SH121: Bans and BANs

01/12/2007

The North Texas Tollway Authority has taken over the concession for the SH 121 toll road concession. The NTTA, a publicly-owned authority that serves the part of North Texas centred on Dallas-Fort Worth, paid $3.197 billion to the Texas Department of Transportation (TxDOT), another state agency, for the right to build and operate the road. It funded the payment, and construction on the road, through a $3.487 billion bridge financing.

The payment ends, as far as TxDOT is concerned, the protracted struggle over the 42km road's financing. The bridge financing, structured as a bond anticipation note (BAN) issue, must be refinanced within 12 months with a longer-term permanent note issue. The NTTA and its adviser, RBC Capital Markets, will be working on a refinancing.

BANs are a common instrument in municipal finance, and are typically used to start construction on a project where long-term funding is not yet available, although they have never been used to fund a concession payment of this size. The notes, due on 19 November 2008, and callable from 3 March 2008, were priced at 4.125%.

The underwriters of the bonds were Lehman Brothers, which took the lead on the transaction, Citigroup and Bear Stearns. Of the three underwriters, only Bear Stearns lacks an established project finance group, and the remaining two have been working to establish a position in US PPP. Citigroup, for instance, co-underwrote the refinancing of Cintra's Skyway concession.

The NTTA bonds invite comparisons with earlier PPPs because the SH121 concession was once destined for Cintra. The struggle between the NTTA, TxDOT and Cintra over the project played out for the last seven months, and embodies the debate, until now largely theoretical, over whether project or municipal finance was the best way of financing new roads in the US.

The NTTA offered a larger payment to TxDOT than Cintra for the right to build and operate the road, even if the two proposals cannot be easily compared, since they use different financing assumptions. But the decision by TxDOT and the gaggle of authorities with overlapping oversight of the project to overturn their earlier decision to award the concession to Cintra was always as much about policy as financial best practice.

Cintra's bid was the indirect victim of an upsurge in sentiment against private – and foreign – ownership of transport assets in the US. The SH121 was not covered by the ban on PPP concessions that Texas' governor signed into law in June 2007. But the ban emboldened the Tollway, which had previously declined to bid on the road, to mount a late challenge to Cintra's bid.

The challenge was late, was opportunistic, and upset both the CDA proponents within TxDOT and their ideological counterparts in the Federal Department of Transportation. USDOT approved for a $1.866 billion allocation of tax-exempt private activity bonds (PABs) for SH121in late 2006, and the road was all set to be a showcase for the untried road funding mechanism.

Instead, the NTTA used its own tax-exempt capacity, as well as the revenue from its existing road network, to fund construction on the SH121 and the concession payment. Cintra would have used a mixture of bank debt, the PAB allocation, all without recourse to its other road holdings, and its own equity to fund the concession.

RBC has a franchise in both municipal finance and PPP, and was at pains to stress that the approaches are complimentary. Its head of municipal finance, Rebecca Hefflin, offered the following formula: "While both NTTA and RBC believe that the private sector has an important role to play in delivering essential infrastructure, the NTTA has proven that a well-run publicly owned tollroad system may well provide more cost effective financing and a better alternative in instances where the risk profile of the project is acceptable under public standards."

The NTTA offers several advantages over a one-off concession. It has an advanced, efficient toll collection system, a good reputation for running toll roads, and an influential political following. It can borrow at low rates, since it is rated A1 (Moody's) and even after downgrades, S&P still has its rating at A, and Fitch has it at A-. The BANs, as short-term obligations, have SP-1 (S&P) and MIG-1 (Moody's) short-term ratings.

But the bonds do not simply have recourse to the project and its cashflows, since they are general obligations of the NTTA and serviced through the revenues of the entire toll system. Since the authority cannot raise equity capital to contribute to the concession fee, and a debt financing based purely on the project's cashflows, such an arrangement is inevitable. It means, however, that its scope for further financings is limited.

The fact that the NTTA's ability to take on further concessions is limited explains the relaxed attitude of banks towards the SH121 reversal. Even with severe restrictions on future concessions in the state, whose efficacy advisers and politicians still dispute, there remain several opportunities for lenders. Cintra's SH130 5 and 6 sections concession is probably the nearest to market.

The SH121 financing does not bring an end to the nascent PPP market in Texas, but its does cap its potential. The tastier concessions will migrate towards the public toll agencies, with the private sector left to take on the more challenging sections. Austin's brief reign as the capital city of US PPP has faded.

North Texas Tollway Authority
Status: Bonds closed November 20, concession transferred 1 December
Size: $3.487 million
Location: Texas
Description: Municipal bridge financing for publicly-held concession of a 42km toll road
Borrower: North Texas Tollway Authority
Financial adviser: RBC Capital Markets
Bookrunners: Lehman Brothers, Citigroup, Bear Stearns
Bond counsel: McCall Parkhurst
Underwriter counsel: Andrews Kurth