The joint subcommittee studying public-private partnerships related to seaports in Virginia held its sixth meeting on September 24, 2009. The legislative members in attendance were Chairman Purkey, Senators Wagner and Lucas, and Delegates Cosgrove, Joannou, and A.T. Howell. Messrs. Cofer, Godfrey, Martinez, Milliken, Moye, Padgett, and Sisco were the nonlegislative members in attendance. Kevin Old attended on behalf of Fred Whyte.

Paul D. Fraim
Mayor
City of Norfolk

Mayor Fraim thanked the subcommittee for allowing him to expand upon his remarks from the previous meeting. He focused on the topic most relevant to the City of Norfolk and the other port host cities: the proposed tax exemption of privately operated port operations. He stated that Norfolk is proud to be the home to the Port of Virginia's largest and busiest facility, Norfolk International Terminals. For more than 300 years, international trade has defined the city. Mayor Fraim explained that the Port of Virginia has been developed and nurtured by Virginians for generations and that we owe it to those generations and to our future generations to be good stewards of the Port.

Mayor Fraim mentioned the recent Virginia Port Authority (VPA), Virginia International Terminals (VIT), and APM Terminals discussions that have been ongoing since December 2008 under a Federal Maritime Commission Discussion Agreement. Although he has been assured that these discussions are not part of the overall Public Private Transportation Act (PPTA) process or the bid review currently underway, he thinks such a development gives greater reason for pause and careful examination. Whatever the outcome, the long-range interests of the Commonwealth and the Port must be kept in view, regardless of how attractive short-term proposals may be.

Next, Mayor Fraim mentioned the three proposals submitted by CenterPoint, Carrix and the Carlyle Group. As he understands it, the Virginia Port Authority would remain an asset of the Commonwealth and continue to be exempted from real property, leasehold, and business property taxation under the provisions set forth in the Virginia Code. However, each of the three proposers has structured its proposal to capitalize and enjoy VPA's tax-exempt status. This would be precedent-setting and contrary to prior experience. As discussed with the subcommittee during the last meeting, when the U.S. Navy leases base property to a McDonald's restaurant, in Virginia, this becomes a taxable event and local taxes are collected on the value of the McDonald's lease in the form of a lease-hold tax. Local business taxes are also collected such as meals tax, machinery and tools tax - even though it is situated on land that is owned by the federal government. Just as an example, the City of Norfolk collected $1.6 million in calendar year 08 in business related taxes from private businesses operating on Norfolk Naval Base. A private port operator, proposing to lease state-owned property and conduct business as a private entity, should be treated no differently.

Mayor Fraim then mentioned the 1999 Joint Legislative Audit and Review Commission's report titled Review of the Impact of State-Owned Ports and Local Governments (http://jlarc.virginia.gov/reports/Rpt241.pdf). According to the report, port host cities in Virginia have a disproportionate cost to share compared against the actual economic benefits received. In fact, under the current structure, the Port actually costs host communities more than they are compensated for in terms of lost tax revenue, additional police, fire, and rescue services, added street maintenance and transportation infrastructure impacts on communities, not counting the truck traffic congestion, noise and pollution that affect citizens' quality of life on a daily basis. As a result of the JLARC Study findings, the 2000 Virginia General Assembly amended the Virginia Code governing the calculation of a Port Service Fee. This legislation outlined a new Payment in Lieu of Taxes (PILOT) methodology for determining what the Commonwealth and the VPA should contribute annually to VPA host localities. Unfortunately, the PILOT program has not been fully funded to date. As Mayor Fraim explained, since becoming law more that nine years ago, Norfolk has had to calculate and collect an annual Port service charge using the same inequitable formula it used prior to the 2000 PILOT legislation. This consistent underfunding and tax exemption of port operations has placed an ever increasing fiscal burden on communities that are already classified by the Commonwealth as recently as March 2009 "fiscally stressed." In FY 09, the City of Norfolk received a combined total of $1.1 million for the city's support and provision of fire-rescue and roadway maintenance costs attributed to port operations. The service charge amount from the VPA totaled $485,000 and Norfolk's proportional share of Port Highway Funds from the Commonwealth totaled $610,000. In estimating the City of Norfolk's Service Charge to be received from the Virginia Port Authority, the city made a variety of assumptions based on the best publicly available information. The 2000 legislation references "Total Tonnage" as a key component of the calculation. It is clear that the City of Norfolk receives a fraction of the potential revenue under existing law, or as would be available to the city if these facilities were fully taxable.

The city understands that these are tough economic times for the region, state, and country. The Commonwealth could potentially gain a significant short-term financial benefit if it were to accept one of the three competing proposals. However such a decision requires careful evaluation of each proposal, including the adequacy of compensation for host communities. Specific to the PPTA process, representatives from the port host communities should be appointed to the PPTA Independent Review Panel, as is typically accomplished in other PPTA processes. As the three conceptual proposals are considered, either the proposers and/or the Commonwealth must identify how they would address the inadequacy of the currently employed PILOT methodology.

In closing, Mayor Fraim stated that whether the VPA operations remain a state function or ultimately are privatized, any successful model must provide equitable compensation for host jurisdictions as a primary component of its overall business plan.

Dr. Robert Martinez

Dr. Martinez began his remarks by stressing that he was speaking solely from his own perspective, not on behalf of his company, Norfolk Southern. His remarks focused on the primary questions that the Virginia Port Authority and the Secretary of Transportation should consider in their review of the proposals. Fifteen years after its passage, Virginia's PPTA remains one of the most progressive, flexible, and market-oriented pieces of legislation. Dr. Martinez believes it would be a mistake to insert the

General Assembly directly into the PPTA process. The current procedures attract private capital to Virginia and allowing direct participation by the General Assembly might hinder the state's ability to attract that capital for other infrastructure projects. He recommends that this subcommittee pull together a series of considerations that the Oversight Board should answer in its deliberations prior to making a decision on these proposals.

Dr. Martinez set out some thoughts to consider as the proposals move through the PPTA process. The VPA has done pretty well over the years. Therefore, it is a business model that works, but that does not mean you do not question it. Virginia must focus attention on its surface transportation connections to inland markets (pertains to road/highway issues and freight rail). In looking at these proposals, it is important to consider how inland transportation connections will be enhanced. Dr. Martinez commented that the timing of this process is not the best. This is perhaps the worst international maritime freight period since World War II. The markets have been in much greater turmoil than prior to last year's financial meltdown, which makes proper valuation more difficult than in normalized markets. Next, he mentioned the length of the proposed concession and stated that no one can accurately undertake a 60-year valuation. Another important consideration involves looking at the treatment of VPA and VIT debt. Dr. Martinez concluded by stating that there are many great items in the proposals (e.g., financing, operating style, or operating management) that are not necessarily related to a privatization proposal per se and that could be pursued without a public-private transportation agreement.

Dr. Wayne K. Talley
Executive Director
ODU Maritime Institute

Dr. Talley presented sets of questions that should be asked in connection with the three proposals. Regarding the private operator payments: Will the payments by the private operator for the right to operate the VPA marine terminals be sent directly to the VPA or another entity? Will the private operator be required to fund VPA expenses using the current agreement for such funding by VIT? Will the private operator payments, over and above those needed to fund VPA expenses, be restricted for VPA marine terminal investments and improvements? Is VPA's Intermodal Terminal being considered for service privatization? Will the cities in which the VPA marine terminals are located receive a portion of the private operator payments? If so, will the payments to the cities be based upon the throughput activities of the terminals (higher when throughput is higher and lower when throughput is lower) or fixed amounts per year? Will the payments to the cities be restricted for funding transportation improvements that will benefit the marine terminals located in the cities?

Regarding quality of service: Will the privatization contract require that the private operator maintain a certain quality of service (i.e., in order for VPA marine terminals to stay competitive with other East Coast ports)? If so, how will the quality of service be evaluated (e.g. by the use of port performance indicators)? Which port performance indicators are to be used?

Questions related to penalties and rewards: If the quality of service of the VPA marine terminals under the private operator declines to (or rises above) a certain level, will there be a mechanism in the contract whereby the operator will be penalized (or rewarded)? If the throughputs of the VPA marine terminals fall below (or rise above) a certain level, will the private operator be penalized (or rewarded)?

Regarding bankruptcy and goals: If the private operator goes into bankruptcy and ceases to operate the VPA marine terminals, will there be a mechanism in the contract to ensure the continuing operation of the terminals? Will the private operator be required to operate the VPA marine terminals in a way that is consistent with the goals and objectives of the VPA (e.g. promoting state employment, economic growth, and a clean marine environment)?

Regarding length of contract: Why are two potential private operators (CenterPoint and Carlyle) seeking a 60-year contract to operate the VPA marine terminals, whereas Carrix, Inc. that owns the world's seventh largest private port operator (SSA Marine) is seeking a 30-year contract?

Regarding the recent VIT/APM proposal: If an agreement is reached for VIT to lease the APM Terminal in Portsmouth, what impact will this have on the privatization contract for VPA marine terminals? Would the private operator of VPA terminals also assume the operation of the APM Terminal? If so, what impact will this have on the value of the privatization contract, since VIT's container throughput capability will have doubled if the APM deal goes through? Is there a need to privatize the VPA marine terminals if the APM deal goes through?

Regarding timing of privatization: Is this a bad time to privatize the operations of VPA terminals? Given that the volume of VIT's throughput is down due to the global recession, should the privatization of the VPA terminals be delayed until the terminals' throughput is higher and the value of the privatization contract is higher? What impact will the new International Longshoremen's Association contract in 2010 and the completion of the widening of the Panama Canal in 2015 have on the value of the privatization contract for VPA terminals?

Jerry A. Bridges
Executive Director
Virginia Port Authority

Mr. Bridges explained that the Port of Virginia is (i) an efficient port and, during its best year in 2007, handled more than 2 million TEUs making it the third busiest container port on the USEC; (ii) a very healthy operation that has the necessary infrastructure in place, or is building it, to handle a growing volume of containers; (iii) a port that continues to use its natural assets to its advantage; and (iv) a port that has historically had good labor relations with its union. All of these things stem from a long-term, forward-thinking relationship of 29 years between the Virginia Port Authority (governmental agency) and Virginia International Terminals Inc. (private operator). In the industry the VPA-VIT set-up is seen as a model owner-operator relationship. They have a close collaboration and work together on multiple fronts: infrastructure development, customer service, economic development, and advance planning. In 1982, TEUs at the Port of Virginia totaled 289,000 and grew to 2 million in 2007. The VPA terminals are run and managed by a private operator and it has been that way for 29 years. Many of the benefits that the Commonwealth has enjoyed as a result of the Port's success are the result of a continual collaborative economic development effort among VPA, VIT, the Virginia Economic Development Partnership, other state agencies and local governments. The most visible result of that effort is that one out every nine jobs in the Commonwealth is in some way tied to the marine cargo operations in Hampton Roads. It is hard to estimate what the job creation and/or impact will be as two out of the three bidders have no experience in maritime operations. Mr. Bridges stressed that job retention and creation are the result of a competitive port and that job loss only comes when the Port cannot compete with other USEC ports.

Next Meeting:
The next meeting will be November 12, 2009, at noon at Old Dominion University.