

IN THE
SUPREME COURT OF VIRGINIA

AT RICHMOND

RECORD NO. 100675

CITY OF FALLS CHURCH,
Petitioner,

v.

FAIRFAX COUNTY WATER AUTHORITY,
Respondent.

BRIEF IN OPPOSITION TO THE PETITION FOR APPEAL

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April 26, 2010

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DX	Defendant's Trial Exhibit
Pet. App.	Petition for Appeal (Apr. 6, 2010)
PX	Plaintiff's Trial Exhibit
R.	Record transmitted by the trial court
Tr.	Trial Transcript, Volumes I-VII (Sept. 14-17, 21-23, 2009)

PRELIMINARY STATEMENT

The petition for appeal should be denied. First, there is no “reversible error.” The trial court properly ruled that the retail water rates charged by the City of Falls Church were an improper revenue generating device; the City deliberately inflated its water rates to generate surplus revenues to divert to its general fund. And because 92% of the City’s water customers who built the system reside in Fairfax County, the surcharge also represented an unconstitutional, extraterritorial tax. Second, the appeal is riddled with procedural error. The City’s main assignments of error have not been preserved, and the City failed to assign error to other key rulings by the trial court that are now the law of the case.

STATEMENT OF THE CASE

This is a dispute about whether a city-run water system can inflate its water rates in order to divert surplus revenues to the general fund so as to reduce local property taxes. This dispute focuses on the constitutionality of taxation-without-representation and the constitutionality of a municipal charter provision that purportedly authorized it.

Fairfax Water, a retail water customer of Falls Church, alleged in Count V of its Amended Complaint that the City was illegally designing its water rates to generate large surpluses for the City’s general fund, reducing

local property taxes to Falls Church citizens at the expense of the City's Fairfax County ratepayers. (R. 87-88, 103-07.) The Amended Complaint alleged that if the City claimed that its charter allowed it to use the water system to generate profits for the general fund, the charter was unconstitutional. (Am. Compl. at 2, R. 88; id. at 19, ¶ 100, R. 105.) Fairfax Water sought declaratory and injunctive relief. (R. 103-06.)

The dispute was tried in September 2009 in the Circuit Court of Fairfax County, the Hon. R. Terrence Ney presiding. (R. 2374; Tr. 1-1594.) In an opinion dated January 6, 2010 (R. 2701), Judge Ney ruled that the City's design of its water rates to generate surplus general revenues amounted to an unconstitutional, extraterritorial tax. (R. 2705.) He struck down the last sentence of § 13.07 of the charter, which permitted surpluses to be transferred to the general fund as a "return on equity." (R. 2700 ¶ 4, 2704-09.) He declined to strike down another provision of the charter, § 13.09, concluding that it already required the City to set its water rates with "receipts equal to expense," without generating surplus revenues for the general fund. (R. 2700 ¶ 3, 2703-4.)¹ The court enjoined the City from transferring further water profits to the general fund for purposes unrelated to the water system, including for Fiscal Year 2009. (R. 2699 ¶ 2.)

¹ The text of §§ 13.07 and 13.09 is reprinted in Appendix 1.

The City moved to reconsider only part of the ruling, the interpretation of § 13.09. (R. 2715.) That motion was denied on January 14, 2010. (R. 2720.) The City filed other motions to alter the decree and stay the injunction pending appeal (R. 3443). Those motions were resolved by a consent order that suspended the injunction with regard to the FY 09 water profit transfer; Falls Church promised to restore those profits to the water fund if this appeal is unsuccessful. (R. 2834.)

STATEMENT OF FACTS²

The City of Falls Church supplies retail drinking water to its own 11,000 citizens (8% of its water customers), and to 110,000 people in eastern Fairfax County (92% of its customers). (R. 90, 351 ¶ 13; Tr. 263:13-22.) Since the 1950s, the City has had far more county than city water customers. (Tr. 1236:19-1237:6.) And because the City built its water system on a “pay as you go basis,” the City’s Fairfax County customers largely paid for its creation and expansion. (Tr. 1234:5-1238:7.)

The City does not “negotiate” its retail water charges. (Tr. 1346:14-1347:6.) The City Council sets the rates. (*E.g.*, PX 37, R. 3057-63.) All

² It is “well established” that a chancellor’s findings after a trial on the merits may not be set aside unless “plainly wrong or without evidence to support them.” *Tauber v. Commonwealth, ex rel. Kilgore*, 263 Va. 520, 525, 562 S.E.2d 118, 120 (2002). The facts and inferences must be taken in the light most favorable to Fairfax Water, the prevailing party below. *Id.*

customers pay the same “published rate.” (Tr. 1346:19-20.) The water rate charged by the City is much higher than that charged by the Fairfax County Water Authority – \$3.03 compared to \$1.83 (per 1,000 gallons). (PX 37 at 32, R. 3059; Tr. 496:5-15.) Fairfax County customers complain that Falls Church overcharges them. (*E.g.*, Tr. 1329:8-19; R. 2799-805.)

The City’s water rates are higher because Falls Church operates its system on a “for-profit basis.” (R. 2702.) The former manager of the City’s water system called it the “goose that laid the golden egg” and a “money making machine” (Tr. 239:6-21, 1254:16-1255:6.) Thus, the City deliberately set its “water rates in 2003, 2004, and 2005 so that receipts would not only exceed expenses but create a substantial profit.” (R. 2703.) These profits – millions of dollars a year, and ranging from 15% to 43% of the water system’s annual operating revenues³ – were in addition to *other* moneys the City already took from the water fund to fully compensate itself. The chancellor noted that, “[a]lthough the City calls the current profit transfer a ‘management fee,’ its corporate designee admitted that the

³ Exhibits summarizing the profits were admitted as PX 3.1-A (R. 3019), PX 3.4 (R. 3028), and PX 3.6 (R. 3032).

‘management fee’ does not pay for any management at all because all such management costs” are already recovered. (R. 2702 n.3.)⁴

The water profits transferred to the general fund “have significantly reduced the local tax burden on Falls Church citizens without any corresponding benefit to the City's Fairfax County ratepayers.” (R. 2703.) In recent years, for instance, the transfers saved as much as 34-cents on the local property tax rate (which ranged from \$1.01 to \$1.10 per \$100 of assessed value). (R. 2615.) In 2009, the tax savings alone for the average City homeowner was worth more than a year’s supply of water. (R. 2593.)

Fairfax Water is a not-for-profit Virginia water authority that serves most of the remaining areas of Fairfax County that are not served by the City. Ironically, however, Fairfax Water is also a retail water customer of the City for two buildings within the City’s historic service area in the

⁴ The City charges “administration” costs to recover *all* direct and indirect costs to manage and operate the water system. (Tr. 229:10-230:7.) It also recovers a “payment in lieu of taxes” that represents the property taxes that the City would have received from the water utility if it were privately owned. (Tr. 324:17-21.) Fairfax Water did not object to these payments and paragraph 2 of the final decree protects them. (R. 2699.) Fairfax Water also did not question the City’s right to charge a *higher* rate to outside-City customers to provide a fair return for any risk to provide service beyond the City limits. (R. 2603-07, 2649.) But the evidence adduced during the impeachment of the City’s expert showed that the City’s current rate – \$3.03 – well exceeded what could be justified even on that basis – \$2.62. (See R. 2606 & n.7, 2616 Table 3.)

eastern part of the county. (Tr. 497:21-499:14.) In 2008, Fairfax Water paid the City nearly \$17,000 for retail water service. (PX 64.)

The City is wrong that Fairfax Water could easily disconnect from the City's system and connect to its own lines "across the street." (Pet. App. 27.) While it is economically feasible for Fairfax Water to serve some properties near existing lines (R. 92-93), the City fought to prevent anyone from switching systems; it sued Fairfax Water in federal court to try to establish a legal water monopoly in the eastern part of the county. *City of Falls Church v. Fairfax County Water Auth.*, 2007 U.S. Dist. LEXIS 36004 (E.D. Va. May 15, 2007) (R. 109-23), *aff'd*, 272 Fed. App'x. 252, 2008 U.S. App. LEXIS 7285 (4th Cir. Apr. 4, 2008) (R. 124-35). After the City lost that case, it continued to claim an "exclusive" service area and blocked one developer from switching to Fairfax Water. (Tr. 504:6-18, 528:1-7.) Indeed, Falls Church continues to control 100% of the market in eastern Fairfax County. (Am. Compl./Answer ¶ 10, R. 90, 351; Tr. 164:7-14.)⁵

Fairfax Water's general manager testified that, after winning the federal case in May 2008, he considered disconnecting Fairfax Water's

⁵ The City's efforts to prevent switches to Fairfax Water was the subject of the remaining Counts of the Amended Complaint. In a February 25, 2010 consent decree, Falls Church agreed to stop claiming an "exclusive" service area in Fairfax County and not to block customers from using Fairfax Water. (R. 2946-50 ¶¶ 2, 4.)

buildings from the City's system and connecting to a Fairfax Water main across Route 50, a "major east-west highway." (Tr. 499:1-6, 501:1-502:3, 505:6-506:5.) But there were major obstacles, including possible relocation of City lines, something the City was preventing one developer from doing. (Tr. 503:16-504:18, 525:7-526:9.) And it would cost \$311,000 to \$457,000 to tunnel under Route 50 (Tr. 501:1-17), meaning it would take up to 30 years to recoup the cost through the savings in water rates. (Tr. 530:5-531:6.) So Fairfax Water did not pursue it. (Tr. 530:5-14.)

The City's trial counsel did not dispute that Fairfax Water itself was one of the City's "captive" customers. (R. 887:9-21.)

ARGUMENT

I. THE TRIAL COURT CORRECTLY RULED THAT THE CITY'S WATER SYSTEM PRACTICES WERE UNCONSTITUTIONAL (Assignments of Error 2-4, 6).

The trial court analyzed one hundred years of this Court's decisions (R. 2704-08) and correctly concluded that the City's water system practices were "plainly unconstitutional." (R. 2709.) In *Marshall v. Northern Virginia Transportation Authority*, 275 Va. 419, 657 S.E.2d 71 (2008), this Court explained that the taxing power in the Virginia Constitution is different from other powers. The Constitution's "explicit language demonstrates *the special status* that the legislative taxing power occupies in the Constitution,

and reflects the *greater restrictions* that the Constitution places on the General Assembly's exercise of the taxing power." *Id.* at 432-33, 657 S.E.2d at 78 (emphasis added). Article I, § 6, in particular, "prohibits taxation of citizens without their consent or that of their elected representatives." 275 Va. at 434, 657 S.E.2d at 79.

Even though statutory enactments are presumed constitutional, the Court struck down the General Assembly's 2007 plan to fund transportation improvements in Northern Virginia through various transportation fees and charges. No one questioned that the fees raised revenues greater than the cost of service to which they related, and thus constituted a "tax." *Id.* at 431, 657 S.E.2d at 77 ("when the primary purpose of an enactment is to raise revenue, the enactment will be considered a tax, regardless of the name attached to the act."). Because the NVRTA, an unelected body, could decide whether to impose these fees, the scheme amounted to taxation-without-representation. *Id.* at 434-35, 657 S.E.2d at 79.

Judge Ney properly concluded that Falls Church's practices were unconstitutional under *Marshall*. For instance, the City raised its rates in 2005, even though it was already making millions of dollars in profit, "simply in order to transfer more money to the general fund." (R. 2705; Tr. 366:4-

374:15.) And 92% of all profits were “funded by Fairfax County customers who are not represented on the Falls Church City Council.” (R. 2705.)

The trial court did not rely solely on *Marshall*. Judge Ney followed other decisions by this Court concerning *when* a municipal fee is void as an unconstitutional, revenue generating device. (R. 2705-07.) The first was *Robinson v. City of Norfolk*, 108 Va. 14, 60 S.E. 762 (1908), where the Court held that the General Assembly could not authorize a city to levy a license fee on a circus located just outside the city limits “for the sole purpose of raising revenue to defray the general expenses of such city.” *Id.* at 21, 60 S.E. at 764. The Court explained the evil of extraterritorial taxes:

To any extent that one man is compelled to pay in order to relieve others of a public burden properly resting upon them, his property is taken for private purposes It is certainly difficult to understand how the taxation of a district can be defended where people have no voice in voting it, in selecting the purposes, or in expending it.

Id. at 17, 60 S.E. at 763 (citation and quotation omitted).

Next, in *City of Charlottesville v. Marks’ Shows, Inc.*, 179 Va. 321, 18 S.E.2d 890 (1942), the Court struck down the city’s practice of profiting from license fees it charged for police protection to carnivals located just outside the city limits. *Id.* at 330, 18 S.E.2d at 895. Charlottesville tried to distinguish *Robinson* on the ground that its charter, unlike Norfolk’s, gave it

regulatory power one mile beyond the City limits. But the Court did not reach that question because it viewed the ordinance at issue as “a mere revenue tax such as was condemned in *Robinson . . .*” *Id.* at 328, 18 S.E.2d at 894. “The exacted charge must bear some reasonable relation to the additional burdens imposed upon the municipality and the necessary expenses involved in the police supervision.” *Id.* at 329, 18 S.E.2d at 895.

This “cost of service” principle was next applied to government-owned utilities. In *McMahon v. City of Virginia Beach*, 221 Va. 102, 267 S.E.2d 130 (1980), the Court upheld a city ordinance requiring owners to pay for new water lines on their properties. Because the revenues raised did not exceed the actual cost of service, the Court said that “a reasonable correlation arose between the benefit conferred and the cost exacted,” so the ordinance was not a “revenue measure.” *Id.* at 107-08, 267 S.E.2d at 134. In *Tidewater Ass’n of Homebuilders, Inc. v. City of Virginia Beach*, 241 Va. 114, 400 S.E.2d 523 (1991), the Court upheld another water charge because the “fee revenues will not exceed the City’s cost in providing the service.” *Id.* at 121, 400 S.E.2d at 527. And in *Mountain View LP v. City of Clifton Forge*, 256 Va. 304, 504 S.E.2d 371 (1998), municipal trash collection fees were upheld, even though they generated a

surplus, because that money was needed “in anticipation of future expenses” for sanitary services. *Id.* at 311, 504 S.E.2d at 375.

The Court in *Eagle Harbor, LLC v. Isle of Wight County*, 271 Va. 603, 628 S.E.2d 298 (2006), surveyed these cases and reaffirmed that “*McMahon* and its progeny establish that the judicial inquiry as to a reasonable correlation relating to a municipal fee is directed to whether that fee is a bona fide fee-for-services or an ‘invalid revenue generating device.’” *Id.* at 615, 628 S.E.2d at 304. The trial court here properly found that Falls Church’s water rates failed this test. (R. 2705-07.)

The distinction between valid user fees and taxes under Virginia law is consistent with the law elsewhere. For instance, applying federal law, the Attorney General of Virginia recently opined that a stormwater fee charged to the U.S. Navy was not a tax on the federal government because it reflected a “fair approximation” of the use by each property owner, was “structured to produce revenues that will not exceed the total costs of benefits supplied,” and was “not designed simply to raise money for general revenue purposes.” Opin. No. 09-098 (Mar. 4, 2010), at <http://www.oag.state.va.us/OPINIONS/2010opns/Mar10opnndx.html>. (The Attorney General had previously opined under Virginia law, as well, that

utility charges to out-of-town customers must be cost-based. 1997 Op. Att’y Gen Va. 77, 1997 Va. AG LEXIS 99 (1997).)

Notably, the leading national association of water utilities, the American Water Works Association (Tr. 230:19-231:1), has also advised since 1965 that “Water utility funds should not be diverted to uses unrelated to water utility services.” AWWA, Manual M5, *Water Utility Management* at 33 (2d ed. 2005). (See Tr. 240:15-241:11, 422:3-15.) Tellingly, Falls Church admitted that it did not know about this policy and did not follow it. (Tr. 241:12-242:3, 1458:13-1459:17.)⁶

A. The City’s Efforts to Distinguish the *Robinson-McMahon-Marshall* Line of Cases Are Unpersuasive and Procedurally Barred.

The City’s main attack on the *Robinson-McMahon-Marshall* line of cases is both without merit and procedurally barred. This Court will generally not consider error to a lower court’s ruling “unless the objection was stated with reasonable certainty *at the time of the ruling*.” Rule 5:25 (emphasis added). This requirement gives “the trial court an opportunity to

⁶ The U.S. Environmental Protection Agency supports the AWWA’s policy (Tr. 426:5-427:4) and warns water utilities that “[r]evenues from overpricing are sometimes used to subsidize other services or functions. Subsidies from ratepayers are inconsistent with cost-based rate making and generally unfair, particularly if customers have not explicitly approved the subsidy.” (Tr. 429:20-430:4.)

rule intelligently on the issues presented” and “the opposing party the opportunity to meet the objection at that stage of the proceeding.”

Nusbaum v. Berlin, 273 Va. 385, 402-03, 641 S.E.2d 494, 503 (2007) (citation and quotation omitted).

For the first time on appeal, the City argues – in Assignments of Error 2 and 3 – that Article VII, § 2, of the Constitution permitted the General Assembly to give Falls Church the power to impose extraterritorial taxes. The City then tries to distinguish *Marshall* by arguing, alternatively: (1) that the NVTAs were not a “county, city, town or regional government” to which such authority could be delegated under Art. VII, § 2; and (2) that Fairfax County residents were adequately represented in the General Assembly when it supposedly gave Falls Church the power to tax them.

These arguments are barred because the City never asked the trial court to consider them. The City never raised these arguments in its:

- answer (2/17/2009) (R. 358);
- pre-trial brief (9/10/2009) (R. 2975);
- post-trial brief (10/21/2009) (R. 3403);
- motion to reconsider (1/13/2010) (R. 2715); or
- other post-trial motions (1/13/2010) (R. 3443).

Instead, the City waited until two weeks after the final decree to file a host of new objections to it, *one* of which, for the first time, mentioned Art. VII, § 2. (R. 2816 ¶ 13). That was insufficient. In *Nusbaum*, the appellant

likewise failed to raise an argument at the time of the bench ruling, did not include it in his motion to reconsider, and simply noted it as an objection to the final order. The assignment of error was deemed waived because he “never asked the circuit court” to rule on it. *Id.* at 403, 641 S.E.2d at 503. For the same reason, Assignments of Error 2 and 3 are likewise waived.

Even if the arguments had not been waived, they are meritless. Falls Church’s extraordinary claim that the General Assembly can authorize a city to impose extraterritorial taxes on other Virginians was specifically rejected in *Robinson and Marks’ Shows*. And nothing in Art. VII, § 2, suggests that it invalidates *other* provisions of the Constitution, such as Art. I, § 6 (the people “cannot be taxed . . . without their own consent, or that of their representatives duly elected”). Equally flawed is the City’s claim that taxation-without-representation is not found here because the General Assembly represented Fairfax County’s interests when it granted Falls Church its charter. If that argument had merit, *Marshall* would have come out the other way, since the Northern Virginia delegates to the General Assembly also represented the Virginians who would have been taxed by the NVTAs in that case.

The City’s other arguments fare no better. Its contention that the “reasonable correlation test” in the “*McMahon* line of cases” is limited to

charges a locality levies on its *own* residents (Pet. App. at 24) was properly rejected by Judge Ney. He explained that those cases must be viewed as a coherent line of authority *originating* with cases that prohibited extraterritorial taxation:

[The City's] argument ignores that these cases flowed from *Robinson* and *Marks' Shows*, both of which involved extraterritorial taxation. The fact that the plaintiffs in the *McMahon* line of cases lived within the particular locality does not demonstrate that those cases overruled *Robinson* or *Marks' Shows*, or that the cost-of-service principle does not apply to municipal fees charged to nonresidents. (R. 2707.)

Nor does it help the City to rely on dictum in *Corporation of Mt. Jackson v. Nelson*, 151 Va. 396, 403, 145 S.E. 355, 357 (1928), that a town need not let surplus water be wasted when it could be sold for profit. The only issue there was whether the town could contract to extend a water line to a single property outside the town, not whether it could inflate its utility rates in an established area to subsidize the general fund. The trial court properly concluded that the dictum was not helpful. (R. 2707-08.)

The City similarly misreads *Westbrook, Inc. v. Town of Falls Church*, 185 Va. 577, 39 S.E.2d 277 (1946). The Court there held that a developer was not being “taxed” when it contracted with Falls Church (then a town) to extend a sewer line to a new area that was not already served. *Id.* at 582,

39 S.E.2d at 280. Having promised to pay the Town to extend a utility line that was *not* required, the developer could not claim that the cost was a tax. Indeed, in that case Falls Church *itself* differentiated between (1) contracting to extend a new service line where none was required, and (2) imposing monthly fees for service *after* the system was established, which Falls Church conceded was a “tax.”⁷

In any case, the City’s narrow focus on *Mt. Jackson* and *Westbrook* has overlooked the elephant in the room. Falls Church has failed to assign error to the trial court’s decision to apply the “holding out” doctrine (R. 2707-09), which provides that the “duty of a municipality owning a public utility to furnish services and supplies without discrimination and at reasonable rates extends to users outside the city . . . where the city has undertaken to serve the public outside the city.” 12 Eugene McQuillin, *The Law of Municipal Corporations* § 35.52 at p. 795-96 (3d ed. 2006). As Judge Ney explained, this doctrine distinguishes between a municipality that has not yet extended its utility lines to the area in question (as in *Mt. Jackson* and *Westbrook*), and a city like Falls Church that has long held

⁷ See Brief of Defendant in Error at 10, *Westbrook, Inc. v. Town of Falls Church*, Record No. 3068 (Va. Apr. 10, 1946) (“Falls Church in levying a monthly charge for the use of sewers . . . is taxing such owners for the later use and not for the initial construction”) (R. 263); *id.* at 13 (describing its “monthly tax” for sewer service) (R. 266).

itself out as the area's utility provider. (R. 2708-09.) So when the City now argues that water service is ordinarily a "proprietary" function, it forgets that the "holding out" doctrine is an "exception." *Town of Rocky Mount v. Wenco of Danville, Inc.*, 256 Va. 316, 321, 506 S.E.2d 17, 20 (1998).⁸

Because the City did not assign error to the holding out doctrine, it has become "the law of the case and is binding on appeal." *Maine v. Adams*, 277 Va. 230, 242, 672 S.E.2d 862, 869 (2009); Rule 5:17(c).

B. Fairfax Water Did Not Consent to Pay an Ongoing Unconstitutional Tax.

Falls Church argues that Fairfax Water "consented" to pay the unconstitutional tax by purchasing water from the City and owning buildings in the City's water service area. This is another version of the City's "waiver, consent and laches" defenses that the trial court rejected on *both* the facts and the law (R. 2709), rulings the City has not appealed.

The City's suggestion that water service is optional also makes no sense. "Utility service is a necessity of modern life; indeed, the discontinuance of water . . . for even short periods of time may threaten health and safety." *Memphis Light, Gas & Water Div. v. Craft*, 436 U.S. 1,

⁸ See also 1989 Va. AG LEXIS 161 (1989) (applying "holding out" doctrine); *Stoneleigh Group, Inc. v. Town of Round Hill*, 50 Va. Cir. 42, 49 (Loudoun County 1999) ("The [holding out] exception is very reasonable and just plain 'makes sense.'").

18 (1978). As this Court said years ago, it is “common knowledge” that “livable premises” require potable water, an “essential” of life. *Kerr v. Clinchfield Coal Corp.*, 169 Va. 149, 154, 192 S.E. 741, 742 (1937). Nor does the trial record suggest that a customer could avoid buying City-water by drilling a well. The City offered no such evidence and Fairfax County requires all businesses and residents to connect to an existing water system, rather than operate a well, if the property is near an existing utility line. Fairfax County Code §§ 65-6-6, 65-6-8 (2008).

The record also does not support the claim that Fairfax Water could stop buying water from the City and simply connect to its own line “across the street.” (Pet. App. 27.) As noted above, *supra* at 6-7, the City not only claimed an “exclusive” service area and refused to permit its own lines to be moved, but the cost was prohibitive to tunnel under Route 50. Moreover, the City’s expert conceded that Falls Church’s water customers were “captive” and had nowhere else to turn. (Tr. 888:13-19.) The City’s trial counsel likewise did not dispute that Fairfax Water itself was among the City’s “captive” retail customers. (Tr. 887:9-13.)

On this record, taken in the light most favorable to Fairfax Water, the City cannot credibly assert that Fairfax Water “consented” to pay an unconstitutional tax. Indeed, in no other case has it been a defense to an

unconstitutional tax to say that the taxpayer chose to be located in a jurisdiction that wanted to tax him.

C. The Trial Court Did Not Grant “Representational Standing.”

The City also wrongly infers from the trial judge’s statement that the City’s customers in Fairfax County were “captive” that he gave Fairfax Water “representational standing.” (Pet. App. 26.) This case was not like *W.S. Carnes, Inc. v. Bd. of Supervisors*, 252 Va. 377, 383, 478 S.E.2d 295, 299 (1996), where the association of builders lacked standing because it had “not paid” the permit fee at issue. Fairfax Water had standing because, as one of Falls Church’s many “captive” customers (Tr. 887:9-13), it was charged the inflated rate (PX 64) and “paid the taxes in question.” *Reynolds Metals Co. v. County of Henrico*, 237 Va. 646, 648, 378 S.E.2d 833, 834 (1989). “An aggrieved party’s right to attack a local tax assessment is well-established.” *Id.* at 647, 378 S.E.2d at 834. The fact that other “captive” customers will benefit from the ruling does not negate Fairfax Water’s standing in its own right. “The jurisdiction of a court of equity to enjoin the enforcement of an unauthorized tax is too firmly established in this jurisdiction to admit of serious question.” *Town of Wytheville v. Johnson’s Ex’r*, 108 Va. 589, 590, 62 S.E. 328, 328 (1908).

II. THE TRIAL COURT PROPERLY INVALIDATED THE LAST SENTENCE OF CHARTER § 13.07 WHILE PRESERVING THE RATE-SETTING MECHANISM OF § 13.09 (Assignment of Error 1).

The City claimed it was allowed to operate its water system for profit based on two provisions of its charter: § 13.07 and § 13.09. (See Appendix 1.) The trial court struck down the last sentence of § 13.07 to the extent it allowed the City to transfer a so-called “return on equity” from the water fund to the general fund. (R. 2700 ¶ 4). (That provision will not be missed. Out of 232 Virginia localities with charters, Falls Church is the *only one* whose charter allowed a “return on equity” to be transferred from the utility fund to the general fund. 1993 Va. Acts ch. 969, § 13.07.⁹)

Section 13.09 (“Changes in Rates”) was not invalidated. The trial court simply rejected the City’s claim that this section authorized profit-making. The court found instead that “the water rates are to be set with ‘receipts equal to expense,’ without building any surplus or ‘return on equity’ into the rates themselves.” (R. 2704; Final Decree ¶ 3, R. 2700.)

Falls Church complains that the chancellor erred in applying this limiting construction to § 13.09 because Fairfax Water supposedly pleaded only a constitutional violation, not a statutory one. (Pet. App. at 2, 9, 13.)

⁹ The Virginia Division of Legislative Services maintains a current inventory of charters at <http://dls.state.va.us/lrc/charters/welcome.htm>.

But although the non-constitutional argument was properly raised, the doctrine of “constitutional avoidance” would apply even if it had not been pleaded at all. For “when a statute can be given two different interpretations, one that is within the legislative power and the other without, [courts] are required to adopt the interpretation that conforms to the Constitution.” *Commonwealth v. Doe*, 278 Va. 223, 230, 682 S.E.2d 906, 908 (2009). And since courts will save a statute from invalidity “whenever possible,” *id.*, they do so “whether or not [the non-constitutional grounds] have been properly raised . . . by the parties,” *Neese v. S. Ry. Co.*, 350 U.S. 77, 78 (1955).

Nonetheless, Fairfax Water’s Amended Complaint provided ample notice that the City’s interpretation of its own charter was squarely at issue. Fairfax Water twice pleaded that the constitutional question turned on whether the City claimed that its charter authorized using the water system to generate surpluses to be transferred to the general fund.¹⁰ This issue

¹⁰ See Am. Compl. at 2, R. 88 (“*To the extent the City claims that its Charter authorizes the use of its water fund to generate such massive subsidies for its general governmental operations, the Charter should also be declared unconstitutional.*”) (emphasis added); *id.* at 19, ¶ 100, R. 105 (“*To the extent the City contends that the Charter of the City of Falls Church permits it to use surplus water revenues to subsidize the City’s general operations unrelated to the water system, the Charter violates the Constitution of Virginia.*”) (emphasis added).

was pleaded from the beginning and discussed in opening statement (Tr. 106:13-115:20), not raised “in the middle of trial” (Pet. App. 12).

As it turned out, the City offered *two* entirely inconsistent interpretations of § 13.09, *either* of which, if accepted, would have led to unconstitutional results. The City’s first theory, which it has now abandoned, was that § 13.09 allowed “profits” to be included as either “receipts” or “expenses” when setting water rates. (R. 3419.) Because that construction would have rendered § 13.09 unconstitutional, Fairfax Water’s *primary* argument was to strike down the statute. (Tr. 615:14-22.)

Respectful of the doctrine of constitutional avoidance, however, Fairfax Water conceded that § 13.09 could be saved by construing it *not* to permit “profits” to be included in “receipts” or “expenses,” a construction strongly supported by the legislative history. (Tr. 548:21-552:18, 555:11-556:3, 615:14-22; R. 2595-96.) The trial court agreed. (R. 2704.)

The City now offers a new theory that contradicts the first one: yes, the second sentence of § 13.09 prohibits profit-making, but it is not triggered unless the water system loses money for three years. (Pet. App. 13). This theory has been waived. The City did not raise it until the motion to reconsider (R. 2715-17), which the trial court denied on January 14, 2010 (R. 2720). The City did not appeal that order (R. 2938) nor assign

error to it.¹¹ So under Rule 5:17(c), the Court should “disregard” the argument. *Caine v. Freier*, 264 Va. 251, 257, 564 S.E.2d 122, 125 (2002).

Even if the new theory could be considered, it is utterly implausible. The City is saying that if it keeps its water prices high enough to avoid losing money, it can generate profits indefinitely on the backs of its Fairfax County customers; only if the City loses money for three years must it reset the rates to forego further profit-making and, only then, “lose the money making machine (the goose) forever.” (Tr. 1254:16-1255:6.) This theory not only fails to cure the constitutional defect, it makes no sense. See *Doe*, 278 Va. at 230, 682 S.E.2d at 909 (“absurd results” should be avoided).

III. THE TRIAL COURT PROPERLY APPLIED ITS RULING TO THE CITY’S 2009 FISCAL YEAR (Assignment of Error 5).

The City also waived its argument that the final decree should not have applied to FY 09. The City raised that claim in motions filed January 13, 2010 (R. 3443), but the City withdrew those motions on January 27, 2010 (R. 2834-35 ¶ 3). The City “never asked” the trial court to rule on the

¹¹ Denial of a motion to reconsider is reviewed only for “abuse of discretion.” *Winston v. Commonwealth*, 268 Va. 564, 620, 604 S.E.2d 21, 53 (2004). Judge Ney could have denied the motion simply because, regarding § 13.09, the City took “successive positions in the course of litigation that are inconsistent with each other or mutually contradictory.” *Eure v. Norfolk Shipbuilding & Drydock Corp.*, 263 Va. 624, 636, 561 S.E.2d 663, 670 (2002).

argument, so it too has been waived. *Nusbaum*, 273 Va. at 403, 641 S.E.2d at 503; Rule 5:25.

And even if this argument had not been waived, the trial court did not abuse its discretion when it prohibited the City from transferring the FY 09 water surplus to the general fund. The Amended Complaint requested such relief; it asked the court to “enjoin the City from using its water fund to subsidize its general fund” and for “such other relief as the Court deems just and reasonable.” (R. 106-07, ¶¶ 5, 8.) When a complaint like this requests special relief and general relief, the chancellor may fashion “any proper relief consistent with the case” as pleaded. *Johnson v. Buzzard Island Shooting Club, Inc.*, 232 Va. 32, 36, 348 S.E.2d 220, 222 (1986).

What this issue really involves is the City’s unilateral decision to transfer the FY 09 water profits *after* the trial was over, while the parties awaited the ruling. At trial on September 23, 2009, the chief financial officer testified that the City would *not* be unduly burdened if the court enjoined further transfers to the general fund. (Tr. 1489:17-18 (“it wouldn’t be a huge problem. We could do it.”).) When Fairfax Water filed its post-trial brief on October 9, 2009, it asked the trial court to apply its ruling *specifically to FY 09*. (R. 2613 & 2618 ¶ 2.) It turns out that the City had already transferred the money two days before. (R. 2783.) (The City told

its auditors that it did not expect an unfavorable decision. R. 2792.) Yet when the City filed its own post-trial brief (R. 3403), it never questioned that the ruling, if adverse, should apply to FY 09, nor did the City disclose that it had *already* made the transfer. In short, the City acted at its peril in taking the FY 09 transfer while the decision was pending. It will simply have to restore those water profits to the water fund, which it has promised to do if its appeal here is unsuccessful. (R. 2834 ¶ 2.)

CONCLUSION

It is extremely unusual for a city water system to have a customer base that is overwhelmingly comprised of non-city residents (92%). Falls Church capitalized on that imbalance – and on its one-of-kind charter provision (§ 13.07) – by charging an inflated water rate to all of its customers, reaping huge profits that allowed it to drastically reduce the local tax burden on its own citizens.

Because the trial court correctly decided this was “plainly unconstitutional” (R. 2709), and because the City has not preserved its main assignments of error, the Petition for Appeal should be denied.

Respectfully submitted,

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CERTIFICATE OF SERVICE

I certify that, on April 26, 2010, a copy of this Brief in Opposition to Petition for Appeal was served by electronic mail and U.S. mail to the offices of each of the following:

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APPENDIX 1 – Provisions of Falls Church City Charter

§ 13.07. Disposition of utility surplus. A sum of money equal to taxes not actually accruing but which would have accrued during such year had the utility not been municipally owned, shall be paid annually by the utility into the general fund. A return on equity that is calculated using generally accepted accounting principles for utility enterprises, when authorized by the council by the affirmative votes of a majority of council, may be transferred to the general fund or to the improvement fund of each utility respectively.

1993 Va. Acts ch. 969, § 13.07.

§ 13.09. Changes in rates. The rates to be charged for the respective services of the water and sanitary sewage utilities shall be fixed from time to time by the council on the recommendation of the director of public utilities and the city manager. If for any three (3) consecutive fiscal years the average annual receipts of any utility shall be less than its average annual expense it shall be the duty of the director of public utilities and the city manager to recommend and the council to adopt for that utility a schedule of rates which in its judgment will produce receipts equal to expense.

1995 Va. Acts ch. 655, § 13.09.