Public Works Financing

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LBJ Managed Lanes, The Ultimate Greenfield Test

By Lori Sharn, Public Works Financing, Washington, DC

In what is the largest greenfield toll road financing ever done in North America, Cintra and Meridiam Infrastructure raised $2.1 billion this month at a debt/equity ratio of 2.2 to rebuild and expand a heavily congested section of the LBJ Freeway (I-635) just north of downtown Dallas, Tex. Those private funds will be combined with $496 million in public money committed by Texas DOT to build one of the most technically complex transportation projects ever attempted in the U.S. under a fixed-price contract.

Tolls will be dynamically priced with peak-period charges as high as $0.75 per mile in 2009 dollars for the 13-mile segment of new tolled express/HOV lanes that are being added in a 3x3 configuration, mainly in cut-and-cover trenches. The tolled lanes will be in direct competition with eight lanes of freeway, which are being rebuilt next to, and in some sections, above the managed HOV lanes. The North Texas Tollway Authority will operate the highly complex system for the investors in the 52-year toll concession.

The construction will be done under traffic in a narrow section of the LBJ freeway, which carries 270,000 vehicles per day.

The design build contract price is $2.069 billion. Approximately 5 years of construction will start in 2011 by a partnership of Spanish constructor Ferrovial-Agroman and its Texas subsidiary W.W. Webber. Cintra and Ferrovial-Agroman are subsidiaries of Spain's Ferrovial Group.

Advised by Macquarie Capital, the project development team, called LBJ Infrastructure Group, achieved financial close June 22. The capital structure includes $665 million in equity, divided between Cintra (51%), Meridiam (42.4%) and the Dallas Police and Fire Pension System (6.6%). Those funds leveraged $1.465 billion in debt, comprising an $850-million federal TIFIA loan at 4.22% with repayment over 40.5 years starting five years after completion. Senior debt of $615 million in 30-year, tax-exempt private activity bonds were issued at 7.23%. The $2.8-billion project cost also includes $126 million in capitalized interest on the TIFIA loan.

Advisors were White & Case, LLP and Bracewell & Giuliani LLP, for the concession company; Nossaman LLP, for TexDOT; and Latham & Watkins LLP, for the lenders. Merrill Lynch was the lead underwriter. Hatch Mott MacDonald was the lenders' traffic advisor.

Investor Comfort

The financing follows a similar structure used by the same three partners on the North Tarrant Express (NTE). That $2-billion managed lanes project in the Fort Worth area closed last December with a debt/equity ratio of 2.5 (PWF 12/10, p. 18). Sponsors of both projects provided a $250-million letter of credit to secure both performance by the design-build contractor and its payment obligation to subcontractors, as well as to protect the lenders.

The LBJ Express "had the advantage of the other financing having been completed. That was a positive," says Nicolas Rubio, president of Cintra US. "In general, the investors in the other project [NTE] feel pretty comfortable with those bones."

Although bank debt was considered once again, it was clear from the NTE experience that private activity bonds were the preferred option, Rubio says.

The LBJ project has more debt per mile than the North Tarrant Express ($23 million vs. $20.75 million) yet is considered a stronger asset, says Fitch Ratings analyst Chad Lewis. That's because of higher traffic volumes. "You have higher debt, but you also have the ability . . . to produce more revenue per lane mile," Lewis says.

The private activity bonds received the lowest investment grade ratings from both Fitch (BBB-) and Moody's (Baa3). Moody's had rated the NTE bonds a notch higher.

Fitch also gave its BBB- rating to the loan from the Transportation Infrastructure Finance and Innovation Act (TIFIA) program. To secure the loan, the private team paid an upfront fee of $28.5 million, reducing the government's subsidy cost to $70 million.

The loan terms are the same as for NTE, with the ability to defer all payments during construction and the first five years of operation. Depending on net toll revenue, lower interest payments than scheduled are possible through year 25 of operations.

Cintra's unsecured corporate guarantee for the equity was enough to achieve an investment grade rating for the NTE debt, as long as certain financial tests were met. A tighter guarantee was needed for the LBJ Express, says Fitch analyst Mike McDermott.

On the LBJ Express, a letter of credit will ensure that Cintra's equity in the project will be delivered as promised. The LOC will not be required if Cintra's parent, Ferrovial, seeks and receives an investment-grade rating. The company is not now rated. ▪

Financial Close of Texas DOT's I-635 Marks Monumental Achievements (6/10, p. 18)

by Brian Papernik and Christine Ryan, Nossaman LLP

The financial close of the I-635 Managed Lanes Project (I-635) on June 22, following the financial close of the initial 13-mile segment of the North Tarrant Express (NTE) on December 17, 2009, are like a blockbuster and its sequel for the Texas Dept. of Transportation.

The 17-mile I-635 in Dallas is the first highway public-private partnership (P3) project to achieve financial close in 2010. The NTE, also in the Dallas-Ft. Worth metropolitan area, is one of three transportation P3s to close in 2009. The initial 13-mile segment of the NTE will be followed by a second 23-mile segment to be delivered through a pre-development agreement. These projects also further the use of managed lanes to address congestion in the U.S.

The I-635 and NTE projects will include newly constructed managed lanes within existing corridors and reconstructed existing facilities. The traveling public will be able to choose either tolled managed lanes or untolled general purpose lanes. The toll on the managed lanes will vary, depending on traffic congestion, in order to ensure speeds of at least 50 miles per hour. Both projects were awarded in separate procurements to separate consortiums consisting of Cintra Infraestructuras, S.A.U., Meridiam Infrastructure Finance and Dallas Police and Fire Pension System. The projects are notable not only for their magnitude and the method in which they will be developed, but also for their unique tolling and financial characteristics.

The Projects

With construction costs of $2.7 billion for the I-635 and $2 billion for the NTE, these projects are the largest transportation greenfield P3 projects in the United States. The projects are among the first managed lanes projects in the United States delivered through a toll concession P3. The Dallas Police and Fire Pension System is an equity partner in the private developer for both projects, making it the first pension fund to invest directly in infrastructure development in the U.S.

NTE was the first project to integrate a toll concession (for the initial segment) and a pre-development agreement (for the remainder of the project), allowing Texas DOT to benefit from linking the two segments together while recognizing the different environmental and other development time lines for the two segments.

Both projects successfully incorporated Alternative Technical Concepts, allowing each private developer to propose innovative technical solutions during the proposal process. This process resulted in significant savings.

Tolling Features

They are the first two projects to obtain federal tolling authorization under the United States Department of Transportation's Express Lanes Demonstration Program.

The local tolling agency, North Texas Tollway Authority, which has its own network of toll roads in the region, will perform toll collection services on the managed lanes. An intergovernmental agreement ensures that transponders used by any of the State's toll agencies are compatible and seamless to the customer.

The private developer can set tolls under a certain cap, and must increase or decrease tolls in accordance with a specified formula if it is necessary for tolls to exceed the cap in order to maintain the required 50 mph minimum speed. To the extent that toll revenues exceed specified levels, the private developer will share up to 75% of the excess toll revenues with the Texas DOT.

Financial Characteristics

The projects confirm the importance of Transportation Infrastructure Finance and Innovation Act (TIFIA) and private activity bonds (PABs) as financing mechanisms. The I-635 includes the largest amount of PABs for a U.S. toll road concession, and the NTE was only the second U.S. toll road concession to use PABs and the first without the use of credit enhancements. The TIFIA loans of $850 million for I-635 and $650 million for NTE are the second and third largest to close. (The Central Texas Turnpike, also in Texas, had the largest TIFIA loan in the amount of $900 million.)

Both projects include interest rate protection. The I-635 includes interest rate protection prior to financial close, generally capped by the maximum amount of public funds made available for the project. Both projects allowed a $250 million letter of credit to secure both performance by the design-build contractor and its payment obligation to subcontractors, as well as to protect the lenders.

The public funds for the I-635 will generally be paid towards the end of the construction phase and the public funds for the NTE will generally be paid proportionally during construction, ensuring that the private developer is investing its money into the project from the beginning.

The I-635 and NTE validate toll concession P3s as a viable method for delivering needed transportation projects in the United States. For example, with the I-635, Texas DOT was able to leverage $489 million in public funds to deliver a project worth over $4 billion including costs for design, construction, operations and maintenance. If past is prologue, the P3 market can expect more P3 toll concessions, as well as managed lanes projects, in the future. ▪

Cintra Innovation Meets I-635 Managed Lanes Challenge (2/09, p. 7)

Cintra soundly trumped its rival ACS Group in Texas this month by offering a much less costly solution for the I-635 managed-lanes project on the LBJ Freeway in north Dallas, one of the most complex transportation projects in the U.S. The Texas Transportation Commission conditionally awarded a 52-year comprehensive development agreement (CDA) to Cintra/Meridiam on Feb. 26, based on a "best value" determination. The $2.7-billion project is made possible by an $800-

million federal TIFIA loan from the US Dept. of Transportation.

Particularly helpful terms were negotiated for the federal government's subordinated loan from the Transportation Infrastructure Finance and Innovation Act (TIFIA) program. The private consortium may defer 75% to 100% of the payments on principal for up to 25 years, if toll revenues are insufficient to cover operations and maintenance, senior debt service and potential revenue sharing with Texas. The TIFIA office has allocated up to $70 million to cover the cost of subsidizing the 35-year loan. The private team anticipates kicking in another $30 million towards the subsidy costs so that it can borrow the full $800 million. The TIFIA interest rate was 3.64% on March 2.

Cintra estimates the I-635 project will create 1,500 to 2,000 jobs, once construction gets started next year or in 2011. “This seems to be a full employment act for North Texas,” said Texas Transportation Commissioner Ted Houghton.

The project includes dynamically priced managed lanes within the right-of-way of the I-635 beltway north of the city center, and elevated tolled managed lane direct connectors along I-35E. The project also completes a continuous frontage road system along I-635 from U.S. 75 to I-35E. All-electronic tolls will be priced based on continuously monitored demand, with the goal of keeping traffic flowing at no less than 50 miles per hour in all segments.

Up to $700 million in public funds were made available by the state to help bidders finance the project, but the Cintra bid taps just $445 million of that money. “It proves once again that this P3 model really works,” says Fred Kessler, Nossaman LLP, the Texas Department of Transportation (TxDOT) procurement advisor.

TxDOT estimates it would take $1.7 billion in public money, plus another $300 million in secured debt, to complete the same $2-billion construction project itself.

ACS Infrastructure Development proposed an alternative and more costly design that included both mined and cut-and-cover tunnels. ACS says its design would reduce the project footprint and the impact on traffic during construction. It would also cost $3.9 billion, including financing.

TxDOT will also be spared from operations and maintenance over the entire 17-mile span, including both tolled and untolled lanes, during the 52-year contract. The net present value of long-term O&M is pegged at $1.5 billion. (cont.)

Project Financing

Execution of the CDA is scheduled for April 28, at which time TxDOT will put the public money in escrow and the concession team will increase its bond from $50 million to $75 million. Once the CDA is signed, it will take about six months for TxDOT and the developer to finalize project management plans and then construction could begin. However, the contract allows financial close to be deferred for as long as 18 months to allow the consortium to seek better terms for bank debt. Thus, five years of construction won't begin until sometime between mid-2010 and mid-2011.

The financing team aims to move as quickly as possible, depending on market conditions. The 52-year term of the concession begins when the CDA is signed; so delaying financial close would mean less time to collect tolls. The initial financing plan of $2.678 billion includes $598 million in private equity, $445 million in public equity, an $800 million federal TIFIA loan and $400 million each in bank debt and private activity bonds. Macquarie Capital is providing financial advice.

Because of the plan to wait for better debt terms, the consortium does not have committed financing at this time. However, it has received support letters from National Australia Bank Limited, RBC Capital Markets, Barclays Capital and Calyon Credit Agricole.

The concession team may lose deposits of $75 million if it fails to reach financial close within about one year. For an additional $25 million deposit, the closing can be deferred for a total of 18 months. However, the money won't be forfeited in a number of circumstances, including the failure of the TIFIA office to provide financing on or after Oct. 1, 2009. The TIFIA program will expire Sept. 30, unless Congress extends or reauthorizes it.

High Stakes Partnership

Adding variable-priced toll lanes to the LBJ Freeway is the top congestion-busting priority for the Dallas area. The highway was designed for 180,000 vehicles a day, but now carries 270,000 a day. By 2020, an estimated 450,000 vehicles will use the corridor daily. Initial toll rates are pegged at $7 for a 13-mile trip during rush hour. High occupancy vehicles (HOV) with two or more people traveling at peak times will pay 50% of the full fare. The Regional Transportation Council will cover the other 50% until the metropolitan area achieves air quality attainment goals, at which time HOV discounts would end.

A success on this project will also provide a shot in the arm for TxDOT and its controversial drive to build new toll roads through concession agreements with private developers.

This is the third toll road concession to be awarded to a public-private partnership in Texas; a Cintra-led consortium is on track to finance, build and operate all three. Construction will begin this spring on segments 5 and 6 of SH 130 between Austin and San Antonio (PWF 11/08, p. 7). Cintra was also selected as the best value proposer in January to take on the $2-billion North Tarrant Express managed-lanes project in the Fort Worth area (PWF 1/09, p. 5.)

Cintra will use the same equity partners and construction team it assembled for the North Tarrant Express. Cintra will provide approximately 51% of the equity, Meridiam Infrastructure Finance about 41% and the remaining share will come from the Dallas Police and Fire Pension System. The design-build team is a joint venture of Ferrovial-Agroman, a unit of Cintra's Spanish parent Ferrovial Group, and Houston-based contractor W.W. Webber LLC, which Ferrovial purchased in 2005.

Webber, which has a large precast concrete capability, is one factor in Cintra's ability to keep costs and prices down. When Cintra was bidding for the right to finish and toll SH 121 in 2007, it estimated its construction costs at $560 million. The North Texas Tollway Authority, which ultimately won the project with a higher upfront concession payment, pegged its construction costs at $700 million. Cintra's parent, Ferrovial Group, didn't lose out entirely on SH 121, however. The NTTA awarded Webber a $220-million contract, its biggest ever, in September to build an interchange at SH 121 and U.S. 75.

The NTTA will provide toll collection services for the LBJ project.

Construction Challenge

Financing the project is not nearly as complex as building and operating it, says Jose Lopez, president of Austin-based Cintra US. The corridor will be expanded to 18-20 lanes by digging a giant trench in the center of I-635. Six new lanes with variable tolls will be built in the trench. Eight reconstructed untolled lanes will be cantilevered above the managed lanes. In addition, at least two lanes of frontage roads in each direction will be improved and made continuous. Lopez says such a system of managed lanes, free lanes and frontage roads exists nowhere else in the world.

"This is not something for newcomers, that's for sure," Lopez says. Adds Joe Aiello, senior investment director for Meridiam: "The financial model is one thing. You really have to deliver on implementation." n

Nossaman LLP and KPMG advised TxDOT during the evaluation process. n