Pennsylvania Rapid Bridge Replacement PPP, US

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The Commonwealth of Pennsylvania's first PPP – the $1.12 billion Pennsylvania Rapid Bridge Replacement project – is also the first US PPP to bundle a large group of assets in a single transaction.

US states have primarily used PPPs to procure large, bulky and complex sections of road. They have used the structure on tunnels and managed lanes, though social infrastructure has recently gained in popularity.

The Rapid Bridge Replacement PPP involves the rehabilitation of 58 bridges and managing a large number of local subcontractors. If Pennsylvania can demonstrate that bundling offers value-for-money, other states may turn to PPP to clear their substantial maintenance and upgrade backlogs.

Trouble-free financing

About $721.5 million in serial and term private activity bonds (PABs) make up the bulk of the Rapid Bridge Replacement PPP's financing, and priced on 24 February 2015 for an all-in interest cost of 4.1%. JPMorgan and Wells Fargo underwrote the bonds.

The response to the bonds, which carry a rating of BBB from Standard & Poor's, was so strong – and the eventual yield on the bonds so low – that the underwriters were able to price the bonds at a premium to par and reduce the size of the issue from a planned $732 million.

The financing does not feature any bank debt despite the presence of large milestone and completion payments from the Pennsylvania Department of Transportation (PennDOT). Sponsors often tap bank debt to finance construction through the receipt of such payments.

The $793 million in proceeds of the bonds, which have a final maturity of 2042, complement $59 million in equity from Plenary Group (80%) and Walsh (20%), $225 million in payments from the state, $35 million in availability payments during construction and $5 million in interest income during construction.

The bulk of the proceeds will go towards the $899 million design-build contract to upgrade the bridges, with interest payments during construction ($99 million), and fees and other financing costs ($41 million) accounting for much of the rest. The bonds, issued through the Pennsylvania Economic Development Financing Authority, settled on 18 March.

The financing continues Plenary's expansion into the US market. Rapid Bridge Replacement PPP is Plenary's third US PPP, and its second there as an equity investor.

Sprawling work programme

Before the Pennsylvania bridges PPP, no ready precedent existed for such an endeavour.

Missouri upgraded 550 bridges in 2008, but under a single design-build contract. The UK, Canada and Belgium have procured bundles of schools – which have a straightforward risk profile – as PPPs. But bridges have acquired the status of bellweather for the health of US infrastructure.

The American Society of Civil Engineers, a hardly disinterested body, rates the state of US bridges as C+, while the US Federal Highway Administration says that 11% of US bridges are structurally deficient. Pennsylvania is a comparative latecomer to PPP, and failed in an earlier effort to close a long-term concession for the state's turnpike.

But it passed PPP legislation in 2012, and PennDOT established a public private partnerships office later that year.

The bridges deal is one of three flagship PPPs – alongside a wireless telecoms partnership and a network of compressed natural gas refuelling stations – and was thus best-positioned to attract interest from the US' private infrastructure industry.

Even then, the 58 bridges are spread out across the entire state, will cost an average of $1.6 million to upgrade, and will employ at least 18 local subcontractors. The lead design & construction contractor, an unincorporated joint venture owned by Walsh (60%) and Granite (40%), will have to manage this sprawling project, though it will be able to stagger some of the work.

Despite the vastness of the project and Pennsylvania's comparative PPP inexperience, PennDOT attracted five bids, with Meridiam, Macquarie, InfraRed and John Laing serving as lead equity sponsor on the four losing bids. The procurement moved at a brisk pace: PennDOT fielded the five bids by February 2014, cut the Macquarie consortium and shortlisted the four others in March 2014, and picked the Plenary consortium in October 2014.

Uncertain political backdrop

PennDOT reached commercial close with project company Plenary Walsh Keystone Partners on 12 January 2015, a little more than a week before Tom Wolf, a Democrat, took office as Pennsylvania's governor. Wolf defeated Tom Corbett, a Republican who had championed PPP in Pennsylvania.

The state's office has been muted since Wolf assumed the governorship, and he has revealed little about his thoughts on the use of PPPs. But Wolf ran on his business credentials, and served in the cabinet of Ed Rendell, the governor from 2003-2011, and who launched the failed effort to lease the state's turnpike.

The bonds' all-in interest cost, at 4.1%, is not far off the 3.35% that Pennsylvania paid for 20-year money earlier in 2015, so the programme should not fall victim to simplistic comparisons of borrowing costs. The bridge upgrades are spread throughout a large number of voting districts, unlike single-project concessions.

Milestone and completion payments make up a small proportion of total costs, and will pay down the shorter-dated serial bonds. The department will make availability payments to the project company over the rest of the design-build-finance-maintain concession's 28-year term.

Whether or not Pennsylvania sticks with its PPP programme, the bundled approach may feature again elsewhere in the US. A package of bridge rehabilitations lacks the glamour of a single greenfield development, but the process is suited to the infrastructure requirements of the north-eastern US, where existing, rather than new infrastructure, is more of a priority.

KPMG and PFM (financial), CDM Smith and Lochner (technical), URS (project management), and Allen & Overy (legal) advised PennDOT on the bridge PPP. The bond counsel was Ballard Spahr and the construction quality adviser was TRC. The lenders' technical advisers were INTECH (insurance) and BTY (independent engineer), while Ashurst was legal adviser. HDR is engineering adviser to the design-build contractor. Legal advisers to the sponsors include Fasken Martineau DuMoulin, Duane Morris, and Gowling Lafleur Henderson. Dorsey & Whitney was legal counsel to US Bank, the bond trustee.