

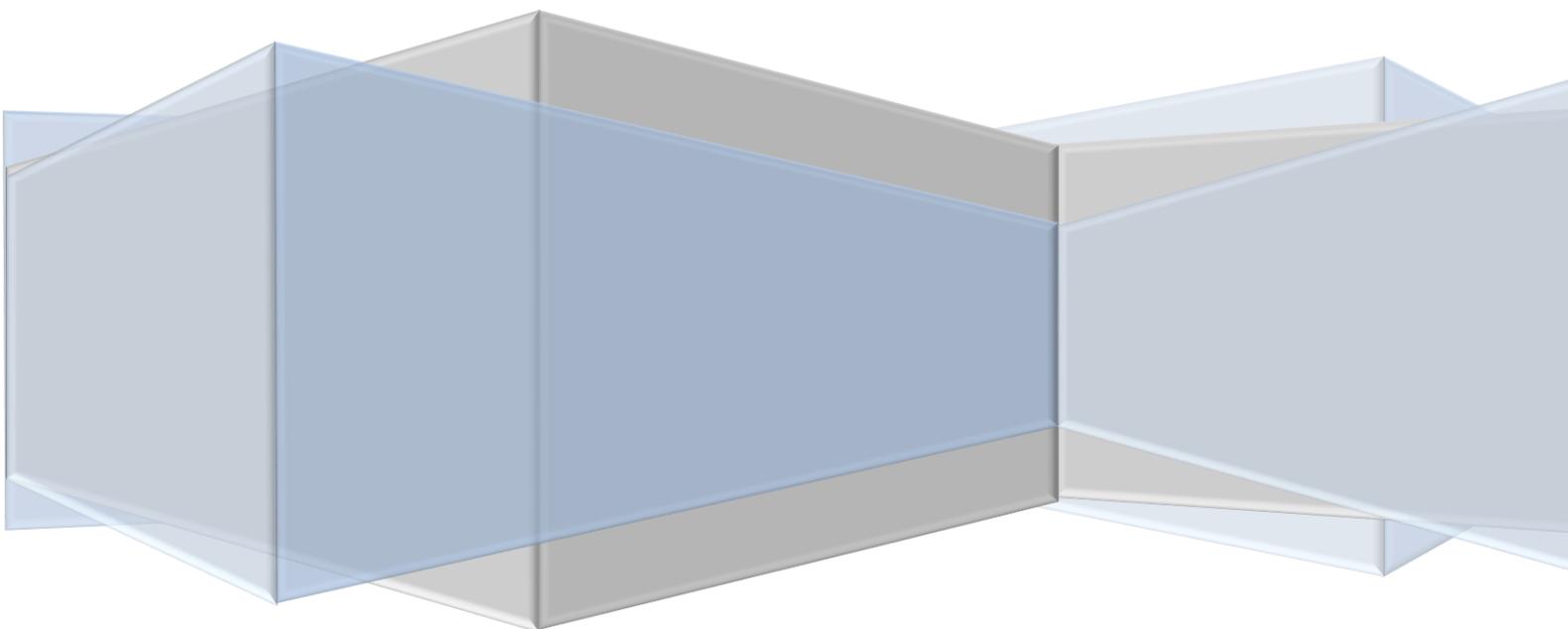


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Analysis of Ohio Power Co. Structuring And Pricing of \$267,408,000 Ohio Phase-In Recovery Bonds

Public Utilities Commission of Ohio Case No. 12-1969-EL-ATS



EXECUTIVE SUMMARY

- Ohio Power Co. (OPCo or the Company) ratepayers will pay **at least an additional \$3 million in interest and fees** on the \$267,408,000 Phase-In Recovery Bonds (PIR Bonds) sold on July 23, 2013. Analyzing the “lessons learned” from this transaction will be useful and will help prevent this outcome from becoming accepted precedent that raises ratepayer costs for future utility securitizations.
- Because these bond issues are complex, the Public Utilities Commission of Ohio (PUCO) retained independent financial advisors, Public Resources Advisory Group and Oxford Advisors (PRAG–Oxford), to “serve as joint decision maker [with the issuer] on all matters related to structure, pricing and marketing of the bonds.”¹
 - PRAG is a top rated general municipal bond advisor, and of the 45 corporate utility securitizations sold since 2000, has been an advisor for one in 2007.
 - Oxford has not been involved in any previous corporate utility securitization.
- To provide transparency and accountability, PUCO directed its advisors to issue a [public report on the bond issue](#), with specific attestations concerning the pricing relative to comparable securities. The docket is open for public comment and this analysis is responsive to PUCO’s requests.
- While the bond coupons benefited from extraordinarily low US Treasury benchmark rates, a conservative analysis of the report reveals that PRAG–Oxford made or recommended decisions on the structuring, marketing and pricing of the PIR Bonds that will cost Ohio ratepayers the following:
 - At least **\$1.3 million in higher interest expense** caused primarily by the decision to sell two tranches of PIR Bonds with 2.25-year and 5.08-year weighted average lives (WALs) instead of one tranche as had been correctly recommended by the underwriters with a 3.34-year WAL and the same amortization schedule. This also appears to have been caused in part by PRAG–Oxford’s use of unusual and inappropriate bond “comparables” in its analysis and decision-making process, *i.e.*, comparing the highest quality PIR Bonds to lesser quality auto loans and floor lease asset backed securities (ABS) that have higher credit spreads and interest rates. For more than 10 years, fixed income research departments, rating agency and other market participants have more appropriately compared utility securitization bonds to AAA-rated credit card ABS or traditional high quality utility bonds.² We know of no published reports from any source that compare these bonds credit quality and structure to the securities identified by PRAG–Oxford. These inappropriate comparisons, presumably used by PRAG–Oxford in negotiations with underwriters and investors in selling the bonds, appear to have led to higher PIR Bond interest rates for OPCo customers.
 - Up to **\$1.6 million in excess servicing costs** for the PIR Bonds under the servicing agreement negotiated and approved by PRAG–Oxford with OPCo. Contrary to established market precedent since 2007, PRAG–Oxford approved annual servicing costs of 10 basis points (0.10%) of the initial principal amount, which were double the 5 basis points (0.05%) most common on other utility securitization deals, both larger and smaller. Furthermore, PRAG–Oxford did not require that any fees exceeding the Company’s demonstrable incremental PIR Bond servicing costs (over costs already recovered in other rates and charges imposed by OPCo) be credited back to Ohio ratepayers. This provision had been included in other utility securitizations, including those by other subsidiaries of OPCo’s parent company, American Electric Power Company.

¹ Saber Partners, LLC has served in this role for five state public utility commissions and on 11 bond offerings of approximately \$8 billion in bonds. See [market list of utility securitizations](#), [Saber engagements](#) and [Saber clients’ testimonials](#).

² See “Absolute Value: Rate Reduction Bond ABS Primer” Wells Fargo Securities, July 17, 2013. See also, Citigroup, “US Fixed Income Strategy – Consumer ABS” August 18, 2006 and Citigroup Research Report (SalomonSmith Barney), “Asset-Backed Global Power/Stranded Asset Roundup,” January 9, 2002.

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Introduction

The PUCO's financing order required the PIR Bonds to be priced to "reflect a market price of most recently issued comparable securities" and to be "consistent with market conditions" at the time of pricing. In furtherance of the PUCO's efforts to achieve transparency and accountability to protect ratepayers while respecting shareholder rights, we have analyzed the reasonableness of the structuring and pricing of the PIR Bonds³ based solely on publicly available information. No part of this analysis is based on "after-the-fact" information.

Unlike other utility bond offerings, every dollar spent in this transaction is a ratepayer dollar. It is important to analyze and discuss these issues to establish "lessons learned" and to prevent these issues from becoming accepted precedent, especially in connection with any future PIR Bonds issued in Ohio.

In finance, the price any new issue of bonds can only be evaluated by examining the "credit" or "pricing" spread of the bonds over established market benchmarks, such as US Treasuries or swap⁴ rates. This is because, while the level of the benchmark rate is not in control of market participants, at least to some extent the spread is. Simply looking at the coupon or yield, which is the combination of the benchmark plus the spread, can be misleading because most of the coupon (the benchmark) is not affected by negotiations with the market. The credit spread or pricing over the appropriate benchmark, however, is.

The following analysis of the PRAG-Oxford report first discusses their structuring decision of whether to issue a one or two tranche transaction based on the interest rate environment at the time. We then analyze the credit and pricing spread issues of comparable securities used by experienced market professionals and those used by PRAG-Oxford. The analysis continues with a review of the role of marketing in achieving a best execution transaction that protects ratepayers and is fair to investors based on specific precedents in the utility securitization market. We conclude with a discussion of one of the key on-going costs of the transaction also compared to other utility securitizations.

Our analysis shows that, while the coupon rates benefitted from the continuing low benchmark interest rate environment as expected⁵, the PIR Bonds were mis-structured and mispriced. In addition, it appears that provisions in the Servicing Agreement relating to certain upfront and ongoing costs were needlessly costly to ratepayers.

PRAG-Oxford's Recommendation of a Two-Tranche Structure

One of the most troubling aspects of the OPCo PIR Bond sale concerns the structuring of the deal into two tranches⁶ rather than one. This caused the bond sale to use a higher

³ The most direct source of information concerning the circumstances under which the PIR Bonds were priced is the PRAG-Oxford report. This was required by PUCO's financing order and is publicly available on the PUCO website under [Case No. 12-1969-EL-ATS](#). In that report, PRAG-Oxford attests that they "participated fully with the Applicant [Ohio Power] . . . as a co-equal in all plans and decisions related to pricing, marketing and structuring of the PIR Bonds". Pricing and other information related to cash flows and tranche credit spreads are on file with the SEC (see OpCo [Prospectus Supplement](#)).

⁴ A common benchmark rate based on LIBOR (London Inter-Bank Offered Rate).

⁵ See Saber [report](#) of May 21, 2013

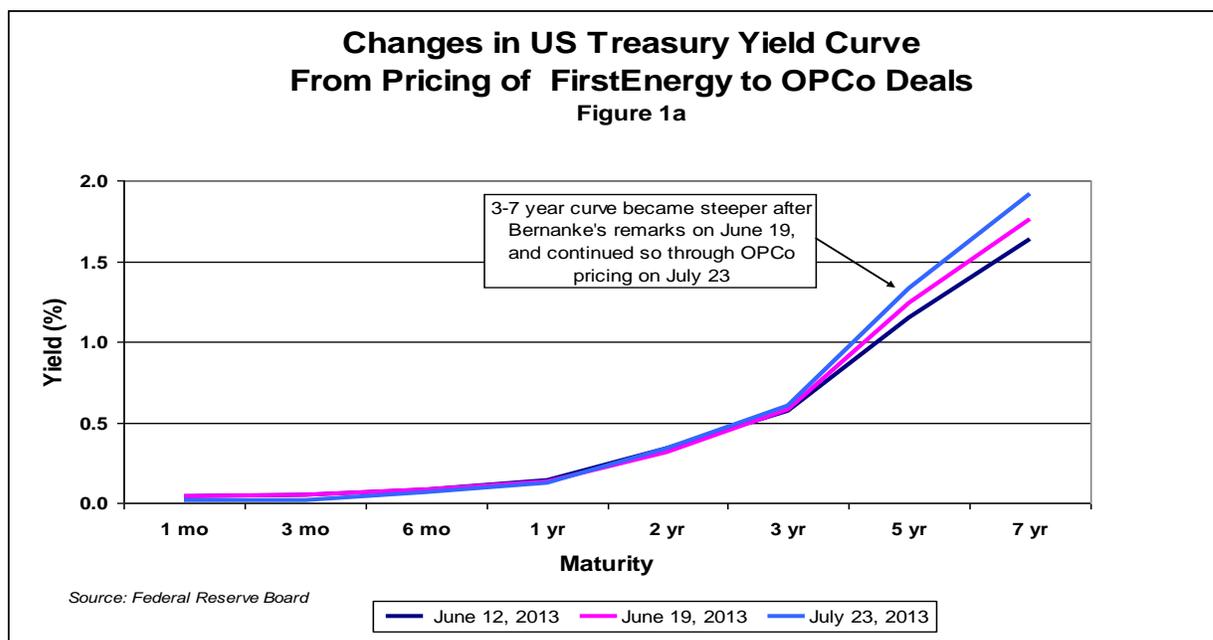
⁶ A "tranche" is similar to a separate class of bonds with its own separate interest rate and maturity/repayment schedule.

benchmark and pricing spread. PRAG-Oxford states in their report that “the underwriters had proposed a single pass-through tranche but PRAG-Oxford requested early in the market discussions that they [the underwriters] continue to evaluate a 2-tranche structure,” which is the structure that was ultimately used.⁷

The PRAG-Oxford report goes on to say that “due to the steepening of the yield curve and changing market conditions, the 2-tranche structure did provide a lower borrowing cost and greater savings for the ratepayers.” However, there is no analysis in the PRAG-Oxford report supporting this claim.

In fact, the evidence cited in the PRAG-Oxford report for a “steepening of the yield curve and changing market conditions” was the rise in yields of 10-year Treasury bonds following comments by Federal Reserve Chairman Ben Bernanke on June 19, 2013 about future Federal Reserve open market bond purchases.

While interesting, the chart in the PRAG-Oxford report showing the rise in 10-year Treasury yields is misleading in the context of PIR Bonds. OPCo bonds have much shorter maturities than 10-year Treasury bonds. As seen in **Figures 1a and 1b**, there was little or no steepening of the yield curve for securities due in three years or earlier.



⁷ The Company had proposed to use a 2-tranche structure under different market conditions. See p. 10 of the financing order: “Ohio Power explains that it will issue two specific tranches (classes) of bonds with different fixed interest rates and maturity dates. Tranche A-1 will be in the amount of \$149,000,000 with a proposed interest rate of .58 percent and an expected maturity of 3.71 years. Tranche A-2 will be in the amount of \$149,018,000 with a proposed interest rate of 1.55 percent and an expected maturity of 6.71 years.” (Ohio Power, Revised Ex. C, March 12, 2013) According to the PRAG-Oxford report, the underwriters prudently suggested changing to a one-tranche structure, but appear to have been overruled by PRAG-Oxford.

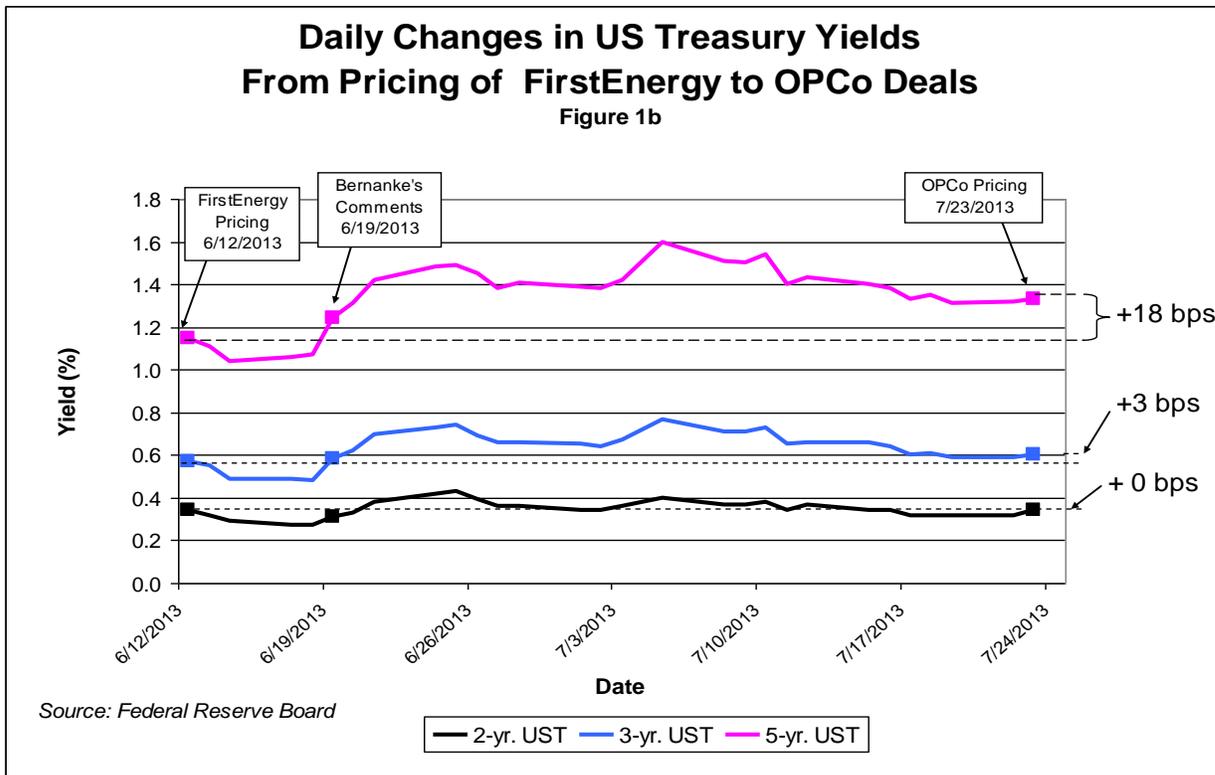
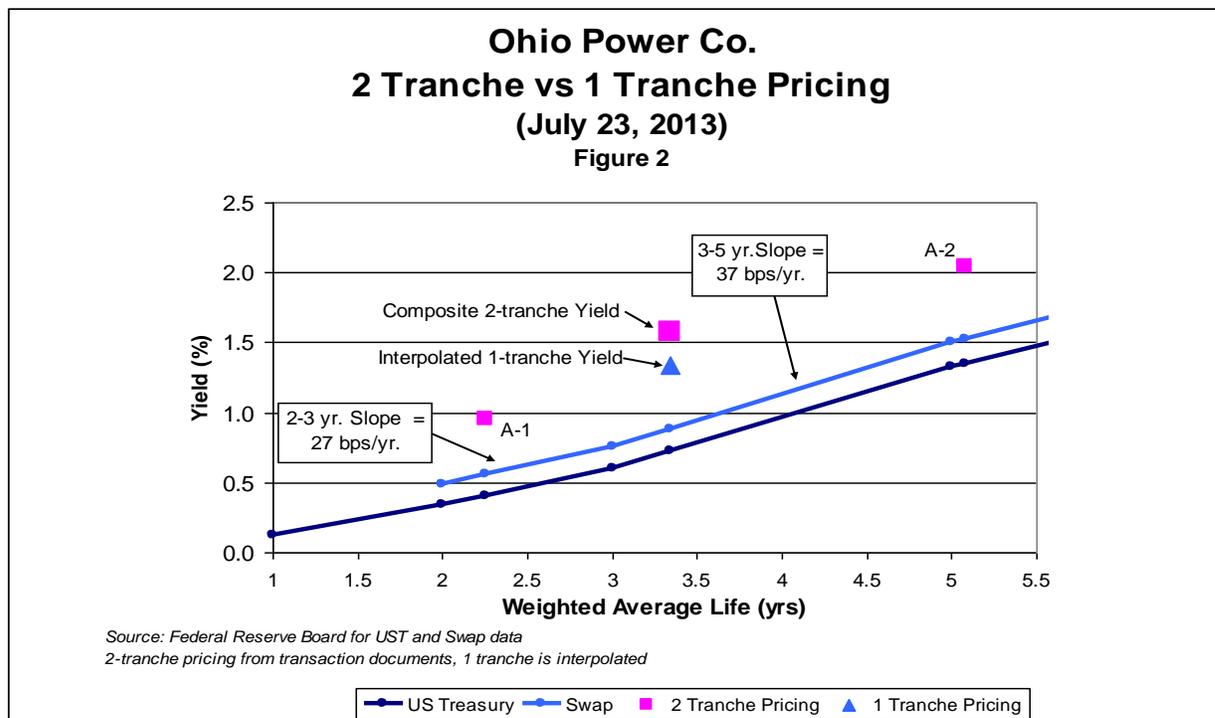


Figure 2, below, shows the yield curves for both US Treasuries and swaps for 2 to greater than 5 years on the day of pricing, July 23. The slope of the swap curve is significantly steeper from 3 to 5 years than from 2 to 3 years (+37 vs. +27 basis points⁸ (bps)/year).

Pricing a single tranche of PIR Bonds at a 3.34-year WAL between OPCo’s 2.25 and 5.08 year WALs *could have avoided* most of the steeper part of the curve. Ratepayer costs could have been reduced by concentrating on market demand from investors preferring three-year securities, like AAA-rated credit card ABS, U.S. agency debt or highly-rated electric utility bonds . . . *without any change* to the scheduled amortization which is the most significant factor affecting the customer’s bill.

⁸ A basis point equals 1/100th of 1%.



Estimating the Yield for Single-Tranche Alternative on July 23, 2013

Using standard market conventions and only information available at the time of pricing (i.e., nothing after-the-fact), it is possible to calculate how a single tranche deal might have been priced. We can thereby estimate the savings that could have been achieved through a single tranche structure.

If OPCo's PIR Bonds had been structured with a single tranche, that single tranche would have had a 3.34-year WAL. It is important to note that the single tranche PIR Bond issue would have required *no change in the schedule of principal payments* from the two-tranche structure.

Using standard market conventions, the yield on this one-tranche structure can then be compared to the actual yield for the 2-tranche OPCo PIR Bond structure. One standard market convention for securitized utility bonds is to develop pricing benchmarks based on the Federal Reserve's Treasury and swap yield curve data on the date of pricing. Another standard market convention is to interpolate on a straight-line basis between actual Treasuries and swap yield data available on the pricing date.

- (i) On July 23, 2013 (the PIR Bond pricing date and according to the pricing memorandum filed by OPCo with the SEC), the swap benchmark rate at 3 years was 0.76% and at 5 years was 1.5%. By interpolation, the swap benchmark rate at 3.34 years was 0.886%.
- (ii) The pricing spread for the A-1 tranche of OPCo's PIR Bonds over interpolated swaps was +40 bps at 2.25 years and for the A-2 tranche was +52 bps over

interpolated swaps at 5.08 years.⁹ **The pricing spread over interpolated benchmark swaps at 3.34 years was therefore 45 bps** (rounding up).

- (iii) 0.886% plus 45 bps (line (i) + line (ii)) produces a yield of 1.336% for a single tranche PIR Bond deal.
- (iv) The PRAG-Oxford report states that the composite rate for the two-tranche deal was 1.580%.¹⁰
- (v) The difference between the 2-tranche yield of 1.58% and the 1-tranche yield of 1.336% is a savings of 0.244% (line (iv) – line (iii)). **That is more than 24 bps savings.**
- (vi) The yield differential times the principal amount times the years outstanding (*i.e.*, WAL) gives a **nominal savings of \$2,177,692.**

⁹ Pricing Term Sheet dated July 23, 2013.
http://www.sec.gov/Archives/edgar/data/1577459/000090514813000747/efc13-465_fwp.htm .

¹⁰ This was verified (roughly) in Table 1, below.

The calculation of single tranche pricing for OPCo's PIR Bonds and forgone savings is shown in **Table 1**, below:

Forgone Savings in OPCo				
2-Tranche Pricing vs. Interpolated Single-Tranche Pricing				
Table 1				
RRB Extrapolated Yield Curve				
Maturity (yrs)	Swap Yield (%)	Pricing Spread (%)	Yield (%)	
2.00	0.490			
2.25	0.558	0.40	0.958	A-1 Tranche yield
3.00	0.760			
3.34	0.886	0.45	1.336	Possible single tranche pricing
5.00	1.500			
5.08	1.528	0.52	2.048	A-2 Tranche yield
7.00	2.120			
Composite Yield for 2-tranche deal			1.580	Wtd. Avg. Yield
interpolated				
Check Composite Yield for 2-tranche deal				
Maturity (yrs.)	Principal Amt. (\$)	PA * WAL (\$ - years)	Yield Calc. Check (%)	
2.25	164,900,000	371,025,000	0.958	
5.08	102,508,000	520,740,640	2.048	
Wtd. Avg	3.34	267,408,000	891,765,640	1.594
Forgone savings				
			Yield (%)	
			2-tranche deal	1.580
			1-tranche deal	1.336
			yield savings	0.244
				x P.A x WAL
			= Nominal \$ Savings	\$ 2,177,692
Sources: Swap spreads from Federal Reserve Board 2-tranche pricing spreads, composite 2-tranche yield, WALs and principal amounts from PRAG Letter				

Single-Tranche Has Savings, Even After Adjustment for Market Judgments

As described in more detail below, only a limited marketing or sales effort was undertaken after filing of the registration statement and preliminary prospectus on May 21, 2013 in connection with OPCo's PIR Bonds. With such short and limited efforts to identify, contact and communicate with investors, it *may* not have been possible to achieve all the savings assumed in the calculations in Table 1 due to the longer payment window (the period during which principal is being repaid) inherent in a single tranche structure. Generally, shorter payment windows are more attractive to investors, which encourage them to accept lower yields. Yet, single-tranche utility securitizations are unusual, but not unheard of, especially for deals with shorter WALs and relatively small principal amounts.

For example, on **August 11, 2010**, Entergy Arkansas Restoration Funding, LLC (Morgan Stanley Lead Underwriter) issued \$124.1 million of Storm Recovery Bonds in a single tranche with a WAL of 5.44 years, a repayment window of 9.5 years and a pricing spread of +55 basis points to swaps. For OpCo, the repayment window of 5.5 years was narrower than the Entergy Arkansas sale, whether OPCo was structured with one tranche or two.¹¹

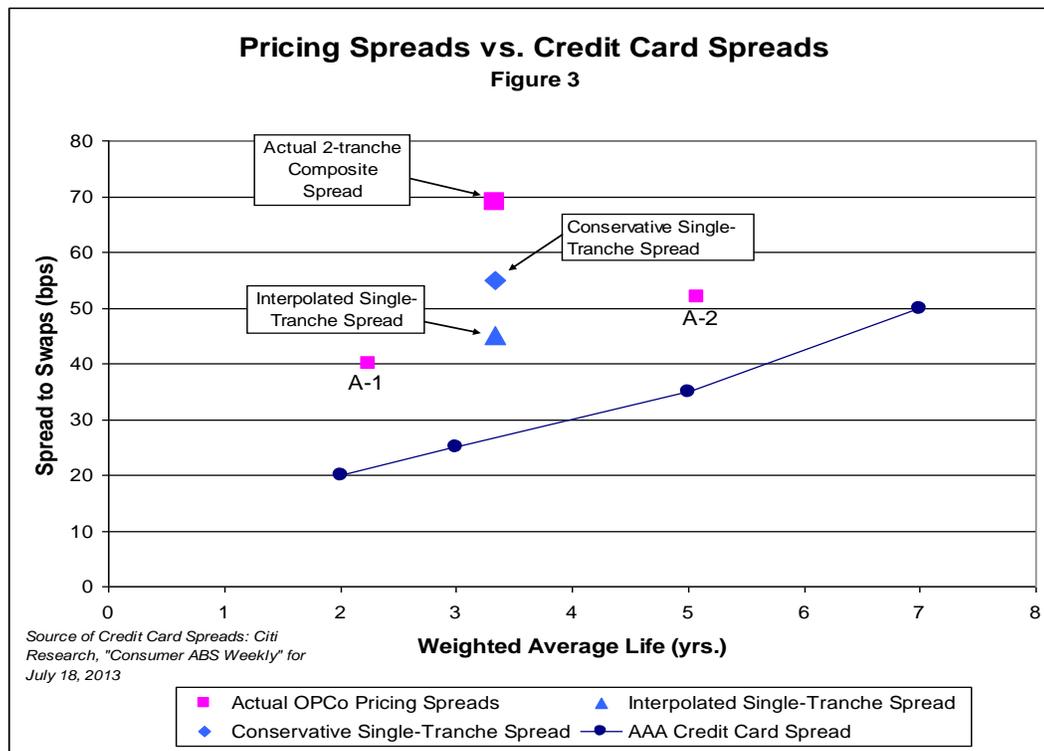
As Table 1 showed, at the time of the OPCo sale, a straight interpolation shows a swap benchmark rate of 0.896% and a pricing/credit spread of +45 bps.

To be conservative, because of the difference between the WAL and the longest possible maturity, we used an additional spread premium of 10 bps as a “fair value” adjustment to the credit spread.

Thus, a 3.34-year swap rate of 0.886% plus a 0.55% (45 bps + 10 bps) credit spread yields a conservatively estimated single-tranche rate of 1.436%. Comparing this to the actual composite rate of 1.58% resulting from the two-tranche structure **still yields a savings of over 14 bps, which translates to nominal interest savings of \$1,285,926.**

The savings from using a single tranche structure is robust: the pricing spread would need to have increased to an unlikely +69 bps rather than +45-55 bps before the savings from a single-tranche structure would have been eliminated. Given the relationship to AAA-rated credit card ABS spreads shown in **Figure 3**, it does not seem plausible that a single-tranche PIR Bond deal would have required a +69 bps pricing spread to attract investors.

¹¹ Sometimes even multi-tranche deals have longer payment windows. For example, on January 29, 2008 CenterPoint Energy priced utility securitization bonds in a 2-tranche structure where the A-1 tranche (\$301 million principal) had a WAL of 5.0 years with a payment window of 8 years. On April 3, 2007 Allegheny Energy (subsidiaries Monongahela and Potomac Edison) priced a 4-tranche deal where the A-1 tranche had a 4-year WAL with a 7-year payment window at spreads *below* credit cards. Saber Partners was the Commission’s advisor on that transaction.



Is PRAG-Oxford's Attestation of "Price Consistent With Market Conditions" Reasonable?

PRAG-Oxford seem to have ignored market research (including that of the underwriters as discussed below) and precedents in their analysis of the PIR Bonds' pricing.¹²

In discussing the pricing of the PIR Bonds, the PUCO's advisors asserted they negotiated narrower spreads than first proposed by underwriters. Those statements rely wholly on the indications of underwriters with no fiduciary duty to the issuer/ratepayers, and are no substitute for an independent, rigorous evaluation of relevant comparable securities, pricing of previous issues and investor preferences. In anticipation of tough negotiations, investment banks commonly propose "generous" spreads so that even if after negotiations result in a spread reduction, the bonds still carry a higher-than-necessary credit spread making the sale easier.

In discussing the A-1 tranche having priced at credit spread of +40 bps over swaps, PRAG-Oxford asserts that the pricing "conforms to the broader Asset Backed Securities ('ABS') new issuance market of utility securitization, prime auto, and auto lease 'ABS.'" They point to "the significant increase in credit spreads" since the FirstEnergy transaction on June 12 (the most recent utility securitization transaction), in addition to the difference in WAL, to explain why the A-1 tranche was priced at 40 bps over swaps, whereas the FirstEnergy A-1 tranche was priced at just 25 bps over the benchmark rate. However, the

¹² See the pricing of PSE&G Transition Funding II, LLC, MP Environmental Funding, LLC, PE Environmental Funding, LLC and FPL Recovery Funding, LLC.

FirstEnergy A-1 tranche benchmark was not the swap curve but the Eurodollar Synthetic Forward (EDSF), so the pricing spread is not strictly comparable.

More importantly, experienced market participants do not view AAA rated auto ABS as the best “comparable securities” to AAA-rated utility bonds like the PIR Bonds. More typically and more appropriately, as numerous fixed income research, rating agency and other market participants have stated for more than 10 years, utility securitization bonds are most comparable to AAA-rated credit card ABS or traditional high quality utility bonds as well as U.S. agencies.¹³ We know of no published reports from any source that compare securitized utility bonds to the securities identified by PRAG-Oxford.

This incorrect selection of comparables makes a material difference to ratepayers.

Table 2, below, shows the difference between yields on AAA-rated auto loan and AAA-rated credit card ABS securities from June 12, 2013, when the FirstEnergy transaction was priced, to July 23, 2013, when OPCo’s PIR Bonds were priced. While AAA-rated credit card ABS spreads to swaps increased by 10-12 bps in the 2-3 year range (comparable to the A-1 tranche WAL of 2.25 years), AAA-rated auto loan ABS spreads increased by 16-18 bps. Thus, by benchmarking against inappropriate “comparables,” the PRAG-Oxford report exaggerated the extent of the increase in credit spreads since the FirstEnergy sale, thus laying the groundwork for mispricing the PIR Bonds.

Credit Spreads for Auto Loan ABS vs. Credit Card ABS Spread to Swaps (bps)					
Table 2					
	AAA Auto Loan ABS		AAA Credit Cards		
	2-year	3-year	2-year	3-year	5-year
June 6, 2013	12	17	10	13	25
July 18, 2013	28	35	20	25	35
Increase	16	18	10	12	10

Source: “Consumer ABS Weekly,” Citigroup Research, July 18, 2013

In discussing the A-2 tranche, PRAG-Oxford takes credit for reducing the underwriters’ initial spread recommendation from +60-65 bps downward to +52 bps. The FirstEnergy A-2 tranche with a similar 5.1-year WAL priced at +40 bps. PRAG-Oxford attributes the increased spread over the FirstEnergy deal to the “considerable movement in the public credit markets,” although the 5-year credit card ABS spread only increased by 10 bps (from +25 to +35 bps) from June 6 to July 18. They also say that their A-2 pricing “conforms to the broader ABS new issuance market of utility securitization and prime auto ABS,” even though there are no 5-year AAA-rated auto ABS issuances with which to compare. Citigroup’s Fixed

¹³ See “Absolute Value: Rate Reduction Bond ABS Primer” Wells Fargo Securities, July 17, 2013. See also, Citigroup, “US Fixed Income Strategy – Consumer ABS” August 18, 2006 and Citigroup Research Report (SalomonSmith Barney), “Asset-Backed Global Power/Stranded Asset Roundup,” January 9, 2002.

Income Research Department does not provide even indicative levels for 5-year auto ABS, although they do so for credit card ABS and utility securitizations (which they refer to as “stranded asset” bonds).¹⁴

The PRAG-Oxford report also states “when PRAG-Oxford pressed the underwriters to lower the spread by another 1-2 bps on the day of pricing, we were informed that the transaction could not handle any additional reduction in spread.” In a negotiated transaction, underwriters may say this, but the proof would be to see the composition of orders from all underwriters with additional due diligence. Was there a written marketing plan? Did co-managers or just the lead managers receive orders? How were the orders distributed? What type of buyers? Were there “crossover” buyers as noted by Citi in the 2008 deal? Is the deal 100% or more “subscribed” at that point, or do the underwriters might still have to actually underwrite some portion of the deal at the time it was priced?

If marketing was limited (offering to a select few buyers favored by the underwriters) and produced only a few investors in the book (e.g., less than 5-10), then that is a self-imposed risk. Broad participation and competition is necessary to avoid a few investors driving the pricing higher.

If the deal is 100% sold and the underwriters do not take any risk of underwriting, then it cannot be said with confidence that the “transaction cannot handle any additional reduction” of even a basis point or two. It is not unusual for underwriters to actually underwrite 5-15% of a transaction in order to achieve efficient pricing without overpaying all investors in the book of orders.

The PRAG-Oxford report does not say if the underwriters actually underwrote any of the PIR Bond transaction. If the A-2 tranche had been priced at +50 bps instead of +52, reflecting just the 10 bp increase in credit card ABS spreads since the FirstEnergy transaction, the nominal savings to OPCo ratepayers would have been an additional \$104,000.

Many Precedents of Utility Securitizations With Narrower Credit Spreads than OPCo

Citigroup, the lead underwriter for the PIR Bonds and an experienced participant in utility securitizations, has in the past compared their new issue pricing to the estimated credit spreads published weekly by Citigroup’s Fixed Income Research group.

In 2008, for example, Citigroup boasted when it sold utility securitization bonds at narrower spreads to benchmark swaps than new credit card ABS issues as well as indicative rates for trades in the secondary market. Many other utility securitizations with WALs comparable to the PIR Bonds have sold with spreads to swaps narrower than those for concurrent credit card ABS.¹⁵ There is ample precedent that investors will accept utility credit spreads on top of or through relative value comparables like credit card ABS.

¹⁴ See, e.g., “Consumer ABS Weekly”, Citigroup Research, which publishes rates for auto ABS for 2 and 3 years only.

¹⁵ See PSE&G Transition Funding II, LLC, MP Environmental Funding, LLC, PE Environmental Funding, LLC and FPL Recovery Funding, LLC.

Citigroup’s 2008 report (available upon request) entitled, “CenterPoint Energy Houston Electric (CEHE) Securitization,” said:

“On Jan. 29, 2008, CEHE priced one of the most successful asset-backed securities (ABS) offering in many months, attracting both traditional asset-backed buyers and corporate “crossover” investors.”

“We estimate that each tranche of the CEHE III offering priced approximately 15-25 bp inside of like-maturity credit card securities.”

That report even cited as corroborating evidence a **Citigroup January 25, 2008 research report**¹⁶, (with them adding and circling the spreads in their CEHE report) for comparable securities, as shown to the right.

Indeed, the 2008 offering sold, according to Citi, with a 5-year tranche at +64 bps over swaps and the 10.5-year tranche at +94 bps over swaps. Both spreads were considerably narrower on a “relative value” basis than those indicated by Citigroup Fixed Income Research for credit card or other utility securitizations widely recognized by ABS professionals as the sole comparable security in the ABS market.¹⁷

		24 Jan 08 Spread (bp)
Triple-A		
2-Yr	Auto	75
	Credit card	58
	Equipment	85
	Stranded Assets	63
3-Yr	Auto	100
	Credit card	68
	Equipment	110
	Stranded Assets	73
5-Yr	Credit card	78
	Stranded Assets	83
7-Yr	Credit card	90
	Stranded Assets	95
10-Yr	Credit card	110
	Stranded Assets	115

¹⁶ See “Citi Bond Market Roundup: Strategy- Data Appendix,” Citigroup Research, January 28, 2008

¹⁷ In addition, utility securitization bonds are more comparable to highest quality utility and corporate including government sponsored agency bonds. Utility securitization bonds have special government i.e., regulatory backing and a pledge of non-interference by the state with U.S. constitutional protections. Unlike typical asset-backed securities, the obligation to repay in utility securitizations is cross-shared among generally all electricity customers in the utility’s service territory. There is no finite pool of receivables as in ABS. In any pricing, choosing, the right bonds to compare to is an important sales point and must be done carefully otherwise it leads to higher interest costs as demonstrated in the OPCO and the First Energy pricings.

Consumer ABS Weekly
18 July 2013

Figure 4. Consumer ABS Fixed-Rate Spreads to Swaps

18 Jul 13
Spread (bp)

Triple-A		
2-Yr	Auto	28
	Credit card	20
	Equipment	45
	Stranded Assets	28
3-Yr	Auto	35
	Credit card	25
	Equipment	50
	Stranded Assets	34
5-Yr	Credit card	35
	Stranded Assets	45
7-Yr	Credit card	50
	Stranded Assets	60
10-Yr	Credit card	55
	Stranded Assets	70

Unfortunately for OPCo ratepayers, in connection with the PIR Bonds, Citigroup appears to have negotiated interest rates with the PUCO's advisors with credit spreads *much wider* than its own research estimates.

Using the same methodology as Citi did in 2008, the most recent data available to PRAG-Oxford before the PIR Bonds were priced included a **similar July 18 2013 Citigroup research report** (arrows and circles added). That report showed spreads in their Figure 4 (to the left) over swaps for comparable securities.

Based on those reported spreads (and using the approach Citi used in 2008), OPCo's 2-year tranche, priced at +40 bps over swaps, was actually +12 to 20 bps wider than the spreads for utility securitizations or credit card ABS, respectively. The 5-year tranche at +52 bps over swaps was +7 bps wider than utility securitizations and +17 bps wider than credit card ABS.

PRAG-Oxford seem to have ignored these estimates - from the research of its lead underwriter - when they attested that "the PIR Bonds reflect a market price of most recently issued comparable securities." If PUCO's PIR Bonds had been priced with credit spreads just equal to other utility securitizations, as estimated by the Citigroup research report (still wider than credit card ABS, not narrower as Citigroup boasted in 2008), ratepayers would have saved an additional \$724,000.

Given the contrast between the PIR Bonds pricing at *wider* spreads to benchmark swaps than credit card ABS, while similar issues in other states have sold at *narrower* spreads to swaps than credit card ABS, diligent financial advisors should be concerned. Credit spreads to comparable securities can be compared over time. Unlike absolute yields, which are dependent mainly on the level of benchmark rates, credit spreads between two types of securities reflect the "relative value" market participants place on the different but comparable securities. Thus, they can be analyzed to determine how investors value specific credits at a specific time and how that changes over time. One of the underwriters of the OPCo transaction research department said specifically "In our opinion, assessing relative value in rate-reduction bond ABS can be best accomplished by reviewing the spread differential between RRBs and benchmark credit card ABS."¹⁸

Diligent financial advisors should ask why proposed pricing levels are much worse than fixed-income research or previous sales would suggest. When investors, bankers and rating

¹⁸ See "Absolute Value: Rate Reduction Bond ABS Primer" Wells Fargo Securities, July 17, 2013, page 6.

agencies agree that utility securitizations are safer, lower risk bonds than those backed by credit card receivables, why should OPCo's new issue of PIR Bonds sell with *higher* yields and *wider* credit spreads than credit card ABS issues, let alone other high quality corporate or other more appropriate comparables?¹⁹ This is what marketing and sales efforts and broad competition among and between underwriters and investors is about.

Today, 2013, market conditions for utility securitization bonds are better than 2008. In fact, all independent observers agree that utility securitizations performed *better* during the credit crisis than other structured securities. For example, S&P published a report in 2009 entitled "The Recession has Not Been Hard on "Ratepayer Obligation Charge" Bonds," their term for utility securitization bonds. At a time when even U.S. Treasury debt lost its triple-A rating, no utility securitization has ever lost its top AAA rating, or been put on a watch list as a candidate for downgrading.

As noted, a co-manager of the OPCo bonds, Wells Fargo, concluded in a July 2013 research report that ratepayer bonds were a better "credit" than credit card ABS (with no mention at all of auto ABS as comparable). He pointed out to investors that, while the utility securitization are a better credit, they are being priced *higher* than credit card ABS and therefore are a better relative value to investors.²⁰ This means investors are receiving a higher yield than is warranted by the risk they are taking. This kind of discrepancy needs to be eliminated or reduced by the diligent efforts of the financial advisor to create a more competitive marketplace for PIR Bonds in negotiations.

If underwriters claimed they couldn't find buyers to pay close to relative value, perhaps additional firms should have been added to the selling group and adequately rewarded for uncovering demand from investors willing to accept lower yields closer to the inherent value received.

If investors were unaware of utility securitizations or resisted lower yields in exchange for greater security, they should have been educated about how such ratepayer bonds provide both higher credit quality and more predictable repayment schedules than asset-backed securities.

As has been shown on numerous other transactions, increased marketing and sales effort to increase competition among underwriters and investors can achieve more efficient (*i.e.*, lower) pricing.

An Active Marketing Effort Demonstrably Drives Pricing Lower

The PRAG-Oxford report states that "the underwriters pre-marketed the transaction starting on Wednesday, July 17, 2013 and continued that process through Friday, July 19, 2013." The deal was "announced" the following Monday and priced on Tuesday, July 23. If this was the extent of the marketing, based on the results described in this analysis, it appears to have been insufficient.

¹⁹ See the pricing of 19-year MP Environmental Funding and PE Environmental Funding utility securitization bonds, December 2009 that priced at +62 to US Treasuries when Goldman Sachs who had been lead manager for another utility securitization estimated that the bonds would require a yield of +106 to US Treasuries to be sold. Jefferies/The Williams Capital Group were underwriters and Saber Partners, LLC was financial advisor to the commission and joint decision-maker with the issuers.

²⁰ See "Absolute Value: Rate Reduction Bond ABS Primer" Wells Fargo Securities, July 17, 2013.

While our analysis is primarily focused on the specific structure and pricing, it is important to understand that marketing efforts significantly impact the ultimate cost of the PIR Bonds. Complex securities need to be “sold” to investors. Also, a broad group of appropriate investors needs to be identified and targeted as part of the marketing effort. Otherwise, a small group of investors may demand too high a premium or there may not be enough competition for the issue. These lead to higher costs.

Based on available information, the marketing for the PIR Bonds seems to have been unnecessarily abbreviated and passive resulting in little competition for the bonds which directly contributed to higher costs.

After filing a registration statement with SEC, active marketing for indications of interest may begin, but not sales. According to the SEC website, [OPCo’s registration statement](#) was filed with the SEC on May 21, 2013—approximately 2 months before PRAG-Oxford state that “pre-marketing” began. Securities laws also allow for the use with investors of a shorter “term sheet” in addition to the registration statement. The term sheet can discuss the key features of the issue and help assess investor demand within 5 days of the initial filing. This also gives an opportunity for the advisor and underwriters to identify appropriate comparables, as well as dispel any misconceptions about the specific issue.

As noted, from the time a registration statement and preliminary prospectus is filed with the SEC, “marketing” may begin. No bonds may be sold during this period or firm orders taken, rather only “indications of interest” may be solicited. However, this is also the time that investor education may be conducted *without any delay* whatsoever of the transaction because a registration statement is on file with the SEC waiting to “go effective.” After a registration statement is effective, the bonds can be sold. Based on the PRAG-Oxford report, this time between filing and pricing seems to have been wasted and used only for “market update” calls between the underwriters and financial advisor.

Term Sheet and Investor Outreach Are Standard in Utility Securitizations

PRAG-Oxford may now claim that they did talk to some investors. However, based on the timeline described in their report and filings with the SEC, it appears they did so without a term sheet or customary marketing materials to help explain the advantages of ratepayer bonds until the very last minute.²¹

A meaningful report of a financial advisor’s activities on behalf of PUCO would describe the extent of the marketing effort: how many investors were contacted, how many meetings or calls with investors were held, what marketing materials were used. Rather than just quoting the investment bankers, a diligent financial advisor would have been involved sufficiently to also detail the size of the “book” at the time of pricing, how those orders were distributed by size and type of investor, the extent of any “over-subscription” and any resultant repricings, and how many investors participated in the final offering.

Not all AAA-rated securities price alike. And not all AAA-rated utility securitization bonds price alike. There are substantive differences that can cost ratepayers money if they are not identified and addressed appropriately. While a lowest cost standard was not mandated by

²¹ According to SEC filings, there was no term sheet for use in discussions with investors about relative values until July 17, a scant four business days before the pricing.

the legislation or the financing order, this does not mean that those responsible for structuring, marketing and pricing should not try to achieve a best execution.

Final pricing (and cost to ratepayers) is normally the culmination of a thorough and energetic marketing effort. Underwriters and advisors should be willing and able to point to specific actions taken to educate investors and broaden investor demand and negotiate a best pricing, fair to all.

On-Going Costs: Over-Recovery of Costs of Providing Servicing to OPCo

The financing order allows the initial PIR Bond servicer to receive both (i) an upfront payment, designed to allow recovery of its initial set-up costs; and also (ii) a fixed periodic fee, designed to allow the initial servicer and any successor servicer to recover their ongoing costs.²² Like most utility securitizations, the initial servicer of the intangible property that secures the PIR Bonds is the sponsoring utility. Most commonly for similar transactions since 2007 (including other subsidiaries of AEP), the fee allowed for sponsoring utilities has been an annual fee of no more than 0.05% of the initial principal amount of the transaction. In fact, as shown in **Table 3** below, since 2007, only two of 18 utility securitizations allowed servicing fees in excess of 0.06% per year, excluding the two recent Ohio transactions.

For bankruptcy law reasons, the aggregate fees paid to the sponsoring utility must reflect arms-length fair market value consideration for the services provided. Bankruptcy lawyers generally interpret this to require aggregate fees that will at least cover an allocable portion of the sponsoring utility's fully-allocated costs of providing servicing functions.

The financing order authorizes OPCo, as initial servicer, to receive an annual fee equal to 0.10% of the initial principal amount of the PIR Bonds:

“Based upon both estimated costs of performing the servicing function and market precedent for such fees, the Commission determines that the annual servicing fee to be paid to Ohio Power should be 0.10 percent of the initial principal amounts of the PIR Bonds issued by the SPE.”²³

For the reasons described above, this represents an allocable portion of the Company's fully allocated costs of providing servicing functions.

²² Because the financing order makes no provision for a successor servicer's recovery of its initial set-up costs, and because a successor servicer presumably would perform no other services in connection with the sponsoring utility, similar financing orders commonly provide for a significantly higher periodic servicing for successor servicers. Thus, page 50 of the financing order allows an annual servicing for successor servicers of up to 0.75% of the initial principal amount of the PIR Bonds.

²³ P. 38 of the financing order, Revised Ex. C, March 12, 2013.

Maximum Allowed Annual Servicing Fees				
Table 3				
Deal #	Deal Name	Principal Amount (\$)	Wtd. Avg. Life (yrs.)	Max. Annual Servicing Fee on Initial P.A.
1	Ohio Phase-In-Recovery Funding LLC (7/23/2013)	267,408,000	3.33	0.10%
2	FirstEnergy Ohio PIRB Special Purpose Trust (6/12/2013)	444,922,000	9.29	0.10%
3	AEP Texas Central Funding III (3/7/2012)	800,000,000	6.93	0.05%
4	Centerpoint Energy Transmission Bond Co. IV (1/12/2012)	1,695,000,000	7.10	0.05%
5	Entergy Arkansas Energy Restoration Bonds (8/11/2010)	124,100,000	5.44	0.12%
6	Louisiana Utilities Restoration Corporation Project/ELL (7/15/2010) [taxable munis]	468,900,000	6.63	0.03%
7	Louisiana Utilities Restoration Corporation Project/EGSL (7/15/2010) [taxable munis]	244,000,000	6.62	0.06%
8	MP Environmental Funding LLC (12/16/2009)	64,380,000	19.02	0.05%
9	PE Environmental Funding LLC (12/16/2009)	21,510,000	19.02	0.05%
10	CenterPoint Energy Restoration Bond (11/18/2009)	664,859,000	7.26	0.05%
11	Entergy Texas Restoration Funding (10/29/09)	545,900,000	7.21	0.05%
12	Louisiana Public Facilities Authority (8/20/2008)	278,400,000	5.75	0.06%
13	Louisiana Public Facilities Authority (7/22/2008)	687,700,000	5.83	0.03%
14	Cleco Katrina/Rita Hurricane Recovery Funding LLC (2/28/2008)	180,600,000	7.09	0.05%
15	CenterPoint Energy Transition Bond Company III (1/29/2008)	488,472,000	7.11	0.05%
16	Entergy Gulf States Reconstruction Funding I, LLC (6/22/2007)	329,500,000	8.05	0.12%
17	RSB BondCo LLC (BG&E sponsor) (6/22/2007)	623,200,000	5.60	0.05%
18	FPL Recovery Funding LLC (5/22/2007)	652,000,000	7.15	0.05%
19	MP Environmental Funding LLC (4/3/2007)	344,475,000	12.01	0.05%
20	PE Environmental Funding, LLC (4/3/2007)	114,825,000	12.07	0.05%
	Average			0.06%
	Mode (most common)			0.05%

So long as the sponsoring utility continues to send monthly bills to its retail customers, and based on the experience with other utility securitization transactions, the sponsoring utility generally incurs few if any incremental ongoing costs by reason of its role as servicer in connection with the bonds. Because sponsoring utilities generally are already allowed to recover 100% of their costs of providing general billing and collection functions from ratepayers through their general rate case proceedings, this generally results in a windfall over-recovery of costs unless some provision is made for adjusting the sponsoring utility's other rates and charges.

When it has served as Financial Advisor to State Commissions in connection with the issuance of other utility securitizations, Saber Partners, LLC has ensured that the financing orders and/or Servicing Agreements include specific provisions requiring such adjustments to the sponsoring utility's other rates and charges. For example, the West Virginia PSC's financing order authorizing the issuance of similar bonds for Monongahela Power and The Potomac Edison Company states:

“The Applicants shall credit to consumers through other electric rates and charges the amount of the Applicants’ Servicing Fee in

excess of any recorded periodic incremental costs of performing the Servicing functions.²⁴

We have been unable to find any such provision in the OPCo financing order or Servicing Agreement allowing other rates and charges of the Company's ratepayers to be credited to reflect the Company's over-recovery of costs. If OPCo, like most other sponsoring utilities, incurs no material *incremental costs* that can be demonstrated by reason of its agreement to function as servicer in connection with the PIR Bonds, the full \$267,408 of *annual servicing fee* might represent over-recovery of costs.

Summary and Conclusion

Whether the PIR Bonds were priced "consistent with market conditions" is an open question. The PIR Bonds clearly were not structured or marketed so as to take maximum advantage of the known market conditions at the time of pricing. Furthermore, it is difficult to give much credence to PRAG-Oxford's attestations since they reference inappropriate, non-comparable securities and, in the case of the A-2 tranche, non-existent 5-year auto ABS securities.

We conservatively estimate that improved pricing and structuring efforts (use of single-tranche structure and appropriate credit spread benchmarking) could have resulted in savings for ratepayers in the amount of \$1,390,074.

In addition, it appears that certain ongoing costs built into the transaction were greater than necessary. The most significant additional cost relates to the ongoing servicing cost of 10 bps/year on the initial principal amount for the life of the bonds, apparently without any provision for crediting the sponsoring utility's revenue requirement for other rates and charges to prevent over-recovery of costs. Based on market precedents described above, this amounts to an additional nominal net cost to ratepayers of \$791,082 due to a cap that is 5 bps *above* the norm and another \$791,082 because there is no provision to credit fees in excess of actual (and verifiable) incremental costs.²⁵ If OPCo can demonstrate actual additional unrecovered costs for any future period, this amount could be less. However, since the issue was never raised, we may never know. One of the responsibilities of an experienced financial advisor to a utility commission is to identify these types of issues for review, investigation and decision.

²⁴ **West Virginia Case Nos. 05-0402-E-CN and 05-0750-E-PC (April 7, 2006), page 86.** See also **California PUC D.04-11-015 (November 2004), page 48** ("PG&E shall credit to electric consumers the amount of this servicing fee in excess of any recorded incremental servicing costs."); **Florida PSC Docket No. 060038-EI, Order No. PSC-06-0464-FOF-EI (May 30, 2006), Finding of Fact 114(b)** ("FPL has not justified that the annual fee is necessary to cover any incremental costs to be incurred by FPL in performing ongoing services as servicer. Thus, we find that FPL shall apply to the Reserve all amounts it will receive under the Servicing Agreement for ongoing services.")

²⁵ The forgone savings related to the annual serving fee, while large in the OPCo deal, are many times larger in the FirstEnergy transaction, where the expected final maturity is in 20.57 years rather than just 5.92 years, and the initial principal amount upon which the fee is calculated is 1.7 times as large.

A summary of the potential forgone savings in this transaction (using the conservative single-tranche pricing calculated above) is presented in **Table 4**, below:

Forgone Savings Table 4		
Item	Quantified by	Approximate Nominal Forgone Savings (\$)
Pricing based on correct AAA- rated credit card ABS benchmark rather than hypothetical AAA- rated auto ABS benchmark	A-2 pricing at +50 vs. 52 bps	\$ 104,148
“Best-Execution” structuring	Conservative estimate of 1-tranche vs. 2-tranche pricing	1,285,926– 2,177,692
Ongoing servicing cost cap consistent with most prior utility securitization transactions	Cap fee at 5 bps/yr. Vs. 10 bps/yr. on initial principal amount	791,082
Credit servicing fee in excess of actual (likely zero) incremental cost	Reducing net cost of servicing fee to zero	791,082
Total²⁶		2,972,238– \$ 3,864,004

Simply by using public information, known market conventions and available market research, we conclude that the OPCo PIR Bond transaction left substantial ratepayer savings “on the table.” This resulted from mispricing and mis-structuring, and from accepting non-standard upfront and ongoing costs. More experience with structuring, marketing and pricing of utility securitizations specifically, and of the unique history of this market, could have helped Ohio capture these savings for the benefit of OPCo’s ratepayers. This likely would have covered the financial advisor’s fee many times over.

²⁶ Note that this total of forgone savings does not explicitly include the amount related to failure to price at the Citigroup published rate for asset backed securities (an additional \$724,000), which is a further indication of the conservative nature of the foregone savings shown in this Table 4.

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July 25, 2013

The Public Utilities Commission of Ohio

180 East Broad Street

Columbus, Ohio 43215

Re: Financing Order - Case No. 12-1969-EL-ATS

Dear Commissioners:

Public Resources Advisory Group and Oxford Advisors (together "PRAG-Oxford") has been engaged to serve The Public Utilities Commission of Ohio ("PUCO" or the "Commission") as its independent financial advisor pursuant to the terms of Financing Order issued *In the Matter of the Application of Ohio Power Company for Authority to Issue Phase-in-Recovery Bonds and Impose, Charge and Collect Phase-in-Recovery Charges for Tariff and Bill Format Changes in Case No. 12-1969-EL-ATS, dated March 20, 2013 as amended by Entry on rehearing, dated April 10, 2013 (the "Financing Order")*. In such capacity and in compliance with the terms and conditions of the Financing Order, PRAG-Oxford makes certifications in this letter related to the issuance of \$267,408,000 Ohio Phase-In-Recover Funding LLC, Tranches A-1 and A-2 (the "A-1's" and the "A-2's" and, collectively, the "PIR Bonds") that were issued to refinance the DARR balance of Ohio Power Company (the "Company") at a lower cost than the authorized rate of return.

PRAG-Oxford's certifications relate to:

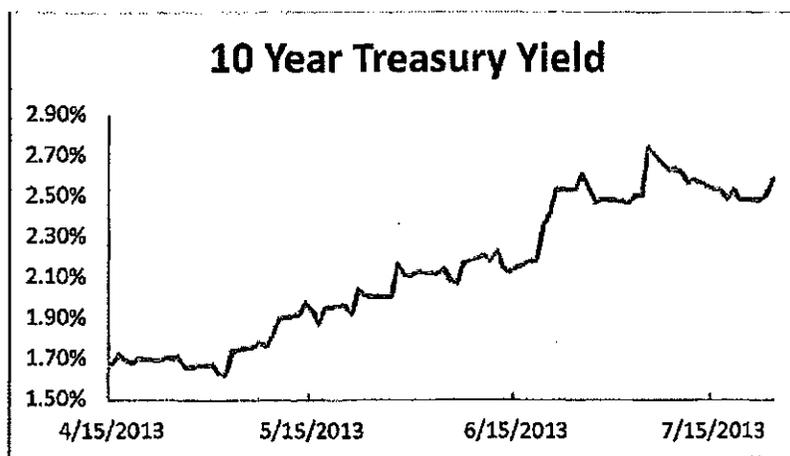
- Confirmation of whether issuance of the PIR Bonds results in measurably enhancing cost savings and mitigating rate impacts to customers compared with traditional financing mechanisms or traditional cost-recovery methods available to the Company;
- Review of the financial terms and conditions of the proposed PIR Bond issuance and attestation that the PIR Bond issuance transaction as proposed is consistent with the Financing Order and requisite statutory provisions of Ohio Revised Code Sections 4928.231 through 4928.2318 (the "Securitization Law");
- Confirmation that the structuring and pricing of the PIR Bonds, as proposed, will result in charges consistent with market conditions and the terms of the Financing Order and will protect the competitiveness of the retail electric market in the State of Ohio as a result of lowering the debt service cost to rate payers in Ohio;
- Attestation that the PIR Bonds reflect a market price of most recently issued comparable securities;
- Confirmation that PRAG-Oxford has participated fully with the Applicant as a co-equal in all plans and decisions related to the pricing, marketing and structuring of the PIR Bonds and that we provided timely information as necessary to fulfill our obligation to advise the Commission in a timely manner; and
- Determination that the costs of the transaction conform to the terms and conditions of debt securities commonly accepted in the financial industry.

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The PIR Bonds were offered in two tranches (A-1 and A-2) by the Underwriters (as defined below) under a registration statement on Form S-3 (Registration Nos. 333-188745 and 333-188745-01), on May 22, 2013 as amended by Amendment No. 1 thereto filed June 25, 2013 and Amendment No. 2 thereto filed July 12, 2013, including a prospectus and a form of prospectus supplement, for the registration under the Securities Act of up to \$278,000,000 aggregate principal amount of the Bonds. Such registration statement, as amended ("Registration Statement Nos. 333-188745 and 333-188745-01"), has been declared effective by the Commission on July 12, 2013 and no stop order suspending such effectiveness has been issued under the Securities Act and no proceedings for that purpose have been instituted or are pending or, to the knowledge of the Issuer, threatened by the Commission. PRAG-Oxford utilized the Prospectus Supplement to the Prospectus dated July 17, 2013. The final Prospectus Supplement to the Prospectus was dated July 23, 2013. The underwriting group serving the Applicant consists of Citigroup Global Markets Inc. and RBC Capital Markets, LLC as Joint Bookrunners and PNC Capital Markets LLC, RBS Securities Inc. and Wells Fargo Securities, LLC as Co-Managers (the "Underwriters"). The Underwriters pre-marketed the transaction starting on Wednesday, July 17, 2013 and continued that process through Friday, July 19, 2013. The Underwriters announced the PIR Bonds transaction at approximately 9:00 a.m. EDT on Monday, July 22, 2013 and provided guidance information to the public credit markets of possible basis point spreads over the US Dollar LIBOR swap curve maturities adjusted to equal the weighted average life ("WAL") of the A-1's and A-2's.

Investors had reacted negatively to comments from Ben Bernanke, Chairman of the Federal Reserve Bank, made during a post Federal Open Market Committee ("FOMC") Meeting press conference on June 19th regarding tapering the pace of open market purchases by the Federal Reserve Board Open Market Committee. Those comments caused U.S. Treasury prices to fall and yields to rise significantly within a short period. The 10-year Treasury rose from 2.18% on June 18th to 2.53% on June 21st. Considerable rate volatility has been experienced since then, although net movement has been limited. The 10-year Treasury yield on the pricing date was 2.51%. Shown below is the 10 year yield history since the 15th of April.



The PIR Bonds were offered by the Underwriters through a negotiated sale consistent with the provisions of the Financing Order. PRAG-Oxford has reviewed the Underwriter Compliance Certificate from the Joint Bookrunners in preparation of this letter. The PIR Bonds were priced at approximately 12:18 p.m. EDT, on July 23, 2013 (the "Pricing Time").

The Financing Order requires the Company to file an Issuance Advice Letter and the Company to file a certification after pricing but before issuance of the PIR Bonds. In its Issuance Advice Letter, filed with the PUCO on July 24, 2013, the Company has set forth the following terms of the PIR Bonds:

PIR Bond Series: Senior Secured Phase-In-Recovery Bonds, Tranches A-1 and A-2

PIR Bond Issuer (SPE): Ohio Phase-In-Recovery Funding LLC

Trustee: U.S. Bank National Association

Closing date: August 1, 2013

Bond ratings: S&P AAA, Moody's Aaa

Amount Issued: \$ 267,408,000

Payments to Investors: Semiannually beginning July 1, 2014

PRAG-Oxford confirms that the PIR Bonds to be issued are consistent with the terms set forth in the Company's Issuance Advice Letter, and will result in the issuance of PIR Bonds in the amounts and with the coupon interest rates identified in the table immediately below. The effective duration weighted average annual interest rate of the PIR Bonds is 1.58%, which is lower than the authorized rate of return on the DARR balance of 5.34%.

Tranche	Coupon Rate	Yield	Weighted Average Life (Years)	Initial Price to Public	Expected Final Maturity	Legal Final Maturity
A-1	0.958%	0.958%	2.25	99.99826%	07/1/2017	07/01/2018
A-2	2.049%	2.048%	5.08	99.99694%	07/1/2019	07/01/2020

Based upon the final results of the structuring, marketing and pricing of the PIR Bonds completed at the Pricing Time, PRAG-Oxford attests to the Commission that issuance of the PIR Bonds on the terms set forth above will result in measurably enhancing cost savings and mitigating rate impacts to customers as compared with traditional financing mechanisms or traditional cost-recovery methods available to the Company.

PRAG-Oxford further attests that the financial terms of the PIR Bonds as described above are consistent with the final terms and conditions of the Financing Order.

PRAG-Oxford further attests that the structuring and pricing of the PIR Bonds issued on the terms set forth above will result in charges consistent with market conditions and the terms of the Financing Order and that it protects the competitiveness of the retail electric market in the State of Ohio.

PRAG-Oxford further attests that the PIR Bonds were issued at a lower cost, 1.58%, than the authorized rate of return of 5.34%.

PRAG-Oxford further attests that the PIR Bonds reflect a market price consistent with current market condition as described below:

- The A-1's pricing at a spread of + 40 basis points over the swaps curve conforms to the broader Asset Backed Securities ("ABS") new issuance market of utility securitization, prime auto, and auto lease "ABS". We note that on the recent First Energy Transaction the 1.6 year average life tranche was priced at a spread of + 25 bps over the swaps curve. Given that the PIR Bonds tranche A-1 has a longer average life of 2.25 years and given the significant increase in credit spreads in the six weeks since the pricing of the First Energy transaction on June 12, 2013, with spreads having increased between +10 and 20 bps on average on other highly rated securities, it is our opinion that +40 bps represents a result consistent with current market conditions. For example, on July 17, 2013, a prime auto loan Honda transaction achieved spread between 14 and 17 bps wider than a similar Honda transaction priced in April 2013. Similarly, a Ford prime auto loan priced on July 23, 2013 was between 11 and 18 bps wider on the AAA rated classes than

a similar transaction Ford priced on May 14, 2013. Furthermore, a Volkswagen auto lease transaction priced on July 17, 2013, with a similar average life, priced at +50 bps. It is also worth noting that we were able to reduce the spread levels proposed by the Underwriters from +45-50 bps down to +40 bps on the A-1 tranche.

- A-2's pricing at a spread of + 52 basis points over the swaps curve conforms to the broader ABS new issuance market of utility securitization and prime auto ABS. For the recent First Energy Transaction, its 5.07 year average life tranche priced at a spread of +40 bps. Given that the PIR Bonds tranche A-2 has a similar average life of 5.08 years and given the considerable movement in the public credit markets in the six weeks since the pricing of the First Energy transaction as referenced above and as seen in the Honda and Ford prime auto loan transaction spread widening, in our opinion a spread of +52 bps is consistent with current market conditions. It is also worth noting that we were able to reduce the initial spread level recommended by the Underwriters from +60-65 bps down to +52 bps. When PRAG-Oxford pressed the Underwriters to lower the spread by another 1-2 bps on the day of pricing, we were informed that the transaction could not handle any additional reduction in spread.
- Another item to note is that the Underwriters had proposed a single pass-through tranche but PRAG-Oxford requested early in the market information discussions that they continue to evaluate a two-tranche structure and to include it as an option in discussions with investors and rating agencies in the event that breaking the issue into two tranches would produce greater savings and benefit to ratepayers. Indeed, due to the steepening of the yield curve and changing market conditions, the two-tranche structure did provide a lower borrowing cost and greater savings for the ratepayers of Ohio. Additionally, PRAG-Oxford recommended reducing the average life of the PIR bonds to reduce the amount of principal that would be amortized at the higher rates – this resulted in additional savings to the ratepayers of Ohio by moving the life of the series down to under 6.0 years from 6.6 years.

PRAG-Oxford has participated fully with the Applicant as a co-equal in all plans and decisions related to the pricing, marketing and structuring of the PIR Bonds and all matters relating to the structuring and pricing of the PIR Bonds were determined through joint decisions with the Applicant. We were provided timely information by the Underwriters as was necessary to fulfill our obligation to advise the Commission in a timely manner. We did not participate in the underwriting of the PIR Bonds. The price discovery process began on May 16, 2013 with weekly market update calls with the two bookrunning underwriters. PRAG-Oxford and PUCO Staff attended the market update calls. The frequency of the market update calls increased to two calls in the Week of July 8th, and numerous calls took place during the Week of July 15th. PRAG-Oxford participated in the decision to pre-market the PIR Bonds beginning on July 17, 2013. PRAG-Oxford participated in the decision to announce the transaction on July 22, 2013 while lowering the spread guidance from that of the whisper numbers. In addition, we participated in the pricing of the A-1 and A-2 PIR Bonds at approximately 12:18 p.m., July 23, 2013. All of these events were communicated frequently to PUCO Staff. PRAG-Oxford believes that the pre-marketing period, commencing on July 17, 2013, was instrumental to building a large book of orders and in the ability to reduce the spread and ultimately deliver a better outcome for the ratepayers of Ohio.

The savings that will result from the PIR Bond issuance transaction, upon the terms set forth above, will be \$18,598,608 in nominal savings and \$23,828,678 in present value savings, which compares to the \$21.9 million and \$28.8 million savings estimate, respectively, that is included in the Financing Order. It should be noted that much of the decline in absolute savings relative to the Financing Order is due to the smaller DARR balance, as percentage savings did not experience such large reductions.

	DARR Initial Principal	Expected Maturity	Coupon	Nominal Savings	PV Savings	% Nominal Savings	% NPV Savings
January Order	291,482,926	10/1/2019		21,909,199	28,754,366	7.52%	9.86%
Pricing	263,667,605	7/1/2019	0.958% / 2.049%	18,598,608	23,828,678	7.05%	9.04%

PRAG-Oxford independently verified the calculation of the savings using its own financial model. That verification process confirmed the expected nominal savings calculation derived from the model used by Citigroup, the Company's structuring advisor, using revenue assumptions based on the Citigroup rate model, when it performed its savings calculation.

PRAG-Oxford is filing this letter within 24 hours of the filing of the Issuance Advice Letter as is consistent with the Financing Order.

This letter is exclusively for your information and may not be used, circulated, quoted or otherwise referred to for any other purpose, except in each case in accordance with the prior written consent of the undersigned. In addition, the information and views provided herein are being furnished to you for the purpose described herein and may not be used or relied upon (i) by you for any other purpose, or (ii) by any other person other than you, in each case without the prior written consent of the undersigned.

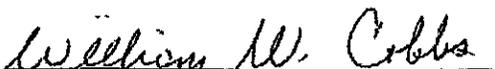
This Certification speaks only as of the date thereof and PRAG-Oxford will have no responsibility or obligation to update this Certification. Further, PRAG-Oxford will have no responsibility to consider its applicability or correctness as to any person or entity other than the PUCO.

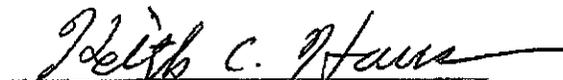
The undersigned specifically disclaims any responsibility or liability to any other person for the content of this letter, whether such person claims rights directly or as a third-party beneficiary. The undersigned do not provide accounting, tax or legal advice, and we make no representations or assurance as to the appropriateness or adequacy of the information contained herein for your purposes and express no view as to the accounting, tax or legal treatment of any such matters.

Respectfully submitted.

PUBLIC RESOURCES ADVISORY GROUP

OXFORD ADVISORS LLC


 William W. Cobbs
 Chairman


 Keith C. Hausman
 Managing Director

Ohio Phase-In-Recovery Funding LLC
Issuing Entity
PRICING TERM SHEET
July 23, 2013
\$267,408,000
Senior Secured Phase-In-Recovery Bonds

Joint Bookrunners: Citigroup Global Markets Inc. and RBC Capital Markets, LLC

Co-Managers: PNC Capital Markets LLC, RBS Securities Inc. and Wells Fargo Securities, LLC.

Expected Ratings: “Aaa(sf)”, “AAA(sf)” by Moody’s and S&P, respectively.*

Closing Date / Settlement Date: August 1, 2013 **

Interest Payment Dates: January 1 and July 1 of each year, and on the final maturity date, commencing on July 1, 2014.

Applicable Time: 12:18 P.M. (ET) on July 23, 2013.

Proceeds to Issuing Entity: The total amount of proceeds to the Issuing Entity (as defined below) after underwriting discounts and commissions of \$1,069,632 and before deduction of expenses (estimated to be \$2,670,763) is \$266,332,362.

Tranche	Principal Amount Offered	Expected Weighted Average Life (years)	Scheduled Final Payment Date	Final Maturity Date	No. of Scheduled Semi-Annual Sinking Fund Payments	Interest Rate	Initial Price to Public***	Underwriting Discounts and Commissions
A-1	\$164,900,000	2.25	7/1/2017	7/1/2018	7	0.958%	99.99826%	0.40%
A-2	\$102,508,000	5.08	7/1/2019	7/1/2020	5	2.049%	99.99694%	0.40%

Ohio Phase-in-Recovery Funding LLC (the “Issuing Entity”) and Ohio Power Company (“OPCo”) have jointly filed a registration statement (including a prospectus and preliminary prospectus supplement) with the Securities and Exchange Commission (the “SEC”) for the offering to which this communication relates. Before you invest, you should read the prospectus and preliminary prospectus supplement in that registration statement and other documents the Issuing Entity and OPCo have filed with the SEC for more complete information about the Issuing Entity and the offering. You may get these documents for free by visiting EDGAR on the SEC web site at www.sec.gov. Alternatively, the Issuing Entity, Citigroup Global Markets Inc. or any dealer participating in the offering will arrange to send you the prospectus and prospectus supplement if you request it by calling Citigroup Global Markets Inc. toll-free at 1-877-858-5407.

* A security rating is not a recommendation to buy, sell, or hold securities and should be evaluated independently of any other rating. The rating is subject to revision or withdrawal at any time by the assigning rating organization.

** It is expected that delivery of the Senior Secured Phase-In-Recovery Bonds (the “Bonds”) will be made to investors on or about August 1, 2013 (such settlement being referred to as “T+7”). Under Rule 15c6-1 under the Exchange Act, trades in the secondary market are required to settle in three business days (such settlement referred to as “T+3”), unless the parties to any such trade expressly agree otherwise. Accordingly, purchasers who wish to trade the Bonds on the date of pricing or on the next business day will be required, by virtue of the fact that the Bonds initially will settle at T+7, to specify an alternate settlement arrangement at the time of any such trade to prevent a failed settlement. Purchasers of the Bonds who wish to trade the Bonds on the date of pricing or the next business day should consult their own advisors.

***Interest on the Bonds will accrue from August 1, 2013 and must be paid by the purchaser if the Bonds are delivered after that date.

	Tranche A-1	Tranche A-2
Reference Benchmark:	interpolated swaps	interpolated swaps
Reference Yield:	0.558%	1.528%
Reoffer Spread:	40 bps	52 bps
Reoffer Yield:	0.958%	2.048%
Interest Rate:	0.958%	2.049%
Net Proceeds: (%)	99.59826%	99.59694%
Net Proceeds: (\$)	\$164,237,530.74	\$102,094,831.26
CUSIP:	67741Y AA6	67741Y AB4
ISIN:	US67741YAA64	US67741YAB48

Expected Amortization Schedule

Semi-Annual Payment Date	Tranche A-1 Balance	Tranche A-2 Balance
Closing Date	\$ 164,900,000.00	\$ 102,508,000.00
7/1/2014	129,963,522.28	102,508,000.00
1/1/2015	107,763,419.81	102,508,000.00
7/1/2015	84,536,959.05	102,508,000.00
1/1/2016	61,790,651.06	102,508,000.00
7/1/2016	38,672,593.03	102,508,000.00
1/1/2017	16,232,132.41	102,508,000.00
7/1/2017	-	94,878,311.39
1/1/2018	-	72,047,743.79
7/1/2018	-	47,922,804.63
1/1/2019	-	24,586,669.65
7/1/2019	-	-

Expected Sinking Fund Schedule

Semi-Annual Payment Date	Tranche A-1 Scheduled Principal Payment	Tranche A-2 Scheduled Principal Payment
Tranche Size on Closing Date	\$164,900,000.00	\$102,508,000.00
7/1/2014	34,936,477.72	-
1/1/2015	22,200,102.47	-
7/1/2015	23,226,460.76	-
1/1/2016	22,746,307.99	-
7/1/2016	23,118,058.03	-
1/1/2017	22,440,460.62	-
7/1/2017	16,232,132.41	7,629,688.61
1/1/2018	-	22,830,567.60
7/1/2018	-	24,124,939.16
1/1/2019	-	23,336,134.98
7/1/2019	-	24,586,669.65
Total Payments	\$164,900,000.00	\$102,508,000.00