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City's Annual Franchise Fee on Telecommunications Providers Upheld

By Carol L. Van Scoyoc

On December 21, 2000, Judge Barrington D. Parker, Jr. of the Southern District of New York, issued a groundbreaking decision for municipalities in telecommunications law in *TCG New York, Inc., et al. v. City of White Plains, New York*, 125 FSupp2d 81 (S.D.N.Y.2000). After a meticulous examination of the history and structure of § 253 of the Federal Telecommunications Act of 1996, 47 U.S.C. §§ 151, *et seq.* (1996) ("TCA"), Judge Parker rejected a number of constitutional and preemption claims asserted by the plaintiffs, subsidiaries of the AT&T Corporation (hereinafter collectively referred to as "TCG"). Further, Judge Parker concluded that a number of key provisions of an ordinance adopted by the City of White Plains, requiring new telecommunications carriers to obtain franchise or license agreements with the City before using the City's rights-of-way, comported with and are consistent with the scope of § 253.

Background

For a number of years prior to the enactment of the TCA, the City of White Plains required that providers of telecommunications services seeking to construct telecommunications facilities and place other equipment (*i.e.*, fiber optic network of cables running through new and preexisting conduits) in the City's rights-of-way, obtain approval from the City's legislative body, the Common Council, and negotiate and enter into a franchise agreement with the City.[1] The franchise agreement, similar to a standard contract, includes, *inter alia*, provisions describing the grant of the franchise and type of services, a map of the proposed location of conduit, term of franchise, City's right to exercise police powers, defense and indemnification, representations, warranties, remedies for breaches, rights of termination, assignments and transfers, and the right of compensation to the City. The typical compensation to the City under these agreements is an annual franchise fee equal to 5% of the gross revenues derived by the provider, or its affiliates, in connection with the operation of the telecommunications facilities located within the City limits.

In 1996, the TCA was signed into law. Among the numerous provisions contained in the Act, is §253, which generally preempts barriers to entry to telecommunications markets. That law also expressly provides, however, that nothing in §253 affects "the authority of a State or local government to manage the public rights-of-way or to require fair and reasonable compensation from telecommunication providers, on a competitively neutral and nondiscriminatory basis, for the use of public rights-of-way, on a nondiscriminatory basis, if the compensation is publicly disclosed by such government."

As a means of addressing §253 of the TCA, the Common Council of the City of White Plains, on December 1, 1997, adopted an ordinance (essentially memorializing its pre-TCA policy and procedures) by which new telecommunication providers could obtain approval to use and place equipment in the City's rights-of-way.[2]

In brief, the City's ordinance requires that a telecommunications provider[3] first submit an application for either a franchise or revocable license to the Commissioner of Public Works and the Corporation Counsel. The application must include, *inter alia*, information concerning the applicant and its affiliates; a description of the telecommunications services proposed to be provided, including a description of facilities and equipment; a description of the proposed franchise area, or in the case of a revocable license, the specifically identified streets and/or portions of streets thereof proposed to be used; the applicant's construction plans; the applicant's legal, financial, technical and other appropriate qualifications; and the financing for the proposed construction. [4]

After the application has been deemed to be complete, the City must enter into negotiations with the applicant to determine whether such applicant and the City are able to reach agreement on the terms and conditions of the franchise or revocable license. Such terms and conditions include, but are not limited to, length of the franchise or revocable license; compensation to the City; insurance; performance bonds; indemnification requirements; the City's right of inspection of facilities and records; non-assignment clauses; and other provisions. [5]

If the telecommunications provider and the City reach an agreement, the application is forwarded to the Common Council for approval by adoption of a separate ordinance or denial. During the aforementioned process, the Common Council may require additional information from the applicant, and seek advice from other City officials and agencies, in the form of reports, which may include recommendations as to the application.[6] In its review, the Common Council may consider a number of factors, including, *inter alia*, the applicant's ability to meet construction and physical requirements and maintain the property of the City in good condition throughout the term of the franchise or revocable license; the adequacy of the proposed compensation to be paid to the City; the adequacy of the terms and conditions of the proposed franchise or revocable license; the legal, financial, technical and other appropriate qualifications of the applicant; and any other public interest factors or considerations pertinent for safeguarding the interests of the City and the public.[7]

In April of 1998,[8] after the enactment of the City's ordinance, TCG originally submitted an application to the City for a revocable license to install a small amount of fiber optic cable and about 240 feet of underground conduit. After a series of meetings and discussions, TCG subsequently decided to request a franchise and submitted an application to the City in February 1999. Since the onset of the application, the parties had been engaged in intense negotiations over a draft May 1999 proposed franchise agreement, substantially similar to the agreement executed by other telecommunications providers with the City, prior to and after the enactment of the TCA and the adoption of the City's ordinance.

TCG's Lawsuit against the City of White Plains

When it was evident that an agreement could not be reached by the parties, TCG filed a lawsuit in Federal District Court for the Southern

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District of New York on June 18, 1999, alleging violations of Federal and State law. Specifically, TCG claimed under the TCA that the City's Ordinance and proposed franchise agreement (subsequently modified and referred to by the Court as the "August Propsoal"[9]) effectively prohibit TCG from providing telecommunications services, and regulate beyond the City's public rights-of-way, violating § 253(a), (b) and (c). TCG also alleged that Bell Atlantic's *de facto* exemption from the City's Ordinance by not having to enter into a franchise agreement[10], is both non-competitive and discriminatory against TCG, in violation of §253(c) of the TCA. TCG also claimed that the City's Ordinance and the August Proposal violate the New York Transportation Corporations Law and the New York Public Service Law. Lastly, TCG alleged that the City has denied TCG's due process rights under the Fourteenth Amendment.

The District Court utilized a two-step analysis to determine whether the City of White Plains' actions violated §253 of the TCA: (1) whether the City's regulations "prohibit or have the effect of prohibiting" the ability of TCG to provide telecommunications services under §253(a); and (2) if so, whether the regulations are "saved" under §253(c) which preserves the authority of local governments to manage the public rights-of-way.[11]

As to the first issue, the District Court found that TCG met its burden in demonstrating that the City's regulations and actions violate §253 (a), since when viewed as a whole and in context, they have the effect of prohibiting the ability of TCG to provide telecommunications services . The District Court noted that the City's Ordinance prohibits a provider from using the City's rights-of-way without first applying for and then obtaining a franchise. The Court further observed that the process of obtaining a franchise has turned into a lengthy and complex negotiation between the parties. While acknowledging that the City's requirements do not impose an explicit prohibition on TCG, the Court reasoned that the Ordinance, coupled with the City's delay in moving forward on the application, have effectively prohibited TCG from providing telecommunications services in the City of White Plains.

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MLRC Director ..... *Lester D. Steinman*
Municipal Law Section Chair ..... *Linda S. Kingsley*
Co-Editors ..... *Lester D. Steinman*
Ralph Bandel
MLRC *914-422-4276*
Pace University
One Martine Avenue
White Plains, New York 10606
www.pace.edu/dyson/mlrc

A finding that the local regulations violates §253(a) of the TCA is not fatal so long as the City can show that those regulations satisfy the safe harbor provisions of §253(c). To determine whether §253(c) was met by the City, the District Court then proceeded to address three questions: (1) Do the City's regulations "manage the public rights-of-way"? (2) Are the required fees "fair and reasonable compensation" for the use of the public rights-of-way? and (3) Is the exemption of Bell Atlantic from the City's regulations competitively neutral and non-discriminatory?

Management of Public Rights-of-Way

In confronting the first question, the District Court looked to both the Ordinance and the August Proposal. After reviewing these documents, the Court found that a number of the terms comported with and were directly related to the management of the public rights-of-way. For instance, items pertaining to the pre-franchise application seeking contact information of the applicant; a description of the proposed franchise area; a proposed construction schedule; a map of the proposed location of the applicant's telecommunications system; and ownership of the applicant and identification of affiliates were sustained. The Court, however, rejected items such as a description of the telecommunications services, information concerning the provider's proposed financing for the operation and construction of the services to be provided, and a description of the applicant's legal, financial, technical and other appropriate qualifications to hold the franchise, as not directly related to the management of the public rights-of-way and preempted by the TCA.

The District Court sustained most of the requirements set forth in the Ordinance for inclusion in the franchise agreement, such as the term, cancellation and termination, performance bonds, security, insurance and indemnification, assignment and transfer limitations, etc., as properly addressing the rights-of-way and related issues. The Court, however, found that a section of the Ordinance permitting the City to include any provisions in the franchise which "it determines are necessary or appropriate in furtherance of the public interest," to be overly vague and overly broad and preempted by the TCA because it affords the City near total discretion to approve or reject an application. The Court also noted that a provision dealing with the City's right to inspect records and require the provider to maintain complete and accurate books must be limited to information necessary to enforce its rights-of-way regulations and ensure that it has received accurate fee information.

The District Court also upheld, for the most part, provisions of the Ordinance concerning review by the Common Council of the franchise agreement after it has been fully negotiated, as falling within the City's authority to manage the public rights-of-way.

Insofar as the August Proposal is concerned, the District Court reviewed each of the provisions objected to by TCG as to whether they comport with §253(c). The Court rejected, *inter alia*, TCG's contentions as to the City's requirements (a) that the franchise be nonexclusive; (b) for an examination of records in connection with the franchise fees; (c) for submission of an annual map; and (d) for submission of any financial information requested by the City concerning TCG's financial capability to comply with the agreement, as well as any information necessary to carry out the City's ability to manage the public streets.

The District Court, however, did find certain provisions beyond the purview of rights-of-way management, and thus, invalid, including, (a) the City's use of a "most favored vendee"[12] clause; (b) requirement that TCG waive its legal right, including those under the TCA, to challenge the terms and conditions of the franchise agreement; (c) the City's right to approve the location of any part of the network prior to its construction; (d) the City's right to audit all accounting and financial records of TCG related to the fiber optic network.

Proposed Franchise Fees As "Fair and Reasonable Compensation"

Perhaps the most hotly disputed provision between the City and TCG pivoted upon whether the proposed fees are "fair and reasonable compensation" under §253 (c) of the TCA. As the District Court noted, the Ordinance itself provides little guidance on the calculation of fees to be imposed, leaving the details of the compensation to be negotiated in the franchise agreement. The Ordinance does state that once the franchise is fully negotiated, the Common Council is permitted to review and pass on the proposed fee. The District Court found that as long as the fees themselves comply with Section 253(c), such provisions are not problematic under the TCA.

The Court then proceeded to examine the four categories of fees and costs to be paid by TCG to the City under the August Proposal. They are as follows: (1) an annual franchise fee equal to five percent (5%) of all revenue derived by TCG or its affiliates in connection with the proposed telecommunications facilities within the City; (2) a minimal annual fee of $5,000 in the first year, gradually increasing to $10,000 after the fifteenth year; (3) the payment for costs of third parties (including attorney's and consultants' fees) in connection with the franchise agreement; and (4) that TCG build 1,000 feet of conduit for the City at points where its proposed network overlaps the City's network currently under construction and install additional conduit for municipal purposes along the proposed network for which the City would reimburse TCG for costs of materials ("in-kind compensation"). Additionally, TCG's parent would be required to guarantee TCG's obligations under the agreement.

In analyzing this issue, the District Court observed that some courts have concluded that to be "fair and reasonable", fees must be directly tied to the provider's use of and/or the municipality's costs of maintaining the public rights-of-way. That approach essentially limits municipalities to the recovery of reasonable costs and does not permit them to profit from the use of its rights-of-way by others. However, the

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District Court noted that other courts[13] have taken a contrary approach, recognizing, (as the parties acknowledged at bar), that calculating the impact or costs of telecommunications providers on the public rights-of-way would not be a simple undertaking.[14] Accordingly, the courts have been willing to permit fees based upon general revenues and other considerations not directly related to a municipality's expenses in maintaining the rights-of-way- charging "rent" for the use of municipally-owned property for private purposes.[15] The "rent" charged must be "fair and reasonable" based upon a totality of the facts and circumstances in the particular case.

The District Court then identified the four factors set forth in the *City of Dearborn* case (in which fees substantially similar to those sought by the City of White Plains were imposed) for determining "fair and reasonable" which are as follows: (1) the extent of the use of the public rights-of-way; (2) whether other providers have agreed to comparable compensation (or comparable uses of public rights-of-way); (3) the course of dealings among the parties; and (4) whether the compensation sought is "so excessive that it is likely to render doing business unprofitable".

Applying those four factors, the District Court found that the City of White Plains has sustained its burden to prove that the fees sought to be imposed are fair and reasonable. Under the first factor, the use proposed by TCG of the City's rights-of-way appears to be extensive. As to the second factor, the Court noted that a number of other providers have agreed to the fee provisions imposed by the City at issue. The Court also remarked that TCG itself appeared to have accepted the fee provisions during negotiations and had entered into other agreements in New York State in which it agreed to pay a franchise fee calculated on the basis of gross revenue. Under the third factor, the record reflects that negotiations were on-going and resulted in extensive give-and-take by the parties, represented by knowledgeable counsel, over numerous proposed provisions. As to the fourth factor, there is no basis to conclude that the fees sought would likely render doing business with the City unprofitable. Indeed, other prospective franchisees have accepted them. The record also indicated that on several occasions, TCG revealed its willingness to pay a 5% franchise fee to the City.

Accordingly, the Court concluded that the City demonstrated that the fees it seeks to impose in the August Proposal, including the guarantee provision, are neither unfair nor unreasonable compensation under §253(c) of the TCA.

Treatment of Bell Atlantic as Competitively Neutral and Non-Discriminatory

The last element of determining whether §253(c) was met by the City centers upon whether the City can prove that the regulations and compensation sought to be imposed are done so on a "competitively neutral and nondiscriminatory basis." TCG contended that Bell Atlantic's exemption from having to enter into a franchise agreement or from having to pay a fee is non-competitive and discriminatory, and therefore the City is in violation of §253(c).

In addressing this argument, the District Court first declared that the City is not required by law to treat Bell Atlantic and TCG identically in order to satisfy §253 (c). The Court looked to the Congressional Record and noted that Congress explicitly rejected a "parity" provision that would have prohibited local governments from imposing a fee that distinguished among different providers.

The District Court pointed to the City's powerful reasons asserted why Bell Atlantic should be treated differently. These reasons included, *inter alia*, that for nearly a century, Bell Atlantic has been installing equipment and facilities under the City's streets. For all these years, Bell Atlantic has, in fact, been paying a fee to the City, in the form of having provided the City with free use of its conduit-a valuable asset-in exchange for using the rights-of-way. Bell Atlantic has provided additional conduit at no cost for the City to construct a communications system involving the City's fire and police facilities, traffic control system, schools, libraries and other governmental buildings. Further, Bell Atlantic must offer universal service and affordable rates to the residents of the City, while new providers such as TCG may limit their offerings to the most profitable business centers.

As to the non-compensation related provisions, the District Court observed that since TCG has not proffered sufficient evidence to demonstrate that Bell Atlantic has newly constructed conduits or is engaged in any activity that may otherwise impact the physical rights-of-way of the City since the adoption of the Ordinance in December of 1997, it cannot be said that exempting Bell Atlantic from those particular regulations has had a discriminatory or non-competitive effect.

In its ruling, the District Court found that the evidence presented of Bell Atlantic's large capital expenditure and compensation-in-kind to the City *e.g.* the extensive underground conduit network throughout the City, housing eleven miles of the City's cable network, free municipal use of conduit for certain governmental agencies, and universal service to all City residents is sufficient to sustain the City's burden that the fees charged to TCG and the fees paid by Bell Atlantic are competitively neutral and nondiscriminatory. Since TCG offers no proof that the fee "charged" to Bell Atlantic, as opposed to that which would be imposed on TCG, would have a non-competitive or discriminatory effect, simply asserting that the fees being charged were "different" or "unequal" is an insufficient demonstration that they are non-competitive or discriminatory in violation of §253(c).

Other Claims

The District Court dismissed TCG's claims brought under §27 of the New York

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A Memorial to Lawrence R. Dittelman

by Henry M. Hocherman

Editor's Note: Lawrence R. Dittelman was a founding member of the Edwin G. Michaelian Municipal Law Resource Center of Pace University and a frequent lecturer on land use and environmental law at Municipal Law Section meetings. He was a senior partner of the law firm of Wormser, Kiely, Galef & Jacobs LLP, and the managing partner of the firm's White Plains office.

It is with extraordinary sadness that I report the loss of a friend and colleague, Larry Dittelman, who died on May 18th after an eight year battle with cancer. It is especially fitting that Larry should be remembered in *Municipal Lawyer* because he was the quintessential municipal lawyer. He served for 27 years as Town Attorney in New Castle, weathering numerous changes in administration and shifts in party control as the demographics of the Town slowly changed. Serving in a position that is often subject to political whim, Larry rose above politics and was retained by Supervisor after Supervisor on the strength of his extraordinary knowledge of the law and his unshakable fairness and integrity. He managed to garner the respect of everyone who worked with him, and as things changed around him, Larry remained true to his basic nature. His dedication to the law and to the ethical standards that govern its practice were constant and unchanging.

In addition to his representation of New Castle, as well as the Villages of Pleasantville and Briarcliff Manor, Larry maintained an active land use practice. In that capacity he and I often found ourselves a part of the traveling circus of engineers, planners, and attorneys who appear before planning and zoning boards in the wee hours of the night. Having little else to do while we await our place on the agenda, we observe each other and get to know each other, professionally and personally. What marked Larry's practice, always, was the gentleness and gentlemanliness with which he approached his work He was modest and self-effacing, but those who knew him and saw him in action learned quickly that his was an incisive intelligence, informed by a broad knowledge of the law, and honed by careful preparation. He was an effective advocate without ever being strident, and he never relinquished his great personal dignity even as the hour grew late and the process grew increasingly frustrating.

As I got to know Larry over the years, I recognized that he was, in his personal life, just as in his professional life, a good and gentle person, devoted to his family, and brave in the face of his illness.

A number of people, Larry's friends, colleagues, and clients spoke at Larry's memorial service. As I sat and listened to them speak I realized that they were describing a person and a lawyer that each of us should aspire to be. As

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Transportation Corporations Law and New York Public Service Law relying upon the wording of the aforementioned statutes and case law. Also, TCG's claims that the City has violated its due process rights under the Fourteenth Amendment by taking, without just compensation, TCG's "right" under the New York Transportation Corporations Law to use the public rights-of-way were also dismissed by the Court. The City has not "taken" property from TCG that was granted under § 27 of the New York Transportation Corporations Law, but, instead, has exercised its right to approve or deny permission as granted by that statute.

Conclusion

The *TCG New York, Inc., et al v. City of White Plains* decision spells positive news for New York municipalities regarding the ability to regulate the installation of a telecommunication provider's fiber optic cable network and the right to receive compensation from the provider for using municipal property to provide services to the public. The District Court explicitly rejected TCG's contentions that compensation should be limited to costs for administering franchise programs and maintaining the rights-of-way. Instead, the District Court, consistent with the *Omnipoint* decision, and applying the four factors set forth by the Courts in *TCG Detroit v. City of Dearborn*, found that the City of White Plains' proposal requiring TCG to pay an annual five percent franchise fee on all revenue derived for operating telecommunications equipment within the City was "fair and reasonable"under §253 of the TCA, based on the totality of the facts and circumstances in the case. The District Court also expressly opined that Bell Atlantic's exemption from having to enter into a franchise or from having to pay a fee is not discriminatory because the City gave "powerful reasons why Bell Atlantic should be treated differently."

While the District Court did strike down certain sections of the City's Ordinance and provisions of the proposed franchise agreement as not directly relating to the management of the City's rights-of-way, the decision is generally a significant victory for municipalities and signals a green light for the adoption of carefully drafted local legislation and franchise agreements governing public rights-of-way. Stay tuned. TCG has filed an appeal and the City of White Plains has filed a cross-appeal in the United States Second Circuit Court of Appeals in the case. Oral argument on the appeal and cross-appeal has been scheduled for October of this year.

Carol L. Van Scoyoc is Chief Deputy Corporation Counsel for the City of White Plains and has been involved in the negotiation and drafting of a number of franchise and cable agreements for the City.

1. The City's authority derives from § 33 of the City Charter governing the use of City property and fair compensation for such use and Section 27 of the Transportation Corporations Law which requires, in pertinent part, that telegraph and telephone companies "obtain permission of the city ... authorities to use local streets for the construction of its lines." This latter requirement has resulted in "companies having to obtain local franchises when they sought to construct ... either above or below the public highways". *See e.g., Staminiski v. Romeo*, 62 Misc2d 1051, 1053 (Suffolk Co. Sup. Ct. 1970).
2. *See* Chapter 4-23 of the White Plains Municipal Code, entitled, "Telecommunications Franchising and Licensing".
3. *See* § 4-23-1 of the White Plains Municipal Code.
4. *See* §4-23-4 of the White Plains Municipal Code.
5. *See* §§4-23-7, 4-23-10 and 4-23-11 of the White Plains Municipal Code.
6. *See* §4-23-9 of the White Plains Municipal Code.
7. *See* §4-23-8 of the White Plains Municipal Code.
8. TCG had previous discussions with the City in 1992 and 1994 regarding the possible use of the City's rights-of-way in connection with TCG's plan to construct telecommunications facilities. No agreement had been reached by the parties.
9. After commencement of the litigation, the parties attempted to resolve their differences. As a result of the negotiations, the City offered a new proposed franchise agreement which sought to address some of TCG's objections. After further negotiations, the City offered additional modifications to the draft agreement which were deemed unsatisfactory to TCG ("August Proposal"). Among other things, the August Proposal provided that TCG pay an annual franchise fee to the City equal to 5% of gross revenues; guarantee payment from its parent corporation; build a limited amount of additional conduit without charge at the City's request; reserve the right of the City to examine TCG's records; impose a most favored vendee status on behalf of the City, and require that upon termination of the agreement, TCG remove its facilities from public property at its own expense.
10. Bell Atlantic is the City's current incumbent local exchange telephone carrier (successors-in-interest to NYNEX and New York Telephone). Since at least 1919, the City has had an arrangement with Bell Atlantic in which it agreed to provide the City with free conduit for certain municipal uses. Further, throughout the years, Bell Atlantic has provided the City free conduit space in exchange for permission to use the City's rights-of-way. Since 1954, Bell Atlantic has constructed an extensive conduit network in the City's downtown area, consisting of over 34 miles of fiber optic cable and copper wire that make up the City's own network; 20 miles are in conduit owned by the City on aerial poles owned by Bell Atlantic and Consolidated Edison; the other 11 miles are run through underground conduit provided by Bell Atlantic to the City at no cost. Bell Atlantic does not have a franchise agreement with the City.
11. The District Court dismissed TCG's claims brought under §253(b), agreeing with other Court decisions holding that §253(b) applies only to state, not local regulation.
12. Under such provision, if the City, or an elementary or secondary educational institution in the City, should contact TCG for any of its services, TCG is required to offer them rates and terms no less favorable than those offered to any other governmental or non-profit agency in Westchester County.
13. *See Omnipoint Communications, Inc. v. The Port Authority of New York and New Jersey,* 1999 WL 494120, at 6 (S.D.N.Y. July 13, 1999) citing *TCG Detroit v. City of Dearborn,* 16 F.Supp2d 785, 789 (E.D.Mich. 1998).
14. For example, a number of intangible factors would have to be weighed, *i.e.* shortened life of pavement; added police costs to deal with traffic; interference with the City's other systems; impact on traffic; and offsetting the benefits to the City from the availability of multiple telecommunications providers.
15. Citing *Omnipoint*, 1999 WL 494120, at 6; *TCG Detroit v. City of Dearborn*, 16 F.Supp2d 785, 789 (E. D. Mich. 1998) *aff'd,* 206 F.3d 618, 625 (6th Cir. 2000); *City of St. Louis v. Western Union Tel. Co.*, 148 U.S. 92, 99 (1893).

Edwin G. Michaelian
Municipal Law Resource Center
Pace University
One Martine Avenue
White Plains, N.Y. 10606

A Memorial

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with all things in our society, the legal profession is changing and practitioners of the "old school" seem to be growing fewer. Larry was an exemplar of that old school; a lawyer who believed that in the matter of ethics there is no compromise. One of the many speakers who eulogized Larry at his memorial service, an old client and friend, told of how, many years before, they had been engaged in a matter and he (the client) suggested to Larry that the circumstances of the transaction presented a little bit of "wiggle room", implying that it would be possible to somehow bend the rules to his advantage. "There *is* no wiggle room" Larry told him, and that's how the matter rested. We have lost a good and an honest man and the world and our legal community are the poorer for it.

Mr. Hocherman is a member of the Executive Committee of the Municipal Law Section and Chair of the Section's Land Use and Environmental Law Committee.