

PUGET ENERGY INC /WA
Form 10-Q
November 03, 2017

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549
FORM 10-Q

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT
OF 1934

For the quarterly period ended September 30, 2017
OR

TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF
1934

For the Transition period from _____ to _____

		I.R.S.
Commission File Number	Exact name of registrant as specified in its charter, state of incorporation, address of principal executive offices, telephone number	Employer Identification Number

PUGET ENERGY, INC.
A Washington Corporation
1-16305 10885 NE 4th Street, Suite 1200 91-1969407
Bellevue, Washington 98004-5591
(425) 454-6363

PUGET SOUND ENERGY, INC.
A Washington Corporation
1-4393 10885 NE 4th Street, Suite 1200 91-0374630
Bellevue, Washington 98004-5591
(425) 454-6363

Indicate by check mark whether the registrants: (1) have filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) have been subject to such filing requirements for the past 90 days.

Puget Energy, Inc. Yes/X/No/ / Puget Sound Energy, Inc. Yes/X/No/ /

Indicate by check mark whether the registrants have submitted electronically and posted on their corporate websites, if any, every interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).

Puget Energy, Inc. Yes/X/No/ / Puget Sound Energy, Inc. Yes/X/No/ /

Indicate by check mark whether registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer or a smaller reporting company. See definition of "large accelerated filer, accelerated filer and smaller reporting company" in Rule 12b-2 of the Exchange Act.

Puget Energy, Inc.	Large accelerated filer	/ /	Accelerated filer	/ /	Non-accelerated filer	/X/	Smaller reporting company	/ /	Emerging growth company	/ /
Puget Sound Energy, Inc.	Large accelerated filer	/ /	Accelerated filer	/ /	Non-accelerated filer	/X/	Smaller reporting company	/ /	Emerging growth company	/ /

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act. //

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Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).
Puget Energy, Inc. Yes/ /No/X/ Puget Sound Energy, Inc. Yes/ /No/X/
All of the outstanding shares of voting stock of Puget Energy, Inc. are held by Puget Equico LLC, an indirect wholly-owned subsidiary of Puget Holdings LLC. All of the outstanding shares of voting stock of Puget Sound Energy, Inc. are held by Puget Energy, Inc.

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DEFINITIONS

ARO	Asset Retirement and Environmental Obligations
ASU	Accounting Standards Update
ASC	Accounting Standards Codification
EBITDA	Earnings Before Interest, Tax, Depreciation and Amortization
EIM	Energy Imbalance Market
ERF	Expedited Rate Filing
FASB	Financial Accounting Standards Board
GAAP	U.S. Generally Accepted Accounting Principles
GRC	General Rate Case
ISDA	International Swaps and Derivatives Association
LIBOR	London Interbank Offered Rate
LNG	Liquefied Natural Gas
MMBtu	One Million British Thermal Units
MWh	Megawatt Hour (one MWh equals one thousand kWh)
NAESB	North American Energy Standards Board
NPNS	Normal Purchase Normal Sale
PCA	Power Cost Adjustment
PCORC	Power Cost Only Rate Case
PGA	Purchased Gas Adjustment
PSE	Puget Sound Energy, Inc.
Puget Energy	Puget Energy, Inc.
Puget Holdings	Puget Holdings LLC
Puget LNG	Puget Liquid Natural Gas
REP	Residential Exchange Program
SERP	Supplemental Executive Retirement Plan
Washington Commission	Washington Utilities and Transportation Commission
WSPP	WSPP, Inc.

FILING FORMAT

This report on Form 10-Q is a Quarterly Report filed separately by two registrants, Puget Energy, Inc. (Puget Energy) and Puget Sound Energy, Inc. (PSE). Any references in this report to “the Company” are to Puget Energy and PSE collectively.

FORWARD-LOOKING STATEMENTS

Puget Energy and PSE include the following cautionary statements in this Form 10-Q to make applicable and to take advantage of the safe harbor provisions of the Private Securities Litigation Reform Act of 1995 for any forward-looking statements made by or on behalf of Puget Energy or PSE. This report includes forward-looking statements, which are statements of expectations, beliefs, plans, objectives and assumptions of future events or performance. Words or phrases such as “anticipates,” “believes,” “continues,” “could,” “estimates,” “expects,” “future,” “intends,” “may,” “might,” “plans,” “potential,” “predicts,” “projects,” “should,” “will likely result,” “will continue” or similar expressions are intended to identify certain of these forward-looking statements and may be included in discussion of, among other things, our anticipated operating or financial performance, business plans and prospects, planned capital expenditures and other future expectations. In particular, these include statements relating to future actions, business plans and prospects, future performance expenses, the outcome of contingencies, such as legal proceedings, government regulation and financial results.

Forward-looking statements reflect current expectations and involve risks and uncertainties that could cause actual results or outcomes to differ materially from those expressed. There can be no assurance that Puget Energy’s and PSE’s expectations, beliefs or projections will be achieved or accomplished.

In addition to other factors and matters discussed elsewhere in this report, some important risks that could cause actual results or outcomes for Puget Energy and PSE to differ materially from past results and those discussed in the forward-looking statements include:

Governmental policies and regulatory actions, including those of the Federal Energy Regulatory Commission (FERC) and the Washington Utilities and Transportation Commission (Washington Commission), that may affect our ability to recover costs and earn a reasonable return, including but not limited to disallowance or delays in the recovery of capital investments and operating costs and discretion over allowed return on investment;

Changes in, adoption of and compliance with laws and regulations, including decisions and policies concerning the environment, climate change, greenhouse gas or other emissions or by products of electric generation (including coal ash or other substances), natural resources, and fish and wildlife (including the Endangered Species Act) as well as the risk of litigation arising from such matters, whether involving public or private claimants or regulatory investigative or enforcement measures;

Changes in tax law, related regulations or differing interpretation or enforcement of applicable law by the Internal Revenue Service (IRS) or other taxing jurisdiction; and PSE’s ability to recover costs in a timely manner arising from such changes;

Inability to realize deferred tax assets and use production tax credits (PTCs) due to insufficient future taxable income; Accidents or natural disasters, such as hurricanes, windstorms, earthquakes, floods, fires and landslides, and other acts of God, terrorism, asset-based or cyber-based attacks, pandemic or similar significant events, which can interrupt service and lead to lost revenue, cause temporary supply disruptions and/or price spikes in the cost of fuel and raw materials and impose extraordinary costs;

Commodity price risks associated with procuring natural gas and power in wholesale markets from creditworthy counterparties;

Wholesale market disruption, which may result in a deterioration of market liquidity, increase the risk of counterparty default, affect the regulatory and legislative process in unpredictable ways, negatively affect wholesale energy prices and/or impede PSE’s ability to manage its energy portfolio risks and procure energy supply, affect the availability and access to capital and credit markets and/or impact delivery of energy to PSE from its suppliers;

Financial difficulties of other energy companies and related events, which may affect the regulatory and legislative process in unpredictable ways, adversely affect the availability of and access to capital and credit markets and/or impact delivery of energy to PSE from its suppliers;

The effect of wholesale market structures (including, but not limited to, regional market designs or transmission organizations) or other related federal initiatives;

PSE electric or natural gas distribution system failure, blackouts or large curtailments of transmission systems (whether PSE's or others'), or failure of the interstate natural gas pipeline delivering to PSE's system, all of which can affect PSE's ability to deliver power or natural gas to its customers and generating facilities;

Electric plant generation and transmission system outages, which can have an adverse impact on PSE's expenses with respect to repair costs, added costs to replace energy or higher costs associated with dispatching a more expensive generation resource;

The ability to restart generation following a regional transmission disruption;

Changes in climate or weather conditions in the Pacific Northwest, which could have effects on customer usage and PSE's revenue and expenses;

Regional or national weather, which could impact PSE's ability to procure adequate supplies of natural gas, fuel or purchased power to serve its customers and the cost of procuring such supplies;

Variable hydrological conditions, which can impact streamflow and PSE's ability to generate electricity from hydroelectric facilities;

Variable wind conditions, which can impact PSE's ability to generate electricity from wind facilities;

The ability to renew contracts for electric and natural gas supply and the price of renewal;

Industrial, commercial and residential growth and demographic patterns in the service territories of PSE;

General economic conditions in the Pacific Northwest, which may impact customer consumption or affect PSE's accounts receivable;

The loss of significant customers, changes in the business of significant customers or the condemnation of PSE's facilities as a result of municipalization or other government action or negotiated settlement, which may result in changes in demand for PSE's services;

The failure of information systems or the failure to secure information system data, which may impact the operations and cost of PSE's customer service, generation, distribution and transmission;

Capital market conditions, including changes in the availability of capital and interest rate fluctuations;

Employee workforce factors, including strikes, work stoppages, availability of qualified employees or the loss of a key executive;

The ability to obtain insurance coverage, the availability of insurance for certain specific losses, and the cost of such insurance;

The ability to maintain effective internal controls over financial reporting and operational processes;

Changes in Puget Energy's or PSE's credit ratings, which may have an adverse impact on the availability and cost of capital for Puget Energy or PSE generally; and

Deteriorating values of the equity, fixed income and other markets which could significantly impact the value of investments of PSE's retirement plan, post-retirement medical benefit plan trusts and the funding of obligations thereunder.

Any forward-looking statement speaks only as of the date on which such statement is made, and, except as required by law, the Company undertakes no obligation to update any forward-looking statement to reflect events or circumstances after the date on which such statement is made or to reflect the occurrence of unanticipated events. New factors emerge from time to time and it is not possible for management to predict all such factors, nor can it assess the impact of any such factor on the business or the extent to which any factor, or combination of factors, may cause results to differ materially from those contained in any forward-looking statement. For further information, see Item 1A, "Risk Factors" in the Company's most recent Annual Report on Form 10-K.

PART I FINANCIAL INFORMATION

Item 1. Financial Statements

PUGET ENERGY, INC.
CONSOLIDATED STATEMENTS OF INCOME
(Dollars in Thousands)
(Unaudited)

	Three Months Ended		Nine Months Ended	
	September 30,		September 30,	
	2017	2016	2017	2016
Operating revenue:				
Electric	\$537,543	\$495,321	\$1,736,335	\$1,622,664
Natural gas	111,516	114,458	691,685	601,309
Other	11,318	8,499	29,356	25,170
Total operating revenue	660,377	618,278	2,457,376	2,249,143
Operating expenses:				
Energy costs:				
Purchased electricity	115,881	94,849	425,263	356,296
Electric generation fuel	66,584	70,503	152,057	165,627
Residential exchange	(14,246)	(15,577)	(52,814)	(49,093)
Purchased natural gas	32,224	34,041	248,208	205,418
Unrealized (gain) loss on derivative instruments, net	(23)	6,327	23,098	(57,218)
Utility operations and maintenance	141,003	138,265	438,622	422,273
Non-utility expense and other	7,319	4,708	18,658	15,520
Depreciation and amortization	120,829	110,022	355,538	328,809
Conservation amortization	25,395	21,800	85,847	77,551
Taxes other than income taxes	66,367	65,268	262,099	235,431
Total operating expenses	561,333	530,206	1,956,576	1,700,614
Operating income (loss)	99,044	88,072	500,800	548,529
Other income (expense):				
Other income	7,151	6,130	19,375	19,187
Other expense	(2,878)	(5,025)	(6,134)	(8,488)
Non-hedged interest rate swap (expense) income	—	563	28	(651)
Interest charges:				
AFUDC	3,123	2,702	7,853	7,663
Interest expense	(88,780)	(89,297)	(265,771)	(266,786)
Income (loss) before income taxes	17,660	3,145	256,151	299,454
Income tax (benefit) expense	4,824	810	80,489	91,380
Net income (loss)	\$12,836	\$2,335	\$175,662	\$208,074

The accompanying notes are an integral part of the financial statements.

PUGET ENERGY, INC.
 CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME
 (Dollars in Thousands)
 (Unaudited)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2017	2016	2017	2016
Net income (loss)	\$12,836	\$2,335	\$175,662	\$208,074
Other comprehensive income (loss):				
Net unrealized gain (loss) from pension and post-retirement plans, net of tax of \$(143), \$(16), \$216 and \$(216), respectively	(266)	(29)	400	(400)
Other comprehensive income (loss)	(266)	(29)	400	(400)
Comprehensive income (loss)	\$12,570	\$2,306	\$176,062	\$207,674

The accompanying notes are an integral part of the financial statements.

PUGET ENERGY, INC.
CONSOLIDATED BALANCE SHEETS
(Dollars in Thousands)
(Unaudited)

ASSETS

	September 30, 2017	December 31, 2016
Utility plant (at original cost, including construction work in progress of \$598,790 and \$420,278, respectively):		
Electric plant	\$7,918,877	\$7,673,772
Natural gas plant	3,253,977	3,051,586
Common plant	738,409	594,994
Less: Accumulated depreciation and amortization	(2,409,508)	(2,161,796)
Net utility plant	9,501,755	9,158,556
Other property and investments:		
Goodwill	1,656,513	1,656,513
Other property and investments	166,996	106,418
Total other property and investments	1,823,509	1,762,931
Current assets:		
Cash and cash equivalents	6,768	28,878
Restricted cash	9,302	12,418
Accounts receivable, net of allowance for doubtful accounts of \$6,088 and \$9,798, respectively	232,699	329,375
Unbilled revenue	126,252	234,053
Purchased gas adjustment receivable	—	2,785
Materials and supplies, at average cost	108,814	106,378
Fuel and natural gas inventory, at average cost	60,645	58,181
Unrealized gain on derivative instruments	16,605	54,341
Prepaid expense and other	35,655	43,046
Power contract acquisition adjustment gain	15,932	33,413
Total current assets	612,672	902,868
Other long-term and regulatory assets:		
Regulatory asset for deferred income taxes	71,566	72,038
Power cost adjustment mechanism	4,540	4,531
Regulatory assets related to power contracts	19,998	22,613
Other regulatory assets	1,014,796	1,034,348
Unrealized gain on derivative instruments	2,877	8,738
Power contract acquisition adjustment gain	163,588	241,648
Other	65,138	58,109
Total other long-term and regulatory assets	1,342,503	1,442,025
Total assets	\$ 13,280,439	\$ 13,266,380

The accompanying notes are an integral part of the financial statements.

PUGET ENERGY, INC.
CONSOLIDATED BALANCE SHEETS
(Dollars in Thousands)
(Unaudited)

CAPITALIZATION AND LIABILITIES

	September 30, 2017	December 31, 2016
Capitalization:		
Common shareholder's equity:		
Common stock \$0.01 par value, 1,000 shares authorized, 200 shares outstanding	\$—	\$—
Additional paid-in capital	3,308,957	3,308,957
Retained earnings	571,588	413,468
Accumulated other comprehensive income (loss), net of tax	(33,312)	(33,712)
Total common shareholder's equity	3,847,233	3,688,713
Long-term debt:		
First mortgage bonds and senior notes	3,164,412	3,362,000
Pollution control bonds	161,860	161,860
Junior subordinated notes	250,000	250,000
Long-term debt	1,883,064	1,812,480
Debt discount, issuance costs and other	(224,336)	(234,679)
Total long-term debt	5,235,000	5,351,661
Total capitalization	9,082,233	9,040,374
Current liabilities:		
Accounts payable	296,659	317,043
Short-term debt	139,000	245,763
Current maturities of long-term debt	200,000	2,412
Purchased gas adjustment payable	5,784	—
Accrued expenses:		
Taxes	81,354	111,428
Salaries and wages	41,121	49,749
Interest	79,213	73,610
Unrealized loss on derivative instruments	49,820	44,310
Power contract acquisition adjustment loss	2,850	3,159
Other	81,486	71,996
Total current liabilities	977,287	919,470
Other long-term and regulatory liabilities:		
Deferred income taxes	1,652,573	1,570,931
Unrealized loss on derivative instruments	15,578	16,261
Regulatory liabilities	611,899	654,622
Regulatory liabilities related to power contracts	179,519	275,061
Power contract acquisition adjustment loss	17,148	19,454
Other deferred credits	744,202	770,207
Total other long-term and regulatory liabilities	3,220,919	3,306,536
Commitments and contingencies (Note 8)		
Total capitalization and liabilities	\$ 13,280,439	\$ 13,266,380

The accompanying notes are an integral part of the financial statements.

PUGET ENERGY, INC.
CONSOLIDATED STATEMENTS OF CASH FLOWS
(Dollars in Thousands)
(Unaudited)

	Nine Months Ended September 30,	
	2017	2016
Operating activities:		
Net income (loss)	\$175,662	\$208,074
Adjustments to reconcile net income (loss) to net cash provided by operating activities:		
Depreciation and amortization	355,538	328,809
Conservation amortization	85,847	77,551
Deferred income taxes and tax credits, net	81,899	90,828
Net unrealized (gain) loss on derivative instruments	22,957	(60,785)
AFUDC – equity	(11,266)	(10,769)
Funding of pension liability	(18,000)	(24,000)
Regulatory assets and liabilities	(83,370)	(138,096)
Other long-term assets and liabilities	8,275	30,766
Change in certain current assets and liabilities:		
Accounts receivable and unbilled revenue	204,477	175,627
Materials and supplies	(2,436)	(28,448)
Fuel and natural gas inventory	(2,789)	(3,222)
Prepayments and other	7,391	(29,352)
Purchased gas adjustment	8,569	(10,743)
Accounts payable	(31,027)	(22,874)
Taxes payable	(30,074)	(36,411)
Other	(2,983)	23,391
Net cash provided by (used in) operating activities	768,670	570,346
Investing activities:		
Construction expenditures – excluding equity AFUDC	(761,968)	(507,703)
Restricted cash	3,116	(1,391)
Other	5,796	(1,781)
Net cash provided by (used in) investing activities	(753,056)	(510,875)
Financing activities:		
Change in short-term debt, net	(106,763)	12,996
Dividends paid	(17,543)	(111,592)
Proceeds from long-term debt and bonds issued	70,583	—
Other	15,999	13,479
Net cash provided by (used in) financing activities	(37,724)	(85,117)
Net increase (decrease) in cash and cash equivalents	(22,110)	(25,646)
Cash and cash equivalents at beginning of period	28,878	42,494
Cash and cash equivalents at end of period	\$6,768	\$16,848
Supplemental cash flow information:		
Cash payments for interest (net of capitalized interest)	\$239,566	\$241,351
Cash payments (refunds) for income taxes	1,649	—
Non-cash financing and investing activities:		
Accounts payable for capital expenditures eliminated from cash flows	\$87,456	\$58,278

The accompanying notes are an integral part of the financial statements.

PUGET SOUND ENERGY, INC.
CONSOLIDATED STATEMENTS OF INCOME
(Dollars in Thousands)
(Unaudited)

	Three Months Ended		Nine Months Ended	
	September 30,		September 30,	
	2017	2016	2017	2016
Operating revenue:				
Electric	\$537,543	\$495,321	\$1,736,335	\$1,622,664
Natural gas	111,516	114,458	691,685	601,309
Other	11,318	8,815	29,356	25,487
Total operating revenue	660,377	618,594	2,457,376	2,249,460
Operating expenses:				
Energy costs:				
Purchased electricity	115,881	94,849	425,263	356,296
Electric generation fuel	66,584	70,503	152,057	165,627
Residential exchange	(14,246)	(15,577)	(52,814)	(49,093)
Purchased natural gas	32,224	34,041	248,208	205,418
Unrealized (gain) loss on derivative instruments, net	(23)	6,327	23,098	(57,218)
Utility operations and maintenance	141,003	138,265	438,622	422,273
Non-utility expense and other	9,994	8,620	27,857	26,474
Depreciation and amortization	120,829	110,022	355,538	328,809
Conservation amortization	25,395	21,800	85,847	77,551
Taxes other than income taxes	66,367	65,268	262,099	235,431
Total operating expenses	564,008	534,118	1,965,775	1,711,568
Operating income (loss)	96,369	84,476	491,601	537,892
Other income (expense):				
Other income	6,778	6,131	18,861	19,184
Other expense	(2,878)	(5,025)	(6,134)	(8,488)
Interest charges:				
AFUDC	3,123	2,702	7,853	7,663
Interest expense	(59,868)	(60,914)	(180,320)	(182,336)
Income (loss) before income taxes	43,524	27,370	331,861	373,915
Income tax (benefit) expense	14,424	8,393	109,015	117,533
Net income (loss)	\$29,100	\$18,977	\$222,846	\$256,382

The accompanying notes are an integral part of the financial statements.

PUGET SOUND ENERGY, INC.
CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME
(Dollars in Thousands)
(Unaudited)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2017	2016	2017	2016
Net income (loss)	\$29,100	\$18,977	\$222,846	\$256,382
Other comprehensive income (loss):				
Net unrealized gain (loss) from pension and post-retirement plans, net of tax of \$939, \$1,422, \$3,813 and \$3,942, respectively	1,744	2,642	7,083	7,322
Amortization of treasury interest rate swaps to earnings, net of tax of \$43, \$43, \$128 and \$128, respectively	79	79	237	237
Other comprehensive income (loss)	1,823	2,721	7,320	7,559
Comprehensive income (loss)	\$30,923	\$21,698	\$230,166	\$263,941

The accompanying notes are an integral part of the financial statements.

PUGET SOUND ENERGY, INC.
CONSOLIDATED BALANCE SHEETS
(Dollars in Thousands)
(Unaudited)

ASSETS

	September 30, 2017	December 31, 2016
Utility plant (at original cost, including construction work in progress of \$598,790 and \$420,278, respectively):		
Electric plant	\$ 10,036,204	\$ 9,813,169
Natural gas plant	3,838,533	3,640,271
Common plant	776,116	632,718
Less: Accumulated depreciation and amortization	(5,149,098)	(4,927,602)
Net utility plant	9,501,755	9,158,556
Other property and investments:		
Other property and investments	78,332	77,960
Total other property and investments	78,332	77,960
Current assets:		
Cash and cash equivalents	5,939	28,481
Restricted cash	9,302	12,418
Accounts receivable, net of allowance for doubtful accounts of \$6,088 and \$9,798, respectively	237,091	344,964
Unbilled revenue	126,252	234,053
Purchased gas adjustment receivable	—	2,785
Materials and supplies, at average cost	108,814	106,378
Fuel and natural gas inventory, at average cost	59,640	56,851
Unrealized gain on derivative instruments	16,605	54,341
Prepaid expense and other	35,655	43,046
Total current assets	599,298	883,317
Other long-term and regulatory assets:		
Regulatory asset for deferred income taxes	71,057	71,517
Power cost adjustment mechanism	4,540	4,531
Other regulatory assets	1,014,804	1,034,352
Unrealized gain on derivative instruments	2,877	8,738
Other	65,138	58,109
Total other long-term and regulatory assets	1,158,416	1,177,247
Total assets	\$ 11,337,801	\$ 11,297,080

The accompanying notes are an integral part of the financial statements.

PUGET SOUND ENERGY, INC.
CONSOLIDATED BALANCE SHEETS
(Dollars in Thousands)
(Unaudited)

CAPITALIZATION AND LIABILITIES

	September 30, 2017	December 31, 2016
Capitalization:		
Common shareholder's equity:		
Common stock \$0.01 par value, 150,000,000 shares authorized, 85,903,791 shares outstanding	\$ 859	\$ 859
Additional paid-in capital	3,275,105	3,275,105
Retained earnings	486,095	359,795
Accumulated other comprehensive income (loss), net of tax	(138,191) (145,511)
Total common shareholder's equity	3,623,868	3,490,248
Long-term debt:		
First mortgage bonds and senior notes	3,164,412	3,362,000
Pollution control bonds	161,860	161,860
Junior subordinated notes	250,000	250,000
Debt discount, issuance costs and other	(27,043) (28,974)
Total long-term debt	3,549,229	3,744,886
Total capitalization	7,173,097	7,235,134
Current liabilities:		
Accounts payable	296,659	317,043
Short-term debt	139,000	245,763
Current maturities of long-term debt	200,000	2,412
Purchased gas adjustment payable	5,784	—
Accrued expenses:		
Taxes	81,354	111,428
Salaries and wages	41,121	49,749
Interest	56,254	48,087
Unrealized loss on derivative instruments	49,820	44,170
Other	81,486	71,996
Total current liabilities	951,478	890,648
Other long-term and regulatory liabilities:		
Deferred income taxes	1,844,886	1,732,390
Unrealized loss on derivative instruments	15,578	16,261
Regulatory liabilities	610,902	653,296
Other deferred credits	741,860	769,351
Total other long-term and regulatory liabilities	3,213,226	3,171,298
Commitments and contingencies (Note 8)		
Total capitalization and liabilities	\$ 11,337,801	\$ 11,297,080

The accompanying notes are an integral part of the financial statements.

PUGET SOUND ENERGY, INC.
CONSOLIDATED STATEMENTS OF CASH FLOWS
(Dollars in Thousands)
(Unaudited)

	Nine Months Ended September 30,	
	2017	2016
Operating activities:		
Net income (loss)	\$222,846	\$256,382
Adjustments to reconcile net income (loss) to net cash provided by operating activities:		
Depreciation and amortization	355,538	328,809
Conservation amortization	85,847	77,551
Deferred income taxes and tax credits, net	109,015	116,982
Net unrealized (gain) loss on derivative instruments	23,098	(57,218)
AFUDC – equity	(11,266)	(10,769)
Funding of pension liability	(18,000)	(24,000)
Regulatory assets and liabilities	(83,370)	(138,096)
Other long-term assets and liabilities	(15,734)	34,128
Change in certain current assets and liabilities:		
Accounts receivable and unbilled revenue	215,674	175,733
Materials and supplies	(2,436)	(28,448)
Fuel and natural gas inventory	(2,789)	(3,222)
Prepayments and other	7,391	(29,352)
Purchased gas adjustment	8,569	(10,743)
Accounts payable	(31,027)	(22,874)
Taxes payable	(30,074)	(36,411)
Other	(857)	22,035
Net cash provided by (used in) operating activities	832,425	650,487
Investing activities:		
Construction expenditures – excluding equity AFUDC	(677,004)	(507,703)
Restricted cash	3,116	(1,391)
Other	6,233	2,519
Net cash provided by (used in) investing activities	(667,655)	(506,575)
Financing activities:		
Change in short-term debt, net	(106,763)	12,996
Dividends paid	(96,546)	(195,865)
Other	15,997	13,510
Net cash provided by (used in) financing activities	(187,312)	(169,359)
Net increase (decrease) in cash and cash equivalents	(22,542)	(25,447)
Cash and cash equivalents at beginning of period	28,481	41,856
Cash and cash equivalents at end of period	\$5,939	\$16,409
Supplemental cash flow information:		
Cash payments for interest (net of capitalized interest)	\$160,426	\$162,091
Cash payments (refunds) for income taxes	3,058	—
Non-cash financing and investing activities:		
Accounts payable for capital expenditures eliminated from cash flows	\$87,456	\$58,278

The accompanying notes are an integral part of the financial statements.

COMBINED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)

(1) Summary of Consolidation Policy

Basis of Presentation

Puget Energy is an energy services holding company that owns Puget Sound Energy (PSE). PSE is a public utility incorporated in the state of Washington that furnishes electric and natural gas services in a territory covering approximately 6,000 square miles, primarily in the Puget Sound region. Puget Energy also has a wholly-owned non-regulated subsidiary, named Puget LNG, LLC (Puget LNG). Puget LNG was formed on November 29, 2016, and has the sole purpose of owning, developing and financing the non-regulated activity of the Tacoma LNG facility, currently under construction. PSE and Puget LNG are considered related parties with similar ownership by Puget Energy. Therefore, capital and operating costs that occur under PSE and are allocated to Puget LNG are related party transactions by nature. As of September 30, 2017, Puget LNG has incurred \$86.5 million in construction work in progress and operating costs related to Puget LNG's portion of the Tacoma LNG facility.

In 2009, Puget Holdings, LLC (Puget Holdings), owned by a consortium of long-term infrastructure investors, completed its merger with Puget Energy (the merger). As a result of the merger, all of Puget Energy's common stock is indirectly owned by Puget Holdings. The acquisition of Puget Energy was accounted for in accordance with Financial Accounting Standards Board (FASB) Accounting Standards Codification (ASC) 805, "Business Combinations" (ASC 805), as of the date of the merger. ASC 805 requires the acquirer to recognize and measure identifiable assets acquired and liabilities assumed at fair value as of the merger date.

The consolidated financial statements of Puget Energy reflect the accounts of Puget Energy and its subsidiaries. PSE's consolidated financial statements include the accounts of PSE and its subsidiary. Puget Energy and PSE are collectively referred to herein as "the Company." The consolidated financial statements are presented after elimination of all significant intercompany items and transactions. PSE's consolidated financial statements continue to be accounted for on a historical basis and do not include any ASC 805 purchase accounting adjustments. The preparation of financial statements in conformity with U.S. Generally Accepted Accounting Principles (GAAP) requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenue and expenses during the reporting period. Actual results could differ from those estimates.

Tacoma LNG Facility

The Tacoma LNG facility will provide peak-shaving services to PSE's natural gas customers, and will provide LNG as fuel to transportation customers, particularly in the marine market. The Tacoma LNG facility is expected to be operational in 2019. Pursuant to the Washington Commission's order, Puget LNG will be allocated approximately 57.0% of the capital and operating costs of the Tacoma LNG facility and PSE will be allocated the remaining 43.0% of the capital and operating costs.

For Puget Energy, \$86.4 million in construction work in progress related to Puget LNG's portion of the Tacoma LNG facility is reported in the "Other property and investments" financial statement line item. For PSE, construction work in progress of \$76.3 million related to PSE's portion of the Tacoma LNG facility is reported in the "Utility plant - Natural gas plant" line item, as PSE is a regulated entity.

(2) New Accounting Pronouncements

Revenue Recognition

In May 2014, the FASB issued ASU No. 2014-09, "Revenue from Contracts with Customers (Topic 606)". ASU 2014-09 and the related amendments outline a single comprehensive model for use in accounting for revenue arising from contracts with customers and supersedes most current revenue recognition guidance, including industry-specific guidance. The Accounting Standards Update (ASU) is based on the principle that an entity should recognize revenue to depict the transfer of goods or services to customers in an amount that reflects the consideration to which the entity

expects to be entitled in exchange for those goods or services. The ASU also requires additional disclosure about the nature, amount, timing and uncertainty of revenue and cash flows arising from customer contracts, including significant judgments and changes in judgments and assets recognized from costs incurred to fulfill a contract. In August 2015, the FASB issued ASU 2015-14, "Revenue from Contracts with Customers (Topic 606): Deferral of the Effective Date", deferring the effective date for ASU 2014-09 to fiscal years, and interim periods within those fiscal years, beginning after December 15, 2017. In addition to the FASB's deferral decision, FASB provided reporting entities with an option to early adopt ASU 2014-09 using the original effective date.

The Company will adopt ASU 2014-09 during the first quarter of fiscal year 2018 by recognizing the cumulative effect of initially applying the new standard as an adjustment to the opening balance of retained earnings, effective January 1, 2018. In preparation for adoption of the standard, the Company has evaluated key accounting assessments related to the standard. As of the date of this report, the Company has not identified material differences in revenue recognition between current GAAP and ASU 2014-09 and as a result, the Company has not identified material cumulative adjustments necessary. The Company's primary revenue sources are from rate-regulated sales of electricity and natural gas to retail customers where revenue is recognized over time as delivered. The Company will include a change in the presentation of alternative revenue program revenue of the Company's consolidated statement of income as well as expanded disclosure around the disaggregation of revenue.

Lease Accounting

In February 2016, the FASB issued ASU 2016-02, "Leases (Topic 842)". The FASB issued this ASU to increase transparency and comparability among organizations by recognizing right-of-use (ROU) lease assets and lease liabilities on the balance sheet and disclosing key information about leasing arrangements. To meet that objective, the FASB is amending the FASB Accounting Standards Codification and creating Topic 842, Leases. ASU 2016-02 requires lessees to recognize the following for all leases (with the exception of short-term leases) at the commencement date: (i) a lease liability, which is a lessee's obligation to make lease payments arising from a lease, measured on a discounted basis; and (ii) a right-of-use asset, which is an asset that represents the lessee's right to use, or control the use of, a specified asset for the lease term. The income statement recognition is similar to existing lease accounting and is based on lease classification. Under the new guidance, lessor accounting is largely unchanged. This amendment is effective for financial statements issued for fiscal years beginning after December 15, 2018, including interim periods within those fiscal years. Earlier adoption is permitted for all entities upon issuance. Reporting entities must apply a modified retrospective approach for the adoption of the new standard. The Company will adopt ASU 2016-02 during the first quarter of fiscal year 2019 and expects the adoption of the standard will result in recognition of right-of-use assets and liabilities that have not previously been recorded, which will have a material impact on the consolidated balance sheets. The Company is considering whether the new guidance will affect the accounting for purchase power agreements, easements and rights-of-way, utility pole attachments, and other utility industry-related arrangements.

Statement of Cash Flows

In August 2016, the FASB issued ASU 2016-15, "Statement of Cash Flows (Topic 230): Classification of Certain Cash Receipts and Cash Payments". The amendments in ASU 2016-15 provide guidance for eight specific cash flow issues that include (i) debt prepayment or debt extinguishment costs, (ii) settlement of zero-coupon debt instruments, (iii) contingent consideration payments made after a business combination, (iv) proceeds from the settlement of insurance claims, (v) proceeds from the settlement of corporate-owned life insurance policies, including bank-owned life insurance policies, (vi) distribution received from equity method investees, (vii) beneficial interest in securitization transactions, and (viii) separately identifiable cash flows and application of the predominance principle. This update is effective for financial statements issued for fiscal years beginning after December 15, 2017, and interim periods within those fiscal years. Early adoption is permitted for all entities upon issuance. The amendments in this update should be applied using a retrospective transition method to each period presented. The Company will adopt ASU 2016-15 during the first quarter of fiscal year 2018 and is in the process of evaluating the impact this standard will have on its consolidated statement of cash flows.

In November 2016, the FASB issued ASU 2016-18, "Statement of Cash Flows (Topic 230): Restricted Cash". The amendments in this update require that a statement of cash flows explain the change during the period in the total of cash, cash equivalents, and amounts generally described as restricted cash or restricted cash equivalents. The new standard is effective for fiscal years beginning after December 15, 2017, and interim periods within those fiscal years. The Company will adopt ASU 2016-18 during the first quarter of fiscal year 2018 retrospectively to all periods presented and does not anticipate the new guidance will have a material impact on the consolidated statement of cash flows.

Definition of a Business

In January 2017, the FASB issued ASU 2017-01, "Business Combinations (Topic 805): Clarifying the Definition of a Business". This ASU clarifies the definition of a business by providing a screen test to determine when a set of acquired assets is not a business. The test requires that when substantially all of the fair value of the gross assets acquired (or disposed of) is concentrated in a single identifiable asset or a group of similar identifiable assets, the set of acquired assets is not a business. This test reduces the number of transactions that need to be further evaluated. This ASU affects all companies and other reporting organizations that must determine whether they have acquired or sold a business. The amendments are intended to help companies and other organizations evaluate whether transactions should be accounted for as acquisitions (or disposals) of assets or businesses.

This amendment is effective for fiscal years beginning after December 15, 2017, including interim periods within those years. The Company will adopt ASU 2017-01 during the first quarter of fiscal year 2018 and do not expect any impacts on the consolidated financial statements.

Retirement Benefits

In March 2017, the FASB issued ASU 2017-07, "Compensation - Retirement Benefits (Topic 715): Improving the Presentation of Net Periodic Pension Cost and Net Periodic Postretirement Benefit Cost". The amendments require that an employer report the service cost component in the same line items as other compensation costs arising from services rendered by the pertinent employees during the period. The other components of net benefit cost (which include interest costs, expected return on plan assets, amortization of prior service cost or credits and actuarial gains and losses) are required to be presented in the income statement separately from the service cost component and outside a subtotal of income from operations. The line item used in the income statement to present the other components of net benefit cost must be disclosed. Additionally, the service cost component of net benefit cost is the only eligible cost for capitalization.

This amendment is effective for fiscal years beginning after December 15, 2017, including interim periods within those years. Early adoption is permitted as of the beginning of an annual period for which financial statements (interim or annual) have not been issued or made available for issuance. The Company will adopt ASU 2017-07 during the first quarter of fiscal year 2018. For the periods presented in the income statement, the Company's non-service components for the nine months ended September 30, 2017, was a credit of \$13.8 million for Puget Energy and \$3.5 million for PSE. The non-service cost components are in an income position and will be presented in the other income section, upon adoption.

(3) Accounting for Derivative Instruments and Hedging Activities

PSE employs various energy portfolio optimization strategies but is not in the business of assuming risk for the purpose of realizing speculative trading revenue. The nature of serving regulated electric customers with its portfolio of owned and contracted electric generation resources exposes PSE and its customers to some volumetric and commodity price risks within the sharing mechanism of the power cost adjustment (PCA). Therefore, wholesale market transactions and PSE's related hedging strategies are focused on reducing costs and risks where feasible, thus reducing volatility of costs in the portfolio. In order to manage its exposure to the variability in future cash flows for forecasted energy transactions, PSE utilizes a programmatic hedging strategy which extends out three years. PSE's energy risk portfolio management function monitors and manages these risks using analytical models and tools. In order to manage risks effectively, PSE enters into forward physical electric and natural gas purchase and sale agreements, fixed-for-floating swap contracts, and commodity call/put options. Currently, the Company does not apply cash flow hedge accounting and therefore records all mark-to-market gains or losses through earnings. The Company manages its interest rate risk through the issuance of mostly fixed-ra