

**A JOINT INVESTIGATION INTO THE
CONTRACT BETWEEN THE NEW YORK STATE
CANAL CORPORATION AND
RICHARD A. HUTCHENS CC, LLC**

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Events Leading to this Report

In an effort to foster economic development along the Erie Canal, the New York State Canal Corporation, in 2001, sold broad and exclusive rights to cut new residential access channels into the Canal to an upstate entity named Richard Hutchens & Associates ("RHA"), a company primarily owned by Richard Hutchens.

In the Spring and Summer of 2003, the Hutchens agreement was the subject of public controversy, and, in early October 2003, the Joint Assembly Standing Committees on Corporations, Authorities and Commissions, and on Transportation, conducted a public hearing in which Assembly members questioned both the fiscal prudence of the deal and the fairness of the process that led to it. Two weeks after the hearing, the New York State Comptroller's Office voided the Hutchens contract after conducting its own examination.

On October 22, 2003, Governor Pataki announced that he was asking the Attorney General to review the issue, and directed the New York State Inspector General to conduct an independent investigation. The Attorney General's authority was formalized in a letter dated December 10, 2003, in which Governor Pataki requested, pursuant to Executive Law Sections 63(3) and 63(8), that the Attorney General "investigate the commission of any indictable offense," and "inquire into all matters relating to the canal development contract" between the Canal Corporation and Hutchens.¹

¹ Section 63(3) authorizes the Attorney General, upon request of the Governor or other state official, to "investigate the alleged commission of any indictable offense or offenses in violation of the law which the officer making the request is especially required to execute or in relation to any matters connected with such department, and to prosecute the person or persons believed to have committed the same and any crime or offense arising out of such investigation or prosecution or both...." Section 63(8) permits the Attorney General, with "the approval of the Governor and when directed by the Governor" to "inquire into matters concerning the public peace, public safety and public justice."

Pursuant to this authority, the Attorney General and Inspector General have jointly taken testimony from numerous witnesses and reviewed thousands of pages of documents relating to the Hutchens transaction. This report summarizes the results of the Attorney General's and Inspector General's investigation.

Introduction

After its completion in 1825, the Erie Canal quickly became one of New York's primary arteries of commerce, connecting the grain producing states of the Midwest with the shipping lanes of the North Atlantic Ocean. Within a century, however, competition posed by new technologies – trains, pipelines, and highways – led to the decline of the Canal's primacy and hurt the economies of many of the communities that had prospered because of the Canal.

In the early 1990s, the State of New York began to think about shifting the Canal's mission to include recreation and development. To that end, it created a public benefit corporation, the Canal Corporation, and an advisory body known as the Canal Recreationway Commission. The Legislature required the Recreationway Commission to develop and regularly update a plan for the Canal that included fostering "clusters of development connected by stretches of undeveloped open space."

This report discusses the circumstances under which the Canal Corporation entered into an exclusive contract with RHA to create channels leading from the Canal to his planned canalside communities. It further outlines the process by which RHA and Hutchens secured the deal.

Hutchens is a Buffalo entrepreneur whose real estate experience is in the construction and management of low income housing. Despite his claims, he had no experience in developing waterside communities. Hutchens's other business enterprises have included selling frozen dandelion leaves and importing melons.

Hutchens's vision for the Canal was to develop clusters of homes around newly constructed in-land marinas that he would join to the main Canal by bank cuts. According to his business plan, residents of the new communities would have (after he stocked the Canal with salmon and built ladders for them to navigate the locks) "four months of boating, four months of snowmobiling and cross country skiing, and approximately four to six weeks of salmon fishing."

Hutchens claimed that he originally sought to do the development himself. And, certainly, the Canal Corporation Board of Directors believed that Hutchens would be the developer. However, even crediting Hutchens's claims as to his original intentions, by the time of the Board's vote to approve the plan, Hutchens had no intention of using his firm to develop canalside residential communities. His undisclosed goal was, instead, to obtain an exclusive option on development, and to sell, or "flip," this exclusive right to other developers.

Hutchens had a low opinion of the Canal Corporation Staff, testifying: "The [acting] director had been a surveyor and that's as near as they had of anybody that had ever been around, to my knowledge, people who knew anything." As to his plans, he testified, "I didn't take them to college, I let them get their own education."

The staff, on the other hand, was impressed with Hutchens, and began focusing on his proposal. They hoped that he would succeed in developing the Canal, and, as one staff member put it, make the staff look good in the process. They referred to Hutchens as "the Golden Goose"

and the “white knight.” He was, to them, a “millionaire with a successful track record” whom they sought to enlist in their development mission. Moreover, in the midst of negotiations between Hutchens and the Canal Corporation, at least one staff member also came to view him as a prospect to be mined for campaign contributions.

In the end, the Canal Corporation awarded Hutchens an exclusive option on what he and Canal Staff believed was the entire developable portion of the Canal System,² and did so for an up front payment of \$30,000, an additional fee ranging from \$15,000 to \$25,000 per canal cut, and an annual \$300 homeowner’s fee pegged to future inflation. For this, Hutchens believed he was able to prevent anyone else in New York State from pursuing a significant residential project along a canal cut unless they purchased the right from him to do so.

The Canal Corporation, a public benefit corporation, was permitted to use sole source contracts, such as the one used here. However, the process that led to the Hutchens contract was tainted by improper conduct, some of which violated the New York Public Officers Law and some of which was simply unseemly. Canal Staff gave Hutchens confidential and privileged documents, responded to calls to open the process to other potential developers by simply going through the motions, pressured an independent consultant into changing its report, and withheld information from and misled its own Board.

One high-ranking Thruway Authority employee, Donald Hutton, repeatedly exercised extraordinarily poor judgment and acted in an inappropriate and unlawful fashion. For example, early on, the negotiating process stalled when the Canal Corporation Board of Directors tabled

² The final contract gave Hutchens exclusive rights to a maximum of 9 % of the shoreline. Canal Staff never informed its Board of Directors that this 9 % represented the entire developable portion of the shoreline.

the proposal over such basic terms as price and exclusivity. In response, Hutton recommended that Hutchens hire a lobbyist to lobby the Canal Board. Hutton personally introduced Hutchens to the lobbyist, and told the lobbyist that he supported Hutchens's plan but that Hutchens needed assistance getting it through the system. Even the seasoned lobbyist described this as unique in his experience.

Hutton also arranged for Hutchens to start attending social/campaign fundraising functions with government officials and others, and introduced Hutchens into his and the lobbyist's social and political circle. As Hutchens testified, "Everybody makes a political contribution for a purpose. . . . Anytime you do anything you do it for a purpose. My purpose was, that I'm living in New York, and I need to be a friend, be acquainted with people that make things happen." Hutton introduced Hutchens into a network where the key players – many of whom were self-described old friends – dined together, golfed together, took vacations together, spent weekends together and attended political fundraisers together.

The lobbyist advanced Hutchens's proposal both through public advocacy and private conversations. His efforts began with meetings and telephone calls to Canal Staff and Board members. He had numerous conversations with Robert King (then the Director of the Division of the Budget) and with King's wife (then Director of Special Projects at the Institute of Entrepreneurship at State University of New York). From his contacts with the Canal Staff, the lobbyist obtained strategic advice, information about the private views of the participants, and confidential documents. From his conversations with King, the lobbyist obtained a promise that King would make telephone calls on his client's behalf.

The participants deny that the contributions, the socializing, or the lobbying of the high-

level official affected the outcome. Hutchens adamantly denied the suggestion that his contributions were intended to directly influence the Canal Staff, and termed the suggestion “bullshit.” Members of the Canal Staff said that their knowledge of Hutchens’s contributions to candidates they supported had no influence on them. King testified that he could not recall whether he placed the telephone call as the lobbyist had asked.

The lobbyist, however, described his job, and his potential to influence the process, thus: “I have a reputation in Albany of being able to get things done by just dint of good hard work and doing things you need to do, which is just a lot of time, effort and whatever. . . . [T]here are commissioners that I literally grew up with. I remember George Pataki when he came in. I mean Eliot Spitzer, for gosh sakes, I knew him. I’ve known I’ve known Alan Hevesi since he was wet behind the ears as an assemblyman. I’ve known these people for all these times. It’s a small world in that sense. But this is not a bad thing. This is just the way it works.”

Whether because of the merits of the proposal or otherwise, in the end, the Canal Corporation Board gave Hutchens a contract that very closely resembled one that the Board had tabled years before.

The first lesson from this investigation is that a lack of staff competence doomed this project to failure. Staff spent years negotiating with Hutchens without testing the market in any serious way for other potential partners, without pursuing a meaningful and thorough valuation of the State asset being sold, and without having conducted even the most minimal due diligence into Hutchens’s background. There is little question that attracting developers to the Canal has been a difficult task, and even a competent effort might have brought little in the way of concrete results. But, in the hands of the Canal Staff, it did not and could not.

Second, a lack of ethics can undermine attempts at oversight. For example, at one point in the process, an advisory board asked that the contracting process be opened up to competition. Instead of doing this, the staff designed a process that had the outward appearance of competitiveness while, in essence, guaranteeing the contract to Hutchens. There must be a commitment to the principles of good government, not simply an effort to get by with technical and superficial compliance.

Third, in a very important way, New York's ethics rules are ineffectual at best: New York's ethics laws apply only to current – not former – State employees. Many of the staff involved in this matter have already left State service, and are, therefore, beyond the reach of the New York State Ethics Commission. The need to amend the law to allow the Commission to apply penalties to those who have left State service is self-evident.

Finally, lobbying, in itself, is legal and common at all levels of government. The potential, however, is always present for the intrusion of interests that do not serve the public interest. Here, the evidence shows that the lobbyist had access to confidential State information that he should not have had, and that his influence over the staff was improper. Yet the process, indeed, the practice of lobbying, was largely invisible to the public. This case demonstrates the need for greater transparency. Had it not been for the calls for this investigation and the lobbyist's records, the public would never have learned the facts.

FACTUAL FINDINGS

1. Background

A. The Erie Canal and The New York State Canal Corporation

The New York State Canal System is composed of the Erie Canal, the Champlain Canal, the Oswego Canal and the Cayuga and Seneca Canal. Ground was broken for the Erie Canal on July 4, 1817, and both the Erie and Champlain Canals were completed by 1825. While originally greeted with skepticism and popularly referred to as “Clinton’s Folly” (after Governor De Witt Clinton), in their first years the Erie and Champlain Canals were a great success, which led to the rapid construction of other waterways.

In the late nineteenth century, competition from railroads threatened the economic viability of the Canal system. New York responded in 1903 by beginning a major expansion to accommodate larger boats. When these improvements were completed in 1918, portions of various canals were abandoned and replaced by the use of rivers that in many instances ran parallel to the canals. Despite these improvements, as the twentieth century progressed, commercial traffic on New York canals again dwindled, due to the system’s inability to handle ships larger than barges, as well as to the development of pipelines, growth in the trucking industry, and the completion of the St. Lawrence Seaway in the 1950s.

Between 1923 and 1992, responsibility for Canal management was assigned to the Department of Public Works and its successor, the Department of Transportation. In 1992, the New York Legislature transferred control over the Canal system from the Department of Transportation to the New York State Canal Corporation, a new public benefit corporation created as a subsidiary of the New York State Thruway Authority. The Canal Corporation is

governed by a three-member Board of Directors, who also serve as the Board of Directors for the parent corporation, the Thruway Authority. The Canal Corporation enjoys wide-ranging powers and a degree of independence similar to other New York public benefit corporations, and is responsible for all aspects of Canal operations.

The Canal Corporation has authority over the “Canal System,” defined by statute to include “canalized lakes and rivers,” such as the Seneca and Oswego rivers. It owns various parcels and easements along the artificial portions of the Canal system, with its property rights generally stopping at the banks of the canalized rivers. As to the lakes, with a few exceptions it owns only a channel dug in the middle of the water.

The canals are operated and maintained primarily on funds drawn from the Thruway Authority. Operation and maintenance costs are approximately \$70 million per year, and annual revenues are less than \$2 million. The Thruway Authority’s desire to avoid toll increases on the Thruway has generated significant pressure on Canal Staff to increase Canal revenues and reduce this shortfall.

In addition to transferring the Canal system to the Thruway Authority, in 1992, the Legislature also created the Canal Recreationway Commission (“Recreationway Commission”). The Legislature charged this group with developing and updating a Canal Recreationway Plan, which consists of recommendations for maximizing the Canal system’s environmental, commercial, agricultural, historic, and recreational resources. The legislation required that the Plan include, among other things, “provisions for fostering . . . clusters of development connected by stretches of undeveloped open space.” The Recreationway Commission’s role is purely advisory.

After extensive technical studies and public comment, the Recreationway Commission issued a plan in August 1995, a scaled-down version of which the Thruway Authority Board approved in September of that year. The plan set forth an ambitious set of proposals for the Canal system, including the establishment of a set of canal “landings” with activities and services for visitors; the expansion of recreational boating opportunities; the completion of a Canal recreation trail; and the construction of “inner harbors.” As to residential development, the plan sought to “encourage” new development to locate “within existing communities” and urged that “new development should avoid the consumption of land with subdivisions that do not respect local tradition, land forms, topography and vegetation.”

B. Richard Hutchens and Associates (“RHA”)

When the Recreationway Commission Plan was approved, Richard Hutchens was managing approximately 500 apartments for the elderly in Western New York. Hutchens had developed and built the housing complexes from 1972 to 1985 with federal funding through the United States Department of Housing and Urban Development (“HUD”). Hutchens’s only experience in waterfront residential development dated back to the 1940s, when as a young man he assisted his maternal uncle in developing a community near Orlando, Florida, by doing manual labor. In the 1950s, Hutchens worked as the foreman on the construction of a drainage canal for the runway of an Air Force base in Texas.

Hutchens has not developed real estate since 1985, and to this day has never developed a canalside community. He has, however, been involved in a series of other business ventures, including a company marketing frozen dandelion leaves, an ATM manufacturer, and a plan to export melons from the Caribbean. Each of these projects is currently inactive. As of 1996,

Hutchens was a litigant in two active lawsuits: one over profits from the melon venture and the other over monies Hutchens claimed the City of Buffalo and others owed him as rental subsidies. In the 1960s, Hutchens was a defendant in a criminal bribery trial that was dismissed on double jeopardy grounds.³

Before the contract award, Hutchens retained Kerry Marsh to lobby on his behalf to obtain the contract. Marsh has practiced law for more than 35 years. After working for several respected law firms, he opened his own office in 1993 and has advocated and lobbied for clients, particularly in the transportation industry, before both legislative houses and the executive branch. Although not legally required to do so, Marsh reported his engagement to the Temporary State Commission on Lobbying.

After terminating his relationship with Marsh, Hutchens hired Frederick Hiffa, another lobbyist, to assist in post-award issues. Before setting up his lobbying firm, Hiffa was the First Deputy Commissioner at the New York State Department of Transportation. At the Department of Transportation, Hiffa worked with Michael R. Fleischer, the current Executive Director of the New York Thruway Authority and Canal Corporation.

C. Key Canal Corporation Personnel

The four government officials who played the most significant roles in the Hutchens transaction were Matthew Behrmann, Robert Brooks, Donald Hutton, and Howard Taylor.

Matthew Behrmann, age 42, was the Director of Canal Corporation Operations from October 17, 1996, through June 13, 2000, interrupted by a leave of absence from July 1, 1998,

³ Hutchens reported during this inquiry that he could not remember whether the Canal Corporation ever asked him about any litigation history, either civil or criminal.

through December 10, 1998, when he served as campaign manager for then Attorney General Dennis Vacco. Before working at the Canal Corporation, Behrmann had been a congressional staffer, staff director for the 1993 Defense Base Closure and Realignment Commission, and a lobbyist. When Behrmann left the Canal Corporation in June 2000, he was earning \$109,856 a year. He is now Senior Vice President for External Affairs of the State University of New York Research Foundation.

Robert Brooks, age 62, joined the Canal Corporation on March 31, 1997, as Director of Canal Program Development.⁴ He served as Acting Director of the Canal Corporation Operations during Behrmann's leave of absence, and was appointed its Director when Behrmann left. Brooks was a surveyor before joining the Canal Corporation, and, by his own account, had no experience with economic development policy. Brooks was discharged in April 2003, at which time he was earning \$118,945 a year.⁵ He is now the Executive Director of Harness Horse Breeders of New York State.

Donald Hutton, age 46, became Deputy Director of the Office of Planning at the Thruway Authority on January 11, 1996. On May 3, 1999, he was promoted to Director of Policy Analysis and Development, and on June 25, 2003, was appointed Director of Operations. In his capacity as Deputy Director of the Office of Planning and Director of Policy Analysis and Development, Hutton was required to devote a portion of his time to Canal Corporation matters. Before joining the Thruway Authority, Hutton had been an Executive Deputy Inspector General

⁴ His starting salary was \$71,534.

⁵ Thruway Authority Chairman John Buono has stated that Brooks was fired because he violated the Governor's ban on non-essential travel by attending a boat show in Florida. Brooks contends he was fired because he opposed re-opening the bids for development of the Syracuse Inner Harbor.

in the Office of the New York State Inspector General for eight months, leaving shortly after a public controversy pertaining to his tenure.⁶ Before joining the Inspector General's Office, Hutton had been a private railroad policeman for approximately 15 years. He has also served as a ward chairman in Buffalo and on the Erie County Republican Party Executive Board. According to his resume, in 1990, he ran unsuccessfully for the State Senate. When he left the Thruway Authority in January 2004 (after the Governor requested this investigation), Hutton was earning \$113,049 a year. He is now the Executive Vice President and Director of Governmental Relations for the New York Regional Railroad.

Howard Taylor, age 61, was a career civil servant, having worked for both the states of New York and Vermont. He became an Assistant Right-of-Way Agent in the Albany Division of the Canal Corporation in 1994.⁷ After taking a competitive examination, Taylor became a Senior Right-of-Way Agent in 1998. In 1999, he became a Real Estate Specialist Second Grade, responsible for reviewing and approving permits and other limited land use rights. Taylor also operated his own real estate appraisal business. When Taylor retired from the Canal Corporation in December 2002, he was earning \$73,137. He is now a salesman at the Otto Oldsmobile Cadillac and Isuzu Dealership in Albany, New York.

Behrmann, Brooks, and Hutton each described how they were appointed to Canal Corporation or Thruway jobs when looking for career changes. Behrmann testified that he

⁶ After an investigation in 1995, the State Ethics Committee took no action concerning the allegation that led to this public controversy.

⁷ Taylor's personnel records show that he was appointed to his position with the Canal Corporation under an exception to the Civil Service Rules. Taylor took a competitive examination in 1998 and won a promotion to the position he held until his retirement on December 31, 2002.

“really didn’t like” his work as a lobbyist and spoke to friends of his in the executive branch (“we were all very social”). When they suggested the Canal Corporation to him (“To me the Erie Canal was something from history. I didn’t even know it existed still.”), he viewed it as “probably a reasonable segue” into state government. Brooks was similarly seeking a change. He viewed his business as “kind of in a rut” or “maybe I was in a mid-life crisis” and spoke to a “personal friend” who was a state senator and to the Director of Operations for the Governor, whom he had known “forever.” Hutton testified that he had originally applied for a job in state government through “the appointments office at the state capital,” expressing a preference to work at the Department of Transportation, asking “for support from elected leaders in my area.” Hutton was instead offered a job as Deputy Inspector General in the State Inspector General’s Office; he testified that he was later “transferred” to the Thruway Authority.

D. The Canal Corporation Board of Directors

Thruway Authority/Canal Corporation Board members are appointed by the Governor with the advice and consent of the State Senate. They work part-time without compensation, and serve for staggered nine-year terms. The Chairman of the Board serves as the Canal Corporation’s Chief Executive Officer. All important decisions made by the Canal Corporation, including decisions to transfer real property rights, must be approved by the Board. The Board meets on a monthly basis. One Board member estimated that the Board spends 90 % of its time on Thruway business and only 10 % on Canal Corporation business.

At the time Hutchens first made contact with the Canal Corporation, its Board consisted of Chairman Howard Steinberg, and members Nancy Carey and William Warren. Governor Pataki appointed Steinberg Chairman in 1995. Previously, Steinberg had been a partner at the

law firm Dewey Ballantine, and a senior executive at Reliance Group Holdings, Inc., an insurance company. Carey (daughter of former governor Hugh Carey) was appointed by Governor Mario Cuomo in 1993. Since 1981, she has been a partner at The Picotte Companies, a commercial real estate development firm. Warren was appointed by Governor Cuomo in July 1993. He was the president of Rochester Carting Co., and served on the Board until 1999.

To replace Warren, the Governor appointed John Riedman, who was confirmed on June 22, 1999. Riedman is the chairman of the Riedman Corporation, an insurance firm in Rochester, New York. Steinberg left the Board on April 29, 1999, and the Governor appointed Louis Tomson to replace him. Tomson previously served in a variety of government positions, including as Governor Pataki's First Deputy Secretary, with responsibility for public authorities. Tomson resigned in June 2002, and was replaced by John Buono, the President of Hudson Valley Community College and the former Executive Director of the State Dormitory Authority.

In January 2000, when the Board approved the Hutchens proposal, the Board members were Tomson, Carey, and Riedman.

E. The Process for Approving Real Estate Transactions

When Canal Staff decides that a sale, lease or other disposition of Canal system land is desirable, the proposed transaction goes through a three-step approval process. First, the Recreationway Commission determines whether the transaction is compatible with the Canal Recreationway Plan. Second, the Canal Corporation's Real Property Management Committee (consisting of the Director of Canal Corporation Operations, the Thruway Authority General Counsel, and the Thruway Authority Chief Financial Officer) determines whether the transaction

is reasonable. Third, the Canal Corporation Board determines whether to approve it.

Approval by the Board authorizes staff to negotiate and enter into a final lease or sales contract and sets the parameters for that negotiation. After the contract is signed, the Canal Board voluntarily submits it to the Comptroller so that it can be reviewed for procedural correctness, that is, to ensure that the agency followed the required steps before awarding the contract and that the transaction is not improvident. As part of the Comptroller's approval process, the Office of the Attorney General reviews the contract. The Attorney General review is for form only, and does not include a substantive review of contract terms.

2. History Of The Hutchens Transaction

A. May 1996 to February 1998: Hutchens's Proposal and Initial Efforts at Securing Board Approval

To advance the Recreationway Plan of transforming the Canal into a center for tourism and recreation, in May 1996, Board Chairman Steinberg sent a letter to approximately 200 companies and individuals. The letter sought to "solicit views regarding the canal's development potential, and in particular, prospective interest in participating in" the effort to revitalize the Canal. The addressees included a broad array of companies and organizations, including theme parks, hotels, and canal boat operators. About twenty were involved in the real estate business.

Hutchens was added to the mailing list after conversing with Donald Hutton, then Deputy Director of Planning at the Thruway Authority. According to Hutchens, he read a newspaper article about Hutton's departure from the Office of the Inspector General and called to ask for assistance with certain ideas for Erie Canal development. According to Hutton, he had never

previously spoken with Hutchens, although Hutton believed they had likely attended political fundraisers together in their native Buffalo. During the call, Hutchens mentioned the name of a mutual acquaintance – Edward Ryan, who was the City of Buffalo Republican Party Chairman.

Hutchens wrote Steinberg a two-page letter in late May 1996, addressing a variety of topics, including “an expansion of the sport of fishing to include salmon, since that would expand the fishing season.”⁸ As to RHA’s participation, Hutchens wrote: “Our company would be interested in the management or ownership of fuel and food barges, assisting in putting together a fleet of cargo barges for shipping to and from New York State, and are most interested in cluster development.”

Hutton followed up on the letter and met with Hutchens in Buffalo in August 1996. In an email to Patrick Garvey, then Director of Canal Business Enterprise, Hutton described a proposal that Hutchens made at the Buffalo meeting to develop canalside residential communities with cuts into the Canal to create marinas.

Hutton’s email stated that Hutchens had “extensive experience” with such developments in Florida. Hutchens, however, had never built marinas, in Florida or anywhere else. Hutchens stated in interviews that he told Hutton of “plans” he once had for a Florida canalside community, but was uncertain as to whether he also revealed that those plans never came to fruition. Other Canal Corporation employees also testified that Hutchens stated to them that he built canal cut communities in Florida.

In September and October of 1996, Hutchens joined the Canal Staff at their invitation for

⁸ Hutchens first faxed the letter to Hutton for review.

the annual end of season inspection tour of the Canal system. During this tour, which was conducted by boat, and traversed the entire length of the Canal, Hutchens identified a total of only 43 sites he believed might be suitable for developments.

In October and November, Hutchens presented draft “business plans” to the Canal Corporation, setting forth his vision for “cluster village developments.” The presentation contained a brief description of the concept with a schematic diagram:

It is our intent to have each village complement the recreational aspects of the state recreationway. We therefore plan to include at least two of the following four amenities in each village: tennis courts, a clay shooting range, horse stables and a golf driving range. Additionally, there would be roughly four months of boating, four months of snowmobiling and cross-country skiing, and a month to a month and a half of salmon fishing.

The reference to salmon fishing concerned Hutchens’s plan to import salmon into the Erie Canal and to construct “salmon ladders” to allow them to navigate past the Canal locks.⁹

Hutchens proposed to target these developments to a demographic group identified in a January 1997 article in *Investors Business Daily* as “lone eagles.” The article described “lone eagles” as telecommuters who, because they do not need to live near their workplace, are able to live at a place that provides such recreational and other amenities as they choose, such as ski resort towns of the Rocky Mountains. Hutchens argued that his canalside communities would attract such individuals, and frequently pointed to the article as proof that there was a market for his proposed developments.

Hutchens’s plan did not discuss the costs of creating such developments or Hutchens’s

⁹ Canal Staff notes show that as late as October 1998, Hutchens had discussions with Canal Staff on the process for stocking the Canal with salmon.

financial status. Internal RHA notes, provided to the Canal Corporation by Hutchens, projected the potential revenue from a single 261-lot community at \$21.68 million.

Under Hutchens' initial proposal and all of his subsequent ones, Hutchens did not seek to buy Canal lands. He sought exclusive rights to purchase easements to cut into the Canal bank so that he would be the only developer in New York who would be able to construct private canals and marinas that had direct access to the Canal for residential developments with at least ten units. His proposals all contemplated that Hutchens would first buy or option the lands necessary to develop his Canal communities. Once he had obtained these properties and had all the appropriate regulatory and zoning approvals, he would then exercise his option to purchase an easement to cut through the Canal bank and open a channel from the land he owned to the Canal. The exclusive right that Hutchens sought was to construct private canals and marinas that had direct access to the Canal.

According to Hutchens, he intended to divide the Canal into six market areas, and select a particular developer for each one. He testified that he hoped to use his exclusive rights to "control" development so as to prevent, in his words, "saturation." That is, he hoped to limit the number of canal cut communities so as to create scarcity and increase price.¹⁰ Hutchens avoided even talking to landowners until, in his words, he had "absolute control." He explained, "[B]ecause you might run the price up. You might bring a competitor in. It's just the last thing you want to do is talk to anybody."

¹⁰ Hutchens argued to the Canal Staff that he needed exclusive rights to prevent "copycat" developers from marketing similar properties. He expressed specific concern that Andrew Cuomo, a prominent Democrat and then-HUD Secretary in the Clinton administration, would become New York Governor and interest additional developers. Thus, he asked for an option to purchase easements for any of the 43 sites he chose, and for protection against competing developers creating similar sites.

In interviews during this investigation, Hutchens voiced a low opinion of the Canal Staff: “They had never done [development], or they wouldn’t be where they’re at. They wouldn’t be working for the [government] if they had.” Talking specifically about Brooks, Hutchens said: “The executive director had been a surveyor and that’s as near as they had of anybody that had ever been around, to my knowledge, people who knew anything.” He continued, “Hutton was railroad police, I think is what he was. Brooks is the only one, he had just been a land surveyor, and all he knew was how to drive stakes and tie flags, and Brooks was Executive Director of the Canal Authority. The rest of them had been there all their lives.”

For the next ten months, Hutchens worked with the staff of the Canal Corporation to polish his proposal. In his words, “I didn’t take them to college, I let them get their own education.” This relationship culminated in a July 9, 1997, memo that Behrmann wrote to the Canal Board in order, according to Behrmann, to lay the groundwork for approval of Hutchens’s plan. In particular, Behrmann hoped to gain the support of Board member Nancy Carey, a commercial real estate developer on whom other Board members frequently relied regarding real estate matters.

Berhmann’s memo described the contemplated Hutchens transaction and reported that “a background check was conducted which revealed that Hutchens has had an [sic] outstanding success with these types of developments in Virginia and Florida.”¹¹ The investigation has uncovered no basis for this assertion. By Hutchens’s own account, he had no such experience, and the Canal Corporation has produced no documents – from any source – purporting to show

¹¹ The initial draft, prepared by Thruway Authority employee Sharon Leighton, did not refer to a background check, and merely asserted that Hutchens had experience with these kinds of communities. Leighton believed she had learned of Hutchens’s purported experience with canalside communities from Donald Hutton.

that he did. Indeed, the whole of the due diligence package produced by the Canal Corporation during the investigation was: (1) two Dun & Bradstreet reports from, respectively, June 1997 and December 1999; (2) an article downloaded from LEXIS/NEXIS on river boat gambling quoting a “William” (not Richard) Hutchens; (3) an article by the Buffalo News food editor titled “Weed or Feed” discussing Hutchens’s frozen dandelion business; and (4) a piece of an article mentioning Hutchens’s low-income housing property.¹² In interviews, Behrmann could not recall any additional background investigation.

Whatever Hutchens may have said orally, in his written submission to the Canal Corporation, he did not claim to have completed canal developments. Instead, he represented that he had been “engaged in land development programs in New York, Oklahoma, Texas, Florida and the Caribbean for over 30 years.” The full truth was that in Florida, he performed manual labor for a relative, and in Texas he was the foreman on a drainage ditch project. In the Caribbean, he had participated, at most, in economic development, namely a melon export venture.

In any event, Behrmann’s effort to persuade Carey foundered. Carey told Behrmann that she was concerned that the Canal Corporation was undervaluing the easements it was selling, then priced at \$35,000 per easement. She told Behrmann that the proposed easement price was “not even close” to the value that the canal cut would add to the private developments.

Several months later, in February 1998, the Hutchens’s proposal for an option formally

¹² Later the Corporation also received a copy of the unaudited personal financial statements that Hutchens submitted to HUD, showing a net worth in 1997 of \$4.4 million, but total cash assets of only \$11,100.

came before the Board under the name “Alpine Keys.”¹³ This proposal, and all subsequent ones, had three components: (1) sites (number and location); (2) length of the option period; and (3) price.

Each component had a number of elements. The first component, the sites, was eventually broken into two subcategories: primary sites and secondary sites. Hutchens would have exclusive development rights to *primary* sites, and only a right of first refusal as to *secondary* sites.

The second component, length of the option, established how many years Hutchens would have to exercise his option, i.e., Hutchens’s lock-up period. Over time, certain conditions were negotiated that Hutchens would have to meet to extend his lock-up period.

The final component, price, included a number of elements. First was the money Hutchens was to pay for the option itself, the “option payment.” (Sometimes this was conceived as a one-time payment and other times as annual payments; sometimes it was conceived of as a lump sum and other times as separate payments for sites.) Second were fees Hutchens was to pay when he connected the communities to the Canal by digging a connecting waterway, fees known as “cut fees.” Third were annual fees that Alpine Keys homeowners would pay for water and dock access, known as “homeowner’s fees.”

¹³ In his interview, in which Hutton described Hutchens stated preference for development sites that were not close to urban areas, he described how Hutchens came to choose the name Alpine Keys for his project:

“The one that sticks in my mind – I thought it was genius when I heard it – was near Frankfort. [W]e asked him why there of all places. And he said it’s got a snow mountain. In fact, he was interested in buying the snow mountain too. That’s where the Alpine Keys concept came from, because you got Florida Keys. He said Alpine Keys. . . . The snow birds would stay, put their boats up and they could ski, have a chalet by the water, and do things.”

Behrmann wrote a memo to the Canal Corporation Board on February 6, 1998, setting forth the proposed terms for Alpine Keys. They were:

Number of sites	Primary	10 sites.
	Secondary	33 sites.
Lock-up period	Total possible lock-up period	10 years for primary sites. 20 years for secondary sites.
	Conditions	If an unspecified number of sites are not developed within a specific number of years, all remaining option(s) may expire.
Price	Option payment	\$750 each for primary sites. \$1,125 each for secondary sites.
	Cut fee	\$15,000 plus 2 % escalation fee per year, less total option fees paid for any primary sites.
	Homeowner's fee	\$250 per year.

This proposal had a broad reach. As to sites, on his tour of the Canal Hutchens had identified a total of 43 sites that he believed could be developed. This proposal sought to encompass all of them, giving Hutchens an effective monopoly. Moreover, if he got the lock-up period he sought, he would have that monopoly for at least a decade, and perhaps two.

As to price, according to Behrmann's memo, the recommendations were based on the "appraised value of a 100' wide bank cut," said to be between \$10,000 to \$15,000. In fact, there had been no such "appraisal." To the contrary, the Canal Corporation's primary appraiser believed it would be impossible to value bank cuts without reference to specific sites, and

recommended that the fees be set “administratively.”¹⁴ The memo justified the exclusivity on the ground that Hutchens should be afforded “protection against copy-cat developers.”

Hutchens believed that he was entitled to “protection” because he was the first to envision canal cut communities, and thus, as he later wrote, his idea was “on the edge of being more fully and correctly identified as an intellectual property right.” Indeed, RHA’s manager later testified at a hearing that no one had constructed this type of development for 180 years. These claims were just wrong. In the late 1960s, two residential communities – Seneca Estates (60 residences) and River Island Estates (30 residences) – were built along the Seneca River with cuts into the Canal, giving residents waterway access from their homes. Moreover, at least one other developer had obtained a permit in 1990 for a canal cut residential development on the Oswego River, although he had not yet commenced building.

Canal Corporation staff involved in the Hutchens transaction, however, apparently made little effort to determine if there were extant canal cut communities. The senior staff seems to have been unaware of such communities until 2004. At that time, a Canal engineer sent an email to the Syracuse Division Director inquiring about the existence of any such sites. He received a reply ten minutes later telling him of “a couple of high price developments” built around a canal cut.

In any event, contemporaneous notes show that the Board was not satisfied with the proposal and tabled the matter, expressing three concerns: (1) the number of sites to be

¹⁴ One measure for such a figure that was discussed within the Canal Corporation was the estimated cost to the Canal Corporation of refilling a canal cut in the event Hutchens was unable to complete a project, calculated to be \$40,000. This figure was based on a canal cut of 60 feet in length. In fact, the real cost of refilling the canal cuts proposed by Hutchens would have been significantly greater. Hutchens submitted documents to the Canal Staff in which he indicated that his contemplated canal cuts would be between 75 feet and 100 feet.

encumbered by the agreement was too large; (2) the time frame for the proposed agreement was too long and should be limited to 10 years; and (3) the fees were too low and should be double or higher.

B. June 1998 to July 1998: The Canal Corporation Enters into Another Deal with Hutchens

After the Board tabled the Alpine Keys proposal, the Canal Corporation staff brought Hutchens into a second venture, which involved an effort to save their failing efforts to run charter boats on the canals. Hutchens entered into a contract for this venture to accommodate the Canal Staff. In the end, Hutchens did not perform under the contract, staff forgave his nonperformance, and new Board members were not told of the failure before they ultimately approved the Alpine Keys proposal.

In its master plan, the Canal Recreationway Commission had recommended the introduction of charter touring boats, which are common on European waterways. Accordingly, in 1996 the Canal Corporation began negotiations with an overseas company, Crowne Blue Lines (“Crowne Blue”), which staff described in a memo as “the only known company” that had in place “the sophisticated marketing system capable of creating a market on the New York State Canal System to support the multi-boat fleet envisioned in the plan.”

In 1997, the Canal Corporation invested \$307,000 to construct a marina for Crowne Blue’s benefit in Frankfort, New York. Crowne Blue, however, had not yet entered into a contract with the State, and the deal collapsed.¹⁵ This left the Canal Corporation with a vacant

¹⁵ Crowne Blue pulled out after Canal Staff insisted that it build a certain number of boats at a boat building company that staff had designated, Penn Yan Marine Manufacturing, Inc., or another New York boat company.

marina that Hutton referred to as a “white elephant.”

Staff viewed the empty marina as, in the words of one, “embarrassing,” and determined to find a new tenant as quickly as possible. They turned to Hutchens, who had no experience with the boating business, to save the project.¹⁶

The Canal Corporation did not advertise the availability of the newly built marina for lease or purchase. Instead, according to Hutchens, Brooks asked him to take over the Frankfort facility during a meal in Albany, after which he drove Hutchens out to see the marina.¹⁷

Hutchens testified that he agreed to lease the building because he “didn’t want to make an enemy” out of Brooks. He testified: “I wanted to keep everybody happy I just assumed that there was heat on Bob, probably” Contemporaneous writings by Hutton corroborate Hutchens’s account; he wrote that Hutchens became involved “at the behest of the NYSCC staff . . . in part as proof of his company’s commitment and willingness of investment to assist the Canal Corporation.”

Crowne Blue had been working with the Town of Frankfort to apply for a HUD loan for Crowne Blue’s boat construction. After Hutchens agreed to step in, Canal Staff sought to convince Frankfort to insert Hutchens in Crowne Blue’s place on the loan application. When Frankfort officials missed a meeting to advance Hutchens stepping in, Canal Staff tried to

¹⁶ Brooks said the Canal Corporation sought to bring canal boat operator Mid-Lakes Navigation into the facility, but it was not interested. Mid-Lakes Captain Dan Wiles has no recollection of such an offer, and was not even aware that Hutchens was given the contract. Brooks could not recall any other contacts made to fill the facility.

¹⁷ Hutchens testified that Brooks took him “in his car a 100 or so miles just to show me the deal right in the middle of the day, and he didn’t even know I was there, and he cancelled everything to take me out there and show it.”

pressure them.

At the time, June 1998, Brooks was living with Lynn Griffiths (they were later to marry), who was Chief of Staff to State Senator Jim Seward. Griffiths wrote a memo to Senator Seward and Assemblyman Marc Butler reporting that Behrmann had placed an “urgent call” to her complaining that certain Frankfort officials had failed to show up for a meeting with Hutchens. The memo quoted Behrmann as saying that Hutchens was “ready to begin building boats,” and planned to build more at a “more accelerated rate than the Crowne Blue operation.” Griffiths wrote that Behrmann and Brooks had “checked [Hutchens’s] credentials out” and found him to be a “millionaire with a successful track record in other states.” She urged the legislators to “turn up the heat” on Frankfort officials to get them to deal with Hutchens. According to Lynn Griffiths, she later learned from conversations with Senator Seward that he called the Mayor of Frankfort to urge him to meet with or call Mr. Hutchens. The Mayor of Frankfort, however, does not remember receiving such a call. Steinberg, Chairman of the Board at the time, did not know of Behrmann and Griffith’s efforts, and testified, “I would question the appropriateness of this kind of local intercession on behalf of a private party. [It] does not look as though they were using the best judgment in doing this.”

Canal Staff proposed to the Board on July 15, 1998, that the Frankfort lease be given to Hutchens. Their supporting memorandum said that Hutchens would “guarantee, as a condition of the lease, that a minimum of five charter boats would be based at the Frankfort facility between June 1st and October 1st each year.” Hutchens’s business plan (which arrived the following day) promised that five “yachts” would be “launched for immediate service.” Contingent on the staff’s evaluation of the adequacy of his business plan, the Board approved the

award of the lease to Hutchens on July 23, 1998.

Hutton later referred to Hutchens as a “*White Knight*’ [who came] to save the deal after British CBL [Crowne Blue Lines] pulled out.” Ultimately, however, Hutchens did not prove to be a savior. A year later, he defaulted on his lease.

C. July 1998 to August 1998: Hutton Encourages Hutchens to Make Campaign Contributions and to Hire a Lobbyist

Also in the summer of 1998, Hutton began to introduce Hutchens to a group of politically influential people in New York State by arranging for him to attend an annual event that involves fundraising and socializing, the National Baseball Hall of Fame weekend hosted by the New York Susquehanna & Western Railroad (“Susquehanna Railroad”) in Cooperstown, New York.

Each year, on the weekend that the Hall of Fame inducts new members, Walter Rich, President of the Susquehanna Railroad, hosts a series of events in Cooperstown. Over the years, attendees have included politicians, government officials, business executives, baseball greats, and guests’ family members. The Susquehanna Railroad provides lodging, lunches, dinners, and tickets to baseball games, at a cost to the company that Rich estimates at approximately \$100,000 per year. A significant feature of the weekend is a series of fundraising events for both Republican and Democratic candidates for office.

Donald Hutton was a regular attendee of Rich’s Hall of Fame weekend event. Hutton first met Rich when Hutton worked for Rich as a private railroad policeman in the late 1980’s, and the two remained close. Indeed, while employed by the State, Hutton sent confidential

documents to Rich, which Rich used for his private benefit.¹⁸ Hutton testified that, in his opinion, Rich valued their relationship because he viewed Hutton as “bright and intuitive.”

Documents show that sometime after June 1998, Hutton arranged for Hutchens to attend that summer’s Cooperstown gathering.¹⁹ Rich testified that Hutton held Hutchens out as a potential political donor, and, in a 1999 email, Hutton promised Rich that Hutchens would be one of Rich’s “future players.”

In fact, Hutchens did make contributions in connection with the Hall of Fame weekend.²⁰ Hutchens testified about his intent in making political contributions: “Everybody makes a political contribution for a purpose. . . . Anytime you do anything you do it for a purpose. My purpose was, that I’m living in New York, and I need to be a friend, be acquainted with people

¹⁸ In one instance, for example, Canadian Pacific Railroad (“CP”) sought the aid of the Thruway Authority in gaining New Jersey approval for a port project, by which it hoped to compete for New Jersey’s chemical transportation business. Hutton discussed the plan with Rich, who advised him to squelch it. Hutton stated to the involved employees – correctly – that the Thruway Authority had no jurisdiction over the matter, and directed them to have nothing further to do with CP, and to refer any contacts on the matter to him. He then forwarded the internal Thruway Authority memos to Rich. Rich acknowledged that he “probably” passed on word of CP’s business plans to two of the Susquehanna Railroad’s shareholders, the Norfolk Southern and CSX Railroads, both of which would compete with CP for the New Jersey business it sought. Rich had not been aware of CP’s plans – which were not public – before being informed of them by Hutton. Hutton has provided Rich other materials, including a New York Department of Insurance legal memorandum on proposed legislation, which Rich gave to an insurance company for which he sits on the board of directors.

¹⁹ One of the documents received from Rich is a document labeled “Hall of Fame Accommodations Needed,” dated July 17, 1998. It is a chart that lists various guests. Next to Hutchens’s name, a column labeled “contact” contains the statement “via Don Hutton.” Under a column labeled “notes,” it states “Attending Boehlert function - etc.”

²⁰ The largest contribution that Hutchens made to any candidate from 1997 through 2003 appears to have been arranged by Hutton: In 1999, Rich’s assistant wrote in an email that Hutton had told her that Hutchens would attend a breakfast for Governor Pataki at the 1999 Hall of Fame weekend. On a printed copy of that email, there is a handwritten note by Rich’s administrative assistant indicating “5,000” – the sum Hutchens eventually donated. In 2001, Hutchens again donated \$3,000, and was named as a vice-chairman for a fund raiser for the Governor at the Hall of Fame weekend.

that make things happen.”²¹

Hutchens testified differently when asked about a particular contribution. Berhmann – who was, by then, on leave from the Canal Corporation to manage the campaign of Attorney General Dennis Vacco – also attended the 1998 Cooperstown weekend. During the weekend, Rich held a breakfast for the Vacco campaign, which approximately ten people attended, including Hutchens, Berhmann, and Hutton. Hutchens testified that Behrman “hit him up” for a contribution, but he could not remember whether this happened at Cooperstown or elsewhere. Records show that Hutchens contributed to the Vacco campaign both before and after the breakfast. When asked whether those were intended to influence Behrman, Hutchens testified, “I can’t see how I could even dream of that,” and said any suggestion to the contrary was “bullshit.” Behrman denied soliciting Hutchens.

Also attending the Hall of Fame weekend in 1998 was Kerry Marsh, a prominent attorney and lobbyist. Marsh was a regular attendee of Rich’s Cooperstown events, and Rich was Marsh’s client. Hutton knew Marsh as well, and introduced Hutchens to him. According to Marsh, Hutton brought Hutchens over to meet him. As Marsh remembered it, Hutton said: “There is someone you need to talk to, Kerry. He has been trying to get a really good project for the better part of a year or two. He might be able to use some help.” Hutchens described his idea and asked if Marsh could “move things forward.”

²¹ In 1997, Hutchens contributed to neither the Vacco nor Pataki campaigns. In 1998, Hutchens contributed \$2,075 to the Vacco campaign and \$1,000 to the “Governor’s Club”; in 1999, \$6,000 to Friends of Pataki (\$5,000 of which appears to have been arranged by Hutton); in 2000, \$1,000 to Friends of Pataki; in 2002 \$3,000 to Friends of Pataki; and in 2003, \$2,500 to friends of Pataki. There is no evidence that the Governor was aware of Hutchens’s contributions. There is plentiful evidence that Hutton and Behrman knew of or assisted both the contributions and the project.

Marsh testified that Hutton told him that he favored Hutchens's proposal but explained, "We are having this difficulty." Then Hutton asked, "Kerry, maybe you can help him out." Marsh additionally testified that he knew Hutton to be politically "connected" and also that he viewed it as significant that Hutton held a post in the Thruway Authority: "I do know he was Director of Planning and I do know he had an official position on this." Marsh stated that he could think of no other instance where he was recommended to take on a client by an employee of the agency he was to lobby. Marsh did not accept the retention until placing a call, in his words, to "someone in the governor's office." Marsh could not remember to whom in the governor's office he spoke.²²

Hutchens socialized with other government officials and political figures at the Hall of Fame weekends. For example, on one occasion, Hutton requested that Hutchens stay in the same lodging with him and Dennis Ryan, Chairman of the City of Buffalo Republican Party Chairman. And Hutchens also met Robert King (then the State's Budget Director), his wife Karen King,²³ and Michael Bragman (the majority leader of the New York State Assembly until 2001 and a

²² Marsh testified that this was part of his "due diligence" before accepting the retention, and that he contacted the Governor's office in order to make sure that he did not hear anything "untoward or bad" about Hutchens.

²³ Hutchens testified that he even took the Kings's daughter fishing on one Hall of Fame weekend. Karen King recalled fishing with Hutton, but not Hutchens. Marsh's notes of a November 1, 1999, conversation with Hutchens about the incident are as follows:

"Bob King went up in helicopter
Hutchens took Jess and Karen fishing . "I 'see ll
to it that you get it."

Karen King denies that she ever told Hutchens that she would "see to it" that Hutchens's project was approved. Hutchens issued a similar denial: "No one ever told me they were going to make something happen. I'm sure they could have said we hope it will happen. We look forward and want to see it happen. Something like that. No one ever positively said they were going to make it happen. No way." Marsh testified that the notes accurately reflect what Hutchens told him. Marsh was uncertain as to what the "it" in the notes referred to.

developer).²⁴ Hutchens later turned to the Kings for help in getting his proposal approved, and tried to develop a portion of the Canal with Bragman.

D. August 1998 to January 1999: Initial Lobbying Efforts

After the 1998 Hall of Fame weekend, efforts increased to get the deal done. Marsh's endeavors began promptly. His billing records reflect that he spoke to Behrmann on Hutchens's behalf on August 11, 1998. Officially, Behrmann was on leave of absence at the time to campaign. The day before, Hutchens had made a donation to Behrmann's candidate. Neither Marsh nor Behrmann remembered the call.

During the fall of 1998, Canal Staff continued developing Hutchens's proposal and working to convince members of the Board to approve it. These efforts entailed sharing internal Canal Corporation documents with Hutchens. In particular, Hutchens produced from his file a copy of a memo that Behrmann wrote to the Board that contained the staff's recommendations to the Board on the project, including recommendations on fees. RHA also sent drafts of submissions to Canal Staff members for prior review. Marsh forwarded to Brooks a proposed business plan for review, and Hutchens had Brooks review presentations to be used with Board members. Similarly, Hutchens met with Canal Staff to discuss how to make his proposal more palatable for the Board. On at least one occasion, Hutchens faxed Brooks a draft of a planned submission to the Board for "approval."

During this period Marsh contacted Nancy Carey, whom he believed was the key decision-maker on the Board. Brooks had informed Marsh that Carey did not think the Hutchens

²⁴ Bragman was removed from his post as majority leader in 2001, after an unsuccessful attempt to unseat Assembly Speaker Sheldon Silver. He resigned from the Assembly effective January 1, 2002.

plan would work and did not want to lock up so many properties.

Marsh arranged a face-to-face meeting for December 7, 1998, at Carey's business offices in Albany, New York. It confirmed what Marsh had learned, namely that Hutchens's request for exclusivity was as yet not acceptable to Carey. Carey was also unpersuaded that Hutchens needed a low entry price for the project to succeed.²⁵

After meeting with Carey, Marsh told Hutchens that the plan would not be passed unless Hutchens modified his request for exclusive rights and offered additional money. Marsh then talked to Brooks and John Platt (then the Executive Director of the Thruway Authority and the Canal Corporation) to jointly develop a strategy to gain approval for the Hutchens deal.²⁶ This strategy involved having Hutchens abandon the idea of exclusivity for the entire Canal and only address the amount that should be paid for canal cuts after Canal Staff made a presentation to the Board projecting the revenue the Canal Corporation would derive from the deal.²⁷

²⁵ Unlike Marsh, Carey recalls the meeting only vaguely.

²⁶ John Platt, who had previously worked as Chief of Staff for the Ohio Transportation Authority, was the Executive Director of the Thruway Authority and the Canal Corporation from 1996 until his resignation in April of 2003. Platt, who was a strong supporter of the Hutchens transaction, died at the age of 61 in September 2004. Because Platt was ill for some time before his death, he could not be interviewed.

²⁷ A September 16, 1999, memo from Marsh to Hutchens, entitled "Status Report," reads, in pertinent part:

I have spoken with John Platt and Bob Brooks. The following is an outline of a strategy we believe will bring this matter (hopefully successfully) to a close by the next meeting of the Canal Board. . . . Bob Brooks will make a "first cut" of canalway sites which are not conducive or which cannot be developed for external reasons. The plan is to give Richard A. Hutchens and Associates an exclusive right to develop a significant portion of broadly identified canalway shoreline, but not an exclusive right to develop the entire state canal system (at least not at this time). Staff and I believe that this will provide a major incentive for the Canal Board to approve your plan. . . . Platt, Behrmann and Brooks are preparing a financial presentation for the Canal Board showing revenue projections, which can be realized, from developed canal residential communities. . . . At this time we should not address the canal cut fee (which some Board members think is too low at \$15,000 per cut), we will address this after the fiscal presentation has been made. Hopefully then, the Canal Board members will see the revenue is dependent on the final development, not the cut

- E. January to February 1999: Behrmann Returns and Recuses Himself, but Continues to Work on Hutchens's Projects

On December 10, 1998, Behrmann returned to the Canal Corporation as Director of Canal Corporation Operations. Aware of Hutchens's campaign contributions, Behrmann removed himself from material dealings with Hutchens. In a letter to Brooks dated January 5, 1999, Behrmann wrote:

Bob:

I wanted to be sure and memorialize our discussion of earlier today regarding the Hutchens project.

As we discussed, I am aware that Mr. Hutchens was a contributor to a number of republican candidates during the last election, including the Attorney General, Dennis Vacco. I never solicited any contributions from Mr. Hutchens and that was the restriction guidance that I was provided by the NYS Ethics Commission prior to my leave to manage Mr. Vacco's campaign. However, to avoid even an appearance of a conflict of interest, I would like you to handle all matters relative to any dealings with Mr. Hutchens.

I intend to not participate in any material way with any projects involving Mr. Hutches [sic] personally or his corporations. The only way I will be forced to be involved with the consideration of any Hutchens related matters may be as the proxy Chair of the Canal Recreationway Commission. In that event, I would like you to lead the discussion/presentation of the matter and I will only proceed over the consideration of the matter and solve conflicts between members.

Bob, I would also greatly appreciate your witness to this discussion and this letter clarifying my position I would like to take to protect my integrity and the integrity of the great system we are privileged to manage.

Brooks countersigned the letter as a witness. Behrmann testified that he did not tell other Canal

fees. Perhaps then, in order to encourage you to develop the sites, they will agree to the proposed \$15,000/cut fee. We can discuss this with Riedman, Tomson and Carey in individual meeting, or at the next Board Meeting where Platt/Brooks want you to appear.

Corporation employees or the Board about his recusal. Nor did he tell Hutchens.²⁸

Behrmann testified that, as set forth in the letter, he did, indeed, cease involvement with Hutchens-related transactions, except for instances where he had unique historical knowledge or was performing ministerial tasks.

The evidence clearly controverts this testimony. Behrmann remained intensely involved with Hutchens's proposals. Between January 7 and January 12, just days after signing the letter, Behrmann recommended that the Corporation enter into the Frankfort lease with Hutchens.²⁹

²⁸ The Canal Corporation withheld Behrmann's recusal memorandum from the legislative committee that later investigated the Hutchens deal, on the stated grounds that the committee had functionally made a freedom of information request of the Corporation rather than issuing it a subpoena. In the Spring of 2003, Assemblyman Richard L. Brodsky, Chairman of the Committee on Corporations, Authorities and Commissions (the "Committee"), conducted public hearings on the Canal Corporation land deals. Initially, Assemblyman Brodsky held hearings on the Inner Harbor Development in Syracuse, New York, for which the Canal Corporation provided land. The hearings concerned allegations of improper political influence in the award process for the development contract, and allegations that Brooks and Thruway Authority Director John Platt had been fired for their dissent from the award. The Committee issued a subpoena to the Canal Corporation for documents related to that project.

During the July 18, 2003, public testimony of Executive Director Michael Fleischer, Assemblyman Brodsky raised the Hutchens transaction. Brodsky subsequently asked for all documents relating to the "sale and/or lease of canal front development rights between Buffalo and Syracuse." No subpoena was issued for these materials, but an August 4, 2003, letter from a Brodsky staff member memorialized the Canal Corporation's commitment, and was then followed by a September 22, 2003, letter from a Brodsky staff member specifically requesting "any and all documents" pertaining to the Hutchens deal.

According to Edna Goldsmith, assistant counsel to the Thruway Authority, while she was reviewing documents to be produced to the committee, Sharon O'Connor, Thruway Authority General Counsel, came into her office and told her that Behrmann (who, by then, was no longer at the Corporation) had called worried that the "Assemblyman is after me," and had asked that staff find and send him a copy of his recusal letter. Staff found the recusal letter, as well as documents demonstrating that Behrmann had continued to be involved with the Hutchens transactions.

Over Goldsmith's objections (which she reduced to writing in a memo to the files) the Canal Corporation decided to withhold Behrmann's recusal letter from the Committee. Goldsmith was informed of this decision by O'Connor after a meeting at which Goldsmith, O'Connor, and now-Executive Director of the Thruway Authority Michael Fleischer discussed whether documents (including non-privileged documents) ought to be withheld.

On July 23, August 2, August 27, and September 3, 2004, the Canal Corporation provided five additional boxes of "documents related to Canal development issues" to Assemblyman Brodsky. The Behrman recusal letter was part of this larger, supplemental response, but was not specifically identified in any of the transmission letters from the Canal Corporation to Assemblyman Brodsky.

²⁹ This recommendation is documented by Behrmann's signature on the contract itself under the endorsement "Recommended." In addition, the contract bears "Approved" signatures, all below the legally binding signature of the Executive Director of the Canal Corporation, then John Platt.

And Behrmann remained deeply involved in Alpine Keys. Marsh wrote a memorandum to Hutchens on January 20, 1999, saying: "I spoke to Matt Behrmann and Bob Brooks regarding immediate procedures and strategies for presentation of the Alpine Keys Project proposal to Howard Steinberg, Chairman, and to other members of the New York State Canal Corporation Board, including William Warren and Nancy Carey." The memo reported that Brooks had represented that "Behrmann will speak directly with Steinberg to enlist his support and then with Carey and Warren, both of whom have indicated their conceptual support. He will then report back to us prior to the Recreationway Commission meeting."

As Marsh's memo to Hutchens reflects, the next step was to schedule a discussion with the Canal Recreationway Commission. Marsh explained to Hutchens their strategy for succeeding before the Commission: "As you are aware, the Canal Recreationway Commission is the advisory commission to the Canal Corporation Board and would normally review a project prior to its going to the Board; however, Behrmann/Brooks think gaining Board support immediately is the best way to 'presell' this project to the Commission." He added, "We will follow their recommendation, obviously."

The proposal to grant Hutchens an exclusive option was presented to the Recreationway Commission on February 17, 1999. Brooks reported that the Canal Corporation's intent was to offer Hutchens "exclusive rights" for a number of years on "large scale residential developments that specifically want access to the canals." Brooks defended the exclusive by stating that Hutchens "intends to invest a large amount of dollars to analyze possible sites, to obtain options on properties, and to buy properties." Behrmann also spoke about the deal at the

meeting, despite his recusal letter. Marsh, who had lobbied some Recreationway Commission members before the meeting, spoke on behalf of the proposal as well.

In a memo, Marsh reported to Hutchens serious reservations by some on the Commission: “While the overwhelming majority of the members endorsed your ideas of development, an equal number expressed severe reservation or outright opposition to granting an exclusive right to you or any developer. Arguments made by me and the staff in support of the need for a form of exclusive arrangement, coupled with the explanation that this current proposal was already a major compromise from that originally submitted, unfortunately were not persuasive.”

Indeed, members of the Commission raised the idea of a competitive process to seek out other developers. Marsh wrote of the meeting: “two members lead by Dominick Jacangelo, Esq., representative of Bernadette Castro, Commissioner of the New York State Department of Parks and Recreation, questioned why this proposal had not been the subject of an [sic] Request for Proposal (“RFP”) because it proposed an exclusive right.”

F. February 1999 to July 1999: The Guise of a Competitive Procedure and the Second Tabling by the Board.

To the extent that either the Canal Corporation staff or members of the Recreationway Commission believed that an RFP – a regulated and orderly method of soliciting business and selecting vendors – was legally required, they were mistaken. Since the Hutchens proposal involved the sale of an interest in real estate and not the acquisition of goods or services, neither

the Public Authorities Law³⁰ nor the Canal Corporation's policies and procedures required that a competitive process be employed. Indeed, as a legal matter, the Canal Corporation was free to negotiate a deal with Hutchens without entertaining any requests for proposals from other developers. This is not, however, what the Canal Staff did. Instead, under the guise of conducting a competitive procedure, which they referred to as an RFP both inside and outside the agency, Canal Staff never deviated from their initial plans, and made no meaningful efforts to ascertain whether other developers were interested.

According to Marsh's notes, at the Recreationway Commission meeting, Behrmann suggested that further meetings would be necessary, and the Executive Director of the Canal Corporation John Platt (whom Marsh described as an "avid supporter") recommended that the Corporation "go out with an RFP to advertise for exclusivity." The matter was then tabled. Marsh wrote to Hutchens: "We will have to explore this strategy with Platt, Behrmann, Brooks." He told Hutchens that he would meet with the three to get "their thoughts as to how to proceed."

Shortly after the Recreationway Commission meeting, Marsh began making calls about the impending RFP. On March 2, 1999, Marsh's notes reflect that Brooks told him that the "RFP" would be "engineered for Alpine Keys." He also recorded that on March 5 someone – his

³⁰ The Canal Corporation, like all public authorities, is required by law to develop guidelines for bid procurement contracts of over \$5,000, which include "the selection of such contractors on a competitive basis." *See* N.Y. Pub. Auth. Law § 2879. The Canal Corporation need not, however, engage in competitive bidding when it leases or abandons canal land, although in the case of abandonment, it must place a notice for three weeks in a newspaper in the county where the property is located. *See* N.Y. Canal Law § 55 (lease); N.Y. Canal Law § 51 (abandonment). In contrast, the Commissioner of General Services – which is responsible for sales of most New York public land – is authorized to sell "at public auction or by sealed bids in such parcels as he deems for the best interest of the state." N.Y. Public Lands Law § 33. The statute specifically authorizes the Commissioner to sell land pursuant to a "requests for proposals." N.Y. Public Lands Law § 33(5). According to OGS personnel, OGS has developed a draft RFP procedure for this eventuality, but it has yet to make any sales under this provision.

notes do not disclose who – told him that the RFP “parameters....will give it to Richard.”

Marsh’s billing summary for March 5 reflects: “Call to Matt Behrmann re status of RFP.”

When asked about these notes, Marsh could not recall the conversations, but insisted, “I never once had a feeling that it was going to be steered.”

In addition, staff did not issue a formal RFP, but instead simply placed an advertisement in the state procurement magazine, the *State Contract Reporter*. Howard Taylor, a civil service employee who had been recently transferred to Canal Corporation headquarters from a regional office in order to provide advice and help coordinate real estate transactions, drafted the advertisement.

Marsh received an advance copy. On March 10, 1999, five days before it was published, Marsh received a faxed printer’s proof of the advertisement bearing Hutton’s name as the sender. Marsh saw the fax the next day and sent it immediately to Hutchens. Hutton did not recall sending the fax, but testified that Hutchens had been dealing with the Corporation “right along to do this project,” so “he knew that we were doing this.” Hutton declined to say whether he believed that such an advance disclosure was appropriate.

The advertisement was published on March 15, and appeared in the *State Contract Reporter* on page 62 under the topic heading “Miscellaneous Services - all services not listed elsewhere.” It read in relevant part:

The NYS Canal Corporation (“Corporation”) is soliciting proposals for the development of canalside residential communities along the four canals that comprise the NYS Canal System Such residential developments would be constructed on privately owned land and could be directly connected by water to one of the above canals. The connection could be made through a cut in the canal bank and the subsequent

construction of either a private marina or private mini-canal system which would provide an individual dock for each residential unit. . . .

As to exclusivity, the ad was understated: “In connection with such developments, the Canal Corporation *may consider* offering exclusive rights for up to five years, with extensions possible based on performance, in return for a to be determined non-refundable fee.” (emphasis added).

No residential developers interviewed in the course of this investigation have ever subscribed to the *Contract Reporter*, which does not even include a category for real estate. The Office of General Services (“OGS”), responsible for the sale of most surplus state lands, does not advertise in the *Contract Reporter*, but instead markets its properties widely in other media. OGS officials stated that they saw the *Contract Reporter* primarily as a place where the government advertised for service contracts, and expressed surprise that any state agency would consider advertising real estate in it, as opposed to a statewide real estate publication like *The New York Real Estate Journal*, or, for more significant projects, a national publication.

Many agencies, such as OGS, maintain lists of interested developers to whom they send notice of real estate opportunities, and to which any developer can add its name. The Canal Corporation had no such list. Nor did it systematically distribute the advertisement to other real estate developers with whom the Thruway Authority had dealt in the past or to the developers who had responded to Steinberg’s letter.³¹ Later, when the Hutchens deal became public as a result of legislative hearings, other developers learned of the opportunity and said they would

³¹ Ultimately, Taylor sent the advertisement to two developers besides Hutchens. One North Tonawanda developer who negotiated a lease with Taylor received a copy after making a general inquiry on other Canal projects. A Long Island developer, who had done no work upstate, requested a copy after seeing the advertisement pursuant to a federal government service on real estate opportunities, to which he subscribed.

have been interested in submitting a proposal had they known.³²

In addition to being posted in a forum inappropriate for a real estate deal, the advertisement called for an unusually short response time given the scope of the undertaking: twenty-two days. This is shorter than a typical response period, and unjustifiably brief for a development under discussion for years. RHA submitted its plan on March 31, 1999, and was the only developer to submit a proposal within the allotted time. When asked how he responded so quickly, Hutchens testified, “We had everything all done.” Unlike other potential respondents, Hutchens had been in negotiations with the Canal Corporation over exactly this sort of project for two and a half years.

On April 7, 1999 – the final day of the submission period – Canal Staff notified Hutchens that his was the only proposal. Hutchens proposed the following terms:

Number of sites	Primary	Unlimited.
	Secondary	None.
Lock-up period	Total possible lock-up period	20 years.
	Conditions	Development of two canal communities within each of four five-year option periods.

³² Two developers who had responded to Steinberg’s 1996 letter wrote to Assemblyman Brodsky, during his hearings on the Hutchens transaction, stating that they would have submitted responses to the *Contract Reporter* advertisement if they had seen it: George Broadwell and Charles Rock. Broadwell said he “certainly” would have responded to the advertisement; Rock said that he “most likely” would have done so. Both are regional developers with a focus on the Syracuse area. Rock had previously developed plans for a canal cut community, but was unable to carry it out due to opposition from the Army Corps of Engineers. At the time of the *Contract Reporter* advertisement, he has stated that he still had an interest in doing this sort of project at one location, which might serve as a model for other such communities. Taylor recalled receiving an inquiry from Rock. Rock has denied this, and there is no documentary evidence of such a response. Taylor’s own written summary, prepared in response to the Comptroller’s inquiries, does not mention a Rock inquiry.

Price	Option payment	None.
	Cut fee	Indicated willingness to make payment but did not specify an amount.
	Homeowner's fee	Indicated willingness to make payment but did not specify an amount.

Two and a half months later, on June 29, 1999, Canal Staff again submitted Hutchens's proposal to the Recreationway Commission. Notes of the Commission's minutes reflect that Brooks summarized the Commission's prior concern that the Canal Corporation "had not made this offering to the general public." According to the minutes, Brooks then said, "Since then, we published a Request for Proposal (RFP). The RFP outlined what we are offering and what types of options we had available. There was only one respondent and that was Mr. Hutchens."

After Brooks's report, the Recreationway Commission approved the project, over one dissent.

In accordance with the usual approval process, the plan was then presented to the Canal Real Property Management Committee, consisting of Behrmann, Thruway Authority General Counsel Sharon O'Connor and then Chief Financial Officer Lawrence DeCosmo. Brooks's memo to the Committee recommending approval represented that the fees had been reviewed by staff for justification and "have been based on available market data." This was untrue. Canal Staff did not look at market data of any kind. The Real Property Management Committee approved the plan on June 28, 1999. DeCosmo reported that he approved the plan in large part because he believed Hutchens had prior experience in constructing canal cut communities, which was not true.

A few days later, an important milestone passed for Hutchens's performance on the

Frankfort Marina deal. By July 1, 1999, the lease had bound Hutchens to have at least five boats in operation on the system for a five-year period. Staff had promised the Board that Hutchens would have five touring boats in service even earlier. He did not. Rather, his efforts to finance the purchase of the boats had completely fallen through. Hutchens had attempted to persuade the village of Frankfort to obtain a HUD loan to help underwrite the boats. He wanted the deal structured so that Frankfort would apply for the loan, but he would receive the money.

Hutchens, however, proposed as collateral only a secondary security interest in the boats to be built – which Hutchens intended to move out of the jurisdiction each winter – and a letter from his bank indicating that he had a line of credit of an unspecified amount.³³ Both the village and HUD determined that this was insufficient.³⁴ When Frankfort asked Hutchens to provide documentation about his financial status, he told them it was “none of their business.” He did not obtain HUD financing, and he did not attempt to make up the difference from another source. He simply went into default.³⁵

Agencies commonly rely heavily on a contractor’s prior performance in determining whether to enter into new deals. But here, the Canal Staff failed to inform the Board that they had asked Hutchens as an accommodation to assume responsibility for the Frankfort deal or that Hutchens had failed to perform on it. They nonetheless recommended Alpine Keys to the Board.

³³ Counsel for Frankfort called the absence of any dollar amount in the bank’s letter “very unusual.”

³⁴ Frankfort’s counsel testified that Canal Corporation staffers, including Brooks, called at one point to say that the Village must accept these terms immediately, or Hutchens would walk away.

³⁵ The contract that Hutchens signed did not make his operation of boats contingent on HUD (or any other) financing. Rather, he was not permitted to remove boats from operation or forbear from building boats until after five years of operation.

In a presentation to the Board on, July 22, 1999, the staff proposed a new set of terms:³⁶

Number of sites	Primary	40 sites.
	Secondary	None.
Lock-up period	Total possible lock-up period	15 years.
	Conditions	Two residential communities under development every five years.
Price	Option payment	\$30,000 for each of three five-year option periods.
	Cut fee	\$15,000 per cut.
	Homeowner's fee	\$300 per year.

Appearing for the first time in this proposal was a \$30,000 option payment every five years, in addition to the cut fees on the sites actually developed. Behrmann's justification memo to the Board incorrectly reported that they derived the \$30,000 figure through a "commonly used" formula for valuing options, which was by calculating 5 % of the "property's fair market value."³⁷ This was not, in fact, the formula that the Canal Staff used. They did not know the property's fair market value, and had made no significant efforts to determine it. Instead, the

³⁶ Behrmann gave a copy of his July 12, 1999, memo to the Canal Board, in which these terms were proposed, to Kerry Marsh. On this copy, which was produced from Marsh's files, Marsh wrote the word "embargoed." Marsh testified that he wrote the word "embargoed" on the document because Behrmann "did not want me sending this all over the place." Marsh further testified that he "did not understand it to be confidential" and that Behrmann "just did not want me to pass it any place, so I just put embargoed on it".

³⁷ The memo to the Board indicated that this was derived from the staff's "review of other option fee schedules." Other documents, however, indicate that Carey had told the staff that a typical option fee was between 5 and 10 % of the property value.

\$30,000 figure represented 5 % of the *cut fees*, a number staff had set themselves.

At the meeting, the Board tabled the proposal because its two new members, John Riedman and Lou Tomson, wanted more time to study the real estate matters before them. Riedman also suggested that the Board seek an outside consultant to look at the Hutchens proposal.

G. July 1999 to November 1999: Hutchens and the Kings

After the Board's decision to table the proposal, Hutchens sought additional outside support, from then New York State Budget Director Robert King³⁸ and his wife Karen King.³⁹ Hutchens and the Kings knew each other from the Hall of Fame weekend, which they all had attended in 1998 and 1999. Kerry Marsh and Robert King have been friends for, by Marsh's estimation, "20-some odd years." They and their wives golf and dine together, and the Marshes often attended the Kings' annual Super Bowl party.

Marsh regarded Robert King as extremely important: "If you are the Director of the Budget, you have official oversight over every dollar in this state. And if . . . people are wasting dollars and not doing it, the Budget Director gets very involved." He testified that he urged Hutchens to talk to the Kings, and volunteered his view that, "If you know Bob King's relationship with George Pataki, they were basically almost roommates," and "Bob King was . . .

³⁸ Robert King is currently the Chancellor of the State University of New York ("SUNY"). Before becoming the Governor's Budget Director in the Fall of 1998, King had served as Monroe County Executive, State Assemblyman, and a prosecutor.

³⁹ Karen King had been Executive Assistant to the Deputy Commissioner for Worker Protection at the New York Department of Labor before she joined the New York State Thruway Authority in 1997 in the Government Relations office. She worked there until July 1998. Thereafter, she became Director of Special Projects at the Institute of Entrepreneurship at the State University of New York. Currently, she is working on the staff of Mary Lou Rath, a State Senator from the Buffalo area.

a kitchen cabinet advisor to the Governor.”

Marsh’s billing records document repeated contact with the Kings in the wake of the July 22 tabling of Hutchens’s proposal:

July 27, 1999:

Discussion with Karen and Bob King re NYS Canal system residential cluster Village Development.

1.00 hour

July 29, 1999

Article re Canals in NY to Richard Hutchens. Phone call to Bob King re Alpine Keys; call re John Riedman to set up meeting.

0.75 hour

July 30, 1999

Phone Karen King re Alpine Keys. Fax to Richard Hutchens re Alpine Keys

0.25 hour

A July 30 fax from Marsh to Hutchens read: “Talked at length with Karen King. Have schedule and strategy. Will discuss next week. Bob is still on budget which goes up and down by the hour. Please call.”⁴⁰ Marsh testified that he and Karen King discussed the delay in the decision making process at the Canal Corporation, and Marsh sought King’s advice and assistance in getting the plan approved. Karen King could not recall the conversation.

When asked what he believed Robert King could do for him, Marsh testified, “He could talk to any number of people. He was the Director of the Budget.” Said Marsh, “I thought this

⁴⁰ Hutchens testified that around this time, at Karen King’s request, he prepared a memo describing his failed efforts to gain Board approval of his project. This memo, which Hutchens testified was delivered to Karen King, is dated July 27, 1999, and closes with the following questions:

“Two questions linger in my mind: Is the Thruway Authority, by requesting an outside study be done, demonstrating a lack of faith in its staff’s abilities? In addition, is it necessary to start over each time there is a change in board members.”

was a perfect example of where New York was sitting on itself and not taking advantage of something that could do something good for the state. He was a natural to talk to on that.”

In particular, Marsh “was suggesting to him that maybe he could speak to Riedman” about price and exclusivity. Marsh also wanted King to vouch for his credibility with Riedman: “As I recall I was asking him to call up and say Kerry Marsh has something he would like to talk to you about. He’s a good guy. Listen to him. It was more of an intro as I recall.”

In addition to his authority as Budget Director, Robert King had personal relationships with many of those involved in the process. He described Riedman as a “friend” who had been a campaign supporter of his when King ran for public office. King knew Tomson “very well.” And King said that Hutton used to work with King’s wife and had been to their home for parties, and that he and his wife had sailed on a trip with Hutton and his wife in the Caribbean.

A few days after his conversation with Karen King, Marsh spoke directly with Robert King and sent a formal letter to him detailing the history of the proposal, and urging that the Canal Corporation forgo hiring an outside consultant to evaluate the deal: “another study will only delay, possibly endangering the only viable development project submitted for revitalization of the canal system.”⁴¹ Marsh sent a memorandum to Hutchens that day memorializing the conversation: “I spoke with Bob King. In the next 2-3 weeks he will speak with John Riedman and also will mention his conversation with Lou Tomson following discussions with me (so that everyone is on the same page).” He added, “In the meantime, I will be speaking with Nancy

⁴¹ King’s files contained a signed letter dated October 8, 1999, to Marsh responding to this letter. Drafted by a budget staff member who described it as “upbeat but noncommittal,” it read, in pertinent part, “I understand from executive staff at the Canal Corporation that the project is under active consideration, and they are hopeful that several proposed modifications to the project plan will be acceptable to Mr. Hutchens.”

Carey.”

Marsh’s efforts with the Kings continued later that month. On August 24, 1999, Marsh wrote to Hutchens that he and his wife had “a ‘hold’ for golf this Sunday with the Kings, and that “This would give me further opportunity to brief Bob and Karen.” Karen King recalled golfing that weekend with the Marsh’s. Robert King, although he did not recall this particular discussion, acknowledged that he and Marsh would, from time to time, discuss business on the golf course. Marsh’s billing summary from that Sunday, August 28, 1999, reads, in part, “Extensive discussion and strategic planning.” It does not say with whom.

Before the 24th, Marsh had learned from Carey that Hutchens’s proposal, indeed, all real estate proposals, had been “put on hold” because Tomson and Riedman wanted a better understanding of the workings of the Authority before they turned to individual projects. Marsh wrote Hutchens, “Nancy advised that because of the ‘learning curve’ issues, we must expect to proceed unfortunately more slowly than would ordinarily be the case.” Marsh concluded, “It would be helpful if in the next week or two we conference with Bob Brooks.”

Marsh’s billing summary shows continued contact with Bob King. It reads:

September 13, 1999:

Phone calls to Bob Brooks and Bob King, continuing discussions and reviews of Alpine Keys proposal; discussion re John Platt’s concern to further proposal; re blocking out certain areas; negotiation of “without prejudice” letter; re exclusivity, re fee structure.

1.50 hour

A few days later, September 16, 1999, Marsh reported progress to Hutchens: “As advised, Bob King has spoken with John Riedman.”

Marsh promptly followed up in an October 6 letter to Riedman asking that Riedman meet with Marsh and Hutchens; Marsh's billing records show that he sent a copy to Robert King. Marsh's billing summary reflects that on October 18, Marsh and Riedman spoke.⁴²

King said that he did not recall whether he ever placed a call to Riedman on Marsh's behalf, but said that he "could have." Riedman did not recall whether he received one. King testified that even if he had called Riedman, the effect of a call would be minimal, because "John is not a guy that is easily pushed around."

As to Tomson, King testified that he was "pretty confident" that he never met with Tomson regarding Hutchens. Similarly, Tomson could not recall communicating with King.⁴³

H. November 1999 to January 2000: The KPMG Report

Whatever the nature of Marsh or King's communications with Riedman, they appear to have had limited effect. At a Board meeting on October 28, 1999, Riedman again requested that a consultant evaluate the Hutchens project. The following day, Marsh spoke with Carey about the meeting. His notes reflect that she said, "will have problem w/ Riedman."

Pursuant to Riedman's request, the Canal Corporation did retain an outside consultant, KPMG, an international accounting and consulting firm. The Canal Corporation accepted a proposal from KPMG, which was also its outside auditor, to perform three discrete tasks with

⁴² According to Marsh, he "had a couple of discussions and tried to talk to John Riedman and John Riedman is a very taciturn type of guy. I never did have the meeting. I talked to him a couple of times and I think you saw some stuff there. 'I don't need anything and that's fine'."

⁴³ Marsh made another lobbying approach, one to Senator Joseph Bruno, Majority Leader of the N.Y. State Senate. On October 6, 1999, Marsh faxed a summary of the Hutchens plan to Richard Burdick, who was a senior staff member for Senator Bruno. Marsh never had any meeting with Senator Bruno or his staff with regard to the Hutchens matter.

regard to the Hutchens transaction. First, it was to gather information from Hutchens to evaluate the proposal, such as operating statements, information about other similar developments, the assumptions used in his proposals, credit information, and the like. Second, it was to present alternatives to the proposal and describe the costs and benefits of each. Finally, KPMG was to formulate an independent analysis of whether the deal made economic sense. If appropriate, KPMG would assist the staff in presenting the proposal to the Canal Board.

Around December 8, 1999, the KPMG engagement got underway. Because the Canal Board wanted KPMG's opinion by the middle of January, KPMG was, in its view, forced to produce "a very short document, in a very short time" and would do so "based on the information provided to it." One member of the KPMG team characterized the engagement as a "high level review under an accelerated time frame."

KPMG did not acquire the extensive financial information called for by its engagement. According to the same KPMG team member, the "state didn't have any of this information and the developer would not share it." The only items that KPMG received from Canal Staff were one of Hutchens business proposals and an internal memorandum from Canal Staff.

One of the KPMG team members testified that the Canal Corporation's staff analysis of the Hutchens transaction was "odd" relative to other government clients at local development corporations where "rigorous analysis is performed." In contrast, the staff's analysis seemed "very preliminary." The member testified that the Canal Corporation staff "lacked a market perspective" and "lacked real estate expertise."

Moreover, a KPMG team member testified that Canal Staff (the KPMG staffer could not

remember who) had told KPMG that Hutchens was the “only game in town” and “no one else was interested.” The week before the KPMG engagement began, however, Howard Taylor wrote a memorandum about another developer who had also been working with the Canal Corporation for years to develop a canal cut community on the Oswego River. Taylor understood that the mere existence of another plan could jeopardize the approval of the Hutchens proposal, writing: “I also question the possible impact on the Hutchens proposal currently in front of the Board.”

Nor did Canal Staff tell KPMG about Hutchens’s failure on the Frankfort marina deal. Hutchens still had no boats in the water, or even on order. Brooks was, at this point, predicting internally that no boats would be in service before June 30, 2000. Indeed, he was urging, by memo of January 13, that Hutchens’s marina rent be lowered, because Hutchens still had not produced any boats.⁴⁴

KPMG also interviewed Hutchens. Among other things, Hutchens said that he had done a similar project in Grand Island, New York. KPMG did not verify this claim. In fact, Hutchens had never done such a project.

Hutchens accurately told a KPMG team member that he had performed no detailed market studies, which the KPMG team member viewed as unusual, except for speculators. As to Hutchens’s basic marketing theory, the KPMG team member disagreed with his prediction that young urban professionals would be moving out of New York City for the countryside around

⁴⁴ According to Hutchens, “I just called Bob up, and said what the hell you doin’ sending me another bill, you know the deal’s not goin’, and you know, and cause I told him, and so they cancelled the lease, and they quit sending the bill.” The documentary record indicates that by letter dated June 5, 2001, Hutchens requested that the lease be cancelled. By letter dated January 15, 2003, Brooks granted the request, retroactively deeming the lease cancelled as of July 1, 2001.

the Canal.⁴⁵ Hutchens declined to provide KPMG with any financial data.

As one KPMG team member conceded, given the scant information provided by both Hutchens and the Canal Corporation, one option available to KPMG would have been to tell the Canal Corporation that the information was insufficient to conduct a meaningful review. Nonetheless, KPMG decided to go forward, relying on the information provided to it, a brief review of newspaper articles and other publicly available sources that mentioned Hutchens, and limited research on the price differential between upstate residences located on land and on waterways.

KPMG provided its first draft report to the Canal Corporation on January 6, 2000, recommending a number of changes in the deal. KPMG proposed cutting the number of sites significantly, reducing the lock-up period, requiring that Hutchens actually complete a project before being permitted to renew, and raising the homeowner’s fee:

		Behrmann 7/99 memo to Board	KPMG First Draft
Number of sites	Primary	40 sites.	6 sites.
	Secondary	None.	None.
	Additional	None.	Unlimited.
Lock-up period	Total possible lock-up period	15 years.	6 years.
	Conditions	Two residential communities “under development” every five years.	Development of at least one site within first 3-year option period.

⁴⁵ KPMG notes read: “I disagree, statistically -- urban areas are growing.”

Price	Option payment	\$30,000 for each of three 5-year option periods.	\$30,000 for primary sites for each of two 3-year option periods. \$5,000 for each additional site within each of two 3-year option periods.
	Cut fee	\$15,000 per cut.	\$15,000 per cut.
	Homeowner's fee	\$300 per year.	\$300 base, escalating \$25 per year until reaching \$600 per year.

The next day, Taylor called KPMG to urge it to change its recommendations. An email from Taylor to Behrmann and Brooks reported that Taylor warned KPMG that its recommendations would “probably kill the Golden Goose.” Taylor also wrote that he “kept explaining how we advertised our RFP and only received one bid and actually only one phone call of interest in the project . . . They keep envisioning several developers lining up to compete with Hutchens and willing to pay us more money! Where were these developers when we were soliciting bids?” According to Taylor’s email, “after what seemed like a protracted stream of arguments,” KPMG agreed to change its recommendations. It did so both as to the number of sites (raising it from six to between 10 to 20 and up, with a right of first refusal for the rest), and as to the lock-up period (extending it from three to five years with a right to renew for three additional five-year periods). In sum, it appears that, within the space of a single one-hour telephone conversation, KPMG substantially reversed its position concerning the breadth of Hutchens’s proposed exclusive. No KPMG witness could recall this conversation.

Although staff members were withholding information about other developers from KPMG, they were telling Marsh. For example, Marsh's January 11 notes of a conversation with Behrmann record a "problem." Marsh's notes report: "There are two other guys who want to do developments [therefore] there is a market." In short, Marsh's contemporaneous notes show both that the Canal Corporation staff knew of other developers, and knew that the existence of a "market" could threaten the Hutchens deal.⁴⁶ They warned Marsh, but told neither KPMG nor their own Board.

Staff was also briefing Hutchens and Marsh on the contents of the KPMG drafts. For example, a Marsh memo to Hutchens of January 12, 2000, reports that Behrmann described the latest draft report to Marsh, and discussed with Marsh how to alter the KPMG draft further in Hutchens's favor. Canal Staff again prevailed on KPMG to change its report, and on January 13, Brooks faxed to Hutchens a subsequent KPMG draft, which was to become the final version. His cover sheet stated that the report was "heading in the right direction."

On January 14, 2000, KPMG submitted its final memorandum, incorporating the changes sought by staff. The chart below shows how the changes from KPMG's first draft to the second moved it closer towards Behrmann's July memo to the Board:

⁴⁶ The investigation was not able to definitively determine the identity of the two developers to whom Marsh referred. On November 30, 1999 – a month and a half before Marsh wrote this note – Taylor copied Brooks on a memorandum regarding a project entitled "Oswego River Meadows" by developer Dan Lyman. The memo noted that "there is canal land involved including a proposed canal bank cut," and expressed concern about its potential impact on the Hutchens transaction. Taylor sent subsequent communications on this project to Behrmann as well. Since these are the only contemporaneous communications concerning a canal cut development, it seems likely that Lyman was one of the two developers referred to in Marsh's notes. It is possible that the other developer was Charles Rock. See Page 40 of this report, footnote 32.

		Behrmann 7/99 memo to Board	KPMG First Draft (1/6/00)	KPMG Final draft (1/13/00)
Number of sites	Primary	40 sites.	6 sites.	10 sites.
	Secondary	None.	None.	30 sites.
	Additional	None.	Unlimited.	Unlimited.
Lock-up period	Total possible lock-up period	15 years.	6 years.	20 years.
	Conditions	Two residential communities “under development” every five years.	Development of at least one site within first three year option period.	Development of at least two sites each within a five year option period.
Price	Option payment	\$30,000 for each of the three five year option periods.	\$30,000 for primary sites for each of the two three year option periods. \$5,000 for each additional site within each of the two three year option periods.	\$30,000 for all primary sites for each of the four five year option periods. \$5000 to convert a secondary site to a primary site. \$10,000 for each additional site.
	Cut fee.	\$15,000 per cut.	\$15,000 per cut.	\$15,000 per cut.
	Homeowner’s fee.	\$300 per year.	\$300 base, escalating \$25 per year until reaching \$600 per year.	\$300 base, escalating \$25 per year until reaching \$600 per year.

In its final memo, KPMG carefully qualified its conclusions. For example, rather than saying that Hutchens was taking on a lot of investment risk, it wrote: “the Developer *perceives* that he is taking on a great deal of risk” (emphasis added). Rather than opining that the transaction’s benefits outweighed its costs, it wrote “it is difficult to estimate the benefits of this

type of non site-specific development.” And rather than endorsing the \$30,000 option price, it wrote that the option price “*may well be* indicative of the maximum a developer would be willing to pay given the speculative nature of the project” (emphasis added).

The primary drafter of the KPMG memorandum said that it had been “hard to write the memo.” This KPMG team member said: “I think we were evasive. Not evasive, we didn’t use strong language either way.” With the benefit of hindsight, this KPMG team member testified that the caveats “all assumptions are provided by the client” and that “this report should not be used by third parties” should have been added to the memorandum.

I. January 2000: Approval by the Canal Corporation Board and Actions by Canal Corporation Staff

Hutchens’s proposal was again presented to the Board on January 27, 2000. The Board’s briefing memorandum was drafted by Taylor, with input from many other Canal Staff members, and went to the Board under Behrmann’s name.⁴⁷

Brooks made the oral presentation on behalf of the proposal, and Behrmann, Taylor and Thruway Authority Counsel Sharon O’Conor were also present. Behrmann had assured Marsh beforehand, according to Marsh’s notes, that he would be there to “say OK to the proposal.”

All three Board members were present. Based on Marsh’s billing summary, between the tabling of the proposal on July 22, 1999, and the beginning of KPMG engagement around December 8, 1999, he contacted Tomson⁴⁸ once, Riedman twice, Behrmann, Brooks, Platt and

⁴⁷ A Canal Corporation “agenda item review” lists Taylor as the person who prepared the Board’s agenda, and is approved by Behrmann’s signature.

⁴⁸ With respect to Marsh, Tomson testified that “....I have to say, candidly, that if Mr. Marsh were representing Mr. Hutchens it would not help Mr. Hutchens that much in my view....Because I don’t have a great regard for Mr. Marsh. I should clarify to say I don’t have a great dislike of Mr. Marsh. I know very little about him

Carey three times, and the Kings seven times. Between the retention of KPMG and final approval by the Board, Marsh contacted Taylor once, Platt, Tomson and Carey twice, Behrmann six times, and Brooks seven times.

Marsh’s discussions with Carey elicited detailed information about the leanings of her colleagues, particularly Riedman.⁴⁹ Although Marsh had the most contact with the Kings, King could not recall whether the communications that Marsh had with him resulted in his calling Riedman or Tomson, and neither Riedman nor Tomson could recall whether they spoke with King about the matter.

In comparison to the proposal presented to the Board two years earlier, the new proposal increased Hutchens’s rights to exclude other developers, and also increased what he would have to pay:

		Presented to Board February 1998	Presented to Board January 2000
Number of sites	Primary	10 sites.	10 sites.

and I wouldn’t think that his representing anybody would make a difference to me.”

⁴⁹ The fact of Carey’s having been lobbied is no longer a matter of dispute, although she initially firmly denied it. In October 2003, the Comptroller rescinded his approval of the contract. In an October 17, 2003, letter, he wrote: “attempts were apparently made to influence at least one of the three board members to support the Hutchens proposal before the formal solicitation,” specifically referring to evidence that he believed tended to show contacts between Carey and Marsh.

In a letter signed by Carey and the other Board members, the Board replied: “This is completely false. Board Member Carey has never met with Hutchens on this matter, and is willing to provide an affidavit to your office as to that effect. It is unfortunate that you did not bother speaking with Board Member Carey before attempting to question her integrity, and had you bothered to do so, your office would have learned that your allegation is groundless . . . There is no truth to the allegation you have now made.”

Carey has subsequently stated that she met with Marsh. Carey said she was at home recovering from surgery when she reviewed the Board’s letter to the Comptroller, and, at the time, did not recall any meetings with Marsh. Although Carey stated that the letter is literally true (she did not meet with Hutchens personally), she conceded that a reader might infer that she was denying all attempts to influence her, including a lobbyist.

	Secondary	33 sites.	30 sites.
	Additional	None.	Unlimited.
Lock-up period	Total Possible lock-up period	10 years for primary sites. 20 years for secondary sites.	5 years with an option to renew for three additional 5-year terms, for a total of 20 years.
	Conditions	If a certain number of sites are not developed within a specific number of years, all remaining option(s) and right of first refusal may expire.	Development of at least two sites each within a 5-year option period.
Price	Option payment	\$750 for each primary site. \$1,125 for each secondary site.	\$30,000 for all primary sites for each of the four 5-year option periods. \$5,000 to convert a secondary site to a primary site. \$10,000 for each additional site.
	Cut fee	\$15,000, plus 2 % escalation fee per year, less total option fees paid for any primary sites.	\$15,000 per cut.
	Homeowner's fee	\$250 per year.	\$300 base, escalating \$25 per year until reaching \$600 per year.

The staff memo to the Board, which was dated January 18, 2000, began by emphasizing the Contract Reporter advertisement: “On March 15, 1999, the Canal Corporation placed an advertisement soliciting interest in the development of canalside residential communities along the Canal System in the New York State Contract Reporter. The only proposal received in response to the ad was from Richard A. Hutchens & Associates.” Staff also annexed the KPMG

report, and represented that KPMG “endorsed” the venture. Finally, the memo stated that RHA “indicated that it had been engaged in residential and commercial land development in New York, Oklahoma, Texas, Florida and the Caribbean for over thirty years.”⁵⁰

The staff memo to the Board also stated that the sites selected by Hutchens would “entail no more than 9 % of the Canal system shoreline.” What this memo did not tell the Board was that that 9 % figure represented, in the view of Canal Staff, and based upon their own analysis, the entire developable portion of the shoreline. Hutchens, whose own site selections represented approximately 8 % of the shoreline, would now have precisely what he always wanted: complete control over the development of canalside communities joined to the main Canal by bank cuts.

Canal Staff did not tell the Board, either orally or in writing: (1) that other developers had expressed interest in creating canal cut communities; (2) that staff had withheld pertinent information from KPMG as it was evaluating the deal; (3) that staff had given inside information to Hutchens’s lobbyist (whom a staff member had recommended that Hutchens hire); or (4) that Hutchens was failing to perform on his Frankfort lease.

The Board unanimously approved the project, adding one stipulation. Taylor’s notes of the decision read “no transferability,” memorializing the Board’s direction that Hutchens not be permitted to assign his rights.

The Board members have indicated that if they had received full disclosure from Hutchens and the Canal Staff, it would have affected their thinking. Subsequently, Carey has

⁵⁰ This was a retreat from earlier staff submissions, in which the staff asserted RHA’s experience as a fact, rather than a report of Hutchens’s own characterization of his business. The change was made by the Canal Corporation’s outside counsel in July 1999.

stated that she would have voted against the proposal had she known that Hutchens had done little due diligence on canalside projects, was not an active real estate developer, or that he intended to sell his right to make canal cuts to others. Tomson, for his part, said that he relied upon Carey's opinion and upon KPMG "to say that the process was adequate and the result was OK," and further testified that he would like to have known the 9 % of the shoreline given to Hutchens represented a large portion of the developable land. Riedman said that, had he known that Hutchens intended to flip his interests, he would "probably not" have approved the deal.

In summing up the process that led to Board approval of the deal, Carey said, "I wish the staff had done their due diligence better, I wish they had presented it in a better format, I wish they had done their homework. But they didn't."

3. What Hutchens Got

A. The Hutchens Contract Is Negotiated And Approved

Board members testified that, in approving the Hutchens proposal, they intended to enter into a relationship with the developer, not a broker. Indeed, the "no transferability" direction recorded by Taylor could scarcely be more unequivocal proof of their intention.

It was, however, Hutchens's clear, undisclosed plan to broker the deal, and, from the moment the Board approved the transaction, he worked to ensure that he would be able to sell his right to develop to others.

First, Hutchens requested and received a letter from Canal Staff that he immediately used to solicit other developers. Second, throughout the contract negotiations, Hutchens pushed to

expand his exclusivity rights and to obtain a right to assign. Third, immediately after the contract went into effect, Hutchens sold (without Canal Corporation approval) the right to make a canal cut to another developer.

Two days before the Board was to meet on the Hutchens proposal, Marsh – apparently confident of a favorable outcome – asked Behrmann to have the Canal Corporation issue a letter stating that Hutchens had been selected as the “preferred developer” for the Erie Canal. Marsh even provided Behrmann with a draft.

Without telling their Legal Department, Canal Staff edited Marsh’s draft and gave Hutchens a final copy, signed by Brooks, on February 1, 2000. This was after the Board had approved the proposal, but well before any contract had been signed. The letter purported to notify Hutchens of the Board’s decision and stated that Hutchens had been named the “selected developer” who had been “granted exclusive rights to develop cluster villages, with canal cut access to proposed private waterways, for an option period of five years.” The letter omitted mention of the “no transferability” condition that had been added by the Board. Hutchens immediately began using Brooks’s letter to solicit developers, sending it to firms nationwide seeking “co-developers” for canalside communities.

As Hutchens was seeking “co-developers,” he was also working to ensure – notwithstanding the Board’s “no transferability” direction – that he could assign his rights. For the next 22 months, Hutchens’s lawyer attempted to renegotiate the deal approved by the Board, including deleting the initial payments in their entirety and trying to extend Hutchens’s

exclusive.⁵¹ The Corporation's counsel rejected most of these efforts.

Unbeknownst to Canal Corporation lawyers, Hutchens had received secret help from Brooks and Taylor in drafting at least one of his counter-proposals. Documents show that Hutchens sent Brooks drafts of the letters his attorney was planning to send to Canal Corporation lawyers some of which bear handwritten notations apparently memorializing subsequent conversations between Hutchens and Brooks. Canal Corporation lawyers testified that they were not aware that Brooks or Taylor had helped draft Hutchens's counterproposal, and that any such secret involvement was inappropriate.

Hutchens had more success in undermining the Board's "no transferability" direction. Initially, in concert with the Board's direction, the Canal Corporation's draft of the contract included a section in which: (1) Hutchens represented that he was not entering into the contract for the purpose of speculation; and (2) Hutchens was prohibited from assigning his rights under the contract without prior Canal Corporation consent. Hutchens aggressively negotiated the second provision, and eventually the Canal Corporation agreed to modify it to read that Hutchens was not permitted to assign his rights without the Canal Corporation's consent, but that such

⁵¹ Hutchens's first formal request for modification was an extensive revision of the April 14 contract draft, sent to the Canal Corporation in August 2000, which deleted the payment of a \$30,000 fee for the initial five year option and each renewal, removed the primary/secondary site structure, and attempted to give Hutchens an exclusive option on all similar residential developments on the entire Canal system for the full five years. Canal legal staff rejected these as contrary to the terms approved by the Board.

In July 2001, Hutchens once again proposed significant modifications to the agreement going beyond the terms approved by the Board. These included: extending the exclusive period over the entire Canal shoreline for identifying primary and secondary sites from two to five years; weakening the requirements for renewal of the option so that Hutchens could renew if he had submitted applications for approvals on two initial sites, whether or not he had received such approvals; strict confidentiality as to the locations of primary and secondary sites; and a requirement that the Canal Corporation fully share with Hutchens all information regarding potential development of canalside residential communities by third parties.

consent “shall not be unreasonably withheld.”⁵²

Moreover, Hutchens obtained in the contract a provision never presented to the Board. Every five years, Hutchens was permitted to replace his previously chosen sites with a new list of “substitute sites.” In short, he could reshuffle his deck – and thereby prevent development in areas he had not previously designated – at no additional cost.

Hutchens signed the contract (“the Option Contract”) on December 14, 2001, and representatives of the Thruway Authority signed on December 20. Although the Canal Corporation staff had been dealing with Richard Hutchens's primary corporate entity – Richard Hutchens & Associates (“RHA”) – throughout the Board approval process and the contract negotiations, and even though the Board authorized the Canal Corporation to enter into a contract with RHA, the final contract actually was between the Canal Corporation and a different entity -- “Richard A. Hutchens CC, LLC.” The Option Contract next went to the Office of the Attorney General and to the Office of the State Comptroller (“Comptroller”) for approvals. The Attorney General approved it for form on January 10, 2002. The Comptroller approved the Option Contract on May 2, 2002.⁵³

⁵² Since Hutchens has now filed a notice of intent to litigate the termination of the contract, a court may determine the interplay between these two provisions. At issue will be both whether or not Hutchens’s actions violated the contract’s non-assignment clause, and whether or not Hutchens’s misrepresentations and omission regarding his prior experience constituted promissory fraud or fraud in the inducement.

⁵³ The Comptroller, whose role was to inquire into the substance of the contract, asked questions about the “RFP” and why there had been only a single bidder. The Canal Corporation responded by stating that there had been “no Request for Proposal,” but describing the 1996 Steinberg letter and 1999 *Contract Reporter* advertisement. It also cited the “endorsement” by KPMG. When the Comptroller asked why none of the 33 entities that responded to Steinberg’s 1996 letter had answered the *Contract Reporter* advertisement, the Canal Corporation answered that only six responders were involved in real estate development, and that “[e]ach of these . . . had visions, priorities or concepts that didn’t work with any of the available property except for Mr. Hutchens.”

B. Hutchens Flips His Interest To Bragman

With the Option Contract signed and approved, Hutchens entered into an assignment agreement with former Assembly Majority Leader and housing developer Michael Bragman, whom he had met at a Hall of Fame weekend event.⁵⁴ In his agreement with Bragman (the “Heather Agreement”), Hutchens purported to assign to Bragman’s company, Heather Associates, Inc. (“Heather”), the development rights in six counties.

Bragman was adamant that Heather and RHA were not partners in this venture: “We work alone. This is our company. I am not a partner. I have not been. I will not be.” Bragman did not want Hutchens doing any actual development, because he did not think that Hutchens had the necessary experience. Thus, under the Heather Agreement, Heather was to do all the actual development and financing, while Hutchens was simply to pay the Canal Corporation the fees required under the Option Contract. For this, Hutchens would receive a “broker’s commission” of 6 % of each lot Bragman sold.

After some analysis, Bragman concluded that the only promising development site was in Clay, New York, and began focusing his efforts there. Canal Staff was involved in discussions, and even assisted, but never told their own Legal Department that Hutchens had some kind of relationship with Bragman. Hutchens did not write the Corporation seeking approval for assignment under the Option Contract, but did correspond with staff about Heather and the project. Staff did not give this correspondence to the Legal Department.

⁵⁴ According to Hutchens, this was the first time he met Bragman. Hutton, however – who was present at the Hall of Fame weekend – asserted that the two had spoken frequently in prior years. Bragman has testified that he first met Hutchens after a chance conversation at Rich’s house between his son and Hutchens. Rich states, however, that he arranged a breakfast between the two and himself, pursuant to Hutchens’s request for aid in finding potential development partners.

The Legal Department finally learned about the RHA/Heather relationship when the Syracuse Post-Standard wrote an article on February 2, 2003, about Heather's difficulty in obtaining permits from the Army Corps of Engineers. After the article appeared, Canal Staff gave the Legal Department the earlier correspondence. At Legal's direction, the Canal Corporation sent a letter to Hutchens stating that he was not permitted to assign without Canal Corporation approval.

Hutchens's first response was to dissemble. A letter of February 5, 2003, from Hutchens's manager contended that Hutchens had not assigned his rights at all, but merely sought to "utilize [the] expertise" of Bragman's companies. It also stated that "it is our intent to replicate our program so as to use local individuals in each area to expedite our program."

On February 7, the Canal Corporation sent a letter reiterating that its approval was required before assignment, asking RHA to explain its reference to the use of "local individuals," and demanding a copy of the Heather Agreement. According to Bragman, Hutchens did not inform him about the correspondence, even though it placed the entire deal into jeopardy.

Despite the unmet demand that Hutchens provide information, Canal Staff continued to help Hutchens and Bragman with the Clay project, including meeting with the Army Corps of Engineers to help get permits. When the Army Corps permits were not forthcoming because of wetlands issues, Bragman and Hutchens wrote to the Governor for assistance.⁵⁵ That letter – which failed to disclose the ongoing assignability dispute – was referred to the Thruway Authority for response, leading the Authority again to write Hutchens and, once again, request

⁵⁵ Hutton prepared the initial draft of the response, which made no mention of the assignment at all, and merely asserted the Canal Corporation's endorsement of the project.

the Heather Agreement.

With the questions of Hutchens's assignment and regulatory approvals unresolved, Hutchens once more sought help from a lobbyist. Again, the recommendation came from Hutton, who suggested that Hutchens hire former Department of Transportation official Frederick Hiffa. Hiffa was a social friend of Hutton and newly appointed Thruway Executive Director Michael Fleischer, with whom Hiffa had worked at the Department of Transportation. Hiffa and RHA signed a letter memorializing Hiffa's representation on May 7, 2003.

On July 21, 2003, Hutchens finally submitted a copy of the Heather Agreement to the Canal Corporation, but he redacted the clause describing his compensation. The Canal Corporation asked its outside counsel to draft a response. Outside counsel did, citing numerous provisions of the Option Contract that Hutchens had "clearly fail[ed]" to satisfy. In an accompanying memo, outside counsel also pointed out to the Legal Department one of Hutchens's possible legal defenses, namely that staff's knowledge could "give rise to a credible waiver argument."

This internal, legally privileged document was improperly given to Hutchens. It is not certain who sent it to him.

On September 22, 2003, the Canal Corporation wrote RHA to notify it that, as a result of the failure to provide further information about the Heather Agreement, RHA was in violation of the contract. Two days later, Bragman and Hutchens formally requested approval for the Heather Agreement.⁵⁶ In reply, the Canal Corporation wrote Hutchens to request: (1)

⁵⁶ The letter also noted that Canal Corporation staff had "attended project meetings with representatives of Heather," and had been "supportive" of the project before it became public.

information about Heather and its relationship with RHA; (2) a description of the “respective roles” that the two companies would play in the project; and (3) an unredacted copy of the Heather Agreement.

Hutchens submitted a response signed by Bragman, which summarized the apportionment of responsibility as follows: “[Heather] is responsible for the development of the project. Richard A. Hutchens is to secure the canal cut permit from the Canal Corporation.” With this response, the Canal Corporation received – for the first time – an unedited copy of the Heather Agreement in October, revealing Hutchens’s 6 % brokerage fee.

The legal staff was astonished. Assistant Counsel Edna Goldsmith immediately sent an email to General Counsel Sharon O’Conor that, in pertinent part, read:

We didn’t want Hutchens acting as a broker; he doesn’t seem to have a heck of a lot of involvement . . .

Hutchens included a letter from Bragman responding to the questions. Bragman says Heather is responsible for the development of the project; Hutchens is to secure the canal cut permit from the Canal Corporation.

This is not what we had in mind (emphasis added).

C. The Effect on Other Developers

Gary Knapp was a developer who had been working on a project of his own since June of 2003. Knapp was planning to build a canalside community and a golf course, and had designed two canal cuts into the golf course to allow the docking of recreational boats.

Knapp contacted the Canal Corporation’s Syracuse division in September of 2003, concerned that the Hutchens agreement could interfere with his right to develop the project. He sought a letter confirming that the Hutchens Contract would pose no obstacle to his project.

Knapp was willing to go so far as to dispense with the canal cuts altogether, if that would lead to an assurance that he could safely forward.

Both the Canal Corporation legal staff and its outside counsel believed that Knapp's project "should not raise any Hutchens issues" if he were to forego the cut. (Indeed, because Knapp's proposed cuts were to the golf course and not residences, they may not have implicated Hutchens's "exclusive" option even if not eliminated.) But afraid of potential legal exposure if Hutchens decided to "play spoiler," the Canal Corporation gave no such assurances to Knapp, whose project is not proceeding.

There have been other collateral effects as well. For example, once the Hutchens agreement was reached, all other projects had to be weighed not simply on their own merits, but also with respect to the Hutchens deal as well. Indeed, shortly after Board approval, Brooks sent an email to senior staff directing that even requests that "clearly are not subject to the Hutchens agreement should be approached cautiously, since the agreement establishes large fees for canal cuts, as well as significant water access fees." One project that was affected was developer Dan Lyman's Oswego Meadows project; in March 2003, Taylor informed Lyman that he would have to pay a base fee of \$25,000 to obtain a lease for a canal cut, or \$10,000 more than Hutchens was to pay. When interviewed, Taylor was unable to explain why he was charging Lyman more than Hutchens.

D. The Cancellation of the Contract

On May 2, 2004, Hutchens wrote the Canal Corporation to identify ten primary and thirty secondary sites, as required by the Option Agreement. The Option Agreement also required

Hutchens to provide on that date a certificate verifying that he had complied with the term of the agreement requiring RHA to satisfy itself as to all aspects of the condition of each site including the “condition of title, the suitability of the Site for the Developer’s intended use, soil conditions, applicable Legal Requirements and the availability of Approvals and municipal services for the Project,” and that the area designated did not exceed 9 % of the Canal System shoreline.

Hutchens did not provide the requisite certificate.

By letter dated May 7, 2004, the Canal Corporation notified RHA that it was cancelling the Option Agreement, effective May 20, 2004. The letter cited two breaches by Hutchens: his assignment of rights without seeking prior approval; and his failure to provide the certifications for the sites he designated.

RHA has provided the Canal Corporation with a Notice of Intention to Make a Claim, a prelude to a possible lawsuit.

CONCLUSIONS AND RECOMMENDATIONS

The evidence developed in the course of this investigation implicates three areas of concern: competence, ethics, and access.

1. Fundamental Competence

The viability of this project was undermined from the outset by an almost total lack of professional competence by senior members of the Canal Staff. Staff ignored the basic elements that constitute any business deal, especially one of this complexity. They failed to test the market in any serious way for other potential developers, to professionally value the asset being

sold, or to conduct even basic due diligence. This was either gross incompetence, abdication of professional responsibility, or both.

2. Ethical Violations

Compounding this incompetence were the ethical lapses by many of the same senior members of the staff. Whether it was by providing Hutchens with confidential and privileged documents, introducing Hutchens to and recommending that he retain a lobbyist, introducing Hutchens into social/campaign fundraising circles, pressuring an independent consultant to modify its report, or misleading the Board of Directors, staff repeatedly ignored its ethical responsibilities.

Many of these ethical lapses violate the Code of Ethics of New York State's Public Officers Law. These violations fall into three main categories: the disclosure of confidential documents, the political solicitation of campaign contributions, and the creation of the appearance of favoritism.⁵⁷ However, because the staff members are no longer employees of the state, the New York State Ethics Commission has no jurisdiction over them.

Confidential Documents: The investigation revealed that Thruway Authority and Canal Corporation staffers provided internal documents to Hutchens. These internal documents included:

- (1) A preliminary draft of a memo by the Canal Corporation staff to the

⁵⁷ Although it is beyond the scope of this report, Rich's provision to state employees of food and lodging to state employee guests also raises questions. Public Officers Law § 73 prohibits state employees from "directly or indirectly, . . . accept[ing] or receiv[ing] any gift having a value of seventy-five dollars or more whether in the form of money, service, loan, travel, entertainment, hospitality, thing or promise, or in any other form, under circumstances in which it could reasonably be inferred that the gift was intended to influence him, or could reasonably be expected to influence him, in the performance of his official duties or was intended as a reward for any official action on his part."

Board, containing the staff's fee recommendations;

(2) A preliminary draft of the report by outside consultant KPMG;

(3) A pre-publication copy of the Contract Reporter advertisement;

(4) A privileged communication from the Canal Corporation's outside counsel regarding the legality of Hutchens's attempted assignment of his rights to Bragman, which included counsel's thoughts on potential weaknesses in the Canal Corporation's legal position; and

(5) Confidential business plans submitted by two other boating companies during the time that Hutchens was negotiating to take over the Frankfort Marina;⁵⁸

In addition, this investigation revealed that Donald Hutton improperly disseminated internal agency materials to other outside parties. On a number of occasions, he sent internal documents to Susquehanna Railroad president Walter Rich, including a memorandum revealing business plans by a competitor of two of the Susquehanna Railroad's board members.

The Code of Ethics provision in section 74(3)(c) of the Public Officers Law states: "No officer or employee of a state agency . . . should disclose confidential information acquired by him in the course of his official duties nor use such information to further his personal interests." Each of the above-described documents had the potential to provide private parties with advantages over their competitors or with information that would assist them in negotiating contracts with the Canal Corporation. Consequently, they appear to fall squarely within the purview of section 74(3)(c).

⁵⁸ Hutchens produced from his files a draft business plan prepared by Crowne Blue, and labeled "Confidential." Taylor, at Hutton's behest, also sent to Hutchens letters he had received from R.L. Foster, proposing a new method of shipping materials along the Canal. Foster said that he had not approved the dissemination of this information to Hutchens.

Soliciting Campaign Contributions: In construing the Code of Ethics, the New York State Ethics Commission has held that a state employee working on a political campaign “may not solicit funds from any individual or business entity (1) which currently has matters before him or before the units he supervises, (2) which he has substantial reason to believe will have matters before him or such units in the foreseeable future, or (3) which had matters before him or such units in the last twelve months.”⁵⁹

Hutchens has testified that Behrmann, during the period Behrmann was managing the campaign of Dennis Vacco, solicited a campaign contribution from him. Behrmann denies this. What is undisputed is this: Behrmann and Hutchens attended a Vacco fundraiser together during the 1998 Hall of Fame weekend; that after that event, Hutchens contributed to the Vacco campaign, a contribution of which Behrmann was knowledgeable; that Behrmann wrote a letter recusing himself from significant involvement in the Hutchens matter, though he subsequently continued to play an active role in it; and that Behrmann never informed the Canal Board of any of these facts.

The Appearance Of Favoritism: The Code of Ethics forbids acts that “give reasonable basis for the impression that any person can improperly influence him or unduly enjoy his favor in the performance of his official duties, or that he is affected by the kinship, rank, position or influence of any party or person.”⁶⁰ The Code further instructs that a public officer “should endeavor to pursue a course of conduct which will not raise suspicion among the public that he is

⁵⁹ New York State Ethics Commission Advisory Opinion 98-12.

⁶⁰ Public Officers Law §74(3)(f).

likely to be engaged in acts that are in violation of his trust.”⁶¹ As the Ethics Commission has interpreted these provisions, a “public official must not only be innocent of any wrongdoing, but he must be alert at all times so that his acts and conduct give the public no cause for suspicion. He must give no appearance of a potential conflict between his duties and personal activities even though an actual conflict is not present”⁶²

This investigation uncovered improper input from Canal Staff into Hutchens’s strategy for securing the approval of their own Board – without the knowledge of the Board or counsel’s office. Among other things, during the course of Hutchens’s dealings with the Canal Corporation, the staff:

- (1) Failed to disclose to the Board the existence of a recusal letter from its Director of Canal Operations, who was intimately involved with the Hutchens matter. The Director of Operations continued to play a central role throughout the process;
- (2) Advised Hutchens’s lobbyist on how to structure his offer so as to lower the fees he would pay to the Canal Corporation;
- (3) Strategized with Hutchens about how to alter a Board-requested outside consultant’s report;
- (4) Provided Hutchens with an early copy of the *Contract Reporter* advertisement, so that he had five days more than others to prepare a response;
- (5) Without the knowledge of Canal Corporation counsel, advised Hutchens on how to negotiate with Canal counsel, which included editing drafts of letters to be sent by Hutchens’s attorney to Canal counsel; and

⁶¹ Public Officers Law §74(3)(h).

⁶² New York State Ethics Commission Advisory Opinion 02-05 (citing 1979 opinion of the Attorney General).

(6) Misled the Canal Corporation's Board through omissions of material aspects of the transaction or through outright misstatements.

Also troubling was Hutton's conduct in relation to Walter Rich's Hall of Fame weekend.

While employed by the Thruway Authority and centrally involved in the Hutchens matter,

Hutton, among other actions:

(1) Held Hutchens out to Walter Rich as a potential campaign contributor and secured Hutchens an invitation to an event whose primary focus was political fundraising;

(2) Asked to and in fact did share lodging with Hutchens at Hall of Fame weekends;

(3) Advised Hutchens to hire a particular lobbyist to influence the Board's decision on the Alpine Keys proposal; and

(4) Communicated to Rich the amounts that Hutchens would contribute to specific candidates, information Hutton could only have learned from Hutchens himself.

All these are actions that provide a "reasonable basis for the impression" that Hutchens "unduly enjoy[ed]" the "favor" of Canal Staff and would "raise suspicion among the public" that the Canal Staff were engaged in a violation of "trust."

Limits on the Enforcement of the Public Officers Law: When state employees violate the precepts set forth in the Code of Ethics, the consequences – for both actual policy and for public confidence in the operations of government – are serious, even if no criminal conduct is involved. It is therefore only right and just that public officials should be held accountable for their ethical transgressions. At present, however, there is no mechanism to address many such violations. First, the Code of Ethics currently attaches no penalties to violations of its

provisions.⁶³ Second, and more relevant to this case, New York courts have determined that the Code does not apply to former government employees.⁶⁴ As a result of the latter rule, Behrmann, Brooks and Hutton, none of whom are currently in the employ of the State of New York, are not subject even to a declaratory finding of violations in connection with their actions in the Hutchens matter.⁶⁵ This case clearly demonstrates the need for legislative reform.

3. Using Lobbyists to Gain Access

At the suggestion of Hutton, Hutchens hired lobbyists – Kerry Marsh and, subsequently, Fred Hiffa who replaced Marsh – who had social relationships with agency decision-makers and other influential individuals to advance the project in a manner not available to interested parties who had not hired lobbyists of their own. Indeed, in this case, Marsh and Hiffa even obtained confidential documents from the staff.

Numerous administrative and legislative solutions to the problem of improper influence of lobbyists have been proposed. The advantages and disadvantages of the varying approaches have been widely discussed, and do not warrant extended discussion here. However, as policy-makers decide among the many available options, they should be guided by the simple principle of transparency. The citizenry cannot make informed decisions in a democracy unless it can see how its government is working.

⁶³ Once it determines that there is reasonable cause to believe that a violation of the Code of Ethics has occurred, the Ethics Commission has the power merely to send a notice of reasonable cause to the state officer or employee's "appointing authority." Executive Law § 94 (12)(b).

⁶⁴ *Flynn v. State Ethics Comm'n*, 87 N.Y.2d 199 (1995).

⁶⁵ As noted earlier, Behrmann is currently employed by State University of New York Research Foundation. In 2003, the State Legislature failed to pass a bill that would have extended the reach of the Public Officers Law to such "affiliated corporations."