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Fort McMurray West transmission, Canada

Rene Lavanchy

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In December 2014, Alberta Electric System Operator awarded the Fort McMurray West transmission line project to Alberta PowerLine, a consortium of Atco-controlled Canadian Utilities (80%) and electrical engineering contractor Quanta Services (20%).

The Fort McMurray project is viewed by those involved as a P3 project, most likely because of its availability-based payment mechanism; but it has four important aspects that make it unique among all the many and various such projects procured in Canada over the years.

Firstly, it is a high-voltage transmission line, well outside the normal P3 sectors. Secondly, the private sector owns the asset outright. And thirdly, instead of carrying out the necessary development work – permitting, environmental approvals, route selection and right-of-way acquisition – before awarding the project, the authority passed all of this to the winning bidder.

Alberta PowerLine did not really win the project in December 2014, but a 'project development agreement' under which the winner agreed to carry out development work, as well as engineering and design, and then enter into a subsequent project agreement to build and operate the project. The development phase was expected to last 2.5 years and the winning bidder had to submit a performance bond of C$15 million to guarantee their obligations. If right-of-way could not be secured in time, for example, this amount might become forfeit.

Despite this additional risk, the procurement was a commercial success. Five consortia formed to bid for the project, and four submitted bids. Alberta PowerLine saw off competition from the following rival consortia:

- Altalink/AEP/SNC Lavalin/Burns and McDonnell
- Epcor/LS Power/Kiewit/Sargent & Lundy
- MidAmerican Energy/TransAlta.

The winning bid was based on the lowest net present value of availability payments requested; the winners bid C$1.433 billion ($1.12 billion) in 2019 dollars.

Paul Blundy, a partner at law firm Bennett Jones which advised Alberta PowerLine, views the multi-phase procurement as a positive as it allows for greater innovation. "The advantage is that the private sector can engage earlier and bring in efficiencies earlier," he says.

Financing

The development phase began in December 2014 and lasted until the spring of 2017, whereupon the consortium turned to financing. Because the project was bid before development work had been done, bidders did not have financial

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commitments when they submitted their proposals. For the same reason, project costs were subject to adjustment following the development phase, with the authority sharing in certain savings.

This led to the fourth innovation of the Fort McMurray project: an authority-mandated debt financing competition. This allowed AESO to bring in the competition on financing that was inevitably absent earlier on. “One of the big knocks on Canadian P3 is that private sector financing is more expensive than public sector financing. The public sector having visibility of this financing is something I think could be replicated elsewhere,” Paul Blundy suggests.

The eventual financing solution was similar to what is seen in many Canadian P3 financings: RBC Dominion Securities and CIBC arranged C$1.38 billion of bonds in two pairs of roughly equal size and tenor:

- C$548.63 million bond with 36 year 1 month tenor
- C$548.61 million bond with 36 year 4 month tenor
- C$143.68 million bond with 14 year 11 month tenor
- C$143.76 million bond with 14 year 7 month tenor

The sponsors committed about C$178 million of equity largely unfunded at close, for a debt-to-equity ratio of around 89:11.

The bonds were fully drawn down at financial close, which took place on 2 October, although the financial documentation includes features to mitigate negative carry. Unlike many Canadian P3s, the project does not feature milestone payments during construction, a fact reflected in the lack of construction-term bank debt.

Moody’s rated the bonds A2 in September 2017, noting that the project had already been substantially de-risked during the development phase. By the time of financial close, development work had been signed off and construction had started, so that lenders were not exposed to development risk. The construction method was tried and tested, and some of those involved appraised the construction risk as lower than for light rail projects.

Moody’s also noted the experience of the design and build consortium – a joint venture of Atco and Quanta subsidiary Valard – in building transmission lines in Alberta, and said the risk of the consortium being terminated and replaced was very low. The security package is understood to have terms common to Canadian P3 deals.

Average DSCR was predicted by Moody’s to be 1.25x, with specified distribution test DSCR of 1.15x and event of default DSCR of 1x.

Despite the project’s novelty, pricing was tight by Canadian P3 standards. The 36-year bond tranches both priced at a spread of 155bp over the Government of Canada benchmark, and the 14-year bonds at 123bp.

Construction is due to last 21 months from financial close and availability payments will run for 35 years, leaving a short tail between bond maturity and final payment.

AESO may well choose to replicate the project structure on the Fort McMurray East transmission project, a nearby project of similar scale which is currently under consideration. Beyond that, the unusual requirements of this project suggest that, however successful it proves to be, similar transmission line deals are not very likely.

Advisory roles

Torys was legal adviser to the lenders, and Altus Group was technical adviser. For the sponsors, RBC was financial adviser and Bennett Jones was legal adviser. For the authority, PwC was financial adviser, Norton Rose Fulbright was legal adviser and P1 Consulting was fairness adviser.

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