INFORMATIONAL REVIEW:
MCI TAX SETTLEMENT WITH THE STATE OF MISSISSIPPI

PHIL BRYANT
STATE AUDITOR

A Report from the Performance Audit Division
100
October 19, 2006
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STATE OF MISSISSIPPI

OFFICE OF THE STATE AUDITOR

PHIL BRYANT
AUDITOR

October 19, 2006

HAND MAIL
Governor Haley Barbour
501 North West Street
15th Floor, Woolfolk Building
Jackson, Mississippi 39201

Dear Governor Barbour:

You will find enclosed, pursuant to your June 5, 2006 request, the Review of the MCI Tax Settlement with the State of Mississippi. I have also enclosed Attorney General Jim Hood's response to our findings and recommendations.

If you should have any questions about this review of the MCI Tax Settlement, please let me know.

Sincerely,

Phil Bryant
State Auditor

PB/mcb

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MISSISSIPPI OFFICE OF THE STATE AUDITOR
PHIL BRYANT, AUDITOR

PERFORMANCE AUDIT DIVISION

INFORMATIONAL REVIEW: MCI'S TAX SETTLEMENT WITH THE STATE OF MISSISSIPPI

Report # 100 10/19/2006

INTRODUCTION

On June 28, 2005, the Office of the State Auditor (OSA) received a Legislative request to review the tax settlement between the State of Mississippi and MCI. The settlement had been reached by Mississippi Attorney General Jim Hood with the assistance of private attorneys, identified as Joey Langston and Tim Balducci, and former State Attorney General Mike Moore, who represented MCI.

Nine specific questions were included as the Legislative request from twenty-four (24) members of the Mississippi Legislative Conservative Coalition (Coalition). The Coalition consists of members of the Mississippi House of Representatives. Representative Joey Fillingane currently serves as President of the Coalition and has been the contact for the Coalition. However, toward the end of this review, Attorney General Hood opined that the Conservative Coalition did not have standing to make such a request. Governor Haley Barbour has now requested that this report be completed.

Based on the nine questions, the OSA conducted interviews, reviewed available documents and information, and compiled the answers of each party into this report. This report represents the results of this effort. Included is a detailed timeline of relevant events leading up to the settlement in question. It is important to note however, that at no time did the Office of the State Auditor independently verify or determine the need for any outside counsel in this particular case nor was there any determination made about whether it was practically necessary or economically reasonable for outside attorneys to be hired to assist in this litigation.

The Office of the State Auditor reviewed the facts and procedures of the underlying case, Mississippi Code statutes, sections of the Constitution, as well as Mississippi Supreme Court cases to make findings and recommendations about the MCI settlement. In doing so, OSA staff have determined that this case involved a tax reduction settlement as part of MCI's bankruptcy proceedings. The settlement agreement clearly states there was a claim for taxes by the State in the amount of $956,559,630 (claim #38343). In addition, section 22 of the settlement agreement states that "issues of tax law will be governed by Mississippi law." The Attorney General clearly has the authority under § 7-5-7, Mississippi Code of 1972, as amended, to work with the State Tax Commission to pursue this recovery. However, the Attorney General is limited in what he can agree to in such cases. He cannot agree to donations of State funds or payments that do not fall within his authority under State law.

Section 23 of the settlement agreement reads:

> *Each person or entity executing this Agreement represents that he/she /it is authorized to execute this Agreement. Each person executing this Agreement on behalf of a Party represents that he or she is authorized to execute this Agreement on behalf of such Party. For avoidance of doubt, the person or entity executing this Agreement on behalf of the State represents that it is authorized to execute this Agreement on behalf of the State, as defined above, including but not limited to the Mississippi State Tax Commission...*

Despite that representation in the settlement agreement, it appears that the Attorney General did not have the authority to agree to all the terms contained in the settlement agreement because payment of legal fees in the amount of $14 million to the Special Assistant Attorneys General was listed in the settlement document. The Attorney General did not have the authority to enter into such an agreement, because he may only pay private attorneys out of contingency funds in his budget or from other funds appropriated to the office of the Attorney General by the Legislature.

In addition, the Attorney General's office did not have the authority to agree for MCI to give to a non-profit organization part of the settlement of taxes due the State. The $4.2 million donation to the Children's Justice Fund was an improper donation, as Mississippi's Constitution allows donations to be made only by the Legislature and then only on a two-thirds vote.[1]

QUESTIONS AND ANSWERS

Q. **How was the independent private attorney selected to represent the State in this matter? What is the Attorney General's authority and what process did he use to select this particular attorney?**

A. According to Attorney General Jim Hood, his first days in office were spent reviewing various cases, which were brought to him from several different attorneys, requesting that they be allowed to represent the State in civil litigations. General Hood indicated that, in theory, the Civil Litigation Division could pursue such cases in-house, but there were only about eight lawyers in the division and priority was typically given to defending the actions of state officials and state agencies. They have stated that they believed it was not practical for the State to litigate anti-trust or other major cases where the State had been allegedly harmed by the actions of a company. The Attorney General's office has handled very complicated Medicaid cases, high profile and time-consuming criminal cases, the "Partnership for a Healthy Mississippi" case, as well as other cases that required a great deal of paperwork and time commitments.

The MCI case was originally brought to the Attorney General's attention by William Quin of Lundy and Davis law firm. This law firm was aware of a theory for the potential recovery from MCI of taxes for the State. This firm was familiar with the report issued by former U.S. Attorney General Richard Thornburgh during MCI's bankruptcy proceedings. This report laid out the potential for tax recovery greater than the income tax claim sought by the State Tax Commission. They were also aware of an upcoming April 1, 2004 deadline to file proofs of claim against MCI. They presented their ideas and research to the Attorney General's office.

According to the Attorney General's office, short briefs were circulated on this matter and other potential cases to a small number of the State's most prominent law firms. The Attorney General wanted to gauge their interest and gather input as to whether these cases appeared worthwhile from the standpoint of the likelihood that they would have positive outcomes for the State. It was made clear to each prospective firm that the law firm would have to pay the full cost of prosecuting the case. They were also told that there would be a sliding scale contract based on the size of the settlement and the legal stage of the case's development at the time of a settlement, which would cap the maximum percentage that could be provided for attorney fees at twenty-five percent (25%). According to General Hood, only Joey Langston of the Langston Law Firm responded with interest in the MCI tax settlement case. Because of his familiarity with the firm, General Hood felt confident that the matter would be handled in the most professional and beneficial manner possible.

[1] Section 66 of the Mississippi Constitution reads, "No law granting a donation or gratuity in favor of any person or object shall be enacted except by the concurrence of two-thirds of the members elect of each branch of the legislature, nor by any vote for a sectarian purpose or use. "

Attorney General's Authority:

Following are several statutes and court cases which provide for the Attorney General's authority to hire outside counsel, public and private, and permissible terms of payment for private counsel:

Section 7-5-37, of the MS Code of 1972, as amended, states:

The attorney general shall, at the request of the governor or other state officer, in person or by his assistant, prosecute suit on any official bond, or any contract in which the state is interested, upon a breach thereof, and prosecute or defend for the state all actions, civil or criminal, relating to any matter connected with either of the state offices. He may require the service or assistance of any district attorney in and about such matters or suits.

Section 7-5-7, of the MS Code of 1972, as amended, states:

The governor may engage counsel to assist the attorney general in cases to which the state is a party when, in his opinion, the interest of the state requires it, subject to the action of the legislature in providing compensation for such services. The attorney general is hereby authorized and empowered to appoint and employ special counsel, on a fee or salary basis, to assist the attorney general in the preparation for, prosecution, or defense of any litigation in the state or federal courts or before any federal commission or agency in which the state is a party or has an interest. The attorney general may designate such special counsel as special assistant attorney general, and may pay such special counsel reasonable compensation to be agreed upon by the attorney general and such special counsel, in no event to exceed recognized bar rates for similar services. The attorney general may also employ special investigators on a per diem or salary basis, to be agreed upon at the time of employment, for the purpose of interviewing witnesses, ascertaining facts, or rendering any other services that may be needed by the attorney general in the preparation for and prosecution of suits by or against the state of Mississippi, or in suits in which the attorney general is participating on account of same being of statewide interest. The attorney general may pay travel and other expenses of employees and appointees made hereunder in the same manner and amount as authorized by law for the payment of travel and expenses of state employees and officials. The compensation of appointees and employees made hereunder shall be paid out of the attorney general's contingent fund, or out of any other funds appropriated to the attorney general's office. [2]

The Attorney General clearly has the authority to have brought the suit against MCI. The Mississippi Supreme Court in *Dunn Construction Company v. Craig*, 191 Miss. 682, 2 So. 2d 166 (1941) held that "...the attorney general is a constitutional officer possessed of all the power and authority vested in such an official at common law, and, in addition, such as have been conferred upon him by statute, including the right to institute, conduct, and maintain all suits necessary for the enforcement of the laws of the state, the preservation of order, and protection of public rights, which right is not confined to enforcement of the criminal laws but applies also to all matters of statewide public interest in any courts of the state."

The position of Attorney General is also authorized in Article 6, Section 173 of the Mississippi Constitution. Commenting in part on this constitutional provision, the Court held in *Kennington-Saenger Theatres v. State* 196 Miss. 841, 18 So. 2d 483 (1944) that the "attorney general is entrusted with management of all legal affairs of state, and prosecution of all suits, civil or criminal, in which state is interested, having power to control and manage all litigation on behalf of state, and to maintain suits necessary for enforcement of state laws, preservation of order, and protection of public rights..."

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[2] However, section 7-5-5, Mississippi Code of 1972 is not pertinent to the facts of the MCI settlement case, because the provision allows the Attorney General to determine the amount of legal fees for private lawyers *only* when they are retained to defend claims *against* the State or its political subdivisions, or against public officials, to engage in lawsuits outside the state and for similar purposes.

The Attorney General's authority in §§ 7-5-7 and 7-5-37, Mississippi Code of 1972, as amended, appears to have been interpreted in recent Mississippi Supreme Court cases such as *Pursue Energy Corporation v. State Tax Commission* , 816 So. 2d 385 (Miss. 2002), as allowing the Attorney General broad powers in hiring outside counsel through a written retention agreement.

Section 7-5-7, Mississippi Code of 1972, as amended specifies that compensation, whether it is a fee or salary, "shall be paid out of the Attorney General's contingent fund, or out of any other funds appropriated to the attorney general's office." But that is not how the outside counsel was paid in the MCI case.

It appears that although the Attorney General appropriately used the authority granted under §7-5-7 to hire lawyers to "assist the Attorney General" in the MCI case, he did not properly follow other parts of this same statute. This same code section sets forth how these lawyers "shall" be paid. This statute does in fact use the word "may" where it means "may" (see how the AG "may" pay travel and other expenses) and "shall" where it means "shall."

In the last sentence of the section, there are only two options for paying outside lawyers (as stated above)—and having the opposing party pay the state's lawyers directly is not one of the options. It appears that the Attorney General's Office may have selectively applied this statute.

***Q.* How were the attorney's fees paid and how much were those fees?**

A. Initially, there was a retention agreement between the Attorney General's Office and the Langston Law Firm, which included a structured contingent fee schedule based on the total amount of the settlement and the legal stage of the case at the time of a settlement, with a cap of twenty-five percent (25%). However, the Office of the Attorney General did not pay the Special Assistant Attorneys General. The attorneys involved argue that they negotiated the attorney fees with MCI separately after the State's settlement was reached. But, the settlement agreement specifically listed the attorneys' fees as part of the payments made by MCI "as payments of tax and interest, to or on behalf of the State" (MCI Settlement Agreement, p. 13).

None of the attorney fees were "*paid out of the Attorney General's contingent fund, or out of any other funds appropriated to the Attorney General's Office*" as required in §7-5-7, MS Code of 1972, as amended. Rather, as part of the settlement, the fees were paid by MCI directly to the Langston Law Firm in the amount of $14,000,000, inclusive of expenses. The Langston Law Firm then paid the Lundy and Davis Law Firm $7,000,000 for the assistance they provided. Fees to other supporting firms (from New York) were also paid out of the $14,000,000 payment from MCI and not from a contract with the State of Mississippi.

This financial arrangement was clearly a part of the settlement of the tax claim pursued by the State of Mississippi. OSA finds that no other conclusion can be drawn from this language in the State's settlement agreement with MCI: "In exchange for the cash payments and property transfer, the State agrees to compromise and fully release [MCI's] obligation to pay all taxes, interest, and penalties..." (MCI Settlement Agreement, p.14). The total cash payments made by MCI in that agreement were $118.2 million. Of that amount, however, the State of Mississippi only received $100 million.

***Q.* How was the amount of the attorney's fees determined?**

A. A written retention agreement, signed September 29, 2004, was entered into between the Attorney General's Office and the Langston Law Firm. The agreement, which was properly constructed under the Attorney General's authority in §7-5-7, Mississippi Code of 1972, Annotated, stated that Joey Langston and Tim Balducci would be designated as "Special Assistant Attorneys General to investigate, research, and file the claims in any appropriate court or courts or before any appropriate governmental agencies." OSA found no indication that Lundy and Davis Law Firm had a retention agreement with the State. Instead, it appears as if these other firms may have had agreements with the Langston Law Firm.

The fee payment section of the retention agreement between Langston and the Mississippi Attorney General's Office was divided into two sub-sections. The first sub-section referred to a structured contingent fee schedule based on the total amount of the settlement and the legal stage of the case at the time of a settlement, with a cap of twenty-five percent (25%). The second sub-section referred to the reimbursement of all reasonable and necessary costs of litigation. Based on this agreement, Langston Law Firm expected to receive $15,000,000 plus expenses.

The establishment of a fee schedule within the retention agreement was completely within the authority of the Attorney General. However, regardless of the amount agreed to in the retention agreement, the Special Assistant Attorneys General could only be paid an amount actually appropriated by the Legislature at its discretion. Instead, after the initial portion of the settlement was reached, the Attorney General apparently suggested that the attorney fees be negotiated with MCI. The attorneys asked for $15,000,000, but MCI only agreed to pay $14,000,000.

***Q.* Can we get the settlement summarized/itemized?**

A. There has not been a summary of the settlement created by the Attorney General's Office or any other group. The Auditor's review of the settlement document revealed that there are two major components to the settlement agreement: The settlement payment and releases to the State and the actions and authorities of the settlement agreed to by the State. Please note, that the entire settlement agreement is attached to the end of this report.

The Settlement Payments and Releases:

Section 8, page 13 of the Settlement Agreement details the payments that were to be made "as payment of tax and interest, to or on behalf of the State":

- A direct payment of $100 million to the State of Mississippi
- Several parcels and buildings (some with outstanding liens) given to the State
- $4.2 million provided as a direct donation to the Children's Justice Center
- The direct payment of $14,000,000 in counsel fees and costs to Joseph C. Langston and Timothy Balducci.

The Actions and Authorities of the Settlement

The nineteen (19) page settlement agreement begins with a Recitals section recounting the series of events preceding the agreement. Section 1 affirms that both parties agree that this is the definitive account of the chain of legal and judicial actions relevant to the settlement agreement.

The next major section (Section 2) consists of a set of definitions, which occupy nearly one-quarter of the entire agreement. These definitions give specificity and meaning to the other actions and agreements which appear elsewhere in the settlement document.

Section 3 states that this agreement requires approval by the Bankruptcy Court and that both parties agree to make a good faith effort to obtain this approval. Without the approval, this agreement becomes null and void.

Section 4 cites the effective date of the agreement to be eleven days after approval by the Bankruptcy Court. Since approval was granted on May 13th, the effective date would have been May 24, 2005. The payments were to occur, according to Section 8, within one day of the effective date.

Section 5 re-states which tax years are included in the settlement so that there can be no misunderstanding about the time period addressed regarding MCI's tax responsibilities. Section 6 defines the tax responsibilities after December 31, 2002.

Section 7 explains that mergers, liquidations, and consolidations occurring during Tax Year 2004 will be treated as tax-free or as a carry-over basis tax deferred transaction for the State tax purposes.

Section 8 is detailed above.

Sections 9 and 10 state that there is no admission of wrongdoing by MCI and that the State of Mississippi does not regard the settlement as being a fine or penalty. These findings are followed by Section 11, which allows MCI to take positions inconsistent with the settlement, should it desire to do so with any parties other than KPMG and Brunini, Grantham, Grower and Hewes. In legal matters pertaining to these two parties, MCI is compelled to act in accordance with the definitions and understandings inherent in the settlement agreement.

The final twelve sections (Sections 12-23) list a number of legal issues pertaining to the validity of the agreement. They include such topics as language conventions pertaining to interpretation of the agreement, governing law, and the authority to execute the agreement.

Q. **What issues were actually filed in bankruptcy court? If more than one, we would like an explanation of those issues.**

A. According to page 55 of the Third and Final Report of Dick Thornburgh, Bankruptcy Court Examiner dated January 26, 2004, "To confirm the anticipated tax treatment of the royalty income to be recognized by the Company, the Company (through special Mississippi tax counsel) and KPMG submitted a joint request to the Mississippi State Tax Commission seeking confirmation, among other things, that royalty income generated from the subsidiaries, many of which resided outside of Mississippi, would be taxed to the Company only to the extent that the subsidiaries earned income in Mississippi. The written ruling request gave the Mississippi State Tax Commission no hint as to the true nature of the intangible assets being licensed and did not mention that the core intangible asset for which the Company would receive royalty payments was 'management foresight'."

Based on royalties and services amounts that MCI had apparently misrepresented, there were two claims and one amendment filed.

1. On March 24, 2004, the Mississippi State Tax Commission filed a claim in bankruptcy court in the Southern District of New York for $3,500,000 for income taxes owed to the State. On March 26, 2004, the Attorney General (AG), along with the Lundy and Davis Law Firm, contacted the Tax Commission to inform them that the AG's office believed the amount that had been filed was underestimated. They believed the amount should have been higher because the entire $20,000,000,000 *($20 billion)*, that was misrepresented, was taxable services rendered in Mississippi.

2. As a result, on March 31, 2004, one day before the deadline to file a claim, the Attorney General's office filed a claim 'on behalf of the Tax Commission' in the amount of $1,000,000,000 *($1 billion)*, which was the State's corporate tax rate of five percent (5%) times the $20,000,000,000. This amount was amended on May 25, 2004, to $956,000,000.

***Q.* How was the settlement arrived at? Who was actually involved in the settlement negotiations, and what was the role of the State Tax Commission, the Governor's Office and the Attorney General's Office in this process?**

A. On April 7, 2005, the Settlement Conference was held at the Attorney General's office. In addition to himself, General Hood indicated that Special Assistant Attorneys General Joey Langston and William Quin were present on behalf of the State, and, representing MCI, former Mississippi Attorney General Mike Moore, Carol Ann Petren, and another outside tax counsel were present. Negotiations began. MCI agreed to pay one hundred million dollars ($100,000,000), which according to the Attorney General was an amount that both the State and MCI felt was reasonably owed, as well as the maximum that MCI would voluntarily pay. The Attorney General proposed that MCI add the building and property at the headquarters facility in Clinton, but because this property was already committed to other claimants, MCI agreed to add in the properties it owned in downtown Jackson. The Attorney General suggested that perhaps a charitable donation be made. After several charities and non-profit organizations were considered, the Children's Justice Center, a project one of the MCI representatives had been working on, was mentioned. Unsure of exactly how much it would take to get the organization up and running, the Attorney General estimated around three million dollars ($3,000,000) to put all the services and resources in place. MCI agreed to that amount. At this point, the negotiations turned to the payment of the attorney fees. The Langston Law Firm expected to receive fifteen million dollars ($15,000,000) plus expenses, based on the sliding fee scale contained in the retention agreement. MCI agreed to pay fourteen million dollars ($14,000,000) in attorney fees. Because the Langston Law Firm did not get the entire amount they expected, MCI offered to contribute an additional one million two hundred thousand dollars ($1,200,000) to the Children's Justice Center. This offer was satisfactory to the Attorney General and the Langston Law Firm.

The role of the Tax Commission was very limited. According to Gary Stringer at the Tax Commission their major concern was the lack of involvement throughout the entire process. They felt as if they were kept out of the loop when they clearly asked, on more than one occasion, to be kept informed. Every time they raised questions about offers being made, they were told no serious offers had been made. The final experience that disturbed the Tax Commission began on April 29, 2005. On this day, the Tax Commission heard a rumor that a settlement had been reached with MCI. They placed a call to the Lundy and Davis Law Firm with questions about this information. The Tax Commission was told that the Attorney General had advised the Lundy and Davis Law Firm not to talk and to refer all questions to his office. The Tax Commission then called the Attorney General's office and left two voice messages. On May 2, 2005, there was a call from the Attorney General's office informing the Tax Commission that no settlement had been reached and if and when it was, he would notify the Tax Commission. Then on May 6, 2005, a settlement was reached. The

Tax Commission didn't receive a call until May 9, 2005, the day the settlement was announced, when General Hood phoned Chairman Joe Blount.

It does not appear the Governor's Office was aware of the settlement until May 9, 2005, the day it was announced to the public. According to the Governor's staff, they were "disturbed and unhappy with the lack of communication from the Attorney General's office during this process."

The Attorney General played a vital part of the entire process. Though the Attorney General hired Special Assistant Attorneys General Joey Langston and Tim Balducci, he in no way relinquished his authority. According to General Hood, he had the sole authority to settle this litigation on behalf of the State of Mississippi. The retention agreement stated that "the law firm shall consult with the Attorney General and obtain his approval on all material matters pertinent to these claims and any litigation arising there from, and the Attorney General shall cooperate with the law firm and use his best efforts to secure the cooperation of other State agencies." It was the Attorney General who signed the MCI Settlement Agreement on behalf of the State of Mississippi.

***Q.* We would like a summary of the disposition of the money from the settlement.**

A. According to the settlement agreement and release entered into on May 6, 2005, there were a total of four (4) payments to be released:

1. One hundred million dollars ($100,000,000) went to the State of Mississippi. This amount was wire transferred into a receiving account according to instructions provided by the Office of the State Treasurer, which was not abnormal procedure. It was then transferred into the general fund where it was allocated in the manner prescribed by the Legislature in a special session including:

    - ✓ $50 million to strengthen the Public Employees Retirement System fund;
    - ✓ $35 million to pay a State loan guarantee on Mississippi Beef Processors;
    - ✓ $10 million to the University Medical Center Cancer Institute; and
    - ✓ $5 million to Department of Public Safety for Mississippi Highway Patrol training.

2. Fourteen million dollars ($14,000,000) in counsel fees and costs to the Langston Law Firm for acting as Special Assistant Attorneys General.

3. Four million two hundred thousand dollars ($4,200,000) to the Children's Justice Center of Mississippi; and

4. Ten property parcels including MCI's main office building in downtown Jackson, along with several other buildings and parking lots, which, according to the Attorney General's Office's May 9th press release, were on the market at that time for approximately seven million dollars ($7,000,000).

***Q.* Which buildings and parcels of real estate were part of the MCI/WorldCom settlement?**

A. According to exhibits B and C of the settlement the following parcels were a part of the settlement:

33-4-1	33-12	33-16	34-17	34-18
34-20	34-20-1	34-21	34-29	34-30-1

The Property includes the real property located at 515 East Amite Street, 229 North State Street, 523 Yazoo Street, 514 East Amite, 517 East Yazoo Street, 203 North State Street, and 508 East Amite Street.

It should be noted that:

- As stated in the agreement, the real property was to be transferred by quitclaim deed, "as is, where is", including land improvements and fixtures in place. However, when the agreement was enacted, there were apparently several state and federal liens against the properties; it is, therefore, likely that the State will not have clear title to them in the near future.

- As long as the lien holders do not object or the State does not decide to sell the property, the State may choose to take all necessary actions towards the ultimate goal of removing all outstanding liens. It should be stressed, however, that the State should not make substantial improvements to these properties until such time as clear title is achieved.

- As to the value of the real property contained in the agreement, the Department of Finance and Administration (DFA) is in possession of two separate appraisals, both dated in 2003, when the State considered purchasing these properties. The appraisals estimate the value of seven of the eight parcels at six million dollars ($6,000,000) and six million one hundred thousand dollars ($6,100,000), respectively. The remaining real property, based on a square footage estimate, according to DFA, might total an addition two hundred fifty thousand dollars ($250,000). However, it could cost around fifty thousand ($50,000) to demolish the deteriorated structure, which currently occupies the site. Therefore, the estimated value of the ten parcels in the agreement would increase to approximately six million two hundred fifty thousand dollars ($6,250,000). The State is yet to receive the title documents, so it would be premature for DFA to make a final determination for capital asset valuation and depreciation purposes.

While stressing that it was impossible to determine at the time of the settlement conference precisely what liens might exist, the Attorney General believed that any claims might ultimately be settled to the State's benefit. It is unknown what legal costs may be associated with any negotiations, which might be required in order for the State to gain clear title.

It should also be noted that since Hurricane Katrina, the State has allowed the Federal Emergency Management Agency to utilize one of the parcels.

***Q.* In what way were the buildings part of the final settlement? (for example: credit in lieu of greater cash payment, in addition to any cash settlement, etc.)**

A. The real property was in addition to the cash settlement. The Attorney General originally proposed that MCI add the building and property at the headquarters facility in Clinton. Because this property was already committed to other claimants, MCI agreed to add in the properties it owned in downtown Jackson.

TIMELINE OF EVENTS LEADING UP TO THE MCI TAX SETTLEMENT

April 30, 1997	KPMG Peat Marwick LLP (KPMG) and MCI execute engagement letter to implement restructuring and Royalty Program.
Summer, 1997	WorldCom, Inc. and MCI merge.
August 21, 1997	Mississippi State Tax Commission (MSTC) responds to ruling request from MCI regarding 1998 Royalty Program.
January 1, 1998	WorldCom implements 1998 Royalty Program.
January 1, 1999	WorldCom implements 1999 Royalty Program.
April 30, 2002	Bernie Ebbers steps down as WorldCom's CEO.
Mid-June, 2002	WorldCom announces initial adjustments to its financial statements totaling $3.8 billion.
July 21, 2002	WorldCom initiates filings for bankruptcy.
July 22, 2002	U.S. Bankruptcy Court for the Southern District of New York begins consolidation of MCI cases.
August 6, 2002	Dick Thornburgh appointed Bankruptcy Court Examiner. Investigation given broad mandate.
Mid-August, 2002	MCI proposes additional restatement of financial statements totaling $3.3 billion.
October 29, 2002	Bankruptcy Court sets deadline of January 23, 2003 for filing proofs of claim.
November 4, 2002	Examiner files First Interim Report identifying preliminary observations and areas needing investigation.
May 13, 2003	Group of MCI bondholders suing WorldCom over Bankruptcy Plan file motion and disclose Royalty Program aimed at state tax minimization.
June 9, 2003	Examiner files Second Interim Report focusing on MCI's system of corporate governance.
September, 2003	Massachusetts and eight other states: New York, Connecticut, New Mexico, Iowa, Illinois, Pennsylvania, North Carolina, and Virginia file a motion to extend the date for submission of claims for Royalty. Programs and related state tax minimization issues until April 1, 2004.
October 31, 2003	Bankruptcy Court confirms MCI Bankruptcy Plan.
November 7, 2003	MSTC files motion to extend bar date for filing proofs of claim for unpaid corporate income taxes.
January 26, 2004	Examiner files Third Interim Report citing numerous matters, including MCI's state tax minimization program.

January 30, 2004	Lundy and Davis Law Firm makes presentation to Attorney General regarding potential claims for back taxes and accounting malpractice.
February 3, 2004	Bankruptcy Court grants Mississippi extension request.
March 26, 2004	MSTC files proof of claim for $3,020,611 for unpaid franchise taxes from 1999-2002.[3]
March 31, 2004	Attorney General's Office files amended proof of claim in the amount of $1 billion.
March 31, 2004	Attorney General informs MSTC it has retained Lundy and Davis Law Firm in the case. However, no retention agreement for this purpose was on file with the Attorney General.
April 1, 2004	Lundy and Davis Law Firm attorneys meet with MSTC staff to discuss the Attorney General's recovery theory.
April 2, 2004	Lundy and Davis Law Firm begins selection of expert to assess recovery theory.
April 8, 2004	Lundy and Davis Law Firm meets with MSTC staff and conducts conference call with Dr. John Swain, hired to evaluate the Attorney General's recovery theory.
April 19, 2004	Dr. Swain provides findings memo reviewed at meeting between MSTC and Lundy and Davis Law Firm attorneys. Dr. Swain participates by telephone.
April 20, 2004	Bankruptcy Plan becomes effective.
May 25, 2004	State files amended claim for tax years 1999-2002 in the amount of $956,559,630.
July 14, 2004	Tax Commission Chairman Joe Blount meets with attorneys from the Office of the Attorney General for further discussion regarding the Attorney General's theory of recovery.
August 29, 2004	MCI tax officials meet with MSTC and lawyers representing Attorney General's Office at MSTC.
September 28, 2004	Mississippi joins Negotiating Committee, which included 17 other states filing claims against WorldCom.
September 29, 2004	General Hood and Langston Law Firm enter into retention agreement.
November 9, 2004	MCI rejects offers made by Negotiating Committee at MCI headquarters meeting.
February 17, 2005	Lundy and Davis Law Firm attorneys meet for the final time with MSTC to go over figures in the State's claim.
March 4, 2005	State submits revised estimate of tax and interest to be $966,396,539 for the period January 1, 1999 to December 31, 2002.
March 7, 2005	MCI makes initial settlement offer of $20 million.

[3] This claim also included $554,168.00 for post-petition administrative expenses, which brought the total amount of the claim to $3,574,779.00.

March 16, 2005	MCI files objection to MSTC claim in Bankruptcy Court.
April 6, 2005	State responds to MCI objection in Bankruptcy Court.
April 7, 2005	Agreement in principle reached at settlement conference between Attorney General's Office and MCI.
May 6, 2005	MCI and the Attorney General sign tax settlement agreement.
May 9, 2005	Attorney General's Office announces tax settlement agreement.
May 12, 2005	Hearing held to consider motion to allow/approve settlement.
May 13, 2005	Bankruptcy Court approves settlement.
May 24, 2005	MCI settlement becomes effective.
June 2, 2005	State uses $35 million from MCI settlement to pay off a guaranteed bank loan.

FINDINGS AND RECOMMENDATIONS

Finding 1: The $4.2 million payment to the Children's Justice Center is clearly part of the settlement on behalf of the State of Mississippi. These funds should have been properly deposited to the State General Fund. If made at all, that donation should have been made through the legislative process as required by section 66 of the Mississippi Constitution. As part of the settlement, these proceeds are public funds made "as payment of tax and interest to or on behalf of the State." Therefore, because the money was paid directly to Children's Justice Center, it was an improper donation.

Recommendation 1: The State Auditor's Office with the assistance of the Mississippi Attorney General should seek recovery of the $4.2 million in public funds and deposit them in the General Fund Account for the State of Mississippi (§7-7-211(g)).

Finding 2: The $14 million paid in attorney's fee is also part of the settlement "as payment of tax and interest to or on behalf of the State of Mississippi." Initially, such payment should have been deposited into the State General Fund with all other MCI settlement funds. Then, there would have been the opportunity, through the legislative process, to set aside funds in an amount the Legislature found to be appropriate to pay outside counsel hired by the Attorney General to represent the people of the State of Mississippi. In such cases where the Attorney General has a contract with a private law firm, it is the Legislature's prerogative to always determine proper payment and appropriate that amount to the Attorney General's Contingency Fund. These funds may then be audited as part of the financial statement of the State. (§7-5-7)

Recommendation 2: Because the legislative process was bypassed in the appropriation of these funds, any portion of the settlement not authorized by the Legislature should be returned to the General Fund. The State Auditor's Office with the assistance of the Mississippi Attorney General should recover these public funds on behalf of the taxpayers of the State.

Finding 3: On March 31, 2004, the Attorney General sent a letter to the Tax Commission acknowledging the Lundy and Davis Law Firm as representing the State of Mississippi in the recovery and collection of tax liabilities from MCI. However, the retention agreement between the Attorney General and the Langston Law Firm was not signed until September 29, 2004. In addition, no retention agreement was signed with the Lundy and Davis Law Firm.

Recommendation 3: The Mississippi Legislature should amend current laws to clarify that before outside counsel can be acknowledged as representing the State of Mississippi, there should be a written retention agreement signed for all parties who will represent the State, and that no private attorneys should receive payments in any amount, directly or indirectly, without a written retention agreement with the State.

Finding 4: The tax settlement included the transfer of two buildings previously owned by MCI/WorldCom. Currently, the property is part of the MCI/WorldCom bankruptcy proceedings and no clear title to the property has been transferred to the State of Mississippi.

Recommendation 4: The Attorney General should petition the U.S. Bankruptcy Court for clear title to the property.

MCI Settlement Agreement

SETTLEMENT AGREEMENT AND RELEASE

This Agreement is made and entered into as of the 6th day of May, 2005, by and among the Parties set forth on the signature pages hereto. This Agreement is made as a compromise between the Parties for the complete and final settlement of their claims, differences and any causes of action with respect to the issues described below. Capitalized terms shall have the meanings assigned to such terms in Section 2 of this Agreement.

RECITALS

A. On July 21, 2002 and November 8, 2002, the Debtors commenced their Chapter 11 Cases.

B. By orders entered by the Bankruptcy Court on July 22, 2002 and November 12, 2002, the Chapter 11 Cases were consolidated for procedural purposes under Case No. 02-13533.

C. On October 29, 2002, the Bankruptcy Court entered its Order Pursuant to Bankruptcy Rule 3003(c)(3) Establishing the Deadline for Filing Certain Proofs of Claim and Approving the Form and Manner of Notice Thereof, establishing January 23, 2003 as the bar date for filing most proofs of claim in the Chapter 11 Cases.

D. On November 7, 2003, the State filed the Motion of the Mississippi State Tax Commission to Extend the Deadline for Filing Proofs of Claim (Docket No. 10007) (the "Bar Date Extension Motion") seeking to extend the Bar Date to April 1, 2004, with respect to certain claims against WorldCom.

E. On February 3, 2004, the Bankruptcy Court entered a Stipulation Regarding Motion by the Mississippi State Tax Commission to Extend the Deadline for Filing Proofs of Claim, which established April 1, 2004, as the bar date for the State to file "Additional Claims"

(as defined therein), consisting of "additional claims relating to certain state taxes as more fully set forth in the [Bar Date Extension] Motion. . . ."

F. To date, the State has filed five (5) Claims in the Chapter 11 Cases which include or which the State contends include Additional Claims, namely (1) Proof of Claim Number 38127 in the amount of $3,574,779.10 (including administrative expense claim), (2) Proof of Claim Number 38136 (an exact duplicate of Claim 38127), (3) Proof of Claim Number 38134 in the amount of "$1,000,000,000.00+", (4) Proof of Claim Number 38135 (an exact duplicate of Claim 38134), and (5) Proof of Claim Number 38343 in the amount of $956,559,630.00 (including administrative expense claim). To the extent the State has filed or does file any other Claims that include or relate to Additional Claims, they are also released, withdrawn and expunged as described below.

G. On October 31, 2003, the Bankruptcy Court entered an order confirming the Plan.

H. On April 20, 2004, the Plan became effective in accordance with its terms, and pursuant to the Plan, WorldCom merged with and into MCI, with MCI being the survivor.

I. By a letter dated March 4, 2005, the State purported to assess tax and interest on WorldCom, Inc. and affiliates in the total amount of $966,396,539.00 for the period January 1, 1999, to July 21, 2002, and the period July 22, 2002, to December 31, 2002 (the "MSTC Assessment").

J. On March 16, 2005, the Reorganized Debtors filed an "Objection to Certain Tax Claims Filed by the Mississippi State Tax Commission" with the Bankruptcy Court in which they objected to Additional Claims filed and asserted by the State.

K. On April 6, 2005, the State filed a "Response of Mississippi State Tax Commission ("MSTC") to Debtors' Objection to Certain MSTC Tax Claims" and a related

motion ("Motion of Mississippi State Tax Commission for Abstention Pursuant to Bankruptcy Code Section 505, Rule 5011 and 28 U.S.C. §1334(c)(1), and for Relief from the Discharge Injunction" (the "Abstention Motion")) with the Bankruptcy Court.

L. The Parties have agreed, subject to Bankruptcy Court approval, to compromise their disputes as set forth below.

AGREEMENT

NOW THEREFORE, for good and valuable consideration, the receipt, adequacy, and sufficiency of which is acknowledged, the Parties agree as follows:

1. Incorporation of Recitals. Each of the Parties represents and warrants that each of the above recitals is true and correct to the best of such Party's knowledge, information, and belief, and such recitals are incorporated herein as part of this Agreement.

2. Definitions. Unless the context requires otherwise, the following terms shall have the following meanings whether with initial capital letters or otherwise. Any term not defined herein shall have the meaning assigned to such term in the Plan. As used herein:

- "Additional Claims" means all Claims (as defined below) filed, asserted and/or held by, or on behalf of, the State, against any or all of the Released Parties, arising out of or relating to the Royalty Program, including, without limitation, Claims Number 38127, 38136, 38134, 38135 and 38343, and the MSTC Assessment. For the avoidance of doubt, to the extent the State has filed or does file any other proofs of claim or other Claims arising out of or relating to the Royalty Program or the MSTC Assessment, such Claims are included within the definition of Additional Claims.
- "Agreement" means this Settlement Agreement and Release.
- "Bankruptcy Code" means title 11 of the United States Code, as amended.

- "Bankruptcy Court" means the United States Bankruptcy Court for the Southern District of New York presiding over the Chapter 11 Cases.

- "Bankruptcy Rules" means the Federal Rules of Bankruptcy Procedure, as amended.

- "Bar Date Extension Motion" is defined in Recital D.

- "Books and Records" means the financial and accounting books, records, ledgers and other documents maintained by the Debtors prior to the effective date of the Plan, and by the Reorganized Debtors on and after the effective date of the Plan, in connection with the operation of their businesses.

- "Chapter 11 Cases" means the cases filed by the Debtors on and after the Commencement Date in the Bankruptcy Court which are consolidated for procedural purposes under Case No. 02-13533.

- "Claims" means any and all known or unknown past, present, future, foreseen or unforeseen, liquidated or unliquidated, actions, assessments, causes of action, claims, proofs of claim, requests for allowance and payment of administrative expenses, demands, determinations, judgments, liabilities, or suits, whether civil or criminal, at law or equity, before any local, state, or federal court, tribunal, administrative agency or governmental entity, filed, asserted and/or held by, or on behalf of, the State, including, without limitation, any Claim for tax, interest, or penalty. "Claims" includes, without limitation, any and all Additional Claims filed, asserted and/or held by, or on behalf of, the State.

- "Consolidated Restatements" means WorldCom's audited financial statements for the years ended December 31, 1999, 2000, 2001 and 2002, including the

audited financial statements for the years ended December 31, 2000, 2001 and 2002 that were included in WorldCom's Annual Report for the period ended December 31, 2002, reflecting restatements and adjustments that include, without limitation, restatement of line cost expenses (or access cost expenses), and write-off of goodwill and write-down of the carrying value of property, plant and equipment and other intangible assets.

- "Debtors" means WorldCom and its direct and indirect subsidiaries that filed the Chapter 11 Cases.
- "Effective Date" means the date set forth in Section 4 of this Agreement.
- "IRS" means the Internal Revenue Service.
- "Massachusetts Motion" means the Motion to Extend the Deadline for Filing Proofs of Claim filed by the State of Massachusetts (on behalf of itself and numerous other states) on September 2, 2003, seeking to extend the Bar Date for filing claims for unpaid income taxes relating to WorldCom's Royalty Program.
- "MCI" means MCI, Inc., on and after the effective date of the Plan.
- "MSTC Assessment" is defined in Recital I.
- "MTC Audit" means the audit of the Royalty Program performed by the Multi-State Tax Commission.
- "Parties" means, collectively, all parties to this Agreement.
- "Party" means a party to this Agreement.
- "Plan" means the Debtors' Modified Second Amended Joint Plan of Reorganization Under Chapter 11 of the Bankruptcy Code, which was confirmed pursuant to an order entered by the Bankruptcy Court on October 31, 2003 and which became effective on April 20, 2004.

- "Released Parties" means, collectively, all of the Debtors and the Reorganized Debtors and all of their respective predecessors, successors, and all their present and former merger partners, parents, subsidiaries, divisions, affiliates, agents, directors, officers, employees, representatives, servants, companies, corporations, limited liability corporations, ventures, partnerships, shareholders, licensees, sublicensees, and assigns. Released Parties do not include KPMG, or any of KPMG's individual partners, merger partners, parents, subsidiaries, divisions, employees, servants, companies, corporations, limited liability corporations, ventures, partnerships, shareholders, managers, agents, directors, officers, affiliates, representatives, licensees and assigns. Further, "Released Parties" do not include the law firm of Brunini, Grantham, Grower & Hewes, or any of their individual partners, merger partners, parents, subsidiaries, divisions, employees, servants, companies, corporations, limited liability corporations, ventures, partnerships, shareholders, managers, agents, directors, officers, affiliates, representatives, licensees and assigns. It is the express intent of the Parties that the settlement reached herein and the release afforded hereby does not extend in any manner to these Non-Released Parties, except as expressly provided in paragraphs 8(a) and 8(b) below.

- "Releasing Parties" means, collectively, the State and all its present and former divisions, agencies, agents, officials, officers, employees, representatives, servants, constituents, and assigns.

- "Reorganized Debtors" means the Debtors on and after the effective date of the Plan, including, without limitation, MCI.

- "Royalty" means an amount paid or accrued by certain WorldCom subsidiaries to WorldCom or a WorldCom subsidiary, pursuant to the Royalty Program (without regard to how such amount might be characterized).

- "Royalty Program" means the program implemented by and among WorldCom and certain of its subsidiaries, as referenced or alleged or otherwise relating to the program referenced in, the Bar Date Extension Motion, the Massachusetts Motion, and the Abstention Motion. The Royalty Program is no longer in effect.

- "Settlement Motion" means the motion to be filed by the Reorganized Debtors requesting, pursuant to Bankruptcy Rule 9019, the Bankruptcy Court to, among other things, approve this Agreement.

- "State" means the State of Mississippi and all subdivisions, agencies, officers and representatives of the State, including, without limitation, the Mississippi State Tax Commission and the Office of the Attorney General.

- "Surviving Claims" means all Claims filed, asserted and/or held by, or on behalf of, the State which shall not be expunged by and shall survive this Agreement, consisting of the proofs of claim and requests for allowance and payment of administrative expenses set forth on **Exhibit A** hereto. The Surviving Claims do not include any of the Additional Claims.

- "Tax Year" means any fiscal period for which taxes have been or may be assessed against one or more of the Debtors or the Reorganized Debtors. For example, "Tax Year 2002" refers to the period starting January 1, 2002 and ending December 31, 2002.

- "WorldCom" means WorldCom, Inc. before the effective date of the Plan.

3. Bankruptcy Court Approval. This Agreement is subject to approval by the Bankruptcy Court, and the Parties agree to use their best efforts and good faith to obtain such approval. Pursuant thereto, the Reorganized Debtors promptly shall file the Settlement Motion seeking approval of this Agreement. In the event the Bankruptcy Court does not approve this Agreement, it shall be null and void.

4. Effective Date. The Effective Date of this Agreement shall be the eleventh (11th) day after the Bankruptcy Court enters a final, non-appealable order granting the Settlement Motion and approving this Agreement.

5. Settlement of Claims Relating to Tax Years Ending On or Before December 31, 2002. The following terms shall apply to any and all Tax Years ending on or before December 31, 2002:

a. All of the Additional Claims, including, without limitation, Claims Number 38127, 38136, 38134, 38135 and 38343, and the MSTC Assessment, are released, discharged, withdrawn, and dismissed with prejudice, and expunged, by the Releasing Parties as against the Released Parties. The Surviving Claims set forth on **Exhibit A** hereto shall not be expunged by and shall survive this Agreement, subject to the terms set forth immediately below.

b. To the extent the liability or amount of any Surviving Claim depends on income, revenue, expense, deduction, asset value, net worth, capital, or any other financial or tax measure of a Debtor, the liability and amount shall be resolved on the basis of the Consolidated Restatements as stated and without challenge.

c. The Reorganized Debtors will not, and will not be required to, file any refund claim or amended income or franchise tax return in the State for Tax Years ended on December 31, 2002 or earlier.

d. Any change in the Debtors' federal taxable income for Tax Years ended on December 31, 2002 or earlier, through audit or final determination with the IRS, shall not affect the terms of this Agreement. The Reorganized Debtors will not be required to report any change in federal taxable income for Tax Years ended on December 31, 2002 or earlier, and will not be required to file amended State tax returns related to any such change in federal taxable income.

6. Subsequent Tax Years. The following terms apply to Tax Years ending on December 31, 2003 and thereafter:

a. The Reorganized Debtors will not report any Royalty income or claim any deduction for a Royalty under the Royalty Program in Tax Year 2003 and later years. Any income tax return previously filed with the State for Tax Year 2003 that includes any Royalty income or deduction will be amended to eliminate any amount reported as Royalty income or deduction. Any franchise tax return previously filed with the State for Tax Year 2003 that includes the effect of the Royalty Program (in the computation of retained earnings or otherwise) will not be amended, and will not be subject to review or challenge by the State on the basis of inclusion or exclusion of amounts reported under the Royalty Program.

b. The Royalty Program will not be the basis for filing any Claim against the Debtors or the Reorganized Debtors for Tax Year 2003 or any later year or any part thereof, including, without limitation, any Claim based on alleged nexus or minimum

contacts between the State and any Reorganized Debtor, any tax, interest or penalty related to Royalty income or Royalty deduction, and any tax, interest or penalty for failing to file an income, franchise, gross receipts or similar tax return, or with respect to the adequacy (or inadequacy) and correctness (or incorrectness) of any return filed or to be filed by the Reorganized Debtors. For avoidance of doubt, the Reorganized Debtors will pay any tax and interest shown as owing on any amended returns filed for Tax Year 2003 as described in paragraph 6.a.

c. With respect to the Reorganized Debtors' state income, franchise, gross receipts or similar tax returns, including any amended returns, for Tax Year 2003 or Tax Year 2004 or any part thereof, that have been, or will be, filed with disclosure statements substantially in the form set out in **Exhibit B**, the State will not treat the Reorganized Debtors as having failed to file a return or as having filed a false or late or improper return and will not claim any tax, interest or penalties based on the use of such language in Exhibit B, or substantially similar language, including any claim of a failure to file or a false or late or improper return.

d. To the extent there was a net loss in any of the Reorganized Debtors for any Tax Year ending on or before December 31, 2002, the Reorganized Debtors will not apply such loss to reduce taxable income in any Tax Year beginning on or after January 1, 2003. To the extent there are any net losses in any of the Reorganized Debtors in Tax Years 2003 or 2004, the Reorganized Debtors will not apply those losses to reduce taxable income in Tax Year 2002 or any earlier year. Notwithstanding same, the entire amount of any loss for any Tax Year ending on or before December 31, 2002, that would be carried forward to Tax Year 2004 under the State's tax rules as generally applied, and

any loss for Tax Years 2003 and 2004, may be used by the Reorganized Debtors in calculating their tax attribute reduction under the cancellation of indebtedness rules (as generally applied for Tax Years ending in or at the end of 2004). The existence and amount of the loss used in applying the cancellation of indebtedness rules shall not be subject to challenge by the State.

e. The intercompany receivables and payables by and among the Reorganized Debtors, that were expunged upon the effective date of the Plan, and the expungement of such receivables and payables, will be disregarded for income tax purposes.

f. The Reorganized Debtors' state income, franchise, gross receipts or similar tax returns, including any amended returns, for Tax Year 2003 and Tax Year 2004 and any part thereof, shall be subject to audit to ensure that any determinations of tax or of income, deductions, credits, or other items are consistent with applicable state law, except that:

(i) The State will not assert the adequacy (or inadequacy) of MCI's Books and Records as the basis for any Claim, demand, tax, interest, penalty or adjustment. However, for avoidance of doubt, the State may question the amount and tax treatment of items of income, deduction, credit or other tax-relevant items, and MCI's Books and Records may be used by MCI and by the State to establish the correct amount and tax treatment of any such items;

(ii) Any item of income, deduction, credit, or other item that is reported by the same entity for tax purposes and for financial accounting purposes will not be challenged as belonging to a different entity; and

(iii) The amount of any tax attribute as of January 1, 2003, including, without limitation, carryforward amounts, net intercompany payables and receivables, and tax basis, that is consistent with tax returns as filed for Tax Years ending before January 1, 2003, will not be challenged.

For avoidance of doubt, (x) a tax accounting method may be addressed on its merits and will not be deemed correct solely because it was used by the Debtors or Reorganized Debtors for Tax Years ending on or before December 31, 2002, (y) the treatment of and amount of any losses shall be as provided in Section 6.d. above, and the treatment of any intercompany payables and receivables that were expunged upon the effective date of the Plan shall be as provided in Section 6.e. above, and (z) any adjustment agreed for federal income tax purposes for Tax Years 2003 or 2004 shall be properly reflected in all State tax returns.

g. The State will not assert any tax, interest, penalty or other Claim in any Tax Year based on an argument that the Books and Records for any Tax Year ending on or before December 31, 2002, were adequate or inadequate. However, for avoidance of doubt, the State may question the amount and tax treatment of items of income, deduction, credit or other tax-relevant items, and MCI's Books and Records may be used by MCI and by the State to establish the correct amount and tax treatment of any such items.

h. The State will not use the Royalty Program, nor any Royalties paid or accrued in connection therewith, as a basis to assert the existence of any nexus or minimum contacts between the State and any Reorganized Debtor, in order to assert any Claims against the Reorganized Debtors, or for any other purpose.

7. Treatment of Intercompany Mergers, Liquidations and Consolidations. The Reorganized Debtors will treat intercompany mergers, liquidations and consolidations that took place during Tax Year 2004 consistently on state and federal tax returns. Any merger, liquidation or consolidation that is treated as tax-free or as a carry-over basis tax deferred transaction for federal income tax purposes, including determinations after audit by the IRS, will be treated as tax-free or as a carry-over basis tax deferred transaction for State tax purposes.

8. Settlement Payment and Releases. In consideration of the release from the State and the other terms of this Agreement, and in full and complete satisfaction of the Additional Claims, MCI (on behalf of itself and the other Reorganized Debtors) will pay the following amounts and transfer the following property as payments of tax and interest, to or on behalf of the State:

(i) One Hundred Million and 00/100 Dollars ($100,000,000.00) to the State;

(ii) Fourteen Million and 00/100 Dollars ($14,000,000.00) in counsel fees and costs to Joseph C. Langston and Timothy R. Balducci of The Langston Law Firm, P.A., tax i.d. number 64-0867806, acting as Special Assistant Attorneys General for the State;

(iii) Four Million Two Hundred Thousand and 00/100 Dollars ($4,200,000.00) to the Children's Justice Center of Mississippi; and

(iv) The WorldCom real property described on Exhibit C hereto.

The payments will be made within 1 day after the Effective Date. The WorldCom real property will be transferred by quitclaim deed, "as is, where is," including land, improvements and

fixtures in place, without any imposition of transfer taxes as provided under Section 13.04 of the Plan, as soon as practicable after the Effective Date. The payment for the Children's Justice Center will be made to a 501(c)(3) entity designated by the Attorney General. In exchange for the cash payments and property transfer, the State agrees to compromise and fully release the Reorganized Debtors' obligation to pay all taxes, interest, and penalties relating to the Royalty Program. The State further agrees that the release afforded herein is a complete and absolute release as to the Released Parties defined herein. Notwithstanding same, the State maintains that its losses and damages relating to the Royalty Program are not satisfied in full and the State retains all legal rights to pursue recovery of said losses and damages from third parties who are not Released Parties, subject to the provisions of this Agreement, including subparagraphs 8(a) and 8(b) below.

(a) The Parties agree that the Released Parties shall not be required to make any additional payments, to any person or entity, that relate in any way to or arise out of Claims relating to any or all of the Additional Claims or the Royalty Program which the State may have against persons or entities who are not Released Parties ("non-Released Party"). Accordingly, if the State asserts a Claim against a non-Released Party relating to any or all of the Additional Claims or the Royalty Program, and prevails on such a Claim in a final, non-appealable judgment, or settles such a Claim, the State agrees not to collect or execute on such award or judgment or settlement amount until any and all issues of indemnification or contribution have been fully and finally resolved (including final resolution of any appeals) between the non-Released Party and the Released Parties. The State further agrees that to the extent the non-Released Party obtains a judgment against any of the Released Parties relating to any or all of the Additional Claims or the Royalty Program, or settles such a Claim with any of the Released

Parties, the State will voluntarily reduce the amount it is entitled to receive from such non-Released Party so as to eliminate any right by such non-Released Party to recover from the Released Parties, provided that if any of the Released Parties wish to settle an indemnification or contribution Claim brought by a non-Released Party relating to any or all of the Additional Claims or the Royalty Program, the Released Parties shall be precluded from settling same without the express written approval of the State, such approval not to be unreasonably withheld. The Released Parties agree to use their reasonable best efforts to defend against any indemnification or contribution Claim against them by a non-Released Party if any such Claim is made. The State will have no responsibility to reimburse the Released Parties for their defense-related costs in any such indemnification or contribution Claim against any of the Released Parties by a non-Released Party.

(b) If paragraph 8(a) is not effective in completely eliminating any right by such non-Released Party to recover from the Released Parties, the State agrees to take such steps as may be required to produce the same result, including but not limited to assigning and transferring to the Released Parties the proceeds or the right to control or obtain the proceeds of any judgment, verdict, award, other relief or settlement the State obtains from or against such non-Released Party.

9. No Admission. It is understood by the Parties that this Agreement is a compromise of disputed Claims and defenses. Nothing herein shall be construed as an admission or other statement against interest, or of liability or wrongdoing by any Party, and the Reorganized Debtors shall not be required to make any admission of liability or wrongdoing.

10. No Penalty. The Reorganized Debtors shall not be required to make any payment of any fine or penalty, and no part of the Settlement Payment is a fine or penalty.

11. No Consistency Requirement. Nothing in this Agreement shall prevent the Reorganized Debtors from taking any position with the federal government, including the IRS, with any private party, or with any state that is not a party to this Agreement, even if such position might be, or appear to be, inconsistent with one or more terms or provisions of this Agreement. Notwithstanding same, the Reorganized Debtors covenant and agree not to take any position inconsistent with any provision of this Agreement in any administrative or legal proceeding involving the State of Mississippi, its divisions, agencies, agents, officials, officers, employees, representatives, servants, constituents, and assigns, versus KPMG, or any of KPMG's individual partners, merger partners, parents, subsidiaries, divisions, employees, servants, companies, corporations, limited liability corporations, ventures, partnerships, shareholders, managers, agents, directors, officers, affiliates, representatives, licensees and assigns; or the law firm of Brunini, Grantham, Grower & Hewes, or any of their individual partners, merger partners, parents, subsidiaries, divisions, employees, servants, companies, corporations, limited liability corporations, ventures, partnerships, shareholders, managers, agents, directors, officers, affiliates, representatives, licensees and assigns.

12. Release in Favor of Released Parties. Except for the obligations of the Reorganized Debtors expressly set forth in this Agreement, each of the Releasing Parties releases, disclaims and forever discharges each of the Released Parties from any and all Additional Claims.

13. Attorneys' Fees, Costs and Expenses. Except as expressly provided in Section 8(ii), each Party shall bear its own respective costs, expenses and attorneys' fees incurred in connection with or relating to the Claims, the Chapter 11 Cases, this Agreement, and otherwise.

14. Additional Documents and Acts. Each Party shall execute or procure and deliver to the other Parties such additional documents and shall perform such acts as shall reasonably be necessary to evidence or effectuate the terms of this Agreement.

15. Headings. The paragraph headings used in this Agreement are for convenience of reference only and do not in any way limit or amplify the terms and provisions hereof.

16. Complete Agreement. This Agreement constitutes a single, integrated written contract that expresses the entire agreement of the Parties with respect to the matters contained herein and supersedes all negotiations, prior discussions, and preliminary agreements, either oral or written. The Parties disclaim reliance on any and all prior agreements, representations, negotiations, and understandings, oral or written, express or implied. Any modification of this Agreement shall be effective only if it is in writing, is signed by the Party to be charged or otherwise adversely affected by it, and is approved by a final, non-appealable order of the Bankruptcy Court.

17. Binding Effect. This Agreement shall be binding upon and shall inure to the benefit of the Parties thereto, their predecessors, successors, parents, subsidiaries, affiliates, assigns, agents, directors, officers, employees, and shareholders.

18. Counterpart Signatures. This Agreement may be executed in any number of counterparts, each of which shall be deemed an original, but all of which, when taken together, shall constitute one and the same instrument. The Parties hereby agree that faxed signatures shall be as binding and enforceable as original signatures. This Agreement shall constitute a binding, enforceable agreement after all Parties have signed and executed this Agreement and after the Bankruptcy Court has entered a final, non-appealable order approving this Agreement.

19. Partial Invalidity. Each provision of this Agreement shall be valid and enforceable to the fullest extent permitted by law. If any provision of this Agreement or the application of such provision to any person or circumstance shall, to any extent, be invalid or unenforceable, the remainder of this Agreement, or the application of such provision to persons or circumstances other than those as to which it is held invalid or unenforceable, shall not be affected by such invalidity or unenforceability, unless such provision or such application of such provision is essential to this Agreement.

20. Interpretation of Agreement. In interpreting this Agreement, each of the Parties expressly agrees that the Agreement was prepared by the Parties jointly, and that no ambiguity shall be resolved against any Party on the basis that it was responsible, or primarily responsible, for having drafted the Agreement. Each of the Parties acknowledges that it did not execute this Agreement under duress and was represented by competent counsel in connection with this Agreement. Whenever the context so requires: (a) all words used in the singular shall be construed to have been used in the plural (and vice versa); (b) each gender shall be construed to include any other genders; (c) the word "person" shall be construed to include a natural person, a corporation, a firm, a joint venture, a trust, an estate, a governmental entity, or any other entity; and (d) the words "and" as well as "or" shall be construed either disjunctively or conjunctively as necessary to bring within the scope of any provision of this Agreement any person, entity, right, obligation or concept which might otherwise be construed to be outside the scope of such provision.

21. No Waiver. No delay or omission in the exercise of any right or remedy shall impair such right or remedy or be construed as a waiver. A consent to or approval of any act shall not be deemed to waive or render unnecessary consent to or approval of any other or

subsequent act. Any waiver of a default under this Agreement must be in writing and shall not be a waiver of any other default concerning the same or any other provision of this Agreement.

22. Governing Law. This Agreement, and all of the documents and instruments executed and delivered in connection with this Agreement, shall be governed by and construed under the internal laws of the State of New York (without regard to conflicts of law rules), except that (a) issues of tax law shall be governed by Mississippi law, and (b) issues of bankruptcy law shall be governed by federal law.

23. Authority to Execute Agreement. Each person or entity executing this Agreement represents that he/she/it is authorized to execute this Agreement. Each person executing this Agreement on behalf of a Party represents that he or she is authorized to execute this Agreement on behalf of such Party. For avoidance of doubt, the person or entity executing this Agreement on behalf of the State represents that it is authorized to execute this Agreement on behalf of the State, as defined above, including but not limited to the Mississippi State Tax Commission.

IN WITNESS WHEREOF, the Parties or their duly authorized representatives have executed this Agreement, consisting of 19 pages (including this signature page, but excluding exhibits).

MCI, INC. (ON BEHALF OF ITSELF AND THE REORGANIZED DEBTORS)

By: _____
Carol Ann Petren

Its: Senior Vice-President and Deputy General Counsel

STATE OF MISSISSIPPI

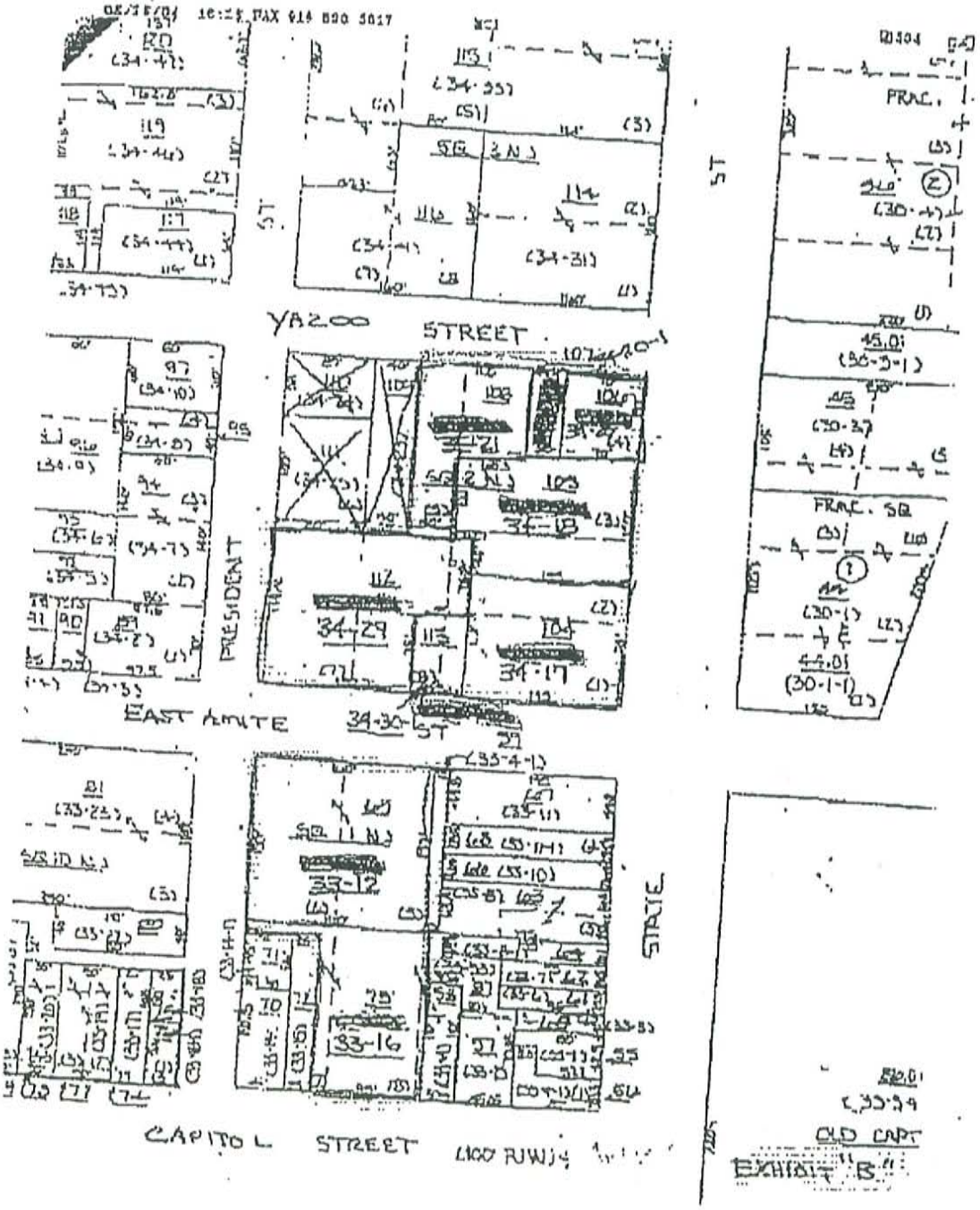
By: _____
Jim Hood

Its: Attorney General

EXHIBIT "A"

DESCRIPTION OF THE PROPERTY

Parcel #33-12 along with the following Parcels:
Parcel #33-16, Parcel #34-17, Parcel #34-18.
Parcel #34-20, Parcel #34-20-1, Parcel #34-21,
Parcel #34-29, Parcel #34-30-1. The Property includes the real property located at 515 East Amite Street, 229 North State Street, 523 Yazoo Street, 514 East Amite Street, 517 East Yazoo Street, 203 North State Street and 508 East Amite Street as depicted on Exhibit "B" attached hereto.
Parcel #33-4-1


YA200 STREET
PRESIDENT
EAST AMITE
CAPITOL STREET
STATE
FRAC.
FRAC. SQ
OLD CAPT
EXHIBIT "B"

06/18/04 18:18 FAX 916 600 5817 XCI 006

EXHIBIT "B"

HE:

PARCEL NUMBER
33-12

LTR101A

NAME: WORLDCOM MANAGEMENT CO INC
ADDRESS: 515 E AMITE ST
JACKSON MS 39201
LOCATION: 515 E AMITE ST

TAX DISTRICT 26
SUBDIVISION NO.
2733

CL	TRUE VAL	ASSD VAL	C. ACR	CULT VAL	IMPROVE	UC. ACR	UC. VAL	TOT ACR	EX
1									
2									
7	STO								15

LEGAL DESC: LOTS 5 & 6 LESS 10 FT N END PO 1 N J

DOES THIS AFFECT HOMESTEAD EXEMPTION ? (Y/N): _ NEXT SCREEN: 2 EXIT----> _

INQUIRY--F1=GO BACK TO MENU F2=GO TO NEXT SCREEN

HE:

PARCEL NUMBER
33-16

LTR101A

NAME: LODS II INC
ADDRESS: P O BOX 23397
JACKSON MS 39225 3397
LOCATION: E CAPITOL ST

TAX DISTRICT 26
SUBDIVISION NO.
2733

CL	TRUE VAL	ASSD VAL	C. ACR	CULT VAL	IMPROVE	UC. ACR	UC. VAL	TOT ACR	EX
1									
2									
7	STO								15

LEGAL DESC: LOT 8 & 5 FT N END LOTS 1 & 2 & 15 FT S/S LOT 7 & A 10 FT ALLEY N END LOT 7 BO 1 N J

DOES THIS AFFECT HOMESTEAD EXEMPTION ? (Y/N): _ NEXT SCREEN: 2 EXIT----> _

INQUIRY--F1=GO BACK TO MENU F2=GO TO NEXT SCREEN

RE:
PARCEL NUMBER
34-17

NAME: LDDB_II_INC
ADDRESS: 500_CLINTON_CENTER_DR
CLINTON_MS_39056
LOCATION: 203 N STATE_ST

LTR101A
TAX DISTRICT 26
SUBDIVISION NO.
2734

CL	TRUE VAL	ASSD VAL	C. ACR	CULT VAL	IMPROVE	UC. ACR	UC. VAL	TOT ACR
1								
2	341070	51161		45906	2255			
T	341070	51161		$5906	2255			

LEGAL DESC: 130_FT_W/S_N_STATE_ST_X_143_FT_W/S_WHITE_ST_
PT_LOTS_1_&_2_SQ_2_N_J_LESS_10_FT_TO_STREET

DOES THIS AFFECT HOMESTEAD EXEMPTION ? (Y/N): _ NEXT SCREEN: 2 EXIT----> _

INQUIRY--F1=GO BACK TO MENU F2=GO TO NEXT SCREEN

RE:
PARCEL NUMBER
34-18

NAME: LDDB_II_INC
ADDRESS: P_O_BOX_23397
JACKSON_MS_39225_3397
LOCATION: N STATE_ST

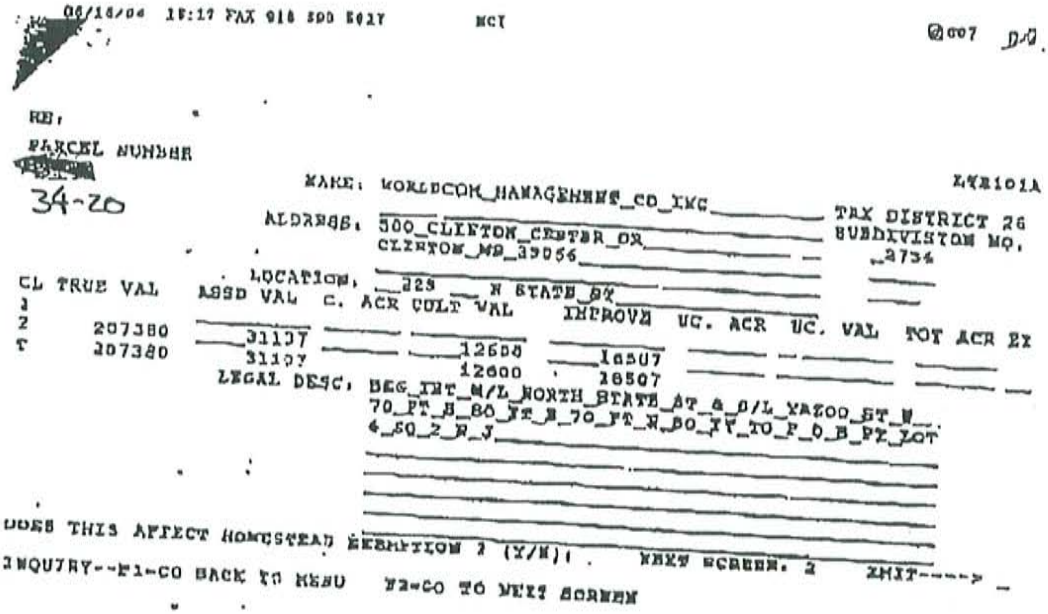
LTR101A
TAX DISTRICT 26
SUBDIVISION NO.
2734

CL	TRUE VAL	ASSD VAL	C. ACR	CULT VAL	IMPROVE	UC. ACR	UC. VAL	TOT ACR
1								
2								
T		STO						15

LEGAL DESC: N_1/2_LOT_2_LESS_20_FT_W_AND_S_LOT_3_LESS_S_
FT_N_&_S_X_60_FT_E_&_W_IN_NW_COR_SD_2_N_J

DOES THIS AFFECT HOMESTEAD EXEMPTION ? (Y/N): _ NEXT SCREEN: 2 EXIT----> _

INQUIRY--F1=GO BACK TO MENU F2=GO TO NEXT SCREEN



06/16/04 15:17 FAX 918 599 5027 MCI @007 DO

RE:
PARCEL NUMBER
[redacted]
34-20

MAKE: WORLDCOM MANAGEMENTS CO INC LTR101A
ADDRESS: 500 CLIFTON CENTER DR TAX DISTRICT 26
CLINTON MS 39056 SUBDIVISION NO.
LOCATION: 223 N STATE ST 2734

CL	TRUE VAL	ASSD VAL	C. ACR	CULT VAL	IMPROVE	UC. ACR	UC. VAL	TOT ACR	EX
1									
2	207380	31107		12600	18507				
T	207380	31107		12600	18507				

LEGAL DESC: BEG INT N/L NORTH STATE ST & E/L YAZOO ST N
70 FT E 80 FT S 70 FT W 80 FT TO P O B PT LOT
4 SQ 2 N J

DOES THIS AFFECT HOMESTEAD EXEMPTION ? (Y/N): NEXT SCREEN: 2 EXIT----->
INQUIRY--F1=GO BACK TO MENU F2=GO TO NEXT SCREEN

RE:
PARCEL NUMBER
[redacted]
34-20-1

MAKE: WORLDCOM MANAGEMENT CO INC LTR101A
ADDRESS: 515 E AMITE ST TAX DISTRICT 26
JACKSON MS SUBDIVISION NO.
LOCATION: 523 YAZOO ST 2734

CL	TRUE VAL	ASSD VAL	C. ACR	CULT VAL	IMPROVE	UC. ACR	UC. VAL	TOT ACR	EX
1									
2	84360	12671		7200	5451				
T	84360	12671		7200	5451				

LEGAL DESC: BEG INT N/L NORTH STATE ST & E/L YAZOO ST N
70 FT TO POB N 30 FT E 80 FT S 30 FT W 80
FT TO POB PT LOT 4 SQ 2 N J

DOES THIS AFFECT HOMESTEAD EXEMPTION ? (Y/N): NEXT SCREEN: 2 EXIT----->
INQUIRY--F1=GO BACK TO MENU F2=GO TO NEXT SCREEN

RE:

PARCEL NUMBER

34-21

NAME: WORLDCOM MANAGEMENT CO INC LTR101A

ADDRESS: 500 CLINTON CENTER DR TAX DISTRICT 26
CLINTON MS 39056 SUBDIVISION NO.
2736

LOCATION: 517 21 YAZOO ST

CL	TRUE VAL	ASSD VAL	C. ACR	CULT VAL	IMPROVE	UC. ACR	UC. VAL	TOT ACR	EX
1									
2	265400	42810		26055	16755				
T	265400	42810		26055	16755				

LEGAL DESC: 60 FT W HWD LOT 6 B 1/2 LOT 5 & 6 STRIP 5 FT
E 60 FT M/S LOT 3 BO 2 M J

DOES THIS AFFECT HOMESTEAD EXEMPTION ? (Y/N): _ NEXT SCREEN: 2 EXIT----> _

INQUIRY--F1-GO BACK TO MENU F2-GO TO NEXT SCREEN

RE:

PARCEL NUMBER

34-29

NAME: LODS XI INC LTR101A

ADDRESS: P O BOX 23397 TAX DISTRICT 26
JACKSON MS 39225 3397 SUBDIVISION NO.
2736

LOCATION: 508 D AMITE ST

CL	TRUE VAL	ASSD VAL	C. ACR	CULT VAL	IMPROVE	UC. ACR	UC. VAL	TOT ACR	EX
1									
2									
T		870						15	

LEGAL DESC: BEG INT N/L AMITE ST & E/L N PRESIDENT ST E
149.42 FT E 126.5 FT N 4.7 FT E 50.5 FT S
75.2 FT W 63 FT S 75 FT W 137.17 FT TO POB FT
LOTS 2 7 & E 50 2 M J

DOES THIS AFFECT HOMESTEAD EXEMPTION ? (Y/N): _ NEXT SCREEN: 3 EXIT----> _

INQUIRY--F1-GO BACK TO MENU F2-GO TO NEXT SCREEN

06/16/04 16:17 FAX 918 580 0817 MCI 008 D.0

RE:
PARCEL NUMBER
34-30-1

NAME: WORLDCOM MANAGEMENT CO INC LTR101A
ADDRESS: 500 CLINTON CENTER DR TAX DISTRICT 26
CLINTON MS 39056 SUBDIVISION NO.
2734
LOCATION: 614 N ANITA ST

CL	TRUE VAL	ASSD. VAL	C. ACR	CULT VAL	IMPROVE	DC. ACR	DC. VAL	TOT ACR	EX
1									
2	153680	23052		12657	10395				
T	153680	23052		12657	10395				

LEGAL DESC: BEG 140 FT W OF N STATE ST N 85 FT W 65 FT S 85 FT E 65 FT TO PT OF BEG PT LOTS 1 & 2 IN 60 2 N J LESS 10 FT FOR STREET

DOES THIS AFFECT HOMESTEAD EXEMPTION ? (Y/N): _ NEXT SCREEN: 2 EXIT----> _

INQUIRY--F1=GO BACK TO MENU F2=GO TO NEXT SCREEN

EXHIBIT A
MISSISSIPPI NON-ROYALTY CLAIMS -- EXCLUDED
April 24, 2005

Creditor	Debtor	Claim Number	Type	Total Claim
Mississippi State Treasurer	WorldCom, Inc.	N/A	Unclaimed Property	364,665.59
Mississippi Corporate Income and Franchise	Intermedia Communications, Inc.	N/A		6,174.00
State of Mississippi	MCIMetro Access Transmission Services	N/A		3,148.00
Mississippi Department of Information Technology Services	WorldCom, Inc.	12435	Lease Payments	62,870.48

Exhibic B

WORLDCOM, INC. & AFFILIATES
EIN: 58-1521612

ATTACHMENT TO (AND A PART OF) RETURN (FORM MS 83-105)

This statement is being attached to this return to disclose certain accounting matters relating to its preparation and content. This return (including the attestation) is subject to, and qualified in its entirety, by the qualifications made in this statement.

The predecessor of MCI, Inc. (WorldCom, Inc.) and many of its subsidiaries (collectively "MCI") entered bankruptcy on July 21, 2002. One of the conditions for MCI to emerge from bankruptcy was for the books and records to be corrected so as to permit the issuance of restated financial statements. Because of MCI's size and complexity, the restatement process was extremely difficult. The process was recently completed, and MCI emerged from bankruptcy on April 19, 2004.

Despite the tremendous effort that went into the restatement, the restatement entries and all other entries on the general ledger were only validated on a consolidated basis. In other words, the restated financials permit MCI to issue consolidated financial statements and to file a consolidated Federal income tax return.

Accurate and reliable separate entity financial statements for 2003 do not exist, and the data in MCI's financial system are an unreliable base from which to prepare accurate 2003 separate legal entity financial statements.

This return is based on the available information, as set forth in MCI's books and records, subject to the concerns set forth above. This information may overstate items for some MCI entities and understate the items for other MCI entities. This could result in an overstatement or understatement of tax, in the aggregate, for the MCI entities included in this return. In consideration of MCI's difficulty in determining the precise amount owed based on its books and records, the non-income-based portion of the tax was increased by 10% over the amount of such portion as shown on the return in determining the amount credited with this return.

MCI is filing returns based on this information because it recognizes its responsibility to file timely returns, and because no more accurate alternative is available.

When the MCI entities filed their 2001 and 2002 returns, a disclosure statement was included that stated, among other things, that it was MCI's intention to file amended returns when the process of restating its books was complete. However, the results of the restatement do not provide a basis for such amended returns to be filed.

MCI would welcome the opportunity to discuss this matter with you further, provide any additional information that you need, cooperate in an audit of current or past returns, or proceed in any other manner that you see fit.

Attorney General Hood's Formal Comments

STATE OF MISSISSIPPI

JIM HOOD
ATTORNEY GENERAL

October 16, 2006

Honorable Phil Bryant
Auditor, State of Mississippi
501 North West Street, Ste. 801
Jackson, MS 39201

Re: WorldCom Partial Settlement

Dear Phil:

In response to your report, I respectfully request that you carefully review several crucial legal errors, correct several factual errors, and delete the unauthorized conclusions in said report. In sum, since the attorneys fees paid by WorldCom were not state funds and neither section 7-5-5 nor any other law contain any requirement that attorneys fees be run through an appropriated account, this so-called "performance audit" should be reduced to its legal significance - a letter from the auditor to the governor. I look forward to an opportunity to further discuss my recommendations with you.

Although your report purports to be a "performance audit", it is not. It is merely a legal opinion. The recommendations for better performance in your first and second draft reports indicate that the report started out as a "performance audit". However, the new report prepared at the behest of Governor Haley Barbour contains preconceived facts and conclusions.

Pursuant to statute, you may "study and analyze existing managerial policies, methods, procedures, duties and services of the various state departments . . . to determine whether and where operations can be eliminated, combined, simplified and improved." MCA § 7-7-211 (c) (Supp. 2006). For instance, you could have conducted a performance audit to determine whether allowing the AG to contract on a contingency basis is good "policy". You have no authority, however, to author a legal interpretation of two statutes to reach a legal conclusion that one applies and one does not, in order to reach the conclusion that the AG had no legal authority to allow MCI to pay the Special Assistant Attorneys General. That is a legal opinion, which exceeds your statutory authority and your expertise.

LEGAL ERRORS

Even if you had authority to make the conclusions in your report, they are wrong.
For example, you wrongly conclude that section 7-5-5 does not apply because it "allows the Attorney General to determine the amount of legal fees for private lawyers only when they are retained to defend claims against the State. . . .". Footnote 2, page 3; emphasis in your report. However, this alleged defense restriction only applied to 3 of the assistants, and in any case was removed by the Legislature in 1970. That amendment to the statute (Miss. Laws 1970, Ch.

348 § 3) clarified that all assistant and special assistant attorneys general could bring suits on behalf of the state.[1]

Your opinion also ignores the fact that the use of a contingency fee contract to collect taxes due the state was approved by the Mississippi Supreme Court in the case of ***Pursue Energy Corp. V. Mississippi State Tax Commission, et al***, 816 So.2d 385, 391 (Miss. 2002). After citing both sections 7-5-5 and 7-5-7, the Court held, "The statute places **no restrictions** upon the type of fee the Attorney General can negotiate, even though the Legislature **could have restricted the use of contingency fees** if it so desired." ***Id***. at 391. (Emphasis added).

It is ludicrous to argue that the Legislature granted the attorney general authority to enter into a contingency fee contract, but did not allow payment pursuant to the contract. By giving the attorney general the power to employ special assistants on a fee or contract basis and to be the sole judge of their compensation (7-5-5), and the power to appoint special counsel on a fee basis not to exceed recognized bar rates (7-5-7), the Legislature merely recognized that no appropriation of contingency fees was necessary since, in such cases, the complainant never receives the fee portion of the settlement. Rather, the fee remains the property of the attorneys. See ***Philip Morris, Inc. v. Glendening***, 349 Md. 660, 709 A.2d 1230 (Md.1998) (Attorneys' contingency fee is not "state" or "public" money subject to legislative appropriation) and ***State ex rel Nixon v. American Tobacco Company***, 34 S.W. 3d 122, 136 (Mo. 2000)(Statute allowing attorney general to hire assistants and pay them from appropriations does not prohibit attorney general in exercise of his common law power from entering into contingency fee arrangements, or agreements that provide for defendants sued by State to pay attorney fees directly to State's outside counsel).

The Legislature has killed several bills over the past few years attempting to take away the authority of the attorney general to enter into contingency fee agreements and to require appropriation for contingent fees. Your "report" adopts a version of the law which the Legislature has repeatedly rejected.

FACTUAL ERRORS

The most glaring factual error is that I recommended that WorldCom make a private donation to a non-profit. I made no such recommendation. After I had recovered the entire amount due to

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[1]The attorney general is hereby authorized, empowered, and directed to designate three (3) of the said assistant attorneys general to devote their time and attention primarily to defending and aiding in the defense in all courts . . . . When the circumstances permit, such assistants may perform any of the attorney general's powers and duties, including but not limited to engaging in lawsuits . . . . To further prosecute and insure such purposes, the attorney general is hereby further expressly authorized, empowered, and directed to **employ such additional counsel as special assistant attorneys general** as may be necessary or advisable, on a **fee** or **contract basis**; and the attorney general shall be the sole judge of the compensation in such cases. MCA § 7-5-5 (Supp. 2006)(emphasis added).

Mississippi, plus interest and the buildings, I then told WorldCom I wanted them to pay our attorneys' fees in addition to and over and above their settlement to the state. During those separate fee negotiations, WorldCom stated it wanted to make the contribution to some charity or non-profit as a good-will gesture to the people of Mississippi who lost money on WorldCom stock . WorldCom's attorneys proposed that if the state's lawyers would agree to take $14 million instead of the amount to which they were contractually entitled, then MCI would pay the extra attorneys' fee and an additional sum to the children's Justice Center. When they presented this to me, I told the attorneys that this was a matter between them and MCI, and the attorneys agreed to the MCI proposal. That is why the lawyers took less than what their contract provided.

Therefore, I respectfully request that you delete from the middle paragraph on page seven the sentence which states, "The Attorney General suggested that perhaps a charitable donation be made."

WorldCom initially suggested that they give money to the Office of Attorney General to distribute to Boys and Girls Clubs of Mississippi and three other children's crime prevention programs administered by this Office pursuant to legislative mandate. I stated that the money could exceed our spending authority and suggested that WorldCom give to another charity. When WorldCom suggested a contribution to the Children's Justice Center, I called one of our staff attorneys who was a volunteer for the Center to determine their needs. WorldCom chose the charity and the amount they gave. The private charitable contribution was not state money.

I respectfully request that you delete the next to the last sentence of the third paragraph on page five, where the report concludes that "after the initial portion of the settlement was reached." The settlement with the state was complete when the attorneys fees were negotiated. This is merely a preconceived conclusion. Every single witness has stated that the settlement was complete at the time WorldCom negotiated with the attorneys to pay the legal fees.

Assuming that you seek to overstep your authority and file an action to set aside the settlement agreement and sue our attorneys to deprive them of their fee, then they would be entitled to seek the equitable remedy of set-off and would stand to recover the additional fees and expenses owed under the contract. Furthermore, WorldCom could seek the return of its charitable contribution.

Corporate wrongdoers who are the targets of civil litigation by the office of the AG have seized on the Auditor's inquiry into the MCI resolution. In fact, at least one defendant in a civil matter being pursued on behalf of the state has withdrawn its offer to pay tens of millions of dollars to the state and cited the auditor's activities and the auditor's interpretation of various statutes as the basis for canceling the final settlement talks. Such will no doubt require further investigation by us. For the defendant to take comfort in how the auditor interprets various statutes clearly signals that we are not working on the same team. While my office is working to collect every dime possible from those who would seek to take advantage of Mississippians, should your office be issuing reports that are seemingly helpful to such defendants ? I think not. Your activities are having a direct and negative impact on our ability to hold civil defendants responsible for their actions detrimental to Mississippians.

It is respectfully submitted that your factual and legal errors be corrected and the improper conclusions be removed. If the report is published, then it should not be styled a performance audit, but a simple "fact" finding letter to the Governor. If you have any questions, please do not hesitate to contact me.

Sincerely yours,

Jim Hood
Attorney General

JMH/dhm