North American Infrastructure Deal of the Year 2005

Neptune: Private cable

The biggest project financing and the longest construction period (24 months) financing to close in the US traditional private placement market, the $647 million Neptune subsea transmission cable project is the first US transmission/wires financing since the Path 15 facility in 2003.

The financing is backed by solid offtake and construction packages and received $1 billion-plus in initial bids. It also features a novel interest rate hedge – Treasury rate locks with delayed takedowns from institutional investors.

Neptune is a 65-mile 500-kv 660MW HVDC underwater transmission cable between Sayreville, New Jersey and Levittown, in Nassau County, Long Island and was the first private investor IPP transmission development to get off the ground in the US. The project is designed to bring power from the high capacity PJM East market to the capacity and transmission constrained Long Island Power Authority (LIPA).

The project began in 2001 as a highly ambitious $4 billion subsea cable system connecting generating capacity-rich regions in Maine, New Brunswick and Nova Scotia with capacity-constrained markets in Boston, New York City, Long Island and Connecticut. The project was to run from four 1200MW interconnections in New Brunswick, Maine and New Jersey to interconnections in downtown Boston, downtown New York City, Long Island and Connecticut – allowing the transmission of 3600MW of power from Maine and Canada to the northeastern US. In addition, Neptune was to facilitate transfers of 1200 MW of power from the PJM region to the New England Power Pool (NEPOOL) and the NYPP.

The downturn in US merchant power meant that by 2003 the project was looking for a new business model. In May 2003, LIPA – which has long suffered from capacity constraints and elderly and inefficient oil-fired capacity – issued a request for proposals for baseload capacity. Neptune was selected from a field of 14, in June 2004 and signed a 22-year contract for 660MW of capacity on 29 September 2004.

The project's developer is Atlantic Energy Partners – a consortium of Cianbro Corporation, ESAI Power, Standard Energy Development, CTSBM Investments and Boundless Energy – through special purpose company Neptune Regional Transmission System. But the $97 million of equity in the deal ultimately came from Energy Investors Funds and Starwood Capital: EIF's investment initially took the form of a convertible loan, which allowed the developers to access early stage capital, and EIF to manage its exposure to the project.

For LIPA, the cable is a useful and flexible means of diversifying away from independent power producers on Long Island: LIPA has also looked at a 150MW offshore wind proposal and a 300MW gas-fired plant which is still set to go ahead. Neptune also provides an alternative to the Cross-Sound cable from Connecticut, which was at the centre of a dispute between Long Island and Connecticut until its settlement in June 2004.

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Although less ambitious than its original incarnation, Neptune was finally a realistic contender for financing.

Arranged by SG CIB with SG Securities as private placement agent, the financing comprises $550 million in 22-year bonds and a $52 million letter of credit. The bonds priced at an unconfirmed 175bp over the equivalent Treasury, for an all in cost of less than 6%. The L/C – provided by DZ Bank and AIB – priced at 150bp and largely supports the obligations of the project to LIPA.

The 22-year contract with LIPA was key to making the deal bankable. LIPA has a rating of A3/A- (S&P/ Moody's), and as the main counterparty, and by far the most substantial credit risk, made the project a candidate for an investment grade rating.

The contract, which specifies payments based largely on the availability of the project, does not expose the cable's owners either to volume or price risk. And the project is expected to produce very stable revenue streams, with limited excess returns available if it consistently reaches high availability levels.

On the construction side, risk is also minimised by EPC contractors Siemens and Pirelli are EPC providing substantial and tight guarantees for their share of work.

At time of financing, rumour in the market was that a competing bid from WestLB using a monoline wrapped bond from FSA could have made the project significant debt savings. But according to Ed Stern, CEO of Neptune, there was little to choose between the bids. "We looked at the balance between pricing and execution risk and followed the path of least resistance. The project needed to get underway and the savings on a wrapped deal were negligible and offset by the added complexity."

Neptune has created a solid template for private transmission financing in the US. The question is, having completed Long Island, will the original project, or at least elements of it, reappear in the market at a later date. ■

Neptune Regional Transmission System

Status: Closed July 2005
Location: Long Island to New Jersey, USA
Description: Private placement backing development of 65-mile subsea transmission cable
Sponsor: Atlantic Energy Partners
Equity providers: Energy Investors Funds, Starwood Capital Group
Lead manager and financial advisor: SG
Participants: AIB; DZ Bank
Debt: $550 million
Equity provider legal: Chadbourne & Parke
Developer legal: Skadden Arps
Underwriter legal: Milbank Tweed
Independent engineer: Stone & Webster
Environmental: Tetra Tech
EPC contractors:
Siemens Power Transmission; Pirelli Power Cables Systems