

Exhibit 5.

**Prof. Joseph Stiglitz on Corporate Conduct in
Alaska**

**(Supplement: Current Constitutional Budget
Reserve Fund Settlement Payments)**

***Questionable Accounting Practices and the
Importance of Audits***

Joseph Stiglitz on Corporate Conduct in Alaska
[Exhibit 5, Pages 1 & 2]

ADOR Fall 2012 Revenue Sources Book, p. 96
[Exhibit 5 Source, Sheet 1]

Questionable Accounting Practices and the Importance of Audits¹

The state's petroleum litigation history clearly demonstrates the importance of validating the revenue calculation starting point – particularly when transfer pricing from one arm of a company to another is involved.

In a 2007 study of multinational oil corporations and resource development, noted economist Joseph Stiglitz portrayed Alaska as the poster-child of corporate cheating. Stiglitz described his first-hand experience with Alaska – in royalty litigation during the 1980's – as follows:

“The prospects of cheating are very real and great, and can arise at every stage of the transaction. The government may get less for the lease than it should – there may even be attempts to restrict competition in bidding. Whatever the contract that has been signed, corporations are tempted to cheat – to pay less than they are supposed to – because the amount of money that can sometimes be made by doing so is so large. The occasions to cheat arise not just in developing countries. In the 1980s I worked on a case involving cheating by the major oil companies in Alaska. This oil-rich state had a mineral lease requiring the oil companies to pay at 12.5 percent of the gross receipts, less the cost of transporting the oil out from the far-flung site at Prudhoe Bay on the Arctic Circle. By overestimating their costs by just a few pennies per gallon (and multiplying those pennies by hundreds of millions of gallons) the oil companies would increase their profits enormously. They could not resist the temptation.

They also found other ways to cheat, such as selling their oil to their own subsidiaries, recording a lower than fair market value (see chapter 4); or using other subsidiaries to ship their oil out and then reporting fictionally high shipping cost. Each piece of the cheating was hard to detect, and government prosecutors had to analyze thousands of transactions- – at a cost of tens of millions of dollars. In the end, there was no doubt that cheating had occurred – and on a massive scale. There followed a series of settlements involving a whose who of global companies – including what are now BP, ExxonMobil and ConocoPhillips – for an amount in excess of 6 billion dollars.²

The \$6-billion estimate by Stiglitz was conservatively cast; state records compiled and reported on by this writer in 2003 showed that the Alaska Dept. of Law reported \$6.8 billion in oil and gas settlement payments for underpayments on taxes and royalties through 2001.³ Since that time,

¹ This exhibit has been updated from Richard A. Fineberg, *Establishing a Rational Foundation for Review, Formulation and Implementation of Alaska's Oil and Gas Fiscal Policy* (April 2011), Section VI., pp. 31-33, with data from the Alaska Department of Revenue's *Fall 2012 Revenue Sources Book*, p. 96.

² Joseph E. Stiglitz, “What Is the Role of the State?” Macartan Humphreys, Jeffrey D. Sachs and Joseph E. Stiglitz (eds.), *Escaping the Resource Curse* (Columbia Univ. Press, 2007), pp. 24-25 (footnotes omitted).

³ See: Richard A. Fineberg, ["Securing the Take: Petroleum Litigation in Alaska,"](#) in *Caspian Oil Windfalls: Who Will Benefit?* [New York: Open Society Institute, 2003], pp. 53-69 [Chapter 3]. (Stiglitz cited the author's 2003 compilation as the source for his statement that the state was short-changed and forced to litigate to recoup “in excess of 6 billion dollars.”)

Although I never met Prof. Stiglitz, while serving in the governor's office between 1987 and 1989 I worked on the royalty case that he discusses in this passage. During this period, in addition to serving with the governor's policy review team, I spent time with the state's contractual staff team tallying data on oil transactions; this experience enabled me to give first-hand information to the governor's policy review team. Given this common background, I can confirm the accuracy of Prof. Stiglitz's observations.

the Constitutional Budget Reserve Fund reports taking in another \$1.7 billion in oil and gas settlements, bringing the total revenue gained through petroleum litigation since Prudhoe Bay entered production to \$8.5 billion.⁴

Is trust or verification the wiser policy? It is difficult to answer this question because the critical facts about these settlements remain shielded behind the veils of taxpayer confidentiality and commercial propriety. However, the softness surrounding important numbers that have swirled around the current petroleum tax discussion suggest to me that at this time we do not have a firm grip on this issue. The following empirical indicators tip the scales toward verification:

- The Department of Law has put in a budget request for \$5 million for the coming fiscal year for outside counsel to assist with oil and gas litigation.⁵
- In my experience, litigation has typically yielded a pay-out on state investment conservatively estimated at 10:1.
- In 2006 and 2007, veteran state oil and gas personnel from the Departments of Revenue and Law assured me that the relatively large sums of money at issue in revenue disputes were a thing of the past – an historical artifact that reflected the fact that nation's largest oil field came on-line in the midst of the two significant price spikes of the 1970's, confronting both the industry and the state with a steep learning curve. Balanced against this sanguine historical interpretation is the fact that \$1.6 billion of the \$1.7 billion in litigation revenue collected since FY 2003 has been collected in the last six years.⁶ This six-year collection average of \$267.17 million per year represents a ten-fold increase over the period between 2003 and 2006.

– *Richard A. Fineberg*

⁴ *Fall 2012 Revenue Sources Book*, p. 96. (Under Article IX, Sec. 17 of the Alaska State Constitution, the state deposits all money received as a result of administrative proceedings or litigation on mineral lease payments or taxes on mineral income into this fund.)

⁵ Alaska Dept. of Law, "Oil and Gas Litigation (Non-Gasline)," Reference No. 51784, Feb. 16, 2011 [FY 2012 Governor Amended Capital Project Summary], pp. 1-2.

⁶ *Fall 2012 Revenue Sources Book*, p. 96. These figures do not include the settlement for revenue last due to the TAPS emergency shutdown in January 2011. Based on the settlement for this amount, the Revenue Department anticipates a deposit of \$255 million to the Constitutional Budget Reserve Fund from BP during FY 2013.

A-5a Total Petroleum Revenue—History
 (\$ million)

FY	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012
Unrestricted Petroleum Revenue										
Petroleum Corporate Income Tax	151.1	298.8	524.0	661.1	594.4	605.8	492.2	446.1	542.1	568.8
Oil and Gas Production Tax	589.8	642.7	854.9	1,191.7	2,198.3	6,810.9	3,100.9	2,860.7	4,543.2	6,136.7
Oil and Gas Hazardous Release	9.2	9.2	8.3	7.8	10.1	11.7	11.1	10.3	9.7	9.4
Oil and Gas Conservation	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Petroleum Property Tax	48.7	47.3	42.5	54.5	65.6	81.5	111.2	118.8	110.6	111.2
Oil & Gas Royalties	825.7	1,042.8	1,401.1	1,772.2	1,563.8	2,420.6	1,451.2	1,469.0	1,821.3	2,022.8
Bonuses, Rents & Interest	14.6	13.3	18.8	11.9	29.2	25.5	14.4	8.0	22.0	8.9
Total Unrestricted Petroleum Revenue	1,639.1	2,054.1	2,849.6	3,699.2	4,481.4	9,956.0	5,181.0	4,912.9	7,048.9	8,857.8
Restricted Petroleum Revenue										
NPR-A Rents, Royalties, Bonuses	34.6	2.5	31.6	4.5	12.8	5.2	14.8	21.3	3.0	4.8
Royalties to Permanent Fund	397.6	354.7	476.9	599.5	535.0	834.0	659.8	696.1	857.3	904.9
Royalties to Public School Fund	6.2	7.1	9.6	12.0	10.6	16.5	11.0	11.1	13.6	14.7
CBRF Deposits	22.3	8.4	27.4	43.7	101.9	476.4	202.6	552.7	167.3	102.1
Total Restricted Petroleum Revenue	460.7	372.7	545.5	659.7	660.3	1,332.1	888.2	1,281.2	1,041.2	1,026.5
Total Petroleum Revenue	2,099.8	2,426.8	3,395.1	4,358.9	5,141.7	11,288.1	6,069.2	6,194.1	8,090.1	9,884.3