

***BP Prudhoe Bay Royalty Trust***  
***2006 Tax Information Booklet***

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IMPORTANT: This booklet contains Income Tax Reporting Information.





The Bank of New York  
Corporate Trust Trustee Administration  
101 Barclay Street  
New York, NY 10286

Dear Present or Former Unit Holder:

This tax booklet is intended to provide information necessary for you to determine Federal and Alaska taxable income relating to your past or present ownership of Units in BP Prudhoe Bay Royalty Trust (the "Trust"). It is being mailed to all persons who appeared as Unit holders on the Trustee's records at any time during 2006.

The "Highlights - Tax Matters Relating to BP Prudhoe Bay Royalty Trust" section gives relevant history regarding the formation of the Trust and also explains why we cannot simply report to each past or present Unit holder the amount taxable in his own case. We suggest that you read this section carefully. Several sections of this booklet are based upon information supplied by BP Exploration (Alaska) Inc., an indirect wholly owned subsidiary of BP AMOCO p.l.c., formerly known as The British Petroleum Company p.l.c. Part I of this booklet reflects the Trust's intention, as previously disclosed, to allocate income and deductions to Trust Unit holders based on record ownership at quarterly record dates. Because it is unknown whether the Internal Revenue Service will accept such allocation, or will require income and deductions of the Trust to be determined and allocated daily, or will require some method of daily pro-ration, Part II of this booklet is also included.

By using either Part I or Part II, any past or present Unit holder will be able to determine his taxable income in accordance with the method he selects.

Please note that the Trust has neither requested nor received from the Internal Revenue Service any rulings on the tax treatment of any items presented in this booklet. Accordingly, the present tax laws and regulations affecting the matters discussed herein are subject to both differences of opinion as to their applicability or interpretation and future legislation.

**THE MATERIAL IN THIS BOOKLET IS INTENDED TO HELP YOU DETERMINE YOUR TAXABLE INCOME ONLY AFTER YOU HAVE SELECTED THE METHOD YOU BELIEVE IS APPROPRIATE FOR DETERMINING SUCH AMOUNT. THIS BOOKLET IS NOT INTENDED TO RENDER PROFESSIONAL ADVICE. WE STRONGLY RECOMMEND THAT YOU CONSULT WITH YOUR TAX ADVISOR.**

THE BANK OF NEW YORK,  
as Trustee

February 14, 2007



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## **HIGHLIGHTS**

### **Tax Matters Relating to BP Prudhoe Bay Royalty Trust**

#### **Description of the Trust**

BP Prudhoe Bay Royalty Trust (the “Trust”) was established by a Trust Agreement dated February 28, 1989 by and among The Standard Oil Company (the “Depositor”), BP Exploration (Alaska) Inc., (the “Company”), The Bank of New York as a trustee and a co-trustee, currently, The Bank of New York (Delaware) (collectively with The Bank of New York, the “Trustee”). On February 28, 1989, the Depositor conveyed to the Trust a royalty interest in the Company’s working interest in the Prudhoe Bay Unit (the “PBU”), located on the North Slope of Alaska.

Specifically, the Trust holds a royalty interest which entitles the Trust to a per barrel royalty on 16.4246% of the first 90,000 barrels of the average actual daily production of oil and condensate less certain chargeable costs and production taxes from the Company’s working interest in the PBU. Pursuant to a Support Agreement among BP AMOCO p.l.c., (BP AMOCO), formerly known as The British Petroleum Company p.l.c., the Company, the Depositor and the Trust, BP AMOCO has guaranteed the performance by the Company of its payment obligations with respect to the royalty interest. The Trust holds the royalty interest in trust for the benefit of holders of equal undivided portions known as Trust Units, subject to the laws of the States of Alaska and Delaware. The Trust Units represent beneficial interests in the Trust and are evidenced by transferable certificates issued by the Trustee. Trust Units are listed and traded on the New York Stock Exchange under the ticker symbol “BPT.”

The Trustee has only such powers as are

necessary for the collection and distribution of revenues, the payment of trust liabilities and the protection of the royalty interest. The Trust has a Co-Trustee in order to satisfy certain requirements of the Delaware Trust Act. The Bank of New York alone is able to exercise the rights and powers granted to the Trustee in the Trust Agreement.

On January 17, April 17, July 17 and October 18, 2006 the Company made payments to the Trust under the royalty interest with respect to production during the calendar quarter ending on the last day of the calendar month preceding such payment. Distributions (i.e., the quarterly income amount) representing primarily the excess of revenues from the royalty interest over expenses and payments of the liabilities of the Trust were made to Unit holders of record at the end of such respective dates. Trust expenses generally consist of Trustee’s fees, engineering fees, accounting and legal fees, production taxes and other chargeable costs.

Unit holders must use either Part I or Part II to compute their 2006 taxable income from the Trust. Part I reflects the Trust’s intention, as previously disclosed, to allocate income and deductions to Unit holders based on record ownership at quarterly record dates during the year. Part II provides an average daily allocation of income and deductions since it is unknown whether the Internal Revenue Service will accept the allocation of income and deductions based on quarterly record dates as reflected in Part I. Accordingly, Part II also includes information regarding the January 17, 2007 distribution which relates to production during the last calendar quarter of 2006.

**IT IS IMPORTANT THAT UNIT  
HOLDERS CONSULT THEIR TAX  
ADVISORS REGARDING THE  
SELECTION OF EITHER METHOD.**

**Federal Income Taxes**

Neither the Trust nor the Depositor has requested (nor does either intend to request) a ruling from the Internal Revenue Service as to the classification of the Trust as a grantor trust rather than an association taxable as a corporation. Should the Internal Revenue Service determine the Trust is an association taxable as a corporation, Unit owners would be treated as shareholders and the Trust would be taxed as if it were a corporation.

This booklet has been prepared based on the assumption that the Trust will be treated as a grantor trust for Federal income tax purposes. Accordingly, Unit holders would be taxable on their pro-rata share of the income and expense of the Trust. The Trust, therefore, pays no Federal income tax but files an information return. In addition, income attributable to ownership of Trust Units that are not debt-financed may not constitute unrelated business taxable income to tax-exempt organizations. However, Unit holders should consult their tax advisors.

**State Income Taxes**

Since the PBU is located entirely within the State of Alaska, all royalty income is deemed to be derived from that state. Alaska does not impose an income tax on individuals or trusts; accordingly, only corporate Unit holders may be subject to Alaska tax on their pro-rata share of Trust income and expense. This booklet assists corporate Unit holders in complying with Alaska tax filing requirements.

**Depletion**

Because a Unit holder's share of the royalty interest is depleted as a result of the production and sale of oil and condensate, Unit holders are entitled to a deduction for depletion. There are two methods of computing a Unit holder's depletion deduction: the cost method and the percentage method. Trust Units generally represent interests in proven property. As a result, Unit holders that acquired Units prior to October 12, 1990 may use the cost method only to compute their depletion deduction. The Omnibus Budget Reconciliation Act of 1990 repealed the rules regarding the use of the percentage method on transferred domestic oil and gas producing properties. As a result, Unit holders who acquired Units after October 11, 1990 may compute their allowable depletion deduction using either the cost method or the percentage method.

The deduction for depletion is computed differently under the cost and percentage methods. For instance, the deduction for depletion under the cost method is computed on a units-of-production basis, and will differ among Unit holders based on their adjusted bases in their Units. Since the Trustee does not maintain records of the price each Unit holder paid for his Units, we cannot compute each Unit holder's actual cost depletion deduction. Parts I and II, however, each include tables that will permit a Unit holder to compute his cost depletion amount.

The deduction for percentage depletion is a statutory deduction that is based on the Unit holder's gross Trust income rather than the adjusted basis in the Units. Specifically, the deduction is computed based on the number of Units acquired by each Unit holder after October 11, 1990; the corresponding gross amount of Trust income allocable to



such Units; and an applicable statutory percentage. Percentage depletion is generally available to independent producers and royalty owners on up to 1,000 equivalent barrels of domestic production per day. Parts I and II each include worksheets that will permit a Unit holder to compute his percentage depletion amount. It should be noted, however, that the Internal Revenue Service may challenge those transfers made solely for the benefit of obtaining percentage depletion. As a result, we recommend that Unit holders consult their tax advisors.

### **Sale of Units**

Unit holders should recognize gain or loss on the sale or exchange of Units as measured by the difference between the amount realized on the sale or exchange and their adjusted basis in their Units. Unit holders' adjusted basis is their initial cost (or other basis) adjusted to reflect the Unit holders' share of depletion deductions from the Trust. The "Sale of Units" section of the Appendix will assist Unit holders in computing their adjusted basis and in determining the appropriate character of the resulting gain or loss. A record of the original cost of each block of Units as well as basis adjustments with respect to each block of Units should be preserved as part of each Unit holder's tax records to determine gain or loss upon disposition of Units.

### **Consultation with Tax Advisor**

THIS BOOKLET IS DESIGNED TO ASSIST UNIT HOLDERS IN THEIR INCOME TAX COMPLIANCE. UNIT HOLDERS SHOULD CONSULT THEIR TAX ADVISORS ON ALL TAX COMPLIANCE MATTERS.

ANY ADVICE IN THIS BOOKLET IS NOT INTENDED TO BE USED, AND CANNOT BE USED, BY ANY PERSON OR ENTITY FOR THE PURPOSE OF (i) AVOIDING PENALTIES THAT MAY BE IMPOSED ON ANY TAXPAYER OR (ii) PROMOTING, MARKETING OR RECOMMENDING TO ANOTHER PARTY ANY MATTERS ADDRESSED HEREIN.

### **Employer Identification Number**

The Federal Employer Identification Number of the Trust is 13-6943724.

### **Contact Information**

Unit holders requiring additional information should contact the Trustee at (212) 815-6908 or write to:

BP Prudhoe Bay Royalty Trust  
c/o The Bank of New York  
Corporate Trust Trustee Administration  
101 Barclay Street  
New York, New York 10286

## **MANNER OF PRESENTATION OF TAX DATA**

This booklet contains worksheets and specific instructions designed to help a Unit holder compute taxable income. The calculations on the worksheets usually consist of multiplying the table amounts by the number of Units in each block of Units. If you owned different blocks of Units purchased at different times, at different prices or held for different periods, you must make your computations for each separate block or period.

Various tables set forth the tax data by means of “per Unit” factors which generally represent decimal fractions of one dollar for any period of ownership. Find the time period correlating to the date of acquisition of a block of Units in the left margin of the table and read across the row to the column corresponding to the last record date on which the block of Units was held.

Unit holders who select Part I in determining taxable income will use the worksheets and tables on pages 6 through 12 of this booklet. Unit holders who select Part II in determining taxable income will, depending on their method of accounting, use the worksheets and tables on pages 14 through 29 of this booklet.

Please note that Unit holders who selected either Part I or Part II in prior taxable years should be consistent in their method of determining taxable income and continue to use the worksheets and tables from the respective Part for the current and subsequent taxable years.

**PART I**

**Record Ownership at  
Quarterly Record Dates  
Method**

## PART I

### HOW TO COMPUTE 2006 TAXABLE INCOME

Part I allocates income and deductions to Unit holders based on record ownership at quarterly record dates.

The sections of Part I of this booklet that a Unit holder will need to compute taxable income will depend on:

when and how the Units were acquired, and

if and when the Units were disposed.

- I. Unit holders acquiring Units on or before January 17, 2006 and holding such Units through December 31, 2006 have the following Federal income tax items to report for such Units:

	<u>Per Unit</u>	<u>Number of Units Owned</u>	<u>Total</u>
Trust Income .....	\$15.14381	X	= \$
Trust Administrative and Other Expenses (show as a reduction to your Trust Income) .....	\$6.55146	X	= \$
Depletion Deduction (from Worksheet B, line 9, page 10) (show as a reduction to your Trust Income) .....			\$

The amounts calculated in this worksheet represent your share of Trust income and expense including your allowable cost or percentage depletion deduction. These amounts should be reported on the appropriate schedule of your income tax return. For example, individual Unit holders will report these amounts on Form 1040, Schedule E, Part I. Corporations, partnerships, and trusts and estates should refer to the instructions for Forms 1120, 1065, and 1041, respectively.

- II. Unit holders who acquired their Units after January 17, 2006 or disposed of their Units on or before October 18, 2006 will use Part I, Worksheet A, page 8, in order to determine their share of taxable income from the Trust.

<b>SCHEDULE E</b> <b>(Form 1040)</b> <small>Department of the Treasury Internal Revenue Service (99)</small>	<b>Supplemental Income and Loss</b> (From rental real estate, royalties, partnerships, S corporations, estates, trusts, REMICs, etc.) <small>Attach to Form 1040, 1040NR, or Form 1041. See instructions for Schedule E (Form 1040).</small>	<small>OMB No. 1545-0074</small> <div style="font-size: 24pt; font-weight: bold; text-align: center;">2006</div> <small>Attachment Sequence No. 13</small>																																																																																																																																												
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<b>Part I Income or Loss From Rental Real Estate and Royalties</b> <small>Note. If you are in the business of renting personal property, use Schedule C or C-EZ (see page E-3). Report farm rental income or loss from Form 4835 on page 2, line 40.</small>																																																																																																																																														
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20 Depreciation expense or depletion (see page E-4) . . . . .	20	8.78		20 8.78																																																																																																																																										
21 Total expenses. Add lines 19 and 20 . . . . .	21	663.93																																																																																																																																												
22 Income or (loss) from rental real estate or royalty properties. Subtract line 21 from line 3 (rents) or line 4 (royalties). If the result is a (loss), see page E-5 to find out if you must file Form 6198 . . . . .	22	850.45																																																																																																																																												
23 Deductible rental real estate loss. Caution. Your rental real estate loss on line 22 may be limited. See page E-5 to find out if you must file Form 8582. Real estate professionals must complete line 43 on page 2 . . . . .	23																																																																																																																																													
24 Income. Add positive amounts shown on line 22. Do not include any losses . . . . .	24			24 850.45																																																																																																																																										
25 Losses. Add royalty losses from line 22 and rental real estate losses from line 23. Enter total losses here . . . . .	25			25 ( 0.00 )																																																																																																																																										
26 Total rental real estate and royalty income or (loss). Combine lines 24 and 25. Enter the result here. If Parts II, III, IV, and line 40 on page 2 do not apply to you, also enter this amount on Form 1040, line 17, or Form 1040NR, line 18. Otherwise, include this amount in the total on line 41 on page 2 . . . . .	26			26 850.45																																																																																																																																										
<small>For Paperwork Reduction Act Notice, see page E-7 of the instructions.</small>			<small>Schedule E (Form 1040) 2006</small>																																																																																																																																											

The above illustration is for an individual Unit holder who purchased 100 units in the initial February 28, 1989 private placement offering for \$2,500 and held such Units through December 31, 2006. The Unit holder's adjusted basis in the Units is \$155.42 (the initial cost of the Units less prior years' depletion deductions). Items of 2006 income and expense were calculated as follows:

<u>Items of Income or Expense</u>	<u>Per Unit</u>	<u>Number of Units Owned</u>	<u>Total</u>	<u>Where to Enter on Schedule E, Form 1040</u>
Trust Income .....	\$15.14381	X 100	=\$1,514.38	Part I, Schedule E
Trust Administrative and Other Expenses (show as a reduction to your Trust Income) .....	\$6.55146	X 100	= \$655.15	Part I, Schedule E
<u>Adjusted Basis of Units Owned</u>				
Depletion Deduction (show as a reduction to your Trust Income)....	0.05652	X \$155.42	= \$8.78	Part I, Schedule E

**PART I**

**WORKSHEET A  
COMPUTATION OF TAXABLE INCOME  
BP PRUDHOE BAY ROYALTY TRUST  
2006 TAX INFORMATION**

THIS WORKSHEET COVERS \_\_\_\_\_ UNITS ACQUIRED \_\_\_\_\_  
(See Specific Instructions on page 9)

Worksheet A should be used by Unit holders who either acquired Units after January 17, 2006 or disposed of Units on or before October 18, 2006. This worksheet allows such Unit holders to compute their taxable income based upon ownership at quarterly record dates.

<u>Items of Income or Expense</u>	<u>Number of Units Owned</u>	<u>Table Amount</u>	<u>Total</u>
I. Trust Income			
Amount calculated using Table I on page 12	_____	X _____	= \$ _____
II. Trust Administrative and Other Expenses (show as a reduction to your Trust Income)			
Amount calculated using Table II on page 12	_____	X _____	= \$ _____
III. Depletion Deduction (from Worksheet B, line 9, page 10) (show as a reduction to your Trust Income)			\$ _____

## **PART I**

### **WORKSHEET A SPECIFIC INSTRUCTIONS**

If you own Units in several blocks or the number of Units you own in a single block changed during the year, you should reproduce the necessary copies of this worksheet and complete a separate worksheet for each block of Units acquired or disposed of on a different date or at a different price or held for a different period.

The amounts from Tables I and II, page 12, are your components of Trust income and expense on a per Unit basis.

Use Worksheet B, page 10, to calculate your depletion deduction.

The amounts calculated in this worksheet represent your share of Trust income and expense including your depletion deduction. These amounts should be reported on the appropriate schedule of your income tax return. For example, individual Unit holders will report these amounts on Form 1040, Schedule E, Part I. Corporations, partnerships, and trusts and estates should refer to the instructions for Forms 1120, 1065, and 1041, respectively.

**PART I**

**WORKSHEET B  
COMPUTATION OF DEPLETION DEDUCTION  
BP PRUDHOE BAY ROYALTY TRUST  
2006 TAX INFORMATION**

THIS WORKSHEET COVERS \_\_\_\_\_ UNITS ACQUIRED \_\_\_\_\_  
(See Specific Instructions on page 11)

Worksheet B should be used by Unit holders in computing their depletion deduction for the year.

**I. Cost Depletion**

Those Unit holders who acquired Units on or prior to October 11, 1990 must compute their depletion deduction under the cost method.

1. Depletable Basis		
A. Original Cost of Units	\$ _____	
B. Less: Depletion Deduction In Prior Years	( _____ )	
C. Adjusted Depletable Basis		\$ _____
2. Cost Depletion Factor (From Part I, Table III, page 12)		X _____
3. Cost Depletion		\$ _____

**II. Percentage Depletion**

The percentage method may be used by Unit holders who acquired their Units after October 11, 1990. Such Unit holders need to compute their depletion deduction under both the percentage method and the cost method utilizing the method producing the greater deduction.

4. Total Gross Income (See Specific Instructions)	\$ _____	
5. Less: Trust Expenses	( _____ )	
6. Income Before Depletion		\$ _____
7. 15% of Line 4		\$ _____
8. Percentage Depletion (Lesser of line 6 or line 7)		\$ _____

**III. Depletion Deduction**

9. Allowable Depletion (Greater of line 3 or line 8, See Specific Instructions) (Transfer this amount to Part I, Depletion Deduction line, page 6 or to Part I, Worksheet A, Section III, page 8)		\$ _____
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**PART I**

**WORKSHEET B**

**SPECIFIC INSTRUCTIONS**

If you own Units in several blocks or the number of Units you own in a single block changed during the year, you should reproduce the necessary copies of this worksheet and complete a separate worksheet for each block of Units acquired or disposed of on a different date or at a different price or held for a different period.

The original cost of your Units should be reduced for the amount of cost or percentage depletion allowed as a deduction in prior years. Once your adjusted basis in the Units has reached zero, cost depletion will no longer be available.

For Units acquired prior to October 12, 1990, only use lines 1 through 3 to compute your allowable depletion deduction with respect to those Units.

For those Unit holders entitled to percentage depletion, the amount of your depletion deduction will be the greater of the amount computed under the cost or percentage method (e.g., the greater of line 3 or line 8).

The total gross income before applicable statutory percentage determined on line 4 represents either Trust income amount computed on page 6 for Unit holders who held their Units throughout the year, or Trust income computed on page 8 for Unit holders who either acquired or disposed of their Units during the year.

The allowable amount of percentage depletion is limited to 100 percent of net Trust income before the deduction for depletion.

Percentage depletion is generally available to independent producers and royalty owners on up to 1,000 equivalent barrels of domestic production per day. Accordingly, Unit holders entitled to percentage depletion will need to determine if their share of total production from all sources (including the Trust) exceeds 1,000 equivalent barrels per day. The Trust receives a royalty each quarter on 16.4246% of the first 90,000 barrels of average daily production or 14,782 barrels per day. For the quarters ending March 31, June 30 and December 31, 2006 a Unit holder will calculate his share of daily production from the Trust by multiplying 14,782 by the ratio of the number of Units acquired after October 11, 1990 over 21,400,000. However, during the quarter ended September 30, 2006 average daily production fell below 90,000 barrels. Therefore, Unit holders who held units on October 18, 2006 should substitute 9,739 for 14,782 when determining daily production for July 1, 2006 through September 30, 2006.

**PART I**

**BP PRUDHOE BAY ROYALTY TRUST  
2006 TAX INFORMATION**

**TABLE I  
Trust Income Per Unit (in Dollars)  
(Cumulative)**

<u>For Unit Acquired of Record</u>		<u>Last Record Date in 2006 That Unit Was Held</u>			
<u>On/after</u>	<u>Not later than</u>	<u>Jan. 17</u>	<u>April 17</u>	<u>July 17</u>	<u>Oct. 18</u>
Inception –	Jan. 17, 2006 .....	3.81384	7.75276	12.18595	15.14381
Jan. 18 –	April 17 .....	0.00000	3.93892	8.37211	11.32997
April 18 –	July 17 .....	0.00000	0.00000	4.43319	7.39105
July 18 –	Oct. 18 .....	0.00000	0.00000	0.00000	2.95786

**TABLE II  
Trust Administrative and Other Expenses Per Unit (in Dollars)  
(Cumulative)**

<u>For Unit Acquired of Record</u>		<u>Last Record Date in 2006 That Unit Was Held</u>			
<u>On/after</u>	<u>Not later than</u>	<u>Jan. 17</u>	<u>April 17</u>	<u>July 17</u>	<u>Oct. 18</u>
Inception –	Jan. 17, 2006 .....	1.69993	3.43054	5.26854	6.55146
Jan. 18 –	April 17 .....	0.00000	1.73060	3.56860	4.85152
April 18 –	July 17 .....	0.00000	0.00000	1.83800	3.12092
July 18 –	Oct. 18 .....	0.00000	0.00000	0.00000	1.28292

**TABLE III  
Cost Depletion Factors  
(Cumulative)**

<u>For Unit Acquired of Record</u>		<u>Last Record Date in 2006 That Unit Was Held</u>			
<u>On/after</u>	<u>Not later than</u>	<u>Jan. 17</u>	<u>April 17</u>	<u>July 17</u>	<u>Oct. 18</u>
Inception –	Jan. 17, 2006 .....	0.01499	0.03046	0.04610	0.05652
Jan. 18 –	April 17 .....	0.00000	0.01547	0.03111	0.04153
April 18 –	July 17 .....	0.00000	0.00000	0.01564	0.02606
July 18 –	Oct. 18 .....	0.00000	0.00000	0.00000	0.01042

The above tables reflect the allocation of income and deductions to Unit holders based on record ownership at quarterly record dates. The depletion table reflects the cost depletion factors to be used for Units acquired of record at different periods and held through the various record dates in 2006.

## **PART II**

### **Average Daily Allocation**

#### **Method**

## PART II

### HOW TO COMPUTE 2006 TAXABLE INCOME

Part II allocates income and deductions to Unit holders based on an average daily allocation during the period the Units were held.

The sections of this booklet that a Unit holder will need to compute taxable income will depend on:  
when and how the Units were acquired,  
if and when the Units were disposed, and  
the Unit holder's method of accounting.

- I. A cash basis Unit holder acquiring Units on or before October 1, 2005 and holding such Units through December 31, 2006 has the following Federal income tax items to report for such Units:

	<u>Per</u> <u>Unit</u>	X	<u>Number</u> <u>of Units</u> <u>Owned</u>	=	<u>Total</u>
Trust Income .....	\$15.14381		_____		\$ _____
Trust Administrative and Other Expenses (show as a reduction to your Trust Income) .....	\$6.55146		_____		\$ _____
Depletion Deduction (from Worksheet B, line 9, page 22) (show as a reduction to your Trust Income) .....					\$ _____

The amounts calculated in this worksheet represent your share of Trust income and expense, including your allowable cost or percentage depletion. These amounts should be reported on the appropriate schedule of your income tax return. For example, individual Unit holders will report these amounts on Form 1040, Schedule E, Part I. Corporations, partnerships, and trusts and estates should refer to the instructions for Forms 1120, 1065, and 1041, respectively.

- II. Cash basis Unit holders (other than those Unit holders described in Section III) who acquired their Units after October 17, 2005 and/or disposed of their Units during 2006 will use Part II, Worksheet A, pages 17 and 18, in order to determine their share of taxable income from the Trust.

- III. Cash basis Unit holders who acquired their Units after the close of a calendar quarter and on or before the next record date (i.e., after December 31, 2005 and before January 18, 2006, after March 31, 2006 and before April 18, 2006, after June 30, 2006 and before July 18, 2006 or after September 30, 2006 and before October 19, 2006) will not be required to report any income upon receipt of their first distribution. However, there will be a basis adjustment required to reflect the non-taxable distribution. Taxable income of such Unit holders should be computed by using Part II, Worksheet A, pages 17 and 18. Cash basis Unit holders who acquired Units on or after October 18, 2006 and held the Units through year end will have no tax consequences for the year but will be required to adjust their bases in the subsequent year.
- IV. Accrual basis Unit holders who owned and/or acquired their Units on January 1, 2006 and held such Units through December 31, 2006 have the following Federal income tax items to report for such Units:

	<u>Per Unit</u>	<u>Number of Units Owned</u>	<u>Total</u>
Trust Income .....	\$15.17494 X	_____	= \$ _____
Trust Administrative and Other Expenses (show as a reduction to your Trust Income) .....	\$6.68450 X	_____	= \$ _____
Depletion Deduction (from Worksheet B, line 9, page 22) (show as a reduction to your Trust Income) .....			\$ _____

The amounts calculated in this worksheet represent your share of Trust income and expense, including your allowable cost or percentage depletion. These amounts should be reported as indicated in Section I, page 14.

- V. Accrual basis Unit holders who acquired or disposed of their Units subsequent to January 1, 2006 will use Part II, Worksheet A-1, page 20 to determine their share of taxable income from the Trust.

<b>SCHEDULE E (Form 1040)</b> Department of the Treasury Internal Revenue Service (99)		<b>Supplemental Income and Loss</b> (From rental real estate, royalties, partnerships, S corporations, estates, trusts, REMICs, etc.)			OMB No. 1545-0074 <b>2006</b> Attachment Sequence No. <b>13</b>	
Name(s) shown on return					Your social security number	
<b>Part I Income or Loss From Rental Real Estate and Royalties</b> Note. If you are in the business of renting personal property, use Schedule C or C-EZ (see page E-3). Report farm rental income or loss from Form 4835 on page 2, line 40.						
<b>1</b>	List the type and location of each rental real estate property:	<b>2</b> For each rental real estate property listed on line 1, did you or your family use it during the tax year for personal purposes for more than the greater of: • 14 days or • 10% of the total days rented at fair rental value? (See page E-3.)			<b>Yes</b>	<b>No</b>
<b>A</b>	-----	<b>A</b>				
<b>B</b>	-----	<b>B</b>				
<b>C</b>	-----	<b>C</b>				
<b>Income:</b>		<b>Properties</b>			<b>Totals</b> (Add columns A, B, and C.)	
<b>3</b>	Rents received	<b>A</b>	<b>B</b>	<b>C</b>	<b>3</b>	
<b>4</b>	Royalties received				<b>4</b>	1,514.38
<b>Expenses:</b>						
<b>5</b>	Advertising					
<b>6</b>	Auto and travel (see page E-4)					
<b>7</b>	Cleaning and maintenance					
<b>8</b>	Commissions					
<b>9</b>	Insurance					
<b>10</b>	Legal and other professional fees					
<b>11</b>	Management fees					
<b>12</b>	Mortgage interest paid to banks, etc. (see page E-4)				<b>12</b>	
<b>13</b>	Other interest					
<b>14</b>	Repairs					
<b>15</b>	Supplies					
<b>16</b>	Taxes					
<b>17</b>	Utilities					
<b>18</b>	Other (list) ▶					
<b>19</b>	Add lines 5 through 18				<b>19</b>	655.15
<b>20</b>	Depreciation expense or depletion (see page E-4)				<b>20</b>	8.78
<b>21</b>	Total expenses. Add lines 19 and 20				<b>21</b>	663.93
<b>22</b>	Income or (loss) from rental real estate or royalty properties. Subtract line 21 from line 3 (rents) or line 4 (royalties). If the result is a (loss), see page E-5 to find out if you must file Form 6198.				<b>22</b>	850.45
<b>23</b>	Deductible rental real estate loss. <b>Caution.</b> Your rental real estate loss on line 22 may be limited. See page E-5 to find out if you must file Form 8582. Real estate professionals must complete line 43 on page 2.				<b>23</b>	
<b>24</b>	<b>Income.</b> Add positive amounts shown on line 22. Do not include any losses				<b>24</b>	850.45
<b>25</b>	<b>Losses.</b> Add royalty losses from line 22 and rental real estate losses from line 23. Enter total losses here				<b>25</b>	0.00
<b>26</b>	<b>Total rental real estate and royalty income or (loss).</b> Combine lines 24 and 25. Enter the result here. If Parts II, III, IV, and line 40 on page 2 do not apply to you, also enter this amount on Form 1040, line 17, or Form 1040NR, line 18. Otherwise, include this amount in the total on line 41 on page 2.				<b>26</b>	850.45

The above illustration is for an individual cash basis Unit holder who purchased 100 units in the initial February 28, 1989 private placement offering for \$2,500 and held such Units through December 31, 2006. The Unit holder's adjusted basis in the Units is \$155.42 (the initial cost of the Units less prior years' depletion deductions). Items of 2006 income and expense were calculated as follows:

<u>Items of Income or Expense</u>	<u>Per Unit</u>	<u>Number of Units Owned</u>	<u>Total</u>	<u>Where to Enter on Schedule E, Form 1040</u>
Trust Income .....	\$15.14381	X 100	= \$1,514.38	Part I, Schedule E
Trust Administrative and Other Expenses (show as a reduction to your Trust Income).....	\$6.55146	X 100	= \$655.15	Part I, Schedule E
			<u>Adjusted Basis of Units Owned</u>	
Depletion Deduction (show as a reduction to your Trust Income)....	0.05652	X \$155.42	= \$8.78	Part I, Schedule E

**PART II**

**WORKSHEET A  
COMPUTATION OF TAXABLE INCOME FOR  
CASH BASIS UNIT HOLDERS  
BP PRUDHOE BAY ROYALTY TRUST  
2006 TAX INFORMATION**

THIS WORKSHEET COVERS \_\_\_\_\_ UNITS ACQUIRED \_\_\_\_\_  
(See Specific Instructions on page 19)

Worksheet A should be used by cash basis Unit holders who either acquired their Units on or after October 1, 2005 or disposed of their Units during 2006. This worksheet reflects the necessary adjustments required in the computation of taxable income.

<u>Items of Income or Expense</u>	<u>Number of Units Owned</u>	<u>Table Amount</u>	<u>Total</u>
<b>I. Trust Income</b>			
<b><u>Steps</u></b>			
1. Amount calculated using Table I (page 28)	_____	X _____	= \$ _____
2. a. Acquisition Adjustments			
Less: Portion allocable to pre-acquisition days in acquiring period	_____ X _____	X _____	= ( _____ )
(# of days prior to acquisition in period)	(Amount from Table IV, Col. b, page 29)	Number of Units acquired	
b. Disposition Adjustments			
Plus: Portion allocable to pre-disposition days in disposing period	_____ X _____	X _____	= _____
(# of days prior to disposition in period)	(Amount from Table IV, Col. b, page 29)	Number of Units disposed of	
3. Trust Income			\$ <u>_____</u>

**PART II**

**WORKSHEET A (CONTINUED)  
COMPUTATION OF TAXABLE INCOME FOR  
CASH BASIS UNIT HOLDERS  
BP PRUDHOE BAY ROYALTY TRUST  
2006 TAX INFORMATION**

<u>Items of Income or Expense</u>	<u>Number of Units Owned</u>	<u>Table Amount</u>	<u>Total</u>
II. Trust Administrative and Other Expenses			
<u>Steps</u>			
1. Amount calculated using Table II _____ (page 28)	X	_____	= \$ _____
2. a. Acquisition Adjustments			
Less: Portion allocable to pre-acquisition days in acquiring period			
_____ X _____	X	_____	= ( _____ )
(# of days prior to acquisition in period)	(Amount from Table IV, Col. c, page 29)	Number of Units acquired	
b. Disposition Adjustments			
Plus: Portion allocable to pre-disposition days in disposing period			
_____ X _____	X	_____	= _____
(# of days prior to disposition in period)	(Amount from Table IV, Col. c, page 29)	Number of Units disposed of	
3. Trust Administrative and Other Expenses (show as a reduction to your Trust Income)			\$ _____
III. Depletion Deduction (from Worksheet B, line 9, page 22) (show as a reduction to your Trust Income)			
			\$ _____



## PART II

### WORKSHEET A SPECIFIC INSTRUCTIONS

If you own Units in several blocks or the number of Units you own in a single block changed during the year, you should reproduce the necessary copies of this worksheet and complete a separate worksheet for each block of Units acquired or disposed of on a different date or at a different price or held for a different period.

The amounts from Tables I and II, page 28, are your components of Trust income and expense on a per Unit basis.

The following cash basis Unit holders must adjust their reportable income and expense (Step 2, Sections I and II of Part II, Worksheet A, pages 17 and 18) to reflect only the portion attributable to the actual number of days the Units are held in the period of acquisition or disposition:

1. Cash basis Unit holders acquiring their Units on or after October 1, 2005, and
2. Cash basis Unit holders disposing of their Units at any time during the 2006 taxable year.

If you acquired your Units on or after October 1, 2005 and disposed of them after December 31, 2005 and on or before January 17, 2006 you do not have to complete Step 1, Sections I and II of Part II, Worksheet A, pages 17 and 18. However, the remaining adjustments to Trust income and expense will need to be made.

If you acquired your Units after the close of a calendar quarter and on or before the next record date, the amount you received for your first distribution should not be included in your Trust income. Thus, the amount calculated from Part II, Tables I and II, page 28 should be reduced for this first distribution.

If you owned your Units as of October 1, 2005 and at all times through 2006, no adjustments are necessary to Trust Income or Trust Administrative and Other Expenses as calculated from Part II, Tables I and II, page 28. That is, you do not have to complete Step 2, Sections I and II of Part II, Worksheet A, pages 17 and 18.

Use Worksheet B, page 22, to calculate your depletion deduction.

The amounts calculated in this worksheet represent your share of Trust income and expense including your allowable cost or percentage depletion deduction. These amounts should be reported on the appropriate schedule of your income tax return. For example, individual Unit holders will report these amounts on Form 1040, Schedule E, Part I. Corporations, partnerships, and trusts and estates should refer to the instructions for Forms 1120, 1065, and 1041, respectively.

**PART II**

**WORKSHEET A-1  
COMPUTATION OF TAXABLE INCOME FOR  
ACCRUAL BASIS UNIT HOLDERS  
BP PRUDHOE BAY ROYALTY TRUST  
2006 TAX INFORMATION**

THIS WORKSHEET COVERS \_\_\_\_\_ UNITS ACQUIRED \_\_\_\_\_  
(See Specific Instructions on page 21)

Worksheet A-1 should be used by accrual basis Unit holders. This worksheet requires such Unit holders to compute their share of income and expense based upon the number of days such Unit holders held their Units in a given period.

**I. CALCULATION OF INCOME AND EXPENSES**

<u>Items of Income or Expense</u>	(a) <u>Number of Units</u>	X	(b) <u>Number of Days Held</u>	X	Average Daily <u>Per Unit Amount</u>	=	<u>Total</u>
1. January 1, 2006-March 31, 2006 (90 days)							
a. Trust Income	_____	X	_____	X	\$0.04376580	=	\$ _____
b. Trust Administrative and Other Expenses	_____	X	_____	X	\$0.01922894	=	\$ _____
2. April 1, 2006-June 30, 2006 (91 days)							
a. Trust Income	_____	X	_____	X	\$0.04871639	=	\$ _____
b. Trust Administrative and Other Expenses	_____	X	_____	X	\$0.02019789	=	\$ _____
3. July 1, 2006-September 30, 2006 (92 days)							
a. Trust Income	_____	X	_____	X	\$0.03215065	=	\$ _____
b. Trust Administrative and Other Expenses	_____	X	_____	X	\$0.01394478	=	\$ _____
4. October 1, 2006-December 31, 2006 (92 days)							
a. Trust Income	_____	X	_____	X	\$0.04179389	=	\$ _____
b. Trust Administrative and Other Expenses	_____	X	_____	X	\$0.01992359	=	\$ _____

**PART II**

**WORKSHEET A-1 (CONTINUED)  
COMPUTATION OF TAXABLE INCOME FOR  
ACCRUAL BASIS UNIT HOLDERS  
BP PRUDHOE BAY ROYALTY TRUST  
2006 TAX INFORMATION**

**II. SUMMARY**

1. Trust Income (Sum of Lines 1a, 2a, 3a, 4a, from Section I)	\$	_____
2. Trust Administrative and Other Expenses (Sum of Lines 1b, 2b, 3b, 4b, from Section I) (show as a reduction to your Trust Income)	\$	_____
3. Depletion Deduction (From Worksheet B, line 9, page 22) (show as a reduction to your Trust Income)	\$	_____

**PART II**

**WORKSHEET A-1  
SPECIFIC INSTRUCTIONS**

If you own Units in several blocks or the number of Units you own in a single block changed during the year, you should reproduce the necessary copies of Part II, Worksheet A-1, pages 20 and 21 and complete separate worksheets for each block of Units acquired or disposed of on a different date or at a different price or held for a different period.

Enter the number of Units you own in each period in Section I, column a.

Enter the number of days you held your Units in each period in Section I, column b.

Total the amounts of Trust income and Trust expenses from each period and enter the totals on the appropriate lines of Section II, Summary.

Enter the depletion deduction calculated on Part II, Worksheet B, page 22 in Section III, line 9.

The amounts calculated in this worksheet represent your share of Trust income and expense including your allowable cost or percentage depletion deduction. These amounts should be reported on the appropriate schedule of your income tax return. For example, individual Unit holders will report these amounts on Form 1040, Schedule E, Part I. Corporations, partnerships, and trusts and estates should refer to the instructions for Forms 1120, 1065, and 1041, respectively.

**PART II**

**WORKSHEET B  
COMPUTATION OF DEPLETION DEDUCTION  
BP PRUDHOE BAY ROYALTY TRUST  
2006 TAX INFORMATION**

THIS WORKSHEET COVERS \_\_\_\_\_ UNITS ACQUIRED \_\_\_\_\_  
(See Specific Instructions on page 23)

Worksheet B should be used by Unit holders in computing their depletion deduction for the year.

**I. Cost Depletion**

Those Unit holders who acquired Units on or prior to October 11, 1990 must compute their depletion deduction under the cost method.

1. Adjusted Depletable Basis (From Part II, Worksheet B-1, line 5, page 24) \$ \_\_\_\_\_
2. Adjusted Cost Depletion Factor (From Part II, Worksheet B-2, line 4, page 26) X \_\_\_\_\_
3. Cost Depletion \$ \_\_\_\_\_

**II. Percentage Depletion**

The percentage method may be used by Unit holders who acquired their Units after October 11, 1990. Such Unit holders need to compute their depletion deduction under both the percentage method and the cost method utilizing the method producing the greater deduction.

4. Total Gross Income (See Specific Instructions) \$ \_\_\_\_\_  
(From Part II, Worksheet A, Section I, line 3, page 17 for cash basis Unit holders)  
(From Part II, Worksheet A-1, Section II, line 1, page 21 for accrual basis Unit holders)
5. Less: Trust Expenses ( \_\_\_\_\_ )
6. Income Before Depletion \$ \_\_\_\_\_
7. 15% of Line 4 \$ \_\_\_\_\_
8. Percentage Depletion (Lesser of line 6 or line 7) \$ \_\_\_\_\_

**III. Depletion Deduction**

9. Allowable Depletion (Greater of line 3 or line 8, See Specific Instructions) \$ \_\_\_\_\_

## PART II

### WORKSHEET B SPECIFIC INSTRUCTIONS

If you own Units in several blocks or the number of Units you own in a single block changed during the year, you should reproduce the necessary copies of this worksheet and complete a separate worksheet for each block of Units acquired or disposed of on a different date or at a different price or held for a different period.

The original cost of your Units should be reduced for the amount of cost or percentage depletion allowed as a deduction in prior years. Once your adjusted basis in the Units has reached zero, cost depletion will no longer be available.

For Units owned or acquired prior to October 12, 1990, only use lines 1 through 3 to compute your allowable depletion deduction with respect to those Units.

For those Unit holders entitled to percentage depletion, the amount of your depletion deduction will be the greater of the amount computed under the cost or percentage method (e.g., the greater of line 3 or line 8).

The allowable amount of percentage depletion is limited to 100 percent of net Trust income before the deduction for depletion.

Percentage depletion is generally available to independent producers and royalty owners on up to 1,000 equivalent barrels of domestic production per day. Accordingly, Unit holders entitled to percentage depletion will need to determine if their share of total production from all sources (including the Trust) exceeds 1,000 equivalent barrels per day. The Trust receives a royalty each quarter on 16.4246% of the first 90,000 barrels of average daily production or 14,782 barrels per day. For the quarters ending March 31, June 30 and December 31, 2006 a Unit holder will calculate his share of daily production from the Trust by multiplying 14,782 by the ratio of the number of Units acquired after October 11, 1990 over 21,400,000. However, during the quarter ended September 30, 2006 average daily production fell below 90,000 barrels. Therefore, Unit holders who held units during the quarter ended September 30, 2006 should substitute 9,739 for 14,782 when determining daily production for days that Units were held between July 1, 2006 and September 30, 2006.

Cash basis Unit holders should transfer the allowable depletion deduction calculated on line 9 to Part II, Section I, Depletion Deduction line, page 14 or to Part II, Worksheet A, Section III, page 18. Accrual basis Unit holders should transfer this amount to Part II, Section IV, Depletion Deduction line, page 15 or to Part II, Worksheet A-1, Section II, line 3, page 21.

**PART II**

**WORKSHEET B-1  
COMPUTATION OF DEPLETABLE BASIS  
BP PRUDHOE BAY ROYALTY TRUST  
2006 TAX INFORMATION**

THIS WORKSHEET COVERS \_\_\_\_\_ UNITS ACQUIRED \_\_\_\_\_  
(See Specific Instructions on page 25)

Worksheet B-1 is used to determine that portion of your original cost that is allocated to your original depletable basis.

1. Original Cost of Units \* \$ \_\_\_\_\_

2. Less: Portion of original cost not allocable to basis \*\*

$$\frac{\text{_____}}{\text{net daily income factor for period of acquisition (Part II, Table IV, Col. d, page 29)}} \times \frac{\text{_____}}{\text{\# of days in period prior to acquisition}} \times \frac{\text{_____}}{\text{\# of Units acquired}} = (\text{_____})$$

3. Original Depletable Basis \$ \_\_\_\_\_

4. Less: Depletion Deduction in Prior Years \$(\_\_\_\_\_)

5. Adjusted Depletable Basis  
(Transfer this amount to Part II,  
Worksheet B, line 1, page 22) \$ \_\_\_\_\_

\* Unit holders who acquired Units during the period following the close of a calendar quarter and on or before the next record date (as discussed in Part II, Section III, page 15) should exclude from their original cost the amount of the first distribution received subsequent to acquisition. Unit holders who acquired Units before October 1, 2005 should skip to line 3.

\*\* Unit holders who held Units from October 1, 2005 are not required to adjust their basis.

## **PART II**

### **WORKSHEET B-1 SPECIFIC INSTRUCTIONS**

If you own Units in several blocks or the number of Units you own in a single block changed during the year, you should reproduce the necessary copies of this worksheet and complete a separate worksheet for each block of Units acquired or disposed of on a different date or at a different price or held for a different period.

You should complete this worksheet in the year you acquire your Units and maintain the completed worksheet as part of your permanent records relating to your interest in the Trust.





## **PART II**

### **WORKSHEET B-2 SPECIFIC INSTRUCTIONS**

If you own Units in several blocks or the number of Units you own in a single block changed during the year, you should reproduce the necessary copies of this worksheet and complete a separate worksheet for each block of Units acquired or disposed of on a different date or at a different price or held for a different period.

**PART II**

**BP PRUDHOE BAY ROYALTY TRUST  
2006 TAX INFORMATION**

**TABLE I  
Trust Income Per Unit (in Dollars)  
For Cash Basis Unit Holders  
(Cumulative)**

<u>For Unit Acquired of Record</u>		<u>Last Record Date in 2006 That Unit Was Held*</u>			
<u>On/after</u>	<u>Not later than</u>	<u>Jan. 17</u>	<u>April 17</u>	<u>July 17</u>	<u>Oct. 18</u>
Inception –	Jan. 17, 2006.....	3.81384	7.75276	12.18595	15.14381
Jan. 18 –	April 17 .....	0.00000	3.93892	8.37211	11.32997
April 18 –	July 17 .....	0.00000	0.00000	4.43319	7.39105
July 18 –	Oct. 18 .....	0.00000	0.00000	0.00000	2.95786

**TABLE II  
Trust Administrative and Other Expenses Per Unit (in Dollars)  
For Cash Basis Unit Holders  
(Cumulative)**

<u>For Unit Acquired of Record</u>		<u>Last Record Date in 2006 That Unit Was Held*</u>			
<u>On/after</u>	<u>Not later than</u>	<u>Jan. 17</u>	<u>April 17</u>	<u>July 17</u>	<u>Oct. 18</u>
Inception –	Jan. 17, 2006.....	1.69993	3.43054	5.26854	6.55146
Jan. 18 –	April 17 .....	0.00000	1.73060	3.56860	4.85152
April 18 –	July 17 .....	0.00000	0.00000	1.83800	3.12092
July 18 –	Oct. 18 .....	0.00000	0.00000	0.00000	1.28292

\* Unit holders who acquired their Units after the calendar quarter and on or before the first record date do not include the first distribution of Trust income/expense in their calculations.

**TABLE III  
Cost Depletion Factors  
For Cash Basis Unit Holders  
(Cumulative)**

<u>For Unit Acquired of Record</u>		<u>Last Record Date in 2006 That Unit Was Held</u>			
<u>On/after</u>	<u>Not later than</u>	<u>Jan. 17</u>	<u>April 17</u>	<u>July 17</u>	<u>Oct. 18</u>
Inception –	Jan. 17, 2006.....	0.01499	0.03046	0.04610	0.05652
Jan. 18 –	April 17 .....	0.00000	0.01547	0.03111	0.04153
April 18 –	July 17 .....	0.00000	0.00000	0.01564	0.02606
July 18 –	Oct. 18 .....	0.00000	0.00000	0.00000	0.01042

**PART II**

**BP PRUDHOE BAY ROYALTY TRUST  
2006 TAX INFORMATION**

**TABLE IV  
Average Daily Net Income Factors (By Period)  
(Noncumulative)**

<u>Period</u>	(a) <u>Days in Period</u>	(b) <u>Trust Income</u>	(c) Trust <u>Administrative and Other Expenses</u>	(d) <u>Daily Net Income Factor</u>
Oct. 1 - Dec. 31, 2005 .....	92	0.04145479	0.01847753	0.02297725
Jan. 1 - Mar. 31, 2006 .....	90	0.04376580	0.01922894	0.02453686
Apr. 1 - Jun. 30 .....	91	0.04871639	0.02019789	0.02851850
Jul. 1 - Sep. 30 .....	92	0.03215065	0.01394478	0.01820587
Oct. 1 - Dec. 31 .....	92	0.04179389	0.01992359	0.02187031

**TABLE V  
Cost Depletion Factors  
For Accrual Basis Unit Holders  
(Cumulative)**

<u>For Unit Acquired of Record</u>		<u>Last Date in 2006 Through Which Unit Was Held</u>			
<u>On/after</u>	<u>Not later than</u>	<u>Mar. 31</u>	<u>Jun. 30</u>	<u>Sept. 30</u>	<u>Dec. 31</u>
Jan. 1 –	Mar. 31, 2006 .....	0.01547	0.03111	0.04153	0.05734
Apr. 1 –	Jun. 30 .....	0.00000	0.01564	0.02606	0.04187
Jul. 1 –	Sep. 30 .....	0.00000	0.00000	0.01042	0.02623
Oct. 1 –	Dec. 31 .....	0.00000	0.00000	0.00000	0.01581

**TABLE VI  
Average Daily Cost Depletion Factors (By Period)  
(Noncumulative)  
For Calendar Quarter Ending**

	<u>2005</u>	<u>2006</u>			
	<u>Dec. 31</u>	<u>Mar. 31</u>	<u>June 30</u>	<u>Sept. 30</u>	<u>Dec. 31</u>
Depletion Factor	0.000163	0.000172	0.000172	0.000113	0.000172

## APPENDIX General Information Contents

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### **Classification of Trust Income**

The Trust receives royalty income which constitutes portfolio income under the passive activity rules of the Internal Revenue Code. As such, the Trust does not engage in an activity which could be considered a trade or business activity for purposes of these rules. Accordingly, Trust income may not be used to offset a Unit holder's losses from passive activities.

Unit holders must include Trust income, net of Trust administrative and other expenses and depletion deductions, in their calculation of net portfolio income. The provisions relating to the various classifications of income and the tax consequences of these classifications are complex. Unit holders should consult their tax advisors to determine the impact of these provisions on their tax situations.

### **Classification of Trust Administrative and Other Expenses**

Trust administrative and other expenses, such as Trustee's fees, engineering fees, accounting and legal fees, production taxes and other chargeable costs, incurred by the Trustee on behalf of the Unit holders, are deductible in arriving at the Unit holders' adjusted gross income since they are attributable to property held for the production of royalty income. These expenses are not subject to the two percent floor affecting miscellaneous itemized deductions. Foreign Unit holders should refer to the discussion under "Foreign Persons."

### **Depletion**

Cost Depletion: The deduction for cost depletion recognizes that a royalty interest is depleted when oil and condensate are produced therefrom.

Cost depletion requires an estimate of the amount of production expected from the property. The formula used is the actual production for a given period divided by the sum of the estimated remaining production at the end of the period and the actual production for the given period. This ratio is then applied to the Unit holder's depletable basis to determine the cost depletion deduction.

Unit holders who select Part I should use Worksheet B on page 10 and Table III on page 12. Unit holders who select Part II should use Worksheets B, B-1 and B-2 on pages 22 through 27 and the Tables on pages 28 and 29 depending on their method of accounting. Foreign Unit holders should refer to the discussion under "Foreign Persons."

Percentage Depletion: The Internal Revenue Code also provides for a statutory method of computing the depletion deduction based upon established percentages. This method is known as percentage depletion and is provided for under Internal Revenue Code Section 613. The allowance for percentage depletion generally did not apply to interests in proven oil and gas properties that were transferred after December 31, 1974 and prior to October 12, 1990. The royalty interest of the Trust is considered transferred proven property and, accordingly, allowance for percentage depletion is not permitted for Units acquired prior to October 12, 1990. The Omnibus Budget Reconciliation Act of 1990 repealed this rule for transfers occurring on or after October 12, 1990, thereby permitting Unit holders who acquired Units in the Trust after such date to compute their depletion deduction using the percentage method.

As provided under Internal Revenue Code Section 613A, percentage depletion is available to independent producers and royalty owners but is limited to 65 percent of

the taxpayer's taxable income, as adjusted, from all sources before the deduction for depletion. This limitation is in addition to the 100 percent of net Trust income limitation and the barrel limitation discussed on pages 11 and 23. The amount of depletion disallowed as a deduction due to the 65 percent of taxable income limitation shall be treated as an allowable deduction for the following tax years, subject to the 65 percent limitation.

Unit holders who select Part I should use Worksheet B on page 10. Unit holders who select Part II will use Worksheets B, B-1 and B-2 on pages 22 through 27. Foreign Unit holders should refer to the discussion under "Foreign Persons."

### **Foreign Persons**

Generally, nonresident alien individuals, partnerships and foreign corporations (i.e., Foreign persons) are subject to a tax of 30 percent on gross income from sources within the U.S. that are not effectively connected with a U.S. trade or business. Income from the Trust is considered income which is not effectively connected with a U.S. trade or business. As a result, Foreign persons would be subject to a 30 percent tax on their gross income from the Trust, without deductions. Usually such tax is to be withheld at the source of payment by the withholding agent (The Bank of New York). However, if there is a treaty in effect between the U.S. and the country of residence of the foreign person, such treaty may reduce the rate of withholding. In order to claim the lower treaty rate, Form W-8 BEN (Certificate of Foreign Status of Beneficial Owner for United States Tax Withholding) should be filed with The Bank of New York.

A Unit holder who is a Foreign person may make an election pursuant to Internal

Revenue Code Section 871(d) or 882(d), or pursuant to any similar provisions of applicable treaties, to treat the income (which constitutes income from real property) from the Trust as income which is effectively connected with a U.S. trade or business. If this election is made such Unit holder will not be subject to withholding but will, however, be taxed on such income in the same manner as a U.S. resident individual, partnership or corporation (i.e., a U.S. person). As a result, such Unit holder will be taxed on his net income as opposed to his gross income from the Trust.

Also, under this election, any gain or loss upon the disposition of a Trust Unit will be deemed to be connected with a U.S. trade or business and taxed in the manner described above.

Unit holders making an election under Internal Revenue Code Section 871(d) or 882(d), or pursuant to similar provisions of applicable treaties, should file Form W-8ECI with the Bank of New York in order to claim an exemption from withholding.

If a Foreign person owns a greater than 5 percent interest in the Trust, that interest is a U.S. real property interest as provided under Internal Revenue Code Section 897. Gain on disposition of that interest will be taxed as though the property was effectively connected with a U.S. trade or business. In addition, Foreign persons subject to Internal Revenue Code Section 897 who are nonresident alien individuals may be subject to an alternative minimum tax of up to 26 percent or 28 percent, (depending upon filing status and taxable income), on the lessor of:

1. the individual's alternative minimum taxable income for the taxable year, or

2. the individual's net United States real property gain for the taxable year.

Gain or loss on the disposition is determined by subtracting the adjusted basis of the Unit from the proceeds received. (See "Sale of Units" discussion).

If the Foreign person is a corporation which made an election under Internal Revenue Code Section 882(d), the corporation would also be subject to a 30 percent tax under Internal Revenue Code Section 884. This tax is imposed on U.S. branch profits of a foreign corporation that are not reinvested in the U.S. trade or business. This tax is in addition to the tax on effectively connected income. The branch profits tax may be either reduced or eliminated by treaty.

THE FEDERAL AND STATE INCOME TAXATION OF FOREIGN PERSONS IS HIGHLY COMPLEX, AND IT IS RECOMMENDED THAT SUCH PERSONS CONSULT THEIR TAX ADVISORS.

### **State Income Taxes**

Unit holders may be required to report their share of income from the Trust to their state of residence or commercial domicile. However, only corporate Unit holders will need to report their share of income to the State of Alaska. Alaska does not impose an income tax on individuals or estates and trusts. Corporate Unit holders should be advised that all Trust income is Alaska source income and should be reported accordingly. It should be noted that certain states either do not allow the depletion deduction to be computed under the percentage method or provide for a different

statutory rate and/or net income limitation. In those situations, Unit holders will be required to report only cost depletion or adjust the statutory rate utilized for the percentage method.

All Unit holders should consult with their tax advisors regarding the state tax implications resulting from their investment in the Trust Units.

### **Nominee Reporting Requirements**

Any nominee holding an interest in the Trust must furnish the Trustee with specific information about the beneficial owner, including the name, address, and taxpayer identification number. In addition, the nominee owner must forward to the beneficial owner specific information supplied by the Trustee pertaining to the beneficial owner's interest. Failure to comply with these requirements results in the imposition of penalties up to \$100,000 on the nominee. Those nominees holding Units for the beneficial ownership of another should obtain tax advice to ensure compliance with nominee reporting requirements.

### **Backup Withholding**

A payor must withhold 28 percent of any reportable payment if the payee fails to furnish his taxpayer identification number ("TIN") to the payor in the required manner or if the Secretary of the Treasury notifies the payor that the TIN furnished by the payee is incorrect. A Unit holder will avoid backup withholding by furnishing his correct TIN to the Trustee in the form required by law.

### **Sale of Units**

If a Unit holder sold Units during the year, the realized gain or loss is the difference between the selling price and the adjusted

basis of the Units sold. However, cash basis Unit holders who select Part II in determining taxable income and disposed of their Units prior to distribution dates will need to reduce their proceeds received on sale by the amount of net income recognized by virtue of the net disposition adjustments in Part II, Worksheet A, pages 17 and 18 (Section I, Step 2b and Section II, Step 2b). The resulting gain or loss from sale or disposition of Trust Units is generally accorded capital asset treatment. However, pursuant to Internal Revenue Code Section 1254, certain depletion deductions claimed with respect to the Units must be recaptured as ordinary income upon sale or disposition of such interest.

Unit holders should consult their tax advisors with respect to computing gain or loss upon a sale of Units.











**THE  
BANK OF  
NEW  
YORK**

Corporate Trust Trustee Administration  
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