

HB

128

(FILE 2)

HOUSE COMMITTEE REPORT

(9)

Date Referred to Committee: March 5, 2007

FURTHER REFERRALS: Finance

Date of Committee Action: 5/04/07

The RESOURCES Committee considered:

HB 128

HOUSE BILL NO. 128

OIL & GAS PRODUCTION TAX: EXPENDITURES

"An Act relating to allowable lease expenditures for the purpose of determining the production tax value of oil and gas for the purposes of the oil and gas production tax; and providing for an effective date."

Recommends it be replaced with HCS or CS for HB 128 (RES)
 For Senate Bills with new title: Technical Title New Title: HCR _____ Same Title New Title

- attach amendments
- add new referral to _____ Committee
- Letter of Intent _____ Committee

List of Abbrev for Depts.:
 ADM
 CED
 COR
 CRT
 EED
 DEC
 DFG
 GOV
 HSS
 LWF
 LAW
 LEG
 MVA
 DNR
 DPS
 REV
 DOT
 UA

<u>NEW FISCAL NOTES</u>				
*Assigned by Chief Clerk's Office				
List by Dept(s):	*FN#	Fiscal	Indet.	Zero
ADM		✓		
ADM				✓

<u>PREVIOUS FISCAL NOTES</u>				
List by Dept(s):	FN#	Fiscal	Indet.	Zero
DEC	1			✓
ADM	2	✓		
REV	3	✓		

<u>Signing with recommendations</u>	Printed Last Name	DP	DNP	NR	AM
<i>Paul K. Seaton</i>	SEATON				X
<i>Bo Edgmon</i>	EDGMON			X	
<i>John Johnson</i>	JOHNSON				X
<i>Bob Ross</i>	ROSS				X
<i>Peggy Wilson</i>	WILSON				X
Chair: <i>Craig Johnson</i>	Johnson				X
Chair: <i>John Gatto</i>	Gatto	X			

AMENDMENT

OFFERED IN THE HOUSE

TO: CSHB 128(O&G)

- 1 Page 3, lines 22 - 23:
- 2 Delete "the standard practices of the inuustry"
- 3 Insert "good oil field practice"

Adopted in HRES
3/23

AMENDMENT #1

OFFERED IN THE HOUSE

TO: CSHB 128(O&G)

- 1 Page 3, lines 22 - 23:
- 2 Delete "the standard practices of the industry"
- 3 Insert "good oil field practice"

5-21-07

Jonathan Iverson

Kevin Banks

Rob Beutz

Don Bullock → Rep. Seaton
question

ak

HB 128

Trevor Fulton

From: Jonathan Iversen [jonathan_iversen@revenue.state.ak.us]
Sent: Thursday, March 22, 2007 4:59 PM
To: Rep. Craig Johnson; Rep. Carl Gatto
Subject: Good oil field practice
Attachments: Good oil field practice.doc; goodoilfield.pdf

Per our conversation today, attached are a couple of definitions we found for good oil field practice.
Thanks,
Jon Iversen

U.S.

California Department of Conservation:

14 CCR § 1774

(e) Pipelines shall be designed, constructed, tested, operated, and maintained in accordance with good oil field practice and applicable standards, such as the American Petroleum Institute (API) (API Rec. Prac. 1110, 3rd Ed., Dec. 1991, and API Spec. effective 1990) or American Society for Testing and Materials (ASTM) (ASTM Designation Stand. Spec., 1991), Code of Federal Regulations 49, Part 192, or other applicable standards for the transportation of oil, gas, produced water, and other fluids.

Good oilfield practice includes, but is not limited to:

- (1) Utilization of preventative methods such as cathodic protection and corrosion inhibitors, as appropriate, to minimize external and internal corrosion.
- (2) Employment, where practical, of equipment such as low-pressure alarms and safety shut-down devices to minimize spill volume in the event of a leak.
- (3) Evaluating the applicability of locating any new pipelines or parts of a pipeline system that are being relocated or replaced above ground.

The use of pipe clamps or screw-in plugs are not considered good oilfield practice for permanent repair of pipeline leaks.

International:

Albania:

1. good oil field practices means practices which are generally accepted in the international petroleum industry as good, safe, economical and efficient."

The second looks like it was adopted by the European Union in regulations this year in the "Hydrocarbons Prospecting, Exploration and Exploitation law"

2. good oil field practices means all those activities that are generally accepted as good, safe, and efficient in the carrying on of hydrocarbon operations, and in accordance with generally accepted practices in the international petroleum industry.

CONCEPTUAL AMENDMENT 1

OFFERED IN THE HOUSE

TO: CSHB 128(O&G)

1 Page 3, lines 21 - 22:

Delete "Alaska Oil and Gas Conservation Commission"

2 Insert "person in the Department of Natural Resources who is the lead person for
3 exercising oversight over the maintenance of oil and gas facilities, equipment, and
4 infrastructure in the state"

Konrad Jackson

From: John Norman [John_Norman@admin.state.ak.us]
Sent: Wednesday, April 25, 2007 11:36 AM
To: Konrad Jackson
Cc: Cathy P Foerster; Dan T Seamount; Kevin R Banks
Subject: Re: HB 128 / SB 80 Amendments
Attachments: John_Norman.vcf

Dear Konrad,

We believe this amendment will simplify and improve the bill. AOGCC is one of the agencies named in Administrative Order No. 234 so we will still be able to provide advice and recommendations to Revenue through PSIO with DNR as lead agency. This will allow us to supply expertise from our area of regulatory oversight within a framework that facilitates coordination with other state agencies.

Thanks for checking with us and please let me know if you or Representative Olson have questions.

John

Konrad Jackson wrote:

Dear Mr. Norman,

As with Senator Wagoner's proposed amendment to SB 80 that would remove the AOGCC and replace it with the PSIO, Representative Olson will be offering the same amendment to HB 128 in House Resources.

I wanted to drop a quick note to inform you of his intentions and get any comments you may have in regards to this amendment.

Thank you for your time.

Konrad Jackson
Staff to Representative Kurt Olson
Phone: 907-465-2693
Fax: 907-465-3835



Sarah Palin
GOVERNOR

STATE OF ALASKA
OFFICE OF THE GOVERNOR
JUNEAU

April 18th, 2007

ADMINISTRATIVE ORDER NO. 234

I, Sarah Palin, Governor of the State of Alaska, under the authority of art. III, secs. 1 and 24, of the Alaska Constitution, and AS 44.17.060, name the commissioner of the Department of Natural Resources as the coordinator of oversight of facilities, equipment, infrastructure, and activities designed to explore for, produce, process, or transport oil and natural gas from, across, or within state oil and natural gas units or leases. This Order authorizes and directs increased and assertive oversight activities on state oil and natural gas units and leases by the Department of Natural Resources. These oversight activities include all activities relating to all facilities, equipment, and infrastructure. This Order also provides for coordination among state agencies of oversight on oil and natural gas matters on state land.

Nothing in this Order affects the authorities or responsibilities of state agencies with permitting, authorization, or oversight authority over oil and natural gas activities on state oil and natural gas units and leases, including advocacy by the Department of Law before the Federal Energy Regulatory Commission and state regulatory commissions, the development of fiscal terms under AS 43.82 or any later-enacted statute on development of such fiscal terms, or construction and maintenance of surface and air transportation infrastructure by the Department of Transportation and Public Facilities under other legal authority.

FINDINGS

1. It is in the best interests of the people of this state and the nation that oil and natural gas exploration, production, and transportation facilities within this state be designed, constructed, operated, and maintained in a safe and environmentally sound manner. Oversight by state agencies with legal jurisdiction over the facilities, equipment, infrastructure, and activities designed to produce and transport oil and natural gas must be efficient, effective, and capable of ensuring compliance with state law.
2. It is in the best interests of the people of this state and the nation that oil and natural gas infrastructure in this state be designed, constructed, operated, and maintained to minimize the economic impacts to ongoing functions of state government caused by unplanned interruptions or reductions in oil and natural gas production in this state.
3. It is in the best interests of the people of this state and the nation that oil and natural gas infrastructure be maintained to avoid premature abandonment, which would

cause waste of the state's resources.

4. It is in the best interests of the people of this state to utilize existing state government structures and processes to the maximum extent possible, and to effectively coordinate all state resources associated with oversight of facilities, equipment, infrastructure, and activities designed to produce oil and natural gas from state oil and natural gas units and leases.
5. The Department of Natural Resources has the authority under AS 38.05 and AS 44.37.020(a), and under state oil and natural gas leases, to exercise oversight of all oil and natural gas facilities, equipment, infrastructure, and activities on state oil and natural gas units and leases.

ORDER

To further these findings, I, Sarah Palin, Governor of the State of Alaska, order and declare the following:

1. In regard to matters other than those relating to the development, and adoption or issuance, of regulations, standards, permits or other authorizations under federal, state, or local law, or to facilities subject to the United States Federal Highway Administration or the United State's Federal Aviation Administration oversight, the commissioner of the Department of Natural Resources is the lead official for communication and coordination with appropriate federal agencies, and with local governments, related to oversight of oil and natural gas exploration, production, and transportation on state oil and natural gas units and leases. The commissioner of the Department of Natural Resources may delegate duties under this Order to a qualified designee from the Department of Natural Resources.
2. The commissioner of the Department of Natural Resources is the lead official for communication and coordination among the following Designated Agencies regarding oil and natural gas infrastructure and activities on state oil and natural gas units and leases: Department of Environmental Conservation; Department of Fish and Game; Department of Public Safety; Department of Revenue; Department of Transportation and Public Facilities; Department of Labor and Workforce Development; Department of Law; Department of Natural Resources; Alaska Oil and Gas Conservation Commission; and the director in the Governor's Office in Washington, D.C.
3. The commissioner shall establish a Petroleum Systems Integrity Office (PSIO) and designate a Petroleum Systems Integrity Office Coordinator (PSIOC). The PSIOC is the lead state official in exercising oversight of the maintenance of facilities, equipment, and infrastructure for the sustained production and transportation of oil and natural gas resources in this state, including such facilities, equipment, and infrastructure not currently within the jurisdiction of a Designated Agency.
4. Each Designated Agency shall appoint a Liaison Officer who shall report to the head of that Designated Agency. The Liaison Officer shall coordinate with the PSIOC. Liaison officers shall serve as the primary point of contact representing their respective Designated Agency.
5. The PSIOC shall establish, conduct, and coordinate through the Liaison Officers a process to comprehensively assess current state agency jurisdictions, standards, and

practices on matters subject to this Order. That assessment shall identify all state agencies' detailed statutory and regulatory authority and practices; any gaps in statutes, regulations, resources, practices, or oversight regarding oil and natural gas facilities, equipment, infrastructure, and activities on state oil and natural gas units and leases; and the risks associated with any gaps. Analysis done under this paragraph is intended to preclude duplication of effort, and provide a comprehensive and cost-effective approach to determine the appropriate state oversight of oil and natural gas facilities, equipment, infrastructure, and activities on state oil and natural gas units and leases.

6. The PSIOC shall lead the interagency effort, through the Liaison Officers, to evaluate industry oversight of oil and natural gas facilities, equipment, infrastructure, and activities on state oil and natural gas units and leases. Designated agencies, to the extent authorized through existing legal authorities, shall require the industry businesses to provide a comprehensive description of current practices that includes the quality control, quality assurance, monitoring, inspection, and other practices the business uses to ensure the integrity and reliability of oil and natural gas facilities, equipment, infrastructure, and activities. The PSIOC shall coordinate the review of these evaluations and descriptions, identify gaps, and seek remedial action. The PSIOC shall make recommendations to the commissioner of the Department of Natural Resources regarding enforcement actions by the Department of Natural Resources and cases to be referred to other state, local, or federal agencies for appropriate civil or criminal penalties available under the law.
7. On an ongoing basis, the PSIOC shall coordinate the oversight activities of the PSIO with the Designated Agencies. The Designated Agencies shall participate in interagency activities led by the PSIO and provide other technical assistance as requested by the PSIO.
8. Unless contrary to any dispute resolution process in statute or regulation, in the event of an interagency dispute between Designated Agencies regarding a matter covered under this Order, Liaison Officers shall raise the issue to the PSIOC, who shall resolve the interagency dispute to the maximum extent possible in accordance with law. If the interagency dispute cannot be resolved by the PSIOC, the matter shall be elevated to the affected Designated Agency heads and the commissioner of the Department of Natural Resources. If an interagency dispute cannot be resolved by the affected Designated Agency heads and the commissioner of the Department of Natural Resources, the matter shall be elevated to the governor.
9. Consistent with AS 44.23.020, the attorney general, as legal advisor for the state, shall provide legal services to the PSIO, the PSIOC, and all Designated Agencies.
10. This Order is for administrative purposes only. It neither creates any third-party rights nor modifies the statutory and regulatory authority of Designated Agencies.
11. The PSIOC shall submit to the commissioner of the Department of Natural Resources and to the governor periodic progress reports that summarize evaluation, coordination, review, and oversight activities done under this Order and accomplishment of those activities.

DEFINITIONS

In this Order,

1. "Designated Agencies" means the Department of Environmental Conservation; Department of Fish and Game; Department of Public Safety; Department of Revenue; Department of Transportation and Public Facilities; Department of Labor and Workforce Development; Department of Law; Department of Natural Resources; Alaska Oil and Gas Conservation Commission; and the director in the Governor's Office in Washington, D.C.;
2. "equipment" means machinery that is not a permanent fixture, is located on either a state oil and natural gas unit or lease, and is used to operate, construct, clean, or otherwise service oil and natural gas infrastructure and facilities;
3. "exploration facility" has the meaning given in AS 46.04.900;
4. "facilities" includes exploration facilities, oil terminal facilities, and production facilities;
5. "infrastructure" means all oil and natural gas pipelines, both onshore and offshore, including production facilities, line pipe, valves, and other appurtenances connected to line pipe, pumping units, and fabricated assemblies associated with pumping units, flow lines, separation facilities such as gathering centers and flow stations; transmission pipeline; above-ground oil storage tanks; oil or natural gas processing facilities, including seawater and produced water facilities; and all offshore platforms intended for use in oil and natural gas exploration or production
6. "Liaison Officer" means an officer or employee from a Designated Agency appointed to represent and report to the head of that Designated Agency and to serve as the primary point of contact between that Designated Agency and the PSIO and PSIOC;
7. "oil terminal facility" has the meaning given in AS 46.04.900;
8. "production facility" has the meaning given in AS 46.04.900;
9. "PSIO" means the Petroleum Systems Integrity Office established under this Order;
10. "PSIOC" means the Petroleum Systems Integrity Office Coordinator designated under this Order;
11. "transmission pipeline" has the meaning given in 18 AAC 75.990.

REVOCATION OF AND RELATIONSHIP TO OTHER ADMINISTRATIVE ORDERS

Administrative Order No. 229 is revoked. This Order supplements Administrative Order Nos. 134 and 187 and shall be interpreted as being complementary to those Orders. Unless contrary to any dispute resolution process in statute or regulation, any conflict among the Orders shall be resolved by the heads of the affected Designated State Agencies; if an interagency disagreement remains, the governor will resolve the conflict.

This Order takes effect immediately.

DATED at Juneau, Alaska, this 18th day of April, 2007.

/s/Sarah Palin
Governor

WWW.GOV.STATE.AK.US

[Administrative Orders 201-present](#) | [Contact the Governor](#) | [Webmaster](#) | [State of Alaska](#)

CONCEPTUAL AMENDMENT 2

OFFERED IN THE HOUSE

TO: CSHB 128(O&G) (Version 25-LS0561K)

1 Add a new paragraph (4) to AS 43.55.165(j):

2 (4) "improper maintenance" is defined as any maintenance that is not
3 consistent with good oil field practice.

4

5 Add a new paragraph (5) to AS 43.55.165(j):

6 (5) "good oil field practice" is defined as a practice that is generally
7 accepted to be good, safe and efficient in carrying out oil field operations,
8 including, but is not limited to, the design, construction, testing, operating, and
9 maintaining of production, processing and transportation facilities and equipment,
10 consistent with standards such as the American Petroleum Institute (API) or
11 American Society for Testing and Materials (ASTM), federal regulations,
12 maintenance programs consistent with the program requirements set forth by the
13 person in the Department of Natural Resources who is the lead person for
14 exercising oversight over the maintenance of oil and gas facilities, equipment,
15 and infrastructure in the state, or other applicable standards for the production,
16 processing and transportation of oil, gas, produced water, and other fluids.

Heath Hilyard

From: Dennis Denney [ddenney@spe.org]
Sent: Monday, March 26, 2007 10:41 AM
To: Heath Hilyard
Subject: good oilfield practice

Hello Heath.

Here is what I found.

"good oilfield practice: a practice that is generally accepted to be good, safe, and efficient in carrying out oilfield operations"

From: Hyne, N.J. 1991. *Dictionary of Petroleum Exploration, Drilling, & Production*. Tulsa, Oklahoma: PennWell Books 224.

As you mentioned, it is a very general term.

Regards,

Dennis Denney
Technology Editor, *JPT*
222 Palisades Creek Drive
Richardson, TX 75080
972.952.9340

The March 2007 issue of *JPT Online* is posted at <http://www.spe.org/jpt>. Remind your colleagues that full-length copies of SPE papers synopsisized in *JPT* are available online free to SPE members for 2 months.



A M E N D M E N T

OFFERED IN THE HOUSE

TO: CSHB 128(O&G)

1 Page 4, lines 9 - 10:

2 Delete "lease expenditures that may not be deducted"

3 Insert "costs that may not be treated as lease expenditures or claimed as a credit based
4 on costs that may not be claimed as lease expenditures"

5

6 Page 4, line 10:

7 Delete "AS 43.55.165(e), as amended"

8 Insert "AS 43.55.165(e)(19), as enacted"

9

10 Page 4, line 13, following "AS 43.55.020(a)":

11 Insert "before the effective date of this Act"

12

13 Page 4, line 15:

14 Delete "lease expenditures that may not be deducted"

15 Insert "costs that may not be treated as lease expenditures or attributable to a credit
16 based on costs that may not be claimed as lease expenditures"

17 Delete "AS 43.55.165(e) as amended"

18 Insert "AS 43.55.165(e)(19), as enacted"

19

20 Page 4, following line 17:

21 Insert a new subsection to read:

22 "(c) Interest on an additional amount of tax due under (a) of this section or on
23 the amount of the underpayment of an installment under (b) of this section does not

1 begin to accrue until 90 days after the effective date of this Act."

A M E N D M E N T

OFFERED IN THE HOUSE

BY REPRESENTATIVE SEATON

TO: CSHB 128(O&G)

1 Page 4, line 1, following "equipment":

2 Insert ";

3 (20) costs related to the maintenance of oil and gas facilities,
4 equipment, and infrastructure that are incurred as a result of a violation of a
5 regulation adopted by the person in the Department of Natural Resources who is
6 the lead person for exercising oversight over the maintenance of oil and gas
7 facilities, equipment, and infrastructure in the state"

8

9 Page 4, lines 4 - 5:

10 Delete all material and insert:

11 "APPLICABILITY. (a) AS 43.55.165(e)(19), as enacted in sec. 1 of this Act, applies
12 to oil and gas produced after March 31, 2006.

13 (b) AS 43.55.165(e)(20), as enacted in sec. 1 of this Act, applies to oil and gas
14 produced after the effective date of the regulations described in sec. 5 of this Act."

15

16 Page 4, line 20:

17 Delete "Section 1 of this Act"

18 Insert "AS 43.55.165(e)(19), as enacted in sec. 1 of this Act,"

19

20 Page 4, line 21:

21 Delete all material and insert:

22 "** Sec. 5. The uncodified law of the State of Alaska is amended by adding a new section to
23 read:

1 CONDITIONAL EFFECT; NOTICE. (a) AS 43.55.165(e)(20), as enacted in sec. 1 of
2 this Act, takes effect only if the person in the Department of Natural Resources who is the
3 lead person for exercising oversight over the maintenance of oil and gas facilities, equipment,
4 and infrastructure in the state adopts regulations related to the maintenance of oil and gas
5 facilities, equipment, and infrastructure in the state.

6 (b) The commissioner of natural resources shall notify the revisor of statutes of the
7 effective date of the regulations described in (a) of this section.

8 * **Sec. 6.** If AS 43.55.165(e)(20), as enacted in sec. 1 of this Act, takes effect, it takes effect
9 on the effective date of the regulations described in sec. 5 of this Act.

10 * **Sec. 7.** Except as provided in sec. 6 of this Act, this Act takes effect immediately under
11 AS 01.10.070(c)."

ALASKA STATE LEGISLATURE

REPRESENTATIVE KURT OLSON

- Chair, Labor and Commerce
- Vice-Chair, Oil and Gas
- Member, Community and Regional Affairs

Session: January – May
State Capitol
Juneau, AK 99801-1182
Phone: 907-465-2693
Fax: 907-465-3835



Interim: May – December
145 Main Street Loop, Ste 221
Kenai, AK 99611
Phone: 907-283-2690
Fax: 907-283-2763

Official Business

Sponsor Statement

HB 128 – Disallows PPT Reductions for Improperly Maintained Facilities

HB 128 cleans up language and closes a loophole in the recently passed Petroleum Production Tax (PPT) legislation.

As currently written, producers may deduct or use as credits, expenses for repairs made to infrastructure that has been improperly maintained. Once HB128 is enacted, deductions or credits against the PPT for these types of repairs will be subject to review and approval.

This bill instructs the Commissioner of the Revenue to consult with the Commissioner of the DEC and the Chair of AOGCC. Relying on standard practices of the industry, they will determine the portion of the costs related to repair or replacement of improperly maintained property or equipment available for deduction or use as a credit

This concept came forward as an amendment in the Senate Resources Committee in early August of 2006. The ongoing corrosion problem currently experienced by BP serves to emphasize the importance of this change in statute.

The responsibility for the expenses related to repairs made to improperly maintained infrastructure should not lie with the State of Alaska.

I respectfully ask for your support of this bill.

ALASKA STATE LEGISLATURE

REPRESENTATIVE KURT OLSON

- Chair, Labor and Commerce
- Vice-Chair, Oil and Gas
- Member, Community and Regional Affairs

Session: January – May
State Capitol
Juneau, AK 99801-1182
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Official Business

Sectional Analysis

HB 128 - Disallows PPT Reductions for Improperly Maintained Facilities

Section 1: amends AS 43.55.165(e) which establishes lease expenditures not available for use as credits or deductions to the Petroleum Production Tax (PPT).

New subsection (19) establishes new language regarding costs related to the repair and replacement of improperly maintained property or equipment.

These costs are subject to review by the Commissioner of The Department of Revenue, the Commissioner of the Department of Environmental Conservation and the chair of the Alaska Oil and Gas Conservation Commission, relying on industry standards.

Section 2: provides for applicability to the oil and gas produced after March 31, 2006, as with the PPT.

Section 3: provides for transitional language for payment of additional taxes or installment payment due as a result of disallowing any expenditure set out in Section 1.

Section 4: provides for retroactive date to the same period as the PPT.

ALASKA STATE LEGISLATURE

REPRESENTATIVE KURT OLSON

- Chair, Labor and Commerce
- Vice-Chair, Oil and Gas
- Member, Community and Regional Affairs

Session: January – May
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Fax: 907-283-2763

Official Business

TO: Representative Carl Gatto, Co-Chair
House Resources Committee

FROM: Representative Kurt Olson

A handwritten signature in black ink, appearing to read "K. Olson".

DATE: March 1, 2007

RE: Hearing on CSHB 128(O&G)

I respectfully request a hearing in the House Resources Committee on CSHB 128(O&G), An Act relating to allowable lease expenditures available for use as credits and deductions from oil and gas production tax, pending referral, at your earliest convenience.

Attached please find a copy of CSHB 128(O&G) and a sponsor statement. Additional information will follow once this bill passes from the House Special Committee on Oil & Gas.

If you need any further information or have any questions, please contact my staff, Konrad Jackson.

Thank you for your attention to this request.

FISCAL NOTE

STATE OF ALASKA
2007 LEGISLATIVE SESSION

Fiscal Note Number: 1
 Bill Version: CSHB 128(O&G)
 (H) Publish Date: 3/5/07

Revision Date/Time (Note if correction): _____ Dept. Affected: Dept of Environmental Conservation
 Title: OIL & GAS PRODUCTION TAX: EXPENDITURES RDU: Spill Prevention and Response
 Component: Director's Office
 Sponsor: Oslo et al
 Requester: House Special Committee on Oil and Gas Component No.: 1392

Expenditures/Revenues (Thousands of Dollars)

Note: Amounts do not include inflation unless otherwise noted below.

OPERATING EXPENDITURES	FY 2008	FY 2009	FY 2010	FY 2011	FY 2012	FY 2013
Personal Services						
Travel						
Contractual						
Supplies						
Equipment						
Land & Structures						
Grants & Claims						
Miscellaneous						
TOTAL OPERATING	0.0	0.0	0.0	0.0	0.0	0.0

CAPITAL EXPENDITURES						
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CHANGE IN REVENUES ()						
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FUND SOURCE (Thousands of Dollars)

1002 Federal Receipts						
1003 GF Match						
1004 GF						
1005 GF/Program Receipts						
1037 GF/Mental Health						
Other (Specify Type-Do not abbreviate)						
TOTAL	0.0	0.0	0.0	0.0	0.0	0.0

Estimate of any current year (FY2006) cost: 0.0

Mark this box (X) if funding for this bill is included in the Governor's FY 2008 budget proposal:

POSITIONS

Full-time						
Part-time						
Temporary						

ANALYSIS: (Attach a separate page if necessary)

No additional costs are expected with this legislation.

Prepared by: Larry Dietrick Phone 465-5250
 Division: Spill Prevention and Response Date/Time 2/20/07 4:00 PM
 Approved by: Larry Hartig Date 2/20/2007
 Agency: Department of Environmental Conservation

FISCAL NOTE

STATE OF ALASKA
2007 LEGISLATIVE SESSION

Fiscal Note Number: 2
 Bill Version: CSHB128(O&G)
 (H) Publish Date: 3/5/07

Revision Date/Time (Note if correction): _____ Dept. Affected: Administration
 Title: Oil and Gas Production Tax RDU: AOGCC
 Component: AOGCC
 Sponsor: Representatives Olson, Harris, Ramras, et. Al.
 Requester: House Oil and Gas Component No.: 2010

Expenditures/Revenues (Thousands of Dollars)

Note: Amounts do not include inflation unless otherwise noted below.

OPERATING EXPENDITURES	FY 2008	FY 2009	FY 2010	FY 2011	FY 2012	FY 2013
Personal Services	0.0	0.0	0.0	0.0	0.0	0.0
Travel	0.0	0.0	0.0	0.0	0.0	0.0
Contractual	250.0	250.0	250.0	250.0	250.0	250.0
Supplies	0.0	0.0	0.0	0.0	0.0	0.0
Equipment	0.0	0.0	0.0	0.0	0.0	0.0
Land & Structures	0.0	0.0	0.0	0.0	0.0	0.0
Grants & Claims	0.0	0.0	0.0	0.0	0.0	0.0
Miscellaneous	0.0	0.0	0.0	0.0	0.0	0.0
TOTAL OPERATING	250.0	250.0	250.0	250.0	250.0	250.0

CAPITAL EXPENDITURES	0.0	0.0	0.0	0.0	0.0	0.0
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CHANGE IN REVENUES ()	0.0	0.0	0.0	0.0	0.0	0.0
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FUND SOURCE (Thousands of Dollars)

1002 Federal Receipts	0.0	0.0	0.0	0.0	0.0	0.0
1003 GF Match	0.0	0.0	0.0	0.0	0.0	0.0
1004 GF	0.0	0.0	0.0	0.0	0.0	0.0
1005 GF/Program Receipts	0.0	0.0	0.0	0.0	0.0	0.0
1037 GF/Mental Health	0.0	0.0	0.0	0.0	0.0	0.0
1162 AOGCC Receipts	250.0	250.0	250.0	250.0	250.0	250.0
TOTAL	250.0	250.0	250.0	250.0	250.0	250.0

Estimate of any current year (FY2007) cost: 0.0

Mark this box (X) if funding for this bill is included in the Governor's FY 2008 budget proposal:

POSITIONS

Full-time						
Part-time						
Temporary						

ANALYSIS: (Attach a separate page if necessary)

If HB128 is passed the AOGCC in conjunction with other State agencies would be charged with determining whether the lease expenditures incurred for repair, replacement, or incremental operating expenses were as a result of a lack of or improper maintenance of property or equipment. The Commission would also need authority under AS 31.05.030 to implement these need responsibilities.

1 contract Engineering Investigator for 2/3 of year, which equals \$250,000 a year.

Prepared by: Jody J. Colombie, Special Assistant I
 Division: Alaska Oil and Gas Conservation Commission
 Approved by: Rachael Petro, Deputy Commissioner
 Agency: Department of Administration

Phone 465-2200
 Date/Time 2/28/07 9:39 AM
 Date 2/28/07 10:00 AM

FISCAL NOTE

STATE OF ALASKA
2007 LEGISLATIVE SESSION

Fiscal Note Number: 3
 Bill Version: CSHB 128(O&G)
 (H) Publish Date: 3/5/07

Revision Date/Time (Note if correction): _____ Dept. Affected: Revenue 04
 Title Oil & Gas Production Tax: Expenditures RDU Taxation and Treasury
 Component Tax Division
 Sponsor Representative Olson
 Requester (H) Oil and Gas Component No. 2476

Expenditures/Revenues (Thousands of Dollars)

Note: Amounts do not include inflation unless otherwise noted below.

OPERATING EXPENDITURES	FY 2008	FY 2009	FY 2010	FY 2011	FY 2012	FY 2013
Personal Services						
Travel						
Contractual	124.9	124.9	124.9	124.9	124.9	124.9
Supplies						
Equipment						
Land & Structures						
Grants & Claims						
Miscellaneous						
TOTAL OPERATING	124.9	124.9	124.9	124.9	124.9	124.9

CAPITAL EXPENDITURES						
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CHANGE IN REVENUES ()	*	*	*	*	*	*
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FUND SOURCE (Thousands of Dollars)

1002 Federal Receipts						
1003 GF Match						
1004 GF	124.9	124.9	124.9	124.9	124.9	124.9
1005 GF/Program Receipts						
1037 GF/Mental Health						
Other (Specify Type--Do not abbreviate)						
TOTAL	124.9	124.9	124.9	124.9	124.9	124.9

Estimate of any current year (FY2007) cost: 31.2

Check this box (X) if funding for this bill is included in the Governor's FY 2008 budget proposal:

POSITIONS

Full-time						
Part-time						
Temporary						

ANALYSIS: (Attach a separate page if necessary)

*This bill would add certain costs relating to improperly maintained property or equipment to the list of costs that do not qualify as lease expenditures under AS 43.55.165, the petroleum profits production tax system. Under the bill, the commissioner of revenue, in consultation with the commissioner of environmental conservation and the chair of the Alaska Oil and Gas Conservation Commission, would determine whether costs are specifically disallowed under this provision. The provision would disallow any costs incurred to (1) repair or replace improperly maintained property or equipment; and/or (2) maintain the operational capability of facilities or equipment that are either shut down or are diminished in capacity. The bill effective date is retroactive to April 1, 2006 - the effective date of the petroleum profits tax (PPT).

Prepared by: Jon Iversen and Cherie Nienhuis Phone 269-1033
 Division Tax Date/Time 2/22/07 11:00 AM
 Approved by: Jerry Burnett Date 2/22/2007
 Agency Department of Revenue

FISCAL NOTE #3

**STATE OF ALASKA
2007 LEGISLATIVE SESSION**

BILL NO. CSHB 128(O&G)

ANALYSIS CONTINUATION

The impact this bill would have on petroleum tax revenues is indeterminate. Costs identified as disallowed under this bill could be categorized as either operating costs or capital costs. The PPT authorizes eligible operating costs to be deducted from the petroleum profits tax at a rate of 22.5%; the PPT authorizes capital costs to be both deducted at a rate of 22.5% and credited at a rate of 20%, for a combined production tax savings of 42.5%. Any set of disallowed costs is likely to be split between these two categories in a way that is distinct from that of another set of costs.

Administering this legislation would require one full-time equivalent (FTE) with expertise in oil and gas industry practices on the level of a petroleum engineer. The department currently contracts with a petroleum engineer for five years at a cost of \$624,650, or \$124,930 per year, for technical support related to petroleum production. It is anticipated that the department would be required to carry a second contract of this magnitude or greater in order to fulfill the requirements of this legislation.

REVISED FISCAL NOTE

STATE OF ALASKA
2007 LEGISLATIVE SESSION

Fiscal Note Number: 4
 Bill Version: CSHB 128(RES)
 (H) Publish Date: 5/5/07

Revision Date/Time (Note if correction): _____ Dept. Affected: Administration
 Title Oil and Gas Production Tax RDU AOGCC
 Component AOGCC
 Sponsor Representatives Olson, Harris, Ramras, et al.
 Requester House Oil and Gas Component No. 2010

Expenditures/Revenues (Thousands of Dollars)

Note: Amounts do not include inflation unless otherwise noted below.

OPERATING EXPENDITURES	FY 2008	FY 2009	FY 2010	FY 2011	FY 2012	FY 2013
Personal Services	0.0	0.0	0.0	0.0	0.0	0.0
Travel	0.0	0.0	0.0	0.0	0.0	0.0
Contractual	0.0	0.0	0.0	0.0	0.0	0.0
Supplies	0.0	0.0	0.0	0.0	0.0	0.0
Equipment	0.0	0.0	0.0	0.0	0.0	0.0
Land & Structures	0.0	0.0	0.0	0.0	0.0	0.0
Grants & Claims	0.0	0.0	0.0	0.0	0.0	0.0
Miscellaneous	0.0	0.0	0.0	0.0	0.0	0.0
TOTAL OPERATING	0.0	0.0	0.0	0.0	0.0	0.0

CAPITAL EXPENDITURES	0.0	0.0	0.0	0.0	0.0	0.0
-----------------------------	-----	-----	-----	-----	-----	-----

CHANGE IN REVENUES ()	0.0	0.0	0.0	0.0	0.0	0.0
-------------------------------	-----	-----	-----	-----	-----	-----

FUND SOURCE (Thousands of Dollars)

1002 Federal Receipts	0.0	0.0	0.0	0.0	0.0	0.0
1003 GF Match	0.0	0.0	0.0	0.0	0.0	0.0
1004 GF	0.0	0.0	0.0	0.0	0.0	0.0
1005 GF/Program Receipts	0.0	0.0	0.0	0.0	0.0	0.0
1037 GF/Mental Health	0.0	0.0	0.0	0.0	0.0	0.0
1162 AOGCC Receipts	0.0	0.0	0.0	0.0	0.0	0.0
TOTAL	0.0	0.0	0.0	0.0	0.0	0.0

Estimate of any current year (FY2007) cost: 0.0

Mark this box (X) if funding for this bill is included in the Governor's FY 2008 budget proposal:

POSITIONS

Full-time						
Part-time						
Temporary						

ANALYSIS: (Attach a separate page if necessary)

Any consultation we provide as part of the Petroleum Systems Integrity Office (PSIO) working group will be part of our ongoing responsibilities at the Alaska Oil and Gas Conservation Commission (AOGCC). Therefore there will be no additional fiscal impact on this agency with the passing of this bill.

Prepared by: Jody J. Colombie, Special Assistant I
 Division: Alaska Oil and Gas Conservation Commission
 Approved by: Rachael Petro, Deputy Commissioner
 Agency: Department of Administration

Phone 793-1221
 Date/Time 4/26/07 3pm
 Date 4/27/07

REVISED FISCAL NOTE

STATE OF ALASKA
2007 LEGISLATIVE SESSION

Fiscal Note Number: 5
 Bill Version: CSHB 128(RES)
 (H) Publish Date: 5/5/07

Revision Date/Time (Note if correction): _____ Dept. Affected: Administration
 Title: Oil and Gas Production Tax RDU: AOGCC
 Component: AOGCC
 Sponsor: Representatives Olson, Harris, Ramras, et al.
 Requester: House Oil and Gas Component No.: 2010

Expenditures/Revenues (Thousands of Dollars)

Note: Amounts do not include inflation unless otherwise noted below.

OPERATING EXPENDITURES	FY 2008	FY 2009	FY 2010	FY 2011	FY 2012	FY 2013
Personal Services	0.0	0.0	0.0	0.0	0.0	0.0
Travel	0.0	0.0	0.0	0.0	0.0	0.0
Contractual	50.0	50.0	40.0	30.0	20.0	20.0
Supplies	0.0	0.0	0.0	0.0	0.0	0.0
Equipment	0.0	0.0	0.0	0.0	0.0	0.0
Land & Structures	0.0	0.0	0.0	0.0	0.0	0.0
Grants & Claims	0.0	0.0	0.0	0.0	0.0	0.0
Miscellaneous	0.0	0.0	0.0	0.0	0.0	0.0
TOTAL OPERATING	50.0	50.0	40.0	30.0	20.0	20.0
CAPITAL EXPENDITURES	0.0	0.0	0.0	0.0	0.0	0.0
CHANGE IN REVENUES ()	0.0	0.0	0.0	0.0	0.0	0.0

FUND SOURCE (Thousands of Dollars)

1002 Federal Receipts	0.0	0.0	0.0	0.0	0.0	0.0
1003 GF Match	0.0	0.0	0.0	0.0	0.0	0.0
1004 GF	0.0	0.0	0.0	0.0	0.0	0.0
1005 GF/Program Receipts	0.0	0.0	0.0	0.0	0.0	0.0
1037 GF/Mental Health	0.0	0.0	0.0	0.0	0.0	0.0
1032 AOGCC Receipts	50.0	50.0	40.0	30.0	20.0	20.0
TOTAL	50.0	50.0	40.0	30.0	20.0	20.0

Estimate of any current year (FY2007) cost: 0.0

Mark this box (X) if funding for this bill is included in the Governor's FY 2008 budget proposal:

POSITIONS

Full-time						
Part-time						
Temporary						

ANALYSIS: (Attach a separate page if necessary)

If HB 128 is passed, the Alaska Oil and Gas Conservation Commission, in conjunction with other State agencies, would be charged with determining whether a taxpayer followed standard industry practices for purposes of eligibility for deductions of costs related to the repair and replacement of improperly maintained property or equipment.

The estimate in this fiscal note is based upon our understanding that the work we may be called upon to perform will be within our traditional area of regulatory oversight (i.e., downhole and at the wellhead); and, that the Petroleum Systems Integrity Office (PSIO) will provide consultation and conduct investigations at the point where our jurisdiction ends.

Prepared by: Jody J. Colombie, Special Assistant I Phone 793-1221
 Division: Alaska Oil and Gas Conservation Commission Date/Time 3/9/07 10:30 AM
 Approved by: Rachael Petro, Deputy Commissioner Date 3/9/2007
 Agency: Department of Administration

LEGAL SERVICES

DIVISION OF LEGAL AND RESEARCH SERVICES
LEGISLATIVE AFFAIRS AGENCY
STATE OF ALASKA

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FAX (907) 465-2029
Mail Stop 3101

State Capitol
Juneau, Alaska 99801-1182
Deliveries to: 129 5th St., Rm. 329

MEMORANDUM

April 23, 2007

SUBJECT: Legislative intent (SB 80; Work Order No. 25-LS0425\A)

TO: Senator Tom Wagoner
Attn: Mary Jackson

FROM: Donald M. Bullock Jr.
Legislative Counsel

Refers to Aug. 8, 2006
Memo from Pedro
- Per Comm. Galvin --- is no longer
confidential

While I was attending the hearing of the Senate Resources Committee on SB 80 on April 20, 2007, a memo was offered for the purpose of explaining the intent behind the enactment of AS 43.55.165(e)(18). You asked whether the memo may be considered as evidence of the legislature's intent behind the enactment of that provision.

The simple and short answer is, no.

I have found no reference to the particular memorandum in the minutes of the August 9, 2006 meeting of the Special Committee on Natural Gas Development at which AS 43.55.165(e)(18) was adopted as an amendment to the bill.¹ Indeed, the commissioner of revenue testified at the Senate Resources Committee meeting on April 20, 2007, that the memo was not publicly released until after the change in administration. Under these facts, the memorandum was never available to the legislature and there is no basis for using the memorandum as evidence of the intent of the legislature at the time the amendment was adopted, and ultimately, when the bill was passed.

Without evidence of legislative intent to the contrary, AS 43.55.165(e)(18) means no more than what it presents:

(e) For purposes of this section, lease expenditures do not include

(18) that portion of expenditures, that would otherwise be qualified capital expenditures as defined in AS 43.55.023(k), incurred during a calendar year that are less than the product of \$0.30 multiplied by the total taxable production from each lease or property, in BTU equivalent barrels.

¹ The minutes for this August 9, 2006 meeting are published on the Internet at: http://www.legis.state.ak.us/basis/get_single_minute.asp?session=24&beg_line=00142&end_line=02090&time=1026&date=20060809&comm=NGD&house=S.

Senator Tom Wagoner

April 23, 2007

Page 2

during that calendar year, except that, when a portion of a calendar year is subject to this provision, the expenditures and volumes shall be prorated within that calendar year.

The paragraph includes no reference to the standard of maintenance or repair required before an expenditure may be deducted.

By comparison, the bill under consideration by the Senate Resources Committee, SB 80, attempts to impose a standard of care on an operator; if an operator falls below the standard, the associated expenditures will be disallowed as a deduction.

If I may be of further assistance, please advise.

DMB:lmb
07-106.lmb

Mary:

This is in reply to your e-mail sending the PSIO amendment to SB # 80 that Senator Wagoner intends to introduce. We reviewed the proposed amendment and believe it will improve the bill.

Attached are written comments we sent to the committee on Wednesday when asked to be available to testify on SB 80. This proposed amendment specifically addresses a concern expressed in section 2 (e) of our attached comments which recommended PSIO be the designated lead because of its responsibility to oversee facility and equipment maintenance. Pursuant to section 2 of Administrative Order No. 234, dated April 18, 2007, AOGCC is one of the participating agencies and will be able to provide coordinated advice and consultation to the Department of Revenue through PSIO.

We also suggested at lines 22 and 23, p.3 of the bill, that the term "good oilfield practices" be substituted in place of "the standard practices of the industry". We don't know if this was considered.

As you know, we have the utmost respect for the sponsors of this bill. Other comments (in our attachment) identify policy considerations we felt obligated to bring forward. Having done so, you may assure Senator Wagoner we will do our absolute best to implement this bill in whatever form it is adopted.

These comments reflect the views of the commissioners of the AOGCC and you may distribute this e-mail as you see fit.

John K. Norman
Chair,
AOGCC

4-20-07

3:45 PM

AMENDMENT

OFFERED IN THE SENATE

BY SENATOR WAGONER

TO: CSSB 80(), Draft Version "M"

1 Page 3, lines 21 - 22:

2 Delete "Alaska Oil and Gas Conservation Commission"

3 Insert "person in the Department of Natural Resources who is the lead person for
4 exercising oversight over the maintenance of oil and gas facilities, equipment, and
5 infrastructure in the state"

**Alaska Oil and Gas Conservation Commission's
Comments regarding SB 80/HB128-OIL and
GAS PRODUCTION TAX: EXPENDITURES**

This legislation is proposed as a law of general application throughout the State of Alaska. With that in mind the Alaska Oil and Gas Conservation Commission's ("AOGCC") comments are framed without regard to any particular incident and instead with a view to how the law might apply throughout the state and in particular to new investors contemplating oil and gas operations in Alaska.

1. Policy Considerations:

- a. Is it advisable to deny leasehold expenditure deductions for costs resulting from errors which are not the consequence of fraud, willful misconduct, or gross negligence? Subsection (6) of AS 43.55.165(e) already disallows deductions for the expenses arising from fraudulent, willful misconduct or gross negligence.

Proposed subsection (19) would extend cost disallowance to acts other than those already addressed by subsection (6). Subsection (6) addresses costs related to willful misconduct or gross negligence, so we interpret subsection (19) as intended to disallow costs arising because of ordinary negligence. This would impose a penalty on the operator beyond what is customary in agreements between co-owners who enter into operating agreements for development of a commonly owned resource. Such agreements almost always absolve an operator of liability for losses sustained or liabilities incurred, except such as may result from gross negligence or willful misconduct. If it were otherwise and operators were liable for ordinary negligence (which is another way of saying making a mistake) they would be in the position of guaranteeing a trouble free operation. No operator would be willing to make that guarantee. It is generally recognized in the business world that mistakes happen but only when they result from willful misconduct or gross negligence is an operating partner normally penalized.

With the foregoing in mind subsection (19) departs from normal business practice and sets a higher standard than business partners in the oil and gas industry normally demand of each other. Similar reasoning could be applied to new operators contemplating operations in the State of Alaska under what they might perceive as a tax structure unforgiving of mistakes.

- b. Denial of Facility Shut Down Expenses. Subsection (19) (B) would deny expenses incurred to maintain operational capability of facility or equipment shut down because of improper maintenance. Is it good policy

to deny operational maintenance costs if the operator believes that the best course of action is to shut down the entire facility in order to carry out necessary repairs? Denial of operational capability maintenance costs could discourage operators from shutting down when in fact a complete shut down is the most prudent course of action.

- c. Should Not Discourage Innovation. The oil and gas industry is constantly evolving. A tax regime should not discourage innovative techniques. Examples of such techniques are the astounding advances that have been made in recent decades in the area of directional drilling, coiled tube drilling, and subsea completions. Any attempt to rigidly codify "good oilfield practices" could inadvertently retard the natural learning experience that comes with allowing operators to experiment with differing techniques.

2. Practical Considerations:

- a. Standard Terminology. The phrase "Standard Practices of the Industry" in subsection (19) is vague and ambiguous. On the one hand it could mean the written standards adopted by professional organizations intended as guidance documents for the industry; or it could simply mean the standard practice prevailing in the industry in a particular locale.

In determining whether an operator's conduct has resulted in waste of a resource the AOGCC has generally used "good oilfield practices" as a standard by which to measure an operators practice in installing operating and maintaining equipment. See AS 31.05.170(15).

- b. AOGCC's preferred term. Good oilfield practices is the term used to indicate that operations are carried out in a proper and workman like manner. It is used in the same way as the phrase "everything is A.P.I.," which refers to the American Petroleum Institute's set of standards covering aspects of petroleum operations. Williams & Meyers, Manual of Oil and Gas Terms (13th ED.) p 453. It is therefore, AOGCC's recommendation that the phrase "good oilfield practices" be substituted for the current phrase "standard practices of the industry".
- c. Absence of Regulatory Guidelines for Maintenance. There is lack of current regulatory guidelines. Much of the equipment and systems in oilfields that are subject to maintenance are not currently regulated by either AOGCC or DEC. This raises questions about how to gauge "improper maintenance" in the absence of regulatory responsibility for such systems and equipment.

- d. Regulations. There will be a need for AOGCC and other agencies to promulgate regulations if AOGCC is assigned responsibility under this bill. These regulations should provide general guidance to the industry, including new operators coming into the State, concerning what constitutes "good oilfield practices." Toward this end we would look to the American Petroleum Institute's standards and recommended practices, as well as standards recognized by the National Association of Corrosion Engineers (NACE), the American Society of Mechanical Engineers (ASME), the International Standards Organization (ISO) and similar respected organizations.
- e. Agency Expertise. There is a need for specialized expertise. AOGCC geologists and engineers work to regulate operations downhole and immediately around the production string but traditionally have not moved further downstream except when required to determine whether a failure of equipment resulted from an operator's failure to employ good oilfield practices thereby resulting in "waste" of hydrocarbon resources.

We are aware that Governor Palin has announced activation of the Petroleum Systems Integrity Office ("PSIO") and AOGCC is one of the agencies designated to participate on that team. We contemplate that the PSIO staff will implement a quality assurance program with inspections conducted by or under the direction of PSIO to ensure compliance with approved programs. AOGCC will have a designated representative working with PSIO and AOGCC expertise can be called upon as necessary to consult with the Department of Revenue through PSIO. Such an arrangement will avoid duplication of effort and ensure consistency of standards, directives, and inspection reports since all would be coordinated through PSIO.

3. Difficulties In Determining Root Cause:

In some instances it will be obvious that there has been improper maintenance. In other instances, the AOGCC would be required to consider design, installation, operation, and maintenance, all of which are integral to a determination of negligence. Additionally some determinations will require detailed investigation including but not limited to destructive and non-destructive metallurgical testing and application of other expertise not readily available within the AOGCC.

4. Date Stamping Negligent Conduct:

Standards are continually evolving and it will be important to decide whether conduct that led to the failure should be judged in light of the standards prevailing when

the original decisions were made or judged by the most current standards. Additionally, properties are often sold or traded within the industry. Is it good policy to deny a good faith purchaser the benefit of leasehold expenditures incurred as result of mistakes which may have been made many years before by the prior owner?

March 2, 2007

The Honorable Kurt Olson
State House of Representatives
Alaska State Capitol, Room 110
Juneau, AK 99801-1182

RE: Response to Prudhoe Bay Pigging Inquiry

Dear Representative Olson:

During Tom Williams' testimony to the House Oil and Gas Committee on behalf of BP Exploration (Alaska) Inc. ("BPXA") on Thursday February 22, 2007, you raised two questions for which Mr. Williams needed to obtain additional information before responding. Specifically, you asked whether BPXA had pigged the oil transit lines since the ARCO acquisition and when the lines had been pigged.

BPXA last ran an in-line inspection tool ("smart pig") in October 2006 in the Eastern Operating Area ("EOA") and in November 2006 in the Western Operating Area ("WOA"), in each case we completed two runs to collect the inspection data required. Prior to these runs in 2006, the last time BPXA ran a smart pig was in 1998. The 1998 smart and maintenance pig runs on the WOA oil transit lines revealed no significant corrosion and only modest solids returns. We also are aware that ARCO Alaska conducted a 1990 pig run in the EOA oil transit lines, while it had operational accountability for facilities on that side of the field. Another smart pig run had been scheduled for mid-2006. Unfortunately the WOA leak occurred before this took place.

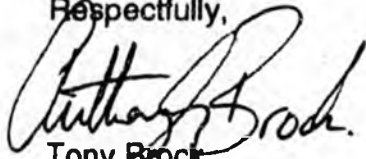
Since this past summer, BPXA has initiated a pigging schedule whereby cleaning (also called maintenance) pigs are run on a weekly basis. In addition to cleaning any solids and water residue that may have accumulated in the lines, pigging is one of a number of techniques used to control corrosion.

BPXA uses pigging, ultrasonic testing (UT), visual inspections, corrosion inhibitors and other techniques as appropriate for each individual oil field's and each line's characteristics and history. While corrosion in oil field production, processing and transmission facilities is a result of natural physical forces and cannot be completely prevented, BPXA's program was designed to control corrosion, extending the useful life of our North Slope infrastructure.

Since August, BPXA has made a number of changes in our operations. The most significant is a change to our organizational structure with the addition of a Technical Director. The Technical Director reports directly to the President of BPXA and provides independent assurance of our infrastructure integrity management.

I trust that this is responsive to your inquiry. If we can be of further assistance to your understanding of these matters, please don't hesitate to contact us.

Respectfully,

A handwritten signature in cursive script, appearing to read "Anthony Brock".

Tony Brock
Technical Director

cc Members House Special Committee on Oil and Gas

Insert":

(19) costs or a portion of the costs determined by the commissioner, in consultation with the commissioner of environmental conservation and the chair of the Alaska Oil and Gas Conservation Commission, to be

(A) related to the repair and replacement of improperly maintained property or equipment; or

(B) incurred to maintain the operational capability of facilities or equipment shut down or operating at diminished capacity because of improper maintenance of property and equipment"

SENATOR GREEN objected for explanation.

SENATOR WAGONER explained that he has presented this amendment on behalf of Senator Therriault.

SENATOR THERRIAULT said the amendment was prompted by the recent shutdown of a portion of the TAPS line due to maintenance issues, which raised the question of how repairs would be handled in a net-based PPT system. The amount of oil produced by the affected fields is approximately 375,000 barrels per day. His calculations indicate that the operating costs, even when there is no production, are about \$1 million per day. The amendment allows the commissioner of revenue, in consultation with the commissioner of the Department of Environmental Conservation (DEC), and the chairman of the Alaska Oil and Gas Conservation Commission (AOGCC) to determine what costs are attributable to lack of maintenance and disallow those costs.

1:38:20 PM

SENATOR BEN STEVENS commented that paragraph (B) on line 8 might encourage a complete shut down, because the operating expenses would not be deductible when operating at diminished capacity.

SENATOR THERRIAULT said he does not think it would have that effect, because agency personnel have the latitude to look at the costs and agree what is and is not reasonable and allowable.

SENATOR BEN STEVENS reiterated that he believes it would encourage a total shutdown and that it might provide a disincentive to replacing bad equipment.

SENATOR THERRIAULT repeated that, because the commissioners have the flexibility to make determinations on a case-by-case basis, he does not believe that would be the case.

CHAIR SEEKINS used an automobile maintenance analogy to illustrate how the agency representatives might make the determination and asked if that is how Senator Therriault sees it working.

SENATOR THERRIAULT agreed with his analogy and emphasized that this refers specifically to improperly maintained equipment.

1:43:47 PM

MR. DICKINSON, Consultant to DOR, commented that his interpretation of the amendment is that all operating costs would be disallowed as long as the plant is operating at

Minutes from:
Senate Special Committee on
Natural Gas Development
RE: shut down costs

LEGAL SERVICES

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LEGISLATIVE AFFAIRS AGENCY
STATE OF ALASKA

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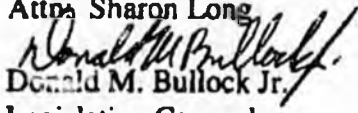
State Capitol
Juneau, Alaska 99801-1182
Deliveries to: 129 6th St., Rm. 329

MEMORANDUM

March 12, 2007

SUBJECT: Disallowance of costs associated with lack of or improper maintenance (CSSB 80(); Work Order No. 25-LS0425\M)

TO: Senator Charlie Huggins
Chair of the Senate Resources Committee
Attn: Sharon Long

FROM: 
Donald M. Bullock Jr.
Legislative Counsel

You asked for an explanation of AS 43.55.165(e)(19)(B) and (C), as offered in CSSB 80() that is being considered by your committee.

CSSB 80() proposes to amend AS 43.55.165(e) by adding an additional category of lease expenditures that are not deductible for the purpose of determining the production tax value of oil and gas. The production tax value of oil and gas is taxed at the rate stated in AS 43.55.011 and is generally determined by deducting certain lease expenditures from the gross value of oil and gas at the point of production.¹ AS 43.55.165(a) provides that, with certain exceptions, the lease expenditures are "the ordinary and necessary costs upstream of the point of production of oil and gas." AS 43.55.165(e) lists 18 types of expenditures that may not be included as lease expenditures for the purpose of determining the production tax value of oil and gas.

CSSB 80() adds an additional category of expenditures that may not be considered lease expenditures. The expenditures that would be disallowed under the bill are expenditures that were incurred because property or equipment had not been maintained or had been improperly maintained. The proposed new paragraph identifies three categories of costs that would be disallowed when the reasons for those costs are related to the failure to maintain property or equipment in accordance with the standard determined by the commissioner of revenue with the advice and counsel of the commissioner of environmental conservation, the commissioner of natural resources, and the Alaska Oil and Gas Conservation Commission.

¹ AS 43.55.160(a).

Senator Charlie Huggins

March 12, 2007

Page 2

The first category of disallowed expenses are the costs of repairing and replacing the actual property or equipment that was neglected.² These costs are described in AS 43.55.165(e)(19)(A), in sec. 1 of the bill.

The costs disallowed under AS 43.65.165(e)(19)(B) and (C) are costs that directly result from the maintenance failure. For illustration purposes, assume that some component of a production facility fails because the operator had not maintained that component as expected, taking into consideration the standard practices of the industry. The costs of replacing or repairing that component would be disallowed under paragraph (19)(A).

Now assume that the component failure took two days to repair and during those two days oil was not delivered to a treatment facility and that facility was then shut down. While that repair was being made, there was no flow of oil, no production tax because no oil was being produced, and there were costs associated with maintaining the shutdown and non-productive facility. Under AS 43.55.165(e)(19)(B) as offered in sec. 1 of the bill, the costs incurred to maintain the facilities or equipment shutdown as the result of failure of the component that had to be repaired or replaced may not be deducted.

Change the facts a little so that the flow to the facility is not completely stopped, but the volume is cut in half. Assume further that the facility described in the previous paragraph continues to operate, but of one-half of the level at which it operates when the failed component is operational. If the costs of operation at one-half the normal volume are actually three-quarters of the cost of operating at full capacity, the difference between half the costs and three-quarters of the costs would be disallowed under AS 43.55.165(e)(19)(C) as proposed in CSSB 80(). The disproportionate costs that resulted from the reduced flow would be disallowed under the bill.

CSSB 80() presents two issues for consideration by the committee. First is the level of diligence expected from a taxpayer with regard to the maintenance of production facilities. Should the state expect a level of diligence consistent with a standard that is determined by taking into consideration the standard practices of the industry, something less, or something more?

Second, if costs associated with a lack of maintenance or improper maintenance are disallowed, should the disallowance of the costs be limited to the failed equipment or all costs that result from that failure? In sec. 1 of CSSB 80(), AS 43.55.165(e)(19)(A) disallows the cost related to the repair or replacement of the equipment that failed and (e)(19)(B) and (C) disallow costs that would not have been incurred or would have been proportionately less had the neglected equipment not failed.

If I may be of further assistance, please advise.

DMB:med
07-166.mcd

² I use the word "neglected" here as a short hand for "not maintained or improperly maintained" and not to introduce a standard not contemplated in the language of the bill.



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BP admits to withholding documents

Executive receives more time to prepare for hearing on N. Slope pipeline corrosion

WASHINGTON - A top BP executive has acknowledged that the company withheld key documents last year from lawmakers who were investigating whether cost-cutting measures were a factor in the pipeline corrosion that caused Alaska's largest onshore oil spill.

In a letter that congressional Democrats disclosed on Wednesday, BP America Chairman and President Robert Malone also said that he was "troubled" by the extent of oilfield workers' frustrations in the period leading up to last year's North Slope oil spill.

Malone, who took over at BP America after the March 2006 spill in the Prudhoe Bay oilfield, said, "We need time to determine how the concerns and frustrations expressed by workers were ultimately resolved."

His letter, dated Monday, was released as leaders of the House Energy and Commerce Committee agreed to postpone a hearing on the Alaska oil spill until May 16.

Malone asked for more time to prepare for the hearing after facing new questions from committee leaders suggesting that company scrimping might have compromised testing and maintenance that could have prevented the 201,000-gallon spill. Subsequent inspections turned up corrosion in another transit pipeline, leading to a partial shutdown of the field in August.

In his plea for more time, Malone echoed some of the committee's concerns, saying some of BP's recently produced records "raise concerns about previous spending decisions that cause me concern."

In keeping with Malone's efforts to portray a new culture of openness at BP, he said that company officials failed to disclose a 2002 state compliance order referring to pipeline sediments that could have contributed to pitting and corrosion.

Malone said the document only recently came to his attention and that of the head of BP Alaska. It also wasn't disclosed to the energy committee during a hearing in September.

While Malone said he's ordered an investigation, some company officials have determined that the document was overlooked because it pertained to leak detection and not specifically to corrosion.

But the connection became clearer as company officials amassed some 20 million documents in connection with congressional and other federal investigations into the spill and subsequent oil disruptions in the nation's top-producing oil field.

"Our process for gathering and producing documents for the committee was not what it should have been," said BP spokesman Ronnie Chappell.

It was during this same time frame, he indicated, that worker frustrations were vented - apparently to no avail. That, he said, will change.

"I want to eliminate the frustration voiced in many of the documents by creating a culture in which workers are confident their concerns will be heard and addressed before they would ever reach the level of frustration expressed in these historical documents," Malone wrote.

Congressional leaders cited Malone's misgivings about the missing documents in their decision to grant the company more time.

"We now know that BP proceeded with cost-cutting measures that may have compromised pipeline safety while earning \$22 billion in profits, but what we don't know is why," said Energy Committee Chairman John Dingell, D-Mich.

In a letter co-signed by fellow Michigan Democrat Bart Stupak, chairman of the panel's oversight subcommittee, Dingell said, "The discovery of this material has clearly raised questions about the adequacy of your response to the committee, as well as previous spending decisions made by your company."

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Oil giant faces questions about deadly blast in Texas

Wednesday, July 27, 2005

By Chip Cummins and Thaddeus Herrick

TEXAS CITY, Texas -- After a huge explosion at a BP PLC plant here in March killed 15 workers in the deadliest U.S. petrochemical-industry accident in 15 years, the company put most of the blame on some of its employees.

But now the search for the cause is raising some unsettling questions.

London-based BP acknowledges faulty equipment and other troubles at the unit at the Texas City refinery where the explosion occurred, although it doesn't directly connect those problems to the accident. In addition to the deaths, more than 170 people were injured.

Two federal agencies have pointed to safety problems at Texas City. And all this comes against the backdrop of cost-cutting in an industry with very old equipment.

Tuesday, BP said that it had set aside \$700 million to cover compensation for victims' families and those injured in the March 23 blast.

But the company could still face regulatory action. Managers at the Texas City refinery "don't have a culture of safety that looks at all the details," said John Miles, Southwest regional director for the Occupational Safety and Health Administration. OSHA is investigating the deadly explosion. Mr. Miles notes that over the past 16 months, there have been two other major accidents at Texas City. In September 2004, two employees were scalded to death while removing a valve from a hot-water line. In March 2004, the refinery had a big, nonfatal fire.

Three significant accidents in that span of time are "a concern," Mr. Miles said. In addition, in May 2004, a contractor was killed in a fall at the refinery, although the contractor's employer, not BP, was cited.

In April, OSHA put the BP refinery on a national watch list of safety violators in all industries. OSHA doesn't publicly release the list but confirmed that BP is one of only two refiners among some 700 companies identified. OSHA said the other is Coffeyville Resources Refining & Marketing LLC, a much smaller operation in Coffeyville, Kan. Coffeyville Resources said that it believes its inclusion on the list reflects the accidental death of an employee in May 2004. The company said that overall it "enjoys a good safety record."

Another federal body, the Chemical Safety and Hazard Investigation Board, is conducting its own probe. Spokesman Daniel Horowitz said the board so far has identified a number of safety problems at Texas City.

BP publicly issued a report in May that accused some of its midlevel plant managers and hourly workers of "surprising and deeply disturbing" mistakes. These errors allegedly included a failure to provide supervision and disregard of company procedures. BP has removed the refinery's top manager and fired a handful of other employees -- but won't say how many.

A lawsuit filed in state court in Galveston claims that the ultimate blame lies with BP. The suit alleges corporate "gross negligence" and seeks unspecified damages on behalf of victims' families and several people injured in March at the sprawling refinery near Galveston Bay.

One of the suit's original plaintiffs was David Crow, a 58-year-old outside maintenance

contractor. In the early afternoon on March 23, he heard a thundering noise and then was buried beneath debris. He fractured six vertebrae and shattered his foot and ankle. "People lost their lives over something that could have been avoided," said Mr. Crow, who now uses a walker to get around. After being interviewed for this article, he agreed to settle his claim against BP on confidential terms.

The explosion occurred when workers restarted a small gasoline-processing unit, an operation that is inherently tricky because many controls are adjusted at once and combustible substances begin moving rapidly.

BP is walking a fine line in its response to the accident. It has denied any negligence and is cooperating with federal investigators. But it also has apologized and promised to continue settling with survivors and victims' families. Many settlements have already been agreed to, the company said, without providing details.

BP has denied any connection between cost-cutting and plant fatalities. It contends that overall safety at its American refineries has improved since it acquired them.

"I think the culture of safety, in terms of policies and procedures, was there," said Ross Pillari, president of BP Products North America. "But the implementation of these policies and procedures was clearly not there, because if it was, the accidents wouldn't have happened."

BP has five refineries in the U.S. Two others that, like Texas City, were acquired during a buying spree started in the late-1990s have also had worker deaths recently.

On New Year's Day 2004, a technician at a plant in Whiting, Ind., fell and cracked his skull after a corroded handrail gave way. BP investigators concluded in an internal report, separate from the one issued in May, that there hadn't been a procedure to inspect and repair the facility's handrails, which date to the 1940s. BP said that it has since inspected all handrails at its refineries. Indiana regulators fined BP \$1,625 over the incident.

In May, a contractor was found dead at BP's refinery in Cherry Point, Wash. An initial company investigation has found no evidence that the death was related to an accident, a person familiar with the inquiry said. The death is under investigation by the county coroner and state safety regulators.

Even excluding the Cherry Point death and the 15 fatalities in March, BP's four other deaths since January 2002 are more than the number recorded by its main rivals in the U.S., according to federal data and information provided by the companies. BP is America's third-largest refiner. No. 1 ConocoPhillips and No. 2 Exxon Mobil Corp. each had one death during that period.

There hasn't been a new oil refinery built in the U.S. since 1976, and most plants show their age. New construction has been discouraged by stricter environmental rules and other factors. Regulators say that old facilities don't necessarily pose unusual dangers, as long as effective safety and maintenance programs are in place.

The world's second-largest publicly traded oil company, BP operates internationally and does everything from drilling for oil to running gasoline stations. Its global safety record -- measured by hours workers miss because of injury and accidents that merit reporting to regulators -- is one of the industry's best.

Using the motto "Beyond Petroleum," the company has promoted its image for social responsibility. Chief Executive John Browne has championed attempts to reduce global warming by lowering carbon-dioxide emissions at BP facilities.

The company grew suddenly when it purchased Amoco Corp. in 1998 and later scooped up

Atlantic Richfield Co. BP's success in improving efficiency and lowering costs at its newly acquired American refineries has been shown in a periodic survey done by the Dallas consulting firm Solomon Associates. Widely used for comparing refinery performance, the survey showed that in 2000, BP's U.S. plants ranked in the middle of the industry on measures such as return on investment. By 2004, BP rose to the top 25 percent. Last year, BP reported overall profit of \$15.7 billion on revenue of \$294.9 billion.

The municipality of Texas City has long been an industrial hub. In 1947, it suffered one of the country's worst industrial accidents ever when a ship full of fertilizer exploded, killing nearly 600 people.

BP acquired the Texas City refinery from Amoco. In the 1990s, Amoco had reduced the plant's unionized work force by 19 percent, to 1,300 people, according to Sonny Sanders, a former Texas City employee and longtime labor-union official. Under Amoco, major maintenance overhauls, called "turnarounds," became less frequent, said Mr. Sanders, now a United Steelworkers representative. BP said it wasn't in a position to comment on Amoco's actions. The steelworkers union, which represents BP employees, has challenged the company's findings on the blast and is conducting its own probe.

As it absorbed its American acquisitions in 1999 and 2000, BP cut its work force of U.S. refinery employees and contractors by 10 percent, largely by means of buyouts in Texas City and Whiting, Ind. At Texas City, the staff of unionized maintenance craftsmen and operators fell by 213, or about 18 percent, the company said in written answers to questions for this article. The reductions were partially offset by greater use of outside contractors, BP added.

"The approach to reducing costs was well thought out and systematic," BP's Mr. Pillari said. It "does not appear, in so far as we have seen, to have had anything to do with the fatalities" at Texas City or anywhere else, he adds. The company said in written answers that it has steadily increased overall spending on maintenance in the U.S. At Texas City in 2003-2004, BP said that it spent 40 percent more per barrel of oil it refined than was spent in 1997-1998 under Amoco. BP declined to disclose dollar figures.

Current and former Texas City employees and contractors paint a different picture. Under BP, the refinery deferred some routine maintenance inspections because of staff shortages, according to three former employees and one current worker. In addition, certain safety procedures have been ignored at the plant, according to seven people who have worked there. Contractors and BP employees sometimes work high above ground without proper safety gear, according to four of these people. BP said that it requires strict compliance with its policies for working at an elevation.

But OSHA's regional director, Mr. Miles, said that managers at other Texas refineries he has inspected, including one nearby owned by Valero Energy Corp., are more actively involved in safety issues. "You don't see that down the street" at BP, he said.

Mr. Crow, the veteran maintenance contractor who was injured in March at Texas City, said disrepair at the plant was worse than what he has seen at comparable refineries. He said he was particularly troubled by corroding metal springs that hold refinery pipes in place. "Everything out there is rusty," he said.

Glenn Alexander, a 45-year-old electrical contractor who suffered shoulder and back injuries in the March blast, said corrosion plagued much of the refinery. Last year, he said, a metal structure supporting power and communications lines high above ground collapsed because of corrosion. No one was injured. Another section of the same sort of structure "was wobbly and could have fallen any minute," he said. Mr. Alexander was a plaintiff in the negligence suit against BP but agreed to a confidential settlement after he was interviewed.

The company said that it aggressively addresses corrosion, sometimes shutting down certain operations to do so. Citing the large size of the plant, BP said it couldn't confirm the incidents

Mr. Alexander described.

Last year, before the March explosion, BP shook up its maintenance-inspection program at Texas City, replacing the top inspectors. But the company emphasized that inspection-staffing levels weren't "a critical issue."

BP executives said that overall, the company's U.S. operations are sound. Still, it is auditing safety procedures at all of its U.S. plants, trying to determine if any are "resource constrained," BP's Mr. Pillari said.

The blast in March occurred in a part of the refinery known as an isomerization unit, or isom. It processes gasoline to boost octane, which prevents engine knocks. BP's report on the accident in May details a series of past problems at the isom but doesn't link that history to the accident.

Since 1986, employees had recorded seven fires at the isom, not including the March blast, the company said. This small section of the refinery consisted of a control room, a 164-foot processing tower and venting equipment, which included a 113-foot "blowdown" stack. The blowdown stack released buildups of dangerous liquid or vapor in emergencies.

BP's report said that a water system used to cool the venting equipment had been out of service for some time before the huge blowup. Baffles, which are metal plates that aid the condensation of vapor, had corroded badly.

In April 1997, Steven Adams, an isom-unit operator, filed a suggestion to Amoco management to replace a faulty pump connected to the venting system. If the pump failed, combustible liquids could overflow into the refinery sewer system and possibly ignite. Amoco apparently never acted on the suggestion. Six months after BP took over the plant, the idea was rejected as "not cost effective," according to an internal company memo.

Mr. Adams was one of the employees fired after the March blast. Last month, he filed a defamation suit against BP in Texas state court, alleging that the company ruined his reputation by unfairly blaming him and others for the deadly explosion. BP declined to comment on the Adams firing or the suit.

The decision not to replace the isom unit's pump could prove significant. In its report, BP said it was possible that combustible material escaped from the venting system into the sewer and ignited there, setting off the blast. But in its written responses to questions for this article, BP said there is no indication the pump malfunctioned.

In February, operators of the isom unit shut it down for maintenance. Mr. Crow and dozens of other outside contractors were working out of trailers nearby. BP said in its report that the contractors weren't warned about the potentially dangerous restarting of the unit, as they should have been.

The isom unit's daytime supervisor, Scott Yerrell, arrived late the morning of March 23, according to BP's report, which didn't identify him by name. Then, just before 11 a.m., he left the plant for personal reasons, the report said. BP fired him after the accident.

Mr. Yerrell is a co-plaintiff in the defamation suit against BP. His attorney, Charles Dunkel, said that his client left to attend emergency surgery for his son, who had broken his arm the day before. Mr. Yerrell lined up a replacement to supervise the start-up and shouldn't have been fired, the lawyer said.

By 12:40 p.m., pressure and heat had climbed above normal levels in the isom unit's processing tower, where gasoline components are separated, the BP report said. A worker outside the unit called the control room to report steam-like vapor coming from the unit's smoke stack, an indication that something might have been going wrong.

At about 1:20, a small explosion occurred, followed by a much louder one. Some people on the scene said that they heard a series of explosions. The blasts shook windows in houses miles away. BP said the most likely cause was that explosive vapor and liquid ignited after operators overfilled the processing tower and the volatile mix vented out of the stack.

While continuing to press its investigation, the federal Chemical Safety Board has said that some of the isom unit's alarms and indicators appear to have failed to notify workers about dangerous levels of liquid building up in the unit's processing tower. The board is also studying why BP placed the contractors' trailers so close to the isom plant.

BP said that the alarms weren't a critical factor in the accident. In its May report, it acknowledged that the trailers were too close to the isom.

Mr. Alexander, the injured electrician, watched the destruction of the trailer in which his wife, Lorena Cruz-Alexander, was working as an administrator. He identified her remains several days later. "If I had known a unit was starting up, Lorie wouldn't have been anywhere near this site," he said. "I wouldn't have been anywhere near the site."

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not" + *fas* "right") 1. gods forbid. 2. Roman law or custom. 3. Hist.

"not" + *fastus* "lawful". A day when it is administered justice, or priests in charge of religious observances established on certain days, devoted to religious or sacred duties. Cf. *dies nefasti*. Cf. *dies*

lily; to render ineffec-

to something bad; not. 2. Of or relating to a negative adjective <a negative an-

of denial or refusal. 2. A word expressing <two negatives and all plate of a photograph are the opposite created and printed on the negatives, were inverted. The power of

ly, nullify, or render fraud>

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patent application, a element is not or does does. [Cases: Patents

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revision requiring without giving security lenders any security lender. 2. A prom-

tion, usu. in a bond indenture, stating that the issuing entity will not pledge its assets if it will result in less security to the bondholders under the indenture agreement.

negative pregnant. A denial implying its affirmative opposite by seeming to deny only a qualification of the allegation and not the allegation itself. • An example is the statement, "I didn't steal the money last Tuesday," the implication being that the theft might have happened on another day. — Also termed *negative pregnant with an affirmative*. Cf. AFFIRMATIVE PREGNANT. [Cases: Pleading §126. C.J.S. Pleading § 191.]

negative prescription. See PRESCRIPTION (4).

negative proof. See PROOF.

negative reprisal. See REPRISAL.

negative right. See RIGHT.

negative servitude. See SERVITUDE (2).

negative statute. See STATUTE.

negative testimony. See *negative evidence* under EVIDENCE.

negative veto. See *qualified veto* under VETO.

neglect, n. 1. The omission of proper attention to a person or thing, whether inadvertent, negligent, or willful; the act or condition of disregarding. 2. The failure to give proper attention, supervision, or necessities, esp. to a child, to such an extent that harm results or is likely to result. Cf. ABUSE. — **neglect, adj.** — **neglectful, adj.**

"Neglect" is not the same thing as "negligence." In the present connection the word "neglect" indicates, as a purely objective fact, that a person has not done that which it was his duty to do; it does not indicate the reason for this failure. "Negligence," on the other hand, is a subjective state of mind, and it indicates a particular reason why the man has failed to do his duty, namely because he has not kept the performance of the duty in his mind as he ought to have done. A man can "neglect" his duty either intentionally or negligently." J.W. Cecil Turner, *Kenny's Outlines of Criminal Law* 108 n.1 (16th ed. 1952).

child neglect. The failure of a person responsible for a minor to care for the minor's emotional or physical needs. • Child neglect is a form of child abuse. Local child-welfare departments investigate reports of child neglect. In a severe case, criminal charges may be filed against a person suspected of child neglect. [Cases: Infants §156.]

culpable neglect. Censurable or blameworthy neglect; neglect that is less than gross carelessness but more than the failure to use ordinary care.

developmental neglect. Failure to provide necessary emotional nurturing and physical or cognitive stimulation, as a result of which a child could suffer from serious developmental delays.

educational neglect. Failure to ensure that a child attends school in accordance with state law.

excusable neglect. A failure — which the law will excuse — to take some proper step at the proper time (esp. in neglecting to answer a lawsuit) not because of the party's own carelessness, inattention, or willful disregard of the court's process, but because of some unexpected or unavoidable hin-

drance or accident or because of reliance on the care and vigilance of the party's counsel or on a promise made by the adverse party. [Cases: Federal Civil Procedure §2656; Judgment §362. C.J.S. Judgments § 320.]

inexcusable neglect. Unjustifiable neglect; neglect that implies more than unintentional inadvertence. • A finding of inexcusable neglect in, for example, failing to file an answer to a complaint will prevent the setting aside of a default judgment. [Cases: Federal Civil Procedure §2656; Judgment §362. C.J.S. Judgments § 320.]

medical neglect. Failure to provide medical, dental, or psychiatric care that is necessary to prevent or to treat serious physical or emotional injury or illness. • In determining whether a parent's refusal to consent to medical treatment is neglectful, courts use any of three approaches: (1) an ad hoc test, (2) a best-interests-of-the-child test, or (3) a balancing test that weighs the interests of the parents, the child, and the state. Cf. FAITH-HEALING EXEMPTION.

physical neglect. Failure to provide necessities, the lack of which has caused or could cause serious injury or illness.

willful neglect. Intentional or reckless failure to carry out a legal duty, esp. in caring for a child.

neglected child. See CHILD.

neglect hearing. See HEARING.

negligentia (neg-li-jen-shee-ə), *n.* [Latin] Roman law. Carelessness; inattentive omission. • *Negligentia* can be of varying degrees, which may or may not result in actionable liability. — Also spelled *negligentia*. See CULPA. Cf. DILIGENTIA.

"In the sources *negligentia* is tantamount to *culpa*, and similarly graduated (*magna, lata negligentia*). Precision in terminology is no more to be found here than in the field of *culpa*. One text declares gross negligence (*magna negligentia*) is *culpa*, *magna culpa* is *dolus*; another says: gross negligence (*dissoluta negligentia*) is near to *dolus* (*prope dolum*). In the saying *lata culpa* is exorbitant (extreme) negligence, i.e., not to understand (*intelligere*) what all understand *negligentia* is identified with ignorance." Adolf Berger, *Encyclopedic Dictionary of Roman Law* 593 (1953).

lata negligentia (lay-tə neg-li-jen-shee-ə). Extreme negligence resulting from an unawareness of something that the actor should have known.

magna negligentia (mag-nə neg-li-jen-shee-ə). See gross negligence under NEGLIGENCE.

negligence, n. 1. The failure to exercise the standard of care that a reasonably prudent person would have exercised in a similar situation; any conduct that falls below the legal standard established to protect others against unreasonable risk of harm, except for conduct that is intentionally, wantonly, or willfully disregarding of others' rights. • The term denotes culpable carelessness. The Roman-law equivalents are *culpa* and *negligentia*, as contrasted with *dolus* (wrongful intention). — Also termed *actionable negligence*; *ordinary negligence*; *simple negligence*. [Cases: Negligence §201, 233, 250. C.J.S. Negligence §§ 14, 34, 59, 118-121, 125-127, 130-131, 133.] 2. A tort grounded in this failure, usu. expressed in terms of the following elements: duty, breach of duty, causa-

tion, and damages. [Cases: Negligence \S 202. C.J.S. Negligence \S 21-31, 64, 649.]

"Negligence in law ranges from inadvertence that is hardly more than accidental to sinful disregard of the safety of others." Patrick Devlin, *The Enforcement of Morals* 36 (1968).

"During the first half of the nineteenth century, negligence began to gain recognition as a separate and independent basis of tort liability. Its rise coincided in a marked degree with the Industrial Revolution; and it very probably was stimulated by the rapid increase in the number of accidents caused by industrial machinery, and in particular by the invention of railways. It was greatly encouraged by the disintegration of the old forms of action, and the disappearance of the distinction between direct and indirect injuries, found in trespass and case . . . Intentional injuries, whether direct or indirect, began to be grouped as a distinct field of liability, and negligence remained as the main basis for unintended torts. Negligence thus developed into the dominant cause of action for accidental injury in this nation today." *W. Puge Keeton et al., Prosser and Keeton on the Law of Torts* \S 28, at 161 (5th ed. 1984).

"Negligence is a matter of risk — that is to say, of recognizable danger of injury . . . In most instances, it is caused by heedlessness or inadvertence, by which the negligent party is unaware of the results which may follow from his act. But it may also arise where the negligent party has considered the possible consequences carefully, and has exercised his own best judgment. The almost universal use of the phrase 'due care' to describe conduct which is not negligent should not obscure the fact that the essence of negligence is not necessarily the absence of solicitude for those who may be adversely affected by one's actions but is instead behavior which should be recognized as involving unreasonable danger to others." *Id.* \S 31, at 169.

active negligence. Negligence resulting from an affirmative or positive act, such as driving through a barrier. Cf. *passive negligence*.

advertent negligence. Negligence in which the actor is aware of the unreasonable risk that he or she is creating; **RECKLESSNESS**. — Also termed *willful negligence*; *supine negligence*.

casual negligence. A plaintiff's failure to (1) pay reasonable attention to his or her surroundings, so as to discover the danger created by the defendant's negligence, (2) exercise reasonable competence, care, diligence, and skill to avoid the danger once it is perceived, or (3) prepare as a reasonable person would to avoid future dangers.

collateral negligence. An independent contractor's negligence, for which the employer is generally not liable. See **COLLATERAL NEGLIGENCE DOCTRINE**.

comparative negligence. A plaintiff's own negligence that proportionally reduces the damages recoverable from a defendant. — Also termed *comparative fault*. See **COMPARATIVE NEGLIGENCE DOCTRINE**. [Cases: Negligence \S 549. C.J.S. Negligence \S 262-264.]

concurrent negligence. The negligence of two or more parties acting independently but causing the same damage. Cf. *joint negligence*.

contributory negligence. 1. A plaintiff's own negligence that played a part in causing the plaintiff's injury and that is significant enough (in a few jurisdictions) to bar the plaintiff from recovering damages. • In most jurisdictions, this defense has been superseded by comparative negligence. See **CONTRIBUTORY NEGLIGENCE DOCTRINE**. [Cases: Negligence \S 547. C.J.S. Negligence \S 293, 297.] 2.

Rare. The negligence of a third party — neither the plaintiff nor the defendant — whose act or omission played a part in causing the plaintiff's injury. [Cases: Negligence \S 540. C.J.S. Negligence \S 267.]

"The contributory negligence of a third party is no excuse for the negligence of the defendant." Thomas E. Holland, *The Elements of Jurisprudence* 154 (13th ed. 1924).

criminal negligence. Gross negligence so extreme that it is punishable as a crime. • For example, involuntary manslaughter or other negligent homicide can be based on criminal negligence, as when an extremely careless automobile driver kills someone. — Also termed *culpable negligence*; *gross negligence*. [Cases: Criminal Law \S 23; Negligence \S 1800-1802. C.J.S. Criminal Law \S 38; Negligence \S 913-914, 916.]

"Though the legislatures and the courts have often made clear that criminal liability generally requires more fault than the ordinary negligence which will do for tort liability, they have not so often made it plain just what is required in addition to tort negligence — greater risk, subjective awareness of the risk, or both. Statutes are sometimes worded in terms of 'gross negligence' or 'culpable negligence' or 'criminal negligence,' without any further definition of these terms . . . The courts thus have had to do their best with little guidance from the legislature, with varying results." Wayne R. LaFare & Austin W. Scott Jr., *Criminal Law* \S 37, at 235-37 (2d ed. 1986).

culpable negligence. 1. Negligent conduct that, while not intentional, involves a disregard of the consequences likely to result from one's actions. 2. See **criminal negligence**.

"'Culpable negligence' while variously defined, has been held incapable of exact definition; it means something more than negligence . . . In connection with negligence, the word 'culpable' is sometimes used in the sense of 'blameworthy,' and it has been regarded as expressing the thought of a breach of a duty or the commission of a fault; but culpable negligence has been held to amount to more than 'blameworthy' conduct . . . It does not involve the element of intent . . . On the other hand, it has been said to be intentional conduct which the actor may not intend to be harmful but which an ordinary and reasonably prudent man would recognize as involving a strong probability of injury to others." 65 C.J.S. Negligence \S 1(13) (1966).

gross negligence. 1. A lack of slight diligence or care. [Cases: Negligence \S 273. C.J.S. Negligence \S 91-97.] 2. A conscious, voluntary act or omission in reckless disregard of a legal duty and of the consequences to another party, who may typically recover exemplary damages. — Also termed *reckless negligence*; *wanton negligence*; *willful negligence*; *willful and wanton negligence*; *hazardous negligence*; *magna negligentia*. [Cases: Damages \S 91; Negligence \S 273. C.J.S. Damages \S 202-207; Negligence \S 91-97.] 3. See **criminal negligence**.

"Negligence is gross if the precautions to be taken against harm are very simple, such as persons who are but poorly endowed with physical and mental capacities can easily take." H.L.A. Hart, "Negligence, Mens Rea, and Criminal Responsibility," in *Punishment and Responsibility* 136, 149 (1968).

"Gross Negligence. As it originally appeared, this was very great negligence, or the want of even slight or scant care. It has been described as a failure to exercise even that care which a careless person would use. Several courts, however, dissatisfied with a term so nebulous . . . have construed gross negligence as requiring willful, wanton, or reckless misconduct, or such utter lack of all care as will be evidence thereof . . . But it is still true that most courts consider that 'gross negligence' falls short of a reckless disregard of the consequences, and differs from ordinary

negligence only in *Keeton et al., Prosser* at 211-12 (5th ed. 19

hazardous negligence. Negligence that exposes injury or to imminent

imputed negligence. Negligence charged to another party's special relationship is originally negligent parent might be held a child. [Cases: Negligence \S 13.5(2), 268-280; Parent and

inadvertent negligence. Actor is not aware or she is creating, avoided it. — Also

joint negligence. Two persons acting together

concurrent negligence

legal negligence. See

negligence in law. Imposed by law. See

negligence per se. Inter of law, so that question. • Negligence statutory violation. [Cases: Negligence \S 134-147.]

ordinary negligence. The failure to use most commonly used negligence and gross negligence \S 232.]

passive negligence. Person's failure of failing to remove lic property. Cf. *active*

professional negligence

reckless negligence.

simple negligence.

slight negligence. Negligence of care of an extraordinary nature involving liability in ; involving bailmen ordinary care would great diligence.

subsequent negligence. Defendant when, after negligence and the plaintiff the defendant discovered — that the danger and fails to the plaintiff's injury negligence. See *LAS Negligence* \S 53(313, 318.)

supine negligence.

tax negligence. Negligence of tax-payment

30 Cents per Barrel Disallowance Example

PPT Calculation

(Revenue - Costs - Investment) x 22.5% - (Investment x 20%) Less Other Credits, Plus Surtax = Tax Owed

$(\$62.66 - \$6.38 - \$6.31) \times 22.5\% - (\$6.31 \times 20\%) = \$9.98 \text{ per barrel}$

$-\$0.30 \qquad \qquad \qquad -\0.30

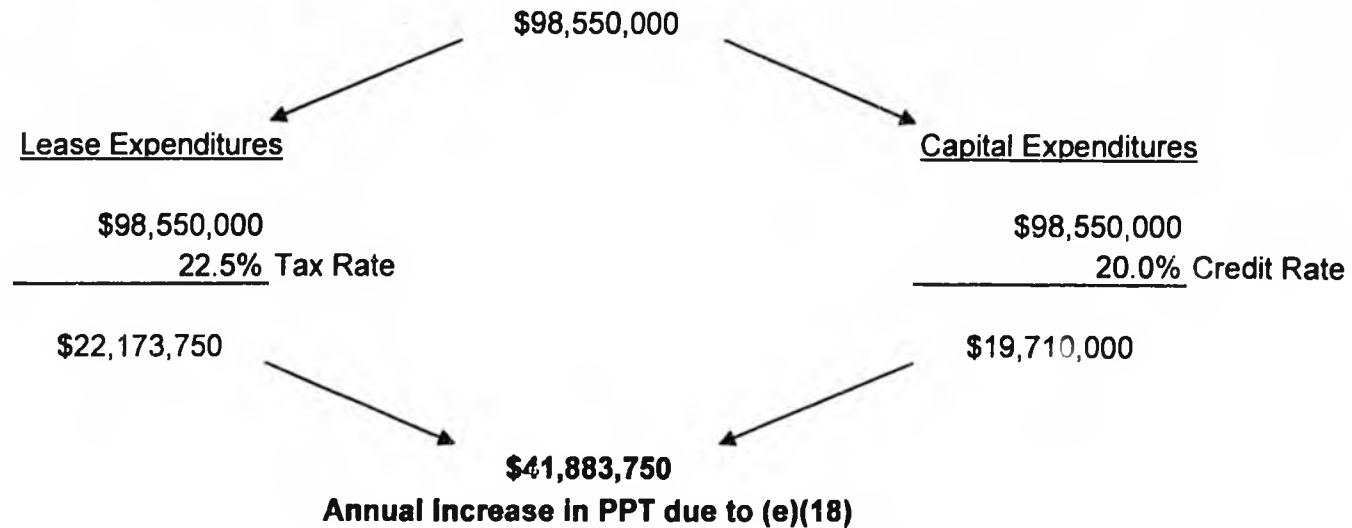
$(\$62.66 - \$6.38 - \$6.01) \times 22.5\% - (\$6.01 \times 20\%) = \$10.11 \text{ per barrel}$

Disallowing "deemed capital maintenance" costs

900,000 barrels/day
365 days/year

328,500,000 barrels/year
0.30 cents/barrel

\$98,550,000 per year reduction for (a) lease expenditures; and (b) capital expenditures



"I believe that this would provide a good answer to possible public criticism that under the PPT we would provide 50% of the replacement costs of pipelines as a result of the Prudhoe Bay shut down."

Pedro van Meurs, August 8, 2006 letter

ALASKA STATE LEGISLATURE

REPRESENTATIVE KURT OLSON

- Chair, Labor and Commerce
- Vice-Chair, Oil and Gas
- Member, Community and Regional Affairs

Session: January – May
State Capitol
Juneau, AK 99801-1182
Phone: 907-465-2693
Fax: 907-465-3835



Interim: May – December
145 Main Street Loop, Ste 221
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Official Business

Sponsor Statement

HB 128 – Disallows PPT Reductions for Improperly Maintained Facilities

HB 128 cleans up language and closes a loophole in the recently passed Petroleum Production Tax (PPT) legislation.

As currently written, producers may deduct or use as credits, expenses for repairs made to infrastructure that has been improperly maintained. Once HB128 is enacted, deductions or credits against the PPT for these types of repairs will be subject to review and approval.

This bill instructs the Commissioner of the Revenue to consult with the Commissioner of the DEC and the Chair of AOGCC. Relying on standard practices of the industry, they will determine the portion of the costs related to repair or replacement of improperly maintained property or equipment available for deduction or use as a credit

This concept came forward as an amendment in the Senate Resources Committee in early August of 2006. The ongoing corrosion problem currently experienced by BP serves to emphasize the importance of this change in statute.

The responsibility for the expenses related to repairs made to improperly maintained infrastructure should not lie with the State of Alaska.

I respectfully ask for your support of this bill.

HOUSE BILL NO. 128

IN THE LEGISLATURE OF THE STATE OF ALASKA

TWENTY-FIFTH LEGISLATURE - FIRST SESSION

BY REPRESENTATIVES OLSON, Harris, Ramras, Guttenberg, Neuman, Holmes, Thomas, Stoltze, Joule, Fairclough, LeDoux, Kerttula, Wilson, Lynn, Crawford, Gara, Gruenberg, Doll, Doogan, Edgmon, Buch

Introduced: 2/12/07

Referred: House Special Committee on Oil and Gas, Resources, Finance

A BILL

FOR AN ACT ENTITLED

1 **"An Act relating to allowable lease expenditures for the purpose of determining the**
2 **production tax value of oil and gas for the purposes of the oil and gas production tax;**
3 **and providing for an effective date."**

4 **BE IT ENACTED BY THE LEGISLATURE OF THE STATE OF ALASKA:**

5 *** Section 1.** AS 43.55.165(e) is amended to read:

6 (e) For purposes of this section, lease expenditures do not include

7 (1) depreciation, depletion, or amortization;

8 (2) oil or gas royalty payments, production payments, lease profit
9 shares, or other payments or distributions of a share of oil or gas production, profit, or
10 revenue;

11 (3) taxes based on or measured by net income;

12 (4) interest or other financing charges or costs of raising equity or debt
13 capital;

14 (5) acquisition costs for a lease or property or exploration license;

- 1 (6) costs arising from fraud, wilful misconduct, or gross negligence;
- 2 (7) fines or penalties imposed by law;
- 3 (8) costs of arbitration, litigation, or other dispute resolution activities
- 4 that involve the state or concern the rights or obligations among owners of interests in,
- 5 or rights to production from, one or more leases or properties or a unit;
- 6 (9) costs incurred in organizing a partnership, joint venture, or other
- 7 business entity or arrangement;
- 8 (10) amounts paid to indemnify the state; the exclusion provided by
- 9 this paragraph does not apply to the costs of obtaining insurance or a surety bond from
- 10 a third-party insurer or surety;
- 11 (11) surcharges levied under AS 43.55.201 or 43.55.300;
- 12 (12) for a transaction that is an internal transfer or is otherwise not an
- 13 arm's length transaction, expenditures incurred that are in excess of fair market value;
- 14 (13) an expenditure incurred to purchase an interest in any corporation,
- 15 partnership, limited liability company, business trust, or any other business entity,
- 16 whether or not the transaction is treated as an asset sale for federal income tax
- 17 purposes;
- 18 (14) a tax levied under AS 43.55.011;
- 19 (15) the portion of costs incurred for dismantlement, removal,
- 20 surrender, or abandonment of a facility, pipeline, well pad, platform, or other
- 21 structure, or for the restoration of a lease, field, unit, area, body of water, or right-of-
- 22 way in conjunction with dismantlement, removal, surrender, or abandonment, that is
- 23 attributable to production of oil or gas occurring before April 1, 2006; the portion is
- 24 calculated as a ratio of the amount of oil and gas production, in barrels of oil
- 25 equivalent, associated with the facility, pipeline, well pad, platform, other structure,
- 26 lease, field, unit, area, body of water, or right-of-way occurring before April 1, 2006,
- 27 to the total amount of oil and gas production, in barrels of oil equivalent, associated
- 28 with that facility, pipeline, well pad, platform, other structure, lease, field, unit, area,
- 29 body of water, or right-of-way through the end of the calendar month before
- 30 commencement of the dismantlement, removal, surrender, or abandonment; a cost is
- 31 not excluded under this paragraph if the dismantlement, removal, surrender, or

1 abandonment for which the cost is incurred is undertaken for the purpose of replacing,
 2 renovating, or improving the facility, pipeline, well pad, platform, or other structure;
 3 for the purposes of this paragraph, "barrel of oil equivalent" means

4 (A) in the case of oil, one barrel;

5 (B) in the case of gas, 6,000 cubic feet;

6 (16) costs incurred for containment, control, cleanup, or removal in
 7 connection with any unpermitted release of oil or a hazardous substance and any
 8 liability for damages imposed on the producer or explorer for that unpermitted release;
 9 this paragraph does not apply to the cost of developing and maintaining an oil
 10 discharge prevention and contingency plan under AS 46.04.030;

11 (17) costs incurred to satisfy a work commitment under an exploration
 12 license under AS 38.05.132;

13 (18) that portion of expenditures, that would otherwise be qualified
 14 capital expenditures as defined in AS 43.55.023(k), incurred during a calendar year
 15 that are less than the product of \$0.30 multiplied by the total taxable production from
 16 each lease or property, in BTU equivalent barrels, during that calendar year, except
 17 that, when a portion of a calendar year is subject to this provision, the expenditures
 18 and volumes shall be prorated within that calendar year;

19 (19) costs or that portion of the costs determined by the
 20 commissioner, in consultation with the commissioner of environmental
 21 conservation and ~~the chair of the Alaska Oil and Gas Conservation Commission~~
 22 and relying on the standard practices of the industry, to be

23 (A) related to the repair and replacement of improperly ^{no} maintained
 24 property or equipment;

25 (B) incurred to maintain the operational capability of
 26 facilities or equipment shut down because of improper maintenance of
 27 property or equipment; or

28 (C) for operating facilities or equipment at diminished
 29 capacity in proportion to the amount of diminished capacity that is caused
 30 by the improper maintenance of property or equipment.

31 * Sec. 2. The uncoded law of the State of Alaska is amended by adding a new section to

1 read:

2 APPLICABILITY. Section 1 of this Act applies to oil and gas produced after
3 March 31, 2006.

4 * Sec. 3. The uncodified law of the State of Alaska is amended by adding a new section to
5 read:

6 TRANSITIONAL PROVISIONS. (a) A person that filed a statement under
7 AS 43.55.030 before the effective date of this Act and deducted lease expenditures that may
8 not be deducted under AS 43.55.165(e), as amended by sec. 1 of this Act, shall file an
9 amended return and pay any additional tax within 90 days after the effective date of this Act.

10 (b) A person required to make an installment payment of estimated tax under
11 AS 43.55.020(a) for a period not included in a return required to be filed before the effective
12 date of this Act shall determine the amount of the underpayment, if any, that is attributable to
13 lease expenditures that may not be deducted under AS 43.55.165(e) as amended by sec. 1 of
14 this Act. The amount of any underpayment determined under this subsection shall be paid
15 within 90 days after the effective date of this Act.

16 * Sec. 4. The uncodified law of the State of Alaska is amended by adding a new section to
17 read:

18 RETROACTIVITY. Section 1 of this Act is retroactive to April 1, 2006.

19 * Sec. 5. This Act takes effect immediately under AS 01.10.070(c).

ALASKA STATE LEGISLATURE

REPRESENTATIVE KURT OLSON

- Chair, Labor and Commerce
- Vice-Chair, Oil and Gas
- Member, Community and Regional Affairs

Session: January – May
State Capitol
Juneau, AK 99801-1182
Phone: 907-465-2693
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Interim: May – December
145 Main Street Loop, Ste 221
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Official Business

Sectional Analysis

HB 128 - Disallows PPT Reductions for Improperly Maintained Facilities

Section 1: amends AS 43.55.165(e) which establishes lease expenditures not available for use as credits or deductions to the Petroleum Production Tax (PPT).

New subsection (19) establishes new language regarding costs related to the repair and replacement of improperly maintained property or equipment.

These costs are subject to review by the Commissioner of The Department of Revenue, the Commissioner of the Department of Environmental Conservation and the chair of the Alaska Oil and Gas Conservation Commission, relying on industry standards.

Section 2: provides for applicability to the oil and gas produced after March 31, 2006, as with the PPT.

Section 3: provides for transitional language for payment of additional taxes or installment payment due as a result of disallowing any expenditure set out in Section 1.

Section 4: provides for retroactive date to the same period as the PPT.

FISCAL NOTE

STATE OF ALASKA
2007 LEGISLATIVE SESSION

Fiscal Note Number: HB 128-DEC-SPAR 2/20/07
 Bill Version: HB 128
 () Publish Date: _____

Revision Date/Time (Note if correction): _____ Dept. Affected: Dept of Environmental Conservation
 Title OIL & GAS PRODUCTION TAX: EXPENDITURES RDU Spill Prevention and Response
 Component Director's Office
 Sponsor Olson et al
 Requester House Special Committee on Oil and Gas Component No. 1392

Expenditures/Revenues (Thousands of Dollars)

Note: Amounts do not include inflation unless otherwise noted below.

OPERATING EXPENDITURES	FY 2008	FY 2009	FY 2010	FY 2011	FY 2012	FY 2013
Personal Services						
Travel						
Contractual						
Supplies						
Equipment						
Land & Structures						
Grants & Claims						
Miscellaneous						
TOTAL OPERATING	0.0	0.0	0.0	0.0	0.0	0.0

CAPITAL EXPENDITURES						
-----------------------------	--	--	--	--	--	--

CHANGE IN REVENUES ()						
-------------------------------	--	--	--	--	--	--

FUND SOURCE (Thousands of Dollars)

1002 Federal Receipts						
1003 GF Match						
1004 GF						
1005 GF/Program Receipts						
1037 GF/Mental Health						
Other (Specify Type--Do not abbreviate)						
TOTAL	0.0	0.0	0.0	0.0	0.0	0.0

Estimate of any current year (FY2006) cost: 0.0
 Mark this box (X) if funding for this bill is included in the Governor's FY 2008 budget proposal:

POSITIONS

Full-time						
Part-time						
Temporary						

ANALYSIS: (Attach a separate page if necessary)
 No additional costs are expected with this legislation.

Prepared by: Larry Dietrick Phone 465-5250
 Division Spill Prevention and Response Date/Time 2/20/07 4:00 PM
 Approved by: Larry Hartig Date 2/20/2007
 Agency Department of Environmental Conservation

FISCAL NOTE

STATE OF ALASKA
2007 LEGISLATIVE SESSION

Fiscal Note Number: HB128 DOR-TAX-2-22-07
 Bill Version: HB 128
 () Publish Date: _____

Revision Date/Time (Note if correction): _____ Dept. Affected: Revenue 04
 Title Oil & Gas Production Tax: Expenditures RDU Taxation and Treasury
 Component Tax Division
 Sponsor Representative Olson
 Requester (H) Oil and Gas Component No. 2476

Expenditures/Revenues (Thousands of Dollars)

Note: Amounts do not include inflation unless otherwise noted below.

OPERATING EXPENDITURES	FY 2008	FY 2009	FY 2010	FY 2011	FY 2012	FY 2013
Personal Services						
Travel						
Contractual	124.9	124.9	124.9	124.9	124.9	124.9
Supplies						
Equipment						
Land & Structures						
Grants & Claims						
Miscellaneous						
TOTAL OPERATING	124.9	124.9	124.9	124.9	124.9	124.9

CAPITAL EXPENDITURES						
-----------------------------	--	--	--	--	--	--

CHANGE IN REVENUES ()	*	*	*	*	*	*
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FUND SOURCE (Thousands of Dollars)

1002 Federal Receipts						
1003 GF Match						
1004 GF	124.9	124.9	124.9	124.9	124.9	124.9
1005 GF/Program Receipts						
1037 GF/Mental Health						
Other (Specify Type--Do not abbreviate)						
TOTAL	124.9	124.9	124.9	124.9	124.9	124.9

Estimate of any current year (FY2007) cost: 31.2

Check this box (X) if funding for this bill is included in the Governor's FY 2008 budget proposal:

POSITIONS

Full-time						
Part-time						
Temporary						

ANALYSIS: (Attach a separate page if necessary)

*This bill would add certain costs relating to improperly maintained property or equipment to the list of costs that do not qualify as lease expenditures under AS 43.55.165, the petroleum profits production tax system. Under the bill, the commissioner of revenue, in consultation with the commissioner of environmental conservation and the chair of the Alaska Oil and Gas Conservation Commission, would determine whether costs are specifically disallowed under this provision. The provision would disallow any costs incurred to (1) repair or replace improperly maintained property or equipment; and/or (2) maintain the operational capability of facilities or equipment that are either shut down or are diminished in capacity. The bill effective date is retroactive to April 1, 2006 - the effective date of the petroleum profits tax (PPT).

Prepared by: Jon Iversen and Cherie Nienhuis
 Division: Tax
 Approved by: Jerry Burnett
 Agency: Department of Revenue

Phone: 269-1033
 Date/Time: 2/22/07 11:00 AM
 Date: 2/22/2007

FISCAL NOTE

STATE OF ALASKA
2007 LEGISLATIVE SESSION

BILL NO. HB 128

ANALYSIS CONTINUATION

The impact this bill would have on petroleum tax revenues is indeterminate. Costs identified as disallowed under this bill could be categorized as either operating costs or capital costs. The PPT authorizes eligible operating costs to be deducted from the petroleum profits tax at a rate of 22.5%; the PPT authorizes capital costs to be both deducted at a rate of 22.5% and credited at a rate of 20%, for a combined production tax savings of 42.5%. Any set of disallowed costs is likely to be split between these two categories in a way that is distinct from that of another set of costs.

Administering this legislation would require one full-time equivalent (FTE) with expertise in oil and gas industry practices on the level of a petroleum engineer. The department currently contracts with a petroleum engineer for five years at a cost of \$624,650, or \$124,930 per year, for technical support related to petroleum production. It is anticipated that the department would be required to carry a second contract of this magnitude or greater in order to fulfill the requirements of this legislation.

STATE OF ALASKA**DEPARTMENT OF NATURAL RESOURCES****DIVISION OF OIL & GAS****SARAH PALIN, GOVERNOR**650 WEST 7TH AVENUE, SUITE 800
ANCHORAGE, ALASKA 99501-3560
PHONE: (907) 269-8900
FAX: (907) 269-8938

The Honorable Tom Wagoner
Alaska State Legislature
State Capitol
Juneau, Alaska 99801-1182

Dear Senator Wagoner,

This is in response to your letter to Tom Irwin dated February 12, 2007. Thank you for the opportunity to review SB 80 regarding certain credits and deductions against the Petroleum Production Tax. I would like to offer a few comments and suggestions regarding the bill. Some of these issues have been discussed with the State Pipeline Coordinator's Office, the Alaska Oil and Gas Conservation Commission (AOGCC), and the Department of Environmental Conservation (DEC).

I agree that the commissioner of Natural Resources should be one of the commissioners with whom the Department of Revenue (DOR) consults on certain costs related to improperly maintained property or equipment. The Department of Natural Resources (DNR), in representing the state as the landowner, is preparing to closely review the issue of system integrity and take necessary action as part of the function of the Petroleum System Integrity Office (PSIO). As the coordinating agency of the DNR, the PSIO will have the leading role coordinating system integrity issues with other agencies such as the DEC and AOGCC.

Second, I would point out that it may be difficult for the agencies to rely on "standard practices of the industry." Although "standard industry practices" is a commonly used term, it is not a term of art. You could attempt to define and reference standards, such as ISO standards and guidelines, set by various associations such as API and ASME. However, standards for corrosion control and monitoring are not well established. There are no standards that the Division of Oil and Gas is aware of that would provide a measure from which to base a decision for corrosion and maintenance of facilities and equipment.

As an alternative, the Division of Oil and Gas is recommending language be included that defines the standard as "considering practices undertaken by a reasonable and prudent operator under the same or similar circumstances."

It may also be difficult for agencies to define or establish "improper maintenance" or "improperly maintained" in order to use it as a standard for costs. The Division of Oil and Gas suggests that you consider wording such as "improper maintenance as indicated by an unanticipated failure." Alternatively, you might consider "proper maintenance" defined as the replacement of equipment based on a regular or routine surveillance of the property, equipment, or facilities.

"Develop, Conserve, and Enhance Natural Resources for Present and Future Alaskans."

DNR LETTER COMP. BILL

STATE OF ALASKA

SARAH PALIN, GOVERNOR

ALASKA OIL AND GAS CONSERVATION COMMISSION

333 W. 7th AVENUE, SUITE 100
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PHONE (907) 279-1433
FAX (907) 276-7542

February 16, 2007

The Honorable Thomas H. Wagoner
Alaska State Legislature
State Capitol, #427
Juneau, AK 99801

Re: SB 80

Dear Senator Wagoner,

This is in response to your February 12 letter requesting comments regarding the referenced legislation.

As an independent regulatory agency, the Alaska Oil and Gas Conservation Commission (AOGCC), does not have a position either in favor of or against this bill. We do however, understand, and agree with the premise that an operator should not be allowed to shift costs resulting from substandard maintenance practices to the State through tax deductions for lease expenditures.

Our main concern with the bill is the absence of a precise definition of improper maintenance. The bill proposes relying on standard practices of the industry to gauge whether there has been improper maintenance; but often there are no established industry standards to rely upon. Even when standards have been established by the American Petroleum Institute (API) or similar professional organizations, they are normally only recommended practices. Also, such industry guidelines are subject to change, which raises a question about whether an operator should be held to the most recent standard or to the standard prevailing when the alleged improper maintenance decision was made.

In some instances it will be obvious that there has been improper maintenance. In other instances (particularly well systems and equipment) the AOGCC will be required to consider design, installation, operation, and maintenance (all are integral to a determination of impropriety); and, making some determinations will require detailed investigation (perhaps including testing- non-destructive, destructive, metallurgic, etc.) and application of expertise not readily available within this agency.

Another concern is the fact that much of the equipment and systems in an oilfield that are subject to maintenance (and thus failure due to improper/inadequate maintenance) are not regulated by either AOGCC or Department of Environmental Conservation. This raises questions about how to judge "improper maintenance" in the absence of regulatory authority and oversight responsibility for such systems and equipment.

AOGCC LETTER COMP. BILL

Division of Oil & Gas

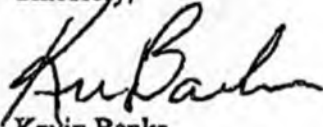
2/15/07

Page 2 of 2

Finally, I would suggest that DOR be required to provide its consulting agencies with specific data and records relevant to the repair, replacement, and maintenance of the property, equipment, or facility for which lease expenditures are being claimed under AS 43.55.165. Of course, the taxpayer confidentiality provisions in AS 43.05.230 would apply to this information.

DNR is continuing to study the bill and may have additional suggestions for you. Again, I appreciate the opportunity to offer comments and to work with you.

Sincerely,



Kevin Banks
Acting Director

cc: Tom Irwin, Commissioner, DNR
Jonne Slemons, Acting Coordinator PSIO
Marie Crosley, DO&G

STATE OF ALASKA

DEPARTMENT OF REVENUE

Tax Division

Sarah Palin, GOVERNOR

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907.269.6620

www.tax.state.ak.us

February 20, 2007

The Honorable Tom Wagoner
State Senate
Alaska State Capitol
Juneau, Alaska 99801-1182

Dear Senator Wagoner:

Thank you for the opportunity to review SB 80 regarding allowable lease expenditures for credits and deductions under the Petroleum Production Tax. I would like to offer a few comments on the bill.

First, the term "standard practices of the industry" may be difficult for the agencies to apply. It is my understanding that "standard industry practices" are not well defined when it comes to corrosion and maintenance. It is thus unclear what mechanism the Tax Division would employ to allow or exclude a deduction or credit for a certain cost.

I am also concerned about "relying on" the "standard practices of the industry" because the taxpayers would be providing and setting the standard. Whether the concept of "standard practices of the industry" is an appropriate benchmark depends on whether the industry has set and followed an appropriate standard.

Accordingly, I suggest changing "relying on" to "taking into consideration." This change would expand what the Department of Revenue could consider in determining whether a taxpayer improperly maintained property or equipment. Changing the language to "taking into consideration" doesn't limit the inquiry to industry practices, where the industry practices are inappropriate.

In addition, section (19)(C) seems unclear. This section excludes costs "for operating facilities or equipment at diminished capacity in proportion to the amount of diminished capacity that is caused by the improper maintenance of property or equipment." A possible interpretation could be that the taxpayers should not operate facilities unless they are going full bore (not at diminished capacity). If there are other facility costs the bill is trying to exclude, the language may need to be more specific, with a focus on "incremental operating expenses incurred as a result of operating facilities or equipment at diminished capacity that is caused by improper maintenance of property or equipment."

DOR LETTER COMP. BILL

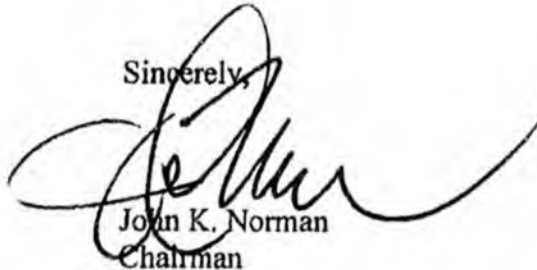
Finally, one can never lose sight of the fact that significant technological advances have occurred as a result of innovations which at the time were departures from standard industry practices. Also, engineers sometimes learn more through failure than from success. Often there is no indication something is being done improperly until a failure has occurred, but it is through analyzing the failure that the root cause can be determined and changes made going forward. This is simply the nature of engineering. In fact, there is a book entitled "To Engineer is Human: The Role of Failure in Successful Design" that describes and gives examples of this process.

Let me reiterate that we understand and agree with the intent of this legislation which is to prevent an operator from shifting financial responsibility to the State for costs resulting from the operator's improper maintenance practices. We do however, wish to point out some of the practical difficulties that may arise in determining whether maintenance has been in proper.

One last point - we suggest deleting the words "the chair of" at line 22 on page 3. It is our supposition that the bill is worded this way to ensure prompt consultations on maintenance issues. We can assure you however that consultation with the commission (as opposed to just the chair) will not delay our response time should we be given this responsibility

Thank you for allowing us this opportunity to comment.

Sincerely,

A handwritten signature in black ink, appearing to read "John K. Norman", written in a cursive style with a long horizontal flourish extending to the right.

John K. Norman
Chairman

cc: Pat Galvin, Commissioner
Department of Revenue

Larry Hartig, Commissioner
Department of Environmental Conservation

Tom Irwin, Commissioner
Department of Natural Resources

Mary Jackson

From: Hay, Linda [Linda_Hay@dec.state.ak.us]
Sent: Monday, February 19, 2007 12:29 PM
To: Mary Jackson; Konrad Jackson
Subject: SB 80 DEC Comments

Attachments: Hay, Linda.vcf



Hay, Linda.vcf (541
B)

Mary & Konrad - Here are the initial reactions from our folks in the Spill Prevention and Response Division. I will be over in the Capitol this afternoon and can stop by if either of you would like. Based on the legislation as currently written, we will be issuing an indeterminate fiscal note. Please bear in mind that this could change with possible amendments:

SB 80 & HB 128 provides a mechanism whereby costs or that portion of the costs related to repair and replacement of improperly maintained property or equipment would not be considered lease expenditures and thereby precluded from consideration for certain deductions or credits.

The legislation requires the determination be made in consultation with the Commissioner of Environmental Conservation and chair of AOGCC.

Whether or not such costs should be considered lease expenditures is a Revenue policy matter outside DEC's jurisdiction.

The extent to which the DEC Commissioner can contribute to the determination is probably limited. DEC may or may not have information or access to information regarding the operation or maintenance of certain property or equipment. It is likely that DEC would not have information or access to information related to property or equipment that is not subject to DEC regulation or oversight. DEC also is not likely to have cost information for property or equipment it does regulate. For example actual spill response costs or costs for repair or replacement of pipelines is not something required by DEC where those costs are directly borne by the operator.

DEC can offer its technical expertise or insights so there is likely no downside to inclusion in the consultation process. It should just be recognized that DEC's ability to be definitive or to have information or access to information important to this determination is probably limited.

It is possible that Revenue or DNR has a better means for acquiring this information through their various leasing or taxing authorities and it would seem that adequate substantiation for such costs would be subject to accounting rules and justification to substantiate any requests. In that regard the PPT regulations might be an avenue where the justification for including any such costs as lease expenditures would have to be documented and substantiated to the extent needed for accountants and the state to make a determination.

Linda Hay
Legislative Liaison
Dept. of Environmental Conservation
Commissioner's Office
907-465-5290 direct

Page 2
The Honorable Tom Wagoner
February 20, 2007

With these edits, the language of the bill would be as follows:

- (e) For purposes of this section, lease expenditures do not include:
- (19) costs or that portion of the costs determined by the
 - (20) commissioner, in consultation with the commissioner of environmental
 - (21) conservation and the chair of the Alaska Oil and Gas Conservation Commission
 - (22) and taking into consideration [relying on] the standard practices of the industry, to be
 - (23) (A) related to the repair and replacement of improperly
 - (24) maintained property or equipment;
 - (25) (B) incurred to maintain the operational capability of
 - (26) facilities or equipment shut down because of improper maintenance of
 - (27) property or equipment; or
 - (28) (C) incremental operating expenses incurred as a result of operating
 - (29) facilities or equipment at diminished capacity that is caused by improper
 - (30) maintenance of property or equipment [for operating facilities or
 - equipment at diminished
 - capacity in proportion to the amount of diminished capacity that is caused
 - by the improper maintenance of property or equipment].

It is worth noting that AS 43.05.230 and AS 40.25.100 protect sensitive taxpayer information through confidentiality. To the extent SB 80 would require the Department of Revenue to share such information with other agencies, those agencies would be subject to the confidentiality requirements.

The Tax Division is studying the bill and will likely have further suggestions. Thanks again for the opportunity to provide input. We look forward to working with you.

Sincerely,



Jonathan E. Iversen
Director



Doug Suttles

President

February 16, 2007

BP Exploration (Alaska) Inc.
P.O. Box 196612
900 E. Benson Boulevard
Anchorage, Alaska 99519-6612

Honorable Members
Alaska State Legislature
State Capitol
Juneau, AK 99801

Dear Ladies and Gentlemen:

A number of questions have been raised about BP's intent to deduct certain costs related to the Prudhoe Bay field shutdown last August. I am writing to confirm our position on this issue and at the same time reiterate BP's commitment to and plans for our business in Alaska.

Direct 907 564 5422
Main 907 561 5111
Fax 907 564 5900
doug.suttles@bp.com

With respect to the deductibility of costs, we can only speak for BP. Taxes are paid on a company wide basis rather than a field specific basis and BP cannot speak for the other Prudhoe Bay owners on tax issues.

BP follows the law when it files its taxes. Accordingly, BP will assume the appropriate deductions & credits for the costs associated with the repair and replacement of the Prudhoe Bay Oil Transit Lines (OTLs). Specifically, BP will deduct appropriate costs associated with repair of the OTLs and will seek authorized credits for capital costs to replace them. Similarly in compliance with the PPT Laws, we will not seek to deduct costs associated with cleaning up the oil spills.

To put this issue into context, I would like to openly share our estimated 2006 production taxes.* For the final nine months of 2006, the period over which PPT was applicable, we estimate that BP's production taxes will almost triple from \$180 million under the old ELF-based tax to more than \$500 million under PPT. Over the same period, BP's share of the deductions and credits associated with the costs of inspection, business resumption, and replacement of the OTLs will result in a total deduction of around \$11 million in 2006, which we have included in our 2006 production tax estimate.

We believe our approach is appropriate for the following reasons:

- 1) It is important to realize that the OTLs are some 30 years old and were sized for significantly higher production than we will have in the future. The OTLs would have been replaced in the normal course of business, even if the events of last year had not taken place.
- 2) We are in the process of building a new state of the art pipeline system for the future life of Prudhoe Bay. This is not a like-for-like replacement. Rather, we are investing in a brand new system, with pipe diameter sizes very different than the original design to reflect the reduced production from these maturing oilfields. The new system will have new chemical injection systems, upgraded pig launchers/receivers, upgraded leak detection system, and a Fusion Bond Epoxy external coating for longer life. The system will be in operation for decades to come. We believe this investment is in the best interests of the State of Alaska and the North Slope producers.

We appreciate the opportunity yesterday to discuss our Alaska business with the Senate Resources Committee and update them on the commitments we made in August 2006.

BP LETTER

February 15, 2007
Page 2 of 2

BP remains fully committed to the ongoing integrity of its facilities. As we embark on a vision of our next 50 years in Alaska, we will continue to make significant investment in facility renewal. This is not about replacement. It is about designing and constructing new facilities in a way that underpins the future and ensures the operability of the North Slope for decades to come.

With respect to PPT, last year the Legislature held long and difficult debates that ultimately led to the passage of PPT. The regulations are still being formalized as this legislation has not been in place for very long. We are only just preparing to submit our first tax returns under this new system. As a result, we believe it is premature to consider changes to the structure or intent of the current legislation. We believe it would be prudent for all parties, including producers and the State, to wait until PPT is fully implemented and we have real experience of its operation and impact before making any changes.

I hope I have provided you with the clarity of BP's intentions that many of you have been seeking and the reasoning behind the decisions we have made.

I look forward to working with the legislature as we progress our vision for our business in Alaska, including the commercialization of Alaska Gas, and as we bring our vision of a 50-year future to reality.

Sincerely,

A handwritten signature in black ink, appearing to read "Doug Suttles", with a stylized, cursive script.

Doug Suttles

- * Please note that, in disclosing in this letter certain specific tax information and BP's tax positions regarding PPT, BP does not intend to waive the confidentiality of any of its tax materials and information under applicable law (including AS 43.05.230), other than the particular information disclosed.

FISCAL NOTE

STATE OF ALASKA
2007 LEGISLATIVE SESSION

Fiscal Note Number: HB089-DNR J&G-02-21-07
 Bill Version: HB89
 () Publish Date: _____

Revision Date/Time (Note if correction): _____ Dept. Affected: Natural Resources
 Title Oil & Gas Production Tax RDU Resource Development
 Component Oil and Gas Development
 Sponsor Rep. Gara
 Requester House Oil and Gas Component No. 439

Expenditures/Revenues (Thousands of Dollars)

Note: Amounts do not include inflation unless otherwise noted below.

OPERATING EXPENDITURES	FY 2008	FY 2009	FY 2010	FY 2011	FY 2012	FY 2013
Personal Services						
Travel						
Contractual						
Supplies						
Equipment						
Land & Structures						
Grants & Claims						
Miscellaneous						
TOTAL OPERATING	0.0	0.0	0.0	0.0	0.0	0.0

CAPITAL EXPENDITURES						
-----------------------------	--	--	--	--	--	--

CHANGE IN REVENUES ()						
-------------------------------	--	--	--	--	--	--

FUND SOURCE (Thousands of Dollars)

1002 Federal Receipts						
1003 GF Match						
1004 GF						
1005 GF/Program Receipts						
1037 GF/Mental Health						
Other (Specify Type--Do not abbreviate)						
TOTAL	0.0	0.0	0.0	0.0	0.0	0.0

Estimate of any current year (FY2007) cost: 0.0
 Check this box (X) if funding for this bill is included in the Governor's FY 2008 budget proposal:

POSITIONS

Full-time						
Part-time						
Temporary						

ANALYSIS: (Attach a separate page if necessary)
 Currently under AS 43.55.025 (Alternative Tax Credit for Oil and Gas Exploration), DNR evaluates, for Dept. of Revenue, both oil and gas wells to determine whether a well or a potential well is directed at a distinctly separate exploration target.
 HB 89 would amend AS 43.55.025 so that it would apply only for gas exploration. In addition, the bill would add a new section to AS 43.55 for an oil exploration tax credit. This new section would continue to charge DNR with the responsibility to evaluate whether a well or potential well is directed at a distinctly separate exploration target.
 (Continued on next page)

Prepared by: Kevin Banks, Acting Director Phone 269-8800
 Division Oil and Gas Date/Time 2/21/2007
 Approved by: Tom Irwin, Commissioner Date 2/21/2007
 Agency Natural Resources

FISCAL NOTE

**STATE OF ALASKA
2007 LEGISLATIVE SESSION**

BILL NO. HB89

ANALYSIS CONTINUATION

In addition, this bill would give AOGCC authority to require, under certain conditions, working interest owners to provide access for other producers to production and other facilities whenever necessary.

There is no anticipated fiscal impact to DNR.

DRAFT CS HB 128

**Comparisons between original bill and draft CS
25-LS0561\E vs work draft 25-LS0561\M**

Page 3:

Line 21:

- Add "commissioner of natural resources"
- Delete "the chair of"

The intent is to include DNR as part of the consulting group and also have all members of AOGCC, not just the chair.

Line 22:

- Delete "relying on" and add "taking into consideration"
Makes language more general in nature.

Subsection (A), beginning on Line 24:

- Delete "improperly maintained property or equipment" and replace with "property or equipment that was not maintained or was improperly maintained".

Clarifies subsection (a) to insure "not maintained" is also established as criteria.

Subsection (B), beginning on Line 27:

- Add "a lack of"
Clarifies subsection (b), that improper or no maintenance are included.

Subsection (C), beginning on Line 29:

- Delete subsection and replace with:
"Incremental operating expenses incurred as a result of operating facilities or equipment at diminished capacity when that diminished capacity is caused by the lack of or improper maintenance of property or equipment"

To clarify incremental expenses for diminished capacity as a result of lack of or improper maintenance of facilities.

25-LS0561VM
Bullock
2/22/07

CS FOR HOUSE BILL NO. 128()

IN THE LEGISLATURE OF THE STATE OF ALASKA

TWENTY-FIFTH LEGISLATURE - FIRST SESSION

BY

**Offered:
Referred:**

Sponsor(s): REPRESENTATIVES OLSON, Harris, Ramras, Guttenberg, Neuman, Holmes, Thomas, Stoltze, Joule, Fairclough, LeDoux, Kerttula, Wilson, Lynn, Crawford, Gara, Gruenberg, Doll, Doogan, Edgmon, Buch

A BILL

FOR AN ACT ENTITLED

1 **"An Act relating to allowable lease expenditures for the purpose of determining the**
2 **production tax value of oil and gas for the purposes of the oil and gas production tax;**
3 **and providing for an effective date."**

4 **BE IT ENACTED BY THE LEGISLATURE OF THE STATE OF ALASKA:**

5 *** Section 1. AS 43.55.165(e) is amended to read:**

6 (e) For purposes of this section, lease expenditures do not include

7 (1) depreciation, depletion, or amortization;

8 (2) oil or gas royalty payments, production payments, lease profit
9 shares, or other payments or distributions of a share of oil or gas production, profit, or
10 revenue;

11 (3) taxes based on or measured by net income;

12 (4) interest or other financing charges or costs of raising equity or debt
13 capital;

14 (5) acquisition costs for a lease or property or exploration license;

- 1 (6) costs arising from fraud, wilful misconduct, or gross negligence;
- 2 (7) fines or penalties imposed by law;
- 3 (8) costs of arbitration, litigation, or other dispute resolution activities
- 4 that involve the state or concern the rights or obligations among owners of interests in,
- 5 or rights to production from, one or more leases or properties or a unit;
- 6 (9) costs incurred in organizing a partnership, joint venture, or other
- 7 business entity or arrangement;
- 8 (10) amounts paid to indemnify the state; the exclusion provided by
- 9 this paragraph does not apply to the costs of obtaining insurance or a surety bond from
- 10 a third-party insurer or surety;
- 11 (11) surcharges levied under AS 43.55.201 or 43.55.300;
- 12 (12) for a transaction that is an internal transfer or is otherwise not an
- 13 arm's length transaction, expenditures incurred that are in excess of fair market value;
- 14 (13) an expenditure incurred to purchase an interest in any corporation,
- 15 partnership, limited liability company, business trust, or any other business entity,
- 16 whether or not the transaction is treated as an asset sale for federal income tax
- 17 purposes;
- 18 (14) a tax levied under AS 43.55.011;
- 19 (15) the portion of costs incurred for dismantlement, removal,
- 20 surrender, or abandonment of a facility, pipeline, well pad, platform, or other
- 21 structure, or for the restoration of a lease, field, unit, area, body of water, or right-of-
- 22 way in conjunction with dismantlement, removal, surrender, or abandonment, that is
- 23 attributable to production of oil or gas occurring before April 1, 2006; the portion is
- 24 calculated as a ratio of the amount of oil and gas production, in barrels of oil
- 25 equivalent, associated with the facility, pipeline, well pad, platform, other structure,
- 26 lease, field, unit, area, body of water, or right-of-way occurring before April 1, 2006,
- 27 to the total amount of oil and gas production, in barrels of oil equivalent, associated
- 28 with that facility, pipeline, well pad, platform, other structure, lease, field, unit, area,
- 29 body of water, or right-of-way through the end of the calendar month before
- 30 commencement of the dismantlement, removal, surrender, or abandonment; a cost is
- 31 not excluded under this paragraph if the dismantlement, removal, surrender, or

1 abandonment for which the cost is incurred is undertaken for the purpose of replacing,
2 renovating, or improving the facility, pipeline, well pad, platform, or other structure;
3 for the purposes of this paragraph, "barrel of oil equivalent" means

4 (A) in the case of oil, one barrel;

5 (B) in the case of gas, 6,000 cubic feet;

6 (16) costs incurred for containment, control, cleanup, or removal in
7 connection with any unpermitted release of oil or a hazardous substance and any
8 liability for damages imposed on the producer or explorer for that unpermitted release;
9 this paragraph does not apply to the cost of developing and maintaining an oil
10 discharge prevention and contingency plan under AS 46.04.030;

11 (17) costs incurred to satisfy a work commitment under an exploration
12 license under AS 38.05.132;

13 (18) that portion of expenditures, that would otherwise be qualified
14 capital expenditures as defined in AS 43.55.023(k), incurred during a calendar year
15 that are less than the product of \$0.30 multiplied by the total taxable production from
16 each lease or property, in BTU equivalent barrels, during that calendar year, except
17 that, when a portion of a calendar year is subject to this provision, the expenditures
18 and volumes shall be prorated within that calendar year;

19 (19) costs or that portion of the costs determined by the
20 commissioner, in consultation with the commissioner of environmental
21 conservation, the commissioner of natural resources, and the Alaska Oil and Gas
22 Conservation Commission and taking into consideration the standard practices
23 of the industry, to be

24 (A) related to the repair and replacement of property or
25 equipment that was not maintained or was improperly maintained;

26 (B) incurred to maintain the operational capability of
27 facilities or equipment shut down because of a lack of or improper
28 maintenance of property or equipment; or

29 (C) incremental operating expenses incurred as a result of
30 operating facilities or equipment at diminished capacity when that
31 diminished capacity is caused by the lack of or improper maintenance of

1 property or equipment.

2 * **Sec. 2.** The uncodified law of the State of Alaska is amended by adding a new section to
3 read:

4 APPLICABILITY. Section 1 of this Act applies to oil and gas produced after
5 March 31, 2006.

6 * **Sec. 3.** The uncodified law of the State of Alaska is amended by adding a new section to
7 read:

8 TRANSITIONAL PROVISIONS. (a) A person that filed a statement under
9 AS 43.55.030 before the effective date of this Act and deducted lease expenditures that may
10 not be deducted under AS 43.55.165(e), as amended by sec. 1 of this Act, shall file an
11 amended return and pay any additional tax within 90 days after the effective date of this Act.

12 (b) A person required to make an installment payment of estimated tax under
13 AS 43.55.020(a) for a period not included in a return required to be filed before the effective
14 date of this Act shall determine the amount of the underpayment, if any, that is attributable to
15 lease expenditures that may not be deducted under AS 43.55.165(e) as amended by sec. 1 of
16 this Act. The amount of any underpayment determined under this subsection shall be paid
17 within 90 days after the effective date of this Act.

18 * **Sec. 4.** The uncodified law of the State of Alaska is amended by adding a new section to
19 read:

20 RETROACTIVITY. Section 1 of this Act is retroactive to April 1, 2006.

21 * **Sec. 5.** This Act takes effect immediately under AS 01.10.070(c).

ENHANCEMENT OF THE "GROSS" CHARACTER OF THE PPT BILL

August 5, 2006

Pedro van Meurs

This memo has been written at the request of Senator Wagoner. The request was to provide ideas as to how the "gross" character of the PPT bill can be enhanced.

This memo does not reflect the views of the Administration and is solely meant to provide Senator Wagoner with my professional advice on these ideas.

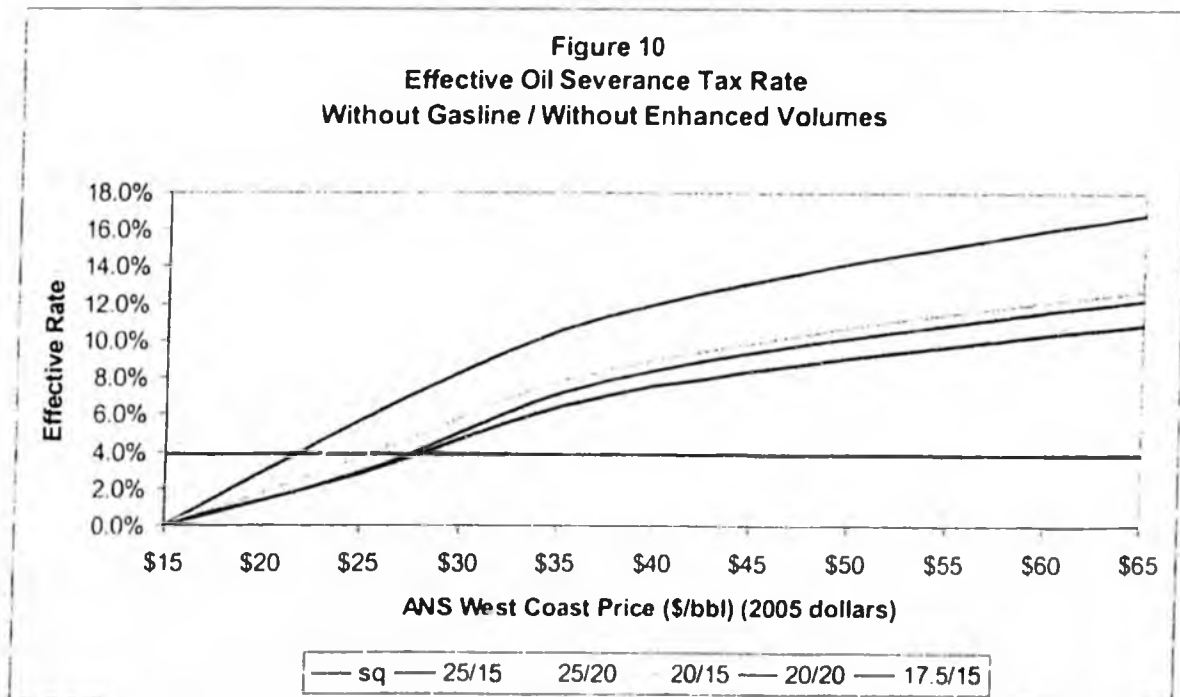
FLOOR

Considerable concern has been expressed about the fact that under some circumstances of low prices and high levels of investment, the PPT may result in less severance tax than we would have received otherwise under the current severance tax.

This can be prevented with the introduction of a "floor", very similar as was introduced in House Bill 3004.

The floor would be based on the **gross value** at the point of production of the taxable oil and gas.

Roger Marks presented to the Legislature in February this year a direct comparison between the various proposed PPT systems and the 4% average on gross that would be otherwise applicable to the year 2006.



These graphs prove that at about \$ 25 per barrel the current ELF produces about the same amount as a 22.5/20 PPT.

If we assume the adoption of a 22.5/20 PPT than one could take the position that the PPT should not be less than 4% of gross when the ANS West Coast price exceeds \$ 25 per barrel.

HB 3004 introduced the concept that at lower prices the North Slope oil becomes obviously less economic and it would be counter productive to continue to tax the oil industry. Therefore HB 3004 proposes a scale with a lower floor at lower prices.

This overall concept could be combined with the results of the analysis of Roger Marks as follows:

Over an ANS price of \$ 25 per barrel	--	4%
When ANS is between \$ 20 and \$ 25 per barrel	--	3%
When ANS is between \$ 17.50 and \$ 20 per barrel	--	2%
When ANS is between \$ 15 and \$ 17.50 per barrel	--	1%
Below \$ 15 per barrel	--	0%

Each year the floor would be compared with the tax payable under the PPT and if the floor is higher, the higher amount would be paid.

Following is an example how the floor would work based on a PPT tax rate of 20% and a floor of 4%:

Gross Revenues	100	100	100
Cost deductions	40	90	120
Net Revenues	60	10	- 20
PPT Tax	12	2	-4
Floor	4	4	4
Tax payable	12	4	4

If the Gross Revenue based PPT is higher than the Net Revenue based PPT this extra payment can not be recovered in following years as a deduction. In other words this excess cannot be carried forward in order to be recovered in future years.

Of course, the payment of the differential between the Gross and Net Revenue based PPT cannot be taken as a deduction for the Net Revenue based PPT.

However, any carry forward credits as a result of a tax loss based on the Net Revenue based PPT remain unaltered.

Also under this scheme companies would not lose their capital investment credits of 20%.

It is also suggested that the additional non-transferable tax credits under Sec. 43.55.024 of the proposed House Bill 3001 (FIN) will still be creditable against the Gross Revenue Based PPT if this is higher than the Net Revenue Based PPT. These additional non-transferable tax credits were meant to protect small companies and encourage companies outside Cook Inlet and the North Slope. The Gross Revenue based PPT should not harm such companies.

INCREASE THE NON DEDUCTABLE ITEMS

The more costs are being excluded from the Net Revenue calculation the more the overall calculation becomes more similar to a Gross Revenue calculation. Therefore, the Gross Revenue character of the tax can be enhanced by simply adding to the list of items that are not considered lease expenditures.

There are two important cost components that could be excluded from lease expenditures:

- Costs related to gas development under a stranded gas contract, and
- Capital maintenance expenditures.

Gas development costs under a stranded gas contract.

Much concern has been expressed about the fact that with a net revenue based system there could be a joint cost problem in Point Thomson and other similar fields if the stranded gas contract would be implemented.

It is argued that all Point Thomson development and operating costs would be deductible under the PPT. At the same time under the stranded gas contract, companies would provide a 7.25% share to the State on gross and not pay the 20% or 22.5% PPT on gas. It is perceived that Point Thomson is being cross subsidized from what otherwise would be tax on oil under the PPT.

My view is that this is not a fair comparison, since reasonably all costs can be absorbed by the condensates. Nevertheless, this issue remains a concern of the Legislators.

It would be possible to add a further item on the list of non deductible costs under proposed AS. 43.55.165 (e) of House Bill 3001 (FIN) written as follows (*non legal language*):

- “(19) 75% of the capital and operating costs associated with the Point Thomson Unit and other gas fields that are being developed under a contract under AS.43.82, with respect to working interest owners which have concluded such a contract.”

The 75% is based on the energy equivalent value considering that Point Thomson may have 400 million barrels of condensates and 7 – 8 Tcf of gas. In other words, the capital and operating costs would be allocated on an energy equivalent basis between condensates and gas. It is believed that many potential gas fields on the North Slope will have condensates and that these percentages may vary. For purposes of the bill, this percentage would be simply fixed.

The 25% allocated to condensates would be deductible for PPT purposes and would receive the related tax credits.

The 75% allocated to gas would not be deductible for PPT purposes and would not receive the related tax credits.

It can be assumed that the PTU would require a \$ 2.5 billion capital expenditure. Based on a 100% working interest, this arrangement would not receive a PPT tax reduction of \$ 750 million during development of the field. Assuming a \$ 1 billion operating expenditure over the life time of the field, it would mean that over time companies would pay \$ 150 million more tax during the operation of the field.

This is a significant tax increase, but in the total scheme of PPT taxation over the next 30 years this may represent only 1%-2% more tax.

Nevertheless, it would make the economics of Point Thomson development less attractive on an incremental basis and it would therefore make the entire gas project less attractive economically.

An interesting side effect of this arrangement is that it would place Chevron and other minority interest holders in a much better position relative to the sponsors. These companies have expressed concern that they would be discriminated against relative to the three sponsors. If Chevron and others do not join the stranded gas contract or would not be able to enter into a uniform upstream contract, they would at least benefit considerably relative to the Sponsors since they would receive the full tax deductions and credits. At the same time such companies would, of course, have to pay the full PPT on their gas income and therefore it is logical to permit them these tax credits and deductions.

Deemed Capital Maintenance Costs

Another concern that is regularly expressed is that the State should not permit the deduction of costs related to replacing equipment that is becoming defective or gathering lines that need to be replaced because of corrosion or other problems. The argument is that these assets should have been better maintained in the first place.

It should be noted that in most oil and gas fields, assets will have to be replaced after the technical life of such assets has expired. Therefore, such replacements are reasonable lease expenditures and are required to protect the health and safety of the workers and to protect the environment. Nevertheless, it is possible to exclude them from the lease expenditures under AS 43.55.165 (e) if this is politically desirable. A section could be added as follows (*non legal language*):

- (20) deemed capital maintenance expenditures which shall be capital expenditures equal to US \$ 0.30 per BTU equivalent barrel taxable production.

The US \$ 0.30 per BTU equivalent barrel is based on reasonable capital maintenance costs of fields for which I have (confidential) information. Based on a production of 900,000 barrel equivalent per day, this means that about \$ 100 million in capital expenditures per year will not be deductible for PPT purposes. Based on a PPT rate of 22.5% and a tax credit rate of 20% this means that the companies will pay \$ 42.5 million more tax per year.

An interesting side effect is that companies that would have a low level of capital expenditure per barrel would feel the effect more on a relative basis than companies that would have a high level of capital expenditures per barrel. Companies that re-invest strongly are therefore harmed less by this provision than typical harvesters.