent one Public Counsel says cost ratepayers dearly.[82]

46 **Ring Fencing Should Enhance PSE's Credit Quality.** Public Counsel also tries to devalue the anticipated benefits to PSE's credit quality occasioned by the Stipulation's ring fencing provisions, on the basis that there is no "guarantee" PSE's credit quality will improve.[83] Public Counsel contends that "as long as the ratings of the parent negatively affect the ratings of PSE, there is harm."[84]

47 In reply, we first note that Public Counsel's argument lacks credibility, because Public Counsel argues the credit quality issue differently, depending on how it fits Public Counsel's particular position at the time. For example, Public Counsel argues that the transaction "will push" PE's bond rating below investment grade, even though such a downgrade has not occurred.[85] Yet, when the evidence shows that the Stipulation will likely improve PSE's credit quality, Public Counsel is quick to claim this result is not "guaranteed."[86] In other words, if it appears that an unfavorable rating action is possible due to the transaction, Public Counsel treats it as a *fait accompli*, but when a favorable rating action is likely, due to the Stipulation, Public

[80] Public Counsel Opening Brief at 31-32, ¶¶ 65-66.
[81] Exh. No. 305C, as explained in the Joint Rebuttal Testimony, Exh. No. 304CT at 5:6 – 7:5.
[82] Staff Opening Brief at 26-27, ¶¶ 74-75, and Hill. Exh. No. 251HCT at 9:8-18.
[83] Public Counsel Opening Brief at 30-31, ¶¶ 64-65.
[84] *Id.* at 31, ¶ 64.
[85] *Id.* at 33, ¶ 71.
[86] *Id.* at 31, ¶ 64.

Counsel stresses the uncertainty of that result. We submit that Public Counsel is not offering the Commission either balanced or complete analysis on this issue.

48 In any event, we refer the Commission to Exhibit 305C. The benefits identified in that exhibit are substantial.[87] There is no showing that these benefits are anything but realistic, despite the lack of a formal "guarantee." Moreover, there will be no harm to ratepayers if PE's credit rating is downgraded, because Commitments 9(iii), 24 and 26 assure that the ratings of the parent will have no adverse effect on PSE's cost of capital.

49 **Commitment 40 - Dividend Restrictions.** Public Counsel also says that Commitment 40's dividend restrictions provide only "limited positive benefits,"[88] but Public Counsel supports this gross understatement by incorrectly alleging that if PSE's credit rating is downgraded, PSE will be able to rebuild its equity ratio by only two percent annually, and in the meantime, PSE will incur higher capital costs due to the downgrade.[89]

50 In fact, the Stipulation creates several layers of protections for PSE. Commitment 35 assures PSE's equity ratio will not need rebuilding because it will be at least 44 percent. And, should PSE's credit be downgraded for reasons attributable to the risks of new ownership, Commitments 9(iii), 24 and 26 assure that ratepayers will not pay any higher rates due to such a rating downgrade.[90] Finally, Commitment 40 assures that in such a ratings downgrade situation, PSE must have an EBITDA to interest expense ratio of at least 3:1, or PSE retains 100 percent of its earnings (*i.e.*, PSE eliminates its dividend).

51 These ring fence protections provide ample protection for ratepayers in a financial crisis. For proof, the Commission needs to look no further than the Energy Crisis of 2001, the result of

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[87] See Joint Rebuttal Testimony, Exh. No. 304CT at 5:6 – 7:5.
[88] Public Counsel Opening Brief at 29, ¶ 62.
[89] *Id.* at 29, ¶ 61.
[90] Staff Opening Brief at 23-24, ¶¶ 66-67.

which led PSE to a long-term program to rebuild its equity back up to 44 percent. Public Counsel recognizes that PSE reduced its dividend at that time,[91] but that was insufficient to maintain its capitalization ratios. The comprehensive protections in the Stipulation are designed to ensure that an equity ratio rebuilding scenario will not happen in the future; a point that Public Counsel consistently fails to address.

52 **Commitment 35 - Puget Holdings can sell equity to protect PSE.** Public Counsel strays even further from the facts by suggesting that Commitment 35's assurance that Puget Holdings will be able to sell equity to the public provides no benefit at all, because nothing requires Puget Holdings to issue equity.[92] This is incorrect, for as Staff explained in its opening brief, Puget Holdings is a signatory to the Stipulation and therefore, the minimum equity ratio commitment in Commitment 35 is enforceable against Puget Holdings. If necessary to assure compliance, this can include requiring Puget Holdings to issue equity.[93]

53 **Commitments 8 and 25 - Non-Consolidation Opinion.** Public Counsel even attacks the requirement in Commitments 8 and 25 that PSE and Puget Holdings file a non-consolidation opinion, on the basis that "Puget" might be unwilling to establish new conditions if it is unable to get a non-consolidation opinion on the first try.[94] This is very surprising, considering that Public Counsel has fully embraced this commitment in at least three prior Commission-approved transactions.[95] Given that Public Counsel fails to refer the Commission to any problems with

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[91] Hill, Exh. No. 261HCT at 9, footnote 3.
[92] Public Counsel Opening Brief at 29-30, ¶¶ 62-63.
[93] Staff Opening Brief at 22-23, ¶¶ 61-63.
[94] Public Counsel Opening Brief at 32-33, ¶¶ 67-68.
[95] *In re Application of MidAmerican Holdings Co. & PacifiCorp, d/b/a Pacific Power & Light Co.,* Docket UE-051090, Order 07 (February 22, 2006), Appendix, Stipulation Appendix A at 16, Commitment "Wa 8;" *In re Application of MDU Resources Group, Inc. & Cascade Natural Gas Corp.,* Docket UG-061721, Order 06 (June 27, 2007), Stipulation, Appendix A at 11, Commitment 30; and *In re Application of Avista Corp.,* Docket U-060273, Order 03 (February 28, 2007), Appendix A, Settlement Stipulation at 7, Commitment 35.

implementing such a commitment, the Commission should reject Public Counsel's current attempt to create a problem where none exists.

54 **Commitment 16 - The "Golden Share."** Public Counsel's hyperbole is showcased again when it attempts to minimize the Commitment 16 "golden share" provisions that protect against PSE's inclusion in bankruptcy proceedings. Public Counsel simply speculates that the independent director will not be independent.[96] In any event, if there is a bankruptcy, the bankruptcy court will decide whether consolidation is allowed, and ratepayers will be protected in that regard by the non-consolidation requirements of Commitments 8 and 25.

55 **Commitment 59 - $200 million equity infusion.** Though Commitment 59 is not a ring fencing measure, Public Counsel is still wrong to minimize its impact.[97] For example, Commitment 59 provides undeniable evidence that the Investor Consortium has the ability to draw on significant finances when necessary. Moreover, Exhibit 503C (which considers the $200 million equity infusion) confirms that Public Counsel's concern about adverse credit quality effects is unwarranted. Finally, even though the $200 million reduces PE's level of debt, the ring fencing will protect ratepayers from the leverage at PE, in any event.[98]

56 **Commitment 38 - Equico.** Public Counsel observes that the creation of Equico by Commitment 38 does not prevent PSE from going bankrupt.[99] However, Equico was not created for that purpose; it was created to protect companies under Equico from the bankruptcy of entities above Puget Energy.[100] Public Counsel has yet to acknowledge this benefit.

57 **Commitment 21 - Transaction costs, including executive payments.** Though Public Counsel acknowledges that the Stipulation prevents ratepayers from paying for transaction costs,

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[96] Public Counsel Opening Brief at 33, ¶ 69.
[97] *Id.* at 28, ¶ 59.
[98] Staff Opening Brief at 12, ¶ 33 to 28, ¶ 78.
[99] Public Counsel Opening Brief at 33, ¶ 69.
[100] Joint Rebuttal Testimony, Exh. No. 304CT at 12:5-7.

Public Counsel says these costs create a "bias" in their beneficiaries, and also add to the debt of PE.[101] However, as we have discussed, the ring fencing protects PSE from the debt at PE. Moreover, if there is any bias, it is neutralized by the corroborating, independent expert analysis of other parties supporting the Stipulation, such as the expert witnesses for Staff and ICNU.

58 In sum, on the critical issue of ring fencing, Public Counsel's opening brief mirrors its case at hearing: Public Counsel either does not address, or attempts to diminish, the significant value of the many ring fencing protections in this transaction. The Commission should reject Public Counsel's opposition for that reason.

D. Public Counsel Says the Transaction Will Increase Capital Costs, But Ignores the Ring Fencing Protections that Will Protect Ratepayers, Should that Occur.

Reply to Public Counsel Opening Brief Part V, Pages 33-36, ¶¶ 70-78

59 Public Counsel boldly asserts that capital costs "will be higher" post-transaction.[102] However, once again, Public Counsel fails to acknowledge that the ring fencing protects ratepayers from that condition, should it materialize. Indeed, Public Counsel's sworn testimony trumps its advocacy here, because as Mr. Hill told the Commission under oath: "*You have the ability to prevent that [higher] capital cost from reaching ratepayers...*"[103]

60 **Cost of debt.** Turning to the details, Public Counsel says PE's cost of debt will increase,[104] but the record citations Public Counsel relies on do not appear sufficient to support this assertion. In any event, Commitments 9(iii), 24 and 26(a) protect PSE and its ratepayers from this impact,[105] should it occur.

61 These same Commitments protect PSE from any increase in capital costs due to PSE's transaction-induced need to refinance $375 million of debt and to replace certain credit facilities,

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[101] Public Counsel Opening Brief at 66-67, ¶¶ 143-144.
[102] *Id.* at 33 (section title).
[103] Hill, TR. 1028:24 - 1029:1 (emphasis added).
[104] Public Counsel Opening Brief at 33, ¶ 71, citing Exh. No. 19 at 8, Exh. No. 51 at 19, and TR. 791:5 – 795:5.
[105] Staff Opening Brief at 23-24, ¶¶ 66-67.

events which Public Counsel describes.[106] It is revealing to note that Staff's direct testimony discussed these very same events, and recommended that the Commission can either address them in the normal course of ratemaking, or order now that these are transaction costs unrecoverable under Commitment 24.[107] In rebuttal, PSE agreed with these recommendations.[108] In its opening brief, however, Public Counsel selectively chose to cite only the Staff testimony identifying these financing events, but not the corresponding Staff testimony explaining how ratepayers are protected from harm.[109]

62 **Cost of equity.** Public Counsel goes on to argue at length that "the cost of equity will be higher" if the Commission approves the transaction.[110] However, Public Counsel neglects to provide the analysis the Commission needs: *i.e.,* precisely *whose* cost of equity will be higher, and does the Stipulation protect ratepayers from such harm? Indeed, analysis of the Stipulation shows ratepayers are protected.

63 If Public Counsel is referring to PSE, PSE's cost of equity will not be higher due to the transaction, because the Commission can continue to use the same comparable company approach as it uses in ratemaking today to determine PSE's cost of equity, which would include only utilities of comparable risk to PSE as a regulated utility. This approach excludes the risks of new ownership from the determination of PSE's cost of equity. Commitments 9(iii), 24 and 26(a) confirm this method and this result.[111]

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[106] Public Counsel Opening Brief at 34, ¶¶ 72-73.
[107] Elgin, Exh. No. HCT at 37:17-39:8.
[108] Elgin, Exh. No. 161 at 38:1 – 39:8 (In this testimony, Staff referred to "Commitment 25," which was later renumbered Commitment 24); Markell, Exh. No. 75CT at 17:15 – 18:8.
[109] Public Counsel Opening Brief at 34, footnote 127, citing Elgin, Exh. No. 161HCT at 39. In this section of Mr. Elgin's testimony, at pages 38:12-19 and 39:5-8, Mr. Elgin explained how to protect rate payers from these impacts.
[110] Public Counsel Opening Brief at 34-35, ¶¶ 75-78.
[111] Panel Testimony, TR. 477:7 - 478:7 (Markell); TR. 479:10 - 481:3 (Elgin); Staff Opening Brief at 23-24, ¶¶ 65-67.

64 Or, if Public Counsel is alleging that there will be an increase in PE's cost of equity due to the transaction, Commitments 9(iii), 24, and 26(a) also protect PSE against the impact of any such increase.[112] In short, the Commitments eliminate the issue now raised by Public Counsel.

65 **Investor benefits.** At the end of its discussion on this subject, Public Counsel notes that the Investor Consortium will "make a lot more money" by using leverage to take PE private rather than buy PE stock in the open market, which would not change PE's status as a publicly traded company.[113] However, missing from Public Counsel's analysis is any explanation of how this violates the Commission's "no harm" standard, if at all. There is nothing evident in the Commission's "no harm" standard that prevents a purchaser from an opportunity to make money on a transaction by accepting the risk of increased financial leverage.

66 Indeed, Staff's own testimony notes that the Investor Consortium's use of debt ("leverage") at the PE level to finance PSE's equity gives the new owners an opportunity to achieve substantial economic benefits.[114] However, the Commission has previously ruled that the new owners alone are entitled to those benefits, so long as the ring fencing provisions insulate ratepayers from the attendant risks: "If the risks and costs of activities at the parent level are born [sic] 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."[115]

67 This Commission ruling refutes Public Counsel's position here.

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[112] Staff Opening Brief at 23-24, ¶¶ 65-67, and Commitments discussed therein, and Panel Testimony, TR. 477:7 - 478:7 (Markell) and TR. 479:10 - 481:3 (Elgin).
[113] Public Counsel Opening Brief at 36, ¶ 78.
[114] Elgin, Exh. No. 161 HCT at 5:10-15.
[115] *Wash. Utilities & Transp. Comm'n v. PacifiCorp, d/b/a Pacific Power & Light Co.,* Docket UE-050684, Order 04 (April 17, 2006) at 103-104, ¶¶ 285.

E. Public Counsel's Discussion of Macquarie's Modeling is Incomplete Because Public Counsel Fails to Analyze How the Investor Consortium Considered That Modeling. Public Counsel's Critique of Macquarie's Business Model Fails to Recognize the Ring Fencing That Protects Ratepayers from the Risks of New Ownership.

Reply to Public Counsel Opening Brief Part VI & VII – Pages 36-51, ¶¶ 79-112, excluding ¶¶ 99-103[116]

68 Public Counsel recites many of the assumptions and other aspects of the model that Macquarie used to analyze the purchase of PE, and to inform potential investors in the transaction. Public Counsel wants the Commission to conclude that all these assumptions and aspects "underscore the tenuous nature of the predicted success of the transaction."[117]

69 Frankly, this was not a major issue for Staff, because the record shows that it is reasonable to expect that the Investor Consortium members employ sophisticated professionals capable of understanding, evaluating and discounting assumptions in making their respective decisions to enter into this transaction and purchase PE.[118] Indeed, a fatal flaw in Public Counsel's analysis is the absence of any evidence of how any particular Investor Consortium member analyzed the model or its inputs and outputs in reaching their decision to invest. Moreover, there is no evidence that any Investor Consortium member considers the model to be sacrosanct, with the effects Public Counsel urges the Commission to accept as inevitable.

70 In any event, the financial landscape of the transaction has changed through the many ring fencing provisions that were added since the Joint Application was filed, yet the Joint Applicants continued to pursue their application. The Commission should not make any conclusions based on computer model outputs that have been overtaken by events.

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[116] In ¶¶ 40-41, at pages 13-14, *supra,* we address Public Counsel's allegations regarding Dr. Schmidt, found on pages 45-47, ¶¶ 99-102, of Public Counsel's Opening Brief. In ¶ 4, at pages 1-2, *supra,* we address Public Counsel's argument regarding the new owners' reliance on credit markets, found on page 47, ¶ 103, of Public Counsel's Opening Brief.

[117] Public Counsel Opening Brief at 36, ¶ 80.

[118] This expectation is confirmed by the qualifications and experience of the Investor Consortium members. See, *e.g.,* the Joint Application at 6-11, ¶¶ 11-21, and Mr. Leslie for Macquarie, Exh. No. 31T at 5-14; Mr. Webb for bcIMC, Exh. No. 141T at 2:6 - 7:2; Mr. Wiseman for CPP, Exh. No. 151T at 2:8 - 7:14, and Mr. McKenzie for AIMCo, Exh. No. 91T at 2:4 - 6:4.

71 As investors in several other regulated public service companies, the Investor Consortium members understand the obvious: The Commission controls PSE's rates, and thus (to a large degree) PSE's earnings.[119] Moreover, ring fencing Commitments 8, 9(iii), 24, 25, 26, 35, 36, 37 and 40 clearly protect PSE from unbridled distributions to the new owners.[120]

72 Public Counsel then takes aim at Macquarie's business model, arguing that typically, it calls for the use of debt to fund the equity investment in the acquired firm.[121] Once again, Public Counsel misses the mark, because as we have explained, the protections offered by the ring fence protect ratepayers from this risk which the new owners plan to undertake here.

F. The Stipulation's Governance Provisions Are Sufficient, and Are Supported By the Oregon Commission Decision Relied on by Public Counsel.

Reply to Public Counsel Opening Brief Part VIII, Pages 51-57, ¶¶ 113-124

73 While apparently conceding that the reporting requirements under the transaction are acceptable as they apply to PSE, [122] Public Counsel complains about "investor control," the loss of some local representation on the PSE board, and an alleged lack of transparency resulting from the transaction.[123]

74 However, Public Counsel cannot prove that "investor control" creates harm as compared to the status quo, because as Public Counsel elsewhere notes, under the status quo, the PSE board's duty already is owed primarily to its shareholders.[124] Similarly, under the status quo, there is no requirement that PSE have *any* local board members. It follows, then, that the board provisions contained in the Commitments cannot constitute a "harm" caused by the transaction, as compared to the status quo.

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[119] *E.g.*, Leslie, Exh. No. 31T at 18:9-19:4.
[120] *E.g.*, see Staff Opening Brief at 21-28, ¶¶ 58-78.
[121] Public Counsel Opening Brief at 44-51, ¶¶ 96-112.
[122] *Id.* at 57, ¶ 124.
[123] *Id* at 51-57, ¶¶ 113-124.
[124] *Id* at 12, ¶ 26.

75 In the Oregon commission decision relied on by Public Counsel in its opening brief, the challengers made arguments about investor control and transparency similar to Public Counsel's arguments here. However, the Oregon commission rejected those arguments on the basis that it had sufficient statutory authority to obtain information from the utility to address any concerns about how the utility was being managed.[125] The Commission has similar broad authority under RCW 80.04.080.[126] Public Counsel fails to distinguish the Oregon decision on this point.

G. The Stipulation Enhances the Commission's Regulatory Reach, and the Commitments are Enforceable.

Reply to Public Counsel Opening Brief Part IX, Pages 57-66, ¶¶ 125-142

76 Staff wholeheartedly agrees with Public Counsel that in evaluating this transaction, it is critical for the Commission to analyze its "authority over the surviving entity," in order to assure that the Commission's regulatory jurisdiction is not impaired.[127] In fact, the Stipulation fully preserves the Commission's jurisdiction because the "surviving entity" is PSE, and PSE will remain a public service company subject to the same statutes, rules and orders as before.[128]

77 Nonetheless, Public Counsel insists there has been "confusion about the scope and interpretation of the commitments," and alleges that the signing parties "pulled back" from some of these commitments.[129] In fact, as we explain next, there was no such "pulling back," and if there is any confusion, it is Public Counsel's.

78 **Commitment 26(b)(2) – "Material" change in control.** Public Counsel first identifies Commitment 26(b)(2)'s use of the term "*material* change in control," but then promptly acknowledges that this term is explained in Exhibit 419.[130] There is no issue here.

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[125] *In re Oregon Elec. Utility Co. LLC, supra,* 240 PUR4th at 162-63.
[126] *See also Qwest Corp. v. Wash. Utilities & Transp. Comm'n,* 140 Wn. App. 255, 262, 166 P.3d 732 (2007) (acknowledging the Commission's "broad authority" under RCW 80.04.080.
[127] Public Counsel Opening Brief at 57, ¶ 125.
[128] Staff Opening Brief at 28-31, ¶¶ 81-85.
[129] Public Counsel Opening Brief at 65, ¶ 141.
[130] *Id* at 58, ¶ 127.

79 **Commitment 28(c) – Compliance with Title 80 RCW.** Public Counsel next addresses Commitment 28(c), which states that "PSE and Puget Holdings will comply with all applicable provisions of Title 80 RCW." On its face, this Commitment contains no ambiguity; it simply reassures that nothing in the transaction changes the "applicability" of Title 80 RCW to PSE and Puget Holdings.[131] Public Counsel attempts to create confusion by saying the signing parties are "pulling back" from Commitment 28(c), based on the claim that originally, this commitment was intended to be a "broad assurance" that Puget Holdings would be subject to Title 80 RCW.[132]

80 Public Counsel provides no support for this claim, and nothing in the words of Commitment 28(c) supports it, either. Indeed, it is not clear why Public Counsel, or anyone, for that matter, would want the Commission to regulate the rates and services of Puget Holdings, which offers no utility services to the public. The bottom line is that Commitment 28(c) provides precisely what Public Counsel wants: A clear commitment that the Commission's jurisdiction under Title 80 RCW will be unimpaired by the transaction.

81 **Compelling attendance of witnesses.** Public Counsel then refers to the issue whether the Commission could compel knowledgeable Investor Consortium witnesses located outside of the United States to attend a future Commission hearing. Public Counsel apparently concedes that Commitment 31 covers this issue, to the extent of issues that "relate to Puget Sound Energy," but Public Counsel wants to convince the Commission that it must have broader authority, up to and including matters that relate to "Puget Holdings and any other entity in the corporate structure."[133]

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[131] Under the status quo, the Commission has limited jurisdiction over PE, such as when PE acts in the capacity as an affiliate of PSE. *RCW 80.16.*
[132] Public Counsel Opening Brief at 58, ¶ 129.
[133] *Id* at 59, ¶ 130.

82 Notably, no such provision is included in the PacifiCorp/MEHC transaction, which Public Counsel fully endorsed,[134] so we suggest this is just another instance of Public Counsel creating an issue where none exists. In any event, like it or not, the Commission's jurisdiction is not unlimited, and it does not extend to matters outside the public service laws.[135] On the other hand, because Puget Holdings is an Applicant and a signatory to the Stipulation, the public service laws make Puget Holdings subject to enforcement of those Commitments.[136] Thus, under the Stipulation, the Commission's enforcement authority over Puget Holdings is *enhanced* as compared to the Commission's regulatory authority over PSE's current parent company (PE) under the status quo. Public Counsel should support this feature, not oppose it.

83 **Commitments 19 & 27 - Access to books and records.** Public Counsel questions whether the Commission will have access to the books and records of companies in the ownership chain "above Puget Holdings."[137] However, today, the Commission currently lacks unlimited access to the books and records of PSE's current parent (PE). Therefore, Public Counsel's argument fails because the lack of unlimited access to the books of companies "above Puget Holdings" is not a "harm" as compared to the status quo.

84 In any event, the Commitments, coupled with the Commission's broad statutory authority in RCW 80.01.040, clearly assure that the Commission will have the same access to documents as in similar Commission-approved transactions, which includes the authority to review any document related to the costs PSE identifies as necessary to provide service to the public, which could include documents at any level within the new ownership structure.[138]

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[134] *In re Application of MidAmerican Holdings Co. & PacifiCorp, d/b/a Pacific Power & Light Co.*, Docket UE-051090, Order 07 (February 22, 2006).
[135] RCW 80.01.040.
[136] RCW 80.04.387 and Staff Opening Brief at 20-21, ¶¶ 54-57. This point was confirmed on the record by counsel for Staff, and counsel for PSE and Puget Holdings. *TR. 506:5-15.*
[137] Public Counsel Opening Brief at 60, ¶ 131.
[138] RCW 80.04.080 and Commitments 19 and 27.

85 Moreover, as we noted earlier,[139] the Oregon commission rejected arguments similar to those advanced by Public Counsel here, based on its broad statutory right to access information relevant to its statutory authority. Public Counsel does not and cannot distinguish that decision on this point, because, as we also mentioned earlier, the Commission has broad authority similar to that of Oregon.[140] In sum, the Commission should reject Public Counsel's claims here.

86 **"Complexity."** Next, Public Counsel offers up the "complexity" of Macquarie's ownership structure in an effort to buttress a claim that this will somehow introduce unspecified "challenges and problems" for Commission regulation of PSE.[141] However, if Public Counsel's concern were valid, the Commission would reasonably expect Public Counsel to document at least one actual problem that has arisen from Macquarie's equally "complex" ownership of other regulated utilities or similar entities. In fact, Public Counsel's opening brief is devoid of even a single example of a problem that materialized from other Macquarie transactions, such as Macquarie's ownership of, say, Duquesne Light Company in Pennsylvania or The Gas Company in Hawaii, or any one of the several other utilities Macquarie owns.

87 One can only conclude that Public Counsel's unsubstantiated claim lacks merit and it should be rejected by the Commission.

H. Miscellaneous Issues.
Reply to Public Counsel Opening Brief Parts X and XI – Pages 66-71, ¶¶ 143-153[142]

88 **Low income/Environmental Commitments.** Public Counsel correctly recognizes that the low income and environmental Commitments in the Stipulation generally reaffirm existing

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[139] See discussion in ¶ 75, at page 25, *supra.*
[140] *Id.*
[141] Public Counsel Opening Brief at 60-62, ¶¶ 132-135. We are tempted to ask the rhetorical question whether this ownership structure is any more complex than the current ownership structure of PacifiCorp (created by a transaction Public Counsel endorsed), or the Bell System in its prime. Public Counsel offers no examples of the Commission's inability to carry out its regulatory responsibilities under these "complex" organizational structures.
[142] In ¶ 57 at pages 19-20, *supra,* we addressed Public Counsel's statements that transaction costs create "bias" and add to the debt at PE, found on pages 66-67, ¶¶ 143-144 of Public Counsel's Opening Brief.

programs and do not constitute incremental transaction "benefits."[143] However, this is not an issue because no party represented these Commitments to do anything else.

89 **Commitment 34 - $100 million in rate credits.** Another non-issue is Public Counsel's claim that the $100 million in rate credits does not mitigate the risks of the transaction,[144] because risk mitigation is not the rationale for Commitment 34.[145] Yet another non-issue is Public Counsel's prediction that the impact of the credits on the local economy will be small,[146] because the Commission's "no harm" standard does not require rate credits, or any other substantial, net positive benefits, for that matter.[147] Therefore, in reply to Public Counsel's attempt to treat $100 million as minimal, Staff will leave it for future economic analysis to determine how much impact this $100 million will actually have on ratepayers and the local economy, should the Commission ever deem that analysis relevant in a future proceeding.

90 However, Public Counsel does not and cannot dispute that these rate credits "exceed, in both quantity and duration, any non-offsettable rate credits previously offered in any precedent transaction before this Commission involving an electric or natural gas utility."[148]

91 **Public comment.** Finally, Public Counsel discusses the public testimony and written comments, noting that almost all of them are in opposition to the transaction.[149] Staff is aware the Commission will keep this issue in proper perspective. Indeed, it is the Commission's job to

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[143] Public Counsel Opening Brief at 68-69, ¶¶ 146-48.
[144] *Id* at 68, ¶ 145.
[145] As Mr. Leslie explained, the rate credits simply were intended to respond to a call the Joint Applicants perceived for "an additional quantifiable customer benefit." Leslie, Exh. No. 38HCT at 24:18-22.
[146] Public Counsel Opening Brief at 68, ¶ 145.
[147] According to the Commission, under the "no harm" standard, applicants are not required "to show that customers or the public generally, will be made better off if the transaction is approved and goes forward." *In re Application of PacifiCorp and ScottishPower PLC, supra,* Third Supplemental Order at 2 (April 2, 1999).
[148] Joint Rebuttal Testimony, Exh. No. 304CT at 19:6-8.
[149] Public Counsel Opening Brief at 69-70, ¶¶ 149-151.

decide controversial issues based on the record and the law. Sometimes, this means the Commission must make a decision over the opposition of many commenters.[150]

92 As the Commission wisely observed just two weeks ago: "While we acknowledge the opposition to any rate increase expressed by members of the public through oral and written comments, our decisions must be made in accordance with law, policy and the factual record before us."[151] The Commission made this statement in a rate case, but it applies equally to the instant docket.

IV. CONCLUSION

93 For the reasons stated above, and in Staff's opening brief, the proposed transaction meets the Commission's "no harm" standard. Therefore, the Commission should grant the Application according to the terms and conditions contained in the Settlement Stipulation. The Commission should reject Public Counsel's opposition to the transaction, including Public Counsel's proposal to expand the Commission's "no harm" standard to include a "threshold" showing of need for the transaction.

DATED this 23rd day of October, 2008.

Respectfully submitted,

ROBERT M. MCKENNA
Attorney General

DONALD T. TROTTER
Senior Counsel
Counsel for the Staff of the Washington
Utilities and Transportation Commission

[150] For example, there was very significant public opposition to the Commission's well-grounded decision to allow PSE's predecessor to recover in rates the costs of its abandoned nuclear projects. Public Counsel and a large consumer group mounted an assault, but the court affirmed the Commission's order, based on the record and the law. *People's Org. For Wash. Energy Resources,* 104 Wn.2d 798, 711 P.2d 319 (1985).
[151] *Wash. Utilities & Transp. Comm'n v. PacifiCorp,* Docket UE-080220, Order 05 (October 8, 2008) at 8, ¶ 31.