Ohio | Public Utilities Commission

Asim Z. Haque, Chairman

FILE

January 19, 2017

Docketing Division
Public Utilities Commission of Ohio
180 East Broad Street
Columbus OH 43215

RE: *In the Matter of the Application of Ohio Valley Electric Corporation for Authority to Issue and Sell Secured or Unsecured Promissory Notes, Debentures or Other Debt Securities to Borrow From or Enter into Other Financing Arrangements with the Ohio Air Quality Development Authority, Indiana Finance Authority or Other Authority, to Enter into One or More Secured or Unsecured Term Loan or Revolving Credit Arrangements and to Enter into Interest Rate Management Agreements, including Assuming Liability on Short-term Notes and Other Evidences of Short-term Indebtedness*

Dear Docketing Division:

Enclosed please find Staff's Review and Recommendation in regard to the application of Ohio Valley Electric Corporation for authority to Issue and Sell Secured or Unsecured Promissory Notes, including Assuming Liability on Short-term Notes and Other Evidences of Short-term Indebtedness for an aggregate principal amount of up to $325 million and to Enter into Interest Rate Management Agreements in Case No. 16-1969-EL-AIS.

Doris McCarter
Division Chief, Forecasting, Markets and Corporate Oversight
Rates and Analysis Department
Public Utilities Commission of Ohio

Enclosure
Cc: Parties of Record

BEFORE
THE PUBLIC UTILITIES COMMISSION OF OHIO

In the Matter of the Application of Ohio Valley Electric Corporation for Authority to Issue and Sell Secured or Unsecured Promissory Notes, Debentures or Other Debt Securities to Borrow From or Enter into Other Financing Arrangements With the Ohio Air Quality Development Authority, Indiana Finance Authority or Other Authority, to Enter into One or More Secured or Unsecured Term Loan or Revolving Credit Arrangements and To Enter into Interest Rate Management Agreements, including Assuming Liability on Short-term Notes and Other Evidences of Short-term Indebtedness	)	Case No. 16-2136-EL-AIS

Staff Review and Recommendation

APPLICATION SUMMARY:

On October 28, 2016, November 22, 2016, and December 30, 2016, Ohio Valley Electric Corporation ("OVEC") filed its Application and Exhibits, Supplemental Application, and Second Supplemental Application, respectively, in the above-captioned case (collectively hereinafter, the "Application"), pursuant to Ohio Revised Code 4905.40, 4905.42, and 4905.401 requesting Public Utilities Commission of Ohio ("Commission") authorization from January 1, 2017 to December 31, 2017 to: (a) issue and sell secured or unsecured promissory notes ("Notes") in one or more series; (b) borrow from the Ohio Air Quality Authority, the Indiana Finance Authority, or another authority through the issuance of tax exempt bonds ("Authority Bonds"); (c) enter into one or more secured or unsecured term loan or revolving credit arrangements ("Credit Facilities"); (d) issue and sell any combination of Notes and Credit Facilities, or issue the Authority Bonds or other tax exempt agency bonds from time to time for maturities with a duration of over 12 months ("Long-term Securities") up to $125 million; (e) enter into indebtedness for maturities of 12 months or under ("Short-term Securities") up to $200 million; and (f) enter into interest rate management agreements ("Interest Agreements").

REVIEW AND ANALYSIS:

OVEC proposes the Notes and the Authority Bonds to mature in not more than 30 years and to carry either a fixed interest rate, a variable interest rate or some combination thereof. The fixed rate for either Notes or Authority Bonds would be no more than 6% over the yield to maturity of comparable U.S. Treasury Bonds. The variable rate for Notes and Authority Bonds would not exceed 9% during the initial period and would be no more than 4% over the LIBOR[1] over the life of the Notes. The arrangement fees would not exceed 3% for Notes or 4% for Authority Bonds. In the event that variable rate Authority Bonds are issued, OVEC requests the authority to enter into one or more bank liquidity facilities with a bank or banks at a fee which would not exceed 6%.

OVEC proposes the Credit Facilities to be issued for periods of not more than 10 years. The interest rates applicable to any of the Credit Facilities would not exceed: (a) the most recent LIBOR plus 4.5%; (b) the then offered rate for certificate of deposit by a selected U.S. major money center bank plus 4.5%; or (c) the prime rate of a selected U.S. major money center bank plus 3.5%. The commitment or facility fees would not exceed 1.5% and other fees and commissions would not exceed 4% on such Credit Facilities.

The parameters OVEC proposes for its Long-term Securities are higher than the parameters the Commission granted to OVEC for issuing Long-term Securities in Case No. 15-1657-EL-AIS. The higher proposed fixed rate cap is meant to provide flexibility for a range of possible outcomes and market conditions during the authorization period especially in the light of recent ratings decisions concerning OVEC. The Moody's Investors Service and Fitch Ratings, Inc. credit rating agencies have placed OVEC's credit rating under review for possible downgrade. Their actions follow the downgrade of FirstEnergy Corp.'s (FE) subsidiaries, FirstEnergy Solutions Corp. (FES) and Allegheny Energy Supply Company (AES),[2] which together are contractually obligated under the Inter-Company Power Agreement with OVEC to cover about 8% (comprised of 4.85% from FES and 3.01% from AES) of OVEC's expenditure.

OVEC proposes to use the proceeds of the $125 million Long-term Securities to extend three letters of credit in 2017, the details of which are as follows: (a) a $25 million letter of credit, expiring February 12 , 2017, that enhances the credit rating of the OVEC $25 million 2009A Ohio Air Quality Development Authority (OAQDA) tax exempt bonds at a lower interest rate than OVEC issued debt; (b) a $50 million letter of credit from,

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[1] London Interbank Offered Rate

[2] The downgrade of FES reflects FirstEnergy management's announcement that it would exit the merchant business entirely within 18 months, even if that required a restructuring or bankruptcy filing.

expiring June 28, 2017, that enhances the credit rating of the OVEC $50 million 2012C Indiana Finance Authority (IFA) tax exempt bonds at a lower interest rate than OVEC issued debt; and (c) a $50 million bank agreement, expiring June 29, 2017, that holds the OVEC $50 million 2010A Indiana Finance Authority (IFA) tax exempt bonds at a lower interest rate than OVEC issued debt.

In the Application, OVEC has requested authority to issue Short-term Securities of up to $200 million, an amount that exceeds its Statutory Exemption limit. As of September 30, 2016, OVEC could borrow up to $72 million under the Statutory Exemption limit, and therefore OVEC requires Commission approval to borrow in excess of this Statutory Exemption amount. OVEC also proposes to use the proceeds of the $200 million Short-term Securities to: (a) finance coal, reagent, environmental allowance costs, material and supplies for Kyger Creek and Clifty Creek Plants, and pay general obligations; and (b) fund working capital and general corporate purposes.

OVEC is also requesting Commission authorization to utilize Interest Agreements to lower its overall effective interest costs. The fees and commissions on such Interest Agreements would not exceed 2% of the amount of the underlying obligation. In general, there would be no proceeds associated with the Interest Agreements since no new obligations are created in this connection.

Staff notes that the proposed financing would not create any change in the capitalization structure of OVEC on a pro forma basis.

Capitalization Structure (current and Pro-forma)

	Actual 06/30/2016 ($millions)	**(%)**	**Pro-forma* Date of issue ($millions)**	**(%)**
Long-Term Debt	$ 1,205	98.5	$ 1,205	98.5
Common Equity	$ 18	1.5	$ 18	1.5
Total Capitalization	$ 1,223	100.0	$ 1,223	100.0

- *Pro forma reflects the issuance of New Debt of $125 million and using the proceeds to replace existing three letters of credit of $125 million.*

RECOMMENDATION:

Upon review of the Application, Staff recommends Commission approval of OVEC's request to issue and sell Notes; borrow Authority Bonds; issue Long-term Securities; and enter into Credit Facilities, Short-term Facilities, and Interest Agreements.