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## NSW's rail future on the fast track

The New South Wales Government's long-term transport plan has taken a giant step forward with the financial close of the operations contract on the North West Rail Link – Australia's biggest public transport project. Allens partner **Phillip Cornwell** and Senior Associate **Scott McCoy**, who worked on the transaction, reflect on the drivers to bring such a significant project together and, in turn, set the groundwork for a major transformation of Sydney's public transport system.

On 15 September 2014, the New South Wales Government formally awarded the Northwest Rapid Transit consortium (**NRT**) the operations contract to deliver Australia's largest public transport project, Sydney's A\$8.3 billion North West Rail Link (**NWRL**). The A\$3.7 billion Operations, Trains and Systems contract is the largest Public Private Partnership ever awarded in NSW and the final of the three major contracts to deliver the NWRL. The project is the first stage of Sydney Rapid Transit, the city's new rapid transit railway and a key plank of Sydney's Rail Future – the Government's plan to modernise Sydney's trains. Financial close was achieved a mere three days later, the culmination of a process which started years earlier and a testament to both the efficient process by which it was run and the high level of support enjoyed by the project.

### Context

With aging rail infrastructure reaching capacity limits and the greater Sydney population of 4.5 million expected to swell to almost 6 million by 2031, the NSW Government developed Sydney's Rail Future, a long term plan to increase the capacity of Sydney's rail network through investment in new services and through upgrading existing infrastructure. The plan aims to modernise and transform Sydney's rail network with the introduction of a new rapid transit network – a new tier of services that will work together with the current suburban rail network.

The North West Rail Link was identified as the first stage of this new rapid transit network.

It will deliver a train every four minutes in the peak – or 15 trains an hour – using a new generation of rapid transit trains. It will be the first fully-automated railway network in Australia.

Detailed planning for the North West Rail Link was completed by the end of 2012 and, by 2013, tenders for all the major works associated with the NWRL had been called, with the works and future operations split into three major contracts:

- › Tunnels and Station Civil Works package, a A\$1.15 billion contract awarded to the Thiess John Holland Dragados consortium on 24 June 2013 as a standard D&C contract, which involves building 15 kilometre twin tunnels, the longest railway tunnels ever to be built in Australia;

- › Surface and Viaduct Civil Works package, a A\$340 million contract awarded to Salini Impregilo on 17 December 2013 as a standard D&C contract, which involves building a four kilometre elevated skytrain; and
- › the A\$3.7 billion Operations, Trains and Systems (**OTS**) package.

The final of the three packages, the OTS package, was tendered as a PPP.

## The project

The NRT consortium will design, build, finance, operate and maintain the 36km rapid transit train service. A typical availability-payment model will be used, with service payments from the State payable once operations commence following completion of construction, and the State taking patronage risk. Fares will be set by the NSW Government in line with the rest of the Sydney railway network, which will also be responsible for the electronic ticketing system.

A four way unincorporated joint venture comprised of John Holland Group, Leighton Contractors, MTR Corporation and UGL Rail Services (the **D&C JV**) is responsible under a D&C contract with NRT for delivery of the greenfield infrastructure and associated rail systems, including:

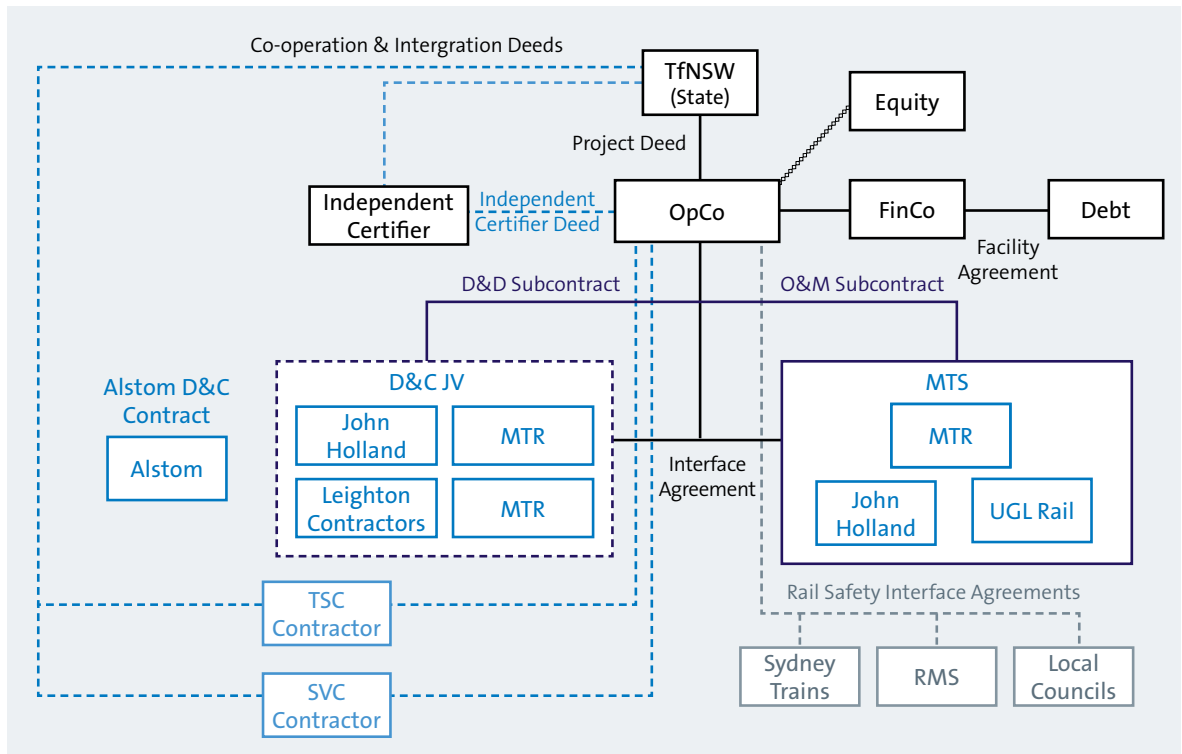
- › construction of 23km of new rail network from Cudgegong Road to Epping in Sydney's north west, including installation of signalling and mechanical and electrical systems;
- › eight new railway stations and 4,000 associated car parking spaces;
- › platform screen doors running the full length of platforms;
- › construction of the Rapid Transit Rail Facility at Tallawong Road, to house and maintain Sydney's new rapid transit fleet; and
- › a state-of-the-art Operations Control Centre, also based at the Tallawong Road facility, to monitor the entire railway, ensuring safe and reliable running.

In addition, the D&C JV is responsible for:

- › the conversion and upgrade to rapid transit standards of the existing 13km railway between Epping and Chatswood; and
- › upgrading five existing stations and converting them to rapid transit standards, including computer based train control, full length platform screen doors, improved information displays and upgrades to fire and life safety systems.

Rail supplier Alstom has been subcontracted by the D&C JV to project manage, design, supply, manufacture, test and commission the rolling stock and signalling system. This will include the supply of 22 Metropolis train sets and the communications based train control signalling system. The new trains will be fully-automated, the first in Australia.

An incorporated joint venture comprising Hong Kong's MTR Corporation, John Holland and UGL Rail Services, will operate and maintain the rapid transit network on completion for the 15 year concession period.



Services will start in the first half of 2019, with the new rapid transit trains running every four minutes during peak hour (15 trains an hour). Key operational performance requirements include an on-time running rate of 98% and availability of 99.5%. Although the North West Rail Link will initially use six-carriage trains, more carriages and trains can be added as demand increases, with the platforms designed to be long enough for eight-carriage trains.

## The key players

The Northwest Rapid Transit consortium is comprised of MTR Corporation, John Holland, Leighton Contractors, UGL Rail Services and Plenary Group, who acted as financial sponsor and capital arranger.

Equity financing will come from three of NRT's consortium members, MTR Corporation (20%), Leighton Contractors (10%) and Plenary Group (10%) and will also include equity investments from Palisade Investment Partners (20%), Partners Group (20%) and Marubeni Corporation (20%).

Debt was provided by three of Australia's major banks in ANZ, NAB and Westpac as well as international banks Standard Chartered, BTMU, ING, HSBC, Mizuho and OCBC.

NRT was advised by Ashurst Australia, while the bank group was advised by a team from Allens. Clayton Utz advised the NSW Government.

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## The bid and financing process

Expressions of interest for the NWRL were called by the NSW Government in December 2012, kicking off an extensive five month process. The NRT Consortium was included in the shortlist of two bidders when it was announced on 30 April 2013, with bids due on 5 December 2013. The competing bidder was TransForm, a consortium comprised of Serco Australia, Bombardier Transportation Australia, SNC-Lavalin Capital, McConnell Dowell Constructors (Australia), John Laing Investments and Macquarie Capital Group.

Following a six week BAFO process, the Northwest Rapid Transit consortium was announced as the preferred bidder on 24 June 2014. The NSW Government had earlier announced that it would contribute to the bid costs of the unsuccessful shortlisted OTS consortium submitting a conforming proposal, intended to reflect the size and complexity of pulling together a proposal for the NWRL contract. Welcomed by the market, this approach is now being more widely adopted, with the Victorian Government also having revised its PPP requirements, announcing in May 2014 it would trial repayment of partial bid costs to encourage competition and attract high-quality bids. The New Zealand Government has also adopted this strategy, agreeing to reimburse costs on its first road PPP, the \$1 billion Transmission Gully project.

An intense 12 week period followed the announcement of NRT as preferred bidder to bring the NWRL project to contractual and financial close. As is often the case, a number of issues were outstanding even at the conclusion of the BAFO stage, and during this time all parties worked tirelessly but constructively to resolve them. Of critical importance to the NSW Government was ensuring that the documentation was sufficiently flexible to allow it to implement its long term Sydney's Rail Future plan. In particular, the NSW Government was focussed on its ability to extend the new rapid transit system from the end of the North West Rail Link at Chatswood under Sydney Harbour, through the CBD with new city stations and then west to Bankstown.

Whilst recognising the importance of flexibility to the State, this had to be balanced against the need for certainty required by the banking group and its focus on ensuring that adequate measures were in place.

The parties worked hard to resolve and document these issues by the target date for contractual close, set months in advance. This was a Herculean effort given the size and complexity of the project, the rail safety and accreditation requirements and interface requirements with other stakeholders, including local councils, Sydney Trains, the government's electronic ticketing system and the civil works contractors responsible for the TSC and SVC works. The NRT consortium, advised by Plenary Group, was widely lauded as running a highly efficient bid and closing process.

Just as impressive was the project reaching financial close just days later, the result of the various advisory teams, including consortium and banks' counsel, ensuring that the project was efficiently and effectively managed, with key documentation and CP workstreams running in parallel with negotiations from the announcement of preferred bidder. The result was a rare smooth financial closing, delivered in what one banker described as a "Zen atmosphere". If only all transactions closed in such manner.

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## Funding

The project's total private capital is over A\$1.8 billion, including a 7.5 year senior debt facility of approximately A\$1.55 billion. The financing was structured using a securitised licence structure, an additional layer of documentation but with which parties are now familiar, its use well established by precedent transactions.

Equity was contributed by way of deferred equity, subject to appropriate equity support being provided for uncalled equity amounts. Consistent with precedent transactions, equity contributions are able to be accelerated following certain events, including an event of default under the financing documents.

The remainder of the financing is to be provided by the NSW Government by way of a 'State Construction Contribution' (**SCC**). Sized at 50% of the total delivery phase project costs (including financing fees and interest during construction) as at financial close, the SCC will consist of monthly construction payments during the delivery phase. This will only be available for utilisation, however, upon certain conditions having first been satisfied, including a minimum contribution of equity having been provided and the construction of the project having advanced to a certain level.

Although the debt tenor of 7.5 years is consistent with recent Australia market terms for debt of this nature, it is shorter than the concession period. This is an issue in financing PPPs in Australia generally, a product of the dominance in Australian project finance of bank lending and the lack of a long-dated project bond market. The Basle III rules and their conservative implementation by the Australian banking regulator, APRA, are not calculated to encourage banks in Australia to lend long term. Arguably the PPP bidding process incentivises bidders to bid the lowest cost of debt, even though any refinancing gains are shared with the public sector. Bidding short term bank debt and taking refinancing risk is the norm.

This risk is partially mitigated in the NWRL transaction by the State proposing the now well-accepted conditional debt pay down ('CDPD') structure. Under this simpler variant of the 'supported debt model' the State agrees to make a lump sum contribution equal to 50% of the senior debt between two and four years post-construction, i.e. when the project has been 'de-risked'. The State's obligation to pay is subject to certain conditions having first been satisfied and the payment being allocated in its entirety to prepay outstanding senior debt.

The debt facilities were hedged using interest rate swaps until the second anniversary of the scheduled date for completion of construction, the anticipated date of the CDPD. After this date, the State bears the floating interest rate risk (net of margin), implemented by way of a floating rate mechanism in the availability charge.

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## Conclusion

The North West Rail Link was a transaction with a number of firsts – the first stage of a new rapid transit railway network for Sydney; the first time fully-automated trains have been used in Australia; the biggest PPP in NSW history; and the first time Sydney commuters won't need a timetable – they'll just turn up and go.

It has laid the groundwork for a major transformation of Sydney's public transport system. As flagged in *Rebuilding NSW: State Infrastructure Strategy 2014*, the State Government has committed – subject to an electoral mandate – a further A\$7 billion for Sydney Rapid Transit, which will extend the North West Rail Link to deliver a new rapid transit rail line under Sydney Harbour, through the CBD and to Bankstown in Sydney's West. The new plan would see construction on the second harbour rail crossing accelerated, with funding expected to flow from 2016-17, construction commencing in 2017 and completion by 2024.

While it may not have been the first time that a project reached financial close only a few days after contractual close, the speedy close was a testament to the dedication, effort and cooperation of all participants in the project – government, contractors or financiers, and their advisers – and evidence of the efficient process applied to bring the deal to a successful close. Let's hope that all future deals should be so lucky.