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The Honorable Lyda Green, Co-Chair  
Senate Finance Committee  
State Capitol  
Juneau, AK 99801

Dear Senator Green:

Thank you for this opportunity to comment on draft "P" (4/16/06) of the proposed Senate Finance Committee Substitute for SB 305. We recognize significant effort has gone into this CS and thank you, your staff and the committee for their continued efforts. We offer the following comments for your consideration:

PPT Rate.

Oil: The proposed rate of 22.5% is an improvement from the 25% rate in the Resources CS, but it is still higher than the 20% in the original bill and considerably higher than the rate which we believe would be best for Alaska. Significant additional investment is urgently required to stem North Slope production decline. More investment, more production, more jobs, and the resulting benefits to the state economy are better for Alaska than short term increases in revenue. And more investment promises greater total state revenue in the long run. We therefore urge the Legislature to adopt an oil tax rate which is less than the 20% the Governor proposed.

Gas: A PPT tax rate of 1/3 that proposed for oil is appropriate for gas.

Progressivity. We remain firmly of the belief that progressivity, over and above that already provided by the PPT structure, is not appropriate for Alaska. However, should the Legislature insist progressivity be part of the solution, a structure based on net "production tax value" as proposed in the draft has merit and is better than those previously proposed which were based on gross value. The \$45/BOE trigger point should escalate annually for inflation.

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PPT Credits. The proposed 25% credit for capital expenditures is an improvement from the 20% in the previous versions of the bill. Increased credits will increase reinvestment in Alaska and is consistent with the need for significant additional investment urgently required to stem North Slope production decline.

Transitional Investment Expenditure (TIE) Credits (clawback). The 2-for-1 provision introduces a hurdle which the producers must overcome before they can take the benefit of the TIE credit. Nevertheless, we recognize this is consistent with the need for significant additional investment being urgently required to stem North Slope production decline and understand the driver behind the 2-for-1 provision. In order that we can reasonably expect to receive the benefit of the provision, we would request that you consider either lengthening the seven-year period or lowering the 2:1 investment ratio.

We also have two technical comments to simplify and clarify the administration of the PPT. We believe they are important because they will significantly reduce or avoid unnecessary disputes in the future about how it is supposed to work.

Definition of deductible “direct, ordinary, and necessary costs”. PPT deductions under AS 43.55.160(c)(1) must be “direct, ordinary, and necessary costs” for exploration and production, but nowhere is this phrase defined. Parts of it are defined — “direct costs” in AS 43.55.160(d)(1) and (2), and “ordinary and necessary” in AS 43.55.160(j)(2) — but these fragmentary definitions do not necessarily add up to define the whole. The lack of a definition for the whole phrase would leave a loophole for taxpayers or DOR to try to interpret it differently from the definitions of its individual parts.

Clarification of deductible costs “upstream of the point of production”. AS 43.55.-160(c)(1) also specifies that deductible lease expenditures are “total costs upstream of the point of production” of oil or gas. As AOGA recommended, this should be “total costs in support of activities upstream of the point of production” in order to avoid uncertainty and disputes over the deductibility of field costs not directly tie-able to any specific point or location along the flow of oil and gas from the reservoir to the point of production, such as helicoptering crew out to the platforms in Cook Inlet or lodging workers on the North Slope.

I hope these comments are clear and helpful in your deliberations. We remain available if we can be of any further assistance to the committee.

Yours Sincerely,

Angus J. Walker