

CONSTRUCTION

ALERT

ALLOWABLE USER FEE OR UNCONSTITUTIONAL TAX? THE TERMS OF THE ELIZABETH RIVER CROSSING PUBLIC PRIVATE PARTNERSHIP

By Jessica Perro

The future of Virginia's Public Private Partnership Projects (P3s) hangs on the Virginia Supreme Court's ruling on the Elizabeth River Crossing Project, a bundled project encompassing the rehabilitation of two existing tunnels, and the construction of one new tunnel which will connect Norfolk and Portsmouth (Project). The dispute concerns the legality of charging tolls on the two existing tunnels in order to finance the construction of the third tunnel. Ultimately, the decision hinges on whether the Supreme Court of Virginia considers the tolls on the two existing tunnels to be an impermissible tax, or a permissible user fee.

Because the General Assembly is prohibited from delegating its power to tax, the entire funding of the project could fall apart if the Supreme Court of Virginia agrees that the tolls on the already-existing facilities are taxes, not user fees. If the funding arrangement is struck down, the ruling could have a limiting effect on future transportation projects in Virginia and may prompt litigation in other states with similar arrangements. P3 projects will still have a place in Virginia, but the 'bundling' aspects may be severely restricted, potentially delaying new construction and improvements. If the tolling is upheld as a permissible user fee, the Elizabeth River Crossing Project financing arrangement could become a model for bundling future transportation projects in Virginia, and serve as a way to make the projects more enticing to private entities.

The Project and the PPTA

The Elizabeth River Crossing Project scope included the construction of a new two-lane tunnel under the Elizabeth River adjacent to the existing Midtown Tunnel, thereby doubling the vehicular capacity at that point. Additionally, the Project includes an extension of the Martin Luther King Freeway and the rehabilitation of the existing Midtown and Downtown Tunnels.

The Concessionaire for the Project, Elizabeth River Crossings, entered into a Comprehensive Agreement with the Virginia Department of Transportation under the Public Private Transportation Act (PPTA), VA Code §56-556 *et seq.* Under the statute, the Virginia Department of Transportation has the ability to enter into agreements with private parties to construct and operate transportation facilities. The operation of the facilities includes collecting tolls as a "user fee" that helps pay back debt incurred in the construction. The purpose of the statute includes enabling Virginia to develop and operate transportation facilities in a more efficient and less costly fashion.

The statute was enacted almost 20 years ago and many projects have been successfully completed under it. A well-recognized P3 project recently completed in Virginia is the Capital Beltway (I-495) HOT Lanes. Currently, there is a \$119.5 million agreement between the Virginia Department of Transportation and Branch Highways, Inc. to build the next portion of Route 58. Other potential PPTA projects

include Route 28, and the Coalfields Expressway. Virginia is also contemplating a public private partnership for I-95 HOT Lanes, the Route 460 Corridor Improvement, I-66 Corridor Improvements and the Hampton Roads Bridge Tunnel.

The Elizabeth River Crossing Project has a unique twist to it that other projects under the PPTA do not. Typically, P3 projects only set tolls on the same transportation facilities they constructed. In this case, however, the Comprehensive Agreement at Elizabeth River Crossing provided for the Concessionaire to set tolls not only for the new tunnel being constructed, but also for the already-existing tunnels that they were rehabilitating. Additionally, it appears that the tolls collected on the already-existing tunnels are not used to pay off the debt incurred for their rehabilitation, but rather to help fund the construction of the new tunnel.

The Comprehensive Agreement states that the total cost of the project was estimated to be about \$2.1 billion, and the funding of the project is somewhat complicated. Under the Comprehensive Agreement, the Virginia Department of Transportation has agreed to contribute \$362 million. The private company agreed to obtain a loan for \$422 million under the federal Transportation Infrastructure Finance and Innovation Act and will provide the remaining amounts through investments, other borrowing, and of course – toll revenues.

The Lawsuit

For over a year, the Virginia Department of Transportation has been defending a Comprehensive Agreement related to the Downtown Tunnel/Midtown Tunnel/Martin Luther King Freeway Extension Project. In 2012, Virginia residents filed a lawsuit against the Virginia Department of Transportation, focused on the so-called ‘bundling’ of three tunnels. Notably, the plaintiffs do not challenge that the tolls in the Elizabeth River tunnel itself are impermissible, but rather, the plaintiffs claim that charging a toll in either the Midtown or Downtown tunnel

to help finance the building of the Elizabeth River tunnel is improper. According to the plaintiffs, the Midtown and Downtown tunnel fees are not a “bona fide fee-for-service, but a device to generate revenue to construct those new facilities.” The plaintiffs argue that the financing “scheme” amounts to a tax, the imposition of which is a legislative power. They argue that the PPTA does not grant (nor could it grant) the Virginia Department of Transportation the ability to tax. Accordingly, the Comprehensive Agreement tries to delegate the power to tax to a private company, something which it cannot do.

As part of the challenge, the plaintiffs point to the fact that the Midtown and Downtown tunnel projects were paid for decades ago. The original Downtown Tunnel project opened in 1952, and included the Berkley Bridge. The debt incurred to fund the project was paid off through tolls on the facilities. Ten years later, in 1962, the Midtown Tunnel project was opened and similarly funded through tolls collected. The tolls on both facilities were stopped in the 1980’s.

At the trial level, Judge James A. Cales Jr. agreed with the residents. In his May 2013 oral ruling, Judge Cales Jr. declared that the Comprehensive Agreement between the Virginia Department of Transportation and Elizabeth River Crossing violated the Virginia Constitution. He reasoned that the bundling of the tunnels and the resulting tolls was done solely to produce revenue, and thus a tax. The litigation is now before the Supreme Court of Virginia. Oral argument was heard in September, and the Supreme Court of Virginia is expected to issue a ruling in early November, in time for the next General Assembly to act in response to the Court’s decision. Fox Rothschild is following the issue and will follow-up with further implications when a decision is released.

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