3

Ohio | Public Utilities Commission

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FILE

April 8, 2019

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

RE: *In the Matter of the Application of the Dayton Power and Light Company for Authority to Issue and Sell an Amount Not to Exceed $425 Million of First Mortgage Bonds, Debentures, Notes, or Other Evidences of Indebtedness or Unsecured Notes, Case No. 18-1795-EL-AIS*

Dear Docketing Division:

Enclosed please find the Staff's Review and Recommendations in regard to the Application of the Dayton Power and Light Company for authority to issue, sell or enter into long-term debt transactions, Case No. 18-1795-EL-AIS.

James Zell

James Zell
Section Chief, Financial Analysis Section
Public Utilities Commission of Ohio

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Enclosure
Cc: Parties of Record

BEFORE
THE PUBLIC UTILITIES COMMISSION OF OHIO

In the Matter of the Application of the Dayton Power and Light Company for Authority to Issue and Sell an Amount Not to Exceed $425 Million of First Mortgage Bonds, Debentures, Notes, or Other Evidences of Indebtedness or Unsecured Notes.	)	Case No. 18-1795-EL-AIS

Staff Review and Recommendation

APPLICATION DESCRIPTION

The Dayton Power and Light Company ("DP&L" or the "Company") filed an application on December 4, 2018; it subsequently amended its application on February 6 and March 14, 2019. Together, the applications and exhibits (collectively, "Application"), were filed pursuant to Ohio Revised Code sections 4905.40 and 4905.41, requesting Public Utilities Commission of Ohio ("Commission") authorization to issue and sell debt securities. The Company seeks to issue up to $425 million principal amount of First Mortgage Bonds, debentures, notes, and/or other evidences of indebtedness, in one or more series ("New Bonds"), from time to time, over a period ending December 31, 2019.

The New Bonds will be issued with the following parameters: (a) an offering price between 96% and 100% of the principal amount; (b) an interest rate (either fixed or variable) which will result in a yield to maturity not to exceed 5.75%; and (c) the commission payable to agents or underwriters will not exceed 1.25% of the principal amount of the New Bonds. It is anticipated that the New Bonds will have a term to maturity of not more than 40 years.

The Company will apply the proceeds from the sale of the New Bonds, in addition to funds from operations, to refinance its existing $436.1 million of outstanding Term Loan B issue ("Term Loan B Facility"). The refinancing is to be facilitated either by repayment or call. The Application includes $7 million in estimated commissions, fees, and other underwriting expenses.

DP&L's Term Loan B Facility originated during a period when the Company was non-investment grade. Since completing the transfer of its generation assets, as required by the

Commission,[1] subsequent credit upgrades by the ratings agencies now allow DP&L to access the investment grade debt market. The Company anticipates that this will permit the placement of longer term debt with favorable terms. In addition, at the time of the refinancing, DP&L intends to pay off a portion of the Term Loan B Facility to lower its debt leverage.

REVIEW AND ANALYSIS

DP&L proposes to use the proceeds from the New Bonds to refinance its Term Loan B Facility. The New Bonds will be secured, First Mortgage Bonds, for terms not to exceed 40 years. By way of contrast, the Term Loan B Facility is debt with less than a three-and-one-half-year term remaining (August 2022). It was issued when the Company's financial difficulties precluded an investment grade rating. It is reasonable to assert that financing long lived assets with long term financing is common industry practice and that approval of a term up to forty years provides DP&L with flexibility.

It is the Company's intent that the New Bonds will be offered with a coupon interest rate that is fixed. The Term Loan B Facility has a variable coupon rate tied to a short term benchmark interest rate that has risen in the past. DP&L anticipates a rising interest rate environment. DP&L anticipates that the proposed transaction will replace the existing variable rate on the shorter-term Term Loan B Facility (recently 3.57%-4.82%) with longer dated debt carrying a comparable coupon rate. This aspect of the Application may be viewed favorably as this removes some of the interest rate risk associated with the variable rate, short dated, Term Loan B Facility.

The Application contemplates issuing the New Bonds in either one series or multiple series with the aggregate total not to exceed $425 million. A single series issued in the public market allows the bonds to be "Index Eligible" and thus enable them to be sold to a broader investor base, according to the Company.

The Company examined private debt issuance as an alternative to issuing the New Bonds in the public market. It was determined that current financing costs in the private market are comparable to those available in the public market.[2] A private debt issuance would also enable DP&L to issue the New Bonds in multiple series, which would yield a favorable maturity profile. However, Staff noted that in the private market being considered there are provisions establishing a potential calling of the bonds in the event of a change of control or cross-default.

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[1] See *In the Matter of the Application of The Dayton Power and Light Company for Authority to Transfer or Sell its Generation Assets,* Case No. 13-2420-EL-UNC, Finding and Order (September 17, 2014).

[2] According to confidential indicative pricing sheets provided to DP&L by the Company's bank advisors during Staff's investigation.

The following table summarizes the pro forma capitalization of the Company giving effect to the refinancing and the concurrent repayment of $18.1 million of the Term Loan B Facility.*

	Actual 12/31/2018 ($ 000s)	**(%)**	**Pro Forma 03/31/2019 ($ 000s)**	**(%)**
Long Term Debt	$ 593,773	57.2%	$ 583,000	55.7%
Common Equity	$ 445,143	42.8%	$ 463,000	44.3%
Total Capitalization	$ 1,038,916	100.0%	$ 1,046,000	100.0%

* *Totals reflect expected operating results, issuance costs, and other adjustments in addition to the issuance of $425 million in New Bonds and repayment of $18.1 million of the Term Loan B Facility.*

As shown on a pro forma basis, the proposed financing will modestly improve the Company's capital structure.

RECOMMENDATION

Upon review of the Application and supporting documentation including responses to data requests, Staff believes DP&L's request appears reasonable and recommends approval of the Company's request to refinance the Term Loan B Facility. Staff recognizes that both of the financing methods DP&L has contemplated in the Application have merits. However, Staff believes a public market issuance with a fixed term in a single maturity may provide DP&L the best overall financing result. Staff bases its opinion on the anticipated pricing of a public issuance in a single series in addition to having the ability to negotiate terms that do not include change of control or cross-default provisions.

Staff further recommends the Commission direct DP&L to file a summary report in this case docket that details all the terms and covenants of the New Bonds within 30 days of issuance.